NASD REGULATION, INC.
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. VTR CAPITAL, INC. (BD #21404) New York, New York, EDWARD J. McCUNE (CRD #1316826) Juno Beach, Florida, HOWARD R. PERLES (CRD #1174341) Staten Island, New York, and LAURENCE M. GELLER (CRD #1533947) Demarest, New Jersey, Respondents.	Disciplinary Proceeding No. CAF980005 Hearing Officer—Andrew H. Perkins **Panel Decision** August 18, 1999

Digest

Howard R. Perles and Laurence M. Geller were charged with the following violations: (1) aiding and abetting an unregistered distribution of common stock; (2) aiding and abetting a manipulation of the market for the stock through wash and matched trading; and (3) failing to

maintain accurate books and records of the wash and matched trading. The Extended Hearing Panel (the "Hearing Panel") found that Mr. Perles and Mr. Geller violated NASD Rule 2110 by engaging in prearranged (or wash and matched) trading and Section 17(a) of the Exchange Act, Rule 17a-3 thereunder, and NASD Conduct Rules 2110 and 3110 by failing to accurately reflect those prearranged trades on the books and records of their respective firms. The Hearing Panel dismissed the remaining charges.

The Hearing Panel fined Howard R. Perles $25,000, suspended him for one year from associating with any member firm in any capacity, and ordered that he requalify as a General Securities Representative by taking the Series 7 Examination. The Hearing Panel fined Laurence M. Geller $25,000 and suspended him for 30 business days from associating with any member firm in any capacity. The Hearing Panel also ordered that the Respondents pay the costs of this proceeding.

Appearances

Jeffrey K. Stith and Rory C. Flynn, Washington, DC, counsel for the Department of Enforcement.

Marc B. Dorfman of Freedman, Levy, Kroll & Simonds, Washington, DC, counsel for Howard R. Perles.

Jeffrey S. Rosen of DeMartino, Finkelstein, Rosen & Virga, Washington, DC, counsel for Laurence M. Geller.

DECISION

I. Introduction And Procedural Background

The Department of Enforcement (Enforcement) filed a seven-cause Complaint in this disciplinary proceeding on February 20, 1998. The first five causes charged VTR Capital, Inc. ("VTR") and its President, Edward J. McCune, with participating in the unregistered distribution of 300,000 unregistered shares of Class A Common Stock issued by Interiors, Inc. ("Interiors Stock"), purchasing the Interiors Stock during the distribution, failure to comply with corporate financing requirements and receipt of unreasonable underwriting compensation, fraud in the sale of Interiors Stock, and violation of VTR's restriction agreement. VTR and Mr. McCune settled these charges;[1] therefore, this Decision only addresses the remaining allegations against Howard R. Perles and Laurence M. Geller in Causes Six and Seven.

The Complaint alleges in Cause Six that Mr. Perles and Mr. Geller violated NASD Conduct Rules 2110 and 2120, and Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act"), 15 U.S.C. § 78(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5, by aiding and abetting VTR and Mr. McCune in a scheme to unlawfully distribute 300,000 unregistered shares of Interiors Stock and to fraudulently manipulate the market in the stock through a series of prearranged, circular trades called "wash" and "matched" trades.[2] Cause Six further alleges that the wash and matched trades among VTR, Mr. Perles, and Mr. Geller served

[1] Order of Acceptance of Settlement by Respondents VTR and Edward McCune, (Dec. 11, 1998).

[2] Compl. ¶¶ 43-44. "A matched order is the entering of a sell (or buy) order knowing that a corresponding buy (or sell) order of substantially the same size, at substantially the same time and at substantially the same price either has been or will be entered. A wash trade is a securities transaction which involves no change in the beneficial ownership of the security." In re Edward Christian Farni, Exchange Act Release No. 39133, 1997 SEC LEXIS 2004, at *3 n.2 (Sept. 25, 1997).

no legitimate economic purpose and operated as a fraud upon both investors and the marketplace.[3] In addition—independent of any violation of the federal securities laws—Cause Six alleges that Mr. Perles and Mr. Geller violated NASD Conduct Rule 2110 by effecting these prearranged trades.[4]

Cause Seven alleges that Mr. Perles and Mr. Geller violated NASD Conduct Rules 2110 and 3110, and Section 17(a) of the Exchange Act, 15 U.S.C. § 78(q), and Rule 17a-3 thereunder by failing to maintain accurate books and records reflecting the alleged prearranged trading. More specifically, the Complaint and the Bill of Particulars filed on September 29, 1998, state that Mr. Perles and Mr. Geller failed to record the oral repurchase agreements underlying the prearranged trades of Interiors Stock and that they falsely recorded them as unrelated trades.

On June 9, 1998, Mr. Perles and Mr. Geller filed a joint motion for summary disposition. They challenged Enforcement's authority to charge persons with aiding and abetting violations of Section 10(b) of the Exchange Act, Rule 10b-5 promulgated thereunder, and NASD Conduct Rule 2120, and they challenged Enforcement's books and records charge on the ground that it "failed to state a claim upon which relief can be granted." The Hearing Panel treated the motion as a motion to dismiss because it attacked the legal sufficiency of the Complaint, not the sufficiency of the evidence. The Hearing Panel denied the motion as to the books and records charge and deferred ruling on the challenge to the Enforcement's aiding and abetting theory until the hearing.

[3] Id. ¶44.

[4] Id. ¶ 46.

A hearing was held in Washington, DC, on March 9 and 10, 1999, by an Extended Hearing Panel composed of the Hearing Officer, a former member of the Committee for District 10, and a former member of the Market Regulation Committee. Enforcement called one witness and introduced 14 exhibits. The Respondents called three witnesses, including themselves, and introduced 15 joint exhibits.[5]

At the conclusion of Enforcement's case-in-chief, the Respondents moved to dismiss the charges against them. Following argument, the Hearing Panel granted the motion with respect to the charge that Mr. Perles and Mr. Geller aided and abetted an unregistered distribution of Interiors Stock. The Hearing Panel found that there was no evidence, direct or circumstantial, showing that either Mr. Perles or Mr. Geller knew, or had a general awareness, that the distribution was unregistered.

Following the presentation of all evidence, the Respondents renewed their motion for summary disposition and moved that the remaining charges be dismissed. For the reasons set forth below, the Hearing Panel granted the motion for summary disposition as to the remaining aiding and abetting theory under Cause Six and denied the motion to dismiss the remaining charges.

II. Findings of Fact

A. Howard R. Perles

Mr. Perles has worked continuously in the securities industry since he joined M. Rimson & Co., Inc. in 1983. (Ex. C1, at 4.) He joined I.A. Rabinowitz & Co. (I.A. Rabinowitz) in 1991,

[5] References to the hearing transcript are cited as "Tr." Enforcement's exhibit references are "Ex. C[number]," and the Respondents' exhibit references are "Ex. R[number]." All transcript cites are to the transcript page numbers, not the exhibit page numbers.

which changed its name to IAR Securities in 1997 and, in 1998, merged with VTR, now known as Fairchild Financial Group, Inc. (Tr. 343.) Mr. Perles is currently associated with Fairchild. (Id.)

Mr. Perles is currently registered as a General Securities Principal, but during the period relevant to this proceeding, April 19-22, 1995, he was registered only as a General Securities Representative. (Tr. 348.) Mr. Perles described his job responsibilities at that time as having two prongs. The first prong was to execute and report all orders from I.A. Rabinowitz's branches. (Tr. 349-50.) The second prong was to maintain the markets in up to 50 securities in which I.A. Rabinowitz made markets. (Tr. 351.) Mr. Perles reported to and was supervised by Mr. Isaac Rabinowitz, who reviewed the firm's trading on a daily basis. (Tr. 349.) Although I.A. Rabinowitz was a market maker, Mr. Perles testified that this was not the firm's primary focus. According to him, the main thrust of the firm's activities was retail sales. To a large measure, its market making activity was limited to stocks in which it had participated in the underwriting and for which it enjoyed a retail following. (Tr. 357.) The other stocks in which I.A. Rabinowitz made a market were those selected personally by Mr. Rabinowitz. (Tr. 358.)

Mr. Perles declined to describe himself as a trader because his authority in the trading room was limited to maintaining an orderly market. Describing his trading authority, Mr. Perles testified: "I was there to buy the stock if we had buyers. I was there to sell the stock if we had sellers." (Tr. 356.) While he was not specific, he testified that "traders" usually possessed other responsibilities, and at his firm those rested with Mr. Rabinowitz. (Tr. 356.)

In April 1995, I.A. Rabinowitz's trading room was not automated. Mr. Perles and his assistant took all orders by telephone and entered them by hand. (Tr. 353-54.) The only computer

or electronic terminal they had was a NASDAQ Workstation with Level 3 Service, which they used to update quotes and access the ACT system.[6] (Tr. 354.)

Mr. Perles was a salaried employee at I.A. Rabinowitz. (Tr. 346.) He did not receive commissions or significant bonuses. His tax return and W-2 form show that in 1995 he earned $35,100. (Ex. R9.) His income from other sources was less than $1,000.

Mr. Perles has been disciplined on three occasions. First, in 1990, he settled charges brought by the Alabama Securities Commission that he had sold securities that were not registered in Alabama. (Ex. C1, at 9-10.) Second, in 1992, Mr. Perles settled a complaint brought by the Market Surveillance Committee of the NASD, which alleged that Mr. Perles had assisted in an unregistered distribution of stock. (Ex. C1, at 7.) Under the terms of the settlement, Mr. Perles was fined $5,000 and suspended for five business days from associating with any NASD member in any capacity. (Ex. C1, at 9.) Third, in 1995, Mr. Perles settled an administrative proceeding brought by the SEC, which charged him with violating Sections 5(a) and 5(c) of the Securities Act of 1933 by facilitating sales of unregistered stock. (Ex. C1, at 5.) Under the terms of the settlement, he was suspended for three months and ordered to cease and desist from further violations.

B. Laurence M. Geller

Mr. Geller entered the securities industry in 1987 when he joined Prestige Investors. (Tr. 250-51.) When that firm went out of business he moved to Vanderbuilt Securities, Inc. where he worked until July 1990. Thereafter, he joined Wien Securities Corp. as a trader. (Tr. 250-52.) Mr.

[6] The Automated Confirmation Transaction Service or ACT system is an automated Nasdaq service for price and volume reporting, comparison, and clearing of pre-negotiated trades completed in Nasdaq and the OTC Bulletin Board Service.

Geller described Wien Securities as a wholesale trading firm. (Tr. 250.) At all times relevant to this proceeding, Mr. Geller was registered as a General Securities Representative. (Ex. C1, at 13.)

In 1995, Mr. Geller was one of 20-25 traders at Wien Securities who traded for the firm's trading account. His particular trading area was NASDAQ, bulletin board, OTC, and pink sheet stocks. (Tr. 252.) He worked a list of approximately 200-300 stocks, of which 20-80 were active on any given day. (Tr. 253, 262.) At that time, most of the trading at Wien Securities was conducted by telephone. (Tr. 261.) Although he had SelectNet[7] available, it was not used much in 1995 for the stocks he traded. (Id.)

Mr. Geller had a fair amount of authority in trading the stocks on his approved list. Wien Securities set volume parameters but not price parameters on his trading. (Tr. 326-27.) Essentially, if he stayed under the volume limit and his trading was within the market, Mr. Geller was left alone. (Tr. 326-29.) Mr. Wien testified that to the best of his recollection the volume limit in 1995 was 25-50,000 shares. (Tr. 329.) If he exceeded the limit, the transaction would pop up on his managers' terminals, and one of the managers would then question Mr. Geller about the trade. In 1995, Mr. Geller traded approximately 156,000,000 shares of stock. (Tr. 306-07.)

Mr. Geller's compensation at Wien Securities was based on the profit he made for the firm. He received one-third of the profit minus charges such as ticket charges, correspondence charges, and SelectNet charges. (Tr. 267.) In 1995, he made between $250,000 and $300,000. (Tr. 274.)

[7] SelectNet is an automated Nasdaq service that enables securities firms to route orders, negotiate terms, and execute trades in Nasdaq securities over an electronic network.

Mr. Geller's disciplinary history shows that he was fined $1,500 and suspended for one day for failing to pay timely four arbitration awards totaling $5,007.

C. Unregistered Distribution of 300,000 Shares of Interiors Stock

1. Background

Interiors is a Delaware corporation engaged in manufacturing and marketing picture frames and a variety of decorative home accessories. (Ex. C4) Its principal offices are in Mt. Vernon, New York.

On June 30, 1994, Interiors issued an Initial Public Offering of its stock which was underwritten by J. Gregory & Company, Inc. (Ex. C3.) The registration statement for the initial offering covered 450,000 Class A shares of common stock, 400,000 Class WA warrants, and 225,000 Class WB warrants. On January 30, 1995, pursuant to the "Alternate A" prospectus, Interiors filed a shelf registration for a proposed additional offering of up to 500,000 shares of common stock. (Ex. C4.)

2. Distribution Of Interiors Stock

On April 18, 1995, Interiors entered into a Financial Consulting Agreement with VTR and McCune, which, among other things, called for VTR to arrange for the sale of 300,000 shares of Interiors' common stock at $0.93 per share within 24 hours of the date of the agreement. (Ex. C5, at ¶ 3.) The signing of the Financial Consulting Agreement triggered two related courses of events that resulted in an unregistered distribution of Interiors Stock. First, Interiors sold 300,000 shares of its stock to five investors. Second, VTR sold more than 300,000 shares of stock to its customers, created a short position in its inventory, and then covered its short position by acquiring the 300,000 shares Interiors had sold to the five investors. The

evidence reflects that this scheme was used by VTR to circumvent its restrictive agreement, which prohibited it from retail trading on a principal basis. (Ex. R13, at ¶ 1.)

Immediately after signing the Financial Consulting Agreement, Interiors sold 300,000 shares of its common stock at $0.93 per share to the following five investors: Hartley Bernstein, VTR's outside attorney; International Reserve Corp.; Ulster Investments; Lidco, Ltd.; and KAM Group, Inc. (collectively the "Short-Term Investors"). Several of these had ties to VTR and McCune. Ulster and Kam Group were customers of McCune, and International Reserve had an account at VTR. (Ex. C7, at 1.)

The Short-Term Investors held the stock they purchased from Interiors for less than eight days. Except for Bernstein, they delivered their shares to VTR on April 24, 1995. (Ex. C6, at 16.) Bernstein delivered his 20,000 shares to VTR two days later, on April 26, 1995. (Tr. 70.) Although the Short-Term Investors delivered their Interiors Stock to VTR on April 24 and 26, VTR did not pay them for the stock until later. VTR paid Bernstein $2.00 per share on May 4. VTR paid Ulster Investments, KAM Group, and International Reserve $0.95 per share on May 22. And VTR paid Lidco $0.95 per share on May 31. (Ex. C9, at 5, 7.)[8]

Also, immediately after VTR and Interiors entered into the Financial Consulting Agreement, VTR began an aggressive campaign to sell Interiors Stock. From April 19 to April 21, VTR sold its customers 366,700 shares of Interiors Stock, resulting in a short position of 337,749 shares at the close of trading on April 21, 1995. (Ex. C6, at 19.) VTR covered this short

[8] VTR also paid International Reserve another $2,100 on May 31, 1995, for which there is no explanation in the record. (Ex. C9, at 7.)

position in large part by acquiring the shares held by the Short-Term Investors on April 24 and 26.

Although VTR denied any involvement in the sale of Interiors Stock to the Short-Term Investors, the Hearing Panel finds that it was involved. Clearly VTR arranged for the Short-Term Investors to purchase the stock from Interiors so that VTR could sell the stock to VTR's retail customers. The Short-Term Investors acquired the stock with a view to distribution and were used by McCune and VTR to facilitate the distribution of 300,000 shares of Interiors Stock to the public.

The distribution of 300,000 shares of Interiors Stock in April 1995 was unregistered. The January 1995 registration statement Interiors filed did not cover the sale to the Short-Term Investors or the subsequent distribution of the 300,000 shares to the public. Moreover, the "Alternate A" prospectus for the shelf registration of an additional 500,000 shares states in the "Plan of Distribution" that an updated prospectus must be prepared and distributed at the time any of the subject shares are offered to the public. But the "Alternate A" Prospectus was not updated or amended for the April 1995 distribution. (Tr. 78-79.)

Neither Mr. Perles nor Mr. Geller was privy to any information regarding the distribution of Interiors Stock in April 1995. They did not know each other, and neither of them knew McCune or the trader at VTR, David Noble. (Tr. 150.) Nor did they know about VTR's Restriction Agreement or the Financial Consulting Agreement between VTR and Interiors. (Tr. 163-64, 167.) They also did not know, or have reason to know, that Interiors and VTR had made an unregistered distribution of 300,000 shares of Interiors Stock in April 1995. (Tr. 168.)

D. Trading Of Interiors' Stock

Between the date VTR entered into the Financial Consulting Agreement with Interiors and the date VTR acquired the 300,000 shares of Interiors Stock from the Short-Term Investors, VTR engaged in a series of prearranged trades with Mr. Perles at I.A. Rabinowitz and Mr. Geller at Wien Securities.

1. Trades By Perles

On April 19, 1995, Mr. Perles at I.A. Rabinowitz completed the following trades of Interiors Stock:[9]

	Time	**Seller**	**Buyer**	**Price**	**Shares**	**Rabinowitz's Inventory**
1	10:59	VTR	Rabinowitz	$1.50	10,000	10,000
2	10:59	Rabinowitz	Customer	$1.75	10,000	-0-
3	11:10	Rabinowitz	VTR	$1.75	19,200	(19,200)
4	11:24	Rabinowitz	VTR	$1.75	5,000	(24,200)
5	11:24	Rabinowitz	VTR	$1.75	10,000	(34,200)
6	11:26	Rabinowitz	VTR	$1.75	3,500	(37,700)
7	11:40	VTR	Rabinowitz	$1.74	10,000	(27,700)
8	11:42	VTR	Rabinowitz	$1.74	10,000	(17,700)
9	11:48	Rabinowitz	VTR	$1.75	8,000	(25,700)
10	11:50	VTR	Rabinowitz	$1.625	10,000	(15,700)
11	11:50	Rabinowitz	Customer	$1.875	10,000	(25,700)
12	11:55	VTR	Rabinowitz	$1.74	25,700	-0-
			Afternoon			
13	12:03	VTR	Rabinowitz	$1.75	20,000	20,000
14	12:03	Rabinowitz	Customer	$1.80	10,000	10,000
15	12:04	Rabinowitz	Customer	$2.00	10,000	-0-
16	12:27	Rabinowitz	VTR	$2.00	14,600	(14,600)
17	12:29	Rabinowitz	VTR	$2.00	9,750	(24,350)

[9] Ex. C13; Ex. R5E.

	Time	Seller	Buyer	Price	Shares	Rabinowitz's Inventory
18	12:32	Rabinowitz	VTR	$2.00	9,000	(33,350)
19	12:40	Rabinowitz	VTR	$2.00	15,000	(48,350)
20	12:46	VTR	Rabinowitz	$1.99	10,000	(38,350)
21	13:03	Rabinowitz	VTR	$2.00	15,100	(53,450)
22	13:08	VTR	Rabinowitz	$1.99	15,000	(38,450)
23	13:29	VTR	Rabinowitz	$1.99	15,000	(23,450)
24	13:34	Rabinowitz	VTR	$2.00	8,300	(31,750)
25	13:43	Rabinowitz	VTR	$2.00	6,500	(38,250)
26	13:46	VTR	Rabinowitz	$1.99	15,000	(23,250)
27	13:55	VTR	Rabinowitz	$1.99	13,250	(10,000)
28	14:01	VTR	Rabinowitz	$1.99	10,000	-0-

As the foregoing chart reveals, I.A. Rabinowitz and VTR swapped Interiors Stock back and forth more than 20 times on April 19, 1995—usually at a penny difference. I.A. Rabinowitz started the day and ended the day holding no shares of Interiors Stock. During the day VTR and I.A. Rabinowitz traded a total of 123,950 shares, which equaled approximately 12.2% of the publicly available shares.[10]

The trading between I.A. Rabinowitz and VTR on April 19, 1995, was remarkable for three reasons. First, the size of the block trades was notable. Interiors Stock was a relatively thinly traded security. In the period leading up to April 19, there was very little activity in the stock. Between April 3 and April 18, 1995, the average volume was just 18,191 shares. In contrast, the volume on April 19 was 441,000 shares, of which a substantial portion was generated by the trading between VTR and I.A. Rabinowitz. (Ex. C12, at 1.)

[10] Interiors had distributed 1,017,500 shares of common stock to the public. (Ex. C10, at 1.)

Second, on April 19, 1995, I.A. Rabinowitz established short positions as great as 53,450 shares—almost three times the average daily volume for the prior 11 days. Despite the size of this short position relative to the overall market volume and Mr. Perles's lack of awareness regarding the number of shares that were available at the firm, Mr. Perles testified that he was not concerned about how he could cover the position. (Tr. 422.) He explained that I.A. Rabinowitz's customers had sufficient shares in their accounts to cover his short positions. But he also admitted that he did not know if any of those customers were interested in selling, he did not follow closely the reported volume in Interiors Stock, and he did not know how much capital I.A. Rabinowitz had. (Tr. 423-24.)

Third, Mr. Perles combined many of the trades with VTR on a single ticket by crossing out the amount of the trade and adding a new trade. For example, Exhibit C13, page 7, is the sell ticket from the morning trading with VTR reflecting a total volume of 45,700. The ticket has five separate entries on the ticket, each crossed through, under the total. These crossed out trades correspond to the trades numbered 3, 4, 5, 6, and 9 on the foregoing chart. Interestingly, the trades were not totaled as they were entered on the ticket, indicating to the Hearing Panel that Mr. Perles left the ticket open because he knew that he would be adding to the ticket as the day went on. Mr. Perles explained the entries differently. He denied that he left the ticket open because he knew there would be additional trades. According to him, he combined the trades because Mr. Rabinowitz wanted him to save on ticket charges. Mr. Perles testified that if the ticket was still in the box next to his desk and had not been billed, he would pull the ticket back and add to it when he got another order.

The Hearing Panel finds this explanation unconvincing and inconsistent with the manner in which the trades were recorded on the ticket. Under Mr. Perles's version, if the ticket had gone to billing before the final entry, the ticket would not have shown the total number of shares traded, and it would not have been possible to know from the face of the ticket that the crossed out trades needed to be added together to determine the total volume.

Mr. Perles denied any arrangement with VTR regarding Interiors Stock. He testified that the trades were just normal order flow. (Tr. 375-76.) Accordingly, he did not record the trades as prearranged on I.A. Rabinowitz's books and records.

From the foregoing, however, the Hearing Panel concludes that Mr. Perles did engage in prearranged circular, or wash and matched, trading with VTR on April 19, 1995, and that this trading had the effect of distorting the apparent volume in Interiors Stock. Alternatively, even if Mr. Perles was not privy to the understanding with David Noble, the trader at VTR, Mr. Perles was negligent in failing to investigate further when he encountered this pattern and volume of trading, at a negotiated price, in a stock that usually had significantly less activity. This activity presented Mr. Perles with red flags of improper conduct that he should not have ignored.

2. Trades By Geller

Mr. Geller at Wien Securities engaged in a nearly identical pattern of prearranged trading of Interiors Stock on April 20 and 21, 1995, as follows:[11]

	Time	Seller	Buyer	Price	Shares	Wien's Inventory
			April 20, 1995			
1	10:25	Wien	VTR	$2.00	8,500	(8,500)
2	10:25	Wien	VTR	$2.00	10,800	(19,300)
3	10:32	Wien	VTR	$2.00	11,000	(30,300)
4	10:36	Wien	VTR	$2.00	20,000	(50,300)
5	10:43	Wien	VTR	$2.00	13,850	(64,150)
6	10:49	VTR	Wien	$1.984375	22,000	(42,150)
7	10:53	Wien	VTR	$2.00	9,800	(51,950)
8	10:58	VTR	Wien	$1.984375	18,000	(33,950)
9	11:04	Wien	VTR	$2.00	11,900	(45,850)
10	11:10	VTR	Wien	$1.984375	15,900	(29,950)
11	11:20	VTR	Wien	$1.984375	12,500	(17,450)
12	11:26	Wien	VTR	$2.00	14,400	(31,850)
13	11:32	Wien	VTR	$2.00	7,400	(39,250)
14	11:37	VTR	Wien	$1.984375	15,000	(24,250)
15	11:40	VTR	Wien	$1.984375	13,500	(10,750)
16	11:46	VTR	Wien	$1.984375	10,750	-0-
			Afternoon			
17	12:01	Wien	VTR	$2.00	8,650	(8,650)
18	12:03	Wien	VTR	$2.00	10,800	(19,450)
19	12:07	VTR	Wien	$1.984375	23,000	3,550
20	14:56	Wien	VTR	$2.125	10,000	(6,450)
21	15:08	Wien	VTR	$2.125	11,200	(17,650)
22	15:20	Wien	VTR	$2.125	8,200	(25,850)
23	15:30	VTR	Wien	$2.00	1,000	(24,850)

[11] Ex. C14, at 1A, 2. Multiple trades executed at the same time have been combined.

	Time	Seller	Buyer	Price	Shares	Wien's Inventory
24	15:34	VTR	Wien	$2.109375	10,500	(14,350)
25	15:43	VTR	Wien	$2.109375	12,000	(2,350)
26	15:56	Wien	VTR	$2.125	1,500	(3,850)
27	15:57	Wien	VTR	$2.125	5,500	(9,350)
28	16:01	VTR	Wien	$2.109375	9,000	(350)
			April 21, 1995			
29	10:17	Wien	VTR	$2.125	14,000	(14,350)
30	10:25	Wien	VTR	$2.125	10,500	(24,850)
31	10:29	Wien	VTR	$2.125	8,700	(33,550)
32	10:31	Wien	VTR	$2.125	6,450	(40,000)
33	10:35	VTR	VTR	$2.109375	17,000	(23,000)
34	10:55	VTR	VTR	$2.109375	14,500	(8,500)
35	11:04	Wien	VTR	$2.125	7,300	(15,800)
36	11:09	Wien	VTR	$2.125	1,000	(16,800)
37	11:12	VTR	Wien	$2.109375	16,450	(350)
			Afternoon			
38	13:31	Wien	VTR	$2.1875	14,700	(12,550)
39	13:32	Wien	VTR	$2.1875	2,600	(15,150)
40	13:41	VTR	Wien	$2.17185	15,200	50
41	15:03	Wien	VTR	$2.1875	6,300	(6,250)
42	15:04	Wien	VTR	$2.1875	1,800	(8,050)
43	15:54	VTR	Wien	$2.171875	8,000	(50)

Over those two days, Mr. Geller swapped 236,800 shares of Interiors Stock with VTR—or approximately 23% of the float. Wien Securities executed only one other trade of 2,500 shares of Interiors Stock on April 20 and 21 with a firm other than VTR. (Ex. C14, at 5, Transaction No. 57.) As Mr. Perles had done, Mr. Geller started and ended each day without a substantial position in the stock. And the trades with VTR were all executed at negotiated prices and for very small

profits to Wien. Except for one trade on April 20, each of the trades with VTR was executed at a spread of 1/64th. (Ex. C15.)

The volume of trading in Interiors Stock on April 20 and 21, 1995, between VTR and Wien Securities was significant. Mr. Geller and VTR swapped 241,850 shares, which was 24.1% of the reported volume between April 19 and April 21, 1995. (Id.) Other than I.A. Rabinowitz, no other firm had as much as 5% of the total reported volume. (Id.) And the circular trading between VTR, Wien Securities, and I.A. Rabinowitz increased the reported volume of Interiors Stock by 56% from 642,730 shares to 1,003,730 shares. (Tr. 108-09.)

Mr. Geller testified that there was nothing unusual about these trades and that he lacked any specific recollection about them. (Tr. 255.) He suggested that it was possible that some of the trades were done on SelectNet, but he also noted that SelectNet was in limited use at that time. (Tr. 259, 261-62.) Indeed, Mr. Geller testified that most of his trading was done by telephone, undercutting his speculation that his trading pattern in Interiors Stock could be attributed to activity on SelectNet.

Mr. Geller also testified that it was not unusual to trade stock for narrow spreads within the market quotes. (Tr. 264.) And he denied that there was an unrecorded repurchase agreement or prearrangement with VTR that he should have reflected on the books and records at Wien Securities. (Tr. 266.)

Stephen S. Wien corroborated a portion of Mr. Geller's testimony. Although Mr. Wien did not address directly the existence of an agreement with VTR regarding the subject trades, he did state that it was not unusual to receive buy and sell orders from the same broker in the course of a day. (Tr. 305.) He also testified that Mr. Geller was properly supervised at the time these

trades were executed, implying that they were handled properly. (Id.) Further, Mr. Wien testified that there was nothing unusual about "shorting a stock into a rising market." (Tr. 307.)

Mr. Geller was vague, however, in his responses to questions about the size of the short positions he established in Interiors Stock on April 20 and 21, 1995. When asked how he had intended to cover the relatively large short positions, he speculated that he could have been looking at two different scenarios. Either he could have had a sell order on the stock, or he could have been working an "arbitrage situation." (Tr. 288.) Mr. Geller explained that a trading strategy that he specialized in was to buy a stock's derivatives when he shorted the stock. (Tr. 290.) However, further questioning revealed no evidence that either situation applied to the trades at issue.

Ultimately, Mr. Geller tried to attribute his trading with VTR to his desire to get "involved" due to the market volume at the time. (Tr. 474.) According to Mr. Geller, increased market volume alone was sufficient reason for him to establish a short position of as many as 60,000 shares when the total daily volume in the stock had been as little as 200 shares just seven trading days earlier. (Ex. C12, at 1.) Mr. Geller maintained that position despite the fact that he admitted that he did not keep track of the specific volume in the stocks he traded. (Tr. 472.)

The Hearing Panel found Mr. Geller's explanations and speculations insufficient. In the Hearing Panel's opinion, Mr. Geller advanced these alternatives without a basis. The Hearing Panel therefore concluded that there was no explanation for Mr. Geller's trading in Interiors Stock in April 20 and 21, 1995, other than that the trades were prearranged.

III. Respondents' Motion To Dismiss And Motion For Summary Disposition

A. Motion To Dismiss

At the conclusion of Enforcement's case-in-chief, the Respondents moved to dismiss the Complaint on the ground that Enforcement had failed to introduce any evidence connecting them to the unregistered distribution of Interiors Stock and had failed to introduce evidence establishing that the trading in Interiors Stock had been prearranged. In response, Enforcement argued that there was sufficient circumstantial evidence to support a finding that the Respondents aided and abetted VTR and McCune in both the unregistered distribution and the wash and matched trading of Interiors Stock. Enforcement asserted that the volume and pricing alone were sufficient "red flags" to prove aiding and abetting. (Tr. 229.) After consideration of the arguments of the Parties, the Hearing Panel granted the motion to dismiss the charge in Cause Six of the Complaint alleging that the Respondents aided and abetted the unregistered distribution of Interiors Stock. The Hearing Panel denied the remainder of the motion.

To establish liability for aiding and abetting a violation of the securities laws, Enforcement must show: (1) the existence of a primary violation; (2) that the respondent knew, or had a general awareness, that his role was part of an overall activity that was improper; and (3) that the respondent rendered substantial assistance to the principal violator.[12] In this case, Enforcement provided no evidence that the Respondents knew, or had a general awareness, that they were assisting VTR and McCune in an unregistered distribution of 300,000 shares of Interiors Stock. Neither the increased volume of trading nor the narrow spreads at which the

[12] See, e.g., Levine v. Diamanthuset, Inc., 950 F.2d 1478, 1483 (9th Cir. 1991). The NASD has adopted a similar formulation. See, e.g., Market Surveillance Comm. v. John Roger Faherty, Complaint No. CMS920005, 1998 NASD Discip. LEXIS 44, at *20 (NAC Oct. 14, 1998).

stock traded is by itself, or together, sufficient to establish the requisite level of knowledge on the Respondents' part. While these factors could be taken into consideration in supporting other circumstantial evidence of knowledge, there was no such other evidence in this case.

Accordingly, the Hearing Panel finds that Enforcement failed to show by a preponderance of the evidence that the Respondents had the required degree of knowledge to support the charge that they aided and abetted the unregistered distribution of Interiors Stock. That charge therefore is dismissed.

B. Motion For Summary Disposition

On June 9, 1998, Mr. Perles and Mr. Geller filed a joint motion for summary disposition. In part, they challenged Enforcement's authority to charge persons with aiding and abetting violations of Section 10(b), Rule 10b-5, and NASD Conduct Rule 2120. The Hearing Panel deferred ruling on the challenge to Enforcement's aiding and abetting theory until the hearing. At the conclusion of the hearing, the Respondents renewed the motion for summary disposition as to the remaining aiding and abetting charge in Cause Six and moved orally for summary disposition as to all of the remaining charges.

The Hearing Panel granted the motion in part and dismissed the charge under Cause Six that the Respondents aided and abetted VTR and McCune in the manipulation of the reported volume of Interiors Stock through wash and matched trading. The Hearing Panel denied the motion as to all of the remaining charges in the Complaint.

After hearing all of the evidence, the Hearing Panel concluded that Enforcement had failed to present sufficient evidence that Mr. Perles and Mr. Geller knew, or had a general awareness, that their role in trading Interiors Stock was part of a scheme to manipulate the

market for Interiors Stock. As with the charge that they aided and abetted the unregistered distribution of Interiors Stock, Enforcement rested its case on two facts: that there was substantially increased volume in the stock and that the trades were made inside the market quotes at very narrow spreads. However, those facts alone are not conclusive. While the Hearing Panel finds that under the circumstances the Respondents were at a minimum negligent in failing to inquire about the trades, that is not the equivalent of knowingly assisting another in manipulating the stock.

In cases where the SEC or the National Adjudicatory Council ("NAC") has found aiding and abetting liability, there has been far greater evidence of the respondent's level of knowledge. For example, in Market Surveillance Comm. v. John Roger Faherty,[13] the NAC emphasized Faherty's knowing and intentional participation in the firm's manipulative scheme. In so doing, the NAC pointed to compelling evidence establishing that it was "inconceivable" that he did not know of the manipulative scheme.[14] In contrast, the evidence Enforcement relied upon in this case is nowhere near as convincing. The Hearing Panel is left to speculate as to the Respondents' knowledge and intent. Consequently, the Hearing Panel dismissed the charge that the Respondents aided and abetted the manipulation of the market for Interiors Stock.

However, even if the evidence were sufficient to establish that the Respondents were aware of VTR and McCune's manipulative scheme, the Hearing Panel concludes that this charge is insufficient as a matter of law under the holding of Central Bank of Denver, N.A. v. First

[13] 1998 NASD Discip. LEXIS 44.

[14] Id. at *25.

Interstate Bank of Denver, N.A., 511 U.S. 164 (1994), a case involving a private right of action under Section 10(b).

In Central Bank, the holders of defaulted bonds, in addition to their claims against the issuer and others alleging primary liability under Rule 10b-5, sued the indenture trustee on the theory that the trustee aided and abetted the other defendants' violations by recklessly ignoring its oversight duties. In holding that the claim against the trustee could not stand, the Supreme Court found that Section 10(b) "prohibits only the making of a material misstatement (or omission) or the commission of a manipulative act. The proscription does not include giving aid to a person who commits a manipulative or deceptive act."[15]

The Supreme Court's opinion focused on the basic requirement for a finding of Section 10(b) liability: there must be a deceptive misstatement (or omission) or the commission of a manipulative act on the part of the defendant.[16] This requirement is in contrast to the usual requirements for aider and abettor liability. Typically these requirements are the following: "(1) the existence of an independent primary wrong; (2) actual knowledge or reckless disregard by the alleged aider and abettor of the wrong and of his or her role in furthering it; and (3) substantial assistance in the wrong."[17] Significantly, there is no requirement that an alleged aider and abettor commit a manipulative or deceptive act. The Supreme Court in Central Bank recognized that "aiding and abetting liability extends beyond persons who engage, even indirectly, in a proscribed activity; aiding and abetting liability reaches persons who do not engage in the

[15] Central Bank at 176.

[16] Id. at 177.

[17] See, e.g., Levine v. Diamanthuset, Inc., 950 F.2d 1478, 1483 (9th Cir. 1991).

proscribed activities at all, but who give a degree of aid to those who do."[18] Thus, the Supreme Court held that aider and abettor liability does not meet the minimum requirements for liability under Section 10(b) of the Exchange Act. Therefore, in a private cause of action, a person cannot be held liable under Section 10(b) and Rule 10b-5 for simply aiding and abetting a primary violation of these provisions.

After Central Bank, the issue of whether the SEC, in a governmental enforcement action, could charge aiding and abetting a violation of Section 10(b) was unclear. Although Central Bank involved a private cause of action, the Supreme Court relied on a strict textual analysis of Section 10(b) and did not limit the holding to private causes of action.[19] Congress therefore amended the Exchange Act to expressly grant the SEC the authority to pursue aiding and abetting charges under Section 10(b).[20] But no similar provision was enacted for private actions, including enforcement actions brought by self-regulatory organizations (SROs) such as the NASD.[21]

Despite the express limitation of Section 20(f) to enforcement actions brought by the SEC, Enforcement here argues that Section 20(f) permits all "regulatory enforcement actions" against persons who aid and abet violations of Section 10(b) and Rule 10b-5.[22] Thus, to the extent any

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[18] Central Bank at 176.

[19] Central Bank at 191.

[20] See Section 20(f) 15 U.S.C. § 78(t).

[21] Section 20(f) provides as follows:

> Prosecution of persons who aid and abet violations.
>
> For purposes of any action brought by the Commission under paragraph (1) or (3) of section 78u(d) of this title, any person that knowingly provides substantial assistance to another person in violation of a provision of this chapter, or of any rule or regulation issued under this chapter, shall be deemed to be in violation of such provision to the same extent as the person to whom such assistance is provided. (Emphasis added).

[22] Complainant's Resp. In Opp'n To Mot. By Resp'ts Perles and Geller For Summ. Disposition at 5.

doubts existed, Enforcement concludes they were resolved when Congress enacted Section 20(f).[23]

Enforcement, however, has not cited any authority for its argument that Congress intended to extend the power to charge aiding and abetting violations of Section 10(b) to SROs by referring to the SEC in Section 20(f). Accordingly, Enforcement's argument must rely on the implicit assumption that, at least for the purposes of Enforcement actions under Section 10(b), the NASD is the functional equivalent of the SEC. The Hearing Panel does not agree with this assumption.

The consequences associated with a claim that the NASD performs functions similar to the SEC, and therefore stands in its shoes, would be significant. For example, if the NASD were considered a governmental entity, then it would be subject to the same restraints applicable to the government such as the Fourth and Fifth Amendments to the Constitution. Such a holding would represent a reversal of well-settled case law holding that the NASD, in the context of its disciplinary proceedings, is a private, non-governmental entity.[24] The Hearing Panel is unwilling to take such a departure from settled law.

Accordingly, to the extent that Enforcement's claims in Cause Six are based on an aider and abettor theory of liability under Section 10(b) and Rule 10b-5, they are dismissed.

Likewise, a person cannot be held to violate NASD Conduct Rule 2120 for aiding and abetting a primary violation of this Rule. Rule 2120 is the equivalent of SEC Rule 10b-5.[25] Rule 2120 provides that no member shall effect any transaction in, or induce the purchase or sale of,

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[23] Id.

[24] See, e.g., Herbert G. Frey, Exchange Act Rel. No. 39007, n.17 (Sept. 3, 1997).

[25] Market Regulation Committee v. Kevin Eric Shaughnessy, Complaint No. CMS950087, 1997 NASD Discip. LEXIS 46, *24-25 (NBCC June 5, 1997).

any security by means of any manipulative, deceptive, or fraudulent device. In order to find a violation of Rule 2120, there must be a showing of a material misrepresentation (or omission) in connection with the purchase or sale of securities which was made with scienter. To establish a violation of Rule 2120, Enforcement must plead and prove a deceptive misstatement (or omission) or the commission of a manipulative act on the part of the respondent. Giving aid to a person who commits a manipulative or deceptive act is not a violation of Rule 2120.[26] Accordingly, Cause Six fails to allege a violation of Rule 2120, and the charge is dismissed.

IV. Conclusions of Law

A. Jurisdiction

The NASD has jurisdiction over the Respondents. At all times relevant to this proceeding, they were registered with the NASD and associated with member firms.

B. Wash And Matched Trading In Violation Of Rule 2110

Independent of the allegations of aiding and abetting in Cause Six of the Complaint, Enforcement alleges that Mr. Perles and Mr. Geller violated NASD Conduct Rule 2110 by engaging in a pattern of contrived, circular trading or wash and matched trading that served no legitimate economic purpose.[27] Enforcement further alleges that their conduct in effecting these trades was inconsistent with the maintenance of a fair and orderly market and with just and equitable principles of trade.

[26] Enforcement did not charge Mr. Perles and Mr. Geller as principal violators of Rule 2120. If the NASD wants to provide for aiding and abetting liability under Rule 2120, the Hearing Panel notes that the NASD could seek to amend the rule.

[27] Compl. ¶¶ 44, 46.

Mr. Perles and Mr. Geller contend that their trading in Interiors Stock was normal market activity and that, as a matter of law, Rule 2110 is too vague to be applied to them in this proceeding. They argue that Rule 2110, under Enforcement's theory, fails to provide them with adequate notice of what specific conduct might subject them to discipline.

Rule 2110 provides that a member, in the conduct of his business, shall observe high standards of commercial honor and just and equitable principles of trade. "The crux of a Conduct Rule 2110 violation is the breach of a duty imposed by just and equitable principles of trade."[28] The Rule goes beyond simple legal requirements in imposing a duty of fair dealing.[29] Thus, a violation of Rule 2110 can be found where no legally cognizable wrong occurred.[30] Challenges to Rule 2110 on the ground of vagueness generally have been rejected by the SEC and the courts where application of the rule to the particular misconduct "cannot come as a surprise."[31]

Wash and matched trading has long been held by the courts, the SEC, and the NASD to be a form of manipulation that violates the securities laws and the rules of the NASD.[32] Indeed, wash and matched trading was one of the specific types of manipulation cited by Congress in enacting

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[28] See, e.g., District Bus. Conduct Comm. for Dist. No. 5 v. Jeffrey O. Putterman, Complaint No. C05960041, 1997 NASD Discip. LEXIS 52, at *22 (NASD October 10, 1997).

[29] Id.

[30] Timothy L. Burkes, 51 S.E.C. 356 (1993), aff'd mem., Burkes v. SEC, 29 F.3d 630 (9th Cir. 1994).

[31] See Alderman v. S.E.C., 104 F.3d 285, 289 (9th Cir. 1997) (duty to protect client funds cannot have come as a surprise); see also Sorrell v. S.E.C., 679 F.2d 1323, 1326 (9th Cir. 1982).

[32] See, e.g. Schreiber v. Burlington Northern, Inc., 472 U.S. 1, 6 (1985); see also In re J. A. Latimer & Co., 38 S.E.C. 790 (1958); In re Thornton & Co., 28 S.E.C. 208 (1948).

Section 10(b) of the Exchange Act.[33] Consequently, Mr. Perles and Mr. Geller cannot claim that they are surprised that such trading constitutes a violation of NASD Conduct Rule 2110.

In addition, Section 9(a)(2) of the Exchange Act makes it unlawful to effect ". . . a series of transactions in any security . . . creating actual or apparent active trading in such security, or raising or depressing the price of such security, for the purpose of inducing the purchase or sale of such security by others." Although this section does not apply to over-the-counter securities, the anti-manipulative prohibitions in Section 9 of the Exchange Act have been referenced and applied repeatedly in decisions involving over-the-counter securities.[34] False trading activity is one common form of manipulation that has often been cited as inimical to a broker's duty to deal fairly with the public.[35] Accordingly, there is no merit to the Respondents' argument that NASD Rule 2110 is vague and unenforceable, as applied to the facts of this proceeding.

Turning to the specific conduct at issue in this proceeding, the Respondents' liability turns on what they knew, or had reason to know, regarding the manipulative trading in Interiors Stock. In the Hearing Panel's view, the pattern of trading in this case would have led any reasonably conscientious broker to be suspicious. The trading was highly abnormal.

Mr. Perles on behalf of I.A. Rabinowitz swapped 123,950 shares of Interiors Stock in just over three hours. This represented over 12% of the total number of shares available for trading by

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[33] See Ernst & Ernst v. Hochfelder, 425 U.S. 185, 96 S. Ct. 1375, 1386 (1976). Section 9(a) (1) of the Exchange Act, 15 U.S.C. § 78i(a)(1), proscribes wash sales and matched orders when effectuated "(f)or the purpose of creating a false or misleading appearance of active trading in any security registered on a national securities exchange, or . . . with respect to the market for any such security."

[34] See, e.g., Market Surveillance Comm. v. Wakefield Financial Corp., Complaint No. MS-936, 1992 NASD Discip. LEXIS 124 (NBCC May 7, 1992).

[35] See, e.g., In re Edward J. Mawod & Co., 46 S.E.C. 865 (1977), aff'd sub nom, Edward J. Mawod & Co. v. S.E.C., 591 F.2d 588 (1979) (holding that activity that creates "a false or misleading appearance of active trading" in a security is manipulative).

the public. Furthermore, many of the block trades were larger than the typical daily volume in this relatively thinly traded security. At the end of the day, I.A. Rabinowitz had no Interiors Stock in inventory, just as it had started the day. And the total profit made on the trading—before expenses—was only a penny a share or $1,239.50. Moreover, the Hearing Panel finds it significant that I.A. Rabinowitz was a co-underwriter for the initial public offering of Interiors Stock and had been an active market maker in the stock since that time. Indeed, Mr. Perles testified that I.A. Rabinowitz had a number of customers with Interiors Stock in their accounts. The Hearing Panel also notes that Mr. Perles worked in a small trading department comprised of himself and one assistant and that he personally filled out the order tickets by hand for each of the 21 trades at issue.

Accordingly, the Hearing Panel believes that Mr. Perles had ample information available to him to appreciate the non-bona fide nature of the trading initiated by VTR and the impact that this activity would have on the market. Without doubt, Mr. Perles should have realized that the trading he was engaged in on April 19, 1995, comprised a substantial volume that would incorrectly make it appear that there was broader market demand for the stock than that which actually existed.

As to Mr. Geller, he likewise had sufficient information available to him so that he could appreciate the non-bona fide nature of the trading with VTR on April 20 and 21, 1995. Mr. Geller executed 43 trades with VTR over those two days, involving 236,800 shares of Interiors Stock—approximately 23% of the shares available for trading by the public. In addition, Mr. Geller could see that there was little other demand for the stock. He had a NASDAQ Workstation with Level 3 Service at his desk. Moreover, he only made one other trade of 2,500 shares during

these two days. Considering the evidence in the light most favorable to Mr. Geller, the pattern of trading suggested an unusual purpose or manipulative intent by VTR, and Mr. Geller should have investigated whether the trading was legitimate.

Both Mr. Perles and Mr. Geller violated NASD Conduct Rule 2110 by participating in this trading. They breached their duty to refrain from activity that would have a deceptive impact on the market.

C. Books And Records Violation

Section 17(a) of the Exchange Act requires registered broker-dealers to "make and keep" appropriate records in the course of conducting their business. Pursuant to Section 17(a), the SEC adopted SEC Rule 17a-3, which lists specific types of documents broker-dealers must create and maintain.[36] SEC Rule 17a-3(a)(6) specifically directs broker-dealers to create and keep memoranda of all brokerage orders, which are to include any instructions given or received for

[36] SEC Rule 17a-3 provides, in part:

> (a) Every member of a national securities exchange who transacts a business in securities directly with others than members of a national securities exchange, and every broker or dealer who transacts a business in securities through the medium of any such member, and every broker or dealer registered pursuant to section 15 of the Securities Exchange Act of 1934 . . . shall make and keep current:
>
> (1) Blotters (or other records of original entry) containing an itemized daily record of all purchases and sales of securities . . . .
>
> (4) Ledgers (or other records) reflecting the following: . . .
>
> (vii) Repurchase and reverse repurchase agreements . . . .
>
> (6) A memorandum of each brokerage order, and of any other instruction, given or received for the purchase or sale of securities, whether executed or unexecuted. Such memorandum shall show the terms and conditions of the order or instructions and of any modification or cancellation thereof, the account for which entered, the time of entry, the price at which executed and, to the extent feasible, the time of execution or cancellation.
>
> (7) A memorandum of each purchase and sale for the account of such member, broker, or dealer showing the price and, to the extent feasible, the time of execution; and, in addition, where such purchase or sale is with a customer other than a broker or dealer, a memorandum of each order received, showing the time of receipt, the terms and conditions of the order, and the account in which it was entered.

the purchase and sale of the securities. Also, SEC Rule 17a-3(a)(7) requires broker-dealers to create and keep memoranda of every purchase and sale for the firm's account, reflecting all terms and conditions of the transactions. In turn, NASD Rule 3110 requires members to make and keep accurate records required by Section 17(a) of the Exchange Act and the rules promulgated by the SEC thereunder. Failure to do so not only violates these rules but also NASD Conduct Rule 2110.[37]

Here, Mr. Perles and Mr. Geller were required to make and keep accurate records of all of the terms and conditions underlying the wash and matched trades they executed with VTR. The SEC has instituted proceedings against firms for similar violations. For example, in In re Jay Joseph Buck,[38] the SEC imposed sanctions pursuant to a settlement where the broker had failed to reflect, or cause others at his firm to reflect, certain repurchase agreements with customers. Instead, the broker had recorded the subject transactions as unrelated purchases and sales. Similarly, in Goldman, Sachs & Co.,[39] a case involving prearranged, circular trading, the SEC approved a settlement finding that the broker-dealer violated Section 17(a) of the Exchange Act and the rules thereunder by not reflecting on its books, including its blotters, that the subject trades were subject to an agreement to reestablish the positions traded, and that the trades were negotiated with the same party to eliminate risks, or that there was any connection at all between the trades.

[37] See generally, In re James S. Pritula, Exchange Act Release No. 40647, 1998 SEC LEXIS 2425 (Nov. 9, 1998) (upholding the NASD's finding that the respondent violated Rule 2110 by causing a member firm to violate SEC Rule 17a-3).

[38] Exchange Act Release No. 31496, 1992 SEC LEXIS 3105 (Nov. 23, 1992).

[39] Exchange Act Release No. 33576, 1994 SEC LEXIS 302 (Feb. 3, 1994).

Accordingly, the Hearing Panel finds that Mr. Perles and Mr. Geller violated NASD Conduct Rules 2110 and 3110, Section 17(a) of the Exchange Act, and SEC Rule 17a-3 by failing to accurately reflect the terms and conditions of the trades they executed in Interiors Stock with VTR, as alleged in Cause Seven of the Complaint.

V. Sanctions

The Hearing Panel first notes that disciplinary sanctions are remedial. Their purpose is to remediate misconduct and to protect the investing public. In setting remedial sanctions, adjudicators must consider the NASD's legitimate policies of special and general deterrence in the public interest. Accordingly, the NASD Sanction Guidelines direct adjudicators to design sanctions to prevent and discourage future misconduct by the respondent, to deter others from engaging in similar misconduct, and to improve the overall business standards in the securities industry.[40] Ultimately, the process of determining an appropriate sanction involves a balancing of the concepts of remediation and deterrence, taking into consideration the particular facts and circumstances of the instant case.[41] Hard-and-fast formulas do not apply.[42]

The Department of Enforcement argues that the Respondents' conduct was serious and deserves sufficiently severe sanctions to deter others from similar misconduct. In addition, the Department of Enforcement argues that Mr. Perles should be sanctioned more severely because he has been sanctioned in three earlier disciplinary actions. The Hearing Panel generally agrees with the Department of Enforcement's assessment. In addition, the Hearing Panel considers Mr.

[40] NASD Sanction Guidelines 3 (2d ed. 1998).

[41] See, e.g., Berko v. SEC, 316 F.2d 137, 141 (2d Cir. 1963).

Perles to be more culpable than Mr. Geller, and it will, therefore, assess sanctions taking into account the differences in their conduct and disciplinary histories.

In arriving at the sanctions in this case, the Hearing Panel consulted the NASD Sanction Guidelines for record keeping violations and for misrepresentations and material omissions of fact. The guideline for record keeping violations recommends a fine of $1,000 to $10,000 and a suspension of the responsible party for up to 30 business days. In egregious cases, the guideline suggests that the Hearing Panel consider a lengthier suspension or a bar.[43] The guideline for misrepresentation recommends a fine of $2,500 to $50,000 and a suspension of up to 30 business days if the respondent was negligent. If the respondent acted intentionally or recklessly, the guideline suggests a fine of $10,000 to $100,000 and a suspension of up to two years or a bar in egregious cases. While neither of these guidelines dictates the result in this case, they provide benchmarks against which the Hearing Panel can measure the Respondents' conduct.

Turning to Mr. Perles, the Hearing Panel determines that he should be fined $25,000, suspended in all capacities for one year, and ordered to requalify as a General Securities Representative by taking the Series 7 Examination. The Hearing Panel considers these sanctions to be appropriately remedial under the facts and circumstances of this case.[44] The Hearing Panel finds that Mr. Perles's defense lacks credibility. He described his role at his firm as quite limited, not at all commensurate with the normal authority of a "trader." Yet, he asserted that with this limited role he nevertheless engaged in a pattern of trading involving substantial risk. His

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[42] Cf. In re Consolidated Inv. Services, Inc., Exchange Act Release No. 36687 61 S.E.C. Docket 19, 32 (Jan. 5, 1996) (stating that sanctions are determined on a case-by-case basis and cannot be determined by comparison with action taken in other cases).

[43] NASD Sanction Guidelines 28 (2d ed. 1998).

explanation that he could cover his short positions by buying from his firm's customers was unsubstantiated. He presented no evidence that any customer was willing to sell or that he had ever engaged in a similar trading strategy in the past. In the Hearing Panel's opinion, his trading can only be explained by the fact that he felt assured that VTR would sell him exactly the same number of shares so that he would be flat in the firm's trading account at the end of the day.

The Hearing Panel also has taken into consideration Mr. Perles's disciplinary history. He has twice been suspended for participating in unregistered distributions. Nevertheless, from observing Mr. Perles's demeanor and evaluating his testimony, the Hearing Panel concludes that he does not appreciate the seriousness of his misconduct and the importance of his obligations as a registered representative. Accordingly, the Hearing Panel finds that a more substantial suspension and requalification by examination is needed in this case.

As to Mr. Geller, the Hearing Panel determines that he should be fined $25,000 and suspended for 30 business days. Mr. Geller's defenses also lacked credibility. Mr. Geller argued that at most he was negligent in not discovering that VTR was manipulating the market for Interiors Stock, and he presented testimony that he often engaged in similar trading. He argued that it was not unusual to trade between the market for nominal profit, and he tried to explain his significant short positions in Interiors Stock as an arbitrage situation. However, Mr. Geller presented no evidence of similar trading, and he admitted that this was not an arbitrage situation.

The Hearing Panel finds his theoretical explanations to be nothing more than an attempt at obfuscation. In the end, Mr. Geller had no reasonable explanation for his actions. Mr. Geller presented himself as a sophisticated trader who carefully watched the positions he carried in the

[44] The Hearing Panel has not imposed a higher fine because of his limited financial resources.

firm's account. Yet, over two days of trading in which there was no change in the ownership of the Interiors Stock he swapped back and forth with VTR, he has no explanation of why he did not investigate if the trading was bona fide. Under these circumstances, the Hearing Panel finds that Mr. Geller knew that the trading was improper and had the effect of distorting the reported trading volume.

On the other hand, the Hearing Panel agrees with Enforcement's assessment that Mr. Geller's disciplinary history is not significant. Late payment of an arbitration award by one day does not indicate that enhanced sanctions are needed in this case to deter him from future misconduct.

VI. Order

Therefore, having considered all of the evidence, the Hearing Panel imposes the following sanctions:

1. Howard R. Perles is fined $25,000, suspended for one year from associating with any member firm in any capacity, and ordered to requalify as a General Securities Representative by taking the Series 7 Examination.
2. Laurence M. Geller is fined $25,000 and suspended for 30 business days from associating with any member firm in any capacity.[45]

Each of the Respondents is further ordered to pay $1,223.25 in costs of this proceeding.

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

The sanctions shall become effective on a date set by the Association, but not earlier than 30 days after the date this decision becomes the final disciplinary decision of the NASD.

_____

Andrew H. Perkins
Hearing Officer
For the Hearing Panel

Copies to:

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