NASD OFFICE OF HEARING OFFICERS

DEPARTMENT OF MARKET REGULATION

Complainant,

v.

YANKEE FINANCIAL GROUP, INC.
(CRD No. 17966)
150 Broadhollow Rd.
Suite 121
Melville, NY 11747,

RICHARD F. KRESGE
(CRD No. 729077)
91 Ocean Ave.
Bay Shore, NY 11706,

JOSEPH C. KORWASKY
(CRD No. 730276)
18 Dick Court
Northport, NY 11786.

Respondents.

Disciplinary Proceeding
No. CMS030182

Hearing Officer – AWH

Hearing Panel Decision

December 10, 2004

Member firm and its president found liable for (1) fraudulent sales practices and unsuitable recommendations of the firm's registered representatives, (2) failure to supervise registered representatives, (3) failure to report customer complaints, and (4) failure to register individual who engaged in conduct requiring registration. Compliance officer, who was employed for six months by the firm, found liable for failing to report one customer complaint, and found not liable for (1) failure to supervise, (2) allowing firm to operate without written supervisory procedures, and (3) failure to register individual requiring such registration. Member firm expelled and its president barred as a principal and in any supervisory capacity; firm and president ordered to pay restitution to customers in the amount of $3,866,426, and assessed costs. Former compliance officer issued a Letter of Caution.

Appearances:

Jeffrey K. Stith, Esq., and Matthew Campbell, Esq.,
for the Department of Market Regulation

Paul J. Bazil, Esq., and Joseph R. Benfante, Esq., of Pickard & Djinis LLP
for Yankee Financial Group, Inc. and Richard F. Kresge

Joseph C. Korwasky, pro se

DECISION

Background

On August 12, 2003, the Department of Market Regulation ("Market Regulation") issued the four-cause Complaint in this proceeding. The first cause alleges that Gary J. Giordano ("Giordano") and other Registered Representatives of Yankee Financial Group, Inc. ("Yankee" or the "Firm") engaged in fraudulent sales practices and made unsuitable recommendations to the Firm's customers, in violation of Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 10b-5, and NASD Conduct Rules 2110, 2120, 2310, and IM-2310-2. The first cause also alleges that Yankee and its President, Richard F. Kresge ("Kresge"), are liable for those violations. Cause two alleges that Yankee, Kresge, Giordano and Joseph C. Korwasky ("Korwasky") failed to supervise the Firm's employees and activities, failed to establish an effective supervisory system, and failed to establish adequate written supervisory procedures, in violation of NASD Conduct Rules 2110 and 3010. The third cause of the Complaint alleges that Yankee, Kresge, Giordano, and Korwasky failed to report customer complaints, in violation of NASD Conduct Rules 2110 and 3070(c). Finally, cause four alleges that Yankee, Kresge, and Korwasky violated NASD Conduct Rule 2110 and Membership and

Registration Rules 1021(a) and 1031(a), IM-1000-1, and IM-1000-3 by failing to register an employee who acted in a capacity that required registration.

On September 26, 2003, Respondents Yankee and Kresge jointly filed an Answer to the Complaint, denying all allegations of wrongdoing and requesting a hearing. Korwasky also filed his Answer to the Complaint that day, likewise denying all charges and requesting a hearing. Giordano filed an Answer on October 29, 2003, and he subsequently entered into a settlement agreement with Market Regulation, under which he consented to certain findings of fact and was permanently barred from the securities industry. A hearing was held on the remaining issues in the Complaint on April 26-29, 2004, before an Extended Hearing Panel composed of the Hearing Officer, a former member of the District 7 Committee, and a former member of the District 3 Committee. Each party filed a post-hearing brief.

On July 29, 2004, Respondents Yankee and Kresge filed a Motion for Leave to Adduce Newly Obtained or Discovered Evidence, to which Market Regulation responded on August 12, 2004.[1] Also, on September 8, 2004, Market Regulation filed a Motion to Strike Respondents' Misstatements of the Evidence, to which Yankee and Kresge responded in opposition on September 17, 2004.[2]

[1] The Motion is granted; however, the Extended Hearing Panel does not find the new evidence to be probative of any issue in the case.

[2] The Motion is denied. The Extended Hearing Panel has carefully evaluated all of the testimony and the documents that were admitted into evidence, and is basing its decision solely on that record. The arguments of counsel are not evidence.

Findings of Fact[3]

A. Respondents

1. Richard F. Kresge

Kresge, the founder, President, financial and operational principal ("FINOP"), and 95% owner of Yankee, has worked in the securities industry since 1978. Tr. 667, 817. He was a registered representative and principal of Yankee. Kresge was also Yankee's Compliance Officer, except from approximately March 2002 through May 2002, when the position was held by Korwasky. Tr. 669-70.

2. Joseph C. Korwasky

Korwasky has also been in the securities industry since 1978. Tr. 491. He became associated with Yankee in January 2002, and served as the Firm's Compliance Officer from March 28, 2002 through May 2002. Korwasky left Yankee in June 2002 and is currently registered with another member firm. RK-1.

3. Yankee Financial Group, Inc.

Since 1986, Yankee has been a registered broker-dealer and NASD member firm, with its business primarily concentrated in bonds. Tr. 819. Its principal office is in Bay Shore, New York. *Id*. The Firm expanded into equity trading in 2001 by acquiring another firm and adding new offices and personnel.

a. Yankee Opens a Melville, NY, Office

In January 2001, Yankee, acting through Kresge, reached an agreement with Kenneth Gliwa ("Gliwa") and Robert Stelz ("Stelz") to acquire the Melville, New York,

[3] References to Market Regulation's exhibits are designated C_; Respondents Yankee and Kresge's exhibits as R-YFG-_; Respondent Korwasky's exhibits as RK_; and the transcript of the hearing, as Tr._.

branch office of member firm Glenn Michael Financial, Inc. ("Glenn Michael"). Tr. 666, 668. Gliwa and Stelz had been registered principals of Glenn Michael since November 1999. C4, at 3. Primarily, their business consisted of municipal bonds, mutual funds, and listed equities. Tr. 667. Glenn Michael conducted very little business in penny stocks. *Id*.

To obtain NASD approval of Yankee's acquisition and expansion, Kresge took an old compliance manual that Glenn Michael had been using and had distributed to its brokers, taped "Yankee" over the firm's name on the cover, and then submitted it to District 10 with virtually no modifications.[4] Tr. 519, 772-73. Beyond the newly "revised" cover, the manual contained no reference to Yankee. Tr. 52-53, 520, 772-73. As a result of the merger, Yankee added two principals, a trading desk, and approximately 50 registered representatives to its existing group of 10-12 employees. Tr. 667.

The new branch office officially opened for business on or about March 21, 2001. It authorized new accounts and reviewed, approved, and executed customer orders. Kresge continued to direct and control the operations of Yankee as President, Compliance Officer, and 95% owner. Tr. 666-67. Gliwa continued servicing his own clients and operating and managing the branch office in Melville. Tr. 780. He also handled administrative matters, after-hours trading, and all technology support. Tr. 779-80. Stelz functioned as office manager of the Melville office and performed some bookkeeping functions. R-YFG-45, at 8-9. Kresge retained his primary office in Bay Shore, visiting the new office only about once every week to ten days. Tr. 669.

[4] District 10 required Yankee to modify only the options section of the compliance manual. Tr. 828-29; R-YFG-6.

b. Yankee Adds a Brooklyn, NY Office

In August 2001, Yankee, acting through Kresge and Gliwa, entered into negotiations with Joseph Ferragamo ("Ferragamo") and Joseph Masone ("Masone"), to open a branch office in Brooklyn. Masone was not registered with NASD. Tr. 671-674. Gliwa explained to Kresge that Masone was a client who knew a group of unhappy brokers[5] interested in joining Yankee. Tr. 671. Kresge did not know Masone. Tr. 672, 675. At their initial meeting, Masone introduced Kresge, Gliwa, and Stelz to Ferragamo, who claimed to be a Vice President of Valley Forge Securities, Inc. ("Valley Forge") and the leader of the group of brokers looking to defect from the New York City branch office of that firm. Tr. 673-75, 707.

All Kresge knew about Ferragamo was that he was a licensed broker. Tr. 705. In actuality, Ferragamo had been in the securities industry since 1997, and had switched firms six times in four years. Tr. 706. Joseph Ferragamo has not been registered with NASD since September 2001. C5. He had never been a registered general securities representative or principal; he was licensed only as a Series 62 corporate securities limited representative. C5, at 4-10. Ferragamo was also the subject of two pending customer arbitrations that claimed total damages of $190,000, allegedly caused by unauthorized trading, unsuitable recommendations, misrepresentations, and breaches of contract and fiduciary duties. C5, at 13-16.

At their initial meeting, Ferragamo represented to Kresge, Gliwa, and Stelz that he and the brokers wanted to leave Valley Forge and that he was always "chasing his commission." Tr. 675. Kresge viewed Ferragamo as the "chief Indian" of this group of brokers. Tr. 693, 713-16. Finally, Ferragamo claimed to own his branch office, and

[5] In this decision, the term "broker" is used synonymously with "registered representative."

suggested that he knew a candidate for the branch manager position in the new office. Tr. 675-76, 678-79.

Following that first meeting, Stelz told both Kresge and Gliwa that he was uneasy about the proposal, and warned them to check Ferragamo's and Masone's backgrounds. R-YFG-45, at 22, 47-48.[6] Kresge was aware that Masone delivered documents between the Melville and Brooklyn offices Tr. 801.

Shortly after the meeting, Ferragamo supplied Kresge with social security or CRD numbers for himself, the other Valley Forge brokers, and Gary Giordano, whom he wanted to serve as branch manager. Tr. 677-79. Kresge checked CRD disciplinary records and NASD's Taping Rule list for information on those individuals. Tr. 680. He did not check CRD records to determine what licenses Ferragamo held, whether he was in fact registered, or confirm his supposed ownership interest in Valley Forge. Tr. 707-09. Moreover, Kresge could not recall asking Ferragamo whether he had been involved in, or the subject of, any compliance or regulatory issues. Tr. 712-13. Kresge only learned about Ferragamo's pending arbitration claims much later, and he never learned that a little more than ten months prior to their initial meeting, federal prosecutors had issued an indictment alleging that Valley Forge's New York City office was controlled by organized crime figures. Tr. 711-12. When Kresge did finally learn about one of the arbitrations, he did not check into the details of the matter, stating "[i]t did not seem, at the time, to be something that would alarm me about him." Tr. 721. He admitted that, had he known there were actually two arbitration claims pending against Ferragamo, "[i]t absolutely would have affected my decision to do business with him." Tr. 728.

[6] *See also* R-YFG-43, at 51 (Gomolak expressing similar feelings of uneasiness and distrust). Scott Gomolak was the Firm's trader in Melville.

There was some controversy at the hearing as to whether Kresge actually placed a call to Robert Montani, a compliance person at Valley Forge. Kresge emphatically insisted not only that he placed the call to check out Ferragamo's and the other brokers' backgrounds, but that he received "a wonderful recommendation" from him. Tr. 707, 710-11. Robert Montani, however, rebutted Kresge's version at the hearing, denying that Kresge called him. Rather, he testifed that he had to call Kresge twice because Yankee brokers were falsely telling Valley Forge customers that the firm was out of business, or about to go out of business, and they needed to move their accounts to Yankee. Tr. 920-21, 926-28. The Hearing Panel credits Montani's testimony, finding it unlikely that Kresge made this call in light of his otherwise minimal due diligence efforts.

Kresge and Gliwa again met with Ferragamo and Masone in early September 2001. Tr. 679-80. Michael Trotta, CEO of Silver Star Foods, joined them. Tr. 680. Kresge neither knew Trotta nor why he attended the meeting; nor did he ask. Tr. 683-84. The meeting concluded with an oral agreement to open a Brooklyn branch office of Yankee. Tr. 692-93.

At Ferragamo's recommendation, Kresge hired Giordano to be the branch manager of what was to become the new Brooklyn branch office. Tr. 691, 728. Giordano had passed his Series 7 examination in December 1997 and had been employed by five different firms in the four years that followed. C6, at 13. He also passed his Series 24 principal's examination in March 2001, six months before he was to lead the new Yankee office. *Id.* Kresge reviewed Giordano's CRD record, but could not recall reviewing his examination history. Tr. 731-33.

Ferragamo and Giordano were to recruit brokers for the office, pay all expenses, and run the day-to-day operations of the branch. Tr. 700, 714, 734-35, 773. Ferragamo, in fact, would finance the branch. Tr. 715-16. Yankee and Kresge would take a $25 charge on every ticket and would receive 15% of that office's gross commissions; the remainder would be sent to Giordano in a single, monthly check made payable only to him. Tr. 693-94. However, the office was never officially designated as a Yankee Office of Supervisory Jurisdiction ("OSJ"). Tr. 867.

There are no records to account for distribution of the money Kresge sent to Giordano by check, and Kresge never asked for an accounting. Tr. 701-02. There was no written agreement describing the arrangement between Kresge and Ferragamo or the ownership and operation of the Brooklyn branch. Tr. 693. Furthermore, Kresge knew that he was required to submit an amended Form BD to disclose that Ferragamo was financing the Brooklyn office, but he never did. Tr. 716. Kresge learned later that Masone had been paying the rent and other branch office expenses through an entity called DJM Holdings. Tr. 839-40.

Giordano recruited brokers for the Brooklyn office. Kresge retained the right of final approval for their hiring, and testified that he interviewed all of them except Dugo. Tr. 733-35, 753-54. Kresge processed the brokers' Forms U-4. He did not ask questions beyond those required by the form, and he did not call any of their prior firms. Tr. 748-54.

Kresge did not know that one of the brokers Giordano hired, Adam Klein, was associated with nine different firms in the six years prior to joining Yankee. Tr. 753. Another broker, Eric Cenname, had been associated with 11 firms in the eight years prior

to being hired as a broker at Yankee. Tr. 749. Moreover, Klein and Cenname had each worked for at least one firm that was subject to the requirements of the Taping Rule. C8-9.

Another new broker, David Anderson, was only 20 years old when he was hired, and during his two years in the industry prior to joining Yankee, he had been associated with four different firms and was the subject of one customer arbitration claim for unauthorized trading. Tr. 746-48. Kresge was unaware of this information and explained at the hearing that all that mattered to him was whether his brokers were Series 7 licensed and whether they had clean CRD disciplinary records. Tr. 740.

Larry Dugo was another broker hired for the Brooklyn office. Kresge had never met Dugo. He hired him solely on the recommendation of Giordano. Tr. 753-54. Dugo had been associated with eight different firms in the six years prior to arriving at Yankee. One of those firms was subject to the Taping Rule, and another, that Kresge recognized as a "bad firm," had closed. Tr. 759-60. Dugo's CRD disciplinary record listed his 1984 arrest and guilty plea for cocaine possession, a felony charge which was later dismissed after he successfully completed a drug treatment program. C10, at 6. Finally, Dugo was the subject of a pending customer arbitration claim when Yankee hired him. C10, at 7. Kresge explained that he might have known about Dugo's CRD disclosure issue, but never asked him about it and, instead, was convinced by Giordano that Yankee should hire him. Tr. 754.

In October 2001, with seven employees, Yankee opened its Brooklyn office, under the management and supervision of Giordano. Masone controlled the entity which held the lease for that office. Tr. 839.

B. Sale of Speculative OTCBB Stocks

The first Cause of the Complaint alleges that Yankee brokers engaged in fraudulent sales and unsuitable recommendations for which Yankee and Kresge are liable. Those transactions are discussed below.

1. Securities

a. Silver Star Foods, Inc.

Silver Star Foods, Inc. ("SSTF") was a distributor of pre-packaged frozen pasta products. C12. Its 10-QSB filed with the Securities and Exchange Commission ("SEC") for the period ended June 30, 2001, reported no revenues, total current assets of $100,883, total current liabilities of $974,480, and a net loss of $67,890. The filing also contained a "going concern" opinion issued by SSTF's accountants. Furthermore SSTF disclosed that it had essentially ceased doing business and that its survival depended upon a "contemplated offering." SSTF also divulged two outstanding legal judgments against it totaling $372,924, owed to vendors in accounts payable. Subsequent SEC filings showed no improvement in the company's financial condition. Masone owned a large quantity of SSTF stock. Tr. 629.

b. Western Media Group, Corp.

Western Media Group, Corp. ("WMGC") operated through three diverse, wholly owned subsidiaries. C13. In its quarterly filing for the period ended September 30, 2001, WMGC reported total current assets of $46,284, of which $3,494 was cash. It had liabilities of $6,452. The Form 10-QSB also noted that WMGC had relied almost exclusively on one customer for its revenue. WMGC's accountants expressed doubt as to the company's ability to continue as a going concern. In their opinion letter from that

quarterly filing, the accountants projected that WMGC only had enough revenue to continue operating for twelve months, unless it obtained additional capital or could acquire and integrate another technology service company. The company reported no improvement in its financial condition in subsequent SEC filings.

c. Golden Chief Resources, Inc.

Golden Chief Resources, Inc. ("GCHR") held gas and oil interests in Texas and Louisiana. C14. On its Form 10-QSB for the period ending June 30, 2001, GCHR reported having no operations from 1986 to 1999, re-entering the development stage, and being entirely dependent on raising new capital, which it doubted being able to do. The company reported total current assets of $23,802, including $102 in cash, total current liabilities of $717,316, and a net operating loss of $994,678. In that filing, GCHR's accountants expressed doubt as to the company's ability to continue as a going concern. Furthermore, the company completed a 1:10 reverse split in December 2001. Subsequent filings showed no improvement.

2. Customer Sales

The Brooklyn office solicited public customers to purchase large quantities of highly speculative OTCBB securities. From October 2001 through April 2002, brokers in Yankee's Brooklyn office sold more than eight million shares of SSTF, WMGC, and GCHR to the public for a total of $8,377,270: $6.3 million in SSTF, $1.6 million in WMGC, and $500,000 in GCHR. C20, at 1-5. The following testimony of ten customers related to these sales is undisputed, and the Extended Hearing Panel finds it both credible and consistent.

a. JC

Customer JC is an 86-year-old retiree with a very conservative investment objective and no experience investing in penny stocks. Tr. 162, 167-68. His Yankee representative was registered broker Anderson, who has subsequently been barred from the industry. JC relied on Anderson's recommendations in making his investment decisions. Tr. 172, 175. Anderson recommended that JC purchase SSTF, but explained none of the risks of that investment or any material negative facts about the company. Tr. 172-75. JC lost $1,150,575 on the investment. Tr. 179. JC later settled a claim against Yankee for $100,000. Tr. 177-78. So far, JC has received $50,000 and a promissory note for the remaining $50,000, leaving him with a net loss of $1,050,575. Tr. 177-78.

b. DW

Customer DW also dealt with Anderson on his Yankee account. In fact, it was Anderson who persuaded DW to transfer his accounts to Yankee. Tr. 69. DW sent Anderson approximately $94,000, which was approximately 75% of his total accumulated savings. Tr. 76. He also enclosed a letter to Anderson, explaining that he had four accounts: one for retirement, and three college saving fund accounts, one for each of his children. Tr. 70, 74-75; C33, at 33. Anderson called DW frequently to recommend purchasing shares of WMGC. Tr. 78. DW decided to invest, based on Anderson's false representations that WMGC was like a Berkshire-Hathaway hedge fund, an investment pool managed by Warren Buffet, who has a well known reputation for investment success. Anderson predicted that the price of WMGC would rise from about $1.50 to $2.00 or $2.25. Tr. 78-80. However, Anderson did not disclose to DW the risks of investing in WMGC or its poor financial condition. Tr. 80-82. DW suffered

a loss on the investment of $62,100. C21, p. 1, C33, p.1. After several attempts, DW finally reached Kresge, who claimed to want to compensate DW for his loss. Tr. 91, 103. Negotiations between the two continued through late 2003. Tr. 96. At one point, Kresge asked DW to submit a letter to NASD, which would show that they were engaged in settlement negotiations. Tr. 94-95. DW refused and has yet to receive any compensation. Tr. 95.

c. WB

Anderson also handled the account of 84-year-old retired customer WB, who told Anderson that he wanted solid investments and insisted on a stop loss for any drop in price of 15% or more for any specific stock. Tr. 187, 196. Anderson placed frequent calls to WB, giving price predictions and urging him to purchase stock. Tr. 200. Anderson strongly recommended SSTF, WMGC, and GCHR, touting each company for its good potential. Tr. 198-99. WB followed Anderson's recommendation and purchased substantial amounts of each stock. Tr. 203-08. Although he gave Anderson a blanket stop-loss order to sell any stock that dropped 15% from its purchase price, WB eventually sustained a loss of $1,219,691. Tr. 196, 217. WB has recouped $27,999.99 as part of a court order in settlement of the state of Oklahoma's claims against Yankee, Kresge and Anderson, resulting in a net loss of $1,191,691.01. Tr. 218-19; C23, at 59-64.

d. GR

Anderson first contacted 68-year-old customer GR in the fall of 2001. Tr. 235, 237-38. GR explained to Anderson that his goal was to save for retirement and not to speculate. Tr. 241-42, 262. Nevertheless, Anderson failed to discuss GR's risk tolerance with him. Tr. 263. Instead, he called GR every two or three days, enthusiastically

recommending WMGC as a lucrative investment, while never mentioning the company's poor financial condition or the risks associated with such an investment. Tr. 245, 248, 251-52. From discussions with Anderson, GR understood WMGC to be a potential future purchase for a Berkshire-Hathaway fund. Tr. 249-50. GR followed Anderson's advice about WMGC, discussed putting in place a stop-loss order, and bought the stock. Tr. 250-53. At some point after the stock price fell, another Yankee broker sent GR a penny stock disclosure form, which GR refused to sign because it was furnished *after* his purchase. Tr. 256-57. GR ultimately lost $42,240. Tr. 258-59; C-21, p. 1.

e. GA

Anderson also targeted 84-year-old Customer GA in September 2001. Tr. 385, 388. Anderson told GA that SSTF was a restaurant undergoing an expansion and its stock would soon double in value. Tr. 391, 396. He also touted WMGC as another company that would do very well. Tr. 391-92. Anderson failed to explain to GA any of the risks of investing in these companies. Tr. 392, 398. GA had most of his investments in savings accounts; but because interest rates had dropped, he decided he wanted to improve his rate of return, and, accordingly, he followed Anderson's advice. Tr. 390. When the price of the stocks fell, GA tried to reach Anderson, and was told that Anderson had left early to care for his mother. Tr. 397. GA lost $992,340. Tr. 398; C22, p. 1.

f. JL

Customer JL is a 66-year-old retiree who was solicited to purchase shares of SSTF by Cenname, who was, at that time, a Yankee broker-trainee. Tr. 109-10, 116-18. Cenname was later barred by NASD. Cenname actually first solicited JL while he was

with LH Ross & Company, Inc. Tr. 115. Cenname called JL several times a week, making price predictions about SSTF and claiming that he and his family were investing in the company. Tr. 117-18. Cenname further claimed that the stock was a new offering, and that he was involved personally with the company. Tr. 119. He did not, however, discuss with JL the risks of investing in SSTF or the company's poor financial condition. Tr. 121-23. Instead, Cenname urged JL to invest the $228,000 in proceeds he received from a recent sale of his former home. Tr. 120-21. JL followed the broker's advice and subsequently lost $224,354. Tr. 123, 136; C27, p. 1. When JL sought reimbursement from the Firm, he was offered $500. Tr. 134. Later, JL spoke with Kresge, who told him that the Firm had limited funds and would only pay JL if JL signed a release of claims against Yankee and Kresge. Tr. 134-35.

g. JH

Sixty-one-year-old retired Customer JH also received solicitations from Cenname. Tr. 268-70. JH was content with smaller gains for less risk, and was more concerned about the downside potential than the upside potential of investments.[7] Tr. 273-74. Cenname recommended SSTF, predicting an inevitable boost in price. He represented to JH that he knew the company's president, he recommended the stock to his own mother, and he would not facilitate an investment which he could not sell later. Tr. 278-79. Cenname never advised JH about the company's financial weaknesses. Tr. 279-80. Cenname purchased about $240,000 of SSTF stock for JH in two transactions, only one of which was authorized. Tr. 277, 281-82, 286. JH still owns the stock, which has

[7] At the hearing, JH noted that, although his new application form stated that he had an interest in speculative investments, he did not authorize that statement and, to the contrary, he had no interest in speculative investments. Tr. 272-73.

declined in value to about a penny per share. Tr. 285-86. His total loss on the investment is $236,985. C26, p. 1.

h. RP

Customer RP was a 57-year-old independent computer consultant who recently had been laid-off from his a job when he was first solicited by Dugo at Yankee. Dugo has since been permanently barred by NASD. Tr. 310, 312, 314. Primarily, RP had been saving for retirement. Tr. 312. Having lost money from stock investments made in 1999 and 2000, he was somewhat risk averse. Tr. 316. Dugo strongly recommended that RP purchase WMGC and SSTF, predicting that each would double or triple in value in the near future. Tr. 316-17, 319-21. Dugo gave RP the impression that he was knowledgeable about WMGC and SSTF, but he failed to inform him of the risks associated with investing in either financially troubled company. Tr. 321-22, 327-28. RP followed Dugo's advice, and lost $7,377. C28, p. 1.

i. GW

Dugo contacted 55-year-old Customer GW sometime shortly before March 1, 2002. Tr. 338, 340, 342. GW explained to Dugo that, while he was willing to assume *some* investment risk, he also had significant financial constraints: he did not have much money to invest and was burdened by substantial outstanding tax liabilities. Tr. 345. GW further expressed a need for fairly liquid investments in light of his financial limitations. Tr. 345. Dugo called GW two to three times a week to recommend investing in SSTF. Tr. 347-48. Dugo gave GW the impression that he had very reliable information about the company because he met regularly with people at Yankee who were in close contact with principals of SSTF. Tr. 350. He told GW that SSTF was

expanding and was about to make a lot of money. Tr. 348. Dugo never mentioned the risks of investing in SSTF or mentioned its poor financial condition. Tr. 355-56. In fact, he noted that the company was performing adequately in its core business of frozen foods, and he pitched the stock as having limited risk. Tr. 348-49, 355-56. Dugo stated that SSTF was selling stock to finance its magazine promotion, but added that, if the magazine failed, the stock price would be unaffected. Tr. 348, 355. Dugo enthusiastically promoted the stock, predicted it would double in price, and said that he had a limited quantity to sell. Tr. 349-50. GW told Dugo that he would have to borrow against his credit card to purchase the stock. He later sent Dugo $14,656.50 to purchase shares in SSTF. Tr. 351, 357-58. Although GW still owns the stock, it is currently worth only a penny per share. Tr. 355. His loss on the investment is $14,400. C31, p.1.

j. AW

Sixty-two-year-old retired Customer AW was also contacted by Dugo. Tr. 377. Dugo recommended purchasing SSTF shares, although he provided him with no financial data about the company. Tr. 378. AW purchased 41,000 shares of SSTF at a cost of about $60,476. He was later able to sell the shares for $1,771.92, resulting in a loss of $58,704.08. *Id.*

3. Kresge's Knowledge of OTCBB Transactions

Every two or three days, Kresge reviewed commission runs which listed stock sales by each registered representative. Tr. 670-71. Kresge knew that the Brooklyn brokers were selling low-priced securities. Those sales had been an ongoing topic of discussion among Kresge, Gliwa, and Stelz because Yankee principals were not entirely comfortable with that aspect of their newly expanded business. R-YFG-45, at 34.

Nevertheless, on occasion, Kresge reviewed and approved order tickets for certain large purchases of stock in SSTF, WMGC, and GCHR.[8] Tr. 439-42. Therefore, he knew or should have known that Ferragamo and Giordano frequently directed the Firm's trader, Scott Gomolak, to purchase shares of SSTF, WMGC, and GCHR, at a specific price from Sierra Brokerage Services, Inc., and Georgia Pacific. Tr. 436-41.

C. Yankee's Supervisory System

1. Kresge's Role

Kresge was overwhelmed by the pace of sales in the Brooklyn office. In its first three months of operation, the brokers in that office sold nearly $3 million of SSTF stock alone. Tr. 782; C20, at 1-2. Kresge did not know whether the brokers were trained to assess the suitability of investments in speculative securities for their customers.[9] Tr. 763-64. He understood the importance of suitability, but he specialized only in bonds and mutual funds. As a result, he left suitability guidelines to be addressed by people supervising the Brooklyn office. Tr. 763-65.

Kresge was generally unaware of what was happening in the Brooklyn office. Tr. 769. He viewed that office as an independent operation not under Yankee's main office supervision. Yankee was compensated only for executing trades solicited by that office. Tr. 773. Kresge knew that the brokers in that office were "aggressive," but he figured that the aggressive brokers were dealing with aggressive customers. Tr. 764.

In the Brooklyn office's second month of operation, Stelz warned Kresge that the activity in that office needed to be closely monitored. R-YFG-45, at 34. He emphasized

[8] Gomolak usually went to Gliwa for approval of these tickets. Infrequently, if Gliwa was not available, he went to Kresge or Steltz for approval. Tr. 440. On one or two occasions, he was told to have Korwasky initial the ticket. Tr. 445.

[9] When asked whether brokers received training in proper sales practices, he replied, "I imagine." Tr. 763.

two concerns: that orders needed to be properly handled and that Yankee principals needed to be "vigilant" about compliance. R-YFG-45, at 35. Through December 2001, during the time he was the compliance officer, Kresge visited the Brooklyn office three times, never for long, and never in a supervisory or compliance capacity. Tr. 776-77. He did not review files or check for customer complaints. Tr. 777. From October 2001 through March 2002, no Yankee representative in the Melville or Brooklyn offices received a copy of written supervisory procedures, or signed a form acknowledging receipt of a copy. Tr. 771; R-YFG-43, at 37, 50.

2. Kresge Delegates Supervisory Responsibilities to Gliwa and Giordano

Kresge delegated his responsibilities for supervising sales practices in Brooklyn to Gliwa, but suitability reviews were to be done by Giordano, who was to involve Kresge or Gliwa only if there was a problem. Tr. 766-67, 773-76. However, Kresge never gave Giordano a set of written supervisory procedures; he assumed someone would "pass along" to him the old Glenn Michael manual. Tr. 770-71. There is no evidence that Gliwa ever received formal supervisory instructions or training at Yankee, but he did have conversations with Kresge about his duties and responsibilities as supervisor of the Brooklyn office. Tr. 833-34.

Kresge never asked Gliwa for a report on compliance at the Brooklyn office; his primary concern was how that office was doing financially.[10] Tr. 778. He knew that Gliwa rarely visited the Brooklyn office, and that Gliwa knew almost nothing about the brokers in that office. Tr. 777-78.

[10] At the hearing, Kresge testified to the contrary and "disputed" his earlier statement, made in on-the-record testimony, that he did not ask Gliwa about compliance at Brooklyn. Tr. 778. The Extended Hearing Panel finds his earlier testimony to be credible and consistent with other evidence of Gliwa's minimal involvement with the Brooklyn office.

During his on-the-record interview, Gliwa confirmed that suitability analysis was the responsibility of the Brooklyn office, and sales practices were supervised from that office. Tr. 768. However, he denied being involved in supervision in Brooklyn, except that, to protect the firm on big trades, he would check to make sure the client had adequate funds to pay for the trade. Tr. 768.

3. Kresge Hires Korwasky

When Kresge learned that Gliwa was overwhelmed with work, regularly working very late hours, "wearing seven or eight hats, [and] running around like a chicken without a head," he hired Korwasky to become the full-time Compliance Officer, including responsibility for compliance in the Brooklyn office.[11] Tr. 778-79, 787. Korwasky had been the Managing Director and Compliance Officer at Jaron Equities Corp. Tr. 493. Korwasky left Jaron in January 1996, and, for ten months thereafter was not employed in the securities industry. From November 1996 to January 2001, Korwasky was the Compliance Officer at J.B. Sutton Group ("Sutton"), where he supervised and conducted surveillance of registered representatives' daily sales activities. Tr. 506-07.

Korwasky began his employment with Yankee on January 1, 2002, and, after a trial period of almost two months as an in-house consultant, he was given the title of "Vice President [of] Compliance." Tr. 513-14. On or about February 19, 2002, Kresge filed a Form U-4 on Korwasky's behalf and updated Yankee's Form BD, documenting Korwasky's new title. Tr. 514; C1, at 24, 32.

On January 7, 2002, Korwasky sent Kresge a memorandum listing 33 compliance issues he suggested they discuss on January 9. R-YFG-15. Those items included written

[11] At the hearing, Kresge tried to "correct" his previous testimony, claiming that Gliwa was accustomed to the high volume of business in that office, and that he could handle it. Tr. 782-83.

supervisory procedures, supervisory structure, CRD check of all new hires, quarterly filing of customer complaints, review of the Brooklyn office, and a telephone "observation" program.

Korwasky's top priority was to establish appropriate written supervisory procedures. Tr. 515-17. Kresge hadn't provided any written supervisory procedures to the Brooklyn office. Tr. 771. In fact, during the several months from the inception of the Melville and Brooklyn offices, there was no revised manual for Yankee, itself. Tr. 869-70. Korwasky reviewed the former Glenn Michael manual that had been re-labeled with Yankee's name, and he realized not only the true urgency of the task, but also that he needed to start "almost from square one" to get an appropriate manual in place. Tr. 521. To accomplish this task, Korwasky began to adapt a supervisory manual from Sutton. Tr. 661.

During his employment with Yankee, Korwasky was not frequently in direct contact with individuals in the Melville office. Tr. 790, 794. He complained about lack of equipment provided to him, and the very small size and physical condition of the office space he was to occupy. As a result, he mainly worked from home and was only present at the Melville location about once or twice per week. Tr. 534-35, 538, 791-92, 794. However, Korwasky communicated with Kresge on a daily basis.[12] Tr. 794.

In mid or late March 2002, Kresge received and read the preliminary supervisory manual prepared by Korwasky. Tr. 805. Kresge made a brief comment to Korwasky that it looked good, but Kresge described it in two on-the-record interviews as grossly

[12] Gliwa complained to Kresge about Korwasky, telling him that he suspected Korwasky had a drinking problem, but Kresge continued to rely on Korwasky. Kresge described Korwasky to NASD District 10 Staff as "useless" and "a drunk." However, at the hearing, he apologized for those words, and said, "I take them back now." Kresge said that in trusting Gliwa over Korwasky, he trusted the wrong man. Tr. 793-95.

deficient.[13] Tr. 525-26, 806-09. After reviewing the manual, Kresge arranged for a private company to prepare an improved version. Tr. 869. As of September 2002, three months after Korwasky left Yankee, no updated manual was in place at the firm.

Kresge also hired Korwasky to conduct an immediate and thorough review of the Brooklyn office. Tr. 578-79, 784-89; R-YFG-45, at 44. Nonetheless, it was not until late February 2002, after the Firm was notified that it was being investigated by NASD, that Kresge and Gliwa first brought Korwasky to the Brooklyn office and introduced him to Ferragamo, Giordano, and the other employees there. Tr. 548-49, 560. Following a series of meetings, when Korwasky learned more about Ferragamo's role in the Brooklyn office, he warned Kresge that Ferragamo should not be involved with that office, and, specifically, should not be financing it. Tr. 556-61. Korwasky explained that Ferragamo chose not to be registered with Yankee so that he could avoid NASD regulation and avoid any award that might result from a pending arbitration. Tr. 552-62. Kresge agreed with Korwasky, and acknowledged that Ferragamo was involved whenever there were discussions about the Brooklyn office. Tr. 556-57, 674, 680, 691. Kresge, nonetheless, accepted Ferragamo's various putative explanations for not wanting to become registered. Tr. 718-19.

Kresge also knew that Masone was unregistered, was in the Melville office frequently, was acting as a courier between that office and the Brooklyn branch, and was permitted to use an office and telephone. Tr. 799-801. It was Korwasky who eventually banned Masone from the firm's offices. Tr. 558-59. Korwasky also concluded that the

[13] Kresge changed his testimony at the hearing, explaining that he only "scanned [the manual] very quickly," that he had been negatively influenced by Gliwa, who did not like Korwasky, and that he now believes Korwasky's manual is good. Tr. 806-07.

brokers in Brooklyn needed to be monitored, and he unsuccessfully urged Kresge to install a telephone monitoring system in that office. Tr. 575-76.

4. The Executive Suite in Staten Island

Some time in April 2002, Kresge discovered that Dugo and another broker, along with two staff members, were operating out of an executive suite in Staten Island. Tr. 541-46. Kresge sent Korwasky to investigate the matter. Korwasky did, and quickly called Kresge, telling him to close that operation immediately. Tr. 541-44. He also recommended heightened supervision for Dugo. Tr. 591-92; R-YFG-17. Kresge and Korwasky told Dugo and the other broker to return to Brooklyn, but they resigned the next business day. Tr. 542. In June 2002, six months after he began his employment with Yankee, Korwasky resigned. RK-1.

5. Closing Up Brooklyn and Acknowledging its Problems

Near the end of July or early August, Kresge placed restrictions on the types of stock that could be sold from the Brooklyn office. Tr. 812, 845-46. In August, he terminated Anderson after receiving several customer complaints and after Anderson failed to appear for an NASD investigative interview. Tr. 845-46. Before he resigned, Korwasky had recommended putting Anderson under heightened supervision as well. Tr. 844-45; R-YFG-17. In September 2002, Kresge terminated Giordano's employment and closed the Brooklyn office. Tr. 844.

D. Customer Complaints

For the fourth quarter of 2001 and the first and second quarters of 2002, Yankee received 18 customer complaints that were not reported in a statistical and summary report required by NASD Conduct Rule 3070(c). C34. Specifically, three were from the

fourth quarter of 2001, and eight were from the second quarter of 2002, for which Kresge was responsible. Seven occurred in the first quarter of 2002, when Korwasky was responsible for reporting complaints.[14] However, although complaints were supposed to be forwarded to Korwasky, he had personal knowledge of only one complaint that was filed during that quarter. Tr. 913-14. Kresge stated that neither he nor anyone else supervised Korwasky on reporting customer complaints under NASD Conduct Rule 3070(c) in the first quarter of 2002. Tr. 790.

Discussion

A. Fraudulent Sales Practices and Unsuitable Recommendations

1. Yankee Brokers' Violations

a. Fraudulent Sales Practices

To establish that Yankee brokers violated Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and NASD Conduct Rule 2120, Market Regulation must prove that: (1) the brokers made omissions or misrepresentations in connection with the purchase or sale of securities; (2) the omissions or misrepresentations were material; and (3) the brokers made them with the requisite intent, i.e., scienter. *See Dis. Bus. Conduct Comm. v. Euripides*, No. C9B950014, 1997 NASD Discip. LEXIS 45, at *18 (NBCC July 28, 1997).

i. Misrepresentations and Omissions

Yankee brokers made no risk disclosures in connection with any of the sales of SSTF, WMGC, and GCHR at issue in this proceeding. Moreover, they often enthusiastically gave false information about the companies' prospects and stability at a

[14] One complaint was withdrawn by the customer four days after it was submitted, because the customer admitted that its basis was erroneous. Tr. 898-99.

time when those companies' losses were mounting and when their auditors placed "going concern" qualifications on their financial statements. The Yankee brokers used other boiler-room type tactics such as creating a false sense of urgency to invest, claiming to be investing themselves or for family members, and making baseless price predictions. As a result, the Yankee brokers' positive spin on the companies' investment potential had no reasonable basis.

ii. Materiality

Ten Yankee customers made their decisions to invest based on these misrepresentations and omissions. The test for materiality is "whether the reasonable investor would consider a fact important" in making an investment decision, or whether disclosure would "significantly alter . . . the 'total mix' of information made available." *Martin R. Kaiden*, Exchange Act Release No. 41,629, 1999 SEC LEXIS 1396, at *18 n.25 (July 20, 1999); *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976). The brokers' omissions or misrepresentations were all in some way tied to the clients' prospects of earning profits on their investments. Therefore, they were material because any reasonable investor would find profitability to be a key reason to invest.[15]

[15] The Extended Hearing Panel notes that predictions of specific and substantial increases in the price of a speculative security within a relatively short period of time, without any reasonable basis, are inherently misleading. *See C. James Padgett*, Exchange Act Release No. 38,423, 1997 SEC LEXIS 634, at **23-24 (Mar. 20, 1997) (finding that predictions of sizeable stock price increases that are made without any reasonable basis are fraudulent), *aff'd*, 159 F.3d 637 (D.C. Cir. 1998) (table format), *cert. denied*, 525 U.S. 1070 (1999); *Richard Bruce & Co., Inc.*, Exchange Act Release No. 8,303, 1968 SEC LEXIS 220, at **12-13 (Apr. 30, 1968) (concluding that predictions of "a sharp increase in earnings with respect to a speculative stock without disclosure of the uncertainties as well as the known facts upon which a prediction rests [are] inherently misleading") (citation omitted). *See also Clinton Hugh Holland*, Exchange Act Release No. 36,621, 1995 SEC LEXIS 3452, at *8 n.16 (Dec. 21, 1995) (implying that the performance of stock of development-stage companies with a limited history of operations and no profitability is unpredictable).

iii. Scienter

Yankee brokers made the misrepresentations and omissions with scienter. Scienter is "a mental state embracing intent to deceive, manipulate, or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976). To prove scienter, there must be a showing that the respondent acted intentionally or with severe recklessness. *See M. Rimson & Co., Inc.*, 1997 SEC LEXIS 486, at *95 (Feb. 25, 1997). Recklessness has been defined as highly unreasonable conduct involving not merely simple or excusable negligence but an extreme departure from the standards of ordinary care. *See In re Michael B. Jawitz*, No. CMS960238, 1999 NASD Discip. LEXIS 24, at **19-20 (NAC July 9, 1999) (citing *Hollinger v. Titan Capital Corp.*, 914 F.2d 1564, 1568-69 (9th Cir. 1990), *cert. denied*, 499 U.S. 976 (1991) (citations omitted)). A respondent may not plead ignorance as a defense to recklessness if a reasonable investigation would have revealed the truth to the respondent. *See SEC v. Infinity Group*, 993 F. Supp. 324, 330 (E.D. Pa. 1998). The brokers' conduct was intentional, or, at the very least, reckless. They easily could have reviewed the companies' public disclosure documents to learn the true financial conditions at SSTF, WMGC and GCHR, and it was their duty to do so. Moreover, in many situations, they could have minimized their customers' losses by honoring those customers' stop-loss orders.

By making intentional omissions of material facts, false statements, inadequate risk disclosures, and baseless price predictions to customers in connection with their purchases of SSTF, WMGC, and GCHR shares, Yankee brokers violated Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and NASD Conduct Rule

2120. As a result of the violations, Yankee brokers also violated NASD Conduct Rule 2110.

b. Unsuitable Recommendations

In proving that Yankee brokers violated NASD Conduct Rule 2310 and IM-2310-2, it is incumbent upon Market Regulation to show that the brokers lacked a reasonable basis for believing that a recommended transaction was in a customer's best interests and was appropriate in light of that customer's investment objectives and financial situation. NASD Conduct Rule 2310; *Wendell D. Belden*, Exchange Act Release No.47,859, 2003 SEC LEXIS 1154, at **10-11 (May 14, 2003). Market Regulation must also show that the brokers recommended "speculative low-priced securities to customers without knowledge of or attempt to obtain information concerning the customers' other securities holdings, their financial situation, and other necessary data." IM-2310-2(b)(1).

Yankee brokers made unsuitable recommendations to ten public customers. Four customers were approximately 60-years-old; two were near or over age 70; and three were well into their 80s. Many of the customers were retirees, and none expressed an interest, or had a history of investing, in speculative stocks. At least one of the customers stated that he had a conservative investment objective, and the others had histories of investing conservatively. Another customer had a need for preserving principal, stating that he was planning for his retirement and for his three children's college education. The brokers ignored their customers' financial information and investment objectives, and failed to assess their customers' risk tolerance. Moreover, there was at least one unauthorized purchase made on behalf of a customer.

None of the brokers had a reasonable basis for believing that any of these transactions were suitable for their clients. Accordingly, the Extended Hearing Panel finds that the Yankee brokers violated NASD Conduct Rule 2310 and IM-2310-2.

2. Yankee's and Kresge's Secondary Liability

Cause one of the Complaint alleges that Yankee and Kresge are liable for the Yankee brokers' fraudulent sales practices and unsuitable recommendations. NASD has long held firms liable for the misconduct of their employees. *See, e.g.*, *Dist. Bus. Conduct Comm. v. A.S. Goldmen & Co., Inc.*, No. C10960208, 1999 NASD Discip. LEXIS 18 (NAC May 14, 1999), *aff'd* Exchange Act Release No. 44,328, 2001 SEC LEXIS 966 (May 21, 2001). A firm contravenes the injunction of Conduct Rule 2110 to "observe high standards of commercial honor and just and equitable principals of trade" when, acting through its registered representatives, it engages in fraudulent sales practices, in violation of Conduct Rule 2120, or makes unsuitable recommendations to its customers, in violation of Conduct Rule 2310. Moreover, the president of a member firm is responsible for compliance "unless and until he reasonably delegates particular functions to another person in that firm, and neither knows nor has reason to know that such person's performance is deficient." *John H. Gutfreund*, Exchange Act Release No. 31,554, 1992 SEC LEXIS 2939, at *44 (Dec. 3, 1992). Accordingly, Yankee and Kresge are liable for those violations by the brokers in the Brooklyn office.

The Complaint alleges two additional theories of the Firm's and Kresge's secondary liability for the misconduct of those brokers: respondeat superior and control person liability. Those theories of liability are consistent with NASD's holding that firms are liable for their employees' misconduct.

a. Respondeat Superior

Under the common law doctrine of respondeat superior, a principal is responsible for its agent's misconduct when it occurs within the scope of the agent's employment. *See* Restatement of Agency (Second) § 266 (1958). This doctrine has traditionally been used in tort law to satisfy the issue of causation. However, "[i]t has long been the position of the [Securities and Exchange] Commission that a broker-dealer may be sanctioned for the wilful violations of its agents under the doctrine of respondeat superior." *In re Bruce William Zimmerman*, Admin. Proc. File No. 3-4498, 1975 SEC LEXIS 2556, at *16 (Aug. 25, 1975). *See also Cady, Roberts & Co.*, Exchange Act Release No. 6,668, 1961 SEC LEXIS 385, at **11-12 (Nov. 8, 1961); *H. F. Schroeder & Co.*, Exchange Act Release No. 4,062, 1948 SEC LEXIS 33 (Mar. 15, 1948). In fact, there is a line of SEC cases, none of which has been overruled, that apply the doctrine of respondeat superior to the relationship between a broker-dealer and its agent. *See, e.g.*, *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, Exchange Act Release No. 14,149, 1977 SEC LEXIS 412 (Nov. 9, 1977); *In re Douglass & Co.*, Admin. Proc. File No. 3-4981, 1977 SEC LEXIS 2778 (May 27, 1977); *In re Shaw Hooker & Co.*, Admin. Proc. File No. 3-5037, 1977 SEC LEXIS 2773 (Mar. 11, 1977); *In re Richard J. Buck & Co.*, Admin. Proc. File No. 3-417, 1967 SEC LEXIS 2608 (June 26, 1967).

"The fact that Congress enacted an additional provision (Exchange Act § 20(a)) giving the Commission the power to impose a sanction on a broker-dealer for failure to adequately supervise its employees does not limit the Commission's power to discipline a broker-dealer for its employees' acts." *Armstrong, Jones & Co. v. SEC*, 421 F.2d 359, 362 (6th Cir. 1970). *See also Douglass & Co.*, 1977 SEC LEXIS 2778 ("[The firm] is of

course responsible for the conduct of its salesmen under the doctrine of respondeat superior.") (citations omitted). Firms are better able to control the behavior of their brokers than customers and regulators. *See, e.g.*, *In re Atlantic Financial Management, Inc.*, 784 F.2d 29, 32 (1st Cir. 1986) ("The business enterprise should bear the burden of the losses created by the mistakes or overzealousness of its agents [because such liability] stimulates the watchfulness of the employer in selecting and supervising the agents. . . . The principal, [having] . . . the opportunity of investigating the agent . . . should guarantee the [agent's] honesty.").

To establish Yankee's and Kresge's strict, vicarious liability under the doctrine of respondeat superior, Market Regulation has the burden of showing (1) that the brokers are "servants" of Yankee; (2) that they engaged in some sort of misconduct; and (3) the misconduct occurred within the servants' "scope of employment." *See* Restatement of Agency (Second) § 219 (1958).

Yankee and Kresge are principals because they were the brokers' employer and ultimate supervisor. Furthermore, Kresge was a registered principal with NASD. The brokers qualify as "servants" of Yankee and Kresge because Yankee and Kresge had the right to control their "physical conduct in the performance of . . . services." Restatement of Agency (Second) § 220(1) (1958). Indeed, it was Yankee's *duty* to establish guidelines for its brokers' conduct and then to monitor their conformity with those guidelines. The brokers' undisputed fraudulent and unsuitable sales practices, discussed above, constitute misconduct. That misconduct was within the "scope of employment" because (1) selling securities was what the brokers were employed to do; (2) the sales took place at Yankee facilities, on company time; and (3) the sales were conducted, at

least in part, to serve Yankee or promote its business. Restatement of Agency (Second) § 228 (1958). Accordingly, the Extended Hearing Panel finds that Yankee and Kresge are strictly, vicariously liable for Yankee brokers' violations.

b. Control Person Liability

As an additional theory of strict liability, Market Regulation asserts that, even if the doctrine of respondeat superior does not apply under the securities laws, Yankee and Kresge are liable for the acts of their employees under the doctrine of control person liability. Respondeat superior and control person liability are not mutually exclusive. *See In re Atlantic Financial Management, Inc.*, 784 F.2d 29, 32-35 (1st Cir. 1986) (engaging in a substantive analysis of vicarious liability and control person liability, and finding them to be independent doctrines); *Hollinger v. Titan Capital Corp.*, 914 F.2d 1564, 1577 (9th Cir. 1990) (*en banc*) ("Only if both respondeat superior and § 20(a) are available is the statutory scheme comprehensive and the public protected by the federal securities laws. 'To allow a brokerage to avoid secondary liability simply by showing ignorance, purposeful or negligent, of the acts of its registered representatives contravenes Congress' intent to protect the public, particularly unsophisticated investors.'") The legislative history of Exchange Act § 20(a)[16] has an expansive, not a restrictive, view of liability. Its purpose is "to prevent evasion of the [Act] . . . by organizing dummies who will undertake the actual things forbidden by the [Act]." *In re Atlantic Financial Management, Inc.*, 784 F.2d 29, 33 (1st Cir. 1986) (quoting relevant legislative history).

[16] Section 20(a) provides: "Every person who, directly or indirectly, controls any person liable under any provision of this chapter or of any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable, unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action."

Under the majority view, in order to establish a violation of § 20(a), Market Regulation must prove: (1) a primary violation by a controlled person; and (2) direct or indirect control of that primary violator by a respondent.[17] In establishing that a respondent had control over a primary violator, courts look for certain indicators, such as the power to influence, or direct, or manage the violator's actions, whether through the ownership of voting securities, by contract, or otherwise. *See First Jersey Secs., Inc.*, 101 F.3d 1450, 1472-73 (2d Cir. 1996). Moreover "[i]t is not necessary to show actual participation or the exercise of actual power . . . [U]nder certain circumstances, 'inaction in the form of a failure to supervise can . . . result in secondary liability.'" *Flood v. Miller*, 2002 U.S. App. LEXIS 10339 at *5 (May 30, 2002) (citation omitted). "[A] broker-dealer is a controlling person under § 20(a) with respect to its registered representatives." *Hollinger*, 914 F.2d at 1574.

The Yankee brokers' undisputed violations satisfy the first element of the test. As a broker-dealer, Yankee and its president, Kresge, qualify as controlling persons. Moreover, as employer and firm principal, they had the right to manage or otherwise control the brokers' conduct. Market Regulation, therefore, satisfied its burden in establishing control person liability.

The burden then shifts to Respondents Yankee and Kresge to show that they acted in good faith and did not directly or indirectly induce the violative actions of the brokers. *See Hollinger*, 914 F.2d at 1574-75 & n.25 ("We do not mean that a broker-dealer is vicariously liable under § 20(a) for all actions taken by its registered representatives. Nor

[17] The Fifth, Seventh, Eighth, Ninth, Tenth and Eleventh Circuits have all rejected a scienter requirement. The Third and Fourth Circuits require scienter, while the Second Circuit has an ambiguous standard, requiring "culpable participation" in the primary violation, that has been applied inconsistently at the District Court level. *See In Re Pub. Offering Sec. Litig.*, 2003 U.S. Dist. LEXIS 2373 at *393 (D.N.Y. Feb. 19, 2003) (citations omitted).

are we making the broker-dealer the "insurer" of its representatives . . . . The "controlling person" can avoid liability if she acted in good faith and did not directly or indirectly induce the violations."). To establish good faith, Yankee and Kresge must show that they properly supervised the brokers, which can be accomplished by demonstrating that they "maintained and enforced a reasonable and proper system of supervision and internal controls." *First Jersey*, 101 F.3d at 1473 (citation omitted). As will be explained in greater detail below, Yankee and Kresge cannot prove proper supervision. Thus, the Extended Hearing Panel concludes Yankee and Kresge are liable, under Exchange Act § 20(a), for the fraudulent and unsuitable sales practices of the Yankee brokers.

B. Supervisory Deficiencies

The Second Cause of the Complaint alleges that Yankee, Kresge, and Korwasky failed to supervise, and failed to establish a supervisory system and written supervisory procedures.[18] The Extended Hearing Panel finds that Yankee, through Kresge, failed adequately to supervise the Melville and Brooklyn offices because Kresge failed to (1) take action and implement procedures that would detect and deter violations of the securities laws, such as investigating the backgrounds of potential employees, properly training supervisors, and reviewing the performance of those supervisors; and (2) monitor, review, and investigate red flags clearly indicating that fraudulent sales practices and unsuitable trades were occurring in the Brooklyn office.

[18] NASD Conduct Rule 3010(a) requires each member to establish and maintain a system to supervise the activities of each representative and associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with NASD Rules. The standard of reasonableness depends upon the facts of the case at issue. *See La Jolla Capital Corp.*, Exchange Act Release No. 41,755, 1999 SEC LEXIS 1642, at *13 (Aug. 18, 1999).

While the Extended Hearing Panel finds that Yankee did have written supervisory procedures at all times, it also finds that those procedures were not distributed to personnel in the Brooklyn office. There is no evidence[19] in the record, nor is there any argument in the briefs, that specifically identifies any particular inadequacy in any version of the written supervisory procedures themselves.[20]

Finally, the Extended Hearing Panel finds that, in his brief six-month tenure at Yankee, Korwasky acted reasonably to detect and deter violations of the securities laws at Yankee and its branch offices. He was faced with overwhelming compliance problems at the outset of his employment, and was not given adequate resources or back-up to solve those problems or to ensure complete compliance with securities laws and regulations.

1. Failure to Maintain an Adequate Supervisory System

Yankee's business primarily involved municipal bonds until it expanded in 2001 by adding two new branches, a large number of new brokers, and a new line of business - retail sales, concentrated in speculative OTCBB stocks. However, Kresge viewed the Brooklyn office as an independent, self-monitoring entity and, accordingly, did not devise an adequate plan for, nor take action to insure, oversight of that office. Specifically, Yankee and Kresge (1) failed to designate the Brooklyn office as an "Office of Supervisory Jurisdiction," as required under Rule 3010(a)(3); (2) did not use reasonable efforts to ensure that the Brooklyn office had a supervisor with sufficient

[19] The Extended Hearing Panel gives no credence to Kresge's criticisms, expressed in his on-the-record testimony, of Korwasky's draft written supervisory procedures. It is obvious that, until sometime after that testimony, Kresge was taken in by Gliwa's attempts to impugn Korwasky's character and performance.
[20] Although on brief Market Regulation alleges that (1) Yankee and Kresge did not designate a principal to be responsible for each type of business that the firm conducts; and (2) each of Yankee's registered brokers was not assigned to an immediate supervisor, those allegations are not supported by any evidence.

experience and training, as required under Rule 3010(a)(6); and (3) did not adequately investigate the backgrounds of the brokers hired to work in the Brooklyn office.

Giordano was the supervisor of the Brooklyn office. His duties included review and approval of new customer accounts and customer orders in that office − activities that required the office to be designated, under Rule 3010(g)(1), as an Office of Supervisory Jurisdiction. Kresge never made such a designation.

Rule 3010(a)(6) requires that members make reasonable efforts to ensure that "all supervisory personnel are qualified by virtue of experience or training to carry out their assigned responsibilities." Kresge hired Giordano, on Ferragamo's recommendation, to oversee a new office, with new brokers for a line of business new to Kresge, although Giordano had no prior experience or training for the position. Giordano had an established pattern of frequently changing firms throughout his career as a broker, and he had only passed his Series 24 exam six months before joining Yankee. Kresge gave Giordano no guidance, formal training, or written supervisory procedures to qualify Giordano to oversee the brokers, make suitability determinations, and manage the daily operations in Brooklyn. Moreover, Kresge failed completely to monitor Giordano's supervisory performance after he was hired.

NASD Conduct Rule 3010(e) states that every firm has "the responsibility and duty to ascertain by investigation the good character, business repute, qualifications, and experience" of an applicant for registration prior to making such application. At a minimum, a firm must review an applicant's CRD history and Forms U-4 and U-5, and contact previous employers. Where a registered representative has a history of

arbitrations or of changing securities firms frequently, the hiring firm should consider heightened supervision for that representative.[21]

Kresge reviewed CRD records, but only for disciplinary disclosures. He reviewed the Taping Rule list, but only to determine whether a new broker's prior firm appeared on it. He made no additional phone calls to ask if brokers had regulatory or compliance issues at prior firms, did not inquire about the brokers' training or experience, and never asked about pending or reported arbitrations involving the brokers. Moreover, Kresge failed to interview Dugo at all, and did not ask him about a CRD disclosure of which Kresge had knowledge. Accordingly, Kresge's level of due diligence fell far short of the requirements of NASD Conduct Rule 3010(e).

2. Failure to Monitor, Review, and Investigate Red Flags

As Yankee's President, Kresge had a duty not only to provide a meaningful supervisory structure, but also to actively monitor and enforce it. *In re Signal Securities, Inc.,* Admin. Proc. File No. 10,304, 2000 SEC LEXIS 2030, at *22 (Sept. 26, 2000) (citations omitted). The president of a member firm "is responsible for compliance with all of the requirements imposed on his firm unless and until he reasonably delegates particular functions to another person in that firm, and neither knows nor has reason to know that such person's performance is deficient."[22] Because Kresge knew of Gliwa's supervisory deficiencies, his continued delegation to him of supervisory authority was not reasonable. His complete delegation of compliance authority to Korwasky was not reasonable, given the magnitude of the task Korwasky faced, the limited tools he had at his disposal to remedy compliance deficiencies, and the short time he was employed by

[21] *See,* NTM 97-19, at 157.
[22] *In re William H. Gerhauser, Sr.*, Exchange Act Release No. 40,639, 1998 SEC LEXIS 2402, at **17-18 (Nov. 4, 1998).

the firm. Kresge failed to maintain an adequate supervisory system because he failed to properly equip Korwasky for his tasks, and failed to follow up on Korwasky's warnings about Ferragamo's registration and the need for heightened supervision and taping in the Brooklyn office.

As the SEC has clearly stated, "[r]ed flags and suggestions of irregularities demand inquiry as well as adequate follow-up and review. When indications of impropriety reach the attention of those in authority, they must act decisively to detect and prevent violations of the federal securities laws." *In re Kantor*, Exchange Act Release No. 32,341, 1993 SEC LEXIS 1240, at *16 (May 20, 1993). A failure to supervise also occurs when "red flags" are evident and are ignored, undetected, or fail to cause reasonable concern. *In re Consolidated Investment Services, Inc.*, Admin. Proc. File No. 3-8312, 1994 SEC LEXIS 4045, at **26-27 (Dec. 12, 1994). As supervisors spot red flags, they have a duty, under NASD Conduct Rule 3010, to follow up and investigate the detected irregularities. *See In re Levitov*, No. CAF97001, 2000 NASD Discip. LEXIS 12, at **26-27 (NAC June 28, 2000) (finding supervisory violation when respondent failed to investigate red flags). There is a heightened standard of supervision when a firm opens a new branch office and employs new personnel. *See LaJolla Capital Corp.*, 1998 NASD Discip. LEXIS 26, at **14-19 (NAC Feb. 27, 1998). Furthermore, a failure to "adequately maintain and enforce supervisory procedures" is also a violation of NASD Conduct Rule 2110. *See Dist. Bus. Conduct Comm.* v. *A.S. Goldmen & Co.*, No. C10960208, 1999 NASD Discip. LEXIS 18, at **44-45 (NAC May 14, 1999).

Kresge had reason to perform extensive due diligence from the very outset of the proposal to open an office in Brooklyn. He did not know Masone, who approached him

with the unsolicited proposal to open a new branch office with a new line of business, staffed by a group of disgruntled brokers who were leaving their firm. He did know that Masone was often in the Melville office, with access to telephones and computers, although he was unregistered. He was never sure how Ferragamo would finance that office or be compensated for its operation. He knew that Ferragamo resisted being registered with Yankee, even though Ferragamo owned and financed the operation, and he eventually knew that Ferragamo did not want to become registered because he was attempting to duck an arbitration proceeding in which he was a respondent.

At the hearing, Kresge acknowledged that a broker who had changed firms frequently in a relatively short period of time was a "red flag" of a potential compliance issue. Nonetheless, Kresge hired several brokers, each of whom had a history of job hopping; yet he failed to implement any form of heightened supervision for those individuals as a condition of their employment.

Kresge also knew that the brokers who were brought in to form the Brooklyn branch were more aggressive than those he had hired in the past. Yet he failed to monitor them, even though he knew that they were selling low-priced securities, at times in large quantities, and that both Steltz and Korwasky warned him that the office needed to be closely monitored, including the brokers' telephone calls. He also knew, or should have known, that Ferragamo was directing trades through the brokers in Brooklyn.

As the compliance officer of the firm, Kresge failed to monitor activities after he delegated a majority of his supervisory duties to other people. Gliwa, who received no formal supervisory instructions or training, was overloaded with his other duties and responsibilities, and rarely visited the Brooklyn office. His only concern there was

whether customers had sufficient funds to cover trades. Kresge was aware that Gliwa was devoting little, if any, time or attention to his supervisory duties; however, he did nothing to remedy Gliwa's deficient supervision. Accordingly, Yankee and Kresge violated NASD Conduct Rules 3010 and 2110, as alleged in Cause Two of the Complaint.

C. Failure to Report Customer Complaints

The third cause of the Complaint alleges that Yankee, Kresge, and Korwasky failed to report to NASD written customer complaints received by the Firm, in violation of Conduct Rules 2110 and 3070(c). As the firm's president and while he was also the compliance officer, Kresge was responsible for ensuring compliance with Rule 3070, which requires NASD members to file quarterly reports with NASD disclosing all customer complaints received by the member. Kresge was directly responsible for performing that task as the compliance officer for the last quarter of 2001 and the second quarter of 2002. As the compliance officer, it was Korwasky's responsibility for only the first quarter of 2002.

Customer complaints were handled sporadically, inconsistently and inappropriately at Yankee. As a result, 18 customer complaints during the last quarter of 2001 and the first and second quarters of 2002 went unreported. Accordingly, by failing to report those complaints, Yankee and Kresge violated NASD Conduct rules 3070(c) and 2110.

As the chief compliance officer, Korwasky was responsible for reporting all customer complaints. However the evidence is clear that, although customer complaints were to be handled by the chief compliance officer, a number of those complaints were

being held in the Brooklyn office and were not sent to Korwasky. The Complaint alleges that he failed to report three customer complaints, but the evidence shows that he received only one.[23] Rule 3070(c) contains no exceptions for reporting customer complaints. Accordingly, by failing to report a single complaint, Korwasky violated Rules 3070(c) and 2110.

D. Failure to Register Ferragamo

The fourth cause of the Complaint alleges Yankee, Kresge, and Korwasky failed to register Ferragamo, in violation of NASD Registration Rules 1021 and 1031, Conduct Rule 2110, IM-1000-1, and IM-1000-3. NASD Membership and Registration IM-1000-3 states:

> [t]he failure of any member to register an employee, who should be so registered, as a Registered Representative may be deemed to be conduct inconsistent with just and equitable principles of trade and when discovered may be sufficient cause for appropriate disciplinary action.

NASD Registration Rule 1021 requires all principals to be registered, and defines "principals" as those sole proprietors, officers, partners, managers of Offices of Supervisory Jurisdiction, and directors of corporations:

> who are actively engaged in the management of the member's investment banking or securities business, including supervision, solicitation, conduct of business, or the training of persons associated with a member for any of these functions.

NASD Registration Rule 1031 is similarly worded and requires all representatives to be registered. The Rule defines "representatives" as:

> [p]ersons associated with a member, including assistant officers other than principals, who are engaged in the investment banking or securities business for the member

[23] The particular complaint was not identified on the record.

> including the functions of supervision, solicitation or conduct of business in securities or who are engaged in the training of persons associated with a member for any of these functions.

From the moment Yankee established the Brooklyn office, Ferragamo owned, financed, and operated it.[24] He was involved in decision-making for that office, including selection of a branch manager and brokers, and maintained a very active presence. Ferragamo was, therefore, required to be, but was not in fact, registered as a representative and as a principal of the Firm.

As President of Yankee, Kresge had an obligation to ensure that the Firm complied with all registration requirements. Kresge was aware of Ferragamo's financial involvement in the Brooklyn office, and, because he reviewed tickets for certain large orders, he should have known that Ferragamo was directing trades in SSTF, WMGC, and GCHR. Furthermore, Korwasky warned Kresge that Ferragamo should not be involved at all with the Brooklyn office while he was unregistered. By failing to register Ferragamo, Yankee and Kresge violated NASD Registration Rules 1021 and 1031, Conduct Rule 2110,[25] IM-1000-1, and IM-1000-3.

The Extended Hearing Panel finds that Korwasky is not liable for failing to register Ferragamo. It was not until late February 2002, that Korwasky was introduced to

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[24] Paying for even minimal firm expenses is a factor to be considered when deciding whether a person should be registered. *See, e.g., Vladislav Steven Zubkis*, Exchange Act Release No. 40,409, 1998 SEC LEXIS 1904 (Sept. 8, 1998) (finding that individual was engaged in the firm's securities business after considering such things as payment of rent and phone bills, compensating brokers); *Gerald M. Greenberg*, Exchange Act Release No. 6,320, 1960 SEC LEXIS 339, at **13-14 (July 21, 1960) (establishing that even paying for minimal telephone expenses should be considered when deciding whether someone is associated with a firm).

[25] IM-1000-1 provides that it is a violation of Conduct Rule 2110 to file information with respect to membership or registration that is inaccurate or so incomplete as to be misleading. The Firm's 2002 Form BD was inaccurate and misleading in that it failed to identify Ferragamo as owning, financing, and operating the Brooklyn office. *See also William S. Mentis*, Exchange Act Release No. 37,952, 1996 SEC LEXIS 3192 at *5 (Nov. 15, 1996).

Ferragamo. Shortly thereafter, Korwasky warned Kresge about Ferragamo's lack of registration, telling Kresge that Ferragamo should not be involved with the Firm. During the remaining three months of his employment at Yankee, Korwasky was unable to convince Kresge to register Ferragamo or end his association with Yankee.

Sanctions

For intentional or reckless misrepresentations and omissions of material facts, the NASD Sanction Guidelines recommend a fine of $10,000 to $100,000, and a suspension in any or all capacities for a period of ten business days to two years. In egregious cases, barring an individual or expelling a firm should be considered.[26] The Guidelines do not include specific principal considerations for those violations; rather, they direct attention to the general Principal Considerations for Determining Sanctions.[27]

For unsuitable recommendations, the Sanction Guidelines recommend a fine of $2,500 to $75,000, and a suspension an individual in any or all capacities for 10 business days to one year. In egregious cases, adjudicators should consider a longer suspension of up to two years or a bar for an individual, and a suspension of a firm for up two years.[28] Again, adjudicators are to apply the Principle Considerations, as appropriate.

For failure to supervise, the Sanction Guidelines recommend a fine of $5,000 to $50,000, and, in egregious cases, a suspension of the firm for up to 30 business days; for the responsible individual, a suspension for up to two years or a bar.[29] In cases involving systemic supervision failures, the firm may be suspended for up to two years, or

[26] NASD SANCTION GUIDELINES, at 94 (2004 ed.).
[27] *Id.* at 89.
[28] *Id.* at 97.
[29] *Id*. at 105.

expelled.[30] The Guidelines provide three additional factors to consider in cases involving supervisory deficiencies: (1) whether respondent ignored "red flag" warnings; (2) the "[n]ature, extent, size, and character of the underlying misconduct"; and (3) the "[q]uality and degree of [the] supervisor's implementation of the firm's supervisory procedures and controls."[31]

The Guideline for failing to disclose reportable events recommends a fine of $5,000 to $100,000 and a suspension of the responsible principal for 10 to 30 business days or, in egregious cases, a suspension of the responsible principal for up to two years or a bar in all supervisory capacities.[32] In addition, the Guideline recommends that the firm be suspended in any or all capacities until the deficiency is corrected.[33]

For registration violations, the NASD Sanction Guidelines recommend a fine of $2,500 to $50,000, and, in the case of an individual, consideration of a suspension for up to six months, or for a firm, a suspension of up to 30 business days.[34] Additionally, adjudicators should consider the nature and extent of the unregistered person's responsibilities at the firm, and whether a registration application had been filed for the individual.[35]

Violations by Yankee and Kresge

The violations by Yankee and Kresge all arise out of a common underlying cause − Kresge's decision to expand Yankee's business into an area of the securities industry with which he was unfamiliar, and to do so by adding an "independent" branch

[30] *Id*.
[31] *Id.* at 105.
[32] *Id.* at 80.
[33] *Id.*
[34] *Id.* at 50. In egregious cases, the recommendation is a suspension for up to 30 business days for the firm, and for the individual, a suspension of up to two years or a bar.
[35] *Id.*

office, financed by an individual who refused to become registered, staffed by brokers with questionable backgrounds in the industry, and over which he did not exercise reasonable supervisory oversight. Accordingly, the Extended Hearing Panel aggregates the misconduct for purposes of imposing severe sanctions. *See DOE v. J. Alexander Securities, Inc., et al.*, No. CAF010021, 2004 NASD Discip. LEXIS 16, at *69 (NAC Aug. 16, 2004).

The fraudulent sales practices and unsuitable recommendations were frequent, numerous, and egregious. They occurred over a period of months, and the ten customers who testified at the hearing lost almost $3.9 million of their invested funds. Kresge's due diligence in investigating the backgrounds of Ferragamo and the brokers in the new Brooklyn office was minimal and grossly insufficient. His oversight of the Brooklyn office, in the face of numerous red flags and the lack of training and direction given to supervisors below him, was not only insufficient, but his indifference to every aspect of its operation except its financial success was reckless and failed to prevent injury to the investing public. Accordingly, the Extended Hearing Panel concludes that Yankee should be expelled, and that Kresge should be barred as a principal and in any supervisory capacity. In addition, Yankee and Kresge will be ordered to pay restitution in the total amount of $3,866,426, plus interest, to the ten customers who are identified in the Addendum to this Decision. Yankee and Kresge will also be assessed costs of $7,820.22, consisting of an administrative fee of $750 and a transcript fee of $7,070.22.

The Violation by Korwasky

Korwasky was employed at Yankee for only six months, and was the designated compliance officer for only four and one-half months. Immediately, he was faced with a

myriad of compliance issues that needed resolution, and he advised Kresge of 33 of those issues. He soon warned Kresge about Ferragamo, the activities of the brokers in Brooklyn, and the existence of the Staten Island executive suite. When he realized that he was not being given adequate resources or back-up by Kresge, he resigned from the firm.

He was responsible for reporting customer complaints, but he received actual knowledge of only one of them, although all complaints were supposed to be sent to him. The evidence does not demonstrate that his failure to report that one complaint, under the circumstances of his employment, was an attempt to conceal it from NASD, rather than a mere oversight, attributable to his attempts to deal with the firm's overwhelming compliance problems. There is no evidence that he was aware that other complaints were not being sent to him. Under the circumstances, the Extended Hearing Panel concludes that a Letter of Caution will satisfy NASD's remedial goals.

Conclusion

For (1) the fraudulent sales practices and unsuitable recommendations of the Firm's registered representatives, in violation of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, and NASD Conduct Rules 2110, 2120, 2310, and IM-2310-2; (2) the failure to supervise the sales activities and conduct of its brokers and unregistered individuals, in violation of NASD Conduct Rules 2110 and 3010; (3) the failure to report customer complaints, in violation of NASD Conduct Rules 2110 and 3070(c); and (4) the failure to register a person who was acting in capacities that required

his registration, in violation of NASD Conduct Rule 2110 and Membership and Registration Rules 1021(a) and 1031(a), and IM-1000-1 and IM-1000-3; (1) Yankee Financial Group, Inc., is expelled from NASD membership; (2) Richard F. Kresge is barred from association with any NASD firm as a principal and in any supervisory capacity; (3) Yankee Financial Group, Inc., and Richard F. Kresge, jointly and severally, are ordered to make restitution to the following customers in the following amounts, plus interest calculated pursuant to 26 U.S.C. § 6621(2)(2),[36] from May 1, 2002, (the sales ceased at the end of April 2002) to the date of payment:

JC	$1,050,575
DW	$62,100
WB	$1,191,691
GR	$42,240
GA	$978,000
JL	$224,354
JH	$236,985
RP	$7,377
GW	$14,400
AW	$58,704;

and (4) assessed costs of $7,820.22.

For failure to file a customer complaint, in violation of NASD Conduct Rules 2110 and 3070(c), Joseph C. Korwasky is issued a Letter of Caution in the form of this Decision.

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

These sanctions shall become effective on a date determined by NASD, but not sooner than 30 days from the date this Decision becomes the final disciplinary action of NASD; except that, if this Decision becomes the final disciplinary action of NASD, the expulsion and bar shall become effective immediately.

SO ORDERED.

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Alan W. Heifetz
Hearing Officer
For the Extended Hearing Panel

Copies to:

Via Facsimile & First Class Mail
Joseph R. Benfante, Esq.
Paul J. Bazil, Esq.

Via First Class Mail & Overnight Courier
Yankee Financial Group, Inc.
Richard F. Kresge
Joseph C. Korwasky

Via Electronic & First Class Mail
Jeffrey K. Stith, Esq.
Matthew Campbell, Esq.