

**Disciplinary Panel
American Stock Exchange LLC**

IN THE MATTER
OF
CHAD MATTHEW

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:
: Case No. 05-210
: AMXC06023

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: Hearing Officer – RSH

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: **DISCIPLINARY PANEL DECISION**
: August 16, 2007
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Digest

Respondent, a former Regular Member and former employee of a Regular Member Organization, violated Article V, Sections 4(b) and 4(c) of the Exchange Constitution and Exchange Rules 16 and 123 by creating false transactions which did not actually occur in the open market and were never reported for public dissemination on the tape. Respondent submitted the false transactions to a clearing firm for clearance. Respondent's conduct also violated Exchange Rule 324 and SEC Rule 17a-3 by causing the creation of inaccurate books and records at the clearing firm and his Member Organization employer. For these violations, Respondent is censured and permanently barred from any association with any Exchange Member or Member Organization in any capacity.

DECISION

1. Procedural History

The Enforcement Department, on behalf of the American Stock Exchange, LLC, issued a Statement of Charges dated September 15, 2006 against Chad Matthew, a former Regular Member and former employee of Kellogg Capital Group, LLC (“Kellogg”), a Regular Member Organization of the Exchange.

The Statement charges that Matthew violated Article V, Sections 4(b) and 4(c) of the Exchange Constitution and Exchange Rules 16 and 123 by creating false transactions which did not actually occur in the open market and were never reported for public

dissemination on the tape. The Statement also charges that by submitting the false transactions to a clearing firm for clearance, Respondent caused the creation of inaccurate books and records at the clearing firm and at Kellogg, thereby violating Exchange Rule 324 and SEC Rule 17a-3. An Exchange Disciplinary Panel held a hearing on the charges on April 24 and 25, 2007 in New York City.

At the hearing, Enforcement offered the testimony of Geoffrey Chan, an Amex Floor surveillance analyst, Nick Passarelli, Kellogg's Chief Compliance Officer and Reginald Browne, Respondent's former supervisor at Kellogg. Matthew also testified at the hearing.¹ Enforcement offered 29 exhibits, which, without objection from the Respondent, were submitted into evidence.² The Respondent did not offer any exhibits; however, the Panel requested three additional documents, which were provided by Enforcement and were accepted into evidence.³

2. Findings of Fact

From June 2004 through August 2004, Respondent was an employee of Kellogg, working as a Regular Member of the Exchange and as an Exchange-Traded Funds ("ETF") market-maker on the Floor of the Exchange. On August 18, 2004, Matthew was terminated from Kellogg and his membership with the Exchange ceased on October 7, 2004.⁴ The Exchange notified Matthew that it was retaining jurisdiction over him by letter dated October 20, 2004.⁵

During the time Matthew was employed by Kellogg, he worked as a market-maker trading, among other securities, S&P 500 Index iShares ("IVV"), which were

¹ The transcript of the hearing is referred to herein as "Tr."

² CX-1-29; Tr. at 362.

³ Panel Exh. 1-3; Tr. at p. 363.

⁴ CX-1.

⁵ CX-5.

listed on the Exchange. On August 16, 2004, five trades, representing the purchase of 18,600 shares of IVV, were sent for clearance to Kellogg's clearing firm, First Options of Chicago ("FOC"). Matthew stated, at the hearing, in prior testimony and in writing, that these were all legitimate purchases that he made in the crowd on the Floor of the Exchange and that he wrote out paper tickets reflecting the trades.⁶

Enforcement contends that Matthews did not actually make the five IVV purchases, but instead entered five fictitious trades in an effort to make up for losses in his market-making account at Kellogg. Virtually all of the testimony and documentary evidence support Enforcement's position; the only support for Matthew's version of events is his own testimony.

a. Testimony

Matthew testified that he learned sometime on August 17 that the five trades had not cleared.⁷ Matthew spoke to his supervisor, Reginald Browne, about the problem trades in the afternoon on that day. Matthew told Browne that he was "taking care of the trades."⁸

On August 18, Matthew learned before the opening of the market that the trades had still not cleared. When Browne called him to inquire why the trades had still not cleared, Matthew testified that he told him, "I'm going to look into it. This is part of the same problem we had yesterday. I don't know why they are still off. They should all be good trades."⁹ Browne also testified that Matthew told him that the trades were being

⁶ Tr. at 300-302; CX-10; On the Record Testimony ("OTR") at 35.

⁷ Tr. at 254-256.

⁸ Tr. at 138, 254-256, 258-259.

⁹ Tr. at 260.

taken care of, and that the problem had been caused by an error with the clearing agent. Browne asked Matthew for a written statement explaining the situation.¹⁰ Matthew e-mailed Browne shortly after their telephone conversation, again stating that the problem with the five trades was due to an error by the clearing firm, which was “taking care of it.”¹¹

Matthew testified that later in the day on August 18, he learned that the trades did not clear because there was no contra party for any of them.¹² Matthew testified that he believed that he made the trades and had no explanation for why there were no contra parties.¹³ He reiterated that he wrote five paper tickets for the trades.¹⁴

Browne testified that at the end of the trading day on August 18, Matthew approached him and confessed that the trades did not clear because they were not real trades; Matthew had fabricated trades in an effort to offset trading losses he had incurred in his market-making account.¹⁵ That afternoon, Browne relayed this conversation to Nick Passarelli, who was then Kellogg’s Director of Human Resources. Shortly thereafter, Browne fired Matthew in Passarelli’s presence.¹⁶

b. Documentary Evidence

The documentary evidence supports Enforcement’s position and corroborates Browne’s claim that Matthew confessed that he had fabricated the trades. Exchange trading records — APL Data Interface,¹⁷ Amex Audit Trail Report¹⁸ and the Amex

¹⁰ Tr. at 140-141.

¹¹ CX-6; Tr. at 141-143, 261.

¹² Tr. at 270, 274.

¹³ Tr. at 279.

¹⁴ Tr. at 282, 300-302.

¹⁵ Tr. at 148-149, 169, 181-182, 188-190.

¹⁶ Tr. at 96-102, 146-148.

¹⁷ CX-11.

¹⁸ CX-12, CX-13, CX-14.

Consolidated Equity Audit Trail¹⁹— show that the times and prices for the IVV trades entered by Matthew do not match the times and prices for the actual IVV trades captured by Amex surveillance on August 16. For example, Matthew claimed he bought 7,500 shares of IVV at 10:03 a.m. for \$107.82. According to the August 16, 2004 Amex Audit Trail Report, which captured IVV trades on the Amex, at 10:03 a.m., IVV was trading for \$107.65. There were no trades made at 10:03 a.m.; the closest trade for \$107.82 occurred at 10:09 a.m. — of 200 shares.²⁰ According to the Consolidated Equity Audit Trail Report, which captured all IVV trades on all exchanges, there was only one other IVV trade all day at the price Matthew recorded and that occurred on the Pacific Coast Stock Exchange at 10:08, for only 2,700 shares.²¹ Similar analyses of the other four trades show that none of Matthew's IVV trades matched any of the trades that were captured by market surveillance on August 16.²² In short, Matthew's trades never took place. The fictitious trades generated an artificial profit of approximately \$7,500, which appeared to more than offset his trading losses, which totaled approximately \$3,000-\$4,000.²³

Matthew's claim that he submitted paper tickets for each of his five trades was not substantiated. Browne testified that when a trade was made on the floor, a paper ticket was written and handed to a clerk for entry. The clerk made a copy of the ticket and one copy was kept by the clearing agent and one copy was kept by Kellogg. Browne testified that Matthew was required to input a ticket within 15 minutes after a trade was made and that Matthew generally complied with that 15-minute policy.²⁴ Thus, for the five trades

¹⁹ CX-15, CX-16.

²⁰ CX-13.

²¹ CX-15, CX-16.

²² Tr. at 42-49.

²³ Tr. at 70, 145-146.

²⁴ Tr. at 131-133.

allegedly made by Matthew, there should have been ten copies of the tickets—five kept by the clearing firm and five kept by Kellogg. Yet, when the Exchange requested copies of the tickets from the clearing firm and from Kellogg, each firm stated that it was unable to locate a single ticket.²⁵ Geoffrey Chan, an Amex floor surveillance analyst, testified that based on his review as well as discussions with Kellogg's clearing firm, Matthew actually entered the fictitious trades electronically.²⁶

Because there were no contra parties on the trades entered by Matthew, the five transactions had to be reversed by offsetting trades, resulting in a loss to Kellogg of over \$50,000.²⁷

3. Discussion

In light of the extensive documentary evidence and testimony which contradicted Matthew's version of events, the Panel did not find his testimony to be credible. The Panel therefore finds that Matthew violated Article V, Sections 4(b) and 4(c) of the Exchange Constitution and Exchange Rules 16 and 123 by creating false transactions which did not actually occur in the open market and were never reported for public dissemination on the tape. Because Respondent submitted the false transactions to a clearing firm for clearance, he also violated Exchange Rule 324 and SEC Rule 17a-3 by causing the creation of inaccurate books and records at the clearing firm and at Kellogg.

4. Penalties

Enforcement requested that as penalties the Panel impose on Matthew a censure and a permanent bar from association with any Exchange Member or Member Organization.

²⁵ Panel Exhibits 1-3; Tr. at 53.

²⁶ Tr. at 49-53.

²⁷ Tr. at 149.

The Amex Sanction Guidelines do not address fictitious trading. The most analogous NASD Sanction Guideline appears to be Forgery and/or Falsification of Records.²⁸ That guideline directs the Panel to consider a bar in egregious cases. In determining whether Matthew's conduct was egregious, the Panel looked to the Principal Considerations that are relevant to all sanctions under both the Exchange Sanction Guidelines and the NASD Sanction Guidelines.

The Panel recognized that Matthew's conduct was a serious violation of one of the bedrocks of the securities laws—insuring the integrity of the stock markets. Everyone involved in the securities markets must be able to rely on the accuracy of trade reporting. It is the basis for the public's trust in market integrity.

In analyzing Matthew's conduct under the Principal Considerations, the Panel determined that it was egregious. Matthew has neither acknowledged nor accepted responsibility for his conduct; indeed, he continued to maintain throughout the hearing that his trades were authentic even in the face of testimony and documentary evidence to the contrary.²⁹ In addition, Matthew attempted to conceal his fabricated trades, telling his supervisor that they were in the process of being corrected, up until the point where he had no choice but to confess the truth. He apparently recanted that confession shortly after making it; he denied that he had ever made any confession to his supervisor.³⁰ Matthew's conduct was intentional and resulted in the loss of over \$50,000 to his firm.³¹

²⁸ NASD Sanction Guidelines at 39 (2006).

²⁹ Principal Consideration #2.

³⁰ Principal Consideration #10.

³¹ Principal Considerations #11, 13.

The Panel determined that Matthew's conduct was egregious and warrants the most severe of sanctions. Therefore, he is censured and permanently barred from association in any capacity with any Exchange Member or Member Organization.

5. Conclusion

For the reasons set forth above, the Disciplinary Panel, by unanimous vote, finds that Respondent Chad Matthew violated Article V, Sections 4(b) and 4(c) of the Exchange Constitution and Exchange Rules 16 and 123 by creating false transactions which did not actually occur in the open market and were never reported for public dissemination on the tape. Because Respondent submitted the false transactions to a clearing firm for clearance, his conduct also violated Exchange Rule 324 and SEC Rule 17a-3 by causing the creation of inaccurate books and records at the clearing firm and his Member Organization employer. For these violations, Respondent is censured and permanently barred from any association with any Exchange Member or Member Organization in any capacity.³²

FOR THE DISCIPLINARY PANEL


Rochelle S. Hall, Chair

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³² The Panel has considered and rejects without discussion all of the parties' other arguments.