

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

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DEPARTMENT OF ENFORCEMENT,	:	
	:	
Complainant,	:	Disciplinary Proceeding
	:	No. CMS970026
v.	:	
	:	Hearing Officer - JMF
OLDE DISCOUNT CORPORATION	:	
(BD # 5979)	:	
Detroit, Michigan	:	
	:	August 26, 1998
	:	
and	:	
	:	
TODD THOMAS WODEK	:	
(CRD # 2142092)	:	
Oxford, Michigan,	:	
	:	
	:	
Respondents.	:	

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**DIGEST**

The Department of Enforcement (“Enforcement”) filed a Complaint alleging that Respondent Todd Thomas Wodek (“Wodek”) violated NASD Conduct Rule 2110 by engaging in anti-competitive conduct. The Complaint specifically alleged that Respondent Wodek harassed another market maker by calling that market maker 20 times over a ninety minute period to sell 100 shares of stock in 20 separate transactions in circumstances where the other market maker quoted the stock in increments of 1/32 and whose posted bid was for 1,000 shares. The Complaint also alleged that Respondent Olde Discount Corporation (“Olde”) violated NASD Conduct Rules 2110 and 3010 by failing to establish, maintain and enforce adequate written supervisory procedures to deter and

detect anti-competitive trading practices. Based on the evidence admitted at hearing, the Hearing Panel found that Respondent Wodek's conduct was anti-competitive and violated NASD Conduct Rule 2110, and that Olde's written supervisory procedures were deficient. The Hearing Panel censured both Respondents, and fined Wodek and Olde \$15,000 and \$20,000, respectively. The Hearing Panel also ordered Respondent Wodek to become qualified as a Limited Representative - Equity Trader (Series 55) within sixty (60) days of the effective date of this decision.

#### Appearances

Michael J. King, Esq., Chief Litigation Counsel, Department of Market Regulation, Rockville, Maryland, (Rory C. Flynn, Esq., Washington, DC, Of Counsel), for the Department of Enforcement.

Harry Frischer, Esq. and Wayne M. Aaron, Esq., Solomon, Zauderer, Ellenhorn, Frischer & Sharp, New York, New York, on behalf of Olde Discount Corporation and Todd Thomas Wodek.

### **DECISION**

#### **I. PROCEDURAL BACKGROUND**

##### **A. Complaint**

The Department of Enforcement ("Enforcement" or "Department") filed a two cause Complaint in this proceeding on September 18, 1997. The Complaint alleges that Olde Discount Corporation ("Olde") failed to establish, maintain and enforce adequate written supervisory procedures to ensure compliance with NASD Conduct Rule 2110 to deter and detect anti-competitive behavior by Olde traders in violation of NASD Conduct Rules 2110 and 3010. The Complaint also alleges that Todd Thomas Wodek ("Wodek"),

a trader and registered general securities representative associated with Olde, engaged in anti-competitive activities designed to harass another market maker for its competitive quotations, and to discourage competitive activities in violation of NASD Conduct Rule 2110.

Enforcement specifically charges that on October 7, 1996, Wodek, rather than directing one order of 2,000 shares or two orders of 1,000 shares, called Ross Securities (“ROSS”) 20 times during the period 2:25 to 3:58 p.m. (the “relevant period”), selling ROSS 100 shares of Oak Technology (“OAKT”) in 20 separate transactions. (Complaint at ¶¶ 6-12). During the relevant period, ROSS was bidding OAKT at 9 29/32 with a posted size of 1,000 shares. ROSS was the exclusive high bid for all but four seconds of the relevant period. ROSS executed each 100 share order and never changed the price or size of its bid.

B. Answer

Respondents filed an Answer on September 18, 1997. Respondents’ Answer admitted that the transactions as alleged in the Complaint occurred, but denied that any violations occurred. Respondents specifically noted that Wodek “executed his orders with ROSS in a manner which, based on past experience with ROSS, was the best way

to achieve a transaction at the price ROSS quoted.” (Answer at ¶12).<sup>1</sup> The Answer also denied that Olde’s supervisory procedures were deficient, noting that “Olde at all times established, maintained and enforced adequate written supervisory procedures to ensure compliance with Conduct Rule 2110.” (Answer at ¶14).

C. The Hearing

The Hearing in this proceeding was held in Southfield, Michigan on April 8, 1998, before a Hearing Panel composed of the Hearing Officer, a former member of the District 8 Business Conduct Committee, and a former member of the Market Regulation Committee.<sup>2</sup> Enforcement presented two witnesses and Respondents presented three witnesses.

Enforcement called Shelly Wilson, a team leader in the Market Integrity Section of the Market Regulation Department, and Robert Ross, a registered securities principal and proprietor of ROSS. Ms. Wilson received a complaint from Robert Ross on October 7, 1996 concerning Olde’s trading with ROSS in OAKT and subsequently conducted the NASD Regulation investigation preceding this disciplinary action. (Tr. 46-47). Mr. Ross is the sole proprietor of ROSS and the firm trader who answered the telephone 20

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<sup>1</sup> Respondents specifically admitted that: Olde and ROSS were registered market makers in OAKT on October 7, 1996 (Answer at ¶ 5); Wodek was Olde’s trader in OAKT on October 7, 1996 (Answer at ¶ 3); Olde was quoting OAKT in 1/8 increments and ROSS was quoting OAKT in 1/32 increments on October 7, 1996 (Answer at ¶ 5); Olde sold OAKT to ROSS in 20 separate 100 share transactions during the period from 2:25 - 3:58 p.m. on October 7, 1996 (Answer at ¶ 7); Olde executed these 20 trades on a principal basis (Answer at ¶ 8); and Olde had no customer sell orders in OAKT that were marketable during the relevant time (Answer at ¶ 9).

<sup>2</sup> Because the allegations in the Complaint contained a cause of action involving a violation of a rule or statute described in Rule 9120(s) (*i.e.*, the execution of transactions and trading practices), the Parties requested that one of the panelists be a current or former member of the Market Regulation Committee. The Deputy Chief Hearing Officer, pursuant to Rule 9231(b)(2), appointed a former member of the Market Regulation Committee to the Hearing Panel in this proceeding.

different times on October 7, 1996, and bought 2,000 shares of OAKT that Wodek sold in 20 transactions. (Tr. 47-48, 121). Mr. Ross testified via telephone.<sup>3</sup>

Respondents' counsel called Wodek, Kenneth Madsen, and James Speight as witnesses. Kenneth Madsen, a Vice President at Olde, is the firm's compliance director and senior registered options principal. (Tr. 205). James Speight currently is employed at Piper Jaffray, an NASD member firm located in Minneapolis, Minnesota. Mr. Speight worked at Olde on the firm's trading desk in various capacities (trader, assistant vice president of trading, vice president of trading, and head of trading) from March 1990 to January 1998. (Tr. 226-227).

The Hearing Officer admitted into evidence 22 exhibits Enforcement offered (CX 1 - CX 10, and CX 12 - CX 23),<sup>4</sup> eight exhibits Respondents offered (RX 1, RX 2 and RX 4 - RX 9),<sup>5</sup> and one exhibit the Parties jointly offered (JX 1).<sup>6</sup> The Parties also filed joint Stipulations concerning many of the factual events that occurred on October 7, 1996.<sup>7</sup> The Stipulations will be referenced in detail in the Findings of Fact portion of this decision.

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<sup>3</sup> The Hearing Officer previously granted the Department of Enforcement's motion for leave to offer telephone testimony of Robert Ross. See Order Granting The Department of Enforcement's Motion For Telephone Testimony dated January 22, 1998.

<sup>4</sup> References to Enforcement's Exhibits admitted at the Hearing will be designated "CX".

<sup>5</sup> References to Respondents' Exhibits admitted at the Hearing will be designated "RX".

<sup>6</sup> References to Joint Exhibits admitted at the Hearing will be designated "JX". JX 1 is the same document that Respondents pre-marked RX 3 and Enforcement pre-marked CX 11. See Stipulations filed on April 2, 1998 at 1.

<sup>7</sup> See Stipulations, filed on April 2, 1998.

## II. FINDINGS OF FACT AND CONCLUSIONS OF LAW

Wodek began working for Olde in 1991 as an assistant on the firm's bond desk. He moved to Olde's NASDAQ trading desk in December 1991 and assumed the responsibilities of a trading assistant. (Tr. 157). After working as a trading assistant for one and one half years, Wodek began trading his own book of 20-25 NASDAQ stocks in the fall of 1993. (Tr. 158). Wodek began trading OAKT stock in May 1996.<sup>8</sup> Wodek is series 4, 7, 8, 24, and 63 qualified and currently trades 21-22 different stocks. (Tr. 158).

### A. Cause One: Anti-Competitive Practices

The underlying facts relating to the OAKT trades effected on October 7, 1996 that relate to Cause One are not in dispute. Olde, a registered broker-dealer and member of the NASD, was registered with the NASD as a market maker in OAKT on October 7, 1996. (Stipulations at ¶¶ 1-2). Wodek was registered with the NASD as a general securities representative on October 7, 1996 and was responsible for trading OAKT securities that day. (Stipulations at ¶ 3). Between 2:25 p.m. and 3:58 p.m. on October 7, 1996, Wodek sold ROSS 2,000 shares of OAKT in 20 separate 100 share transactions. (Stipulations at ¶ 4). Wodek or his trading assistant,

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<sup>8</sup> Wodek testified that he traded stocks that Olde recommended and other stocks in which he was interested. OAKT was not a stock that Olde recommended. Wodek purchased OAKT for his personal account in December 1995 and began trading OAKT on behalf of Olde in May 1996 after the Olde trader who followed OAKT left the firm. (Tr. 161).

Chris Chakford, who was acting on Wodek's behalf, called ROSS 20 times offering to sell 100 shares at ROSS' bid; ROSS executed each order and never changed the price or size of its bid. (Stipulations at ¶ 4).<sup>9</sup> Olde effected all 20 trades as principal and had no customer sell orders in OAKT that were market qualified during the relevant time period. (Stipulations at ¶¶ 5-6).

Robert Ross faxed two complaints to the Department of Market Regulation on October 7, 1996, concerning the manner in which Olde sold OAKT to ROSS on October 7, 1996.<sup>10</sup> Mr. Ross explained that Olde's repeated telephone calls were disruptive and required him to divert his attention away from monitoring the markets he made in 75-100 other securities. (Tr. 129). Mr. Ross noted that he considered Wodek's behavior to be harassment,<sup>11</sup> and a response to his quoting OAKT in 1/32 increments, which he referred to as "breaking a spread." (CX 1 and Tr. 125). On cross examination, Mr. Ross admitted that he had filed complaints with the NASD about other market makers harassing him on many occasions. (Tr. 147).

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<sup>9</sup> The Parties incorporated into their Stipulations two pages from the Equity Trade Journal for OAKT on October 7, 1996. This attachment provides detailed information concerning Olde's trading in OAKT on October 7, 1996. According to this attachment, Olde effected 33 trades in OAKT involving 9,705 shares on October 7, 1996.

<sup>10</sup> The first fax complained that from 2:25 to 2:57 p.m. Olde called him eight times to sell 100 shares as principal each time, and noted that "[h]ere is an example of what I have to put up with when I break spreads." (CX 1, CX 2 and Tr. 125).

<sup>11</sup> Mr. Ross noted that "generally speaking I do not get phone calls to do trades; it's done [via] a SelectNet system where I can just press a button and excuse [execute] it. Instead in this case, I had to pick up the phone, talk to the person on the other end, find out who they were, find out not only who they were, which firm they were, had to find out the individual's name, I had to confirm that I would do the trade when he said he wanted to sell me a hundred shares. Then I had to -- in this case ask him -- I was so surprised about the trade-- whether or not this was being done as an agent, because I was a little shocked that they were doing this. Then I had to hang up the phone and then print the trade through our ACT system. Then I had to confirm that they printed their side, and then I had to confirm that the trades locked in together. All that for that hundred shares." (Tr. 128).

Wodek indicated that he telephoned Mr. Ross rather than preferencing him on SelectNet<sup>12</sup> because at that time he preferred the telephone and infrequently used SelectNet outside of being busy at the open or close, or when he had something going on in two or three different stocks. (Tr. 170). Wodek also testified that he did not offer Mr. Ross 2,000 shares of OAKT the first time he spoke with him on October 7, 1996 because Wodek “believed if [he] offered him two thousand shares that he would back away from his market, that he would not buy two thousand shares from [Wodek] based on the previous experiences that [he’d] had with Mr. Ross and based on experience that other traders at Olde Discount had with Mr. Ross.” (Tr. 169).<sup>13</sup>

Ms. Wilson testified that on October 7, 1996, during the period in question, nine broadcast orders on SelectNet were priced better than the NASDAQ inside bid of 9 29/32.<sup>14</sup> Ms. Wilson further testified that if Mr. Wodek was attempting to obtain best

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<sup>12</sup> SelectNet is a screen-based trading system offered to members of the NASD to facilitate negotiation of transactions in securities through automated means, by-passing the need for telephone contact. SelectNet allows members to enter orders, direct orders to one or all market makers in a security, and negotiate the terms of the order through counter-offers entered in the system. A broadcast order on SelectNet is an order that is sent to every registered market maker in that particular security. (Tr. 67).

<sup>13</sup> Mr. Wodek stated: “[p]reviously on certain occasions, not always, I would try to do trades with Mr. Ross and he would answer the phone -- actually, before he would answer the phone, he would move his market and decline to do trades with me at which point, you know, there was no recourse for me.” (Tr. 169).

<sup>14</sup> (Tr. 65). See also CX 9 at 2-3. This exhibit is the SelectNet Activity Report in OAKT for October 7, 1996. Respondents’ counsel objected to the admission of CX 9 on relevance grounds and referenced the Hearing Officer’s January 22, 1998 Order denying Respondents’ Motion to Compel Production of Documents. (Tr. 62-64). Respondents had requested that the Hearing Officer, pursuant to Code of Procedure Rule 9252(a), issue Rule 8210 requests for information to Instinet, an NASD member firm, for all orders entered into the Instinet System on October 7-9, 1996 in four securities other than OAKT. The Hearing Officer denied Respondents’ request for information under Rule 9252(a) on relevance grounds, and, also, because Respondents failed to demonstrate, as required by Rule 9252(b), that the requested information would be material and non-cumulative. See Order Denying Respondents’ Motion to Compel Production of Documents, dated January 22, 1998 at 10-13.

execution through obtaining a higher price for the OAKT that he wanted to sell on behalf of Olde, he could have done so using SelectNet. (Tr. 66-70).

The only issue for the Hearing Panel then is: why did Wodek call ROSS 20 times in the span of 90 minutes to sell 100 shares of OAKT in 20 separate transactions?<sup>15</sup> The Hearing Panel considered the testimony of Messrs. Ross and Wodek and found Mr. Wodek's testimony less than credible with respect to why he sold OAKT to ROSS in 20 separate 100 share transactions. Wodek's principal claim is that he sold OAKT to ROSS in the manner that he did because of past experiences with ROSS backing away from its quotes. Wodek further testified that he did not actively use SelectNet or Instinet in October 1996, and did not see on his trading screen during the subject period either the SelectNet broadcast orders (Tr. 170-71), or Instinet orders (Tr. 171-72) at a higher bid than ROSS.<sup>16</sup>

The Hearing Panel concluded that Mr. Wodek's explanation was not credible for several reasons. First, if Wodek's prior experience with ROSS involved instances of backing away, Wodek could have effected the trade via SelectNet and obtained empirical evidence to demonstrate that ROSS in fact backed away from his OAKT

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<sup>15</sup> None of the 20 trades when reviewed as individual transactions violates NASD rules.

<sup>16</sup> The better bids in OAKT available via SelectNet in four of the nine instances referenced by Ms. Wilson were available for execution by any OAKT market maker for more than two minutes. See CX 9 at 2-3, Tr. 68-69. Mr. Wodek's trading screen was set up in October 1996 so that SelectNet orders were visible at the top of the screen with a maximum of four display lines. As SelectNet orders in the various securities Wodek traded appeared on his screen, earlier orders would scroll off his screen. (Tr. 171). Mr. Wodek nevertheless admitted that he knew how to execute SelectNet orders on October 7, 1996, (Tr. 184-85, 192) and that the nine SelectNet orders in OAKT at a higher bid than ROSS posted during the relevant period would have appeared on his trading screen.

quote.<sup>17</sup> Instead, Wodek decided to telephone ROSS and give ROSS an opportunity to change his quotation before answering the phone, the very process Wodek testified was the source of his concern.

Second, assuming that Wodek infrequently used SelectNet or did not see the better OAKT offers scroll across his terminal's screen, Wodek's testimony fails to explain, in the Hearing Panel's judgment, why Wodek did not attempt to sell the second thousand shares of OAKT to ROSS in one transaction. After Wodek sold 100 shares to ROSS on ten occasions without ROSS moving its quotes or reducing its size, Wodek's concerns or fears about ROSS backing away should have been eliminated.<sup>18</sup> At that point, regardless of whatever may or may not have happened between Wodek and ROSS in the past, the Hearing Panel could find no convincing explanation why Wodek sold an additional one thousand shares of OAKT to ROSS in ten 100 share transactions between 3:11 p.m. and 3:58 p.m.<sup>19</sup> Consequently, the Hearing Panel concluded that Wodek intended to harass ROSS for narrowing the spread in OAKT.<sup>20</sup>

On August 8, 1996, the Securities and Exchange Commission issued an order instituting and settling an administrative proceeding against the NASD.<sup>21</sup> Among other

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<sup>17</sup> See colloquy between one Hearing Panelist and Wodek at Tr. 200-02.

<sup>18</sup> In fact, after successfully selling 100 shares of OAKT to ROSS in several transactions (i.e., three or four) without ROSS moving its quotation or changing its size, Wodek's backing away fears, presumably, should have been assuaged.

<sup>19</sup> See Tr. 181-84.

<sup>20</sup> Each of the registered market makers in OAKT on October 7, 1996, except ROSS, quoted OAKT in 1/8 increments. ROSS, however, quoted OAKT that day in increments of 1/32, which narrowed the differential between market makers' bid and ask quotations.

<sup>21</sup> See Exchange Act Release No. 37538 (August 8, 1996) and Report Pursuant to Section 21(a) of the Securities Exchange Act of 1934 Regarding the NASD, the Nasdaq Market, and Nasdaq Market Makers, Exchange Act Release No. 37542 (August 8, 1996), and Appendix thereto.

things, that order made certain findings about the NASD and conduct on the NASDAQ market and imposed remedial sanctions, which included an agreement by the NASD to a series of specific undertakings. Undertaking 12 required the NASD “[t]o enforce NASD [Conduct Rule 2210] with a view to enhancing market maker competitiveness by: (a) acting to eliminate anticompetitive or unlawfully enforced or maintained industry pricing conventions, and to discipline market makers who harass other market makers for narrowing the displayed quotations in the Nasdaq market, trading not more than the quantities of securities they are required to trade under the NASD’s rules, or otherwise engaging in competitive conduct.”<sup>22</sup> The Commission also clearly indicated that the behavior prohibited under the NASD’s proposed rule change responding to Undertaking No.11 “has continually been violative of NASD Rule 2110 and the federal

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<sup>22</sup> Id. Undertaking 11 specifically required the NASD to propose a rule or rule interpretation for Commission approval which expressly makes unlawful the coordination by or among market makers of their quotes, trades and trade reports, and which prohibits retribution or retaliatory conduct for competitive actions of another market maker or other market participants. The NASD submitted a proposed rule change to the Commission, which was approved on July 17, 1997, that, among other things, defined as conduct inconsistent with just and equitable principles of trade for a member firm to engage in conduct that threatens, harasses, coerces, intimidates or otherwise improperly attempts to influence another member in a manner that interferes with or impedes the forces of competition among member firms in the Nasdaq Stock Market. See Exchange Act Release 38845 (July 17, 1997), 1997 WL 401052.

securities laws....”<sup>23</sup> In short, engaging in conduct toward another market maker that is designed to harass or punish that person for quoting in increments that narrow market makers’ spreads or otherwise designed to discourage competitive practices is and has been violative of NASD Conduct Rule 2110 (formerly Article III, Section 1 of the Rules of Fair Practice).<sup>24</sup>

B. Cause Two: Olde’s Written Supervisory Procedures

Count Two of the Complaint alleges that Olde failed to establish, maintain and enforce adequate written supervisory procedures to deter and detect anti-competitive behavior by Olde traders in violation of Conduct Rules 2110 and 3010. (Complaint at ¶14). Conduct Rule 3010 requires member firms to establish a supervisory system reasonably designed to achieve compliance with applicable laws, rules and regulations. The Rule further requires that, as a component of the supervisory system, a member must establish and maintain written supervisory 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 laws, rules and regulations.

The National Adjudicatory Council (“NAC”) and SEC provide guidance as to what is required for written supervisory guidelines to comply with NASD Conduct Rule

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<sup>23</sup> Exchange Act Release No. 38845 (July 17, 1997), 1997 WL 401052.

<sup>24</sup> See also IM-21105-5, where the Board of Governors noted that it is “issuing this interpretation to codify a longstanding policy.”

3010(b). In the Matter of the Application of Gary E. Bryant, Exchange Act Release No. 32357 (May 24, 1993), 51 S.E.C. 463, 1994 SEC LEXIS 1347 at \*19, the SEC affirmed an NASD disciplinary proceeding and found Respondent's written supervisory guidelines deficient because there were no mechanisms for ensuring compliance and the guidelines did not establish specific functions to be followed by the person identified as responsible for ensuring compliance by the firm and its registered representative.<sup>25</sup>

The Parties agree that written supervisory procedures covering Olde's trading department existed on October 7, 1996, and do not contest the content of those procedures.<sup>26</sup> Enforcement argues Olde's written procedures are deficient because they make "no mention of any prohibition against anti-competitive behavior by Respondent's registered representatives and associated persons... and do not provide for: (1) identification of the person(s) responsible at Olde to ensure compliance with the prohibition against anti-competitive behavior; (2) a statement of the step(s) that such person(s) would take to ensure compliance therewith; (3) a statement as to how often

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<sup>25</sup> In Bryant, the Respondent firm's written supervisory procedures consisted of "two pages of specific procedures with a one-page addendum enumerating 18 'prohibited business practices.'" Market Surveillance Committee v. Anderson, Bryant & Co., Complainant No. MS-803 at 18 (August 1, 1991). In sustaining the Association's decision, the SEC found that the Respondent firm's written supervisory procedures provided "nothing more than a list of things that the firm and its representatives should not do." 1994 SEC LEXIS 1346 at 19. The SEC also found that "the firm's structure included no specific controls or supervisory procedures designed to deter and detect misconduct." Id. See also Market Regulation Committee v. Castle Securities Corp., Complaint No. CMS 940100, 1996 NASD Discip. LEXIS 37, at \*24-6 (NBCC October 21, 1996), aff'd., In re Castle Securities Corp., Exchange Act Release No. 39523, 66 S.E.C. Docket 531, 1998, SEC LEXIS 24 (Jan. 7, 1998); In re Freeland, Exchange Act Release No. 32192, 53 S.E.C. Docket 2452, 1993 SEC LEXIS 878 at \*6 (April 22, 1993). As the SEC noted in Bryant, "to ensure investor protection, a broker-dealer must establish and enforce effective procedures to supervise employees (citation omitted). The procedures must assure that restrictions issued are not ignored by branch managers, registered representatives or any other office personnel." Bryant, supra, 1994 SEC LEXIS at \*19.

<sup>26</sup> The Parties submitted as a joint exhibit Olde's OTC Trading Department's written policies and procedures in effect on October 7, 1996. See JX 1, at 6-34.

such person(s) would take such step(s); or (4) a statement as to how enforcement of such written supervisory procedures would be evidenced at OLDE.”<sup>27</sup>

Respondent Olde contends that its policies and procedures for supervising its OTC traders were reasonable, (Tr. 205, 163-68) but does not contest that its policies and procedures did not identify the persons responsible for ensuring compliance with the prohibition against anti-competitive behavior, a statement of the steps such persons would take to ensure compliance therewith, a statement as to how often such persons would take those steps, or a statement as to how enforcement of such supervisory procedures would be evidenced at Olde.<sup>28</sup>

Olde also claims that its policies and procedures were not deficient in that the firm was in the process of revising its policies and procedures in the fall of 1996, as were other broker-dealers that make markets in NASDAQ securities, to reflect developments relating to the Department of Justice’s investigation into trading practices in the NASDAQ Stock Market. Olde further notes that Conduct Rule 3010(b)(3) provides, in pertinent part, that “[e]ach member shall amend its written supervisory procedures as appropriate within a reasonable time after changes occur in applicable securities laws and regulations, including

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<sup>27</sup> Department of Enforcement’s Statement of Undisputed Facts and Memorandum of Points and Authorities in Support of Motion for Partial Summary Disposition, at 1-2. See also JX 1, at 6-34. On March 11, 1998, the Hearing Panel denied Enforcement’s Motion for Partial Summary Disposition with respect to Cause Two. See Final Pre-Hearing Conference Order, Order granting Respondents’ Motion to Adjourn the March 17, 1998 Hearing, Order Rejecting Respondent Wodek’s Contested Offer of Settlement, And Order Denying the Department of Enforcement’s Motion for Partial Summary Disposition, dated March 11, 1998 at ¶ 14.

<sup>28</sup> Respondent Olde acknowledges in its Response to Enforcement’s Motion for Partial Summary Disposition that it “agrees to the narrow facts alleged as undisputed by Enforcement in that section of its motion.” Olde Response To Motion For Partial Summary Disposition, at 1.

the Rules of this Association, and as changes occur in its supervisory system, and each member shall be responsible for communicating amendments through its organization.”<sup>29</sup>

Messrs. Wodek, Madsen and Speight each testified that in July 1996 Olde undertook a series of steps to communicate to its employees its policy on market maker harassment,<sup>30</sup> as well as how Olde de facto monitored for anti-competitive trading practices.<sup>31</sup> Among other things, traders attended at least two meetings at which Olde’s senior legal and compliance officials discussed prohibited, anti-competitive practices, including harassing other market makers who narrowed spreads by quoting in smaller increments. (Tr. 164-65). Traders and assistant traders received copies of a portion of Olde’s Stipulation and Order settling a Department of Justice civil action relating to anti-competitive practices by NASDAQ market makers, and were required to sign an annual NASDAQ certification form acknowledging they had read and agreed to abide by the terms of the Stipulation and Order entered in the Department of Justice’s civil action. (CX 22).<sup>32</sup> The prohibited conduct specifically included “[e]ngag[ing] in any harassment or intimidation of any other market maker, whether in the form of written, electronic, telephonic, or oral communications, for decreasing its dealer spread

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<sup>29</sup> Conduct Rule 3010(b)(3). See Olde’s Response to Motion for Partial Summary Disposition, at 2.

<sup>30</sup> See CX 22, which is a July 23, 1996 memorandum from Olde’s General Counsel to all Olde NASDAQ traders and assistant traders referencing a July 17, 1996 meeting between the General Counsel and the traders and assistant traders where Olde’s settlement with the Justice Department concerning anti-competitive market maker behavior was discussed. The July 23, 1996 memorandum attached an excerpt from the Stipulation and Order entered in the Department of Justice’s civil action against Olde and other market makers that specifically referenced prohibited market maker conduct.

<sup>31</sup> (Tr. 163-68, 205-11, 227-30).

<sup>32</sup> Wodek signed such a Nasdaq trader certification form dated November 21, 1996. (CX 21 at 3).

or the inside spread in any Nasdaq security.” (CX 22 at 8). In addition, James Speight served as Olde’s trading supervisor, sitting on the trading floor among the traders and monitoring their activities and conversations.

The Hearing Panel found Olde’s written supervisory procedures as it relates to the trading desk to be inadequate for purposes of Conduct Rule 3010 for several reasons. First, Olde’s written procedures in effect on October 7, 1996 were silent with respect to anti-competitive practices and do not identify specific supervisors who are responsible for ensuring that Olde’s traders are not engaging in anti-competitive behavior or practices, including harassing other market makers. Although Mr. Speight sat on the trading desk, had no trading responsibilities himself, monitored trading activities, and listened to traders on the telephone, neither he nor Mr. Madsen could specifically and directly explain Olde’s supervisory procedures for detecting and deterring anti-competitive activity in October 1996.<sup>33</sup>

Mr. Madsen testified that Mr. Speight received a copy of the July 17 memorandum from Olde’s General Counsel attaching a copy of the prohibited anti-competitive activities “so that he would know and read about what type of conduct that he should be listening for while he was on the trading desk, and to investigate any issues that came to his attention as a result of that.” (Tr. 210). At no time, however, did Mr. Madsen indicate that he or any one else in the firm instructed Mr. Speight, orally or in writing, as to what steps he should take as a trading supervisor to monitor for compliance, what exception reports to review, what to investigate, or how to document any such investigations.

Mr. Speight's testimony indicated that he was in charge of risk management for the trading desk and had an ability to monitor each trader's positions and how much capital each trader was tying up. (Tr. 228). Mr. Speight also indicated that he reviewed exception reports on a daily basis and "was in proximity to everybody, so [he] kept [his] ears open, [his] eyes open." (Tr. 228). Although Mr. Speight provided the Hearing Panel with some examples of the kinds of things he would listen for during the course of the trading day,<sup>34</sup> the Hearing Panel concluded that Mr. Speight's principal considerations involved customer order executions, concentrated positions and general risk management matters relating to Olde's capital. (Tr. 228-29). As a result, the Hearing Panel concluded that Olde's written supervisory procedures did not provide reasonable guidance to Mr. Speight as to what he was or was not to do to assure that Olde's traders were not engaged in anti-competitive activities.

Messrs. Madsen and Wodek also repeatedly indicated that Olde's trading policies were being revised in light of the new rules and regulations. (Tr. 208 ).<sup>35</sup> The Hearing Panel, however, found the suggestion that the NASD or Securities and Exchange Commission had adopted new rules or regulations relating to anti-competitive conduct by NASDAQ market makers troubling. Anti-competitive practices generally, and harassment against a market maker for reducing the spread in Nasdaq securities in particular, are and

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<sup>33</sup> See Tr. 209-11, 228-30.

<sup>34</sup> For example, Mr. Speight noted: "If I heard something that was being said on the phone that I thought was inappropriate, I would not hesitate to go over there and tell the person stop or put it on hold. And lots of times they weren't saying anything wrong, I just wanted to make sure that indeed they weren't saying anything wrong." (Tr. 228).

<sup>35</sup> Mr. Madsen stated that throughout the July - November 1996 period "Olde was in the process of reviewing its procedures, updating its procedures **in light of the new rules and regulations.**" (emphasis added) (Tr. 208).

have been practices that are inconsistent with just and equitable principles of trade. (See IM-2101-5, Exchange Act Release No. 37538 (August 8, 1996)).

The Hearing Panel also determined that even if the SEC or NASD had adopted new rules or regulations regarding anti-competitive behavior or practices in the July-August 1996 period,<sup>36</sup> Conduct Rule 3010(b)(3) would provide Olde with a reasonable period of time to amend its written supervisory rules. The Hearing Panel concluded that the two-to-three month period between the Department of Justice's July 17, 1996 Stipulation and the SEC's August 8, 1996 action against the NASD, and Wodek's harassment of ROSS on October 7, 1996, provided Olde with ample time to amend its written supervisory procedures. Although the Hearing Panel recognizes that Olde took some steps to make its traders aware of specific prohibitions against anti-competitive practices, its written policies and procedures on October 7, 1996 nevertheless were deficient.

Olde's written supervisory procedures on October 7, 1996 made no reference to anti-competitive practices or harassing other market makers for narrowing spreads. Olde merely distributed lists of prohibited anti-competitive activities to its traders, which, as the SEC made clear in Bryant, are not adequate written supervisory procedures for purposes of NASD Rule 3010(b). Notwithstanding Mr. Speight's presence among Olde's traders on the trading floor, a generally positive supervisory and compliance step, the Hearing Panel concluded that Mr. Speight was not adequately instructed by Olde as to what he was to do to monitor for anti-competitive behavior. (Tr. 227-29). Consequently, the Hearing Panel

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<sup>36</sup> The Hearing Panel specifically found that neither the NASD nor the SEC adopted any new rules or regulations concerning anti-competitive behavior or conduct by market makers during this period.

concluded that Olde's written supervisory procedures as they relate to anti-competitive activities by the firm's traders were deficient and in violation of NASD Conduct Rules 3010 and 2110.

### III. SANCTIONS

#### A. Cause One: Wodek's Anti-Competitive Conduct

There is no specific Sanction Guideline<sup>37</sup> addressing anti-competitive conduct that violates Conduct Rule 2110. In the absence of a sanctions guideline for a specific violation, adjudicators are encouraged to look to the Sanction Guidelines for analogous violations,<sup>38</sup> and generally consider the principals and considerations that are applicable whenever an adjudicator must impose sanctions.<sup>39</sup> The Hearing Panel, for the reasons discussed below, determined to censure Wodek, fine him \$15,000, and require him to become qualified as a Limited Representative - Equity Trader (Series 55) within sixty (60) days of this decision for harassing ROSS on October 7, 1996.<sup>40</sup>

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<sup>37</sup> The National Adjudicatory Council (formerly known as the National Business Conduct Committee) establishes and periodically revises its Sanction Guidelines so that member firms may become more familiar with some of the typical securities industry violations and the disciplinary sanctions that may result. The Sanction Guidelines serve as a guide to adjudicators in an effort to achieve greater consistency, uniformity, and fairness when imposing sanctions.

<sup>38</sup> NASD Sanction Guidelines (May 1998) at 2.

<sup>39</sup> NASD Sanction Guidelines (May 1998) at 3-9. E.g., The respondent's relevant disciplinary history, if any; whether respondent engaged in numerous acts and or a pattern of misconduct; whether the respondent's misconduct occurred over an extended period of time; and the number, size and character of the transactions at issue.

<sup>40</sup> See NASD Rule 1032(f). The qualification examination for Limited Representative - Equity Trader, or Series 55, became effective on April 1, 1998. Although traders who have registered for the Series 55 examination by May 1, 1998, which has since been extended to August 31, 1998, are given until May 1, 2000 to pass the examination pursuant to Rule 1032(f)(2)(B), the Hearing Panel determined that Wodek should be required to become Series 55 qualified as soon as reasonably practicable. See NASD Notice to Members 98-17 (February 1998) and NASD Notice to Members 98-60 (July 1998).

Enforcement argued that the Hearing Panel should consider as aggravating factors the fact that Wodek's conduct occurred in close proximity to the SEC's enforcement proceeding against the NASD and involved "precisely the type of conduct which the SEC directed the association to eliminate in its August 8, 1996, administrative proceeding." (Tr. 245). In addition, Enforcement forcefully argued that Wodek's "anti-competitive behavior harms not only the target of the harassment, but other market participants as well." (Tr. 247). Enforcement also argued that Mr. Wodek should be suspended for a period of time, at least two weeks. (Tr. 245).

Respondents argued that any suspension of Wodek would be unnecessary and inappropriate under the circumstances of this case. (Tr. 265-66).<sup>41</sup>

The Hearing Panel agreed that Wodek's conduct was serious, particularly in light of the publicity attendant to the Department of Justice's civil actions relating to NASDAQ market makers' anti-competitive activities and the SEC's administrative action against the NASD. The Hearing Panel, however, also determined that Wodek's anti-competitive behavior should be analyzed for sanction purposes as one occurrence,<sup>42</sup> even though multiple transactions were involved, and that Wodek's behavior on October 7, 1996 was an isolated event.

The Hearing Panel found that Wodek, albeit somewhat reluctantly, understands that the behavior he engaged in is improper. Wodek has no disciplinary history, and there

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<sup>41</sup> Respondents' counsel devoted his closing argument principally to demonstrating that Wodek had not engaged in anti-competitive behavior designed to harass ROSS (rather than focusing on sanctions) and that Olde had reasonable supervisory procedures in place to detect and deter anti-competitive behavior by the firm's traders. (Tr. 252-66).

<sup>42</sup> All of Wodek's transactions in OAKT with ROSS that are involved in this proceeding occurred over a ninety minute period on one day, October 7, 1996.

is no suggestion that he engaged in this kind of anti-competitive behavior on any other occasion. Moreover, each of the trades Wodek effected with ROSS on October 7, 1996, when viewed in isolation, was not in violation of any specific NASD rule.

The Hearing Panel considered a suspension and determined that, based on the circumstances of this proceeding, a suspension was not warranted. In lieu of a suspension, and to ensure that Wodek fully understands securities industry regulations relating to the NASDAQ Stock Market and market maker obligations, the Hearing Panel concluded that Wodek should be required to become qualified as a Limited Representative - Equity Trader (Series 55) by passing the Series 55 examination as soon as practicable, rather than permitting him to continue trading without having passed the Series 55 examination until May 1, 2000.<sup>43</sup> The Hearing Panel concluded that a censure, the adverse publicity attendant to the imposition of a \$15,000 fine, and early qualification as a Limited Representative - Equity Trader were sufficiently remedial to deter future misconduct by Wodek and others. The Hearing Panel, therefore, based on the record in this proceeding, censured Wodek, fined him \$15,000, and required him to qualify as a Limited Representative - Equity Trader within sixty (60) days of the effective date of this decision.

B. Cause Two: Olde's Written Supervisory Procedures

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<sup>43</sup> But for the decision in this disciplinary proceeding, Wodek would have until May 1, 2000 to pass the Series 55 examination. See Rule 1032(f)(2) and NASD Notice to Members 98-60. If Wodek fails to become registered as a Limited Representative - Equity Trader by taking and passing the Series 55 examination within 60 days of this decision, he will be violating Rule 1032(f) if he continues to function as an equity trader.

The Sanction Guidelines provide that the appropriate sanction for deficient written supervisory procedures in violation of NASD Conduct Rules 2110 and 3010 is a fine of \$1,000 to \$25,000; generally no other sanction is recommended.<sup>44</sup>

In addition to the principal considerations adjudicators generally should consider,<sup>45</sup> the Sanction Guidelines provide that adjudicators specifically should consider whether deficiencies in written supervisory procedures allowed violative action to occur or escape detection, and whether the deficiencies made it difficult to determine the persons responsible for specific areas of supervision.<sup>46</sup>

The Hearing Panel concluded that the deficiencies in Olde's written supervisory procedures, while disturbing, were not egregious. The Hearing Panel's decision to fine the firm \$20,000, while at the high end of the fine range, relates principally to the fact that Olde failed to provide adequate guidance to Mr. Speight as to what he, as a

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<sup>44</sup> In egregious cases, adjudicators also should consider suspending the firm with respect to any or all relevant activities or functions for up to 30 business days and, thereafter, until the supervisory procedures are amended to conform to rule requirements. NASD Sanction Guidelines (May 1998) at 90.

<sup>45</sup> NASD Sanction Guidelines (May 1998) at 8-9.

<sup>46</sup> See id. at 90.

supervisor present on Olde's trading desk, was expected to do to detect and deter anti-competitive behavior by Olde's traders. The Hearing Panel found this lack of guidance particularly disturbing in light of Olde's settlement with the Department of Justice in July 1996. In this regard, Olde was aware of the Department of Justice's investigation for some time prior to the July 17, 1996 Stipulation and Order; yet Olde failed to modify its written supervisory procedures to provide guidance to Olde's supervisors concerning what they should be doing to reasonably review for anti-competitive behavior by the firm's traders. In addition, the Hearing Panel concluded that Olde's recent disciplinary sanctions for deficient supervisory procedures<sup>47</sup> were an aggravating factor warranting a higher fine.

#### IV. CONCLUSION

The Hearing Panel found that Respondent Wodek engaged in anti-competitive activities and harassment on October 7, 1996 by calling another market maker 20 times over a ninety minute period and selling 100 shares in 20 separate transactions when the other market maker was the only market maker quoting OAKT in increments of 1/32 and whose bid was for 1,000 shares. The Hearing Panel censured Wodek, fined him \$15,000 for violating NASD Conduct Rule 2110, and required him to qualify as a Limited Representative - Equity Trader within sixty (60) days of the effective date of this decision.

The Hearing Panel concluded that Olde failed to establish, maintain and enforce written supervisory procedures that were reasonably designed to prevent its traders from engaging in anti-competitive behavior in violation of NASD Conduct Rules 2110 and

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<sup>47</sup> See CX 23 at 1-2. The NASD censured and fined Olde \$5,500 on August 22, 1997 for, among other things, having inadequate written supervisory procedures to ensure compliance with various NASD marketplace rules. The NASD also censured and fined Olde \$8,000 on April 23, 1997 for trading through two limit orders and failing to establish, maintain and enforce written supervisory procedures to prevent the violations.

3010. The Hearing Panel censured Olde and fined the firm \$20,000. The Hearing Panel assessed costs against Respondent Olde in the amount of \$1,627.25, consisting of a \$300 administrative fee and \$1,327.50 for the cost of the hearing transcript.<sup>48</sup>

Hearing Panel

by: \_\_\_\_\_  
Joseph M. Furey  
Deputy Chief Hearing Officer

Dated: August 26, 1998  
Washington, DC

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<sup>48</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.