SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 58916 / November 7, 2008

Admin. Proc. File No. 3-12926

In the Matter of the Applications of

JAMES W. BROWNE

and

KEVIN CALANDRO

For Review of Disciplinary Action Taken by

NASD

OPINION OF THE COMMISSION

REGISTERED SECURITIES ASSOCIATION -- REVIEW OF DISCIPLINARY PROCEEDING

Alleged Failure to Provide Written Notice to, and Obtain Prior Approval from, Member Firm Employer Regarding Private Securities Transactions

General securities representatives of member firms of registered securities association charged with engaging in private securities transactions without giving prior notification to, or obtaining prior approval from, members. Held, association's findings of violation and sanctions imposed are set aside.

APPEARANCES:

Brian L. Rubin and Shanyn L. Gillespie, of Sutherland, Asbill & Brennan LLP, and Christopher Bebel, for James W. Browne.

E. Steve Watson, for Kevin Calandro.

Marc Menchel, Alan Lawhead, and Andrew J. Love, for NASD.

Appeal filed: January 14, 2008
Last brief received: April 23, 2008

I.

James W. Browne and Kevin Calandro, general securities representatives associated with NASD member firms, appeal from NASD disciplinary action. 1/ NASD found that Browne and Calandro (together, "Applicants") engaged in private securities transactions involving the securities of e2 Communications, Inc. ("e2") 2/ without prior notice to, and prior written approval from, their member firms, in violation of NASD Conduct Rules 3040 and 2110. 3/ For these violations, NASD imposed upon Browne a six-month suspension and $25,000 fine and imposed upon Calandro a three-month suspension and $5,000 fine. 4/ We base our findings on an independent review of the record and, as explained more fully below, have determined to set aside NASD's findings of violation and the sanctions imposed.

II.

Browne has been a registered representative since 1983, Calandro since 1988. In 1994, while working at broker-dealer Kidder, Peabody & Co., Inc. ("Kidder"), Browne and Calandro became partners and served clients under a joint broker number. Shortly after Browne and Calandro partnered, Kidder was acquired by PaineWebber, Inc. ("PaineWebber").

1/ On July 26, 2007, the Commission approved a proposed rule change filed by NASD to amend NASD's Certificate of Incorporation to reflect its name change to Financial Industry Regulatory Authority, Inc., or FINRA, in connection with the consolidation of the member firm regulatory functions of NASD and NYSE Regulation, Inc. See Securities Exchange Act Rel. No. 56146 (July 26, 2007), 72 Fed. Reg. 42,190 (Aug. 1, 2007) (SR-NASD-2007-053). Because NASD instituted the disciplinary action before that date, we continue to use the designation NASD.

2/ e2 was originally known as e2 Software Corporation, but changed its name in April 2000.

3/ NASD Conduct Rule 3040 prohibits involvement in a private securities transaction outside the regular course or scope of employment without providing prior written notice to the member firm. NASD Conduct Rule 2110 requires members to observe high standards of commercial honor and just and equitable principles of trade; NASD General Rule 115 extends the applicability of NASD rules governing members to their associated persons.

4/ Respondents were also ordered to pay, jointly and severally, $9,930.30 in costs.

Initial Contacts with e2

While at PaineWebber, Browne and Calandro brought in as their first joint client Jeff Farris, an entrepreneur who had become wealthy from the 1995 sale of a software company he founded. Farris invested about $20 million from that sale with PaineWebber in accounts that Browne and Calandro managed.

In October 1997, Farris founded e2, whose business was to develop and sell software designed to help companies market their products and services through e-mail. Farris asked Browne, known to be very technologically savvy, to review the e2 business plan. Browne was impressed with the plan and forwarded the document to his friend and client Ian Bonner, who was a vice president at IBM and, as described by Browne, "one of the world leaders in technology and marketing." Bonner testified that he was "intrigued with the technology," so much so that Bonner was instrumental in establishing a marketing relationship between IBM and e2 and eventually became a full director of the company.

In late 1997 and early 1998 Applicants also introduced three others to e2. Browne introduced his longtime friend Myles Kelley, a commercial real estate broker, "to assist [e2] in finding office space." Browne and Calandro introduced their joint client Barry McCook, a vice president of sales at computer retailer CompUSA, to e2 in hopes that, like the large retailer JC Penney, CompUSA would become an e2 customer. Browne stated in a response to NASD's requests for information that McCook "became aware of e2 when the Company solicited CompUSA to become a customer of e2" and that "I do not recall whether it was Mr. Calandro or I who told Mr. Farris to contact Mr. McCook about CompUSA becoming a customer of e2." 5/ Browne and Calandro also introduced David Galinet to Farris. Galinet, a joint client of Browne and Calandro, was the largest reseller of Hewlett Packard computer and office equipment in the southwestern United States. Galinet became a supplier of computer and office equipment for e2 and later became a reseller of e2's software.

e2's 1998 Common Stock Offering

In the spring of 1998, e2 initiated a private offering of common shares. 6/ McCook and Galinet purchased e2 common shares in the summer of 1998.

5/ McCook signed a letter in April 2003 stating that neither Browne nor Calandro "directly or indirectly solicited in any way the undersigned to subscribe for or invest in e2 . . . stock." As with Browne's statements about investor Kelley, NASD offers no evidence to refute applicants' statements that McCook was introduced to e2 for purposes other than investing.

6/ NASD did not charge Applicants with any violations in connection with the 1998 common stock offering.

Browne and Calandro also sought to purchase common shares for their own portfolios. In May 1998, Browne consulted his manager, Charles Eldemire, about the PaineWebber approvals necessary for him to purchase e2 shares. Eldemire advised Browne to submit a written request to buy the shares, which Browne immediately completed. When Browne became concerned that e2 would close its common stock offering before PaineWebber would respond to his request for approval, Eldemire suggested that, if Browne's wife purchased the shares in her name, no approval from PaineWebber would be necessary. Browne's wife purchased $50,000 (44,445 shares) 7/ and Calandro's wife purchased $15,187.50 (13,500 shares) of e2 common stock in June 1998.

As a result of Browne's inquiries, Eldemire wanted to purchase e2 stock for himself because, he testified, internet stocks were a "hot area." Eldemire testified that he asked Browne for e2's contact information and then called the company. On May 26, 1998, Eldemire purchased $33,750 (30,000 shares) of e2 common stock.

Browne and Calandro told several people about the company and about their wives' 1998 purchases of e2 common stock. Calandro spoke to his brother (John Calandro) and stepfather (Leonard Ciokajlo) about e2, and mentioned to them that Calandro's wife had purchased e2 shares. 8/ Calandro testified, however, that he did not refer his brother to Farris and that he did not arrange for his stepfather to meet Farris. Browne noted in a written response to an NASD request for information that Browne "disclosed my investment in e2" to his father, Robert Browne Sr., and "gave his name to the Company." John Calandro, Ciokajlo, and Browne Sr. purchased e2 common shares in June 1998.

In late 1998 or early 1999, Browne spoke about e2 to his client, J. Robert Carter. Browne testified that Carter co-owned an insurance company with a partner; this partner "independently prospected e2 for all their insurance business." Browne explained in a written response to an NASD request for information that Carter "is also a friend and neighbor of mine and I did disclose to him my investment in e2." 9/ Carter purchased e2 common shares in January 1999; Browne's wife also purchased more e2 common shares at this time.

In November 1999, Browne sought permission from PaineWebber to become an advisory director of e2. In December 1999, PaineWebber responded to Browne's request by approving him to serve as a full director of e2 on condition that, among other things, Browne would not "discuss the investment merits of this entity with any PaineWebber client or PaineWebber

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7/ PaineWebber ultimately approved Browne to purchase shares of e2 himself, but because Browne's wife made the purchase, Browne considered the approval moot.

8/ Calandro's brother is a registered representative and investment advisor.

9/ The record does not indicate whether Browne had any role in Carter's company becoming e2's insurer.

Financial Advisor." 10/ An unexecuted copy of a directorship agreement between Browne and e2 stated that Browne would "perform such duties as the Company's management may request from time to time, including, without limitation, providing the Company with advice pertaining to strategic planning and management . . . ." 11/ Browne explained in a response to NASD's request for information that, as advisory director, he "engage[d] in a wide range of networking activities [including] introductions to potential suppliers, customers, employees, and investors." 12/

The Series B Offering

In late 1999, e2 initiated another round of financing, the Series B Preferred. In support of that effort, in September 1999 and again in November 1999, e2 sent letters directly to investors who had purchased common shares in 1998 and early 1999 soliciting them to participate in the company's issuance of Series B Preferred stock. Eldemire, Galinet, McCook, Carter, John Calandro, Ciokajlo, and Browne Sr., all of whom had purchased e2 common stock in 1998 or early 1999, also purchased Series B shares. NASD points to no additional evidence in the record with respect to Applicants' involvement with these particular transactions.

Browne sent e2's business plan to the investment banking group within PaineWebber in hopes that the firm would underwrite a potential e2 initial public offering. 13/ Browne contacted a regional manager at Morgan Stanley named William Vogel. Browne testified that he had known Vogel for years and contacted him "in an effort to get Morgan Stanley's investment banking department to look at e2" so that e2 would have several opportunities to find an underwriter. Vogel purchased Series B Preferred shares.

10/ The record is unclear whether Browne sought permission from PaineWebber before beginning his term as director. Documents in the record place Browne's start date as advisory director on either April 15, 1999 or September 25, 2000. We need not resolve this factual discrepancy because NASD has not charged Browne with failing to comply with NASD Conduct Rule 3030 by promptly notifying his firm of an outside business activity.

11/ This unexecuted copy is the only version of this agreement in the record.

12/ Browne was granted options to purchase 25,000 shares of e2 common stock when he assumed his directorship, which he never exercised.

13/ Browne testified that he began promoting e2 to PaineWebber's investment banking group in the spring of 1998. PaineWebber appears to have taken seriously Browne's enthusiasm, as it performed due diligence on the company and, in the spring of 2000, produced a proposal for a $20 million private placement and an initial public offering of $75-100 million.

Browne disclosed in a written response to an NASD request for information that he "referred" his father-in-law, Sam Fullerton, to e2. There is no further elaboration in his responses about what Browne did or said regarding e2, and there is no testimony from Fullerton or Browne on the matter. 14/ Browne further stated that he had some involvement with the investment in e2 made by Sudershan Shaunak, a venture capitalist and longtime friend of Browne's father. Browne noted, "My father actually told Mr. Shaunak about his investment in and my involvement with e2 Communications. My father informed me of Mr. Shaunak's interest in the Company and I requested that the Company contact him." During the hearing Browne reiterated that it was not he but his father who "told Mr. Shaunak about e2 Software and e2 Communications." 15/

Three PaineWebber brokers who worked with Browne purchased Series B shares in early 2000. Pat McLochlin testified that many brokers were looking for available investments in the booming internet sector and that there was "a lot of talk about e2" generally and in the office. McLochlin and fellow broker Myron Bond asked Browne if e2 needed investors, and Browne replied that it did. McLochlin and Bond purchased Series B shares without any further involvement from Browne. Broker Glenn Duphorne, who discussed e2, among other internet companies, with Browne, asked Browne if he could invest in e2. Browne gave e2 Duphorne's telephone number. Duphorne purchased Series B shares without further involvement from Browne.

Calandro also discussed e2 with two persons who purchased Series B shares. There is limited evidence in the record about these discussions, however. Calandro testified that he spoke about e2 with his long-time friend Alex Lucido, who had an account with Calandro at PaineWebber. Calandro said that, during a conversation about people who had recently made money investing in internet stocks, Calandro mentioned to Lucido his wife's investment in e2. When Lucido asked if e2 needed more capital, Calandro "probably said at some point they might." According to Lucido's January 3, 2006 affidavit, Lucido, "[m]otivated by [his] own interests, . . . searched for e2 on the internet, found the company's website and directly contacted e2 . . . ." Lucido purchased Series B shares in March 2000. Lucido further stated in his affidavit that Calandro "did not participate in any manner or in any part of the decision-making or investment process. I only informed Kevin Calandro that I had made the investment in e2 after the fact." Lucido had also signed a letter in April 2003 stating that neither Browne nor Calandro "directly or indirectly solicited in any way the undersigned to subscribe for or invest in e2 . . . stock."

14/ Fullerton was not called as a witness; Browne testified but was not asked about Fullerton.

15/ Shaunak was not called as a witness. Although Browne testified briefly about Shaunak during his direct testimony, NASD did not question him about his involvement with Shaunak's transaction.

The other person with whom Calandro discussed e2 was his client Dale Taylor. Calandro testified that he told Taylor, who published a newsletter about the computer industry and with whom Calandro often discussed internet stocks generally, that his wife had purchased shares of e2. Calandro testified that he "thought that [he] possibly had passed along" Taylor's name to e2. Taylor did not purchase shares of e2, but a Taylor/Good Partnership purchased Series B Preferred shares in March 2000. Although Calandro states in his brief that he was "aware that Mr. Taylor made an investment in the e2 Series B Preferred Stock through the Taylor/Good Partnership," the Taylor/Good Partnership was not Calandro's client, and the record does not contain evidence about its structure. Calandro testified, "The Good side of the partnership I don't know anything about. In fact, I don't know anything about the Taylor/Good partnership, per se." Like Lucido, Taylor signed a letter to Calandro's attorney in April 2003 stating that Calandro did not solicit him "in any way" to purchase e2 stock.

On March 11, 2000, e2 closed its issuance of Series B Preferred stock. Browne, in his own name, purchased 7,143 Series B Preferred shares, and Calandro's wife purchased 2,000 shares. Bonner and Kelley, whom Browne introduced to e2 in late 1997, also purchased Series B shares in 2000; however, there is no evidence in the record that Browne or Calandro was involved in these transactions.

On April 11, 2000, e2's attorney sent a Unanimous Written Consent ("UWC") for signature to Bennie Bray, who at the time served as e2's only other board member with Farris. The UWC bears an "effective date" of March 11, 2000 and states that e2 "agreed to pay finders' fees" to Browne and Calandro "in connection with the private placement of 750,000 shares of Series B Convertible Preferred Stock." Noting that Browne had "requested that the shares of Common Stock to be issued to him instead be issued to his wife Priscilla F. Browne," the UWC states that e2 "authorize[d] the issuance" of 10,177 e2 common shares to Browne's wife and 3,137 common shares to Calandro.

Sometime thereafter, in the spring of 2000, Browne's wife received 10,177 shares of e2 common stock in the mail from e2 and Calandro received 3,137 shares. Neither Browne nor Calandro paid for the shares, and no cover letter accompanied them. Browne and Calandro both assert that they did not learn of the existence of the UWC until approximately May 2003, during the course of NASD's investigation, and that they were not expecting to be paid finders' fees. Browne stated in response to an NASD request for information that "in or about March 2000," Farris had advised Browne that "he wished to have the company issue common stock in recognition of my services as an Advisory Director," and that Farris "suggested that these shares be issued in my wife's name because she had previously purchased shares in 1998 and 1999 and this would lower her average price." Browne further stated that he "understood that the shares were provided to my wife in recognition of all of my services as an Advisory Director and that they were not compensation for the solicitation or sale of e2 shares." Calandro testified that he received the shares in the mail in "May or June of 2000" with no explanation or cover letter, prompting him to telephone Browne, who told him the shares were "for the overall contribution of what we had done." It is undisputed that Browne and Calandro did not report their receipt of these shares to PaineWebber.

Subsequent Events

Browne and Calandro left PaineWebber to join Lehman in September 2000. 16/ When Browne joined Lehman, he disclosed his e2 advisory directorship to the firm, his receipt of options in connection with the directorship, and all holdings of e2 stock in his own and his wife's names. 17/ Browne "did not receive written instructions from Lehman but [he] did understand that [his] activities were to comply with NASD Rule 3040." Browne began almost immediately to encourage Lehman to invest in e2, 18/ communicating with several of Lehman's investment bankers and venture capitalists in an attempt to secure Lehman's participation in e2's Series C Preferred round of financing in early 2001. 19/

By 2001, e2 was experiencing financial difficulties. In February 2002, due in significant part to Browne's efforts to recover his own and other shareholders' investments, e2 consented to the filing of an involuntary petition for bankruptcy under Chapter 11 of the Bankruptcy Code. e2 shareholders who opted to participate in the litigation trust established with Browne's assistance had received over $1 million in distributions from e2's bankruptcy estate as of the hearing in 2006.

Subsequent to e2's bankruptcy filing, NASD's Department of Enforcement ("Enforcement") filed a complaint alleging violations of Rule 3040 by Browne and Calandro. Cause One of the complaint alleged, "During the period from December 1999 through March 2000, Browne solicited and/or referred 24 investors to e2, all as more fully detailed on Exhibit 'A,' attached hereto." Cause Three of the complaint alleged similarly that, "[d]uring the period from January 2000 through March 2000, Calandro "solicited and/or referred nine investors to e2,

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16/ There is no evidence in the record that their departures from PaineWebber were related to their dealings with e2. To the contrary, Browne testified without dispute that a manager at Lehman encouraged Calandro and Browne, who was one of PaineWebber's top producers, to move to Lehman. A May 1999 letter from this Lehman manager to Browne stressing the firm's success in recent private equity deals and encouraging Browne to visit the firm's Dallas office supports Browne's testimony.

17/ The disclosure of his holdings was given as a single number representing the total value of all Browne's and his wife's holdings, including the 10,177 shares issued in March 2000.

18/ Lehman performed due diligence on e2, and, although Lehman decided against a direct investment in e2, it proposed a merger between e2 and another e-mail marketing company in which Lehman had already invested significant capital. This merger never materialized.

19/ See discussion infra, Section IV, regarding Browne's involvement in the Series C round.

as more fully detailed on Exhibit 'A,' attached hereto." 20/ Exhibit A is a spreadsheet that lists the names of seventy-five purchasers of e2's Series B Preferred Stock. On this spreadsheet, a column titled "source" lists Browne or Calandro's name next to some of the investors. The complaint also alleged that Browne and Calandro were compensated for these activities.

Browne and Calandro filed motions with the NASD hearing officer objecting that the complaint did not state with sufficient particularity the conduct Applicants were alleged to have engaged in that violated Rule 3040. The hearing officer ordered Enforcement to file a bill of particulars. There, Enforcement alleged that Browne and Calandro participated in private securities transactions by engaging in "one or more" of a list of activities with respect to "transactions of the investors listed on Exhibit A," and "by receiving and accepting shares of e2 as a finder's fee in exchange for their participation." With respect to certain transactions related to Calandro, including his stepfather Ciokajlo's purchase, the bill of particulars alleged that his participation "consisted of receiving and accepting shares of e2 for these transactions after the customers purchased shares of e2 as a result of learning of the investment opportunity from other customers of Calandro." Enforcement further clarified its theory of liability during the hearing, stating that "the receipt of selling compensation alone constitutes participation in the transactions for purposes of Rule 3040."

The NASD Hearing Panel ultimately rejected Exhibit A as "not reliable," noting that the document was "not an e2 corporate record, and none of the Parties presented credible evidence of the document's origin." The panel concluded nonetheless that Browne participated in securities transactions involving the purchase of e2's Series B Preferred shares by nine investors listed on Exhibit A: Bonner, Kelley, Galinet, McCook, Fullerton, Browne Sr., Shaunak, Carter, and Vogel. However, the panel "determined that Browne did not participate in the transactions made by other brokers in his office" whose names were listed on Exhibit A, namely Eldemire, McLochlin, Bond, and Duphorne. The panel found that "there was no evidence that [Browne] had any involvement with [Eldemire's] transaction whatsoever," that Browne's conduct did not constitute "participation in any manner" with respect to the McLochlin and Duphorne purchases, and that there was "insufficient evidence" to prove that Browne participated in Bond's purchase. The panel concluded that Calandro participated in the Series B transactions of six investors listed on Exhibit A: Galinet, John Calandro, Ciokajlo, Lucido, and Taylor, as well as Calandro's brother-in-law, Richard Cieszowski. The panel found that Browne and Calandro were paid finders' fees in connection with these transactions "as authorized by the March 2000 UWC."

On appeal, NASD's National Adjudicatory Council ("NAC") affirmed the Hearing Panel's finding that Browne participated in private securities transactions involving the purchase of e2's Series B Preferred shares by the same nine investors and that Calandro participated in Series B

20/ Cause Two of the complaint dealt with Browne's involvement with certain transactions related to e2's Series C Preferred stock issuance in 2001, which we address in Section IV of this opinion.

transactions involving Galinet, John Calandro, Ciokajlo, Lucido, and Taylor. 21/ Relying on the UWC, the NAC also found that the 10,177 and 3,137 shares that Browne and Calandro received, respectively, in the spring of 2000 were selling compensation "in connection with the introduction of investors to e2 Communications and their investments in e2 Communications."

III.

Exchange Act Section 19(e) provides that, in reviewing a disciplinary proceeding by a self-regulatory organization ("SRO"), we shall determine whether the associated person engaged in the conduct found by the SRO, whether the conduct violated the SRO rules at issue, and whether those rules were applied in a manner consistent with the purposes of the Exchange Act. 22/ In conducting our review, we apply a preponderance-of-the-evidence standard to determine whether the record supports NASD's findings that the conduct of Browne and Calandro violated this rule. 23/

NASD Conduct Rule 3040 provides that "[n]o person associated with a member shall participate in any manner in a private securities transaction" unless he or she provides prior written notice to the member and, if the person has received or may receive selling compensation, receives written permission to engage in the transaction.

Our cases have consistently affirmed a broad interpretation of the Rule and its operative phrase, "participate in any manner." 24/ For example, we held a broker liable in Gilbert M. Hair when he referred a customer to a specific investment instrument (certain promissory notes issued

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21/ The NAC rejected the panel's finding that Calandro participated in Cieszowski's purchase, stating that "the record does not support a finding that Calandro had any conversations with or played any role in [Cieszowski's] purchase." We do not discuss Cieszowski's transaction in this opinion, therefore, because the issue of whether Calandro participated in this transaction is not before us.

22/ 15 U.S.C. § 78s(e).

23/ See Seaton v. SEC, 670 F.2d 309 (D.C. Cir. 1982) (upholding preponderance of evidence standard in NASD disciplinary proceeding).

24/ See, e.g., Mark H. Love, 57 S.E.C. 315, 319 (2004) (emphasizing that the phrase "participates in any manner" "should be read broadly"); See also Joseph Abbondante, Exchange Act Rel. No. 53066 (Jan.6, 2006), 87 SEC Docket 203, 215 (noting that "Conduct Rule 3040 is broad in scope"), aff'd, 209 Fed. Appx. 6 (2d Cir. 2006); Stephen J. Gluckman, 54 S.E.C. 175, 182-83 (1999) (stating that "[t]he reach of Conduct Rule 3040 is very broad").

by an investment banker) and then received a commission for the sale. 25/ In Stephen J. Gluckman, we found a broker liable under Rule 3040 when he informed an investor that an issuer was seeking funds, provided the investor's contact information to the issuer, helped prepare the purchase agreements, received investor funds, and received a referral fee. 26/ In John P. Goldsworthy, a broker violated Rule 3040 by signing the investment instruments, making arrangements to sell them, receiving investor checks made payable to him, and accepting funds from the proceeds of sales of the instruments. 27/ We held in Mark H. Love that a broker may violate Rule 3040 when he specifically recommends an investment to customers and then facilitates the mechanics of the transaction by, among other things, assisting the customers with transferring funds and liquidating their firm accounts to purchase the recommended investments. 28/

The scope of Rule 3040 is not without some limitation, however. Moreover, the parameters of the rule must be sufficiently clear so that associated persons have fair notice of what conduct is proscribed. 29/ Our precedent described above, while describing a wide range of conduct that may be considered violative of Rule 3040, delineates those parameters. We have found participation where the applicant took specific actions to effect the particular transaction or profited from specific involvement in a particular transaction. Hair referred a customer to a particular instrument and received a commission for that sale. Gluckman not only provided buyer contact information to the issuer but also assisted in completing the transactions and received a fee for his assistance with those particular transactions. Goldsworthy signed, sold, and collected payment for investments and then received proceeds from the transactions. Love recommended a specific investment and then assisted customers in funding their purchases of the security.

In contrast, the record before us does not establish by a preponderance of the evidence such a factual nexus between the conduct of Browne or Calandro and the specific Series B

25/ 51 S.E.C. 374, 375 (1993).

26/ 54 S.E.C. at 182.

27/ 55 S.E.C. 817, 835 (2002).

28/ 57 S.E.C. at 320-21.

29/ Cf. Jay Alan Ochanpaugh, Exchange Act Rel. No. 54363 (Aug. 25, 2006), 88 SEC Docket 2653, 2661 (setting aside NASD disciplinary action where NASD decision broadly interpreted the scope of Rule 8210 without offering legal or analytical support for its interpretation and requiring a "fuller exploration of the appropriate scope" of the rule); cf. Rock of Ages Corp. v. Sec'y of Labor, 170 F.3d 148, 156 (2d Cir. 1999) (holding that regulations satisfy due process as long as a "reasonably prudent person, familiar with the conditions the regulations are meant to address and the objectives the regulations are meant to achieve, has fair warning of what the regulations require").

purchases at issue. With respect to Bonner, Galinet, Kelley, McCook, and Vogel, the record does not establish a connection between Browne's introductions of these persons to e2 and those persons' purchases of Series B shares in 2000. Browne, in Rule 8210 responses and in testimony, stated that he introduced these persons to e2 for non-investment purposes. Browne introduced Bonner, an IBM executive, to e2 in 1997. Bonner helped establish a partnership between e2 and IBM, among other contributions to e2. 30/ Browne introduced Galinet, Kelley, and McCook to e2 in 1997 or 1998. Galinet was a provider of computer and office equipment; Kelley was expected to help e2 find office space; McCook was an executive at a software retail chain which became a customer of e2. Browne hoped that Vogel would interest Morgan Stanley in funding an e2 public offering. There is a considerable (or, in the case of Vogel, simply unknown) amount of time that elapsed between the introduction of these customers and the Series B purchases at issue. Nothing in the record contradicts Browne's assertions that his purpose in introducing these individuals to e2 was unrelated to investing. Nothing in the record suggests that Browne was otherwise involved in these purchases.

For some investors, there is both a lapse of time and intervening events between Applicants' introduction and the investor's eventual purchase of Series B shares. NASD found that Browne and Calandro were liable for having introduced to e2 six persons who purchased common shares in 1998 and then purchased Series B shares in 2000 (Galinet 31/ and McCook, as discussed above, and Browne Sr., Carter, J. Calandro, and Ciokajlo). NASD did not charge Browne or Calandro with having participated in the 1998 transactions. The record demonstrates that e2 itself solicited these common stockholders to buy Series B shares by sending letters to all participants in the 1998 offering asking for additional investments. NASD points to no evidence that Applicants were involved in these investors' Series B purchases.

NASD instead presents a new theory of liability under Rule 3040. NASD suggests that "[i]t is common knowledge that start-ups often seek funding from their advisors, suppliers, consultants, and other individuals involved with the company, and under the facts and circumstances Calandro and Browne should have known that their introductions [in 1998] would

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30/ We note that, in any event, Browne was not charged with having participated in Bonner's purchase of Series B shares, raising an issue as to whether Browne received sufficient notice that he needed to defend against a Rule 3040 violation stemming from his introduction of Bonner to e2.

31/ We note that the complaint and bill of particulars allege that Browne, but not Calandro, participated in Galinet's purchase of Series B shares. No motion was made to amend the complaint to include a charge against Calandro with respect to Galinet's purchase. Nevertheless, both the Hearing Panel and NAC found Calandro liable for it. Because only Browne was charged with this transaction, Calandro was not afforded an opportunity during the hearing to present any evidence or witnesses in his defense regarding this transaction. We therefore dismiss the finding of liability for Galinet's purchase with respect to Calandro on this additional basis.

lead to investments in e2 Communications [in 2000]." NASD states that Browne and Calandro "were or should have been aware that e2 Communications, as a start-up technology company, would have ongoing capital needs and would likely initiate a number of rounds of private placements." Thus, NASD appears to have found that Browne and Calandro "participated" in these transactions because they "should have been aware" that their earlier referrals to e2 would eventually result in subsequent purchases of Series B stock. NASD's theory encompasses a much broader range of conduct than contemplated by the accepted definition of "participate" 32/ or by our earlier cases, which required a reasonably close factual nexus between the participatory conduct and a specific securities transaction. We believe that NASD has created a novel interpretation of Rule 3040. However, NASD has provided no prior notice to Applicants of the applicability of this new theory of liability to the proceeding against them. This lack of notice alone raises concerns sufficient to warrant dismissal of the charges against Browne and Calandro.

Aside from the notice question, NASD fails to establish a connection between Applicants' referrals and the complained-of Series B transactions. 33/ We explained in Love that a broker does not violate Rule 3040 when the broker "does nothing more than refer a customer to another investment opportunity." 34/ Although one might reasonably conclude that wealthy individuals with liquid assets have the wherewithal to invest in a company, it does not necessarily follow that they will invest in every company to which they are introduced. We also cannot conclude that, once that investor buys stock in a particular company, he or she will necessarily do so again. We do not understand why the NASD Hearing Panel found that Browne and Calandro "should have been aware" that certain individuals would invest in e2 based on an introduction to the company, while declining to find that they participated in the purchases by the four PaineWebber brokers, such as Eldemire, who purchased e2 shares under similar circumstances. When Browne and Calandro raised this argument on appeal, the NAC stated without explanation or analysis that the panel's decision contained "no such inconsistency."

NASD argues that Browne and Calandro received selling compensation from e2, and that this selling compensation serves as evidence of their participation in investors' purchases of Series B shares. NASD cites the UWC, which purported to issue 10,177 and 3,137 shares to Browne's wife and Calandro, respectively, in the spring of 2000. NASD argues that the UWC

32/ See AMERICAN HERITAGE DICTIONARY OF THE ENGLISH LANGUAGE (4th ed.) (defining "participate" as "to take part in something" or "to share in something").

33/ Compare Ronald J. Gogul, 52 S.E.C. 307, 310 (1995) (finding associated persons liable under Rule 3040's predecessor Rule 40 for referring clients "for the purpose of investing" in certain securities and being compensated therefor) and Terry Don Wamsganz, 48 S.E.C. 257, 258 (1985) (finding broker violated Rule 3040's predecessor Rule 40 when he referred two clients "who wanted to acquire control of a business" to a company seeking additional capital and then received a finder's fee).

34/ Love, 57 S.E.C. at 321.

"unambiguously states that these shares were finders' fees earned by Calandro and Browne in connection with the Series B Preferred offering . . . ." However, Rule 3040 defines "selling compensation" as "any compensation paid directly or indirectly from whatever source in connection with or as a result of the purchase or sale of a security." 35/ The UWC does not link the shares given to Browne and Calandro to the particular Series B "purchase or sale" of any of the thirteen investors for whose purchases Browne and Calandro were charged and found liable.

Although the record contains a May 2000, internal e2 email from e2's CFO characterizing the share issuance as "payment for Pref. B round," the email was not discussed in any detail at the hearing and does not identify the transactions or services for which the shares purport to be "payment." Similarly unhelpful are a letter Bray wrote to NASD in 2003 and Bray's hearing testimony about the letter. That letter can reasonably be read to support Applicants' contention that the shares were issued in recognition of their overall efforts in support of e2 and not tied to any of the specific transactions at issue in this case. Based on the ambiguity of the UWC and the lack of other reliable record evidence demonstrating that Browne and Calandro received shares from e2 as compensation for participation in the specific Series B share purchases charged, rather than as a general reward for their support of e2, we cannot conclude that Applicants' receipt of the shares covered by the UWC provides meaningful evidence that they participated in private securities transactions as prohibited by Rule 3040.

We also find that the evidence is insufficient to find Applicants liable under Rule 3040 for participating in the purchases of Fullerton, Shaunak, Lucido, and the Taylor/Good Partnership. The record as to these transactions is limited to referrals. 36/ With respect to Fullerton, the only information available about Browne's connection to Fullerton's purchase of Series B shares is Browne's own response to NASD's request for information in which Browne simply included Fullerton's name in a list of persons Browne "referred to e2, who invested in e2." Browne was not asked about Fullerton's purchases during the hearing, and Fullerton himself did not testify. With respect to Shaunak, the record demonstrates only, according to unopposed testimony from Browne and his own brief response to NASD's request for information, that Browne requested that e2 contact Shaunak after Shaunak learned of the company from other sources and had decided to invest.

With respect to Lucido, Calandro testified without opposition that, in the context of general discussions about internet stocks, he told Lucido that his wife had purchased e2 shares. Calandro also told Lucido, in response to direct questioning about whether e2 would need more capital, that Calandro "probably said at some point they might." Lucido's affidavit supports the conclusion that Lucido pursued this investment on his own initiative. The record does not indicate that Calandro had any further involvement with Lucido's purchases.

35/ NASD Rule 3040(e)(2).

36/ See Love, 57 S.E.C. at 321.

We also find that the evidence does not establish that Calandro participated in the Series B purchase of the "Taylor/Good Partnership." The only evidence presented with respect to this purchase was testimony by Calandro regarding discussions about e2 that he had with his client Charles Taylor. No evidence was adduced regarding Taylor's relationship to the Taylor/Good Partnership or whether Taylor or Calandro had any role in the purchase, or in the decision to purchase, by the partnership. We therefore dismiss this finding of liability because it was not proven as charged.

* * *

For the reasons explained above, we dismiss NASD's findings of liability with respect to the Series B purchases by the thirteen investors at issue.

IV.

Exchange Act Section 15A(h)(1) ensures fairness in NASD proceedings by requiring that specific charges be brought, that notice be given of such charges, that an opportunity to defend against such charges be given, and that a record be kept. 37/ Count Two of the complaint alleged that Browne participated in certain purchases of e2 common shares and Series C Preferred shares by Steve Flory. Flory testified that, although he did purchase some e2 common stock himself, a limited partnership he assertedly managed, CBI-Eastchase, was the purchaser of the remaining shares at issue. Flory also testified that he was not the majority owner of CBI-Eastchase, and that the majority owner lent the partnership most of the funds it used to buy those shares. Thus, at the hearing, there arose an issue as to whether Flory could properly be deemed the "purchaser" of all e2 stock as alleged in Cause Two of the complaint.

During the hearing, Browne objected repeatedly to this apparent disparity between the complaint and the evidence with respect to these transactions, and Enforcement responded by moving to "conform the pleadings to the evidence." However, the hearing officer never issued a ruling on the motion, leaving the scope of Cause Two's allegations unclear.

We believe the hearing officer's failure to rule on Enforcement's motion introduced confusion into an already unclear theory of the case. Browne's continuing objections, unresolved by the hearing officer, suggested that Browne had not "'understood the issue'" and was not

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37/ 15 U.S.C. § 78o-3(h)(1). See also James L. Owsley, 51 S.E.C. 524, 527-28 (1993) (dismissing "findings of misconduct on matters that have not been charged and which respondents [did not have] a fair chance to rebut"); Paulson Investment Co., Inc., 47 S.E.C. 886, 890 (1983) (setting aside NASD findings of violation where the complaint did not charge applicants with the deficiencies at issue and where the Commission was unable, on the basis of its review of the record, to "conclude that applicants were subsequently given adequate notice of these additional allegations, or a proper opportunity to defend themselves against them").

"'afforded full opportunity' to justify [his] conduct during the course of litigation." 38/ We cannot know how Browne's defense of Cause Two might have changed or been augmented if Enforcement had given Browne notice with more specific charges of the reasons Browne allegedly participated in the purchases by CBI-Eastchase. 39/ We therefore dismiss this finding of liability.

V.

In sum, we conclude that the record in this case provides insufficient support for a finding that Browne or Calandro participated in private securities transactions with respect to investor purchases of e2 Series B shares in violation of NASD Rule 3040 and dismiss those charges. We also dismiss the findings of liability based on Flory's and CBI-Eastchase's purchases of e2 common and/or Series C stock. 40/

An appropriate order will issue. 41/

By the Commission (Chairman COX and Commissioners CASEY, AGUILAR, and PAREDES; Commissioner WALTER not participating).

Florence E. Harmon
Acting Secretary

38/ Wanda P. Sears, Exchange Act Rel. No. 58075 (July 1, 2008), __ SEC Docket __, __ (quoting Aloha Airlines, Inc. v. CAB, 598 F.2d 250, 262 (D.C. Cir. 1979) (quoting NLRB v. McKay Radio & Tel. Co., 304 U.S. 333, 350 (1938))).

39/ See Owsley, 51 S.E.C. at 527-28. Compare Nicholas A. Codispoti, 48 S.E.C. 842, 845 n.14 (1987) (rejecting applicant's claim of prejudice and noting that "the record reflects that [applicant] had sufficient opportunity to introduce evidence with respect to" certain securities at issue in the case).

40/ We note that, in affirming the sanctions upon Browne and Calandro, the NAC considered it an aggravating factor that "Browne's misconduct resulted in claims against PaineWebber." The "claim" against PaineWebber involved a settled arbitration proceeding brought by an e2 investor about which there is scant information in the record. NASD elected not to charge Browne with having participated in this investor's purchase of e2 shares. We would find it inappropriate to consider as aggravating information about an arbitration settled by a person's former firm that has not been adequately developed in the record.

41/ 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 in this opinion.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 58916 / November 7, 2008

Admin. Proc. File No. 3-12926

In the Matter of the Applications of

JAMES W. BROWNE

and

KEVIN CALANDRO

For Review of Disciplinary Action Taken by

NASD

ORDER SETTING ASIDE DISCIPLINARY ACTION TAKEN BY REGISTERED SECURITIES ASSOCIATION

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

ORDERED that the sanctions and costs imposed by NASD against James W. Browne and Kevin Calandro be, and they hereby are, set aside.

By the Commission.

Florence E. Harmon
Acting Secretary