

**FINANCIAL INDUSTRY REGULATORY AUTHORITY  
OFFICE OF HEARING OFFICERS**

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DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

MIDAS SECURITIES, LLC  
(CRD No. 103680),

WORLD TRADE FINANCIAL CORPORATION  
(CRD No. 42638),

JASON TROY ADAMS  
(CRD No. 2137404),

FRANK EDWARD BRICKELL  
(CRD No. 3257725),

JAY S. LEE  
(CRD No. 4338187),

and

RODNEY PRESTON MICHEL  
(CRD No. 1275392),

Respondents.

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Disciplinary Proceeding  
No. 2005000075703

Hearing Officer—Andrew H. Perkins

**AMENDED EXTENDED HEARING  
PANEL DECISION<sup>1</sup>**

May 12, 2009

**Respondents World Trade, Midas Securities, and Brickell violated NASD Conduct Rule 2110 by selling unregistered securities in violation of Section 5 of the Securities Act of 1933. For this violation World Trade and Brickell are fined \$15,000 each, Brickell is suspended from associating with any member firm in any capacity for 30 business days, and Midas Securities is fined \$30,000. For related**

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<sup>1</sup> This Amended Decision is issued to clarify the Hearing Panel's findings regarding the supervisory violations of World Trade Financial Corporation, Midas Securities, and Rodney Preston Michel set forth in Parts IV.B at page 23, and Part IV.C at page 24. There is no change in the sanctions assessed against any Respondent.

**supervisory violations of NASD Conduct Rules 3010 and 2110, Respondent World Trade is fined an additional \$15,000, Midas Securities is fined an additional \$25,000, Michel is fined \$15,000 and suspended in all principal capacities for 45 days, Lee is fined \$20,000 and suspended from associating with any member firm in any principal capacity for two years, and Adams is fined \$10,000 and suspended from associating with any member firm in any principal capacity for 30 business days.**

### **Appearances**

For Complainant: Jonathan I. Golomb and Gregory R. Firehock, FINRA,  
DEPARTMENT OF ENFORCEMENT, Washington, DC.

For Respondents: Irving Einhorn, Manhattan Beach, CA.

### **DECISION**

#### **I. INTRODUCTION**

The Department of Enforcement (“Enforcement”) brought this disciplinary proceeding against Respondents Midas Securities, LLC (“Midas Securities”), World Trade Financial Corporation (“World Trade”), Jason Troy Adams (“Adams”), Frank Edward Brickell (“Brickell”), Jay S. Lee (“Lee”), and Rodney Preston Michel (“Michel”).<sup>2</sup> Enforcement alleges that the Respondents sold unregistered securities in violation of Section 5 of the Securities Act of 1933 (“Securities Act”) and violated NASD Conduct Rules regarding the supervision of those sales.<sup>3</sup>

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<sup>2</sup> The original Complaint also named the following respondents: Barron Moore, Inc., Katherine Anne Moore, William E. Kassar, Jr., Jeffrey Ken Santohigashi, Benjamin Centeno, and Patrick Francis Harte, Jr. With the exception of Harte, each of the foregoing entered into settlements with FINRA. On September 16, 2008, the Hearing Officer granted Enforcement’s motion to dismiss the charges against Harte so that they could be consolidated with other charges in another pending disciplinary proceeding.

<sup>3</sup> As of July 30, 2007, NASD consolidated with the member regulation and enforcement functions of NYSE Regulation and began operating under a new corporate name, the Financial Industry Regulatory Authority (FINRA). References in this decision to FINRA include, where appropriate, NASD. Following consolidation, FINRA began developing a new FINRA Consolidated Rulebook. The first phase of the new consolidate rules became effective on December 15, 2008, including certain conduct rules and procedural rules. See Regulatory Notice 08-57 (Oct. 2008). This decision refers to and relies on the NASD Conduct Rules that were in effect at the time of Respondents’ alleged misconduct. In addition, because the Complaint was filed before December 15, 2008, the NASD Procedural Rules were applied in this disciplinary proceeding.

## **II. PROCEDURAL HISTORY**

Enforcement filed a Complaint with the Office of Hearing Officers on March 31, 2008, and an Amended Complaint on September 17, 2008. Respondents World Trade, Adams, Brickell, and Michel filed their Answer to the Amended Complaint with the Office of Hearing Officers on October 6, 2008. Respondents Midas Securities and Lee filed their Answer to the Amended Complaint on October 16, 2008.

The Extended Hearing Panel, which is comprised of the Hearing Officer, a current member of the District 5 Committee, and a former member of the District 2 Committee, held three days of hearing in Los Angeles, California, on November 10-12, 2008. Enforcement presented eight witnesses (including the individual Respondents) and introduced 61 exhibits.<sup>4</sup> The Respondents presented one witness, Respondent Lee, and introduced no exhibits.<sup>5</sup>

Based upon a careful review of the entire record, the Extended Hearing Panel makes the following findings of fact and conclusions of law.

## **III. BACKGROUND**

### **A. Investigation of Sales of iStorage Unregistered Stock**

FINRA's investigation into the sales of iStorage Networks, Inc. ("iStorage") stock was triggered by its receipt of spam e-mails touting the stock in December 2004 and January 2005.<sup>6</sup> FINRA also uncovered a press release announcing that iStorage had begun trading as a public company on the over-the-counter market on December 9, 2004, as well as several other press releases dated December 2004 and January 2005 that

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<sup>4</sup> Enforcement's exhibits are labeled "CX" followed by the exhibit number.

<sup>5</sup> Midas Securities and Lee offered a single exhibit, which the Hearing Officer rejected. The exhibit was marked as WTF-5 for identification, and was preserved as a supplemental document in accordance with Procedural Rule 9267(b). By Order dated October 16, 2008, Midas Securities and Lee were prohibited from introducing documentary evidence at the hearing because they failed to file pre-hearing submissions in accordance with the scheduling order in this proceeding.

<sup>6</sup> Tr. 52-53; CX-8.

announced positive news concerning iStorage's business and operations.<sup>7</sup> FINRA staff suspected that the spam e-mails and press releases might be part of a scheme to manipulate the price of iStorage stock.

Upon investigation, FINRA staff determined that iStorage was incorporated in 1997 as Camryn Information Services, Inc.<sup>8</sup> Between 1999 and early May 2004, Camryn was a shell company with four shareholders. Doyle Mark White ("White"), president of iStorage, owned 5 million shares, and the remaining balance of 3 million shares was held equally by Paul Johnson ("Johnson"), Joel Holt ("Holt"), and Gary Zinn ("Zinn").<sup>9</sup> The shares they held were restricted shares.<sup>10</sup>

In early November 2004, Camryn entered into a reverse merger with iStorage, which at the time was a development-stage corporation. Following the reverse merger, the company changed its name to iStorage and issued a 3.334 to 1 forward stock split by which Johnson, Holt, and Zinn each received 3.334 million shares on November 8, 2004.<sup>11</sup> On November 15, 2008, White stepped down as President of iStorage and all of his shares in the company were canceled.<sup>12</sup>

FINRA staff further determined that immediately following the reverse merger Johnson, Holt, and Zinn deposited 4,511,000 shares of iStorage into their accounts at World Trade and Midas Securities, and then proceeded to sell 3,070,800 of those shares

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<sup>7</sup> Tr. 54; CX-9.

<sup>8</sup> Stipulations of Fact between Enforcement and Respondents Midas Securities and Lee ("Midas Stip.") ¶ 8; Stipulations of Fact between Enforcement and Respondents World Trade, Adams, Brickell, and Michel ("World Trade Stip.") ¶ 8.

<sup>9</sup> Midas Stip. ¶ 9; World Trade Stip. ¶ 9.

<sup>10</sup> CX-4, at 17. "Restricted" stock is defined as "securities acquired directly or indirectly from the issuer, or from an affiliate of the issuer, in a transaction or chain of transactions not involving any public offering." 17 C.F.R. § 230.144(a)(3)(i).

<sup>11</sup> Midas Stip. ¶¶ 8, 12; World Trade Stip. ¶¶ 8, 11; CX-10; CX-17, at 1.

<sup>12</sup> CX-17, at 1.

to other individuals and entities.<sup>13</sup> None of the shares was registered with the Securities and Exchange Commission (“SEC”).<sup>14</sup> Because the trading pattern looked like it could be an unlawful public distribution of unregistered securities, FINRA staff examined the firms’ involvement in the transactions.

**B. Respondents**

**1. Midas Securities**

Midas Securities is a registered broker-dealer and member of FINRA located in Anaheim, California. The firm has been a member of FINRA since 2000. Its principal owner is MidasTrade.com, Inc. (“MidasTrade”).<sup>15</sup> During the relevant period, Midas Securities’ brokerage business was almost exclusively limited to the receipt and liquidation of over-the-counter securities in unsolicited transactions.<sup>16</sup> MidasTrade’s and Midas Securities’ principal business was the provision of direct market execution services for Korean brokerage firms seeking to trade securities in the U.S. securities markets.<sup>17</sup>

**2. Jay S. Lee**

Respondent Lee is, and at all times relevant to the Complaint has been, the President, Chief Executive Officer, Chief Compliance Officer, and Financial and Operations Principal of Midas Securities. Lee has been registered as a General Securities Representative, General Securities Principal, and Equity Trader since 2001, and as an

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<sup>13</sup> CX-10; CX-11; CX-17, at 1. Johnson also deposited and liquidated iStorage shares through accounts at Barron Moore and Milestone Group Management, Inc. (“Milestone”). All told, Johnson, Holt, and Zinn distributed 3,773,300 shares of iStorage into the public market between November 9, 2004, and March 24, 2005.

<sup>14</sup> CX-4, at 3; Midas Stip. ¶ 18.

<sup>15</sup> Midas Stip. ¶ 1.

<sup>16</sup> Tr. 65.

<sup>17</sup> Tr. 485-86.

Options Principal since 2002. He has been registered with Midas Securities since March 2002.<sup>18</sup>

### **3. World Trade**

World Trade is, and at all times relevant to this Complaint was, a registered broker-dealer and a member of FINRA located in San Diego, California. World Trade has been a member of FINRA since 1998. Respondent Michel is the majority owner of World Trade Financial, and Respondent Adams is a minority owner of the firm.<sup>19</sup> Approximately 75% of World Trade's business during the relevant period involved the receipt and liquidation of over-the-counter securities in unsolicited transactions. None of the stock World Trade receives in connection with this business is registered.

### **4. Rodney P. Michel**

Respondent Michel entered the securities industry in 1991 and joined World Trade in 1998. At all times relevant to the Complaint, he has been the President, Financial Operations Principal, and majority owner of World Trade. He is registered with World Trade as a General Securities Representative, General Securities Principal, Municipal Securities Representative, Municipal Securities Principal, and Financial and Operations Principal, and Equity Trader.<sup>20</sup>

Pursuant to World Trade's Supervisory Procedures Manual, Michel had overall responsibility for compliance and supervision at the firm and had specific responsibility for supervising home office personnel and penny stock trading, for reviewing customer transactions and customer account activity on a daily, weekly, and monthly basis, and for conducting daily spot checks of trade confirmations. As the firm's Chief Compliance

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<sup>18</sup> Midas Stip. ¶ 6.

<sup>19</sup> World Trade Stip. ¶ 1.

<sup>20</sup> *Id.* ¶ 4.

Officer, he was assigned responsibility under the Supervisory Procedures Manual “for establishing supervisory systems.”<sup>21</sup> In addition, Michel had joint responsibility with Adams for “sales of control or restricted stock,”<sup>22</sup> and they both reviewed monthly account statements and blotters to monitor the activity in customer accounts.<sup>23</sup>

## **5. Jason T. Adams**

Respondent Adams entered the securities industry in 1991. Adams joined World Trade in 1999, at which time he registered as a General Securities Representative. Since then, he also has registered with World Trade as a General Securities Principal and an Equity Trader. At all times relevant to the Complaint, he was Vice President, Trade Desk Supervisor, and part owner of World Trade.<sup>24</sup> In addition to the joint responsibilities he shared with Michel mentioned above, he received copies of all stock certificates received for deposit into accounts at World Trade.<sup>25</sup>

## **6. Frank E. Brickell**

Respondent Brickell first entered the securities industry in 1999. Since 2001, Brickell has been associated with World Trade and registered as a General Securities Representative and an Equity Trader. In May 2006, he registered as a General Securities Principal; he became World Trade’s Chief Compliance Officer in April 2007.<sup>26</sup>

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<sup>21</sup> *Id.* ¶ 21.

<sup>22</sup> World Trade Stip. ¶ 19.

<sup>23</sup> *Id.* ¶ 20.

<sup>24</sup> *Id.* ¶ 3.

<sup>25</sup> *Id.* ¶ 20.

<sup>26</sup> *Id.* ¶ 2.

## C. Sales of Unregistered iStorage Shares

### 1. Overview

iStorage began trading on December 9, 2004, on the over-the-counter securities market. At the time, it was a development-stage company with neither an operations nor an earnings history.<sup>27</sup> None of the individual Respondents knew anything about iStorage before their customers asked Midas Securities and World Trade to liquidate their recently-acquired shares.

There was no disagreement regarding the transactions at issue. In the six days beginning November 9, 2004 (the day following the forward stock split of iStorage), Johnson, Holt, and Zinn transferred in certificate form approximately 9.5 million shares of iStorage shares to 65 people and entities. In doing so, Johnson, Holt, and Zinn divested themselves of nearly all of their shares of iStorage. More than half of those shares, or approximately 5.2 million shares, went to customers of Midas Securities, World Trade, Barron Moore, and Milestone.

With respect to the transactions at issue in this proceeding, Johnson, Holt, and Zinn made the following transfers of iStorage stock on November 15, 2004:<sup>28</sup>

- Zinn transferred 2,805,000 shares to a World Trade customer, Robert Koch.
- Johnson transferred 746,000 shares to Anthony Caridi and 200,000 shares to Kimberly Koch, both World Trade customers.
- Holt transferred 760,000 shares to Midas Securities customer, Petar Mihaylov.

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<sup>27</sup> CX-4. A development stage enterprise is defined by Statement of Financial Accounting Standards No. 7 as “a company that: [d]evotes substantially all of its efforts to establishing a new business and has not yet begun planned principal operations; or [h]as begun operations, but has not generated significant revenue.” ACCOUNTING AND REPORTING BY DEVELOPMENT STAGE ENTERPRISES, Statement of Financial Accounting Standards No. 7 (Financial Accounting Standards Bd. 1975), *available at* <http://www.fasb.org/pdf/fn%207.pdf>.

<sup>28</sup> CX-11.



Robert Koch deposited his iStorage shares into his World Trade account in certificate form on November 26, 2004; Anthony Caridi deposited his iStorage shares into his World Trade account in certificate form on December 2, 2004; Kimberly Koch deposited her iStorage shares into her World Trade account in certificate form on December 20, 2004, and Petar Mihaylov deposited all of his iStorage shares into his Midas Securities account in certificate form on November 26, 2004.<sup>29</sup> None of the certificates bore a restrictive legend.

Each customer had established his or her securities account for the limited purpose of “stock deposit and liquidation.” Robert Koch opened a brokerage account at World Trade in August 2004.<sup>30</sup> Robert Koch referred Anthony Caridi to World Trade, who opened an account in November 2004.<sup>31</sup> Robert Koch also referred his sister, Kimberly Koch, to World Trade. She opened an account at World Trade in December 2004.<sup>32</sup> Petar Mihaylov opened his brokerage account at Midas Securities on December 4, 2003.<sup>33</sup>

Upon receipt of the certificates from the foregoing four customers, Midas Securities and World Trade sent them to their clearing firm, Computer Clearing Services, Inc., to be recorded in “street name” by the Depository Trust Company (“DTC”). Once iStorage’s transfer agent, Routh Stock Transfer, Inc., reissued the shares in street name to DTC, Computer Clearing Services deposited the iStorage shares in the respective customers’ accounts. Shortly thereafter, Midas Securities and World Trade began selling

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<sup>29</sup> World Trade Stip. ¶ 10; Midas Securities Stip. ¶¶ 10-11.

<sup>30</sup> World Trade Stip. ¶ 5; CX-27. He had another account open at World Trade before the account he used for this transaction.

<sup>31</sup> World Trade Stip. ¶ 6; CX-28.

<sup>32</sup> CX-29; World Trade Stip. ¶ 7.

<sup>33</sup> Midas Stip. ¶ 7; CX-40.

the shares to members of the public.<sup>34</sup> Neither Computer Clearing Services nor Routh Stock Transfer reported any restrictions on the shares.

Robert Koch sold 1,456,800 shares of iStorage stock between December 20, 2004, and January 7, 2005, for approximately \$212,000.<sup>35</sup> Anthony Caridi sold 746,000 shares between December 22, 2004, and March 7, 2005, for approximately \$71,000.<sup>36</sup> Kimberly Koch sold 108,000 shares between December 22, 2004, and March 24, 2005, for approximately \$11,300.<sup>37</sup> And Petar Mihaylov sold 760,000 shares between December 20, 2004, and February 11, 2005, for approximately \$102,000.<sup>38</sup>

## **2. Respondent Firms' Policies and Procedures for Handling Unregistered Securities**

Midas Securities and World Trade never made any inquiry about any unregistered stock they received for liquidation. Neither firm ever questioned how customers obtained the shares, nor did they perform any due diligence on the issuers.<sup>39</sup> Indeed, both firms asserted that they had neither the duty nor the means to make such inquiries. Accordingly, neither firm maintained written supervisory procedures requiring their brokers to make any inquiry when they received unregistered shares for liquidation.<sup>40</sup> If the stock certificates did not bear a restrictive legend, both firms assumed that the shares were unrestricted. They relied on their clearing firm, Computer Clearing Services, as well as the issuers' transfer agents to catch any discrepancies.

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<sup>34</sup> Tr. 253.

<sup>35</sup> World Trade Stip. ¶ 13.

<sup>36</sup> World Trade Stip. ¶ 14.

<sup>37</sup> *Id.* ¶ 15.

<sup>38</sup> Midas Securities Stip. ¶ 17.

<sup>39</sup> Tr. 299.

<sup>40</sup> Tr. 298, 324, 342.

### 3. Distribution through Midas Securities

Mihaylov, a Bulgarian national and resident, opened a brokerage account at Midas Securities on December 4, 2003.<sup>41</sup> According to his new account form, at the time he opened the account, he was 25 years old and had been employed as a “web designer” for the previous two years.<sup>42</sup> Mihaylov further stated on his new account form that his risk tolerance was high and that his investment objective was long-term growth.<sup>43</sup> Former respondents Benjamin Centeno (“Centeno”) and Jeffrey Santohigashi (“Santohigashi”) signed the new account form as the registered representatives on Mihaylov’s account. During the relevant period, Centeno and Santohigashi shared responsibility for Mihaylov’s account and split commissions from activity in his account.<sup>44</sup> Neither Centeno nor Santohigashi ever met Mihaylov.<sup>45</sup>

Although Mihaylov’s new account form indicates that he opened the account at Midas Securities to invest for the long term, Mihaylov told Centeno and Santohigashi that he actually was a stock promoter and that he intended to use the Midas Securities account to sell unregistered stock he received in connection with his stock promotion activities.<sup>46</sup> He expressed no intent to buy and hold securities despite his stated objective on the new account form.

Consistent with Mihaylov’s oral representations, once he established the account at Midas Securities, approximately 90 to 95% of his activity involved the sale of unregistered shares of bulletin board and Pink Sheets securities.<sup>47</sup> Mihaylov began selling

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<sup>41</sup> CX-40; Tr. 94-95.

<sup>42</sup> CX-40, at 1; Tr. 95.

<sup>43</sup> CX-40, at 1.

<sup>44</sup> Midas Securities Stip. ¶ 7.

<sup>45</sup> Tr. 226. Mihaylov had been referred to Centeno and Santohigashi by another customer.

<sup>46</sup> Tr. 228-29.

<sup>47</sup> Tr. 230-32.

stock within six months of opening the account.<sup>48</sup> Santohigashi testified that Mihaylov periodically would deposit a substantial number of shares for liquidation—often in the range of 500,000 to 1 million shares for a single issuer—which Midas Securities sold into the market.<sup>49</sup> All of Mihaylov’s sales were approved by Lee, Midas Securities’ President.<sup>50</sup>

In furtherance of his stock promotion activities, Mihaylov entered into a Finder’s Agreement with Midas Securities dated March 30, 2004.<sup>51</sup> Under this agreement, Midas Securities was to be paid 10% of any cash or stock Mihaylov received if he performed unspecified services for a company referred to him by Midas Securities.<sup>52</sup> The Finder’s Agreement did not require Midas Securities to do anything more than refer potential business to Mihaylov.

On November 26, 2004, Mihaylov deposited 760,000 shares of iStorage stock into his Midas Securities account in certificate form. Then, on 16 days between December 20, 2004, and February 11, 2005, Midas Securities sold all 760,000 shares into the market in agency trades. Mihaylov realized approximately \$102,000 in proceeds from these sales, which generated approximately \$2,200 in commissions. Mihaylov directed Midas Securities to wire the proceeds from these sales to him shortly after the funds were received.<sup>53</sup> No one at Midas Securities ever attempted to determine if the sales and transfers of iStorage stock qualified for any exemption from registration.

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<sup>48</sup> Tr. 230, 309.

<sup>49</sup> Tr. 231.

<sup>50</sup> Tr. 232.

<sup>51</sup> CX-43.

<sup>52</sup> *Id.*; CX-61, at 2.

<sup>53</sup> Midas Securities Stip. ¶ 17; CX-42.

#### **4. Distribution through World Trade**

Brickell was the broker responsible for Robert Koch's, Kimberly Koch's, and Anthony Caridi's accounts at World Trade. Brickell opened the accounts for Kimberly Koch and Anthony Caridi, and he handled all of their transactions at issue in this proceeding. Similarly, Brickell handled all of the transactions at issue in Robert Koch's accounts although they were opened by another broker.<sup>54</sup> Each account was established to facilitate the customers' deposit and liquidation of securities, which Brickell knew.

Between December 20, 2004, and March 24, 2005, World Trade and Brickell sold more than 2.3 million shares of iStorage stock owned by Robert Koch, Kimberly Koch, and Anthony Caridi, generating proceeds of nearly \$295,000.<sup>55</sup> No one at World Trade ever attempted to determine if the sales and transfers of iStorage stock qualified for any exemption from registration. Brickell specifically did not try to determine if any customer was an affiliate of the issuer.<sup>56</sup>

##### **(a) Robert Koch Account**

Robert Koch founded and was employed by Dailyfinancial.com, Inc. ("Daily Financial"), a stock promotion and investor relations consulting firm located in Katonah, NY.<sup>57</sup> Daily Financial also had a securities account at World Trade, as did Mihaylov. World Trade's books reflected journal transfers of stock between Daily Financial's account and Mihaylov's account.<sup>58</sup> Enforcement did not present further evidence of their relationship however.

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<sup>54</sup> World Trade Stip. ¶¶ 5-7; Tr. 317

<sup>55</sup> World Trade Stip. ¶ 12.

<sup>56</sup> Tr. 326.

<sup>57</sup> Tr. 101.

<sup>58</sup> Tr. 101.

Robert Koch sold 1,456,800 shares of iStorage stock on 14 days between December 20, 2004, and January 7, 2005, into the market in agency trades. Robert Koch realized approximately \$212,000 in proceeds from these sales, which generated approximately \$5,470 in commissions. At Robert Koch's request, World Trade wired more than \$210,000 of the sales proceeds to him shortly after the funds were received.<sup>59</sup>

**(b) Kimberly Koch Account**

Kimberly Koch, had been employed as a "personal assistant" at her brother's company, Daily Financial, for about one year at the time she opened her account at World Trade. She reported on her new account form that she had no investment experience, limited investment knowledge, less than \$15,000 in liquid net assets, and annual income of less than \$25,000.<sup>60</sup> Nonetheless, she stated that her investment objective was "speculation."<sup>61</sup> Kimberly Koch told Brickell that she wanted to use the account to deposit and liquidate securities. Brickell understood that she would be selling stock that she received in compensation for her work at Daily Financial.<sup>62</sup>

Kimberly Koch sold 108,000 shares of iStorage stock into the market in agency trades on four days between December 22, 2004, and March 24, 2005. She realized approximately \$11,300 in proceeds from these sales, which generated approximately \$300 in commissions. At her request, World Trade wired the sales proceeds to her shortly after the funds were received.<sup>63</sup>

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<sup>59</sup> World Trade Stip. ¶ 13.

<sup>60</sup> CX-29, at 4.

<sup>61</sup> *Id.* at 1; Tr. 104-05.

<sup>62</sup> Tr. 322-23.

<sup>63</sup> World Trade Stip. ¶ 15.

**(c) Anthony Caridi Account**

Anthony Caridi also worked at Daily Financial although on his new account form he indicated that he was a self-employed consultant.<sup>64</sup> As with Kimberly Koch, Brickell understood that Caridi opened the account at World Trade to deposit and sell stock he received in connection with his work at Daily Financial.<sup>65</sup> Brickell believed that he learned this from Robert Koch.<sup>66</sup>

Anthony Caridi sold all 746,000 shares of iStorage stock into the market in agency trades on 28 days between December 22, 2004, and March 7, 2005. He realized approximately \$71,000 in proceeds from these sales, which generated approximately \$3,500 in commissions. At his request, World Trade wired the sales proceeds to him shortly after the funds were received.<sup>67</sup>

**D. Midas Securities' and Lee's Supervision of Centeno and Santohigashi**

Midas Securities started business in February 2002 when Midas Trade acquired Liquid Green, LLC, a licensed but non-operating broker-dealer in Santa Monica, CA.<sup>68</sup> Midas Trade set up Midas Securities to implement its business plan to operate a service bureau in the United States for Korean brokers and customers.<sup>69</sup> At this time, Lee was hired as Midas Securities' President. Midas Trade and Lee did not intend to operate a retail brokerage business.<sup>70</sup> Indeed, Lee estimated that for the period in question he spent

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<sup>64</sup> Tr. 320; CX-28, at 3. The mailing address he supplied was Daily Financial's office address.

<sup>65</sup> Tr. 322-23.

<sup>66</sup> Tr. 323.

<sup>67</sup> World Trade Stip. ¶ 14.

<sup>68</sup> Tr. 388-90.

<sup>69</sup> Tr. 389.

<sup>70</sup> Tr. 391-92.

approximately two thirds of his time in Korea working on the development of the firm's business relationship with the Korean Securities Depository.<sup>71</sup>

Despite the fact that Midas Securities' business plan did not call for a retail operation, in or about March 2003, the President of Computer Clearing asked Lee to consider hiring several brokers and support staff who had been with Equitrade Securities Corporation ("Equitrade"), a firm which had recently ceased operations.<sup>72</sup> Computer Clearing wanted to find a new firm for the former Equitrade brokers and their customers to avoid a loss from Equitrade's closure.<sup>73</sup>

Lee then met with Don Carrig, the only full time broker at Equitrade. Don Carrig explained that the former Equitrade brokers would join Midas Securities as a group. Centeno and Santohigashi were the two other Equitrade brokers. Don Carrig told Lee that Centano worked part time and that Santohigashi had no experience as a broker although he had passed the Series 7 examination. Santohigashi had worked in Equitrade's back office.<sup>74</sup> Don Carrig further assured Lee that he need not be concerned with the supervision of the Equitrade brokers if they were to join Midas Securities because the Equitrade personnel also included a supervisory principal, Randy Wong.<sup>75</sup>

Lee agreed to hire all of the Equitrade brokers and staff.<sup>76</sup> At first, Lee intended to have Randy Wong supervise the retail brokers. However, not long after they joined Midas Securities, Wong decided to leave the firm to finish his education.<sup>77</sup> Randy Wong left Midas Securities in or about February 2004. At that point, Lee assumed responsibility

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<sup>71</sup> Tr. 398.

<sup>72</sup> Tr. 393.

<sup>73</sup> Tr. 393.

<sup>74</sup> Tr. 394.

<sup>75</sup> Tr. 394.

<sup>76</sup> Tr. 397.

<sup>77</sup> Tr. 399-400.



for the supervision of the retail brokers, including Centeno and Santohigashi. Under Midas Securities' Supervisory Procedures Manual, Lee was designated the firm's Chief Supervisory Officer.<sup>78</sup>

Nonetheless, Lee conceded that he made no effort to supervise Centeno and Santohigashi. Indeed, Lee testified that he neither understood the nature of their business nor knew what due diligence, if any, they conducted upon receipt of unregistered shares for liquidation.<sup>79</sup> Moreover, Lee could not have provided reasonable supervision of the brokers' activities given the substantial amount of time he spent away from the office. By his own estimate, he spent approximately two thirds of his time in Korea during the applicable period.

Centeno and Santohigashi testified that no one supervised them. More specifically, both testified that they did not need authorization from anyone at Midas Securities to sell stock from a customer's account and that the firm placed no restrictions on their trading activities involving Bulletin Board and Pink Sheet securities.<sup>80</sup> Centeno testified that Lee never supervised his activities.<sup>81</sup> Santohigashi likewise testified that his activities at Midas Securities were unrestricted and that Lee did very little as his supervisor.<sup>82</sup> Santohigashi further testified that Lee did not require anyone else at the firm to supervise his activities.<sup>83</sup>

Nonetheless, Lee disclaimed all supervisory responsibility for Centeno and Santohigashi. Lee claimed that he hired William Cantrell to replace Randy Wong and

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<sup>78</sup> CX-52, at 12; Tr. 442.

<sup>79</sup> Tr. 436, 477.

<sup>80</sup> Tr. 303.

<sup>81</sup> Tr. 303-04.

<sup>82</sup> Tr. 245-46.

<sup>83</sup> Tr. 246.

supervise Centeno and Santohigashi.<sup>84</sup> However, Centeno and Santohigashi each specifically contradicted Lee's claim. Cantrell testified that he was hired to help with Midas Securities' back office, including recordkeeping and support services, and that Lee specifically had rejected Cantrell's offer to become a supervisor because Lee did not want to pay him for those added responsibilities.<sup>85</sup> Ultimately, the only supervisory responsibility Cantrell assumed was the approval of new account forms. Lee delegated this limited function because of his frequent and lengthy trips to Korea.<sup>86</sup>

Lee sought to discredit Centeno and Santohigashi by accusing them of fabricating their testimony to protect Cantrell from any claims that he failed to adequately supervise the brokers. Lee testified that the three were friends and that they may have held a grudge against him because he had fired Cantrell and Centeno.<sup>87</sup> However, the Hearing Panel did not detect any bias and found their testimony credible. In particular, the Hearing Panel found Cantrell to be far more credible than Lee on the subject of Cantrell's duties and responsibilities at Midas Securities. The Hearing Panel did not find credible Lee's claim that Cantrell was the broker's designated supervisor. All of the other evidence in the record shows that Lee never delegated supervisory responsibility for the day-to-day supervision of the brokers to anyone else at Midas Securities after Randy Wong resigned. The Hearing Panel further found that Lee took no steps to supervise Centeno and Santohigashi during the period in question.

**E. Midas Securities' Written Supervisory Procedures did not Require any Inquiry Regarding the Status of Unregistered Securities**

In addition to not supervising the firm's brokers, Lee did not implement written supervisory procedures to prevent and detect violations of Section 5 of the Securities

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<sup>84</sup> Tr. 419-20.

<sup>85</sup> Tr. 168-70.

<sup>86</sup> Tr. 170-71.

<sup>87</sup> Tr. 420.

Act.<sup>88</sup> Midas Securities' Supervisory Procedures Manual contained no guidance on the firm's and the brokers' responsibility to assure that it was permissible to sell unregistered stock. This was not surprising because Lee took the position that he would not have allowed the brokers to make such an inquiry.<sup>89</sup> According to Lee, the brokers' role was limited to gathering the needed paperwork to send the unregistered shares to the clearing firm, and it was the clearing firm's responsibility to determine if the shares could be traded.

**F. World Trade's, Michel's, and Adams' Supervision of Brickell**

Michel and Adams were responsible for Brickell's supervision. Adams testified that he supervised all of World Trade's registered brokers in 2004, including Brickell.<sup>90</sup> And Michel, World Trade's President, testified that he and Adams were jointly responsible for the supervision of the firm's registered representatives.<sup>91</sup> In addition, they were jointly responsible for sales of restricted stock. They both reviewed monthly account statements and blotters to monitor the activity in customer accounts, and Adams received copies of all stock certificates World Trade received for deposit into customer accounts.<sup>92</sup>

Despite their broad supervisory responsibilities, Michel and Adams each testified that he did not consider it within his responsibility to conduct an inquiry to determine the tradability of unrestricted stock. Accordingly, neither of them asked Brickell if he had conducted such an inquiry when he received unregistered certificates for liquidation, as in

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<sup>88</sup> Midas Securities' Supervisory Procedures Manual designated Lee as the principal responsible for the firm's written supervisory procedures, and Lee admitted during his on-the-record interview on September 25, 2007, that he did not delegate this responsibility to anyone else. Tr. 441.

<sup>89</sup> Tr. 119.

<sup>90</sup> Tr. 340. Michel and Adams were the majority owners of World Trade. Michel owned 52%, and Adams owned 24%. Another entity owned the remaining 24% interest. Tr. 359.

<sup>91</sup> Tr. 363. Michel also testified that in 2004 he filled in as the firm's chief compliance officer. Tr. 361, 365.

<sup>92</sup> Tr. 341, 364.

this case. As did Lee at Midas Securities, Michel and Adams assumed that all shares without a restrictive legend could be freely traded.<sup>93</sup> Thus, they took no steps to investigate any of the facts and circumstances surrounding a customer's acquisition of unregistered securities; they left it to the clearing firm to determine if the shares they received for liquidation could be sold without violating the registration requirements of the Securities Act.

**G. World Trade's Written Supervisory Procedures did not Require any Inquiry Regarding the Status of Unregistered Securities**

Michel also was responsible for World Trade's written supervisory procedures. The firm's Supervisory Procedures Manual, which Michel authored along with his management staff, stated that he was responsible for establishing "supervisory systems and overall oversight of compliance functions."<sup>94</sup>

World Trade's Supervisory Procedures Manual did not require anyone at the firm to make any inquiry to determine whether unregistered shares could be sold without violating Section 5 of the Securities Act. No matter what the surrounding facts and circumstances, World Trade did not require its brokers to ask its customers for any information about the shares they desired to liquidate.

**IV. CONCLUSIONS OF LAW**

**A. World Trade, Midas Securities, and Brickell Violated NASD Conduct Rule 2110 by Selling Unregistered Securities in Violation of Section 5 of the Securities Act**

**1. Enforcement Established a Prima Facie Case for a Violation of Section 5 of the Securities Act**

Securities Act Section 5(a) prohibits any person, directly or indirectly, from selling a security in interstate commerce unless a registration statement is in effect as to

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<sup>93</sup> Tr. 342-44.

<sup>94</sup> CX-51, at 15; Tr. 365.

the offer and sale of that security or there is an applicable exemption from the registration requirements. Securities Act Section 5(c) prohibits the offer or sale of a security unless a registration statement as to such security has been filed with the SEC, or an exemption is available.<sup>95</sup> The purpose of the registration requirements is to “protect investors by promoting full disclosure of information thought necessary to informed investment decisions.”<sup>96</sup> A violation of Section 5 of the Securities Act constitutes a violation of NASD Conduct Rule 2110.<sup>97</sup>

To establish a *prima facie* case of a violation of Sections 5(a) and 5(c) of the Securities Act, Enforcement must show that (1) no registration statement was in effect as to the securities; (2) Respondents sold or offered to sell these securities; and (3) interstate transportation or communication were used in connection with the sale or offer of sale.<sup>98</sup> A showing of scienter is not required because “[t]he Securities Act of 1933 imposes strict liability on offerors and sellers of unregistered securities.”<sup>99</sup>

The parties stipulated to facts sufficient to prove a *prima facie* case—World Trade, Midas Securities, and Brickell sold and transferred unregistered shares of iStorage stock using means or instruments of transportation or communication in interstate commerce in connection with those transactions. None of the iStorage shares was covered by registration statements filed pursuant to Section 5 of the Securities Act.<sup>100</sup>

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<sup>95</sup> 15 U.S.C. § 77e(a) and (c); see also *Jacob Wonsover*, 54 S.E.C. 1, 8 (1999), *petition denied*, 205 F.3d 408 (D.C. Cir. 2000).

<sup>96</sup> *SEC v. Ralston Purina Co.*, 346 U.S. 119, 124 (1953).

<sup>97</sup> *Alvin W. Gebhart*, Exchange Act Release No. 53136, 2006 SEC LEXIS 93, at \*54 n.75 (Jan. 18, 2006) *rev'd and remanded in part on other grounds sub. nom Gebhart v. SEC*, 2007 U.S. App. LEXIS 27183 (9<sup>th</sup> Cir. Nov. 21, 2007) (“Further, because we have consistently held that a violation of a Commission or NASD rule or regulation is inconsistent with just and equitable principles of trade, we find that the Gebharts’ sale of the unregistered MHP notes also constitutes a violation of NASD Conduct Rule 2110.”); *Stephen J. Gluckman*, Exchange Act Release No. 41628, 1999 SEC LEXIS 1395 (July 20, 1999); see *William H. Gerhauser*, 1998 SEC LEXIS 2402 (Nov. 4, 1998).

<sup>98</sup> *Gebhart*, at \*53; *SEC v. Cont'l Tobacco Co.*, 463 F.2d 137, 155 (5<sup>th</sup> Cir. 1972).

<sup>99</sup> *Gebhart*, at \*53 n.73 (quoting *Swenson v. Engelstad*, 626 F.2d 421, 424 (5<sup>th</sup> Cir. 1980)).

<sup>100</sup> World Trade Stip. ¶ 16; Midas Securities Stip. ¶ 18.

## 2. World Trade, Midas Securities, and Brickell Failed to Prove that the Transactions were Exempt from Registration

Once Enforcement presents a *prima facie* case, the burden shifts to the Respondents to prove that the transactions qualify for exemption from registration.<sup>101</sup> “Exemptions from registration are affirmative defenses that must be established by the person claiming the exemption.”<sup>102</sup> Further, evidence in support of an exemption must be “explicit, exact, and not built on mere conclusory statements.”<sup>103</sup>

World Trade, Midas Securities, and Brickell did not meet their burden of proving that the iStorage shares were exempt from the registration requirements of Section 5 of the Securities Act. They admitted that they did not ascertain whether any particular exemption from registration was available before the sales took place because they did not consider it their responsibility to do so. Accordingly, the Hearing Panel finds that, because World Trade, Midas Securities, and Brickell failed to establish that the iStorage stock was exempt from registration, they violated Section 5 of the Securities Act and thereby violated NASD Rule 2110.<sup>104</sup>

Respondents’ reliance on Section 4(4) of the Securities Act, which exempts “brokers’ transactions executed upon customers’ orders on any exchange or in the over-the-counter market but not the solicitation of such orders” from the registration requirements of Section 5 of the Securities Act, is misplaced. “A registered representative relying on the Section 4(4) exemption must make whatever inquiries are necessary to

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<sup>101</sup> *Gebhart*, at \*53; *SEC v. Cavanagh*, 1 F. Supp. 2d 337, 361-363 (S.D.N.Y.), *aff’d*, 155 F.3d 129 (2d Cir. N.Y. 1998); *John A. Carley*, Initial Decision Rel. No. 292, 2005 SEC LEXIS 1745, at \*87 (July 18, 2005), *aff’d*, 2008 SEC LEXIS 222 (Jan. 31, 2008) (citing *Swenson v. Engelstad*, 626 F.2d 421, 425 (5<sup>th</sup> Cir. 1980)).

<sup>102</sup> *John A. Carley*, Exchange Act Release No. 57246, 2008 SEC LEXIS 222, at \*24 (Jan. 31, 2008).

<sup>103</sup> *Robert G. Weeks*, Securities Act Release No. 8313, 2003 SEC LEXIS 2572, \*42 n.34 (Oct. 23, 2003).

<sup>104</sup> *Dep’t of Enforcement v. Morgan Keegan & Co.*, No. CAF040073, 2006 NASD Discip. LEXIS 24, at \*40 (July 21, 2006).

determine that the transaction is not part of an unlawful distribution.”<sup>105</sup> Further, a broker may not delegate his responsibility completely to others and thereby relieve himself of all liability for violations of the registration requirements of Section 5 of the Securities Act, as the Respondents did in this case.<sup>106</sup> Accordingly, World Trade, Midas Securities, and Brickell did not meet their burden of proving that they were entitled to rely on the brokers’ exemption contained in Section 4(4) of the Securities Act.

**B. World Trade, Midas Securities, Lee, and Michel Failed to Develop and Maintain Adequate Supervisory Procedures**

Conduct Rule 3010(a) requires firms to “establish and maintain a system to supervise the activities of each registered representative, registered principal, and other associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable NASD Rules.” An adequate supervisory system must guard against the illegal sale of unregistered securities.<sup>107</sup> Under Rule 3010(b), these systems must be documented in the firm’s written supervisory procedures. Further, the procedures must be tailored to the specific nature of the firm’s business.<sup>108</sup>

Midas Securities and World Trade failed to establish and maintain adequate supervisory systems to achieve compliance with the requirements of Section 5 of the Securities Act although a substantial proportion of their business involved the liquidation

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<sup>105</sup> *John A. Carley*, Initial Decision Release No. 292, 2005 SEC LEXIS 1745, at \*108 (July 18, 2005), *aff’d*, 2008 SEC LEXIS 222 (Jan. 31, 2008).

<sup>106</sup> *Jacob Wonsover*, Exchange Act Release No. 41123, 1999 SEC LEXIS 1, at \*15 (Mar. 1, 1999), *aff’d*, *Wonsover v. SEC*, 205 F.3d 408, (D.C. Cir 2000) (finding that registered representative was not relieved of his obligation to explore whether shares are freely tradable “simply because the transfer agent and Restricted Stock Department eventually cleared the stock”); *Robert G. Leigh*, 50 S.E.C. 189, 194 (2008) (finding that, “as the courts and this Commission have held, the transfer agent’s willingness to reissue the certificates without restrictive legends did not relieve [the registered representative] of his obligation to investigate”).

<sup>107</sup> *Sales of Unregistered Securities by Broker-Dealers*, 1971 SEC LEXIS 19, at \*4–6.

<sup>108</sup> NASD Membership and Registration Rule Interpretive Material (“IM”) 3010-1, *available at* [http://finra.complinet.com/en/display/display\\_main.html?rbid=2403&element\\_id=3718](http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=3718).

of shares of Pink Sheet and Bulletin Board stocks deposited in certificate form. Rather than develop any procedures in this area, the firms relied upon their clearing firm and the issuers' transfer agents to undertake any necessary inquiry regardless of the circumstances surrounding the transactions.

Both firms' supervisory systems lacked adequate procedures governing the sale of large quantities of penny stock that lacked a trading history, such as was the case with iStorage. Neither firm had procedures for determining whether stock should be considered restricted, or for addressing the circumstances under which its registered representatives should inquire into the registration or exemption status of shares in customer accounts. Specifically, neither firm had written procedures that detailed the circumstances under which the firm's registered representatives were obligated to inquire as to how and when their customers acquired the shares they sought to liquidate. Accordingly, the Hearing Panel finds that Midas Securities, World Trade, Lee, and Michel violated Conduct Rules 3010(a), 3010(b), and 2110. They failed to establish and maintain a system and written procedures to supervise the activities of the registered representatives who sold unregistered securities. Conduct Rule 3010(a) requires that the firms' written supervisory procedures state the specific steps needed to achieve compliance with Section 5 of the Securities Act, as well as set out what conduct is prohibited.<sup>109</sup>

**C. World Trade, Midas Securities, Adams, Michel, and Lee Failed to Reasonably Supervise Persons Selling Unregistered iStorage Shares**

A supervisor is responsible for "reasonable supervision," a standard that "is determined based on the particular circumstances of each case."<sup>110</sup> The SEC has held that

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<sup>109</sup> *John A. Chepak*, 54 S.E.C. 502, 505, 2000 SEC LEXIS 97, at \*7 (2000); *A.S. Goldmen & Co.*, Exchange Act Release No. 44328, 2001 SEC LEXIS 966, at \*31-32 (May 21, 2001).

<sup>110</sup> *Christopher J. Benz*, 52 S.E.C. 1280, 1284 (1997), *petition for review denied*, 168 F.3d 478 (3d Cir. 1998) (table).



“[r]ed flags and suggestions of irregularities demand inquiry as well as adequate follow-up and review.”<sup>111</sup> A failure to supervise is a violation of NASD Rules 3010(a) and 2110.<sup>112</sup>

Numerous red flags indicated that Brickell, Centeno, and Santohigashi could have been engaged in the illegal sales of unregistered securities. In light of these factors, Michel, Adams, and Lee should have followed up to assure that an exemption from registration applied to the sales of unregistered iStorage shares.<sup>113</sup>

At World Trade, Michel and Adams reviewed monthly account statements and blotters to monitor the activity in customer accounts, and Adams received copies of all stock certificates deposited into customer accounts. Thus, Michel and Adams had notice that Brickell’s customers, Robert Koch, Kimberly Koch, and Anthony Caridi, had deposited large quantities of iStorage shares for immediate liquidation. They also knew that iStorage was a penny stock that had not traded publicly before Brickell’s customers deposited their shares with World Trade. Michel and Adams further knew that Brickell’s customers began selling the stock and wiring the sales proceeds from those sales from their accounts immediately after depositing the stock. Indeed, their sales activities were consistent with the vast majority of World Trade’s business. Nonetheless, neither Michel nor Adams recognized these factors as red flags, and they failed to conduct any inquiry regarding unregistered sales of iStorage stock. Particularly significant is the fact that neither Michel nor Adams did anything to investigate the source of the stock despite the

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<sup>111</sup> *Benz*, 52 S.E.C. 1280, 1283 n.13 (quoting cases); *see also Michael T. Studer*, Exchange Act Rel. No. 50543A, 2004 SEC LEXIS 2828, at \*23 (Nov. 30, 2004), *aff’d*, 260 Fed. Appx. 342, 2008 U.S. App. LEXIS 837 (2d Cir. 2008).

<sup>112</sup> *Dep’t of Enforcement v. Ronald Pellegrino*, No. C3B050012, 2008 FINRA Discip. LEXIS 10, at \*47 (N.A.C. Jan. 4, 2008).

<sup>113</sup> *Cf. George Kolar*, 55 S.E.C. 1009, 1016 (2002) (“Decisive action is necessary whenever supervisors are made aware of suspicious circumstances, particularly those that have an obvious potential for violations.”). *Cf. also Michael H. Hume*, 52 S.E.C. 243, 1995 SEC LEXIS 983, at \*12 (April 17, 1995) (When a supervisor discovers reds flags, indicating irregularities, he cannot “discharge his supervisory obligations simply by relying on the unverified representations of employees.”).

fact that they knew that Brickell had not made such an inquiry. World Trade's business practice was to avoid undertaking any responsibility for verifying the status of stock deposited for liquidation. The Hearing Panel finds that Michel and Adams abdicated all responsibility for assessing Brickell's sales activities in connection with the liquidation of iStorage stock. Their reliance on the word of iStorage's transfer agent or World Trade's clearing firm was a "woefully inadequate" method for assessing Brickell's activities.<sup>114</sup>

For these reasons, the Hearing Panel concludes that Michel and Adams, and World Trade acting through them, failed to reasonably supervise Brickell, in violation of NASD Conduct Rules 3010(a) and 2110.<sup>115</sup>

At Midas Securities, Lee likewise took no steps to follow up on red flags that should have caused him to question the activity in Mihaylov's account. Perhaps most significantly, Lee knew from his approval of the Finder's Agreement between Midas Securities and Mihaylov that Mihaylov was engaged in the business of promoting stock for penny stock issuers, which paid him for his services with shares of their stock. Nonetheless, Lee did nothing to supervise Centeno and Santohigashi. Although, Midas Securities' written procedures required that Lee approve every sale of potentially restricted stock, he did not question the activity in Mihaylov's account. Further, Lee prohibited others at Midas Securities, including Centeno and Santohigashi, from making an inquiry regarding the origin of the iStorage shares Mihaylov deposited for liquidation.

Lee abdicated all responsibility for Centeno's and Santohigashi's supervision. Even though Lee was absent from the office at least 50% of the time, he did not effectively delegate his supervisory responsibility to another qualified supervisor.

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<sup>114</sup> Cf. *Carley*, 2008 SEC LEXIS 222, at \*64 (finding that supervisor's reliance on unverified representations of their subordinates is a "woefully inadequate" method of assessing account activity") (citing *Quest Capital Strategies*, 55 S.E.C. 362, 374 (2001)).

<sup>115</sup> See *Dep't of Enforcement v. Castle Sec. Corp.*, 2004 NASD Discip. LEXIS 1 at \*19-23 (N.A.C. Feb. 19, 2004).

Instead, he left Centeno and Santohigashi unsupervised, as they testified. Accordingly, no one at Midas Securities reviewed the sales of the unregistered iStorage shares from Mihaylov's account to determine if an exemption from registration applied to the sales.

For these reasons, the Hearing Panel concludes that Lee, and Midas Securities acting through Lee, failed to reasonably supervise Centeno and Santohigashi, in violation of NASD Conduct Rules 3010(a) and 2110.

## V. SANCTIONS

### A. Selling Unregistered Securities

The FINRA Sanction Guidelines ("Guidelines") for the sale of unregistered securities provide for a fine of \$2,500 to \$50,000 and consideration of a suspension or bar in egregious cases.<sup>116</sup> The Guidelines further set forth three specific considerations for such violations: (1) whether the respondent attempted to comply with an exemption from registration; (2) whether respondent sold before effective date of registration statement; and (3) share volume and dollar amount of transactions involved.<sup>117</sup> In addition, the Hearing Panel considered the Principal Considerations in Determining Sanctions.<sup>118</sup>

The Hearing Panel found numerous aggravating factors. Foremost, the Hearing Panel found that the Respondents willfully violated Section 5 of the Securities Act by failing to make any inquiry regarding the status of the iStorage shares. The Respondents did not undertake the "reasonable inquiry" required to rely on the brokers' exemption found in Section 4(4) of the Securities Act. As the SEC made clear in a release in 1962,

The amount of inquiry called for necessarily varies with the circumstances of particular cases. A dealer who is offered a modest amount of a widely traded security by a responsible customer, whose lack

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<sup>116</sup> FINRA Sanction Guidelines 26 (2007), available at [www.finra.org/oho](http://www.finra.org/oho) (then follow "Enforcement" hyperlink to "Sanction Guidelines").

<sup>117</sup> *Id.*

<sup>118</sup> *Id.* at 6-7.

of relationship to the issuer is well known to him, may ordinarily proceed with considerable confidence. On the other hand, when a dealer is offered a substantial block of a little-known security ... where the surrounding circumstances raise a question as to whether or not the ostensible sellers may be merely intermediaries for controlling persons or statutory underwriters, then searching inquiry is called for.<sup>119</sup>

Here, however, the Respondents were not presented with sales of modest amounts of stock or a widely traded security. As discussed in detail above, iStorage had not yet traded publicly when the various customers deposited the stock with World Trade and Midas Securities for liquidation. In addition, there were ample circumstances that raised questions about whether the selling customers were intermediaries for controlling persons or statutory underwriters. Accordingly, a “searching inquiry” was called for under all of the facts and circumstances presented here. However, World Trade and Midas Securities employed a reckless business model that called for no inquiry when selling unregistered securities, relying instead on their clearing firm and iStorage’s transfer agent to clear the stock for sale.<sup>120</sup>

The Hearing Panel also noted that a substantial number of shares were sold to members of the public. World Trade sold more than 2.3 million shares, and Midas Securities sold 760,000 shares. The total sales proceeds equaled \$396,300. Clearly, the volume of sales and the dollar amount involved created the potential for significant harm to investors.

For the foregoing reasons, and in the absence of any mitigating factors, the Hearing Panel will impose the following sanctions for Brickell’s and the firms’ violations of Section 5 of the Securities Act and NASD Conduct Rule 2110. World Trade and Brickell will be fined \$15,000 each, Brickell will be suspended in all capacities for 30 business days, and Midas Securities will be fined \$30,000.

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<sup>119</sup> *Distribution by Broker-Dealers of Unregistered Securities*, Securities Act Rel. No. 4445 (Feb. 2, 1962).

<sup>120</sup> *Wonsover v. SEC*, 205 F.3d. at 415.

The Hearing Panel determined that a higher fine was warranted in the case of Midas Securities because it had been sanctioned for selling unregistered stock just six weeks before the conduct in question in this proceeding.<sup>121</sup> In December 2004, Midas Securities and Lee were sanctioned in a Letter of Acceptance, Waiver and Consent (“AWC”) for violating Section 5 of the Securities Act in connection with the sale of unlegended shares of Midas Trading.<sup>122</sup> Lee submitted the AWC to the staff on November 10, 2004—shortly before the violative activity in this case began—accompanied by a letter in which he represented that Midas Securities undertook corrective actions “to prevent any future sale of unregistered securities.”<sup>123</sup> Lee represented that:

- “The firm has done a thorough review of procedures for the acceptance of restricted and Rule 144 securities.”
- “The firm will obtain an expert opinion such as outside legal counsel when it is unclear if securities are unregistered or registered.”<sup>124</sup>

Despite Midas Securities’ commitment to undertake corrective measures, it did not change its procedures for compliance with the registration requirements of Section 5 of the Securities Act, and it did not seek outside advice when three weeks later it accepted the deposit of Mihaylov’s iStorage stock certificate for liquidation.

## **B. Deficient Supervisory Procedures and Supervision**

The Guidelines for failing to supervise recommend, in egregious cases, suspending the responsible individual in any or all capacities for up to two years or imposing a bar. The Guidelines further recommend a fine of \$5,000 to \$50,000, which

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<sup>121</sup> General Principles Applicable to all Sanctions No. 2, FINRA Sanction Guidelines 2 (“Adjudicators should consider imposing more severe sanctions when a respondent’s disciplinary history includes (a) past misconduct similar to that at issue; or (b) past misconduct that evidences disregard for regulatory requirements, investor protection, or commercial integrity.”).

<sup>122</sup> CX-1.

<sup>123</sup> CX-2.

<sup>124</sup> *Id.*

amount may be increased by the amount of the respondent's financial benefit.<sup>125</sup> In a case against a member firm involving systemic supervision failures, the Sanction Guidelines recommend suspending the firm with respect to any or all activities or functions for up to two years or expulsion of the firm.<sup>126</sup>

The Guidelines for deficient written supervisory procedures provide for fines ranging from \$1,000 to \$25,000.<sup>127</sup> In egregious cases, the Guidelines recommend suspending the firm with respect to any or all relevant activities for up to 30 business days and thereafter until the supervisory procedures are amended to conform to rule requirements.<sup>128</sup> The Guidelines for deficient supervisory procedures provide two considerations in determining the appropriate sanctions: (1) whether the deficiencies allowed violative conduct to occur or to escape detection; and (2) whether the deficiencies made it difficult to determine the individual or individuals responsible for specific areas of supervision or compliance. The second consideration does not apply here or serve to aggravate the firms' misconduct.

In determining the appropriate sanctions, the Hearing Panel also took into account the principal considerations applicable to all violations.<sup>129</sup>

In applying the Guidelines to the conduct at issue, the Hearing Panel determined to aggregate the Respondents' supervisory violations because they stemmed from a common problem at each firm—their decision to rely on the clearing firm and iStorage's transfer agent to determine whether the shares could be traded without registration rather than exercise any independent inquiry. The Hearing Panel finds that these were serious

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<sup>125</sup> FINRA Sanction Guidelines 108.

<sup>126</sup> *Id.*

<sup>127</sup> *Id.* at 109.

<sup>128</sup> *Id.*

<sup>129</sup> *Id.* 6-7.

violations and that World Trade and Midas Securities knowingly failed to implement procedures tailored to their business. As previously noted, both firms omitted any policies and procedures governing their brokers' duty to ascertain whether unregistered securities could be traded without violating Section 5 of the Securities Act. These omissions were not the result of oversight. Both firms and their respective responsible principals determined that there was no need for such policies and procedures. Indeed, Lee at Midas Securities went so far as to ban the firm's registered representatives from asking any questions regarding the origin of the stock deposited for liquidation. Further, Michel, Adams, and Lee failed to conduct a sufficient inquiry into the iStorage transactions. Furthermore, they failed to recognize the red flags in the accounts of the customers selling iStorage shares.

In addition, the Hearing Panel found the nature, extent, size, and character of the transactions aggravating. As discussed in detail above, the firms sold more than 3 million shares of unregistered iStorage stock to the public, and the total sales proceeds equaled \$396,300. This activity posed a significant risk of harm to investors. The Hearing Panel also found aggravating that the Respondents sought to shift the blame to others instead of accepting responsibility for their conduct.

Taking all of the foregoing factors into careful consideration, the Hearing Panel finds that the following sanctions are warranted: World Trade will be fined \$15,000; Midas Securities will be fined \$25,000; Michel will be fined \$15,000 and suspended in all principal capacities for 45 days; Lee will be fined \$20,000 and suspended in all principal capacities for two years; and Adams shall be fined \$10,000 and suspended in all principal capacities for 30 business days.<sup>130</sup>

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<sup>130</sup> As discussed above, the Hearing Panel took into consideration Midas Securities and Lee's prior disciplinary history in concluding that greater sanctions were needed to prevent future misconduct and to protect the investing public.

## **VI. ORDER**

For violating NASD Conduct Rule 2110 by selling unregistered securities, World Trade and Brickell are fined \$15,000 each, Brickell is suspended from associating with any member firm in any capacity for 30 business days, and Midas Securities is fined \$30,000. For violating NASD Conduct Rules 3010(a), 3010(b), and 2110 by failing to establish and maintain a system to supervise the activities of each registered representative, registered principal, and other associated person that is reasonably designed to achieve compliance with Section 5 of the Securities Act, and for failing to supervise the registered representatives selling unregistered iStorage shares, World Trade is fined an additional \$15,000 (for a total of \$30,000), Midas Securities is fined an additional \$25,000 (for a total of \$55,000), Michel is fined \$15,000 and suspended in all principal capacities for 45 days, Lee is fined \$20,000 and suspended from associating with any member firm in any principal capacity for two years, and Adams is fined \$10,000 and suspended from associating with any member firm in any principal capacity for 30 business days.

The Respondents are jointly and severally ordered to pay costs in the amount of \$4,207.13, which includes a \$750 administrative fee and the cost of the hearing transcript. The fines and costs shall be payable on a date set by FINRA, but not less than 30 days after this decision becomes FINRA's final disciplinary action in this matter.

If this decision becomes FINRA's final disciplinary action, the suspensions shall run as follows:

Brickell's suspension shall begin at the opening of business on July 6, 2009, and end at the close of business on August 14, 2009.

Michel's suspension shall begin at the opening of business on July 6, 2009, and end at the close of business on August 19, 2009.



Lee's suspension shall begin at the opening of business on July 6, 2009, and end at the close of business on July 5, 2011.

Adams' suspension shall begin on the opening of business on July 6, 2009, and end at the close of business on August 14, 2009.<sup>131</sup>

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Andrew H. Perkins  
Hearing Officer  
For the Extended Hearing Panel

Copies to:

Irving M. Einhorn, Esq. (electronic and first-class mail)  
Midas Securities, LLC (FedEx, next day delivery, and first-class mail)  
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Jason Troy Adams (FedEx, next day delivery, and first-class mail)  
Frank Edward Brickell (FedEx, next day delivery, and first-class mail)  
Jay S. Lee (FedEx, next day delivery, and first-class mail)  
Rodney Preston Michel (FedEx, next day delivery, and first-class mail)  
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David R. Sonnenberg, Esq. (electronic mail)

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<sup>131</sup> The Hearing Panel has considered and rejects without discussion all other arguments of the parties.