BEFORE THE NATIONAL ADJUDICATORY COUNCIL

NASD

In the Matter of Department of Market Regulation, Complainant, vs. Joseph A. Geraci, II Minneapolis, MN, Respondent.	DECISION Complaint No. CMS020143 Dated: December 9, 2004

Respondent engaged in insider trading in violation of the antifraud provisions of the federal securities laws and NASD rules. Held, Hearing Panel's findings of violation are affirmed and sanctions are modified.

Appearances

For the Complainant: Jeffrey K. Stith, Esq., and Michael J. Dixon, Esq., NASD Department of Market Regulation.

For the Respondent: Steven E. Rau, Esq.

Opinion

Respondent Joseph A. Geraci, II ("Geraci") appeals an August 7, 2003 decision of an NASD Hearing Panel. After a review of the entire record in this matter, we affirm the Hearing Panel's findings that Geraci violated Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act"), Securities and Exchange Commission Rule 10b-5, and NASD Conduct Rules 2110 and 2120 by engaging in insider trading. We bar Geraci from associating with any NASD member in any capacity and order him to pay $2,160.83 in hearing costs.

I. Background

Geraci entered the securities industry in 1991 as a general securities representative. Geraci has been associated with several NASD member firms since 1991. Geraci's conduct relevant to this decision occurred during the time when he was associated with Maven Securities, Inc. ("Maven" or the "Firm"), which was from August 2, 1999, to September 15, 2000. He is currently associated with another NASD member firm.

Central to our finding that Geraci engaged in insider trading is the evidentiary issue of the Hearing Panel's adverse credibility finding in response to Geraci's testimony that he traded Minnesota American, Inc. ("MNAC") stock based on his own research. The Hearing Panel gave specific, cogent reasons for its disbelief of Geraci, noting a number of inconsistencies and implausibilities in Geraci's testimony and other evidence, including: (1) that one of Geraci's customers testified that Geraci told him to purchase shares of MNAC because of the company's involvement in a merger, which contradicted Geraci's testimony; (2) that Geraci was inconsistent regarding how he obtained information on the fundamentals of MNAC; (3) that Geraci's given reason for the timing of his trades was implausible because MNAC's dramatic upswing in volume occurred after he placed his order; (4) that it was implausible that Geraci did not learn of the merger given that all the Maven brokers were trading or attempting to trade MNAC, that he had long-established friendships with several of the Maven brokers, and that he worked closely with these brokers in Maven's small office; and (5) that it was implausible that Geraci and his officemate made contemporaneous trades of MNAC and had no knowledge of the merger. It is of considerable importance here that, in making its finding, the Hearing Panel relied upon the uncontroverted testimony of Geraci's customer who discredited Geraci's version of events. As analyzed in detail later in this decision, we too find that, when confronted with these inconsistencies and implausibilities, Geraci's explanations are not convincing.

II. Procedural History

On August 15, 2002, the Department of Market Regulation ("Market Regulation") filed a complaint against Geraci, Thomas D. Krosschell ("Krosschell"), and Troy W. Johnson ("Johnson"), which alleged violations of the antifraud provisions of the Exchange Act and NASD rules. Krosschell and Johnson settled the disciplinary actions against them. A hearing was held on May 7 and 8, 2003, as to the allegations against Geraci. The Hearing Panel found that Geraci engaged in the misconduct as alleged in the complaint. This appeal followed.

III. Facts

This case arose out of Market Regulation's investigation of certain Maven brokers' trading activity regarding common stock of MNAC, a holding company with two subsidiary companies whose product lines included high school memorabilia products and locker organizers. At issue here is whether Geraci traded on material, nonpublic information concerning a reverse merger between MNAC and Berthel Fisher & Co. Financial Services, Inc. ("Berthel Fisher"), a privately held financial services company and broker-dealer, which is headquartered in Cedar Rapids, Iowa.[1]

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[1] In the type of reverse merger at issue here, a privately held company merges with a publicly held "shell" company, thereby rendering the privately held company's stock publicly tradeable. Typically, the public shell company issues a substantial majority of its shares to the private company's shareholders and also turns over board control to the private company's shareholders. The shareholders of the privately held company pay for the shell company and

[Footnote continued on next page…]

A. MNAC Retains Maven as Its Investment Banker

During the first half of 1999, MNAC's stock traded on the Over-the-Counter Bulletin Board with little trading volume or price movement. The average daily trading volume between January and July 1999 was 546 shares. In February 1999, MNAC's Chairman and Chief Executive Officer ("CEO"), Pierce McNally ("McNally"), retained Maven to act as MNAC's investment banker in an effort to garner interest in and bolster the price of MNAC stock. In February 1999, Maven's two principals, Daniel J. Shrader ("Shrader")[2] and Krosschell, entered into a financial consulting agreement with MNAC in which they agreed to advise MNAC regarding the identification and evaluation of new strategic business opportunities, the sale of MNAC's subsidiaries, and the negotiation and financial structure of any transaction between MNAC and a target company. As set forth in the consulting agreement, MNAC agreed to compensate Shrader and Krosschell with 300,000 MNAC warrants, exercisable at $0.30 per share, and a cash payment equal to four percent of the sale price of the two subsidiaries.[3]

B. The Preliminary Reverse Merger Discussions

Prior to discussing a reverse merger with MNAC, Shrader and Krosschell met with Berthel Fisher executives on June 8, 1999, and explained the benefits of Berthel Fisher becoming a public company through a reverse merger with a publicly traded company.[4] After this meeting, Krosschell sent a letter dated June 23, 1999, to the president of Berthel Fisher in which Krosschell reiterated the benefits of a reverse merger and stated that Maven had established relationships with two publicly traded shell corporations interested in a reverse merger involving Berthel Fisher.

Shrader and Krosschell met with MNAC executives on July 7, 1999, and first proposed a reverse merger as a strategic business opportunity for MNAC to pursue. Without revealing the company names, Shrader and Krosschell discussed two private companies as potential reverse merger candidates for MNAC. One of these companies was Berthel Fisher. After the meeting,

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contribute their private company shares to the shell. Upon completion of the reverse merger, the public company's name and ticker symbol are often changed to reflect the name of the original private company.

[2] Shrader was also Maven's president. Shrader settled with NASD a disciplinary action against him.

[3] The warrants had a term of five years.

[4] Berthel Fisher had established a relationship with Maven at some point during the winter of 1998-1999 when Maven sought broker-dealers to sell shares of an Internet-based retailer in a private offering.

McNally authorized Shrader and Krosschell to evaluate reverse merger candidates and locate buyers for the MNAC subsidiaries.

On July 21, 1999, after several conversations with Shrader and Krosschell, the CEO of Berthel Fisher invited the two Maven principals to Berthel Fisher's headquarters in Iowa for meetings with Berthel Fisher's senior management and board of directors on July 29-30, 1999. At the conclusion of the meetings in Iowa, Berthel Fisher provided Shrader and Krosschell with copies of the company's most recent audit and shareholder list. The Berthel Fisher board of directors referred the reverse merger idea to its accounting firm to determine whether the strategy was appropriate for the company.

Two days before this meeting with Berthel Fisher's executives, on July 27, 1999, Krosschell purchased 3,500 shares of MNAC. During his investigative interview with NASD, Krosschell stated that he bought these shares of MNAC because he was encouraged that MNAC was going in a different direction by pursuing a reverse merger and that he believed the price of the shares was reasonable. MNAC's interest in pursuing a reverse merger, however, was not publicly disclosed when Krosschell purchased these shares.

C. The Reverse Merger Discussions Intensify, Geraci Joins Maven, and the Principals Buy MNAC Shares

On August 2, 1999, the next business day after returning from Iowa, Shrader and Krosschell called Berthel Fisher to determine the board of directors' reaction to the proposed merger and inquire as to whether the company was interested in moving forward. Berthel Fisher stated that it was working with its accountants to clarify certain issues. Later that day, Berthel Fisher concluded that the reverse merger could proceed.

Krosschell and Shrader also briefed McNally from MNAC on their two days of meetings in Iowa, but they did not disclose that the meetings were with Berthel Fisher. While speaking with McNally, Shrader and Krosschell raised the issue of buying MNAC stock and adjusting the financial consulting agreement to increase the number of warrants they would receive under the agreement.

On August 2, 1999, contemporaneously with the reverse merger discussions between Maven and Berthel Fisher and Maven and MNAC, Geraci began working for Maven. Prior to joining Maven, Geraci had worked with, resided with, or was an acquaintance of many of the Maven employees. Geraci testified at the hearing to these prior relationships. Geraci stated that he knew Shrader and Krosschell because he previously had handled private placements for Maven. Geraci had worked with two Maven brokers, Isaac Sibley ("Sibley") and Johnson while employed by another firm. For a period of time before Geraci joined Maven, he and Sibley were roommates. Geraci, moreover, had co-owned a bar and restaurant with Johnson. At the hearing, Geraci also described the office configuration at Maven. Geraci shared an office and an order entry computer terminal with Johnson. Krosschell worked in an office adjacent to Geraci and

Johnson's office, while Shrader's office was approximately 50 feet away. Maven had a total of seven employees; all of whom worked at the same location.[5]

Shrader and Krosschell continued discussions with Berthel Fisher throughout the week of August 2, 1999, and ultimately identified MNAC as the public company in the transaction during a telephone conversation with Berthel Fisher executives. Shrader and Krosschell later sent the executives via facsimile a MNAC brochure.[6] In addition, the parties discussed drafting a confidentiality agreement and a letter of intent. Shrader requested that Berthel Fisher provide Maven with several documents, including a copy of a blank confidentiality agreement.

Between Thursday, August 5 and Monday, August 9, 1999, while continuing to negotiate the details of the reverse merger, Shrader and Krosschell purchased a combined total of 104,250 shares of MNAC. Shrader's and Krosschell's purchases accounted for two thirds of the MNAC trading volume during this period.[7] At no point during this period had the reverse merger discussions between MNAC and Berthel Fisher been publicly disclosed.

On August 5, 1999, Shrader and Krosschell each purchased, for their individual accounts at Maven, 25,000 shares of MNAC at a negotiated price of $0.30 per share from McNally and an MNAC director who had opened brokerage accounts at Maven. Krosschell and Shrader stated in their investigative interviews that they had purchased the MNAC shares because they liked the direction that the company was headed and were "reinvigorated" in completing the reverse merger. Krosschell purchased another 5,000 shares of MNAC later that day on the open market. Krosschell further testified that he elected not to exercise any of the MNAC warrants and instead bought on the open market at a higher price per share because the warrants would have been converted to restricted stock that he could not sell for one year.

On August 6, 1999, Shrader and Krosschell purchased additional shares of MNAC on the open market for their personal accounts. Krosschell purchased 14,500 shares, and Shrader purchased 14,000 shares, ranging in price per share from $0.46875 to $0.625.

Shrader and Krosschell made their final purchases of MNAC on August 9, 1999, before restricting their own trading of MNAC. Shrader purchased 18,750 shares of MNAC in the open market for his individual account. The price per share ranged from $0.6875 to $0.75. Shrader also entered two orders to purchase a total of 2,000 shares of MNAC for Krosschell. In total, as of August 9, 1999, Krosschell held 50,000 shares of MNAC and Shrader held 57,750 shares.

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[5] One of the seven Maven employees, Joseph Stansberry ("Stansberry"), worked primarily from home and went into the Maven office approximately twice a month.

[6] Maven's telephone records from August 2-6, 1999, reveal eight telephone calls between Maven and Berthel Fisher.

[7] The total reported volume for these three trading days was 154,750 shares.

Later in the day on August 9, MNAC and Berthel Fisher signed a "Non-Disclosure/Non-Compete Agreement" (the "Confidentiality Agreement"). Under the Confidentiality Agreement, MNAC and Berthel Fisher agreed to keep confidential all information that they exchanged and to refrain from publicly disclosing any information concerning the proposed reverse merger between the two companies. Once the two companies had executed the Confidentiality Agreement, Shrader and Krosschell restricted their own trading in MNAC. Shrader stated during an investigative interview that the signing of the Confidentiality Agreement signified that the companies were serious about moving ahead with the transaction and that it would be inappropriate for him and Krosschell to continue buying MNAC stock. They did not, however, place a Firm-wide restriction on all Maven employees trading MNAC stock until Berthel Fisher and MNAC signed a letter of intent on August 18, 1999.[8] The trading restriction prohibited all Maven employees from buying or selling shares of MNAC.

D. Geraci and Other Maven Brokers Buy MNAC Shares

Each of the brokers who worked on a daily basis at Maven with Shrader and Krosschell purchased or attempted to purchase MNAC stock prior to the public announcement of the reverse merger.[9] Several of these brokers also recommended MNAC stock to family members, friends, and customers of the Firm.

1. Michael Cain

The first Maven broker to buy was Michael Cain ("Cain"). Cain made three purchases totaling 5,200 shares of MNAC on August 9, 1999. Cain's transactions occurred on the same day that Berthel Fisher and MNAC executed the Confidentiality Agreement.[10]

2. Geraci

Two days later, at 9:45 a.m. Eastern Time on August 11, 1999, Geraci bought 5,000 shares of MNAC at prices ranging from $1.63 to $1.75 per share for his personal account at Maven. Geraci also recommended the stock to his girlfriend, KF, and his father, both of whom purchased shares. KF bought 2,000 shares of MNAC in her individual retirement account at Maven on August 11, 1999. Geraci's father purchased 500 shares on August 11, 1999, and 500 additional shares on August 16, 1999, through an on-line broker.

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[8] The letter of intent instructed that the reverse merger was to be finalized by October 1, 1999. In addition, the letter of intent described the share exchange provision between the companies, the corporate name change, and the elimination of the officers and directors of MNAC upon completion of the transaction.

[9] One Maven broker who primarily worked offsite, Stansberry, did not purchase shares of MNAC.

[10] Cain settled with NASD a disciplinary action that arose out of this misconduct.

Geraci also recommended MNAC to two of his Maven customers, SZ and DW. On August 17, 1999, SZ bought 10,000 shares, and DW purchased 8,000 shares. Geraci testified at the hearing that he recommended MNAC to these customers because of the company's fundamentals, the movement of the price, and the trading volume of the stock. He claimed that he did not mention the reverse merger to his customers because he did not know about it himself at that time. DW, however, testified at the hearing and directly contradicted Geraci. DW stated that Geraci recommended MNAC to him because "it was going to be merging with another company," which made it an attractive stock. According to DW, Geraci told him that the price of MNAC would likely increase because of the merger.

Geraci placed orders to purchase MNAC stock on the same days that his officemate, Johnson, purchased MNAC and recommended it to others who purchased it. Geraci testified at the hearing that he did not realize that Johnson was also buying MNAC contemporaneously with Geraci's own purchases and recommendations.

3. Johnson

Johnson, the representative with whom Geraci shared an office and a computer terminal at Maven, purchased shares for himself and recommended MNAC to his parents, two customers, and a friend who all bought shares of MNAC. On August 11 and 17, 1999, Johnson's parents purchased a total of 35,000 shares of MNAC, while, on those same days, one of Johnson's customers, EG, purchased a total of 50,000 shares. On August 16 and 17, 1999, Johnson purchased a total of 25,000 shares of MNAC in his personal Maven account. Johnson recommended MNAC to another of his customers who purchased 19,000 shares on August 17, 1999, and to his friend who purchased 5,000 shares on the same day.

Johnson testified in an on-the-record interview with NASD that, in early August 1999, Krosschell and Shrader suggested that he look at MNAC because the share price would be increasing. Johnson further stated that Shrader and Krosschell told him to look at MNAC approximately a week or two before he bought it.

4. Sibley

Sibley attempted to purchase 1,000 shares of MNAC on August 19, 1999. Sibley's order was never processed, however. Shrader cancelled Sibley's order as a result of the Firm-wide restriction imposed on trading MNAC that was in effect at the time.

5. Stansberry

Stansberry admitted in a stipulation offered at the hearing that in June or July 1999, Krosschell told him that Maven was "working with, or looking to work with" MNAC and that MNAC was a good reverse merger candidate. Stansberry purchased no shares of MNAC, because, as he stipulated, he had no funds to invest. Stansberry subsequently told three

customers about MNAC, and they purchased shares from another firm on August 17 and 18, 1999.

E. Public Announcement of the Reverse Merger and Sale of MNAC Stock

At the suggestion of Shrader and Krosschell, MNAC issued a press release on August 19, 1999, over Business Wire that stated MNAC was "working on a financial transaction involving a reverse merger with a company in the financial services industry." MNAC determined that this press release was necessary because of the increased trading activity and corresponding increased price of MNAC stock over the previous weeks.[11]

On August 25, 1999, prior to the opening of the market, MNAC and Berthel Fisher jointly announced over Business Wire that the companies had executed a letter of intent to merge by October 1, 1999. The announcement further stated that the merger would result in Berthel Fisher becoming a public company and MNAC selling its subsidiaries. MNAC's stock closed on August 25, 1999, at $3.00 per share, an increase of $0.50 from the previous day's closing price, on reported volume of 265,800 shares.

Immediately after the companies issued the letter of intent to merge, Shrader and Krosschell began selling their shares of MNAC. That day, the two Maven principals sold 4,000 shares of MNAC. In addition, between August 26 and September 7, 1999, Shrader sold 15,500 MNAC shares, while Krosschell sold 18,500. Shrader realized a gross profit of $36,000, and Krosschell realized a gross profit of $52,219.

Geraci sold 1,000 shares of MNAC on September 10, 1999. Geraci realized a gross profit of $1,875 and had a gross unrealized profit of $11,000. MNAC announced on September 17, 1999, that the reverse merger negotiations with Berthel Fisher were terminated.

IV. Discussion

After a thorough review of the record, we affirm the Hearing Panel's findings that Geraci recommended and effected the purchase of MNAC stock while in possession of material, nonpublic information, in violation of Section 10(b) of the Exchange Act, SEC Rule 10b-5, and NASD Conduct Rules 2110 and 2120. We find that Geraci engaged in insider trading as a "tippee" when he traded MNAC stock on the nonpublic information that he gained from the Maven principals, Shrader and Krosschell. Shrader and Krosschell, who were engaged in a confidential relationship with MNAC while acting as the company's investment bankers, conveyed information concerning the reverse merger. Geraci, acting with scienter, traded on that

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[11] The closing price and volume of MNAC escalated as follows: August 2, 1999 - $0.28, no volume; August 9, 1999 - $0.88, 53,950 shares traded; August 11, 1999 - $1.33, 523,429 shares traded; August 16, 1999 - $2.03, 195,591 shares traded; and August 19, 1999 - $2.75, 479,705 shares traded.

information and recommended MNAC stock to others prior to a public announcement of the reverse merger negotiations, to the benefit of Shrader and Krosschell as well as himself.

A. Classical Theory of Insider Trading Liability

Section 10(b) of the Exchange Act makes it "unlawful for any person . . . to use or employ, in connection with the purchase or sale of any security . . ., any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe." 15 U.S.C. § 78j (2001). SEC Rule 10b-5 prohibits the use, "in connection with the purchase or sale of any security," of "any device, scheme, or artifice to defraud" or any other "act, practice, or course of business" that "operates . . . as a fraud or deceit."[12] 17 C.F.R. § 240.10b-5 (2004). Trading on the basis of material, nonpublic information violates these antifraud provisions when the trading arises "in connection with" a breach of a fiduciary duty. Dirks v. SEC, 463 U.S. 646, 663 (1983). Market Regulation alleged that Geraci breached a fiduciary duty and violated the antifraud provisions of the securities laws and NASD rules under the classical theory of insider trading.

Under the classical theory, Section 10(b) and SEC Rule 10b-5 are violated when a corporate insider purchases or sells securities of his corporation on the basis of material, nonpublic information. United States v. O'Hagan, 521 U.S. 642, 651-52 (1997). The Supreme Court has found that trading on such information is a "deceptive device" under Section 10(b) because "a relationship of trust and confidence [exists] between the shareholders of a corporation and those insiders who have obtained confidential information by reason of their position with that corporation." Chiarella v. United States, 445 U.S. 222, 228 (1980). The corporate insiders of a company are the company's controlling shareholders, directors, officers, and advisors. See O'Hagan, 521 U.S. at 652. These corporate insiders have a fiduciary duty "to disclose [or to abstain from trading] because of the necessity of preventing a corporate insider from . . . taking unfair advantage of . . . uninformed . . . stockholders." Chiarella, 445 U.S. at 228-29 (internal quotation omitted).

The classical theory of insider trading applies to both temporary insiders and "tippees." See Dirks, 463 U.S. at 655 n.14. Temporary insiders are those individuals such as attorneys, underwriters, accountants, and investment bankers, who temporarily gain access to nonpublic information about the company and become fiduciaries as a result of this temporary relationship. Id. "The basis for recognizing this fiduciary duty is . . . that [temporary insiders] have entered into a special confidential relationship in the conduct of the business of the enterprise and are given access to information solely for corporate purposes." Id.

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[12] Conduct Rule 2120 is NASD's antifraud rule and is the equivalent of Section 10(b) and Rule 10b-5. Market Regulation Comm. v. Shaughnessy, Complaint No. CMS950087, 1997 NASD Discip. LEXIS 46, at *24 (NBCC June 5, 1997), aff'd, Kevin Eric Shaughnessy, 53 S.E.C. 692 (1998).

Tippees are individuals who trade based on nonpublic information gained from insiders. Id. at 660 n.19. A tippee is liable for insider trading if: (1) the tipper possessed material, nonpublic information regarding the corporation; (2) the tipper disclosed this information to the tippee and the tippee traded the corporation's securities while in possession of that nonpublic information provided by the tipper; (3) the tippee knew or should have known that the tipper violated a relationship of trust by conveying the information; and (4) the tipper benefited by the disclosure to the tippee. SEC v. Warde, 151 F.3d 42, 47 (2d Cir. 1998). A tippee has a derivative fiduciary duty to the company's shareholders not to trade the company's stock based on material, nonpublic information provided by the insider. Dirks, 463 U.S. at 660. The central issue for finding a tippee liable for insider trading is whether a tippee knew or should have known that he was trading on improperly obtained inside information. See id.

B. Geraci Is Liable for Insider Trading as a Tippee

1. Shrader and Krosschell Were MNAC Insiders Who Possessed Material, Nonpublic Information

The record overwhelmingly supports, and Geraci does not dispute, that Shrader and Krosschell were temporary insiders at MNAC. Shrader and Krosschell entered into a financial consulting agreement in February 1999 with MNAC to act as consultants and as its investment bankers in an effort to garner interest in and bolster the price of MNAC stock. Toward that end, Shrader and Krosschell located Berthel Fisher as a viable reverse merger candidate and advised MNAC regarding the transaction. Shrader and Krosschell frequently acted as intermediaries between MNAC and Berthel Fisher both in bringing the two companies together and throughout the merger negotiations. Thus, Shrader and Krosschell were insiders by reason of the special relationship they had established with MNAC. See, e.g., SEC v. Ingram, 694 F. Supp. 1437, 1440 (C.D. Cal. 1988) (finding stockbroker who attended critical meetings, advised company on aspects of a merger, and arranged several meetings during the merger negotiations had a special relationship with company and was therefore a temporary insider).

In addition, we find that the potential reverse merger between MNAC and Berthel Fisher was material, nonpublic information. Whether information is material "depends on the significance the reasonable investor would place on the . . . information." Basic, Inc. v. Levinson, 485 U.S. 224, 240 (1988). Information is material "'if there is a substantial likelihood that a reasonable [investor] would consider it important in deciding how to [invest].'" SEC v. Mayhew, 121 F.3d 44, 51 (2d Cir. 1997) (quoting Basic, Inc., 485 U.S. at 231). The information at issue must "have been viewed by the reasonable investor as having significantly altered the total mix of information made available." Basic, Inc., 485 U.S. at 231-32 (internal quotation omitted). In the context of preliminary merger discussions, the Supreme Court held that the materiality of such a transaction depends on a '"balancing of both the indicated probability that the event will occur and the anticipated magnitude of the event in light of the totality of the company activity.'" Id. at 238 (quoting SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 849 (2d Cir. 1968) (en banc), cert. denied, 394 U.S. 976 (1969)). The Supreme Court and other federal courts of appeals have held that even preliminary merger negotiations could be viewed as material, particularly when the corporate entities are small because a merger is a significant

event for a small company. See Basic, 485 U.S. at 238; see also SEC v. Ginsburg, 362 F.3d 1292, 1302 (11th Cir. 2004) ("A merger is an event of considerable magnitude to an investor, and preliminary merger negotiations constitute concrete steps indicating an increasing possibility of a merger occurring."); SEC v. Geon Indus., Inc., 531 F.2d 39, 47-48 (2d Cir. 1976) ("Since a merger in which it is bought out is the most important event that can occur in a small corporation's life, to wit, its death, we think that inside information, as regards a merger of this sort, can become material at an earlier stage than would be the case as regards lesser transactions—and this even though the mortality rate of mergers in such formative stages is doubtless high."); SEC v. Shapiro, 494 F.2d 1301, 1306-07 (2d Cir. 1974) (holding merger negotiations material despite progress of transaction not probable); SEC v. Falbo, 14 F. Supp. 2d 508, 521 (S.D.N.Y. 1998) (deeming nonpublic information regarding a merger of firms material).

Under the facts of this case, we find that on August 11, 1999, the prospect of a reverse merger between Berthel Fisher and MNAC was material information. Because of the nature of the parties involved, a reverse merger would alter the total mix of information available and clearly influence a potential investor's decision to purchase MNAC stock. As of August 11, 1999, the status of the merger negotiations would have been significant to a potential investor in that MNAC stock might increase or decrease in value; thus, the magnitude of this transaction and its potential impact made the merger discussions material information. The significance of the reverse merger and, in turn, its materiality, is also evidenced by the market's reaction to news of this transaction. Shrader stated in an investigative interview that the signing of the Confidentiality Agreement reinforced that the companies were serious about moving ahead with the transaction. After MNAC publicly announced on August 19, 1999, that it was working on a reverse merger with an unnamed company, the price of MNAC shares rose from $2.25 to $2.75. See Elkind v. Liggett & Meyers, 635 F.2d 156, 166 (2d Cir. 1980) (determining materiality by "whether the tipped information, if divulged to the public, would have been likely to affect the decision of potential buyers and sellers"). We conclude that the reverse merger discussions between MNAC and Berthel Fisher were material.

The record amply supports the finding that the reverse merger was also nonpublic information. Shrader and Krosschell handled the details of the merger on behalf of MNAC. Up until the week of August 2, 1999, Shrader and Krosschell had not revealed to either Berthel Fisher or MNAC the identity of the other company involved in the merger discussions. Even after Shrader and Krosschell revealed to MNAC and to Berthel Fisher the identity of the other merging company, the companies limited communicating the information to only a few select executives from each company. Moreover, the Confidentiality Agreement that the companies executed further evidenced the nonpublic nature of the reverse merger. See Ginsburg, 362 F.3d at 1302 (holding as a reasonable inference that merger negotiation was nonpublic as evidenced by a confidentiality agreement). MNAC and Berthel Fisher agreed to keep confidential all information that they exchanged and to refrain from publicly disclosing any information concerning the proposed reverse merger between the two companies. The evidence supports that the merger negotiations were confidential and therefore also nonpublic information. No evidence suggests that the information was public.

In sum, we conclude that Shrader and Krosschell were temporary insiders of MNAC who possessed inside information (i.e., material, nonpublic information) related to the reverse merger between MNAC and Berthel Fisher.

2. Shrader and Krosschell Disclosed the Inside Information to Geraci Which Geraci Used to Trade MNAC's Securities

Geraci challenges Market Regulation's evidence supporting the Hearing Panel's finding that Shrader and Krosschell conveyed to Geraci inside information about the MNAC-Berthel Fisher reverse merger. Geraci contends that he had no conversations with anyone at Maven regarding MNAC around the time when he purchased or recommended the MNAC stock, and because Market Regulation offered no direct evidence that the Maven principals tipped Geraci, its case must fail. We disagree.

Contrary to Geraci's argument, circumstantial evidence is sufficient to prove insider trading and is frequently the only way to adduce evidence of this fraudulent scheme. See, e.g., Warde, 151 F.3d at 48 (holding that circumstantial evidence supported finding of insider trading and pointing to parallel trading as support of the inference); SEC v. Burns, 816 F.2d 471, 474 (9th Cir. 1987) (agreeing that insider trading allegations are "often based on inferences from circumstantial evidence"); Sidney C. Eng, 53 S.E.C. 709, 714 (1998) (rejecting argument that direct evidence must be adduced to sustain a finding of insider trading). "[P]roof of insider trading can well be made through an inference from circumstantial evidence and not solely upon a direct testimonial confession" from the tipper or the tippee. SEC v. Singer, 786 F. Supp. 1158, 1164 (S.D.N.Y. 1992) (internal quotation omitted). The Commission has found that circumstantial evidence may be probative and reliable despite other explanations for an inference. Eng, 53 S.E.C. at 716. Furthermore, minimal information may constitute a tip. Robert Bruce Lohmann, Initial Decision Rel. No. 214, 2002 SEC LEXIS 2380, at *29 (Sept. 19, 2002), aff'd, Exchange Act Rel. No. 48092, 2003 SEC LEXIS 1521 (June 26, 2003); see also Texas Gulf Sulphur Co., 401 F.2d at 848, 852 (calling a security "a good buy" and "recommending" it, when communicated by a person having material, nonpublic information, is a tip and a violation of SEC Rule 10b-5).

We are persuaded that Geraci was tipped with material, nonpublic information. As set forth in detail below, we have considered myriad factors that, when linked together, create a compelling inference that Geraci was tipped about the MNAC-Berthel Fisher reverse merger and that Geraci traded on the basis of that information.

a. Customer Testimony

The single most persuasive and unequivocal piece of evidence is the testimony of Geraci's customer, DW. DW described for the Hearing Panel his first-hand account of a conversation that he had with Geraci concerning MNAC. DW testified that Geraci called him on August 17, 1999, and told him about MNAC. DW stated that Geraci told him MNAC was an attractive stock because it was going to merge with another company. According to DW, Geraci told him that the merger would cause the stock price of MNAC to rise. DW further stated that

Geraci provided no reason for recommending MNAC beyond the anticipated merger. DW also stated that he had never heard of MNAC prior to Geraci calling him. This conversation between Geraci and DW took place two days before MNAC first publicly announced that it was going to be involved in a merger.

DW's testimony, which the Hearing Panel found was reliable, is significant and wholly supports the inference that Geraci was tipped. Outside of Geraci's self-serving testimony, which the Hearing Panel found not credible, DW's recollection of the conversation with Geraci went unchallenged. Whereas DW was a disinterested witness and had no reason to lie, Geraci had substantial motivation to provide tainted testimony throughout these proceedings. We find DW's testimony both credible and persuasive. As with the Hearing Panel, we do not find Geraci's testimony to be credible, which we discuss in further detail below.

b. Relationship with and Access to the Maven Principals and Brokers

Geraci had established a relationship with Shrader while working on Maven's private placements before Geraci joined Maven on August 2, 1999. Geraci testified that the reason he went to work for Maven was his interest in its investment banking business. It appears possible then that the topic of Maven acting as the investment banker for MNAC in the merger transaction would have arisen in conversations between Geraci and Shrader and Krosschell. Geraci, however, denied that anyone at Maven discussed the merger with him or Maven's role in it even though Geraci, with his interest in investment banking, began working for Maven the very week when Shrader and Krosschell were heavily involved in orchestrating the deal between MNAC and Berthel Fisher. Shrader and Krosschell's activities that week included meeting with the MNAC executives in the Maven offices and speaking on the telephone with Berthel Fisher.

In addition, two Maven brokers, Stansberry and Johnson, admitted that Krosschell and Shrader had discussed MNAC with both of them. Stansberry stipulated that in June or July 1999, Krosschell told him that MNAC was a good reverse merger candidate. Stansberry passed this information on to his Maven clients who bought MNAC on August 17 and 18, 1999, as the public announcement of the reverse merger was imminent. Johnson admitted in his investigative testimony that, in early August 1999, Krosschell and Shrader told him to look at MNAC and told him to buy it because it was "moving." Indeed, Johnson, his parents, and several of his customers purchased MNAC stock on August 11, 16, and 17, 1999.

The configuration of the Maven offices and Geraci's testimony regarding the office space support the inference that Geraci had access to information about the reverse merger. The Maven office space was small with Geraci's office adjacent to Krosschell's. Geraci testified that he could hear in his office if someone called to him from the Maven reception area. Geraci could have heard from Krosschell or Shrader about the merger while working in the small confines of Maven, particularly given the significance of the MNAC-Berthel Fisher transaction and the central role that Maven played in facilitating the merger. Cf. Ginsburg, 362 F.3d at 1299 (discussing temporal proximity and stating the "closer in time the trader's exposure to the insider, the stronger the inference that the trader was acting on the basis of inside information").

Geraci had close friendships with two other Maven brokers who also traded or attempted to trade MNAC prior to the public announcement of the reverse merger. Geraci was Sibley's roommate for several years prior to joining Maven. Furthermore, Geraci and Johnson were good friends who co-owned a bar and restaurant in addition to working together at Maven. Geraci also shared an office and computer quote system with Johnson. We view as particularly significant that Geraci's pattern of trading in MNAC paralleled Johnson's MNAC trades. Cf. Warde, 151 F.3d at 48 (discussing parallel trading of speculative security supports inference that insider disclosed material, nonpublic information). Specifically, Geraci and Johnson each made purchases for themselves or others on August 11 and 17, 1999, just prior to the companies signing the letter of intent and the implementation of the Firm-wide restriction on trading MNAC. At one point on August 17, 1999, Geraci and Johnson were entering orders to buy MNAC stock simultaneously—Geraci placed his customers' orders by phone while Johnson entered his orders through their shared computer terminal. This parallel trading activity is especially revealing when juxtaposed with Johnson's admission that Shrader and Krosschell told him to look at MNAC, and he then traded based upon that information.

c. Maven Principals and Brokers Were Trading MNAC

It is undisputed that Krosschell and Shrader were trading MNAC for themselves until August 9, 1999. Indeed, Shrader and Krosschell purchased numerous shares of MNAC during Geraci's first week of employment with Maven. The record shows that together Shrader and Krosschell bought 104,250 shares during the three trading days from August 5 to August 9, 1999. Krosschell admitted in his on-the-record interview with NASD that he was buying MNAC because he was encouraged by the prospect of an MNAC merger.

Despite Shrader and Krosschell's August 9, 1999 restriction of their own trading of MNAC shares, they did not place a Firm-wide restriction on the Maven brokers until sometime around August 17 or 18, 1999, shortly before MNAC released its announcement that it was working on a reverse merger. Shrader and Krosschell knew that the Maven brokers were trading MNAC as evidenced by Krosschell's investigative testimony. Krosschell stated that when it became clear to Shrader and him that MNAC and Berthel Fisher were close to signing a letter of intent, they "ran out" and told the Maven brokers "you have to stop now. . . . [N]o more trading in [MNAC]." By Shrader and Krosschell allowing the Maven brokers to trade MNAC shares until August 17 or 18, 1999, they encouraged the increase in the share price from which they ultimately benefited. Shrader and Krosschell began selling their MNAC shares on August 25, 1999, which was the day MNAC announced its intent to merge with Berthel Fisher.

The pattern of trading activity engaged in by Geraci and his fellow Maven brokers also supports the inference that Geraci was tipped. Cf. Warde, 151 F.3d at 48. Between August 9 and August 17, 1999, Geraci, Johnson, and Cain all bought MNAC stock. Geraci and Johnson each made purchases for themselves or others on August 11 and August 17, 1999. As we discuss in more detail below, several of Geraci's and Johnson's purchases on August 17, 1999, were synchronal and support the inference that Geraci was tipped.

d. Geraci's Stated Reasons for Trading Were Not Credible

The Hearing Panel found that Geraci's stated reasons for his purchases and recommendations of MNAC stock were not credible and that his testimony was totally unbelievable. The initial fact-finder's credibility determinations are entitled to considerable deference, which may only be overcome by substantial evidence. Joseph S. Barbera, 54 S.E.C. 967, 977 n.30 (2000); see also Dane S. Faber, Exchange Act Rel. No. 49216, 2004 SEC LEXIS 277, at *17-18 (Feb. 10, 2004) (stressing that deference is given to initial decision maker's credibility determination "based on hearing the witnesses' testimony and observing their demeanor"). We will not disturb the Hearing Panel's findings here.

Geraci told the Hearing Panel that he discovered MNAC on his own shortly after he began work at Maven. He decided to purchase MNAC in part because he researched the company by reviewing either its annual report or a research report on the company and a price and volume chart for MNAC that he obtained prior to his purchase on August 11, 1999. With respect to the price and volume chart that he stated he viewed prior to his August 11 purchase, he claimed that he might have obtained this information from the Internet. Geraci admitted at the hearing, however, that he was unable to recall any of the details of how or from where he obtained any of the information related to MNAC and that he had no Internet access at Maven. Hence, he conceded that if he wanted to research MNAC at Maven, he "couldn't have" used the Internet.

Geraci further testified that he had not heard any rumors about the MNAC merger, but rather it was MNAC's significant upswing in price and volume that alerted him to the stock. Geraci stated that he frequently invested in companies that displayed a "hockey stick" formation on a price and volume chart. According to Geraci, these companies demonstrate a period of level trading volume and then trend upward at about a 45-degree angle. The record belies Geraci's purported explanation for his trading. Geraci purchased 5,000 shares of MNAC on August 11, 1999, at 9:45 a.m. Eastern Time. MNAC's trading volume on August 5, 6, 9, and 10, 1999, was relatively flat with 64,000 shares, 37,000 shares, 54,000 shares, and 74,000 shares trading respectively.[13] Geraci is correct that MNAC saw a significant spike in its volume when more than 500,000 shares were traded on August 11, 1999. However, this upswing and purported hockey stick formation could not have factored into his decision to purchase MNAC because the stock's dramatic activity came after Geraci placed his order on August 11, 1999. Thus, the record contradicts Geraci's explanation because, when he bought MNAC, only the price had increased but not the volume. We reject Geraci's explanation as a fabrication to conceal insider trading as his true reason for investing in MNAC. See SEC v. Moran, 922 F. Supp. 867, 893 n.20 (S.D.N.Y. 1996) (acknowledging that tippees often manufacture "cover stories" to conceal insider trading).

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[13] August 7, and 8, 1999, were weekend days and therefore no trading occurred.

Geraci disputed that any employee of Maven (or anyone outside of Maven) relayed confidential information to him about the reverse merger. We find this testimony beyond credulity given the totality of the facts, including that all of the Maven brokers in the office were actively trading or attempting to trade MNAC, Geraci's interest in investment banking, the close proximity of Geraci's office to the principals' offices, and his long-established friendships with Shrader, Krosschell, Sibley, and Johnson. It is implausible that Geraci and the other Maven brokers each purchased MNAC shortly before the public announcement of the reverse merger without discussion among one another while the two principals of the Firm were coordinating details of the merger. Furthermore, the uncontroverted testimony of Geraci's customer, DW, readily supports the inference that Geraci traded MNAC stock because he knew that MNAC was going to be involved in a merger. Geraci asks us to believe that he also had no knowledge of any of the MNAC purchases made by Shrader, Krosschell, Cain, or Johnson despite the fact that they worked together in Maven's small office. Indeed, Geraci admitted at the hearing that "[e]verything in that office space was close to each other" and that if someone called to him from the Maven reception area, he would have heard it in his office. Most notably, Geraci and Johnson shared an office and a computer terminal, and their desks were a few feet from one another. Geraci also testified that he could overhear Johnson's telephone conversations with his clients. The evidence of his and Johnson's contemporaneous MNAC trades executed on August 17, 1999, undercuts Geraci's denial of knowing anything about the MNAC-Berthel Fisher merger. The timing of these trades was as follows: At 12:23 p.m.,[14] Johnson entered an order through the shared computer terminal to buy MNAC. One minute later, at 12:24 p.m., Geraci entered an order by telephone to buy MNAC for his customer SZ. Johnson entered another order to buy MNAC via the shared computer terminal at 12:44 p.m. At 12:45 p.m., Geraci entered an order by telephone for customer DW to buy MNAC. Geraci avers that these purchases were purely serendipitous. We think not. We believe that Geraci has not offered a credible—or even a remotely believable—reason for his trading and that the Hearing Panel aptly rejected Geraci's testimony as beyond belief.

* * * *

We conclude that the testimony elicited throughout these proceedings, together with the documentary evidence in the record, establish by a preponderance of the evidence that Shrader and Krosschell relayed the confidential information either directly or indirectly to Geraci, as well as other Maven brokers, regarding the potential reverse merger, and that Geraci traded MNAC stock and recommended MNAC stock to others based upon that material, nonpublic information.

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[14] We have shown the times for Geraci's and Johnson's trades entered on August 17, 1999, in Eastern Time. Maven's clearing firm, located in Scottsdale, Arizona, provided the record evidence from which this data is culled and noted the order entry times in Mountain Time.

3. Geraci Acted with Scienter

Geraci disputes the Hearing Panel's finding that he knew or should have known that Shrader and Krosschell were acting as MNAC's investment bankers and thus violated a relationship of trust to the company. We disagree and uphold the Hearing Panel's finding that Geraci acted with the requisite scienter when he traded MNAC stock.

The Supreme Court has defined scienter for purposes of securities fraud cases as "a mental state embracing intent to deceive, manipulate, or defraud." Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 n.12 (1976). A tippee who knows or is reckless in not knowing that he was trading on nonpublic information acts with scienter. Dirks, 463 U.S. at 660; see also SEC v. Maio, 51 F.3d 623, 634 (7th Cir. 1995) (stating tippee has duty not to trade when he "knew or should have known that [tipper's] disclosure was improper"). A finding of scienter is not limited to those persons who have direct contact with the original tipper. SEC v. Ferrero, No. IP91271C, 1993 U.S. Dist. LEXIS 21379, at *37 (S.D. Ind. Nov. 15, 1993), aff'd sub nom. Maio, 51 F.3d 623. Even if Geraci was one tippee in a chain of tippees, we may find that Geraci acted with scienter if he knew or was reckless in not knowing that he was trading on improperly obtained information. See Maio, 51 F.3d at 633; SEC v. Musella, 678 F. Supp. 1060, 1062 (S.D.N.Y. 1988). A confluence of factors demonstrates that Geraci acted with the requisite scienter.

First, Geraci's long-established relationships with Krosschell and Shrader, as well as with Maven brokers Johnson and Sibley, provide for the inference that Geraci knew that Krosschell and Shrader were acting as MNAC's investment bankers in August 1999 and, accordingly, stood in a position of trust with respect to MNAC. See Warde, 151 F.3d at 48 (inferring from friendship that tippee had knowledge of insider's breach of duty to corporation). Geraci testified that he knew Shrader and Krosschell had previously engaged in investment banking business, that "the firm was an investment banking firm," and that Geraci wanted to work for Maven because it was an investment banking firm. Once Geraci began working for Maven, the office configuration and small size provided Geraci with access to Krosschell and Shrader during the height of the merger negotiations with MNAC. The record demonstrates that several meetings between MNAC executives and Shrader and Krosschell took place at Maven. In addition, Geraci's office was adjacent to Krosschell's office. Geraci, moreover, testified that the close quarters at Maven allowed for him to hear if someone called to him from the reception area. Geraci also acknowledged his friendship with Johnson, with whom he shared an office at Maven and owned a bar and restaurant, and with Sibley, who was his former roommate. Under these circumstances, we believe that through Geraci's friendships and business relationships he was told of Shrader and Krosschell's investment banking business with MNAC.

Second, Geraci has been in the industry as a registered representative since 1991. A representative's experience in the industry, in combination with other factors, may support a showing that a party acted with scienter. Ingram, 694 F. Supp. at 1441. At the time Geraci traded the MNAC stock in August 1999, he had eight years of securities industry experience. He knew or was reckless in not knowing that the information that he learned at Maven regarding the MNAC-Berthel Fisher merger was confidential and that trading on such material, nonpublic information was a breach of duty to MNAC. See, e.g., Eng, 53 S.E.C. at 719 (finding that broker

with lengthy experience acted recklessly by trading on information provided by company insider).

Third, Geraci's advice to his father, girlfriend, and clients to purchase MNAC prior to the August 19, 1999 merger announcement illustrates that Geraci was cognizant of the importance of the reverse merger discussions to MNAC. See SEC v. Blackman, No. 3:99-1072, 2000 U.S. Dist. LEXIS 22358, at *22-23 (M.D. Tenn. May 31, 2000) (rejecting motion to dismiss and finding alleged facts supported finding that defendants acted with scienter as illustrated by recommendation to friends and client to purchase stock before public announcement of merger). Geraci's adroitly timed recommendations of MNAC stock to others "manifest[s his] awareness of the timeliness of this information." See id. at *23. Indeed, customer DW's testimony establishes Geraci's awareness that the merger was a significant event in that he recommended MNAC to DW because the company was going to be involved in a merger and the share price would increase as a result.

Finally, from the high degree of materiality of the reverse merger information, we can surmise that Geraci was aware, or was reckless in not knowing, that Shrader and Krosschell were breaching a duty to MNAC by revealing the reverse merger information before the public announcement. See Ingram, 694 F. Supp. at 1441 n.5. We have already stated that the merger was paramount to MNAC's business strategy and, therefore, highly material. "[A]s the materiality of the information increases, the more likely the [tippee] is aware that [the insider] is conferring a benefit or breaching a duty." Id.

Thus, when viewing several factors in the aggregate, the evidence establishes a compelling inference that Geraci knew or, at a minimum, was reckless in not knowing that he was trading on inside information. We find that a preponderance of the evidence proves that Geraci acted with scienter.

4. Geraci's Trading Activity Benefited Shrader and Krosschell

To establish liability, Market Regulation need not show that Shrader and Krosschell received a direct benefit from Geraci's trading. SEC v. Yun, 327 F.3d 1263, 1270 (11th Cir. 2003). Rather, Market Regulation has to prove that Shrader and Krosschell merely intended to benefit themselves by disclosing the confidential information to Geraci and the others at Maven. See Dirks, 463 U.S. at 664. The Supreme Court has construed the "benefit" requirement expansively. See id. Among other examples, the Court provided an "actual pecuniary gain" to the insider or when an insider "makes a gift to a trading relative or friend" as sufficient to create a benefit to the tipper. Id.; see also Warde, 151 F.3d at 49 (holding close friendship between tipper and tippee demonstrated that insider intended to benefit by gifting insider information to his friend).

In this case, the evidence establishes that Shrader and Krosschell intended to receive an actual pecuniary gain by disseminating the confidential information to Geraci and the other Maven brokers. The Maven principals had together amassed an MNAC holding of more than 100,000 shares by the time they restricted their own trading on August 9, 1999. Knowing that

purchases by others would drive up the price of MNAC and thereby increase their own profits, Shrader and Krosschell told at least two of the Maven brokers significant information related to MNAC. Johnson testified that he was told by Shrader or Krosschell to look at MNAC because the stock was "moving." Stansberry stipulated that Krosschell told him MNAC was a good reverse merger candidate and that Maven was looking to work with the company.

In furtherance of their intent, Shrader and Krosschell did not restrict the Maven brokers from trading MNAC until shortly before a public announcement of the merger. Moreover, Shrader and Krosschell benefited from their breach of fiduciary duty to MNAC by gifting the merger information to Maven's brokers. We find that Shrader and Krosschell intended to reap a benefit from the disclosure of the confidential information that they gleaned from their positions as fiduciaries to MNAC, and as such, Geraci inherited the duty to either publicly disclose information related to the merger or abstain from trading based upon it.

* * * *

In sum, we find that Geraci violated the antifraud provisions of the federal securities laws and NASD rules as alleged in the complaint by trading MNAC stock based upon material, nonpublic information conveyed to him by fiduciaries of MNAC.

V. Sanctions

For Geraci's violation of Section 10(b) of the Exchange Act, SEC Rule 10b-5, and NASD Conduct Rules 2110 and 2120, the Hearing Panel imposed a $15,000 fine and barred Geraci from association with any NASD member in any capacity. For the reasons discussed below, we affirm the order of a bar. In light of the bar, we find it appropriate to eliminate the fine.

While the NASD Sanction Guidelines do not provide recommended sanctions specific to insider trading violations, the Guideline for intentional or reckless misrepresentations or omissions of material facts under NASD Rules 2110 and 2120 recommends a fine of $10,000 to $100,000, and a suspension of 10 business days to two years.[15] In an egregious case, the Guideline recommends a bar.[16]

Geraci argues that it was inappropriate for the Hearing Panel to sanction him as severely or more severely than the other respondents who engaged in this misconduct involving MNAC, but who settled the matter with NASD thereby forgoing a hearing. We disagree. The sanctions imposed in settled matters are not relevant to Geraci's misconduct here. "It is well recognized that the appropriate sanction depends upon the facts and circumstances of each particular case and cannot be determined precisely by comparison with actions taken in other proceedings or

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[15] Sanction Guidelines (2001 ed.) at 96 (Misrepresentations or Material Omissions of Fact).

[16] Id.

against other individuals in the same proceeding." Christopher J. Benz, 52 S.E.C. 1280, 1285 (1997); see Butz v. Glover Livestock Comm'n Co., 411 U.S. 182, 187 (1973). Moreover, as Geraci acknowledges, he exercised his right to a hearing whereas the other respondents did not. In settled cases, the parties forgo the cost of litigation and often agree to lesser sanctions; this is well recognized as a "settlement discount."[17] See Dep't of Enforcement v. Belden, Complaint No. C05010012, 2002 NASD Discip. LEXIS 12, at *27 (NAC Aug. 13, 2002), aff'd, 2003 SEC LEXIS 1154 (May 14, 2003); see also Howard R. Perles, Exchange Act Rel. No. 45691, 2002 SEC LEXIS 847, at *34 (Apr. 4, 2002) (noting that "pragmatic considerations justify lesser sanctions in negotiated settlements"). We reject Geraci's argument as not relevant and without merit.

Insider trading is an extremely serious violation and warrants significant sanctions. See Martin B. Sloate, 52 S.E.C. 1233, 1236 (1997); Lohmann, 2002 SEC LEXIS 2380, at *39. Geraci's misconduct is totally at odds with the integrity required of securities industry professionals. As the Commission has affirmed, "[i]nsider trading constitutes clear defiance and betrayal of basic responsibilities of honesty and fairness to the investing public." Eng, 53 S.E.C. at 722 (ordering a respondent barred for engaging in insider trading to best protect the public and the integrity of the securities markets). We believe that barring Geraci is necessary given the seriousness of the violation and Geraci's total lack of candor. See id. (identifying a respondent's lack of candor when testifying before NASD as an aggravating factor in support of significant sanctions). We believe that Geraci's demonstrated indifference to the securities laws and NASD's rules poses a serious risk to the investing public.

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[17] Geraci cites several criminal cases to bolster his argument that he received excessive sanctions because he exercised his right to a hearing and in turn was selectively prosecuted. These cases are inapposite to NASD proceedings. In any event, there is no evidence to support Geraci's contention. In order to support a claim of selective prosecution, Geraci must establish that he was singled out for enforcement action while others who were similarly situated were not and that his prosecution was motivated by an arbitrary or unjust consideration such as race, religion, or a constitutionally protected right. See Robert Tretiak, Exchange Act Rel. No. 47534, 2003 SEC LEXIS 653, at *34 (Mar. 19, 2003). Geraci has made no such showing and there is no evidence in the record to support his assertion. To the contrary, NASD disciplined Shrader and Krosschell and each of the Maven brokers who purchased MNAC stock in August 1999.

Accordingly, we affirm Geraci's bar in all capacities. In light of the bar, we find it appropriate to eliminate the $15,000 fine. Geraci is also ordered to pay hearing costs of $2,160.83. Geraci's bar is effective upon the issuance of this decision.[18]

On Behalf of the National Adjudicatory Council,

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Barbara Z. Sweeney, Senior Vice President
and Corporate Secretary

[18] We have considered and reject without discussion all other arguments of the parties.

Pursuant to NASD Procedural Rule 8320, any member that fails to pay any fine, costs, or other monetary sanction imposed in this decision, after seven days' notice in writing, will summarily be suspended or expelled from membership for nonpayment. Similarly, the registration of any person associated with a member who fails to pay any fine, costs, or other monetary sanction, after seven days' notice in writing, will summarily be revoked for nonpayment.