BEFORE THE NATIONAL ADJUDICATORY COUNCIL

FINANCIAL INDUSTRY REGULATORY AUTHORITY

In the Matter of Department of Enforcement, Complainant, vs. Anthony A. Grey Winter Park, FL, Respondent.	DECISION Complaint No. 2009016034101 Dated: October 3, 2014

Registered representative willfully engaged in undisclosed interpositioning, charged customers unfair prices and excessive mark-ups, and engaged in fraud. Held, findings affirmed and sanctions modified.

Appearances

For the Complainant: Michael A. Gross, Esq., Department of Enforcement, Financial Industry Regulatory Authority

For the Respondent: Peter J. Aldrich, Esq.

Decision

Pursuant to FINRA Rule 9311, Anthony A. Grey ("Grey") appeals a June 20, 2013 Hearing Panel decision. The Hearing Panel found that, in 10 municipal bond transactions, Grey violated MSRB Rule G-17 by interpositioning and failing to disclose his deceptive and unfair practice, MSRB Rule G-30 by charging unfair prices and excessive mark-ups, and Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") by charging fraudulently excessive mark-ups (ranging from 8.62% to 19.12%) that he willfully failed to disclose to retail customers.[1] The Hearing Panel fined Grey $30,000, suspended him from associating with any FINRA member firm in any capacity for two years, and ordered him to pay $16,000 in disgorgement. The Hearing Panel also found Grey's misconduct to be willful, which caused

[1] The conduct rules that apply in this case are those that existed at the time of the conduct at issue.

him to be statutorily disqualified. After an independent review of the record, we affirm the Hearing Panel's findings of violation, but modify the sanctions it imposed.

I. Background

Grey entered the securities industry in May 1980. During the relevant period, Grey was a registered general securities representative with Gardnyr Michael Capital, Inc. ("GMCI"). While employed with GMCI, Grey had two personal accounts that are at issue in this matter—a personal prime brokerage account with Triad Securities Corporation and an IRA account with GMCI that he routinely utilized to buy and sell municipal bond securities. Grey voluntarily ended his employment with GMCI on October 25, 2012, and is no longer associated with a FINRA member firm.

II. Procedural History

In December 2011, the Department of Enforcement ("Enforcement") filed a six-cause complaint against Grey and three other respondents—three causes of action remain at issue in this case.[2] Cause one alleged that, in 10 municipal bond transactions, Grey intentionally or recklessly charged unfair, unreasonable, and excessive mark-ups, and in some transactions, fraudulently excessive mark-ups; interposed an account maintained and controlled by him between the firm's customers and the prevailing market price in the bond transactions; and failed to disclose his interpositioning and the excessive mark-ups in violation of the fair-dealing requirement of MSRB Rule G-17, the fair pricing requirement of MSRB Rule G-30, Exchange Act Section 10(b), and Exchange Act Rule 10b-5. Cause two separately alleged that Grey intentionally and willfully charged unfair, unreasonable, and excessive mark-ups that he failed to disclose to customers in violation of MSRB Rules G-17 and G-30. Cause three alleged that Grey interposed his personal account that he maintained and controlled between the firm's customers and the prevailing market price and failed to disclose his interpositioning in violation of MSRB G-17.[3]

A two-day hearing took place in Boca Raton, Florida in February 2013. The Hearing Panel rendered a decision in June 2013 making the findings and imposing the sanctions as described above. This appeal followed.

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[2] Enforcement's complaint alleged violations against Grey, GMCI, and two other general securities representatives. In December 2012, FINRA entered into an offer of settlement with the other respondents. Thus, the findings set forth in this decision solely pertain to Enforcement's claims against Grey.

[3] We affirm the Hearing Panel's findings, including the mark-ups charged in seven of the transactions that Enforcement found to be fraudulently excessive in violation of Exchange Act Section 10(b) and Exchange Act Rule 10b-5, and discuss Grey's misconduct and the applicable violations to avoid the duplication of addressing each cause of action.

III. Interpositioning, Mark-ups, and Fraud

A. Facts

A routine FINRA cycle examination found that, between October 2008 and July 2009, Grey conducted 99% of GMCI's municipal bond business. During this time, Grey routinely engaged in a pattern of routing municipal bonds through his personal account before selling the bonds to GMCI's customers. In the 10 municipal bond transactions at issue, Grey followed the same four-legged pattern.[4] In the first leg, Grey purchased through GMCI a specific quantity of municipal bonds from the "street" at a designated price. In the second leg, he sold the same quantity of bonds to his own personal account at a higher price that he determined. In the third leg, Grey sold the bonds from his personal account to GMCI at an even higher price. In the fourth leg, he sold the bonds through GMCI to his customer at a final price determined by him and based on what he testified that he believed the fair market value of the bonds was at the time of sale.

As an example, one of the bond transactions involved Osceola municipal bonds. On October 22, 2008, Grey, through GMCI, bought $20,000 par amount of Osceola County Florida Industrial (Wells Charter School Project-A) revenue bonds with a maturity date of August 1, 2031, from the street, at a dollar price of $71.25, for a total cost of $14,250. On the same day, Grey sold the same quantity of the Osceola bonds to his IRA account at a price of $72.25. Three trading days later, Grey then sold the Osceola bonds on October 27, 2008, from his IRA account back to GMCI, at a price of $81.17. Finally, on the same day, Grey, through GMCI, sold the Osceola bonds to GMCI's customer at a sales price of $84.17.

The following chart represents the increases in prices of the bonds between the date of Grey's (GMCI's) purchase and the date of sales to the customers:

Osceola	GMCI purchased at	$71.2500	10/22/08
	Customer purchased at	$84.1700	10/27/08
Ocala	Grey purchased at	$84.2500	10/29/08
	Customers 1 and 2 purchased at	$88.7700	10/30/08
Collier	GMCI purchased at	$76.8800	11/06/08
	Customers 1 and 2 purchased at	$92.1740	11/11/08
Florida State	GMCI purchased at	$59.0000	12/16/08
	Customer purchased at	$72.5250	12/22/08

[4] The transactions at issue involved six different municipal bonds: Osceola, Ocala, Collier, Florida State, Highlands (Health), and Highlands (School). FINRA's examiner testified to producing a schedule of customer transactions involving 36 municipal bonds that were executed through Grey's personal accounts during the review period. Enforcement determined to charge Grey in connection with six municipal bonds listed on the schedule.

Highlands (Health)	Grey purchased at	$69.1940	12/18/08
	Customers 1, 2, and 3 purchased at	$76.0300	12/22/08
Highlands (School)	GMCI purchased at	$85.5690	07/23/09
	Customer purchased at	$91.2500	07/27/09

In each bond transaction, the customers purchased bonds at prices higher than—and in some cases significantly higher than—what Grey originally paid. In all of the transactions, no inter-dealer trades occurred between Grey's acquisition and the retail sales to GMCI's customers. On average, the sales occurred one to four trading days after Grey's acquisition. The aggregate "mark-up" that resulted from this pattern of trading ranged between 5.36% and 19.12%.[5]

Grey engaged in thousands of bond transactions in the course of a year, generating almost half of his income from his personal bond trading.[6] Grey maintained and controlled the accounts, including his IRA account, to where he routed the bonds before selling them to the customers. He solicited all of the transactions at issue, and, in some cases, he had discretionary authority over the customer account. GMCI's written supervisory procedures limited the amount of mark-ups on municipal bond transactions to 3% without the approval of a firm designated principal.[7] GMCI's procedures also prohibited interpositioning.

Grey does not dispute his pattern of trading in these transactions, nor the prices he charged. He testified that trading in this manner generated profits for him. Grey claimed that he routed the bonds through his personal accounts because the firm did not have a proprietary trading account, and, until July 2009, GMCI required him to trade at his own risk instead of the firm's. Grey also admitted that he did not disclose to the customers that he routed the bonds through his personal accounts or the mark-ups he charged on each leg of the transactions.

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5 A "mark-up" is defined as the "difference between the aggregate price paid by a customer for securities and the (lower) prevailing market price." *See* MSRB Notice 2010-10 (April 21, 2010), *available at* www.msrb.org/Rules-and-Interpretations/Regulatory-Notices/2010/2010-10.

6 Grey earned over $1.5 million in income for years 2008 and 2009.

7 While the Hearing Panel discussed Section 12.4.1 of GMCI's written supervisory procedures titled "Fixed Income," and we agree that this section adequately covers our present situation, the procedures more pointedly, under Section 15.26 (MSRB Rule G-30: Prices and Commissions) prohibit the sale of municipal securities to a customer with mark-ups (or mark-downs) that exceed 3% without the approval of a designated principal.

B. Discussion

The main dispute in this appeal is how Grey determined the prevailing market price for the subject bonds. Grey argues that he did not charge excessive or any mark-ups at all to the customers. Rather, he contends that he sold the bonds at "wholesale" prices that were fair and reasonable. According to Grey, because he purchased the bonds at such distressed prices in unusual market conditions, it is inconceivable that his acquisition cost could have represented the true prevailing market price.[8] Grey asserts that the prevailing market price of the bonds should be based on the yield curve of other bonds of like quality, and not contemporaneous cost.

For the reasons we discuss below, we affirm the Hearing Panel's liability findings. We first discuss the MSRB rules that apply to Grey's violations in all 10 bond transactions. We then discuss the cause of action related to fraud, which applied to seven of the 10 bond transactions.

1. Unfair and Excessive Mark-ups

Municipal bonds are debt securities issued by governmental entities such as cities, counties, or states to finance capital projects and fund day-to-day obligations. *Grandon v. Merrill Lynch & Co.*, 147 F.3d 184, 189 (2d Cir. 1998). The Municipal Securities Rulemaking Board ("MSRB") is the self-regulatory organization that adopts and interprets rules that govern the municipal securities market.[9] The MSRB's rule on fair dealing generally sets forth customer protection obligations of dealers when executing municipal securities with or on behalf of customers.[10]

MSRB Rule G-17 specifically requires that, "[i]n the conduct of its municipal securities . . . activities, each broker, dealer, municipal securities dealer, and municipal advisor shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice."[11]

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[8] Grey claims that a volatile and "severely distorted municipal securities market" at the height of the financial crisis allowed him to acquire the bonds at "extraordinarily low prices."

[9] The MSRB is the self-regulatory organization charged with primary rulemaking authority for the municipal securities activities of broker-dealers. The MSRB does not have enforcement authority. FINRA administers and enforces its members' compliance with the MSRB rules. *See* NASD Manual, *Plan of Allocation and Delegation of Functions by NASD to Subsidiaries*, Section II.A.b.

[10] *See* MSRB Answers to Frequently Asked Questions Regarding Dealer Disclosure Obligations under MSRB Rule G-17 (November 30, 2011), *available at* www.msrb.org/Rules-and-Interpretations/MSRB-Rules/General/Rule-G-17.

[11] MSRB Rule G-17 is the MSRB corollary to FINRA Rule 2010, which requires broker-dealers to observe high standards of commercial honor and just and equitable principles of trade.

Implicit in MSRB Rule G-17 is the anti-fraud provision and general duty for dealers in municipal securities to deal fairly with their customers, even in the absence of fraud.

MSRB Rule G-30 is the fair pricing rule, which requires dealers to trade with customers at prices that are fair and reasonable, taking into consideration all relevant factors. In relevant part, MSRB Rule G-30 provides that "[n]o broker, dealer or municipal securities dealer shall purchase municipal securities for its own account from a customer or sell municipal securities for its own account to a customer except at an aggregate price (including any mark-down or mark-up) that is fair and reasonable."[12]

The MSRB has interpreted the "fair and reasonable" pricing requirement for municipal securities to include two main elements. First, the price must be reasonably related to the market value of the municipal securities in the transaction. Second, the mark-up or mark-down for a transaction must not exceed a fair and reasonable amount.[13] Mark-ups and mark-downs are determined from the prevailing market price. In municipal mark-up cases, proper determination of the prevailing market price thus becomes critical.[14]

As a general rule, the best measure of a prevailing market price is the dealer's contemporaneous cost for the securities – or put another way – "the price at which dealers trade with one another, i.e., the current inter-dealer market."[15] *Grandon*, 147 F.3d at 189; *see also Andrew P. Gonchar*, Exchange Act Release No. 60506, 2009 SEC LEXIS 2797, at *26 (Aug. 14, 2009) (holding that a dealer that is not a market maker must base its prices on its own contemporaneous cost); *First Honolulu Sec.*, 51 S.E.C. 695, 697 (1993) (holding that the best evidence of market prices, absent countervailing evidence, is the dealer's contemporaneous cost); *Dep't of Market Regulation v. Lane*, Complaint No. 20070082049, 2013 FINRA Discip. LEXIS 34, at *23 n.20 (FINRA NAC Dec. 26, 2013), *appeal docketed*, SEC Admin. Proceeding

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[12] *See* MSRB Rule G-30, *available at* www.msrb.org/Rules-and-Interpretations/MSRB-Rules/General/Rule-G-30.

[13] *See* MSRB Notice 2010-10 (April 21, 2010), *supra* note 7. *See also Grandon*, 147 F.3d at 190 (noting that the MSRB has provided no benchmark or specific percentage guideline for a reasonable mark-up in view of the heterogeneous nature of municipal securities transactions and dealers).

[14] *Dep't of Enforcement v. David Lerner Associates, Inc.*, Complaint No. 20050007427, 2012 FINRA Discip. LEXIS 44, at *60 (FINRA Hearing Panel Apr. 4, 2012) ("The 'key issue' in a mark-up case is determining the 'prevailing market price' for the securities at issue," *quoted in Orkin v. SEC*, 31 F.3d 1056, 1063 (11th Cir. 1994)).

[15] A dealer's cost is considered "contemporaneous" if the inter-dealer transaction occurs close enough in time to the transaction at issue that it reasonably is expected to reflect the current market price of the security. *See* MSRB Notice 2010-10 (April 21, 2010).

No. 3-15701 (Jan. 22, 2014) (noting the best indication of the prevailing market price is a member's own contemporaneous cost). This standard reflects the fact that the prices broker-dealers pay for securities in transactions closely related in time to retail sales to customers are a high indication of the prevailing market price. *Grandon*, 147 F.3d at 189.

When a broker-dealer asserts a different prevailing price, the burden shifts to the dealer to provide sufficient evidence to overcome the presumption that contemporaneous cost is the best measure of determining the prevailing market price. *Lerner*, 2012 FINRA Discip. LEXIS 44, at *61 ("[a] broker's contemporaneous cost is presumptively the fair market value, and [r]espondents have the burden to show otherwise."); *Gonchar*, 2009 SEC LEXIS 2797, at *28 ("[o]nce NASD presents evidence of contemporaneous cost, the burden shifts to [a]pplicants to refute that evidence."). The key question here is whether Grey overcame this burden. We find that he did not.

We first find that Enforcement reliably established Grey's contemporaneous cost as the prevailing market price. Grey, through the firm's account, made contemporaneous purchases in the subject bonds. In each transaction, his purchase constituted the last inter-dealer trade in the bond. No intervening dealer trades occurred between Grey's acquisition of the bonds and his sales to the customers. In each of the 10 transactions, his final sales of the bonds to customers occurred on average one to four days after Grey's acquisition, which is a reasonable timeframe for estimating the bonds' current market prices.

We also find Enforcement's expert testimony to be reliable. Enforcement presented James McKinney as an expert on municipal bond pricing and industry practices. McKinney has 40 years of experience in fixed income securities, and supervising his firm's municipal bond and fixed income sales and trading business. McKinney used conventional industry standard that is supported by case precedent in assessing the bond transactions at issue and determined that, for each transaction, the best evidence of the prevailing market price for the bonds at issue was the last inter-dealer trade, or the price at which Grey acquired the bond. To determine the prevailing market price, McKinney looked at Grey's original date of purchase for the bonds and the purchase price. He testified that there were no other trades to review as comparables between the time of acquisition and the date Grey sold the bonds to the customers.

His calculations, however, were not just a restatement of Grey's acquisition price. In determining fair market value, McKinney attributed only those market movements based on the Municipal Market Data or MMD scale that increased the bond's fair market value.[16] With a maximum allowable mark-up of 3%, McKinney concluded that Grey charged excessive mark-ups ranging between 5.36% and 19.12%. Based on McKinney's calculations, Grey's mark-ups on each bond at issue was excessive by the following percentiles:

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[16] Both Enforcement and Grey's experts testified that there were no large market movements related to the bonds at the time of the transactions.

Osceola	14.38%
Oscala	5.36%
Collier	19.12%
Florida State	16.88%
Highlands (Health)	8.62%
Highlands (School)	6.64%

Grey failed to provide sufficient evidence that the prevailing market price was different than his contemporaneous cost. Rather, Grey contends that yield to the customer was the most important factor in determining the prevailing market price. In noting that the yield of the bonds at issue were "attractive," Grey's expert, John Bagley, assessed the yield curve of unrelated bonds using those yields as comparables. He also testified to reviewing historical trading data of the unrelated bonds that, in some cases, went back to two years. From this, he concluded that the customers paid a reasonable price of the bonds at issue.

We find that Bagley's methodology was flawed and therefore unreliable for several reasons. He did not use conventional measures in determining fair pricing.[17] Even using his unconventional approach, his comparables were flawed in that the bonds were selected by Grey and were opposite in character of the bonds at issue.[18] He admitted in his testimony that his use of historical trading data from two years prior to the transactions was irrelevant to his analysis of the prevailing market price of the subject bonds. Bagley even testified that Grey "determined the price to the customer ultimately based upon what he *felt* was the appropriate price and then determined the amount of the mark-up . . . out of that." (Emphasis added.) Determining prices based on one's own subjective judgment, however, does not support Grey's claim that yield was the better measure of price. *Cf. Horner v. SEC*, 994 F.2d 61, 63 (2d Cir. 1993) (rejecting petitioner's claim that, in lieu of contemporaneous cost, the price at which the securities were sold to customers was the better indication of market price thereby making the mark-up zero). Finally, while Bagley stated that the customer prices had attractive yields, he did not conclude that the customer prices reflected the prevailing market price.

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[17] Bagley testified: "I didn't look at the fair price between two inter-dealer trades . . . there were many times I threw out inter-dealer trades because I didn't think they were relevant."

[18] For example, Bagley's comparable bonds were general obligation round-lot bonds instead of revenue odd-lot bonds like the ones at issue.

Grey also fails to demonstrate how market conditions at the time changed the prevailing market price of the subject bonds. *LSCO Sec., Inc.*, 50 S.E.C. 518, 520 (1991) ("absent some showing of a change in the prevailing market, a dealer's inter-dealer cost may be used to establish market price . . ."). At the time of sale, the bond prices had not changed to any meaningful degree to warrant a different measure of pricing. We find persuasive both experts' testimony that no extraordinary market events or large movements in the bonds occurred during the time Grey acquired the bonds until he sold them to the customers.

Using contemporaneous cost as the basis for determining the prevailing market price, we find abundant evidence that Grey charged customers unfair prices and excessive mark-ups in violation of MSRB Rules G-17 and G-30. The evidence sufficiently demonstrates that, in all instances, Grey deliberately charged the Firm's customers excessive mark-ups over his contemporaneous cost that ranged between 5.36% and 19.12%, which is well above industry practices for municipal securities.[19] We also find that his actions were willful.[20]

2. Fraud and Interpositioning

The Hearing Panel found that Grey willfully violated Section 10(b) of the Securities Exchange Act when he charged excessive mark-ups that ranged from 8.62% to 19.12% and failed to disclose the excessive mark-ups and his interpositioning. We affirm the Hearing Panel's finding.[21]

Section 10(b) of the Exchange Act makes it unlawful for any person to use or employ any manipulative or deceptive device or contrivance in connection with the purchase or sale of a security. Rule 10b-5, promulgated under Section 10(b), makes it unlawful to make material misstatements or to omit material facts in connection with the purchase or sale of a security. *SEC v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1466 (2d Cir. 1996); *Grandon*, 147 F.3d at 188.

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[19] *See Lerner*, 2012 FINRA Discip. LEXIS 44 at *17 (noting that market participants understand that municipal bond mark-ups had to be substantially less than 5% and holding that mark-ups above 3% were subject to regulatory scrutiny).

[20] Pursuant to Sections 3(a)(39) and 15(b)(4)(D) of the Exchange Act, broker-dealers are subject to disqualification from the securities industry for willful violations of the federal securities laws or the MSRB rules. 15 U.S.C. 78c(a)(39), 15 U.S.C. 78o(b)(4)(D). The term "willful" means in this context intentionally committing the act which constitutes the violation. *Mathis v. SEC*, 671 F.3d 210, 216-18 (2d Cir. 2012). There is no requirement that the actor be aware that he or she is violating a particular rule or regulation. *Id.*; *see also Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (holding that the term "willful" means that the person with the duty knows what he is doing, but does not require that one know that he is breaking the law).

[21] Specifically, we find the following excessive mark-ups to violate the antifraud rules: 8.62% on three of the Highlands (Health) trades, 14.38% on the Osceola trade, 16.88% on the Florida State trade, and 19.12% on two of the Collier trades.

Liability under Section 10(b) requires that the respondent, acting with scienter, made a material misrepresentation or omission of fact or used a fraudulent device. *First Jersey*, 101 F.3d at 1467 ("In order to establish primary liability under § 10(b) and Rule 10b-5, a plaintiff is required to prove that in connection with the purchase or sale of a security the defendant, acting with scienter, made a material misrepresentation (or a material omission if the defendant had a duty to speak) or used a fraudulent device").

Scienter is a mental state embracing intent to deceive, manipulate, or defraud, *see, e.g.*, *Tellabs Inc. v. Makor Issues & Rights., Ltd.*, 127 S. Ct. 2499, 2507 n.3 (2007), or at least knowing misconduct. *First Jersey*, 101 F.3d at 1467 (citing *Wechsler v. Steinberg*, 733 F.2d 1054, 1058 (2d Cir. 1984) (holding that to prove scienter in a Section 10(b) case, plaintiff must demonstrate "knowing or intentional misconduct" or an "intent to deceive, manipulate or defraud investors")). Scienter may be established by a showing that a respondent acted recklessly. *Alvin W. Gebhart, Jr.*, Exchange Act Release No. 58951, 2008 SEC LEXIS 3142, at *26 (Nov. 14, 2008), *aff'd*, 595 F.3d 1034 (9th Cir. 2009). Recklessness in this context is a "highly unreasonable omission, involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the [respondent] or is so obvious that the actor must have been aware of it." *Id.* at *26 n.26.

We find the evidence compelling that Grey knowingly or recklessly charged the customers excessive mark-ups at prices that were not reasonably related to the prevailing market price. Grey admitted that he determined the mark-ups charged on each leg of the bond transactions. Charging excessive mark-ups is material information.[22]

In seven of the 10 bond transactions, Grey charged fraudulently excessive mark-ups that he failed to disclose to GMCI's customers. In those transactions, the mark-ups Grey charged ranged from 8.62% to 19.12%, which are well above industry standards. *See Grandon*, 147 F.3d at 191 (noting that proper mark-ups for municipal bonds are significantly lower than other mark-ups, which were not in excess of five percent of the prevailing market price); *Donald T. Sheldon*, 51 S.E.C. 59, 77 (1992) (finding fraud when respondent's undisclosed mark-ups for municipal bonds exceeded 8%). Grey knew, or recklessly disregarded knowing, that such mark-ups were exceedingly high. *Sheldon*, 51 S.E.C. at 78 (holding that respondent knowingly engaged in conduct that he knew, or was reckless in not knowing, was violative of mark-up restrictions). As a professional in the securities industry for over 30 years, Grey was required to understand his compliance obligations with the firm's written supervisory procedures that limited mark-ups to no more than 3%. *First Jersey*, 101 F.3d at 1467 (holding that defendants acted with scienter when they used fraudulent devices to charge excessive mark-ups knowing they were violating the law). Nevertheless, Grey charged the prices anyway without disclosing

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[22] *David Disner*, 52 S.E.C. 1217, 1219 (1997) (noting that basic to the federal securities laws is the notion that an excessive mark-up or mark-down is material to the purchaser of a security, and holding that a dealer violates the antifraud provisions of the federal securities laws when, with scienter, he marks up the price of the security and charges his retail customer a price not reasonably related to the prevailing market price and fails to disclose this to his customer).

this material information to GMCI's customers.[23] *Meyer Blinder*, 50 S.E.C. 1215, 1230 (1982) (finding scienter "[w]here a dealer knows the circumstances indicating the prevailing inter-dealer market price for the securities, knows the retail price that it is charging the customer, and knows or recklessly disregards the fact that its mark-up is excessive, but nonetheless charges the customer the retail price"). We find that for seven of the 10 bond transactions, Grey knowingly or recklessly charged undisclosed excessive mark-ups that violated Exchange Act Section 10(b) and Rule 10b-5.[24]

Grey's interpositioning, which involved undisclosed, excessive mark-ups within one to four days of acquiring the bonds, and is unchallenged by him, further supports our finding that he violated Exchange Act Section 10(b) and Rule 10b-5. The SEC has long held that interpositioning can result in fraud where it is done with scienter and results in the charging of excessive and undisclosed mark-ups. *Cf. Gonchar*, 2009 SEC LEXIS 2797, at *36 ("[P]ersons engaged in the securities business cannot be unaware . . . that interpositioning is bound to result in increased prices or costs."). We find that Grey acted with scienter because he knowingly routed the bonds through his personal accounts before he sold them to the customers. Grey testified that he set the prices for each leg of the transactions and therefore controlled the amount of the mark-ups. We also find that Grey's successive mark-ups on each leg of the transactions and his failure to disclose those mark-ups demonstrated his intention to conceal his excessive profits from GMCI and its customers to their detriment, which is fraudulent.[25] *In re*

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[23] *See generally Norris & Hirshberg, Inc. v. SEC*, 177 F.2d 228, 232-33 (D.C. Cir. 1949). "A broker-dealer commits fraud (in violation of §10(b) and Rule 10b-5) by charging customers excessive mark[-]ups without proper disclosure." *Grandon*, 147 F.3d at 190.

[24] Mark-ups greater than 10% on equity securities "generally are not reasonably related to the prevailing market price." *D.E. Wine Inv., Inc.*, 53 S.E.C. 391, 394 (1998). In fact, undisclosed mark-ups of that size have been held to constitute "fraud per se." *First Jersey*, 101 F.3d at 1469; *Dep't of Enforcement v. Galasso*, Complaint No. C10970145, 2001 NASD Discip. LEXIS 2, at *54 (NASD NAC Feb. 5, 2001) (same), *aff'd in relevant part*, 56 S.E.C. 76 (2003); *NASD Notice to Members 92-16*, 1992 NASD LEXIS 47, at *8 (Apr. 1992); *James E. Ryan*, 47 S.E.C. 759, 763 (1982) (noting that mark-ups exceeding 10% generally "are fraudulent, even in the sale of low priced securities"). We find that grossly excessive mark-ups on debt securities are fraudulent as well. *Investment Planning, Inc.*, 51 S.E.C. 592, 595 (1993) (stating, in case involving corporate debt securities, that "a 5% mark-up serves merely as an outside limit" and "lies above what may be permissible in particular instances"); *Lake Sec., Inc.*, 51 S.E.C. 19, 21 (1992) (holding, in a case involving debt securities, that "mark-ups in excess of 7% above the prevailing market price may be fraudulent").

[25] We also affirm the Hearing Panel's finding that Grey willfully engaged in interpositioning in violation of MSRB Rule G-17, which was Enforcement's third cause of action. Unbeknownst to GMCI's customers, Grey intentionally structured the transactions to profit from the prices he set in each leg of the transactions that resulted in mark-ups in excess of 3%, which constitutes unfair dealing. Grey argues that interpositioning is no more of a conflict than that which exists in proprietary trading and the profits received from proprietary trades are

[Footnote continued on next page]

Investment Placement Group, Exchange Act Release No. 66055, 2011 SEC LEXIS 4547, at *3 (Dec. 23, 2011) (holding that respondent's undisclosed, excessive mark-ups were part of a fraudulent interpositioning scheme and resulted in ill-gotten gains).

Grey argues, however, that he did not possess the intent to defraud and therefore his actions did not violate Section 10(b). In support of his claim, he contends that all of the customers received bonds at better yields than the MMD scale, and that none of the customers complained about their transactions. One customer filed an affidavit during Grey's proceeding stating that they had no issues with Grey's actions. Grey also points to the amount of profit he received in connection with the trades and argues that it was insignificant. All of Grey's arguments, however, fail to negate our finding of securities fraud.

A trader is obligated to know the standards for determining fair prices. *John Montelbano*, 56 S.E.C. 76, 96 (2003). Grey knew, or was reckless in not knowing, that his prices included excessive mark-ups that bore no reasonable relation to the prevailing market price at the time. A customer complaint is neither a prerequisite to a finding of securities fraud, nor does the absence of it absolve Grey of his duty to disclose his self-dealing. *Dep't of Enforcement v. Cipriano*, Complaint No. C07050029, 2007 NASD Discip. LEXIS 23, at *39 (NASD NAC July 26, 2007) (finding the absence of customer complaints as irrelevant to the finding of violation). Further, the appropriate time for Grey to disclose his impositioning scheme and excessive mark-ups was at the time of the sales transaction—and not as a defense to his misconduct. Lastly, there is no *de minimis* exception to the receipt of ill-gotten gains, and thus the dollar amount of Grey's ill-gotten gains, which was approximately $15,750, serves as no defense to his misconduct.

Accordingly, we find that Grey violated Section 10(b) of the Exchange Act and Rule 10b-5 when he willfully charged excessive mark-ups and failed to disclose the excessive mark-ups and his interpositioning to GMCI's customers in the seven transactions identified in the first cause of the complaint.

[Cont'd]

not disclosed. Grey also argues that GMCI knew of his interpositioning and required him to execute bond trades through his personal account to avoid risk exposure to the firm. We do not find Grey's arguments valid.

Fundamental to MSRB Rules is the duty to deal fairly with customers and to ensure that a broker-dealer charges prices that are reasonably related to the best available price in the market. Grey willfully interposed himself between the firm and the firm's customers and charged excessive mark-ups. The firm's customers did not receive the most favorable price available in the market. Grey's mark-ups, and specifically when he bought from and sold to the firm, went undisclosed, and as a result, he enriched himself to the detriment of the customers. Moreover, the firm's own written supervisory policies explicitly prohibited interpositioning. We conclude that Grey's actions constitute interpositioning in violation of MSRB Rule G-17.

IV. Sanctions

In assessing sanctions, we considered FINRA's Sanction Guidelines ("Guidelines"), including the Principal Considerations in Determining Sanctions set forth therein and any other case-specific factors.[26] For Grey's interpositioning, excessive mark-ups, and fraud violations, the Hearing Panel suspended Grey from associating with any member firm in any capacity for two years, fined him $30,000 and ordered him to pay $16,000 in disgorgement, along with costs. As discussed below, instead of $16,000, we order Grey to pay $15,750 in disgorgement, plus prejudgment interest, and suspend him for 18 months.

As an initial matter, because Grey's violations resulted from the same course of conduct and violated rules that have similar purposes, we find that a unitary sanction is appropriate. For excessive mark-ups, the Guidelines recommend a fine of $5,000 to $100,000 plus, if restitution is not ordered, the gross amount of the excessive mark-ups (or mark-downs). In addition, the Guidelines recommend suspension in any or all capacities for up to 30 business days. In egregious cases, we are to consider imposing a suspension in any or all capacities for up to two years or a bar.[27]

For negligent misrepresentations or material omissions of fact, the Guidelines recommend a fine between $2,500 and $50,000, and a suspension in any or all capacities for up to 30 business days.[28] For intentional or reckless misrepresentations or material omissions of fact, the Guidelines recommend that adjudicators consider imposing a fine between $10,000 to $100,000, a suspension in any or all capacities of 10 business days to two years, and, in egregious cases, a bar.[29]

A. Suspension

There are several aggravating factors in this case. Grey routinely engaged in the practice of interpositioning that resulted in excessive mark-ups, and had done so for quite some time. By concealing his misconduct, Grey insulated himself from the possibility that the customers would learn how much he was marking up the bonds.[30] He acted deliberately and

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[26] *See FINRA Sanction Guidelines* 6 (2013), *available at* http://www.finra.org/web/groups/industry/@ip/@enf/@sg/documents/industry/p011038.pdf [hereinafter "*Guidelines*"].

[27] *Id.* at 90 & n.1 (stating that this Guideline is also appropriate for violations of excessive mark-ups under MSRB Rule G-30).

[28] *Id.* at 88 & n.1 (stating that this Guideline is also appropriate for violations of MSRB Rule G-17).

[29] *Id.* at 88.

[30] *Id.* at 6 (Principal Considerations in Determining Sanctions, No. 10).

purposefully.[31] He has yet to acknowledge that his misconduct is in violation of the securities laws.[32] Instead, he posits a number of excuses for his actions. For example, he suggested that the customers were getting a good deal, and that the bond prices were "below" the prevailing market price given the existing market conditions. These claims are false. Grey's multi-leg transactions benefitted him at the expense of the customers.

Another aggravating factor is Grey's attempt to pass off his regulatory obligations to GMCI. By his own admission, Grey asserted that mark-ups of 3% or less are proper for municipal securities. He blamed GMCI for his interpositioning, contending that the firm required him to hold the bonds in his personal accounts to avoid firm risk. Grey produced no evidence, however, that the firm instructed him to interject himself between the firm and the prevailing market price and charge undisclosed excessive mark-ups—which is the offending conduct at issue. Further, GMCI's written supervisory procedures explicitly prohibited interpositioning, and the charging of mark-ups in excess of 3%. Moreover, we agree with the Hearing Panel that Grey, not GMCI, bears responsibility for the mark-ups. Even if Grey's assertion was true, which it is not, it is well established that a registered representative cannot shift to his firm his own responsibility to comply with the federal securities laws and, in this case, MSRB rules. *Gonchar*, 2009 SEC LEXIS 2792, at *35 n.35.

We have considered each of Grey's claims of mitigation and find them to lack merit. Although Grey claims that he never had a regulatory action against him since he entered the securities industry, a "lack of disciplinary history is not mitigating for purposes of sanctions because an associated person should not be rewarded for acting in accordance with his duties as a securities professional." *Dep't of Enforcement v. Craig*, Complaint No. E8A2004095901, 2007 FINRA Discip. LEXIS 16, at *24 (FINRA NAC Dec. 27, 2007) (rejecting argument that absence of disciplinary history and prior customer complaints deserved mitigation), *aff'd*, Exchange Act Release No. 59137, 2008 SEC LEXIS 2844 (Dec. 22, 2008).

It is also not mitigating that none of Grey's customers complained. *Mission Sec. Corp.*, Exchange Act Release No. 63453, 2010 SEC LEXIS 4053, at *23 (Dec. 7, 2010) (holding that FINRA's "power to enforce its rules is independent of a customer's decision not to complain") (citation omitted); *Dep't of Enforcement v. Jennings*, Complaint No. 2008013864401, 2013 FINRA Discip. LEXIS 18, at *62 (FINRA Hearing Panel Mar. 4, 2013) (noting that customer harm is not a necessary element of a self-regulatory rule violation) (citation omitted). In this respect, we have also considered the affidavit from a customer and find it not material to our consideration of the seriousness of Grey's misconduct. Lastly, we note that Grey's misconduct was difficult to detect and violated the important principle that customers can trust registered persons to treat them fairly.

Considering the totality of these facts and circumstances, we find that Grey's interpositioning, excessive mark-ups, and fraudulent omissions were egregious. To remedy

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31 *Id.* at 7 (Principal Considerations in Determining Sanctions, No. 13).

32 *Id.* at 6 (Principal Considerations in Determining Sanctions, No. 2).

these violations, we agree with the Hearing Panel's order of suspension against Grey from associating with any member firm in any capacity, but reduce his term of the suspension from two years to 18 months.

B. Fine

We affirm the Hearing Panel's order of a $30,000 fine. The Guidelines recommend a fine between $5,000 and $100,000 for excessive mark-ups, and the recommended fine for reckless misrepresentations or material omissions of fact is between $10,000 to $100,000. We believe that the appropriate balance has been struck in ordering Grey to pay a $30,000 fine for his misconduct, which is in the mid-range of the Guidelines. The $30,000 fine should deter Grey from any recurrences of his wrongful actions and complete disregard for his regulatory obligation as a securities professional.

C. Disgorgement

The Guidelines also instruct us to consider a respondent's ill-gotten gains when fashioning an appropriate sanction.[33] We affirm the Hearing Panel's order of disgorgement, but slightly reduce the disgorgement amount to $15,750.

"[D]isgorgement is intended to force wrongdoers to give up the amount by which they were unjustly enriched." *Michael David Sweeney*, 50 S.E.C. 761, 768 (1991). "We may order disgorgement after a reasonable approximation of a respondent's unlawful profits." *Dep't of Enforcement v. Evans*, Complaint No. 2006005977901, 2011 FINRA Discip. LEXIS 36, at *40 n.42 (FINRA NAC Oct. 3, 2011); *Laurie Jones Canady*, 54 S.E.C. 65, 84 (1999) (noting that "courts have held that the amount of disgorgement ordered need only be a reasonable approximation of profits causally connected to the violation") (internal quotation marks omitted), *aff'd*, 230 F.3d 362 (D.C. Cir. 2000). Any risk of uncertainty in calculating disgorgement "falls upon the wrongdoer whose misconduct created the uncertainty and who bears the burden of proving that the measure is unreasonable." *Evans*, 2011 FINRA Discip. LEXIS 36, at *40 n.42.

In 10 municipal bond transactions, Grey charged GMCI customers excessive mark-ups that ranged from 5.36% and 19.12%. The mark-up range is uncontested and supported by Enforcement's expert witness, who we found to be reliable. Giving Grey the maximum allowable mark-up of 3% and accounting for any increases in the market at the time of sale, we accept Enforcement's expert's testimony that Grey received approximately $15,750 in ill-gotten

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33 *Guidelines*, at 5 (General Principles Applicable to All Sanction Determinations, No. 6).

profits.[34] We order that Grey pay $15,750 in disgorgement to FINRA, plus prejudgment interest, calculated from July 27, 2009.[35]

V. Conclusion

We find that Grey charged excessive mark-ups in violation of MSRB Rules G-17 and G-30, and failed to disclose (in seven of the transactions with customers) the excessive mark-ups and his interpositioning in violation of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. Because the violations were willful, Grey is statutorily disqualified.

Grey is suspended from associating with any member firm in any capacity for 18 months, and is ordered to pay a fine of $30,000, and disgorgement of $15,750 to FINRA, including prejudgment interest on the disgorgement amount calculated from July 27, 2009. Finally, we affirm the Hearing Panel's order that Grey pay $5,267.32 in hearing costs.[36]

On Behalf of the National Adjudicatory Council,

Marcia E. Asquith

Marcia E. Asquith,
Senior Vice President and Corporate Secretary

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[34] The Hearing Panel ordered a disgorgement of $16,000, but we do not find support for this amount in the record.

[35] The prejudgment interest rate shall be the rate established for the underpayment of income taxes in Section 6621(a) of the Internal Revenue Code, 26 U.S.C. § 6621(a), the same rate that is used for calculating interest on restitution awards. *Guidelines*, at 11 (Technical Matters).

[36] We also have considered and reject without discussion all other arguments advanced by the parties. Pursuant to FINRA Rule 8320, the registration of any person associated with a member who fails to pay any fine, costs, or other monetary sanction imposed in this decision, after seven days' notice in writing, will summarily be revoked for non-payment.