

**NASD REGULATION, INC.
OFFICE OF HEARING OFFICERS**

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

MICHAEL HENRY CHRIST
(CRD No. 1664410),
Lynbrook, NY,

Respondent.

Disciplinary Proceeding
No. C10000029

Hearing Officer—Andrew H. Perkins

**HEARING PANEL DECISION AGAINST
MICHAEL HENRY CHRIST**

July 23, 2001

The Department of Enforcement filed a Complaint alleging fourteen causes of action against Global Equities Group, Inc. and several of its officers and registered representatives, including Michael Henry Christ, the firm's President and Director of Compliance. Respondent Christ was charged in one cause of the Complaint with supervisory violations, including failing to implement, maintain and enforce an effective supervisory system at the firm, in violation of NASD Conduct Rules 2110 and 3010.

The Respondent answered and waived a hearing. Based upon the Department's written submission, the Hearing Panel found that the Respondent violated NASD Conduct Rules 2110 and 3010. The Hearing Panel ordered that Respondent Christ be barred from association with any NASD member firm in any capacity.

Appearances

Jay M. Lippman, Assistant Chief Counsel, New York, New York, and Rory C. Flynn, Chief Litigation Counsel, Washington, DC, for the Department of Enforcement.

Michael Henry Christ appeared *pro se*.

DECISION

I. Introduction

The Department of Enforcement (the “Department”) filed the Complaint in this proceeding on February 17, 2000, alleging fourteen causes of action against Michael Henry Christ (“Christ” or the “Respondent”), Global Equities Group, Inc. (“Global” or the “Firm”), Aleksandr Shvarts, Damiano S. Coraci, Eric Kuvykin and Thomas M. McDermott.¹

In summary, the first three Causes of the Complaint allege that Global, Shvarts, Coraci, and Kuvykin violated Sections 10(b) and 15(c) of the Securities Exchange Act of 1934 (“Exchange Act”), SEC Rules 10b-5 and 15c1-2, and NASD Conduct Rules 2110 and 2120 by using various manipulative, deceptive, or fraudulent devices in connection with the initial public offering of CluckCorp International, Inc. (“CluckCorp IPO”) in 1996. The Fourth Cause alleges that Global, Shvarts, Coraci and Kuvykin violated Section 10(b) of the Exchange Act, SEC Rule 10b-6, and NASD Conduct Rules 2110 and 2120 by illegally bidding for, purchasing, or inducing others to purchase CluckCorp securities in the secondary market while still engaged in a distribution of CluckCorp securities. The Fifth, Sixth, Seventh, and Eighth Causes allege that Global, Shvarts and Coraci violated NASD Conduct Rule 2110 by violating the NASD’s Free-Riding and Withholding Interpretation. The Ninth Cause alleges that Global, Coraci and Kuvykin violated NASD Membership and Registration Rules 1031 and 1021 and NASD Conduct Rule 2110 by permitting unregistered persons to engage in activities that

¹ Respondents Shvarts, Coraci, and McDermott submitted Offers of Settlement, which the National Adjudicatory Council accepted. Respondents Global and Kuvykin defaulted by failing to answer the Complaint, and a Default Decision was issued against them dated May 16, 2001. Accordingly, this Hearing Panel Decision applies only to Respondent Christ.

required registration and by permitting Kuvykin to act in a principal capacity even though he was not registered as such with the National Association of Securities Dealers, Inc. (“NASD”). The Tenth Cause alleges that Global, Christ, and McDermott violated NASD Conduct Rules 3010 and 2110 by failing to implement, maintain, and enforce an effective supervisory system reasonably designed to achieve compliance with the federal securities laws and the NASD’s Rules and by failing to establish, maintain, and enforce written procedures pertaining to the Firm’s underwriting and retail brokerage activities, including procedures covering the qualification and registration of associated persons. The remaining Causes of the Complaint allege that various of the Respondents failed to respond truthfully at their on-the-record interviews or falsified account records at the Firm.

II. Procedural History

On February 16, 2000, the Department served Christ with a copy of the Complaint and Notice of Complaint. On March 31, 2000, Christ filed his Answer to the Complaint, in which he denied the allegations against him and specifically stated that he was an employee of the Firm under the control of its owner, Aleksandr Shvarts. (Ans. at 2.)

During the course of the proceeding and at the Department’s request, the Hearing Officer scheduled a pre-hearing conference for November 7, 2000. The purpose of the pre-hearing conference was to determine if Christ intended to appear at the hearing scheduled to commence on December 11, 2000. At the conference, Christ stated that he would not appear at the hearing, and, upon further questioning by the Hearing Officer, he waived his right to a hearing. Accordingly, because the remaining Respondents had either settled or defaulted, the Hearing Officer concluded that a hearing in this proceeding was unnecessary. The Hearing

Officer therefore ordered that the hearing schedule be vacated and that the case against Christ be decided on the written record, as defined in NASD Code of Procedure Rule 9267. The Hearing Officer also set deadlines for the Parties to file written submissions in support of or in opposition to the charges in the Complaint against Christ.

On February 9, 2001, the Department filed a motion for entry of an Hearing Panel Decision imposing sanctions against Christ. The motion is supported by the Declaration of Jay M. Lippman (“Decl.”), a Memorandum on Liability and Sanctions, and 105 exhibits (CX-1 through CX-105). Christ did not file an opposition to the Department’s motion.

For the reasons discussed below, the Department’s motion for entry of a Decision against Christ is granted.

III. Findings of Fact

A. Background

1. The Respondent’s Background in the Securities Industry

According to the NASD’s Central Registration Depository (“CRD”), Christ first registered as a General Securities Representative with the NASD on May 27, 1992, through member firm Berkeley Securities Corporation.² On February 25, 1993, while he was employed by member firm S.D. Cohn & Co., Inc., Christ registered as a General Securities Principal.³ From November 29, 1994, until December 29, 1997, Christ was associated with Global where he was registered in a number of capacities, including registration as a General Securities Representative, a General Securities Principal, and a Financial and Operations Principal.⁴ During

² CX-1, at 5.

³ Id. at 9.

the period relevant to the allegations in the Complaint, Christ was Global's President⁵ and Director of Compliance. (CX-102, at 7484.) Christ also is listed as a control person⁶ on the Firm's Uniform Application for Broker-Dealer Registration (Form BD).⁷

Christ is no longer registered with the NASD or employed in the securities industry. Indeed, Christ has been barred twice before by NASD Regulation, Inc. ("NASD Regulation") from associating with any member firm in any capacity. In November 1998, he was barred after he failed to answer a Complaint charging that he failed to appear at two on-the-record interviews that NASD Regulation staff had scheduled pursuant to NASD Procedural Rule 8210 in connection with the investigation that led to the institution of this proceeding.⁸ Then, in December 2000, he was barred after he failed to answer a second Complaint charging him with failure to appear at two on-the-record interviews that NASD Regulation staff had scheduled pursuant to NASD Procedural Rule 8210 after Christ filed his Answer in this proceeding.⁹

⁴ Id. at 6.

⁵ CX-3, at 156-70.

⁶ "Control" is defined on the Form BD as follows:

The power, directly or indirectly, to direct the management or policies of a company, whether through ownership of securities, by contract, or otherwise. Any *person* that (i) is a director, general partner or officer exercising executive responsibility (or having similar status or functions); (ii) directly or indirectly has the right to vote 25% or more of a class of a voting security or has the power to sell or direct the sale of 25% or more of a class of voting securities; or (iii) in the case of a partnership, has the right to receive upon dissolution, or has contributed, 25% or more of the capital, is presumed to control that company. (Form BD at ¶ 4(1).)

⁷ Id.

⁸ Decl. ¶¶ 16, 17; Department of Enforcement v. Christ, No. C10980047 (OHO Nov. 23, 1998).

⁹ Decl. ¶¶ 18-22; Department of Enforcement v. Christ, No. C10000132 (OHO Dec. 6, 2000).

Christ's CRD record indicates that his last registration with the NASD terminated on September 11, 1998.¹⁰

2. Origin of the Proceeding

The filing of the Complaint in this proceeding arose from an investigation of Global's underwriting and aftermarket activities in connection with the CluckCorp IPO, for which Global served as the managing underwriter. The investigation was conducted by the staff of NASD Regulation's District 10 Office from 1996 through 1999.¹¹ NASD Regulation commenced the investigation as a routine audit of Global's activities in 1995 and 1996.¹² Ultimately, however, the staff focused on Global's apparent violation of the NASD's Free-Riding and Withholding Rules, as set forth under IM-2110-1. In reviewing its allocation of CluckCorp securities offered in the CluckCorp IPO, NASD Regulation staff found that the Firm had assigned a relatively substantial portion of its overall allocation to a number of accounts that were prohibited from receiving securities in an initial public offering that is deemed a "hot issue" under Free-Riding and Withholding Rules.¹³ Later, the staff expanded the examination to address whether Global and its associated persons had complied with certain antifraud provisions of the federal securities laws and the NASD's Conduct Rules in connection with its underwriting activities in the CluckCorp IPO.¹⁴

¹⁰ CX-1, at 8.

¹¹ CX-25 through CX-30.

¹² Decl. ¶ 10.

¹³ Id., at ¶ 11.

¹⁴ Id., at ¶ 12.

As a result of the broadening of the examination, the Staff also scrutinized: (i) whether Global complied with the NASD's Conduct Rules that mandate the registration of associated persons performing the functions of registered representatives and principals; and (ii) whether Global was properly supervised.¹⁵

During the investigation, NASD Regulation staff conducted 26 on-the-record interviews of individuals formerly associated with Global. Each interview focused on Global's activities in connection with the CluckCorp IPO and the immediate aftermarket trading in CluckCorp securities.¹⁶ The Department submitted the transcripts of 18 of these interviews with the instant motion.¹⁷

3. Global Equities Group, Inc.

Global first became a member of the NASD in 1994 under the name of Star Financial Network, Inc. ("Star").¹⁸ In or around mid-1994, Star filed a Broker-Dealer Withdrawal Form.¹⁹ At that juncture, Shvarts purchased Star and changed its name to Global.²⁰ During its operation, Global engaged in a general securities business, which included retail sales, investment banking, and market making activities.²¹ At all times relevant to the Complaint, Global was a member of the NASD.²²

¹⁵ Id. at ¶ 13.

¹⁶ Id. at ¶¶ 14, 15.

¹⁷ CX-34 through CX-51.

¹⁸ CX-2, at 145.

¹⁹ Decl. ¶ 25.

²⁰ CX-45, at 4192-4195.

²¹ CX-2, at 150.

²² CX-2, at 145.

Shvarts, Kuvykin, Coraci, and Christ comprised Global's senior management team. Shvarts, Global's owner, ran Global on a day-to-day basis and managed some client accounts.²³ Kuvykin and Coraci reported to Shvarts and managed the Firm's sales force.²⁴

4. Christ's Responsibilities at Global

Christ served as the Firm's President, FINOP and Chief Executive Officer ("CEO") from the commencement of his employment at Global until the firm ceased operations in December 1997.²⁵ According to Global's Written Supervisory Procedures, Christ also served as Global's compliance officer.²⁶ More specifically, Christ was responsible for the following:

- i) the overall supervision of the Firm, including immediate supervision of two brokers, Coraci and McDermott, and the firm's back office;²⁷
- ii) enforcing, distributing, and revising Global's written supervisory procedures;²⁸
- iii) conducting training sessions on compliance;²⁹
- iv) handling Global's financial operations, including notifying the brokers of commissions earned in connection with aftermarket trading in CluckCorp;³⁰
- v) preparing Global's FOCUS reports and net capital computations;³¹

²³ CX-3; CX-47, at 5102-04, 5108-5112; CX-46, at 4858-61; CX-38, at 1862, 1866.

²⁴ CX-46, at 4858-61; CX-38, at 1862-63, 1872-73, 1895-96; CX-44, at 3973; CX-47, at 5113-14.

²⁵ CX-1, at 6; CX-3; CX-45, at 4225.

²⁶ CX-102, at 7484; CX-103, at 7676.

²⁷ CX-103, at 7661-63; CX-92, at 7287-89; CX-37, at 1527-28, 1535; CX-40, at 2636, 2646-47, 2621, 2632; CX-41, at 2909; CX-51, at 5636-37; CX-47, at 5096-97.

²⁸ CX-40, at 2641; CX-37, at 1562-63.

²⁹ CX-51, at 5682-83, 5691-92; CX-37, at 1564-65, 1533-34; CX-46, at 4906-07.

³⁰ CX-45, at 4226-27; CX-37, at 1559-60, 1611; CX-40, at 2674, 2803; CX-51, at 5703.

³¹ CX-102, at 7484.

- vi) hiring and firing brokers and staff;³²
- vii) handling registration issues for new brokers;³³
- viii) attending and conducting all sales meetings, including those that pertained to the solicitation of interest in the CluckCorp IPO;³⁴
- ix) monitoring brokers' telephone calls;³⁵
- x) reviewing customer complaints;³⁶
- xi) handling allegations of unauthorized trading;³⁷
- xii) reviewing new account forms and order tickets;³⁸
- xiii) monitoring brokers' production levels;³⁹
- xiv) retaining and working with Global's law firm in connection with the CluckCorp IPO;⁴⁰
- xv) executing the CluckCorp underwriting agreement on behalf of Global;⁴¹
- xvi) approving the settlement of indications of interest from other broker-dealers in connection with the CluckCorp IPO;⁴²

³² CX-45, at 4231; CX-37, at 1523, 1574-75, 1580-85; CX-40, at 2667.

³³ CX-92, at 7287; CX-37, at 1737-38; CX-51, at 5625-26; CX-46, at 5023.

³⁴ CX-91, at 7279; CX-37, at 1613-20, 1675-76.

³⁵ CX-92, at 7288; CX-37, at 1587-88, 1704-05.

³⁶ CX-40, at 2655; CX-51, at 5652; CX-46, at 4883, 4887-88; CX-37, at 1572.

³⁷ CX-37, at 1546-47, 1559-60; CX-51, at 5683; CX-46, at 4883.

³⁸ CX-37, at 1541-42, 1592-94; CX-44, at 3984-85, 4049; CX-50, at 5575-76; CX-51, at 5652-53; CX-46, at 4876-78; CX-47, at 5116.

³⁹ CX-37, at 1559-60; CX-51, at 5699-70; CX-46, at 4931-32.

⁴⁰ CX-40, at 2717-19.

⁴¹ CX-25.

⁴² CX-40, at 2626-27, 2684.

- xvii) receiving the “all sold” notifications in connection with the CluckCorp IPO;⁴³
- and
- xviii) ensuring that the “all sold” notices pertaining to the CluckCorp IPO were made timely to the SEC and the NASD.⁴⁴

The documentary evidence further shows that Christ authorized its clearing firm to deliver prospectuses for the CluckCorp IPO to prospective purchasers.⁴⁵

5. Global’s Fraudulent Boiler Room Sales Practices and other Securities Violations Surrounding the CluckCorp IPO

Christ’s supervisory violations are premised on the pervasive fraudulent sales practices and other securities violations committed by the remaining Respondents surrounding the CluckCorp IPO.⁴⁶ Overwhelming evidence of those violations is itemized in the Department’s 274-paragraph declaration submitted in support of the motion for entry of a Decision against Christ. For the purposes of this Decision, it is unnecessary to restate the evidence in corresponding detail. The basic facts are quite clear. During the period June through October 1996, Global operated a classic boiler room⁴⁷ fraud. All 30 registered representatives at Global

⁴³ Id. at 2646-47.

⁴⁴ Id. at 2690-91.

⁴⁵ CX-97, at 7318, 7357.

⁴⁶ The securities of CluckCorp were listed on the Nasdaq SmallCap Market. The common stock traded under the symbol ROTI and the warrants traded under the symbol ROTIW. The effective date for the CluckCorp IPO was July 9, 1996, but secondary market trading did not begin until 3:22 p.m. on the following day. (CX-66.)

⁴⁷ A “boiler room” is defined as a “place where high-pressure salespeople use banks of telephones to call lists of potential investors (known in the trade as sucker lists) in order to peddle speculative, even fraudulent, securities. They are called boiler rooms because of the high-pressure selling.” Barron’s Dictionary of Finance and Investment Terms 54 (4th ed. 1995). See also, Hanly v. SEC, 415 F.2d 589, 597 n.14 (2nd Cir. 1969) (a boiler room selling is characterized by salesmen soliciting new customers who are given favorable earnings projections, predictions of price rises and other optimistic prospects without a factual basis, leaving the prospect with a deliberately created expectation of gain without risk).

solicited customers to purchase CluckCorp securities by telling them “more or less whatever [they] wanted” provided it was not “too outrageous.”⁴⁸ To sell out the CluckCorp IPO, they intentionally misrepresented material facts regarding CluckCorp and the known investment risks associated with purchasing securities in the CluckCorp IPO. At the direction of Shvarts, Coraci and Kuvykin, Global’s sales force, which included unregistered persons, also made baseless and fraudulent price predictions⁴⁹ to induce customers to purchase CluckCorp securities, which created an unreasonable expectation of gain without risk.

CluckCorp was incorporated in Texas in 1993 under the name of “Cluckers Tex-Mex Venture, Inc.” and changed its name to CluckCorp International, Inc. in April 1995. (CX-28, at 0674.) Prior to November 1994, the company “was an area developer for Cluckers Wood Roasted Chicken, Inc. (“CWRC”), the developer and franchisor of the ‘Cluckers’ restaurant concept.” (Id.) In November 1994, Kenny Rogers Roasters, Inc. acquired a controlling interest in CWRC. CluckCorp then exchanged its rights under the area development agreement for certain franchising materials, systems and signage along with the exclusive right to use the Cluckers name, trademark and service mark solely in Texas. (Id.)

According to the final prospectus, CluckCorp “intend[ed] to own, operate and franchise quick service restaurants” that featured wood-roasted rotisserie chicken, oak roasted turkey, roast ham, meat loaf, and other fresh homestyle foods under the name of ‘Harvest Rotisserie.’ (CX-28, at 674) CluckCorp had operated only the single Cluckers restaurant in

⁴⁸ CX-44, at 3978-83.

⁴⁹ See, e.g., In re Crow, Brouman & Chatkin, Inc., 42 S.E.C. 938 (1966) (“we have repeatedly held that predictions of specific and substantial increases in the price of a speculative security are inherently fraudulent”).

Texas, which it used as both a training facility and a public restaurant. That restaurant had operated at a loss since it had opened in January 1994. (Id. at 677.) In fact, CluckCorp itself had operated at a net loss since it commenced operations in June 1993. (Id.) As of December 31, 1995, CluckCorp had a deficit: (i) in working capital of \$876,097; and (ii) in shareholder equity of \$365,817. (Id.) A report prepared by CluckCorp's independent accountants, dated March 15, 1996, indicated that these deficits, among other factors, "raise[d] substantial doubt about [CluckCorp's] ability to continue as a going concern." (Id. at 710.) Additionally, in 1995 and 1996, CluckCorp faced substantial market competition from several established and well known national chains, including Boston Chicken (a/k/a Boston Market) and Kenny Rogers Roasters, which offered the same products as CluckCorp. (Id. at 695).

News reports at the time of the IPO presented a dire picture of CluckCorp's prospects. First, in January 1996, the San Antonio Business Journal, Inc. reported that in November 1995, CluckCorp had filed an amended offering plan with the SEC in which the firm reported increasing net operating losses and shareholders' deficits. (CX-32, at 745-46.) The article reported that some analysts questioned whether the CluckCorp IPO would be successful in light of its increasing losses. In April 1996, the San Antonio Business Journal, Inc. further reported that "CluckCorp has not been flying high financially as of late." (CX-32, at 748.) In its amended filings with the SEC the company reported increasing operating losses and shareholder deficits and that it had already altered its expansion plans. (Id.) In 1995, CluckCorp disclosed that it planned to open seven or eight new restaurants in San Antonio and Houston, and up to 30 restaurants in the San Francisco Bay area. (Id.) However, by April 1996, those plans were no longer mentioned in its filings with the SEC. Instead, CluckCorp announced that it had

executed an area development agreement with an affiliate to develop up to 10 restaurants in Singapore and that it had entered into an agreement with an outside party that could lead to the establishment of 50 restaurants in Baltimore. (Id.) Significantly, however, the news report stated that at least one quoted analyst doubted the likelihood of the development plans materializing, stating that the company needed “to build some (restaurants) in this country first and earn some money before they think about going international.” (Id.)

The sales force enthusiastically recommended the purchase of CluckCorp securities to numerous customers. They made unfounded claims about the merits of the investment and predicted rising stock prices without disclosing CluckCorp’s financial situation. Shvarts told Global’s sales force that CluckCorp stock was going to trade at a two-and-a-half point premium. (CX-38, at 2058.) At Firm meetings, Global’s managers stated that CluckCorp would go up five points within the first day or so or in aftermarket trading. (CX-44, at 3981-83.) Global’s managers also prepared and distributed sales scripts to be used by the sales force, which favorably compared CluckCorp to Boston Chicken. (CX-38, at 2002-04; CX-46, at 4914-15.) The registered representatives further told purchasers that there was “tremendous franchise store growth from area developers with initial plans tied to Agreement and Letters of Intent for 130 franchise stores.” (CX-46, at 5054.) Many customers filed sworn declarations stating that their registered representative told them that CluckCorp was a sure investment. For example, customer LF stated that he was told that CluckCorp was a “guaranteed winner” and a “home run” and that its price would rise to anywhere between \$9 and \$11 per share. (CX-52.) Other customers were told that the CluckCorp IPO would be a “hot issue.” (CX-56.) These representations about CluckCorp were knowingly false, and, in

making them, the sales force violated Section 10(b) of the Exchange Act, SEC Rule 10b-5, and NASD Conduct Rules 2110 and 2120.

The evidence also establishes a number of other violations regarding the manner in which Global handled the CluckCorp IPO, which was a hot issue. (CX-33.) For example, Global impermissibly allocated CluckCorp securities to persons restricted from purchasing hot issues, in violation of the NASD's Free-Riding and Withholding Interpretation,⁵⁰ and Global made a market in CluckCorp securities before the distribution ended, in violation of SEC Rule 10b-6. (CX-81; 82 [Market Maker Price Movement Reports]).

Finally, the evidence shows that Global, through Christ, adopted an undisclosed allocation policy for the CluckCorp IPO (the "3:1 Policy"). Under this policy, purchasers were advised that for each warrant they purchased in the CluckCorp IPO they had to purchase approximately three and one-half shares of CluckCorp common stock. (CX-38, at 2032-34, 2056-58; CX- 37, at 1697-98; CX-47, at 5157-58, 5179-80; CX-46, at 4867-69, 4957; 4983-85; CX-51, at 5732-38, 5741-42.) The policy, however, was in contravention of the terms of the offering as it was described in the offering documents. In effect, Global offered CluckCorp IPO securities as a unit, which was not disclosed in the final prospectus. Consequently, the prospectus Christ authorized to be delivered to prospective purchasers was materially false.

The evidence of these various violations includes investigative testimony given by numerous former Global brokers (CX-34 through CX-51); numerous customer declarations

⁵⁰ Shvarts, Kuvykin and Coraci offered CluckCorp IPO warrants to prospective employees as an inducement for them to join the Firm. (CX-38, at 1864-65; CX-47, at 5153-59.)

(CX-52 through CX-63); the underwriting agreement, prospectus and related registration documents for the CluckCorp IPO (CX-25 through CX-29; CX-31); internal sales records for Global's brokers (CX-66 and CX-67); numerous customer account documents (CX-68 through CX-76); documents pertaining to restricted accounts (CX-85 through CX-87; CX-90); and other materials. These documents establish in convincing detail that Global operated as a boiler room in the sale of CluckCorp securities, which fraudulent activity is clearly and convincingly summarized in the Department's declaration.⁵¹

IV. Discussion

A. Jurisdiction

The NASD has jurisdiction over this proceeding under Article IV, Section 4 of the NASD's By-Laws. Christ was last registered with NASD member firm Morgan Grant Capital Corp. as a General Securities Principal, General Securities Representative, Financial and Operations Principal, and other in capacities until September 11, 1998. (CX-1, at 8.) The Complaint alleges misconduct while Christ was registered with Global, and it was filed within two years after the effective date of termination of his registration with Morgan Grant.

B. Inadequate Supervisory System and Procedures

NASD Conduct Rule 3010 requires NASD members to "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 the Rules of [the NASD]."⁵² The Rule specifically requires, among other things, that a

⁵¹ Operation of a boiler room in and of itself constitutes a violation of the antifraud provisions of the Exchange Act. See SEC v. Charles A. Morris, 386 F. Supp. 1327, 1336 (W.D. Tenn. 1973).

⁵² Rule 3010(a).

member “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 that are reasonably designed to achieve compliance with applicable securities laws and regulations, and with the applicable Rules of [the] Association.”⁵³ Whether a particular supervisory system or set of written procedures is in fact “reasonably designed to achieve compliance” depends on the facts and circumstances of each case.⁵⁴

1. Global’s Written Procedures

NASD Rule 3010 requires NASD members to establish and maintain written procedures “reasonably designed to achieve compliance” with applicable laws and rules. Global’s compliance manual, which set forth the Firm’s written procedures, fell far short of this standard. For example, the manual lists prohibited activities, such as Unregistered Activity and Free-Riding and Withholding involving “Hot Issues” sold to restricted accounts, but fails to spell out the specific steps to be taken by unnamed supervisors to adequately monitor, detect, and prevent the substantive violations. (CX-102; CX-103.) The manual also does not delineate specific procedures for preventing unregistered persons from engaging in activities for which registration is required.⁵⁵ Moreover, the manual does not even mention: (i) Misrepresentations in the offer and sale of securities; (ii) Manipulation; (iii) Prohibited trading by participants interested

⁵³ Rule 3010(b)(1).

⁵⁴ Christopher J. Benz, 52 S.E.C. 1280, 1284 & n.19 (1997), aff’d, 168 F.3d 478 (3d Cir. 1998) (Table).

⁵⁵ Gary E. Bryant, 51 S.E.C. 463 (1993) (finding a violation where firm’s written procedures provided a list of things not to do, but did not establish a mechanism for ensuring compliance).

in a distribution; and (iv) Canceled trades review.⁵⁶ (Id.; Decl. ¶ 268.) Thus, for example, the manual fails to address such practices as overly-optimistic forecasts and recommending purchases or sales without a reasonable basis for such recommendations. Accordingly, there are no specific procedures set forth that managers should use to detect or prevent those practices. This is a serious deficiency that so severely undercuts the value of the written procedures as to render them nothing more than window dressing. In short, the Firm's written procedures are woefully inadequate; they fail to meet the Rule 3010(b) standard.

The Hearing Panel finds that Christ is responsible for Global's inadequate written procedures. The Firm's compliance manual itself lists Christ as responsible for ensuring Global's compliance with the federal securities laws and the NASD's conduct rules. Moreover, Christ was a principal and the Firm's President. In addition, Christ acknowledged his responsibility for all areas of compliance at Global, and there is no evidence that Christ delegated any of his responsibilities.⁵⁷ The Hearing Panel thus finds it appropriate to hold Christ responsible for Global's inadequate written procedures. Accordingly, the Hearing Panel finds that Christ violated NASD Conduct Rules 2110 and 3010, as alleged in the Complaint.

2. Global's Supervisory System

NASD Conduct Rule 3010(a) requires NASD members to "establish and maintain a system to supervise the activities of each registered representative and associated person that is

⁵⁶ See Castle Securities Corporation, Exchange Act Rel. No. 39,523 (Jan. 7, 1998) (finding a supervisory violation where procedures manual failed to address the determination of fair prices in a dominated and controlled market and did not provide for prevention and detection of manipulation of the market).

⁵⁷ Cf. Everest Securities, Inc., Exchange Act Release No. 37,600 (Aug. 26, 1996) (president of broker-dealer held liable for supervisory violations in absence of evidence that she reasonably delegated her compliance responsibilities).

reasonably designed to achieve compliance with applicable securities laws and regulations, and the Rules of [the NASD].” Global had no such system. Indeed, the evidence shows clearly that Global operated in a free-for-all atmosphere where senior management encouraged fraudulent sales practices and unregistered persons openly engaged in selling securities. Global was able to operate as a boiler room because it had no supervisory system. Many of the Firm’s registered representative confirmed in their on-the-record interviews that Global was devoid of supervision. Richard Singer, one of the more seasoned registered representatives at Global, testified at his on-the-record interview that “[Global’s management] did not know how to run a broker-dealer.” (CX-47, at 5116-17.) Coraci testified that there was no training whatsoever in the area of compliance.⁵⁸ (CX-37, at 1624-25.) Michael Dunbar similarly testified that Christ stayed in the background until something “hit the fan,” at which point he would make an appearance and talk about the problem, but “that would be about it.” (CX-38, at 1945-50, 2104-05.) Donald St. Jean testified that he could not recall any discussions at the Firm regarding how to make an accurate and factual sales presentation, or, for that matter, any instructions not to make misrepresentations to customers. (CX-46, at 4882.) St. Jean also could not recall Christ ever taking action against a registered representative accused of wrongdoing. (*Id.* at 4883-84.) With respect to the CluckCorp IPO, there is substantial evidence that Christ and the remainder of Global’s senior management team knew that the sales force was making misrepresentations, but they did nothing to stop them. (*See, e.g.*, CX-38, at 1953-56.)

⁵⁸ *See, Market Reg. Comm. v. La Jolla Capital Corp.*, No. CMS950110, 1998 NASD Discip. LEXIS 26, *16-17 (NAC Feb. 27, 1998), *aff’d* Exchange Act Release No. 41,755, 1999 SEC LEXIS 1642 (Aug. 18, 1999) (The reasonableness of a supervisory system . . . depends [in part] on how well it accounts for the past and future training of the personnel being supervised.”).

The record is replete with examples of Christ's inadequate supervision. For example, he attended sales meetings but failed to take any action to reverse the instructions from senior management that the sales force could say almost anything they wanted to get the CluckCorp IPO sold. Christ also failed to detect and deter the use of fraudulent sales scripts that were discussed at the sales meetings he attended. And he failed to implement any procedures to assure compliance with SEC Rule 10b-6 and the NASD's Free-Riding and Withholding Interpretation.⁵⁹ Christ also ignored numerous red flags of improper conduct. A clear example of this involves his treatment of Chris Margaritis, whom the NASD has barred in an unrelated action. Christ heard Margaritis committing a fraud by making material misrepresentations of fact to a customer when attempting to solicit indications of interest in the CluckCorp IPO. The misrepresentations were based on a false claim that CluckCorp had multiple operational stores. The only sanction Respondent Christ imposed was to warn Margaritis; he neither terminated him because of the securities fraud nor reported him to securities regulators. (CX-37, at 1548-49.) Not only should Christ have taken immediate and firm action in response to this misconduct, but Christ should have investigated to determine if this was an isolated event or whether other registered representatives at the Firm were similarly misrepresenting the CluckCorp IPO.

Based upon the foregoing, the Hearing Panel finds that Christ is responsible for Global's lack of a supervisory system that complied with Rule 3010. He was the head of compliance and the President of the Firm. As such, he had the ultimate responsibility to ensure that Global had a

⁵⁹ See District Bus. Conduct Comm. v. Equity Securities Trading Co., No. C04940053, 1996 NASD Discip. LEXIS 42, *13 (Oct. 23, 1996) (firm found to have violated supervisory system requirement because the

proper system in effect and to implement procedures that would ensure the Firm's compliance with applicable securities laws, regulations and rules. Accordingly, the Hearing Panel finds that Christ violated NASD Conduct Rules 2110 and 3010, as alleged in the Complaint.

V. Sanctions

The Department requests that Christ be barred and fined a total of \$75,000, the maximum sanctions recommended under the NASD Sanction Guidelines for Failure to Supervise and for Deficient Written Supervisory Procedures.⁶⁰

The Hearing Panel concludes that it is appropriate to impose a single sanction for the violations in this case, rather than separate sanctions for the failure to establish and maintain a supervisory system and the failure to establish, maintain, and enforce written procedures to supervise the types of business in which Global engaged. The Department's submission establishes that the violations in this case were part of an overall abdication by Christ of all of his supervisory responsibilities, which in turn led to the boiler room atmosphere at the Firm. Under such circumstances, it is appropriate to consider the totality of Christ's misconduct rather than view each element in isolation.

When viewed as a whole, there is no question that Christ's misconduct was egregious and that it contributed directly to the fraudulent sales practices and other misconduct at Global. Indeed, Christ's failure to implement and enforce a proper supervisory system created the "free-for-all" atmosphere that was the hallmark of Global's efforts to sell out the CluckCorp IPO. Under these circumstances, and taking into consideration his disciplinary history of refusing

supervisory system permitted the sale of "hot issues" to CBOE market makers).

⁶⁰ NASD Sanction Guidelines 108-09 (2001 ed.) < http://www.nasdr.com/pdf-text/sanction_guide-lines.pdf>.

to appear and testify when requested to do so by NASD Regulation under NASD Procedural Rule 8210, a bar is clearly warranted. Christ would pose a serious threat to the investing public if he were allowed to ever return to the securities industry in any capacity. The Hearing Panel will not, however, impose a fine in light of the fact that he has been barred twice before.⁶¹

VI. Order

Therefore, having considered all of the evidence submitted by The Department, the Hearing Panel orders that Respondent Michael Henry Christ be barred from association with any NASD member firm in any capacity. The bar shall become effective immediately upon this Decision becoming the final disciplinary action of the NASD.

Andrew H. Perkins
Hearing Officer

Copies to:

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⁶¹ NASD Sanction Guidelines at 13.