UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 72293 / June 2, 2014

Admin. Proc. File No. 3-15869

In the Matter of the Application of THE DRATEL GROUP, INC. and WILLIAM M. DRATEL for Review of Action Taken by FINRA	ORDER DENYING STAY AND SCHEDULING BRIEFS

The Dratel Group, Inc. ("DGI"), a FINRA member firm, and William M. Dratel, DGI's principal and a registered person, appeal from a FINRA disciplinary action, which found, in part, that applicants willfully engaged in a fraudulent trade allocation scheme known as "cherry picking" and willfully falsified and backdated order tickets, time stamped blank order tickets, and failed to identify customer names on order tickets until after execution. For these violations, FINRA expelled DGI from membership; barred Dratel in all capacities; and ordered Dratel to disgorge $489,000, plus interest, and to pay certain costs.[1] Applicants now move to stay imposition of these sanctions pending their appeal, relief that FINRA opposes. For the reasons

[1] FINRA also found that applicants failed to establish, maintain, and enforce supervisory procedures adequate to prevent post-execution allocation of trades and ensure timely and accurate completion of customer order tickets and that they willfully failed to update certain customer account information periodically. FINRA further found that DGI opened new customer accounts without requiring the customers to show photographic identification and failed to independently test its anti-money laundering ("AML") program. FINRA did not impose additional sanctions for these violations because it already imposed an expulsion and bar for the causes of action related to cherry picking. *Dep't of Enforcement v. The Dratel Group, Inc.*, Compl. No. 2008012925001, 2014 WL 1803377 (May 2, 2014). The additional violations listed in this footnote are therefore not at issue for purposes of applicants' motion to stay the sanctions.

below, applicants' motion is denied.[2] The deadlines for parties to file briefs regarding DGI and Dratel's underlying application for review is also set forth below.

Background

In May 2010, FINRA's Department of Enforcement filed a complaint against applicants, alleging, in part, (i) that between October 1, 2005 and December 31, 2006, applicants willfully executed a fraudulent trade allocation scheme by cherry picking profitable day and overnight trades for Dratel's personal account while steering less profitable trades to their customers' accounts; (ii) that during the same period, applicants willfully falsified and backdated order tickets and time stamped blank order tickets to further the cherry-picking scheme; and (iii) that, between February 2005 and December 2006, applicants failed to identify customer names on order tickets until after execution to further the cherry-picking scheme.

A. A FINRA hearing panel found violations and barred DGI from day trading, barred Dratel in all capacities, imposed monetary sanctions, and ordered disgorgement.

After holding a hearing, an extended hearing panel found applicants liable for the alleged violations, including that DGI and Dratel willfully engaged in a fraudulent trade allocation scheme by using falsified and backdated order tickets. For these violations, the hearing panel barred DGI from day trading, fined DGI $185,000, barred Dratel from associating with any member firm in any capacity, ordered Dratel to disgorge $489,000 in ill-gotten gains, and imposed certain costs.

In reaching this conclusion, the hearing panel found that Dratel had used one of two omnibus firm accounts to place trades for himself and his clients, all while using the same clearing broker. In 2006, these trades yielded profits of almost $500,000 for Dratel and losses of more than $200,000 for his customers. This profit disparity, the hearing panel found, could not "be explained by market forces and [was] more likely than not . . . caused by cherry-picking."[3]

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[2] Applicants' motion also asks for an "interim stay" pending a decision on their request for a stay and for "expedited consideration." Our rules do not provide for such interim relief, but FINRA has represented that it would "not impose the sanctions of a bar for Dratel and expulsion for DGI until the Commission rules on applicants' motion for a stay, and then only if the Commission denies applicants' motion for stay."

[3] The hearing panel limited its findings of violations under cause one (cherry picking) to 2006 only. It found that Dratel's personal account and the discretionary customers' accounts

According to the hearing panel, Dratel would wait to allocate trades between his and his customers' accounts until after he had determined how the trades would perform. Dratel accomplished this, the hearing panel found, by directing his staff to time stamp blank order tickets when he first placed an order. The staff would wait for instructions from Dratel before completing the time-stamped tickets and inputting the allocations into the clearing broker's back-office system, thus allowing Dratel to cherry pick the most profitable trades for himself, at his customers' expense.

Dratel disputed some of these findings. For example, he testified that he faxed allocation instruction sheets to the New York City office throughout the trading day, not just at the end of the day. But the hearing panel found his testimony to be contradictory and noted that numerous order tickets and allocation instructions showed that Dratel faxed the allocation instructions after he had closed out the stock position. Dratel also testified that, even if he waited until later in the day to indicate the proper allocation, he always made allocation decisions before purchasing stock and maintained a running allocation list at his desk. But the hearing panel did not credit this testimony, noting his use of blank tickets and the existence of manually altered and incorrect order tickets and his inability to produce a copy of the list of allocations for the majority of trades at issue.

One member of the hearing panel dissented as to part of the majority's findings and recommended imposing a lesser sanction. In particular, the dissenting member found that "there was no direct evidence of cherry-picking" and that FINRA's "entire case was circumstantial and built exclusively on the statistical unlikelihood of Dratel's day trading success being attributable to anything other than cherry-picking." The statistical evidence, the dissenting member concluded, was based on an arbitrary and unrepresentative sample of applicants' overall trades. The dissenting member also found no evidence that Dratel personally altered order tickets, or directed anyone else to do so, and that it was "not clear that allocations were made (as opposed to transmitted) after the fact."

B. On appeal, the NAC affirmed the findings of violations and increased the sanctions.

Applicants appealed the hearing panel's decision to FINRA's National Adjudicatory Council. In affirming the hearing panel's findings, the NAC rejected the dissenting hearing panel member's finding that FINRA had used arbitrary and unrepresentative data to support its allegations. The NAC found that FINRA's focus on a nine-month period was reasonable because

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generated nearly the same amount of profit for day and overnight trading during the last quarter of 2005, but that their profitability diverged dramatically in early 2006.

Dratel had "significantly increased the amount of day trades that he executed in his own account in October 2005." The NAC further observed that, although Dratel may have been less profitable than his customers before 2006, that did "not counteract the extreme nature of the reversal that occurred in 2006 and the extent of the differences in 2006 between the performance of day and overnight trading in Dratel's personal account and day and overnight trading in the [customers'] accounts, particularly given that Dratel and the customers often traded the same or similar securities."[4] The NAC found that "an overwhelming 83% of Dratel's day and overnight trades were profitable [during the review period] with an average per trade profit of $1,374 per trade." By comparison, only 28% of the customers' day and overnight trades were profitable during the same period, and 72% were unprofitable.

The NAC found applicants' misconduct to be "highly egregious, pervasive, [and] premeditated" and affirmed the hearing panel's decision to bar Dratel in all capacities and order him to disgorge $489,000 in ill-gotten gains. The NAC also increased the sanctions against DGI by replacing the bar from day trading and $100,000 fine with an expulsion from membership. Applicants appeal that decision and ask for a stay of the sanctions pending their appeal.

ANALYSIS

The Commission considers the following in determining whether to grant applicants' motion for a stay: (i) the likelihood that movants will succeed on the merits of their appeal; (ii) the likelihood that movants will suffer irreparable harm without a stay; (iii) the likelihood that another party will suffer substantial harm as a result of a stay; and (iv) a stay's impact on the public interest.[5] Applicants have the burden of establishing that a stay is warranted.[6] For the reasons below, applicants have not met this burden.

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[4] The NAC also found that many of Dratel's earlier losses resulted from Dratel willingly executing cross trades between his and his customers' accounts at above market prices to generate profits for his customers, which contributed to Dratel's increasingly strained financial situation.

[5] *See, e.g.*, *Intelispan, Inc.*, Securities Exchange Act Rel. No. 42738, 54 SEC 629, 2000 WL 511471, at *2 (May 1, 2000).

[6] *See, e.g.*, *Millenia Hope, Inc.*, Exchange Act Rel. No. 42739, 2000 WL 511439, at *1 (May 1, 2000) ("The party requesting the stay has the burden of proof.").

A. Applicants have not shown a likelihood that they will succeed on the merits of their appeal.

Final resolution of applicants' appeal must await the Commission's determination on the merits. But based on the briefs the parties have filed so far, there does not appear to be a strong likelihood that applicants will succeed. Applicants largely repeat the arguments made by the dissenting hearing panel member, which the NAC squarely rejected. The NAC's reasoning is supported by the record before us.[7]

For example, applicants contend that the NAC relied on an arbitrary and unrepresentative sample of applicants' trades and order tickets, instead of finding direct evidence that applicants engaged in a cherry-picking scheme. But based on the record before us, it does not appear that the NAC relied on arbitrary or unrepresentative evidence. Among other things, the NAC considered direct testimony from DGI staffers and order tickets from the firm showing that Dratel would wait until the end of the day, or even after the market closed, before allocating trades made earlier in the day.[8] The NAC also found that Dratel began generating "far more" profits for himself than for his clients at the same time he "dramatically" increased the level of day and overnight trading in his customers' accounts—from an average of 19.2 such trades per month before October 2005 to an average of 82.9 such trades per month during the relevant period.[9] And as the NAC further observed, even if the findings of violations were limited to only some of applicants' trades in certain customer accounts, applicants were "required to comply with [FINRA's] high standards of conduct at all times."[10]

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[7] Applicants contend that the NAC "almost totally ignored" the hearing panel dissent by referring to it in only four footnotes. While the NAC's opinion may have directly mentioned the dissent only four times, much of the NAC's substantive analysis concerned the dissenting member's arguments.

[8] *Cf. James C. Dawson*, Investment Advisers Act Rel. No. 3057, 2010 WL 2886183, at *1 (July 23, 2010) (barring respondent who engaged in a fraudulent cherry-picking scheme by trading for himself and his clients through a single suspense account during the day, but waiting to allocate the trades between his and his clients' accounts until as late as 7 p.m.).

[9] *Cf. SEC v. K.W. Brown & Co*, 555 F. Supp. 2d 1275, 1304 (S.D. Fla. 2007) (finding defendants guilty of fraud where the disparity between the success of their and their customers' trades, "cannot be explained through market forces and . . . is more likely than not . . . caused from cherry picking").

[10] Quoting *Rooms v. SEC*, 444 F.3d 1208, 1214 (10th Cir. 2006); *see also Donner Corp. Int'l*, Exchange Act Rel. No. 55313, 2007 WL 516282, at *11 (Feb. 20, 2007) (finding that respondent's "compliance with the law in some instances does not excuse its dissemination of these violative research reports"); *Robert Fitzpatrick*, Exchange Act Rel. No. 44956, 55 SEC

Nor did the NAC act arbitrarily by considering both day *and* overnight trades as part of the alleged cherry-picking scheme. Applicants claim that cherry picking "is associated almost wholly with day trading," but this is not always the case. The Commission has imposed sanctions for such schemes involving overnight trades,[11] and the NAC's findings do not depend on whether applicants were using day or overnight trades, or whether they had been using the same trading procedures for years, but rather on the specifics of whether applicants were using those procedures to fraudulently cherry pick day and overnight trades during the relevant period.

Applicants also argue that they are likely to succeed on the merits of their appeal because the NAC relied on two cases—*James C. Dawson*[12] and *SEC v. K.W. Brown & Co.*,[13]—which applicants contend "are not remotely close to the facts at hand except for the one part of the *Brown* case where overall profitability of the customers is considered an issue that should be given weight." Applicants contend that, unlike in *Dawson*, their case included two customers who testified favorably about Dratel's character (applicants also attach fifteen letters of additional customer support to their present motion for a stay).[14] Yet the Commission in *Dawson* rejected

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419, 2001 WL 1251680, at *6 (Oct. 19, 2001) (finding that NASD "correctly ruled that prompt compliance with some requests for information does not excuse dilatory compliance with other requests"). The NAC also correctly noted that circumstantial evidence is sufficient to prove a violation of the securities laws and to establish scienter in fraud cases. *See, e.g.*, *Herman & MacLean v. Huddleston*, 459 U.S. 375, 390 n.30 (1983) (noting the sufficiency of circumstantial evidence, particularly in fraud cases); *Valicenti Advisory Servs., Inc. v. SEC*, 198 F.3d 62, 65 (2d Cir. 1999) ("Proof of scienter under the securities laws need not be direct, but may be a matter of inference from circumstantial evidence." (quotation marks omitted)); *Donald M. Bickerstaff*, Exchange Act Rel. No. 35607, 52 SEC 232, 1995 WL 237230, at *5 (Apr. 17, 1995) (finding witness's testimony to be "persuasive evidence" even though it was "circumstantial").

[11] *See, e.g.*, *MiddleCove Capital, LLC*, Exchange Act Rel. No. 68669, 2013 WL 166331, at *1 (Jan. 16, 2013) (imposing remedial sanctions in a settled matter where respondent used a master account for block purchases of securities that he allocated to personal and client accounts, sometimes the day after the trade).

[12] 2010 WL 2886183, at *1 (barring an investment advisor who engaged in a cherry-picking scheme to divert profitable securities trades he made on behalf of a hedge fund to his personal trading account).

[13] 555 F. Supp. 2d at1304 (finding defendants guilty of fraudulent cherry-picking scheme).

[14] FINRA states that these letters should not be given any weight because applicants did not present them below, but given the decision to deny applicants' stay request, we defer questions about the letters' admissibility until the Commission's consideration of applicants' appeal.

just such a reference to clients, noting that it "look[s] beyond the interests of particular investors in assessing the need for sanctions, to the protection of investors generally."[15]

Regarding *Brown*, applicants argue that, unlike their own case, the customers in *Brown* experienced overall losses, that the defendant often got better prices than his customers, and that there was evidence that he failed to identify customer allocations until after execution. But the NAC *also* found that applicants' customers experienced significant losses in day and overnight trades during a specified period of time, that applicants got better prices, and that applicants failed to identify customer allocations until after execution.

We are similarly unpersuaded by applicants' claim that the NAC erred by not citing another case, *SEC v. Slocum, Gordon & Co.*[16] There, a district court credited the defendants' explanations for their trades and found that the Commission had not proved that defendants engaged in a cherry-picking scheme. Here, the hearing panel expressly did *not* credit Dratel's explanations about his trades. And there is no evidence at this point that provides a basis for overturning that credibility finding.[17] Applicants also argue that *Slocum* supports their appeal because the court found that the defendants' customer accounts had "performed extremely well" (a point applicants make about their own customers' overall performance in day trading from 1999 to 2006).[18] But applicants' reliance on *Slocum* is misguided. The court's observation concerned customers' success during *the relevant period* covered by the Commission's charges, not overall. The court found that this success undermined the Commission's allegation that the

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[15] *Dawson*, 2010 WL 2886183, at *4; *cf. also Eric J. Weiss*, Exchange Act Rel. No. 69177, 2013 WL 1122496, at *9 (Mar. 19, 2013) (holding that FINRA's "power to enforce its rules is independent of a customer's decision not to complain" (quoting *Maximo Justo Guevara*, Exchange Act Rel. No. 42793, 54 SEC 655, 2000 WL 679607, at *6 (Mar. 18, 2000), *pet. for review denied*, 47 F. App'x 198 (3d Cir. 2000))). Applicants further contend that the NAC exhibited prejudice and vindictiveness by not considering Dratel's favorable relationship with his customers, such as his efforts to cover his customer's losses in 2004 and 2005 with cross trades, which he claims the NAC wrongly labeled as a "negative." To the contrary, the NAC's consideration of Dratel's cross trades was reasonable and fairly limited, noting that the cross trades partly explained why his customers had not suffered greater losses in 2004 and 2005 and that the cross trades also contributed to Dratel's increasingly strained financial situation.

[16] 334 F. Supp. 2d 144 (D.R.I. 2004).

[17] Credibility determinations of the initial fact finder are entitled to considerable weight and "can be overcome only when there is substantial evidence for doing so." *Dennis Todd Lloyd Gordon*, Exchange Act Rel. No. 57655, 2008 WL 1697151, at *9 (Apr. 11, 2008) (declining to overturn a hearing panel's credibility determination).

[18] Quoting *Slocum*, 334 F. Supp. 2d at 173.

defendants were cherry picking the most profitable trades for themselves during that period.[19] The NAC, by comparison, cited to the customers' *lack* of success during the relevant period, which supports FINRA's allegation that applicants were cherry picking trades. We thus see nothing in *Slocum* that demands a different result than the NAC reached.

B. Applicants have not shown a likelihood that they or another party will suffer irreparable harm.

Applicants state that, without a stay, "Dratel would be barred from a business he has been a part of for over thirty-seven years and [that is] his only source of income." Yet applicants provide no further detail about how this would cause him irreparable harm, and the Commission has held repeatedly that "'the fact that an applicant may suffer financial detriment does not rise to the level of irreparable injury warranting issuance of a stay.'"[20]

Applicants also claim that their customers "will suffer should they lose access to [Dratel's] honesty, integrity and investing acumen." But this vague reference to his customers' lost access to applicants' services is not enough to demonstrate irreparable harm.[21] If anything, the record before us suggests that applicants' customers may be better served if applicants are not participating in the securities industry pending their appeal. As the NAC found, "Dratel engaged in an ongoing pattern of placing his own interests before those of his customers."

C. Denying applicants' motion will serve the public interest.

As explained above, applicants have been found to have engaged in fraud and have not demonstrated a likelihood that they will overturn that finding on appeal. Nor have applicants demonstrated a likelihood that they or another party will suffer irreparable harm without a stay. Applicants also have disciplinary history in addition to the NAC decision in this matter. In 2006,

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[19] *Id.*

[20] *Mitchell T. Toland*, Exchange Act Rel. No. 71875, 2014 WL 1338145, at *2 (Apr. 4, 2014) (quoting *Robert J. Prager*, Exchange Act Rel. No. 50634, 2004 WL 2480717, at *1 (Nov. 4, 2004)); *see also Associated Sec. Corp. v. SEC*, 283 F.2d 773, 775 (10th Cir. 1960) (stating that the "necessity of protection to the public far outweighs any personal detriment"); *Michael A. Rooms*, Admin. Proc. File No. 3-11621, 2004 SEC LEXIS 3158, at *5 (Nov. 17, 2004) (denying stay by concluding that applicant's argument that "the bar imposed on him ha[d] resulted in severe financial loss and damages to his reputation . . . d[id] not rise to the level of irreparable injury").

[21] *Cf. Rooney, Pace Inc.*, Exchange Act Rel. No. 23763, 1986 WL 626057, at *5 (Oct. 31, 1986) (finding suspension to be in the public interest despite mitigation claim that suspension would "depriv[e] registrant of the services of its key executive officer").

applicants settled a matter in which FINRA found, in part, that applicants failed to timely report two customer complaints that they subsequently settled, failed to amend and update Dratel's Form U4, and failed to timely obtain an opinion of counsel concerning a lawsuit that could have had a material impact on DGI's net capital computation. In 2003, DGI settled a matter in which FINRA found that the firm failed timely to report equity transactions, failed to accurately disclose required information, failed to report time on order tickets completely, and failed to properly prepare certain order tickets.[22] We therefore find that the public interest favors denial of their motion.[23]

Accordingly, IT IS ORDERED that, pending Commission review of his appeal, applicants' motion to stay the sanctions FINRA imposed is denied.

Furthermore, IT IS ORDERED, pursuant to Rule 450(a) of the Rules of Practice,[24] that a brief in support of DGI and Dratel's application for review shall be filed by July 2, 2014. A brief

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[22] Although not cited by the NAC, we note that another FINRA hearing panel recently found, in an unrelated case, that applicants engaged in "numerous rules violations . . . relate[d] to disclosure of liens and judgments, creation and preservation of order memoranda, maintenance of books and records, and other fundamental requirements" that the hearing panel found "depict a pattern of non-compliance with requirements imposed by securities laws and regulations governing some of the most basic aspects of operating a brokerage firm." *Dep't of Enforcement v. The Dratel Group, Inc.*, FINRA Discp. Proc. No. 2009016317701, 2013 WL 6835085, at *1 (Sept. 19, 2013) (suspending Dratel for twenty-five business days, jointly and severally fining applicants $31,000, fining Dratel an additional $5,000, fining the firm an additional $2,500, and ordering applicants to pay certain fees and costs).

[23] *Cf. Hans N. Beerbaum*, Exchange Act Rel. No. 55731, 2007 WL 1376365, at *5 (May 9, 2007) (rejecting applicant's argument that "allowing [him] to remain in the industry would serve the interest of investors"); *Barr Fin. Group, Inc.*, Investment Adviser Act Rel. No. 2179, 56 SEC 1243, 2003 WL 22258489, at *7 (Oct. 2, 2003) (finding a bar "amply warranted" where, "[a]lthough there is no evidence that any customer lost money as a result of respondents' violations, their actions clearly posed a threat to the investing public").

[24] 17 C.F.R. § 201.450(a). FINRA filed a copy of the index to the record on May 23, 2014, pursuant to Rule 420(e) of the Rules of Practice, 17 C.F.R. § 201.420(e).

in opposition shall be filed by August 1, 2014, and any reply brief shall be filed by August 15, 2014.[25] Pursuant to Rule 180(c) of the Rules of Practice,[26] failure to file a brief in support of the application may result in dismissal of this review proceeding.

For the Commission, by the Office of the General Counsel, pursuant to delegated authority.

Jill M. Peterson
Assistant Secretary

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[25] As provided by Rule 450(a), no briefs in addition to those specified in this schedule may be filed without leave of the Commission. Attention is called to Rules of Practice 150–153, 17 C.F.R. §§ 201.150–153, with respect to form and service, and Rule of Practice 450(b) and (c), 17 C.F.R. § 201.450(b), (c), with respect to content and length limitations. Requests for extensions of time to file briefs will be disfavored.

[26] 17 C.F.R. § 201.180(c).