

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. E072005009201**

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REGISTRATION & DISCLOSURE

TO: Department of Enforcement
Financial Industry Regulatory Authority ("FINRA")

RE: GunnAllen Financial, Inc., Respondent
[CRD No. 17609]
and
Kelley A. McMahon, Respondent
Equity Trader, Financial and Operations Principal, General Securities Principal,
General Securities Representative and Municipal Securities Principal
[CRD No. 2394493]

Pursuant to NASD Rule 9216 of FINRA's Code of Procedure, GunnAllen Financial, Inc. and Kelley A. McMahon submit this Letter of Acceptance, Waiver and Consent ("AWC") for the purpose of proposing a settlement of the alleged rule violations described below. This AWC is submitted on the condition that, if accepted, FINRA will not bring any future actions against me alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

- A. I hereby accept and consent, without admitting or denying the findings, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to which FINRA is a party, prior to a hearing and without an adjudication of any issue of law or fact, to the entry of the following findings by FINRA:

BACKGROUND

GunnAllen Financial, Inc. has been a member of FINRA (f/k/a National Association of Securities Dealers or NASD) since June 10, 1986. During all periods mentioned herein, GunnAllen Financial, Inc. was a registered broker-dealer with the United States Securities and Exchange Commission and a member of FINRA.

Kelley A. McMahon entered the securities industry on September 15, 1993 as a General Securities Representative of Citigroup Global Markets Inc., a member of FINRA (f/k/a National Association of Securities Dealers or NASD). Kelley A. McMahon, during all periods mentioned herein, was associated with member firm GunnAllen Financial, Inc., and was registered with FINRA under Article V of the By-Laws as an Equity Trader,

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Financial and Operations Principal, General Securities Principal, General Securities Representative and Municipal Securities Principal, which registrations remain currently in effect.

RELEVANT PRIOR DISCIPLINARY HISTORY

GunnAllen Financial, Inc. has been the subject of the following relevant formal disciplinary actions:

NASD Case No. C07030033: On May 13, 2003, a Letter of Acceptance, Waiver and Consent submitted by GunnAllen Financial, Inc. was accepted wherein the firm, on the basis of findings by FINRA of violations of Conduct Rule 3070(A)(8) and By-Laws Art. V. Sec. 2, in that it failed to report five settlements of customer claims in excess of \$25,000 within ten business days and failed to report two Form U-4s to reflect that customer arbitrations had been settled, agreed to sanctions consisting of a \$7,500 fine.

NASD Case No. C07030066: On September 29, 2003, a Letter of Acceptance, Waiver and Consent submitted by GunnAllen Financial, Inc. was accepted wherein the firm, acting through an individual, on the basis of findings by FINRA of violations of Membership and Registration Rule 1017, in that it failed to obtain FINRA approval prior to effecting a material change in business operations by expanding its number of registered representatives and branch offices beyond the limits delineated in IM-1011-1, agreed to sanctions consisting of a censure and fine of \$10,000, of which \$5,000 was joint and several.

NASD Case No: C07050004: On January 18, 2005, a Letter of Acceptance, Waiver and Consent submitted by GunnAllen was accepted wherein the firm agreed to a \$30,000 fine for violations of, among other rules, NASD Conduct Rule 3011, in that the firm had failed to obtain at least two foreign bank certificates and had not closed the subject accounts within 10 days as required by its written supervisory procedures.

Kelley A. McMahon has not previously been the subject of a formal disciplinary action by any regulatory body.

OVERVIEW

This case involves violations by GunnAllen Financial and one of its principals based upon conduct that occurred between 2000 and 2007 (as more fully particularized herein), including a violative trade allocation scheme perpetrated by the firm's former head trader; a failure to report a business relationship with a barred individual; deficient

supervision and supervisory procedures relating to certain activities; deficient filings of Forms U4 and U5; filing deficiencies under Conduct Rule 3070; failure to preserve instant messages and e-mails; and failure to implement an adequate anti-money laundering compliance program.

FACTS AND VIOLATIVE CONDUCT

1. Alexis J. Rivera's Trade Allocation Scheme

GunnAllen Financial, Inc., acting through Alexis J. Rivera, its former head trader, engaged in a violative trade allocation, or "cherry picking," scheme during the period from January 2002 through December 2003.

During the relevant period, certain registered representatives of the firm aggregated retail customers' day trading orders and communicated an opening transaction to Rivera by telephone or instant messaging. Rivera, knowing by experience that the representatives generally engaged in day trading and that an opening transaction would be followed the same day by a closing transaction, would work the order in a firm proprietary account, sometimes allocating a first profitable trade to his wife's personal account. For example, on October 8, 2003, at 11:47:22, Rivera received an order to short sell 10,000 shares of Linear Technology Corporation common stock (LLTC) and executed the trade at a price of 39.40. At 11:47:43, Rivera covered the short position at a price of 39.335 for a profit of \$650 and allocated the trades to his wife's account. Later the same day, at 14:24:33, Rivera again sold short 10,000 shares of LLTC at a price of 39.32 and then covered the position between 15:09:28 and 15:45:45 at an average price of 40.14. He allocated those trades and the resulting loss of \$8,200 to the accounts of the customers whose orders comprised the 10,000 share block order.

During the relevant period, Rivera effected 446 buy and 446 sell transactions in his wife's account, most of which were handled in substantially the manner described above. Of these transactions, 91 percent were profitable, earning his wife \$270,194.¹

In addition, by virtue of this conduct, the firm, acting through Rivera, at times did not give the affected customers best execution when it delayed execution of customer orders, allowing Rivera's wife to take trading profits, and subsequently executed trades for the customers at prices less favorable than the prevailing inter-dealer price at the time of receipt of the customers' orders.

¹ On September 2, 2005, the Firm terminated Rivera. On December 8, 2006, FINRA accepted a Letter of Acceptance Waiver and Consent submitted by Rivera in which, without admitting or denying FINRA's findings relating to the matter described herein, he agreed to accept sanctions of a bar from association with any member of FINRA in any capacity.

In addition, the firm, acting through Rivera, neglected to maintain accurate times of entry and execution for the customer orders discussed above, or to make and retain memoranda of purchases and sales for the account of Rivera's wife.

By virtue of such conduct, GunnAllen Financial, Inc. violated Section 10(b) of the Securities Exchange Act of 1934, SEC Rule 10b-5 thereunder, Section 15(c) of the Exchange Act, SEC Rule 15c1-2 thereunder, Section 17(a) of the Exchange Act and SEC Rules 17a-3 and 17a-4 thereunder, NASD Conduct Rules 2120, 2320 and 2110; and NASD Conduct Rule 2110 by violating Section 17(a) of the Securities Act of 1933.

2. Failure to report business activity with person subject to statutory disqualification

GunnAllen Holdings (the majority owner of GunnAllen Financial, Inc.) entered into a contract dated January 30, 2003, with Richard J. Gladstone, a barred individual.² Pursuant to the contract, which was reviewed and approved internally at GunnAllen Financial, Inc. and signed by Richard A. Frueh (Chief Executive Officer of GunnAllen Financial, Inc.) and by Gladstone. Gladstone was to be paid \$5,500 per month for providing to GunnAllen Financial, Inc. services relating to its business. In fact, Gladstone was paid at irregular intervals through 2004. GunnAllen Financial, Inc., failed to report to FINRA the business relationship with Gladstone.

Such acts, practices, and conduct constitute separate and distinct violations of NASD Conduct Rules 3070(a)(9) and (b) and 2110 by GunnAllen Financial, Inc.

3. Supervisory Deficiencies

During the period from 2002 through 2005, the firm's supervisory systems and written procedures were deficient in the following areas:

- a. Between January 2003 through December 2003, the firm, acting through Kelley A. McMahon, failed reasonably to supervise Alexis J. Rivera in connection with Rivera's fraudulent trade allocation scheme discussed in Section I A 1 above. McMahon was manager of the Trading Desk and was Rivera's immediate supervisor. In particular, the supervision of Rivera's trading in his wife's personal account was deficient, as there was no follow up on the red flags raised by the extraordinary percentage of profitable trades in the account.
- b. Prior to March 2005, the firm's investment banking department was supervised by a three or four member committee that was made up of persons whose responsibilities included structuring investment banking deals, informing retail staff about firm underwritings and controlling proprietary accounts that traded stocks to be underwritten by the firm during periods when trading should have been restricted.

² See DBCC No. 7 v. Morgan Gladstone & Co., Complaint Nos. ATL-1084 (C07890005) and ATL-1224 (C07900030), 1992 NASD Discip. LEXIS 100 (NBCC 1992).

Prior to March 2005, the firm never put any stock on a restricted or watch list, notwithstanding the need to do so because of investment banking business being conducted by the firm. Prior to March 2005, the investment banking department did not inform the compliance department in writing of its banking activities. During the relevant time period, the firm never put written procedures in place to prevent trading in stocks while the firm was in possession of investment banking information. Thus, during the relevant time period, the firm did not establish, maintain and enforce written policies and procedures reasonably designed to prevent the misuse of material, nonpublic information by the firm or its associated persons.

- c. Between April 2003 and January 2005, GunnAllen Financial, Inc. failed to have a supervisory system, including written procedures, reasonably designed to ensure that mark-ups and commissions on equity securities transactions were fair and reasonable. The firm allowed its brokers significant discretion in setting commissions on transactions. Although the firm's written procedures made reference to the seven factors for determining the reasonableness of charges as set forth in IM-2440, in practice, the procedures at the Firm's headquarters consisted primarily of a review of transactions by a designated employee to ensure that charges did not exceed 5 percent. The firm employed inadequate systems and procedures with respect to determining the reasonableness of such charges.
- d. Between April 2003 and January 2005, the firm's supervisory system was deficient as it related to the surveillance of accounts for excessive trading or churning, in particular, with respect to small accounts.

By virtue of such deficiencies in the firm's supervisory systems and written procedures, GunnAllen Financial, Inc. violated Section 15(f) of the Securities Exchange Act of 1934 and NASD Conduct Rules 3010 and 2110, and Kelley A. McMahon violated NASD Conduct Rules 3010 and 2110.

4. Rule 3070 reporting violations and Forms U4 and U5 Filing Violations

During the period from July 1, 2003 through June 1, 2007, GunnAllen Financial, Inc. failed to properly file reports pursuant to NASD Conduct Rule 3070 as follows:

Disclosures relating to complaints, settlements, arbitrations/litigations, and regulatory actions required under Rule 3070(a): Five disclosures not filed and one disclosure filed late.

Quarterly reports required under Rule 3070(c): Four reports not filed and ten reports filed late. In addition, the quarterly reports filed during the relevant time period contained 87 errors.

Each such instance of a report that was not filed, filed late, or filed with errors constitutes a separate and distinct violation of NASD Conduct Rules 3070 and 2110 by GunnAllen Financial, Inc.

During the period from March 1, 2004 through February 15, 2005, GunnAllen Financial, Inc. failed to properly amend or file Forms U4 and U5 as follows: ten Forms U4 not amended as required; six amended Forms U4 filed late, one of which contained inaccurate information; eleven Forms U5 not amended as required; and ten Form U5 amendments filed late.

Each such instance of a Form U4 or Form U5 or amendment thereto that was not filed properly, not amended, or filed with inaccurate information constitutes a separate and distinct violation of FINRA Bylaws Article V, Sections 2(c) and 3(b) and NASD Conduct Rule 2110 by GunnAllen Financial, Inc.

5. Failure to Preserve E-mails and Instant Messages

During the period from January 2000 through September 2003, GunnAllen Financial, Inc. failed to preserve copies of all electronic communications sent and received by the firm's trading department. The firm did not retain copies of all instant messages and lost access to certain e-mails generated from January 2000 through September 2003 as a result of a change of the vendor providing e-mail services.

Such acts, practices, and conduct constitute separate and distinct violations of Section 17(a) of the Exchange Act and SEC Rule 17a-4, and NASD Conduct Rule 2110 by GunnAllen Financial, Inc.

6. Failure to implement an Anti-Money Laundering ("AML") compliance program

During the period from June 2003 through June 2005, GunnAllen failed to implement the firm's AML compliance program. In several instances, the firm failed to monitor, analyze, and report highly suspicious transactions.

Although the firm maintained certain AML procedures, as detailed below, in various instances these procedures were either deficient or not enforced. For instance, during the relevant period, the firm's AML procedures identified as possible AML "red flags" customers with multiple accounts under a single name or multiple names, with a large number of inter-account or third party transfers. The procedures also identified as possible AML red flags customer accounts with a large number of wire transfers to unrelated third parties. Upon identifying AML red flags, the firm's procedures required it to conduct further investigation of the activity that included gathering additional information internally or from third party sources, contacting the government, freezing the account and/or filing a SAR-SF. The firm failed to identify the above-mentioned red flags and/or failed to respond to them in accordance with its own procedures. In addition, the firm's AML procedures identified potential account-holders with questionable backgrounds as AML red flags and possible sources of money laundering and terrorist financing. However, the firm's procedures did not adequately specify what steps would be taken to monitor the added risk of those account-holders as red flags if their accounts

were opened.

Furthermore, the firm failed to provide adequate AML training to firm personnel who conducted AML surveillance reviews during the relevant period. Specifically, the firm's AML officer and surveillance analysts were not trained on how to conduct AML reviews, how to identify AML "red flags" and how to determine if and when to file Suspicious Activity Reports. In fact, during the period from June 2003 through June 2005, the firm provided no AML training in the aforementioned areas to the individuals working in the AML and surveillance departments.

Such acts, practices, and conduct constitute separate and distinct violations of NASD Conduct Rules 3011(a), (b) and (e) and 2110, and MSRB Rule G-41 by Respondent GunnAllen Financial, Inc.

OTHER FACTORS

B. I also consent to the imposition of the following sanctions:

As to GunnAllen Financial, Inc.: a censure and fine in the amount of \$750,000, \$25,000 of which is joint and several with Kelly A. McMahon.

As to Kelley A. McMahon: a fine in the amount of \$25,000 (joint and several with GunnAllen Financial, Inc.) and a six-month suspension from association with any member of FINRA in any principal capacity.

We agree to pay the monetary sanction(s) upon notice that this AWC has been accepted and that such payment(s) are due and payable. We have submitted an Election of Payment form showing the method by which we propose to pay the fine imposed.

We specifically and voluntarily waive any right to claim that we are unable to pay, now or at any time hereafter, the monetary sanction(s) imposed in this matter.

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

II.

WAIVER OF PROCEDURAL RIGHTS

I specifically and voluntarily waive the following rights granted under FINRA's Code of Procedure:

A. To have a Formal Complaint issued specifying the allegations against me;

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

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

I further specifically and voluntarily waive any right to claim that a person violated the ex parte prohibitions of NASD Rule 9143 or the separation of functions prohibitions of NASD Rule 9144, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including its acceptance or rejection.

III.

OTHER MATTERS

I understand that:

- A. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by the NAC, a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs ("ODA"), pursuant to NASD Rule 9216;
- B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against me; and
- C. If accepted:
 - 1. this AWC will become part of my permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against me;
 - 2. this AWC will be made available through FINRA's public disclosure program in response to public inquiries about my disciplinary record;

3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with NASD Rule 8310 and IM-8310-3; and

4. We may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. I may not take any position in any proceeding brought by or on behalf of FINRA, or to which FINRA is a party, that is inconsistent with any part of this AWC. Nothing in this provision affects my right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.

D. We may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. I understand that I may not deny the charges or make any statement that is inconsistent with the AWC in this Statement. This Statement does not constitute factual or legal findings by FINRA, nor does it reflect the views of FINRA or its staff.

I certify that I have read and understand all of the provisions of this AWC and have been given a full opportunity to ask questions about it; that I have agreed to its provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce me to submit it.

Jan 11, 2008
Date

GunnAllen Financial, Inc.

By: David H. Joris
DAVID H. JORIS
[Name and Title]
Executive Vice President
& General Counsel.

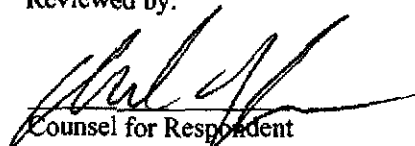
Reviewed by:

[Signature]
Counsel for Respondent
GunnAllen Financial, Inc.

1/11/08
Date

Keffey A. McMahon
Keffey A. McMahon, Respondent
Equity Trader, Financial and Operations
Principal, General Securities Principal,
General Securities Representative and Municipal
Securities Principal

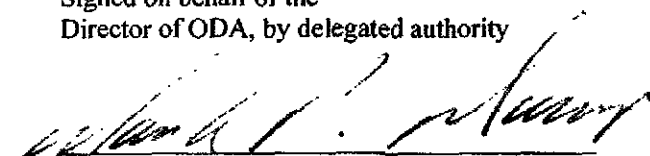
Reviewed by:


Counsel for Respondent
Kelley A. McMahon

Accepted by FINRA:

May 8, 2008
Date

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


Mark P. Dauer, Deputy Chief Litigation Counsel
FINRA, Department of Enforcement
1100 Poydras Street, Suite 850
New Orleans, Louisiana 70163-0802
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Attachment: Election of Payment Forms