

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934  
Rel. No. 51633 / April 29, 2005

Admin. Proc. File No. 3-10391r

---

In the Matter of the Application of

NICHOLAS T. AVELLO  
4N080 Verrill Avenue  
Addison, Illinois 60101

For Review of Disciplinary Action Taken by

NASD

---

OPINION OF THE COMMISSION

REGISTERED SECURITIES ASSOCIATION - REVIEW OF DISCIPLINARY  
PROCEEDINGS

Sanctions For Recordkeeping Violations

On remand to registered securities association for clarification of its calculation of net capital issues, association found that former associated person of former association member was not responsible for allowing former member to operate a securities business without adequate net capital but was responsible for recordkeeping violations and reduced sanctions, imposing letter of caution in lieu of fine. Held, association's findings and sanctions sustained.

APPEARANCES:

Nicholas T. Avello, pro se.

Marc Menchel, Alan Lawhead, and Gary J. Dernelle, for NASD Regulation, Inc.

Appeal filed: September 17, 2004  
Last brief received: January 4, 2005

## I.

Nicholas T. Avello, formerly limited principal -- financial and operations ("FINOP") for Hudson Knight Securities, Inc. ("HKS"), a former NASD member, appeals from NASD disciplinary action. Avello appeals from NASD's August 11, 2004 decision ("NASD 2004 Decision") imposing sanctions pursuant to our remand order of December 3, 2003. The NASD 2004 Decision vacated NASD's determination in its earlier decision of November 6, 2000 ("NASD 2000 Decision") that Avello was liable for a net capital violation by HKS on June 28, 1996, vacated the \$5,000 fine and \$665.80 in costs it had imposed in the NASD 2000 Decision and determined that the NASD 2004 Decision should serve as a letter of caution with respect to the findings of recordkeeping and reporting violations in the NASD 2000 Decision, which we sustained in our opinion of November 7, 2002 ("Commission 2002 Opinion"). <sup>1/</sup> We base our findings on an independent review of the record.

## II.

In the Commission 2002 Opinion, we sustained NASD's findings that Avello was liable for HKS's net capital violation on June 28, 1996 and also for various violations of recordkeeping and reporting rules. Specifically, the Commission 2002 Opinion sustained NASD's findings that Avello violated Exchange Act Rule 17a-3 and NASD Conduct Rule 3110 by failing to maintain accurate financial records and making inaccurate reports to NASD. <sup>2/</sup> That Opinion also sustained NASD's findings that Avello violated Exchange Act Rule 17a-5 and NASD Conduct Rule 2110 by filing six inaccurate quarterly FOCUS reports on behalf of HKS between 1995 and 1997. <sup>3/</sup> As found by the Commission 2002 Opinion, Avello's handling of corporate credit-card debt, payment-for-order-flow receivables, a sole-recourse loan, a furniture-and-equipment lease, and other HKS assets and liabilities caused the violations of NASD and Commission rules.

Avello appealed the Commission 2002 Opinion to the United States Court of Appeals for the Seventh Circuit, where briefing identified an issue regarding the calculation of HKS's net capital position on June 28, 1996, the sole date for which Avello had been held liable for a net capital violation. On August 20, 2003, the Seventh Circuit granted our request to remand the entire case to our jurisdiction. On December 3, 2003, we issued a partial remand to NASD for the limited purposes of clarifying Avello's liability for any HKS net capital violation on June 28, 1996 and modifying the sanctions initially imposed on Avello if warranted by such clarification.

---

<sup>1/</sup> Nicholas T. Avello, Securities Exchange Act Rel. No. 46780 (Nov. 7, 2002), 78 SEC Docket 2859.

<sup>2/</sup> 17 C.F.R. § 240.17a-3. NASD found that Avello submitted inaccurate financial reports to NASD for the following periods: November and December 1995; January through March, and May through September 1996; and January through August 1997.

<sup>3/</sup> 17 C.F.R. § 240.17a-5.

The NASD 2004 Decision found that Avello was not liable for the HKS net capital violation on June 28, 1996. The NASD 2000 Decision had held Avello liable for the HKS net capital violation on that date even though the deficiency calculation for the firm's liability included a \$47,000 liability which the NASD 2000 Decision expressly absolved Avello of responsibility for recording. The NASD 2004 Decision concluded that, absent this liability, the firm would not have had a net capital deficiency and therefore Avello could not be held liable for the firm's deficiency on that date. Accordingly, NASD reversed its previous finding that Avello was responsible for the Firm's operating on June 28, 1996 below its minimum net capital requirement.

In reconsidering the sanctions it had imposed, the NASD 2004 Decision determined that, in light of the dismissal of the net capital violation, the \$5,000 fine and \$665.80 in costs it had imposed in the NASD 2000 Decision were no longer appropriate. However, NASD determined it was necessary to impose some sanction for the violations for which Avello was responsible. The NASD 2000 Decision had found that Avello was responsible for books and records and reporting violations that occurred over nineteen months, a prolonged period of violation. The NASD 2000 Decision also found that Avello had continued to file FOCUS reports even though he knew that he was not receiving accurate financial information from the Firm's accountant in 1997. NASD considered that Avello, as the FINOP for HKS, was responsible for keeping accurate books and records and for filing accurate FOCUS reports. The NASD 2004 Decision determined that a letter of caution was an appropriate sanction and stated that the NASD 2004 Decision would serve as the letter of caution.

### III.

We agree with NASD that some sanction is appropriate in this case. <sup>4/</sup> As we noted in the Commission 2002 Opinion, Avello continued to file FOCUS reports even though he knew the information he received from the Firm's accountant was not accurate. We find that the NASD 2004 Decision has appropriately balanced the need to sanction a FINOP for engaging in specific books and records and reporting violations under these circumstances with the fact that, more generally speaking, Avello made good faith efforts to report accurately, to keep HKS in net capital compliance, and to keep the Firm from doing business when its net capital computation was in question. We find that the imposition of a letter of caution as the sole sanction for Avello's violations is neither excessive nor oppressive and, accordingly, we sustain NASD's sanction.

---

<sup>4/</sup> We have jurisdiction over NASD disciplinary actions, such as this one, in which a letter of caution is the only sanction imposed as a result of a disciplinary proceeding. Martin Lee Eng, Exchange Act Rel. No. 42962 (June 20, 2000), 72 SEC Docket 2078.

## IV.

The other findings of the Commission 2002 Opinion were not remanded to NASD, are not now before the Commission, and remain undisturbed by NASD's dismissal of the net capital charge. However, despite the limited scope of the remand to NASD and the limited scope of the NASD 2004 Decision, Avello's brief in this appeal restates in detail his objections to the findings of the Commission 2002 Opinion regarding his recordkeeping and reporting violations. The Commission 2002 Opinion constitutes the Commission's decision on Avello's responsibility for the recordkeeping and reporting violations, and we reaffirm the findings in that decision here. Avello waived his right to seek reconsideration of these matters when he chose not to file a timely motion for reconsideration pursuant to Rule 470 of our Rules of Practice. <sup>5/</sup> Consequently, Avello's objections to the findings that he violated recordkeeping and reporting rules -- which the Commission has heard and rejected in the Commission 2002 Opinion -- will not be heard now. <sup>6/</sup>

In this appeal, Avello raises four new arguments in his defense that he did not raise in his initial appeal. Avello has waived his right to raise any new issues not raised in the initial appeal. <sup>7/</sup> Moreover, none of the newly-raised arguments would provide any basis for modifying the findings of the Commission 2002 Opinion regarding Avello's books and records violations. Avello argues that NASD lacks the authority to require broker-dealers to file a FOCUS report on a monthly, rather than quarterly, basis. Without reaching the merits of Avello's argument, we note that NASD's allegations did not concern any monthly filings by HKS, but only its quarterly filings, and that Avello's argument is therefore not relevant to our findings. Similarly, Avello argues that NASD lacked authority to impose a restrictive agreement on HKS requiring HKS to maintain a higher minimum net capital requirement than that required by applicable regulations. Because all of NASD's net capital allegations referred to HKS's failure to meet the net capital minimum set by regulation, not by the restrictive agreement, and because there are no net capital issues outstanding in this case, we do not reach Avello's argument. Avello argues also that there is a requirement that NASD find there was bad faith before finding liability under NASD Conduct Rule 2110. When a violation of Conduct Rule 2110 is not based on the violation of some other rule, we have required a showing that the respondent has acted in bad faith before

---

<sup>5/</sup> 17 C.F.R. § 201.470.

<sup>6/</sup> The theories under which Avello now claims he should be exonerated do not depend on newly discovered evidence or an intervening change in the governing law and are not, therefore, within an exception to the law of the case doctrine. Compare Key v. Sullivan, 925 F.2d 1056, 1060 (7th Cir. 1991) (exceptions to law of the case doctrine).

<sup>7/</sup> Northwestern Indiana Tel. Co. v. FCC, 872 F.2d 465, 470 (D.C. Cir. 1989) ("where an argument could have been raised on an initial appeal, it is inappropriate to consider that argument in a second appeal . . .").

liability can be found. 8/ There is no bad faith requirement, however, when, as here, a violation of Conduct Rule 2110 is based upon the violation of a Commission rule. 9/ Finally, Avello argues that he cannot be held to have violated NASD Membership and Registration Rule 1022(b) because he was not charged with any such violation. Rule 1022(b), which defines the duties and responsibilities of FINOPs, was cited in the NASD 2000 Decision and the Commission 2002 Opinion because it describes the duties of a FINOP as encompassing the responsibility to ensure compliance with the rules allegedly violated.

Accordingly, we find that the sanctions imposed on Avello by NASD in the NASD 2004 Decision are neither excessive nor oppressive, and we sustain them. An appropriate order will issue. 10/

By the Commission (Chairman DONALDSON, Commissioners GLASSMAN, GOLDSCHMID, and ATKINS); Commissioner CAMPOS not participating.

Jonathan G. Katz  
Secretary

---

8/ Robert J. Jautz, 48 S.E.C. 702, 703 - 04 (1987) (if obligation to "observe high standards of commercial honor and just and equitable principles of trade" is only violation alleged, there must be a finding of bad faith).

9/ See L.H. Alton & Co., 53 S.E.C. 1118, 1122 (1999) (violations of SEC rules are violations of NASD Conduct Rule 2110).

10/ We have considered all of the arguments advanced by the parties. We have rejected or sustained them to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA  
before the  
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934  
Rel. No. 51633 / April 29, 2005

Admin. Proc. File No. 3-10391r

---

In the Matter of the Application of

NICHOLAS T. AVELLO  
4N080 Verrill Avenue  
Addison, Illinois 60101

For Review of Disciplinary Action Taken by

NASD

---

ORDER SUSTAINING DISCIPLINARY ACTION TAKEN BY REGISTERED SECURITIES  
ASSOCIATION

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

ORDERED that the disciplinary action taken by NASD against Nicholas T. Avello be,  
and it hereby is, sustained.

By the Commission.

Jonathan G. Katz  
Secretary