BEFORE THE NATIONAL BUSINESS CONDUCT COMMITTEE

NASD REGULATION, INC.

In the Matter of District Business Conduct Committee For District No. 3 Complainant, vs. Aspen Capital Group, Inc. Denver, Colorado and Stephen Carlson Denver, Colorado, Respondents.	DECISION Complaint No. C3A940064 District No. 3 Dated: September 19, 1997

Aspen Capital Group, Inc. ("Aspen") and Stephen Carlson ("Carlson") have appealed, pursuant to NASD Procedural Rule 9310, a June 21, 1996, decision of the District Business Conduct Committee for District No. 3 ("DBCC"). We find that Aspen and Carlson violated Conduct Rule 2110 (formerly Article III, Section 1 of the Association's Rules of Fair Practice) by attempting to obtain stock at below-market prices by use of threats and coercion. Accordingly, it is ordered that: Aspen and Carlson be censured; fined $10,000, jointly and severally; and assessed $1,102.30 in costs, jointly and severally. It is also ordered that Carlson be barred in all capacities from associating with any member of the Association.

Factual Background

Carlson entered the securities industry in 1981, when he began working in the corporate finance department of Merrill Lynch. Carlson founded Aspen in 1985, and, at all times relevant to the complaint, was Aspen's sole owner, general securities principal, and president. Aspen became a member of the Association in 1985. Aspen's primary business was short-selling stocks, and Carlson was known in the industry for successful short-selling.[1]

[1]Neither Carlson nor Aspen remain in the securities industry: Aspen filed a Uniform

Prior to June 1994, Carlson recognized a short-selling opportunity in the stock of Teletek, Incorporated ("Teletek"). The price of Teletek stock recently had risen from pennies a share to more than $3 a share, but Carlson thought that Teletek's fundamentals failed to justify that valuation. Aspen became a market-maker for Teletek and assumed a short position. Aspen was short 3,000 shares as of March 31, 1994; 27,000 shares as of April 30, 1994; 62,300 shares as of May 31, 1994; 85,700 shares as of June 30, 1994, and 54,200 shares as of July 31, 1994.

According to Carlson, Paramount Securities was a primary buyer of Teletek stock. Carlson's industry sources informed him that Mike Swann and Lawrence Erber ("Erber") were undisclosed principals of Paramount Securities who were promoting Teletek stock. Carlson testified that large blocks of Teletek stock were being reported sold at prices 25 to 30 percent below the prevailing market price. Carlson formed the opinion that:

> this was Erber selling stock at two and three-quarters outside the market because he had it for nothing or for pennies per share, if he even paid for it, and he wasn't price sensitive. He in turn could offer that stock to his crooked brokers who can mark it up, not only to the offering but 5% above, and be able to illegally obtain a profit margin on the transactions not permitted by NASD guidelines.

Erber was familiar to Carlson prior to this time. Carlson believed that Erber was a former member of the securities industry; that Erber had pleaded guilty to felony charges of conspiracy to manipulate stock prices and wire fraud; and that Erber was permanently enjoined from engaging in a wide range of activities in the industry. Carlson also believed that Erber previously had manipulated the price of stock of American Gladiator ("GLAD"). Aspen had taken a short position in GLAD because, Carlson claimed, GLAD was a storefront operation with no business operations. Carlson claimed that he was instrumental in the Nasdaq Stock Market's ("Nasdaq") decision to delist GLAD's stock because he brought GLAD to the attention of Nasdaq officials. According to Carlson, Aspen profited when Nasdaq delisted GLAD's stock.

Carlson's alleged misconduct occurred during a June 9, 1994 telephone conversation with Erber, the substance of which is undisputed.[2] Erber placed the June 9, 1994 telephone call, in response to Carlson's earlier call. Carlson initially "congratulated" Erber on the GLAD situation, because he felt that "there were strong similarities between the GLAD situation and Teletek," and

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Termination Notice for Securities Industry Registration ("Form U-5") for Carlson in December 1995, and it filed its own Uniform Request for Broker-Dealer Withdrawal ("Form BDW") in January 1996. The Association, however, retains jurisdiction over the respondents pursuant to Article IV, Section 4 and Article III, Section 6 of the Association's By-Laws.

[2]It is also undisputed that the transcript derived from a tape recording of the conversation that Erber made. The staff obtained the tape recording from the Office of the U.S. Attorney for the Central District of California in November 1994.

he wanted to "let [Erber] know that I knew what he was up to, that he was up to another one of these stock manipulations, and that he wasn't pulling the wool over my eyes."

Carlson then requested a block of Teletek stock at a discounted price in exchange for Carlson's keeping silent about Erber's alleged promotion and manipulation of Teletek stock:

> Let me tell ya, we were intimately involved in getting GLAD delisted. OK? I am going to do the same thing to Teletek -- unless I get some stock from you on a favorable basis. I am gonna do what's called a magic trick--that's where I take your money and I turn it into my money.

Carlson repeated this quid pro quo later in their conversation:

> So, on Teletek--either I get a block of cheap stock or I am going to play a magic trick on you--OK--I am going to get that stock delisted next.

Carlson then accused Erber of being an undisclosed owner of Paramount Securities, an act that would violate a federal court order restricting Erber's participation in the securities industry. Carlson continued:

> Ya, if you want me to serve you up and wrap your f***ing nuts around your head I will. So you decide what you want Larry, we either play hard ball or . . . I get some of this cheap stock that keeps on printing in this pig.

Carlson concluded the conversation as follows: "[s]ave your breath--OK--buy me some stock or I'm gonna f***ing--I'm going to go after Teletek. Those are my terms--please get back to me--thank you."

Carlson did not speak with Erber again. Aspen later covered its short position in Teletek in the open market and made a profit on the transaction.

On April 21, 1995, the DBCC issued a decision finding that the respondents' conduct during the June 9, 1994, telephone conversation violated Conduct Rule 2110. The DBCC imposed the following sanctions: censure, $10,000 fine, joint and several, and $1,102.30 in costs, joint and several. The DBCC also suspended Carlson for 30 days. The respondents appealed. On September 6, 1995, we granted the staff's motion to adduce new evidence and to remand the

matter to the DBCC.[3] On June 21, 1996, the DBCC issued a new decision, reiterating the findings and imposition of sanctions contained in the initial decision.

Discussion

Respondents raise three issues on appeal: (1) whether the DBCC erred in concluding that Carlson and Aspen attempted to extort stock from Erber at below-market prices; (2) whether Carlson's use of profane language, in and of itself, violated Conduct Rule 2110; and (3) whether the proceedings were so tainted by an alleged leak of confidential information by the staff, that fairness requires us to dismiss the complaint. After a thorough review of the record and for the reasons discussed below, we affirm the DBCC findings and imposition of sanctions.

Conduct Rule 2110 requires adherence to "high standards of commercial honor and just and equitable principles of trade." Section 15A of the Securities Exchange Act of 1934 requires that registered securities associations have rules that "promote just and equitable principles of trade." Disciplinary hearings under Conduct Rule 2110 are ethical proceedings, and one may find a violation of the ethical requirements where no legally cognizable wrong occurred. In re Timothy L. Burkes 51 S.E.C. 356 (1993), aff'd mem., Burkes v. SEC, 29 F.3d 630 (9th Cir. 1994). The NASD has authority to impose sanctions for violations of "moral standards" even if the conduct was not "unlawful" or fraudulent. In re Benjamin Werner, 44 S.E.C. 622 (1971). The ethical standards imposed in disciplinary proceedings go beyond simple legal requirements and depend on general rules of fair dealing, the reasonable expectations of the parties, marketplace practices, and the relationship between the firm and the customer. See, e.g., In re E.F. Hutton & Co., Inc., 49 S.E.C. 829 (1988) ("Manning") (holding that the firm violated its fiduciary duty to its customer not to trade ahead of a limit order even though the firm was acting in good faith).[4]

The Association has a long-standing policy prohibiting members and associated persons from using threats, coercion, or intimidation. For example, in In re Jay F. Keeton, 50 S.E.C. 1128 (1992), the Commission upheld the NASD's finding that attempting to coerce payment of commissions by threatening to injure a company's reputation violates high standards of commercial honor and just and equitable principles of trade. In that case, Keeton formed several investment partnerships that purchased stock of Spacehab, Inc. ("Spacehab"). Spacehab paid

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[3]The new evidence consisted of testimony from NASD employees Don Johnson and Lisa Chaney about the delisting of GLAD, and a tape-recorded telephone conversation between Carlson and Brett Bouchy ("Bouchy"), another individual from whom the staff alleged that Carlson attempted to obtain stock at below-market prices.

[4]Carlson and Aspen misunderstand the nature of NASD disciplinary proceedings. They argue that their conduct did not constitute extortion because Carlson never threatened to do anything illegal, an element of criminal extortion. Whether Carlson's conduct violated state and federal extortion laws (which it very well may have) is irrelevant; these are not criminal proceedings. Therefore, respondents' reliance upon cases applying criminal extortion statutes is misplaced.

Keeton commissions for those purchases but refused to pay Keeton a commission when Keeton referred an individual investor. Keeton sent Spacehab a proposed tombstone announcement describing an unfair practices action Keeton planned to file, accompanied by a letter from Keeton threatening to publish the tombstone and promising "an escalation of events" that could "damage [Spacehab's] ability to raise funds. . ." The NASD found that "regardless of the merits of Keeton's underlying claim for compensation, his method of pursuing that claim represented intentional and abusive misconduct." The Commission agreed:

> It is possible that Keeton deserved compensation. Nevertheless, in a dispute over a commission, it was hardly necessary to threaten to place a company's reputation and financial position at risk. Keeton should have focused on the normal consequences that would flow from pursuing the merits of his cause, not on Spacehab's vulnerable position . . . [h]e irresponsibly attempted to coerce payment from Spacehab by threatening adverse publicity . . . .

Id. at 1135. The Commission concluded that using such tactics violated high standards of commercial honor and just and equitable principles of trade.

The combination of threats, coercion, and intimidation that Carlson communicated to Erber on June 9, 1994, was more egregious than the respondent's conduct in Keeton. As in Keeton, Carlson preyed on Erber's vulnerability by: (1) informing Erber that Carlson had the ability to cause GLAD (a stock in which Carlson believed Erber had been involved) to be delisted; and (2) claiming to have information about Erber's status as an undisclosed principal of Paramount Securities, a fact that could violate a court order restricting Erber's participation in the securities industry. Carlson then repeatedly attempted to coerce Erber to sell him Teletek stock at below-market prices by exploiting Erber's perceived vulnerability. Carlson's vocabulary during the taped conversation underscores the abusiveness and seriousness of his threats and intimidation.[5]

The proceedings below were clouded with immaterial disputes. For instance, the parties spent considerable time supporting or attacking the accuracy of Carlson's statements to Erber during the June 9, 1994, conversation (viz, whether Carlson was instrumental in the delisting of GLAD and whether Erber was an undisclosed principal of Paramount Securities). It was the connotation of Carlson's statements, not their veracity, that was critical to Carlson's scheme: Carlson expressed his intent to cause Erber trouble unless Erber granted Carlson a concession on the price of Teletek stock, an action Erber may have been able, but certainly was not obligated, to take. Carlson's attempt to coerce Erber, successful or not, violated high standards of commercial honor.

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[5]We need not decide Carlson's argument that vulgar language, in and of itself, does not violate Conduct Rule 2110 because Carlson's conduct included not only vulgarity, but also threats and intimidation.

Erber's conduct and credibility are similarly immaterial. Respondents argue that Erber was not the "victim" of extortion that the DBCC portrayed him as, because Erber allegedly: (1) is a convicted felon; (2) violated a federal injunction against participation in the securities industry; (3) exaggerated or misstated the nature and intensity of Carlson's threats against him; and (4) did not feel threatened by Carlson's statements during the June 9 conversation.[6] These allegations, even if true, do not change the fact that Carlson was attempting to coerce Erber to do that which Erber was not obligated to do. Such conduct violated the high standards of commercial honor that Conduct Rule 2110 demands.

Finally, the record does not establish either: (1) that the staff disclosed to the public confidential information concerning the complaint against Aspen and Carlson; or (2) that Aspen and Carlson were prejudiced by any alleged disclosure of confidential information.

Sanctions

Carlson's abusive conduct represents a profound departure from the high standards of commercial honor that the Association demands of its members and associated persons. Conduct Rule 2110 sets forth broad moral and ethical standards, including a long-standing prohibition against threats, coercion, and intimidation. In Keeton, supra, the NASD fined and barred a respondent who engaged in threats and intimidation to resolve a payment dispute. The Commission affirmed, finding such conduct to be irresponsible even in the midst of a legitimate dispute. Here, unlike in Keeton, there was no pre-existing, legitimate dispute between Carlson and Erber.

The seriousness of Carlson's conduct outweighs several factors that might otherwise favor imposing lighter sanctions. For example, neither Carlson nor Aspen followed through on the threat to get Teletek delisted or to injure Erber; and neither Carlson nor Aspen has any prior similar disciplinary history.[7] Nonetheless, Carlson's and Aspen's conduct so seriously undermined the fair and efficient operation of the market and so clearly threatened the public's confidence in those markets, that it cannot be tolerated, even as a first violation.[8]

Accordingly, we order that Carlson and Aspen be: (1) censured; (2) fined $10,000, jointly and severally; and (3) assessed $1,102.30 in DBCC hearing costs and $750 in appeal costs, jointly

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[6]The NBCC denied the respondents' December 11, 1996 request to supplement the record with two indictments of Erber handed up by the federal grand jury for the District of Nevada that had not been introduced before the DBCC.

[7]Carlson and Aspen were fined $1,000, jointly and severally, for a net capital violation in 1994.

[8]The seriousness of this type of conduct and its potential to undermine the integrity of markets is evidenced by the Association's recent rule filing SR NASD 97-37, which codifies the NASD's longstanding policy against threats and harassment, especially with respect to quotations and other market activity.

and severally. We further order that Carlson be barred, effective immediately, from associating with any member of the Association in any capacity.[9]

On Behalf of the National Business Conduct Committee,

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Joan C. Conley, Corporate Secretary

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[9]We have considered all of the arguments of the parties. They are rejected or sustained to the extent inconsistent or in accord with the views expressed herein.

Pursuant to NASD Procedural Rule 8320, any member who fails to pay any fine, costs, or other monetary sanction imposed in this decision, after seven days' notice in writing, will be summarily suspended or expelled from membership for non-payment. Similarly, the registration of any person associated with a member who fails to pay any fine, costs, or other monetary sanction, after seven days' notice in writing, will be summarily revoked for non-payment.