NASD OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. KEVIN CALANDRO (CRD No. 1459109), and JAMES W. BROWNE (CRD No. 1189996), Respondents.	Disciplinary Proceeding No. C05050015 Hearing Officer—Andrew H. Perkins **EXTENDED HEARING PANEL DECISION** August 1, 2006

The Respondents participated in private securities transactions without prior written notice to their member firm. Respondent Browne is suspended in all capacities for six months and fined $25,000, and Calandro is suspended in all capacities for three months and fined $5,000. In addition, the Respondents are ordered to pay costs.

Appearances

Sean W. Firley, Senior Regional Attorney, Boca Raton, FL, and Mark P. Dauer, Senior Counsel, New Orleans, LA (Rory C. Flynn, NASD Chief Litigation Counsel, Washington, DC, Of Counsel) for the Department of Enforcement.

E. Steve Watson, Esq., Allen, TX, for Kevin Calandro.

Christopher J. Bebel, Esq., Houston, TX, for James W. Browne.

DECISION

This case arose from an investigation of James W. Browne and Kevin Calandro's involvement with e2 Communications, Inc. ("e2" or the "Company"). NASD initiated the

investigation after it received certain documents from UBS PaineWebber, Inc. ("PaineWebber"), which showed that Browne might have participated in private securities transactions involving the sale of e2 stock.[1] PaineWebber, the Respondents' former firm, had uncovered the documents in connection with a customer arbitration brought by W.P.M. against Browne and PaineWebber, concerning W.P.M.'s investment in e2.[2] The investigation led to Calandro as well because he and Browne worked as a team on many accounts.

The Department of Enforcement ("Enforcement") charged Calandro and Browne with participation in private securities transactions ("selling away") for compensation, in violation of NASD Conduct Rules 3040 and 2110. The Complaint, as supplemented by the Bill of Particulars dated June 15, 2005, contains three causes of action. The first and third causes of the Complaint charged that Browne and Calandro solicited and participated in sales of e2 Series B Convertible Preferred Stock ("Series B Preferred Stock"). The second cause of the Complaint charged that Browne solicited and participated in customer SF's purchase of shares of e2 common stock from a private investor and shares of e2 Series C Convertible Preferred Stock ("Series C Preferred Stock") directly from e2. The Complaint further charged that the Respondents received shares of e2 common stock as "finders' fees," which constituted selling compensation under Conduct Rule 3040, and that they failed to provide written notice of the e2 transactions to their firm, as required by NASD Conduct Rule 3040.

Browne and Calandro denied the charges and requested a hearing. The Respondents denied that they solicited investors to purchase e2 stock or otherwise referred investors to e2. Further, they denied that they ever received selling compensation from e2. Browne contended that he received the e2 stock in recognition of his business advice and service as an advisor to

[1] Tr. 247. References to the hearing transcript are cited as "Tr." followed by the page number. References to the Complainant's exhibits are cited as "C" followed by the exhibit and page number, and references to the Respondents' exhibits are cited as "R" followed by the exhibit and page number.

[2] Tr. 247-48. W.P.M. was one of Browne's customers at PaineWebber.

e2's board. Browne became an advisory director on April 15, 1999.[3] Calandro, on the other hand, contended that the shares he received were a gift.

In addition, the Respondents raised a number of affirmative defenses. Among them, the Respondents argued that many of the transactions referenced in the Complaint involved purchases of e2 stock by their immediate family members, which transactions were exempt from the notice requirements of Conduct Rule 3040, and that Enforcement violated fundamental principles of fairness by relying on documents Enforcement knew were "corrupt, fabricated corporate documents."[4] Accordingly, the Respondents urged the Extended Hearing Panel to dismiss all of the charges against them.

The Panel, comprised of the Hearing Officer and two current members of the NASD District committee for District 6, held the hearing in this matter in Dallas, Texas, on January 23-27, 2006. In addition, the Panel heard the balance of one witness's testimony by telephone on February 3, 2006, and closing arguments by telephone on February 15, 2006.

For the reasons discussed below, the Panel finds that Calandro and Browne violated NASD Conduct Rules 3040 and 2110 by participating in private securities transactions without first providing appropriate written notice to their firm. For these violations, Browne is suspended in all capacities for six months and fined $25,000, and Calandro is suspended in all capacities for

[3] C 17 at 3 (Browne's response to NASD staff dated May 13, 2003). *See also* R 66 at 1 (Board of Directors Minutes). Browne was granted an option to purchase 25,000 shares of e2 common stock at this time in recognition of his services as an advisory director. *See* C 18 at 6. However, at the hearing, Browne testified that he did not become an advisory director until September 2000 when the board formalized agreements with its board members, including Browne. In connection with this process, the board again elected Browne as an advisory director and approved an Advisory Director Agreement and an Indemnification Agreement between him and the Company. *See* R 206 at 4-5, 11-16. In rejecting Browne's contention that his appointment as an advisory director was not effective until September 2000, the Panel notes that the evidence shows that Browne acted as an advisory director between April 1999 and September 2000. Indeed, Browne points to that activity to explain why e2 issued 10,177 shares of common stock in March 2000, which e2's records denoted as "finders' fees."

[4] *See* Second Affirmative Defense, Browne Ans. at 8.

three months and fined $5,000. In addition, the Respondents are ordered to pay the costs of this proceeding.

I. INTRODUCTION

This case presents an uncommon pattern of private securities transactions in connection with Browne and Calandro's efforts to obtain business from e2, an Internet start-up company founded by J.L.F., the former President and Chief Executive Officer of Saber Software Corporation.[5]

Browne and Calandro teamed up shortly after Calandro joined Kidder, Peabody & Co. ("Kidder Peabody") in 1994. J. Patrick McLochlin, their branch manager, introduced them because they both had an interest in money management through the use of portfolio tracking software.[6] Browne particularly was very knowledgeable about computers and software, and he had become an early and adept user of portfolio tracking software.[7] Under their teaming arrangement, they placed all their new customers under a joint executive account number. Browne and Calandro continued their teaming arrangement after they joined PaineWebber in January 1995.[8]

Browne and Calandro's first joint customer was J.L.F. In May 1995, Saber Software was purchased by McAfee Associates, Inc., a manufacturer and supplier of network security software. J.L.F. netted approximately $20 million from the sale, which he invested with Browne and Calandro.[9]

---

[5] R 9 at 26. Saber Software, was a developer of network systems management software. Under J.L.F.'s leadership, Sabre Software experienced fast growth between its founding in 1986 and 1994, when it had a successful initial public offering. J.L.F. was well known to the investment community in Dallas due to his success with Saber Software.

[6] Tr. 909-10.

[7] Tr. 1031-33.

[8] PaineWebber acquired Kidder Peabody in or about December 1994.

[9] Tr. 914-15.

In October 1997, J.L.F. founded e2 to develop and sell software designed to help companies sell and market their products over the Internet.[10] e2 developed a proprietary server technology that allowed companies to manage email marketing efforts based upon information provided by the customers.[11] A common example of this form of permission-based email marketing is the system Amazon.com uses to identify a customer's preferences and then market other products to the customer based on those preferences.[12]

e2 needed capital to develop and market its services. Thus, between 1998 and 2000, the Company completed four private offerings—one of common stock and three of convertible preferred stock. e2 completed the offering of common stock in May 1998.[13] Browne and Calandro purchased shares in their wives' names in this initial round of financing.[14]

e2 completed the offering for the Series A Convertible Stock in February 1999. Monarch Partners' Venture Fund I, LP, a venture capital fund co-founded by B.M.B. purchased the entire offering of 300,000 shares.[15] Browne and Calandro introduced B.M.B. to J.L.F. and were instrumental in securing his involvement with e2.[16]

---

[10] R 8 at 6.

[11] R 81 at 14. J.L.F. had formed a company called ediSys Corp. to develop software and serve as an incubator of future technology ventures. e2 was the first such venture spawned by ediSys. Tr. 917; R 9 at 9 (e2's Private Placement Memorandum, Jan. 24, 1998).

[12] *See* R 81 at 10-11.

[13] Initially, e2 Communications was closely held by a small group of founders, most of whom were friends of J.L.F. Tr. 1041; R 85 at 77.

[14] Tr. 1048-49. Browne and Calandro purchased the stock in their wives' names because they then did not need to secure PaineWebber's approval of the investments. Their branch manager testified that PaineWebber did not require compliance approval of such purchases. Tr. 155-56. On the other hand, if the broker made the purchase in his own name, he was required to submit an employee outside investment form and receive approval from the PaineWebber's compliance department before making the purchase. *See* C 13 (PaineWebber Compliance bulletin).

[15] R 81 at 55; R 85 at 80.

[16] *See* Tr. 826, 885.

In March 2000, e2 completed the Series B Preferred Stock Offering of 750,000 shares. Calandro's wife and Browne each purchased shares in this offering.[17] And, in or about November 2000, e2 completed the Series C Preferred Stock Offering of 6 million shares.[18]

Upon becoming involved with J.L.F. and e2, Browne and Calandro quickly concluded that the Company had great potential. Not only did they believe that J.L.F. had developed an innovative product, but also they believed that e2 would benefit from the hot technology market, as other Internet start-ups had. Browne pointed to a broker at PaineWebber who was reputed to have made $10 million on a $50,000 investment in an Internet start-up company.[19] Browne and Calandro believed that e2 might go public in the near future. If it did, they wanted to be in on the ground floor. Indeed, Calandro viewed this as a life-changing prospect.[20] He reasoned that not only would Browne and he be entitled to a percentage of the investment banking fee PaineWebber stood to earn, but they also would have the chance of securing all of the insiders' accounts.[21] Consequently, Browne and Calandro put a considerable amount of effort into assisting e2 to secure customers, investors, advisors, and business partners.[22] As discussed below, some of these activities constituted participation in private securities transactions involving the purchase of e2 stock by the Respondents' family members, friends, and business associates.

[17] R 85 at 81.

[18] R 85 (Stock Purchase Agreement dated Nov. 15, 2000).

[19] Tr. 84, 209-10.

[20] Tr. 956-57.

[21] Tr. 956.

[22] *See* Tr. 1079.

II. FINDINGS OF FACT

A. Respondent Browne

Browne entered the securities industry in 1983 shortly after graduating from Southern Methodist University. He first worked at E.F. Hutton & Company, Inc. and then joined Bear, Stearns & Co., Inc. ("Bear Stearns"), where his father also was a broker. Browne left Bear Stearns in 1987 and joined Kidder Peabody.

When PaineWebber acquired Kidder Peabody, Browne and Calandro were assigned to separate offices. Because Browne was one of the highest grossing brokers in Kidder Peabody's Dallas branch office, he and a handful of other top producers were invited to move to PaineWebber's Sherry Lane office that was managed by Philip C. Eldemire, while Calandro was assigned to PaineWebber's downtown office.[23] Despite their physical separation, Browne and Calandro continued their team approach to asset management, and, significantly, they continued working jointly on the J.L.F. account.

In early 1999, Lehman Brothers, Inc. ("Lehman") began recruiting Browne to join Lehman's Dallas office.[24] In September 2000, Browne accepted Lehman's offer. Browne was associated with Lehman until he was terminated in August 2003 after Lehman determined that he had participated in private securities transactions related to e2.

Browne is currently registered as a General Securities Representative with Marymont Partners, Inc., an NASD member firm. Browne has no disciplinary record.

1. Respondent Calandro

Calandro graduated from Michigan State University in 1985 with a Bachelor of Science in Mechanical Engineering. After college, he worked briefly for an electronics manufacturing

[23] Tr. 914. Calandro eventually was permitted to transfer to PaineWebber's Sherry Lane office where Browne worked.

[24] R 162.

firm in Dallas before joining Smith Barney. In early 1994, Calandro joined Kidder Peabody as a General Securities Representative where he met Browne. Calandro followed Browne to PaineWebber and then on to Lehman Brothers. Calandro, however, left Lehman in October 2002 to take a position with Sanders Morris Harris where he is currently registered as a General Securities Representative. Calandro has no disciplinary record.

2. Browne's and Calandro's Involvement with e2

To increase the chances that e2 would place its investment banking business with PaineWebber, Browne and Calandro worked hard to attract customers, investors, advisors, and business partners to e2. Browne and Calandro were quite successful on all fronts. For example, one of the first people Browne recruited was I.B., who became a valuable resource for e2.[25] I.B. was recognized by many in the high technology industry as a leader in technology and marketing.[26] He had 15 or more years experience with high technology companies, and at the time was in senior management at IBM where he was responsible for IBM's worldwide business partnering and marketing.[27] In that position, I.B. had considerable influence over IBM's decisions to invest in technology companies such as e2, and he proved to be instrumental in e2's securing a joint marketing relationship with IBM.[28] In addition, I.B. invested in e2 and served first as an advisory director and later as a full director.[29] As a director, I.B. provided advice to e2 on its technology and the potential of its technology in various marketplaces, and he referred investors, customers, and some of his former senior employees to e2.[30]

[25] Tr. 458-59.

[26] Tr. 1037.

[27] Tr. 458-59.

[28] Tr. 460-61, 469-73.

[29] I.B. was elected as a full director on October 23, 2000. R 187 at 36.

[30] Tr. 461.

Calandro recruited B.M.B. and introduced him to J.L.F. and I.B.[31] Calandro knew B.M.B. because his wife and B.M.B.'s wife had been friends since they met in college.[32] B.M.B. was important to e2 because of his access to venture capital financing. B.M.B. also had significant experience with new technology companies, including the successful initial public offering in June 1998 for his own company, Inktomi Corporation, which had developed an Internet search engine. In addition, B.M.B. was an important financial resource. He knew many venture capitalists in Silicon Valley, who were important sources of capital for companies at e2's stage of development. B.M.B. also joined e2's board.

The evidence shows that Eldemire and other managers at PaineWebber were aware of Browne and Calandro's efforts. Browne and Calandro openly solicited e2's business. For example, they arranged the initial meeting among J.L.F., I.B., B.M.B., and B.G.[33] at PaineWebber's hospitality tent at the Byron Nelson Golf Classic in May 1998.[34] Moreover, in August 1999, Browne told Eldemire that he was working with PaineWebber's investment bankers to secure e2's business.[35] Eldemire cautioned Browne that he could not do private placements without PaineWebber's approval.[36]

Browne and Calandro also invested personally in e2. In June 1998, Browne invested $50,000, and Calandro invested $15,187.50.[37] And, in January 1999, Browne invested an additional $50,000.[38] Browne and Calandro made these investments in their wives' names to

---

[31] Tr. 826-28.

[32] Tr. 826, 885.

[33] B.G. was another person Browne and Calandro referred to e2. Browne claimed that B.G. was the largest distributor of Hewlett Packard computer equipment in the Southwest.

[34] Tr. 919; C 18 at 4. The Byron Nelson Golf Classic is a golf tournament on the PGA Tour. The tournament is held each May at the Four Seasons Resort and Club in Irving, Texas, a suburb of Dallas.

[35] Tr. 55; C 7 at 12.

[36] C 7 at 12.

[37] R 85 at 78.

[38] *Id.*

avoid compliance review and restrictions by PaineWebber.[39] Eldemire explained to Browne that PaineWebber would not permit him to manage any e2 accounts if he was an e2 stockholder. But, if he made the investment in his wife's name, the restriction would not apply. Eldemire pointed out that he made investments in his wife's name for that reason. Thus, although Browne had received written authorization from PaineWebber's compliance department to make the initial $50,000 purchase of e2 stock in his own name,[40] Browne decided to follow Eldemire's advice and make the investment in his wife's name so that he could continue to manage J.L.F.'s accounts.[41]

3. Browne's Role as an Advisory Director

Browne became even further involved with e2 when, on April 15, 1999, he became an advisory director. Browne assumed this role without PaineWebber's approval in contravention of PaineWebber's written supervisory procedures.[42] Browne did not seek PaineWebber's approval until the fall of 1999.[43] When Browne finally approached Eldemire for approval, Eldemire informed Browne that he needed to submit a written request and obtain written approval from PaineWebber's compliance department before he assumed the position of an advisory director.[44] Browne did not disclose that he had been serving as an advisory director for the prior seven months.

Browne submitted the necessary form to Eldemire on November 8, 1999. In addition to other representations, Browne affirmed that he would not receive any fees from e2 for his service

---

[39] PaineWebber did not require compliance approval of such purchases. Tr. 155-56.

[40] PaineWebber approved Browne's request (C 11 at 1) on June 1, 1998, and sent Browne an interoffice memorandum dated June 5, 1998, which set forth the conditions attached to the approval. C 11 at 2.

[41] C 7 at 13 (notes of meeting); Tr. 50. However, Browne's father and brother invested.

[42] *See* C 33.

[43] Tr. 57.

[44] C 14.

as an advisory director.[45] PaineWebber approved Browne's request on December 7, 1999.[46] The approval contained a number of restrictions, including a prohibition against his discussing the merits of e2 with any PaineWebber client or financial advisor. Importantly, PaineWebber required Browne to update the representations in the approval request if "the scope of his duties, responsibilities, involvement, or compensation change other than nominally."[47]

Browne's role as an advisory director ended in about January 2002 when e2's employees forced e2 into bankruptcy. Despite e2's early market success, by 2001, the company was experiencing financial difficulties and the board began to fractionalize over the best course of action. Some board members favored cost cutting measures, while others disagreed as to the amount and extent. Eventually a consensus began to develop that the company either needed to liquidate or receive an infusion of capital from some other outside source.

Various disputes emerged between J.L.F. on the one hand and the other directors and shareholders on the other, which culminated in a failed effort in April 2001 to remove J.L.F. as President.[48] Browne sided with the opposition group and helped the outside board members retain a law firm to advise them.[49] Finally, in January 2002, the employees filed an involuntary petition against e2 in the United States Bankruptcy Court for the Northern District of Texas under Chapter 11 of the Bankruptcy Code.[50] Later, e2 entered into a voluntary petition under Chapter 7 of the Bankruptcy Code and sold its assets to another company.

---

[45] *Id.*

[46] C 15.

[47] *Id.*

[48] The outside directors had concluded that J.L.F. should be removed for alleged financial improprieties and mismanagement of the company. C 17 at 1.

[49] Tr. 854-55.

[50] Tr. 571.

In the course of the bankruptcy proceedings, Browne hired an attorney and formed a litigation trust to pursue claims on behalf of e2's stockholders against J.L.F. and other former directors and officers of e2.[51] Browne was the principal proponent of the plan. He paid a substantial portion of the initial retainer to bankruptcy counsel, marshaled documents, edited various pleadings, and attended all of the bankruptcy court hearings.[52]

The Shareholder Trust was successful; the participating shareholders recovered more than their initial investments.[53] J.L.F., on the other hand, lost his claims to the Company's assets.[54] Although Browne and J.L.F. had become good friends,[55] Browne's opposition to J.L.F. in his struggle to retain control of e2 alienated the two. Browne points to J.L.F.'s resulting animosity to support Browne's theory that J.L.F. fabricated some of the documentary evidence relied upon by Enforcement in this proceeding, including the list of the subscribers to the Series B Preferred Stock Offering dated March 2, 2000 (the "Series B Subscription List") that is attached as Exhibit A to the Complaint.[56]

B. Browne and Calandro's Participation in the Series B Preferred Stock Offering

Enforcement charged that Browne and Calandro participated in the Series B Preferred Stock Offering by referring and soliciting the investors attributed to them on the Series B Subscription List.[57] Enforcement further charged that Browne and Calandro each received shares of e2 common stock in payment of "finders' fees" due them for their participation in securing

[51] Tr. 572, 575.

[52] Tr. 573.

[53] Tr. 607. Browne did not participate in the recovery.

[54] Tr. 1160.

[55] Tr. 915.

[56] The list is Exhibit C 7 at 18.

[57] Bill of Particulars ¶¶ 3, 10.

those investors. Because Enforcement principally relied upon the Series B Subscription List,[58] the Panel began its analysis with that document.

1. The Series B Subscription List

Enforcement contended that e2 paid Browne and Calandro finders' fees for their assistance in securing some of the investors listed on the Series B Subscription List, which is attached as Exhibit A to the Complaint.[59] Opposite the name of each investor on the Series B Subscription List there are three categories of information: (1) "Amount"; (2) "Shares"; and (3) "Source." The Department assumed that the source column references the name of the person responsible for obtaining the corresponding investor.[60] In addition, the Series B Subscription List contains a calculation of the "Shares Due" Browne and Calandro.[61] The calculation matches the number of shares e2 paid to Browne and Calandro. Enforcement argued that this document alone was sufficient to establish that Browne and Calandro participated in the securities transactions for which they are designated as the "source."

Although the Series B Subscription List appeared to corroborate other evidence in the record, the Panel found that the list was not reliable. The Series B Subscription List was not an e2 corporate record, and none of the Parties presented credible evidence of the document's origin.[62] Enforcement contended that Browne created the list to bolster Browne's and Calandro's claims to finders' fees due them for their participation in the Series B Preferred Stock Offering.[63] Enforcement based its argument on B.M.B.'s letter of March 6, 2003, which he wrote to

---

[58] Indeed, Enforcement's central theory was that the receipt of the finders' fees reflected on the Series B Subscription List "in itself constitute[d] participation in the [private securities] transactions." Tr. 18.

[59] C 7 at 18.

[60] The Department presented no evidence to support their assumption or to explain how each investor was paired with a "source." In Browne's case, the "Source" reference is "Wade," which is Browne's middle name.

[61] In addition, the list contains a calculation of shares due other "sources."

[62] R 245.

[63] C 7 at 17.

Browne's and PaineWebber's attorney in the W.P.M. arbitration to clarify e2's issuance of 10,177 shares of e2 common stock to Browne's wife.[64]

In the letter, B.M.B. stated that Browne had come to him on an unspecified date with two spreadsheets that he attached to the letter, "one created by [J.L.F.] another one from [Browne]."[65] One was the Series B Subscription List and the other was a fairly similar list. B.M.B. testified that he had not seen either spreadsheet before Browne produced them when they met regarding the letter Browne had requested, but B.M.B. "surmised" that J.L.F. created both because Browne did not have access to the information reflected on the two spreadsheets.[66] B.M.B. further testified that he had not meant to imply by his letter that Browne had created the Series B Subscription List. However, B.M.B. could not explain his statement in the letter that one of the spreadsheets was "from [Browne]." B.M.B. testified that the confusion might have resulted because he wrote the letter in haste and he referenced events in the same paragraph that actually had occurred several years apart.[67] The Series B Subscription List attributed more investors to Browne and Calandro than the other. The Department therefore assumed that Browne created the Series B Subscription List.

Browne on the other hand asserted that J.L.F. created the Series B Subscription List to help his friend W.P.M. win his arbitration claim against Browne and PaineWebber. But Browne did not present evidence to show how the document had been used or to explain how it would have helped W.P.M. in the arbitration. The Panel found this omission significant because, as a party to the arbitration, Browne was privy to the information needed to answer these questions.

[64] Tr. 16-17; C 7 at 15.

[65] C 7 at 16.

[66] Tr. 839-40.

[67] Tr. 844.

The Panel concluded that it could not determine the circumstances surrounding the creation of the Series B Subscription List. The Panel doubts that Browne created the list because there would have been no reason for him to have created a comprehensive list that showed finders' fees due other persons. It is more likely that J.L.F. or e2's Chief Financial Officer prepared the list to work out the calculations of all finders' fees paid on the Series B Preferred Stock Offering. But, even if that were true, there were unresolved questions regarding the probative value of the Series B Subscription List to prove that Browne and Calandro "participated" in the transactions for which they were designated as the source.

Browne and Calandro did not know, or have any ties to, some of the investors attributed to them. Thus, while there may have been a valid business reason for e2 to have credited those transactions to the Respondents, there is no evidence that the standard employed in devising the list corresponds to the definition of private securities transactions in NASD Conduct Rule 3040. J.L.F. or others at e2 might well have credited the Respondents with those transactions even though they had not "participated" in the transactions.

In sum, considering all of the evidence, the Panel concluded that the Series B Subscription List was unreliable. Accordingly, the Panel gave it no weight. Nonetheless, the Panel concluded that there was sufficient other evidence to establish that Browne and Calandro participated in private securities transactions involving the sale of e2 stock.

2. Browne's Participation in Sales of Series B Preferred Stock

Browne admitted that he referred a number of investors to e2. On September 26, 2003, Browne sent NASD staff a written response to the staff's written request for information dated September 5, 2003.[68] In his response, Browne admitted that he referred five family members and four other investors to e2. Of the family members Browne listed, e2's corporate records show that his father, R.A.B., purchased 5000 shares for $35,000 and that his father-in-law, S.C.F.,

[68] C 18 at 2.

purchased 3000 shares for $21,000.[69] The remaining family members Browne listed, including his wife, are not shown on e2's records as purchasers of Series B Preferred Stock.

The four non-family investors Browne listed are I.B., M.H.K., W.G.V., and S.K.S.[70] As to them, e2's corporate records show that I.B. purchased 7143 shares for $50,001, M.H. K. purchased 3500 shares for $24,500, W.G.V. purchased 3000 shares for $21,000, and S.K.S. purchased 7000 shares for $49,000.[71] At the hearing Browne testified that, with the exception of S.K.S., he had referred each of the foregoing investors to e2.[72] With regard to S.K.S., Browne admitted that he requested e2 to contact S.K.S. after Browne's father told her about the Company.[73]

In addition, Browne admitted that he was involved with introducing D.B., B.G., and J.R.C. to e2.[74] B.G. purchased 14,286 shares of Series B Preferred Stock for $100,002, and J.R.C. purchased 7000 shares for $49,000.[75] Browne also disclosed that either he or Calandro told J.L.F. to contact B.C.M. about purchasing shares of Series B Preferred Stock.[76] And, according to e2's records, B.C.M. thereafter purchased 7000 shares for $49,000.[77] Based on Browne's admissions, the Panel concluded that he participated in the foregoing transactions.

---

[69] R 85 at 81.

[70] C 18 at 2.

[71] R 85 at 81-82.

[72] *See also* Tr. 1188-89.

[73] C 18 at 4.

[74] C 18 at 4. J.R.C. was Browne's friend and neighbor.

[75] R 85 at 81.

[76] C 18 at 4.

[77] R 85 at 81.

3. Calandro's Participation in Sales of Series B Preferred Stock

Calandro also admitted to participating in sales of Series B Preferred Stock. Calandro admitted that he talked to his brother, stepfather, and brother-in-law about e2 and its capital needs.[78] Indeed, Calandro admitted that his stepfather learned about e2 from Calandro and that he introduced his stepfather to J.L.F. at PaineWebber's offices.[79] Calandro also admitted in an on-the-record interview that he gave his brother-in-law's name to J.L.F.[80] Each of these family members eventually purchased shares of e2 Series B Preferred Stock through family trusts. The Calandro Living Trust maintained by his brother purchased 8500 shares for $59,500.[81] The L.E.C. Living Trust maintained by Calandro's stepfather purchased 2000 shares for $14,000.[82] And the R.M.C. Living Trust purchased 29,143 shares for $204,001.[83]

In addition to the foregoing family members, Calandro admitted that he referred two of his friends and clients to e2. The first, A.L., was Calandro's best friend in high school and his college roommate.[84] A.L. maintained a securities account with Calandro at PaineWebber in which he invested heavily in technology companies, including speculative issues.[85] Calandro testified that he spoke to A.L. regularly about internet companies and that in the course of those conversations Calandro introduced A.L. to e2.[86] Calandro told A.L. that his family had invested in e2 and that it might need additional investors.[87] Calandro also gave A.L.'s name to e2.[88]

---

[78] Tr. 971, 977-78; C 35.

[79] Tr. 977-79.

[80] C 35.

[81] R 85 at 81.

[82] *Id.* at 82.

[83] *Id.*

[84] Tr. 928.

[85] *See* R 237 (A.L. Affidavit).

[86] Tr. 979.

[87] Tr. 980.

[88] Tr. 981.

Following those conversations, A.L. purchased 7000 shares of Series B Preferred Stock for $49,000.[89]

Calandro also testified that he told D.T., another client, about e2.[90] D.T. was interested in technology companies, and Calandro spoke to him about his technology holdings three to four times per week.[91] In the course of those conversations, Calandro told D.T. about e2 and its need for additional capital.[92] As with A.L., Calandro told D.T. that he would give D.T.'s name to e2.[93] D.T. later purchased 7000 shares of Series B Preferred Stock through the T/G Partnership account for $49,000.[94]

4. Payment of Finders' Fees to Browne and Calandro

In March 2000, the e2 board, which was comprised of J.L.F. and B.M.B. at the time, authorized the issuance of stock to Browne and Calandro in payment of finders' fees due them for their efforts in connection with the Series B Preferred Stock Offering. The board action is reflected in the Unanimous Written Consent in Lieu of a Special Board Meeting of the Board of Directors dated March 11, 2000 (the "March 2000 UWC").[95] The March 2000 UWC states that e2 is obligated to pay Browne and Calandro "finders' fees" in connection with the Series B Preferred Stock Offering. The March 2000 UWC further states that Browne and Calandro requested e2 to pay the finders' fees in common stock at a value of $7.00 per share and that

[89] R 85 at 82.

[90] Tr. 973.

[91] Tr. 932.

[92] Tr. 973-74.

[93] Tr. 981.

[94] R 85 at 82.

[95] C 5.

Browne had requested e2 to issue the shares in his wife's name.[96] Nonetheless, Browne and Calandro urged the Panel to reject the March 2000 UWC because it was inaccurate.

In support of their contention, the Respondents called B.M.B. to testify that despite the language of the March 2000 UWC, e2 never paid finders' fees or commissions in connection with any private placement, including the Series B Stock Offering.[97] Indeed, B.M.B. testified that the Series B Private Placement Memorandum prohibited the payment of such fees. But B.M.B. was wrong on both counts. Browne produced evidence to show that e2 paid MG Securities Corp. a finder's fee in connection with the original sale of common stock in May 1998.[98] And the Private Placement Memorandum of the Series B Preferred Stock Offering did not prohibit the payment of finders' fees.[99] These errors seriously undercut the reliability of B.M.B.'s testimony.

B.M.B.'s disavowal of the accuracy of the March 2000 UWC was undercut further by his explanation of why he signed the document since he knew at the time that it was inaccurate. B.M.B. testified that the finders' fee language was "inconsequential" and that he regularly signed corporate documents without reading them.[100] In essence, B.M.B. viewed such board documents as meaningless, and, therefore, he signed whatever documents J.L.F. requested without regard to their accuracy. B.M.B. also found no significance in the transmittal letter that accompanied the March 2000 UWC from e2's corporate counsel that asked B.M.B. to sign the consent "to complete the issuances in connection with the second round [of financing]."[101]

The Panel rejects B.M.B.'s disavowal of the March 2000 UWC. B.M.B.'s testimony lacked any credibility. Not only was the consent's sole purpose to authorize the payment of the

[96] C 5 at 1.

[97] Tr. 836-37, 845, 851, 856.

[98] Tr. 1047-48.

[99] *See* R 81.

[100] Tr. 850, 862-63.

[101] C 4.

finders' fees due Browne and Calandro, but the accompanying cover letter from e2's corporate attorney clearly stated the purpose of the consent. Neither was ambiguous. The cover letter began,

> I'm enclosing a Unanimous Written Consent relating to the issuance of 10,177 shares of common stock to [Browne's wife] in payment of finders' fees owed to [Browne], and of 3,137 shares of common stock to Kevin Calandro, in payment of finders' fees owed to him.

In addition, the Panel notes that B.M.B. had considerable experience with corporate governance. As such, he understood the nature and importance of corporate records such as the March 2000 UWC. The Panel does not believe that he would have considered the payment of finders' fees to be inconsequential if he believed that their payment was prohibited by the offering documents.

Moreover, the Panel notes that, at Browne's request, B.M.B. wrote a letter dated March 6, 2003, that contradicts his hearing testimony. Browne had requested the letter in connection with the W.P.M. arbitration to clarify the circumstances surrounding e2's issuance of 10,177 shares of common stock to Browne's wife.[102] B.M.B. wrote that he questioned Browne and J.L.F. about the March 2000 UWC and that J.L.F. "was adamant that [issuing the stock] was something the Company should do."[103] B.M.B. further noted that Browne and J.L.F. had disagreed about the number of shares Browne should receive, but in the end e2 accepted Browne's computation.[104] Significantly, B.M.B. did not raise any question about either the accuracy of the March 2000 UWC or Browne's entitlement to the finders' fees.

Based on the foregoing, the Panel finds that e2 paid Browne and Calandro finders' fees in connection with the Series B Preferred Stock Offering, as authorized by the March 2000 UWC.

---

[102] C 7 at 15. The letter was addressed to the attorney defending Browne and PaineWebber in the W.P.M. arbitration.

[103] *Id.*

[104] *Id.* at 16.

C. Browne's Participation in the Series C Preferred Stock Offering

Browne took an active and substantial role in the Series C Preferred Stock Offering. In connection with the offering, e2 wanted to control the 1 million shares of common stock held by J.Y.A.[105] (the "J.Y.A. shares") at a low price to help in the company's negotiations with potential purchasers of Series C Preferred Stock.[106] In this manner the company would be able to tell prospective investors in the Series C Offering that they could also purchase shares of common stock at a low price, thereby giving the purchaser a lower average cost without lowering the price of the Series C Preferred Stock.[107]

At J.L.F.'s request,[108] Browne negotiated a series of option agreements covering the J.Y.A. shares.[109] Browne negotiated the original option agreement in early 2000.[110] On February 16, 2000, Browne wrote a letter to J.Y.A. that confirmed that he would be "endeavoring to locate a purchaser for the shares held by her" and that she had granted Browne the right to purchase up to 500,000 shares of e2 common stock at $5.00 per share.[111]

By August 2000, Browne was actively negotiating with investors to participate in the Series C Preferred Stock Offering and to purchase some or all of the J.Y.A. shares. One of those investors was S.K.F.[112]

---

[105] The stock was owned by J.Y.A., wife of J.L.A., the ousted former President of e2. To get e2 up and running, J.L.F. initially brought in a number of people who had worked with him at Saber Software. Among those was J.L.A., who served as the company's first President and Chief Executive Officer. Tr. 1040.

[106] Tr. 1090-91, 1095.

[107] Tr. 1095.

[108] R 34 (email from J.L.F. providing J.L.A.'s contact information).

[109] C 18 at 6 (Ans. To Question 16b).

[110] Browne negotiated another option agreement with J.Y.A. dated January 10, 2001 (C 18 at 59), and an extension to that agreement dated February 13, 2001 (C 18 at 65). These agreements were used in the negotiations with Avenue A to purchase additional Series C Preferred Stock.

[111] C 20 at 1.

[112] S.K.F. first learned about e2 in late 1999 from I.B. and P.N., who was a friend of S.K.F.'s and a business associate of I.B. Tr. 636. S.K.F. is listed as a founder on e2's records. R 85 at 77. S.K.F. purchased stock in the Series B Preferred Stock offering. Tr. 637.

S.K.F. testified that Browne encouraged him to participate in the Series C Preferred Stock Offering.[113] Browne discussed the potential for an initial public offering ("IPO") and the terms of the Series C Preferred Stock Offering.[114] Browne told S.K.F. that the Series C Preferred Stock Offering was going to be the final round of capitalization before the IPO or other disposition of the company.[115] In addition, Browne advised S.K.F. about the J.Y.A. option and explained how that would relate to the Series C Preferred Stock Offering.[116] Browne told S.K.F. that if he would purchase $300,000 of Series C Preferred Stock, he would also have the right to purchase $300,000 of e2 common stock from J.Y.A. at a favorable price.[117] Browne also told S.K.F. that Avenue A was going to invest $5 million in the Series C Preferred Stock Offering.[118] Avenue A's investment was important to S.K.F.'s decision to purchase additional shares because it meant that there was a substantial capital commitment in place from an experienced technology company.[119] Once S.K.F. decided to participate in the Series C Preferred Stock Offering, J.L.F. directed S.K.F. to deal with Browne to complete the transactions.[120]

In October 2000, S.K.F. and CBI-Eastchase, L.P., a limited partnership he managed, purchased approximately $300,000 of common stock from J.Y.A. in connection with the Series C Preferred Stock Offering.[121] Browne participated in these transactions. He performed many of the tasks expected of a broker. Browne communicated with the parties regarding the terms of the

[113] S.K.F. testified that Browne solicited him to purchase e2 stock. Tr. 649.

[114] Tr. 639-40.

[115] Tr. 638.

[116] Tr. 640.

[117] Tr. 641.

[118] Tr. 643.

[119] Tr. 643-44.

[120] Tr. 645.

[121] R 243.

transaction,[122] forwarded documents for signature,[123] and assisted with the transmittal of the purchase proceeds to the seller.[124] Indeed, Browne admitted that he helped facilitate S.K.F.'s purchase of common stock from J.Y.A. although he did not consider his involvement to rise to the level that required him to provide his firm with written notice of his activities under Conduct Rule 3040.[125]

In addition, Browne participated in S.K.F.'s purchase of Series C Preferred Stock.[126] For example, Browne forwarded the subscription documents to S.K.F.[127] and provided him with wiring instructions for his purchases.[128] Furthermore, other evidence in the record reflects that Browne encouraged additional investors to purchase Series C Preferred Stock.[129]

On March 5, 2001, the e2 board of directors authorized the issuance of 150,000 shares of common stock to Browne "with respect to the services [he] rendered in connection with the financing of the Company."[130] These shares were paid to Browne as compensation for his efforts "in connection with the private placement of certain shares of [e2's] capital stock,"[131] which included the purchases by S.K.F. and CBI-Eastchase. The board minutes further state that J.L.F. negotiated the amount of the payment due Browne.[132]

---

[122] C 25.

[123] C 21; Tr. 1096.

[124] C 26; C 27; Tr. 1092.

[125] Tr. 1092.

[126] The purchase of $300,000 worth of Series C Preferred Stock ultimately was made in the name of CBI-Eastchase, L.P. *See* C 23.

[127] R 244.

[128] Tr. 1111.

[129] *See* R 126; R 127; R 128. These documents undercut Browne's assertion that he never participated in any efforts to raise capital for e2.

[130] C 32 at 1 (Minutes of Board of Directors Meeting).

[131] *Id.* at 2.

[132] *Id.*

At the hearing, Browne took the position that e2 issued the 150,000 shares to him in recognition of his varied contributions to the company as an advisory director. Browne pointed out that even assuming a relatively small value per share, 150,000 shares would equal an unreasonably high commission on S.K.F. and CBI-Eastchase's total investment of $600,000.[133] But Browne's email to J.L.F. just two days before the board meeting demonstrates that Browne had demanded compensation for the capital he helped raise.[134]

Browne wrote the email in response to J.L.F.'s email inquiry referenced "Payment for Services."[135] J.L.F. asked Browne to supply a number for "the total capital [he had] helped raise for the company to date."[136] Browne responded by first pointing out that Avenue A's investment in the Series C Preferred Stock Offering, which totaled approximately $13.25 million, would not have closed but for his efforts along with others. Browne then claimed that he participated in helping raise approximately another $15.9 million. He reminded J.L.F. of their agreement that he would be entitled to 5% on the Series C Preferred Stock Offering and an additional 5% on the J.Y.A. shares.[137] Browne specifically included S.K.F. as one of the investors for whom he should be credited.

Browne dismissed his email as "facetious." But the Panel does not find his testimony credible. Indeed, his various explanations were contradictory. Browne testified that, in June or July of 2000, J.L.F. promised him that he would be paid 5% of the next round of financing.[138] Browne characterized the offered payment as compensation for all of the work he had put into e2

[133] *See* Tr. 1101-02.

[134] C 3.

[135] *Id.*

[136] *Id.*

[137] *Id.*

[138] Tr. 1153-54.

up to that point. Nevertheless, Browne dismissed the notion that he was to be paid for raising capital.

The Panel concluded that Browne considered J.L.F.'s promise an inducement to continue to raise capital for e2. As Browne reminded J.L.F. in the email leading up to the March 5, 2001, board meeting, Browne had continued to assist e2 with its financing in reliance on J.L.F.'s promise to pay him for his efforts. In other words, Browne expected to receive further compensation when he negotiated the J.Y.A. transactions and participated in the Series C Preferred Stock Offering.

III. CONCLUSIONS OF LAW

NASD Conduct Rule 3040 requires that an associated person who intends to participate in any manner in a securities transaction outside the regular course or scope of employment must provide his employer with prior written notice describing in detail the proposed transaction, including the associated person's proposed role in the transaction, and stating whether he or she may receive selling compensation.[139] If the associate person is compensated, or may be compensated, for the transaction, he or she must receive the employer's prior written approval.[140] Scienter is not a required element of a violation of NASD Rule 3040.[141]

"The policy reasons behind Rule 3040 mandate that the Rule be interpreted broadly…. Rule 3040 serves not only to protect investors, but also to permit securities firms, which may be subject to liability in connection with transactions in which their representatives become involved, to supervise such transactions."[142] Accordingly, both the Securities and Exchange Commission ("SEC") and NASD have found that very limited involvement by an associated

[139] *Alvin W. Gebhart, Jr.*, Exchange Act Release No. 53136, 2006 SEC LEXIS 93, at *54-55 (Jan. 18, 2006).

[140] *Id.* at *55.

[141] *Id.*

[142] *Mark H. Love*, Exchange Act Release No. 49248, 2004 SEC LEXIS 318, at *9 (Feb. 13, 2004).

person is sufficient to trigger the notice requirement of Conduct Rule 3040.[143] For example, in *Terry Don Wamsganz*, Exchange Act Release No. 22411, 1985 SEC LEXIS 695 (Sept. 16, 1985), the SEC held that merely introducing a client seeking to purchase control of a company to company management, and later receiving a finder's fee when the transaction is consummated, is sufficient participation to subject the registered representative to NASD's notice requirement.[144] Contrary to the Respondents' arguments here, application of Conduct Rule 3040 is not dependent on whether the registered representative "solicited" the investor or "made the sale."[145] Nor is it a defense that the purchaser's decision to invest in a security resulted from the representations of third parties,[146] or that the purchaser was satisfied with the investment.[147] The important factor is whether the registered representative's participation in the transaction was sufficient to bring into play the policy reasons behind the Rule.

In this case there is sufficient evidence of Browne's and Calandro's participation in private securities transactions in connection with the Series B Preferred Stock Offering. Each referred purchasers to e2, and each received a finder's fee for the effort. The Panel does not find credible the Respondents' story that they did not expect to receive finders' fees for their efforts in referring potential investors to e2. Indeed, the credible evidence is to the contrary. First, the March 2000 UWC states that Browne and Calandro requested that e2 pay them the finders' fees

---

[143] *See, e.g., Charles A. Roth*, Exchange Act Release No. 31085, 1992 SEC LEXIS 2006, *aff'd* 22 F.3d 1108 (D.C. Cir.), *cert. denied*, 513 U.S. 1015 (1994).

[144] Applying language "involved in any way" from predecessor rule. *See also John P. Goldsworthy*, Exchange Act Release No. 45926, 2002 SEC LEXIS 1279, at *29 (May 15, 2002) (citing *Gilbert M. Hair*, Exchange Act Release No. 32187, 1993 SEC LEXIS 883, at *11 (Apr. 21, 1993)).

[145] *Joseph Abbondante*, Exchange Act Release No. 53066, 2006 SEC LEXIS 23, at * 29 (Jan. 6, 2006); *Stephen C. Gluckman*, Exchange Act Release No. 41628, 1999 SEC LEXIS 1395, at *17 (July 20, 1999). Solicitation has been defined to mean in the investment context an attempt "to produce the sale by urging or persuading another to act." *Meadows v. S.E.C.*, 119 F.3d 1219, 1225 (5th Cir. 1997).

[146] *Abbondante*, 2006 SEC LEXIS 23, at *29.

[147] *Hair*, 1993 SEC LEXIS 883, at *12.

they were due in shares of common stock.[148] Neither Respondent presented any credible evidence to support his argument that J.L.F. had e2's corporate attorney create the document solely to harm Browne in connection with the W.P.M. arbitration. Not only was the March 2000 UWC signed by their friend B.M.B., but also he indicated in his letter in support of Browne that he had discussed the payment of the finders' fees with Browne before he signed the consent.[149] There is no evidence that either B.M.B. or Browne questioned the language of the March 2000 UWC or objected to the statement that the shares were to be issued in payment of finders' fees e2 owed Browne and Calandro.

Second, payment of the finders' fees on the Series B Preferred Stock Offering is supported by other internal e2 documents. For example, e2's CFO referenced the finders' fees paid to Browne and Calandro in an email dated May 31, 2000.[150] Furthermore, the email undermines the Respondents' contention that the March 2000 UWC was fabricated by J.L.F. after he and Browne had a falling out. The animosity between Browne and J.L.F. developed later, and J.L.F. bore no ill will toward Calandro. The facts do not support the Respondents' contention that J.L.F. fabricated the documents reflecting the payment of finders' fees to Browne and Calandro.

The Panel also rejects the Respondents' argument that their activities fell within their regular course or scope of employment. PaineWebber did not permit its registered representatives to sell unregistered securities, such as the e2 Series B and Series C Preferred Stock Offerings, without PaineWebber's written approval. In August 1999, Eldemire warned Browne about this restriction.[151] Thus, although Browne and Calandro's managers may have

[148] C 5 at 1.

[149] C 7 at 15.

[150] C 6 at 1.

[151] C 7 at 12.

been aware generally of the Respondents' efforts to assist e2 and secure its potential investment banking business, their managers' general awareness did not modify the firm's written policies prohibiting the sale of unregistered securities and requiring written approval of outside activity. The fact that Browne and Calandro openly pursued their capital raising activity on behalf of e2 over a period of many months while associated with PaineWebber means nothing more than that they violated Conduct Rule 3040 on a regular basis.[152] Assumptions that they may have drawn from PaineWebber's "silence [in the face of their efforts generally on e2's behalf] cannot substitute for the written permission clearly required by Rule 3040 and the relevant [PaineWebber] policies."[153] Moreover, it is undisputed that Browne and Calandro never provided PaineWebber with written notice describing the details of their activity. For example, neither Respondent argues that he provided PaineWebber with copies of the relevant offering documents. In any event, oral notice does not satisfy NASD Conduct Rule 3040.[154]

The Respondents argument that Conduct Rule 3040 does not cover transactions with immediate family members also is without merit. Conduct Rule 3040(e) provides that "transactions *among* immediate family members" for which the associated person does not receive selling compensation are exempt from the definition of private securities transactions.[155] Here, however, the purchases of e2 Series B Preferred Stock were made by the family members from e2. As such, the stock did not move "solely within the family circle" as the rule envisions.[156] In other words, the purchases the Respondents' family members made from e2

---

[152] *Charles A. Roth*, Exchange Act Release No. 31085, 1992 SEC LEXIS 2006, at *10 (Aug. 25, 1992).

[153] *Gebhart*, 2006 SEC LEXIS at *57. PaineWebber's written policies required its registered representatives to obtain prior written approval before engaging in a broad range of outside activities and investments. *See* C 33 (PaineWebber Compliance Manual); C 13 (PaineWebber Compliance Bulletin).

[154] *See, e.g., Department of Enforcement v. Van Dyk*, No. C3B020013, 2004 NASD Discip. LEXIS 12, at *22-23 (Aug. 9, 2004).

[155] Conduct Rule 3040(e)(1) (emphasis added).

[156] *Gilbert A. Zwetsch*, Exchange Act Release No. 30092, 1991 SEC LEXIS 2839, at *3-4 (Dec. 18, 1991) (decided under Rule 40 of NASD's Rules of Fair Practice, the predecessor to Conduct Rule 3040).

cannot be considered transactions solely *among* family members. Thus, the Respondents were required to provide PaineWebber with written notice of their proposed participation in their family members' transactions.

On the other hand, the Panel determined that Browne did not participate in the transactions made by other brokers in his office, Eldemire, McLochlin, Myron H. Bond, and Glenn Duphorne.[157] Eldemire first learned of e2 from Browne shortly after he joined PaineWebber. In May 1998, Browne requested approval from Eldemire to invest in e2. Browne told Eldemire that J.L.F. had requested that Browne invest, and he wanted to know if PaineWebber would allow it. In the course of the conversation, Eldemire asked Browne about e2.[158] Thereafter, without further involvement from Browne, Eldemire purchased 30,000 shares of common stock on May 26, 1998.[159] Eldemire testified that he made the investment because e2 was an Internet company, and Internet stocks were a "hot area" at the time.[160] The Complaint does not charge Browne with participating in this transaction. Then, in March 2000, Eldemire purchased an additional 5000 shares in the Series B Offering.[161] Although the Department charged Browne with participating in this transaction, there is no evidence that he had any involvement with the transaction whatsoever.

McLochlin, who had been Browne's supervisor at Kidder Peabody, purchased 10,000 shares of Preferred B Stock on March 11, 2000.[162] McLochlin testified he and many other

---

[157] Bond invested in the name of the Myron H. Bond Family Partnership and the Myron H. Bond Family Trust, and Duphorne invested in his wife's name. R 85 at 81-82.

[158] Tr. 61.

[159] R 85 at 78.

[160] Tr. 89-90. Eldemire testified that Browne did not solicit his investment or otherwise influence him to make the investment. Tr. 100, 103.

[161] R 85 at 81.

[162] R 85 at 82.

brokers at PaineWebber were looking for a way to invest in the Internet boom.[163] McLochlin had heard about e2, and he asked Browne if it was looking for investors.[164] Browne told him it was. Thereafter, without Browne's assistance, McLochlin obtained the necessary subscription materials directly from e2 and completed them. McLochlin asked Browne if he should mail the completed documents back to the Company. Browne told him he should. Enforcement presented no evidence that Browne participated in those transactions. Indeed, McLochlin testified that Browne did not solicit the transactions, and McLochlin was not unaware of Browne's involvement with the Company. In short, the evidence showed that the discussions between Browne and McLochlin were nothing more than two brokers discussing a new company that was "in the market."[165] Browne's conduct did not constitute "participation" in McLochlin's transactions under Conduct Rule 3040.

Bond[166] also purchased shares of Series B Preferred Stock in March 2000.[167] Bond knew about e2 from general discussion in the office, and he knew that Browne was associated with the Company. Bond also knew that e2 was looking to sell shares in the Series B Preferred Stock Offering. "It was common knowledge in the office."[168] Bond asked Browne if there were shares available for purchase. Browne got back to him and said there were. Thereafter, Bond purchased shares of Series B Preferred Stock. Browne did not participate in those transactions in any manner. Indeed, there is no evidence of when Browne learned that Bond made the investments.

[163] Tr. 210.

[164] Tr. Tr. 204, 211. McLochlin could not remember how he first learned of e2, but he stated that there was a lot of talk about e2 in the office and generally. Tr. 211.

[165] Tr. 211.

[166] Bond had been a friend of Browne's father for 38 years.

[167] R 85 at 82.

[168] Tr. 186-87.

Browne also was charged with participating in Duphorne's transactions. Like the other brokers, Duphorne purchased shares of Series B Preferred Stock in March 2000.[169] Duphorne, who has 40 years experience in the securities industry, jointly worked with Browne on some accounts.[170] And in the course of their joint working relationship, they had conversations about e2 among other companies.[171] Duphorne eventually told Browne that he had an interest in e2 and asked if it were possible to purchase shares. Browne told him it was, and several days later Duphorne received subscription information directly from the Company. Duphorne later made an investment in his wife's name without Browne's involvement or knowledge. The Panel concluded that the foregoing evidence was insufficient to prove by a preponderance of the evidence that Browne participated in the Bond transaction.[172]

In conclusion, the Panel found that Browne and Calandro violated NASD Conduct Rules 3040 and 2110 by engaging in several private securities transactions in connection with the Series B Preferred Stock Offering, as detailed in Parts II.B.2 and II.B.3, and that Browne also violated both rules by engaging in private securities transactions in connection with the Series C Preferred Stock Offering.[173] Conduct Rule 3040 required them to provide detailed written notices to PaineWebber[174] before they participated in any process that could have led to the purchase of e2 stock or their receipt of compensation for such participation.[175]

---

[169] R 85 at 81.

[170] Tr. 342-43.

[171] Tr. 343.

[172] *Cf. Mark H. Love*, 2004 SEC LEXIS 318, at *10 (holding that a broker who does nothing more than refer a customer to another investment opportunity would not ordinarily run afoul of Rule 3040). In this case, neither Duphorne nor his wife was Browne's customer, and Browne did not recommend the investment or facilitate the mechanics of the transaction.

[173] A violation of Conduct Rule 3040 also constitutes a violation of Conduct Rule 2110. *Love*, 2004 SEC LEXIS 318, at *13.

[174] In addition, Browne was required to provide the same notice to Lehman Brothers.

[175] *Jay Frederick Keeton*, Exchange Act Release No. 31082, 1992 SEC LEXIS 2002, at *10 n.13 (Aug. 24, 1992).

IV. SANCTIONS

The starting point under the NASD Sanction Guidelines ("Guidelines") for determining the appropriate remedial sanctions for violations of Conduct Rule 3040 is for the Panel to assess the extent of the violation measured by the dollar amount of the sales, the number of customers involved, and the length of time over which the violations occurred.[176] The Guidelines suggest a fine of between $5,000 and $50,000 and, depending on the amount of the sales, a suspension of between 10 business days and one year or, in cases involving sales in excess of $1 million, a longer suspension or a bar.[177]

Based primarily on the dollar amount of the sales reflected on the Series B Subscription List and the amount of the purchases made by S.K.F. and CBI-Eastchase, Enforcement argued that Browne should be suspended for 30 months and fined $50,000 and that Calandro should be suspended for 6 months and fined $15,000.[178] The Respondents on the other hand urged the Panel to dismiss the Complaint because they contended that Enforcement had failed to show that they had participated in any manner in any private securities transaction.

The Panel began its consideration of sanctions by assessing the dollar amount of sales attributable to each Respondent's participation. The Panel concluded that, in connection with the Series B Preferred Stock Offering, Browne participated in transactions totaling approximately $398,000,[179] and Calandro participated in transactions totaling approximately $475,500.[180] In addition, the Panel concluded that Browne participated in transactions totaling $600,000 in connection with the Series C Preferred Stock Offering.

---

[176] NASD SANCTION GUIDELINES at 15 (2006 ed.)

[177] *Id.*

[178] Enforcement's Pre-Hr'g Br. at 13.

[179] *See infra* Part II.B.2.

[180] *See infra* Part II.B.3. The total includes B.G.'s investment of $100,000, which also is included in Browne's total because they both participated in his transaction and shared responsibility for his account.

Based on the foregoing sales totals, the Guidelines suggest a suspension of 6 to 12 months for Browne and 3 to 6 months for Calandro before other factors are considered. In this case, however, the dollar amount of the sales is a less reliable measure of the extent of the Respondents' participation than similar dollar values in other cases. Several of the investors had significant independent ties to e2. For example, I.B. was a founding investor and member of e2's board, B.G. was a software reseller with an interest in doing business with e2,[181] and J.R.C. was in the insurance business with an interest in securing e2 as a client.[182] And S.K.F., whom I.B. originally introduced to e2, first invested before Browne became involved with him in connection with the J.Y.A. shares and the Series C Preferred Stock Offering. In summary, while Browne, and to a lesser extent Calandro,[183] participated to some degree in these investors' purchases of stock from e2, the Respondents were not the sole source of information about e2. In fact, there is no evidence that any investor relied on any information the Respondents supplied.

The Panel also notes that Browne's father was a registered representative with the ability to evaluate the risks and potential rewards associated with an investment in e2 by him and other members of his family. Although his father's status did not excuse Browne from his obligation to provide PaineWebber with written notice of his outside sales activity, it is a factor the Panel considered in weighing the total sales dollar volume for purposes of determining the appropriate sanctions under the facts and circumstances of this case.

Next, the Panel considered the Principal Considerations in Determining Sanctions under the Guidelines for private securities transactions[184] and the General Principles Applicable to All Sanction Determinations and the Principal Considerations in Determining Sanctions set forth in

[181] Tr. 921.

[182] Tr. 1056.

[183] Calandro and Browne were involved jointly with B.G.

[184] GUIDELINES at 15.

the Guidelines.[185] The Panel found the following circumstances aggravating: (1) the number of customers; (2) the length of time over which the activity took place; (3) some purchasers were firm customers; and (4) the Respondents' refusal to accept responsibility for their actions. On the other hand, there is no evidence that the Respondents attempted to conceal their conduct or told any purchaser that PaineWebber was involved in the e2 offerings.

On balance, and considering all of the circumstances surrounding the Respondents involvement with e2, the Panel concluded that their violations were not minor or technical. As the SEC has noted, "[o]utside sales activities, even if uncompensated, expose investors to possible losses and employers to possible liability."[186] Here, the Respondents efforts contributed to their family and friends investing a considerable amount in e2. The fact that they had to recover their investments through litigation in the bankruptcy proceedings shows the potential of harm associated with their e2 investments. In addition, their actions exposed PaineWebber to possible claims from disgruntled customers. In fact, one customer, W.P.M. did file an arbitration claim against PaineWebber concerning Browne and e2. None of this might have happened if the Respondents had given the written notice required by Conduct Rule 3040.

In conclusion, the Panel determined that significant sanctions were warranted under the facts and circumstances of this case. In the Respondents' eagerness to land e2's business, they participated in a number of private securities transactions. Their belief, however sincere, that their extensive involvement with e2 did not constitute participation in those transactions does not excuse their failure to notify their firm of their intended activities. In addition, the Panel is troubled by their failure to appreciate their errors after NASD commenced its investigation and instituted this proceeding. Accordingly, to ensure that the Respondents appreciate the significance of their misconduct, and to deter them and others from similar misconduct in the

[185] GUIDELINES at 2-7.

[186] *Keeton*, 1992 SEC LEXIS 2002, at *4.

future, more than minimum sanctions are required. Accordingly, the Panel will suspend Browne in all capacities for six months and fine him $25,000, and the Panel will suspend Calandro in all capacities for three months and fine him $5,000.

V. ORDER

For the reasons set forth above, Browne is suspended in all capacities for six months and fined $25,000, and Calandro is suspended in all capacities for three months and fined $5,000.[187] In addition, the Respondents are ordered jointly and severally to pay $9,930.30 in costs.[188]

These sanctions shall become effective on a date set by the NASD, but not earlier than 30 days after this Decision becomes the final disciplinary action of the NASD; except, if this Decision becomes NASD's final disciplinary action, Browne's suspension shall begin at the opening of business on October 2, 2006, and end on April 1, 2007; and Calandro's suspension shall begin at the opening of business on October 2, 2006, and end on January 1, 2007.

_____

Andrew H. Perkins
Hearing Officer
For the Extended Hearing Panel

Copies to:

Kevin Calandro (FedEx, next day delivery, and first-class mail)
James W. Browne (FedEx, next day delivery, and first-class mail)
E. Steve Watson, Esq. (facsimile and first-class mail)
Christopher J. Bebel, Esq. (facsimile and first-class mail)
Sean W. Firley, Esq. (electronic and first-class mail)
Mark P. Dauer, Esq. (electronic and first-class mail)
Rory C. Flynn, Esq. (electronic and first-class mail)

[187] The Hearing Panel has considered all of the parties' arguments. They are rejected or sustained to the extent that they are inconsistent with the views expressed herein.

[188] The costs are composed of an administrative fee of $750 and transcript costs of $9,180.30.