BEFORE THE NATIONAL ADJUDICATORY COUNCIL

NASD REGULATION, INC.

In the Matter of	DECISION
Department of Enforcement,	Complaint No. C8A980097
Complainant,	Dated: June 4, 2001
vs.	
Michael F. Flannigan Excelsior, MN	
and	
Protective Group Securities Corporation Minneapolis, MN,	
Respondents.	

Respondents, a member firm and its president, violated NASD registration and discretionary trading rules by executing trades in an initial public offering even though representatives of another member firm solicited the customers' indications of interest and confirmed the trades. Respondents also followed the instructions of the representatives of another member firm with respect to executing customer trades in the aftermarket. Held, Hearing Panel findings and sanctions affirmed.

Protective Group Securities Corporation ("Protective" or "the Firm") and Michael F. Flannigan ("Flannigan"), its president, appealed this matter pursuant to NASD Procedural Rule 9311. Under review is a July 28, 2000 decision of an NASD Regulation, Inc. ("NASD Regulation") Hearing Panel. We affirm the Hearing Panel's finding that respondents violated NASD registration requirements by using representatives who were not registered with Protective, but who were registered with another member firm, to sell interests in an initial public offering ("IPO"). We also affirm the Hearing Panel's finding that respondents exercised discretion in customer accounts without written authority to do so by

following directions from registered representatives of the other member firm with respect to aftermarket trading in Protective's customer accounts. In light of our findings, we bar Flannigan in all supervisory capacities, jointly and severally fine Flannigan and Protective $25,000, and affirm the Hearing Panel's imposition of costs.

Background

Protective became a member firm on April 12, 1983. Its membership currently remains in effect. Flannigan entered the securities industry in 1983 and became a general securities principal at Protective on February 22, 1989. His principal registration remains in effect. During the period relevant to this matter (September through December 1996), Flannigan was president of Protective, and he ran the Firm. He still serves as Protective's president and chief operating officer and is part-owner and a control person of the Firm.

The Department of Enforcement ("Enforcement") filed the complaint in this matter after investigating possible free-riding and withholding violations in connection with the IPO for Room Plus, Inc. ("Room Plus").[1]

Facts

The Room Plus IPO. Room Plus, a New York corporation, offered its securities for sale in an IPO that went effective November 1, 1996.[2] Protective was a member of the syndicate for the Room Plus IPO[3] and received an allocation of 200,000 shares of common stock and 200,000 warrants. Protective earned compensation of $30,000 in the Room Plus IPO.

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[1] A "free-riding and withholding" violation is a violation of Conduct Rule 2110 and IM-2110-1 (Free-Riding and Withholding). Under IM-2110-1, it is a violation of Conduct Rule 2110 for a member or person associated with a member to fail to make a bona fide public distribution at the public offering price of securities of a public offering which trade at a premium in the secondary market. IM-2110-1 also indicates that it is a violation of Rule 2110 for a member firm or person associated with a member to sell securities of a public offering which trade at a premium in the secondary market to certain restricted persons and entities (identified in IM-2110-1) and for those restricted persons or entities to purchase or hold the securities.

[2] In the IPO, Room Plus offered 1,100,000 shares of common stock at $5 per share and 2,200,000 redeemable common stock purchase warrants at 10 cents per warrant. Each warrant entitled the holder to purchase one share of common stock at a price of $5.50 per share commencing November 1, 1997 and ending on November 1, 2000 and was redeemable by Room Plus at a redemption price of five cents per warrant on 30 days' prior written notice.

[3] A "syndicate" is a group of broker-dealers who agree to purchase a new issue of securities from the issuer for distribution to the investing public. The marketing process includes the distribution of a preliminary prospectus (also called a "red herring") to prospective purchasers and the solicitation of indications of interest as to how many shares each investor would like to purchase in the IPO. Indications of interest do not commit investors to buy securities. On the day the offering registration becomes effective with the Securities and Exchange Commission ("SEC" or "the Commission"), broker-dealer syndicate members must confirm customers' indications of interest prior to executing trades on the customers' behalf. Subsequently, the broker-dealers must send the customers written confirmations of the executed trades.

AGS Financial Services, Inc. AGS Financial Services, Inc. ("AGS"), another NASD member firm, originally hoped to participate in the Room Plus IPO syndicate. In 1996, however, AGS had a $5,000 minimum net capital requirement, which meant, under the Securities and Exchange Commission's net capital provisions, that AGS could not participate in the Room Plus IPO. See Securities Exchange Act Rule 15c3-1. In 1996, Adam Galas ("Galas") owned AGS. In August of that year, David Shapiro ("Shapiro") infused $150,000 into AGS and became part owner of the firm. Shapiro's infusion of cash relieved AGS of its net capital impediment to participation in the Room Plus syndicate, but AGS' NASD membership agreement nonetheless contained a similar restriction. AGS therefore needed to negotiate with NASD staff to revise the membership agreement before AGS could participate as a syndicate member in the Room Plus IPO. See Membership and Registration Rule 1014.

In October 1996, Galas and Shapiro commenced negotiations with NASD staff to amend AGS' membership agreement. As AGS' negotiations with NASD staff continued, the effective date of the Room Plus IPO quickly approached. NASD staff recommended that AGS formulate a contingency plan to implement in the event that AGS did not receive staff approval of an amendment to its membership agreement before the Room Plus IPO effective date.

AGS representatives discussed their interest in participating in the Room Plus syndicate and AGS' inability to do so with AGS' clearing firm, RPR Correspondent Services ("RPR"). RPR also served as Protective's clearing firm. RPR suggested to AGS that Protective might be willing to take AGS' allocation in the Room Plus IPO if AGS was unable to amend its membership agreement.

Protective's Agreement with AGS. On October 20 or 21, 1996, Flannigan agreed to act as AGS' "standby" in the Room Plus IPO. Flannigan testified that, according to his agreement with AGS (which was not reduced to writing), he had understood that he would not know until immediately before the Room Plus IPO effective date whether or not AGS was able to amend its membership agreement. Flannigan and AGS agreed that, if AGS was not successful in amending its membership agreement, Protective would step in immediately before the IPO's effective date and become a member of the syndicate in place of AGS. In the interim, AGS representatives had been soliciting and continued to solicit indications of interest for the Room Plus IPO. Under the terms of the agreement, Protective would take AGS' syndicate allocation, open accounts at Protective for the AGS customers who had expressed interest in Room Plus, and execute the customers' orders in the Room Plus IPO.[4] AGS and Flannigan agreed that Protective would keep all of the proceeds of the IPO sales. AGS and Flannigan also agreed that Protective would act as a market maker in Room Plus and would pay AGS all commissions that it earned in the Room Plus aftermarket, less Protective's expenses plus two cents per share (for Protective's trader). Flannigan also agreed that Protective would return the AGS customer accounts back to AGS after AGS amended its membership agreement.

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[4] Some of the customers solicited for the Room Plus IPO by AGS representatives never actually became AGS customers before becoming customers of Protective.

AGS' attorneys drafted form letters dated October 31 or November 1, 1996 that AGS sent to customers of the possibility of purchasing Room Plus through Protective. The AGS customers were instructed to authorize the opening of a brokerage account at Protective and the transfer of funds from their AGS accounts to Protective accounts by signing and returning the letter to AGS. The form letter did not direct or authorize the purchase of a specific amount of Room Plus securities in the IPO or in the aftermarket.

AGS determined on October 28, 1996 that it would not be able to participate in the Room Plus IPO.[5] Thereafter, John Flynn ("Flynn"), AGS' trader, sent to Protective customer account information for all of the customers who had returned a signed form letter. The information included net worth, income and investment objectives. Flannigan opened new accounts at Protective for these customers, relying primarily on information provided by AGS. In some instances, Flannigan simply copied all of the information that Flynn had provided. In other cases, if information was missing, Flannigan attempted to contact the customer directly. If he was unable to reach the customer, he obtained the additional information that he needed from Flynn or someone else at AGS. Flannigan did not undertake any additional investigation to verify the accuracy of the information that AGS had provided. Flannigan opened 155 new accounts at Protective, each of which listed Flannigan as the account representative and all of which were dated between October 29 and mid-November 1996.

During the two to three days prior to the effective date of the Room Plus IPO, AGS representatives contacted the AGS customers (many of whom were by then also Protective customers) who previously had expressed interest in Room Plus and confirmed their indications of interest. Flannigan relied on a list of customers provided by Shapiro (at AGS) and represented to the underwriter that Protective had sold its allocation of Room Plus stock and warrants in the IPO.

AGS, not Flannigan or Protective, determined the final allocations to Protective's customers in the Room Plus IPO on or about November 6, 1996.[6] Protective's customers learned of their final allocations when they received their confirmations in the mail.[7]

Protective Group and Flannigan executed Room Plus IPO purchases in 155 accounts. Flannigan acknowledged that all of the 155 accounts belonged to customers who had been referred by

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[5] The record indicated that, although AGS had determined that it would not participate in the Room Plus IPO, AGS representatives continued to solicit indications of interest subsequent to AGS' determination.

[6] Sales of most of the IPO stock were finalized on November 4. The warrant sales were not finalized until November 6.

[7] The final distribution of Room Plus securities was modified numerous times by AGS and RPR because of account input errors, address corrections, and checks returned for insufficient funds. Furthermore, RPR had instructed Protective not to fill customer orders unless the customers had completed new account forms and held funds in their Protective accounts. Some customers who had expressed and confirmed interest in the Room Plus IPO did not meet these requirements and therefore did not receive allocations. Other customers, however, were able to purchase securities in the Room Plus IPO notwithstanding their failure to complete new account forms.

AGS and had been solicited and confirmed by AGS representatives.[8] Flannigan also admitted that he had not contacted these customers before executing their IPO purchases and that neither he nor other representatives of Protective had confirmed the customers' indications of interest. Flannigan relied entirely on AGS representatives to confirm the Room Plus indications of interest.

Protective's Aftermarket Trading in Room Plus. On November 1, 1996 (the effective date of the Room Plus IPO), Room Plus common stock and warrants became immediately tradeable. AGS received solicited and unsolicited customer orders from Protective's customers for sales and purchases of Room Plus securities in the aftermarket. Some of the customers did not understand that they needed to contact Protective to sell their Room Plus securities from their Protective accounts. Other customers understood that they needed to contact Protective, but were unable to reach anyone there, so they contacted their representatives at AGS. AGS representatives referred customer orders in the Room Plus aftermarket to Shapiro (at AGS), who ultimately referred them to Flynn (AGS' trader).[9] Flynn then called the trader at Protective to advise him of the customer orders and also sent directions regarding customer orders to Protective via facsimile.

The orders that AGS sent to Protective via facsimile generally included customers' names, the number of shares or warrants for purchase or sale, and the commissions to be charged. Flannigan admitted that he received customer orders in this manner. Flannigan generally reviewed customer orders that Protective had received from AGS and forwarded the orders to Protective's trader for execution. Flannigan testified that he tried to contact customers before executing aftermarket trades, but he admitted that he executed orders without having contacted customers.

Protective earned $86,000 in commissions for aftermarket trading in Room Plus securities. Flannigan had agreed to pay AGS the commissions that Protective earned in Room Plus aftermarket trading less its costs plus two cents per share. After subtracting Protective's costs ($57,535.76) plus two cents per share from the total, Protective owed AGS $28,947.24, of which it paid $20,000.

Protective's Reliance on AGS for Other Customer-Related Issues. Flannigan also had numerous conversations with and sent many facsimiles to Shapiro and Flynn regarding customers who had not paid for trades or who had paid with checks that were returned for insufficient funds in both the Room Plus IPO and aftermarket. Flannigan also contacted AGS regarding IPO customers for whom he had not received signed letters of authorization to transfer accounts or who had debit balances in their accounts. Flannigan referred complaints of unauthorized trading in the Room Plus aftermarket to

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[8] Most of the AGS representatives who had solicited and confirmed customer interest in the Room Plus IPO were registered with AGS, although none were registered with Protective. The record suggests, however, that some of the AGS representatives were not even registered with AGS when they solicited and confirmed indications of interest in the Room Plus IPO.

[9] In some instances, if a customer was unable to reach an AGS representative, Flynn spoke to the customer. When this occurred, Flynn attempted to arrange a three-way conversation between himself, the customer and someone from Protective. The record is unclear as to whether three-way conversations actually occurred and, if so, how often.

AGS, and he followed AGS' directions to cancel, rebill or reverse the trades at issue. Flannigan generally referred all customer complaints to AGS and relied on AGS to ensure the absence of free-riding and withholding violations in the IPO.

Discussion

Although respondents' notice of appeal indicated that respondents sought NAC review of both the Hearing Panel's findings and the sanctions imposed, respondents indicated in their appeal brief that they primarily sought review only of sanctions. We nonetheless have reviewed the evidence supporting the Hearing Panel's findings. We find that Protective and Flannigan violated Membership and Registration Rule 1031 and Conduct Rules 2110 and 2510 by knowingly permitting individuals who were not registered with Protective to solicit and confirm Protective's sales in the Room Plus IPO and by accepting AGS' directions regarding trading in Protective's customer accounts in the Room Plus aftermarket without a written grant of discretion from the customers.

Registration Violations. Conduct Rule 1031(a) states in part that all persons engaged or to be engaged in the investment banking or securities business of a member who are to function as representatives shall be registered as such in the category of registration appropriate to the function to be performed. Section (b) of Conduct Rule 1031 defines "representative" as a person associated with a member who is engaged in the investment banking or securities business for the member. The clear purpose of Rule 1031 is that individuals who engage in the investment banking or securities business of a member firm must be registered with the Association and associated with that member.[10] The Commission similarly has held that an individual who solicits customers on behalf of a member firm must be registered as an associated person of that firm, regardless of whether he also is registered with another firm. See Cambridge Group, Inc., 50 S.E.C. 752 (1991) (registration violation found in case in which registered person who was associated with one member firm solicited investors on behalf of a second member firm with which he was not associated), mod., Hately v. SEC, 8 F.3d 653 (9th Cir. 1993).[11]

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[10] See NASD Notice to Members 88-50 (July 1988) (members are required to register persons who accept orders from the public, share in commissions generated in customer accounts, or solicit accounts on behalf of the firm); NASD Notice to Members 88-24 (March 1988) (members are required to register any person who contacts potential customers of the firm for the purpose of opening accounts, soliciting orders, or qualifying potential customers for the firm).

[11] Respondents argued that the Hearing Panel erred in relying on the Cambridge decision because the facts in Cambridge differ from the facts in this case. We do not agree that the Hearing Panel erred in this regard. Although the underlying facts differ, the SEC's holding in Cambridge is instructive. In Cambridge, a three-person firm (Cambridge) entered into a finder's fee agreement with Lawrence Hold ("Hold") (also a respondent in the matter), an individual who was registered with another firm but not registered with Cambridge. During the life of the agreement, Hold's referrals to Cambridge resulted in $55,000 in commissions for Cambridge, which the firm shared with Hold. The SEC's holding that Cambridge violated Part III, Section 1(a) of Schedule C of the NASD's By-Laws (now Membership and Registration Rule 1031) by allowing Hold to solicit on behalf of Cambridge when he was registered with another firm but not with Cambridge is directly applicable to this case.

Respondents do not dispute that AGS representatives solicited and confirmed indications of interest for Protective's sales in the Room Plus IPO before and after October 28, 1996, the date when AGS determined that it could not participate in the offering. Flannigan knew that AGS representatives were soliciting customers in the Room Plus IPO and that Protective, not AGS, would be executing (and, in fact, did execute) the trades. Flannigan also knew that none of the AGS representatives were registered with Protective, and Flannigan had agreed, on behalf of Protective, to compensate AGS. We find that, by soliciting and confirming indications of interest for the Room Plus IPO, AGS representatives engaged in the securities business of Protective and should have been registered as associated persons of Protective. Protective and Flannigan consented to this arrangement and therefore violated Rule 1031. See Donald R. Gates, Exchange Act Rel. No. 41777 (Aug. 23, 1999) (registration required to purchase and sell securities in customer accounts and to receive transaction-based compensation); Brian Kormos, 52 S.E.C. 303 (1995) (registration required to solicit securities business); First Capital Funding, Inc. 50 S.E.C. 1026 (1992) (registration required to solicit investors in private offerings and to distribute pre-qualification forms); Voss & Co., Inc., 47 S.E.C. 626 (1981) (registration required to receive orders for securities and to derive compensation from those orders).

Improper Exercise of Discretion. Conduct Rule 2510 states in part that no member or registered person shall exercise discretionary power in a customer's account unless the customer has given prior written authorization and the member has accepted the discretionary authority. The Hearing Panel found that Protective and Flannigan improperly exercised discretionary authority in customer accounts when, in the Room Plus aftermarket, they relied on information from AGS representatives to execute transactions without obtaining written authorizations from the customers. We agree.

Flannigan opened approximately 155 customer accounts for trading in Room Plus based on information that AGS provided. All of these accounts listed Flannigan as the account executive and none were discretionary accounts. None of the customers appointed Protective representatives -- much less AGS representatives -- as official customer designees. Flannigan admitted that, in the aftermarket, many of Protective's customers contacted AGS, not Protective, to communicate their orders and that Flynn or other AGS representatives called Flannigan to relay customer trade information and sent customer orders to Protective via facsimile. In most instances, Flannigan relied on information provided by AGS, not the customers themselves, to execute trades in the customer accounts.[12] We find that this conduct violated Conduct Rule 2510. See Thomas E. Warren, 51 S.E.C. 1015 (1994) (violation found in case in which respondent accepted discretionary orders for the accounts of minors from their mother without proper written authorization).

In sum, we affirm the Hearing Panel's findings that Flannigan and Protective violated Membership and Registration Rule 1031 and Conduct Rule 2510 and that, by doing so, they

[12] Flannigan testified that, during some of the calls that he received from AGS representatives, Protective's customers also would be on the line. Flannigan also testified that he sometimes contacted customers to confirm trade information that had been relayed by AGS. Flannigan admitted, however, that he did not confirm order information with customers in every instance and that he executed aftermarket trades based predominantly on information provided by AGS alone.

contravened high standards of commercial honor and just and equitable principles of trade and violated Conduct Rule 2110.[13] See William H. Gerhauser, Sr., Exchange Act Rel. No. 40639 (Nov. 4, 1998) (a violation of an SEC or NASD rule constitutes a violation of the requirement to adhere to just and equitable principles of trade embodied in the NASD Rules).[14]

Sanctions

The Hearing Panel barred Flannigan in all supervisory capacities, fined Flannigan and the Firm $25,000, jointly and severally, and assessed each respondent one-third of the Hearing Panel costs. Respondents argued that the sanctions are excessive. We have considered respondents' arguments, and we hereby affirm the sanctions imposed by the Hearing Panel.[15]

Respondents propounded several arguments to support their request for a reduction of sanctions. Respondents argued as a mitigating factor that NASD staff had advised AGS to "figure out a contingency plan" for the Room Plus IPO and that staff therefore was aware of Protective's agreement with AGS. There is no evidence in the record, however, that NASD staff knew the details of AGS' arrangement with Protective or that staff approved of the arrangement. In any event, respondents cannot shift their responsibility for compliance with NASD rules to NASD staff. See Stephen J. Gluckman, Exchange Act Rel. No. 41628 (July 20, 1998) (respondents cannot shift compliance responsibilities to NASD staff). We therefore reject as a mitigating factor respondents' purported reliance on NASD staff.

Respondents similarly argued that AGS' lawyer was aware of AGS' agreement with Protective and that he had drafted letters to AGS clients advising them that, if they wanted to purchase securities in the Room Plus IPO, they would have to transfer funds to Protective. Respondents argued that their reliance on AGS' counsel should be considered as a mitigating factor with respect to sanctions.[16] The

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[13] Rule 115 indicates that persons associated with a member shall have the same duties and obligations under the NASD's Rules as members. Thus, the ethical standards imposed on members in Rule 2110 apply equally to persons associated with members.

[14] On appeal, Flannigan and Protective filed a motion to adduce Protective's FOCUS reports and net capital computations for June 30, July 31, and August 31, 2000 and Flannigan's W-2 forms for 1996, 1997, 1998 and 1999. Respondents argued that the proposed evidence related to their inability to satisfy a fine. Based on the unique facts and circumstances of this case, we have determined to enter the evidence into the record and have considered it in connection with our determination as to sanctions. We note that in the future, absent compliance with Rule 9346(b), we may find that a respondent who fails to raise and prove inability to pay in proceedings before an initial-level Hearing Panel is precluded from asserting the defense on appeal. See Terry T. Steen, Exchange Act Rel. No. 40055 (June 2, 1998) (respondent who failed to introduce evidence of inability to pay before the law judge may be deemed to have waived issue on appeal).

[15] The Hearing Panel fined respondents $15,000 for violating Rule 1031 (registration) and $10,000 for violating Rule 2510 (exercise of discretion). We affirm the Hearing Panel's apportionment of sanctions.

[16] If reliance on the advice of counsel is asserted as a substantive defense, the party asserting the defense must: 1) make a complete disclosure to the attorney of the intended action, 2) request the attorney's advice as to the

NASD Sanction Guidelines ("Guidelines") list as a principal consideration whether respondent demonstrated reasonable reliance on competent legal advice. Respondents have not demonstrated that reliance on AGS' counsel could be viewed as "reasonable" or that they even discussed with AGS' attorney the legality of their intended actions. Respondents also have not demonstrated that AGS' attorney advised them that their conduct would not violate NASD rules. We therefore reject as a mitigating factor respondents' purported reliance on AGS' counsel.

Respondents also argued, with respect to the IPO sales, that Protective, not AGS, mailed to the customers their confirmations and a final prospectus after the effective date of the offering and that Flannigan became familiar with each customer based on detailed account information that he had received from AGS. Respondents contended that these facts mitigated the severity of their violations. We do not agree. With respect to the majority of customers who purchased securities in the Room Plus IPO, Flannigan, the representative responsible for each sale, had no first-hand knowledge as to who at AGS actually solicited the customers' indications of interest, when and how they did so, and what representations they made during the solicitation. Flannigan also had no personal knowledge of the customers' individual representations as to investment objectives, income, net worth, the number of shares sought, and whether or not they wanted to speculate with their investments. Similarly, Flannigan did not confirm directly with most of the IPO customers their addresses, telephone numbers, and employment information. By relying on AGS for customer information in both the IPO and aftermarket sales, respondents undercut important customer safeguards that the registration rules are designed specifically to provide. "The NASD's registration requirement '[p]rovides an important safeguard in protecting public investors' and, consequently, 'strict adherence to that requirement is essential'" Patricia H. Smith, 52 S.E.C. 346, 348-349 (1995) (citations omitted).

Respondents also argued as a mitigating factor that many of the aftermarket trades were unsolicited. Respondents relied, however, on AGS to determine whether or not the trades were solicited. In a majority of the trades, respondents never obtained first-hand knowledge as to whether or not the trades were solicited. We therefore reject this as a mitigating factor.

Respondents also argued that the respondents in Cambridge, supra, received less significant sanctions for more egregious misconduct and that the NAC therefore should reduce the sanctions that the Hearing Panel imposed. "The appropriate remedies in a disciplinary action[, however,] depend on the circumstances of each particular case." John F. Noonan, 52 S.E.C. 262 at n. 9 (1995). It is not appropriate to compare the sanctions imposed in one disciplinary matter to the sanctions imposed in another where, as here, the issues under review differ significantly. In Cambridge, unlike in this case, a main issue on appeal was disgorgement of ill-gotten gains and whether the record supported the disgorgement order. Furthermore, at the time that the NASD issued its decision in Cambridge, the NASD was authorized to impose a fine of only $15,000 per violation.[17]

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legality of the action, 3) receive counsel's advice that the conduct would be legal, and 4) rely in good faith on that advice. William H. Gerhauser, Exchange Act Rel. No. 40639 (Nov. 4, 1998).

[17] The Hearing Panel noted in its consideration of sanctions that respondents' reliance on customer information and orders from AGS representatives resulted in Flannigan's failure to make his own suitability and free-

We also have considered respondents' claims of inability to satisfy the monetary sanction that the Hearing Panel imposed. The evidence shows Flannigan's total yearly income from Protective, but it does not show his income from other sources or his total assets and liabilities. Based on this evidence, we do not find that Flannigan has demonstrated an inability to pay.

Similarly, we do not find that the evidence demonstrates Protective's inability to pay. The evidence relates primarily to Protective's net capital and financial situation in June, July and August of 2000. The amount of a fine against a member firm need not be related to or limited by a firm's required minimum net capital. See F.B. Horner & Assoc., Inc., 50 S.E.C. 1063, 1068 (1992) ("[T]here is no reason why the amount of a fine must be related to or limited by a firm's net capital."), aff'd, 994 F.2d 61 (2d Cir. 1992). Furthermore, the evidence that respondents propounded regarding Protective's net capital included net capital information for only three months in 2000. This evidence neither demonstrates the Firm's current inability to satisfy the $25,000 fine nor shows that the Firm could not obtain additional capital to satisfy the fine. We therefore reject respondents' inability to pay argument.

Turning next to the principal considerations listed in the NASD Sanction Guidelines ("Guidelines"), we find that several aggravating factors are present. Both Flannigan and Protective have disciplinary histories. Although they do not have a history of engaging in similar misconduct, their disciplinary histories suggest insufficient attention to regulatory compliance. Additionally, although the misconduct at issue involved only one offering, it encompassed 155 customer accounts and numerous IPO and aftermarket trades. Furthermore, the misconduct resulted in the potential for respondents' significant monetary gain.[18] We also have considered that, in our view, Flannigan did not act in good faith. He made little effort to ensure that his conduct did not violate NASD rules, and he opened accounts and executed transactions for numerous customers without ever talking with them, discussing their financial situations and needs, or satisfying himself that the customers understood the investments

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riding determinations and his failure to ensure that all of the aftermarket trades were authorized. Respondents argued that, by considering these factors, the Hearing Panel improperly considered uncharged misconduct. We disagree. The Hearing Panel did not find that respondents had executed unsuitable or unauthorized trades or that they had executed trades in violation of the NASD's Free-Riding Interpretation. Rather, the Hearing Panel found that respondents' failure to obtain first-hand knowledge of their customers resulted in their corresponding failure to ensure that they were not violating other rules by executing these trades.

We find that, by relying on AGS representatives for personal information about Protective's customers and for trading directions, respondents undermined important customer safeguards and treated AGS as customer designees without authority from their customers to do so. We have not considered possible suitability, free-riding or unauthorized trading violations with respect to our sanctions determinations, since misconduct of that nature has not been alleged.

[18] Respondents argued that they lost money as a result of their agreement with AGS. They asserted that their expenses and re-billing charges absorbed their profits. They also asserted that they covered customer losses that resulted from AGS' sales practice misconduct. The record indicates, however, that respondents received a $30,000 allowance fee in the IPO and $85,000 in commissions for aftermarket trading, of which they paid only $20,000 to AGS. Additionally, Flannigan testified that, when he agreed to this deal, he expected to generate a profit. Potential profit therefore factored into Flannigan's decision to proceed in a manner contrary to NASD Rules.

and affirmatively wanted to proceed with the trades. As a securities professional, he should have been more attuned to his obligations fully and fairly to service his customers.[19]

The Hearing Panel also found as an aggravating factor Flannigan's continued failure to appreciate the gravity of his misconduct and the potential threat that his actions posed to the Firm's customers. We agree that Flannigan failed to appreciate that his actions threatened the financial safety of Protective's customers and possibly enabled AGS to engage in misconduct that went undetected by regulatory authorities. The sanctions that we impose, including the supervisory bar, are necessary to protect the investing public, to deter Flannigan from repeating this misconduct, and to disabuse Flannigan of the idea that Protective's agreement with AGS complied with NASD Rules.

Accordingly, Flannigan is barred in all supervisory capacities. The bar imposed herein shall commence upon service of this decision. Additionally, Flannigan and Protective are fined $25,000 jointly and severally, and costs of $1,577.63 are imposed as to each of them individually. The sanctions that we impose are appropriately remedial and consistent with the applicable Guidelines. See Guidelines at 43 (Registration Violations) and 78 (Discretion - Exercise of Discretion Without Customer's Written Authority).[20]

On Behalf of the National Adjudicatory Council,

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Barbara Z. Sweeney, Senior Vice President and
Corporate Secretary

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[19] See Guidelines at 43 (Registration Violations) and 78 (Discretion - Exercise of Discretion Without Customer's Written Authority).

[20] We have considered all of the arguments of the parties. They are rejected or sustained to the extent that they are inconsistent or in accord with the views expressed herein.

Pursuant to NASD Procedural Rule 8320, any member who fails to pay any fine, costs, or other monetary sanction imposed in this decision, after seven days' notice in writing, will summarily be suspended or expelled from membership for non-payment. Similarly, the registration of any person associated with a member who fails to pay any fine, costs, or other monetary sanction, after seven days' notice in writing, will summarily be revoked for non-payment.