

BEFORE THE NATIONAL ADJUDICATORY COUNCIL

NASD REGULATION, INC.

In the Matter of

Department of Enforcement,

Complainant,

vs.

Averell Golub

Brooklyn, N.Y.,

Respondent.

Decision

Complaint No. C10990024

Dated: November 17, 2000

**Registered representative made material misrepresentations and omissions when soliciting customers to purchase a security. Held, findings and sanctions modified in part and affirmed in part.**

We called this matter to review the findings and sanctions of the February 17, 2000 decision of an NASD Regulation, Inc. ("NASD Regulation") Hearing Panel, and respondent Averell Golub ("Golub") also appealed the matter. We modify the Hearing Panel's findings in part and affirm the findings in part. We hold that Golub engaged in material misrepresentations and omissions in the sale of securities to two customers. We order that Golub be suspended for one year; fined \$10,000, or, in lieu of the fine, be required to supply proof of payment of full restitution plus interest to one customer; be required to pay \$20,527.48 in restitution plus interest to the other customer; and be required to pay hearing costs.

Background

This case involves allegations that Golub made material misrepresentations and omissions when soliciting three customers to purchase shares of Music & Entertainment Network ("MENW"), a company whose shares traded on the OTC Bulletin Board.<sup>1</sup> The

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<sup>1</sup> The OTC Bulletin Board is a quotation service that displays real-time quotes, last-sale prices, and volume information in domestic and certain foreign securities. Although the OTC Bulletin Board is operated by the NASD, it is unlike The Nasdaq Stock Market, Inc. ("Nasdaq") or other listed markets where individual companies apply for listing and must meet and maintain strict listing standards; instead, individual brokerage firms or market makers initiate quotations for specific securities on the Bulletin Board. NASD Notice to Members 99-15 (Feb. 1999).

complaint alleged, among other things, that Golub misrepresented that MENW traded on the Nasdaq SmallCap Market; that MENW would undergo a public offering within a three-week period and would be traded on the Nasdaq National Market; and that MENW did not represent a speculative investment. The complaint also alleged that Golub omitted the following negative information about MENW: the speculative nature of the stock, that MENW had experienced losses since its inception, and that MENW had no prior performance with respect to its then-current business plan. The Hearing Panel found that Golub made material misrepresentations and omissions of material facts to two customers.<sup>2</sup> We modify the Hearing Panel's findings, but also hold that Golub made material misrepresentations and omissions when soliciting the two customers.

Golub entered the securities industry in 1990.<sup>3</sup> From February to June of 1996, he was employed by First American Equities, Inc. ("FAE") as a general securities representative.<sup>4</sup> In

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<sup>2</sup> NASD Regulation investigated this matter after receiving customer complaints involving Golub. The Department of Enforcement ("Enforcement") filed a three-cause complaint alleging that Golub had violated Sections 10(b) and 15(c) of the Securities Exchange Act of 1934 ("Exchange Act"), Exchange Act Rules 10b-5 and 15c1-2, Section 17(a) of the Securities Act of 1933 ("Securities Act") through Conduct Rule 2110, and NASD Conduct Rule 2120, by making material misrepresentations and omitting material information when soliciting customers MB, CB, and a third customer, RW. The Hearing Panel ultimately dismissed the allegations relating to RW after finding that Enforcement had failed to prove by a preponderance of the evidence that Golub had solicited RW. The Hearing Panel also found that Section 15(c) of the Exchange Act and SEC Rule 15c1-2 did not apply here. We affirm the Hearing Panel's dismissal of the allegations relating to RW. We also affirm the Hearing Panel's findings that Section 15(c) and Exchange Act Rule 15c1-2 only apply to broker-dealers or to representatives who aid and abet broker-dealer violations. See Richard H. Morrow, Exchange Act Rel. No. 40392 (1998). Here, Golub's firm was not named as a party to the complaint.

<sup>3</sup> Golub currently is not associated with a member firm.

<sup>4</sup> After Golub was employed by FAE, from January until February 3, 1997, he was associated with Corporate Securities Group, Inc. ("Corporate Securities"). On March 4, 1997, NASD Regulation received a Uniform Notice of Termination of Securities Industry Registration ("Form U-5") from Corporate Securities describing Golub's termination. In Golub's answer to the complaint in this matter, he moved to dismiss the proceeding on the grounds that the NASD lacked jurisdiction over him because the complaint, filed on February 25, 1999, was filed more than two years after he ended his employment with Corporate Securities. The Hearing Panel denied the motion and found that because the NASD had received Golub's Form U-5 within two years of the filing of the complaint, the Association had jurisdiction over him under Article V, Section 4(a) of the NASD By-Laws. We agree and affirm the Hearing Panel's ruling.

April of 1996, FAE began soliciting customers to purchase shares of MENW and Golub assisted with the preparation of "sales scripts" to use in "cold calling" customers. In April and May of 1996, Golub successfully solicited MB and CB to purchase shares of MENW.

MENW. MENW was a "developmental stage" company engaged in the business of producing records, concerts, and special events and in the sales of classic rock videos, CDs, and related products. MENW was formerly known as Blue Grizzly Trucking, Inc., prior to the amendment of its articles of incorporation to reflect the company's name change to MENW on January 2, 1996. Prior to that, the company was known as Sabel Palm Airways, Inc.; the company was originally incorporated as U.S. Retail, Inc., in 1987. According to MENW's unaudited financial statement, "from its inception on June 10, 1987 through February 29, 1996," MENW had "0" revenues and net losses totaling \$139,857. For the two months ending February 29, 1996, the unaudited financial statement showed that MENW had no revenues and losses of \$63,024.

NASD Regulation staff obtained copies of MENW's SEC Rule 15c2-11 Information Statement,<sup>5</sup> MENW's unaudited financial statement, and other information from FAE in response to a Rule 8210 request for FAE's due diligence information on MENW.<sup>6</sup>

FAE produced an April 3, 1996 letter from MENW's President, which stated that MENW's unaudited financial statement "was prepared prior to the merger of our company to a

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<sup>5</sup> MENW was traded on the OTC Bulletin Board and in the "Pink Sheets" (currently known as "Pink Sheets, LLC" and formerly published by the National Quotation Bureau, Inc.), a provider of pricing information for over-the-counter securities. Prior to 1999, there was no requirement for an issuer whose shares traded on the OTC Bulletin Board to file reports on the issuer's financial condition with the SEC or otherwise to make such reports publicly available. See, e.g., NASD Notice to Members 99-15 (SEC Approves Rule Amendments Limiting Quotations on OTC Bulletin Board to Reporting Securities). SEC Rule 15c2-11, however, required broker-dealers who submitted and published quotations for trading certain non-Nasdaq over-the-counter equity securities in any interdealer quotation medium, including the OTC Bulletin Board and the National Quotation Bureau, Inc.'s "Pink Sheets," to review and maintain certain specified information about the issuer before publishing a quotation for that security. See NASD Notice to Members 92-50 (Oct. 1992).

<sup>6</sup> As part of the information provided to FAE pursuant to Rule 15c2-11, MENW provided an April 30, 1995 audited financial statement of Sabel Palm Airways, Inc. The audited financial statement showed that the company was seeking the acquisition of any and all types of assets, properties and businesses; that it was dependent upon financing to continue operations; that it had recurring losses; and that it had no assets.

publicly trading shell." The letter indicated that prior to the merger, the company had "net assets consisting primarily of a music library with a value in excess of \$3,000,000" and "virtually no liability." MENW further indicated that as a result of the merger, MENW "[would] have net tangible assets of an excess of \$3,000,000." The letter represented that certified financial statements were being prepared and would be forwarded to FAE upon completion. No copies of any such certified financial statements, however, appear in the record.

One of the items that NASD Regulation obtained from FAE was a research report prepared by Tellerstock, Incorporated ("Tellerstock"), which stated that MENW's trading symbol was "NASDAQ 'MENW.'" The research report also reported MENW's current price as of April 2, 1996 as "\$5.00," and forecasted a price of "\$15-17." The report described several projects MENW was developing, including "Earthrise on QVC," a record release party and concert to announce the release of a 3 CD/cassette package called "Earthrise I and II" to be sold on the QVC Shopping Network on April 22, 1996. In an April 22, 1996 press release, MENW claimed that it had begun selling its "Earthrise I & II CDs and cassettes on QVC Shopping Network."

Customer MB. In early 1996, Golub contacted MB and recommended that he purchase shares of Intel stock. MB stated that he informed Golub that he would watch Intel to test Golub's advice before purchasing any shares of Intel. Golub called MB several more times and in April of 1996, MB contacted Golub and indicated an interest in purchasing Intel. MB subsequently transferred shares of stock from another brokerage account and opened an account with FAE. On May 7, 1996, Golub contacted MB and stated that "it was too late to capitalize on Intel because he had a better recommendation." During this conversation, MB had a copy of The Wall Street Journal on his desk and he attempted to locate MENW's listing in the Journal. MB indicated to Golub that he could not find MENW in The Wall Street Journal. According to MB, Golub informed him "not to worry about it" and that MENW would periodically show up in the Nasdaq SmallCap listings of the Journal. MB asked Golub to send him a prospectus and any research or literature he had on MENW. According to MB, Golub stated that MENW "was not a risky stock" and MB "finally gave in and agreed" to purchase 3,000 shares of MENW for \$20,625.

On May 17, 1996, MB received a news article on MENW from Golub. On about May 20, 1996, MB contacted Golub and asked why he had not received a prospectus; MB also informed Golub that he still could not find MENW in The Wall Street Journal. On May 20, 1996, MB received a facsimile copy of the Tellerstock research report on MENW from Golub. (Neither the research report nor the article contained any negative information on MENW.) In the summer of 1996, after reading an article on "shyster brokers," MB thought "it sounded alot like Mr. Golub and some of the other brokers that had made calls" to him. MB contacted the NASD and was told that Golub was not on record as being associated with FAE. MB subsequently transferred his MENW stock to another firm. MB then received Federal Express packages and calls from Golub "pressur[ing] [him] to transfer his stock to [Golub's] new firm."

On August 28, 1996, MB submitted a complaint letter to the NASD describing his dealings with Golub.

MB testified that at the time of the hearing before the Hearing Panel (October 26, 1999), he still held the 3,000 shares of MENW stock because his new broker had told him that the stock was not worth selling. MB testified that he had 40 shares worth \$97.52 of MENW's successor company, Informatrix Holdings, Inc., due to certain reverse stock splits of MENW shares. MB testified that Golub had not "characterize[d] [MENW as a] risky stock" when soliciting his purchase. MB further testified that Golub did not inform him that MENW was a non-Nasdaq over-the-counter security, that MENW had generated no revenue since its inception, and that it had no operating history with respect to its then-current business plan. MB testified that if Golub had informed him of those facts, he would not have purchased the stock.

Customer CB. CB was unavailable to testify at the hearing below and apparently was traveling at the time that Enforcement staff attempted to locate him. According to CB's sworn declaration, Golub "cold called" him several times in April 1996, stating that he was a branch manager of FAE. On April 24, 1996, CB opened an account with FAE and purchased 500 shares of "LoJack Corp." as a result of a cold call. At that same time, Golub solicited CB to purchase MENW, but he declined, stating that he "only bought stocks that were listed." According to CB, on May 1, 1996, Golub told him that MENW was going to have a public offering and would be listed on the Nasdaq National Market within three weeks. CB stated that Golub told him that MENW would be offered at \$8 to \$10 per share and that he would have an almost immediate profit of \$2 per share. CB purchased 1,000 shares of MENW for \$6,685. In the following weeks, CB attempted to contact Golub by telephone to check on the status of MENW's public offering but was put on hold several times, and eventually was told that Golub no longer worked at FAE. According to CB, a FAE branch manager informed him that MENW was "off by about \$2.00," that MENW was not going to be listed on the Nasdaq, and that he (CB) was "not the only one [Golub] lied to." CB stated that he filed a complaint with the SEC on August 20, 1996, and that on December 17, 1996, he complained to the NASD.

### Discussion

We called this matter to review the Hearing Panel's findings and sanctions, and in particular, to consider whether the Hearing Panel should have ordered Golub to pay restitution to the customers for their losses. In addition, Golub appealed the Hearing Panel's findings and sanctions. Although there is no dispute that Golub solicited MB and CB to purchase MENW through his "cold calls," he denies that he "misrepresented the status of MENW." For the reasons discussed below, we find that Golub made material misrepresentations and omissions when inducing MB and CB to purchase MENW. We base our holdings largely on Golub's own admissions.

The Hearing Panel found that Golub misrepresented the status of MENW as a Nasdaq-listed security when soliciting MB and CB. The Hearing Panel also found that Golub omitted to disclose negative information about MENW to both customers -- namely, that MENW "had no track record in the entertainment industry," that MENW "had no revenue" and that it had "accrued losses." The Hearing Panel concluded that Golub's material misrepresentations and omissions violated Section 10(b) of the Exchange Act, SEC Rule 10b-5, Section 17(a) of the Securities Act and NASD Conduct Rules 2110 and 2120, as alleged in the complaint.<sup>7</sup> We find violations of each of these provisions, but we modify the Hearing Panel's findings, and we tailor our findings consistent with the specific factual allegations of the complaint.

Golub's Material Misrepresentations. The complaint alleged that Golub misrepresented that MENW traded on the Nasdaq SmallCap Market with respect to MB, and that to CB, he misrepresented that MENW was going to have a public offering within three weeks and that it would be traded on the Nasdaq National Market. The record evidence shows that MENW was traded on the OTC Bulletin Board from January of 1996 through at least September of 1996, during the several months before and after Golub recommended MENW to the customers. In addition, NASD Regulation staff testified that it had been unable to locate any registration statement filed with the SEC for MENW, or for Informatix Holdings, Inc., MENW's successor as of July 1998, thereby indicating that MENW did not in fact engage in a public offering as Golub had represented would occur to CB.<sup>8</sup>

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<sup>7</sup> Section 10(b) of the Exchange Act and SEC Rule 10b-5, and NASD Conduct Rule 2120 prohibit any fraudulent scheme or device in connection with the purchase or sale of securities. Exchange Act Rule 10b-5 specifically makes it unlawful for any person to "make any untrue statement of material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading." Section 17(a) of the Securities Act provides, in part, that it is unlawful for any seller to sell securities to obtain money by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statement made, in light of the circumstances under which they were made, not misleading.

<sup>8</sup> We note that Francis Martorana ("Martorana"), an NASD Regulation staff examiner, testified as to various aspects of NASD Regulation's investigation of Golub. The examiner who actually conducted the investigation, however, did not testify because he was no longer employed by the NASD. Martorana testified as to how the examiner conducted the investigation, and Martorana authenticated certain hand-written notes that the examiner apparently had taken during conversations with CB. We disregard the portions of Martorana's testimony that describe those aspects of the investigation with which Martorana was not personally involved, and we instead rely on the official documents on those points. We also place no weight on the examiner's hand-written notes reflecting his conversation with CB.

We agree with the Hearing Panel's finding that Golub informed MB that MENW would appear in the Nasdaq SmallCap section of The Wall Street Journal. We note that MB's testimony on this point was consistent with his 1996 complaint letter submitted to the NASD. We also find CB's sworn declaration to be sufficiently reliable.<sup>9</sup> The declaration, which is consistent with his 1996 complaint to the NASD, stated that Golub informed him that there would be a public offering within three weeks and that MENW would be listed on Nasdaq.<sup>10</sup> Indeed, Golub's own admissions largely support the customer's assertions. Golub admitted that he thought MENW would go through a public offering. He also admitted that he informed his customers that MENW was a Nasdaq stock when he testified: "I told them it was a Nasdaq stock . . . . I said it was a Nasdaq Bulletin Board stock. I did not know if you were a pink sheet you were a Non-Nasdaq . . . . [MENW was] trying to get to the SmallCap." Accordingly, Golub's own admissions give credence to the customers' statements that Golub informed MB that MENW would be listed in the SmallCap section of the newspaper, and that he informed CB that MENW would go through a public offering and be listed on Nasdaq.<sup>11</sup>

The Hearing Panel found that Golub was "reckless in making the misrepresentation regarding the listing of MENW on the Nasdaq SmallCap Market and in failing to disclose negative information, which was in FAE's files." Although Golub claims he was confused over whether MENW was a Nasdaq stock, he knew at the time of the sale that MENW was trading on the OTC Bulletin Board, and not on the Nasdaq SmallCap Market. Even if he might have been informed by members of his firm that MENW would go up in price and that a public offering was expected, he had no reason to believe that this would occur within three weeks or

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<sup>9</sup> Golub objected to CB's declaration on the grounds that he did not testify and that Golub had no opportunity for cross-examination. We note that NASD Regulation staff was unable to locate CB to procure his testimony at the time of the hearing. We find, however, that CB's declaration, while hearsay, is sworn and is consistent with his 1996 complaint to the NASD, and therefore provides ample indicia of reliability. In addition, we note that, as discussed above, Golub's own admissions to a large extent corroborate CB's statements regarding the public offering and Golub's nondisclosure of negative information. Finally, we note that the Commission has stated that hearsay evidence may under appropriate circumstances constitute the sole basis for findings of fact. See In re Carlton Wade Fleming, Jr., 52 S.E.C. 409, 411 (1995); In re Charles D. Tom, 50 S.E.C. 1142, 1445 (1992).

<sup>10</sup> The complaint also alleged that Golub misrepresented to CB that "the shares of MENW would be offered at between \$8 to \$10," that CB would "realize a \$2.00 profit per share on any investment in MENW," and that "shares of MENW would increase to \$16.00 per share." Because the Hearing Panel failed to make findings on whether Golub made these alleged misrepresentations, and because there was little testimony at the hearing on this point from Golub or others, we dismiss those allegations.

<sup>11</sup> In addition, Golub sent MB a copy of the Tellerstock research report falsely identifying MENW's trading symbol as "'NASDAQ' MENW."

that MENW would become a Nasdaq-listed security. In addition, Golub admittedly helped members of his firm prepare sales scripts on MENW. Accordingly, we find that Golub acted at a minimum recklessly in making the misrepresentations,<sup>12</sup> and we affirm the Hearing Panel's finding that he violated Section 10b-5 of the Exchange Act, SEC Rule 10b-5, Section 17(a) of the Securities Act and Conduct Rule 2110, and Conduct Rule 2120.

Golub's Material Omissions. We, like the Hearing Panel, also find that Golub omitted certain negative material information about the issuer when he recommended MENW to the customers. We, however, modify those findings. The Hearing Panel found that Golub omitted informing the customers that "MENW had no track record in the entertainment industry, had no revenue, and had accrued losses." The complaint specifically alleged, however, that Golub omitted informing them of "the speculative nature" of MENW, that MENW "had experienced losses since its inception," and that "MENW had no prior performance with respect to its then current business plan." Based on the record before us, we are unable to uphold the complaint's allegation that MENW had "no prior performance with respect to its then current business plan" because we cannot determine what MENW's "current business plan" was, as no such business plan is in the record.

In addition, although the Hearing Panel apparently construed the allegation to mean that MENW had no track record in the entertainment industry, we cannot discern from the record the extent of MENW's past and present business in the industry, if any. Although we are aware that MENW's unaudited financial statement stated that it had no revenue, we note that there are press clippings and various other documents in the record indicating that in April of 1996, MENW apparently launched sales of certain CDs on QVC Shopping Network. We also note that in an April 3, 1996 letter to FAE, MENW's president, a former popular musician, indicated that MENW had certain net assets "consisting primarily of a music library" and virtually "no liability." We are unable to discern what credence, if any, to give to this letter or to MENW's press releases. Based on the record before us, we cannot determine the extent of MENW's "prior performance" or MENW's "then current business plan" to make findings consistent with the complaint's allegation. We therefore dismiss that allegation.

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<sup>12</sup> We also find that the misrepresentations were material. Whether information is material "depends on the significance the reasonable investor would place on the withheld or misrepresented information." Basic, Inc. v. Levinson, 485 U.S. 224, 240 (1988). The information in question must "have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." Id., 485 U.S. at 231-32 (quoting TSC Indus. v. Northway, Inc., 426 U.S. 438, 449). Material information includes "not only information disclosing the earnings . . . of a company but also those facts which affect the probable future of the company and which may affect the desires of investors to buy, sell, or hold the company's securities." SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 849 (2d Cir. 1968).



We do note, however, that MENW described itself as a "development stage company" and that its unaudited financial statement reported no revenues and losses totaling \$63,024 for the two-month period ending in February 1996, and an aggregate loss of \$139,857 since its inception in 1987. There can be no doubt that MENW was a speculative stock based on the fact MENW was a development-stage company that had suffered losses since its inception. We uphold the complaint's allegations that Golub omitted informing the customers of MENW's "speculative nature" and that MENW had "experienced losses since its inception."<sup>13</sup> We note that MB testified that Golub in fact did not disclose any negative information about MENW to him. CB's declaration stated that he found out that MENW "had no business" after he had purchased MENW.

We base our finding that Golub omitted the negative material information primarily on Golub's own testimony in which he admitted that he was not aware of any negative information about MENW when he recommended it to his customers.<sup>14</sup> Although the customers knew that they were purchasing a stock valued at around \$6 per share, their decision to purchase the stock necessarily rested on information about MENW supplied by Golub. Golub testified that he conducted "no research" on MENW before soliciting the customers and that he read only the research report and the press releases. Not only did Golub fail reasonably to ascertain whether there was negative information on MENW before recommending that his customers purchase it, but also he admitted that he conducted virtually no investigation of MENW whatsoever before he recommended it to his customers.<sup>15</sup> Accordingly, Golub violated his duty to deal fairly with

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<sup>13</sup> We note that the Hearing Panel made no ruling on the complaint's allegation that Golub made "statements that conveyed directly or created the impression that a purchase of MENW did not represent a speculative investment." We dismiss this allegation because no findings were made by the Hearing Panel as to whether Golub made affirmative statements misrepresenting that the stock was not a risky investment. Instead, we sustain the finding that Golub omitted disclosing the "speculative nature of an investment in MENW." We again note that Golub admitted disclosing no negative information on MENW.

<sup>14</sup> We also find that the above information was material, *i.e.*, that it would change the "total mix" of information available on a security to the reasonable investor. In general, the "speculative nature" of a security and an issuer's negative earnings are "something to which a reasonable investor attaches importance." SEC v. Hasho, 784 F. Supp. 1059, 1109; *see* SEC v. R.A. Holman & Co., 366 F.2d 456, 459 (2d Cir. 1966); SEC v. Capital Counsellors, Inc. 332 F. Supp. 291, 302 (S.D.N.Y. 1971).

<sup>15</sup> Before making a recommendation to customers, brokers are under a "duty to investigate" the recommendation. Hanly v. SEC, 415 F.2d 589, 595 (2d Cir. 1969). (When making a recommendation, a broker "implicitly represents he has an adequate basis for the opinions he renders."); SEC v. Hasho, 784 F. Supp. at 1107 (A broker "cannot deliberately ignore that which he has a duty to know and recklessly state facts about matters of which he is ignorant . . . . [Rather,] [h]e must analyze sales literature and must not blindly accept

his customers under Conduct Rule 2110. In addition, Golub violated the antifraud provisions of the federal securities laws and NASD Conduct Rule 2120 when he recklessly turned a blind eye to the negative information contained in FAE's files and omitted informing the customers of MENW's speculative nature and the fact that the company had suffered losses since inception.<sup>16</sup> He acted at a minimum recklessly, and with scienter. Knowing that he was failing to disclose any negative information about MENW, he fraudulently induced his customers to purchase MENW.

### Sanctions

The Hearing Panel ordered that Golub be suspended for one year and fined \$50,175 (\$50,000 plus \$175 in commissions fined away).<sup>17</sup> We think the one-year suspension is amply

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recommendations made therein."); see In re Michael J. Fee, 50 S.E.C. 1124, 1125 (1992), cert. denied, 998 F.2d 1002 (3d. Cir. 1993) (table format).

A broker who breaches this duty and makes a recommendation to purchase a security without a reasonable basis also violates Conduct Rule 2110, which requires a member, in the conduct of his business, to "observe high standards of commercial honor and just and equitable principles of trade." Rule 115(a) indicates that persons associated with a member shall have the same 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.

<sup>16</sup> Violations of the antifraud provisions of the federal securities laws and the NASD's antifraud rule are found when a broker has made: (1) a material misrepresentation or has omitted disclosing a material fact; (2) in connection with the offer or sale of a security; (3) with scienter. See SEC v. Hasho, 784 F. Supp. 1059. Scienter is a "mental state embracing intent to deceive, manipulate, or defraud." Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193-94 n.12 (1976). The Commission and courts of appeals in eleven circuits have held that recklessness suffices to show scienter. See Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1568-69 (9th Cir. 1990), cert. denied, 499 U.S. 976 (1991); In re Kevin Eric Shaughnessy, Exchange Act Rel. No. 40244, at 5 (July 22, 1998). Recklessness is "not merely simple, or even excusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the [respondent] or so obvious that the actor must have been aware of it." Hollinger, 914 F.2d at 1569. Scienter is not required for violations of Section 17(a)(2) or 17(a)(3). See Aaron v. SEC, 446 U.S. 680, 686-87 n.6 (1980).

<sup>17</sup> In assessing the appropriate sanctions, the Hearing Panel stated: "With respect to the misrepresentation concerning the status of the security as well as the omission of negative information, Respondent relied on information provided by his employer, FAE. Although reliance does not excuse the conduct, it does convince the Hearing Panel that respondent did

warranted in this instance given Golub's complete failure to acknowledge his duty to his customers.<sup>18</sup> Because we are ordering Golub to pay restitution, and because we have modified the Hearing Panel's findings, we reduce the fine imposed by the Hearing Panel to \$10,000. In lieu of payment of this fine, however, Golub may supply proof that he has paid restitution plus interest to CB for account losses caused by the MENW purchase. Because there is no evidence in the record regarding whether CB has retained the investment in MENW or sold it, we are unable to calculate the specific amount of losses for Golub's payment. We therefore provide that Golub shall supply such proof that he has paid CB full restitution plus interest or be required to pay the \$10,000 fine. In addition, we order Golub to pay \$20,527.48 in restitution, plus interest, to MB.<sup>19</sup> We find that equity demands restitution in this instance because Golub fraudulently induced the customers to purchase MENW.<sup>20</sup>

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not willfully lie or withhold information." We reject the Hearing Panel's suggestion that it was somehow mitigating that Golub merely relied on information provided by his employer. Cf. SEC v. Hasho, 784 F. Supp. at 1107 ("[R]egistered representatives have certain duties that they cannot avoid by reliance on either their employer or an issuer."). Moreover, Golub admits that he assisted with the preparation of the sales script presumably on behalf of FAE. His turning a blind eye to any negative information on MENW was therefore intentional and certainly not mitigating.

<sup>18</sup> We note that the one-year suspension and \$10,000 fine would be warranted even for Golub's misconduct with respect to one customer.

<sup>19</sup> We calculate the amount of restitution as follows: The record contains a confirmation sheet and an account statement indicating that MB purchased 3,000 shares of MENW at \$6.875 per share (totaling \$20,625). According to an account statement that was provided just prior to the hearing below, MB's investment in Informatix Holdings, Inc. (MENW's successor) is worth \$97.52. Accordingly, MB lost \$20,527.48 on the transaction. We recognize that our calculation of MB's losses as totaling \$20,527.48 differs from the \$14,625 restitution amount specified by Enforcement in certain pleadings in the record. We are unable, however, to determine how Enforcement arrived at the \$14,625 figure. We calculate MB's losses based on his September 1999 account statement showing the value of his investment in Informatix Holdings to be worth \$97.52, and MB's testimony at the hearing confirming this. We note that Enforcement's schedule of losses, labeled Exhibit 41, appears to have been excluded from the record at the hearing below.

We order that Golub also pay interest on the \$20,527.48, payable from May 7, 1996, at the rate established for underpayment of income taxes in Section 6621(a) of the Internal Revenue Service, 26 U.S.C. § 6621(a).

<sup>20</sup> The Hearing Panel was silent on the issue of why restitution to the customers was not ordered. The Hearing Panel did state, however, that "[a]s early as 1996, both [MB] and [CB]

Restitution "seeks either to prevent a wrongdoer from being unjustly enriched by his or her wrongdoing or, alternatively, to require the wrongdoer to restore the victim to the status quo ante. Equity demands that, as between [the customer] and [the broker], [the broker] should bear the loss." In re Charles E. French, 52 S.E.C. 858, 864 (1996). We reject Golub's argument that he should not be responsible for additional losses that MB incurred after he transferred his account to another broker and after Golub left FAE. MB's decision to purchase MENW in the first instance was based on Golub's misrepresentations and omissions and therefore Golub should be required to return him to the status quo ante. We also reject Golub's argument that he should not be ordered to pay restitution because he earned only \$17,000 while employed by FAE and his commissions on the sales amounted to only about \$175.<sup>21</sup> We note that the Commission has "sustained restitution orders where the amount exceeds the amount by which the wrongdoer was wrongfully enriched 'if equity would demand that the wrongdoer, rather than the customer, bear the loss.'" In re Franklin N. Wolf, 52 SEC 517, 526 (1995) (restitution upheld even though there had been no showing of the extent Wolf "personally profited"); In re David Joseph Dambro, 51 S.E.C. 513 (1993) (upholding restitution order where amount ordered exceeded amount by which applicant was enriched).

We think that the one-year suspension, the \$20,527.48 in restitution plus interest payment to MB, and Golub's proof of restitution payment with interest to CB or, failing proof of restitution to CB, his payment of a \$10,000 fine, are appropriate in this instance. We think these sanctions will serve as a deterrent and impress upon Golub and other brokers their duty to

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(continued...)

were aware of problems with the stock and failed to take action." We note that both customers did complain to the NASD in 1996. We also note that MB testified that his broker informed him that the MENW shares were not worth selling. We find that the customers should not be responsible for assuming the losses because their purchases were based on a fraud. Finally, we reject the Hearing Panel's finding that it was mitigating that Golub did not "continue to falsely reassure customers [MB] and [CB] that MENW was a good investment." The Hearing Panel apparently inferred that because Golub had virtually no follow-up conversations with the customers shortly after their purchases, he did not continue to perpetuate the fraud. In fact, the record indicates that Golub was employed by FAE only a few months after the customers purchased MENW, and that he made no affirmative efforts to correct any of their misimpressions regarding MENW. We find that there are no mitigating factors present here.

<sup>21</sup> We note that Golub was employed by FAE for only about four months, from February to June of 1996. During this time, he also was employed in another capacity as a court clerk. Golub's assertion that Enforcement improperly reported his activities to his other employer is not relevant to this disciplinary proceeding in determination of whether he violated the federal securities laws and NASD rules. Finally, we affirm the Hearing Panel's determination to deny Golub's motion for sanctions against the Department of Enforcement for contemptuous conduct under Rule 9280 .

deal fairly with customers. We have not specifically ordered Golub to requalify by examination because he has been out of the industry for more than two years and will be required to requalify by examination prior to re-entering the industry.

Accordingly, we order Golub to pay a \$10,000 fine or to supply proof satisfactory to the Department of Enforcement that he has paid restitution to customer CB for the full amount of the account's losses due to the purchase of MENW, plus interest beginning on May 1, 1996 in accordance with Section 6621(a) of the Internal Revenue Code; to pay restitution to customer MB of \$20,527.48, plus interest as specified in note 19; and we affirm the assessment of \$2,255 in costs imposed by the Hearing Panel.<sup>22</sup> We also order that Golub be suspended for one year from association with any member firm in any capacity.<sup>23</sup> Golub must submit proof to the Department of Enforcement that he has paid customer MB the \$20,527.48 in restitution plus interest within 60 days of the date of this decision.<sup>24</sup>

On Behalf of the National Adjudicatory Council,

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Joan C. Conley, Senior Vice President and  
Corporate Secretary

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<sup>22</sup> In the event that MB cannot be located, unpaid restitution should be paid to the appropriate escheat, unclaimed-property, or abandoned-property fund for the state of the customer's last known residence.

<sup>23</sup> The recommended sanctions are consistent with the applicable NASD Sanction Guidelines ("Guidelines"). See Guidelines (1998 ed.) at 80 (Misrepresentations or Material Omissions of Fact).

<sup>24</sup> 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.