

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

SECURITIES AND EXCHANGE COMMISSION,
450 Fifth St., N.W.
Washington, DC 20549-0800,

Plaintiff,

v.

DWARKA P. RATHI and
CHARLES H. PENNINGTON,

Defendants.

CASE NUMBER 1:03CV01617
JUDGE: James Robertson
DECK TYPE: General Civil
DATE STAMP: 07/31/2003

COMPLAINT

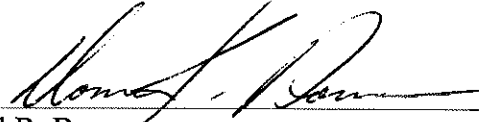
Plaintiff Securities and Exchange Commission ("Commission") alleges:

SUMMARY

1. During November and December 1999, defendants Dwarka P. Rathi ("Rathi") and Charles H. Pennington ("Pennington") each separately engaged in a fraudulent wash sales trading scheme designed to create artificial tax losses. The Defendants placed near-simultaneous matching limit orders to buy and sell the same stock, at artificial prices, in taxable and tax-sheltered accounts they each controlled. These matching limit orders were typically placed at prices that were outside the existing national best bid and offer prices and, when executed, created a loss in the taxable account and a profit in the tax-sheltered account. These wash sales did not result in any ultimate change in ownership over the shares being traded and created the false appearance of market activity in several thinly traded securities. The Defendants were able to match up their respective limit orders by trading illiquid stocks and by trading

PRAYER FOR RELIEF

16. The Commission respectfully requests that this Court (i) enter a Final Judgment against Rathi and Pennington ordering each of them to pay a civil penalty pursuant to Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)], and (ii) grant such other relief as this Court deems just and proper.



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Dated: *July 31, 2003*

those stocks in the less liquid after-hours trading market using the Island ECN – and thereby taking advantage of the fragmented nature of the after-hours market. Rathi and Pennington, in the aggregate, but in separate trades, executed 155 wash sales involving the securities of over 30 companies. In so doing, each violated the antifraud provisions of the federal securities laws.

2. The Commission brings this action pursuant to the authority conferred upon it by Section 21(d)(3) of the Securities Exchange Act of 1934 (“Exchange Act”) [15 U.S.C. § 78u(d)(3)] and seeks to impose a civil penalty to be paid by each of the defendants.

JURISDICTION

3. This Court has jurisdiction pursuant to Sections 21 and 27 of the Exchange Act [15 U.S.C. §§ 78u and 78aa].

THE DEFENDANTS

4. Defendant Rathi, age 49, is a self-employed physician residing in Scarsdale, New York.

5. Defendant Pennington, age 39, is a professor in the Department of Physics at The Ohio State University and resides in Columbus, Ohio.

FACTS

6. Defendants Pennington and Rathi have no connection to each other and acted independently while engaging in the similar wash sales scheme described herein. Each Defendant executed wash sales between taxable and tax-sheltered brokerage accounts they each separately controlled. Each Defendant effected his wash sales by placing near-simultaneous matching limit orders to both buy and sell the same stock for

Pennington's wash sales were conducted in the after-hours market. As a result of this wash sale trading scheme, Pennington created artificial losses of \$77,662 in his taxable account and gains of \$74,940 in his tax-sheltered account.

12. The Defendants' wash sales created a false appearance of market activity, were affected at contrived prices, and did not reflect the supply and demand for the stocks in which those individuals were trading.

CLAIM

**Violations of
Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)],
and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5]**

13. Plaintiff realleges and incorporates by reference paragraphs 1 through 12, above.

14. Wash sale transactions involve no change in beneficial ownership and constitute a manipulative device under Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

15. By reason of the foregoing, the Defendants violated Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

the same artificial price. Each Defendant was able to match up his limit orders by trading illiquid stocks and by trading those stocks in the less liquid after-hours trading market using the Island ECN – and thereby taking advantage of the fragmented nature of the after-hours market.

7. Each of the Defendants has claimed that he engaged in this wash sales scheme as a strategy to save on taxes.

8. Each of the Defendants' after-hours wash sales, along with the artificial prices at which they were executed, was publicly reported as a result of NASD Rules 4632 and 6620, which obligated Island to report its participants' trades within ninety seconds of execution to NASDAQ through the Automated Confirmation Transaction Services.

9. In a number of instances, the wash sales effected by the Defendants constituted the only after-hours trade in a particular stock. In other instances, the Defendants' trades constituted over half of the after-hours trading volume in a particular security.

Defendants' Trades

10. Between November 23 and December 23, 1999, Defendant Rathi executed 132 wash sales involving the stocks of 28 different companies. 130 of Rathi's wash sales were conducted in the after-hours market. As a result of this wash sale trading scheme, Rathi created artificial losses of \$221,698 in his taxable accounts and gains of \$245,174 in his tax-sheltered accounts.

11. Between October 29 and December 15, 1999, Defendant Pennington executed 23 wash sales involving the stock of seven different companies. 22 of