

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934  
Rel. No.49666 / May 7, 2004

Admin. Proc. File No. 3-11329

In the Matter of the Application of  
CITADEL SECURITIES CORP.  
45 Church Street  
Freeport, New York 11520  
For Review of Action Taken by  
NASD

OPINION OF THE COMMISSION

REGISTERED SECURITIES ASSOCIATION - REVIEW OF DENIAL OF  
MEMBER'S CONTINUANCE APPLICATION

Registered securities association denied member firm's application to retain its membership if it employed an individual who is subject to statutory disqualification because a permanent injunction was entered against individual for violation of the securities laws. Held, appeal proceeding dismissed.

APPEARANCES:

Shakespeare Newsome, for Citadel Securities Corp.

Marc Menchel, Alan Lawhead, and Leavy Mathews III, for NASD.

Appeal filed: November 14, 2003  
Last brief received: February 18, 2004

I.

Citadel Securities Corp. ("Citadel"), an NASD member firm, appeals from the denial by NASD of Citadel's application to remain an NASD member if Michael T. Studer is associated with Citadel. Studer is subject to a statutory disqualification because he was enjoined from violation of the antifraud and securities registration provisions of the securities laws by a

federal district court. 1/ We base our findings on an independent review of the record.

## II.

At the time of the hearing before NASD, Studer was president, treasurer, and limited principal - financial and operations ("FINOP") of Citadel. Citadel is wholly-owned by Castle Holding Company ("CHC"). Studer and certain trusts of which Studer is trustee own between 25% and 35% of the shares of CHC.

In 1994 the Commission brought a civil action alleging violations by Castle Securities Corp. ("Castle") (a former NASD member firm) 2/ and Studer with respect to the public offering of Windfall Capital Corp. shares in 1989 and the subsequent trading of shares of U.S. Environmental, Inc. (which had merged with Windfall). On July 21, 2003, following a bench trial, the United States District Court for the Southern District of New York found that Castle and Studer had engaged in an unregistered and fraudulent blind pool offering and in a subsequent market manipulation. 3/ Concluding that these violations were "egregious and repeated," that Studer "played an intimate role in the fraudulent transactions," and that there was a reasonable likelihood that the respondents would "continue to engage in conduct violative of the federal securities laws," the court enjoined Castle and Studer from violating Sections 5(a), 5(c), and 17(a) of the Securities Act of 1933, Sections 10(b) and 15(c)(1) of the Securities Exchange Act of 1934, Exchange Act Rules 10b-3, 10b-5, and 15c1-2, and Rule 101 of Regulation M. 4/ They were also ordered, jointly and severally, to disgorge

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<sup>1</sup> See note 4 and accompanying text.

<sup>2</sup> CHC also wholly owned Castle. Castle and Citadel shared the same address. In October 2003, Castle filed a Form BDW, withdrawing its registration as a broker-dealer.

<sup>3</sup> SEC v. U.S. Environmental, Inc., et al., 2003 U.S. Dist. Lexis 12580, \*1, Fed. Sec. L. Rep. (CCH) P 92,471 (S.D.N.Y. July 21, 2003).

<sup>4</sup> 15 U.S.C. Sections 77e(a), 77e(c), 77q(a), 78j(b), 78o(c)(1); 17 C.F.R. Sections 240.10b-3, 10b-5; 240.15c1-2; 242.101. 2003 U.S. Dist. LEXIS at \*70, \*72,\*74, and \*84-\*90.

\$134,224 plus prejudgment interest. <sup>5/</sup> As a result of the court's order, Studer was statutorily disqualified from association with an NASD member. <sup>6/</sup>

On August 6, 2003, Citadel filed a Membership Continuance Application with NASD ("Application") seeking approval to remain a member if it continued to employ Studer. <sup>7/</sup> The Application sought to continue Studer's association as Citadel's general securities principal, general securities representative, municipal securities principal, municipal securities representative, and FINOP. The Application stated that Shakespeare Newsome, who had been Citadel's Director of Compliance since 1998, would supervise Studer.

At the hearing, Studer, then Citadel's president, testified on behalf of Citadel. He stated that Citadel had no customers, and had stopped making markets in November 2002. Studer also stated that Citadel had limited its activities to selling its remaining proprietary securities positions, that Newsome would replace Studer as president and sole director of Citadel, and that Newsome would supervise Studer. Studer noted further that Newsome had no prior disciplinary history and no customer complaints.

Studer explained that, in his role as Citadel's FINOP, he prepared accounting reports and made required filings. Studer and Newsome admitted that Newsome would have difficulty supervising Studer's accounting activities because Newsome did not have a FINOP registration and had little experience or training in financial matters. Therefore, during the hearing, Studer suggested that he be supervised by Robert Neal, a certified public accountant who held a FINOP registration and who had worked for both Castle and Citadel, under Studer's supervision, for a number of years. Studer stated that Neal had

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<sup>5</sup> 2003 U.S. Dist. LEXIS 12580 at \*90.

<sup>6</sup> Exchange Act Section 3(a)(39)(D), 15 U.S.C. Section 78c(a)(39)(D).

<sup>7</sup> Castle also filed an application seeking to remain a member in spite of its statutory disqualification and a second application seeking to continue to be a member if Studer remained associated with Castle. NASD denied both applications. Neither Castle nor Studer applied for review of these determinations.

prepared numerous FOCUS reports for Citadel and could review all of Studer's work that Newsome was not qualified to review. 8/

In addition to the testimony about Citadel's activities and supervisory plans, the Hearing Panel reviewed Studer's disciplinary history. Among other things, the panel found that both NASD and the State of Georgia had disciplined Studer. 9/

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<sup>8</sup> According to Studer, Neal also had worked for Studer's private accounting practice. Neal did not appear at the hearing.

<sup>9</sup> On October 21, 1996, NASD found that Castle and Studer had failed to establish, implement, and enforce reasonable supervisory procedures to prevent a fraudulent manipulation and markup scheme. NASD further found that Castle had manipulated the market in the common stock of a NASDAQ-listed company and charged excessive and fraudulent markups. Studer was censured, fined \$25,000, jointly and severally with Castle, and, also jointly and severally with Castle, required to make restitution to customers in the amount of \$13,686.05 plus interest, and to pay costs in the amount of \$1,750. Studer also was suspended in all capacities for 30 days and required to re-qualify by examination as a general securities principal. We sustained the NASD action. Castle Securities Corporation, 53 S.E.C. 406 (1998). The activity on which this NASD proceeding was based occurred during the period that our staff was investigating Studer's conduct in connection with Windfall and U.S. Environmental, Inc.

On December 10, 1991, the Commissioner of Securities for the State of Georgia issued an order finding that Castle and Studer had sold unregistered securities. The Commissioner

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## III.

Section 19(f) of the Exchange Act provides the standards that govern our review of this appeal. If we find that (1) "the specific grounds" on which NASD based its action "exist in fact," (2) NASD's prohibition of Studer's association is in accordance with its rules, and (3) such rules were applied in a manner consistent with the purposes of the Exchange Act, we must dismiss Citadel's appeal unless we find that NASD's action imposes an undue burden on competition. 10/

Studer is subject to statutory disqualification by virtue of the injunction entered against him by the federal district court. Under Article III, Section 3 of NASD's By-laws, NASD may bar a person from becoming associated with or continuing in association with a member if such person is subject to a "statutory disqualification."

Studer has appealed the injunction order and sought a new trial, and those matters are still pending. 11/ Citadel argues

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<sup>9</sup>(...continued)

ordered Studer to cease and desist, fined Studer \$10,000, and barred Studer from

association with a registered dealer, a limited dealer, or an investment advisor until the

fine was paid. See note 24, infra.

<sup>10</sup> 15 U.S.C. Section 78s(f).

<sup>11</sup> Citadel challenges the district court's findings (on which the Hearing Panel relied) that Castle and Studer failed to disclose material facts in connection with the initial public offering of Windfall Financial Corp. Challenges to the district court's findings are not appropriately addressed to the Commission. Demetrius Julius Shiva, 52 S.E.C. 1247, 1249 (1997) (appropriate forum to challenge district court findings resulting in a statutory disqualification is court of appeals).

Citadel also argues that the Hearing Panel, by concluding that Studer was "essential" to

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that, as a result, the finding that Studer is statutorily disqualified is premature. As we have stated previously, an injunction is the action of a court of competent jurisdiction, and the fact that an appeal is taken does not affect the injunction's status as a statutory disqualification. 12/ If the appeal is successful, Citadel could apply for modification of this action. 13/

Citadel notes that, although the injunction was entered in July 2003, the conduct underlying the proceeding took place in 1989 and 1990. Citadel argues that to weigh Studer's fitness based on conduct from 1989 and 1990 is "Orwellian." Although the conduct on which the injunction was based is old, Studer elected to contest the proceeding, which was his right. Citadel cannot thereafter complain of the delay from the resulting

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<sup>11</sup>(...continued)

the market manipulation scheme, misconstrued the district court's findings. We find no error. The Hearing Panel relied on the following quotation from the district court's opinion: "the success of this scheme was dependent upon the trading services of Castle, under the supervision of Studer." See SEC v. U.S. Environmental, Inc., 2003 U.S. Dist. Lexis 12580 at \*65.

<sup>12</sup> Charles Phillip Elliot, 50 S.E.C. 1273, 1277 n.17 (1992) (finding statutory disqualification based on conviction which had been appealed), aff'd 36 F.3d 86 (11th Cir. 1994) (per curiam), citing C.R. Richmond & Co., 46 S.E.C. 412, 414 n.11 (1976) (upholding statutory disqualification based on injunction under appeal). See also Robert J. Sayegh, 52 S.E.C. 1110, 1112 (1996) (upholding disqualification based on injunction during pendency of petition for rehearing, stating that existence of petition "would not alter the 'factual' existence of the injunction 'and its public interest importance.'").

<sup>13</sup> Charles Phillip Elliot, 50 S.E.C. at 1277 n.17.

litigation. 14/

We also find that NASD complied with its rules. 15/ Citadel complains that, contrary to NASD rules, it was denied its right to counsel at the hearing. After neither Studer nor counsel appeared for the initial hearing in this matter, the Hearing Panel determined to postpone the hearing to permit Citadel to retain counsel and allow counsel time to prepare. The Hearing Panel subsequently agreed with Studer and Citadel's attorney to hold the hearing on September 30, 2003. The evening before that hearing (after business hours), Citadel's attorney transmitted by facsimile a request for another postponement. On September 30, Studer appeared without counsel. Studer, who was then Citadel's president, elected to go forward with the proceeding without counsel. At the conclusion of the hearing, the Hearing Panel ordered the record held open for over a week to allow Studer and Citadel's attorney to provide further information if they wished to do so. Nothing was forthcoming.

While NASD Code of Procedure Rule 9524(a)(4) permits a respondent to retain counsel, it neither affords a right to attorney representation nor requires that previously scheduled hearings be postponed to allow respondents time to retain counsel. We previously have found that "[t]here is no constitutional or statutory right to representation of counsel in administrative proceedings," such as NASD proceedings. 16/ We find that NASD followed NASD's By-Laws and the Code of Procedure in processing this matter, and that NASD accorded Citadel proper notice and a hearing pursuant to Article III, Section 3 of NASD By-laws.

We also find that NASD applied its rules in a manner consistent with the purposes of the Exchange Act and with the public interest in ensuring the integrity of the securities

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<sup>14</sup> See Rosario R. Ruggiero, 52 S.E.C. 725, 727 (1996). During the pendency of the civil injunctive action, Studer was not subject to any statutory disqualification.

<sup>15</sup> See NASD Code of Procedure Rules 9521 - 9527.

<sup>16</sup> See Mark H. Love, Exchange Act Rel. No. 49248 (Feb. 13, 2004), \_\_ SEC Docket \_\_, citing SEC v. Jerry T. O'Brien, Inc., 467 U.S. 735, 742 (1984); see also Sundra Escott-Russell, Exchange Act Rel. No. 43363 (Sept. 27, 2000), 73 SEC Docket 1265, 1270, and Sheen Fin. Res., Inc., 52 S.E.C. 185, 192 (1995).

industry. <sup>17/</sup> We have consistently held that, in order to ensure the protection of investors, NASD may demand a high level of integrity from securities professionals. <sup>18/</sup> NASD expressed concern about Studer's lengthy disciplinary history. Citadel claims that Studer has never had a customer complaint directed against him and that all past allegations against him involve an alleged "failure to supervise." Even accepting Studer's argument that these prior violations were supervisory, we agree with NASD that they were serious and relevant to his fitness to associate with a member firm. In 1998, we sustained NASD's finding that Studer failed to supervise employees in connection with another market manipulation scheme. <sup>19/</sup> Studer's statutory disqualification arises from his participation in a fraudulent market manipulation scheme. We find that NASD properly considered Studer's prior disciplinary history.

We agree with NASD that Citadel failed to propose an effective plan to supervise Studer. We have stated previously that, "[i]n determining whether to permit the employment of a statutorily disqualified person, the quality of the supervision to be accorded that person is of utmost importance. We have made it clear that such persons must be subject to stringent oversight by

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<sup>17</sup> See, e.g., United States v. O'Hagan, 521 U.S. 642, 658 (1997)(stating that one of the primary objectives of Congress in passing the Exchange Act was "to insure honest securities markets and thereby promote investor confidence."). See also Morton Kantrowitz, 52 S.E.C. 721, 724 n.11 (1996); and Halpert and Company, Inc., 50 S.E.C. 420, 422 (1990) ("Particularly in matters involving a firm's employment of persons subject to a statutory disqualification, it is appropriate to recognize the NASD's evaluation of appropriate business standards for its members").

<sup>18</sup> See, e.g., William J. Haberman, 53 S.E.C. 1024, 1029 (1998) (holding that to protect investors and maintain investor confidence in the markets, securities professionals are obliged to maintain high ethical standards), aff'd, 205 F.3d 1345 (8th Cir. 2000) (Table).

<sup>19</sup> See note 9, supra.

supervisors who are fully qualified to implement the necessary controls." 20/

Citadel proposes to employ Studer as its FINOP. That role is of critical importance and would place him in a position of power and influence over Citadel's activities. Newsome, who would be assigned general responsibility to supervise Studer, admitted that he did not have a Series 27 registration, and had no training in accounting. Accordingly, he would not be appropriately equipped to supervise Studer's activities. Citadel therefore proposed that Neal supervise Studer in these areas. However, Neal did not appear before NASD to explain how he would supervise Studer, or to describe his experience. In a letter dated November 28, 2003, Newsome informed us that Neal was resigning from Citadel and, therefore, would not supervise Studer. Citadel again proposes that Newsome supervise Studer.

We have previously noted it to be difficult for employees to supervise effectively the activities of the owner of a firm. 21/ Newsome's supervision of Studer would face the obstacle of Studer's controlling ownership interest in CHC, which wholly owns Citadel, and Newsome's admitted lack of experience with financial matters. Furthermore, neither Studer nor Newsome identified any proposed special supervisory efforts or plans that Newsome would undertake. 22/

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<sup>20</sup> Morton Kantrowitz, Exchange Act Rel. No. 44239 (May 1, 2001), 74 SEC Docket 2406, 2409; William J. Haberman, 53 S.E.C. at 1032 n.24 ("As necessary or appropriate in furtherance of the purposes of the Exchange Act, we may require stringent supervision of any statutorily disqualified individual, regardless of the size or structure of the supervising firm, whether or not such a requirement places a burden on competition.").

<sup>21</sup> See, e.g., Kirk A. Knapp, 51 S.E.C. 115, 128-29 (1992) (owner of over 90% of firm barred from acting as general securities principal still exercised control and fired new president of firm when president disagreed with owner).

<sup>22</sup> Citadel argues for the first time in its Reply Brief that NASD's action imposes an undue burden on competition because Studer, as a certified public accountant, is

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Citadel now seeks to have Studer continue to be associated with Citadel in "at least a clerical capacity," although it did not make this request to the Hearing Panel. Citadel does not explain the proposed duties encompassed in Studer's "clerical capacity." Under Exchange Act Section 19(f), we consider only the record presented to NASD. In any event, NASD Sanctions Rule Interpretation IM-8310-1 clearly states that a member shall not allow a barred individual to remain associated with it "in any capacity, including a clerical or ministerial capacity." 23/

In light of the foregoing, we have determined to dismiss this review proceeding. 24/

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<sup>22</sup>(...continued)

needed to prepare and file Forms 211. We find Citadel's argument unconvincing.

Forms 211 are filed by a firm seeking to make a market in a security. Citadel has represented that it has not made markets since November 2002, and has no plan to do so in the future.

<sup>23</sup> NASD Manual, Investigations and Sanctions Rules, IM-8310-1.

<sup>24</sup> The Hearing Panel considered a number of disciplinary actions involving Studer which we did not consider in rendering this opinion.

NASD cited a September 4, 1990 NASD District Business Conduct Committee for

District 12 Decision and Order of Acceptance of Respondent's Offer of Settlement.

However, Studer and Castle agreed to the settlement for purposes of that proceeding only.

Therefore, we have not considered it. See Howard R. Perles, Exchange Act Rel. No.

45691 (April 4, 2002), 77 SEC Docket 896 (in reviewing disciplinary history,

Commission will not consider offer of settlement which stated that it may not be used in another proceeding).

(continued...)

An appropriate order will issue. 25/

By the Commission (Chairman DONALDSON and Commissioners  
GLASSMAN, GOLDSCHMID, ATKINS and CAMPOS)

Jonathan G. Katz  
Secretary

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<sup>24</sup>(...continued)

On March 4, 2004, Studer appealed to us an NASD disciplinary action against him. That matter is now pending, and we have not considered it in our resolution of this matter.

<sup>25</sup> 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 herein.

UNITED STATES OF AMERICA  
before the  
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934  
Rel. No.49666 / May 7, 2004

Admin. Proc. File No. 3-11329

In the Matter of the Application of

CITADEL SECURITIES CORP.  
45 Church Street  
Freeport, New York 11520

For Review of Action Taken by  
NASD

ORDER DISMISSING APPEAL OF DENIAL OF MEMBER'S CONTINUANCE  
APPLICATION BY REGISTERED SECURITIES ASSOCIATION

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

ORDERED that the appeal taken by Citadel Securities Corp.  
from the denial by NASD of Citadel's application to continue as a  
member if it employs Michael T. Studer in any capacity be, and it  
hereby is, dismissed.

By the Commission.

Jonathan G. Katz  
Secretary