FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. EDWARD S. BROKAW (CRD No. 1162997), Respondent.	Disciplinary Proceeding No. 2007007792902 **Extended Hearing Panel Decision** Hearing Officer – SNB June 11, 2010

For engaging in market manipulation, in violation of Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and NASD Rules 2120 and 2110, Respondent is barred in all capacities.[1] In light of the bar, no further sanctions are imposed for Respondent's failure to ensure the accuracy of order tickets, in violation of Rules 3110 and 2110.

Appearances

Lane A. Thurgood, Esq., Washington, DC, and Margaret M. Tolan, Esq., New York, NY, for the Department of Enforcement.

Kevin T. Hoffman, Esq., Greenwich, CT, for Respondent.

DECISION

I. Procedural History

On December 12, 2008, the Department of Enforcement ("Enforcement") filed a three-count Complaint against Respondent Edward S. Brokaw ("Respondent"). Count One of the Complaint alleges that Respondent manipulated the price of Monogram Biosciences, Inc.

[1] In light of this finding as to Count one of the Complaint, the alternative charge that Respondent failed to make an adequate inquiry regarding the trading instructions in Count two of the Complaint is dismissed.

("MGRM") on behalf of his client, hedge fund principal KT, in violation of Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and NASD Rules 2120 and 2110, or aided and abetted violations of these provisions. Count Two alleges, in the alternative to Count one, that Respondent failed to make an adequate inquiry regarding the propriety of KT's trading instructions, in violation of NASD Rule 2110. Count Three alleges that Respondent failed to ensure the accuracy of order tickets associated with the sales referenced in the first and second counts of the Complaint, in violation of NASD Rules 3110 and 2110.[2]

Respondent filed an Answer to the Complaint, denying the allegations and requesting a hearing. The Extended Hearing Panel, composed of a FINRA Hearing Officer and two former members of the District 10 Committee, held the hearing on this matter in New York, New York on six hearing days.[3] At the hearing, Enforcement called eight witnesses – two sales traders, two equity traders, two sales assistants, one compliance officer, and one supervisor. Respondent called one witness – the customer who placed the orders at issue in the case, and he testified on his own behalf. Enforcement and Respondent submitted post-hearing briefs on January 8, 2010, and January 28, 2010, respectively.

[2] NASD consolidated with the member regulation and enforcement functions of NYSE Regulation in July 2007 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 consolidated rules became effective on December 15, 2008. See Regulatory Notice 08-57 (Oct. 2008). This decision refers to and relies on the Rules that were in effect at the time of Respondent's alleged misconduct. In addition, because Enforcement filed the Complaint before December 15, 2008, NASD's procedural rules govern this proceeding. The applicable rules are available at www.finra.org/rules.

[3] References to the testimony set forth in the transcripts of the Hearing are designated as "Tr. __," with the appropriate page number. References to the exhibits provided by Enforcement are designated as "CX-___," and Respondent's exhibits are designated as "RX-___." Joint exhibits are designated as "JX-_," Respondent's exhibits RX-2-46, Enforcement's exhibits CX-1, 2, 4, 6, 7, 9-13, 21-22, 24-31, 34-37, 39-45, 47-57, 59-69, 70-72, and JX-1 were admitted into the record. Tr. 1022, 1025-26, 1028, 1428, 1681-82.

II. Respondent

Respondent has been registered as a General Securities Representative with various member firms since March 1983. From January 13, 2001, through June 28, 2006, he was registered with Deutsche Bank Securities, Inc. ("Deutsche Bank" or the "Firm") and was employed in its Greenwich, Connecticut, office. CX-1 p. 2; Tr. 1448-51. Respondent is currently registered with another FINRA member firm. CX-1 p. 1.

III. Discussion

This case involves the issue of whether Respondent engaged in market manipulation when he placed orders to sell MGRM securities near the open and close of the market on three successive trading days, on behalf of a hedge fund client, (the "Fund"), which was controlled by KT. Based principally upon tape-recorded conversations between Respondent and his Firm's sales traders, Enforcement alleges that Respondent placed orders to sell MGRM shares at the open and the close of the market for the purpose of increasing the value of MGRM contingent value rights ("CVRs")[4] that were held by both Respondent and KT.[5] Enforcement also alleges that Respondent failed to ensure the accuracy of the order tickets associated with these sales.

A. Background on KT, MGRM, and the CVRs

KT was Respondent's longtime friend and former colleague. Tr. 1035, 1091, 1451-52. At the time at issue in this case, KT was the principal of the Fund. KT used brokers at various firms to execute trades for the Fund; a portion of this business went to Respondent and Deutsche

[4] A CVR is a commitment by an issuer to pay additional cash or securities to CVR holders, contingent on the occurrence of a specific event, such as in this case the issuer's share value falling below a certain level by a specified time.

[5] The Complaint alleges, in the alternative, that Respondent aided and abetted KT's manipulation of MGRM shares.

Bank. The Fund and KT were among Respondent's largest and most important client relationships.[6] Tr. 1038, 1455-56.

At the time relevant to this proceeding, the Fund held approximately 18.5 million of the 64.8 million total MGRM CVRs outstanding. CX-34 p. 1, RX-8 p. 1; Tr. 1058, 1062. The CVRs were created in December 2004 in connection with the merger of Aclara BioSciences, Inc. and ViroLogic, Inc.[7] Tr. 1051-52. The merged entity changed its name to MGRM and issued one CVR for each share of Aclara held just prior to the merger. CX-27; Tr. 1340. The Fund received 8 million CVRs in connection with this original issuance, and purchased 10.5 million additional CVRs in the secondary market. Tr. 1053, 1056.

The CVRs were to be valued during a 15-day pricing period scheduled to occur 18 months after the merger, beginning on May 19, 2006, and ending on June 9, 2006. CX-26 – 31, RX-8 p. 2; Tr. 1053-56. The value of the CVRs would be established based upon the volume weighted average price ("VWAP") of MGRM shares traded during the pricing period. Id.; Tr. 734-35. The VWAP for each day of the pricing period would constitute 1/15 of the final VWAP for determining the value of the CVRs, regardless of the volume on that day. Tr. 1261-62.

At the conclusion of the pricing period, CVR holders would receive a payment from MGRM, most or all of which would be in cash, based upon the VWAP of MGRM shares during the pricing period unless the MGRM VWAP was at or above $2.90, in which case the CVRs would be worthless.[8] If the MGRM VWAP was below $2.90, the CVR holders would receive a

[6] Respondent believed that he could develop more business from KT. He also acknowledged "he does make me a lot of money…." JX-1 pp. 20, 38; Tr. 269, 290, 1455, 1520. Respondent continues to do business with KT at his current firm. Tr. 1458.

[7] KT was a board member of Aclara, a shareholder of both Aclara and Virologic, and was involved in the negotiations surrounding the CVRs. Tr. 1096-97, Tr. 1257-58.

[8] MGRM had the option to pay 30% or 40% of the CVR payout in the form of MGRM stock. Tr. 1054. On May 26,

penny-for-penny payment for the amount at or below $2.90, down to $2.02. The maximum payout of $.88 per CVR would be achieved if stock traded at or below $2.02 during the trading period. CX-30 p. 22; Tr. 1055.

Based upon the Fund's ownership of 18.5 million CVRs, if it received the maximum payout of $.88 per CVR, it would receive approximately $16 million.[9] Tr. 1112-14. Respondent and his family owned 217,000 CVRs, with a maximum contingent payout of $188,000.[10] RX-20; Tr. 1339-45, 1478-80. For every penny the VWAP dropped below $2.90, down to $2.02, the value of the Fund's CVRs increased by $185,000, and the value of Respondent's CVRs increased by $2,170. Tr. 1114-15, 1481-82.

Eleven days before the pricing period, on May 8, 2006, MGRM announced an investment by Pfizer, and MGRM shares rose from the prior day's close of $1.69 to a closing price of $2.30. RX-6 p. 2; Tr. 1111. On May 18, 2006, MGRM opened at $2.35 and closed at $2.19. RX-6 p. 2; Tr. 1357. If the price of MGRM shares remained at or above $2.02 during the pricing period, the VWAP would exceed $2.02, and CVR holders would receive less than the maximum payout.

B. Friday, May 19 – The Pricing Period Begins and Respondent Places Orders to Sell 50,000 shares of MGRM for the Fund at the Open and the Close

Prior to the open of the market on Friday, May 19, 2006, the Fund placed an order with Respondent to sell 50,000 MGRM shares close to the open. Although KT had never previewed future orders to Respondent, he did so in this case, telling Respondent that he also wanted to sell

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2006, MGRM announced that the CVR liabilities would be paid in all cash. RX-3.

[9] KT estimated that the cost basis for these CVRs was $.2357 per CVR. RX-8 p. 7; Tr. 1062.

[10] Respondent estimated that the cost basis for these CVRs was $.25-$.27 per CVR. Tr. 1348.

another 50,000 shares close to the close.[11] Tr. 70, 1068-70, 1073-74, 1376, 1484-85. Although KT typically placed orders by sending e-mails to the sales traders at Deutsche Bank, this time he called Respondent directly. Tr. 60, 170-171, 294. Deutsche Bank procedures required Respondent to ensure that an order ticket was created when he received the order from KT. CX-24 p. 6, CX-25b p. 85; Tr. 198, 300-302, 832-35, 843-44, 1544. However, he failed to do so. Id.

KT testified that he told Respondent to sell the shares aggressively near the open and close of the market; he was not price sensitive.[12] Tr. 1375-76. KT shared with Respondent the mechanics of the CVRs, the pricing period, and the significance of the VWAP, and his objective to liquidate his stock position by the time the CVRs expired. Tr. 1249-50. Respondent was aware that this was the first day of the pricing period, and CVR holders would benefit if the price of MGRM shares dropped. Tr. 1486-88. KT testified that he conveyed to Respondent that he was "bearish" on MGRM shares, and planned to sell his remaining three million shares during the 15-day pricing period, which meant he had to sell 200,000 shares per day on average.[13] Tr. 1063, 1070, 1074, 1145.

[11] He gave the same instructions to sell the same number of MGRM shares near the open and close to two other firms. Tr. 1151, 1217. However, there is no evidence that Respondent was aware that KT was using other firms to sell MGRM during the pricing period, until after the last of the six trades at issue.

[12] KT claimed that he wanted to sell his MGRM shares at the open and close to get a better price and increase his chances of getting his orders done; it was his impression that the price of MGRM shares spiked at the end of the day and sometimes in the morning. Tr. 1074-76, 1279-80. To support his testimony, he referred to a summary that his office prepared for the period May 19 through May 26, 2006, which asserted that 16% of the trading occurred during the first and last five minutes of trading. RX-45; Tr. 1081. However, the data in the summary covered trading only after the pricing period had begun, so Respondent could not have relied upon it in formulating his strategy. Moreover, as KT acknowledged, a significant portion of the volume reflected in the summary was attributable to his own sales. Tr. 1256. Finally, there was no evidence that KT conveyed these views to Respondent at the time of the orders. Accordingly, the Panel gave KT's testimony on this issue no weight.

[13] In support of his claim that he was bearish on MGRM, KT testified that the Fund sold eight million shares over the 16 months prior to the pricing period. Tr. 1246. However, just three weeks before the pricing period, KT purchased 468,000 shares of MGRM for the Fund. Tr. 1142-43, 1216. Moreover, on May 8, 2010, sales trader Jennifer Watson sent KT an e-mail stating that she had a buyer for 100,000 shares of MGRM; however, KT did not inquire further or attempt to sell his shares. RX-24; Tr. 135-37. Although Respondent knew that KT was bearish on MGRM, there is no evidence that Respondent was aware of these additional facts.

After receiving KT's order to sell 50,000 shares of MGRM, Respondent called Deutsche Bank sales trader Jennifer Watson ("Watson") in New York, NY, to facilitate the trade.[14] Tr. 59. The 9:30 a.m. telephone call was recorded; there is no dispute as to what Respondent said: "Take 50,000 MGRM at the market. Sell it down. Sell it as low as you want. Sell it hard, 50,000." JX-1 p. 1.

At 9:30:36 a.m., Watson entered the order to sell 50,000 shares of MGRM for the Fund into Deutsche Bank's electronic system. At 9:31:21 a.m., Watson conveyed Respondent's order to Chad Messer ("Messer"), the Deutsche Bank equity trader who made a market in MGRM. JX-1 p. 3; Tr. 113-14, 663, 667. The sales began at 9:31:29 a.m., and lasted a little more than a minute, finishing at 9:32:46 a.m. During this brief period, the price of MGRM shares dropped from $2.06 to $1.94. RX-17 pp. 32-35.

At 9:33 a.m., Watson called Respondent's office to report that the order to sell 50,000 shares of MGRM had been filled at an average price of $1.9574. She spoke with one of Respondent's assistants, William Ewing ("Ewing") who told her there would be another order to sell 50,000 shares of MGRM at the close. JX-1 p. 4; Tr. 68-69, 177-78. At 9:36 a.m., Respondent called Watson again to confirm that KT had an additional 50,000 shares of MGRM to sell at the end of the day. Respondent told Watson: "they're all set up on these CVRs. Do you realize what's going on here? . . . [C]all me back and I'll explain it." JX-1 pp. 5-6; Tr. 117-18. Watson thought that was curious, because KT generally did not show his hand beyond his current order. Tr. 70.[15]

[14] May 19, 2006, was Watson's last day of work before taking maternity leave, so she was not involved in Respondent's MGRM sell orders after that date. Tr. 56.

[15] At 9:44 a.m., Watson entered the afternoon order to sell 50,000 shares of MGRM for KT in the Firm's electronic system. The order would remain there until she sent it to a trader later in the day. CX-50 p.4, RX-17 p. 35; Tr. 116-17.

Respondent called Watson again at 2:09 p.m. to instruct her to sell the shares within the last five to ten minutes of trading. Respondent told Watson that, after liquidating three million shares of MGRM, KT intended to short MGRM shares because the Fund owned "a ton" of the CVRs.[16] JX-1 p. 10. Respondent then explained the pricing of the CVRs and the instructions to sell MGRM shares close to the open and close of the market, to "hammer" the stock and reach the $2.02 "target price":

> He [KT] wants it close to the close, and you did a great job hammering, and they all just want to hammer it again to today to do the wake up call here. So what's happening, so you know what's happening, is there's these rights that are out there which are the MGRMRs…and they start pricing off of the average over the next 15 days…And he owns a ton of the rights, right. So and the math works that is the closer at 2.02 you get to, uh, the full value of the rights are realized at 2.02 on the stock.…Just so you know what the target price is…. So yeah, understand the game that's being played for the next 15 days. It's good versus evil….It's you know, the company, the company – the company versus us because, see, the company issued these things thinking they would never….typical, um [BS] you know, optimistic company….never succeed on anything that they promised everyone, and that's why the stock went to a buck-fifty, and then what they did is they got this deal for Pfizer done which moved the stock, and their whole goal here is to keep the stock up while they did this pricing period because, you know, obviously the higher the stock is, the less the CVR they have -- the less cash and stock they have to potentially have to pay out. So that's the whole key. It's a sliding scale from 2.02 to 2.90. At 2.90, they owe the CVRs nothing. At 2.02, they owe … them everything, 88 cents. You follow me? . . . So that's why the game is being played the way it is. JX-1 pp. 8-12.

Watson conveyed the order to Messer, stating that she had an order to sell 50,000 shares of MGRM, with discretion, in the last two minutes of trading. Tr. 88-91. At 3:47 p.m., she sent an electronic instant message ("IM") reiterating the order to Messer, to remind him of the order to sell MGRM close to the close. She sent a follow-up IM at 3:48 p.m., stating, "ok to work til close." RX-26 p. 1.

[16] In fact, KT shorted 290,000 shares of MGRM during the pricing period. Tr. 1142-43.

Messer began selling MGRM shares at 3:47:47 and finished a little more than ten minutes later, at 3:58:02, just before the close of the market. The records reflect that Messer sold 4,400 shares in 18 transactions during a two-second period from 3:47:47 p.m. – 3:47:49 p.m., then stopped trading for almost four minutes, during which time, MGRM shares dropped approximately eight cents. At 3:51:47, he resumed selling at $2.06. At 3:58:02, the order was filled with a last sale at $2.01.[17] RX-17 pp. 35-41, CX-50 pp. 4-10; Tr. 121-22. At the end of the day, Respondent's second assistant, Dan Aliperti ("Aliperti"),[18] prepared a "billing" or "booking" ticket ("booking ticket"), combining the morning and afternoon sales, and falsely reflecting that KT placed the orders directly with the sales trader.[19] CX-53 pp. 2-4; Tr. 296, 822-25, 964, 1544-45.

For the May 19 trading day, MGRM opened at $2.18, reached a high of $2.20, a low of $1.90, and closed at $2.06, with approximately two million shares traded during the day. CX-51 p. 7; Tr. 738. The VWAP for the day was $2.0803. CX-49 p. 10. The Fund's average selling price for the day was $.08 per share lower than the VWAP, at $1.9964. CX-50 p. 3; Tr. 1222.

C. Monday, May 22 - Respondent Again Places Orders to Sell 50,000 shares of MGRM for the Fund at the Open and the Close

KT and Respondent both testified that, prior to the open of the market on Monday, May 22, 2006, KT gave Respondent the same order to sell two 50,000 share blocks of MGRM near the open and close, specifying that the shares should be sold aggressively and quickly within the first and last five minutes of trading. JX-1 p. 29; Tr. 189, 195, 1147, 1151, 1157, 1401, 1503-04,

[17] At 8:17 p.m., Aliperti gave KT a final report of the trading: "SLD 100,000 MGRM @ 1.9964 …" RX-16 p. 4.

[18] After Respondent was terminated from Deutsche Bank, he hired Aliperti to work with him at his new firm. Tr. 288-89.

[19] A "booking ticket" is used when a client order is placed directly with the sales trader. In these cases, the branch creates a "booking ticket" after the order is executed to facilitate proper accounting for the trade. Tr. 201.

1625. KT did not complain about the prior day's executions despite the fact that they were $.08 below the VWAP. Tr. 1502. Again, despite the requirement to do so, Respondent failed to ensure that an order ticket was prepared. CX-24 p. 6, CX-25b p. 85; Tr. 198, 300-302, 832-35, 843-44, 1544.

Respondent told his sales assistant, Ewing, to call the order in to the sales desk. Tr. 189, 1403, 1504. At 9:20 a.m., Ewing called sales trader Dave Zitman ("Zitman") to convey KT's order to sell 50,000 shares of MGRM at the open and another 50,000 shares at the close. JX-1 pp. 22-23, Tr. 189. At Respondent's instruction, Ewing told Zitman to "sell it hard . . . sell it on the opening." JX-1 p. 24. Respondent was listening to the call, and he cut Ewing off after he told Zitman: "They're pricing the rights off the stock." JX-1 p. 24, Tr. 189-93, 1504. Toward the end of the call, Zitman confirmed: "[H]e wants to be done on 50 ASAP." JX-1 p. 24; Tr. 189-90, 192, 424. At 9:22 a.m., Zitman entered the order into the Firm's electronic system. RX-17 p. 43; Tr. 549.

A few minutes later, at 9:26 a.m., Zitman called Respondent's office to say that he had conveyed the order to Messer with instructions to trade it like he did last week. JX-1 pp. 28-29. Zitman asked Respondent: "Take the [f---]ing thing down (inaudible) a dollar?" to which Respondent replied: "Yeah, 50 cents, yes." JX-1 p. 30. Zitman wanted to make sure that Respondent understood that a large market order may cause the price of MGRM shares to move dramatically. Tr. 444. He asked: "He wants it to be done – and if I take the thing down to $1.50 and it bounces back to $2, he doesn't care?" Respondent confirmed: "No, right." JX-1 p. 30; Tr. 432.

The MGRM sales began at 9:30:05 a.m., and finished in less than two minutes, at 9:31:46 a.m. Over the course of the 98 sales transactions, MGRM shares dropped from $1.95 to $1.91. RX-17 pp. 43-45, CX-50 pp.14-15.

At 3:22 p.m., Zitman called Respondent's office to confirm the afternoon order, and spoke with Ewing, who reiterated Respondent's order to sell 50,000 shares of MGRM "as late as you can." Zitman confirmed: "as close to market on close as we can." JX-1 p. 32; Tr. 447.

In an apparent oversight, Messer did not execute the trade before the close of the market. Accordingly, at 4:05:29, he filled the order by taking shares into inventory at the closing price, $1.89. RX-17 p. 45, CX- 50 p. 14. At 4:06 p.m., Respondent called Zitman to confirm that KT's order was filled. Zitman told Respondent that they sold 50,000 shares of MGRM at $1.89, to which Respondent commented: "you must have been like printing it at the very, very end of the day where it went out at 89, right?" Zitman inaccurately answered: "yeah." JX-1 pp. 37-38, RX-17 p. 45; Tr. 1505. At the end of the day, Aliperti again prepared a booking ticket, combining morning and afternoon sales, and falsely reflecting that KT placed the orders directly with the sales trader. CX-53 p. 4; Tr. 303-304, 822-25, 964, 1544-45.

For the May 22 trading day, MGRM opened at $2.06, which was the high of the day, and reached a low of $1.89, which was also the closing price, with approximately 2.4 million shares traded during the day. CX-51 p. 8; Tr. 739. The VWAP for the day was $1.96. CX-49 p. 10. The Fund's average selling price was $.05 per share lower, at $1.91. CX-53 p. 4; Tr. 1225.

D. Tuesday, May 23 - Respondent Places Order to Sell 50,000 Shares of MGRM for the Fund at the Open and Close

At 9:27 a.m., just before the market opened on May 23, 2006, Zitman called Respondent's office to find out if there was another order, and spoke to Respondent's partner,

Mary Mayer ("Mayer"). JX-1 p. 42; Tr. 462. Mayer conferred with Respondent, who was then speaking with KT. Respondent confirmed KT's request: "Same order as yesterday," which Mayer conveyed to Zitman. JX-1 p. 43; Tr. 1147, 1163, 1412-13. Again, KT did not complain about the execution of the previous day's sales, despite the fact that they were $.05 lower than the VWAP for the day.[20] Yet again, despite the requirement to do so, Respondent failed to ensure that an order ticket was prepared. CX-24 p. 6, CX-25b p. 85; Tr. 198, 300-302, 832-35, 843-44, 1544.

Zitman entered the order in the Firm's electronic system at 9:28 a.m. RX-17 p. 51. Selling began at 9:30.07, and the 50,000 share order was filled in just 13 seconds, with the price dropping from $1.90 to a low of $1.86, finishing at $1.88. RX-17 pp. 51-52; Tr. 598-99, 1415. At 9:31 a.m., Zitman called Respondent to report the 50,000 share sale at an average price of $1.8798. JX-1 pp. 44-45; Tr. 469, 1507. Respondent thanked Zitman, noting: "you just like banged them," and told Zitman that there was an order to sell another 50,000 shares of MGRM for KT at the close. JX-1 pp.45-46.

At 3:50 p.m., Respondent again spoke with Zitman to confirm KT's order to sell 50,000 shares of MGRM.[21] JX-1 pp. 46-48. Respondent told Zitman that KT wanted the order "spread out a little bit." Respondent explained: "…just take it with a minute to go and spread it out a little bit . . . hit the bids…." Id.; Tr. 478-79, 1510-11. Zitman was concerned about KT's request,

[20] At this time, KT was not aware that the afternoon trade was done after market hours. Tr. 1413.

[21] Zitman testified at his on-the-record interview that this call probably occurred at 2:50, rather than 3:50. However, at the hearing, Zitman was uncertain of his earlier testimony, because it was his practice to promptly put orders in the electronic system, and he placed the order in the system at 3:51 p.m. in this case. Tr. 633-34. Moreover, in his contemporaneous telephone call with Respondent, Zitman asserted that he had received the order less than ten minutes before the close, and Respondent did not dispute it. JX-1 p. 56, RX-17 p. 53, CX-50 p. 160; Tr. 475, 633, 638-639, 657. Moreover, Deutsche Bank's metadata records indicate that the call was placed at 3:50. CX-71; Tr. 1430. Based upon this evidence, the Panel concluded that the call occurred at 3:50 p.m.

reasoning that, while traders sometimes spread out an order during the day, it is not typical to spread out an order a minute prior to the close. Tr. 478-80. Zitman asked Respondent if KT was trying to mark the close,[22] and Respondent acknowledged that he was. JX-1 p. 48. When Zitman became agitated and told Respondent that marking the close was illegal, Respondent agreed with Zitman that he did not want to lose his license. Nonetheless, Respondent closed the call by reiterating: "50,000, market on close." JX-1 p. 48. Zitman entered the order to sell the shares in the Firm's electronic system at 3:51 p.m.

Deutsche Bank records reflect that KT's order to sell 50,000 MGRM shares was filled and the shares were purchased into Deutsche Bank's inventory at 4:11 p.m. RX-17 p. 53, CX-50 p. 16, RX-43 p. 89. As before, Aliperti prepared a booking ticket, combining the morning and afternoon sales, and falsely reflecting that KT placed the orders directly with the sales trader. CX-53 p. 3; Tr. 302, 822-26, 964, 1544-45.

At 4:12 p.m., Zitman spoke with Respondent's partner, Mayer, and reported the sale of 50,000 shares of MGRM at $1.84. JX-1 p. 51. At 4:25 p.m., Mayer called Zitman and asked: "That trade wasn't printed after the close, was it?" Zitman denied that to be the case, claiming instead it was the last print. Mayer expressed doubt, and indicated that Respondent would call him to discuss it further. JX-1 pp. 52-53; Tr. 483. Six minutes later, at 4:31 p.m., Respondent called Zitman, who indicated that he was in the process of gathering information as to the order execution. Respondent emphasized: "Just make sure it's in the VWAP." JX-1 p. 55. Zitman noted, incorrectly, that the Fund received an execution of $1.89 on his sale, which was better

[22] Marking the close, a well-recognized form of manipulation, is the practice of "attempting to influence the closing price of a stock by executing purchase or sale orders at or near the close of the market." Dep't of Market Reg. v Morgan Stanley & Co., No. CMS960235, 2000 NASD Discip. LEXIS 1, at *59-60 (NAC Jan. 18, 2000) ("Marking the close conveys false information to the market as to a stock's real price level and demand for it.").

than the closing price of $1.84. Respondent was unimpressed with the price improvement, restating several times that the only thing that mattered was that the sales occurred in the VWAP, underscoring, "that's all [KT] wants to know." JX-1 p. 58, Tr. 492. Respondent asked Zitman to have Messer call him.

Zitman was concerned that KT's purported objective was that his MGRM stock sales be in the VWAP, regardless of the execution price. Tr. 494. He spoke with Messer, who said that there were rights attached to the stock that were priced based upon the VWAP of MGRM shares, and he concluded that KT and Respondent were trying to affect the VWAP so that the rights would be priced more favorably. Tr. 508-09, 655. Messer was also concerned, and raised the issue with the senior person at his equity desk, William Matthews ("Matthews"). Tr. 508-09, 655, 689. Matthews and Messer both discussed the matter with Respondent. See, JX-1 pp. 63-65; Tr. 671, 745. Respondent expressed anger that the sale did not occur in the open marketplace, to which Messer responded that the trading desk fulfilled its obligation to execute the sale at the closing market price. Tr. 671-72, 719. Matthews also questioned why Respondent would take issue with the manner in which the sale was executed if the market on close instructions were met. Tr. 745-46. Matthews was not comfortable with Respondent's position, so he elevated the issue to Compliance. Tr. 509, 689, 746-47.

At some point, Respondent got the false impression that 12,600 shares of the order were sold during the trading day, and the remaining 37,400 shares were taken into Firm inventory after the close of the market.[23] JX-1 p. 63; Tr. 748-49. Based upon this understanding, KT requested and received a cancellation of the 37,400 share sale that he believed occurred after the close of

[23] As noted above, Deutsche Bank records indicate that the 50,000 share sale occurred after the close of the market. RX-17 p. 53, CX-50 p. 16.

the market, because it was inconsistent with KT's directions. JX-1 p. 63; CX-53 p. 5; Tr. 391, 747-48, 1083, 1230.

For the May 23 trading day, MGRM opened at $1.91, reached a high of $2.11, a low of $1.81, and closed at $1.84, with 1.9 million shares traded. CX-51 p. 8; Tr. 739. The VWAP for the day was $1.91. CX-49 p. 10. KT's average selling price, after the partial reversal of the execution, was $.04 per share lower, at $1.8718. CX-53 p 5; Tr. 1222, 1225.

E. Deutsche Bank Compliance Reviews the Trading Activity and Terminates Respondent.

The next morning, May 24, 2006, at 8:12 a.m., Respondent called Zitman to complain that KT's order was not filled before the close. "All we're trying to do is print as much stock between, you know, the last minute and the close." JX-1 p. 63. Respondent acknowledged that Matthews was concerned about KT's order, but Respondent did not share his concern, saying: "This is the way this guy wants to trade this stock"; adding: "It's a free country." JX-1 p. 64.

After reviewing KT's orders, Deutsche Bank Compliance personnel determined to no longer execute MGRM sales for the Fund's account. Tr. 748. Respondent was suspended, and later terminated, based upon his MGRM sales orders for the Fund. CX-1, CX-70; Tr. 817-18; 846-51. When Respondent met with his branch supervisors, he admitted that what he did was "stupid." CX-70 p. 1; Tr. 848. He did not offer an explanation for his statements on the taped calls, and did not claim that his orders to sell MGRM were part of a legitimate trading strategy. Tr. 851, 1447-48.

IV. Violations

A. Market Manipulation

The Complaint alleges that Respondent engaged in market manipulation of MGRM securities by placing sell orders near the open and close of the market, in violation of Section 10(b) of the Exchange Act,[24] SEC Rule 10b-5 thereunder,[25] and NASD Conduct Rules 2120[26] and 2110, which prohibit the use of any manipulative, deceptive, or otherwise fraudulent device or contrivance in connection with the purchase or sale of securities.[27]

Manipulation is "the creation of deceptive value or market activity for a security, accomplished by an intentional interference with the free forces of supply and demand." Swartwood, Hesse, Inc., Exchange Act Rel. No. 31212, 1992 SEC LEXIS 2412, at *16-17 n.16 (Sept. 22, 1992). "When investors and prospective investors see activity, they are entitled to assume that it is real activity." Edward J. Mawod & Co., 46 S.E.C. 865, 871-872 (1977), aff'd, 591 F.2d 588 (10th Cir. 1979).

To establish a violation, Enforcement must show that Respondents acted with scienter–"a mental state embracing intent to deceive, manipulate, or defraud." Ernst & Ernst v. Hochfelder, 425 US 185, 193 n. 12 (1976). Scienter may be "established through a showing of recklessness

[24] "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange . . .to use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

[25] "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange, (a) to employ any device, scheme, or artifice to defraud, . . . or (c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security."

[26] "No member shall effect any transaction in, or induce the purchase or sale of, any security by means of any manipulative, deceptive or other fraudulent device or contrivance."

[27] Count One of the Complaint alleged, in the alternative, that Respondent aided and abetted violations of these provisions. In light of the Panel's finding that Respondent was a primary violator of these provisions, it did not

amounting to an extreme departure from the standards of ordinary care …." Dep't of Market Reg. v Morgan Stanley & Co., Inc. No. CMS960235, 2000 NASD Discip. LEXIS 1, at *60-61 (NAC Jan. 18, 2000).

Most courts considering the issue have held that that market manipulation can occur "through otherwise legal means, such as short sales and large or carefully timed purchases or sales of stock." SEC v. Masri, 523 F. Supp. 2d 361, 367, 2007 US Dist. LEXIS 86163, at *13-14 (SDNY 2007). See, Michael J. Markowski, Exchange Act Rel. No. 43259, 54 SEC 830, 835, 2000 SEC LEXIS 1860, at *10 (Sept. 7, 2000), (holding that manipulative acts, "are not rendered innocent simply because they fail to achieve the desired result"), aff'd, 274 F.3d 525, 529, 2001 US App. LEXIS 27007, at **7 (DC Cir. 2001)(noting Congress's determination that "'manipulation' can be illegal solely because of the actor's purpose").

The elements of market manipulation are satisfied here. Respondent placed large orders to sell MGRM shares within minutes of the open and close of the market over successive days.[28] The timing of the orders was deceptive because it did not represent the free forces of supply and demand. Instead, Respondent acted with scienter; his taped instructions to sell "literally . . . as late as you can," "ASAP," or "on the opening," with directions to " "hammer it," "sell it down,"

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reach the issue of whether Respondent aided and abetted these violations.

[28] Large orders near the open and close, termed "marking the open" and "marking the close" when done with the intent to affect the price of a security, have been considered to be manipulative. Morgan Stanley & Co., 2000 NASD Discip. LEXIS 1, at *60 (holding that manipulators mark the open or close to convey "false information to the market as to the stock's real price level and demand for it").

"sell it as low as you want," and stated goal of reaching the $2.02 "target price," reflect an explicit intent to drive the price of MGRM shares down.[29] JX-1 pp. 1-2, 8, 10.

In an attempt to overcome the plain wording in taped conversations, Respondent offered several alternative explanations for the sales strategy, none of which the Panel found credible. First, Respondent pointed to KT's claim at the hearing that the large sales in the first and last minutes of trading was designed to get the best price, based upon KT's impression that prices were higher at the open and the close of the market. However, as noted above, the Panel did not find this claim to be credible.[30] Moreover, KT's stated goal to obtain the best price was directly at odds with his instructions to sell without regard to price. Additionally, despite the fact that KT consistently received executions that were below the average price for the day, he never complained about the executions or adjusted his strategy. Likewise, the Panel questioned the insistence that the sales occur within the VWAP and the rejection of sales at purportedly superior prices, simply because the sales were not included in the VWAP. These factors indicated that the objective of the selling strategy was to drive down the price of MGRM shares rather than to obtain the best price.

Respondent also asserted that the Fund owned approximately 2.9 million shares of MGRM stock, so it stood to lose money if the price of MGRM shares dropped below $2.02. Tr.

[29] Contrary to Respondent's assertion, the Hearing Panel's finding is not inconsistent with GFL Advantage Fund, LTD. v. Colkitt , 272 F.3d 189, 211 (3d Cir. 2001); 2001 US App. LEXIS 24572, *50 (holding that a finding of manipulation based upon open market sales required "some other type of deceptive behavior in conjunction with [the] short selling that either injected inaccurate information into the marketplace or created artificial demand for the securities"). As the court in GFL Advantage Fund stated, the difficulty in "open market" cases is to "distinguish between legitimate trading strategies intended to anticipate and respond to prevailing market forces and those designed to manipulate prices and deceive purchasers and sellers." Id. at 205, *31. However, no such difficulty exists in this case. Respondent's tape recorded conversations make clear that his orders to sell MGRM within minutes of the open and close were not part of a legitimate strategy; they were designed to "hammer" or drive down price of MGRM shares to maximize the value of the CVRs. Respondent underscored the purpose of the sales when he provided a lengthy explanation of "why the game is being played the way it is," including why CVR holders would benefit from a drop in the price of MGRM shares to a target price.

1064. However, the Panel did not find this persuasive because, as the price of MGRM shares dropped, the $182,000 per penny gain on the CVRs far exceeded the $29,000 per penny loss on the shares. In addition, since the Fund was liquidating the Fund's stock position, by the end of the pricing period, there would be no remaining stake. Tr. 1266. Moreover, Respondent and KT suggested that it was unlikely that the VWAP for the pricing period would be above $2.02, so there was no need to manipulate the market in order to realize the maximum payout on the CVRs. However, because each day counted as 1/15 of the calculation, the outcome could not be assured, particularly during the early part of the pricing period.

In addition, Respondent argued that he had no motive to manipulate the price of MGRM shares because commissions on the sales of MGRM shares at issue were minimal. RX-18 p. 2; Tr. 1352-53. However, Respondent's motives were clear. As Respondent acknowledged, KT and the Fund were among his most important customers. Accordingly, Respondent's desire to serve KT and ensure that KT received the $16 million maximum payout on the CVRs was a powerful incentive to manipulate the price of MGRM shares. Moreover, Respondent and his family held 217,000 CVRs and stood to receive a potential payout of $188,000. For these reasons, the Panel found that Respondent had compelling motives to manipulate the price of MGRM shares.

In summary, the Panel found that the tape-recorded conversations provided overwhelming evidence of Respondent's intent to manipulate the market for MGRM shares. Respondent's arguments to refute the plain meaning of the tapes were unpersuasive. After careful consideration of the evidence presented at the hearing, the Panel concluded that, based

[30] See note 12.

upon the preponderance of the evidence presented, the sales of MGRM shares near the open and close of the market during the pricing period did not reflect a legitimate strategy. Instead, the Panel found that Respondent placed the orders to artificially depress the price of MGRM to impact the pricing of the CVRs. Accordingly, the Panel found that Respondent engaged in market manipulation with respect to MGRM shares, in violation of Section 10(b) of the Exchange Act, SEC Rule 10b-5 promulgated thereunder, and NASD Conduct Rules 2120 and 2110.[31]

B. Books and Records - False Order Tickets

The Complaint alleges that Respondent failed to ensure the preparation of order tickets reflecting KT's sales of MGRM shares, thereby causing his Firm's books and records to be inaccurate, in violation of NASD Rules 3110 and 2110.

NASD Rule 3110(a) requires member firms to "make and preserve books, accounts, records, memoranda, and correspondence in conformity with all applicable laws, rules, regulations," including Exchange Act Rule 17a-3. Exchange Act Rule 17a-3 requires member firms to make and keep "[a] memorandum of each brokerage order, and of any other instruction, given or received for the purchase or sale of securities." 17 C.F.R. § 240.17a-3(a)(6)(i). Consistent with these requirements, Deutsche Bank's Code of Conduct and its Policies and Procedures Manual require a person accepting a client order to initiate an order ticket "immediately upon receipt of an order."[32] CX-24 p. 6, CX-25b p. 85; Tr. 198, 300-302, 811-15, 832-35, 843-44, 1544.

[31] Although Rules 2110 and 2120 discuss only FINRA members, Rule 115 states that FINRA rules shall apply to all members, as well as to "persons associated with a member."

[32] This requirement is also designed to provide a surveillance tool for the Firm's compliance function and to facilitate proper posting and billing to the appropriate client account. Tr. 810.

While Respondent was permitted to direct one of his sales assistants to complete required order tickets, it was still his responsibility to ensure that the tickets were accurately completed.[33] Tr. 852, 994. However, Respondent did not do so. No order tickets were prepared when Respondent received the orders from KT. Tr. 406, 984, 989, 991, 1151-52, 1163, 1324-25, 1531-32, 1544. Instead, Aliperti completed booking tickets, combining the morning and afternoon sales at the end of each trading day, which made it appear that KT placed the orders with the sales traders rather than Respondent.[34] CX-53 pp. 2-4; Tr. 296, 822-25, 964. Each of the booking tickets for the three days at issue showed a single, 100,000 share, order to sell, with an average price, only one time stamp, and a false notation that the order was given by the client directly to the trading desk.[35] Id. Tr. 200-06, 300-02, 809-32, 1544-45. Because it appeared that

[33] Respondent argued that he relied upon one of his sales assistants, Ewing, to prepare required tickets. Tr. 1330-31. Although Respondent did not specifically recall conveying the orders to Ewing, he claimed that Ewing should have known about the orders. Tr. 1330-32, 1325, 1330-32. Respondent testified: "[M]y job was not to look at order tickets." Tr. 1327. However, neither Ewing nor Aliperti completed the order tickets on Respondent's behalf.

[34] At the hearing, Aliperti testified that he received the information from Ewing or the trading desk. RX-31 p. 87; Tr. 296, 361-69. Ewing did not recall instructing Aliperti to prepare order tickets for the transactions. Tr. 222.

[35] When pressed for an explanation, Respondent asserted, incredibly, that the branch manager, Zbynek Kozelsky ("Kozelsky"), enforced a practice of preparing booking tickets instead of order tickets, and placing false statements on the booking tickets to indicate that orders were placed with the sales traders, even when this was not the case and orders were received by branch personnel. Tr. 1648-50. However, Kozelsky testified, consistent with Deutsche Bank procedures, that Respondent was required to ensure completion of an order ticket when he received orders directly from KT. Tr. 813-15. The failure to ensure completion of order tickets, along with the submission of false booking tickets, resulted in circumvention of Kozelsky's branch office compliance review. Tr. 200-06, 300-02, 809-32; CX-53. The Panel found Kozelsky's testimony on this point to be credible because it was consistent with the Firm's policies and the testimony of Respondent's sales assistants, and Kozelsky had no motive to enforce a practice that ran so counter to his responsibilities. Tr.198, 300-02. Moreover, regardless of the Firm's policy or practice, it is a violation of FINRA Rules to enter false information on official Firm records. The entry of accurate information on official Firm records is a predicate to the FINRA's regulatory oversight of its members. It is critical that associated persons, as well as firms, comply with this basic requirement. Charles E. Kautz, Exchange Act Rel. No. 37072, 1996 SEC LEXIS 994, at *11–12 (Apr. 5, 1996) (citations omitted); see also Geoffrey Ortiz, Exchange Act Rel. No. 58416, 2008 SEC LEXIS 2401, at *22–23 (Aug. 22, 2008); Dep't of Enforcement v. Cuozzo, No. C9B050011, 2007 NASD Discip. LEXIS 12 (NAC Feb. 27, 2007). Therefore, even giving credit to Respondent's assertion that it was Kozelsky's policy to enter false information, Respondent violated Rules 3110 and 2110 by acquiescing to it.

KT placed the orders directly with the sales traders, the typical branch office compliance review was circumvented.[36]

The Panel found that it was Respondent's responsibility to ensure that order tickets were prepared when he received orders directly from KT, but he failed to do so. As a result, he caused his Firm's books and records to be inaccurate, in violation of NASD Rules 3110 and 2110.

V. Sanctions

A. Market Manipulation

The FINRA Sanction Guidelines ("Guidelines") for marking the close or open recommend a fine of $25,000 to $200,000 and a suspension of up to two years for intentional or reckless misconduct; and, in egregious cases, a bar and a fine in excess of $200,000. Guidelines p. 58 (2007). Enforcement requests a bar.

Market manipulation is a serious violation. As the National Adjudicatory Council observed in Market Surveillance Committee v. Markowski: "The integrity of the securities markets is paramount, and those who engage in activities that manipulate markets cause great harm not only to investors who are involved in the manipulated markets, but to the overall public perception that the markets are driven by the free forces of supply and demand." 1998 NASD Discip. LEXIS 35, at *56-57. Because manipulation is a serious offense, there is "no basis for leniency"–the sanction must be significant. Pagel, Inc., Exchange Act Rel. No. 22280, 48 SEC 223, 232, 1985 SEC LEXIS 988, at *22 (Aug. 1, 1985); Dep't of Enforcement v. Levitov, No. CAF970011, 2000 NASD Discip. LEXIS 12, at *28 (NAC June 28, 2000).

[36] If a client places an order with a sales trader, the trader is required to input the order into the Firm's electronic system. Tr. 641, 985. Then, at the end of the day, the client's broker would prepare a booking ticket, consolidating all the trading in a particular stock into one ticket, which would facilitate proper accounting for the transaction. Tr. 964.

Here, a number of aggravating factors have led the Panel to conclude that Respondent's misconduct is egregious and warrants a bar. The Principal Considerations under the Guideline include whether the misconduct was isolated or involved a pattern, and whether the respondent stood to benefit from it. Although only one stock was involved, this was not an isolated incident; Respondent placed six orders for KT over a three-day period. The orders were significant in size and were designed to drive down the price of MGRM shares. Moreover, Respondent indicated that he would have continued to place these orders if his Firm had permitted him to do so. Tr. 1631. While the commissions on the orders were not significant, KT was among Respondent's most important clients, and Respondent and his family also held CVRs. Accordingly, Respondent stood to gain from the misconduct.

The Panel also considered that Respondent's misconduct was not inadvertent; he placed the sell orders intending to drive down the price of MGRM shares. In addition, the Panel was particularly concerned that, even with the benefit of hindsight, Respondent did not appreciate that what he did was wrong.

For these reasons, the Panel concludes that Respondent's misconduct was egregious and a bar is appropriate.

B. Books and Records

The Sanction Guideline for recordkeeping violations recommends a suspension of up to 30 business days and a fine of $1,000 to $10,000, or a lengthier suspension or bar and a fine of $10,000 to $100,000 in egregious cases. Guidelines p. 30 (2007). Enforcement requests a bar.

The Principal Considerations under the Guideline suggest particular consideration of the nature and materiality of the inaccurate or missing information. Here, the failure to ensure the preparation of accurate order tickets was significant because the absence of the order tickets,

along with the false booking tickets, would have misled the branch supervisor into thinking that the client had placed the orders directly with the sales traders rather than with Respondent. Rather than accepting responsibility, Respondent blamed his assistants and suggested that the Firm's Compliance Officer was enforcing a practice of falsifying documents. Respondent's misconduct was egregious. The Panel concluded that a one-year suspension and a $25,000 fine was warranted. However, in light of the bar for market manipulation, no further sanction is imposed for this violation.

VI. Conclusion

For engaging in market manipulation, in violation of Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and NASD Conduct Rules 2120 and 2110, Respondent is barred in all capacities.[37] In light of the bar, no further sanctions are imposed for Respondent's failure to ensure the accuracy of order tickets, in violation of NASD Conduct Rules 3110 and 2110. Respondent shall pay costs in the amount of $ 13,207.85, which include an administrative fee of $750 plus the cost of the hearing transcripts.

The bar shall become effective immediately if this Decision becomes the final disciplinary action of FINRA.[38]

HEARING PANEL.

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By: Sara Nelson Bloom
Hearing Officer

[37] In light of this finding as to Count one of the Complaint, the alternative charge, that Respondent failed to make an adequate inquiry regarding the trading instructions in Count two of the Complaint, is dismissed.

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

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