

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF FLORIDA

CASE NO.:  
**08-81039-CIV-MARRA/JOHNSON**

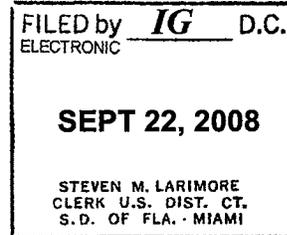
SECURITIES AND EXCHANGE  
COMMISSION,

**Plaintiff,**

v.

**GARY J. GROSS,**

**Defendant.**



**COMPLAINT**

Plaintiff Securities and Exchange Commission alleges:

**I. INTRODUCTION**

1. From at least early 2004 through approximately September 2006, Gary Gross, a former registered representative with broker-dealer Axiom Capital Management, Inc., defrauded several of his customers by making material misrepresentations and omissions about the risks and suitability of securities he bought for them, churning customer accounts, and fabricating customer account values. Many of Gross' victims were elderly Jewish investors who trusted Gross based on his statements that he was involved in the Jewish community and their perceived personal relationships with him.

2. Gross persuaded many customers to open Axiom brokerage accounts and transfer existing accounts to Axiom by pledging he could deliver greater income from and safety in their investments than their current brokers. Once customers invested funds, Gross frequently disregarded their largely conservative investment objectives in favor of unsuitable mutual and closed-end funds without disclosing the associated risks. Gross also frequently churned his

customers' accounts and made other unsuitable trades that benefited him at the expense of his customers.

3. In 2005, Gross began purchasing risky, illiquid private placements and private investments in public equities in his customers' accounts. Gross emphasized the purported profit potential of these investments while failing to disclose their substantial risks. In late summer 2005, Gross also began recommending and making purchases of a highly speculative penny stock for his customers – all contrary to their generally risk-averse investment objectives.

4. Beginning in September 2005, when some customers complained about their losses and asked questions about their account statements, Gross again abused their trust and lied. He told them to ignore the account statements as inaccurate and created fraudulent documents that misrepresented the actual value of their investments and sometimes included baseless projections. Through his misconduct, Gross generated substantial commissions and other fees, while many customers lost large amounts of their investments. While Gross reaped more than \$700,000 in ill-gotten gains, his customers lost more than \$2.7 million.

5. By engaging in the conduct described above, and described more fully below, Gross violated Section 17(a) of the Securities Act of 1933 (“Securities Act”), 15 U.S.C. § 77q(a); and Section 10(b) and Rule 10b-5 of the Securities Exchange Act of 1934 (“Exchange Act”), 15 U.S.C. § 78j(b) and 17 C.F.R. § 240.10b-5. Unless enjoined, Gross is reasonably likely to continue violating the securities laws.

## **II. DEFENDANT AND RELEVANT ENTITY**

6. Gross, 56, is a resident of Far Rockaway, New York. From January 2003 through early January 2007, Gross lived in Boca Raton, Florida and was associated as a registered representative with Axiom in its Boca Raton branch office. Gross is the subject of more than

twenty customer complaints filed with the Financial Industry Regulatory Authority in connection with his activities at Axiom. While Gross is not currently associated with a broker-dealer, he still maintains Series 7, 63 and 65 securities licenses.

7. **Axiom** is a Delaware corporation with its principal place of business in New York, New York. It has been registered with the Commission since June 22, 1990 as a broker-dealer. Axiom was also registered as an investment adviser from June 2004 through October 2006. From December 2002 through early 2007, Axiom maintained its only branch office in Boca Raton.

### **III. JURISDICTION AND VENUE**

8. This Court has jurisdiction over this action pursuant to Sections 20(b), 20(d), and 22(a) of the Securities Act, 15 U.S.C. §§ 77t(b), 77t(d), and 77v(a); and Sections 21(d), 21(e), 21A and 27 of the Exchange Act, 15 U.S.C. §§ 78u(d), 78u(e), 78u-1 and 78aa.

9. This Court has personal jurisdiction over Gross and venue is proper in the Southern District of Florida because Gross' acts, transactions, practices, and courses of conduct giving rise to the violations alleged in this Complaint occurred in the Southern District of Florida. Specifically, during the events alleged in the Complaint, Gross resided in the Southern District of Florida, and conducted business and engaged in the abusive sales practices described in this Complaint there.

10. Gross, directly and indirectly, made use of the means and instrumentalities of interstate commerce, the means and instruments of transportation and communication in interstate commerce, and the mails, in connection with the acts, transactions, practices, and courses of conduct set forth in this Complaint.

#### **IV. FACTS**

11. From at least early 2004 through approximately September 2006 (“the relevant time”), Gross convinced customers to open accounts with him at Axiom or switch their brokerage accounts there. Many of Gross’ customers often were elderly, unsophisticated investors, who wanted only to preserve their principal and grow their portfolio while investing with minimal risk. Instead of helping these people pursue their goals, Gross defrauded them by making materially misleading and unsuitable recommendations, engaging in unauthorized trading and churning, and giving them falsified and baseless account statements.

##### **A. Gross’ Misleading and Unsuitable Recommendations and Unauthorized Purchases**

###### **1. Misleading and Unsuitable Recommendations**

12. During the relevant time, Gross recommended placing, and placed, customers in mutual and closed-end funds, while failing to disclose the risks associated with those investments and their unsuitability for his customers’ investment objectives.

13. Once customers transferred their accounts to Axiom, Gross routinely liquidated substantial portions of their investments, often consisting of diversified, relatively low-risk securities such as conservative mutual funds, blue chip stocks and bonds, and replaced them with large concentrations of funds such as the Kelmoore Strategy Eagle Fund and another Kelmoore mutual fund.

14. Gross failed to disclose to his customers the risk factors associated with Kelmoore funds, including Kelmoore Eagle’s covered call option strategy and the volatility inherent in the mid-cap companies Kelmoore Eagle held, among other things. He failed to make these disclosures despite the fact that Kelmoore prospectuses discussed these risks and described an investment strategy contrary to that which Gross’ customers sought. As discussed in more detail

below, after investing heavily in Kelmoore, Gross made these unsuitable investments even less appropriate for his customers by liquidating them after only a short period, also in disregard of the Kelmoore prospectuses' recommendations.

15. For example, one of Gross' customers was a 69-year-old retiree whose investment objectives were income and growth. In March and April 2005, Gross invested more than half of her portfolio in Kelmoore Eagle, telling her it provided good income and falsely stating there was no risk. In just six weeks, Gross purchased \$575,000 of Kelmoore Eagle in her account. Gross liquidated the entire position 33 days later for a net loss of approximately \$13,500, while generating approximately \$15,000 in sales charges from these transactions.

16. Gross' abusive activity was exacerbated by his practice of trading on margin in his customers' accounts. Gross used margin to effect larger purchases of unsuitable funds than his customers could have made had they not used margin. Gross never discussed margin trading with his customers prior to utilizing it in their accounts, and did not disclose the risks associated with margin, such as higher costs through interest payments and potentially increased losses.

17. Further, while Gross promised his customers large monthly income payments, he failed to disclose the income they received from Kelmoore and other, similar funds was reduced by the margin interest charged. Gross told some of his customers not to worry about margin call letters they received, and directed them to throw the letters away.

18. Gross also materially misled his customers about other unsuitable funds he pitched. For example, he recommended his customers invest in initial public offerings, even though these funds had no track record. He also recommended non-diversified funds such as those limited to a particular country. Gross failed to disclose to his customers the risks associated with these investments.

## **2. Gross' Unauthorized Trading**

19. Additionally, Gross often conducted unauthorized trading on behalf of his customers. Although Gross did not have discretionary customer accounts, he often effected transactions in various securities without obtaining the customers' authorization. This trading usually cost his customers money but generated more than \$500,000 in commissions for himself.

20. For example, in the account of a 97-year-old customer, Gross made seventeen unauthorized buys of unsuitably risky funds between February and October 2006, purchasing an aggregate amount of \$1,558,000. He falsely marked eight of those transactions as ones he did not solicit from the customer. During this same period, Gross made seven sales transactions in these funds, even though the customer had held them for less than two months, and even though the sale price was almost always the same as or lower than the purchase price. During those nine months, Gross generated approximately \$40,000 in commissions from this trading in the customer's account. The customer's account lost \$420,300 in net equity and was charged \$46,000 in margin interest, while developing a margin debt of more than \$675,000 by the end of November 2006.

## **3. Misleading and Unsuitable Recommendations of Private Placements and PIPEs**

21. From early 2005 through approximately September 2006, Gross touted the purported profit potential of various private placements and investments known as PIPEs (private investments in public equities) to his customers. Gross told his customers the private placements and PIPEs were riskless and the issuers were high-quality companies. Gross promised some customers they would be able to sell these investments within months and reap large profits.

22. Gross, however, failed to disclose the risks accompanying these investments. For example, contrary to his representations, the companies were start-up ventures in search of

funding, with little or no track record. Gross also did not tell customers they would receive restricted stock they could not trade until the issuers' registration statements were declared effective. Additionally, Gross did not tell his customers that the issuers' registration statements could be delayed, and that customers would consequently be unable to convert their restricted shares into free-trading common stock within the time Gross promised.

23. The private placements and PIPEs were unsuitable recommendations for at least four of Gross' customers who, in light of their need for low-risk and conservative investment objectives, could ill afford the risks associated with these speculative and illiquid securities. At least four of the customers Gross defrauded into investing in the private placements and PIPEs were elderly and risk-averse, with limited annual income and an investment objective of income and growth.

24. In the case of one elderly female customer, who had invested approximately \$700,000 with Gross in 2005, Gross liquidated \$500,000 of her portfolio to purchase private placement and PIPE offerings, and margined other parts of her portfolio for additional, similar investments during the spring and summer of 2005. In August 2005, in response to her concerns about the risky nature of the private placements and PIPEs, Gross told the customer her purchases were in high-quality companies guaranteed to make money. He also promised nothing could happen to her money with those investments, and if they did not work out he could return her money by selling her holdings to institutional clients. Gross never told her he was using margin for her purchases and never explained the risks or costs of margin.

25. In December 2005, Gross further deflected the customer's concerns with fraudulent written calculations showing her \$75,000 PIPE investment was worth \$129,500.

Gross based these calculations on a value of \$3.50 per share, which was baseless because the free-trading stock of the company was, at most, \$1.95 per share.

26. In March 2006, Gross opened a new account for a couple in their late seventies. The husband suffered from mild dementia, and the wife handled most investment decisions by herself. Without explaining the purpose, Gross convinced the customer to liquidate more than 33% of the account's net equity, or approximately \$250,000. Gross then used that money to buy a private placement in a company called Mobilier, Inc. without getting prior authorization for the purchase.

27. When the customer received her statement in the spring of 2006, she called Gross for an explanation. Gross falsely told her he had purchased the shares from an initial public offering that would start generating \$2,500 in monthly income within a few weeks. In reality the Mobilier purchase was a secured convertible promissory note related to bridge financing, and Mobilier was not publicly traded at the time and would not be until approximately a year later. The customer never received any income from the purchase. Gross never disclosed the true nature of the investment, much less any of the associated risks.

28. Gross similarly misled younger customers into high-risk investments, even when they clearly had conservative investment objectives. Promising tremendous rates of return, Gross convinced one couple in their late forties, with income and growth as their investment goals, to invest 75% of their portfolio and all of the equity in their home in four private placements and PIPEs. Gross did not disclose the risks of the investments, or that his promises of high returns were baseless.

29. At least seven of Gross' customers purchased more than \$1.5 million in private placements and PIPEs, each losing almost their entire investment. Meanwhile, Gross generated more than \$75,000 personally in fees from those transactions.

#### **4. Gross' Misleading, Unsuitable Recommendations and Unauthorized Purchases of a Penny Stock**

30. During 2005 and 2006, Gross touted the penny stock of Vistula Communication Services, Inc. to his customers. Gross falsely told his customers Vistula stock was a great investment because Vistula was the only firm marketing a voice-over-internet communication system. He disclosed none of the significant risks associated with Vistula, or the risks concerning investments in penny stocks in general, which include increased potential losses due to the speculative nature of penny stocks and their generally low trading volume.

31. Gross bought large amounts of Vistula stock for his customers in purchases that were unsuitable for them due to their investment objectives and desire to minimize risk. He sometimes used margin to do so, and purchased the stock for customers' portfolios without prior authorization.

32. For example, between July and October 2005, Gross concentrated almost half of one 69-year-old customer's portfolio in Vistula. Without telling the customer, he used margin to effect a portion of the Vistula purchases. This contradicted the customer's modest and low-risk investment objectives. When the customer realized she had bought Vistula stock on margin, she told Gross she did not want to do so. Gross told her it was "nothing," and she should stop worrying. During 2005 and 2006, the customer's realized and unrealized losses from the Vistula purchases were more than \$43,000.

33. In another instance, in September and October 2005, for two married customers in their late seventies, Gross purchased more than 30,000 shares of Vistula stock without telling

them. By June 2006, Vistula stock comprised approximately 15% of their account's net equity, despite their conservative investment objectives of income and growth with low risk. When the couple asked Gross why their account statement showed minus signs in the net debit balance, Gross groundlessly promised the Vistula stock would generate \$150,000 for them within a few weeks. These customers, however, never received any payment and their unrealized losses in Vistula stock totaled more than \$31,000 by the end of September 2006.

34. Gross failed to give his customers any adverse information about Vistula, continuing instead to push the profit potential of Vistula's penny stock and offer baseless share price projections, often even as Vistula's stock price declined.

35. In December 2005, Gross falsely told one customer her Vistula stock was worth almost twice the actual amount. In the fourth quarter of 2006, Gross left another customer a voice mail message baselessly saying she should be hearing "very positive" information from Vistula from that point forward, something that never happened.

36. During the year Gross hyped Vistula to his customers, he failed to disclose there were other publicly held companies marketing, developing, and implementing a voice-over-internet system, or that Vistula's stock price dropped by more than 50%. Additionally, Gross did not tell his customers that while he was purchasing Vistula stock for them, Vistula's public filings with the Commission disclosed the company's cash flow had declined and the company needed capital.

37. Gross also never disclosed to his customers that Vistula's Form 10-QSB for the quarter ending June 2006 showed Vistula's net losses had almost doubled from the same period in 2005, it had prepared its financial statements on a going concern basis, and it had net losses of more than \$7 million and a working capital deficit of more than \$3 million.

38. Gross bought 315,650 shares of Vistula stock worth approximately \$508,052 for seven customers. By the end of September 2006, they collectively had lost 54% of their investment – about \$274,564.

### **B. Gross' Churning of Customer Accounts**

39. Gross also churned customer accounts, often treating non-discretionary accounts as if he had discretion over them, and using that control to churn the accounts.

40. Turnover ratios measure the number of times per year new securities replace securities already in a customer's account. A turnover ratio of six or greater generally indicates that excessive trading has occurred. During the relevant time, the turnover ratios for at least four of Gross' customers' accounts ranged from six to nineteen.

41. Breakeven analysis determines the rate of return an account must earn annually to cover transaction costs such as commissions. Trading practices that require an account to appreciate in excess of 20% to break even generally indicate excessive trading. The breakeven analysis for the same four customer accounts showed these customers would have had to realize annual returns of between 19% and 49% to break even.

42. Gross often purchased and liquidated his customers' positions within a week, and sometimes in as little as two trading days. Gross often made these transactions without obtaining the customers' authorization.

43. For example, between March and September 2006, Gross made 131 transactions in one 74 year-old customer's account. Gross' trading of funds and individual equities resulted in a turnover rate of 11.1 for that period and an annualized turnover rate of 19. Gross never informed the customer of these trades, and failed to disclose that he used margin to effect many of the transactions. During this period, the account had a margin debit as high as \$277,518 when

the net equity of the account was only approximately \$340,000. The customer ultimately lost approximately \$350,000 due to Gross' churning and other misconduct.

44. For two married customers in their sixties, with income and growth as their investment objectives, Gross made 230 transactions in their account from mid-2003 through January 2007, resulting in an annual turnover rate of 9.2. Many of these were unauthorized trades, and Gross additionally used margin without explaining the risks to the customers. He eventually drove their account's margin debt in August 2004 to approximately \$399,000 compared to net equity of only \$292,894. When the customers discovered Gross' trading, the wife told Gross they did not want to invest on margin. Gross baselessly told her not to worry because she and her husband would get back the margin interest. However, due to Gross' churning and other misconduct, these customers lost at least \$150,000.

### **C. Fabricated Customer Account Values and Baseless Projections**

45. During 2005 and 2006, Gross created documents for several customers that misrepresented the value of their investments and contained baseless projections of future performance. Gross then orally reiterated these misrepresentations.

46. In the fall of 2005, several customers expressed concern that their account statements reflected large investment losses. Gross' customers were also confused when they noticed that the private placements and PIPEs were listed on their account statements as either unpriced or restricted. In meetings with customers from the fall of 2005 until late 2006, Gross resorted to misrepresenting the value of their accounts and providing baseless projections.

47. In these meetings, Gross told his customers that their Axiom monthly account statements were not accurate. He claimed the account values were actually much higher, primarily because the value of the private placements and PIPEs were not reflected, or were

improperly reflected, on their statements. Gross made unfounded handwritten notations on account statements and other documents adding the purported values of amounts invested in private placements, PIPEs, and Vistula stock to the account values on the statements. He falsely told the customers his handwritten calculations reflected the true value of their accounts.

48. For example, in around June 2006, a married couple in their forties asked Gross why the balance on their Axiom statements was much lower than the amount they initially invested with Gross. Gross lied, telling them their account statement did not show the actual value of their investments because it did not reflect the value of their investments in private placements and PIPEs. Gross wrote a list of the amounts they invested in each private placement and PIPE (totaling \$418,000) and then wrote the figure \$730,000, stating that this larger figure represented their actual account value. Finally, Gross also wrote the figure \$948,000, and told his customers that in thirty or sixty days the value of their account would grow to that amount.

49. Gross' representations were false and his projections were groundless. The customers' shares in the private placements and PIPEs were restricted and illiquid, making them far less valuable than he stated. There was no public information to support Gross' valuations or projections.

50. Gross' representations to his customers of the value of their portfolios were baseless because the PIPEs and private placements generally involved restricted shares, which were illiquid. Additionally, Gross falsely represented Vistula stock was trading at a much higher price than it sold for in actual trading. There was no information to support the higher value he used or even any projections the price would eventually rise as high as he indicated.

## COUNT I

### Fraud in Violation of Section 17(a)(1) of the Securities Act

51. The Commission repeats and realleges Paragraphs 1 through 50 of this Complaint as if fully set forth herein.

52. During the relevant time period, Gross, directly or indirectly, by use of the means or instruments of transportation or communication in interstate commerce or by use of the mails, in the offer or sale of securities, as described in this Complaint, knowingly, willfully or recklessly employed devices, schemes, or artifices to defraud.

53. By reason of the foregoing, Gross has directly or indirectly violated and, unless enjoined, is reasonably likely to continue to violate, Section 17(a)(1) of the Securities Act, 15 U.S.C. § 77q(a)(1).

## COUNT II

### Fraud in Violation of Sections 17(a)(2) and 17(a)(3) of the Securities Act

54. The Commission repeats and realleges Paragraphs 1 through 50 of this Complaint as if fully set forth herein.

55. During the relevant time period, Gross, directly or indirectly, by use of the means or instruments of transportation or communication in interstate commerce or by the use of the mails, in the offer or sale of securities, as described in this Complaint: (a) obtained money or property by means of untrue statements of material facts and omissions to state material facts necessary to make statements made, in light of the circumstances under which they were made, not misleading; and/or (b) engaged in transactions, practices and courses of business which operated or would have operated as a fraud or deceit upon purchasers of securities.

56. By reason of the foregoing, Gross has directly or indirectly violated and, unless enjoined, is reasonably likely to continue to violate, Sections 17(a)(2) and 17(a)(3) of the Securities Act, 15 U.S.C. § 77q(a)(2) and 77q(a)(3).

### **COUNT III**

#### **Fraud in Violation of Section 10(b) of the Exchange Act and Rule 10b-5**

57. The Commission repeats and realleges Paragraphs 1 through 50 of this Complaint as if fully set forth herein.

58. During the relevant time period, Gross, directly or indirectly, by use of the means and instrumentality of interstate commerce or of the mails in connection with the purchase or sale of the securities, as described in this Complaint, knowingly, willfully or recklessly: (a) employed devices, schemes or artifices to defraud: (b) made untrue statements of material fact and omitted to state material facts necessary in order to make statements made, in light of the circumstances under which they were made, not misleading; and/or (c) engaged in acts, practices and courses of business which operated as a fraud or deceit upon purchasers of such securities.

59. By reason of the foregoing, Gross has directly or indirectly violated and, unless enjoined, is reasonably likely to continue to violate, Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5.

## **RELIEF REQUESTED<sup>1</sup>**

**WHEREFORE**, the Commission respectfully requests that the Court:

### **Declaratory Relief**

Declare, determine and find Gross committed the violations of the federal securities laws alleged in this Complaint.

### **Permanent Injunctive Relief**

Issue a Permanent Injunction, restraining and enjoining Gross from violating Section 17(a) of the Securities Act, 15 U.S.C. §77q(a), and Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5.

### **Disgorgement and Prejudgment Interest**

Issue an Order directing Gross to disgorge all ill-gotten gains, including prejudgment interest, he received as a result of the acts or courses of conduct alleged in this Complaint.

### **Civil Money Penalty**

Issue an Order directing Gross to pay a civil money penalty pursuant to Section 20(d) of the Securities Act, 15 U.S.C. § 77t(d), and Section 21(d) of the Exchange Act, 15 U.S.C. § 78u(d).

---

<sup>1</sup> On November 21, 2007, Gross filed a pending Chapter 7 voluntary petition for bankruptcy in the United States Bankruptcy Court for the Southern District of Florida. *In re Gary Jay Gross*, Case No. 07-20281-BKC-PGH (Bankr. S.D. Fla.). Although the Commission's claims for disgorgement, prejudgment interest and penalties are non-dischargeable under Sections 523(a)(7) and (a)(19) of the Bankruptcy Code, the Commission has filed a proof of claim in Gross' bankruptcy case. This civil action brought by the Commission continues during Gross' pending bankruptcy case as an action by a governmental unit to enforce the Commission's police or regulatory power, in accordance with the exception to the automatic stay provided in Section 362(b)(4) of the Bankruptcy Code. Any monetary judgment entered against Gross in this civil action will be a non-dischargeable debt pursuant to Section 523(a)(19) of the Bankruptcy Code, and the Commission will seek a finding to that effect in this civil action. While the Commission seeks to establish the amount of disgorgement, plus prejudgment and post-judgment interest, and the amount of civil money penalty in this action, the Commission will pursue any enforcement of a money judgment against Gross, his bankruptcy estate or property of Gross' bankruptcy estate in accordance with the Bankruptcy Code and Rules.

**Penny Stock Bar**

Issue an Order prohibiting Gross from participating in any future offering of a penny stock security pursuant to Section 20(g) of the Securities Act, 15 U.S.C. §77t(g), and Section 21(d)(6) of the Exchange Act, 15 U.S.C. § 78u(d)(6).

**Further Relief**

Grant such other and further relief as may be necessary and appropriate.

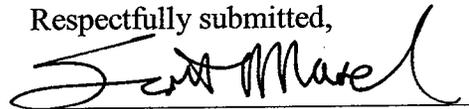
**Retention of Jurisdiction**

Further, the Commission respectfully requests the Court retain jurisdiction over this action in order to implement and carry out the terms of all orders and decrees that may hereby be entered, or to entertain any suitable application or motion by the Commission for additional relief within the jurisdiction of this Court.

Dated: September 22, 2008.

Respectfully submitted,

By:



Scott A. Masel  
Senior Trial Counsel  
Fla. Bar No. 007110  
[masels@sec.gov](mailto:masels@sec.gov)  
Direct Dial: (305) 982-6398

Elisha L. Frank  
Senior Counsel  
Fla. Bar No. 49689  
[franke@sec.gov](mailto:franke@sec.gov)  
Direct Dial: (305) 982-6392

Attorneys for Plaintiff  
**U.S. Securities and Exchange Commission**  
801 Brickell Avenue, Suite 1800  
Miami, Florida 33131  
Telephone: (305) 982-6300  
Facsimile: (305) 536-4154