

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

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DEPARTMENT OF ENFORCEMENT,	:	Disciplinary Proceeding
	:	No. CAF000040
Complainant,	:	
	:	<b>Hearing Panel Decision</b>
v.	:	<b>Granting Complainant's</b>
	:	<b>Motion for Summary</b>
MICHELLE McDONOUGH,	:	<b>Disposition as to</b>
(CRD #501445)	:	<b>Respondent</b>
North Tarrytown, NY	:	<b>Michelle McDonough</b>
	:	
	:	Hearing Officer--SW
Respondent.	:	
_____	:	Date: June 26, 2001

**Former registered representative barred for violating Rules 8210 and 2110 by failing to appear for an on-the-record interview scheduled pursuant to Rule 8210.**

On September 21, 2001, the NASD Regulation, Inc. Department of Enforcement (“Enforcement”) filed a Complaint alleging that Respondent Michelle McDonough (“Respondent”) violated NASD Conduct Rule 2110 and NASD Procedural Rule 8210 by failing to appear for an on-the-record interview scheduled pursuant to Rule 8210.<sup>1</sup> Respondent filed an Answer on October 19, 2001, denying that she had intentionally or willfully failed to appear, and claiming that she was invoking her right against self-incrimination under the Fifth Amendment to the United States Constitution.

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<sup>1</sup> The Complaint contained nine counts, only one of which, count nine, contained allegations against Respondent. Charges in counts one through eight, which related to other respondents, have (i) settled, (ii) been stayed pending approval of settlement offers, or (iii) been admitted and default decisions will be issued because the respondents failed to answer the Complaint.

Enforcement filed a Motion for Summary Disposition on April 9, 2001 and supplemented it on June 12, 2001.<sup>2</sup> Respondent filed an opposition to Enforcement's Motion for Summary Disposition on April 26, 2001 ("Opposition"). However, the Opposition did not dispute that (i) the NASDR scheduled an on-the record interview on January 20, 2000 pursuant to Rule 8210, (ii) Respondent had notice of the scheduled interview, and (iii) Respondent failed to appear for the interview. The Opposition simply reiterated that Respondent, despite being aware that the NASDR staff refused to further postpone the interview, failed to appear for the scheduled interview in reliance on her Fifth Amendment right.

For the reasons set forth below, the Hearing Panel grants Enforcement's Motion for Summary Disposition.

## **FINDINGS OF FACT AND CONCLUSIONS OF LAW**

### **I. Background**

In 1998, the NASDR staff began an investigation of the April 17, 1997 initial public offering of D.G. Jewellery & Co., Inc. ("D.G.") by Joseph Dillon & Co., Inc. ("Dillon"). (CX-2 at ¶2). The D.G. initial public offering registration statement included 250,000 shares that were held by two selling shareholders, JB and BH, and were subject to a two-year lock up agreement with Dillon. (CX-2 at ¶3). During the investigation, the staff learned that BH had opened an account at Fahnestock & Co. ("Fahnestock") where Respondent was BH's

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<sup>2</sup> Enforcement's Motion for Summary Disposition was accompanied by seven exhibits, including the declaration of an NASD staff member. At the request of the Hearing Panel, Enforcement supplemented its Motion for Summary Disposition with Respondent's Form U-4 as an additional exhibit. Hereinafter Enforcement's exhibits will be designated as "CX-" with the appropriate page or paragraph numbers.

broker.<sup>3</sup> (CX-2 at ¶4). On April 18, 1997, Dillon released the lock-up agreements, and Respondent executed the sale of all of BH's 180,000 shares of D.G. to Dillon's inventory. (Id.). In connection with the investigation of the trading activity in D.G. stock, the NASDR staff decided to interview Respondent concerning her sale of BH's D.G. stock. (CX-2 at ¶5).

On November 19, 1999, NASDR sent a letter, scheduling an on-the-record interview, to Respondent's address of record as reflected in the Central Registration Depository ("CRD") and to an alternate address.<sup>4</sup> (CX-4). The November 19 letter specifically requested that Respondent appear on December 3, 1999 for an on-the-record interview.

On December 2, 1999, an attorney representing Respondent left a voice mail message for the staff indicating that he was representing Respondent. (CX-3; Opposition, p. 3). On December 15, 1999, counsel for Respondent telephoned the NASDR staff and advised them that because Respondent was under indictment in the Eastern District of New York and the criminal charges related to the topic of the NASDR interview, Respondent was invoking her right against self-incrimination under the Fifth Amendment and requesting a postponement of the interview. (CX-2 at ¶7; Opposition, p. 4).

On December 15, 1999, in a letter to Respondent's counsel, the NASDR staff confirmed the conversation with Respondent's counsel and indicated that the interview would be postponed until January 20, 2000. (CX-3; CX-2 at ¶7). The letter also specifically

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<sup>3</sup> Respondent became associated with Fahnstock in December 1992. (CX-1, p. 1).

<sup>4</sup> Respondent's CRD Address is \_\_\_\_\_, N. Tarrytown, NY \_\_\_\_\_. (CX-8). The alternate address is \_\_\_\_\_, Scarsdale, NY \_\_\_\_\_. (CX-4).

indicated that failure to provide testimony could serve as the basis for the initiation of a disciplinary action against Respondent. (CX-3).

Respondent acknowledged that NASDR scheduled the on-the-record interview for January 20, 2000. (Opposition, p. 4). Respondent also acknowledged that there was no further contact between the parties until September 21, 2000 when the Complaint was filed. (Id.). During the eight month period between January and September, Respondent made no effort to reschedule the on-the-record interview. (Id.).

## **II. Legal Discussion**

### **A. Jurisdiction**

On September 21, 2000, when the Complaint was filed, Respondent was registered with the Association, and the NASD thus has jurisdiction.<sup>5</sup>

### **B. Summary Disposition**

Rule 9264(e) of the NASD Code of Procedure permits a Hearing Panel to grant summary disposition when “there is no genuine issue with regard to any material fact and the Party that files the motion is entitled to summary disposition as a matter of law.” In this case there is no issue of material fact. It is not contested that Respondent failed to appear for the on-the-record interview scheduled for January 20, 2000. Respondent does not deny that she had notice of the January 20, 2000 scheduled interview.

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<sup>5</sup> In a New York Stock Exchange (“NYSE”) proceeding, Respondent consented to a censure and bar because of her failure to provide on-the-record testimony concerning her activities at Fahnestock. (Opposition, p. 3, fn. 1). The NYSE bar, effective November 17, 2000, remains in place until Respondent complies with the request for information. (CX-1, p. 7). As a result of the NYSE bar, a statutory disqualification, the NASD barred Respondent on November 17, 2000. (CX-1, p. 1; Article 3, Section 4 of the NASD Bylaws). When Respondent is no longer subject to the NYSE bar, she will no longer be subject to the NASD statutory disqualification.

With no issue of material fact present, the only issue to be determined in this action is whether Respondent raised a defense, as a matter of law, for her failure to appear.

Respondent's sole defense was that she was invoking her Fifth Amendment privilege against self-incrimination.

**C. Fifth Amendment defense not valid**

NASD Procedural Rule 8210(a)(1) authorizes the NASD to require an associated person "to provide information orally, in writing, or electronically . . . with respect to any matter involved in [an] investigation . . . ." The Rule provides a means for the NASD to carry out its regulatory mandate in the absence of subpoena power. As such, the Rule is a "key element in the NASD's effort to police its members."<sup>6</sup> A failure to respond "undermines the NASD's ability . . . to carry out its self-regulatory functions,"<sup>7</sup> and frustrates its ability "to conduct investigations and thereby protect the public interest."<sup>8</sup>

Respondent argues in her Opposition that she did not refuse to appear, but invoked her Fifth Amendment privilege by asking for a limited postponement of her testimony until the conclusion of her criminal case.

Constitutional privileges, including the Fifth Amendment, provide protection against governmental, not private, action. The Supreme Court has repeatedly held that private entities, even those intimately involved in governmental regulatory schemes, are not thereby made

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<sup>6</sup> In re Richard J. Rouse, 51 S.E.C. 581, 1993 SEC LEXIS 1831, at \*7 (1993).

<sup>7</sup> In re John J. Fiero, Exchange Act Release No. 39544, 1998 SEC LEXIS 49, at \*5 (Jan. 13, 1998).

<sup>8</sup> In re Barry C. Wilson, Exchange Act Release No. 37867, 1996 SEC LEXIS 3012, at \*14 (Oct. 25, 1996) (quoting Rouse, 51 S.E.C. at 588, 1993 SEC LEXIS 1831, at \*16).

government actors.<sup>9</sup> The NASDR is a private not-for-profit corporation organized under the laws of Delaware and is a self-regulatory organization registered with the SEC as a national securities association pursuant to the 1938 Maloney Act Amendment to the Securities Exchange Act of 1934, 15 U.S.C. §78o et seq.<sup>10</sup> The courts have specifically held that the NASD, in performing its statutory mandate and central role, is not a government actor.<sup>11</sup>

Recently, in D.L. Cromwell Investments, Inc. v. NASD Regulation, Inc., No. 01 Civ. 0728, 2001 U.S. Dist. LEXIS 1912 (S.D.N.Y. Feb. 26, 2001), the plaintiffs, subjects of a federal grand jury investigation, sought an injunction barring the NASDR staff from compelling them to testify in an investigation and from commencing any proceeding to punish them for asserting their privileges against self-incrimination. The plaintiffs contended that the “Rule 8210 demands [had] been issued by [NASDR] as an agent for the government in order to coerce them into surrendering their privileges against self-incrimination by threatening them with permanent banishment from the securities industry if they declined to testify in the NASD investigation.” (Id. at \*\*12). The court specifically stated “Hence, even if the individual plaintiffs are being compelled to give evidence against themselves by the threat of NASD sanctions, [NASDR’s] actions raise no Fifth Amendment issue . . . .” (Id. at \*\*13).

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<sup>9</sup> See National Collegiate Athletic Ass'n v. Tarkanian, 488 U.S. 179, 193 (1988); San Francisco Arts & Athletics, Inc. v. United States Olympic Comm., 483 U.S. 522, 544 (1987).

<sup>10</sup> Desiderio v. National Association of Securities Dealers, Inc., 191 F.3d 198, 199 U.S. App. LEXIS 23269 (Sept. 22, 1999), cert. denied, 2001 U.S. LEXIS 112 (Jan. 8, 2001).

<sup>11</sup> See Jones v. S.E.C., 115 F.3d 1173, 1182-83 (4th Cir. 1997) (rejecting claim based on the Fifth Amendment's Double Jeopardy Clause because NASD is not a government agency), cert. denied, 118 S. Ct. 1512 (1998); Datek Secs. v. NASD, 875 F. Supp. 230, 234 (S.D.N.Y. 1995) (dismissing Fifth and Fourteenth Amendment claims regarding a disciplinary proceeding because the NASD is not a state actor); First Jersey Secs., Inc. v. Bergen, 605 F.2d 690, 698 & 699 n.5 (3d Cir. 1979), cert. denied, 444 U.S. 1074 (1980) (holding that NASD is not a state actor); Graman v. NASD, No. Civ. A. 97-1556, 1998 WL 294022 (D.D.C. Apr. 27, 1998) (same); United States v. Bloom, 450 F. Supp. 323, 330 (E.D. Pa. 1978) (same).

The SEC has also held that an NASD member may not “second guess” or “impose conditions” on the NASD’s request for information.<sup>12</sup> Consequently, Respondent could not force NASDR’s staff to postpone her interview.

The Hearing Panel concludes, based on controlling precedent, that Respondent failed to raise any legally valid defense for her failure to appear. Failure to provide testimony to the NASD, absent a legally recognizable justification for such a failure, is a violation of Conduct Rule 2110 and Procedural Rule 8210.

### **III. Sanction**

The applicable NASD Sanction Guideline recommends that, where an individual respondent does not respond, a bar should be standard and a fine ranging between \$25,000 and \$50,000 should be imposed.<sup>13</sup> The Guidelines also provide that adjudicators generally should not impose a fine if the individual is barred in a failure to respond case when there is not customer loss.<sup>14</sup> Enforcement requested that Respondent be barred.

Respondent agreed to abide by the NASD’s rules and regulations, including Rule 8210, when she executed the Form U-4 to register with the Association.<sup>15</sup> Considering the importance of Rule 8210 and noting the extensive case law addressing the need to respond to Rule 8210 requests, the Hearing Panel finds no mitigating factors and no reasons to impose a sanction below those recommended by the Guidelines.

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<sup>12</sup> In re Joseph Patrick Hannan, Exchange Act Release No. 40438, 1998 SEC LEXIS 1955, at \*11 (Sept. 14, 1998).

<sup>13</sup> NASD Sanction Guidelines, p. 39 (2001).

<sup>14</sup> Id. at 13.

Accordingly, the Hearing Panel bars Respondent from association with any NASD member in any capacity.

### **CONCLUSION**

The Hearing Panel determines that there are no disputes of material fact in this proceeding, and that Enforcement is entitled to summary disposition as a matter of law. Therefore, the Hearing Panel grants Enforcement's Motion for Summary Disposition, and bars Respondent from associating with any member in any capacity. The bar shall become effective immediately upon this Decision becoming the final disciplinary action of the NASD.<sup>16</sup>

### **SO ORDERED**

Hearing Panel

by: \_\_\_\_\_  
Sharon Witherspoon  
Hearing Officer

Date: Washington, D.C.  
June 26, 2001

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<sup>15</sup> Signing as "Michelle Sarian," Respondent executed the Form U-4 without alteration on December 16, 1992. (CX-8).

<sup>16</sup> The Hearing Panel considered all of the arguments of the Parties. They are rejected or sustained to the extent they are inconsistent or in accord with the views expressed herein.