BEFORE THE NATIONAL ADJUDICATORY COUNCIL

NASD

In the Matter of Department of Enforcement, Complainant, vs. J. Alexander Securities, Inc. Los Angeles, CA, Richard Newberg Golden Beach, FL, James Alexander Los Angeles, CA, Respondents.	DECISION Complaint No. CAF010011 Dated: June 14, 2005

The Hearing Panel found that branch office manager engaged in manipulative activities, sold unregistered securities, maintained outside securities accounts and engaged in outside business activities without providing the proper notice of either to his firm, and provided false testimony in an investigative interview. Held, findings and sanctions affirmed.

Firm's president failed to provide adequate supervision and was responsible for the Firm's deficient written supervisory procedures. Held, findings affirmed and sanctions modified.

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Appearances

For the Complainant Department of Enforcement: Jonathan Golomb, Esq.

For the Respondents: Richard Friedman, Esq.

Opinion

Pursuant to Procedural Rule 9311, Richard Newberg ("Newberg") appealed a September 3, 2003 Hearing Panel decision, and the Department of Enforcement ("Enforcement") cross-appealed the Hearing Panel's decision not to impose monetary sanctions against Newberg. J. Alexander Securities ("Alexander Securities" or "the Firm") and James Alexander ("Alexander") also appealed the Hearing Panel's decision.

We affirm the Hearing Panel's findings that Newberg: (1) participated in the sale of unregistered securities (cause one); (2) engaged in manipulative activity (cause two); (3) failed to disclose outside securities accounts (cause five); (4) failed to disclose outside business activities (cause six); and (5) testified falsely in his on-the-record testimony (cause seven). We also affirm the Hearing Panel's findings that Alexander failed to supervise Newberg adequately (cause eight) and that he failed to establish, maintain, and enforce adequate written supervisory procedures (cause nine). Furthermore, because we find Newberg liable for manipulative activity under cause two, we affirm the Hearing Panel's dismissal of the alternative allegation under cause three that Newberg aided and abetted manipulative trading activity.

As to sanctions, we affirm the Hearing Panel's imposition of a bar against Newberg for the unregistered securities, manipulative activity, and false testimony violations. We also affirm the Hearing Panel's decision to impose a fine of $90,000 against Alexander, but modify the Hearing Panel's imposition of a 90-day suspension in all capacities against Alexander by increasing the length of the suspension to one year in all capacities. Finally, we also affirm the Hearing Panel's imposition of joint and several hearing costs against Newberg and Alexander, and we impose appeal costs against them, joint and several.

I. Background

Alexander Securities is, and was during the relevant period, a registered broker-dealer and member of NASD, with its principal place of business and headquarters in Los Angeles, California. The Firm has been a member of NASD since January 17, 1979. At the time of the allegations in this matter, Alexander Securities had its principal office in Los Angeles and operated a branch office in Aventura, Florida and two other offices in California.

Alexander, the owner of Alexander Securities, became registered as a general securities representative and general securities principal in May 1979, at the same time that he became associated with Alexander Securities. Alexander is, and was at all times during the relevant period (from mid-1996 through December 1998), the president of Alexander Securities. Alexander Securities presently is not conducting a securities business, and Alexander currently is not associated with another member firm.

Newberg entered the securities industry in 1967. He joined Alexander Securities in 1995 and was registered as a principal and general securities representative at the Firm until August 2004. Newberg was the manager and principal in charge of the Firm's Aventura office during the relevant period. Newberg is presently not associated with a member firm.

II. Procedural History

On April 10, 2002, the Department of Enforcement ("Enforcement") filed a nine-cause Amended Complaint against Alexander Securities, Alexander, Newberg, and Dennis Sturm ("Sturm"), a former trader at the Firm's Aventura office. The Hearing Officer granted Sturm's request to have his case severed from that of his co-respondents. Sturm eventually settled with Enforcement. The proceeding went to hearing against the Firm, Newberg, and Alexander. On October 18, 2004, subsequent to the filing of Alexander Securities' appeal in this matter, the Firm filed a voluntary petition in bankruptcy, under Chapter 11 of the Bankruptcy Code. As a result, the appeal proceedings against Alexander Securities are stayed under the automatic stay provision of the Bankruptcy Code, 11 U.S.C. §362(a) (2005). The automatic stay provision does not extend to non-debtors, including co-defendants and owners. <u>Seiko Epson Corp. v. Nu-Kote Int'l</u>, 190 F.3d 1360, 1364 (Fed. Cir. 1999). Therefore, these proceedings are not stayed against Alexander.

As noted, on September 3, 2003, the Hearing Panel made findings of violations against the Firm, Newberg, and Alexander. The Hearing Panel's findings against Alexander Securities are not at issue in this proceeding and are stayed until such time as the automatic stay under the Bankruptcy Code is lifted.[1]

III. Facts

This matter involves transactions in the securities of 29 Florida corporations that had no business operations, known as shell corporations ("Shell Companies"). Eric Littman ("Littman"), a Florida attorney who had known Newberg since 1983 and was a friend of his, reinstated incorporation with the State of Florida for most of the Shell Companies and formed new corporations that he incorporated in Florida with respect to some of the Shell Companies. Littman prepared minutes of Board meetings and issued minority interests to approximately 20

[1] The Hearing Panel found that Alexander Securities: (1) engaged in sales of unregistered securities; (2) engaged in manipulative activity; (3) filed false information under Section 15(c) of the Securities Exchange Act of 1934 ("Exchange Act") and SEC Rule 15c2-11; (4) failed to supervise adequately; and (5) failed to have adequate written supervisory procedures.

to 30 stockholders per Shell Company. A majority of these initial minority stockholders had connections to Littman, Newberg, and Sturm.[2] Most of the minority shareholders received their shares as gifts, while others paid a nominal fee for the shares. A majority of the controlling interests in the Shell Companies were held by Littman or by individuals connected to him, Newberg, or Sturm.[3]

Newberg and Sturm admitted assisting Littman locate Shell Companies. Newberg testified that he sold Littman a Shell Company that he thought might have been one of the 29 Shell Companies at issue in this matter.[4] Newberg and Sturm also admitted providing Littman with names of prospective candidates who were interested in serving as shareholders for Shell Companies.[5]

After the Shell Companies were established and the shares distributed to the minority shareholders, Littman arranged with Alexander Securities, through Sturm and Newberg, to have the Shell Companies listed on the over-the-counter Bulletin Board ("OTC Bulletin Board") so that trading could begin. Littman testified in his on-the-record interview before the SEC that his purpose in listing the shares of the Shell Companies on the OTC Bulletin Board was to make them "valuable" to other companies that eventually would purchase them for "anywhere between

2 Fifty-eight of 761 initial minority shareholders were persons who had a direct connection to Newberg. An additional 290 minority shareholders had associations with the Aventura office through Kevin Brodsky, who was a trader there, and his family (with which Newberg had a long-standing relationship), Brodsky's son's wife's family, and Sturm.

3 Specifically, the controlling shareholders, and the number of Shell Companies they controlled, are as follows: (1) Littman (11); (2) NS, Newberg's sister (four); (3) LS, the husband of NS (one); (4) IS, the nephew of Newberg (one); (5) SB, the brother of Alexander Securities trader Keith Brodsky ("Brodsky") (one); (6) MB, an attorney who represented Littman (four); (7) MK, an attorney who shared space with Littman (three); (8) SH, who was a friend of Sturm (one); (9) LA, a friend of Littman (one); (10) RH, Sturm's sister (one); and (11) RM, whose relationship to Newberg, Sturm, or Littman is unknown (one).

4 Newberg initially denied in his on-the-record interview knowing whether Littman was involved in forming any of the Shell Companies: "What [Littman] does, I do not know, and what companies he forms, I do not know." Newberg acknowledged later in the hearing, however, that he was aware through his conversations with Sturm that Littman had formed some of the Shell Companies at issue here.

5 Although Newberg denied specifically arranging for shareholders of the Shell Companies, he testified that it was possible he informed Littman on "maybe an occasion" about individuals he thought, "might want to purchase . . . stock in one of these situations." Newberg admitted that seven names out of 27 that are included on a shareholder list in the record were in his handwriting. Newberg testified that he supplied the names in response to Sturm's inquiry about whether he knew anyone "that would be interested in purchasing the public companies that Eric [Littman]" might be "putting together."

$120,000 and [$250,000]." For each Shell Company, Alexander Securities filed an application with NASD, as required under SEC Rule 15c2-11 (known as a "Form 211"), seeking clearance to list the Shell Company securities on the OTC Bulletin Board.[6]

Once NASD cleared the shares of the 29 Shell Companies for trading, many of the minority shareholders began selling their shares to Alexander Securities through two brokerage firms with which Newberg and Sturm had associations: (1) First Security Investment Corp., later known as First Security Investments ("FSIC"); and (2) Litwin Securities, Inc. ("Litwin Securities"), a firm that Shochet Securities, Inc. purchased during the period under review (referred to herein as "Litwin/Shochet").[7]

After purchasing the Shell Company shares, Alexander Securities subsequently re-sold the shares to a group of entities domiciled in the Cayman Islands that also maintained securities accounts at Litwin/Shochet ("Cayman Islands Accounts").[8] The sales of shares to the Cayman Islands Accounts occurred on the same dates or within several days of the date of the purchases, or, in some cases, several weeks after the purchases. Additionally, the sales generally involved the same or similar number of shares that Alexander Securities had purchased and were effected at prices similar to those Alexander Securities had paid to the minority shareholders. Robert Oosterwyk ("Oosterwyk"), a Cayman Islands resident who had connections to both Newberg and Sturm, had the trading authority for the Cayman Islands Accounts.[9]

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6 Although Sturm handled most of the work associated with the preparation and filing of the Forms 211, Newberg testified that he reviewed the filings when Sturm was not available. With respect to two of the forms, Newberg notarized signatures on the papers accompanying the filings. He also signed off on certain amended Forms 211 that purportedly reflected trade prices.

7 Sturm worked at Litwin Securities from April 1992 to May 1997, as a general securities representative and a general securities principal. The owner of the Firm, Richard Litwin ("Litwin"), testified that Newberg and Sturm referred customers to him and that his firm directed its OTC Bulletin Board trades to the Firm's Aventura office. He stated that he usually dealt with Newberg on the OTC Bulletin Board transactions that he directed to Alexander Securities. Additionally, two companies with which Newberg was affiliated maintained brokerage accounts at Litwin/Shochet: Dale Financial Consulting Services ("Dale Financial") (a purported financial consulting business that Newberg's wife owned) and Sturm & Newberg, L.P. (a business that Newberg and Sturm owned). Six of the minority shareholders maintained securities accounts at FSIC. Sturm, Dale Financial, and one of the Cayman Islands Accounts also held accounts at FSIC. Sturm testified that he referred people to FSIC "all the time."

8 The five companies that were located in the Cayman Islands and traded shares of the Shell Companies were: Derco Ltd. ("Derco"), Redco Financial, Ltd. ("Redco"), Greenvale Holdings ("Greenvale"), Wyn Investments ("Wyn"), and Securities International, Ltd. ("Securities International").

9 Although Newberg and Sturm each acknowledged knowing Oosterwyk, they denied being aware that the other knew him despite evidence of a Federal Express receipt that Sturm addressed to Oosterwyk and Newberg had signed. Newberg testified that he met Oosterwyk in

[Footnote continued on next page…]

Other market makers eventually came into the market. At about the time that the price of the Shell Company shares began to rise, the companies were sold, in accordance with Littman's plans. The Cayman Islands entities sold the shares they had accumulated for total profits of $805,150.38.[10]

In December of 1998, Newberg deposited a $300,000 check from Littman into the bank account of a company known as "Sturm & Newberg, L.P." Newberg testified that the $300,000 deposit was money that Littman owed to Sturm, and that he did not know why Sturm was entitled to the funds. The deposit slip was in Newberg's name.

IV. Discussion

A. Newberg Engaged in Manipulative Trading Activity

The SEC has held that manipulation is "'the creation of deceptive value or market activity for a security, accomplished by an intentional interference with the free forces of supply and demand.'" Howard R. Perles, Exchange Act Rel. 45691, 2002 SEC LEXIS 847, at *15 & n.14 (Apr. 4, 2002) (quoting Swartwood, Hesse, Inc., 50 S.E.C. 1301, 1307 (1992)). To establish that an individual has engaged in manipulative practices in violation of Section 10(b) of the Exchange Act and SEC Rule 10b-5, there must be proof that the individual acted with scienter.[11]

The U.S. Supreme Court has stated that manipulation is often accomplished through a myriad of devices, including matched orders. Ernst & Ernst v. Hochfelder, 425 U.S. 185, 205 n.25 (1976). "'Matched' orders are orders for the purchase/sale of a security that are entered with the knowledge that orders of substantially the same size, at substantially the same time and price,

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the 1980s in the Cayman Islands, and that he developed a social relationship with him. Oosterwyk was a representative of Thunder Bay Finance Co., Ltd. ("Thunder Bay"), an entity from which Newberg admitted having received mortgage advances on his personal residence. The mortgage advances totaled $1,930,000 between March 1996 and January 1998. Thunder Bay shared the same mailing address with the five companies comprising the Cayman Islands Accounts -- P.O. Box 1068, Grand Cayman. Sturm also knew Oosterwyk. Sturm testified that while he was employed at Litwin Securities he was the registered representative that handled the accounts of a number of companies for which Oosterwyk served as director, including Derco and Wyn.

[10] A few of the Cayman Islands Accounts sold their Shell Company shares at a loss; others did not sell certain Shell Company shares during the period under review.

[11] The Supreme Court has defined scienter as a "mental state embracing intent to deceive, manipulate or defraud."[11] Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976). Scienter also may be established through reckless conduct. Hollinger v. Titan Capital Corp., 914 F.2d 1564 (9th Cir. 1990).

have been or will be entered by the same or different persons for the sale/purchase of such security." Id. As the SEC has noted previously, "[t]he purpose of this illicit practice is to give investors and market participants the false impression that there is interest in the stock." Howard R. Perles, 2002 SEC LEXIS 847, at *15. "Proof of a manipulation almost always depends on inferences drawn from a mass of factual detail." Pagel, Inc., 48 S.E.C. 223, 226 (1985), aff'd Pagel, Inc. v. SEC, 803 F.2d 942 (8th Cir. 1986).

We find by a preponderance of the evidence that Newberg was involved in manipulative activity. The circumstantial evidence shows that Newberg and Sturm participated in the initial stages of the manipulation by helping Littman find shell companies and shareholders for those companies. Newberg and Sturm also served a critical role in the manipulation by having the Forms 211 filed with NASD so that the Shell Companies, which had no business operations or value, could begin trading on the OTC Bulletin Board. Once the Shell Companies were cleared for trading, some of the minority shareholders with connections to Littman, Newberg, and Sturm, and a few unidentified customers at other firms, began selling their stock to Alexander Securities. The evidence shows that during the initial stages of trading Alexander Securities made 17 calls to minority shareholders who had connections to Littman, Newberg, or Sturm. We consider this to be circumstantial evidence that Newberg or Sturm directed certain of the minority shareholders to start trading their shares to ensure that Alexander Securities would have shares available to sell to the Cayman Islands Accounts. The evidence shows that many of the minority shareholders started selling shares to Alexander Securities during the same period and at similar prices to one another. Alexander Securities was the initial market maker in all 29 issues, and it handled nearly all of the trading volume during this initial period that preceded the entry of other market makers into the market.

Alexander Securities, through Newberg,[12] then sold substantially the same number of Shell Company shares at prices similar to those at which Alexander Securities purchased them to the Cayman Islands Accounts. The sales to the Cayman Islands Accounts occurred at different time intervals, sometimes immediately after the purchases, but other times days or weeks later. The circumstantial evidence suggests that this pattern of trading was designed to evade regulatory scrutiny. Further, in many instances, the sales to the Cayman Islands Accounts occurred on the same days on which Oosterwyk received telephone calls from Alexander Securities.[13] The purchases and sales set forth below, which occurred in relatively close proximity to each other, are evidence of "matched" trades:

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[12] Newberg was in charge of the proprietary account through which the trades were effected and made most of the trading decisions for it, although Sturm made trading decisions in Newberg's absence.

[13] With respect to the Cayman Islands Accounts, we find a preponderance of circumstantial evidence linking Newberg and Sturm with those accounts. Alexander Securities made 360 telephone calls to Oosterwyk (who had trading authority over the Cayman Islands Accounts) during the relevant period. Newberg offered no explanation for the calls. Moreover, Newberg had received mortgage loans from Oosterwyk totaling $1.9 million. There is also evidence that Newberg and Sturm took steps to conceal their affiliation with the Cayman Islands entities given

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Date of Transaction	Company	Seller(s)	Number of Shares Bought by Alexander Securities	Price Per Share	Date Shares Re-sold to Cayman Islands Accounts by Alexander Securities	Number of Shares Sold	Re-sale Price Per Share
07/17/1998	Arngre, Inc.	Sturm's aunt	1,000	$.50	07/20/1998 (the next business day)	1,000	$.52
07/20/1998	Arngre, Inc.[14]	Sturm's friend and two unidentified customers of another broker-dealer	4,000	$.50	07/20/1998 (minutes later)	4,000	$.52
06/12/1998	Coffeeworks, Inc.	Sturm's friends and a friend of Littman	6,000	$.25	06/12/1998 (one hour later)	6,000	$.28125

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their refusal to provide NASD Enforcement staff with the necessary authorization to obtain information from the entities located in the Cayman Islands.

14 Oosterwyk received a telephone call from Alexander Securities on July 20, 1998 at 12:16 p.m. One of the Cayman Islands entities then bought the 5,000 shares later the same day at 3:49 p.m.

Date of Transaction	Company	Seller(s)	Number of Shares Bought by Alexander Securities	Price Per Share	Date Shares Re-sold to Cayman Islands Accounts by Alexander Securities	Number of Shares Sold	Re-sale Price Per Share
06/17/1998	Coffeeworks,[15] Inc.	Another firm that had earlier purchased shares from a friend of Littman	4,000	$.35	06/17/1998 (one minute later)	4,000	$.375
08/05/1998	Computer Vending Inc.[16]	A friend of Newberg and a former secretary for Sturm	4,000	$.25	08/06/1998 (the next morning, following an afternoon purchase)	4,000	$.26
05/21/1997	Create-a-Basket, Inc.	Sturm's friends and former secretary	40,000	$.05	05/21/1997 (two hours later)	40,000	$.06
06/02/1998	First Geneva Investments, Inc. [17]	Sturm's friends	4,000	$.25	06/4/1998 (two days later)	4,000	$.28125
06/04/1998	First Geneva Investments, Inc.	Various friends and relatives of Sturm	8,000	$.25	06/04/1998 (three hours later)	8,000	$.28125
11/25/1996	First New York Investment, Inc.	Relatives of Sturm	15,000	$.1563	11/25/1996 (55 minutes later)	15,000	$.16

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15 The broker-dealer from which Alexander Securities bought the 4,000 shares of Coffeeworks on June 17, 1998 had purchased the shares in two separate transactions earlier the same day at 10:07 and 10:34 a.m., respectively, from minority shareholders that were friends of Littman. Alexander Securities made three telephone calls to Oosterwyk on June 17, 1998 at 9:43 a.m., 11:16 a.m., and 1:33 p.m. that preceded the purchase by a Cayman Islands entity.

16 Alexander Securities placed a call to Oosterwyk on the morning of August 6, 1998, the day after its 4,000-share purchase of Computer Vending, Inc. stock. One of the Cayman Islands entities then bought the 4,000 shares from Alexander Securities 36 minutes after Oosterwyk received a telephone call from Alexander Securities.

17 The 4,000-share sale to Alexander Securities consisted of 2,000 shares each from two minority shareholders. Alexander Securities made a telephone call to one of the minority shareholders at 10:36 a.m. on June 4, 1998. At 11:00 a.m. that same morning, the minority shareholder sold 2,000 shares of First Geneva to Alexander Securities. At 2:05 p.m. on June 4, 1998, Alexander Securities placed a call to Oosterwyk. Eight minutes later, at 2:13 p.m., a Cayman Islands entity bought the 4,000 shares that Alexander Securities had purchased on June 2, 1998 and the 8,000 shares that Alexander Securities had purchased three hours earlier that day.

Date of Transaction	Company	Seller(s)	Number of Shares Bought by Alexander Securities	Price Per Share	Date Shares Re-sold to Cayman Islands Accounts by Alexander Securities	Number of Shares Sold	Re-sale Price Per Share
10/22/1996	First Zurich Investments, Inc.	Friends of Sturm	5,000	$.1563	10/25/1996 (three days later)	5,000	$.1719
04/22/1997 04/23/1997	Littman[18] Ventures, Corp.	Unidentified customer of another broker-dealer	7,000	$.25	04/23/1997 (4,000 shares sold one day later and 3,000 shares sold same day)	7,000	$.27
11/11/1997	Snak-N-Pop Vending, Inc.[19]	Minority stockholder with unidentified relationship	1,000	$.50	11/12/1997 (one day later)	1,000	$.52
07/23/1998	Southern Cargo, Inc. [20]	Newberg's sister	1,000	$.50	07/28/1998 (five days later)	1,000	$.55
07/28/1998	Southern Cargo, Inc.[21]	Sturm's relatives	1,000	$.50	07/28/1998 (same day)	1,000	$.55

[18] The 7,000 shares of Littman Ventures were sold to Alexander Securities in three separate transactions on two different dates. Two sales occurred on April 22, 1997, at 12:42 p.m. (2,000 shares) and 1:34 p.m. (2,000 shares). Another sale occurred on April 23, 1997, at 9:38 a.m. (3,000 shares). All sales were executed at a price of $.25 per share. Alexander Securities then sold the accumulated 7,000 shares to a Cayman Islands entity later in the day on April 23, 1997 (at 3:55 p.m.) at $.27 per share.

[19] The Cayman Islands entity purchased 1,000 shares of Snak-n-Pop Vending from Alexander Securities approximately one half hour after Alexander Securities placed a telephone call to Oosterwyk.

[20] On July 23, 1998, Newberg's relative sold 1,000 shares of Southern Cargo to Alexander Securities at $.50 per share. Then, on July 28, 1998, at 10:55 a.m., Sturm's relative sold 1,000 shares of Southern Cargo to Alexander Securities at the same price.

[21] At 12:43 p.m. on June 28, 1998, a Cayman Islands entity purchased 2,000 shares of Southern Cargo from Alexander Securities 14 minutes after Oosterwyk received a telephone call from Alexander Securities.

This circumstantial evidence leads us to conclude that Newberg and Sturm used the minority shareholders and the Cayman Islands entities as nominee accounts[22] to effect matched trades. The use of nominee accounts to effect trades is an indication of manipulation. See Pagel, Inc., 803 F.2d 942, 946 (8th Cir. 1986). We find that these trades were made with the manipulative purpose of creating the false appearance of volume and market activity. See Markowski v. SEC, 274 F.3d 525, 528 (D.C. 2001) (noting that a classic manipulative scheme uses fraudulent devices such as wash or matched sales to trade targeted securities back to the sellers or among known parties to give a "false appearance of sales and market interest").

In addition to the matched trades that we have identified, we also find the pattern of Alexander Securities' purchases and sales of Shell Company shares to be evidence of Newberg's manipulative trading activity. Like the matched trades, a majority of the Firm's purchases and eventual sales to the Cayman Islands Accounts were effected at prices similar to each other and involved the same or a similar number of shares. The main distinction between the matched trades and the other trades is that the trades not identified as matched trades typically occurred more than a couple of days apart, but usually within a couple of weeks from the date on which the Firm had purchased the shares. We infer from this trading pattern that the trades were effected in this manner in an effort to evade detection by regulators, but that they nonetheless were effected with the same manipulative purpose as the matched trades.

The evidence shows that after Alexander Securities effected its purchases and sales of Shell Company shares through nominee accounts, other market makers joined the market. We find that Alexander Securities' synthetic trading activity was designed to bring in these new market makers to the market place for the ultimate purpose of enhancing the Shell Companies' merger prospects. "The more frequently a security is quoted, or the greater the number of dealers quoting the security, the broader and more active the appearance of the market for that security." Edward J. Mawod & Co, 46 S.E.C. 865, 870 (1977), aff'd, Mawod & Co., 591 F.2d 588 (10th Cir. 1979). This was yet another component of the manipulative scheme.

We find that Newberg and Sturm acted intentionally and that Newberg thus possessed the necessary scienter. Proof of scienter need not be direct, but rather may be inferred from circumstantial evidence. See, e.g., Herman & MacLean v. Huddleston, 459 U.S. 375, 390-91 n.30 (1983); Pagel, Inc. v. SEC, 803 F.2d 942, 946 (8th Cir. 1986). The following facts provide persuasive circumstantial evidence that Newberg's participation in the manipulative scheme was intentional.[23] The use of nominee accounts is evidence of a manipulative intent. See Pagel, Inc.

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22 The use of nominee accounts, accounts over which the manipulator has control, is a way of creating the appearance of "genuine demand." See SEC v. Kimmes, 700 F. Supp. 852, 859 (N.D. Ill. 1992).

23 Newberg claims that the Hearing Panel failed to cite any evidence to support a finding of scienter. In fact, although the Hearing Panel stated that matched transactions are per se manipulative under Section 9(a)(1) of the Exchange Act, it cited much of the same evidence that we cite in our decision to support its finding that Newberg acted with scienter by intentionally or recklessly engaging in manipulative conduct, as alleged. We find that there is sufficient evidence to conclude that Newberg's conduct was intentional, rather than intentional or reckless.

v. SEC, 803 F.2d at 946. In addition, the telephone records from Alexander Securities showing calls made to the minority shareholders and to Oosterwyk (the individual that had trading authority over the Cayman Islands Accounts) on days that those parties bought or sold shares constitute circumstantial evidence that Newberg, Sturm, or someone that they directed made telephone calls to the minority shareholders and Oosterwyk to effect the matched and other manipulative trades. Finally, the fact that the minority shareholders and Cayman Islands entities all maintained accounts at the same firms with which Newberg and Sturm also had close associations provides further evidence of manipulative intent.

Newberg argues that his trading activity was consistent with the normal activities of a market maker. This argument is unpersuasive for a number of reasons. The evidence establishes that telephone calls were made from the Firm to certain minority shareholders, some of whom were friends or relatives, and to Oosterwyk, who had trading authority over the Cayman Islands Accounts. We infer from the evidence that Newberg and Sturm were responsible for these calls, and that the calls and trading activity demonstrate that Newberg and Sturm arranged trades by the ultimate sellers and buyers of the securities under review that involved the same or similar numbers of shares that were traded in close proximity and at similar prices. This arranging of trades by Newberg and Sturm is conduct that is inconsistent with normal market-making activity.

Newberg argues that the Hearing Panel's finding that the matched trading was designed to create the appearance of market activity is negated by evidence that shows only minor fluctuations in the prices prior to the "pre-merger share prices." We presume that Newberg is referring to the prices of the shares during the initial couple of months of trading when there was not much fluctuation in price as compared to the eventual higher prices that permitted the Cayman Islands Accounts to sell their shares for a substantial profit. A finding of manipulative activity, however, is not contingent on finding intent to manipulate the price of the shares. The creation of a false appearance of supply or demand for a particular security is enough to establish manipulation. See, e.g., Adrian C. Havill, 53 S.E.C. 1060 (1998).[24]

Newberg also argues that Alexander Securities' trading in the shares of the Shell Companies was not particularly profitable. Although the record does not include definitive information regarding the total profits that Alexander Securities earned on the trades, the profitability of the trades is not necessary to establish manipulative intent. See Howard R. Perles, 2002 SEC LEXIS 847, at *29 n.31 (finding that "the absence of profit from manipulative conduct does not negate that conduct") (citations omitted).

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[24] Newberg also argues that "transaction causation" is an essential element of a "Rule 10b-5 claim." This contention lacks merit. Causation is not an element of a cause of action in an Enforcement disciplinary proceeding such as this. See, e.g., Dep't of Enforcement v. Ryan Mark Reynolds, Complaint No. CAF990018, 2001 NASD Discip. LEXIS 17, at *28 n.19 (June 25, 2001) (citation omitted).

We find that Newberg acted with the requisite scienter and that he engaged in manipulative activity, in violation of Section 10(b) of the Exchange Act, SEC Rule 10b-5, NASD Conduct Rule 2110,[25] and NASD Conduct Rule 2120[26] (cause two).[27]

B. Newberg Sold Unregistered Securities

Section 5 of the Securities Act of 1933 ("Securities Act") prohibits sales of securities unless a registration statement is in effect or an exemption from registration is available. There is no dispute that the securities of the Shell Companies were not registered under the Securities Act. And it is well settled that the burden of proving entitlement to an exemption from registration is on the party making the claim. Michael A. Niebuhr, 52 S.E.C. 546, 549 & n.17 (1995) (citing SEC v. Ralston Purina Co., 346 U.S. 119, 126 (1953)). Although Newberg claims entitlement to a number of different exemptions from registration under the Securities Act, he has failed to satisfy the requirements necessary to qualify for such exemptions.

1. The Section 4(1) Exemption is Not Applicable to the Transactions

Newberg contends that the trading that occurred in the securities of the Shell Companies was exempt from registration under Section 4(1) of the Securities Act, which exempts "transactions by any person other than an issuer, underwriter, or dealer." The complaint alleges that Newberg was acting as an "underwriter." The Securities Act defines "underwriter" as

> any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking . . . . As used in this paragraph the term "issuer" shall include, in addition to an issuer, any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer.

Section 2(a)(11) of the Securities Act (emphasis added).

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25 A violation of an NASD rule is also a violation of just and equitable principles of trade under NASD Conduct Rule 2110. Guang Lu, Exchange Act Rel. No. 51047, 2005 SEC LEXIS 117, at *15 n.17 (Jan. 14, 2005).

26 NASD Conduct Rule 2120 is NASD's antifraud rule and is the equivalent of Section 10(b) and SEC Rule 10b-5. See 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).

27 We affirm the Hearing Panel's decision not to analyze the alternative aiding and abetting allegation (third cause), given Newberg's liability under the cause of action alleging manipulative activity (cause two).

We agree with the Hearing Panel's conclusion that the evidence supports the finding that the minority shareholders and Newberg were acting as underwriters. Because the Section 4(1) exemption is not available to underwriters, Newberg cannot invoke it to avoid liability for selling unregistered securities.

We first address the facts supporting our conclusion that the minority shareholders were underwriters. We make this finding to show that the minority shareholders and Newberg were acting as "conduit[s] for the transfer of securities to the public," and thus were underwriters. Ackerberg v. Johnson, 892 F.2d 1328, 1335 (8th Cir. 1989). The minority shareholders satisfy the statutory definition of underwriter because they purchased securities from an issuer with "a view to distribute" those securities. Id. Littman was an "issuer," as that term is defined in Section 2(a)(11) of the Securities Act. The definition of issuer includes "any person directly or indirectly controlling . . . the issuer." Section 2(a)(11) of the Securities Act. See SEC v. North Am. Research & Dev. Corp., 424 F.2d 63, 74 (2d Cir. 1970) (concluding that certain individuals who controlled the issuer companies were "issuers"). Littman admitted forming shell companies and distributing shares in those companies to groups of shareholders. He further admitted that his reason for doing so was to have the shares listed on the OTC Bulletin Board so that they would become valuable to companies that wanted to purchase them as a means to become publicly traded. The evidence establishes that Littman distributed these shares to the minority shareholders as part of his manipulative plan that included listing the Shell Company shares at issue on the OTC Bulletin Board and using nominee accounts to trade the shares to give the appearance that there was market interest in the Shell Company shares. Thus, the minority shareholders obtained the shares from an issuer.

Newberg implies in his brief that the shares Littman distributed to the minority shareholders as gifts did not constitute sales and that, therefore, the minority shareholders were not underwriters because they did not "purchase" the shares from an issuer. This argument is unpersuasive. The SEC previously has concluded "that the fact that recipients may not have provided direct monetary consideration for the shares does not mean that there was not a sale or offer for sale for the purposes of Section 5." Capital Gen. Corp., Exchange Act Rel. No. 32669, 1993 SEC LEXIS 1880, at *28-29 (July 23, 1993). The SEC stated that such distributions of securities constituted a sale within the meaning of the Securities Act because "the distributions were dispositions for a value." Id. Moreover, the SEC has stated that, "a gift of stock is a 'sale' within the meaning of the Securities Act when the purpose of the 'gift' is to advance the donor's economic objectives rather than to make a gift for simple reasons of generosity." Universalscience.com, Inc., Securities Act Rel. No. 7879, 2000 SEC LEXIS 1632, at *4 (Aug. 8, 2000). As shown, Littman gifted the shares at issue to the minority shareholders or sold shares to them for a nominal fee as part of his manipulative plan to have the shares traded so that the Shell Companies would appear valuable and be purchased by companies interested in becoming publicly traded. Thus, Littman's purpose in gifting shares of the Shell Companies to the minority shareholders was to advance his own economic objective. Id. Newberg has failed to show that the gifted shares in this matter did not constitute sales.

Having found that the minority shareholders purchased the securities from an issuer, we next review the evidence establishing that they did so with "a view to" distribute those securities.

To decide whether there has been a distribution as opposed to mere trading, the courts often look to whether the "security holder has held the securities long enough to negate any inference that his intention at the time of acquisition was to distribute them to the public." See Norman J. Ackerberg, 892 F.2d at 1336. A number of courts consider that the acquisition of shares is not made "with a view to" distribution if the shares have been held for two years. Id. ("[T]he courts look to whether the security holder has held the securities long enough to negate any inference that his intention at the time of acquisition was to distribute them to the public. Many courts have accepted a two-year rule of thumb to determine whether the securities have come to rest.") (citing United States v. Sherwood, 175 F. Supp. 480, 483 (S.D.N.Y. 1959)); Hedden v. Marinelli, 796 F. Supp. 432, 437 (N.D. Cal. 1992) (same). "This two-year rule has been incorporated by the SEC into Rule 144, which provides a safe harbor for persons selling restricted securities acquired in a private placement." Ackerberg v. Johnson, 892 F.2d at 1336.

Newberg has the burden of proving there was no distribution, and he has not satisfied this requirement. See, e.g., Gary E. Bryant, 51 S.E.C. 463, 466-67 (May 24, 1993) (finding that the purchases and resales were part of a distribution and that Bryant had failed to establish that any of the sales were exempt). Although the Shell Company shares here purportedly were issued years before the minority shareholders began selling their shares, NASD examiner Park testified that there was no evidence to show that the shares actually were delivered to the minority shareholders at the time the companies were formed. Moreover, Littman testified that he probably did not send the certificates to the shareholders at the time that he formed the companies, which typically were formed two or more years before the commencement of trading. The evidence further shows that in many cases the shares were not deposited into the minority shareholders' accounts until just a couple of months or less before they sold their shares to Alexander Securities. The "[minority shareholders] lack of intention to hold the securities for investment purposes" is evidenced by "[t]he immediacy of the resales" to Alexander Securities. Gary E. Bryant, 51 S.E.C. at 467. We conclude that the minority shareholders that sold their shares to Alexander Securities did so with a view to distribution and therefore were underwriters. Even if the minority shareholders had held their shares for two years, however, the transactions would not be exempt from registration. In a no-action response letter, the SEC staff stated that the resale of shares in circumstances similar to those at issue here involving the gifting of shares to a limited number of individuals who held their shares for two years would require registration, regardless of whether an exemption under SEC Rule 144 would appear to be available after the lapse of some period of time. See NASD Notice to Members 00-49 (July 2000) (discussing NASD Regulation, 2000 SEC No-Act. LEXIS 42 (Jan. 21, 2000)).

Turning next to Newberg's role in the distribution, we find that he purchased Shell Company shares from the minority shareholder underwriters "with a view" to distribution to the public and that he participated in the distribution. The evidence shows that shortly after purchasing Shell Company shares from minority shareholders, Newberg sold those shares to the Cayman Islands Accounts as part of Littman's manipulative plan to create the appearance of a public market for the shares at issue. The evidence also establishes that Newberg used the minority shareholders and Cayman Islands entities as nominees to effect the manipulation of the Shell Company shares, which was an essential step in Littman's plan to take Shell Companies with no inherent value and turn them into attractive merger candidates. Thus, the evidence amply demonstrates that Newberg purchased the shares "with a view to distribution" and that he participated in the distribution. Newberg, therefore, was acting as an underwriter. It is not necessary to find that Newberg purchased the shares at issue from an issuer to conclude that he acted as an underwriter.[28] See SEC v. North Am. Research & Dev. Corp., 424 F.2d 63, 74 (2d Cir. 1970) ("Although [the alleged underwriter's] purchases from minority shareholders . . . were not from issuers, they were made with 'a direct or indirect participation' in [the] distribution scheme.")

Accordingly, we find that Newberg was a participant in a plan to distribute the Shell Company securities to the public and that he was acting as an underwriter.[29] The securities at issue therefore were not exempt from registration under Section 4(1) of the Securities Act.[30]

2. SEC Rule 144 Is Inapplicable

Newberg argues that the Shell Company shares were sold pursuant to SEC Rule 144 and therefore were exempt from the registration requirement. The rule is a "safe-harbor" provision under Section 4(1) of the Securities Act. If sales are made in compliance with the specific provisions of SEC Rule 144, the seller is not considered to be acting as an underwriter. The safe-harbor is not available, however, if the transactions were part of a plan to distribute securities to the public. In the adopting release to SEC Rule 144 the SEC stated that, "the rule shall not be

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[28] The statutory definition of underwriter covers every person who participates in a distribution of securities. See SEC v. Van Horn, 371 F.2d 181, 188 (7th Cir. 1966); Ingenito v. Bermec Corp., 441 F. Supp. 525, 536 (S.D.N.Y. 1977) ("An underwriter buys securities directly or indirectly from the issuer and resells them to the public, or he performs some act (or acts) that facilitates the issuer's distribution. He participates in the transmission process between the issuer and the public"). The minority shareholders and Newberg were underwriters. They engaged in "steps necessary" to the distribution of Shell Company shares to the public by serving vital roles in the distribution. The "Sec. 4 exemption . . . 'does not in terms or by fair implication protect those who are engaged in steps necessary to the distribution of security issues.'" (quoting SEC v. Chinese Consol. Benev. Ass'n., Inc., 120 F.2d 738, 741 (2d Cir. 1941)).

[29] As to one Shell Company (Littman Ventures Corp.), there is no evidence that Alexander Securities purchased shares from any of the minority shareholders. The shares of Littman Ventures Corp. that Alexander Securities purchased were from an unidentified customer or customers of another broker-dealer. Thus, we find that the record does not include sufficient evidence from which to conclude that there were any minority shareholders that were underwriters with respect to that company. We therefore find that Newberg was an underwriter with respect to all of the Shell Companies, except Littman Ventures Corp.

[30] The Section 4(1) exemption exempts only trading transactions between individual investors with respect to securities already issued. SEC v. Lybrand, 200 F. Supp. 2d 384, 393 (S.D.N.Y. 2002). It does "not exempt distributions by issuers or the acts of individuals who engage in steps necessary to such distributions." Id. (citations omitted).

available to any individual or entity with respect to any transaction which, although in technical compliance with the provisions of the rule, is part of a plan by such individual or entity to distribute or redistribute securities to the public. In such case, registration is required." Securities Act Rel. No. 5223, 1972 SEC LEXIS 49, *29 (Jan. 11, 1972). On facts similar to the facts here, the SEC staff stated in a no-action letter that neither Section 4(1) nor SEC Rule 144 would apply to circumstances in which stock promoters sought to sell unregistered shares of shell companies after the lapse of a period of time following the issuance of shares to other persons. See NASD Notice to Members 00-49 (July 2000) (discussing NASD Regulation, 2000 SEC No-Act. LEXIS 42 (Jan. 21, 2000)).[31]

Thus, the shares at issue are not exempt under SEC Rule 144 because, as we concluded above, Newberg was a participant in a plan to distribute securities to the public and therefore was acting as an underwriter.

* * *

The securities that Newberg sold were neither registered under Section 5 of the Securities Act, nor eligible for an exemption from registration.[32] We find that Newberg, an underwriter, sold unregistered securities, in violation of Section 5 of the Securities Act, and that he therefore did not comply with high standards of commercial honor and just and equitable principles of trade, in violation of NASD Conduct Rule 2110 (cause one).[33]

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[31] Newberg argues that the allegation against him is a "test case" in support of NASD Notice to Members 00-49. He argues that the principles set forth in the SEC's no-action letter (2000 SEC No-Act. LEXIS 42 (Jan. 21, 2000)) are not applicable to this matter because the letter was issued after the events that occurred in this case. This argument is without merit. As the court stated in SEC v. Lybrand, 200 F. Supp.2d at 397, the SEC's no-action letters do not change the existing law, although they may be treated as persuasive.

[32] Newberg claims that the initial issuance of shares to the minority shareholders was exempt from registration under Section 4(2) of the Securities Act and that the minority shareholders were permitted to resell the shares under the SEC Rule 144 safe harbor provision. Newberg has the burden of proving an exemption under Section 4(2) with respect to each offeree, and he has failed to do so. See Western Fed. Corp. v. Erickson, 739 F.2d 1439, 1442 (9th Cir. 1984); SEC v. Life Partners, Inc., 912 F. Supp. 4, 10 (D.D.C. 1996). Further, as noted above, SEC Rule 144 is not applicable to the transactions at issue. Moreover, we have concluded that the minority shareholders, Newberg, and Sturm were participants in a distribution and therefore were underwriters. Thus, the securities in the transactions at issue in this case are not exempt from registration.

[33] Our finding is applicable to the sales in all of the Shell Companies, except for those sales that occurred in the shares of Littman Ventures Corp., which is the entity we identified as having no sales from a minority shareholder to Alexander Securities. See supra note 29.

C. Newberg Failed to Advise His Firm About Outside Securities Accounts

The complaint alleged that Newberg failed to provide written notice to his Firm of securities accounts in which he had a financial interest that were maintained at other broker-dealers, as required under NASD Conduct Rules 2110, 3050(c), and 3050(e). NASD Rule 3050(e) specifies that the notice requirement applies only "to an account . . . in which an associated person has a financial interest or with respect to which such person has discretionary authority."

The Hearing Panel found that Newberg had a financial interest in Dale Financial, the company that his wife owned, and its securities accounts, and that he failed to provide the required notification about those accounts to Alexander Securities. The parties did not appeal this finding of violation. We find that the evidence, as detailed in the Hearing Panel's decision, supports the Hearing Panel's finding of violation. Thus, we find that Newberg violated NASD Conduct Rules 2110 and 3050(c) by failing to provide the required notification to his Firm of the Dale Financial accounts (cause five).[34]

D. Newberg Engaged in Outside Business Activities

NASD Conduct Rule 3030 requires that an associated person give "prompt written notice" to his or her firm with respect to the acceptance of compensation from "any other person as a result of any business activity . . . outside the scope of his relationship with his employer." The complaint alleged that Newberg violated Conduct Rules 2110 and 3030 by receiving "finder's fees" and "profits from [the] Cayman Account trading" without providing the required notice to his Firm.

The Hearing Panel found that Newberg failed to provide prompt written notice to Alexander Securities regarding a $300,000 finder's fee that he received through Sturm & Newberg, L.P. The Hearing Panel also found, however, that Enforcement failed to prove by a preponderance of the evidence that Newberg was obligated under Conduct Rule 3030 to treat the profits from the Cayman Islands Accounts as an outside business activity to be reported to his Firm. The parties did not appeal these findings. We find that the evidence in the record, as set forth in the Hearing Panel's decision, supports the Hearing Panel's findings. We therefore find that Newberg violated NASD Conduct Rules 2110 and 3030 by receiving finder's fees as alleged in cause six.

E. Newberg Provided False Investigative Testimony

The complaint alleged that Newberg testified falsely under oath in an on-the-record interview with NASD staff, in violation of NASD Conduct Rule 2110 and Procedural Rule 8210.

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[34] We agree with the Hearing Panel's finding that there is insufficient evidence to find, as the complaint alleged, that Newberg had a financial interest in the Cayman Islands Accounts and that he therefore failed to provide written notice of those accounts as required under NASD Conduct Rule 3050(c). We thus dismiss the allegation.

The complaint states that Newberg falsely denied being employed by Dale Financial or performing any services for the company and that he falsely denied knowing anyone who had any business relationship with "Robert Oosterwyk, the nominee for the Cayman Accounts." We analyze separately the allegations with respect to each on-the-record statement at issue.

1. Newberg's Denial that He Had Ever Performed Services for Dale Financial Was False

Newberg responded, "[n]o," to the question of whether he "had ever provided any consulting or any type of service to Dale Financial Consulting?" He also responded, "[n]o," when he was asked if he had "ever managed any financial activity of Dale Financial Consulting." Contrary to Newberg's denials, the record demonstrates that Newberg provided a myriad of services to Dale Financial. Newberg admitted filling out portions of the new brokerage account applications for Dale Financial and participating in financial transactions. Those financial transactions included checks that Newberg drew on Dale Financial's account, payable to himself, and checks that he drew from the Newbergs' joint account, payable to Dale Financial.

Thus, we affirm the Hearing Panel's finding that Newberg provided false testimony in response to questions about whether he provided services to or managed any financial activity for Dale Financial.

2. Newberg Gave False Testimony About His Relationship with Oosterwyk

In his on-the-record interview Newberg was asked whether he "kn[e]w of anybody who has any business relationship" with Oosterwyk, to which he answered, "[n]o." The evidence establishes that this response was false. Newberg and his wife had a significant business relationship with Oosterwyk, the Cayman Islands banker who had trading authority for the Cayman Islands Accounts that served as nominee accounts for the manipulative scheme. Over the course of nearly two years, from early 1996 through early 1998, the Newbergs received $1.9 million from Oosterwyk through a number of six-figure mortgage advances. The Newbergs' debt to Oosterwyk was still outstanding in March 2000 when Newberg gave his on-the-record interview. When Newberg was given the opportunity to explain his having testified that he did not know of anyone who had a business relationship with Oosterwyk, he claimed that he did not consider the mortgage a business relationship because he knew Oosterwyk "in a personal context, a social context" and because the mortgage was on his "personal residence." The Hearing Panel implicitly did not credit Newberg's hearing testimony:

> The notion that a banker in the business of making mortgage loans would arrange a $1.9 million loan as a 'personal' matter for the benefit of someone who was not a friend and whom he had met only twice[35] makes no sense.

35 Newberg testified in his on-the-record interview that he had met Oosterwyk only twice.

We defer to the Hearing Panel's implicit credibility determination. See Dist. Bus. Conduct Comm. v. Bernadette Jones, Complaint No. C02970023, 1998 NASD Discip. LEXIS 60, at *8 (NAC Aug. 7, 1998) (holding that the fact-finders' implicit determination that respondent's testimony was not credible was entitled to considerable weight). A fact finder's credibility determinations are entitled to considerable weight and deference because they are based on hearing the respondent's testimony and observing his demeanor. See Keith L. DeSanto, 52 S.E.C. 316, 319 (1995).

Therefore, we reject Newberg's attempts to portray the $1.9 million in loans that he received from Oosterwyk as a "personal" matter rather than a business matter and conclude that Newberg indeed had a business relationship with Oosterwyk. Because Newberg denied in his on-the-record interview that he knew of anyone with a business relationship with Oosterwyk, he testified falsely.

* * *

Newberg contests the Hearing Panel's findings that he gave false on-the-record testimony with respect to his denial that he performed any services for Dale Financial and his denial that he knew anyone that had a business relationship with Oosterwyk. In support Newberg cites decisions in criminal actions brought under the federal perjury statute, 18 U.S.C. §1621, in which defendants were found not to have violated the perjury statute. Because criminal cases require a different standard of proof than the preponderance of the evidence standard applicable in self-regulatory disciplinary actions, court decisions that analyze whether a criminal statute has been violated have no applicability to this disciplinary action. See, e.g., MeritQuest Group, Inc., 51 S.E.C. 223, 226 & n.4 (1992) (rejecting respondent's argument that the NASD allegation against him must be proven beyond a reasonable doubt and finding that preponderance of the evidence is the proper standard of review) (citing Steadman v. SEC, 450 U.S. 91 (1981)). We therefore reject Newberg's attempt to apply a different standard of proof to these proceedings.

Newberg's false testimony falls far short of his obligation as an associated person "to cooperate fully" with requests for information under Procedural Rule 8210. Joseph G. Chiulli, 54 S.E.C. 515, 523 (2000). Newberg's false statements also violate the "broad ethical principle" embodied in NASD Conduct Rule 2110. Dep't of Enforcement v. Bendetsen, Complaint No. C01020025, 2004 NASD Discip. LEXIS 13, at *16 (NAC Aug. 9, 2004) (citation omitted).

In sum, we find that Newberg gave false investigative testimony about: (1) whether he had provided any services to or managed any financial activity for Dale Financial; and (2) whether he knew anyone who had a business relationship with Oosterwyk, in violation of Conduct Rule 2110 and Procedural Rule 8210 (cause seven). In addition, we find that the record supports the Hearing Panel's finding that Enforcement failed to prove by a preponderance of the evidence that Newberg gave false testimony when he testified that he did "not believe" that he had ever been employed by Dale Financial. We therefore dismiss that allegation.

F. Supervisory Failures

The evidence establishes that Alexander failed to supervise adequately the activities of Newberg and Sturm in the Firm's Aventura office. The evidence also establishes that Alexander failed to establish, maintain, and enforce written supervisory procedures that were tailored to the nature of the business that the Firm conducted. Accordingly, we find that Alexander violated NASD Conduct Rules 2110, 3010(a), and 3010(b).

1. Failure to Supervise

The complaint alleged that Alexander failed to supervise adequately Newberg and Sturm's trading and market-making activity at the Firm's Aventura office. NASD Conduct Rule 3010(a) requires that each member establish and maintain a system to supervise the activities of each registered representative and associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations and with NASD Rules.

As the Firm's president, Alexander had ultimate responsibility for supervising the Firm's trading activities. See Michael T. Studer, Exchange Act Rel. 50543, 2004 SEC LEXIS 2347, at *22 (Oct. 14, 2004) ("Final responsibility for supervision of the trading activities at a member firm . . . rests with the firm's president, unless the president reasonably delegates the duties to someone else and has no reason to know that person is not properly performing the delegated duties"). Alexander admits that he had ultimate supervisory responsibility at the Firm, including over compliance matters. The evidence shows, however, that he failed reasonably to exercise that supervisory responsibility with respect to the market-making and trading activities of Newberg and Sturm.

Although Alexander delegated to Newberg the duty of supervising the Firm's Aventura branch office, he did not "follow-up and review that delegated authority to ensure that it [was] being properly exercised." Castle Sec. Corp., 53 S.E.C. 406, 412 (1998). Such review was necessary given that Alexander permitted Newberg and Sturm to engage in market-making activities in a branch office that was located far from the Firm's headquarters. Id. at 414. Alexander acknowledged having visited the office only once or twice in 1997 and only once in 1998. He further acknowledged that the Firm's review of Aventura's trading blotters on a daily basis was "cursory" and that such reviews did not reveal a "preponderance of matched trades."

Alexander also performed no oversight with respect to the hundreds of Forms 211 that the Aventura office filed during the review period, stating that he did not require the Forms 211 to be sent to the Firm's main office for review. Alexander testified that Newberg was "in charge of his [Newberg's] filings" and that he was permitted to file the Forms 211 "without any comment from me [Alexander]."[36]

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[36] Alexander acknowledged having received copies of comment letters from NASD stating that the Forms 211were no longer deficient. He did not testify, however, about having any involvement in the Forms 211 filing process.

Alexander argues that the Firm's records did not indicate any evidence of "matched trading" or, if there was, any failure to detect it "was reasonable under the facts and circumstances." In support, Alexander asserts that he reviewed trading blotters and net inventory positions daily. Any review of such information by Alexander, however, was admittedly only "cursory." Moreover, Alexander admitted that he was not interested in monitoring the profitability of the Shell Company trading.[37]

Additionally, Alexander contends that Newberg and Sturm hid their use of Forms 211 from him to conduct outside business activities. Alexander also claims that the Forms 211 did not involve shell companies, but if they did, "he did not know which transactions involved shells." These arguments have no merit. Alexander admitted that he did not require the Forms 211 to be reviewed by the Firm's main office. Alexander was aware that the Firm's Aventura office was the Firm's only wholesale trading office and that Newberg was one of the Firm's top producing traders. Furthermore, if Alexander did not know which transactions involved shell companies, it was because he chose not to monitor that type of trading activity. His testimony on this point is instructive:

> **Q.** When you were reviewing the trading the Aventura office was doing, how did you know which stock traded by Aventura was a . . . shell company?
>
> **R.** I didn't.
>
> **Q.** So --
>
> **R.** I didn't unless I had kept track of all the comment letters, which I didn't.

The evidence establishes unequivocally that Alexander exercised no meaningful oversight of the Aventura office. Alexander's failure to exercise supervisory responsibility over market-making and trading activities of Newberg and Sturm allowed Newberg effectively to act without supervision, which is not permitted. See Michael T. Studer, 2004 SEC LEXIS 2347, at *23-24. This serious supervisory failure permitted the unregistered distribution and manipulative activities to occur repeatedly without detection or restriction. We therefore find that Alexander violated NASD Conduct Rules 2110 and 3010 (cause eight).

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[37] In explaining his lack of interest in supervising the trading activities of the shares of Shell Companies, Alexander stated:

> I really was not monitoring the shell companies' profitability to me. When I see a position of two thousand shares, or five thousand shares in a fifty cent stock, that didn't concern me to zero in on the profit motivation as much as the risk factor if they had a hundred thousand dollars in an issue.

2. Deficient Written Supervisory Procedures

In addition to Alexander's failure adequately to supervise Newberg and Sturm, the evidence demonstrates that Alexander also is liable for the Firm's deficient written supervisory procedures. NASD Conduct Rule 3010(b)(1) requires that member firms[38] "establish, maintain, and enforce written procedures to supervise the types of business in which it engages and to supervise the activities of registered representatives and associated persons." (emphasis added).

Alexander testified at the hearing that he was the individual responsible for all compliance matters. The record includes copies of the Firm's written supervisory procedures manuals dated 1995 and 1998 that were in effect during the period under review. Neither of those manuals, however, contained any written supervisory procedures addressing the type of business in which the Aventura office was engaged, including market making and underwriting activities, and the filing of Forms 211. Alexander testified at the hearing that the Aventura office filed approximately 200 Forms 211 per year during the period from 1997 to 1999, and that the majority of those filings were for shell companies. The written supervisory manuals, however, did not set forth any procedures assigning responsibility to someone to review the Forms 211. The Firm's Aventura office engaged in these activities without any scrutiny by Alexander or the Firm's main office. The provision in the Firm's written supervisory procedures that required the Compliance Officer to "review all account transactions, including a daily review of all purchases or sales" does not satisfy NASD Conduct Rule 3010(b)'s requirement for procedures "to supervise the types of business in which [the firm] engages." (emphasis added.) Under proper procedures, a mere "cursory" review of trading records is wholly insufficient.

Alexander argues that NASD should have alerted him to any deficiencies in the Firm's written supervisory procedures. This assertion has no merit. As the SEC repeatedly has stated, "the responsibility for compliance with applicable requirements cannot be shifted to regulatory authorities." John Montelbano, Exchange Act Rel. 47227, 2003 SEC LEXIS 153, at *26-27 (Jan. 22, 2003). In James L. Owsley, 51 S.E.C. 524, 534 n.27 (1993), the SEC applied that principle in rejecting the respondents' argument that the firm's compliance manual routinely "passed muster" with NASD and the SEC.

We find that Alexander failed to establish, maintain and enforce adequate written supervisory procedures, in violation of Conduct Rules 2110 and 3010 (cause nine).

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[38] NASD Rule 115 provides that NASD's Rules apply to all members "and associated persons associated with a member" and that such persons have the same duties and obligations as a member under the Rules.

V. Sanctions

A. Newberg

1. Manipulation

In determining the appropriate level of sanctions, we have considered a number of factors.[39] As the SEC has emphasized, "there are few, if any, more serious offenses than manipulation. Such misconduct 'is a fraud perpetrated . . . on the entire market. It 'attacks the very foundation and integrity of the free market system.'" John Montelbano, Exchange Act Rel. No. 47227, 2003 SEC LEXIS 153, at *49.

Newberg played a crucial role in the manipulative scheme by ensuring, through use of the nominee minority shareholders and Cayman Islands Accounts, that there would be a willing buyer and that the share prices would not decline once the minority shareholders started selling their shares to Alexander Securities. A number of these trades were "matched" trades. Such matched trades and the other manipulative trading constituted a key step in the manipulation because they gave the false appearance that there was market interest in the Shell Company securities, which had no inherent value. The Guidelines instruct us to consider whether the misconduct at issue was "the result of an intentional act, recklessness, or negligence."[40] As noted in our findings, Newberg violated the Exchange Act's antifraud provisions as a result of his intentional participation in the manipulative trading activity. Newberg's actions therefore constitute egregious misconduct.

We also have consulted the Guidelines' Principal Considerations, which apply to all violations, in determining appropriate sanctions. The Guidelines instruct us to consider whether "the respondent engaged in numerous acts and/or a pattern of misconduct,"[41] and whether his activities resulted in his monetary gain.[42] Newberg engaged in a pattern of misconduct evidenced by his efforts to have the Shell Company shares listed and the matched trading that he effected. We further conclude that Newberg profited from his activities. Newberg received finder's fees through a limited liability company of which he was part owner. He also received a favorable loan for approximately $1.9 million from Oosterwyk. Further, Newberg asserts that he was engaged in normal market-making activities. Yet substantial evidence establishing Newberg's central role in the manipulation belies this assertion.

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[39] The NASD's Sanction Guidelines ("Guidelines") do not include a guideline specifically relevant to manipulation cases.

[40] Guidelines (2001 ed.) at 10 (Principal Considerations in Determining Sanctions, No. 13).

[41] Guidelines (2001 ed.) at 9 (Principal Considerations in Determining Sanctions, No. 8).

[42] Guidelines (2001 ed.) at 10 (Principal Considerations in Determining Sanctions, No. 17)

Enforcement argues that disgorgement is an appropriate sanction for Newberg's manipulative activity. For the reasons stated below, we decline to order disgorgement.

We first address Enforcement's argument that Newberg should disgorge profits in the Dale Financial securities account of $1,015,656, plus pre-judgment interest. Newberg argued that the profits from the sales of securities from the accounts of Dale Financial were not attributable to him because his wife owned the company. Enforcement argued that the securities of five shell companies that the Dale Financial accounts received constituted payments attributable to Newberg's work in locating shell companies for Littman. Although the record includes an NASD-staff generated chart setting forth the alleged profits that the Dale Financial accounts made from selling the shares at issue, the chart does not sufficiently link the information depicted with source documents that would permit us to reach the conclusion that Enforcement is urging regarding the amount of profits that accrued to the Dale Financial securities accounts.

We next address Enforcement's argument that Newberg should disgorge the $300,000 payment to Sturm & Newberg, LP. Newberg asserted that the $300,000 payment represented money that Littman owed to Sturm. He also claimed that Sturm & Newberg, L.P. was formed as a defined pension benefit plan. The Hearing Panel rejected as not persuasive Newberg's claim that he did not know the nature of the alleged payment to Sturm and his further assertion that the payment represented Sturm's contribution to a pension plan. These credibility determinations are entitled to considerable weight. See Keith L. DeSanto, 52 S.E.C. at 319. We find no basis to make a different determination than the Hearing Panel. Sturm testified that Sturm & Newberg, L.C was formed as a vehicle to enable him and Newberg to provide assistance with mergers. Newberg denied that the payment represented a finder's fee as payment for locating merger partners for the Shell Companies. Newberg nevertheless claimed that he was entitled to half of the money deposited into the Sturm & Newberg, L.P. account. Newberg's 1998 tax documents show that he received $100,000 as an employee of Sturm & Newberg, L.P. These facts, combined with Newberg and Sturm's admissions about their involvement in seeking companies to merge with Shell Companies, provide persuasive circumstantial evidence that the $300,000 payment from Littman represented a finder's fee associated with those efforts. The record, however, does not include adequate evidence for us to discern the portion of that payment distinctly attributable to Newberg.

In view of Newberg's egregious misconduct, the additional aggravating factors discussed above, and the lack of any mitigating factors, we have determined that a bar is required. A bar will prevent Newberg from again jeopardizing the integrity of the markets and will serve to deter others from engaging in similar misconduct.[43]

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[43] The Hearing Panel stated that but for the imposition of the bar, it would have fined Newberg $725,000 ($25,000 for each of the 29 securities involved in the manipulative scheme). Enforcement argues that a fine of $725,000 should be imposed because Newberg's misconduct involved "deliberative violative conduct for financial gain." The Guidelines do not include a sanction recommendation specifically designed to address manipulative conduct. As a matter of

[Footnote continued on next page…]

2. The Sale of Unregistered Securities

The Guidelines for unregistered securities recommend a fine in the range of $2,500 to $50,000. In egregious cases, the Guidelines recommend a suspension for up to two years or a bar. We conclude that Newberg's conduct was egregious. Newberg engaged in a pattern of misconduct that covered 28 distributions spanning a period of more than two years. The facts and circumstances lead us to conclude that Newberg attempted to avoid registration rather than comply with an exemption.[44] The conclusory statements in the documents accompanying the Forms 211 that "Section 4 of the [Securities] Act provides several transactional exemptions" and that the shares "are freely tradable under the [Securities] Act" do not constitute evidence of an attempt to comply with an exemption. See Lively v. Hirschfeld, 440 F.2d 631, 633 (10th Cir. 1971) (finding that "the evidence in support of an exemption must be explicit, exact, and not built on mere conclusory statements").

Newberg's activities show that he was willing to totally disregard his duty as an associated person to abide by NASD rules in order to enrich himself. See, e.g., Brian L.Gibbons, 52 S.E.C. 791, 794 n.12 (1996). There also is no evidence that Newberg has any understanding of the seriousness of his violations and that he would not engage in similar misconduct if permitted to remain in the securities industry. In light of these factors, a bar is required to protect investors and the securities markets.[45]

3. Failure to Report Outside Securities Accounts and Outside Business Activities

We agree with the Hearing Panel's decision to treat Newberg's failure to report outside securities accounts and outside business activities as a single course of action. Based on the fact that Newberg's violations occurred over a number of years and constituted an attempt to conceal his violations from regulators, we find that his misconduct was egregious.[46] The applicable

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course, however, we typically do not impose fines if an individual is barred. See Guidelines at 13-14 (2001 ed.) (Technical Matters).

[44] The applicable Guideline instructs us to consider whether the respondent attempted to comply with an exemption from registration. Guidelines (2001 ed.) at 30 (Unregistered Securities -- Sales Of).

[45] We agree with the Hearing Panel's conclusion that an otherwise appropriate fine of $50,000 for this violation should not be imposed in light of our decision to bar Newberg for this violation. See supra note 43.

[46] See Guidelines (2001 ed.) at 9 (Principal Considerations in Determining Sanctions, Nos. 8 and 9).

Guidelines recommend a suspension for up to two years or a bar for egregious cases.[47] We agree with the Hearing Panel that a one-year suspension and $75,000 fine for this violation would be an appropriate sanction.[48] In light of our imposition of a bar for the manipulation, sales of unregistered securities violations, and providing false testimony violations, however, we decline to impose a sanction for the failures to report outside securities accounts and outside business activities.

4. False Testimony

The Guidelines recommend a bar as the standard sanction for a failure to respond. We find that the false testimony that Newberg provided during his on-the-record interview requires the imposition of a bar.[49]

The questions to which Newberg responded falsely were related to an NASD investigation under NASD Conduct Rule 8210. We find that Newberg's denial that he had performed "any type of service" for Dale Financial, given the substantial evidence to the contrary, as described in our findings, is egregious. Newberg's denial that he knew anyone who had a "business relationship" with Oosterwyk is also egregious. Oosterwyk represented an essential link in the manipulative activity because he had trading authority for the Cayman Islands Accounts that played such a significant role in the manipulation and the sales of unregistered shares violations. Newberg's denial of knowing anyone that had a business relationship with Oosterwyk was an obvious attempt to hide the fact that Newberg had received an extraordinarily favorable $1.9 million mortgage loan from Oosterwyk.[50] A bar is the appropriate sanction for such a serious departure from the duty to abide by NASD rules. Newberg's false answers resulted in the concealment of information from NASD staff that was materially important to the investigation.[51]

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[47] See Guidelines (2001 ed) at 21 (Transactions For Or By Associated Persons -- Failure to Comply with Rule Requirements); Guidelines (2001 ed.) at 18 (Outside Business Activities -- Failure to Comply with Rule Requirements).

[48] The fine represents the total of the maximum fines recommended under each of the applicable Guidelines.

[49] See Guidelines (2001 ed.) at 39 (Failure to Respond or Failure to Respond Truthfully, Completely, or Timely To Requests Made Pursuant to NASD Procedural Rule 8210).

[50] See Guidelines (2001 ed.) at 9 (Principal Considerations in Determining Sanctions, No. 10).

[51] The nature of the information requested is a principal consideration under the applicable Guideline. See Guidelines (2001 ed.) at 39 (Failure to Respond or Failure to Respond Truthfully, Completely, or Timely To Requests Made Pursuant to NASD Procedural Rule 8210).

B. Alexander's Supervisory Failures

We consider the specific Guidelines applicable to the failure to supervise and the deficient written supervisory procedures violations, and we aggregate the misconduct alleged because it stemmed from a continuous course of action.[52]

As an initial matter, we note that Alexander has a serious disciplinary history. The Guidelines instruct us to consider both "past misconduct similar to that at issue" and, while unrelated to the misconduct at issue, past misconduct that "evidences disregard for regulatory requirements, investor protection, or commercial integrity" as relevant disciplinary history.[53] In September 1995, NASD sanctioned Alexander in a case alleging that the Firm, through Alexander, issued confirmations that falsely disclosed that the Firm was acting as agent for the customer when it was acting as principal. NASD sanctioned Alexander in January 1999 on the basis of allegations that Alexander allowed an employee who was subject to a statutory disqualification to function as a principal. In February 2002, Alexander settled allegations by NASD that he was responsible for several serious supervisory violations. Finally, in May 2002, a state regulator sanctioned Alexander based on allegations that the Firm sold securities in the state without the requisite registration.

Based on Alexander's disciplinary history involving supervisory and other violations, we find that he has shown a general indifference to regulatory matters over a sustained period of years. See, e.g., Dist. Bus. Conduct Comm. v. Montano, Complaint No. C02950050, 1999 NASD Discip. LEXIS 37, at *10-11 (NAC Jan. 27, 1999) (finding Montano's disciplinary history over a five-year period important not only because it contains similar past misconduct, but also because it demonstrates a "general indifference to the rules and regulations of the securities industry"). The Guidelines' General Principle No. 2 specifically recommends imposing

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52 The Guidelines for failure to supervise recommend a monetary sanction in the range of $5,000 to $50,000, and a suspension of the responsible individual in all supervisory capacities for up to 30 business days. See Guidelines (2001 ed.) at 108 (Supervision -- Failure to Supervise). The Guidelines also recommend limiting the activities of the appropriate branch office or department for up to 30 business days. Id. In egregious cases, the Guidelines recommend limiting the activities of the branch office or department for a longer period or suspending the firm with respect to any or all activities or functions for up to 30 business days, and considering suspending the responsible individual in any or all capacities for up to two years or barring the responsible individual. Id. With respect to a case against a member firm involving systemic supervision failures, the Guidelines recommend a longer suspension of the firm with respect to any or all activities or functions (of up to two years) or expulsion of the firm. Id.

The Guidelines for deficient written supervisory procedures recommend a fine from $1,000 to $25,000. See Guidelines (2001 ed.) at 109 (Supervisory Procedures--Deficient Written Supervisory Procedures).

53 NASD Notice to Members 03-65, at 688 (Oct. 2003).

"increasingly severe monetary sanctions for second and subsequent disciplinary actions" in certain cases. NASD Notice to Members 03-65, at 688 (Oct. 2003).

In assessing sanctions, we also have looked to the principal considerations in determining sanctions listed in the respective Guidelines for failure to supervise and deficient written supervisory procedures. We have concluded that the quality and degree of Alexander's implementation of the firm's supervisory procedures fell far short of the requirements under NASD Conduct Rule 3010. Alexander's supervision of the Firm's Aventura office was extremely limited. He admittedly performed only a "cursory" review of the trading records from the Firm's Aventura office and acknowledged visiting the office no more than once or twice per year.[54] Had Alexander adequately reviewed the trading records for the Firm's Aventura office, the suspicious trading pattern could have been detected. Moreover, the fact that Alexander did not devise written procedures tailored to the nature of the business conducted by the Aventura office or adequately scrutinize the trading records showing patterns of matched trading allowed Newberg and Sturm's manipulative conduct to escape the Firm's detection.[55]

Additionally, the principal considerations in determining sanctions applicable to all violations instruct us to consider whether there was a pattern of misconduct and whether the misconduct occurred over an extended period of time. We note that Alexander's supervisory failures permitted Newberg and Sturm to engage in a pattern of manipulative conduct for more than two years, from approximately mid-1996 through the end of 1998.[56] As the Hearing Panel observed, however, even more rigorous supervision would not likely have detected the relationships between the Shell Company shareholders and Newberg and Sturm, or the fact that Newberg and Sturm had connections to the Cayman Islands Accounts because of their relationship with Oosterwyk.

In weighing all of these considerations, we have determined to impose the following sanctions on Alexander: a fine of $90,000[57] (which is higher than any previous fine that has been imposed on Alexander in any matter that has been fully adjudicated); and a suspension in all capacities for one year. We conclude that Alexander's supervisory failures were egregious, and that a one-year suspension is therefore necessary for purposes of remediation. Thus, the Hearing Panel's decision to suspend Alexander in all capacities for 90 days is vacated. Additionally, we do not concur with some of the conclusions that the Hearing Panel reached in support of its

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[54] See Guidelines at 108 (2001 ed.) (Supervision -- Failure to Supervise).

[55] Id.; Guidelines at 109 (2001) (Supervisory Procedures -- Deficient Written Supervisory Procedures).

[56] See Guidelines at 9 (Principal Considerations in Determining Sanctions, Nos. 8 and 9).

[57] The $90,000 fine is more than the combined maximum fines recommended in the Guidelines for failure to supervise ($50,000) and deficient written supervisory procedures ($25,000). A fine slightly higher than the fines recommended in the applicable Guidelines is necessary, however, to impress upon Alexander the seriousness of his supervisory responsibility.

sanctions. The Hearing Panel stated "that Alexander got virtually nothing out of Newberg[] and Sturm's misconduct." Even if this were true, which we do not find, it is not mitigating. Having a supervisory system that is reasonably designed to achieve compliance with applicable securities laws and regulations is an affirmative duty. See NASD Conduct Rule 3010(a). Therefore, it is not relevant whether Alexander profited from Newberg and Sturm's misconduct. Additionally, in assessing sanctions for Alexander's supervisory failures, the Hearing Panel concluded that Alexander was the victim of the failures to report outside securities accounts and outside business activities. Such conclusion has no applicability to our assessment of sanctions for Alexander's supervisory failures. The failure to supervise allegation does not charge Alexander with failures in supervision associated with overseeing the proper reporting of outside securities accounts and outside business activities, thus we do not adopt the Hearing Panel's conclusion in that regard.

VI. Conclusion

Accordingly, we order that Newberg be barred from association with any NASD member firm in any capacity for manipulative activity, sales of unregistered securities, and providing false testimony. The bar will be effective as of the date of this decision. Alexander is fined $90,000 and suspended in all capacities for a period of one year. We also impose hearing costs of $13,510.28 on Newberg and Alexander, jointly and severally, and assess appeal costs of $1,634.19 (consisting of $1,000 in appeal costs and $634.19 in appeal hearing transcript costs) on Newberg and Alexander, jointly and severally.[58]

On Behalf of the National Adjudicatory Council,

Barbara Z. Sweeney
Senior Vice President and Corporate Secretary

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[58] We also have considered and reject without discussion all other arguments advanced by 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 non-payment. 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 non-payment.