UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 83840 / August 14, 2018

ADMINISTRATIVE PROCEEDING
File No. 3-18640

In the Matter of **NW CAPITAL MARKETS INC. AND JAMES A. FAGAN,** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTIONS 15(b), 15B(c), AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 15(b), 15B(c), and 21C of the Securities Exchange Act of 1934 ("Exchange Act") against NW Capital Markets Inc. ("NW Capital") and James A. Fagan ("Fagan") (collectively, the "Respondents").

II.

In anticipation of the institution of these proceedings, Respondents have submitted Offers of Settlement (the "Offers"), which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over Respondents and the subject matter of these proceedings, which are admitted, and except as provided herein in Section V, Respondents consent to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Sections 15(b), 15B(c), and 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and Respondents' Offers, the Commission finds[1] that:

Summary

1. These proceedings arise out of improper trading in municipal bonds between Charles Kerry Morris, the head of municipal underwriting, sales, and trading at registered broker-dealer NW Capital Markets Inc. ("NW Capital"), and NW Capital customer James P. Scherr and his firm, Core Performance Management, LLC ("CPM"). As discussed below, Scherr and CPM engaged in a market practice called "flipping." In the municipal bond context, flipping involves obtaining allocations of new issue municipal bonds from underwriters and then immediately re-selling or "flipping" the bonds at a profit once trading begins.[2]

2. Between May 2012 and September 2014, Morris allocated certain new issue bonds to Scherr and CPM as part of offerings underwritten by NW Capital, with the understanding that Morris would buy the bonds back into NW Capital's inventory. In exchange, Morris agreed to pay Scherr and CPM a higher price than Scherr and CPM paid for the bonds. These "parking"[3] transactions created the false appearance of a sale when, in fact, Morris and NW Capital were effectively retaining control of the bonds, and were therefore able to sell them again into the secondary market.

3. In addition, Morris placed orders on behalf of NW Capital with Scherr and CPM to obtain new issue bonds that Scherr and CPM had obtained from other underwriters. Scherr and CPM were acting as brokers because they were in the business of regularly soliciting, accepting and executing orders for the purchase and sale of securities from others for which they received transaction-based compensation. Neither Scherr nor CPM was registered with the Commission as a broker at the time of these transactions. Morris and NW Capital's conduct in buying from and selling to Scherr and CPM was a cause of Scherr and CPM's unregistered broker activity.

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[1] The findings herein are made pursuant to Respondents' Offers and are not binding on any other person or entity in this or any other proceeding.

[2] The Municipal Securities Rulemaking Board ("MSRB") defines "flipping" as the immediate resale of allotted bonds in a primary offering, which may involve a prearranged trade, where the initial purchaser does not intend to hold the bonds for investment purposes but instead expects to make a profit from such immediate resale.

[3] The MSRB defines "parking" as a practice, in violation of securities industry rules, consisting of selling securities to a customer and, at the same time, agreeing to repurchase the securities at a future date with an unbooked transaction (with the transaction later booked as an ostensibly unrelated trade). The term "parking" is used generally to refer to an arrangement in which "a person 'sells' securities to a purchaser subject to an agreement or understanding that the seller will repurchase the securities at a later time at a price that leaves the economic risk with the seller." Thomas C. Gonnella, S.E.C. Rel. No. 34-78532, Comm. Op., 2016 WL 4233837, at *17 n.26 (Aug. 10, 2016) (internal citations omitted).

4. Morris's direct supervisor, James Fagan, failed reasonably to supervise Morris's activities by failing to implement the written supervisory policies and procedures in place at NW Capital. During the relevant period, Fagan did not conduct regular reviews of parking as required by the firm's written supervisory policies and procedures.

Respondents

5. **NW Capital Markets Inc.**, incorporated in Delaware and headquartered in Hoboken, New Jersey, is registered with the Commission as a broker-dealer.

6. **James A. Fagan**, age 70, resides in Neptune, New Jersey. He currently is a Managing Director and chief compliance officer at NW Capital, and a Managing Director at NW Financial ("NW Financial"), an affiliate of NW Capital that is registered with the Commission as a municipal advisor.

Related Individuals and Entity

7. **Charles Kerry Morris**, age 63, resides in Manasquan, New Jersey. He joined NW Capital in 2004 and, until December 31, 2017, was a Managing Director, primarily responsible for underwriting, sales, and secondary market trading of municipal securities. Morris was also a Managing Director at NW Financial.

8. **James P. Scherr**, age 61, resides in Boca Raton, Florida. Scherr was majority owner and managing director of Core Performance Management, LLC, and at all relevant times controlled CPM.

9. **Core Performance Management, LLC** ("CPM"), founded by Scherr, was a Florida LLC located in Boca Raton that was dissolved as of July 27, 2016. CPM primarily bought and sold new issue bonds and was never registered with the Commission.

Background

10. Municipalities often raise money by issuing municipal bonds to the public. Many of those bonds are sold to the public through a "negotiated" bond offering. In a negotiated bond offering, the municipal issuer selects a broker-dealer firm to act as the bonds' underwriter and sell the bonds to the public.[4] The underwriter negotiates with the municipal issuer to determine the price at which the new municipal bonds should be offered. The underwriter has an obligation to make a bona fide offering of the bonds to the public at that initial offering price.

[4] The selected broker-dealer firm may act as the sole underwriter for a particular offering, or may be the lead underwriter (also sometimes referred to as the senior manager) among a group of broker-dealers, which is known as an underwriting syndicate.

11. Often, preliminary orders from customers for new municipal bonds exceed the amount of bonds available for sale. When a bond offering is oversubscribed, customer orders are typically prioritized over orders from broker-dealers, with the result that broker-dealer firms are often unable to purchase bonds in the initial offering.

Unregistered Broker Activity of Scherr and CPM

12. Morris had a long-standing relationship with Scherr and understood that Scherr operated a securities trading business known as "flipping" and was known in the industry as a "flipper." "Flipping" is the immediate resale of new issue bonds, where the initial purchaser does not intend to hold the bonds for investment purposes but instead expects to make a profit from that immediate resale. The resale may be prearranged with the subsequent purchaser before the flipper makes the initial purchase of bonds.

13. The flipping business of Scherr and CPM involved soliciting orders from and prearranging trades with broker-dealer firms to purchase new issue municipal bonds that Scherr and CPM planned to purchase from underwriters in new bond offerings. Broker-dealer firms placed orders with Scherr and CPM because they were typically unable to purchase the bonds directly from the underwriter, for the reasons noted above.

14. As part of their business, Scherr and CPM solicited broker-dealer firms to place preliminary orders for new municipal bonds with them.[5] They then placed orders for the bonds with the underwriter for the bond offering. If they successfully obtained the new issue bonds, they immediately resold the bonds to the broker-dealer firms that had placed preliminary orders with them. Scherr and CPM charged those broker-dealer firms (which were their own customers) a fee on the sale of those bonds. Scherr and CPM were acting as brokers because they were in the business of regularly soliciting, accepting and executing orders for the purchase and sale of securities from others for which they were receiving transaction-based compensation. Neither Scherr nor CPM has ever been registered with the Commission as a broker.

15. While employed at NW Capital, Morris placed orders with, and purchased new issue bonds from, Scherr and CPM. These orders were for NW Capital's account.

16. In addition, when Morris and NW Capital were underwriting new bond offerings, Morris also frequently accepted orders from Scherr and CPM for bonds. In accepting their orders for bonds, Morris understood that Scherr and CPM were placing those orders on behalf of others, including other broker-dealer firms.

[5] The orders the broker-dealer firms placed with Scherr and CPM were preliminary in the sense that Scherr and CPM typically had not yet obtained the new bonds at the time of the order and therefore did not yet have them available to sell.

Morris "Parked" Bonds Underwritten by NW Capital

17. In certain offerings underwritten by NW Capital between May 2012 and September 2014, Morris engaged in unlawful parking transactions with Scherr and CPM. In these transactions, Morris allocated and sold bonds to Scherr and CPM with the understanding that Scherr and CPM would temporarily hold the bonds for a short period of time (typically one business day or less) until Morris bought them back into NW Capital's inventory. Morris bought the bonds back at higher prices, thereby guaranteeing that Scherr and CPM would make a profit. The prearranged nature of these trades meant that the market risk of owning the bonds never actually passed to Scherr or CPM.

Fagan Failed Reasonably to Supervise Morris

18. Throughout his employment at NW Capital, Morris reported to Fagan as his first-level supervisor. During the relevant period, Fagan also was the supervisor responsible for implementing procedures related to parking in NW Capital's written supervisory policies and procedures.

19. As Morris's supervisor, Fagan was responsible for supervising Morris's underwriting activities, and for reviewing Morris's trades.

20. NW Capital's written supervisory policies and procedures prohibit "parking" securities, which NW Capital defines as "an illegal practice intended to hide the real beneficial ownership of the securities," comprising "a variety of schemes that violate securities laws." NW Capital's written supervisory policies and procedures required Fagan to "ensure that there is no illegal parking of securities in any of our customer accounts, or in any firm accounts (if we maintain such accounts)." These written supervisory policies and procedures also required Fagan to review transactions at least quarterly for specific parking schemes.

21. Fagan failed to review the firm's customer accounts, including the accounts of Scherr and CPM, to determine whether NW Capital employees, including Morris, were engaging in illegal parking using customer accounts. Although he reviewed the firm's trades monthly, Fagan did not specifically review them to detect parking schemes and did not conduct quarterly reviews for parking as required by NW Capital's written supervisory policies and procedures.

Legal Discussion

NW Capital Violated MSRB Rule G-17

22. "Parking" refers generally to an unlawful arrangement in which "a person 'sells' securities to a purchaser subject to an agreement or understanding that the seller will repurchase the securities at a later time at a price that leaves the economic risk with the seller." Thomas C. Gonnella, S.E.C. Rel. No. 34-78532, Comm. Op., 2016 WL 4233837, at *17 n.26 (Aug. 10, 2016) (internal citations omitted).

23. As a result of the parking conduct by Morris described above, NW Capital willfully[6] violated MSRB Rule G-17.

Fagan Failed Reasonably to Supervise Morris

24. Section 15(b)(4)(E) of the Exchange Act authorizes the Commission to impose sanctions against a broker-dealer for failing reasonably to supervise another person subject to the firm's supervision who committed a securities law violation. Section 15(b)(6)(A)(i) incorporates by reference Section 15(b)(4)(E) and provides for the imposition of sanctions against any individuals associated with a broker or dealer who fail reasonably to supervise others. Such individuals may be held liable for failing to follow or implement a firm's procedures. See, e.g., In the Matter of John A. Carley et. al., Exch. Act Rel. No. 57246 at 26-28 (Jan. 31, 2008).

25. MSRB Rule G-27(a) requires that each broker, dealer, and municipal securities dealer "shall supervise the conduct of the municipal securities activities of the dealer and its associated persons to ensure compliance with [MSRB] rules and the applicable provisions of the [Exchange] Act and rules thereunder." [7]

26. Morris violated Securities Act Sections 17(a)(1) and (3), Exchange Act Section 10(b) and Rule 10b-5(a) and (c) thereunder, and MSRB Rule G-17 by engaging in the parking scheme with Scherr and CPM, as described above.

27. Fagan failed to implement the firm's procedures requiring Fagan to review Morris's transactions quarterly to identify parking schemes.

28. As a result, Fagan failed reasonably to supervise Morris, an associated person, within the meaning of Section 15(b)(4)(E) of the Exchange Act, with a view to prevent and detect Morris's violations of Securities Act Sections 17(a)(1) and (3), Exchange Act Section 10(b) and Rule 10b-5(a) and (c) thereunder, and MSRB Rule G-17, and willfully violated MSRB Rule G-27.

NW Capital Caused Violations of Section 15(a)(1) of the Exchange Act

29. To establish causing liability, the Commission must find: (1) a primary violation; (2) the respondent's act or omission contributed to the violation; and (3) the respondent knew or should have known that the act or omission would contribute to the violation. See 15 U.S.C. §

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[6] A willful violation of the securities laws means merely "'that the person charged with the duty knows what he is doing.'" Wonsover v. SEC, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting Hughes v. SEC, 174 F. 2d 969, 977 (D.C. Cir. 1949)). There is no requirement that the actor "'also be aware that he is violating one of the Rules or Acts.'" Id. (quoting Gearhart & Otis, Inc. v. SEC, 348 F.2d 798,803 (D.C. Cir.1965)).

[7] Subject to certain exceptions, MSRB Rule D-11 includes "associated persons" within the definitions of brokers, dealers, and municipal securities dealers for purposes of all other MSRB rules. See Wheat, First Securities, Inc., 80 SEC Docket 3406, 2003 WL 21990950, at *8 n. 29 (Aug. 20, 2003).

78u-3(a); Robert M. Fuller, 56 S.E.C. 976, 984 (2003), pet. denied, 95 F. App'x 361 (D.C. Cir. 2004). Negligence is sufficient to establish "causing" liability, at least in cases where a person is alleged to "cause" a primary violation that does not require scienter, such as Section 15(a)(1) of the Exchange Act. VanCook, Rel. No. 34-61039A (Nov. 20, 2009) (Opinion of the Commission) (quoting KPMG Peat Marwick LLP, S.E.C. 1135, 1175 (2001)), pet. denied, 289 F.3d 109 (D.C. Cir. 2002).

30. Under Section 15(a)(1) of the Exchange Act, it is unlawful for a broker or dealer "to effect any transactions in, or to induce or attempt to induce the purchase or sale of, any security . . . unless such broker or dealer is registered" with the Commission pursuant to Section 15(b) of the Exchange Act. Under Section 3(a)(4)(A) of the Exchange Act, a "broker" is "any person engaged in the business of effecting transactions in securities for the account of others."

31. The Exchange Act's definition of "broker" "connote[s] a certain regularity of participation in securities transactions at key points in the chain of distribution." Mass. Fin. Serv., Inc. v. Sec. Inv. Prot. Corp., 411 F. Supp. 411, 415 (D. Mass. 1976), aff'd, 545 F.2d 754 (1st Cir. 1976); see also SEC v. Martino, 255 F. Supp. 2d 268, 283 (S.D.N.Y. 2003).

32. Scherr and CPM violated Section 15(a)(1) of the Exchange Act because they were acting as brokers without being registered with the Commission.

33. NW Capital's purchase of bonds from and sales of bonds to Scherr and CPM, through Morris, contributed to the operation of Scherr and CPM as unregistered brokers. NW Capital, through Morris, knew or should have known that Scherr and CPM werenot registered with the Commission.

34. As a result of the conduct described above, NW Capital caused the violations of Section 15(a)(1) of the Exchange Act by Scherr and CPM.

NW Capital Violated Section 15B(c)(1) of the Exchange Act

35. Section 15B(c)(1) of the Exchange Act prohibits a broker, dealer or municipal securities dealer from affecting interstate transactions in, or inducing or attempting to induce the purchase or sale of, any municipal security in contravention of any rule of the MSRB.

36. As discussed above, NW Capital violated MSRB Rule G-17. As a result, NW Capital willfully violated Section 15B(c)(1) of the Exchange Act.

IV.

In view of the foregoing, the Commission deems it appropriate, in the public interest to impose the sanctions agreed to in Respondents' Offers.

Accordingly, pursuant to Sections 15(b), 15B(c), and 21C of the Exchange Act, it is hereby ORDERED that:

NW Capital

A. Respondent NW Capital cease and desist from committing or causing any violations and any future violations of Sections 15(a)(1) and 15B(c)(1) of the Exchange Act and MSRB Rule G-17.

B. Respondent NW Capital is censured.

C. Respondent NW Capital shall, within 10 days of the entry of this Order, pay disgorgement of $41,770.58 and prejudgment interest of $5,295.21 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury, subject to Exchange Act Section 21F(g)(3). Respondent NW Capital shall, within 10 days of the entry of this Order, pay a civil money penalty in the amount of $40,000 to the Securities and Exchange Commission, of which $10,000 shall be transferred to the Municipal Securities Rulemaking Board in accordance with Section 15B(c)(9)(A) of the Exchange Act, and of which the remaining $30,000 shall be transferred to the general fund of the United States Treasury in accordance with Section 21F(g)(3) of the Exchange Act. If timely payment of disgorgement and prejudgment interest is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600; if timely payment of the civil money penalty is not made, additional interest shall accrue pursuant to 31 U.S.C. § 3717.

Fagan

D. Respondent Fagan cease and desist from committing or causing any violations and any future violations of MSRB Rule G-27.

E. Respondent Fagan be, and hereby is, suspended from acting in a supervisory capacity with any broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization for a period of six months, effective on the second Monday following the entry of this Order.

F. Respondent Fagan shall, within 10 days of the entry of this Order, pay a civil money penalty in the amount of $10,000 to the Securities and Exchange Commission, of which $2,500 shall be transferred to the Municipal Securities Rulemaking Board in accordance with Section 15B(c)(9)(A) of the Exchange Act, and of which the remaining $7,500 shall be transferred to the general fund of the United States Treasury in accordance with Section 21F(g)(3) of the Exchange Act. If timely payment of the civil money penalty is not made, additional interest shall accrue pursuant to 31 U.S.C. § 3717.

All Respondents

G. Payment must be made in one of the following ways:

(1) Respondents may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;

(2) Respondents may make direct payment from a bank account via Pay.gov through the SEC website at http://www.sec.gov/about/offices/ofm.htm; or

(3) Respondents may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter separately identifying NW Capital or Fagan as a respective Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Ivonia K. Slade, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549.

H. Amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondents agree that in any Related Investor Action, Respondents shall not argue that they are entitled to, nor shall Respondents benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that they shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

V.

It is further Ordered that, solely for purposes of exceptions to discharge set forth in Section 523 of the Bankruptcy Code, 11 U.S.C. § 523, the findings in this Order are true and admitted by Respondent Fagan, and further, any debt for disgorgement, prejudgment interest, civil penalty or other amounts due by Respondent Fagan under this Order or any other judgment, order, consent order, decree or settlement agreement entered in connection with this proceeding, is a debt for the violation by Respondent Fagan of the federal securities laws or any regulation or order issued under such laws, as set forth in Section 523(a)(19) of the Bankruptcy Code, 11 U.S.C. § 523(a)(19).

By the Commission.

Brent J. Fields
Secretary