BEFORE THE NATIONAL ADJUDICATORY COUNCIL
NASD

In the Matter of Department of Enforcement, Complainant, vs. Joseph Abbondante Freehold, NJ, Respondent.	DECISION Complaint No. C10020090 Dated: April 5, 2005

Respondent fraudulently misrepresented material facts and failed to disclose a material fact to customers; engaged in private securities transactions without giving his firm prior written notice and receiving prior written approval; engaged in outside business activities without giving his firm written notice; and assisted in the preparation of false account statements. Held, findings and sanctions modified.

Appearances

For the Complainant Department of Enforcement: Gary Chodosh, Esq. and William St. Louis, Esq.

For the Respondent: Louis Maione, Esq.

Opinion

Joseph Abbondante ("Abbondante") has appealed a November 7, 2003 decision of a Hearing Panel pursuant to NASD Procedural Rule 9311(a). The Department of Enforcement ("Enforcement") has cross-appealed, pursuant to NASD Procedural Rule 9311(d). After a complete review of the record, we find that Abbondante violated Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act"), SEC Rule 10b-5, and NASD Conduct Rules 2110 and 2120 by making fraudulent misrepresentations and an omission of a material fact to customers of the firm with which he was associated. We also find that Abbondante violated NASD Conduct Rules 2110 and 3040 by engaging in private securities transactions without providing prior written notice and receiving prior written approval. Further, we find that Abbondante violated NASD Conduct Rules 2110 and 3030 by engaging in outside business activities without providing his employer firm with prompt written notice. Finally, we find that Abbondante violated NASD Conduct Rule 2110 by assisting with the preparation of false account statements.

We find Abbondante's activities to be egregious and bar him from associating with any member firm in all capacities. We also order Abbondante to pay restitution. We affirm the hearing costs imposed below and order that Abbondante pay appeal costs.

I. Background

Abbondante first became registered with NASD as an investment company/variable contracts representative in October 1988. Abbondante was registered as a general securities representative with Chase Investment Services Corp. ("CIS") from September 1996 through November 1999, when he voluntarily terminated his association with CIS. Abbondante was last registered with an NASD member firm as a general securities representative from February 2002 through September 2002.

II. Facts

A. Iris LP

Iris Limited Partnership ("Iris LP"), a Nevada limited partnership, was formed primarily to trade stocks, bonds, and mutual funds. From September 1998 through March 1999, Jerry A. Womack ("Womack"), the general partner of Iris LP, sold interests in Iris LP. Womack represented to prospective investors that Iris LP would invest their money using a successful trading strategy that he called the "Womack Dow Principal," or the "Dow Jones Formula."

In May 2001, Womack was convicted in the United States District Court for the Central District of California of wire and mail fraud and money laundering in connection with his Iris LP sales activities. On July 1, 2003, Womack was sentenced to approximately 16 years in prison and ordered to pay more than $6 million in restitution to investors in Iris LP. After Womack's conviction and prior to the hearing in this matter, Abbondante and Enforcement entered into a stipulation in which they agreed to findings that Womack had not invested customers' funds using the alleged successful trading formula but, instead, had operated a "Ponzi" scheme, paying many investors purported trading profits from funds that other investors contributed to Iris LP.

B. Abbondante Discusses Iris LP with CIS Customers AC, KC, and RS

On September 18, 1998, a banker at Chase Manhattan Bank ("CMB"), an affiliate of CIS, introduced Womack to CIS registered representative SF, advising her that Womack was depositing a large sum of money at CMB and that he was interested in opening a brokerage account at CIS. That same month, SF opened a brokerage account for Womack, who advised SF that he would be using his account to trade equities and that he had a formula that would generate high returns.[1] SF subsequently introduced Womack to Abbondante because SF and Abbondante shared business under a joint brokerage number and because Abbondante handled the actively-traded accounts.

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[1] Womack represented on the account application that he had a net worth of $18 million, investment assets of $18 million, and an approximate annual salary of $180,000.

Abbondante testified that Womack opened his CIS brokerage account with a check for $900,000 from an entity called "Iris LP." Womack told Abbondante that he was the general partner of Iris LP, which he described as an investment vehicle that traded equities. Abbondante testified that he understood from his conversations with Womack and other Iris LP employees that Iris LP also had investments in real estate, art, record companies, and a golf course. Abbondante testified that Womack advised him that he was employed as a mechanic but that he had used his mathematical aptitude to analyze trends in the equities market to develop a successful trading strategy called the "Dow Jones Formula" that he employed to trade funds that limited partners had invested in Iris LP. When Abbondante asked Womack for information about the trading strategy, Womack told him that he could not divulge any details about it except to state that it involved the buying or selling of all 30 Dow Jones Industrial Average stocks simultaneously in response to short-term market movements.

Abbondante testified that Womack used his Dow Jones Formula for only a few days after he commenced trading his personal account and that he sustained losses of approximately $30,000. After abandoning his Dow Jones Formula, Womack employed a number of other trading strategies in the three-month period (from September through November 1998) during which he traded in his personal account.

On November 9, 1998, Womack opened a second account at CIS in the name of Iris LP and transferred money from his personal account at CIS to the Iris LP account. Abbondante testified that Womack stated that he would be employing a trading strategy different from the Dow Jones Formula in the Iris LP account. The trading in that account produced net trading losses from November 1998 through February 1999.

Abbondante nonetheless made representations about Iris LP and its professed successful trading strategy to three individuals who eventually decided to invest in Iris LP after hearing for the first time about the investment from Abbondante. The first individual, AC, testified that he and Abbondante were good friends who used to commute together from New Jersey into New York City. During these commutes, Abbondante told AC: (1) Womack was a high net worth individual and the general partner of a limited partnership that traded stocks on the basis of a formula that was conducive to making superior returns as long as the market stayed volatile; (2) the trading formula produced returns that were "[s]upposed to average eight to ten percent per month"; (3) Womack was successful in trading his own formula; and (4) CMB had performed a due diligence background check on Womack and found no adverse information. In addition, Abbondante told AC that he was going to invest his own money with Womack.

On December 31, 1998, AC went to Abbondante's office for the purpose of investing in Iris LP, at which time Abbondante arranged for him to talk by telephone to GB, an employee of Iris LP. GB, a supposed investor in Iris LP, told AC that Iris LP was striving to earn a rate of return in the range of eight to 10 percent per month and that the trading formula that Iris LP used was based on the "Dow." Afterward, Abbondante gave AC a wire transfer form and helped AC complete it. AC left the form with Abbondante, and within a day or two, $25,000 was transferred from AC's CMB account to an Iris LP account in Nevada. AC testified that he was

aware that his investment in Iris LP was not a CIS approved product and that it was a limited partnership that Womack managed on behalf of the limited partners.

A couple of months later, on March 22, 1999, AC opened a brokerage account at CIS with a broker other than Abbondante. On March 30, 1999, AC completed another wire transfer form in Abbondante's office for the purpose of making an additional investment in Iris LP, resulting in a second $25,000 wire transfer from AC's CMB account to Iris LP's account in Nevada. Prior to AC's decision to invest additional funds in Iris LP, AC spoke to CN, an Iris LP employee and alleged investor in Iris LP, who stated that her investment in Iris LP had done very well. AC made a subsequent contribution in the amount of $1,000 on May 17, 1999.

AC testified that he lost $19,400 of his $51,000 investment. He received $7,600 from Iris LP as a purported return on his investment and recovered $24,000 as a result of a settlement of a claim against CIS arising out of the collapse of Iris LP.

The second individual, KC, a relative of Abbondante's wife, was a CIS customer of Abbondante since June 1997. In February 1999, KC attended a birthday dinner in Manhattan for Abbondante's wife during which he overheard Abbondante talking to Daniel Pszanka ("Pszanka")[2] (a CIS registered representative who worked in a different CIS office than Abbondante), AC, and others about Iris LP. KC became interested in finding out more about Iris LP and asked Abbondante how the investment worked. Abbondante told KC that: (1) Iris LP invested money by trading stocks on the basis of a formula that relied on the volatility of the stocks that comprise the Dow Jones Industrial Average; (2) the formula had a history of doing very well in volatile markets; (3) he had learned from one investor that she had earned returns from Iris LP of a few hundred percent on her investment; (4) the minimum return on investment was 10 percent per month; and (5) Womack was a client of his; and (6) CMB had performed a background check on Womack. Abbondante also told KC that Iris LP was separate from his CIS business and was not a CIS product.

After advising Abbondante that he wanted to invest in Iris LP, on March 30, 1999, KC transferred $30,000 from his brokerage account to his CMB checking account. Abbondante then filled out a wire transfer form for KC that KC signed and returned, resulting in the transfer of $30,000 from KC's CMB account to Iris LP's account in Nevada. KC testified that his net loss on the investment was $12,840, after his receipt of $3,660 in purported returns on his investment and $13,500 from his settlement of a claim against CIS.

The third individual, RS, a high net worth individual, was a customer of Abbondante since 1995. RS had inherited wealth and was interested in generating income from his portfolio to meet his expenses because he was not employed. In late March 1999, RS and his friend, JW, met with Abbondante at Abbondante's CIS office. RS and JW testified that Abbondante solicited RS's investment in Iris LP by touting the limited partnership. Abbondante told RS that he had

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[2] The complaint in this matter also included allegations against Pszanka. Pszanka failed to file an answer to the complaint, and NASD issued a default decision against him.

invested in a successful trading formula through a "partnership" that made money whether the market went up or down. Abbondante also told RS that he had received monthly returns for a couple of months of six to seven percent per month from this investment. As a result, RS decided to invest $250,000 in Iris LP. Abbondante then had RS sign an authorization to transfer $250,000 from his personal bank account to the Iris LP bank account in Nevada. The transfer occurred on March 31, 1999. RS declared in an affidavit that he submitted for the record that he received only two checks totaling $5,975 from Iris LP, resulting in a loss on his investment of $244,025.

The record shows that after the CIS customers invested in Iris LP, Abbondante received a check in the amount of $51,500 from Iris LP, dated April 5, 1999. The check, which was made out to Abbondante, included a notation on its face that it was "for Referral." An Iris LP spreadsheet showed that Abbondante was credited with bringing in eight investor deposits (attributable to three CIS customers that Abbondante introduced to Iris LP and five CIS customers that Pszanka introduced to Iris LP) with deposits totaling $1,030,000, and that he earned a five-percent commission on those deposits that amounted to $51,500. Nonetheless, Abbondante denied that the check was a commission payment. He asserted, instead, that the check represented a "return on his investment" and that the word "Referral" that was written on the memo line of the check was merely a "bookkeeping entry" for tax purposes. The Hearing Panel did not find Abbondante's assertion to be credible.

C. Abbondante Establishes a Business Entity Not Affiliated with CIS

On May 12, 1999, Abbondante and Pszanka established DJIA LLC ("DJIA"), a Nevada limited liability company, to pursue various business ventures, including investment opportunities. DJIA was an acronym for "Dan [Pszanka] and Joe [Abbondante] Investment Account." In on-the-record interviews that Abbondante and Pszanka gave to staff of the Securities and Exchange Commission,[3] Abbondante and Pszanka testified that Womack deposited into the DJIA checking account the funds of seven CIS customers who had invested in Iris LP.[4] Womack made two separate deposits: one on June 7, 199, for $39,054, and the other on July 9, 1999, for $29,455.[5] Abbondante and Pszanka testified that these funds did not belong to DJIA and that Womack had deposited them without their prior knowledge or permission. Abbondante testified that when he asked Womack to reverse the deposits, Womack refused. According to Abbondante, Womack advised him that the individuals' deposits had to be held in

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[3] Abbondante and Pszanka gave on-the-record interviews to Commission staff with respect to the Commission's investigation of Womack's securities activities.

[4] The seven CIS customers were KC and RS, two CIS customers that Abbondante solicited to invest in Iris LP, and IS, GM, GL, SM, and JG, five CIS customers that Pszanka solicited to invest in Iris LP.

[5] Abbondante testified that Womack knew about the DJIA account because Abbondante had Womack deposit Abbondante's earnings from his investment in Iris LP directly to that account.

the DJIA account because he could not accept any additional funds into Iris LP until such time as he had other openings resulting from the redemption of interests by other limited partners. Womack nonetheless told Abbondante that he would provide him with investment and performance information relevant to the Iris LP investment as to each of these individuals and that Abbondante could make disbursements to them on that basis. Abbondante testified that he was concerned about Womack's decision to place CIS customer funds in the DJIA account that were intended for investment in Iris LP. Abbondante testified that he also was concerned about Womack's decision to abandon the formula that he had used to trade funds invested in Iris LP and to have Iris LP investors transfer their funds to a different investment vehicle that Womack called "Womack LLC."

Abbondante and Pszanka both testified in their on-the-record Commission interviews that, while confused about exactly what steps to take regarding the funds Womack had placed in the DJIA account, they ultimately decided to begin disbursing those funds in accordance with Womack's suggestion. The record shows that during June through August 1999, Abbondante and Pszanka disbursed $19,200 to four of their CIS customers ($6,460 to SM; $3,660 to KC; $5,975 to RS; and $3,105 to GM) based on information that Womack gave to Abbondante about those customers' "earnings." Abbondante and Pszanka also made disbursements of $16,250 to Pszanka and $6,020 to Abbondante's wife, in spite of the fact that neither of them had ever invested in Iris LP. Abbondante also disbursed $25,000 to himself.

D. Pszanka Sends Account Statements to CIS Customers

During the period from June through August 1999, Pszanka sent account statements to five CIS customers that he solicited to invest in Iris LP (customers IS, GM, GL, SM, and JG) and two CIS customers that Abbondante solicited to invest in Iris LP. The statements were on DJIA letterhead and purported to show investment information pertinent to their respective investments in Iris LP. Although Abbondante admits that he provided Pszanka with the investment information that Pszanka included in the account statements, he claims he was unaware when he gave the information to Pszanka that Pszanka would use it to prepare and send false customer account statements to the seven individuals whose funds Womack had placed in the DJIA account. Abbondante admitted that he and Pszanka had discussed the possibility of preparing account statements, but he claimed he had advised Pszanka that he was against the idea. Abbondante stated that his purpose in providing Pszanka with such information was only to enable Pszanka to respond to any inquiries from individuals about rates of return applicable to their investment in Iris LP.

III. Discussion

Abbondante does not dispute the facts that he made certain representations to CIS customers related to Iris LP and that those customers ultimately decided to invest in Iris LP. Abbondante argues, however, that these activities did not amount to participation in the transactions at issue. The facts do not support Abbondante's argument. As explained below, there is extensive evidence that Abbondante participated in the sale of interests in Iris LP to CIS customers AC, KC, and RS, for compensation, and that he failed to give his firm prior written notice and to obtain written approval from his firm. We therefore find that he engaged in private securities transactions without giving prior written notice to, and obtaining prior written approval

from, his firm, in violation NASD Conduct Rules 2110 and 3040. The evidence also supports our findings of violation that Abbondante: (1) engaged in material misrepresentations and omissions of material facts in connection with his touting of the Iris LP investment to CIS customers; (2) engaged in outside business activities through DJIA; and (3) assisted in the creation of false account statements.

A. Private Securities Transactions

NASD Conduct Rule 3040(a) provides that "[n]o person associated with a member shall participate in any manner in a private securities transaction except in accordance with the requirements of this Rule." An associated person who intends to participate in a securities transaction outside the regular course or scope of employment must give prior written notice to his or her employer describing the proposed transaction in detail and stating whether he or she may receive selling compensation. NASD Conduct Rule 3040(b). If selling compensation is to be received, the associated person may not engage in the transaction unless the employer gives its prior approval in writing. NASD Conduct Rule 3040(c). The record demonstrates that Abbondante did not provide CIS with prior written notice of his involvement with the sales of Iris LP interests to CIS customers and that he did not obtain prior written approval from CIS before engaging in these transactions.

As an initial matter, we concur with the Hearing Panel that the limited partnership interests in Iris LP are investment contracts and thus securities.[6] One way to determine if an interest in an investment vehicle is an investment contract is to analyze "whether [it] involves an investment of money in a common enterprise with profits to come solely from the efforts of others." SEC v. W.J. Howey Co., 328 U.S. 293, 301 (1946). We conclude that the Iris LP interests are investment contracts because they represent an investment in a common enterprise (Iris LP) with a reasonable expectation by the limited partners that profits would be produced by the trading efforts of others -- in this case by Womack.[7]

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[6] Section 3(a)(10) of the Exchange Act defines the term "security" to include "any . . . investment contract."

[7] Abbondante argued in the proceedings below that interests in Iris LP were not securities because they returned profits based on a number of investment components within the limited partnership, such as investments in real estate, fine art, and the stock market. We are not persuaded by this argument. As noted by the Commission in Joseph J. Vastano, Jr., Exchange Act Rel. No. 50219, 2004 SEC LEXIS 1806, at *17 (Aug. 19, 2004) (quoting SEC v. Edwards, 540 U.S. 389, 394 (2004) (citations omitted)), the U.S. Supreme Court has affirmed that an "investment contract" under Howey is a contract or scheme for "the placing of capital or laying out of money in a way intended to secure income or profit from its employment." Here, investors sent funds to Iris LP with the expectation that they would participate in excellent earnings resulting from their investment in Iris LP and the use of their funds by Womack. Thus, the investors in Iris LP expected "profits" based on their investment in Iris LP. It is irrelevant whether Iris LP returned profits based on a single investment component or many different components.

Abbondante asserts that he did not "solicit" the customers who purchased interests in Iris LP and, therefore, was not required under NASD Conduct Rule 3040 to provide written notice to CIS of the investments made by CIS customers. This argument has no merit because NASD Conduct Rule 3040 prohibits an associated person from participating "in any manner" in a private securities transaction except in accordance with the requirements of the rule. See Keith L. Mohn, 54 S.E.C. 457, 463 (1999); see, also, Mark H. Love, Exchange Act Rel. No. 49248, 2004 SEC LEXIS 318, at *10 (Feb. 13, 2004) (finding a violation of NASD Conduct Rule 3040 where the respondent recommended the investment to customers and facilitated the transfer of customers' funds from their brokerage accounts to the recommended investment vehicle); Stephen J. Gluckman, 54 S.E.C. 175, 183 (1999) (finding that "an associated person who introduces clients to an investment and later receives a finder's or referral fee participated in the transaction [under] Rule 3040").

Moreover, the evidence demonstrates that Abbondante participated in the sales of Iris LP interests to AC, KC, and RS by soliciting and facilitating their investments. Abbondante admitted in his on-the-record interview before the Commission that he "brought in" investors to Iris LP. Indeed, none of the three CIS customers to whom Abbondante spoke about Iris LP had any knowledge about the investment prior to their discussions with Abbondante. In addition, Abbondante made representations to the CIS customers about Iris LP that were designed to persuade them to invest in Iris LP. The evidence also shows that Abbondante facilitated the investments of all three CIS customers in Iris LP by assisting them with the mechanics of transferring their funds to Iris LP.

Abbondante also asserts that the $51,500 check that he received from Womack does not constitute selling compensation for purposes of NASD Conduct Rule 3040. We disagree. Abbondante testified that Womack merely included the notation "for Referral" as a bookkeeping entry for tax purposes. This self-serving testimony, however, is contrary to a preponderance of the evidence and was rejected as not credible by the Hearing Panel. We find no reason to disturb the Hearing Panel's credibility determination. Dane S. Faber, Exchange Act Rel. No. 49216, 2004 SEC LEXIS 277, at *17-18 (Feb. 10, 2004). The spreadsheet that the FBI seized from Iris LP in the course of its investigation includes a column entitled "Commissions," with a notation immediately to the left of the column showing that Abbondante earned a "5%" commission on deposits of $1,030,000, totaling $51,500. Hence, the $51,500 commission figure listed on the spreadsheet is identical to the amount listed on the check that Abbondante received from Womack.

We conclude that the check for $51,500 that Abbondante received from Womack was unmistakably a referral fee that falls within the meaning of "selling compensation" under NASD Conduct Rule 3040(e)(2). Given that Abbondante received selling compensation related to his participation in the sales of interests in Iris LP to CIS customers, he was required pursuant to NASD Conduct Rule 3040(c) to obtain prior written approval from CIS to participate in the Iris LP sales transactions. Abbondante failed, however, to obtain such written approval.

We find that Abbondante violated NASD Conduct Rules 2110 and 3040, as alleged,[8] based on evidence establishing that Abbondante participated in the sales of Iris LP interests without providing prior written notice to CIS and that he received "selling compensation" without obtaining written approval before engaging in sales of interests in Iris LP. We therefore affirm the Hearing Panel's finding of violations for this cause.

B. Fraudulent Misrepresentations and Omissions

Section 10(b) of the Exchange Act forbids any person from "us[ing] or employ[ing], in connection with the purchase or sale of any security . . . , any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe." SEC Rule 10b-5 makes it unlawful to "make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading." NASD Conduct Rule 2120 has requirements similar to Section 10(b) of the Exchange Act.[9]

A violation of Exchange Act Section 10(b), SEC Rule 10b-5 and NASD Conduct Rule 2120 requires a showing that: (1) the misrepresentations or omissions were made in connection with the purchase or sale of a security;[10] (2) the misrepresentations or omissions were material; and (3) the misrepresentations or omissions were made with scienter. SEC v. First Jersey Secs., Inc., 101 F.3d 1450, 1467 (2d Cir. 1996).

1. Materiality

A fact is material if there is a substantial likelihood that a reasonable investor would view the fact as significantly altering the total mix of information available. See In re Time Warner, Inc. Secs. Litig., 9 F.3d 259, 267-68 (2d Cir. 1993); see also Basic, Inc. v. Levinson, 485 U.S. 224, 240 (1988).

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[8] NASD Conduct Rule 2110 requires NASD members and associated persons to observe high standards of commercial honor and just and equitable principles of trade. Our determination that Abbondante violated Rule 2110 is in accord with the Commission's policy that a violation of another NASD rule also constitutes a violation of Rule 2110. See Chris Dinh Hartley, Exchange Act Rel. No. 50031, 2004 SEC LEXIS 1507, at *9 (July 16, 2004).

[9] NASD Conduct Rule 2120 provides that "[n]o member shall effect any transaction in, or induce the purchase or sale of, any security by means of any manipulative, deceptive, or other fraudulent device or contrivance."

[10] The evidence establishes that Abbondante made representations that resulted in the purchases by CIS customers of interests in Iris LP. See SEC v. Hasho, 784 F. Supp. 1059, 1106 (S.D.N.Y. 1992). Moreover, Abbondante does not deny that he discussed Iris LP with CIS customers AC, KC, and RS and that they subsequently purchased interests in Iris LP.

We find Abbondante's misrepresentations and his failure to disclose certain information to CIS customers AC, KC, and RS to be material.[11] "Materiality depends on the significance the reasonable investor would place on the withheld or misrepresented information." SEC v. Hasho, 784 F. Supp. at 1108. Abbondante told AC that it was possible to make better than average returns in a volatile market based on Womack's purported trading formula and that Womack's trading strategy was yielding investment returns of eight to 10 percent per month. Abbondante made similar representations to KC, telling him: (1) that Womack invested in Dow Jones Industrial stocks for an investment fund based on a mathematical program that produced returns averaging over 10 percent per month and that the minimum payout to investors was 10 percent per month; (2) that if KC invested in the investment fund, investment returns of 10 percent per month should not be a problem; and (3) that one investor already had earned returns of a few hundred percent on her investment. Abbondante also advised RS about Iris LP's past performance, stating that Iris LP used a trading formula that generated an average return of six to seven percent per month. Additionally, Abbondante testified that he advised KC that "investors" had told him that the investment had produced returns of 200 to 300 percent in a "very short period of time."

We conclude that these representations were materially false and misleading given that Abbondante knew of no verifiable facts that would support such optimistic statements regarding the profitability and likely success of the investment. See Hanly v. SEC, 415 F.2d 589, 595 (2d Cir. 1969) (upholding the Commission's finding that affirmative falsehoods and recommendations made without disclosure of known or reasonably ascertainable adverse information were fraudulent). "A securities dealer occupies a special relationship to a buyer of securities in that by his position he implicitly represents he has an adequate basis for the opinions he renders." Id. The facts show that Abbondante had no basis for the optimistic representations that he made concerning Iris LP.

Additionally, Abbondante failed to disclose to AC, KC, and RS that he had firsthand knowledge, as the registered representative handling Womack's trading accounts, that Womack's investments were producing losses. This omission of material fact would be important to a reasonable investor in light of Abbondante's excessively optimistic statements about Iris LP's prospects.[12] See Hanly, 415 F.2d at 595.[13]

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[11] In his brief on appeal, Abbondante argues, citing decisions in private Rule 10b-5 actions, that he cannot be held liable for any representations that he made because "[a]n investor may not justifiably rely on a misrepresentations [sic] if, through minimal diligence, he should have discovered the truth." This argument is misplaced. As compared to a plaintiff in a private action for damages, it is not necessary to prove investor reliance to establish a violation of the antifraud rules in an NASD disciplinary proceeding. See Jay Houston Meadows, 52 S.E.C. 778, 786 (1996).

[12] We thus reverse the Hearing Panel's findings that Abbondante did not omit material facts in making representations to CIS customers concerning Iris LP.

[13] Abbondante claims that his representations were not actionable because they amounted to "mere sales puffing." This argument has no merit. The Commission has not embraced the

[Footnote continued on next page]

2. Scienter

Scienter is defined as "a mental state embracing intent to deceive, manipulate, or defraud." Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 (1976). Scienter may be shown through reckless conduct. See Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1569 (9th Cir. 1990) (en banc); Dirks v. SEC, 681 F.2d 824 (D.C. Cir. 1982), rev'd on other grounds, 463 U.S. 646 (1983); Coastline Fin., Inc., Exchange Act Rel. No. 41989, 1999 SEC LEXIS 2124 (Oct. 7, 1999). Numerous courts have found that recklessness satisfies the scienter requirement of SEC Rule 10b-5.[14]

Reckless conduct has been defined as a highly unreasonable misrepresentation or omission, "involving not merely simple, or even inexcusable 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 defendant or is so obvious that the actor must have been aware of it." Hollinger, 914 F.2d at 1569. Further, "the danger of misleading buyers must be actually known or so obvious that any reasonable man would be legally bound as knowing." Id. at 1569-71 (citations omitted).

The Hearing Panel found that Abbondante's actions were merely negligent and that he therefore did not act with scienter.[15] We disagree and find that Abbondante's omissions and

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"puffery" defense. John R. Brick, 46 S.E.C. 43, 52 (1975) (finding that the concept of "puffing" has no place in these [anti-fraud] consumer protection statutes). In any event, a number of the representations that Abbondante made to customers were fact-based representations rather than opinions.

[14] Although some courts use the term severe recklessness, not recklessness, the distinction is not relevant. As the United States Court of Appeals for the Eleventh Circuit stated, "[a]lthough the [Fifth Circuit] used the modifier 'severe' in its characterization of what kind of reckless conduct can satisfy [the Rule] 10b-5 scienter requirement, its definition of severe recklessness is identical to that used by other courts to describe what conduct they considered reckless." Woods v. Barnett Bank, 765 F.2d 1004, 1011 n.9 (11th Cir. 1985).

[15] The Hearing Panel cited our decision in Ryan Mark Reynolds to conclude that Abbondante did not act with scienter. Dep't of Enforcement v. Reynolds, Complaint No. CAF990018, 2001 NASD Discip. LEXIS 17 (NAC June 25, 2001). There were a number of factors in that case, however, not present here, that led us to conclude that Reynolds acted with gross negligence rather than recklessness in making misrepresentations regarding the stock of a company. We found that Reynolds performed a basic investigation that included personally inspecting the company's main asset, holding discussions with some of the company's potential competitors, and reviewing a study and news articles about the company. We also found that Reynolds had limited experience in the industry and that he did not attempt to conceal his actions. Here, Abbondante, an experienced registered representative, failed to obtain any information about Womack and Iris LP from objective third parties or to take any significant

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misrepresentations with respect to Iris LP were, at a minimum, extremely reckless. The record shows that Abbondante emphasized Iris LP's positive returns while he failed to disclose to AC, KC, and RS that he knew Womack had consistently incurred losses in his trading accounts at CIS. Further, Abbondante admitted that he did not read the Iris LP prospectus because it did not make sense to him and that he never asked for or reviewed any financial or performance information related to Iris LP. Rather, he relied on unsubstantiated testimonials about the success of Iris LP from employees of Iris LP and on Womack's representations that he made profits in volatile markets. As the Commission previously has stated, "a salesman cannot deliberately ignore that which he has a duty to know and recklessly state facts about matters of which he is ignorant." Nassar & Co., 47 S.E.C. 20, 22 (1978). Under the circumstances here, including the fact that Abbondante did not fulfill his duty as a salesman to make an adequate investigation of Womack and Iris LP to ensure that Abbondante's representations to customers had a reasonable basis, we find that Abbondante acted at least recklessly and thus had scienter. See Dane S. Faber, 2004 SEC LEXIS 277, at *20.

Accordingly, we find that Abbondante violated Section 10(b) of the Exchange Act, SEC Rule 10b-5, and NASD Conduct Rules 2110 and 2120.

C. Outside Business Activities

NASD Conduct Rule 3030 provides that persons associated with a member in any registered capacity shall not be employed by, or accept compensation from, any other person as a result of any business activity, other than a passive investment, outside the scope of his or her relationship with the employer firm, unless prompt written notice to the member has been provided. The evidence establishes that Abbondante violated NASD Conduct Rule 3030 by failing to report his involvement in DJIA.

The evidence establishes that Abbondante engaged in outside business activities by forming DJIA, receiving and disbursing Iris LP funds through DJIA, and assisting in the creation of false Iris LP account statements that were issued on DJIA letterhead. Moreover, Abbondante, his wife, and Pszanka received payments from the DJIA checking account subsequent to Womack's deposit of Iris LP customer funds in that account. Contrary to Abbondante's contention, all of these activities created an obligation on Abbondante to notify his firm of his involvement with DJIA.

Abbondante contends that the fact that he and Pszanka formed DJIA to conduct business in the future did not create an obligation for him to notify his employer of an outside business activity. We reject this argument. Disclosure of outside business activities is required when a registered representative takes steps to commence a business activity unrelated to his relationship with his firm. See Micah C. Douglas, 52 S.E.C. 1055, 1058-59 (1996) (finding that completion

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[cont'd]
steps to corroborate the veracity of the claims of Womack or others who were associated with him about Iris LP's professed success. Furthermore, Abbondante knew and withheld from potential investors the extent of Womack's personal trading losses.

of a questionnaire in an effort to solicit business within a state constitutes an outside business activity in violation of NASD Conduct Rule 2110).

We affirm the Hearing Panel's finding that Abbondante engaged in an outside business activity without providing prompt written notice to CIS, in violation of NASD Conduct Rules 2110 and 3030.

D. False Account Statements

The complaint also alleges that Abbondante facilitated Pszanka's provision of false account statements to seven CIS customers, in violation of NASD Conduct Rule 2110. Account statements are critically important documents, and the creation of false statements "is the antithesis of a registered representative's [duty to uphold] high standards of commercial honor." Dist. Bus. Conduct Comm. v. Mangan, Complaint No. C10960162, 1998 NASD Discip. LEXIS 33, at *16 (NAC July 29, 1998).

Abbondante contends that he cannot be held liable for assisting Pszanka in the preparation of account statements that included false information because he merely supplied Pszanka with the investment information to enable Pszanka to provide Iris LP investors who also were CIS customers with information about the performance of their investment if they called to inquire about it. Abbondante further claimed that he did not know what Pszanka was planning to do with the investment information that he gave to him with respect to the seven individuals whose funds Womack deposited in the DJIA account. This claim is undermined, however, by Abbondante's on-the-record testimony in which he admitted that Pszanka had advised him that he would be sending account statements to his own customers.

The evidence shows that Abbondante entered into a factual stipulation prior to the hearing below in which he admitted that there was no evidence that Iris LP generated the average returns indicated in the investment summary portion of the statements that Pszanka issued to the seven customers.[16] The record also amply demonstrates that Abbondante should have known that the performance information that he received from Womack had no basis in fact and that the account statements at issue therefore included false information. Abbondante knew that a portion of the funds that CIS customers had invested in Iris LP had not been invested in Iris LP. Womack instead had placed those funds in the DJIA account. Therefore, Abbondante should have been aware of the falsity of any purported performance information that Womack gave to him regarding the CIS customers' investments in Iris LP.[17] Moreover, Abbondante admitted in his on-the-record testimony before the Commission that he had become extremely concerned when Womack deposited Iris LP customer funds into the DJIA account. Abbondante's concerns

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[16] The seven CIS customers were KC and RS (the two CIS customers that Abbondante solicited) and IS, GM, GL, SM, and JG (the five CIS customers that Pszanka solicited).

[17] The Hearing Panel concluded that Abbondante had no way of knowing that the investment information that Womack gave to him was false. We do not agree with the Hearing Panel's finding in light of the cited evidence.

were heightened when Womack stated that he was abandoning his formula that he had used to trade funds in Iris LP and that he therefore wanted the Iris LP investors to deposit their funds instead in his Womack LLC investment vehicle so that he could implement a new trading strategy in Womack LLC that would give him higher returns. Finally, the evidence establishes that the account statements were false on their face. The account statements were sent on "DJIA" letterhead and included investor "[p]ositions] in DJIA," even though, as admitted by Abbondante, the investment information in the statements was not based on any investment in DJIA.

Furthermore, a preponderance of the evidence shows that Abbondante facilitated Pszanka's preparation of false account statements. It is undisputed that Abbondante gave Pszanka all of the investment information that Pszanka included in the account statements that Pszanka sent to the seven CIS customers whose funds Womack had placed in the DJIA account. Additionally, we conclude that the level of detail that Abbondante supplied to Pszanka with respect to each of the seven individual's investments, and which Pszanka included in the account statements, is consistent with the type of information routinely included in such statements.[18] Moreover, the fact that Abbondante supplied Pszanka with such detailed information undermines Abbondante's claim that he only gave Pszanka this information because Pszanka needed to be able to provide his own customers[19] with information about their rates of return. This claim makes no sense given that, in addition to supplying Pszanka with detailed information about Pzsanka's accounts, Abbondante also provided the same level of detail about the CIS customers that he had solicited to invest in Iris LP. We note that, presumably, Abbondante, not Pszanka, would have responded to any inquiries from those individuals that he had solicited, two of which were his own customers.[20]

Additionally, when asked in his on-the-record testimony before the Commission about why an account statement had been sent to customer IS even though she had not received a disbursement from the DJIA account, Abbondante responded that he and Pszanka had decided that they just had to be "very consistent" with respect to sending out account statements. We conclude from this testimony that Abbondante and Pszanka had decided, as a matter of consistency, that they needed to send account statements to all seven individuals whether or not they also had received a disbursement from the DJIA account. As noted above, the evidence shows that four of the seven individuals received disbursements from the DJIA account.

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[18] Abbondante gave Pszanka the purported earnings, cash positions, and average percentage return for each customer.

[19] On March 29, 30, and 31, 1999, five of Pszanka's CIS customers (IS, GM, GL, SM, and JG) invested a total of $725,000 in Iris LP.

[20] KC and RS were CIS customers of Abbondante. AC became a CIS customer after he made his first investment in Iris LP; however, the evidence shows that he opened an account with a CIS registered representative other than Abbondante.

We therefore find that Abbondante knowingly facilitated Pszanka's provision of false account statements to seven CIS customers, as alleged, in violation of NASD Conduct Rule 2110.

IV. Sanctions

After careful consideration of the facts and circumstances presented by this matter, we conclude that Abbondante's misconduct, which includes our finding that Abbondante acted recklessly, is egregious and order that he be barred in all capacities to protect the investing public.[21] We also order Abbondante to pay restitution to customers AC, KC, and RS, plus interest from the date of investment, as follows: $19,400 to customer AC for his purchase of interests in Iris LP on March 30, 1999;[22] $12,840 to customer KC for his purchase of interests in Iris LP on March 30, 1999; and $244,025 to customer RS for his purchase of interests in Iris LP on March 31, 1999.[23] In imposing sanctions on Abbondante, we have consulted the Guidelines for guidance in determining the appropriate level of sanctions. Applying the Guidelines to the facts relevant to each violation, we have identified a significant number of aggravating factors, as discussed below.[24]

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[21] The applicable NASD Sanction Guideline ("Guideline") for each violation, with the exception of the Guideline for private securities transactions violations, recommends a bar in egregious cases. Although the Guideline for private securities transactions violations suggests a bar when the dollar amount of the sales exceeds $1 million, it also states that "[t]he presence of one or more mitigating or aggravating factors may either raise or lower the sanctions." We conclude that the aggravating factors, as further discussed herein, applicable to Abbondante's NASD Conduct Rule 3040 violation require the sanction of a bar. Additionally, we find that Abbondante's conduct was egregious as applicable to his other violations. Thus, the sanction of a bar is consistent with the relevant Guidelines. In light of our policy determination that, in certain cases involving the imposition of a bar, no further remedial purpose is served by the additional imposition of a monetary sanction, we do not impose a fine for Abbondante's violations. See Guidelines (2001 ed.) at 13-14 (Technical Matters). Additionally, based on our decision to bar Abbondante, we eliminate the Hearing Panel's sanctions of a fine of $96,500, a suspension in all capacities for one year, and an order to requalify by examination as a general securities representative.

[22] Customer AC invested $25,000 on December 31, 1998, and another $25,000 on March 30, 1999. For purposes of calculating interest, we have used the later date.

[23] The Guidelines recommend that we consider ordering restitution where appropriate to remediate misconduct. See Guidelines (2001 ed.) at 6 (General Principles Applicable to All Sanction Determinations, No. 5). We find that the facts of this case support our decision to order restitution because the losses are quantifiable and attributable to Abbondante's violations. Id. The Hearing Panel erred in not ordering restitution.

[24] We reject Abbondante's argument that he was a victim of Womack's fraudulent scheme. The record shows that Abbondante made money on Iris LP purchases that he recommended to CIS customers who followed his recommendations and invested in Iris LP. An abundance of

[Footnote continued on next page]

Turning first to Abbondante's material misrepresentations and omission, we note that Abbondante's activity caused three CIS customers to invest in an unapproved product that was a Ponzi scheme. The Guidelines instruct us to consider: (1) whether the respondent's conduct resulted directly or indirectly in injury to other parties and the extent of that injury; and (2) whether the respondent's misconduct was reckless.[25] The facts establish that Abbondante's actions were directly responsible for the losses that the CIS customers incurred through their investments in Iris LP because they would not have known about the investment but for their conversations with Abbondante. Moreover, the extremely positive statements that Abbondante made to CIS customers concerning Iris LP's prospects and the fact that he omitted a material fact from his presentation constituted reckless activity and thus was fraudulent. Additionally, Abbondante's misconduct exposed CIS to litigation by the Iris LP investors, resulting in CIS having to pay customers AC and KC $24,000 and $13,500, respectively, for losses they incurred from their investment in Iris LP. Abbondante's activities directly thwarted the purpose of NASD Conduct Rule 3040. As the Commission has noted, "Rule 3040 is designed not only to protect investors from unmonitored sales, but also to protect securities firms from exposure to loss and litigation in connection with sales made by persons associated with them." Jim Newcomb, Exchange Act Rel. No. 44945, 2001 SEC LEXIS 2172, at *19 (Oct. 18, 2001). We conclude that these activities are evidence of egregious misconduct.

As to the NASD Conduct Rule 3040 violation,[26] we have applied the principal considerations from the Guideline for private securities transactions to the facts of this case and found a number of aggravating circumstances relevant to Abbondante's misconduct.[27] We note that Abbondante's activity resulted in the sale of interests in Iris LP of $330,000 to three customers of his firm and that he made the sales over a three-month period. Abbondante significantly assisted in transferring their funds to Iris LP. We have further considered that the CIS customers that Abbondante introduced to Iris LP sustained losses on their investments in Iris LP as follows: (1) AC lost $19,400 out of his $51,000 investment; (2) KC lost $12,840 out of his $30,000 investment; and (3) RS lost $244,025 out of his $250,000 investment.

Moreover, Abbondante created the appearance that CIS sanctioned his activity by using CIS facilities to introduce and explain to RS the Iris LP investment, to introduce AC to an Iris LP

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evidence establishes that Abbondante played a critical role in causing the CIS customers to invest in Iris LP. In our view, Abbondante was not a victim of Womack. Rather, he participated whole-heartedly in the fraud.

[25] See Guidelines (2001 ed.) at 10 (Principal Considerations in Determining Sanctions, No. 11).

[26] Abbondante asserts that CIS customers knew that Iris LP was not a CIS-approved product. We reject Abbondante's argument that this serves as a mitigating factor.

[27] See Notice to Members 03-65 (NASD Revises NASD Sanction Guidelines) (Oct. 2003).

employee, and to assist AC, KC, and RS with wiring funds from their accounts to an Iris LP account. We also note that Abbondante obtained a financial benefit from his misconduct in the form of a $51,500 referral commission and additional payments to himself and his wife and that he did not inform his firm about any of these payments.[28]

With respect to our finding that Abbondante engaged in outside business activities, we have reviewed the principal considerations listed in the Guideline for that violation[29] and consider the following facts to be aggravating: (1) CIS customer funds were held in the DJIA checking account, and disbursements of funds to CIS customers were made from the same DJIA account;[30] (2) false account statements were sent to CIS customers on DJIA letterhead that purported to give customers information about their earnings with respect to investments they made in Iris LP; and (3) Abbondante attempted to actively conceal from his superiors the fact that he was engaged in an outside business activity. He testified that he did not advise anyone at CIS that customer funds had been deposited in his DJIA account because: "It would open up a whole can of worms. . . . I would have to explain [why I had] bank customers' money . . . in my own account . . . ." We also have considered that Abbondante disbursed funds from the DJIA account to Pszanka and Abbondante's wife, neither of whom had invested in Iris LP. Abbondante also exhibited a lack of candor with respect to his denials that the $51,500 check that he received from Womack that was deposited in his DJIA checking account was a commission check when the evidence plainly establishes that it was a commission payment for CIS customers that he and Pszanka referred to Iris LP. In light of these aggravating factors, we consider Abbondante's conduct to be egregious.[31]

Turning finally to the false account statements violation, we conclude that the nature of the false documents that Abbondante assisted in preparing -- false customer account

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[28] See Guidelines (2001 ed.) at 10 (Principal Considerations in Determining Sanctions, No. 17). Abbondante received $4,067 from Iris LP as alleged investment returns. He also disbursed $25,000 to himself and $6,020 to his wife from the Iris LP funds that Womack had placed in the DJIA account.

[29] See Guidelines (2001 ed.) at 18 (Outside Business Activities -- Failure to Comply with Rule Requirements).

[30] We conclude that Abbondante's decision to disburse funds to CIS customers from the DJIA account and his failure to notify his firm or authorities of Womack's placement of funds in his DJIA account are evidence of his desire to keep his outside business activities concealed from the firm. We therefore reject Abbondante's argument on appeal that he "was attempting to do the right thing with monies [that] did not belong to him."

[31] The Guideline for outside business activities states that "in egregious cases, including those involving a substantial volume of activity or significant injury to customers of the firm, consider a longer suspension or a bar." We conclude that the totality of the circumstances related to Abbondante's outside business activities requires a finding of egregious misconduct.

statements -- is extremely aggravating. The fact that customers received statements purportedly showing their Iris LP investment activity permitted Womack to continue to perpetrate his fraudulent scheme by falsely representing to the CIS customers that their funds were in a legitimate investment vehicle. The record demonstrates that Abbondante should have been aware of the unreliability of any investment figures that Womack gave to him. Yet Abbondante accepted Womack's figures as to the purported investment information without question and relayed those figures to Pszanka despite knowing that Pszanka was planning on sending account statements to his customers. These facts lead us to conclude that Abbondante's conduct with respect to the false account statements violation is egregious.

We conclude that the extent of Abbondante's violations demonstrates Abbondante's complete lack of understanding of his duties as a registered person. Accordingly, based on all of the foregoing facts and circumstances and the lack of any mitigating circumstances, we find that Abbondante's misconduct is egregious and that it thus warrants a bar in all capacities.

V. Conclusion

We find that Abbondante: (1) violated NASD Conduct Rules 2110 and 2120, Section 10(b) of the Exchange Act, and SEC Rule 10b-5 by making material misrepresentations and by omitting a material fact; (2) violated NASD Conduct Rules 2110 and 3040 by engaging in private securities transactions without providing the requisite prior written notice and obtaining prior written approval; (3) violated NASD Conduct Rules 2110 and 3030 by engaging in outside business activities without providing the necessary prompt written notice; and (4) violated NASD Conduct Rule 2110 by assisting Pszanka with his preparation of false account statements.[32] For each of these violations, we bar Abbondante from associating with any NASD member firm in any capacity. The bar will be effective as of the date of this decision. We also order restitution to the customers in the total amount of $276,265, plus interest from the date of investment.[33] Abbondante is also assessed costs of $6,990.09, consisting of $5,415.82 in hearing

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[32] We also have considered and reject without discussion all other arguments advanced by the parties.

[33] The amount of restitution to be paid to each customer is as follows: $19,400 (AC); $12,840 (KC); and $244,025 (RS). In the event that these individuals cannot be located, unpaid restitution should be paid to the appropriate escheat, unclaimed-property, or abandoned-property fund. Interest on the restitution amount will be paid at the rate established in Section 6621(a) of the Internal Revenue Code, 26 U.S.C. 6621(a).

costs and $1,574.27 in appeal hearing costs ($1,000 in appeal hearing costs and $574.27 in appeal transcript costs).

On Behalf of the National Adjudicatory Council,

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Barbara Z. Sweeney
Senior Vice President and Corporate Secretary