FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. NATHALO MENENDEZ (CRD No. 4882003) and ANTHONY SPAGNOLO, III (CRD No. 4726651), Respondents.	Disciplinary Proceeding No. 2009016159110 Hearing Officer—LOM **HEARING PANEL DECISION AS TO SPAGNOLO** May 4, 2015

The charges against Respondent, Anthony Spagnolo, III, are dismissed. Enforcement did not establish by a preponderance of the evidence that he opened and traded in eight customer accounts without authorization (in violation of NASD Rule 2110 and FINRA Rule 2010) or that he provided his firm false and inaccurate information regarding those customers (in violation of NASD Rules 3110(a) and 2110 and FINRA Rule 2010).

Appearances

Jonathan Golomb and Edwin T. Aradi, Rockville, Maryland, representing the Department of Enforcement.

Stephen B. Wexler and Brian Boxler, Wexler Burkhart Hirshberg & Unge, LLP, Uniondale, New York, representing Respondent.

I. NATURE OF THE CASE

The Department of Enforcement ("Enforcement") for the Financial Industry Regulatory Authority ("FINRA"), a self-regulatory organization for the securities industry, brought this disciplinary proceeding against Respondent, Anthony Spagnolo, III, alleging two causes of action against him.[1] Spagnolo's alleged misconduct occurred while he was employed by FINRA member firm iTradedirect.com (the "Firm" or "iTrade").

The First Cause of Action charges that Spagnolo opened accounts on behalf of eight customers and initiated trades in those accounts without their authorization. This conduct is alleged to violate NASD Rule 2110 and FINRA Rule 2010, which require members and their associated persons (through NASD Rule 0115 and FINRA Rule 140) to observe high standards of commercial honor and just and equitable principles of trade.

The Second Cause of Action charges that Spagnolo created and maintained new account documentation that was false and inaccurate as to the risk tolerances, investment objectives, investment experience, and/or financial situations of many of the eight customers. In so doing, Spagnolo is alleged to have caused the Firm's books and records to be false and inaccurate in violation of its obligations under the Securities and Exchange Act of 1934. This conduct is alleged to violate NASD Rules 3110(a) and 2110 and FINRA Rule 2010.

A FINRA Hearing Panel held a two-day hearing in October 2014. This is its decision after careful review of the record as to the claims against Spagnolo.[2]

As discussed below, the Hearing Panel finds that, although there was reason to be suspicious of the circumstances in which Spagnolo opened the eight customers' accounts and initiated trading in their names, Enforcement failed to prove by a preponderance of the evidence that he did so without authorization. Spagnolo's customers provided him with social security numbers and other personal information necessary to open accounts and initiate trading, although

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[1] FINRA is responsible for regulatory oversight of securities firms and associated persons who do business with the public. It was formed in July 2007 by the consolidation of NASD and the regulatory arm of the New York Stock Exchange. FINRA is developing a new "Consolidated Rulebook" of FINRA Rules that includes NASD Rules. The first phase of the new Consolidated Rulebook became effective on December 15, 2008. See FINRA Regulatory Notice 08-57 (Oct. 2008). Because the Complaint in this case was filed after December 15, 2008, FINRA's procedural Rules apply to the proceeding. The applicable FINRA and/or NASD Conduct Rules are those that existed when the conduct at issue occurred. FINRA's Rules (including NASD Rules) are available at www.finra.org/industry/finra-rules.

[2] This decision refers to the transcript of hearing testimony as "Hearing Tr." and cites the relevant page or pages. A reference to the transcript includes a parenthetical identifying the witness or speaker. For example, Spagnolo's testimony is cited "Hearing Tr. (Spagnolo) 408-13." The decision refers to exhibits using a prefix to identify the proponent. Enforcement's exhibits are identified by the prefix "CX" (as in CX-2). Spagnolo did not offer any exhibits of his own. There were no post-hearing briefs relating to the charges against Spagnolo.

Spagnolo testified on his own behalf. Other witnesses in addition to Spagnolo were the following: the Firm's Chief Compliance Officer, [redacted], Customers ES, REM, RLE, and CLH, and FINRA Examiner, Michael DiTrapani ("DiTrapani").

they denied giving him authority to do so. The customer testimony and declarations on which Enforcement relied were confused and contradictory.

Similarly, Enforcement failed to prove by a preponderance of the evidence that Spagnolo caused false and inaccurate information regarding the customers to be entered into the Firm's books and records. Some of the customers who testified said that the information regarding their financial situation was accurate, contrary to allegations in the Complaint. This testimony cast doubt on the reliability of the declarations used by Enforcement to support its case.

The Hearing Panel dismisses both Causes of Action brought against Spagnolo.

II. STANDARD OF PROOF

Enforcement has the burden of proof. That burden is met if Enforcement establishes its claims by a preponderance of the evidence.[3] The preponderance of evidence standard of proof requires more than a scintilla of evidence and is a higher standard than substantial evidence.[4] However, a preponderance of evidence standard demands less proof than the clear and convincing standard.[5] The preponderance standard requires only that the complainant "prove it is more likely than not" that the allegations are true.[6] Essentially, the balance of the evidence must tip at least slightly in favor of the complainant.

As discussed below, the Hearing Panel concludes that Enforcement did not prove its case by a preponderance of the evidence. The evidence did not show that it was more likely than not

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[3] *Dep't of Enforcement v. Claggett*, No. 2005000631501, 2007 FINRA Discip. LEXIS 2, at *25 (NAC Sept. 28, 2007) (Enforcement had burden of proof, which it had to satisfy by a preponderance of the evidence).

See also Luis Miguel Cespedes, Exchange Act Release No. 59404, 2009 SEC LEXIS 368, at *18 and n.11 (Feb. 13, 2009) (citing *David M. Levine*, 57 S.E.C. 50, 73 n.42 (2003) (holding that preponderance of the evidence is the standard of proof in self-regulatory organization ("SRO") disciplinary proceedings)); *Kirk A. Knapp*, 51 S.E.C. 115, 130 n.65 (1992) (stating the "the correct standard is preponderance of the evidence" in an SRO proceeding). In *Cespedes*, the Securities and Exchange Commission ("SEC") upheld FINRA disciplinary sanctions imposed on the respondent for unsuitable transactions in the accounts of fourteen customers. The testifying customers were found credible by the SRO. *Cespedes*, 2009 SEC LEXIS 368, at *120 and n.15.

The Second Circuit Court of Appeals noted in *Gonchar v. SEC*, 2010 U.S. App. LEXIS 25763, at **3-4 (Dec. 17, 2010) that the U.S. Supreme Court held in *Steadman v. SEC*, 450 U.S. 91 (1981) that SEC disciplinary proceedings are governed by the preponderance of the evidence standard. The Second Circuit concluded that there is no reason to apply a different standard where discipline is initially imposed by an SRO and then sustained by the SEC. *Gonchar, 2010 U.S. App. LEXIS 25763, at **3-4.*

[4] *See John D. Audifferen*, Exchange Act Release No. 58230, 2008 SEC LEXIS 1740, at *12 and n.9 (July 25, 2008) (substantial evidence means more than a scintilla but less than a preponderance of evidence). *See also Wash. Metro. Area Transit Auth. v. Local 2, Office & Prof'l Employees Int'l Union*, 965 F. Supp. 2d 13, 33 (D.D.C. 2013) (substantial evidence means "such relevant evidence as a reasonable mind might accept as adequate to support a conclusion"); *Toms v. Office of the Architect of the Capitol*, 650 F. Supp. 2d 11, 27 n.13 (D.D.C. 2009) (standard of evidence in termination hearing was substantial evidence, a lesser standard than preponderance of the evidence).

[5] *See, e.g., Dep't of Enforcement v. Belden*, 2002 NASD Discip. LEXIS 12, at *19-20 (NAC Aug. 13, 2002) (preponderance standard applies, not clear and convincing, in both SEC and NASD disciplinary decisions).

[6] *Herman & MacLean v. Huddleston*, 459 U.S. 375, 390 (1983) (discussing nature of standard and holding that it applies to civil damage actions for securities fraud).

that Spagnolo acted without authorization in connection with the opening of accounts and initial trades for the eight customers. Nor did Enforcement prove by a preponderance of the evidence that Spagnolo provided false and inaccurate information to be entered into the Firm's books and records.

III. FINDINGS

A. Spagnolo

Spagnolo has been employed in the securities industry as a cold caller and account opener since 2003 (except for a year and a half when he did other work).[7] He was employed by iTrade starting in mid-2006.[8]

Currently, Spagnolo is working in the industry and holds series 7 and series 63 licenses.[9] Because he is registered, FINRA has jurisdiction under its By-Laws (Art. V, Section 4) to bring this proceeding against him.

B. The Investigation

This proceeding against Spagnolo has its genesis in the 2008 and 2009 cycle examinations of iTrade. The examination staff identified issues and referred them to Enforcement for further investigation. Among the concerns were a high number of cancelled trades and a high number of exception reports indicative of possible excessive trading. Ultimately, Enforcement brought proceedings against iTrade and eleven individuals (including Spagnolo). Most of the cases involved sales practice violations such as unauthorized opening of accounts, unauthorized trading, and excessive trading.[10] The Firm was expelled from FINRA in a default decision issued on June 28, 2011, for opening accounts without customer authorization, unauthorized trading, suitability violations, false books and records, and other violations.[11]

As to Spagnolo, examiners identified instances during the review period from April 2008 through December 2009 in which Spagnolo opened accounts for customers and initiated trading in those accounts but where the customers refused to pay for the trading. FINRA staff contacted some, but not all, of the customers who refused to pay. Based on what the customers said in conversations with FINRA staff, the staff drafted declarations for the customers.[12]

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[7] Hearing Tr. (Spagnolo) 409-11.

[8] Hearing Tr. (Spagnolo) 411-12.

[9] Hearing Tr. (Spagnolo) 408-09.

[10] DiTrapani Decl. ¶¶ 3-8, 12-16; Hearing Tr. (DiTrapani) 280-81, 288-90.

[11] Disciplinary Proceeding No. 2009016059110.

[12] Hearing Tr. (DiTrapani) 290-92, 294-97, 352-58.

C. This Proceeding

Initially, the charges against Spagnolo were part of a Complaint that included separate claims against three other respondents, Nathalo Menendez, DP, and [redacted]. Menendez and DP, like Spagnolo, were registered representatives of the Firm who were charged with various sales practice violations. Menendez defaulted and did not defend the charges against him. DP died prior to the hearing, and the charges against him were dismissed.

[redacted] was the Chief Compliance Officer. He was charged with failing to supervise adequately and failing to report numerous customer complaints to FINRA. Prior to the hearing, [redacted] vigorously denied liability. At the hearing, he delivered an opening statement. However, he then announced that he did not intend to present any evidence in his defense and left without presenting any.[13] After the hearing, the Hearing Officer severed the charges against [redacted] and provided him additional time to submit written materials in his defense. The Hearing Panel is simultaneously issuing a separate decision on the charges against him finding that he committed the supervisory and reporting violations alleged in the Complaint. For the supervisory violations, the Hearing Panel bars him from associating with any FINRA member firm in any capacity.[14]

Although he declined to participate in the evidentiary portion of the hearing on his own behalf, [redacted] returned later to testify on Spagnolo's behalf.[15] [redacted] testimony established that the environment in which Spagnolo operated enabled, rather than proscribed, potential unauthorized and excessive trading.

D. The Firm's Method Of Doing Business And Spagnolo's Role

The Firm's representatives obtained business by cold-calling potential customers by telephone. The representatives used purchased lead cards. Each lead card contained some information about the customer, and after a call with the customer a representative would write down additional information learned on the call. Sometimes representatives would call a potential customer repeatedly. Sometimes customers would ask for materials to be sent to them. Sometimes new accounts would be opened as a result of these efforts and trading initiated. Information gathered from the telephone calls with customers would be memorialized on a new account application form and a type of trade confirmation and bill would be created as a notification of transaction.[16]

At iTrade, Spagnolo performed a specialized function that did not involve an ongoing relationship with customers. In his role as a cold caller and account opener, Spagnolo had the first contact with a prospective customer. He was responsible for obtaining authorization to open an account and for the initial trade in the account.[17] Spagnolo used lead cards in the initial

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[13] Hearing Tr. [redacted] 35-60.

[14] Disciplinary Proceeding No. 2009016159111.

[15] Hearing Tr. [redacted] 444-95.

[16] Hearing Tr. [redacted] 478-80; Hearing Tr. (DiTrapani) 283-86.

[17] Hearing Tr. (Spagnolo) 413-14.

contact with a prospect and kept notes of his subsequent conversations with the person on the card.[18]

When the prospect gave Spagnolo the information he needed to open an account, he would make a trade and give the lead card and notes to a sales assistant who would complete the account opening form.[19] Spagnolo needed a social security number before he could make a trade for the person.[20]

After the account was opened, Spagnolo generally would make a follow-up call to let the customer know he had sent the customer a package of information by FedEx. The package contained a return FedEx envelope for the customer to send payment for the initial trade. The follow-up call was also part of an effort "to get the money in."[21] After five days, if the Firm did not receive payment, the transaction was treated as a "renege," meaning that the customer had decided to back out of the transaction.[22] Spagnolo testified that he did not pursue a customer after the customer reneged on a trade. Any subsequent contacts between the Firm and the customer were with another broker who partnered with Spagnolo.[23]

At least some of the time, Spagnolo had the highest renege rate of any of the account openers at iTrade.[24] During the relevant period, his renege rate was close to 30%.[25] Spagnolo explained the large number of reneges by the fact that he also had the most accounts opened.[26] During the review period, from April 2008 through December 2009, Spagnolo was responsible for opening approximately 200 new accounts. Out of the 200 new accounts, 59 were cancelled by the customers and treated by the Firm as reneges.[27]

E. The Firm's Lack Of A Good Compliance Culture

The Firm lacked a good compliance culture. The problem started at the top, with [redacted] the Chief Compliance Officer. Although between April 2008 and the end of 2009 customers rejected more than 18% of the initial trades in new accounts that iTrade submitted to its clearing firm, and some representatives, including Spagnolo, had a renege rate as high as 30%, [redacted] showed little concern.[28]

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[18] Hearing Tr. (Spagnolo) 414-15, 417-18.

[19] Hearing Tr. (Spagnolo) 413-24 (discussing a specific example).

[20] Hearing Tr. (Spagnolo) 421.

[21] Hearing Tr. (Spagnolo) 514.

[22] Hearing Tr. (Spagnolo) 516.

[23] Hearing Tr. (Spagnolo) 415-20, 514-18.

[24] Hearing Tr. (Spagnolo) 539-40.

[25] Hearing Tr. (DiTrapani) 294-96, 369-70; Hearing Tr. (Sanders) 457-58.

[26] Hearing Tr. (Spagnolo) 540.

[27] Hearing Tr. (DiTrapani) 294-95.

[28] Hearing Tr. [redacted] 457-58.

testified that customer reneges are common and inevitable in the cold-calling business. Customers first say they want to make a trade and then later refuse to pay, particularly if the investment has declined in value between the initial telephone authorization and the completion of the paperwork for the transaction. According to even when he investigated why a customer refused to pay for a trade he determined that 99% of the time "it was authorized and it's just a renege."[29] He was vague, however, on what if anything he did beyond exhorting registered representatives to decrease the number of customer reneges.[30]

also asserted that registered representatives at the Firm had no incentive to engage in unauthorized account opening or unauthorized trading, an argument made by Spagnolo. explained that representatives bore various costs if a customer refused to pay for a trade, including a $50 cancellation fee, a $50 ticket fee, FedEx charges of $16 to $20 each way for the paperwork sent to the customer, and any loss on the trade—while the Firm retained any gain on the trade.[31]

As a factual matter, assertion is incorrect. failed to recognize that a registered representative might make up the costs of some unauthorized trades if the representative's volume was increased by persuading at least some customers to ratify trades they did not initially intend to authorize. Nor did he recognize that the high pressure tactics that led to unauthorized trades might yield a higher rate of authorized transactions, making up for some of the losses associated with customer reneges. also failed to recognize that the Firm itself had an incentive to permit unauthorized trading if it retained the gains on such trades without absorbing the costs or losses associated with them. The Hearing Panel did not find credible on his views about the inevitability of large numbers of reneges.

Indeed, in another disciplinary proceeding, *Shevlin*, the same argument was rejected. In that proceeding, a Hearing Panel found "it more likely that [the respondent] was willing to take the chance that potential customers would not complain, and that he could retain them as customers."[32]

testimony illustrated the environment in which Spagnolo operated. It was an environment that did not support ethical conduct or good care in the treatment of customers. There was little concern for the duties that the Firm and its registered representatives owed their customers—duties to act honestly, ethically, and in good faith.

evidence set a backdrop for Spagnolo's conduct and showed that it was *possible* that he engaged in unauthorized account opening and unauthorized trading that the Firm did not recognize as wrongdoing, and that it was *possible* that he provided false and inaccurate information on new account forms to facilitate his unauthorized trading. Even so, the lack of ethics at the Firm is not enough to prove Enforcement's case.

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[29] Hearing Tr. 451.

[30] Hearing Tr. 470.

[31] Hearing Tr. 446-49.

[32] *Joseph Brian Shevlin, Jr.*, No. C10020075, 2003 NASD Discip. LEXIS 46, at *32 (OHO Oct. 2, 2003).

F. Customer Evidence On Lack Of Authorization (First Cause Of Action) And Accuracy Of Information Provided To Open Accounts (Second Cause Of Action)

With respect to Spagnolo, Enforcement alleged that he opened accounts for eight customers and made initial trades in the accounts without authorization. It also alleged that he provided false and inaccurate information regarding the customers' financial situation, investing experience, and goals.

The Hearing Panel does not doubt that Spagnolo applied high pressure tactics when he contacted the customers, but the record is insufficient to establish that Spagnolo was not authorized by the eight customers to do what he did. The evidence supports an inference that he had a colorable basis for thinking that he was authorized, although it also supports an inference that he pressed exasperated customers into giving him the information required to authorize the opening of accounts and trading knowing that no one could say for sure whether the customers did or did not authorize it. The evidence does not provide the tipping point in favor of Enforcement required by the preponderance of the evidence standard.

Similarly, the customers' evidence regarding their financial situation was contradictory, casting doubt on evidence that Spagnolo provided false and inaccurate information to the Firm when he opened the accounts. The evidence did not rise above the level of suspicion.

1. Four Customers Who Testified

All four customers who testified denied authorizing Spagnolo to trade on their behalf. They did say that they had multiple conversations with him and that they asked him to send them information.

The four customers did not merely provide mailing address information, however. They provided Spagnolo with the kind of personal information that is required to open an account and trade. In particular, they provided him with social security numbers. They also provided birth dates, annual income, amounts invested in other investments, prior investment experience, and other items that were unnecessary if all they asked was to receive a packet of information.

The Hearing Panel finds that the provision of such personal information, particularly including the social security numbers, undercuts the assertion that the customers did not authorize Spagnolo to open an account or to trade. The provision of such information is consistent with a grant of authority. This evidence does not affirmatively show that Spagnolo was authorized, but it has significance in balancing the evidence.

The Hearing Panel also finds the testimony of some of the four customers who testified was confused, contradictory, and generally unreliable. The testimony of one customer even suggested that the customer planned to renege. Sometimes their testimony contradicted what they had previously told Enforcement.

The testimony of the four customers is discussed below in more detail.

(a) Customer ES

ES, now fifty-six years old, was working as a vice president of operations for a manufacturing company in California in 2008 when Spagnolo called him. ES had not heard of iTrade and did not know Spagnolo.[33]

ES testified that Spagnolo pushed him to buy a particular stock referred to as UYM. ES denied authorizing Spagnolo to do it. ES claimed that he had told Spagnolo to send him information that he would consider before making his decision.[34]

According to ES, Spagnolo told him that he needed information from ES before he could do that. In particular, Spagnolo told him that he could not send him information without obtaining ES's social security number. ES gave Spagnolo an incorrect social security number because was worried about what was going on.[35]

Spagnolo sent ES a packet of material after having opened an account and bought shares of UYM on behalf of ES. ES told Spagnolo he was not buying anything, but Spagnolo and others from the Firm made multiple calls that ES described as harassment to persuade ES to pay for the stock.[36] ES did not pay for the stock.[37]

Some of ES's testimony undercuts his assertion that he did not authorize Spagnolo to open an account and trade on his behalf.

First, ES acknowledged that he gave Spagnolo a large amount of personal information in addition to the social security number, including his wife's name, his home address, and his business, home and cell telephone numbers. He also told Spagnolo about his bank account and how he was interested in experimenting in the stock market.[38] That information—and particularly the social security number—was unnecessary if ES told Spagnolo only that he should send some information for ES to consider.

Second, ES was unsophisticated about the stock market but he was actively engaged in it. He testified that during the same period he had an account at E*Trade in which he had bought six to eight stocks. He had gotten interested in trading and making his own decisions because he had friends who were trading.[39] ES testified, "The market was down, so I thought it might be a good time to try it."[40] ES testified that the amount in his E*Trade account was only $10,000. It was a

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[33] Hearing Tr. (ES) 70-72.

[34] Hearing Tr. (ES) 72.

[35] Hearing Tr. (ES) 73, 76.

[36] Hearing Tr. (ES) 73-74, 86.

[37] Hearing Tr. (ES) 90, 92-93.

[38] Hearing Tr. (ES) 94-96.

[39] Hearing Tr. (ES) 96-98.

[40] Hearing Tr. (ES) 97.

small amount compared to his income.[41] The small amount he was willing to risk suggests that he was not very aggressive overall in his investment strategy, but he was in a position to risk that relatively small amount on more speculative investments and to experiment.

Third, ES testified that he "wanted to see what [Spagnolo] had. If I thought it was a good deal, I could have called him back and given him the correct [social security] number."[42] This testimony can be interpreted as ES intentionally misleading Spagnolo as to his authorization. It appeared that ES planned to accept any transaction after the trade if it suited him to do so. At the same time, by providing Spagnolo a false social security number ES thought he could walk away from any trading if he wanted to do that.

In sum, the testimony of ES was wholly inadequate to establish by a preponderance of the evidence that Spagnolo acted without authorization.

(b) Customer REM

REM was seventy-three at the time of his testimony. After graduating from college, he worked at IBM for forty-three years. He traveled all over the world developing IBM products for key customers like Boeing. In 2008, he retired, taking his retirement money in a lump sum, which he then began investing. Prior to retirement, he had relied on IBM to invest his retirement account.[43]

Spagnolo first called REM in spring 2009. REM did not know Spagnolo or the Firm.[44] Spagnolo called REM approximately once a week, then once a day, and finally several times a day. At first they spoke generally, but then the conversation focused on a particular stock that Spagnolo wanted REM to purchase. That stock was referred to by the initials CBI. Spagnolo was "opinionated" and "determined." REM said that on one day they had a three-hour conversation. Sometimes one or the other would hang up. But then one or the other would call back and restart the conversation.[45]

In September 2009, REM received material from iTrade and from Sterne Agee, iTrade's clearing firm,[46] that indicated stock had been purchased in his name. REM protested to Spagnolo that he had never said he would buy the stock. Spagnolo argued with him that he needed to accept the trade or he would ruin Spagnolo. REM then called Sterne Agee to cancel the transaction, saying that he did not agree to buy the stock. Sterne Agee said it would cancel the transaction and directed him to customer service at iTrade and a government agency. He

[41] Hearing Tr. (ES) 96, 101-02.

[42] Hearing Tr. (ES) 99.

[43] Hearing Tr. (REM) 123-25, 132.

[44] Hearing Tr. (REM) 125.

[45] Hearing Tr. (REM) 126-28, 148-49.

[46] Hearing Tr. (REM) 139-40.

then called iTrade, which agreed to do what was necessary at its end to cancel the transaction. He never called the government agency.[47]

Although REM clearly believed he never authorized Spagnolo to open an account and trade, he gave Spagnolo the information necessary to trade. He gave Spagnolo his social security number, along with his birth date, home telephone number, and information regarding the credit union with which he had an account. In his testimony, REM confirmed that information on the new account form at the Firm that Spagnolo filled out for him was correct, including the amount that REM had invested in stock and REM's net worth.[48] It was not necessary for REM to provide such information if he and Spagnolo were just talking.

REM's testimony also was somewhat confused and imprecise. At first, he did not understand a question about annual income and asked if it was a question of whether he made $100,000 every month.[49] Once he understood the question, REM still did not answer it correctly. He talked about the sums he received on a monthly basis ($4,000 out of his retirement account, supplemented by $1,800 in social security), which totaled $69,600 on an annual basis.[50] He forgot until later in his testimony that he also had some investment returns.[51]

REM's testimony as to his net worth and the value of stocks differed from statements he initially made to Enforcement regarding these matters. Enforcement appropriately acknowledged the difference in closing argument and modified its charges against Spagnolo to eliminate charges based on net worth and stock value.[52]

REM also was confused about the circumstances in which his declaration had been created. He testified that his declaration was written within days of the September 2009 transaction at issue, but the document was actually dated roughly a year later, in September 2010. When asked about the discrepancy, REM testified that he may have misdated it. He then asserted that the misdating did not matter. Additional questioning made it plain, however, that the declaration was not misdated. It was the result of emails and drafts exchanged with FINRA in 2010.[53] REM also testified that he composed and typed the declaration, but it became apparent that he did not type the declaration. Rather it was typed by FINRA staff based on what he told them.[54]

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[47] Hearing Tr. (REM) 128-30, 139-40, 166-73.

[48] Hearing Tr. (REM) 153-159

[49] Hearing Tr. (REM) 134.

[50] Hearing Tr. (REM) 124-25.

[51] Hearing Tr. (REM) 160-62.

[52] Hearing Tr. (Enf. closing) 571.

[53] Hearing Tr. (REM) 173-75.

[54] Hearing Tr. (REM) 162-65; Hearing Tr. (DiTrapani) 292.

In sum, REM's testimony did not establish by a preponderance of the evidence that Spagnolo acted without authorization or that he provided false and inaccurate information on the account opening form.

(c) Customer RLE

RLE has been semi-retired since 2009. He was almost ninety years old at the time of the hearing. Prior to retirement he was an independent distributor for Shaklee products.[55]

Spagnolo first called RLE in 2008, trying to sell him stock. RLE described him as aggressive. RLE testified that he never agreed to purchase any securities from iTrade.[56]

When RLE received a bill and some stock certificates he was shocked. He tried complaining to iTrade, but found them unresponsive.[57]

RLE's daughter sent a letter to iTrade saying her father would not pay for the trade.[58] However, RLE was not positive that she did so. The letter was accompanied by a declaration signed by RLE and dated February 16, 2010. RLE could remember nothing about the declaration including who wrote it. He was unsure whether he or his daughter wrote it.[59]

By November 2008, RLE considered himself a conservative investor because he was "no longer speculating."[60] He testified that he had held an interest in a gold mining company. He could not recall whether he told that to Spagnolo. He testified that he lost $1.3 million on that investment. Even so, he declined to call it speculative.[61]

RLE could remember almost nothing that he might have told Spagnolo about his risk tolerance, experience, annual income, or net worth.[62] However, at least some of the information on the new account form regarding his annual income and net worth appeared to be accurate. In 2008, RLE had a residual annual income from Shaklee of over $500,000, just as reflected on the new account form.[63] That was information that could have only come from RLE, and that information was only necessary if he was going to open an account to trade.

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[55] Hearing Tr. (REM) 183-84.

[56] Hearing Tr. (RLE) 184-86.

[57] Hearing Tr. (RLE) 186-87.

[58] Hearing Tr. (DiTrapani) 304-06; CX-7.

[59] Hearing Tr. (RLE) 187-88, 204-208, 214-17.

[60] Hearing Tr. (RLE) 188-89.

[61] Hearing Tr. (RLE) 202-04.

[62] Hearing Tr. (RLE) 192-95.

[63] Hearing Tr. (RLE) 190-94, 198.

RLE also provided Spagnolo with his social security number and birth date, along with additional telephone numbers.[64] He could not remember doing so, but he testified that he "maybe" provided the information or "must have" provided it.[65]

RLE's testimony regarding his annual income contradicted what he had previously told Enforcement. He testified that his annual income was $500,000 per year, as recorded in the new account form. But he had told Enforcement that his annual income was $350,000.[66]

The Hearing Panel finds that RLE's memory was imperfect at best. He remembered being pressured by Spagnolo, but he could not remember any details. It is apparent that he provided Spagnolo a substantial amount of information that was accurately reflected in the account opening form and that was only necessary if authorizing an account to be opened for trading. RLE's testimony does not establish that Spagnolo acted without authorization or that Spagnolo provided false and inaccurate information on the account opening form.[67]

(d) Customer CLH

CLH owns a small construction company and a management company in South Carolina. He is now fifty-nine years old.[68]

CLH did not know Spagnolo or iTrade before Spagnolo started calling him.[69] CLH said that he gets calls like Spagnolo's on a regular basis.[70]

CLH denied authorizing Spagnolo to open an account or to purchase stock on his behalf.[71] However, he did not recall the specifics of his conversations with Spagnolo, and he hedged much of his testimony with contingent language. He spoke in terms of what "would have been" and "could possibly have been."[72] He said, "I'm speculating."[73] He acknowledged that he "may have" discussed topics like his experience and the value of his stock holdings with Spagnolo.[74] He continued in that vein, discussing what he "would have" said to Spagnolo, but

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[64] Hearing Tr. (RLE) 209-14.

[65] Hearing Tr. (RLE) 208-13.

[66] Hearing Tr. (DiTrapani) 401-04.

[67] Sanders, the Chief Compliance Officer, testified that he spoke to RLE's daughter and that she told him that her father had dementia. Hearing Tr. (Sanders) 450-52, 458-60. The Hearing Panel does not rely on this testimony because it does not find Sanders credible with regard to customer interactions. The contradictions in RLE's hearing testimony, however, also made it impossible to rely on RLE's testimony.

[68] Hearing Tr. (CLH) 229-30.

[69] Hearing Tr. (CLH) 230-31.

[70] Hearing Tr. (CLH) 230, 232, 253.

[71] Hearing Tr. (CLH) 232-33.

[72] Hearing Tr. (CLH) 233.

[73] Hearing Tr. (CLH) 233.

[74] Hearing Tr. (CLH) 233.

not what he did say.[75] He admitted he did not remember specifically his discussion with Spagnolo regarding opening an account.[76]

Like the other customers who testified, CLH gave Spagnolo his social security number. Although he did not recall giving that information to Spagnolo, it was entered on CLH's new account form.[77] Spagnolo had other personal information that CLH testified had to come from him, although he did not recall giving it to Spagnolo. CLH said that the figures Spagnolo had supplied for annual income, net worth, and common stock investments were what he would have told Spagnolo.[78]

CLH said that he did not worry much about talking with people.[79] When asked why he provided so much personal information to Spagnolo, he said he was just "listening."[80] He described himself as too nice to hang up the telephone.[81]

CLH could not remember the circumstances in which he signed his declaration. He could not even remember whether he had prepared and typed it or had been handed it to sign.[82]

~~CLH volunteered that he had "backed out" of a Sterne Agee account some years ago, but~~ asserted that he "had quit doing this at this time frame."[83] It was unclear what CLH meant by this, but it could have meant that he had reneged on some trades in the past. He also testified that in the past he had speculated and lost substantial amounts of money.[84] CLH volunteered that he had received such cold calls before. He said that others had called and pushed him to buy stock. This suggests that he was accustomed to high pressure sales tactics and knew the significance of the information he provided Spagnolo.[85]

Spagnolo bought three hundred shares of a stock for CLH. CLH refused to pay for the stock. He asserted that he had not authorized Spagnolo to open an account or buy stock on his behalf.[86]

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[75] Hearing Tr. (CLH) 234-35.

[76] Hearing Tr. (CLH) 252.

[77] Hearing Tr. (CLH) 265-66.

[78] Hearing Tr. (CLH) 266-71.

[79] Hearing Tr. (CLH) 266.

[80] Hearing Tr. (CLH) 271.

[81] Hearing Tr. (CLH) 272.

[82] Hearing Tr. (CLH) 263-64.

[83] Hearing Tr. (CLH) 253-54.

[84] Hearing Tr. CLH) 254-55, 257-58.

[85] Hearing Tr. (CLH) 230, 232.

[86] Hearing Tr. (CLH) 238-42, 274-78.

The Hearing Panel finds that CLH's testimony is insufficient to establish that Spagnolo acted without authorization or that he provided false and inaccurate information on the account opening form.

2. Four Customers Who Did Not Testify

As to the four customers who did not testify, their declarations and new account forms were admitted into evidence. Three of these customers asserted that they did not authorize Spagnolo to open an account or to trade on their behalf. The fourth declared that he authorized Spagnolo to open an account but not to trade.[87]

The new account forms filled out on behalf of these four customers, like the new account forms of the four customers who testified, contain social security numbers and other personal information.[88] This information could only have come from the customers and was necessary only if Spagnolo was going to open an account and trade for the customer. As noted above, the provision of such information to Spagnolo is consistent with authorization to open an account and trade in it. Although giving Spagnolo a social security number does not prove that a customer authorized Spagnolo to do what he did, it creates a need for reliable evidence, rather than suspicion, to establish that he was not authorized.

The examiner who discussed the preparation of the declarations could not remember which ones he drafted and which ones were drafted by others. Although he spoke to seven of the eight customers, he also could not remember any specifics of the conversations. He relied on the declarations to be accurate reflections of what the customers said.[89]

The Hearing Panel declines to rely on the declarations of the four customers who did not testify, either in connection with the claim of unauthorized trading or in connection with the claim of providing false and inaccurate information to be entered into the Firm's books and records. In light of the inconsistencies and problems uncovered in the testimony of the four customers who testified, and the examiner's lack of specific recollection regarding the FINRA staff's conversations with the non-testifying customers, the declarations are too unreliable.[90] In the circumstances of this case, the declarations are insufficient to establish by a preponderance of the evidence that Spagnolo acted without authorization or that he provided false and inaccurate information on the new account forms.

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[87] CX-4, CX-12, CX-18, and CX-20.

[88] Hearing Tr. (DiTrapani) 291-92. See the discussion of the declarations of the other four customers: Hearing Tr. (DiTrapani) 299-303 (customer MB, CX-4 and CX-5); Hearing Tr. (DiTrapani) 309-21 (customer BL, CX-12 and CX-13); Hearing Tr. (DiTrapani) 327-31 (customer JS, CX-18 and CX-19); Hearing Tr. (DiTrapani) 331-36 (customer HW, CX-20 and CX-21).

[89] Hearing Tr. (DiTrapani) 371-82 (discussion of all eight customer declarations relating to Spagnolo).

[90] Hearing Tr. (DiTrapani) 377.

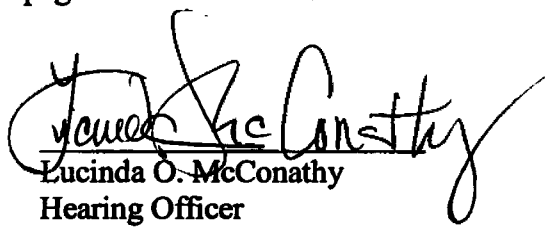
IV. CONCLUSIONS

The Hearing Panel concludes that Enforcement failed to prove by a preponderance of the evidence that Spagnolo lacked authorization to open accounts for the eight customers or to initiate trades on their behalf. At most, Enforcement proved that Spagnolo's renege rates were suspiciously high and that it was possible that he took advantage of ambiguities in his discussions with the customers. Although the SEC has said that renege rates as high as Spagnolo's are red flags that require an immediate and intensive investigation,[91] the high renege rates alleged in the Complaint are not sufficient without more to prove that the particular transactions were unauthorized.

Similarly, the Hearing Panel concludes that Enforcement failed to prove by a preponderance of the evidence that Spagnolo provided false and inaccurate information on new account forms for entry into the Firm's books and records. All of the customers who testified appeared somewhat confused and uncertain regarding what they told Spagnolo. At least two of the customers who testified said that information Spagnolo entered on their forms was correct, contradicting their own declarations and allegations in the Complaint regarding them.

V. ORDER

The charges against Respondent Anthony Spagnolo are dismissed.[92]



Lucinda O. McConathy
Hearing Officer
For the Hearing Panel

Copies to: Anthony Spagnolo, III (via first-class, overnight mail and email)
Stephen B. Wexler, Esq. (via first-class mail and email)
Brian Boxler, Esq. (via email)
Nathalo Menendez (via first-class mail)
Jonathan Golomb, Esq. (via first-class mail and email)
Edwin T. Aradi, Esq. (via email)
Jeffrey D. Pariser, Esq. (via email)

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[91] *Monroe Parker Securities, Inc.*, Exchange Act Release No. 39057, 1997 SEC LEXIS 1885, at *11 (Sept. 11, 1997). The SEC said that a firm's high rate of reneges, close to 38% but sometimes as low as 26.99%, was "by any objective standard" a "red flag" that "should have indicated an urgent need for investigation of the Firm's sales practices." The SEC continued, "We have frequently found that excessive reneges or cancellations are indicative of underlying compliance problems and may be evidence of violations. Our concern is heightened by the [f]irm's casual response to the excessive cancellations. Its failure to investigate or institute remedial measures demonstrates a lack of adequate supervision...." *Id.* at *11-12.

[92] The Hearing Panel has considered and rejects without discussion any other arguments made by the Parties that are inconsistent with this decision.