

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934  
Rel. No. 55828 / May 30, 2007

Admin. Proc. File No. 3-12498

In the Matter of the Application of  
  
SKY CAPITAL LLC  
  
For Review of Action Taken by  
  
NASD

OPINION OF THE COMMISSION

REGISTERED SECURITIES ASSOCIATION - REVIEW OF ASSOCIATION ACTION

Jurisdiction to Review Association Action

NASD member firm applied for Commission review of certain actions by NASD staff directed at firm. Held, the matter is not reviewable under Section 19(d) of the Securities Exchange Act of 1934. Application for review is therefore dismissed.

APPEARANCES:

Steven Altman, of Altman & Company P.C., for Sky Capital LLC.

Marc Menchel, Alan Lawhead, and Terry L. Reicher, for NASD.

Appeal filed: November 28, 2006

Last brief received: December 27, 2006

I.

Sky Capital LLC (“Sky Capital”), an NASD member firm, seeks Commission review of what it characterizes as NASD staff’s “campaign of harassment” against the firm and of NASD’s purported failure to provide an internal procedure for member complaints of staff misconduct. NASD has moved to dismiss the application. The parties do not differ substantially in their description of the facts. For purposes of our review, we accept the facts as described in NASD’s

decisions and the parties' briefs. <sup>1/</sup> For the reasons set forth below, we conclude that we lack jurisdiction to consider Sky Capital's application under Section 19(d) of the Securities Exchange Act of 1934. <sup>2/</sup>

## II.

Sky Capital is a broker-dealer firm principally located in New York City. <sup>3/</sup> Sky Capital applied for NASD membership in June 2001. On February 13, 2002, NASD's Department of Member Regulation for District No. 10 ("Member Regulation") denied the membership application. Sky Capital appealed the membership application denial to NASD's National Adjudicatory Council ("NAC"). During the pendency of that appeal, Member Regulation and Sky Capital agreed to a membership agreement that included restrictions on certain activities of Ross H. Mandell, Sky Capital's chief executive officer. Member Regulation withdrew its denial decision and approved the firm's membership application, subject to the agreed-to restrictions imposed on Mandell. Sky Capital became an NASD member in May 2002. Sky Capital alleges that NASD staff employed "delay tactics" in reviewing its membership application, and that NASD staff was biased against Mandell due to his regulatory history and past substance abuse problems. Sky Capital acknowledges, however, that following the firm's appeal to the NAC, Member Regulation "reverse[d] course" and approved its membership application.

Subsequently, the firm sought to expand its business. Sky Capital's NASD membership agreement limited the firm's market making activities to forty over-the-counter securities. It also limited the number of associated persons that Sky Capital could employ to seventy-five. In November 2002, Sky Capital applied to expand its market making activities to 600 securities and

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<sup>1/</sup> See Joseph Dillon & Co., 54 S.E.C. 960, 962 (2000) (dismissing appeal of NASD decision denying firm exemption from NASD Conduct Rule 3010(b)(2) for lack of jurisdiction under Exchange Act Section 19(d)).

<sup>2/</sup> See 15 U.S.C. § 78s(d). Sky Capital has requested oral argument. The Commission's Rule of Practice 154(a) states that "[n]o oral argument shall be heard on any motion unless the Commission or the hearing officer otherwise directs." 17 C.F.R. § 201.154(a). We have determined that the presentation in the briefs and the decisional process would not be significantly aided by oral argument. See 17 C.F.R. § 201.451(a) (stating that "[t]he Commission will consider appeals, motions and other matters properly before it on the basis of the papers filed by the parties without oral argument unless the Commission determines that the presentation of facts and legal arguments in the briefs and record and the decisional process would be significantly aided by oral argument"). Accordingly, Sky Capital's request for oral argument is denied.

<sup>3/</sup> Sky Capital is wholly owned by Sky Capital Holdings Ltd., a Delaware corporation whose common stock is listed on the Alternative Investments Market of the London Stock Exchange.

to relocate the majority of its trading operations from New York to Red Bank, New Jersey. In December 2002, Sky Capital applied to increase the number of associated persons it could employ to 200. Member Regulation initially denied both applications, and Sky Capital appealed. The NAC vacated the denials and remanded for reconsideration. Member Regulation ultimately allowed Sky Capital to expand as requested.

Sky Capital further asserts that, in 2002, NASD staff “obstructed” its plans to acquire assets from The Thornwater Company, L.P., another member firm, by imposing restrictions on Thornwater. Sky Capital admits, however, that NASD subsequently lifted those restrictions. In 2003, Sky Capital sought to acquire a Florida broker-dealer. Sky Capital concedes that NASD staff approved the transaction, but asserts that it did so only after substantial delay.

Sky Capital complains that, between 2002 and 2005, NASD staff initiated eight separate examinations of the firm and its employees. NASD states that the first examination, which concerned deficiencies in Mandell’s Form U-4, resulted in the issuance of a “letter of caution” and Minor Rule Violation Letter against Mandell. <sup>4/</sup> Mandell agreed to waive his right to appeal to the Commission in connection with the matter. The second examination, a routine examination of Sky Capital’s first six months of operation, closed without any action taken by NASD. The third examination, also routine, related to Sky Capital’s operations in 2003. It resulted in the firm’s execution of a Letter of Acceptance, Waiver and Consent and payment of two fines. <sup>5/</sup> Sky Capital agreed to waive its right to appeal to the Commission in connection with the matter.

According to NASD, the fourth, fifth, and sixth examinations were instituted for cause. The fourth examination related to a customer complaint against a Sky Capital broker for alleged misconduct at the broker’s previous place of employment. The fifth examination related to Mandell’s adherence to certain restrictions placed upon him by the firm’s membership agreement. The sixth examination related to political contributions made by Sky Capital employees. All three examinations closed without any action taken by NASD.

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<sup>4/</sup> Mandell paid a \$2,500 fine for failing to amend his Form U-4 to disclose the fact that he had been named as a defendant in an investment-related civil litigation, in contravention of Article V, Section 2 of NASD’s By-Laws.

<sup>5/</sup> Sky Capital paid a \$12,000 fine for acting as a placement agent in three best-efforts private placement offerings involving minimum-maximum contingencies without being a party to escrow agreements regarding the funds raised, in violation of Exchange Act Rule 15c2-4. Sky Capital paid a \$3,000 fine for permitting an employee, who was inactive due to the failure to complete the Regulatory Element of NASD’s Continuing Education Requirement, to act in a capacity that required NASD registration, in violation of NASD Rule 1120.

The seventh examination relates to late trading and market timing practices by a Sky Capital trader. NASD states that this examination, as well as an eighth, routine examination of Sky Capital, are ongoing. NASD represents that, if either examination results in a disciplinary complaint against the firm, Sky Capital will have the right to litigate the issues raised and to seek appellate review.

Sky Capital does not dispute that it will have the right to litigate. However, Sky Capital asserts that all of the examinations were designed to drain its financial resources and harass its personnel. Sky Capital acknowledges that none of the examinations has resulted to date in any enforcement action against the firm.

In 2003, Sky Capital filed a complaint with NASD's Department of Internal Review concerning the staff's "inappropriate treatment of [its] membership applications and harassment through the examination process." Sky Capital's complaint was referred to the Office of the Ombudsman. Sky Capital states that no action was taken by the Ombudsman at that time. In 2006, Sky Capital complained to the Ombudsman about the actions of a former NASD examiner, J. Kirby Neill, who allegedly provided a Sky Capital customer with the name and number of an attorney and encouraged the customer to complain about the firm. <sup>6/</sup> Sky Capital asserts that its complaints to the Ombudsman have "fallen on deaf ears." <sup>7/</sup>

### III.

Sky Capital alleges that NASD staff's actions with respect to the firm violate the fair process requirements of Exchange Act Section 15A(b)(8) <sup>8/</sup> and the constitutional requirements of due process. In addition, Sky Capital asserts that the lack of an internal procedure for NASD member complaints of staff mistreatment constitutes a denial or limitation of access to NASD

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<sup>6/</sup> NASD states that it has terminated the examiner's employment.

<sup>7/</sup> In its application, Sky Capital alleges further that the staff "provoked, caused and/or aided and abetted" a recent federal criminal investigation of the firm. Sky Capital bases this allegation on "information and belief," but does not set forth the sources of its information or the grounds for its belief. The United States Supreme Court has stated that a prosecutor has considerable discretion in determining matters such as which persons should be targets of investigation and what methods of investigation should be used. See Young v. U.S. ex rel. Vuitton et Fils SA, 481 U.S. 787, 807 (1987).

<sup>8/</sup> 15 U.S.C. § 78o-3(b)(8) (requiring self-regulatory organizations to provide "fair procedures").

services, as well as a violation of NASD rules and a 1996 Commission report issued under Exchange Act Section 21(a). 9/

Our authority to review an action of a self-regulatory organization (“SRO”), including NASD, is governed by Exchange Act Section 19(d). 10/ That provision authorizes Commission review of an SRO action that: (1) imposes a final disciplinary sanction on any member or person associated with a member; (2) denies membership or participation to any applicant; (3) prohibits or limits any person in respect to access to services offered by such organization or a member of the organization; or (4) bars any person from becoming associated with a member. If we find that we do not have jurisdiction, we must dismiss the proceeding. 11/ Sky Capital’s allegations fail to invoke any of these four jurisdictional categories.

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9/ See NASD and The Nasdaq Market, Report Pursuant to Section 21(a) of the Securities Exchange Act of 1934, 52 S.E.C. 882 (1996) (“Report”). In the Report, the Commission made certain findings regarding deficiencies in NASD’s oversight of Nasdaq and NASD’s failure to enforce compliance with NASD rules and the federal securities laws. NASD entered into a settlement with the Commission, pursuant to which NASD agreed to certain undertakings, including undertakings to ensure the existence of a substantial internal audit staff to address complaints from NASD members. See Order Instituting Public Proceedings Pursuant to Section 19(h)(1) of the Securities Exchange Act of 1934, Making Findings and Imposing Remedial Sanctions, 52 S.E.C. 875, 880 (1996).

10/ Contrary to Sky Capital’s assertions, Exchange Act Section 19(f) does not establish a basis for Commission jurisdiction here. We have stated that, “[u]nless an appeal meets the threshold requirement for jurisdiction under Section 19(d), the standard of review under Section 19(f) is not an issue.” Larry A. Saylor, Securities Exchange Act Rel. No. 51949 (June 30, 2005), 85 SEC Docket 3118, 3120-21 n.3.

11/ If, on the other hand, we find that jurisdiction is present, we are authorized, pursuant to Exchange Act Section 19(e), 15 U.S.C. § 78s(e), to affirm, modify, or set aside an SRO’s sanctions in any proceeding to review a final disciplinary sanction. Pursuant to Exchange Act Section 19(f), 15 U.S.C. § 78s(f), we are authorized to dismiss or set aside any SRO action in a proceeding to review a denial of membership or participation in an SRO, the barring of any person from association with a member, or a prohibition or limitation by an SRO of a person’s access to SRO services.

The Commission has no authority to grant much of the relief sought by Sky Capital. In its application, Sky Capital requests, among other things, that the Commission award the firm at least \$300 million in damages and penalties and “reassign regulatory oversight of Sky Capital to another qualified self-regulatory organization . . . or to another NASD District Office.” Under Exchange Act Sections 19(e) and (f), we do not have the authority to order such relief.

We have stated that a “disciplinary action” is “an action that responds to an alleged violation of an SRO rule or Commission statute or rule, or an action in which a punishment or sanction is sought or intended.” <sup>12/</sup> We also have stated that Section 19(d) grants us jurisdiction to review only those disciplinary actions in which a final disciplinary sanction is imposed. <sup>13/</sup>

Sky Capital alleges generally that “punishment has been inflicted” against the firm. However, the only final disciplinary sanctions cited are a Minor Rule Violation Letter (as well as a “letter of caution”) and Letter of Acceptance, Waiver and Consent. Sky Capital and Mandell consented to those sanctions and waived their rights to appeal to the Commission. Two NASD staff examinations remain ongoing. Neither one has led to the institution of any disciplinary action, let alone a final sanction. <sup>14/</sup> We have stated that SRO action “is not reviewable merely because it adversely affects the applicant.” <sup>15/</sup>

Sky Capital has not been denied NASD membership or barred from associating with an NASD member. Sky Capital complains about the staff’s handling of its application for NASD membership. However, the staff approved that application. Sky Capital does not allege, nor do we find, that it has been barred from associating with an NASD member.

Sky Capital has not been denied access to any services offered by NASD. Sky Capital complains about the staff’s handling of the firm’s applications to expand its business. <sup>16/</sup> Yet, NASD staff ultimately rendered decisions on those applications that were favorable to the firm.

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<sup>12/</sup> Russell A. Simpson, 53 S.E.C. 1042, 1046 (1998).

<sup>13/</sup> Id.

<sup>14/</sup> Thus, there was no action for which notice to the Commission was required under Exchange Act Section 19(d)(1). See 15 U.S.C. § 78s(d)(1) (requiring, in part, that an SRO promptly file with the Commission notice of any final disciplinary action taken with respect to any person or organization); see also, e.g., Tague Sec. Corp., 47 S.E.C. 743, 745 (1982) (dismissing proceeding for lack of jurisdiction where SRO did not attempt to penalize or discipline applicant and no notice of disciplinary action was filed by SRO, as required by Section 19(d)(1)).

<sup>15/</sup> Joseph Dillon, 54 S.E.C. at 964.

<sup>16/</sup> The Commission reviews denials of requests to modify NASD membership agreements as denials of access to NASD services under Exchange Act Section 19(f). See, e.g., Sierra Nevada Sec., Inc., 54 S.E.C. 112 (1999) (upholding NASD’s denial of member’s request to modify the terms of its restrictive agreement to permit it to make markets in the securities of more than fifty issuers).

Sky Capital also complains that it was denied access to NASD's internal complaint process. <sup>17/</sup> NASD created the Office of the Ombudsman, a position within NASD's Department of Internal Review, <sup>18/</sup> in order to provide a forum for members to voice their concerns of unfair practices or disparate treatment by the staff. <sup>19/</sup> Sky Capital's application makes clear that the firm has had access to the Ombudsman's Office and voiced its complaints about the staff's actions. <sup>20/</sup>

Moreover, "[i]n those cases in which we have found a denial of access, an SRO had denied or limited the applicant's ability to utilize one of the fundamentally important services offered by the SRO. The services at issue were not merely important to the applicant but were central to the function of the SRO." <sup>21/</sup> In William J. Higgins, <sup>22/</sup> for example, we held that the New York Stock Exchange's denial of a member's request to install telephone link-ups on the trading floor to permit direct communication between the floor and non-member customers constituted a denial of access to the Exchange's services. We found that "[t]he operation of a

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<sup>17/</sup> Sky Capital notes that, under NASD's settlement with the Commission, NASD was required to "ensure the existence of a substantial, independent internal audit staff which reviews all aspects of the NASD (including the regulatory function, the disciplinary process and [Nasdaq])," which would report directly to the Board of Governors' audit committee. 52 S.E.C. at 880. In the accompanying Report, the Commission stated that "[t]his measure should ensure that the NASD engages in a process of comprehensive ongoing self-evaluation." 52 S.E.C. at 920.

<sup>18/</sup> NASD Notice to Members 96-45, NASD Appoints Ombudsman (July 1996).

<sup>19/</sup> NASD has stated that complaints regarding decisions made or actions taken by the staff that are "inconsistent, biased, or result in disparate treatment" may be directed to the Office of the Ombudsman. NASD Notice to Members 98-30, NASD Office of the Ombudsman Clarifies its Role (Mar. 1998).

<sup>20/</sup> Under "The Ombudsman Association Standard of Practice," the Ombudsman has discretion in determining whether to act on a concern brought to its attention. See <http://www.nasd.com/AboutNASD/CorporateInformation/OfficeoftheOmbudsman/index.htm>.

<sup>21/</sup> Morgan Stanley & Co., Inc., 53 S.E.C. 379, 385 (1997).

<sup>22/</sup> 48 S.E.C. 713 (1987).

trading floor . . . is the principal service offered by a national securities exchange to its members, and by its members to investors.” 23/ By contrast, Sky Capital has not shown that the Office of the Ombudsman provides a “fundamentally important service” that is central to the function of NASD. 24/

Sky Capital seems to complain that the current examinations of the firm continue. NASD actions generally may not be appealed to the Commission until they have been reviewed by the NAC. 25/ A hearing before a Hearing Panel and review of any Hearing Panel decision by the NAC would be available to Sky Capital if the current examinations result in disciplinary action against the firm. Sky Capital cannot now deprive NASD of its review function by filing a premature appeal to us. 26/

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23/ Id. at 718; see also Scattered Corp., 52 S.E.C. 812, 813 (1996) (finding jurisdiction to review Chicago Stock Exchange’s refusal to process firm’s request for registration as a market maker in certain issues because such action limited the firm’s access to Exchange services); Creative Med. Dev., Inc., 52 S.E.C. 968 (1996) (assuming jurisdiction over NASD action denying issuer temporary exception from automatic quotation system’s inclusion standards).

24/ We have stated that “[w]e do not view permitting any person to file a complaint against an NASD member or associated person and conducting any resulting proceeding as offering a ‘service’ for purposes of Section 19(d).” Simpson, 53 S.E.C. at 1047.

25/ See, e.g., Avello v. SEC, 454 F.3d 619, 623 (7th Cir. 2006) (noting that an appeal to the NAC precedes a petition for review by the Commission). We reject the suggestion that Sky Capital’s “efforts for relief internally at the NASD are in any event futile, as the bias and prejudice against it permeates, and emanates from, the highest levels at the NASD.” Sky Capital has not shown the kind of “thoroughgoing taint” necessary to establish that resort to the proper appeals procedure would be a “futile” act. Swirsky v. NASD, 124 F.3d 59, 63 & n.3 (1st Cir. 1997).

26/ Insofar as Sky Capital suggests that the Commission investigate NASD’s treatment of the firm, we point out that the determination of whether to investigate is a matter that resides within our discretion. See Exchange Act Sections 17(d)(1), 19(h), & 21(a)(1), 15 U.S.C. §§ 78q(d)(1), 78s(h), 78u(a)(1). The Supreme Court has recognized that “an agency’s decision not to prosecute or enforce . . . is a decision generally committed to an agency’s absolute discretion. This recognition of the existence of discretion is attributable . . . to the general unsuitability for judicial review of agency decisions to refuse enforcement.” Heckler v. Chaney, 470 U.S. 821, 831 (1985); see also Bd. of Trade v. SEC, 883 F.2d 525, 530 (7th Cir. 1989) (citing Heckler v. Chaney). Our decision whether to undertake such matters is separate from our disposition of this proceeding.



Sky Capital's application for review is dismissed. An appropriate order will issue. 27/

By the Commission (Chairman COX and Commissioners NAZARETH and CASEY);  
Commissioners ATKINS and CAMPOS not participating.

Nancy M. Morris  
Secretary

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27/ We have considered all of the parties' contentions. We have rejected or sustained them to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA  
before the  
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934  
Rel. No. 55828 / May 30, 2007

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SKY CAPITAL LLC  
  
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ORDER DISMISSING APPLICATION FOR REVIEW OF ACTION OF REGISTERED  
SECURITIES ASSOCIATION

On the basis of the Commission's opinion issued this day, it is

ORDERED that Sky Capital LL's application for review be, and it hereby is, dismissed.

By the Commission.

Nancy M. Morris  
Secretary