

AUGUST 2005

# Notice to Members

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Reported for August



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# Notice to Members

AUGUST 2005

## SUGGESTED ROUTING

Legal & Compliance  
Operations  
Registered Representatives  
Senior Management  
Executive Representatives  
Insurance  
Variable Contracts

## KEY TOPICS

Equity-Indexed Annuities  
Rule 3030 (Outside Business Activities  
of an Associated Person)  
Rule 3040 (Private Securities Transactions  
of an Associated Person)  
Supervision

## GUIDANCE

### Equity-Indexed Annuities

#### Member Responsibilities for Supervising Sales of Unregistered Equity-Indexed Annuities

#### Executive Summary

This *Notice to Members* addresses the responsibility of firms to supervise the sale by their associated persons of equity-indexed annuities (EIAs) that are not registered under the federal securities laws.<sup>1</sup>

#### Questions/Further Information

Questions concerning this *Notice* may be directed to Thomas M. Selman, Senior Vice President, Investment Companies/Corporate Financing, (240) 386-4500.

#### Background and Discussion

Equity-indexed annuities are financial instruments in which the issuer, usually an insurance company, guarantees a stated interest rate and some protection from loss of principal, and provides an opportunity to earn additional interest based on the performance of a securities market index. Some EIAs are not registered under the Securities Act of 1933 (the Securities Act) based on a determination that they are insurance products that fall within that statute's Section 3(a)(8) exemption and therefore are not considered to be securities.<sup>2</sup>

According to one recently published estimate, in 2004 sales of equity-indexed annuities increased over 50 percent, from \$14 billion in 2003 to an estimated \$22 billion.<sup>3</sup>

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## 1. Investor Protection Issues Presented by Equity-Indexed Annuities

EIAs are complex investments. Many EIAs permit investors to participate in only a stated percentage of an increase in an index. Many of these investments also impose a “cap rate” that represents the maximum annual account value percentage increase allowed to investors. Unregistered EIAs typically do not provide for investor participation in the dividends accumulated on the securities represented by the index.<sup>4</sup> EIAs have other features that contribute to their complexity such as minimum guarantees and fees and expenses, including surrender charges, premium bonuses, and multiple premium payment arrangements. In addition, investors may assume mistakenly that EIAs provide the same returns as an index mutual fund.

NASD is concerned about the manner in which associated persons are marketing and selling unregistered EIAs, and the absence of adequate supervision of these sales practices. We have seen sales material for unregistered EIAs that do not fully describe the features and risks of the product. For example, we have seen the following claims:

- ◆ “What if the market goes down and you would lose nothing?  
The market goes up-you gain!”
- ◆ “A Win/Win Investment Vehicle!”
- ◆ “How Your Retirement Funds Can Have: Security of Principal, Higher Than CD Rates of Interest, Opportunity for Growth (No Losses)”
- ◆ “Pick up where Social Security leaves off with NEW tax-deferred annuities...featuring... 2 indexed accounts linked to a popular stock market index.”
- ◆ If you’re looking for upside potential and no market downside look no further than [name of EIA]. This fixed annuity... enables you to make the most of S&P 500 Index gains...”
- ◆ “Growth Potential *without* Market Risk.”

We understand that some associated persons who also act as insurance agents might be using this type of sales material in their insurance sales capacity. NASD is concerned that the unsupervised use of such sales material could confuse or mislead investors. If sales pieces containing these statements were deemed to be broker-dealer communications with the public, then they would be subject to the NASD advertising rules, and would have to provide a balanced description of the features and risks of the product.

Moreover, because of the product’s complexity, some associated persons might have difficulty understanding all of the features of the product and determining the extent to which those features meet the needs of the customer. While unregistered EIAs may be appropriate for some retail investors, they are not suitable for all investors. For example, possible surrender charges and the combination of caps and participation rates associated with a particular product are factors that must be considered in any suitability determination.

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## 2. The Uncertain Status of Unregistered Equity-Indexed Annuities

The question of whether a particular EIA is an insurance product or a security is complicated and depends upon the particular facts and circumstances concerning the instrument offered or sold. NASD does not seek to resolve that issue in this *Notice*; nor is this *Notice* intended to describe those circumstances in which an EIA might be deemed to be a security. However, a brief summary of the applicable provisions of the federal securities laws may be useful.

Section 2(a)(1) of the Securities Act broadly defines “security” to include such financial instruments as evidence of indebtedness, participation in profit-sharing agreements, and investment contracts. Section 3(a)(8) generally exempts from the Securities Act any security that is an “insurance or endowment policy or annuity contract or optional annuity contract, issued by a corporation subject to the supervision of the insurance commissioner, bank commissioner, or any agency or officer performing like functions, of any State or Territory of the United States or the District of Columbia.”

In 1986, the Commission adopted Rule 151, a “safe harbor” under the Securities Act, which clarifies when certain annuity contracts are exempted securities under Section 3(a)(8). The fundamental construct of Rule 151 is derived from prior judicial interpretations of Section 3(a)(8). Consequently, the Commission has stated that the rationale underlying the conditions set forth in the rule are, along with applicable judicial interpretations, relevant to any Section 3(a)(8) analysis.<sup>5</sup>

In order for the Rule 151 safe harbor to apply:

- ◆ the product must be issued by an insurer that is subject to state insurance regulation;
- ◆ the insurer must assume investment risk, as provided in paragraph (b) of the rule; and
- ◆ the product may not be marketed primarily as an investment.

As noted above, the status of any particular EIA under the safe harbor (or under Section 3(a)(8)) will depend on the facts and circumstances. In 1997 the Commission issued a concept release requesting comment regarding EIAs.<sup>6</sup>

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### 3. Supervision under Rule 3030 and Rule 3040

Many firms assume that EIAs that are not registered under the Securities Act are insurance products and not securities. These firms treat the sale of unregistered EIAs by associated persons in their capacity as insurance agents as an outside business activity under Rule 3030, beyond the mandated purview of the firm's supervision. Rule 3030 does not require that the firm supervise or even approve an outside business activity, although a firm may choose to deny or limit the ability of associated persons to engage in the activity. Rule 3030 simply requires that an associated person promptly notify the firm in writing that he is engaging in a business activity outside the scope of his relationship with the firm.

However, if a particular EIA were a security, and an associated person sold the EIA outside the regular scope of his employment with the firm, Rule 3040 requires that the firm treat the sale as a private securities transaction and supervise the sale in accordance with the provisions of that rule. The associated person must notify the firm in writing before participating in a private securities transaction. If the associated person will receive compensation for the transaction, the firm must provide written approval of his participation in the transaction. If the firm does approve the participation, it must record the transaction on its books and records and supervise the associated person's participation in the transaction as if the transaction were executed on behalf of the firm.

A broker-dealer runs certain risks in applying Rule 3030 to the sale of an unregistered EIA on the assumption that the product is not a security. It is often unclear whether a particular EIA qualifies for the exemption under Section 3(a)(8), since the analysis is made on a case-by-case basis and may turn on the particular features and marketing materials associated with the product. As a result, if a particular EIA did not qualify for the exemption, a firm might incorrectly treat the EIA transaction as an outside business activity under Rule 3030 rather than a private securities transaction under Rule 3040 and thereby fail to supervise sales of the product as required by NASD rules.

Perhaps for these reasons, some firms require that associated persons obtain firm approval to sell exempt insurance products. Other firms require that their associated persons obtain more specific approval to sell unregistered EIAs. Still other firms maintain a list of approved EIAs and prohibit the sale of all others.

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#### 4. Supervisory Measures

Due to the uncertainty as to whether a particular unregistered EIA may be a security, as well as the potential regulatory violations and investor protection issues that would arise by the marketing and sale of unregistered EIAs that are deemed to be securities, firms must adopt special procedures under Rule 3030 with respect to these products. In particular, firms must require that their associated persons promptly notify the firm in writing when they intend to sell unregistered EIAs. Moreover, all recommendations to liquidate or surrender a registered security such as a mutual fund, variable annuity, or variable life contract must be suitable, including where such liquidations or surrender are for the purpose of funding the purchase of an unregistered EIA.

As discussed above, NASD is not taking a position on whether a particular EIA is a security, nor are we attempting to describe the circumstances in which an EIA would be deemed a security. However, the uncertainty of this matter has led some firms to treat an associated person's sale of an unregistered EIA outside the regular course or scope of his employment with the firm, as a private securities transaction. These firms supervise the sale according to Rule 3040 procedures. Firms are well advised to consider whether they should take a similar approach. Firms should consider maintaining a list of acceptable unregistered EIAs and prohibiting their associated persons from selling any other unregistered EIA, unless the associated person notifies the firm in writing that he intends to recommend an unregistered EIA that is not on the firm's list, and receives the firm's written confirmation that the sale of the unregistered EIA is acceptable.

Firms are encouraged to consider whether other supervisory procedures also might help protect the firm's customers. For example, a firm could require that all sales of unregistered EIAs occur through the firm. If an associated person is selling the unregistered EIA through the firm, the firm must supervise the marketing material, suitability analysis, and other sales practices associated with the recommendation of unregistered EIAs in the same manner that it supervises the sale of securities.

Firms also must provide any associated person selling any unregistered EIA through the firm with the proper training to understand the EIA's features and the extent to which the EIA meets the needs of a particular customer. The fact that an associated person holds a license as an insurance agent may not adequately qualify him to understand the features of an EIA or the extent to which an EIA meets the needs of a particular customer.

Of course, in this as in all other areas, NASD expects every associated person to comply with the procedures adopted by his firm.

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## Endnotes

- 1 The sale of an EIA registered under the federal securities laws is subject to the full panoply of regulation applicable to the sale of any security.  
  
The principles articulated in this *Notice* apply to EIAs that are sold by associated persons of a broker-dealer, whether the EIA has been manufactured by an insurance company that is affiliated with the broker-dealer or by an unaffiliated insurance company.
- 2 The Securities and Exchange Commission (the Commission) has previously stated that Congress intended any insurance contract falling within Section 3(a)(8) to be excluded from all provisions of the Securities Act notwithstanding the language of the Act indicating that Section 3(a)(8) is an exemption from registration but not the antifraud provisions. See Definition of "Annuity Contract or Optional Annuity Contract," Securities Act Release No. 6558 (Nov. 21, 1984), 49 Fed. Reg. 46750, 46753 (Nov. 28, 1984).
- 3 "A Do-It-Yourself Kit for Investors: Build Your Own Equity-Indexed Annuity," *The Wall Street Journal* (January 26, 2005).
- 4 The index return may be calculated in a variety of ways, such as the "annual reset" method, under which the index starting point is reset each contract year; the "point-to-point" method, under which the change in the index from the start of a term is compared to the index at the end of the term; and the "annual high-water mark with look-back" method, which is a variation on the point-to-point method except that it compares the index starting point to the highest anniversary value during the term.
- 5 Securities Act Release No. 6645, 35 SEC Docket 952 (May 29, 1986) (adopting Rule 151) ("Adopting Release").
- 6 Request for Comment on Equity-Indexed Products, Securities Act Release No. 7438; File No. S7-22-97 (August 20, 1997). At least one court has ruled on the question of whether an EIA is a security. The court granted a motion to dismiss based upon the finding that the EIA, which was the subject of litigation, in that case was exempt from the federal securities laws. See *Malone v. Addison Insurance Marketing*, 225 F. Supp. 2d 743 (W.D. Ky. 2002).

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# Notice to Members

AUGUST 2005

## SUGGESTED ROUTING

Capital Markets  
Executive Representatives  
Legal & Compliance  
Operations  
Senior Management  
Trading

## KEY TOPICS

Conflicts of Interest  
Order Handling  
Supervision

## ACTION REQUIRED

### Volume-Weighted Average Price Transactions

#### Member Obligations with Respect to Volume-Weighted Average Price Transactions

#### Executive Summary

NASD reminds members that when executing a volume-weighted average price (VWAP) or other large, potentially market-moving transactions for a customer,<sup>1</sup> it is inconsistent with just and equitable principles of trade (Rule 2110) and a member's best execution obligations (Rule 2320) to engage in proprietary trading activity that compromises the customer's interest in favor of a member's proprietary trading interest. Moreover, members who have received such orders have a duty to disclose in writing to the customer that the member may engage in hedging or other positioning activity that could affect the market for a security that is involved in the transaction. Depending on the nature of the order and the specificity known about it by the member, a duty to disclose such trading activity may arise even before a member is awarded the order for execution.

Members are further cautioned against manipulative activity or impermissible market conditioning in connection with executing a VWAP or other large order and reminded that best execution obligations always pertain once an order is received. Members also must establish and maintain information barriers and appropriate supervisory procedures reasonably designed to ensure the integrity of the trading activity and to evaluate the execution quality of VWAP and other large orders.

#### Questions/Further Information

Questions concerning this *Notice* may be directed to the Legal Section, Market Regulation, at (240) 386-5126; or Philip A. Shaikun, Associate General Counsel, Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8451.

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## Background and Discussion

Adherence to just and equitable principles of trade as mandated by Rule 2110 requires that members handle and execute any order received from a customer in a manner that does not disadvantage the customer or place the member's financial interests ahead of those of its customer. Furthermore, Rule 2320 requires a member to fill an order for a customer at a price as favorable as possible under prevailing market conditions; consequently, transactions by a member that disadvantage or place the member's financial interests ahead of those of its customer may violate Rule 2320. In the context of certain large, potentially market-moving orders—VWAPs, large institutional orders, and basket transactions, for example—a member's duty to a customer may arise even prior to the actual receipt of an order and may include an additional obligation to disclose hedging or other positioning activity that could affect the market for a security that is involved in the transaction.

The potential for the duty to arise prior to receipt of the order results from the process involved in negotiating and executing such large transactions. Typically, a customer will procure confidential bids to execute a large order in one or more stocks that could move the market if known publicly. In order to minimize its risk, a member that is awarded the order may engage in bona fide hedging or positioning activity prior to execution of the order. In some instances, members that are competing to fill the order also will enter into similar transactions in anticipation of winning the bid. Such trading activity might include buying or selling a security (if known) that is involved in the bid or buying an option or a future on the underlying security or basket of securities.

While these transactions do not constitute a per se violation of NASD rules, they can have an effect on the market for the security or securities that are the subject of the solicited transaction. For example, a member competing for a VWAP buy order might, in anticipation of winning the bid, begin to accumulate a sizeable position in the security that is being bought by the customer. Such buying activity could affect the trading price of the security and consequently the VWAP to the customer.<sup>2</sup>

When a member receives the customer's order, its duty to the customer is unequivocally established, and the member therefore is obligated to: (1) refrain from any conduct that could disadvantage or harm the execution of the customer's order or place the member's financial interests ahead of those of its customer's, and (2) if applicable, disclose in writing to the customer that the member intends to engage in hedging and other positioning activity that could affect the market for the security that is the subject of the transaction, and consequently the cost or proceeds to the customer (collectively referred to as "the duty to refrain and disclose"). The disclosure must be made prior to receipt and/or execution of the order and be in the form of an affirmative consent letter that covers potential hedging and positioning transactions related to the handling of VWAP and other large orders. Members need not obtain affirmative consent on a transaction-by-transaction basis; however, members should at least annually take steps to have their customers reaffirm their consent.

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Whether the same duty exists before a member is awarded an order for execution will turn on, among other factors, the type of order and the specifics of the order known by the member. Depending on the type of order, the specifics might include the name of the security, the size of the order, the side of the market (*i.e.*, buy or sell), the weighting of a basket order, and the timing for completion of the order. Thus, a duty could be established as early as the initial contact by the customer to seek bids for its order. In any event, once a member knows or has reason to know the order details to a degree of confidence whereby the member can engage without undue speculative risk in targeted hedging or positioning activity, then the same duty under Rules 2110 and 2320 to refrain and disclose attaches as if the member had actually received the order. This duty remains in place until the transaction is completed or the information upon which the member bid for the transaction becomes stale or obsolete. In addition, a member that bids unsuccessfully for the transaction, yet knows or has reason to know the order details to a degree of confidence, similarly must refrain from trading on, or communicating to another party, the information gleaned during the bidding process until the transaction is completed or the information becomes stale or obsolete, unless the trading is carried out by individuals who have been sufficiently walled off from obtaining the non-public information.

Other than for the purpose of fulfilling the customer order, under no circumstances may a member trade for its proprietary account on the non-public information it receives from the current or prospective customer or communicate such non-public information to another entity or person outside of the member. Such conduct is inconsistent with Rule 2110 and may also violate other NASD rules or the federal securities laws. A member may continue to engage in market making or proprietary trading in the subject securities only where the member has established effective information barriers reasonably designed to prevent internal disclosure of the non-public information.<sup>3</sup>

NASD cautions that, irrespective of whether a member is competing for or has received an order, under no circumstances may a member engage in manipulative market activity. Disclosure of hedging and positioning trading set forth above does not create a safe harbor from market manipulation, fraud, or best execution violations. Accordingly, members are reminded that they may not take any steps to create an artificial appearance of demand (supply) for the security or establish artificially high (low) prices by engaging in unnecessary trading, increased quote activity, or entering orders around the close of when a VWAP or other large order is executed. NASD will aggressively pursue any such conduct to manipulate or condition the market to achieve a favorable execution of a large customer order.<sup>4</sup>

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## Marking of Orders

Depending on the terms and characteristics of an order, a VWAP or similar transaction must be classified as either long or short for purposes of order entry and reporting. Short sale orders must be executed in compliance with all applicable NASD and SEC short sale rules and regulations. With respect to a VWAP, both the individual trades by the member to accommodate the VWAP and the aggregate VWAP trade itself are subject to those short sale rules and regulations. In the event that a member is short the securities underlying a VWAP sell order, the member's order(s) may need to be marked "short" (or "short exempt," if applicable), depending on the firm's (or aggregation unit's) overall position, even if the customer is long the subject securities. Members should refer to applicable NASD and SEC rules, interpretations, and no-action letters when determining how to mark the individual trades by the member to accommodate the VWAP and the aggregate VWAP trade itself.

Failure to accurately mark orders also may result in disciplinary action for failure to maintain proper books and records.

## Compensation

Members that receive a VWAP or similar order must disclose to the customer in writing the specifics of the terms of compensation it will receive to execute the order. Thus, for example, a member must disclose if it intends to retain or split with the customer any profits that result if the member improves upon the VWAP.

## Supervision

Pursuant to Rule 3010, members must have in place supervisory procedures reasonably designed to ensure that the order handling and trading activities discussed in this *Notice* comply with NASD Rules and the applicable federal securities laws. Thus, members should establish and maintain adequate procedures to evaluate the quality of execution of VWAP and other large orders. Those procedures should include, without limitation, an evaluation of proprietary trading that took place in advance of the execution of such orders. If applicable, the procedures also should be designed reasonably to ensure that customers affirmatively acknowledged the receipt of notice that the member may engage in hedging or other trading activity related to the execution of the customer's order.

Members should specify in their written supervisory procedures the circumstances under which hedging or positioning trades will be reviewed and identify which trades will be reviewed and the manner in which such review will take place. The written procedures further should identify who will conduct the review, how often the review will occur, what steps should be taken if suspicious activity is discovered, and how the discharge of the supervisory responsibilities will be documented. In addition, members should establish and maintain adequate information barriers to prevent and surveil for suspect simultaneous trading away from the sales desk.

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## Endnotes

- 1 Consistent with NASD Rule 0120(g), the term "customer order" for purposes of this *Notice* shall not include an order received from another broker-dealer.
- 2 Members are encouraged to review the March 2004 decision of the United Kingdom's Financial Services Authority in which it levied a £190,000 fine against Morgan Grenfell & Company Limited for failing to disclose its hedging activity in anticipation of winning a blind bid to execute a customer's program trade. The firm's proprietary trading caused the customer to pay more to execute the transaction. The decision and findings can be found at: [www.fsa.gov.uk/pubs/final/m-grenfell\\_18mar\\_04.pdf](http://www.fsa.gov.uk/pubs/final/m-grenfell_18mar_04.pdf).
- 3 Even where a duty exists to a customer, a member is not precluded from all trading activity related to the subject securities or required to disclose every such transaction. Thus, for example, members may execute: a prior customer order; bona fide hedge transactions that the member can demonstrate are unrelated to the information received in connection with the VWAP or other large customer orders and where the member has information barriers established to prevent internal disclosure of non-public information; "black box" orders where the member has no actual knowledge that such order has been routed for execution; trades to correct a bona fide error; and odd-lot transactions to offset odd-lot orders. Furthermore, this *Notice* is not intended to prevent a member from handling multiple customers' orders that might compete with or disadvantage each other. However, it may be a violation of Rule 2110 for a member to share information about the order other than to facilitate that specific customer transaction.
- 4 This *Notice* is not intended to set out all violations that may occur in connection with the execution of VWAP orders and other large orders; members should be aware that the conduct described may also violate other NASD rules or federal securities laws.

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# Notice to Members

AUGUST 2005

## SUGGESTED ROUTING

Legal and Compliance  
Operations  
Registered Representatives  
Senior Management  
Technology  
Training

## KEY TOPICS

Debt Securities  
Operations  
Rule 7010  
Transaction Reporting

GUIDANCE

## Trade Reporting and Compliance Engine (TRACE)

SEC Approves Amendments to TRACE Fee Structure Establishing an Enterprise Fee and Lowering Fee for Receipt of Real-Time TRACE Transaction Data via Web Browser; **Effective Date: October 1, 2005**

### Executive Summary

On August 1, 2005, the Securities and Exchange Commission (SEC or Commission) approved an amendment to Rule 7010(k), adding an enterprise fee structure and lowering another fee related to the receipt of Real-Time TRACE transaction data. This fee change will enable an enterprise such as a broker-dealer to display Real-Time TRACE transaction data on an unlimited number of internal display devices for a fee of \$7,500 per month. The fee for Level II Full Service Web Browser Access also has been lowered, so that the charge for the first user ID obtained for such access will be \$50 per month rather than the current \$80 per month.

The rules, as amended, are set forth in Attachment A.

The amendments become effective October 1, 2005.

### Questions/Further Information

Questions concerning this *Notice* should be directed to James L. Eastman, Assistant General Counsel, Office of General Counsel (OGC), Regulatory Policy and Oversight (RPO), at (202) 728-6961; Sharon K. Zackula, Associate General Counsel, OGC, RPO, at (202) 728-8985; or David Lefferts, Associate Vice President, Corporate Debt, at (212) 858-4389.

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## Background and Discussion

On August 1, 2005, the SEC approved an amendment to Rule 7010(k)(3)(A)(i), the Bond Trade Dissemination Service (BTDS) Professional Real-Time Data Display Fee, to enable an enterprise such as a broker-dealer to display Real-Time TRACE transaction data within the enterprise on an unlimited number of internal display devices for a fee of \$7,500 per month.<sup>1</sup> The SEC also approved an amendment to Rule 7010(k)(1)(A), Web Browser Access, to lower the fee for Level II Full Service Web Browser Access, so that the charge for the first user ID obtained for such access will be \$50 per month rather than the current \$80 per month.

NASD has modified the TRACE fee structure because NASD believes the new structure may significantly increase the use of Real-Time TRACE transaction data among users of such data (Subscribers) such as registered representatives, investment advisors, and other persons serving retail investors, as well as address cost concerns that have been expressed by members. NASD believes that broadening the distribution of Real-Time TRACE transaction data will facilitate its use by persons who provide brokerage and/or advisory services to retail investors, and will provide such professionals with an additional tool to better serve and inform retail investors. Moreover, broadening the distribution of Real-Time TRACE transaction data is likely to have an incremental, beneficial effect on corporate bond market transparency and pricing by generally raising the level of awareness and overall knowledge of specific bond issues as well as the bond market generally.

### Proposed "Enterprise" Fee

Currently, NASD charges Subscribers \$60 per month, per terminal (the BTDS Professional Real-Time Data Display Fee) to display Real-Time TRACE transaction data. Members have indicated that this \$60 per month, per terminal charge is cost prohibitive for organizations with large numbers of potential internal users of the data. Subscribers serving large numbers of retail investors have indicated that they likely would distribute Real-Time TRACE transaction data much more widely within their organizations if the costs were reduced.

To address these concerns, NASD has amended Rule 7010(k)(3)(A)(i) to provide Subscribers the option of paying a flat, enterprise fee of \$7,500 per month instead of \$60 per terminal (*i.e.*, per screen or interrogation or display device). This amendment is intended to benefit Subscribers that have a large staff of potential internal data users who desire access to Real-Time TRACE transaction data. Instead of paying multiple \$60 BTDS Professional Real-Time Data Display Fees, a Subscriber would have the option to pay a flat fee of \$7,500 per month to display Real-Time TRACE transaction data on an unlimited number of internal terminals/workstations.

The proposed amendment to Rule 7010(k)(3)(A)(i) will apply only to a Subscriber's internal display of Real-Time TRACE transaction data and will be independent of access method or data vendor. The proposed \$7,500 enterprise fee option will include unlimited terminal display use for individual access for all of a Subscriber's employees and the employees of certain of its corporate affiliates.<sup>2</sup>

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### Level II Full Service Web Browser Access Fee

To encourage use of Real-Time TRACE transaction data among Subscribers of varying sizes, NASD also has amended Rule 7010(k)(1)(A) to reduce the fees paid by Subscribers who receive Real-Time TRACE transaction data through Level II Full Service Web Browser Access. Such smaller Subscribers are unlikely to directly benefit from the new enterprise pricing structure.

Currently, the implicit cost for Level II Full Service Web Browser Access used to receive Real-Time TRACE transaction data is \$60 per month (per user ID).<sup>3</sup> NASD has reduced the cost of the first user ID per Subscriber to receive Level II Full Service Web Browser Access from \$80 per month to \$50 per month. This change will reduce a Subscriber's marginal cost for the data portion of Level II Full Service Web Browser Access for the first user ID by 50 percent to \$30 per month.

### Endnotes

- 1 See Securities Exchange Act Release No. 52183 (August 1, 2005), 70 FR 46239 (August 9, 2005) (SR-NASD-2005-063).
- 2 A Subscriber wishing to take advantage of this option must first enter into an agreement directly with NASD, which in turn will notify the data vendors with which the Subscriber does business to provide blanket permission for use of Real-Time TRACE transaction data to any user within that organization. A Subscriber interested in this option should contact NASD's TRACE group at (888) 507-3665.
- 3 Level II Full Service Web Browser Access today costs \$80 per month. However, Level II Full Service Web Browser Access also grants users Level I Web Trade Report Only Browser Access (for trade reporting), which otherwise would cost an additional \$20 per month per user ID. Therefore, prior to the fee changes adopted by NASD the marginal cost of Level II Full Service Web Browser Access was \$60 per month, per user ID.

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## ATTACHMENT A

### 7010. System Services

(a) through (j) No change.

#### (k) Trade Reporting and Compliance Engine (TRACE)

The following charges shall be paid by participants for the use of the Trade Reporting and Compliance Engine ("TRACE"):

System Fees	Transaction Reporting Fees	Market Data Fees
Level I Trade Report Only Web Browser Access - \$20/month per user ID  Level II Full Service Web Browser Access - \$80/month per user ID, <u>except that the charge for the first such user ID shall be \$50/month</u>	Trades up to and including \$200,000 par value - \$0.475/trade; Trades between \$201,000 and \$999,999 par value - \$0.002375 times the number of bonds traded/ trade; Trades of \$1,000,000 par value or more - \$2.375/trade	BTDS Professional Real-Time Data Display - \$60/month per terminal, <u>or a flat fee of \$7,500/month entitling Professionals to make unlimited internal use of Real-Time TRACE transaction data on any number of interrogation or display devices</u>
CTCI/Third Party - \$25/month/per firm	Cancel/Correct - \$1.50/trade	Vendor Real-Time Data Feed - \$1,500/month for Real-Time TRACE transaction data, except for qualifying Tax-Exempt Organizations
	"As of" Trade Late - \$3/trade	Vendor Real-Time Data Feed - \$400/month for Real-Time TRACE transaction data for qualifying Tax-Exempt Organizations
		BTDS TRACE Non-Professional Real-Time Data Display – No charge

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## **(1) System Related Fees**

There are three methods by which a member may report corporate bond transactions that are reportable to the Association pursuant to the Rule 6200 Series. A member may choose among the following methods to report data to the Association: (a) a TRACE web browser; (b) a Computer-to-Computer Interface ("CTCI") (either one dedicated solely to TRACE or a multi-purpose line); or (c) a third-party reporting intermediary. Fees will be charged based on the reporting methodology selected by the member.

### **(A) Web Browser Access**

The charge to be paid by a member that elects to report TRACE data to NASD via a TRACE web browser shall be as follows: \$20 per month, per user ID for Level I Web Trade Report Only Browser Access and \$80 per month, per user ID for Level II Full Service Web Browser Access, except that the charge for the first such user ID for Level II Full Service Web Browser Access shall be \$50 per month.

(B) No change.

(C) No change.

## **(2) Transaction Reporting Fees**

For each transaction in corporate bonds that is reportable to the Association pursuant to the Rule 6200 Series, the following charges shall be assessed against the member responsible for reporting the transaction:

(A) through (C) No change.

## **(3) Market Data Fees**

Professionals and Non-Professionals may subscribe to receive Real-Time TRACE transaction data disseminated by NASD in one or more of the following ways for the charges specified, as applicable. Members, vendors and other redistributors shall be required to execute appropriate agreements with NASD.

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**(A) Professional Fees**

Professionals may subscribe for the following:

(i) Bond Trade Dissemination Service (“BTDS”) Professional Real-Time Data Display Fee of \$60 per month, per terminal charge for each interrogation or display device receiving Real-Time TRACE transaction data, or a flat fee of \$7,500 per month entitling Professionals to make unlimited internal use of Real-Time TRACE transaction data on any number of interrogation or display devices.

(ii)-(iii) No change.

(B) through (D) No change.

(l) through (v) No change.

# Special Notice to Members

AUGUST 25, 2005

INFORMATIONAL

## SUGGESTED ROUTING

Legal and Compliance  
Senior Management

## KEY TOPICS

National Adjudicatory Council

## NAC Nominee

NASD Announces Nominee for Regional Industry  
Member Vacancy on the National Adjudicatory Council

### Executive Summary

The purpose of this *Special Notice to Members* is to announce the nominee for the National Adjudicatory Council (NAC) from the North Region. The nominee, nominated for a three-year term beginning in January 2006, is listed in Exhibit I. The nominee will be proposed to NASD's National Nominating Committee unless an additional candidate comes forward within 14 calendar days from the date of this Special Notice.

We appreciate the interest shown by many members in expressing their desire to serve on the NAC and thank everyone for their continuing support of the self-regulatory process. The North Regional Nominating Committee thoroughly reviewed the background of every candidate before selecting their nominee in an effort to secure appropriate and fair representation of the region.

### Contested Election Procedures

If an officer, director, or employee of an NASD member in the North Region has not been proposed for nomination by the Regional Nominating Committee and wants to seek the nomination, he or she should send a written notice to Barbara Z. Sweeney, NASD's Corporate Secretary, at the address below within 14 calendar days after the publishing date (August 25) of this *Special Notice*.

Barbara Z. Sweeney  
NASD  
Office of the Corporate Secretary  
1735 K Street, NW  
Washington, DC 20006-1506

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The Contested Nomination Procedures can be found in Article VI of the NASD Regulation By-Laws. If no additional candidate comes forward within 14 calendar days, the North Regional Nominating Committee shall certify its candidate to the National Nominating Committee.

## Questions/Further Information

Questions concerning this *Special Notice* may be directed to Barbara Z. Sweeney, Senior Vice President and Corporate Secretary, at (202) 728-8062, or via email at: [barbara.sweeney@nasd.com](mailto:barbara.sweeney@nasd.com).

## National Adjudicatory Council Membership and Function

### Membership

The NAC consists of 14 members—seven Industry members and seven Non-Industry members. Two Industry members are nominated by NASD's National Nominating Committee and are appointed by the Board of Directors of NASD Regulation, Inc., as at-large members. Five Industry members each represent one of the following geographic regions:

- Midwest Region:** Illinois, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota, and Wisconsin (Districts 4 and 8)
- New York:** New York (the counties of Nassau and Suffolk, and the five boroughs of New York City) (District 10)
- North Region:** Connecticut, Delaware, the District of Columbia, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York (except for the counties of Nassau and Suffolk, and the five boroughs of New York City), Pennsylvania, Rhode Island, Vermont, Virginia, and West Virginia (Districts 9 and 11)
- South Region:** Alabama, Arkansas, Florida, Georgia, Louisiana, Mississippi, North Carolina, Oklahoma, South Carolina, Tennessee, Texas, the Canal Zone, Puerto Rico, and the Virgin Islands (Districts 5, 6, and 7)
- West Region:** Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington, Wyoming, and the former U.S. Trust Territories (Districts 1, 2, and 3)

One region (North) has a vacancy for this election. NAC members for the other four regions (New York, Midwest, South, and West) are indicated in Exhibit II, along with the year in which their terms expire.

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### **Function**

According to the NASD Regulation By-Laws, the NAC is authorized to act for the NASD Board of Governors in matters concerning:

- ◆ appeals or reviews of disciplinary proceedings, statutory disqualification proceedings, or membership proceedings;
- ◆ the exercise of exemptive authority; and
- ◆ other proceedings or actions authorized by the Rules of NASD.

The NAC also considers and makes recommendations to the Board on enforcement policy and rule changes relating to the business and sales practices of NASD members and associated persons.

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### **EXHIBIT I**

#### **Nominee for NAC Industry Member Vacancy**

<b>North Region (Districts 9 and 11)</b>	<b>Stephanie L. Brown</b>	Linsco/Private Ledger Corporation	Boston, MA
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### **EXHIBIT II**

#### **NAC Member with Term Expiring in January 2006**

<b>North Region</b>	<b>A. Louis Denton</b>	Philadelphia Corporation for Investment Services	Philadelphia, PA
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#### **NAC Members with Terms Expiring in January 2007**

<b>New York</b>	<b>Judith R. MacDonald</b>	Rothschild, Inc.	New York, NY
<b>West Region</b>	<b>Neal E. Nakagiri</b>		Van Nuys, CA

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#### **NAC Members with Terms Expiring in January 2008**

<b>Midwest Region</b>	<b>Timothy Henahan</b>	Baker & Co., Inc.	Rocky River, OH
<b>South Region</b>	<b>W. Dennis Ferguson</b>	Sterne Agee Clearing	Boca Raton, FL

# Notice to Members

AUGUST 2005

## SUGGESTED ROUTING

Legal and Compliance

## KEY TOPICS

Discovery-Related Motions

Dispute Resolution

## GUIDANCE

### Discovery-Related Motions

SEC Approves Amendments to IM-10104 to Provide Payment to Arbitrators for Deciding Discovery-Related Motions; **Effective Date: September 26, 2005**

#### Executive Summary

The Securities and Exchange Commission (SEC) has approved an amendment to Interpretive Material (IM) 10104 of the NASD Code of Arbitration Procedure (Code) to provide payment to arbitrators for deciding discovery-related motions without a hearing session.<sup>1</sup>

The text of the amendment is set forth in Attachment A. The amendment will become effective on **September 26, 2005**, and will apply to any arbitrator order issued on or after September 26, 2005, that decides a discovery-related motion.

#### Questions/Further Information

Questions regarding this *Notice* may be directed to Mignon McLemore, Assistant Chief Counsel, NASD Dispute Resolution, at (202) 728-8151, or via email at [mignon.mclemore@nasd.com](mailto:mignon.mclemore@nasd.com).

#### Background and Discussion

When parties have a dispute over the pre-hearing production of information or documents ("discovery"), an arbitrator may choose to hold a hearing to hear arguments from the parties.<sup>2</sup> The arbitrator conducts such hearings as pre-hearing telephone conferences, for which the arbitrator receives an honorarium of \$200. Arbitrators currently are not, however, compensated for deciding discovery-related motions without a hearing ("on the papers"). In arbitrator focus groups conducted across the country, one of the consistently raised concerns was the amount of time and effort invested by arbitrators, particularly chairpersons, in reviewing and deciding various discovery motions. NASD considered these concerns and determined that the arbitrators performed a substantial amount of uncompensated work in resolving discovery-related motions.

05-55

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In light of these findings, NASD has amended IM-10104 of the Code to provide payment to arbitrators for deciding discovery-related motions without a hearing session. NASD believes this amendment will motivate a greater number of arbitrators to accept assignments as chairpersons, thus expanding the pool of qualified arbitrators willing to serve in this role. Moreover, NASD believes the amendment will encourage arbitrators to decide discovery-related motions on the papers without scheduling a pre-hearing conference, thereby expediting the pace of arbitrations.

Under amended IM-10104, an arbitrator will be paid \$200 to decide a discovery-related motion without a hearing session. This is the same amount an arbitrator receives to participate in a pre-hearing conference regarding discovery. For purposes of amended IM-10104, a discovery-related motion and any replies or other correspondence relating to the motion will be considered to be a single motion.<sup>3</sup> If more than one arbitrator considers a discovery-related motion, each arbitrator will receive \$200. The panel will allocate the cost of the honoraria as part of the allocation of fees in the eventual arbitration award. The rule will not apply to simplified cases administered under Rules 10203 and 10302.

## Effective Date Provisions

The amendment described in this *Notice* will become effective on **September 26, 2005**. The amendment will apply to any arbitrator order issued on or after September 26, 2005, that decides a discovery-related motion.

## Endnotes

- 1 Exchange Act Release No. 51931 (June 28, 2005) (File No. SR-NASD-2005-052), 70 Federal Register 38989 (July 6, 2005).
- 2 Rule 10321(d) provides that the Director of Arbitration may appoint a person to preside at a pre-hearing conference to deal with the exchange of information, the exchange or production of documents, identification of witnesses, and other pre-hearing matters. Normally, the single arbitrator or the chair of a three-arbitration panel will be appointed to preside.
- 3 A motion for sanctions for failure to comply with discovery will be considered a "discovery-related" motion.

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## ATTACHMENT A

New language is underlined; deletions are in brackets.

### Code of Arbitration Procedure

\* \* \*

#### IM-10104. Arbitrators' Honorarium

(a) All persons selected to serve as arbitrators pursuant to the Association's Code of Arbitration Procedure shall be paid an honorarium for each hearing session (including a prehearing conference) in which they participate.

(b) The honorarium shall be \$200 for each hearing session and \$75 per day additional honorarium to the chairperson of the panel. The honorarium for a case not requiring a hearing shall be \$125.

(c) The honorarium for travel to a canceled hearing session shall be \$50. If a hearing session other than a prehearing conference is adjourned pursuant to Rule 10319(d), each arbitrator shall receive an additional honorarium of \$100.

(d) The Director may authorize a higher or additional honorarium for the use of a foreign hearing location.

#### (e) Payment for Deciding Discovery-Related Motions Without a Hearing Session

(1) NASD will pay each arbitrator an honorarium of \$200 to decide a discovery-related motion without a hearing session. This paragraph does not apply to cases administered under Rules 10203 and 10302.

(2) For purposes of paragraph (e)(1), a discovery-related motion and any replies or other correspondence relating to the motion shall be considered to be a single motion.

(3) The panel will allocate the cost of the honoraria under paragraph (e)(1) to the parties pursuant to Rules 10205(c) and 10332(c).

\* \* \*

# Notice to Members

AUGUST 2005

## SUGGESTED ROUTING

Institutional  
Legal & Compliance  
Options  
Senior Management  
Trading  
Training

## KEY TOPICS

Exercise Limits  
Options  
Position Limits  
Rule 2860

## GUIDANCE

### Options Position and Exercise Limits

#### Extension of Pilot Program Increasing Position and Exercise Limits for Stock Options

#### Executive Summary

On August 10, 2005, NASD filed for immediate effectiveness with the Securities and Exchange Commission (SEC) amendments to Rule 2860, which extend a pilot program that increases certain stock options position and exercise limits to **March 3, 2006**. The pilot program was scheduled to expire on September 2, 2005.

The rules, as amended, are set forth in Attachment A. The amendments became effective August 10, 2005.

#### Questions/Further Information

Questions concerning this *Notice* may be directed to Gary L. Goldsholle, Associate Vice President and Associate General Counsel, Office of General Counsel (OGC), Regulatory Policy and Oversight (RPO), at (202) 728-8104, or James L. Eastman, Assistant General Counsel, OGC, RPO, at (202) 728-6961.

#### Background and Discussion

On August 10, 2005, NASD filed for immediate effectiveness with the Securities and Exchange Commission (SEC) amendments to Rule 2860, which extend a pilot program that increases certain stock options position and exercise limits to **March 3, 2006**.<sup>1</sup> The pilot program was scheduled to expire on September 2, 2005.<sup>2</sup> NASD extended the pilot program to allow it to continue without interruption and to conform to similar pilot programs that were recently extended by other self-regulatory organizations (SROs) with options rules.<sup>3</sup>

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NASD Rule 2860(b)(3)(A) imposes a ceiling or position limit on the number of conventional and standardized equity options contracts in each class on the same side of the market (*i.e.*, aggregating long calls and short puts, or long puts and short calls) that can be held or written by a member, a person associated with a member, a customer, or a group of customers acting in concert.<sup>4</sup> The rule provides that the position limits for stock options are determined according to a five-tiered system in which more actively traded stocks with larger public floats are subject to higher position limits. Pursuant to a pilot program that began March 30, 2005, and now ends March 3, 2006, (unless extended) (Pilot Period), the limits for each of the tiers remains increased as follows: a) 13,500 contracts has been increased to 25,000 contracts, b) 22,500 contracts has been increased to 50,000 contracts, c) 31,500 contracts has been increased to 75,000 contracts, d) 60,000 contracts has been increased to 200,000 contracts, and e) 75,000 contracts has been increased to 250,000 contracts. These tiers apply to both conventional and standardized options. Options exercise limits, which are set forth in Rule 2860(b)(4), and which incorporate by reference the position limits in Rule 2860(b)(3), also have been increased during the Pilot Period.

## Endnotes

- 1 Securities Exchange Act Release No. 52271 (August 16, 2005), 70 FR 49344 (August 23, 2005) (SR-NASD-2005-097).
- 2 See Securities Exchange Act Release No. 51520 (April 11, 2005), 70 FR 19977 (April 15, 2005) (SR-NASD-2005-040); NASD Notice to Members 05-31 (April 2005).
- 3 See Securities Exchange Act Release No. 52260 (August 15, 2005), 70 FR 48991 (August 22, 2005) (SR-AMEX-2005-082); Securities Exchange Act Release No. 52261 (August 15, 2005), 70 FR 49004 (August 22, 2005) (SR-PHLX-2005-51); Securities Exchange Act Release No. 52262 (August 15, 2005), 70 FR 48995 (August 22, 2005) (SR-CBOE-2005-61); Securities Exchange Act Release No. 52263 (August 15, 2005), 70 FR 49003 (August 22, 2005) (SR-PCX-2005-95); Securities Exchange Act Release No. 52264 (August 15, 2005), 70 FR 48992 (August 22, 2005) (SR-BSE-2005-37); Securities Exchange Act Release No. 52265 (August 15, 2005), 70 FR 48996 (August 22, 2005) (SR-ISE-2005-39).
- 4 A "standardized equity option" is an equity options contract issued, or subject to issuance by, The Options Clearing Corporation that is not a FLEX Equity Option. NASD Rule 2860(b)(2)(VV). A "conventional option" is an option contract not issued, or subject to issuance by, The Options Clearing Corporation. NASD Rule 2860(b)(2)(N). NASD's limits on standardized equity options are applicable only to those members that are not also members of the exchange on which the option is traded; the limits on conventional options are applicable to all NASD members. NASD Rule 2860(b)(1)(A).

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## ATTACHMENT A

Additions are underlined; deletions are in brackets.

### 2800. SPECIAL PRODUCTS

#### 2860. Options

(a) No Change.

(b) Requirements.

(1) and (2) No Change.

#### (3) Position Limits

(A) Stock Options—Except in highly unusual circumstances, and with the prior written approval of NASD pursuant to the Rule 9600 Series for good cause shown in each instance, no member shall effect for any account in which such member has an interest, or for the account of any partner, officer, director or employee thereof, or for the account of any customer, non-member broker, or non-member dealer, an opening transaction through Nasdaq, the over-the-counter market or on any exchange in a stock option contract of any class of stock options if the member has reason to believe that as a result of such transaction the member or partner, officer, director or employee thereof, or customer, non-member broker, or non-member dealer, would, acting alone or in concert with others, directly or indirectly, hold or control or be obligated in respect of an aggregate equity options position in excess of:

(i) 13,500 (or 25,000 during the pilot period from March 30, 2005 through [September 2, 2005] March 3, 2006 (“Pilot Period”)) option contracts of the put class and the call class on the same side of the market covering the same underlying security, combining for purposes of this position limit long positions in put options with short positions in call options, and short positions in put options with long positions in call options; or

(ii) through (viii) No Change.

(B) through (D) No Change.

(4) through (24) No Change.

# Disciplinary and Other NASD Actions

## REPORTED FOR AUGUST

NASD® has taken disciplinary actions against the following firms and individuals for violations of NASD rules; federal securities laws, rules, and regulations; and the rules of the Municipal Securities Rulemaking Board (MSRB). The information relating to matters contained in this *Notice* is current as of the end of July 2005.

### Firms Fined, Individuals Sanctioned

**David A. Noyes & Company (CRD #205, Chicago, Illinois) and Anthony Michael Quirini (CRD #369593, Registered Principal, Kenilworth, Illinois)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$10,000, jointly and severally with Quirini. The firm was fined an additional \$30,000, and must obtain a "no objection" letter from the NASD Advertising Regulation Department on any proposed sales literature or advertising prior to its use for one year. Quirini was suspended from association with any NASD member in any capacity for 10 business days. Without admitting or denying the allegations, the firm and Quirini consented to the described sanctions and to the entry of findings that Quirini created and distributed sales literature in the manner of form letters to the public that the firm failed to file with NASD's Advertising Regulation Department. NASD found that these form letters contained statements that exaggerated the safety of the products and failed to reflect the risks of fluctuating prices and the uncertainty of rates of return and the yield of investments.

The findings stated that the form letters failed to provide balanced presentations of the risks and rewards of the products offered, failed to disclose material information regarding the risks of each proposed investment, and failed to provide a sound basis for evaluating the recommendations contained in the letters. The findings also stated that the firm failed to adequately and properly supervise the use of these form letters and failed to establish, maintain, and enforce adequate written supervisory procedures designed to achieve compliance with applicable securities laws and regulations.

Quirini's suspension began July 18, 2005, and concluded at the close of business July 29, 2005. (NASD Case # C8A050058)

**Jersey Shore Trading Group, Inc. (CRD #47440, Red Bank, New Jersey) and John F. Helbock (CRD #1593811, Registered Principal, Holmdel, New Jersey)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$25,000, \$15,000 of which was jointly and severally with Helbock. Helbock was suspended from association with any NASD member in any principal or supervisory capacity for 30 business days. Without admitting or denying the allegations, the firm and Helbock consented to the described sanctions and to the entry of findings that the firm, acting through Helbock, permitted a statutorily disqualified person to be associated with and conduct activities on behalf of the firm. NASD also found that the

firm executed order tickets for equity and municipal transactions that were deficient. The findings also stated that the firm was late in reporting municipal securities transactions executed by the firm.

Helbock's suspension began July 5, 2005, and will conclude at the close of business August 15, 2005. (NASD Case #C9B050038)

**Stoever, Glass & Company Inc., (CRD # 7031, New York, New York) and Michael Francis Carrigg (CRD #1061325, Registered Principal, Sandy Hook, Connecticut)** submitted a Letter of Acceptance, Waiver, and Consent in which they were censured and fined \$7,500, jointly and severally. The firm was fined an additional \$5,000, and Carrigg was suspended from association with any NASD member in any financial and operations principal (FINOP) capacity for 10 business days. Without admitting or denying the allegations, the firm and Carrigg consented to the described sanctions and to the entry of findings that the firm commingled customer securities with non-customer securities to collateralize bank loans. The findings also stated that the firm, acting through Carrigg, collateralized the loan set up for firm trades with a customer security position that was not fully paid and permitted a customer's fully paid securities to remain in a non-control location for an extended period of time. In addition, NASD determined that the firm neglected to report to the Trade Reporting and Compliance Engine (TRACE) the underlying yield to inter-dealer corporate debt security transactions. NASD also found that the firm failed to make a timely transaction report to TRACE.

Carrigg's suspension began July 5, 2005, and concluded at the close of business July 18, 2005. (NASD Case #C10050045)

**Strasbourg Pearson Tulcin Wolff Inc. (CRD #5133, New York, New York) and Michael J. Schumacher (CRD #415895, Registered Principal, Purchase, New York)** submitted a Letter of Acceptance, Waiver, and Consent in which they were fined \$12,500, jointly and severally. The firm was censured and fined an additional \$17,500, and Schumacher was suspended from association with any NASD member in all principal capacities for 15 business days. Without admitting or denying the allegations, the firm and Schumacher consented to the described sanctions and to the entry of findings that the firm, acting through Schumacher, failed to establish and maintain a supervisory system, including adequate written supervisory procedures, reasonably designed to achieve compliance by the firm and its representatives with numerous NASD rules. The findings also stated that the firm, acting through Schumacher, permitted a registered representative to conduct a securities business while his registration was inactive. In addition, NASD determined that the firm failed to conduct independent testing of its anti-money laundering (AML) compliance programs, collect all

required information for wire order/transfers, review wire orders, and verify the identities of customers who open accounts in violation of NASD Rules 2110 and 3011.

Schumacher's suspension began July 5, 2005, and concluded at the close of business July 25, 2005. (NASD Case #C07050040)

## Firm and Individual Fined

**Coburn & Meredith, Inc. (CRD #164, Hartford, Connecticut) and Barry Mohun Coburn (CRD #49264, Registered Principal, West Simsbury, Connecticut)** submitted a Letter of Acceptance, Waiver, and Consent in which they were censured and fined \$10,000, jointly and severally. The firm was fined an additional \$7,500, \$5,000 of which was assessed jointly and severally with another individual. Without admitting or denying the allegations, the firm and Coburn consented to the described sanctions and to the entry of findings that the firm, acting through an individual, failed to comply with their claimed exemption under Section 15c of the Exchange Act, Rule 15c3-3(k)(2)(ii) in that the firm received checks made payable to the firm rather than to the firm's clearing firm. NASD also found that the firm, acting through an individual, used the instrumentalities of interstate commerce to conduct a securities business while failing to maintain its required minimum net capital. NASD determined that the firm, acting through Coburn, failed to establish, maintain, and enforce written procedures reasonably designed to achieve compliance with applicable securities laws, regulations, and NASD rules regarding the receipt of customer checks. The findings also stated that the firm was late in filing municipal securities transaction reports to the Municipal Securities Rulemaking Board (MSRB). In addition, NASD found that the firm, acting through Coburn, sent confirmations to customers involving municipal transactions that improperly disclosed to the customer that the firm was acting in a principal capacity when, in fact, the transactions effected involved cross trades between the customer and another person. (NASD Case #C11050018)

## Firms Fined

**Ariel Distributors, Inc. (CRD #38333, Chicago, Illinois)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$40,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it used the mails or other means of interstate commerce to effect transactions in securities when it failed to maintain the minimum required net capital. The findings also stated that the firm prepared inaccurate trial balances, general ledgers,

and net capital computations. NASD also found that the firm filed FOCUS (Financial and Operational Combined Uniform Single) IIA reports and an annual audit that overstated the member's net capital. In addition, NASD found that the firm failed to implement and exercise adequate supervisory controls to monitor and verify the accuracy of the amounts of 12b-1 fees payable that were computed by a non-affiliated entity that resulted in inaccurate net capital computations. **(NASD Case #C8A050056)**

**Chicago Investment Group, L.L.C. (CRD #11853, Chicago, Illinois)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$22,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it used the mails or other means or instrumentalities of interstate commerce to effect transactions in securities when it failed to maintain the minimum required net capital. The findings also stated that the firm prepared inaccurate trial balances, general ledgers, and net capital computations. The findings also stated that the firm filed FOCUS IIA reports that overstated the member's net capital. NASD found that the firm failed to prepare and maintain adequate written supervisory procedures to ensure that employees whose registrations were subject to numerous strict supervisory guidelines and restrictions by several state securities regulators remained in compliance with those restrictions. NASD also found that the firm failed to obtain NASD approval prior to effecting a material change in business operations in that the firm increased the number of associated persons involved in sales activities beyond the limits delineated in IM-1011-1. **(NASD Case #C8A050052)**

**CJS Securities, Inc. (CRD #44823, White Plains, New York)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$40,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it permitted its analysts to sell securities issued by companies for which the analysts were primarily responsible for research coverage at times when the firm's recommendation was to buy or hold the security. The findings stated that the firm's analysts bought or sold securities issued by companies for which the analysts were primarily responsible for research coverage during a period of time prior to or after the issuance of research reports concerning those companies. The findings also stated that the firm issued research reports covering companies from which the firm had received, or expected to receive, compensation for investment banking services in connection with participation in public offerings of the companies' securities. NASD found that the firm did not have written supervisory procedures reasonably designed to achieve compliance with NASD Rule 2711. **(NASD Case #C3A050031)**

**Equity Trading Online, LLC (CRD #104038, New York, New York)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$13,500, \$6,000 of which was jointly and severally with an individual. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it permitted an individual to park his registration with the firm by maintaining his registration as a general securities representative through his purported association with the firm when, in fact, he was not actively involved in the firm's securities or investment banking business or otherwise functioning as a representative of the firm. NASD found that the firm, acting through an individual, failed to designate properly a branch office as an Office of Supervisory Jurisdiction (OSJ). In addition, NASD determined that the firm inaccurately reported to the MSRB the capacity for transactions by publishing an extraneous transaction report, failing to timely report transactions, and inaccurately reporting inter-dealer transactions as customer transactions. The findings also stated that the firm failed to report accurately the capacity on certain customer confirmations. **(NASD Case #C10050057)**

**The Huntington Investment Company (CRD #16986, Columbus, Ohio)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$10,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it paid non-cash compensation for a sales contest that weighted the firm's proprietary mutual funds and variable annuity products more than other investment products offered by the firm. **(NASD Case #C8A050063)**

**LaSalle Street Securities, LLC (CRD #7191, Elmhurst, Illinois)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured, fined \$125,000, and required to disgorge \$46,500 and pay \$46,281.84 in restitution. The firm was also required to certify to NASD, within 90 days, that it has reviewed its procedures regarding market timing and the preservation and retention of electronic mail communications, and that it has established systems and procedures reasonably designed to achieve compliance with applicable laws, regulations, and rules relating to market timing activities and the preservation and retention of electronic mail communications.

Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that the firm, through a registered representative, facilitated deceptive market timing practices in the sub-accounts of variable annuities for a hedge fund client by enabling the hedge fund client to use accounts to carry out frequent transfers among the sub-accounts of variable annuities without being detected, despite their attempts to enforce restrictions on market timing to protect the interest of

long-term investors. NASD found that the firm continued to sell variable annuity policies to the hedge fund client after receiving written notice that the client's trading strategy was considered disruptive and contrary to the interest of long-term investors. NASD determined that the fund client was able to execute transfers in the sub-accounts that yielded profits in excess of \$46,000 at the expense of long-term investors. The findings stated that the the firm did not maintain adequate written supervisory procedures to address market timing and failed to implement a supervisory system designed to monitor the activity of its associated persons with regard to market timing. In addition, NASD found that the firm failed to preserve for three years, and/or to preserve in an accessible place for two years, electronic mail communications received and sent by its agents and employees that related to its business as a broker or dealer. The findings also stated that the firm lacked adequate systems or procedures for the preservation of all electronic mail communications. (NASD Case #CE2050012)

**McLaughlin, Piven, Vogel Securities, Inc. (CRD #7404, New York, New York)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$13,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it reported transactions to TRACE late, reported principal transactions to TRACE as agency transactions, reported inter-dealer transactions to TRACE as customer transactions, and failed to report to TRACE the cancellation of transactions. The findings also stated that the firm failed to have adequate written procedures to ensure compliance with TRACE reporting requirements and failed to monitor adequately its trade reporting to ensure compliance with TRACE reporting requirements. The findings further stated that the firm failed to develop and implement an anti-money laundering (AML) program reasonably designed to achieve and monitor compliance with the Bank Secrecy Act and the implementing regulations promulgated thereunder by the Department of Treasury. (NASD Case #C10050055)

**Mid-Ohio Securities Corp. (CRD #6634, Elyria, Ohio)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$10,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to have its AML compliance program approved in writing by a member of the firm's senior management. The findings also stated that the firm's AML supervisory procedures were deficient or failed to address certain issues. The findings further stated that the firm failed to establish an adequate customer identification program based on its failure to meet specific criteria outlined under the PATRIOT Act and the Bank

Secrecy Act regarding reliance on another financial institution to identify potentially problematic customers. In addition, NASD determined that the firm failed to establish an independent testing function for its AML program. (NASD Case #C04050025)

**Multitrade Securities LLC (CRD #47485, New York, New York)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$13,500. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it permitted a registered person to act in a capacity that required registration while that person's registration status with NASD was inactive due to his failure to complete the Regulatory Element of NASD's Continuing Education Requirement. NASD also found that the firm failed to show the required time of receipt, entry, and/or execution of order tickets. In addition, NASD determined that the firm conducted a securities business while failing to maintain its minimum net capital after its debt to debt-equity ratio had exceeded 70 percent for a period greater than 90 days. (NASD Case #C10050056)

**Nalico Equity Corporation (CRD #15530, Giessen, Germany)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$30,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to create and maintain a complete and accurate itemized daily record of all receipts and disbursements of funds and purchases and sales of securities. The findings stated that the firm's net capital computation was inaccurate several times because it mischaracterized as an allowable asset controlled by persons no longer associated with the firm. The findings also stated that the firm did not maintain its daily record of all receipts and disbursements of funds and of purchases and sales of securities and ledgers reflecting debits and credits and did not maintain its checkbooks, bank statements, cancelled checks, and bank account reconciliations as required by SEC and NASD rules and regulations.

NASD found that the firm's supervisory system and procedures were inadequate with respect to annual compliance interviews, obtaining suitability information, compliance with financial recordkeeping rules, monitoring employee transactions at firms other than Nalico Equity Corporation, compliance with Regulation S-P, detecting and preventing unauthorized transactions, enforcing NASD Conduct Rule 3060 regarding gifts and gratuities, timely and accurate submission of Forms U4 and U5, and monitoring mutual fund transactions for unsuitable "B" share recommendations and violations of rules governing non-cash compensation. In addition, the findings stated that the firm did not maintain a

current firm element continuing education program in that its needs analysis and training plan were not updated annually and its firm element training included only participation in the annual compliance interview. Furthermore, the findings stated that the firm's AML test was not independent, and its AML program was not approved by senior management after the customer identification program provisions became effective, and was not reasonably designed to achieve compliance with all aspects of the Bank Secrecy Act and the regulations promulgated thereunder. (NASD Case #C3A050032)

**Pershing Trading Company L.P. (CRD #36671, Jersey City, New Jersey)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$22,500. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it reported TRACE eligible securities transactions late or containing inaccurate information. The findings also stated that the firm failed to establish written policies, procedures, and internal controls reasonably designed to achieve compliance with all requirements imposed by the Bank Secrecy Act and the regulations promulgated thereunder. (NASD Case #C9B050041)

**Securian Financial Services, Inc. (CRD #15296, Saint Paul, Minnesota)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$10,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to supervise adequately and properly a registered representative with respect to his recommendations to public customers. (NASD Case #C8A050068)

**Spectrum Asset Management, Inc. (CRD #18217, Stamford, Connecticut)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$15,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to develop and implement a written AML program and internal controls reasonably designed to achieve and monitor compliance with the requirements of the Bank Secrecy Act and the regulations promulgated thereunder. The findings also stated that the firm failed to have its AML procedures approved, in writing, by a member of the firm's senior management, have independent testing conducted on its AML program, and designate the firm's AML compliance officer in its procedures. (NASD Case #C3A050037)

**VSR Financial Services, Inc. (CRD #14503, Overland Park, Kansas)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$10,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that the firm established and maintained a supervisory system designed to prevent and detect excessive trading in

customer accounts that was deficient. The findings also stated that the firm's written supervisory procedures failed to specify expressly the action to be taken if the individual reviewing the exception reports discovered "red flags" indicating excessive trading. (NASD Case #C04050029)

**Zions Investment Securities, Inc. (CRD #17776, Salt Lake City, Utah)** submitted a Letter of Acceptance, Waiver, and Consent in which the firm was censured and fined \$35,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to report in a timely manner customer grievances required to be reported with quarterly statistical information or to be reported no more than 10 days following the firm's discovery of the grievances. NASD also found that the firm failed to amend Forms U4 and U5 as required, and that registered representatives of the firm failed to participate in a required annual compliance interview. The findings also stated that registered representatives of the firm did not complete one or both of two components of the required firm element continuing education program developed by the firm.

The findings further stated that the firm settled a customer complaint by means of a settlement agreement that contained language implying that the customer could not voluntarily assist NASD or any self-regulatory organization with respect to the subject matter of the settlement. Furthermore, NASD found that the firm utilized two forms of written supervisory procedures that evidenced two forms of supervisory systems, both of which were not reasonably designed to achieve compliance with the reporting obligations of NASD Rule 3070, requirements to amend Forms U4 and U5, requirements to monitor for compliance with variable annuity and mutual fund compensation rules, rules pertaining to retail transaction in fixed income securities and corporate bond trading, continuing education provisions, SEC Rule 15c2-12, and the requirements for office inspections in NASD Conduct Rule 3010. In addition, NASD found that the firm did not enforce its supervisory system and procedures relating to annual compliance interviews, firm element continuing education, office inspections, and advertising and sales literature reviews. (NASD Case #C3A050027)

## Individuals Barred or Suspended

**Juan Carlos Alb (CRD #4182760, Registered Representative, Stafford, Virginia)** submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Alb consented to the described sanction and to the entry of findings that he agreed to deposit \$18,200 in cash received from another person into a bank account that Alb maintained at a bank

where he worked, made two separate deposits of less than \$10,000 on separate days to his account at the bank, and then gave the person from whom he had received the cash a check for \$18,500. The findings also stated that Alb intended to prevent the bank from filing a currency transaction report as required by federal law for any cash deposit exceeding \$10,000. (NASD Case #C9A050026)

**Nicholas Apodikos (CRD #1595927, Registered Representative, Brighton, Massachusetts)** submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Apodikos consented to the described sanction and to the entry of findings that he induced a public customer to withdraw \$60,000 in the form of checks from her brokerage account and to sell her shares in a mutual fund to purchase a tax-free investment. The findings also stated that the checks were made payable to a third party who cashed the checks and split the proceeds with Apodikos. (NASD Case #C11050002)

**Carlos Aponte, Jr. (CRD #4211338, Registered Representative, Brooklyn, New York)** was barred from association with any NASD member in any capacity. The sanction was based on findings that Aponte willfully failed to amend his Form U4 to disclose a material fact. The findings also stated that Aponte failed to respond to NASD requests for information. (NASD Case #C07050006)

**Randall Patrick Aungst (CRD #2476968, Registered Representative, Saline, Michigan)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for one year. The fine must be paid before Aungst reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Aungst consented to the described sanctions and to the entry of findings that he participated in private securities transactions, for compensation, failed to give written notice of his intention to engage in such activities to his member firm, and failed to receive written approval from his member firm prior to engaging in such activities.

Aungst's suspension began August 1, 2005, and will conclude at the close of business July 31, 2006. (NASD Case #C8A050070)

**Hoyit Allen Bacon (CRD# 1974347, Registered Principal, Bixby, Oklahoma)** submitted an Offer of Settlement in which he was censured, fined \$5,000, ordered to pay \$11,793.59 in restitution to a public customer, and suspended from association with any NASD member in any capacity for one year. The fine and restitution must be paid before Bacon reassociates with any NASD member following the suspension

or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Bacon consented to the described sanctions and to the entry of findings that he engaged in outside business activities without providing written notice to his member firm. The findings also stated that Bacon violated standards of commercial honor and just and equitable principles of trade by billing one client for the same advisory services under both an agreement with his member firm and through his outside business.

Bacon's suspension began August 1, 2005, and will conclude at the close of business July 31, 2006. (NASD Case #C05050010)

**Charles Gabriel Bourdreaux, IV (CRD #3231717, Registered Representative, Lafayette, Louisiana)** submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Bourdreaux consented to the described sanction and to the entry of findings that he engaged in a scheme to evade federal cash reporting requirements by advising the purchase of multiple money orders in amounts less than \$3,000 and causing money orders totaling \$11,650 to be deposited into a brokerage account maintained at his member firm. The findings also stated that Bourdreaux failed to respond to NASD requests for information. (NASD Case #C05050014)

**Fredericia Joyce Brant (CRD #2893512 Registered Representative, Westerville, Ohio)** submitted a Letter of Acceptance, Waiver, and Consent in which she was fined \$5,000 and suspended from association with any member of NASD in any capacity for three months. The fine must be paid before Brant reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Brant consented to the described sanctions and to the entry of findings that she failed to disclose material information on her Form U4.

Brant's suspension began July 18, 2005, and will conclude at the close of business October 17, 2005. (NASD Case #C8A050059)

**Michael Robert Brooks (CRD #2086694, Registered Representative, Bainbridge Island, Washington)** was barred from association with any NASD member in any capacity and ordered to pay \$8,740, plus interest, in restitution to a public customer. The sanctions were based on findings that Brooks received \$8,740 from a public customer for investment purposes and, without the customer's knowledge or consent, deposited the funds into a bank account he controlled, thereby converting the customer's funds to his own use and benefit. The findings also stated that Brooks failed to respond to NASD requests for

information. (NASD Case #C3B040035)

**Vincent Anthony Buchanan (CRD #34247, Registered Principal, New York, New York)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$15,000 and suspended from association with any member of NASD in any capacity for 20 business days. Without admitting or denying the allegations, Buchanan consented to the described sanctions and to the entry of findings that member firms, acting through Buchanan, engaged in the securities business while failing to have and maintain sufficient net capital.

Buchanan's suspension began July 18, 2005, and concluded at the close of business August 12, 2005. (NASD Case #C10050050)

**Mark Bradley Clausen (CRD #1752792, Registered Representative, Burbank, California)** submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Clausen consented to the described sanction and to the entry of findings that he misappropriated insurance premiums from public customers totaling \$5,307.41. (NASD Case #C02050046)

**David Edward Cook (CRD #2503250, Registered Principal, Warren, Ohio)** submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Cook consented to the described sanction and to the entry of findings that he affixed the signatures of public customers to Individual Retirement Account (IRA) distribution forms and submitted the forms to a clearing firm to cover margin calls in the customers' accounts as an accommodation. The findings stated that Cook, in response to NASD requests for information, submitted to NASD falsified IRA distribution forms purportedly signed by the customers to support his claims that the customers authorized IRA distributions to cover margin calls. The findings also stated that Cook failed to respond to NASD requests for information. (NASD Case #C8A050030)

**Kevin Edward Davis (CRD #1643435, Registered Principal, Columbia, Maryland)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$7,500, jointly and severally, and suspended from association with any NASD member in a FINOP capacity for 15 business days. Without admitting or denying the allegations, Davis consented to the described sanctions and to the entry of findings that a member firm, acting through Davis, used the means or instrumentalities of interstate commerce or the mails to effect transactions in non-exempt securities while failing to maintain a minimum required net capital. NASD also found that Davis,

acting on behalf of his firm, filed materially inaccurate FOCUS Reports with NASD that failed to include the firm's liability amounts relating to an unsatisfied arbitration award and materially overstated the firm's net capital.

Davis' suspension began July 18, 2005, and concluded at the close of business August 5, 2005. (NASD Case #C9A050033)

**Robert Eugene Donley, Jr. (CRD #4689962, Associated Person, Perry, Michigan)** was fined \$10,000 and suspended from association with any NASD member in any capacity for one year. The fine shall be due and payable when and if Donley seeks to re-enter the securities business. The sanctions were based on findings that Donley willfully failed to disclose a material fact on his Form U4.

Donley's suspension began June 20, 2005, and will conclude at the close of business June 19, 2006. (NASD Case #C8A040112)

**Sean Everett Falk (CRD #2961005, Registered Principal, Mount Airy, Maryland)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$2,500 and suspended from association with any NASD member in any capacity for 30 days. Without admitting or denying the allegations, Falk consented to the described sanctions and to the entry of findings that he engaged in a business activity for compensation outside the scope of his relationship with his member firm without providing his firm prompt written notice of the activity.

Falk's suspension began August 1, 2005, and will conclude at the close of business August 30, 2005. (NASD Case #C9A050036)

**Joe Manuel Fernandez (CRD #3015002, Registered Principal, Villa Park, California)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for 18 months. The fine must be paid before Fernandez reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Fernandez consented to the described sanctions and to the entry of findings that he learned that another registered representative of his member firm had impersonated him and had completed the firm element continuing education training module in his place. The findings stated that Fernandez also learned that the other registered representative had submitted a completion certificate to the firm falsely indicating that Fernandez had completed the training module, causing the firm's books and records to be inaccurate. NASD also found that Fernandez failed to take any action to correct the firm's books and records or to report the other representative's misconduct.

Fernandez' suspension began August 1, 2005, and will conclude at the close of business January 30, 2007. (NASD Case #C02050051)

**Valerie Marie Fricke (CRD #4572380, Associated Person, Jacksonville, Florida)** submitted a Letter of Acceptance, Waiver, and Consent in which she was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Fricke consented to the described sanction and to the entry of findings that she converted \$129,986 from public customers. (NASD Case #C07050039)

**John J. Gariepy, Jr. (CRD #3200145, Registered Representative, Scranton, Pennsylvania)** submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Gariepy consented to the described sanction and to the entry of findings that he caused his firm to issue checks totaling \$43,400 to a public customer drawn against the customer's securities account without the customer's knowledge or authorization, caused the checks to be delivered to him, forged the customer's signature on the checks, negotiated the checks, and used the bulk of the funds to his own use and benefit. The findings also stated that Gariepy failed to respond to NASD requests for information. (NASD Case #C9A050027)

**Todd Grafenauer (CRD #4408817, Registered Representative, Mukwonago, Wisconsin)** was barred from association with any NASD member in any capacity. The National Adjudicatory Council (NAC) imposed the sanction following appeal of an Office of Hearing Officers (OHO) decision. The sanction was based on findings that Grafenauer falsified internal documentation so that he would be able to utilize uncompensated interns to promote his securities business and that of his partner. (NASD Case #C8A030068)

**Alvin Waino Gebhart, Jr. (CRD #1005905, Registered Principal, Fallbrook, California)** and **Donna Traina Gebhart (CRD #2708528, Registered Principal, Fallbrook, California)**. Gebhart, Jr. was barred from association with any NASD member in any capacity. Donna Gebhart was fined \$15,000, suspended from association with any NASD member in any capacity for one year, and ordered to requalify by exam before re-entering the securities industry. The sanctions were imposed by the NAC following its call for review of an OHO decision. The sanctions were based on findings that the respondents sold unregistered securities that were not exempt from registration; engaged in private securities transactions without providing written notice to, or receiving written approval from, their firm; and recklessly omitted material facts in connection with the sales of securities.

Gebhart Jr. and Donna Gebhart have appealed this decision to the United States Securities Exchange Commission (SEC) and the sanctions, except for the bar, are not in effect pending review. (Case #C02020057)

**David Augustus Green (CRD #2787039, Registered Principal, Coral Springs, Florida)** submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Green consented to the described sanction and to the entry of findings that he effected, or caused to be effected, transactions in the accounts of public customers without the customers' prior authorization. (NASD Case #C07040084)

**Kerry John Grinkmeyer (CRD# 2267687, Registered Principal, Birmingham, Alabama)** submitted an Offer of Settlement in which he was fined \$10,000 and suspended from association with any NASD member in a general securities principal capacity for one month. The fine must be paid before Grinkmeyer reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Grinkmeyer consented to the described sanctions and to the entry of findings that he failed to perform certain supervisory duties, including delegating certain compliance responsibilities to his unregistered assistant, failed to show evidence of review of and follow-up on certain exception reports, and failed to provide copies to his firm of certain executed forms. In addition, registered representatives assigned to Grinkmeyer's Office of Supervisory Jurisdiction (OSJ) effected all transactions under his advisor number and, as a result, neither Grinkmeyer nor his firm could monitor the activity of individual registered representatives.

Grinkmeyer's suspension began August 1, 2005, and will conclude at the close of business September 1, 2005. (NASD Case #C05050022)

**Garik Hakobyan (CRD #4651839, Associated Person, Glendale, California)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$10,000 and suspended from association with any NASD member in any capacity for one year. The fine must be paid before Hakobyan reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Hakobyan consented to the described sanctions and to the entry of findings that he willfully failed to disclose material facts on his Form U4.

Hakobyan's suspension began July 18, 2005, and will conclude at the close of business July 17, 2006. (NASD Case #C02050044)

**John Herbert Herzog (CRD #1515035, Registered Principal, Orland Park, Illinois)** submitted a Letter of Acceptance, Waiver, and Consent in which he was suspended from association with any NASD member in any capacity for 90 days, and fined \$59,300.22, including disgorgement of \$44,300.22, representing, in part, commissions charged back as a result of market timing activity and certain expenses incurred with the variable annuity business of a hedge fund client. Without admitting or denying the allegations, Herzog consented to the described sanctions and to the entry of findings that he facilitated deceptive practices regarding market timing in the sub-accounts of variable annuities for a hedge fund client that purported to manage money for wealthy individuals and corporate entities they established for that purpose. The hedge fund client used a number of different accounts to purchase variable annuity contracts from an insurance company, and enabled the hedge fund client to use these accounts to carry out frequent transfers among the sub-accounts of variable annuities without being detected by the insurance company or by mutual fund managers.

NASD determined that after the insurance company notified Herzog that it was exercising its contractual right to terminate transfer privileges on contracts, Herzog submitted new applications to the insurance company for the same product on behalf of the same business entities, sometimes listing another employee of the hedge fund client as the annuitant, and sometimes using different corporate identities with different account numbers and tax ID numbers in an attempt to avoid detection as a market timer. In fact, the annuitants were officers of employees of the hedge fund client. NASD determined that Herzog's conduct was intended to deceive the insurance company and allow the hedge fund client to continue trading contracts. NASD also found that Herzog continued to process orders to sell variable annuity policies for the hedge fund client after receiving written notice from the insurance company that it considered the client's trading strategy to be disruptive and contrary to the interest of long-term investors.

Herzog's suspension began July 18, 2005, and will conclude October 15, 2005. (NASD Case #CE2050013)

**Kyle Timothy Holland (CRD #2308543, Registered Principal, Austin, Texas)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$25,000, suspended from association with any NASD member in any capacity for one month, and suspended from association with any NASD member in any principal capacity for three months. Without admitting or denying the allegations, Holland consented to the described sanctions and to the entry of findings that he failed to ensure that his member firm included a \$500,000 settlement agreement as a liability of the firm. The findings stated that he filed inaccurate FOCUS Reports with NASD that significantly overstated the firm's net

capital position and Holland failed to give NASD notice of the firm's net capital deficiencies. The findings also stated that Holland participated in private securities transactions and failed to give his member firm prior notice of his transactions involving a stock, his role therein, and whether he might receive compensation in connection with the transactions.

Holland's suspensions began July 18, 2005; the suspension in any capacity will conclude at the close of business August 17, 2005, and the suspension in any principal capacity will conclude at the close of business October 17, 2005. (NASD Case #C06050016)

**Bambi Iris Holzer (CRD #1088028, Registered Representative, Los Angeles, California)** submitted a Letter of Acceptance, Waiver, and Consent in which she was fined \$100,000, suspended from association with any NASD member in any capacity for 21 days, and required to attend and satisfactorily complete 16 hours of continuing education concerning variable annuities. Without admitting or denying the allegations, Holzer consented to the described sanctions and to the entry of findings that she made negligent misrepresentations to public customers regarding certain product features in connection with the purchase and sale of variable annuities.

Holzer's suspension began July 18, 2005, and concluded August 7, 2005. (NASD Case #C02050049)

**Scott West Jones (CRD #3083008, Registered Representative, Lake Forest, California)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for 18 months. The fine must be paid before Jones reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Jones consented to the described sanctions and to the entry of findings that he impersonated another registered representative of his member firm who was scheduled to complete a firm element continuing education training module, and completed the training module in his place. The findings stated that following his completion of the training module, Jones submitted a completion certificate to the firm, falsely indicating that the other representative had completed the training module, causing the firm's books and records to be inaccurate.

Jones' suspension began August 1, 2005, and will conclude at the close of business January 30, 2007. (NASD Case #C02050050)

**Ram Kapara (CRD #2589146, Registered Representative, Brooklyn, New York)** was barred from association with any NASD member in any capacity and ordered to pay \$780,000,

plus interest, in restitution to public customers. The sanctions were imposed by the NAC following appeal of an OHO decision. The sanctions were based on findings that Kapara failed to respond to NASD requests for information and to appear for on-the-record interviews. The findings also stated that Kapara submitted a copy of his purported signed resignation letter bearing a date that was false and misleading to NASD. In addition, NASD found that Kapara made material misrepresentations to public customers in connection with the sale of securities to public customers. Moreover, NASD found that Kapara effected private securities transactions and failed to provide prior written notice to his member firm describing the proposed transaction, his proposed role therein, and stating whether he had or might receive compensation for it. The NAC reversed the finding that Kapara exercised discretion in the account of a public customer without the customer's written authorization and his firm's written acceptance of the account as discretionary. (NASD Case #C10030110)

**Michael Eugene Kelly (CRD #4447819, Registered Representative, Wadsworth, Ohio)** submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any member of NASD in any capacity. Without admitting or denying the allegations, Kelly consented to the described sanction and to the entry of findings that he effected transactions in the account of a public customer without having reasonable grounds for believing that these recommendations and resultant transactions were suitable for the customer on the basis of her financial situation, investment objectives, and needs. (NASD Case #C8A050069)

**Sandeep David Kitson (CRD #2508526, Registered Principal, New York, New York)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$5,000 and suspended from association with any member of NASD in any capacity for two years. The fine must be paid before Kitson reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Kitson consented to the described sanctions and to the entry of findings that he made unsuitable securities recommendations and executed unsuitable transactions for the accounts of public customers. The findings also stated that Kitson willfully failed to disclose material facts on his Form U4.

Kitson's suspension began July 18, 2005, and will conclude at the close of business July 17, 2007. (NASD Case #C04050028)

**Kevin Arthur Kowalczyk (CRD #2262204, Registered Representative, Chicago, Illinois)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$2,500 and suspended from association with any NASD member in any capacity for 10 business days. Without admitting or denying the allegations, Kowalczyk consented

to the described sanctions and to the entry of findings that he effected discretionary transactions in securities accounts of public customers without prior written authorization from the customers and prior written acceptance of the accounts as discretionary by his member firm.

Kowalczyk's suspension began August 1, 2005, and concluded at the close of business August 12, 2005. (NASD Case #C8A050065)

**Danny Carl Lancaster (CRD #2070421, Registered Representative, Toledo, Ohio)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$6,333, including \$1,333 as disgorgement in commissions earned, and suspended from association with any NASD member in any capacity for two months. The fine must be paid before Lancaster reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Lancaster consented to the described sanctions and to the entry of findings that he recommended and effected securities transactions in the accounts of public customers without having reasonable grounds to recommend that customers borrow 80 percent of their home equity by executing a 30-year mortgage in order to invest in mutual funds.

Lancaster's suspension began August 1, 2005, and will conclude at the close of business September 30, 2005. (NASD Case #C8A050066)

**Stephen Phillip Lewis (CRD #820773, Registered Principal, Boynton Beach, Florida)** submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Lewis consented to the described sanction and to the entry of findings that he engaged in an outside business activity for compensation without providing written notice to his member firm. The findings also stated that Lewis failed to respond to NASD requests for information. (NASD Case #C07050047)

**Esteban E. Llavallol (CRD #2879044, Registered Representative, New York, New York)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$2,500 and suspended from association with any NASD member in any capacity for 15 business days. Without admitting or denying the allegations, Llavallol consented to the described sanctions and to the entry of findings that, while employed as a registered representative of a member firm, he handled securities transactions on behalf of a third-party money manager through the prime brokerage department of an affiliated broker-dealer of his member firm and caused \$2,249 to be transferred from an omnibus account established by the affiliated firm for the benefit of

the third-party money manager into an account maintained by Llavallol's father at his member firm. The findings also stated that Llavallol failed to obtain proper supervisory approval from his member firm and/or the affiliated broker-dealer to transfer these funds to his father's account.

Llavallol's suspension began August 1, 2005, and will conclude at the close of business August 19, 2005. **(NASD Case #C10050060)**

**David Keith Locy (CRD #817730, Registered Representative, Cincinnati, Ohio)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for six months. The fine must be paid before Locy reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Locy consented to the described sanctions and to the entry of findings that he engaged in an approved outside business activity where he was a third-party administrator for small 401(k) plans and failed to forward received checks promptly to the 401(k) plans.

Locy's suspension began July 18, 2005, and will conclude at the close of business January 17, 2006. **(NASD Case #C8A050050)**

**Juan Carlos Ly (CRD #2520403, Registered Representative, Maiden, North Carolina)** submitted an Offer of Settlement in which he was fined \$20,000, \$10,000 of which represents partial disgorgement of commissions, and suspended from association with any NASD member in any capacity for 20 business days. Without admitting or denying the allegations, Ly consented to the described sanctions and to the entry of findings that he did not have a reasonable basis for recommending variable annuity switches to public customers. NASD also found that Ly misrepresented on his member firm's variable products broker-dealer account form that a new variable annuity had a lower cost structure than the annuity being relinquished.

Ly's suspension began July 18, 2005, and concluded at the close of business August 12, 2005. **(NASD Case #C07040092)**

**Roger Parker May (CRD #717728, Registered Principal, Golden, Colorado)** was fined \$30,000, ordered to pay \$91,158 in restitution to a public customer, and suspended from association with any NASD member in any capacity for one year. The findings stated that May made an unsuitable recommendation to a public customer, and executed, or caused the execution of, unauthorized trading in the account of a public customer.

May's suspension began July 5, 2005, and will conclude July 4, 2006. **(NASD Case #C3A030050)**

**Frank Mayol (CRD #4494246, Registered Representative, Yonkers, New York)** was barred from association with any NASD member in any capacity for failure to respond to NASD requests for information. NASD also found that Mayol forged a public customer's signature on an IRA authorization for release of transfer of assets form without the customer's knowledge or authorization. **(NASD Case #C10040122)**

**Randy Lawrence McClure (CRD #1289750, Registered Principal, Dunedin, Florida)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$10,000 and suspended from association with any NASD member in any capacity for 10 business days. The fine must be paid before McClure reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, McClure consented to the described sanctions and to the entry of findings that he failed to conduct the necessary due diligence prior to his member firm's sale of stock. The findings also stated that the shares of stock were received from affiliates of the issuer and were restricted because the stock was not registered and no applicable exemption from registration was available to the firm.

McClure's suspension began June 6, 2005, and concluded at the close of business June 17, 2005. **(NASD Case #CE3050008)**

**Rose Marie McKesson (CRD#1880804, Registered Representative, West Hills, California)** submitted a Letter of Acceptance, Waiver, and Consent in which she was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, McKesson consented to the described sanction and to the entry of findings that she converted \$92,000 from public customers for her personal use. **(NASD Case #C02050047)**

**William Ramey Mead, Jr. (CRD #330671, Registered Representative, St. Louis, Missouri)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$88,000, including disgorgement of excessive commissions, and suspended from association with any NASD member in any capacity for 90 days. The fine must be paid before Mead reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Mead consented to the described sanctions and to the entry of findings that he made unsuitable recommendations to public customers in that he offered Class B share mutual funds that were not the lowest-cost alternative available and recommended the use of margin to a public customer for the

purchase of mutual fund shares, which was unsuitable in view of the customer's limited assets, lack of investment experience, and knowledge.

Mead's suspension began July 5, 2005, and will conclude October 2, 2005. (NASD Case #C07050041)

**Robert Earl Messinger (CRD #1234161, Registered Representative, Cincinnati, Ohio)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$10,000, ordered to pay \$30,711.71 in partial restitution to public customers, and suspended from association with any NASD member in any capacity for 10 business days. Without admitting or denying the allegations, Messinger consented to the described sanctions and to the entry of findings that he recommended that public customers purchase and accumulate large positions in mutual fund Class B shares and Class C shares without a reasonable basis to believe that the recommendations were suitable for each customer because the customers could have purchased Class A shares in each fund at a reduced sales charge by applying breakpoints, using letters of intent, and/or using rights of accumulation.

Messinger's suspension began July 18, 2005, and concluded at the close of business July 29, 2005. (NASD Case #C8A050053)

**Virginia Kaye Millage (CRD #4594079, Associated Person, Puyallup, Washington)** submitted a Letter of Acceptance, Waiver, and Consent in which she was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Millage consented to the described sanction and to the entry of findings that she converted proceeds totaling \$5,000 belonging to a public customer for her own use and benefit. (NASD Case #C3B050013)

**Steve Eric Milstein-Roth (CRD #2457324, Registered Representative, West Hollywood, California)** submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Milstein-Roth consented to the described sanction and to the entry of findings that he participated in private securities transactions without prior written notice to, or approval from, his member firm. The findings also stated that Milstein-Roth failed to respond to NASD requests for documents and information. (NASD Case #C02050035)

**John Daniel Minerva (CRD #2702468, Registered Principal, Jackson, New Jersey)** submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any member of NASD in any capacity. Without admitting or denying the allegations, Minerva consented to the described sanction and to the entry of findings that he participated in a private securities transaction

without prior written notice to, or prior written approval from, his member firm. The findings also stated that Minerva failed to respond to NASD requests for information. (NASD Case #C9B050043)

**Alfred Peter Montgomery (CRD# 4721887, Associated Person, Baton Rouge, Louisiana)** was barred from association with any NASD member in any capacity for failing to disclose material information on his Form U4. (NASD Case #C05040088)

**Paul Robert Olsen (CRD #2611306, Registered Principal, Denver, Colorado)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$10,000 and suspended from association with any NASD member in any capacity for 30 days. The fine must be paid before Olsen reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Olsen consented to the described sanctions and to the entry of findings that while recommending that his public customers exchange several annuities, he negligently failed to disclose to the customers the actual expenses associated with new annuities and the elected sub-accounts.

Olsen's suspension began July 18, 2005, and will conclude at the close of business August 16, 2005. (NASD Case #C3A050036)

**Anthony John Orlando, Jr. (CRD #2497838, Registered Principal, New York, New York)** and **Philip Anthony Orlando (CRD #2839212, Registered Principal, Pelham, New York)** were barred from association with any NASD member in any capacity. The sanctions were imposed by the NAC following appeal of an OHO decision. The sanctions were based on findings that the respondents failed to respond to NASD requests for documents and failed to appear for on-the-record interviews to provide testimony. (NASD Case #CMS030269)

**Bryan N. Polozola (CRD #4370964, Registered Principal, New York, New York)** submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Polozola consented to the described sanction and to the entry of findings that he converted funds totaling \$49,350 from his member firm's bank account to his personal bank account for his own use and benefit. The findings also stated that Polozola failed to respond to NASD requests for information. (NASD Case #C10050023)

**Stephen Michael Rhoads, Sr. (CRD #3265781, Registered Representative, Wyckoff, New Jersey)** was barred from association with any NASD member in any capacity. The sanction was based on findings that Rhoads received checks

totaling \$3,677.42 from a public customer for investment purposes, deposited the checks into his own personal account, and personally paid the initial premium for the customer's disability insurance policy with a cashier's check. The findings stated that Rhoads set up a pre-authorization check premium payment service (PAC) to arrange for automatic monthly withdrawals from his personal account to pay the premium on the customer's policy, without the customer's knowledge, authorization, or consent. The findings also stated that because the PAC had insufficient funds to make the automatic premium payments, the disability policy lapsed due to nonpayment. In addition, the findings stated that Rhoads failed to respond to NASD requests for information and documents. (NASD Case #C10040116)

**Terry Lee Ringer (CRD #2309959, Registered Representative, Vienna, West Virginia)** submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Ringer consented to the described sanction and to the entry of findings that he failed to respond to NASD requests for information. (NASD Case #C9A050035)

**Eugene Paul Rivera (CRD# 4054915, Registered Representative, Hoboken, New Jersey)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$10,000 and suspended from association with any member of NASD in any capacity for three months. The fine must be paid before Rivera reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Rivera consented to the described sanctions and to the entry of findings that he recommended and effected a transaction in the account of a public customer without having a reasonable basis for believing the transaction was suitable based upon the customer's investment objectives, financial situation, and needs. The findings also stated that Rivera signed a public customer's name to a variable annuity surrender request form without the customer's knowledge, authorization, or consent.

Rivera's suspension began July 18, 2005, and will conclude at the close of business October 17, 2005. (NASD Case #C10050054)

**Edwin Rodriguez, Jr. (CRD #1952747, Registered Representative, New York, New York)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$10,000 and suspended from association with any NASD member in any capacity for 10 business days. Without admitting or denying the allegations, Rodriguez consented to the described sanctions and to the entry of findings that he sent a letter to a public customer concerning a transaction in the customer's account that was not on firm letterhead,

was not made available for supervisory review, and was sent without his member firm's knowledge or consent.

Rodriguez's suspension began June 6, 2005, and concluded at the close of business June 17, 2005. (NASD Case #C10050020)

**David John Rossignol (CRD #2231527, Registered Principal, Boston, Massachusetts)** submitted a Letter of Acceptance, Waiver, and Consent in which he was suspended from association with any NASD member in any capacity for 15 business days and suspended from association with any NASD member in any principal or supervisory capacity for 45 days. In light of the financial status of Rossignol, no monetary sanction has been imposed. Without admitting or denying the allegations, Rossignol consented to the described sanctions and to the entry of findings that he failed to take appropriate action to supervise a registered representative that was reasonably designed to prevent the representative's violations and achieve compliance with applicable securities laws, regulations, and NASD rules. The findings also stated that Rossignol became concerned about the volatility of a stock the representative had purchased in several customer accounts before the representative's termination and liquidated the positions of some of the customers without their consent.

Rossignol's suspensions began June 6, 2005; the suspension in any capacity concluded June 24, 2005, and the suspension in any principal or supervisory capacity concluded July 20, 2005. (NASD Case #C11050010)

**David Alan Settle (CRD #4245687, Registered Representative, Nephi, Utah)** submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Settle consented to the described sanction and to the entry of findings that he obtained approximately \$88,000 from the securities accounts of public customers by causing unauthorized withdrawals from the accounts and used the funds for his personal benefit. (NASD Case #C3A050028)

**Mason Speed Sexton (CRD #819953, Registered Representative, New York, New York)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$2,500 and suspended from association with any NASD member in any principal capacity for eight months. Without admitting or denying the allegations, Sexton consented to the described sanctions and to the entry of findings that he failed to supervise adequately the activities of a former trader at his member firm.

Sexton's suspension began August 1, 2005, and will conclude at the close of business March 31, 2006. (NASD Case #C10050062)

**Tomislav Skibola (CRD #2791236, Registered Representative, Long Island City, New York)** submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Skibola consented to the described sanction and to the entry of findings that he executed transactions in the account of a public customer without the customer's prior knowledge, authorization, or consent. The findings also stated that Skibola engaged in the short-term trading of mutual fund shares in the account of a public customer, which was inconsistent with his fundamental responsibility for fair dealing with the customer, and also entailed the recommendation of securities transactions that were not suitable for the customer. In addition, NASD found that Skibola generated, or caused to be generated, false or inaccurate records in that he took actions to create the false appearance in firm records that the customer placed the orders via the Internet and were thus unsolicited when, in fact, Skibola caused the placement of the orders from his firm's offices. **(NASD Case #C10050042)**

**Jennifer Anne Stephenson (CRD #4156971, Registered Representative, Indianapolis, Indiana)** submitted a Letter of Acceptance, Waiver, and Consent in which she was barred from association with any NASD member in any capacity and ordered to pay \$3,700, plus interest, in restitution to a public customer. Restitution must be paid before Stephenson reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Stephenson consented to the described sanctions and to the entry of findings that she converted funds belonging to a public customer by electronically transferring \$4,000 from the account of the customer to Stephenson's personal checking account and then using \$3,700 of the funds for her own use and benefit without the knowledge or consent of the customer. The findings also stated that Stephenson failed to respond to NASD requests for information. **(NASD Case #C8A050057)**

**Lawrence Lee Sullivan (CRD #2491233, Registered Principal, Honolulu, Hawaii)** submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Sullivan consented to the described sanction and to the entry of findings that he failed to respond to NASD requests for information and documents. **(NASD Case #C01050011)**

**Clayton Richard Waldie (CRD #4476389, Registered Representative, Springfield, Missouri)** submitted a Letter of Acceptance, Waiver, and Consent in which he was barred from association with any NASD member in any capacity.

Without admitting or denying the allegations, Waldie consented to the described sanction and to the entry of findings that he failed to respond to NASD requests for information. **(NASD Case #C04050027)**

**Michael Floyd Whitley (CRD #2259737, Registered Representative, Pineville, North Carolina)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$5,000 and suspended from association with any member of NASD in any capacity for 30 business days. The fine must be paid before Whitley reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Whitley consented to the described sanctions and to the entry of findings that he effected discretionary trades in a public customer's account without obtaining discretionary authority from the customer in writing and without having the account accepted as discretionary by his member firm.

Whitley's suspension began July 18, 2005, and will conclude at the close of business August 26, 2005. **(NASD Case #C07050049)**

**Stephen Michael Williams (CRD #3185644, Registered Representative, Clarksburg, West Virginia)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for one month. Without admitting or denying the allegations, Williams consented to the described sanctions and to the entry of findings that he signed insurance policy delivery receipts as a witness to the signatures of public customers even though he had not actually witnessed any of the customers sign the delivery receipts.

Williams' suspension began August 1, 2005, and will conclude at the close of business August 31, 2005. **(NASD Case #C9B050040)**

**Jeffrey Scott Woods (CRD #4834919, Registered Representative, Weatherford, Texas)** submitted a Letter of Acceptance, Waiver, and Consent in which he was fined \$3,500 and suspended from association with any member of NASD in any capacity for 45 days. The fine must be paid before Woods reassociates with any NASD member following the suspension or before requesting relief from any statutory disqualification. Without admitting or denying the allegations, Woods consented to the described sanctions and to the entry of findings that he failed to disclose a material fact on his Form U4.

Woods' suspension began July 18, 2005, and will conclude at the close of business August 31, 2005. **(NASD Case #C06050018)**

**Martin Paul Lonski (CRD #1142988, Registered Representative, Minneapolis, Minnesota)** submitted a Letter of Acceptance, Waiver, and Consent in which he was censured and fined \$10,000. Without admitting or denying the allegations, Lonski consented to the described sanctions and to the entry of findings that he exercised discretion in public customers' accounts without written authorization from the customers and written acceptance of the accounts as discretionary from his member firm. **(NASD Case #C04050023)**

## Complaints Filed

NASD issued the following complaints. Issuance of a disciplinary complaint represents the initiation of a formal proceeding by NASD in which findings as to the allegations in the complaint have not been made, and does not represent a decision as to any of the allegations contained in the complaint. Because these complaints are unadjudicated, you may wish to contact the respondents before drawing any conclusions regarding the allegations in the complaint.

**Russell James Bjerke (CRD #3178233, Registered Representative, Ashland, Oregon)** was named as a respondent in an NASD complaint alleging that he received \$6,187 from a public customer for investment purposes, deposited the funds in a bank account under his control, and converted the funds to his own use and benefit without the customer's knowledge, authorization, or consent. The complaint also alleges that Bjerke failed to respond to NASD requests for information. **(NASD Case #C3B050015)**

**Daniel William Bukovcik (CRD #1684170, Registered Representative, Dewitt, Michigan)** was named as a respondent in an NASD complaint alleging that he affixed the signatures of public customers to account documents related to the purchases of mutual funds, variable products, annuities, and 529 plans without the written authorization of the customers; submitted the documents to his member firm; and failed to inform anyone at the firm that he had signed the customers' names to the forms. **(NASD Case #C8A050055)**

**Ronald Charles Crockett, Jr. (CRD #1682593, Registered Representative, West Chester, Pennsylvania)** was named as a respondent in an NASD complaint alleging that he caused securities transactions to be effected in customers' IRA accounts and affixed, or caused to be affixed, signatures purporting to be that of customers to brokerage account agreements without the customers' authorization or consent. The complaint also alleges that Crockett failed to respond to NASD requests for information. **(NASD Case #C9A050034)**

**Stephen Patrick Dunbar (CRD #2041644, Registered Representative, Atlanta, Georgia)** was named as a respondent in an NASD complaint alleging that he engaged in

unsuitable trading in the accounts of public customers without the customers' knowledge or authorization. The complaint further alleges that he invested in unduly concentrated equity positions, engaged in excessive trading in equity stocks, provided false and misleading account summaries that concealed equity trading and margin debits, failed to disclose stock positions and margin debit balances, and falsely reported non-existent cash balances. In addition, the complaint alleges that Dunbar effected transactions in the accounts of public customers without written authority from the customers or acceptance of the accounts as discretionary by his member firm. **(NASD Case #C07050050)**

**Carole Gurgone Ferraro (CRD #1174904, Registered Representative, Boynton Beach, Florida)** was named as a respondent in an NASD complaint alleging that she recommended and effected investments in variable annuities in the accounts of public customers without having a reasonable basis for her recommendations based on the limited benefit available to the customers from either the death benefit or the tax deferral features of the variable annuities, the costs associated with the products, the limited liquidity, and the failure of the variable annuities to satisfy the customers' goals of income and safety. **(NASD Case #C05050005)**

**Heather Jannelle Furgason (CRD #4241326, Registered Representative, Kalamazoo, Michigan)** was named as a respondent in an NASD complaint alleging that she misused public customer's funds by effecting unauthorized money transfers from and between customers' bank accounts without the knowledge, authorization, or consent of the customers. **(NASD Case #C8A050054)**

**Gregory Gassoso (CRD #2873605, Registered Representative, Staten Island, New York)** was named as a respondent in an NASD complaint alleging that he effected transactions in the accounts of public customers without the customers' prior knowledge, authorization, or consent. The complaint further alleges that Gassoso failed to forward incoming and outgoing electronic correspondence with a public customer to his member firm for review as required by the firm's written procedures. **(NASD Case #C10050048)**

**Arthur Harry Guterding, Jr. (CRD #1053453, Registered Representative, Henderson, Nevada)** was named as a respondent in an NASD complaint alleging that he obtained and exercised discretion in public customer accounts when he was prohibited from obtaining discretionary power by his member firm. **(NASD Case #C02050045)**

**Sherri Lynn Herrera (CRD #4491409, Registered Representative, Pueblo, Colorado)** was named as a respondent in an NASD complaint alleging that she received

\$718.44 from public customers in payment of premiums for insurance policies and used the funds for her own benefit without the customers' knowledge, authorization, or consent. The complaint also alleges that Herrera deposited \$153 to the account of a public customer three weeks after receiving the funds. (NASD Case #C3A050029)

**Karen Jean Hill (CRD #1018669, Registered Representative, Saginaw, Michigan)** was named as a respondent in an NASD complaint alleging that she recommended that public customers sell an existing mutual fund and purchase another mutual fund without any review of the customers' investment objectives, financial situation, and needs, and without reasonable efforts to obtain that information. The complaint also alleges that Hill, by the use or instrumentalities of interstate commerce or the mails, intentionally or recklessly misrepresented and employed devices to defraud public customers by making untrue statements of material fact and/or omitting to state material facts necessary to make the statements, in light of the circumstances in which they were made, not misleading in connection with the purchase or sale of securities.

The complaint further alleges that Hill represented to customers that there would be no surrender charge or initial sales charge in connection with the mutual fund switches that she recommended when, in fact, there were charges associated with the switches. In addition, the complaint alleges that Hill arranged for the customers to sign blank switch forms, filled in the correct surrender charge and initial sales charge as well as placed false and inaccurate reasons for the mutual fund switch on the switch forms, and submitted the forms to her member firm's principal review desk for approval. Furthermore, the complaint alleges that Hill created false documents purporting to show that the customers acknowledged the information on the switch forms and submitted them to her member firm as accurate switch forms. (NASD Case #C8A050060)

**Cesar Roel Perez (CRD #3091992, Registered Representative, Olmito, Texas)** was named as a respondent in an NASD complaint alleging that he converted at least \$125,000 from public customers without the customers' knowledge, authorization, or consent. The complaint also alleges that Perez failed to respond to NASD requests for information and to appear for an on-the-record interview to provide testimony. (NASD Case #C06050019)

**Jack Mace Schwartz (CRD #1027281, Registered Principal, Salina, Kansas)** was named as a respondent in an NASD complaint alleging that he made unsuitable recommendations

to public customers without having reasonable grounds for believing that his recommendations were suitable for the customers based on their financial situation and needs. (NASD Case #C04050024)

**Wanda Pittman Sears (CRD #2214419, Registered Representative, Roanoke, Virginia)** was named as a respondent in an NASD complaint alleging that she failed to provide her member firm with written notice of her outside business activity and effected transactions in the accounts of public customers without prior authorization from the customers. The complaint also alleges that Sears forged, or caused to be forged, customer signatures on forms establishing investment advisory services and payment for the services. (NASD Case #C07050042)

**Jon Martee Wade (CRD #1642488, Registered Representative, Little Rock, Arkansas)** was named as a respondent in an NASD complaint alleging that he purchased and sold mutual fund shares and municipal bonds in the account of a public customer that was excessive. The complaint also alleges that Wade's trading activity in the customer's account was without reasonable grounds for believing the recommendations and transactions were suitable in view of the frequency and nature of the recommended transactions, the customer's age, sophistication, and financial condition. In addition, the complaint alleges that Wade failed to respond to NASD requests for information and documents. (NASD Case #C8A050048)

### **Firm Suspended Pursuant to NASD Rule Series 9510 for Failure to Comply with an Arbitration Award or a Settlement Agreement**

(The date the suspension began is listed after the entry. If the suspension has been lifted, the date follows the suspension date.)

**Sands Brothers & Co. Ltd**  
New York, New York  
(June 20, 2005 – June 28, 2005)

### **Firm Suspended for Failure to Supply Financial Information**

The following firm was suspended from membership in NASD for failure to comply with formal written requests to submit financial information to NASD. The action was based on the provisions of NASD Rule 9552. The date the suspension commenced is listed after the entry. If the firm has complied with the requests for information, the listing also includes the date the suspension concluded.

#### **Investment Researched Plans, Inc.**

Los Angeles, California  
(July 11, 2005–July 28, 2005)

### **Individuals Suspended Pursuant to NASD Rule 9552 for Failure to Provide Information Requested under NASD Rule 8210**

(The date the suspension began is listed after the entry. If the suspension has been lifted, the date follows the suspension date.)

#### **Hunter, Robin C.**

Mesa, Arizona  
(June 21, 2005)

#### **Motarjeme, Richard Kevin**

Denver, Colorado  
(June 20, 2005)

#### **Ornelas, Joe Samora**

Albuquerque, New Mexico  
(June 20, 2005)

### **Individuals Barred Pursuant to NASD Rule 9552 for Failure to Provide Information Requested under NASD Rule 8210**

#### **Lowe, Phillip Alexander**

Los Angeles, California  
(June 27, 2005)

#### **Morris, Frank Caleal**

Ann Arbor, Michigan  
(June 20, 2005)

### **Individuals Suspended Pursuant to NASD Rule Series 9510 for Failure to Comply with an Arbitration Award or a Settlement Agreement**

(The date the suspension began is listed after the entry. If the suspension has been lifted, the date follows the suspension date.)

#### **Bartlett, Brian Lee**

Austin, Texas  
(June 20, 2005–June 23, 2005)

#### **Belmonte, Noel James**

Bellport, New York  
(June 27, 2005)

#### **Bravin, Erik Anthony**

Staten Island, New York  
(July 5, 2005)

#### **Cordery, Will**

Las Vegas, Nevada  
(June 30, 2005)

#### **Cuillo, Robert James**

Kings Park, New York  
(June 14, 2005)

#### **Febert, Michael Jeffrey**

Olympia, Washington  
(July 11, 2005)

#### **Ikwue, Sunny Michael**

Queens Village, New York  
(July 18, 2005)

#### **Misaraca, Kimberly Jean f/k/a Kimberly Carrella**

Bellport, New York  
(June 27, 2005)

#### **Moyer, Jr., Kenneth William**

Orlando, Florida  
(July 18, 2005–August 1, 2005)

#### **Nickens, Larry Bernard**

Brooklyn, New York  
(June 14, 2005)

#### **Zeidenfeld, Jr., Ilya Steven**

New York, New York  
(July 7, 2005)

## NASD Orders Morgan Stanley to Pay over \$6.1 Million for Fee-Based Account Violations

### Firm's Customers to Receive \$4.6 Million in Restitution

NASD fined Morgan Stanley DW, Inc., \$1.5 million and has ordered the firm to pay more than \$4.6 million in restitution for failing to adequately supervise its fee-based brokerage business. More than 3,500 Morgan Stanley customers will be receiving restitution.

Fee-based brokerage accounts are an alternative to traditional commission-based accounts. In a fee-based account, a customer is charged an annual fee that is either fixed or a percentage of the assets in the account, rather than a commission for each transaction as in a traditional brokerage account.

"Fee-based accounts can be appropriate for a wide range of customers," said NASD Vice Chairman Mary L. Schapiro. "But firms have an obligation to their customers to periodically reassess whether a fee-based account, like that offered by Morgan Stanley, remains appropriate. Firms must have systems and procedures in place that adequately evaluate the continued appropriateness of these accounts for their customers."

The Securities and Exchange Commission issued a report (commonly known as the "Tully Report") in 1995, noting that fee-based accounts are appropriate for investors who are building assets in their accounts, and may be appropriate for investors with moderate trading activity. But it also noted that because of the imposed annual fee, small and low-trading-activity accounts would pay higher costs as a fee-based account than as a commission-based account.

The following year, Morgan Stanley began offering its customers a fee-based brokerage account program, called "Choice." NASD found that Morgan Stanley recognized and instructed its brokers, consistent with the Tully Report, that Choice accounts were not appropriate for certain categories of investors, including buy-and-hold customers and certain accounts that fall below \$50,000. The firm typically required a minimum of \$50,000 in eligible assets to open a Choice account and charged an annual fee based on the total amount and type of eligible assets held in the account.

NASD found that between 2001 and 2003, all Choice accounts, regardless of size, paid a minimum annual fee of \$1,000. By the end of 2001, the firm had 129,630 Choice accounts, holding \$19.8 billion in assets. By the end of 2002, there were 157,143 Choice accounts, holding over \$21.2

billion in assets. Morgan Stanley had 176,274 Choice accounts holding \$30.6 billion in assets by the end of 2003.

NASD's investigation showed that from January 2001 through December 2003, Morgan Stanley failed to establish and maintain a supervisory system reasonably designed to review and monitor its fee-based brokerage business to determine whether Choice accounts remained appropriate for its Choice customers. As a result of the firm's deficient system and procedures, Morgan Stanley allowed 3,549 of its customers to continue using Choice accounts without adequately reassessing whether the accounts remained appropriate for them. These customers, who either conducted no trades in their Choice accounts for at least two consecutive years or had Choice accounts whose assets averaged below \$25,000 for at least one full year, or both, will be receiving restitution under the settlement announced today.

NASD found that Morgan Stanley's written procedures did not prescribe a system for ongoing supervisory review of the appropriateness of Choice accounts until June 2003. Beginning in December 2003, the firm's branch managers began receiving monthly exception reports based on a suppressed-commission-to-fee ratio for all Choice accounts with an anniversary date within that month. At that time, Morgan Stanley provided the branch managers with specific guidance on the review to be conducted and the specific actions to be taken with respect to accounts that appeared on the exception report. Although the firm improved its system and procedures, Morgan Stanley's system and procedures still were fundamentally flawed, in that the exception reports failed to capture any accounts that fell below \$50,000 in assets.

NASD also found that between January 2001 and December 2003, there were 1,818 Choice customers whose billable asset level averaged below \$25,000 for at least one full year. Morgan Stanley's supervisory system failed to capture these accounts, so the firm failed to conduct an adequate supervisory review to determine whether the accounts should remain in the Choice program. All of these customers paid at least the minimum annual fee of \$1,000 applicable at the time, which represented at least four percent of the assets in their Choice accounts—well in excess of Morgan Stanley's stated maximum rate of 2.25 percent. Those customers paid a total of \$2.7 million in Choice fees.

In addition, NASD found that 2,062 customers conducted no trades in at least two consecutive Choice years. Although many of these customers had traded previously in their Choice accounts, after these customers went an entire Choice year without trading, the firm's system and procedures failed to determine whether these accounts remained appropriate for Choice. Consequently, without an adequate supervisory review

of their particular circumstances, these 2,062 customers remained in Choice for at least an additional year, in which they incurred an additional \$2.8 million in fees without conducting any trades.

In sanctioning Morgan Stanley, NASD took into account the firm's demonstrable steps, undertaken shortly after NASD's inquiry began, to enhance its system and procedures and which led to the firm's identification and removal of large numbers of accounts for which the Choice program was not appropriate.

In settling these matters, the firm neither admitted nor denied the charges, but consented to the entry of NASD's findings.

This case is part of NASD's continuing focus on fee-based brokerage accounts. In April, NASD fined Raymond James & Associates, Inc., \$750,000 and ordered the firm to pay \$138,000 in restitution for fee-based account violations. In November 2003, NASD issued Notice to Members 03-68, reminding firms that before opening a fee-based account they must have "reasonable grounds for believing that a fee-based program is appropriate for that particular customer"—taking into account the services provided, the projected cost to the customer, alternative fee structures available and the customer's fee structure preferences. In that notice, firms were also reminded that after a fee-based account has been opened, firms should implement procedures requiring a periodic review to determine whether the fee-based account remains appropriate for each of their customers.

## **NASD Fines Hornor, Townsend & Kent, Inc., \$325,000 for Improper Sales Contests, Email and Supervision Violations**

### **Firm Ordered to Prohibit Variable Product Sales Contests for Three Years**

NASD fined Hornor, Townsend & Kent, Inc. (HTK), of Horsham, PA, \$325,000 for conducting prohibited sales contests for its brokers and managers, as well as for email and supervision violations. The contests violated NASD rules by awarding exclusive or greater weight to the sales of proprietary variable life and variable annuity products over non-proprietary products, thereby creating improper incentives for brokers to sell those products instead of focusing on the investment's merits and the customer's financial interests. In resolving this matter, HTK agreed to prohibit any sales contests promoting the sale of variable life or annuity products for the next three years.

NASD also found that HTK failed to retain the email communications of approximately 83 employees. Those employees included HTK's president and two other senior managers, who approved at least some of the violative

national sales contests. NASD rules require that email communications be retained for at least three years.

"By favoring the sale of some variable life and annuity products over others, these contests created conflicts of interest that could undermine the broker's obligation to recommend suitable investments based on the needs of the customer," said NASD Vice Chairman Mary L. Schapiro. "NASD rules are designed to prevent such conflicts between the broker's self-interest and the customer's."

Between 2001 and 2003, HTK conducted six national and numerous branch office sales contests to promote the sale of variable life and variable annuity products. When a firm stages a sales contest for a particular product line, NASD rules require that it cover all products the firm offers within that line, and that equal weight be given to the sales of all products within that line.

NASD found that several of the national sales contests were based only on the sale of variable products offered by Penn Mutual Life Insurance Company, HTK's parent company. In determining the winners for some of the national contests, sales of Penn Mutual variable life products were given exclusive or greater weight than sales of Penn Mutual variable annuity products.

HTK offered or awarded substantial rewards for the national contest winners, including weekend trips to New York City, New Orleans, and Las Vegas; vouchers worth \$400 or \$800 that could be used for personal entertainment or education; and gift cards that could be used to purchase items from a number of brand-name merchants. The total value of the national sales contest awards exceeded \$200,000.

Between 2001 and 2003, HTK's branch offices conducted additional sales contests. Nine were based solely on the sale of proprietary Penn Mutual variable products. In another four, sales of proprietary products were given greater weight than sales of non-proprietary products. Prizes for the branch contests included such items as golf trips, tickets to sporting events and other entertainment events, dinners, high-definition television sets, and other expensive electronic goods.

NASD found that the non-cash compensation that HTK provided to its sales force was substantial enough to provide the improper incentives that the non-cash compensation rules were designed to prevent.

NASD also found that HTK did not have in place an adequate supervisory system and procedures with respect to the non-cash compensation rules.

In settling this matter, the firm neither admitted nor denied the charges, but consented to the entry of NASD's findings.