

**UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION**

SECURITIES AND EXCHANGE COMMISSION,)	
)	
Plaintiff,)	Case No. 17-cv-6917
)	
v.)	
)	
JASON NAPODANO,)	
BILAL BASRAI, and)	
BRYCE STIRTON,)	
)	
Defendants.)	

COMPLAINT

Plaintiff Securities and Exchange Commission (the “Commission”) for its Complaint against Defendants Jason Napodano (“Napodano”), Bilal Basrai (“Basrai”), and Bryce Stirton (“Stirton”) (collectively “Defendants”), alleges as follows:

SUMMARY

1. This case involves insider trading by Napodano, the former head research analyst at Zacks Small Cap Research (“SCR”), Basrai, the former head of the investment banking division of LBMZ Securities, Inc. (“LBMZ”), formerly known as Zacks & Company, a registered broker-dealer, and Stirton, a former employee at LBMZ’s investment banking division. Napodano also committed securities fraud by making material misrepresentations or omissions in research reports and articles he authored that were disseminated through SCR and a financial website. Defendants collectively generated profits of approximately \$185,000 from their illegal trading.

2. On three separate occasions in 2014, Defendants traded securities while in possession of material nonpublic information they learned through their work for issuer clients of LBMZ and/or SCR. In January 2014, Defendants traded in advance of an announcement by a biotechnology company (“Company A”) regarding a licensing agreement, which Defendants learned about through LBMZ’s and SCR’s business relationships with Company A. In November 2014, Defendants traded in advance of an announcement by a medical technology company (“Company B”) regarding the termination of a merger agreement, which Defendants learned about through LBMZ’s business relationship with Company B. And in August of 2014, Defendants traded in advance of an announcement by a pharmaceutical company (“Company C”) that it had been approved for listing on the NASDAQ Capital Market, which Defendants learned about through SCR’s business relationship with Company C.

3. In another instance in May 2014, Napodano and Basrai traded securities while in possession of material nonpublic information Basrai received when he was personally solicited by another investment banking firm as a potential investor in a secondary public offering by a biotechnology company (“Company D”). Basrai had affirmatively agreed not to use, trade on, or disclose any confidential information about the company or the transaction, but breached this duty when he traded in advance of the announcement of the offering and passed the information to Napodano.

4. Defendants also traded while in possession of material nonpublic information regarding the timing and substance of SCR-issued research reports. Between August 2012 and June 2015, Napodano traded profitably around the publication of 42 SCR research reports he or his subordinates authored. The reports were the property of SCR and Napodano owed a fiduciary duty to SCR to maintain their confidentiality until they were published. In July 2014,

Basrai and Stirton also traded in advance of the publication of one of these SCR-issued reports, which they learned about through LBMZ's business relationship with SCR.

5. Defendants each had a relationship of trust and confidence with their respective employers and were regularly in possession of sensitive and confidential information. Both SCR and LBMZ had insider trading policies which prohibited employees from buying or selling securities while in possession of such nonpublic information. Defendants' purchases of securities while in possession of material nonpublic information obtained through their employment breached their respective duties to their employers.

6. Between August 2012 and June 2015, Napodano traded profitably in advance of 100 SCR reports and financial website articles that he authored. Each of the SCR reports and financial website articles contained a material misrepresentation or omission regarding Napodano's ownership of stocks mentioned in the publications. The financial website articles also contained an additional material misrepresentation or omission regarding Napodano's business relationships with companies mentioned in the articles.

7. Based on actual and imputed profits from their illegal trading, Napodano made a profit of \$143,865.48, Basrai made a profit of \$39,668.37, and Stirton made a profit of \$2,218.87.

VIOLATIONS AND RELIEF SOUGHT

8. As a result of the conduct alleged herein, Defendants violated Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. § 78j(b)], and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

9. In the interest of protecting the public from the Defendants engaging in any further acts, practices or courses of businesses like those set forth in this Complaint, the

Commission seeks an order permanently enjoining Defendants from further violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

10. The Commission further seeks an order requiring Defendants to disgorge their ill-gotten gains from their illegal trading, together with prejudgment interest thereon, and to pay civil monetary penalties.

11. Finally, the Commission seeks an order permanently barring Napodano and Basrai, and barring Stirton for five years, from participating in an offering of penny stock 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)].

JURISDICTION AND VENUE

12. This Court has jurisdiction over this action under Sections 21(d), 21(e), 21A, and 27 of the Exchange Act [15 U.S.C. §§ 78u(d), 78u(e), 78u-1 & 78aa]. The Defendants, directly and/or indirectly, made use of the means or instrumentalities of interstate commerce, or the mails, or the facilities of a national securities exchange in connection with the transactions, acts, practices, and courses of business alleged in this Complaint.

13. Venue in this District is proper under Section 27 of the Exchange Act [15 U.S.C. § 78aa] because the acts, practices, transactions and courses of business constituting the alleged securities law violations occurred in substantial part within this District.

DEFENDANTS

14. **Jason Napodano**, age 43, resides in Waxhaw, North Carolina. During the relevant time period, Napodano was the Managing Director and Senior Biotechnology Analyst at

SCR, a division within Zacks Investment Research, in which he supervised a research staff of between eight and 10 analysts and personally covered and issued research reports on approximately 50 small cap biotechnology companies.

15. **Bilal Basrai**, age 43, resides in Naperville, Illinois. During the relevant time period, Basrai was the Managing Director and head of Investment Banking at LBMZ. Basrai was a registered representative licensed by FINRA and held Series 7, 24, 63, 86 and 87 licenses.

16. **Bryce Stirton**, age 29, currently resides in West Palm Beach, Florida. During the relevant time period, Stirton was an associate in the Investment Banking Division at LBMZ. Stirton was a registered representative licensed by FINRA and held Series 63 and 79 licenses.

OTHER RELEVANT ENTITIES

17. **LBMZ Securities, Inc. f/k/a Zacks & Company**, is an Illinois corporation with its principal place of business in Chicago, Illinois. LBMZ is a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act.

18. **Zacks Investment Research (“ZIR”)** is an Illinois corporation with its principal place of business in Chicago, Illinois.

19. **Zacks Small Cap Research** is a division of ZIR. Since its inception in 2009, SCR has provided small-cap issuers with “sponsored research,” in which covered issuers pay SCR an annual fee in exchange for the issuance of research reports.

FACTS

I. DEFENDANTS HAD DUTIES OF TRUST AND CONFIDENCE TO THEIR EMPLOYERS

20. As an employee of SCR, Napodano had duties of trust and confidence to SCR and was subject to SCR's insider trading policy, which expressly prohibited employees from trading while in possession of material nonpublic information. Napodano was also subject to an SCR policy that prohibited research analysts from trading in stocks they covered. In his capacity as an employee of SCR, Napodano regularly possessed sensitive and confidential information.

21. As employees of LBMZ, Basrai and Stirton had duties of trust and confidence to LBMZ and were subject to LBMZ's insider trading policy, which expressly prohibited employees from trading while in possession of material nonpublic information. In their capacity as employees of LBMZ, Basrai and Stirton regularly possessed sensitive and confidential information.

II. DEFENDANTS TRADED ON THE BASIS OF MATERIAL NONPUBLIC INFORMATION THEY LEARNED IN THE COURSE OF THEIR EMPLOYMENT

A. Company A

22. Company A is a small cap biotechnology company that retained SCR in February 2013 to provide sponsored research and LBMZ in June 2013 to act as its financial adviser. Each Defendant worked with Company A and owed a duty to his employer not to trade on material nonpublic information he learned in the course of his employment.

23. On January 10, 2014, Company A's CEO ("the CEO") told Defendants in an email that Company A had completed a licensing agreement for a Phase-2-ready drug and would be filing a Form 8-K announcing the news on January 13, 2014. The CEO provided Defendants with this information in the course of Company A's business relationships with both LBMZ and

SCR. Defendants knew, or were reckless in not knowing, that the information the CEO provided them was material and nonpublic.

24. After learning about the licensing agreement and upcoming announcement, each Defendant purchased Company A shares. Napodano purchased 505,000 shares between January 10, 2014 and January 13, 2014 for an average price of \$0.087/share. Basrai purchased 56,305 Company A shares on January 10, 2014 for an average price of \$0.085/share. And Stirton purchased 45,000 Company A shares on January 10, 2014 for \$0.083/share.

25. Defendants knew, or were reckless in not knowing, that they breached their fiduciary duties to their employers by trading on the information provided by the CEO.

26. On January 14, 2014, after delaying the announcement one day, Company A issued a press release and filed a Form 8-K announcing the licensing agreement. Company A's stock closed on January 14, 2014 at \$0.119/share. Company A's trading volume on January 14, 2014 was over seven times higher than its average trading volume for the prior year.

27. Each Defendant sold his Company A shares on January 14, 2014 after the announcement. Napodano sold his shares for an average price of \$0.099/share, making a profit of \$6,117.50. Basrai sold his shares for an average price of \$0.092/share, making a profit of \$413.09. And Stirton sold his shares for \$0.105/share, making a profit of \$990.00.

B. Company B

28. Company B, a medical technology company, signed a financial advisory agreement with LBMZ on August 5, 2014 to advise the company in connection with a possible merger with another company. Company B was placed on LBMZ's restricted list, which prohibited LBMZ's employees from trading in the stock. Basrai and Stirton worked on the transaction and owed duties to LBMZ not to trade on the basis of material, nonpublic information they learned through the course of their work.

29. Company B executed a merger agreement with the other company on October 21, 2014. The merger agreement provided that the merger could be terminated by either party if the transaction did not close by November 19, 2014.

30. The merger did not close by November 19, 2014, and both parties elected to terminate the agreement on that date. Basrai and Stirton knew that the merger had been terminated and conveyed this information to Napodano.

31. Basrai and Stirton received a personal benefit from tipping Napodano by increasing the likelihood that Napadano would likewise share material, nonpublic information about his clients in the future, which he, in fact, did. Defendants knew, or were reckless in not knowing, that the information shared with Napodano was material and nonpublic. Basrai and Stirton knew, or were reckless in not knowing, that Napodano would trade on the basis of that material, nonpublic information.

32. Before the termination of the merger agreement was publicly announced, Defendants sold short shares of Company B in a brokerage account opened in the name of Small Cap Advisors LLC (“SCA”), an entity Defendants and another SCR employee jointly formed in March 2014. Between November 20, 2014 and November 24, 2014, Defendants sold short 13,345 shares of Company B in SCA’s account at prices between \$1.05 and \$1.15/share.

33. At the time of these trades, Company B was one of only two companies on LBMZ’s restricted list.

34. Defendants knew, or were reckless in not knowing, that Basrai and Stirton breached their fiduciary duties to LBMZ both by trading on the information and by tipping Napodano.

35. On November 26, 2014 (the Wednesday before Thanksgiving), Company B announced the termination of the merger agreement by filing a Form 8-K after the market closed.

On December 1, 2014, the first full trading day after the announcement, Company B's stock price closed at \$0.87/share. Company B's trading volume on December 1, 2014 was over five times higher than its average trading volume for the prior year.

36. Defendants covered SCA's short position on December 1, 2014 by purchasing 13,345 Company B shares at prices between \$0.85 and \$0.86/share, making a profit of \$3,857.50. SCA profits were divided based on each member's initial investment in SCA, with Basrai and Napodano receiving 33.5% of any profits SCA generated, and Stirton and the other SCR employee receiving 16.5% of any profits generated.

C. Company C

37. Company C, a pharmaceutical company, was a client of SCR. Napodano personally covered Company C as an analyst and owed SCR duties of trust and confidence not to trade on material, nonpublic information he learned through the course of his work.

38. On August 18, 2014, Napodano received a call from Company C's Director of Investor Research ("the Director") in which he learned that Company C was going to announce the next day that it had been approved for listing on the NASDAQ Capital Market. The Director provided Napodano with this information in the course of Company C's business relationship with SCR.

39. After learning the news about Company C, Napodano called Basrai and Stirton and shared the news with them. Napodano received a personal benefit in exchange for tipping Basrai and Stirton by increasing the likelihood that they would likewise share material nonpublic information about their clients in the future, which they, in fact, did. Defendants knew, or were reckless in not knowing, that the information the Director provided to Napodano was material and nonpublic. Napodano knew, or was reckless in not knowing, that Basrai and Stirton would trade on the basis of that material, nonpublic information.

40. Each Defendant bought shares in Company C that same day. Napodano purchased 6,000 shares at \$3.95/share, Basrai purchased 15,000 shares at \$3.92/share, and Stirton purchased 3,000 shares at \$3.92/share.

41. Basrai and Stirton knew, or were reckless in not knowing, that Napodano breached the fiduciary duty he owed to SCR by tipping them.

42. On August 19, 2014, before the market opened, Company C issued a press release announcing that it had been approved for listing on the NASDAQ Capital Market and that it expected to begin trading on that exchange on August 21, 2015. Following the announcement, Company C traded as high as \$4.20/share on August 19, 2014, before closing at \$4.00. Company C's trading volume on August 19, 2014 was approximately 1.8 times higher than its average trading volume for the prior year.

43. After the announcement, Defendants sold their Company C shares. Stirton and Basrai sold a portion of their Company C shares on August 19, 2014, with Stirton selling 100 shares for \$4.15/share and Basrai selling 7,150 shares for \$4.00/share. While Stirton sold his remaining 2,900 shares on August 21, 2014 for \$4.00/share, Napodano and Basrai elected to hold their remaining shares for longer periods. Based on the actual profits Stirton and Basrai earned from their August 19, 2014 sales and the imputed profits earned from their retained shares based on the closing price on August 19, 2014, Napodano made a profit of \$300, Basrai made a profit of \$1,218.15, and Stirton made a profit of \$265.38.

III. NAPODANO AND BASRAI TRADED ON THE BASIS OF MATERIAL NONPUBLIC INFORMATION THEY LEARNED THROUGH A PERSONAL SOLICIATION OF BASRAI

44. On May 1, 2014, another investment banking firm contacted Basrai and asked if he was interested in personally participating in an upcoming public offering. Before learning any details about the proposed offering, Basrai affirmatively agreed to abide by the firm's

confidentiality and non-disclosure agreement, which prohibited Basrai from using or disclosing any confidential information about the company or transaction or trading based on such information. The investment banking firm then provided Basrai with details about the offering, which concerned Company D, a biotechnology company.

45. After learning the details about the offering, Basrai violated his duties of trust and confidence to the investment banking firm and informed Napodano of the impending Company D offering. Basrai provided the information to Napodano as a *quid pro quo* for material, nonpublic information Napodano had earlier provided to him. Basrai and Napodano knew, or were reckless in not knowing, that the information Basrai learned regarding the offering and provided to Napodano was material and nonpublic.

46. On that same day, May 1, 2014, Napodano shorted 5,000 Company D shares at \$2.17/share. On May 2, 2014, Basrai shorted 25,000 Company D shares at \$2.05/share, and on May 5, 2014, Basrai shorted an additional 15,000 shares at \$1.80/share.

47. Basrai knew, or was reckless in not knowing, that he breached his duties of trust and confidence when he traded on the basis of the material, nonpublic information he received from the investment banking firm and when he tipped Napodano. Basrai further knew, or was reckless in not knowing, that Napodano would trade on the basis of that material, nonpublic information.

48. Napodano knew, or was reckless in not knowing, that Basrai breached his duties of trust and confidence when Basrai provided Napodano with the material, nonpublic information. Napodano was an experienced analyst who covered many companies that used secondary public offerings to raise cash. He was familiar with the process by which investment banks require potential investors to agree to confidentiality before being brought “over the wall.” Despite this knowledge, Napodano traded on the information Basrai provided to him.

49. On May 6, 2014, Company D announced that it was selling 12,175,000 shares in an underwritten public offering at a price of \$1.15 per share. Company D's stock price closed at \$1.15 on May 6, 2014, and its trading volume was over 13 times higher than its average trading volume for the prior year.

50. After the announcement, Napodano and Basrai purchased Company D shares in the market to cover their short positions. Napodano bought 5,000 shares at \$1.09/share for a profit of \$5,400 and Basrai bought 40,000 shares at \$1.14/share for a profit of \$32,532.

IV. DEFENDANTS TRADED IN ADVANCE OF THE PUBLICATION OF SCR-ISSUED RESEARCH REPORTS

A. Napodano Traded in Advance of the Publication of 42 SCR-Issued Research Reports

51. Between August 2012 and June 2015, Napodano traded profitably in advance of the publication of 42 SCR reports. Although he and his subordinates authored the reports, they were property of SCR and were nonpublic until the reports were published. In addition, information regarding the timing of the reports' publication was also material and nonpublic. Napodano owed a fiduciary duty to SCR to maintain the confidentiality of his reports until they were published and not to trade on the basis of material, nonpublic information the reports contained and about the timing of their release.

52. Napodano knew, or was reckless in not knowing, that his reports were material and nonpublic. Napodano executed these trades based on his knowledge that SCR reports often caused the issuers' stock prices to increase. Napodano was a well-regarded and much-followed research analyst in the small-cap biotechnology sub-sector, and frequently cited the market impact of his and his subordinates' reports as a selling point when soliciting potential new SCR clients.

53. Napodano knew, or was reckless in not knowing, that he breached his duty to SCR when he traded in advance of the publication of SCR-issued reports. Napodano knowingly or recklessly violated SCR's policies against insider trading and against trading in stocks covered by SCR research analysts.

54. Napodano made profits of \$64,984.69 by trading in advance of the publication of SCR reports.

B. Basrai and Stirton Traded in Advance of the Publication of a SCR-Issued Report

55. On July 7, 2014, an SCR Analyst ("the SCR Analyst") who reported to Napodano told Basrai and Stirton that his first report on a clinical laboratory company ("Company E") would be coming out the next day. The SCR Analyst provided Basrai and Stirton with this information because of SCR's business relationship with LBMZ's investment banking division. Basrai and Stirton owed duties to LBMZ not to trade on information they learned through their work involving Company E, and knew, or were reckless in not knowing, that the information the SCR Analyst provided them was material and nonpublic.

56. On July 7, 2014, Basrai purchased 25,000 shares of Company E at \$2.23/share and Stirton purchased 2,500 shares at \$2.27/share. Basrai and Stirton knew, or were reckless in not knowing, that they breached their fiduciary duties to LBMZ by trading on the information provided by the SCR Analyst.

57. The next day, SCR published the report. The report initiated coverage on Company E, which was covered by only one other research analyst, rated the company an "outperform," and included a price target of \$3.50/share at a time when the stock was trading around \$2.27/share. The stock closed at \$2.52 on July 8, 2014, and its average trading volume was 1.6 times higher compared to its average trading volume for the prior year.

58. On July 9, 2014 Basrai and Stirton each sold their Company E shares at \$2.40/share, making Basrai a profit of \$4,212.87 and Stirton a profit of \$327.00.

V. NAPODANO MADE MATERIAL MISREPRESENTATIONS OR OMISSIONS IN HIS SCR REPORTS AND FINANCIAL WEBSITE ARTICLES

59. Between August 2012 and June 2015, Napodano traded profitably in advance of the publication of 100 SCR reports and financial website articles he authored. Each of these reports and articles contained one or more material misrepresentations or omissions.

60. In each of his financial website articles, Napodano represented that he had “no position in any stocks mentioned, and no plans to initiate any positions within the next 72 hours.”

61. Through mid-April 2014, Napodano’s SCR reports contained a disclaimer that “Zacks SCR analysts are restricted from holding or trading securities in the issuers which they cover.”

62. After mid-April 2014, Napodano’s SCR reports stated that “Zacks SCR Analysts are restricted from holding or trading securities placed on the ZIR, SCR, or [LBMZ] restricted list, which may include issuers in the Small-Cap Universe.” While LBMZ maintained a restricted list, neither SCR nor ZIR (SCR’s parent company) maintained a restricted list of securities that analysts were prohibited from holding or trading.

63. Each time Napodano traded just prior to the publication of one of his financial website articles or pre-April 2014 SCR reports, the representation in the report or article that he did not trade stock or hold a position in the covered company was false.

64. Each time that Napodano traded in advance of the post-April 2014 SCR reports, the representation in the report that he was restricted from holding or trading securities on a restricted list that may include all of the SCR companies was misleading.

65. Napodano knew that each of these disclosures regarding his trading and holding of securities was false or misleading, but he nevertheless made them or failed to correct them to ensure that his trading, which violated SCR policy, would not be discovered by anyone at SCR.

66. When recommending stocks to others, Napodano assumed a duty to disclose that he owned the stock and his intent to sell the stock shortly after publication of his reports and articles. Napodano breached this duty when he published SCR reports and financial website articles that recommended stocks without disclosing that he owned the stock and intended to sell shortly after publication.

67. The articles Napodano published on the financial website also contained a disclaimer that he had “no business relationship with any company whose stock is mentioned” in the article. This representation was false or misleading because Napodano and his employer, SCR, had contractual arrangements with each of the covered companies through which SCR provided sponsored research about the companies. Between August 2012 and June 2015, Napodano knowingly published at least 60 financial website articles that contained this misrepresentation.

68. Each of these misrepresentations and omissions impacted the objectivity of Napodano’s investment advice and were important to an investor’s decision whether to purchase or sell the company’s stock based on his recommendation.

69. Napodano made profits of \$130,755.72 by trading around his financial website articles and SCR reports.¹

¹ This amount includes the profits Napodano made from trading in advance of the publication of SCR reports, as stated in paragraph 54, *infra*.

FIRST CLAIM FOR RELIEF

**Violations of Section 10(b) of the Exchange Act and Rule 10b-5 Thereunder
(Against Defendants Napodano, Basrai and Stirton)**

70. The Commission realleges and incorporates by reference paragraphs 1 through 69 of this Complaint.

71. In connection with the purchase and sale of securities described herein, Defendants, by the use of the means and instrumentalities of interstate commerce and by the use of mails, directly and indirectly:

- a) employed devices, schemes, and artifices to defraud;
- b) made untrue statements of material facts and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and
- c) engaged in acts, practices, and courses of business which would and did operate as a fraud and deceit upon the purchases of such securities, all as more particularly described above.

72. Defendants knowingly, intentionally, and/or recklessly engaged in the aforementioned devices, schemes and artifices to defraud, and engaged in fraudulent acts, practices and courses of business.

73. By reason of the foregoing, Defendants directly and indirectly, have violated and, unless enjoined, will continue to violate Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. 240.10b-5].

PRAYER FOR RELIEF

WHEREFORE, the Commission respectfully prays that the Court enter the Proposed Final Judgments against Defendants Napodano, Basrai and Stirton:

I.

Permanently enjoining Defendants and their officers, agents, servants, employees, attorneys, and all persons in active concert or participation with them who receive actual notice of the order by personal service or otherwise, from violating Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)], and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

II.

Ordering Defendants to disgorge all ill-gotten gains received as a result of the conduct alleged in this Complaint, with prejudgment interest.

III.

Ordering Defendants to pay civil penalties under Section 21(d)(3) and Section 21A of the Exchange Act [15 U.S.C. § 78u(d)(3) and § 78u-1].

IV.

Pursuant to Section 21(d)(6) of the Exchange Act [15 U.S.C. § 78u(d)(6)], permanently barring Napodano and Basrai, and barring Stirton for five years, from participating in an offering of penny stock, including engaging in activities with a broker, dealer, or issuer for purposes of issuing, trading, or inducing or attempting to induce the purchase or sale of any penny stock.

V.

Grant such other and further relief as this Court may determine to be just and necessary.

Dated: September 26, 2017

Respectfully submitted,

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