

NASD
LETTER OF ACCEPTANCE, WAIVER AND CONSENT

20050002450-03

TO: Department of Market Regulation
NASD

RE: First New York Securities L.L.C.
BD No. 16362

Michael Lawrence Friedman
CRD No. 214675

Pursuant to Rule 9216 of the NASD Code of Procedure, First New York Securities L.L.C. (the "firm" or "FNYS") and Michael Lawrence Friedman ("Friedman") (together "Respondents") submit this Letter of Acceptance, Waiver and Consent ("AWC") for the purpose of proposing a settlement of the alleged rule violations described in Part II below. This AWC is submitted on the condition that, if accepted, NASD will not bring any future actions against the firm and Friedman alleging violations based on the same factual findings.

The Respondents understand that:

1. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by NASD's Department of Market Regulation and the National Adjudicatory Council ("NAC") Review Subcommittee or Office of Disciplinary Affairs, pursuant to NASD Rule 9216;
2. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against Respondents; and
3. If accepted:
 - a. this AWC will become part of Respondents' permanent disciplinary record and may be considered in any future actions brought by the NASD or any other regulator against them;
 - b. this AWC will be made available through NASD's public disclosure program in response to public inquiries about the firm's and Friedman's disciplinary record;
 - c. NASD may make a public announcement concerning this agreement and the subject matter thereof in accordance with NASD Rule 8310 and IM-8310-2; and

- d. Respondents may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or indirectly, any allegation in this AWC or create the impression that the AWC is without factual basis. Nothing in this provision affects Respondents' testimonial obligations or right to take legal or factual positions in litigation or other legal proceedings in which the NASD is not a party.

Respondents also understand that their experience in the securities industry and their respective disciplinary histories may be factors that will be considered in deciding whether to accept this AWC.

FNYS became a member of NASD in 1985, and its registration remains in effect. The firm has no relevant disciplinary history.

Friedman was first registered with NASD in 1968. He has been registered with FNYS since 1985. Friedman has no relevant disciplinary history.

I.

WAIVER OF PROCEDURAL RIGHTS

Respondents specifically and voluntarily waive the following rights granted under the NASD's Code of Procedure:

- A. To have a Formal Complaint issued specifying the allegations against them;
- B. To be notified of the Formal Complaint and have the opportunity to answer the allegations in writing;
- C. To defend against the allegations in a disciplinary hearing before a hearing panel, to have a written record of the hearing made and to have a written decision issued; and
- D. To appeal any such decision to the NAC and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, Respondents specifically and voluntarily waive any right to claim bias or prejudgment of the General Counsel, the NAC, or any member of the NAC, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including acceptance, or rejection of this AWC.

Respondents further specifically and voluntarily waive any right to claim that a person violated the *ex parte* prohibitions of Rule 9143 or the separation of functions prohibitions of Rule 9144,

in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including their acceptance or rejection.

II.

ACCEPTANCE AND CONSENT

This AWC is the result of the following three investigations conducted by the Department of Market Regulation:

- FNYS's trading in the securities of CompuDyne Corporation ("CDCY") from September 28, 2001, to October 31, 2001 (investigation no. 20050002450);
 - FNYS's trading in the securities of Aphton Corporation ("APHT") (May 31 to September 26, 2003), Lynx Therapeutics, Inc. ("LYNX") (February 1 to July 31, 2002), Axonyx, Inc. ("AXYX") (November 1, 2003, to April 30, 2004), and New Century Financial Corporation ("NCEN") (February 1 to May 31, 2002) (investigation no. 20041000028); and
 - FNYS's trading in the securities of Pegasus Communications Corporation ("PGTV") from December 26, 2003, to March 2, 2004 (investigation no. 2004100072).
- A. Respondents hereby accept and consent, without admitting or denying the allegations or findings, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of NASD, or to which NASD is a party, prior to a hearing and without an adjudication of any issue of law or fact, to the entry of the following findings by NASD:

Investigation No. 20050002450 (CompuDyne Corporation)

1. On or about September 28, 2001, a hedge fund manager registered with the firm received material, non-public information about a "PIPE" ("private investment in public equity") offering in CDCY from CDCY's placement agent.
2. On October 8, 2001, the hedge fund manager agreed to invest in the PIPE for a personal account and for the account of a hedge fund affiliated with FNYS. The hedge fund manager submitted two Purchase Agreements agreeing to buy a total of 475,000 shares of CDCY.
3. The morning of October 9, 2001, beginning at 8:22 a.m. and continuing until the PIPE transaction was made public at 11:44 a.m., the hedge fund

manager sold short about 122,900 shares of CDCY while in possession of material, non-public information. This misconduct constituted violations of Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, Sections 17(a)(1) and 17(a)(3) of the Securities Act of 1933, and NASD Conduct Rules 2110 and 2120.

4. From October 9 to October 29, the hedge fund manager sold short for a personal account and for the hedge fund's account about 455,000 shares of CDCY, without borrowing shares and while intending to cover the sales from the 475,000 shares bought in the PIPE. The registration of the CDCY PIPE shares was not declared effective until after the close of trading on October 29, 2001. This misconduct constituted violations of Section 5 of the Securities Act of 1933 and NASD Conduct Rule 2110.
5. The total profits from covering the short positions established by the hedge fund manager for the personal account and for the hedge fund's account were approximately \$1,100,000.
6. From October 9 to October 29, 2001, FNYS failed to detect the hedge fund manager's improper short selling and also failed to detect that FNYS had executed the short sales without making or annotating affirmative determinations that the hedge fund manager and hedge fund could borrow the securities or otherwise provide for delivery of the securities by settlement date. In addition to the violations committed by the hedge fund manager, this conduct constitutes separate and distinct violations by FNYS of NASD Conduct Rules 2110 and 3370.
7. From October 9 to October 29, 2001, FNYS failed to report to the Automated Confirmation Transaction Service the correct symbol indicating that these CDCY sell transactions were short sales. This conduct constitutes separate and distinct violations by FNYS of NASD Marketplace Rule 6130(d).

Investigation No. 2004100028

8. From February 1, 2002 to April 30, 2004, FNYS effected 37 short sales in APHT, AXYX, LYNX, and NCEN for a proprietary account and for a hedge fund customer and failed to make an affirmative determination that the firm and hedge fund could borrow the securities or otherwise provide for delivery of the securities by settlement date. During the same period, FNYS effected 25 short sales in APHT and LYNX for a proprietary account and for a hedge fund customer and failed to annotate an affirmative determination that the firm could borrow the securities or otherwise provide for delivery of the securities by settlement date.

Investigation No. 20041000072 (Pegasus Communications Corporation)

9. From December 26, 2003 to March 2, 2004, FNYS effected three short sales in PGTV for a proprietary account and for a hedge fund customer and failed to make an affirmative determination that the firm and hedge fund could borrow the securities or otherwise provide for delivery of the securities by settlement date. During the same period, FNYS effected three short sales in PGTV for a proprietary account and for a hedge fund customer and failed to annotate an affirmative determination that the firm and such hedge fund could borrow the securities or otherwise provide for delivery of the securities by settlement date.
10. The conduct described in paragraphs eight and nine constitute separate and distinct violations of NASD Conduct Rules 2110 and 3370.

Supervision Violations

11. At all relevant times, Friedman was an FNYS Managing Member and the firm's compliance director. Friedman was responsible for establishing and maintaining a supervisory system and written supervisory procedures reasonably designed to achieve compliance with applicable securities laws and regulations to supervise the types of business that FNYS engages in and to supervise the activities of its registered representatives.
12. Friedman was responsible for supervising the general securities representative and equity traders who were directly responsible for the underlying violations stated herein.
13. The firm's supervisory system failed to provide for adequate and reasonable supervision of the activities of this registered representative and the firm's trading department. The firm's supervisory system and written procedures did not provide for supervision reasonably designed to achieve compliance with respect to NASD Conduct Rules 2110, 2120, 3370, and Marketplace Rule 6130 and to detect violations of Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and Sections 5, 17(a)(1), and 17(a)(3) of the Securities Act of 1933 by its registered representatives. The firm's supervisory system did not include written supervisory procedures providing for: (1) identification of the person responsible for supervision with respect to the applicable rules; (2) a statement of the supervisory steps to be taken by the identified person; (3) a statement as to how often such person should take such steps; and (4) a statement as to how the completion of the steps included in the written supervisory procedures should be documented.

14. The conduct described in paragraph 13 constitutes violations by FNYS and Friedman of NASD Conduct Rules 2110, 3010(a), and 3010(b).

B. Respondents consent to the following sanctions:

1. FNYS consents to the imposition, at a maximum, of the following sanctions:
 - (i) A censure;
 - (ii) a fine of \$100,000; and
 - (ii) The firm also consents to an undertaking to revise its written supervisory procedures with respect to the areas described in Section II.A. Within 30 days of acceptance of this AWC by the NAC, a registered principal of the firm shall submit to the **COMPLIANCE ASSISTANT, LEGAL SECTION, DEPARTMENT OF MARKET REGULATION, 9509 KEY WEST AVENUE, ROCKVILLE, MARYLAND 20850**, a signed, dated letter, providing the following information: (1) a reference to this matter; (2) a representation that the firm has revised its written supervisory procedures to address the deficiencies described in paragraph II.A.; and (3) the date the revised procedures were implemented.
2. Friedman consents to the imposition, at a maximum, of the following sanctions:
 - (i) A censure; and
 - (ii) a fine of \$100,000.

The sanctions imposed herein shall be effective on a date set by NASD.

III.

OTHER MATTERS

- A. Respondents understand that they may attach a Corrective Action Statement to this AWC, which is a statement of demonstrable corrective steps taken to prevent future misconduct. Respondents understand that they may not deny the charges or make any statement that is inconsistent with the AWC in their Statements. The Statements do not constitute factual or legal findings by NASD, nor do they reflect the views of NASD or its staff.

- B. Respondents agree to pay any monetary sanctions imposed on them upon notice that this AWC has been accepted and that such payments are due and payable, and they have attached the Election of Payment forms showing the method by which they propose to pay any fine imposed.
- C. Respondents specifically and voluntarily waive any right to claim that they are unable to pay, now or at any time hereafter, any monetary sanction imposed in this matter.

Respondents certify that they have read and understand all of the provisions of this AWC and have been given a full opportunity to ask questions about it, and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein, has been made to induce Respondents to submit it.

Respondent,
First New York Securities L.L.C.

8-1-06
Date

By: Donald Erenberg

Name: Donald Erenberg

Title: Managing Member

Reviewed by:

Bob P. Lehman
Counsel for First New York Securities L.L.C.

Respondent,

Michael Lawrence Friedman
Michael Lawrence Friedman

8-1-06
Date

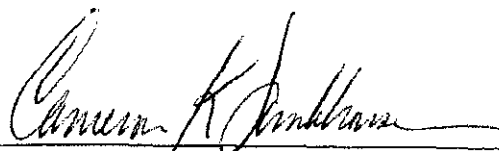
Reviewed by:

Bob P. Lehman
Counsel for Michael Lawrence Friedman

Accepted by NASD:

9/15/06

Date



Cameron K. Funkhouser
Senior Vice President
Department of Market Regulation

Signed on behalf of the Director of ODA,
by delegated authority

Attachments:

Standard Election of Payment Forms for:

- First New York Securities L.L.C. and
- Michael Lawrence Friedman