NASD REGULATION, INC.
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,	:	
Complainant,	:	Disciplinary Proceeding No. CAF010009
v.	:	
	:	Hearing Officer - AWH
DANE STEPHEN FABER (CRD #1020637), Sausalito, CA	:	**Hearing Panel Decision**
Respondent.	:	May 3, 2002

Registered representative (1) made material misrepresentations and omitted to state material facts to customers, in violation of Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and NASD Conduct Rules 2110 and 2120; and (2) made unsuitable recommendations to a customer, in violation of NASD Conduct Rules 2110 and 2310(a). Respondent fined $20,000, suspended in all capacities for one year, and ordered to pay restitution in the amount of $82,220, plus interest, for the material misrepresentations and omissions. Respondent fined $15,000, suspended in all capacities for one year, and ordered to pay restitution in the amount of $52,215, for the unsuitable recommendations. Respondent assessed costs of $3,500.76.

Appearances:

Rodney W. Turner, Esq., and Brian L. Rubin, Esq., for the Department of Enforcement

Patrick Baldwin, Esq., and Christine McNamara, Esq., for Dane Stephen Faber

DECISION

Introduction

On April 6, 2001, the Department of Enforcement ("Enforcement") filed the Complaint in this matter, alleging that Dane Stephen Faber ("Faber" or "Respondent") engaged in fraudulent sales practices by making material misrepresentations and failing to disclose material

facts to customers, and that he made unsuitable recommendations to one of those customers.[1] Both causes of the Complaint concern Interbet, Inc. ("Interbet"), a speculative security. On May 29, 2001, Respondent filed an Answer to the Complaint, denying the allegations against him. A hearing was held in San Francisco, California, on November 14 and 15, 2001, before a hearing panel composed of the Hearing Officer and two current members of District No. 1. Both parties filed post-hearing briefs.

Findings of Fact[2]

I. SMITH CULVER, INC. AND DANE S. FABER

Smith Culver, Inc., a/k/a Smith Culver Investments ("Smith Culver"), became an NASD member firm in 1989, and it ceased operations in August 1997. CX 6C; Tr. 434. The principals and owners of the firm were Thomas Smith and Wayne Culver. RX 15, at R00357, 358. The firm initially had two offices in California – one in Larkspur, a suburb of San Francisco, and the other in Beverly Hills; a third office was located in Palm Beach, Florida. CX 6A, at 6; Tr. 250-51. In approximately March 1997, Smith Culver opened a San Francisco office, moving its operations from Larkspur. Tr. 366.

Dane S. Faber entered the securities industry in 1981, associating with California Municipal Investors ("CMI"), a small regional municipal bond firm located in San Rafael, California. Tr. at 245. He worked at several other firms until he associated with Smith Culver in January 1990 as a registered representative. He joined Smith Culver at the invitation of Wayne Culver, a part owner of the firm, who had worked with Faber at CMI. CX 4, at 6; Tr. 245, 261. By the time Faber joined Smith Culver, he held the following licenses: Municipal Securities

[1] The Complaint originally named two other respondents who resolved the charges against them by settlement.

[2] References to Enforcement's exhibits are designated as CX_; Respondent's exhibits, as RX_; and the transcript of the hearing, as Tr._.

Representative (1981); General Securities Representative (1983); NYSE Supervisor (1985); General Securities Principal (1985); Registered Options Principal (1986); Multi-State Registration (1987); and Municipal Securities Principal (1988). CX 4, at 7; Tr. 246. At one of his previous firms, Faber supervised approximately 25 brokers for two or three years. Tr. 368-69. At Smith Culver, Faber was a senior broker in the San Francisco office, and he was the firm's top producer. Tr. 84. After Smith Culver closed in August 1997, he joined First Securities USA, Inc., and at the time of the Hearing, he was registered with that firm and its successor, Brookstreet Securities. CX 4, at 6; Tr. 245.

On March 14, 1996, through an Order of Acceptance of an Offer of Settlement, Faber was censured, fined $10,000, and suspended for 10 days for making unsuitable recommendations to one of his customers. CX 4, at 13; CX 41.

II. THE SILICON VALLEY IPO NETWORK AND INTERBET, INC.

A. Silicon Valley IPO Network and Its Promoter, Ed Durante

The Silicon Valley IPO Network ("SVIPON") was an entity consisting of ten companies that were allegedly going to be brought public through Initial Public Offerings ("IPOs"). Tr. 54, 105. Ed Durante organized, controlled, and marketed SVIPON through an entity he controlled known as Diablo Associates ("Diablo"). Tr.74-5, 80, 364. Durante had previously worked with Wayne Culver and Faber at CMI. Tr. 261, 364. To fund the operations of these companies, SVIPON sold convertible debentures to investors who would be entitled to shares of each company as it went public. Tr. 252. Interbet was one of those ten companies. Tr. 53, 105.

In approximately November 1996, Thomas Smith, Wayne Culver, and Durante visited Smith Culver's office in Beverly Hills and met with Terry Buffalo[3] and Jonathan Worley[4] to

[3] Buffalo was Smith Culver's president from the middle of 1996 until March 1997. Tr. 78-9.

persuade them to support selling SVIPON. Tr. 54, 80. After hearing the presentation and reviewing materials regarding SVIPON, Buffalo and Jonathan Worley became skeptical of SVIPON and Durante. Tr. 55-7, 80-1. They investigated Durante by searching the Internet and contacting the NASD, and discovered that Durante had been barred by the NASD in 1983. CX 12, at 7; Tr. 55, 84. Buffalo and Jonathan Worley also spoke with Faber about Durante's disciplinary history. Jonathan Worley testified that:

> Dane had called Terry and I to talk specifically about the Silicon Valley deal, what we thought. From that point, Terry and I went into the information that we had about Ed Durante, that he was barred from the NASD, that he had been investigated by the FBI for fraud, or whatever that was, and described what we knew and what we felt about Durante. Dane took it the next level further to describe that he had worked with Durante at a previous firm and he described him as a slick and sleazy person and that he wouldn't put any money into any deal that Ed Durante was involved with.

Tr. 59. Similarly, Buffalo testified that:

> I spoke to Dane a lot about bonds in general, but I know in a conversation that we had it was very obvious to me that Mr. Faber knew Ed Durante from the past. He said that he had worked with him sometime earlier in his career, that he knew that the guy had been barred and wasn't the most upstanding citizen.

Tr. 85. Other brokers in the Larkspur office also had learned from one another that Durante had been barred from the securities industry. Tr. 107-8. Buffalo and Jonathan Worley spoke with Smith and Culver about Durante's bar, warning them that the firm could not engage in business with him. Tr. 62. Because they refused to work on and support the Durante/SVIPON deal, Buffalo and Jonathan Worley were fired in March 1997. Tr. 62-3, 88.[5]

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[4] Jonathan Worley ran the bond trading desk in the Beverly Hills office from the middle of 1996 until March 1997. Tr. 52-3. His brother, Jason Worley, worked in the North Palm Beach, Florida, office from October 1996 until July 1997. Tr. 135.

[5] The Hearing Panel finds both Buffalo and Jonathan Worley to be credible witnesses. They were candid and forthright, and had nothing to gain or lose by testifying in this case. In particular, had they remained with Smith Culver, they would not have been adversely impacted financially by Faber's sale of securities relating to SVIPON. Tr. 64-5; 89.

Once Smith Culver agreed to work with Durante on SVIPON, a number of changes occurred at the firm. Faber believed that, at the time of the Interbet sales, Durante and his associates had an ownership interest, or controlling interest, in Smith Culver. Tr. 336, 348, 354, 363-64. Smith Culver's main office moved from Larkspur to San Francisco, where it shared the same address as a number of SVIPON entities. In particular, Interbet received mail at the same street address as did Smith Culver, _____. RX 7, at R00268; Tr. 295. In addition, representatives of Market Financial, another one of the ten SVIPON companies, also shared Smith Culver's office space. CX 39; Tr. 367. Furthermore, SVIPON and Diablo Associates started working together with the Smith Culver representatives. For example, Durante and Culver issued joint memoranda. CX 33.

B. Faber and Durante's Relationship at Smith Culver

Faber was under the impression that Durante had left CMI "under unusual circumstances," and that there "had been some impropriety." Tr. 261, 263. On November 6, 1996, when Faber saw Durante in the Smith Culver office, he asked Culver whether Durante left the securities industry "under some arguably poor business practice or something." Tr. 262. Culver responded that he was under that impression also, but that "it had been merely rumor." Tr. 263. Faber made no further inquiry into Durante's status in the securities industry.

Durante and Diablo granted certain incentives to Faber for his sales efforts on their behalf. According to an April 1, 1997, letter on Smith Culver Investments letterhead, Faber was to receive a special "incentive package" for selling SVIPON. The letter was signed by Durante for Diablo, and by Culver for Smith Culver. The letter also stated that "Diablo will cause to have paid to Dane Faber through Smith/Culver $50k gross additional compensation + 250 broker

warrants/units." CX 33.[6] The letter also stated that "Diablo Associates and Mr. Faber are desirous of pursuing additional conversations on future option/stock plans as Diablo Associates/Smith/Culver's overall expansion progresses. This bonus plan has been agreed to by Diablo Associates." Durante also presented Faber with two letters from a trust company in Colorado that indicated Faber was to receive shares of Interbet and another SVIPON entity as sales incentives. R15, at R00379, 80, 85-6; Tr. 336.

In addition to the special compensation arrangements he made for Faber, Durante sought to place Faber in a management position at Smith Culver. On June 18, 1997, shortly before the transactions at issue took place, Durante and an associate signed a memo on Smith Culver letterhead which was distributed to all Smith Culver brokers, announcing that Faber "has been named Managing Director of Smith Culver Inc." and that "[a]ll brokers should address daily operational issues to Dane." CX 39. After Dave Cave, the Trading Manager at Smith Culver from March until August 1997, received a copy of the memo, he spoke with Faber about it. Faber told him that Tom Smith and Wayne Culver "were not doing a great job of – they hadn't done such a great job of running the company and that he was looking at what he could do to improve things." Tr. 121. During their conversation, Durante entered Faber's office and talked about "how now things were going to get better and Smith Culver was going to become a real player in the OTC market, that he envisioned Smith Culver being a market maker in all 10 of the Silicon Valley companies when they all went public, and that we were all going to make lots of money and everything was going to be just wonderful from that point on." Tr. 121.[7]

[6] Faber testified that he never actually received any compensation for selling SVIPON, and received only his regular commission for Interbet sales. Tr. 350-51. While he testified that he received commissions of 10%, his later testimony was that he received 50 cents per share, when the shares were executed at $6.00. Tr. 356, 375.

[7] Approximately one month later, on July 23, 1997, Faber signed and sent out a letter using the title of Managing Director. CX 40. However, at the Hearing, Faber denied that he was promoted to Managing Director. Tr. 334. He testified that Tom Smith tore up the memo that same day, as a statement that Durante had neither the authority to

C. Interbet, Inc.

Interbet was a development stage company that was incorporated in Nevada in 1996. It planned to offer Bingo and other waging related games on the Internet. CX 7, at 8-9; CX 8, at 6-7; CX 9, at 4-5. By June 1997, however, none of Interbet's casino games had been established on the Internet, and according to the company's then most recent financial statements, Interbet had generated no revenue, sustained net losses of approximately $196,552, and held only $3,660 in cash. CX 8, at 22-8; CX 9, at 18-24.

On June 6, 1997, Interbet, then a privately held company, entered into an agreement to complete a reverse merger with Bio-Chem, Inc., a publicly held shell company. CX 8, at 3-4; CX 9, at 1-2. Like Interbet, Bio-Chem was also a development-stage company and had never generated any net sales or revenues. CX 10, at 3-5. However, Bio-Chem had $50,000 in cash that it had recently raised through the sale of 100,000 shares of its stock at $.50 per share. CX 10, at 2-3.

Bio-Chem's stock traded on the Over-the-Counter Bulletin Board ("OTCBB") under the symbol "BLXI." CX 11A, 11B, 11E. At the end of May and during the month of June 1997, the stock traded at prices ranging from approximately $.50 per share to $6.25 per share. CX 11 A; 11E. On its last day of trading under the symbol "BLXI", Friday, June 27, 1997, the stock's last trade was at $6.25 per share. *Id*., at 2.

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issue the memo on Smith Culver letterhead, nor the authority to promote him. Tr. 348, 352. Faber stated that he never assumed any supervisory or managerial responsibilities at Smith Culver, and that he used the title of Managing Director "as a marketing tool." Tr. 349. There is insufficient evidence upon which the Hearing Panel could find that Faber actually exercised any supervisory or managerial responsibilities. However, the Hearing Panel notes that Faber's version of the facts is suspect. He admitted that, five weeks after Tom Smith allegedly tore up the June 18 promotion memo, Smith reviewed, initialed, and approved the July 23 letter that Faber signed as Managing Director. Tr. 349, 52-3. The July 23 letter contains Smith's initials in a box on the top right hand corner of the first page of the letter. Faber did not call Smith as a witness to corroborate his story.

Interbet's reverse merger with Bio-Chem was effective on June 13, 1997, and announced in a press release on June 20, 1997. CX 8, at 3-4, CX 9, at 1-2, CX 11B, 11C.[8] On June 30, 1997, the stock resumed trading on the OTCBB under the new symbol "EBET." CX 11D, 11E. On that day, the stock began trading at $6.25 per share. CX 11A; 11E, at 2. The Interbet shares that were sold to Smith Culver's retail customers were not IPO shares; rather, they came from two customer accounts that were opened by Tom Smith just prior to July 8, 1997. Tr. 110-12, 429-31.[9]

Most of the brokers in the San Francisco office of Smith Culver sat in a large boardroom. Durante came into that boardroom and told the brokers, as they were selling the Interbet shares, that the transaction was a reverse merger. Tr. 108-9. Cave testified:

> they came in – and I believe it was Ed Durante that said, 'I want everybody to understand that this is a reverse merger, not an IPO.' . . . In one of the conversations, he said, 'Well, I want to make sure everybody understands this is a reverse merger and this is how it's gonna work,' that there was this company, Bio-Chem, that they were going to deposit stock and that that was going to be the source of the shares for Interbet.

Tr. 108-9. Cave also told Steve Munoz, sales manager of the San Francisco office, that he had to tell his brokers to stop referring to Interbet as an IPO. Tr. 132.[10] There is no evidence that

[8] Jonathan Worley testified that, in late 1996 or early 1997, there was publicly available information about the contemplation of the reverse merger. Tr. 57-8. Buffalo testified that prior to his leaving the firm in March 1997, he learned from Durante, Culver, or Smith that they were trying to complete a reverse merger to obtain a reporting company for Interbet. Tr. 86. During late 1996 or early 1997, Worley mentioned the reverse merger to Faber, who responded that he knew about it, and that "I'm not going to do any of it." Tr. 59-61, 68. Faber denied that anyone told him about a reverse merger and asserted that a public company would not announce news related to an upcoming merger. Tr. 258. However, Faber admitted that he was "vaguely" aware of news reports of a fight between Sun Trust and First Union over a proposed merger with Wachovia. Tr. 297-98.

[9] When actual IPO shares are sold, the issuer's shares are deposited into a Syndicate account and those shares are sold to customers. Tr. 431-32. At Smith Culver, there was no Syndicate account for Interbet shares, and Interbet never registered stock to sell to the public. Tr. 432. Therefore, there is no evidence that Interbet received any proceeds from the shares sold by Smith Culver.

[10] Four or five of the 40 brokers had been referring to Interbet as an IPO. Tr. 126, 131.

Faber heard Durante's comments to the brokers in the boardroom, or that Munoz spoke to him about any reference to an IPO.[11]

III. FABER'S DUE DILIGENCE REGARDING INTERBET

Faber reviewed Interbet's marketing materials[12] and a business plan. Tr. 311, 317, 332. Faber did not recall seeing a prospectus, but testified that the "business plan" was "interchangeable in [his] mind" with a prospectus. Tr. 317. There was, in fact, no prospectus, and Interbet never filed a registration statement to sell securities. Tr. 109-10, 432. Faber also spoke with Smith and Culver who represented that Smith Culver had done due diligence on Interbet, that Smith Culver had retained attorneys to review Interbet, and that those attorneys who assisted in the due diligence were buying Interbet for themselves. Tr. 258-59, 311-12. Faber also relied on the opinion of two of his clients and his father, which was that SVIPON was a "unique and innovative debt financing instrument." Tr. 253-54. Finally, he relied on the fact that the logo of Brookstreet Securities appeared on the SVIPON offering memorandum, believing that the appearance of the logo lent "a certain credibility to the issue." Tr. 254.

Faber knew that Interbet was a development stage company, but he did not know that it had no business, or that it had lost approximately $200,000 since its inception. Tr. 327-29. He did not recall whether he knew Interbet had no revenues. Tr. 328. He did not review publicly available information, such as Interbet's June 24, 1997, Form 8-K, or Bio-Chem's most recent quarterly report. Tr. 316. Prior to selling the shares, he was not aware that Interbet had filed an 8K or a 10Q. Tr. 351. He did not consult a Bloomberg machine for information regarding

[11] Faber's office was in the southeast corner of the 30,000 square foot office of Smith Culver. Tr. 251.

[12] Faber relied on the projections contained in the marketing materials, which were described as "merely estimates of possible results based on assumptions which may or may not be true." RX 3, at R000121; Tr. 329-30.

Interbet or Bio-Chem. Tr. 314.[13] He did not research Interbet or Bio-Chem on the Internet. Tr. 314. He did no independent research regarding Interbet or Bio-Chem to find any information, news, trading information, public filings, or registration statements. Tr. 314, 317.[14] He did no research on possible competitors to Interbet. Tr. 317.

IV. FABER'S SALES OF INTERBET TO CUSTOMERS

A. Customer R.K.

R.K., a retired federal government employee and attorney, began investing with Faber prior to his arrival at Smith Culver. Tr. 158-60. R.K., an experienced investor who began investing in securities in 1959, originally held municipal bonds in his Smith Culver account with Faber. Tr. 160, 162. According to R.K., he and Faber had established a "friendship" over the phone, and R.K. relied upon Faber's recommendations. Tr. 163. On those occasions when R.K. did not follow Faber's recommendations, it was because R.K. needed the money for other reasons and not due to any doubts about Faber's recommendation. Tr. 163-64.

In June 1997, R.K. received a telephone call from Faber during which Faber recommended that he purchase an Internet "IPO opportunity." Tr. 164-66. R.K. had assumed that an initial offering of common stock was to "capitalize a company that was about to expand its operations" Tr. 165. Faber did not tell him that the stock was being sold by individuals and that proceeds from the sale would not go to Interbet. Tr. 178. Faber presented Interbet as a different type of investment from R.K.'s previous purchases with Faber. R.K. testified that "it

[13] A Bloomberg machine is part of an independent computer network system that provides financial information and news. Faber testified that, as a broker, he did not have access to the Smith Culver Bloomberg machine. Tr. 271-72, 312. However, his testimony is inconsistent with testimony of Grace Stoneham, another broker who worked side-by-side with Faber. She testified that she did have access to the Bloomberg machine. RX 21, at R00826-27. Faber had a computer on his desktop that gave him access to stock quotes, and financial news and information. Tr. 365-66.

[14] He did not recall whether he had read any press releases announcing Bio-Chem's acquisition of Interbet or Bio-Chem changing its name to Interbet. Tr. 313-14.

was presented to me as an opportunity, as something different and something perhaps a little more volatile, in the sense of making more money and probably in a shorter time frame than municipal bonds." Tr. 166. Faber told him that he thought "it was a chance for us to double our money." Tr. 166.[15] R.K. never received a prospectus for Interbet. Tr. 169. After Faber's recommendation, R.K. had a positive impression of Interbet, thinking it was a good investment opportunity and, ultimately, he purchased the stock because he had "faith and confidence" in Faber. Tr. 167, 169-70. On July 8, 1997, R.K. purchased 5,000 shares of Interbet at $6 per share (price of $5.73 and $0.27 markup), for total cost of $30,005. CX 19A, at 2, CX 19B; Tr. 170-71.

While soliciting R.K. to purchase Interbet, Faber did not disclose any specific risks about the stock. Tr. 175. Faber did not disclose that Interbet had suffered losses since its inception. Tr. 176. According to R.K., knowledge of Interbet's losses would have been an important factor that he would have considered in deciding whether to purchase shares of Interbet. Tr. 176. Faber failed to disclose that Interbet had not generated any revenues since the company's inception. Tr. 176. This lack of revenue is another factor that R.K. would have considered, had he known about it, when he was deciding whether to purchase Interbet. Tr. 176. Faber did not disclose to R.K. that Interbet's stock had traded publicly prior to the purported IPO date. Tr. 178. R.K. would have considered that fact when deciding whether to purchase Interbet. Tr. 178.

R.K. still owns his Interbet stock, now known as Virtual Gaming. His 5,000 shares became 100 shares following a reverse split. CX 19C, at 2; Tr. 180. He has not sold those shares because they are worthless. Tr. 180. R.K. still has an account for which Faber is his registered representative, but there has been no activity in it since Faber sold Interbet shares to R.K. Tr. 181.

[15] R.K. elaborated that "it was an estimate by him, it was not presented as a guarantee, and I didn't take it that way." Tr. 167.

B. Customer D.M.

1. Background

D.M. is 56 years-old and has been a bookkeeper/office manager for the past ten years. Tr. 187-88. From 1995 through 1997, her income ranged from approximately $21,000 to $32,000. CX 25, at 1; Tr. 188-89. In February 1996, she opened an IRA rollover account with Smith Culver, using the approximately $20,500 she had in a pension fund. At the end of 1996, she also had approximately $30,000 in an IRA at a savings and loan association, and $26,000 in a savings account. CX 25, at 1; Tr. 189-90. She owns a house, valued at $175,000, where she has lived for 26 years, and she paid off the mortgage in 1994. CX 25, at 1; Tr. 186, 228-29.

Prior to February 1996, D.M. never had a brokerage account, and all of her savings were invested in certificates of deposit and bank accounts. Tr. 191-93. Her mother suggested that she seek a better return on her money since D.M. was planning to retire in 12 years, and that she open an account with Faber, who had been her mother's broker for several years. Tr. 193.

During their initial conversation, D.M. explained to Faber that she planned to retire when she was 62 years old and wanted to purchase bonds so that she would make a little more than she was then earning through her savings account and certificates of deposit. CX 20A, at 10-11. D.M. has no recollection of Faber asking about her assets or her income, and she does not recall providing him with that information. Tr. 194-95. Faber did not produce any documents containing that information at the Hearing.

In February 1996, when she opened her Smith Culver IRA Rollover account with a deposit of approximately $20,500, D.M. instructed Faber to buy bonds. Tr. 191, 197. In accordance with those instructions, her deposit was used to purchase OMI Corporate bonds. Those bonds were called in August 1996, and the proceeds were used to purchase Roadmaster

Industry bonds. CX 23 A-R; Tr. 198. Faber did not discuss the transactions with D.M. prior to effecting them. After D.M. received a transaction notice reflecting the purchase or sale of a bond, she would call Faber for an explanation of the transaction. RX 20 at R00720; Tr. 215-16, 235, 237. Essentially, she accepted Faber's purchases and sales because she "trusted him to do good for me," She testified that "[h]e was always very knowledgeable, very nice to me," and "I had no reason not to [trust him]." Tr. 215, 217.

Pleased with the performance of the bonds in her pension fund rollover, D.M. opened a second account with Faber in May 1997, using the proceeds of approximately $29,000 from a recently matured certificate of deposit in a non-qualified account. CX 24 A, at 2; Tr. 199, 201. She told Faber that she wanted to buy bonds in her new account. Tr. 199, 202. Accordingly, Faber recommended, and D.M. purchased, Wickes Lumber Company bonds. CX 24 A, at 2; Tr. 202. D.M. held the Wickes bonds until they were sold out of her account approximately one month later, on June 27, 1997. CX 21; Tr. 202-3.

2. Faber's Recommendation of Interbet

In late June or early July, 1997, after receiving the transaction notice reflecting the sale of her Wickes bonds, D.M. called to ask Faber why they were sold. Tr. 203, 205. Faber told her that he had a great opportunity for her to purchase an IPO stock that could triple her money in a short period of time. CX 20A, at 4-6; Tr. 211-12. Since she did not know what an "IPO" was, he explained the concept to her, and at that time, she wrote down the words "Initial Public Offering" on the Wicks transaction notice. CX 21; Tr. 203-4. D.M. did not recall whether Faber mentioned Interbet's name. Tr. 205. However, at the time of this phone call, she was under the impression that Faber had already purchased the initial public offering stock for her account. Tr. 236.

Faber did not mention anything to D.M. about Interbet's business or its revenues. Tr. 211-12. Faber did not disclose to her any risks involved with purchasing Interbet. Tr. 213. He failed to disclose that Interbet had suffered losses since its inception, and he did not disclose that Interbet had not generated any revenue since its inception. Tr. 213. Had these facts been disclosed to D.M., she would have told Faber that she did not want to purchase shares of Interbet. Tr. 213.

Following this conversation, D.M. received both her IRA Rollover account statement and her Non-Qualified Investment account statement. She then learned that Interbet was the name of the initial public offering company, and that Faber had sold all of her bonds to purchase Interbet for each account. CX 22A, at 2; CX 22D, at 2; RX 20, at R00709; Tr. 207-9.[16]

D.M. never sold these shares, despite their decline in value, because Faber encouraged her to hold them, and because, subsequently, they became nearly worthless. CX 26; Tr. 220, 223, 226. As the price was falling precipitously, Faber continuously encouraged her to keep the stock by making optimistic statements about Interbet.[17] Due to a reverse split, D.M. now owns 178 shares of Virtual Gaming. CX 22C, 22F; Tr. 223-26.

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[16] In her IRA Rollover account, the following transactions occurred:

On July 8, 1997 (settlement date of July 11), after the June 27 sale of Wickes bonds, 400 shares of Interbet common stock were purchased at $6 per share (price of $5.73 and $0.27 markup) for $2,405. CX 22A, at 2, CX 22B, at 2; Tr. 206.

On July 17, 1997 (settlement date July 22nd), after the July 17 sale of Roadmaster bonds, 3,500 shares of Interbet were purchased at $6 per share (price of $5.73 and $0.27 markup) for $21,005. CX 22A, at 2; CX 22B, at 1.

In her Non-Qualified Investment account, the following transaction occurred:

On July 8, 1997 (settlement date of July 11), after the June 27 sale of Wickes bonds, 4,800 shares of Interbet common stock were purchased at $6 per share (price of $5.73 and $0.27 markup) for $28,805. CX 22D, at 2, CX 22E; Tr. 207-08.

[17] Faber 2/6/98 e-mail (comparing Interbet to Netscape and telling her to "Keep the faith"); CX 26, at 1; Tr. 220, 226-27. Faber 6/22/98 e-mail (reporting "Good News!" about "our little company"; "I continue to have great expectations despite being behind schedule"; advising at a time when price was less than $1, "I wouldn't advise anyone to sell for less than $7 a share, at this point"; "I remain confident in this investment and this news merely buoys my optimism." CX 26, at 2. Faber 5/3/99 e-mail ("[I]t now appears that our little company will be sold to another bigger company. Of course, you and all the other shareholders will have to approve of the price, and I don't think too many people will sell for much less than what they paid"). CX 26, at 4.

V. FABER'S CREDIBILITY

In making the preceding findings of fact, the Hearing Panel has resolved a number of credibility issues against Faber on the basis that his Hearing testimony was contradicted by contemporaneous documents and inconsistent with the testimony of other credible witnesses and with testimony that he gave earlier in this proceeding. The following examples are illustrative.

A. Whether Faber Recommended Interbet

At the Hearing, Faber denied that he recommended that D.M. purchase Interbet. Tr. 272. Instead, he asserted that D.M., at her mother's direction, called him and insisted that he purchase Interbet stock for her. Tr. 272-73. Faber testified that D.M's mother found out about Interbet when he called her and, he "think[s]," he recommended it. Tr. 356. In support of his story, Faber claimed that he learned at a meeting with D.M. and her mother that they had taken classes about investing, and that her mother had gotten information about "a balanced portfolio." Tr. 274. Faber also testified that D.M. talked about the balanced portfolio concept when he talked to her about investing in Interbet. *Id.* However, D.M. testified that she had only one face-to-face meeting with Faber, and that meeting took place in the Fall of 1997, well after the purchase of Interbet. Tr. 232. Moreover, Faber could not explain how D.M. sought to "balance" her portfolio by replacing all of her bonds with one speculative stock, Interbet. Tr. 383-87. Had the purchase of Interbet resulted from an unsolicited order, there would have been no reason for D.M. to write the words "Initial Public Offering" on her Wickes sales confirmation when she asked Faber why those bonds had been sold on June 27. Neither Interbet purchase confirmation notice carries a notation that the purchase was unsolicited. CX 22B, at 1-2. Moreover, Faber himself, in an e-mail to D.M., referred to the transaction as a recommendation. CX 26 at 3, (8/11/98 e-Mail from Faber) ("Undoubtedly the background of Durant (sic), Vishno, Zink and

Deck would have prevented me from *recommending the stock to you*") (emphasis added).[18] Finally, prior to the Hearing, Faber acknowledged that he recommended that D.M. purchase Interbet. In Faber's Opposition to Enforcement's Motion for Summary Disposition/Motion to Strike at 7, he claimed that the "NASD failed to properly and timely investigate any wrongdoing in connection with Interbet, even though it received complaint letters from [another customer], . . . long before *Respondent recommended Interbet to [R.K. and D.M.]*" The Opposition also recites that "Respondent *recommended* Interbet in reliance on Smith Culver, Inc.'s ('SC') approving it for sale, SC's due diligence, and SC's representations to him in that regard," and that "Respondent has *recommended* Interbet in reliance on the conduct of SC" (emphasis added).

B. D.M.'s Inheritance

Faber testified that D.M. was going to inherit funds from her mother, and that he took that inheritance into account when she made her purchase. Tr. 275, 380. D.M. denied that she had any expectation of receiving an inheritance. In fact, her mother explicitly told her that she had been left out of her will. Tr. 233. Faber's testimony about an inheritance is based upon his recollection of a conversation that took place at D.M.'s mother's house, involving Faber, D.M., and her mother. Tr. 231-33; 380. D.M. recalled that the meeting took place in October or November 1997 because they were talking about computers and she had just purchased one. The Hearing Panel credits D.M.'s testimony and finds that the the conversation took place several months after the purchase of Interbet, and that, therefore, Faber could not have taken into

[18] Next to the text of that e-mail, D.M. handwrote the phrase "He did not recommend." CX 26, at 3. She used that phrase because he did not talk to her specifically about a stock with the name Interbet prior to the purchase. Rather, she found out that it was Interbet that she had purchased only after she received her account statements. Tr. 222. When she earlier found out that her Wickes bond had been sold, Faber told her about a great IPO opportunity, but she did not recall whether he mentioned the name of the company at that time. Tr. 211.

consideration the possibility of an inheritance in assessing her financial suitability to purchase Interbet.

C. Faber's Experience With IPOs

Faber's testimony was inconsistent about his prior experience with IPOs and transactions involving common stock. Twice during the Hearing, Faber testified that he had previously been involved with only one initial public offering. Tr. 246, 353-54. However, during the investigation, he testified to the staff that he had been involved with half a dozen. CX 31 at 17-8.

D. Prior Disciplinary History

Faber's testimony about his prior disciplinary action was inconsistent with documentary evidence. First, he claimed that the prior disciplinary proceeding involved "suitability regarding a corporate bond," when, in fact, it concerned unsuitable recommendations during a two and one-half year period. Faber eventually settled a parallel arbitration claim for $155,000. CX 4 at 14; Tr. 248, 295, 337. Second, although he testified that the client involved in the action died unexpectedly, she was over 100 years of age at the time of her death. Tr. 295. Third, although he recalled that he was fined $7,500, in fact, he was fined $10,000. CX 4, CX 41; Tr. 247, 296. Fourth, he testified that he was not aware that the settlement of the disciplinary action could be put in issue in future matters. However, the Offer of Settlement that he signed clearly states that the information could be used for that very purpose. CX 41; Tr. 247. Fifth, he claimed that his statement of corrective action, appended to the Offer of Settlement, was meant to deal only with bonds Tr. 339. In fact, it required him to "provide written evidence of the basis for *each* recommendation made in *all* customer accounts . . . [and] a brief statement regarding the suitability of the recommendation for the customer and how it compares with stated account objectives." (Emphasis added.) CX 41. Finally, the Hearing Panel notes that he admitted that

he failed to comply with the statement of corrective action. He testified that it was not his practice to make notes reflecting the basis for a recommendation, a comparison of the recommendation with the customer's current holdings, or the suitability of the recommendation as it related to the customer's stated account objectives. Tr. 303.

Discussion

I. FABER MADE MISREPRESENTATIONS AND OMISSIONS OF MATERIAL FACT

A. Legal Standard

To establish that Faber violated Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and NASD Conduct Rule 2120, Enforcement must prove that: (1) Faber's misrepresentations and/or omissions were made in connection with the purchase or sale of securities; (2) his misrepresentations and/or omissions were material;[19] and (3) he made them with the requisite intent, i.e., scienter.[20] *See DBCC v. Euripides*, No. C9B950014, 1997 NASD Discip. LEXIS 45, at *18 (NBCC July 28, 1997).[21]

The duty of fair dealing requires that stock brokers have an adequate basis for their recommendations, and those recommendations should be based on a reasonable investigation.

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[19] The test for materiality is "whether the reasonable investor would consider a fact important" in making an investment decision, or whether disclosure would "significantly alter . . . the 'total mix' of information made available." *Martin R. Kaiden*, No. 41629, 1999 SEC LEXIS 1396, at *18, n.25 (July 20, 1999); *TSC Indus., Inc. v. Northway, Inc.* 426 U.S. 438, 449 (1976).

[20] Scienter is "a mental state embracing intent to deceive, manipulate, or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976). To prove scienter, there must be a showing that the respondent acted intentionally or with severe recklessness. *See M. Rimson & Co.*, Inc., 1997 SEC LEXIS 486, at *95 (Feb. 25, 1997). Recklessness has been defined as highly unreasonable conduct involving not merely simple or excusable negligence but an extreme departure from the standards of ordinary care. *See Market Reg. Comm. v. Michael B. Jawitz*, No. CMS960238, 1999 NASD Discip. LEXIS 24, at **19-20 (NAC July 9, 1999) (citing *Hollinger v. Titan Capital Corp.*, 914 F.2d 1564, 1568-69 (9th Cir. 1990) *cert. denied*, 499 U.S. 976 (1991) and cases there cited). A respondent may not plead ignorance as a defense to recklessness if a reasonable investigation would have revealed the truth to the defendant. *See SEC v. Infinity Group*, 993 F. Supp. 324, 330 (E.D. Pa. 1998).

[21] Conduct Rule 2110 requires member firms or persons associated with member firms to observe "high standards of commercial honor" and "just and equitable principles of trade." Misrepresentations violate Conduct Rule 2110. *Ramiro Jose Sugranes*, No. 35311, 1995 SEC LEXIS 234, at **3-4 (Feb. 1, 1995). Proof of scienter is not required to prove a misrepresentation violation under Rule 2110. *See Euripides*, 1997 NASD Discip. LEXIS 45, at *18.

Hanly v. SEC, 415 F.2d 589, 597 (2d Cir. 1969); *Steven D. Goodman*, No. 43889, 2001 SEC LEXIS 144, at *12 (Jan. 26, 2001). The Second Circuit summarized the responsibilities of brokers under the antifraud provisions as follows:

> [T]he standards by which [registered representatives] . . . must be judged are strict. [A salesman] cannot recommend a security unless there is an adequate and reasonable basis for such recommendation. He must disclose facts which he knows and those which are reasonably ascertainable. By his recommendation he implies that a reasonable investigation has been made and that his recommendation rests on the conclusions based on such investigation. Where the salesman lacks essential information about a security, he should disclose this as well as the risks which arise from his lack of information.

Hanly, 415 F.2d at 597.

A broker is "under a duty to investigate" before making a recommendation, and he "cannot deliberately ignore that which he has a duty to know and recklessly state facts about matters of which he is ignorant. He must analyze sales literature and must not blindly accept recommendations made therein." *Id*. at 595-96; *see also DOE v. Averell Golub*, No. C10990024, 2000 NASD Discip. LEXIS 14, at *20, n.15 (NAC Nov. 17, 2000). "Elementary prudence" requires brokers to review public filings when making recommendations. *Bruce William Zimmerman*, No. 12690, 1976 SEC LEXIS 1096, at *6 (Aug. 5, 1976). The degree of independent investigation varies in each case; however, smaller companies of recent origin require thorough investigation. *See SEC v. Hasho* 784 F. Supp. 1059, 1107 (S.D.N.Y. 1992). Brokers cannot hide behind reliance on employers and issuers to insulate them from liability for violation of the anti-fraud provisions of the securities laws. *See id*, at 1108.[22]

[22] Respondent tendered Allan Rockler as an expert witness to opine on industry standards for the extent to which brokers could rely on a firm's due diligence. He testified that no registered representative is required to do his own due diligence and that, if Faber made any misrepresentation based on information given to him by his firm, he is not responsible for the misrepresentation, only the firm is responsible. Tr. 396. The Hearing Panel does not give any weight to his testimony for the following reasons: (1) Mr. Rockler has conducted no study of the issue upon which he was called to testify; (2) he has not published on any securities issue; (3) he has never read any SEC cases on the issue; (4) he has read only some NASD disciplinary decisions, but believes that they are not to be relied upon as

B. Faber's Misrepresentations and Omissions of Material Fact

While soliciting his customers to purchase Interbet common stock, Faber misrepresented that Interbet was being sold pursuant to an Initial Public Offering, and made baseless price predictions and generalized assurances of success regarding the stock. He omitted to give them negative financial information about the issuer and failed fully to disclose the speculative nature of the security.

Customers R.K. and D.M. both bought shares of Interbet on July 8, 1997, at a $6.00 per share ($5.73 plus $0.27 markup). They were told by Faber that they had purchased the shares in an Initial Public Offering. In fact, Interbet had begun trading on the OTCBB nine days earlier at $6.25 per share. There was no registered offering of Interbet stock after the reverse merger with Bio-Chem, and the customers were actually buying Interbet in the secondary market. Moreover, those customers purchased their stock from two accounts that were opened at Smith Culver, and not from the issuer. The misrepresentation that they were purchasing shares in an IPO was material. Faber described Interbet as an "IPO opportunity," suggesting that the fact it was an IPO was significant.[23] A reasonable investor would consider whether shares were trading in the secondary market to be an important fact in making an investment decision. Especially at a time when the IPO market was hot, disclosure that shares were trading in the secondary market, and at

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precedent; (5) he gave no rationale for the opinion he offered; and (6) his opinion is contrary to more than 30 years of established case law.

[23] Faber's reliance on *DBCC v. Richard Earl Gregory*, No. C06940002, 1995 NASD Discip. LEXIS 16 (NBCC April 6, 1995) is misplaced. Although the broker in that case failed to disclose that the company went public via a reverse merger, the company did register the offering, and the customer was told that the offering had been completed and that the stock was trading in the secondary market. The NBCC did not find credible the customer's assertions that he thought he was buying an IPO. Under those circumstances, the NBCC found that the offering was correctly described as an IPO because it was the first registered offering of stock to the public. Here, there was no registered offering of stock, the customers were not told that the stock was trading in the secondary market, and the customers credibly testified that they thought they were buying shares in an IPO.

a price that had gone down since trading began, would "significantly alter the 'total mix' of information made available." *TSC Indus*., 426 U.S. at 449.

Faber failed to disclose that Interbet had no business, never generated any revenues, and had suffered losses since its inception. Faber did not know about that negative information, even though it was publicly available. As a result, he did not educate himself about the full range of risk factors involved in a purchase of the stock. Material facts include not only earnings of a company, but also those facts that affect the probable future of a company and that may affect the desires of investors to buy, sell, or hold the company's securities. *See Hasho*, 784 F. Supp. at 1108. Failure to disclose the speculative nature of a recommended security or negative financial information about the issuer violates the anti-fraud provisions of the securities laws and NASD rules. *See id.* at 1109.

Predictions of specific and substantial price increases for speculative securities of unseasoned companies are inherently fraudulent and unjustifiable. *See id*.; *Steven D. Goodman*, No. 43889, 2001 SEC LEXIS 144, at *14 (Jan. 26, 2001).[24] Predictions of a substantial increase in the price of any security without a reasonable basis is also fraudulent. *See Hasho*, 784 F. Supp. at 1109; *C. James Padgett*, No. 38423, 1997 SEC LEXIS 634, at **23-24 (Mar. 20, 1997), *aff'd*, 159 F.3d 637 (D.C. Cir. 1998) (table). Courts and the SEC have found no reasonable basis for price predictions where the issuers had suffered losses or operated at small profits. *See, e.g., Hasho*, 784 F. Supp. at 1109; *Martin Herer Engelman*, No. 35729, 1995 SEC LEXIS 1197, at *22 (May 18, 1995). Moreover, the Court in *Hasho* stated:

> The fraud is not ameliorated where the positive prediction about the future performance of securities is cast as opinion or possibility rather than as a

[24] Securities of "development-stage companies with a limited history of operations and no profitability" are speculative. *Clinton Hugh Holland*, No. 36621, 1995 SEC LEXIS 3452, at *9, n.16 (1995), *aff'd*, 105 F.3d 665 (9th Cir. 1997) (table).

> guarantee. Such material statements violate the anti-fraud provisions if no adequate basis existed for making such a statement.

784 F. Supp. at 1109 (citation omitted). Therefore, Faber's prediction of a substantial increase in the price of Interbet to customers R.K. and D.M. had no reasonable basis in fact. In none of his testimony did he offer any basis for making price predictions. Because he was unaware of Interbet's financial posture, he could have no reasonable basis for making such predictions, and accordingly, they were fraudulent.[25]

C. Faber's Misrepresentations and Omissions Were Reckless

Throughout this proceeding, Faber has taken the position that he was entitled to rely on Smith Culver's approval of Interbet as a product, and on Smith Culver's due diligence. Not only is that reliance misplaced, but it flies in the face of numerous red flags that Faber chose to ignore - red flags that should have prompted him to question the representations made to him by Tom Smith, Wayne Culver, and Ed Durante.

Faber admitted to speaking with Buffalo and Jonathan Worley about Durante, and the fact that Durante had left his earlier firm "under unusual circumstances." Tr. 261, 304. Faber claimed that he checked with Culver who said that it was "merely a rumor" that Durante had left the firm because of "some impropriety." Tr. 262-63, 381-82. Faber failed to explain why he did not act to resolve the conflicting assertions, by Buffalo and Jonathan Worley, on the one hand, and Culver, on the other, regarding Durante's status. He easily could have done so by contacting the NASD or searching the Internet. Faber obviously thought that the information on Durante's

[25] Respondent argues that *Hasho* is not relevant because it involved a boiler room operation with high pressure sales tactics. However, the fact that disciplinary actions, arising out of baseless price predictions, often involve boiler room type operations does not excuse such predictions where they are not accompanied by high pressure sales tactics. *See, e.g. Dan King Brainard*, No. 20408, 1983 SEC LEXIS 293, at *12-14 (Nov. 22, 1983). Moreover, although Enforcement did not allege a boiler room operation in this case, the Hearing Panel notes that there is evidence of special compensation arrangements for Faber, and an unusually close relationship between the issuer and Smith Culver. When Buffalo and Jonathan Worley refused to work on the SVIPON deal, they were fired.

status was material. He testified that had he known the truth about Durante's background, he would not have sold Interbet.[26] Tr. 304.

Faber testified that he relied upon the due diligence that Smith Culver had conducted regarding SVIPON. Tr. 258-59, 291. However, that "due diligence" was not conducted by disinterested parties. Smith Culver had a close business relationship with Durante and Diablo, and the attorneys who were retained to do the due diligence were investors in Interbet. Tr. 71-2. Notwithstanding his conversations with Buffalo and Jonathan Worley about Durante's background, Faber read only marketing materials and a business plan. Those conversations never prompted him to review the firm's due diligence file regarding Interbet, or to conduct any type of investigation of the issue or Durante on his own.

There were a number of facts that should have put Faber on notice that Interbet was not an IPO. First, he had conversations with Buffalo and Jonathan Worley who told him that Interbet was a reverse merger. Second, the memorandum, addressed to Faber on Smith Culver letterhead, which described the incentive package he was to receive for selling SVIPON, clearly stated that free trading stock would be derived from, among other sources, "full reporting publicly traded shells." Third, he never saw an actual prospectus for Interbet, nor was there one that he could have sent to his customers.[27] Others at the firm stated that they realized that they were not selling IPO shares because they knew that there was no prospectus. CX 37(1), at 54, 80; CX 37(3), at 113-14, 132; CX 37(4), at 139; CX 37(5), at 81-3, 85. Finally, the confirmation notices did not state that Interbet was a new issue, but they did show that Faber was earning compensation that included a portion of the spread and a markup of 27 cents per share.

[26] As noted previously, Faber told Buffalo that he knew Durante had been barred. Tr. 59.
[27] Had Interbet been an IPO, there would had to have been a prospectus and Faber would have been obliged to furnish his customers with one, unless the firm's compliance manual specified that the firm would do so for the representative. Faber did not introduce evidence that the firm obligated itself to distribute prospectuses.

These red flags should have put Faber on notice to conduct a reasonable investigation into the Interbet issue. Had he done so, he would have informed himself of the truth of those matters that he misrepresented to his customers. Having failed to do so, his actions were reckless, in that they departed from the standards of ordinary care, and they subjected his customers to the loss of their funds.[28] By recklessly making those material misrepresentations to R.K. and D.M. in connection with the sale of Interbet stock, Faber violated Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and NASD Conduct Rules 2110 and 2120.

II. FABER MADE UNSUITABLE RECOMMENDATIONS

A. Legal Standard

Conduct Rule 2310(a) provides that, in recommending a purchase of a security to a customer, a broker "shall have reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts, if any, disclosed by such customer as to his other security holdings and financial situation and needs." The suitability rule requires more than mere risk disclosure. A broker must ensure that the customer understands the risks involved in a recommended securities transaction. *DOE v. Chase*, No. C8A990081, 2001 NASD Discip. LEXIS 30 at* 17 (NAC Aug. 15, 2001) (citing *Patrick G. Keel*, No. 31716, 1993 SEC LEXIS 41, at **9-13 (Jan. 11, 1993)). Even if a customer seeks to engage in highly speculative or otherwise aggressive trading, a broker is under a duty to refrain from making recommendations

[28] On brief, Faber cites *DOE v. Ryan Mark Reynolds*, No. CAF990018, 2001 NASD Discip. LEXIS 17 (NAC June 25, 2001) and argues that his good faith, - evidenced by his own, and his father's, purchase of Interbet, in addition to his reliance on the word of Wayne Culver, his best friend for 20 years - prevents a finding of intentional or reckless misrepresentations. The Hearing Panel is not persuaded by that argument because the facts in that case differ significantly from those in this case. *Reynolds* involved a representative who had less than two years experience in the securities industry, had little guidance or supervision, yet had performed a basic investigation of the company, including inspection of assets, discussions with potential competitors, and review of a study and news articles about the company. Moreover, violation of the duty to investigate brings the misrepresentations within the term "willful" in the Exchange Act. *Hanley*, 415 F.2d at 595-97.

that are incompatible with the customer's financial profile.[29] *DOE v. Jack H. Stein,* No. C07000003 (NAC Dec. 3, 2001), *at* http://www.nasdr.com/pdf-text/nac1201_01.pdf.

B. Faber's Recommendations to D.M. were Unsuitable

Faber's recommendation of a speculative security to D.M. was contrary to her stated investment objectives.[30] She sought moderately conservative investments for her anticipated retirement, which was about ten years in the future. Prior to the Interbet purchases, she had invested only in certificates of deposit and savings accounts. When she opened a brokerage account, she invested only in corporate bonds. Her investment objectives never changed. The only reason Interbet appeared in her account was because Faber purchased it for her. Faber did not have reasonable grounds for concentrating her entire investment portfolio in one speculative stock. The only rationale he could provide was to assert that D.M. sought a "balanced portfolio." However, the Hearing Panel does not find as a fact that she sought a balanced portfolio, and, in any event, even Faber conceded that with her portfolio consisting only of Interbet, it certainly could not be considered to be balanced. The concentration of an account into one speculative stock was clearly unsuitable. *See Clinton H. Holland, Jr*., No. 36621, 1995 SEC LEXIS 3452, *12 (Dec. 21, 1995) (concentration of high risk and speculative securities and shift from conservative to speculative investments were not suitable), *aff'd*, 105 F.3d 665 (9th Cir. 1997) (table); *DOE v. Chase*, 2001 NASD Discip. LEXIS 30, at *19 ("We also find that contrary to Chase's assertion that concentration in one or two speculative stocks can be a sound investment

[29] By definition, the NASD suitability rule, Conduct Rule 2310, applies to "recommendations to customers." Faber's expert witness testified that there "is no suitability issue" regarding D.M. because the purchases of Interbet were unsolicited. Tr. 396, 426-28. That opinion is of no import because the Hearing Panel finds that Faber recommended the purchases.

[30] The fact that Faber purchased Interbet for D.M.'s account without first informing her does not change the analysis. Transactions that were not specifically authorized by a client, but were executed on the client's behalf, are considered to have been implicitly "recommended" under NASD rules. *Paul C. Kettler*, No. 31354, 1992 SEC LEXIS 2750, *5, n.11 (Oct. 26, 1992).

strategy, and regardless of YH's alleged change in investment objectives, Chase's recommendations to purchase FHC shares until it was the only stock in YH's entire portfolio were unsuitable"); *Daniel R. Howard*, No. C11970032, 2000 NASD Discip. LEXIS 16, at *19 (NAC Nov. 16, 2000) ("[u]ndue concentration of these speculative securities [approximately 90 percent of the customer's holdings], [made] the recommendations particularly unsuitable").

Even if the Hearing Panel were to find that D.M. told Faber that she would inherit money from her mother, that possibility does not provide an adequate basis upon which he could make a suitability determination. Representatives must make recommendations "only on the basis of the concrete information that [the customer] did supply and not on the basis of guesswork as to the value of other possible assets." *Eugene Erdos*, No. 20376, 1983 SEC LEXIS 332, at *7 (Nov. 16, 1988), *aff'd*, 742 F.2d 507 (9th Cir. 1984).

SANCTIONS

I. MISREPRESENTATIONS AND OMISSIONS

For reckless misrepresentations and omissions of material facts, the NASD Sanction Guidelines recommend a fine of $10,000 to $100,000, and a suspension in any or all capacities for a period of 10 business days to two years. NASD SANCTION GUIDELINES, at 96. Citing what it considers to be numerous aggravating factors, Enforcement seeks a suspension for one year, a fine of $50,000, and restitution for the two customers. Respondent argues that he incurred significant legal fees to defend himself in this matter; that he has suffered personal difficulty in knowing that his very close friend, Wayne Culver, lied to him regarding Interbet; and that, as a sole practitioner working out of a home office, there is no one else to handle his business if he is suspended, and therefore, a suspension will essentially put him out of business permanently. In coming to the conclusions that follow, the Hearing Panel has considered the arguments of the

parties, as well as the General Principals set forth in the Sanction Guidelines and the Principal Considerations noted therein.

At the outset, the Hearing Panel notes that Faber's conduct was reckless and must be deterred. His past disciplinary conduct requires that the sanctions in this case be progressive. There are multiple violations at issue; and the two customers, who, for all practical purposes, have lost their entire investments, should receive restitution. In making his misrepresentations and omissions, Faber ignored a number of red flags that should have prompted him to initiate his own independent investigation of Interbet. Moreover, after the price of the stock began to drop, he continued to encourage D.M. to hold the stock, sending her encouraging messages about its future. Even if he naively continued to rely on the word of his "dear friend," Wayne Culver, - to the point of investing his own, and his father's funds in Interbet – he allowed that reliance to trump his obligation to observe high standards of commercial honor and equitable principles of trade when dealing with his customers.

The Hearing Panel will impose a fine and a one-year suspension for the misrepresentations and omissions. However, because the Hearing Panel believes that restitution is appropriate in this case, but has concerns that Enforcement's proposed fine might affect Faber's ability to pay full restitution, the fine will be reduced in an effort to provide greater assurance that the customers will recover their losses. Accordingly, the Hearing Panel will order that Faber pay a fine of $20,000, be suspended in all capacities for one year, and make restitution to customers R.K. and D.M. for the amount of their losses, plus interest.

II. UNSUITABLE RECOMMENDATIONS

For unsuitable recommendations, the NASD Sanction Guidelines recommend a fine of $2,500 to $75,000, and a suspension in any or all capacities for a period of 10 business days to

one year. NASD SANCTION GUIDELINES, at 99. Enforcement argues that because Faber was responsible for investing D.M.'s entire portfolio in one risky stock, denied that he recommended the stock to her, and was not forthcoming about his prior disciplinary history, he should be suspended for six months, fined $25,000, and ordered to pay restitution.

The Hearing Panel agrees that Faber should be ordered to pay restitution to customer D.M. However, because of his complete lack of understanding of his suitability obligation, his conduct warrants an increase in the suspension from six months to one year. For the same reasons that fine for misrepresentations and omissions was reduced, the Hearing Panel will fine Faber $15,000, instead of the requested $25,000, and order that the suspension be served concurrently with the suspension for misrepresentations and omissions.

Conclusion

For violation of Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and NASD Conduct Rules 2110 and 2120, Dane Stephen Faber is fined $20,000, suspended in all capacities for one year, and ordered to pay restitution (1) to customer R.K. in the amount of $30,005, plus interest calculated pursuant to 26 U.S.C. § 6621(a)(2),[31] from July 8, 1997 (the date of sale) to the date of payment, and (2) to customer D.M. in the amount of $52,215, plus interest calculated pursuant to 26 U.S.C. § 6621(a)(2) on $31,210 from July 8, 1997, and on $21,005 from July 17, 1997 (all dates of sale) to the date of payment.

For violation of NASD Conduct Rules 2110 and 2310(a), Dane Stephen Faber is fined $15,000, suspended in all capacities for one year, and ordered to pay restitution to customer D.M. in the amount of $52,215, plus interest calculated pursuant to 26 U.S.C. § 6621(a)(2) on

[31] The interest rate used by the Internal Revenue Service to determine interest due on underpaid taxes. This rate, which is adjusted each quarter, reflects market conditions, and thus approximates the time value of money for each quarter in which customers lost the use of their funds.

$31,210 from July 8, 1997, and on $21,005 from July 17, 1997 (all dates of sale) to the date of payment.

In addition, Dane Stephen Faber shall be assessed costs in the amount of $3,500.76, consisting of a $750 administrative fee and a $2,750.76 transcript fee.

These sanctions shall become effective on a date determined by the Association, but not sooner than 30 days from the date this Decision becomes the final disciplinary action of the Association; except that, if this Decision becomes the final disciplinary action of the Association, restitution to customer D.M. shall not exceed $52,215, plus interest, and the suspensions shall run concurrently and commence at the opening of business of Monday, July 1, 2002, and end at the close of business on July 1, 2003.

_____

Alan W. Heifetz
Hearing Officer
For the Hearing Panel

Copies to:
Via First Class Mail & Facsimile
Patrick Baldwin, Esq.
Christine McNamara, Esq.

Via First Class & Electronic Mail
Rodney W. Turner, Esq.
Brian L. Rubin, Esq.
Rory C. Flynn, Esq.

Via First Class Mail & Overnight Courier
Dane S. Faber