

FINANCIAL INDUSTRY REGULATORY AUTHORITY

OFFICE OF HEARING OFFICERS

Department of Enforcement,

Complainant,

v.

DISCIPLINARY PROCEEDING NO.
2008011743303

Neftali Mercedes (CRD No. 3201827),

Respondents.

COMPLAINT

The Department of Enforcement alleges:

SUMMARY

1. From September 2007 to December 2009 (the relevant time period), [REDACTED] [REDACTED] or "the Firm") and several individuals associated with the Firm engaged in a host of misconduct involving fraud, anti-money laundering violations, violations in connection with private placement offerings, failure to report customer complaints, and numerous supervisory failures, including inadequate written supervisory procedures.

2. As a result, [REDACTED] violated Section 17(a) of the Securities Exchange Act of 1934, Rules 17a-3 and 17a-4 thereunder, SEC Regulation M, NASD Rules 2110, 2860, 3010, 3011, 3013, 3110, and 3070, and FINRA Rules 2010, 3130 and 5190.
3. [REDACTED] Chief Executive Officer, [REDACTED] violated NASD Rules 2110 and 3013, and FINRA Rules 2010 and 3130.
4. Neftali Mercedes, a registered representative at the Firm, violated Exchange Act Section 10(b), Rule 10b-5 thereunder, NASD Rules 2110 and 2120, and FINRA Rules 2020 and 2010.
5. Most notably, the fraud charge stems from Mercedes making false and/or misleading statements and omissions to customers in connection with a series of private placement offerings of a company called Six Diamond Resorts, International (SDRI).

RESPONDENTS AND JURISDICTION

6. [REDACTED] is a small one-office New York-based broker dealer. It has been a NASD/FINRA member firm continuously since 1987. During the relevant time period, [REDACTED] employed approximately twenty registered representatives.
7. [REDACTED] chief executive officer, first became registered with a FINRA/NASD regulated broker-dealer in 1985. In April 1997, [REDACTED] became associated with [REDACTED] as an investment banker. Two months later, he became [REDACTED] president, an office he has held since that time. During the relevant time period, [REDACTED] held exclusive responsibility for the Firm's investment banking activities, including private placements. [REDACTED] currently holds Series 7, 24, 55 and 63 licenses.

8. Neftali Mercedes was first registered with a FINRA/NASD regulated firm in 1998. From July 2007 until June 2009, Mercedes was registered with [REDACTED] as a registered representative. He was last registered from June 15, 2009 until June 1, 2010 as a registered representative at another FINRA regulated firm and is not currently registered with a FINRA regulated broker-dealer. Mercedes holds Series 7, 24, and 63 licenses. Although Mercedes is no longer registered or associated with a FINRA member, he remains subject to FINRA's jurisdiction for purposes of this proceeding, pursuant to Article V, Section 4 of FINRA's By-Laws, because (1) the Complaint was filed within two years after the effective date of termination of Respondent's last registration with a FINRA regulated firm, namely, June 24, 2010 (the date Form U5 was filed), and (2) the Complaint charges him with misconduct committed while he was registered or associated with a FINRA member.

OTHER ENTITIES

9. SDRI is a Cayman Islands corporation formed in March 2006. In October 2007, SDRI acquired Six Diamond Resorts International, S.A. (SDRISA), a Panamanian company formed seven months earlier for the purpose of engaging in real estate development in the Republic of Panama. SDRI's business became that of SDRISA.

10. UniPixel is a Delaware development stage corporation headquartered in the Houston, Texas area engaged in the development of "flexible printed electronics" as well as optical and energy efficiency, fingerprint resistant films. Its stock trades on the NASDAQ. In 2005, and again in 2009, [REDACTED] conducted private placement offerings on UNXL's behalf.

THE FACTS

Mercedes Made False and Misleading Statements and Omissions to Prospective Investors in Connection with Private Placement Offerings in the Securities of Six Diamond Resorts International Underwritten by [REDACTED]

11. From August 2008 through April 2009, Mercedes recommended and sold private placement interests in SDRI to at least three customers. During this time, Mercedes relayed information about SDRI's business operations, the status of its construction projects, financial condition, and investment potential to his customers. Mercedes knew or was reckless in not knowing that this information was false or exaggerated. Mercedes also failed to inform a customer of material facts about SDRI, including a previous default on debts to investors.

12. According to an April 2007 Private Placement Memorandum that [REDACTED] distributed to its customers, SDRI's business plan was to develop real estate for tourism and retirement destinations in Panama. The April 2007 private placement generated over \$9.9 million for SDRI. By August 2008, however, SDRI had not broken ground on any construction projects and was seeking additional financing.

13. From August through October 2008, in an attempt to raise additional capital for SDRI, [REDACTED] offered investors an opportunity to invest in a bridge loan (the "First Bridge Loan") through another private placement that was to be repaid in April 2009 with 8% interest. Approximately fifty [REDACTED] customers invested over \$2.2 million in this First Bridge Loan. Mercedes made the following material misrepresentations to customers when recommending this investment:

- Mercedes recommended this First Bridge Loan to customer TLE, telling him that a majority of the condominium units had been pre-sold to a British soccer team and that SDRI was going public “very soon.” TLE invested \$25,000 in August 2008.
- Mercedes also recommended this First Bridge Loan to customer TG, telling him that the SDRI “bond deal” had no risk whatsoever. Mercedes also encouraged TG to make the investment notwithstanding the fact that TG told Mercedes that he could not afford the investment and would have to take out a loan to cover it. TG invested \$22,500 in August 2008.

14. At the time Mercedes made these statements to the above customers, SDRI had not broken ground on any construction projects. In fact, Mercedes had visited the SDRI property in Panama during the late summer/early autumn of 2007 and described it as nothing more than a “raw plot of land.” Mercedes did not have an adequate basis for making these statements to his customers.

15. As of January 2009, SDRI still had not broken ground on any construction projects but was again seeking additional financing. That month, an additional bridge loan was executed between SDRI and three [REDACTED] customers, raising approximately \$200,000 for SDRI. This “Second Bridge Loan” was payable in April 2009 at 8% interest and purported to be subordinate to the rights of the First Bridge Loan investors. One of the three investors in this Second Bridge Loan was also an investor in the holding company owning [REDACTED]

16. Beginning in February 2009, [REDACTED] offered yet another bridge loan for SDRI. Approximately seventeen [REDACTED] customers participated, investing over \$780,000 in exchange for promissory notes offering 8% interest and payable by December 31, 2009, plus “bonus” payments equal to 50% of the investment (25% of which would be payable in March 2010 and

the other 25% in June 2010). One of the stated purposes of this “Third Bridge Loan” was to repay the note holders from the Second Bridge Loan, despite its supposed subordinated nature.

17. In April 2009, when recommending that his customer LS invest in this Third Bridge Loan, Mercedes made material misrepresentations to him. Mercedes told LS that the Third Bridge Loan was a “bond deal” with no risk, assuring LS that his capital would be completely safe. Mercedes also told LS that SDRI was breaking ground on an 18-hole golf course and that SDRI had successfully developed other properties. This statement was completely at odds with what Mercedes had seen for himself during his visit to Panama in late 2007. At the time, Mercedes made this statement to LS about the 18-hole golf course, SDRI still had not broken ground on any construction project and, more important, it was in default on the First Bridge Loan notes. Not only did Mercedes tell LS that a golf course was being constructed, he also failed to tell LS a very important fact: None of the First Bridge Loan investors had been repaid. LS invested \$50,000 in the Third Bridge Loan in April 2009.

18. TLE, TG, and LS have not received any money back from their SDRI investments. In fact, none of the approximately sixty-seven investors who participated in the First or Third Bridge Loans have received any money back. Mercedes realized \$59,590 in gross commissions from his customers’ SDRI private placement investments.

19. Throughout this period, Mercedes did not attempt in any way to verify the information about SDRI he was conveying to his customers.

██████ Fails to File Restricted Period Notification in Connection with, and Fails to Restrict Trading of UniPixel Stock during, a Private Placement of UniPixel Securities

20. On or about April 30, 2009, ██████ commenced a private placement offering on behalf of UNXL. This was a best efforts private placement of up to 80 units, each consisting of a \$50,000 convertible promissory note and warrants to purchase 25,000 of UNXL common stock. From April 30, 2009 through July 9, 2009, ██████ raised approximately \$650,000 in this offering. ██████ however, failed to file a Restricted Period Notification, as required under FINRA Rule 5190, in connection with this offering. Moreover, ██████ failed to restrict its trading of UNXL and/or its solicitation of orders in the company's securities during the Regulation M period associated with this offering. As a result of this failure, ██████ through its agents and employees, improperly solicited nineteen customer purchases during the Regulation M period. In addition, one ██████ registered representative improperly made two purchases of UNXL stock for his own account during the Regulation M period.

21. The ██████ registered representatives who made the above described twenty one trades were unaware that solicitation in UNXL was not permitted, because they were never informed that the security was subject to restriction. ██████ had not placed UNXL on its restricted list.

22. During the period from April 30, 2009 through July 9, 2009, ██████ accounted for more than 56% of the total trading volume in UNXL stock.

██████ Fails to Record Time of Order Receipt

23. From January 2008 through December 2009, despite the existence of a field to capture this information in the firm's electronic trading system, ██████ failed to record the time of receipt of customer orders.

██████ Fails to Timely Report Customer Complaints

24. ██████ failed to timely report to FINRA, or failed to report at all, eleven customer complaints, in violation of NASD Rule 3070(c), as specified below:

Complaint Date	Date ██████ Reported to FINRA	Customer	Substance of Complaint
1/4/08	4/8/09	SH	<i>Unauthorized use of margin</i>
1/22/08	4/15/09	SL	<i>Unauthorized transactions</i>
2/12/08	4/8/09	MH	<i>Improper handling of account</i>
5/28/08	10/15/08	KF	<i>Unauthorized trades/excessive commissions</i>
4/24/08	7/21/09	SSK	<i>Unauthorized trades</i>
7/14/08	10/26/09	EF	<i>Unauthorized trades</i>
10/30/08	Never reported	DB	<i>Unauthorized trades</i>
10/30/08	4/8/09	GH	<i>Unauthorized use of margin</i>
11/22/08	4/8/09	EL	<i>Unauthorized trades</i>
11/25/08	9/23/09	AG	<i>Failure to record transactions/post dating</i>
2/24/09	7/22/09	SOK	<i>Unauthorized trades</i>

██████ Fails to Retain Customer Option Account Agreements

25. During the relevant time period, out of twenty three accounts the FINRA examination staff sampled, ██████ improperly permitted options trading in two customer accounts, failed to retain option agreements in two more, and failed to obtain essential information on the Client Option Agreement for another two customers.

26. Specifically, ██████ permitted options trading in two customer accounts (those of customers AF and JH) before an options account agreement was in place and before the account could be approved for options trading. On June 9, 2008, customer AF covered a short position of 150 Syntax Brilliant Corp. puts and a second short position of 50 Syntax Brilliant Corp. puts. Yet AF's account was not approved to trade options until June 29, 2009, more than a year after these options transactions had already occurred. Similarly, on March 24, 2009 customer JH purchased 50 Citigroup Inc. calls. On April 14, 2009, JH sold 50 Calls Citigroup Inc. But JH's account was not approved to trade options until nearly a month after the purchase, on April 20, 2009.

27. ██████ also failed to retain completed copies of customer Client Option Agreements and to obtain essential information contained on Client Option Agreements. Specifically, ██████ failed to retain Client Option Agreements for two customer accounts (customers EL and SS), both of whom traded options. ██████ also failed to obtain essential information within the Client Option Agreement for customers RB and CL, both of whom traded options as well. Customer RB's Option Agreement did not contain his employment status, age, marital status, number of dependents, and a date upon which the customer received the required Options Risk/Disclosure Document. CL's Option Agreement did not reflect his employment status,

options investment objective, and a date upon which the customer received the required Options Risk/Disclosure Document.

28. Those remaining facts relating to the Causes of Action alleged herein are included below.

FIRST CAUSE OF ACTION

Making and Causing to be Made False and Misleading Statements in Connection with the Sale of Private Placements (Securities Exchange Act of 1934, Section 10(b), Rule 10b-5 thereunder, NASD Rules 2120 & 2110, and FINRA Rules 2020 & 2010) (Mercedes)

29. Paragraphs 1 through 28 are re-alleged and incorporated herein by reference.

30. Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and NASD Rule 2120 (the antifraud rules) collectively proscribe fraudulent conduct in connection with the purchase or sale of securities. Mercedes violated these antifraud rules by making false and misleading statements and omitted material facts in connection with the sale of SDRI private placements between August 2008 and April 2009.

31. Those misstatements and omissions were material in that they concerned facts such as the timing and amount of repayments and interest payments to investors, the progress of SDRI's underlying development projects, the ability of SDRI to cover its expenses, and the ability of SDRI to pay previous investors. In sum, Mercedes knowingly or recklessly made material misrepresentations and omissions to investors regarding the true financial condition of SDRI and its progress.

32. Specifically, Mercedes falsely told customer TLE that almost all of the SDRI condominium units had already been pre-sold, that an English soccer team had purchased a majority of those units, and that SDRI was going public within a matter of months. Mercedes

lacked an adequate basis to support any of these statements, nor did he seek any. Mercedes also falsely told customer LS that SDRI was breaking ground on an 18 hole golf course and that SDRI had successfully developed other properties. Again, Mercedes lacked an adequate factual basis for making any of the aforementioned statements. Moreover, his own experience visiting the site directly contradicted what he was telling his customers. Each of these statements was false and/or without basis. Moreover, the information he conveyed was material to his customers in deciding whether or not to invest in SDRI.

33. Similarly, Mercedes made material misrepresentations concerning the safety of the investment, completely minimizing any risk involved and touting the SDRI notes as a safe “bond deal.” Mercedes represented to customers TLE, LS, and TG that there was “no risk whatsoever,” referring to the SDRI investments as a “slam dunk,” and “no brainer.” At the time Mercedes made these representations, SDRI had not generated any profits, had not repaid any of its debts, and had sought to raise capital several times in order just to meet everyday expenses. Mercedes was aware of these facts, which were material in nature.

34. None of the aforementioned statements were true or had any basis in fact, and it was at least reckless of Mercedes to make them in connection with the sale of the SDRI private placement investments.

35. Mercedes also failed to inform customer LS that SDRI had not repaid previous bridge loans, and that the holders of the First Bridge Loan had not been repaid. These were facts a reasonable investor would have wanted to know before deciding to invest in SDRI’s Third Bridge Loan.

36. A number of Mercedes' had invested in the First Bridge Loan and had not been repaid in a timely fashion. Therefore, he knew or recklessly disregarded evidence of SDRI's failure to meet its existing debt obligations.

37. Accordingly, Mercedes was at least reckless in failing to convey this information to LS.

38. During the course of conduct described above, Mercedes, in connection with the purchase or sale of securities, directly or indirectly, by the use of the means or instrumentalities of interstate commerce, or of the mails, or of any facility of any national securities exchange, knowingly or recklessly: employed devices, schemes, or artifices to defraud; engaged in acts, practices, or courses of business which operated or would operate as a fraud or deceit upon any person; and/or effected transactions in, or induced the purchase or sale of, any security by means of any manipulative, deceptive, or other fraudulent device or contrivance.

39. By virtue of the foregoing, with regard to those statements and omissions made before December 15, 2008, Mercedes willfully violated § 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and NASD Rules 2120 and 2110. With regard to the statements and omissions made on or after December 15, 2008, Mercedes willfully violated § 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010.

SECOND CAUSE OF ACTION

(IN THE ALTERNATIVE)

Failure to Observe High Standards of Commercial Honor and Just and Equitable Principles of Trade (Negligent Misrepresentations and Omissions in Connection with the Sale of Private Placements) -- NASD Rule 2110 and FINRA Rule 2010 (Mercedes)

40. Paragraphs 1 through 28 are re-alleged and incorporated herein by reference.

41. NASD Rule 2110, and on or after December 15, 2008, FINRA Rule 2010, requires members, in the conduct of their business, to observe high standards of commercial honor and just and equitable principles of trade. As specified above, in paragraphs 11 through 19, 32, 33, 35, and 36, from August 2008 to April 2009, Mercedes negligently made material misstatements and/or omitted material facts in connection with the offer and sale of private placement units in SDRI to investors. Those misstatements and omissions concerned material facts for investors, namely, the progress of the underlying SDRI business projects, the safety of the investment, and the ability of SDRI to pay previous investors. In so doing, Mercedes was negligent and violated his obligation to observe high standards of commercial honor and just and equitable principles of trade.

42. Those acts, practices, and conduct by Mercedes alleged above occurring before December 15, 2008 constitute violations of NASD Rule 2110. Those occurring on or after December 15, 2008, constitute violations of FINRA Rule 2010.

THIRD CAUSE OF ACTION

Failure to Restrict Trading of UniPixel Securities during Private Placement and Failure to File Notification of Offering (SEC Regulation M, Rule 101 and FINRA Rules 5190 and 2010)

██████████

43. Paragraphs 1 through 42 of this Complaint are re-alleged and incorporated herein by reference.

44. FINRA Rule 5190(c)(1) requires that a member firm acting as a manager of a distribution of any security covered by, and subject to a restricted period under, SEC Regulation M, Rule 101 must provide FINRA with the written notice described in subparagraph (A). This notice is called a Regulation M Restricted Period Notification Form. ██████████ filed no such form in connection

with the private placement offering it commenced on April 30, 2009 on behalf of UNXL. This offering was a distribution within the meaning of SEC Regulation M, Rule 100, 17 C.F.R. § 242.100. Therefore, it was subject to the requirements of the regulation and of FINRA Rule 5190(c).

45. Under SEC Regulation M, Rule 101, 17 C.F.R. § 242.101, a distribution participant (defined in Regulation M, Rule 100 to include an underwriter, broker-dealer, or other person participating, or who has agreed to participate, in a distribution) must restrict its trading of securities in the issuer and/or its solicitation of orders in the issuer's securities during the appropriate Regulation M restricted period associated with that offering. Under Regulation M, Rule 100, for any security with an average daily trading value of less than 100,000 and whose public float is less than \$25,000,000, the restricted period begins on the later of five business days prior to the determination of the offering price or such time that a person becomes a distribution participant and ends upon completion of participation in the distribution.

46. UNXL's average daily trading volume and the value of its public float, as those terms are defined in Regulation M, Rule 100, was just over \$15,000 and approximately \$9.6 million, respectively. The offering price was determined after the close of business on April 30, 2009. Accordingly, the Regulation M period for the UNXL offering began on April 24, 2009, and [REDACTED] should have restricted its trading in UNXL and the solicitation of trades in that company's securities beginning on that date. It did not.

47. As a result, between April 24, 2009 and July 9, 2009, when the offering was cancelled following discovery by [REDACTED] outside counsel of the firm's failure to file the Restricted Period Notification Form, [REDACTED] through its agents and employees, improperly solicited

nineteen customer purchases, and a [REDACTED] registered representative improperly made two purchases of UniPixel stock for his own account.

48. By means of the above conduct, [REDACTED] willfully violated SEC Regulation M, Rule 101, and FINRA Rules 5190(c)(1)(A) & 2010.

FOURTH CAUSE OF ACTION

Failure to Record Time of Order Receipt (Securities Exchange Act of 1934, Section 17(a), Rules 17a-3 and 17a-4 thereunder, NASD Rules 3110 and 2110, and FINRA Rule 2010)

[REDACTED]

49. Paragraphs 1 through 48 are re-alleged and incorporated herein by reference.

50. NASD Rule 3110(a) requires member firms to “make and preserve books, accounts, records, memoranda, and correspondence in conformity with all applicable laws, rules, regulations, and statements of policy promulgated thereunder and with the Rules of this Association and as prescribed by the Securities Exchange Act of 1934, Rule 17a-3.” In turn, Exchange Act Rule 17a-3 requires member firms to make and keep, among other things, “[a] memorandum of each brokerage order, and of any other instructions, given or received for the purchase or sale of securities.” That memorandum must show, among other things, “the time the order was received.”

51. By virtue of the Firm’s failure to capture the times of its receipt of customer orders, for those failures occurring before December 15, 2008, [REDACTED] willfully violated Exchange Act 17(a), Rules 17a-3 & 17a-4 thereunder, and NASD Rules 3110(a) and 2110 by failing to record the time of receipt for its customer orders. For those failures occurring on or after December 15, 2008, [REDACTED] willfully violated Exchange Act 17(a), Rules 17a-3 & 17a-4 thereunder, NASD Rule 3110(a), and FINRA Rule 2010.

FIFTH CAUSE OF ACTION

Failure to Establish and Implement Customer Identification Program (NASD Rules 3011 and 2110)

██████████

52. Paragraphs 1 through 51 are re-alleged and incorporated herein by reference.

53. As ██████████ anti-money laundering compliance officer, PH, and later Christopher Mattei,¹ was responsible for the implementation of the Firm's anti-money laundering (AML) compliance program. NASD Rule 3011(b) provides that firms must establish and implement policies and procedures and internal controls reasonably designed to achieve compliance with the Bank Secrecy Act (31 U.S.C. 5311 et seq.) and the implementing regulations thereunder. As implemented by PH and Mattei, ██████████ AML policies, procedures, and internal controls were not reasonably designed to achieve compliance with the Bank Secrecy Act (BSA) and its implementing regulations.

54. Under 31 C.F.R. 103.122, FINRA member firms are required to have risk-based Customer Identification Programs (CIPs) that provide reasonable assurance that they know the true identity of each of their customers. They are also required to document the method and results of verification. Between September 2007 and September 2008, ██████████ failed to do this. Specifically, between September 2007 and March 2008, PH was responsible for approving the opening of new accounts and for verifying and documenting customer identification information required by 31 C.F.R. 103.122 and the BSA. Mattei had the same responsibilities from March 2008 to February 2009. Through their failure to adequately implement ██████████ CIP, ██████████

¹ As a result of a FINRA disciplinary action relating in part to his conduct while he was associated with ██████████ on July 5, 2011, Mr. Mattei was permanently barred from associating with a FINRA regulated firm.

violated NASD Rule 3011(b) by failing to establish and implement a CIP that satisfied rule requirements.

55. ██████ CIP, dated August 13, 2007, required the use of documentary and/or non-documentary means to verify the identity of its customers. Non-documentary identification was required in addition to documentary verification where there was no face-to-face contact between the Firm and the customer. In practice, this meant that non-documentary verification was required in virtually all cases, because customers did not come to ██████ offices to open accounts. Further, ██████ CIP required documentation of the verification of each customer's identity, including descriptions of any non-documentary measures taken.

56. Between September 2007 and September 2008, ██████ failed to adequately implement its CIP in that it failed to document that it a) had obtained certain required pieces of information to verify the customer's identity in five of fifty one accounts sampled by FINRA's examination staff, b) had performed any verification of the customer's identity at all in sixteen of fifty one accounts sampled, and c) had performed the required non-documentary verification for twenty eight accounts. In all, forty nine of the fifty one accounts sampled by FINRA's examination staff demonstrated a deficiency in the documentation of ██████ verification of the customer's identity.

57. Based on the foregoing, ██████ violated NASD Rules 3011(b) and 2110 by failing to implement policies, procedures, and internal controls reasonably designed to achieve compliance with the BSA and the implementing regulations thereunder.

SIXTH CAUSE OF ACTION

Failure to Develop and Implement Procedures Designed to Ensure Independent Testing (NASD Rules 3011 and 2110 and FINRA Rule 2010)

██████████

58. Paragraphs 1 through 57 are re-alleged and incorporated herein by reference.

59. Under NASD Rule 3011, each member firm must “develop and implement a written anti-money laundering program reasonably designed to achieve and monitor the member’s compliance with the requirements of the [BSA], and the implementing regulations promulgated thereunder by the Department of the Treasury.” At a minimum, such programs must, among other things, according to Rule 3011(c), “[p]rovide for annual ... independent testing for compliance” with its AML obligations.

60. From January 2007 to May 2009, ██████████ failed to provide for annual independent testing complying with these obligations.

61. Specifically, ██████████ 2007, 2008, and 2009 independent AML tests were inadequate for three reasons: First, as set forth in the Reports of that testing, they were limited in scope to those areas of “primary responsibility” for detecting money laundering, rather than the full AML program. Second, in January 2007, the test was conducted by ██████████ chief financial officer, RA, who was not independent, as he was responsible for reviewing operational aspects of the Firm’s business, including the receipt and disbursement of customer funds and securities. Third, in July 2007, January 31, 2008 and March 12, 2009, the tests were conducted by JP, a firm vice president who was not independent, experienced, or trained in AML. Moreover, JP’s testing consisted of a general review without a specific review period, specific instructions, or provisions for follow-up to ensure that recommendations would be implemented. Further, at the

time of JP's testing, the Firm's Written Supervisory Procedures continued to show that RA was designated to perform the independent AML testing.

62. As a result of the foregoing, █████ failed to establish and enforce an adequate AML Compliance Program, in violation of NASD Rules 3011(c) and 2110 (for conduct prior to December 15, 2008) and NASD Rule 3011(c) and FINRA Rule 2010 (for conduct on or after December 15, 2008).

SEVENTH CAUSE OF ACTION

Failure to Report Customer Complaints (NASD Rules 3070 and 2110, and FINRA Rule 2010)

█████

63 Paragraphs 1 through 63 are re-alleged and incorporated herein by reference.

64 NASD Rule 3070(c) requires each member firm to report to FINRA customer complaints no later than the fifteenth day following the end of the calendar quarter in which those complaints are received by the member.

65. By virtue of the foregoing failures to report customer complaints occurring before December 15, 2008, █████ violated NASD Rules 3070(c) and 2110. For those failures occurring on or after December 15, 2008, █████ violated NASD Rule 3070(c) and FINRA Rule 2010.

EIGHTH CAUSE OF ACTION

Failure to Retain Customer Option Agreements (NASD Rules 2860, 3110, & 2110, and FINRA Rule 2010)

█████

66. Paragraphs 1 through 65 are re-alleged and incorporated herein by reference.

67. NASD Rule 3110(a) requires firms to make and preserve certain books and records in accordance with NASD Rules and the federal securities laws. NASD Rule 2860(b)(16)(D) requires that, within fifteen days after a customer has been approved for options trading, a firm “obtain from the customer a written agreement that the customer is aware of and agrees to be bound by the Rules of the Association applicable to the trading of options contracts and, if he desires to engage in transactions in options issued by the Options Clearing Corporation, that the customer has received a copy of the current disclosure document(s) required to be furnished ... and that he is aware of and agrees to be bound by the rules of the Options Clearing Corporation.”

68. Moreover, Rule 2860(b)(16)(A) requires that no member shall accept an order from a customer to purchase or write an option contract or approve the customer’s account for trading options unless the customer has been furnished the appropriate options disclosure documents and the customer’s account has been approved for options trading. Rule 2860(b)(16)(B) requires that a member shall exercise due diligence to ascertain the essential facts relative to the customer, his financial situation, and investment objectives. That Rule also states that members shall seek to obtain information, including but not limited to, employment status, investment objectives, marital status, number of dependents, and age.

69 By virtue of the Firm’s failures with respect to its Option Account Agreements described above, for that conduct occurring before December 15, 2008, ████████ violated NASD Rules 2860(b)(16), 3110(a), and 2110. For that conduct occurring on or after December 15, 2008, ████████ violated NASD Rules 2860(b)(16), 3110(a), and FINRA Rule 2010.

NINTH CAUSE OF ACTION

Failure to Maintain a System to Supervise and Failure to Establish, Maintain, and Enforce Written Supervisory Procedures (NASD Rules 3010 and 2110 and FINRA Rule 2010)

██████████

70. Paragraphs 1 through 69 are re-alleged and incorporated herein by reference.

71. During the period from September 2007 through July 2009, ██████████ violated NASD Rules 3010 and 2110 and FINRA Rule 2010 in three ways.

██████████ Fails to Establish, Maintain, and Enforce Written Supervisory Procedures Addressing SEC Regulation M and FINRA Rule 5190.

72. First, NASD Rule 3010(b) requires each NASD/FINRA registered firm to

establish, maintain, and enforce written procedures to supervise the types of business in which it engages and to supervise the activities of registered representatives, registered principals, and other associated persons that are reasonably designed to achieve compliance with applicable securities laws and regulations, and with the applicable Rules of [NASD/FINRA].

73. During the period of January through July 2009, ██████████ failed to establish, maintain, and enforce written supervisory procedures (WSPs) reasonably designed to achieve compliance with SEC Regulation M, Rules 100 through 105 and FINRA Rule 5190.

74. While ██████████ WSPs in effect between January 1, 2009 and July 12, 2009 addressed SEC Regulation M, Rules 100 through 105, they failed to mention FINRA Rule 5190. They also contained no procedures to monitor for violations of Regulation M, Rule 101. ██████████ procedures contained no means of ensuring that registered representatives and/or traders were informed of a restriction due to an issue being subject to a Regulation M restricted period, and they were deficient with respect to adding securities to the firm's restricted list.

75. ████████ WSPs failed to provide 1) reasonable written standards or criteria for placing a security on and deleting it from such lists, 2) that that documentation must include the date and time the security was added to or deleted from the list, and 3) the name of each contact person who was responsible for the addition or deletion and can answer questions regarding the timing and circumstances surrounding the addition or deletion.

76. The deficiencies in ████████ WSPs outlined above contributed to the firm's violations of SEC Regulation M, Rule 101, and FINRA Rule 5190. They also helped cause the firm's failure to inform its registered representatives of the restriction associated with UNXL stock and its failure even to place UNXL on its restricted list. This failure led directly to the violations of Regulation M, Rule 101, violations for which the procedures provided no means of detecting.

77. By failing to establish, maintain, and enforce written supervisory procedures reasonably designed to achieve compliance with SEC Regulation M, Rule 101 and FINRA Rule 5190(c), ████████ violated NASD Rule 3010(b) and FINRA Rule 2010.

████████ Fails to Enforce Written Supervisory Procedures to Supervise its Registered Representatives (failure to conduct transaction reviews)

78. Second, NASD Rule 3010(d)(1) requires FINRA regulated firms to establish written supervisory procedures for the review and endorsement by a registered principal, in a written internal record, of all transactions. Such procedures must be "designed to reasonably supervise each registered representative." Moreover, firms must maintain evidence that these supervisory procedures have been implemented.

79. ████████ WSPs provided for, among other things, daily review of all order tickets by a designated principal. Moreover, the Firm's procedures also called for a review by a designated

principal of random customer monthly account statements (selected in a manner so that all accounts were reviewed semi-annually). In accordance with Rule 3010(d), the procedures also required written documentation of all reviews undertaken to be maintained that indicated (as appropriate) the scope of the review, the individual conducting the review, the findings of the review, any remedial actions undertaken following the review, and any other relevant information relating to the review. From October 2007 through February 2008, [REDACTED] failed to implement these procedures.

80. Beginning in or about August 2007, [REDACTED] Chief Compliance Officer (CCO) PH ceded her daily review of all transactions to RA. RA, however, did not hold a Series 24 license and was not a registered principal of the Firm. Accordingly, from October 2007 through February 2008, when Mattei took over the position and duties of CCO from PH, the daily trading reviews required under [REDACTED] WSPs were being conducted by a person not legally qualified to conduct them.

81. Moreover, between October 2007 and February 2008, PH failed to conduct the account statement reviews required by the Firm's procedures. Instead, she chose to review commission runs on a monthly basis. Nor were the required account statement reviews conducted by anyone else during that time.

82. Further, aside from notations on a few paper order tickets when the vast majority of [REDACTED] orders were entered electronically, and contrary to both the Firm's procedures and Rule 3010(d), [REDACTED] kept no records or other evidence of any of the reviews required under those procedures.

83. As a result of the foregoing, for those violations occurring before December 15, 2008, [REDACTED] violated NASD Rules 3010(b) and 3010(d), as well as 2110. For those violations occurring on or after December 15, 2008, [REDACTED] violated NASD Rules 3010(b) and 3010(d), as well as FINRA Rule 2010.

[REDACTED] Fails to Enforce Written Supervisory Procedures to Supervise its Registered Representatives (failure to establish and enforce heightened supervision)

84. Third, in its October 4, 2007 and December 14, 2007 WSPs, [REDACTED] set forth that “[h]eightedened supervisory procedures will be put into place to monitor and supervise the activities of (a) Registered Representatives with an egregious history of customer complaints, disciplinary actions and/or arbitrations.” Those WSPs further stated that “[e]vidence of all special supervision will be retained.”

85. On October 30, 2007, [REDACTED] placed registered representative JC on heightened supervision for six months to address sales practice concerns. The parameters and requirements of this heightened supervision were expressly set forth in a heightened supervision agreement signed by JC, [REDACTED] PH, and CG. Among other things, the heightened supervision agreement provided that if JC were the subject of a customer complaint during the six month time period that had begun on October 30, 2007, then [REDACTED] heightened supervision of JC would be extended for an additional six months from the date of that complaint. During that six month period, JC received four customer complaints, three of which alleged that he had engaged in unauthorized trading. Yet [REDACTED] failed to extend its heightened supervision of JC.

86. [REDACTED] also failed to establish a heightened supervision plan for registered representative CMS, who had an extensive history of regulatory actions and customer

complaints. When CMS became registered with [REDACTED] in September 2007, he had been the subject of a regulatory action for unauthorized trading, and he had been terminated for cause from two FINRA-regulated firms and involuntarily terminated from two others. He was also the subject of three outstanding customer complaints and had been the subject of numerous complaints for unauthorized trading and other sales practice violations in the past. He had also recently worked for a firm that had been expelled from FINRA membership for sales practice violations. Despite all these factors necessitating heightened supervision of CMS, [REDACTED] failed to implement such supervision of him.

87. By failing to adhere to the heightened supervision agreement it had entered into with JC and by failing to establish a heightened supervision plan for CMS, [REDACTED] failed to enforce WSPs reasonably designed to supervise the activities of its registered representatives.

88. As a result of the foregoing, [REDACTED] violated NASD Rules 3010(b) and 3010(d), as well as NASD Rule 2110.

TENTH CAUSE OF ACTION

Failure to Complete Chief Executive Officer Certifications (NASD Rules 3013 and 2110, and FINRA Rules 3130 and 2010)

[REDACTED] and [REDACTED]

89. Paragraphs 1 through 87 are re-alleged and incorporated herein by reference.

90. NASD Rule 3013(b) and FINRA Rule 3130(b) provide that

[e]ach member shall have its chief executive officer(s) . . . certify annually . . . that the member has in place processes to establish, maintain, review, test, and modify written compliance policies and written supervisory procedures reasonably designed to achieve compliance with applicable FINRA rules, MSRB rules, and federal securities laws and regulations, and that the chief executive

officer(s) has conducted one or more meetings with the chief compliance officer(s) in the preceding 12 months to discuss such processes.

91. As [REDACTED] chief executive officer during the relevant time period, [REDACTED] was required to sign such certifications on behalf of [REDACTED]. [REDACTED] failed to sign such certifications for the years 2008 and 2009.

92. By virtue of the foregoing, for those failures occurring before December 15, 2008, [REDACTED] and [REDACTED] violated NASD Rules 3013(b) and 2110 by failing to certify [REDACTED] written compliance policies and written supervisory procedures. For those failures occurring on or after December 15, 2008, [REDACTED] and [REDACTED] violated FINRA Rules 3130(b) and 2010.

RELIEF REQUESTED

WHEREFORE, the Department respectfully requests that the Panel:

- A. Order that one or more of the sanctions provided under FINRA Rule 8310(a), including monetary sanctions, be imposed against all Respondents;
- B. Order that the Respondents bear such costs of proceeding as are deemed fair and appropriate under the circumstances in accordance with FINRA Rule 8330;
- C. Make specific findings that the Respondents committed each of the violations alleged in the Complaint;
- D. Make specific findings that Mercedes willfully violated Exchange Act Section 10(b) and Rule 10b-5 thereunder, and that [REDACTED] willfully violated Exchange

Act Section 17(a), Rules 17a-3 and 17a-4 thereunder, and SEC Regulation M,
Rule 101; and,

E. Impose any other fitting sanction.

FINRA DEPARTMENT OF ENFORCEMENT

Date: May 31, 2012



R. W. Sardegna
Senior Litigation Counsel
Frank D. Mazzarelli
Senior Counsel
FINRA Department of Enforcement
15200 Omega Dr.
Suite 300
Rockville, MD 20850
Phone: (301) 258-8576 (Sardegna)
Fax: (202) 721-6578 (Sardegna)
e-mail: robin.sardegna@finra.org