

Respondent 1 was associated with Firm A. On August 31, 1994, Firm A's assets were transferred to Firm B, another member firm, and Respondent 1 resigned as Firm A's compliance director. Respondent 1 is not currently associated with another member firm.

Respondent 2 entered the securities industry in 1991. From June 22, 1992, until March 31, 1995, Respondent 2 was associated with Firm A, and from September 1, 1994, until at least December 21, 1994, she was employed by Firm A as its compliance director. Respondent 2 is not currently associated with another member firm.

Facts

The late Form U-4 and U-5 filings at issue in this matter encompassed a period from January 1994, when the first complaint was received by the Firm, until December 1994, when the last form was filed. The complaint alleged that Respondent 1 and Respondent 2 violated Conduct Rule 2110 by failing promptly to amend and file with the NASD 35 Forms U-4 and U-5 as required by Article IV, Sections 2 and 3 of the NASD By-Laws, respectively.² The DBCC found that of the remaining 30 late filings, 18 were attributable to Respondent 1 and 12 were attributable to Respondent 2.

March 1993 to August 31, 1994 (Respondent 1's Tenure as Compliance Director). Respondent 1 served as Firm A's compliance director from March 1993 through August 31, 1994. The late Form U-4 and U-5 filings at issue with respect to Respondent 1 involved customer complaints that were filed from January through August 1994, during which time the compliance staff of Firm A consisted of the compliance director (Respondent 1), three compliance officers: Respondent 2, Compliance Officer 1 and Compliance Officer 2 and two registration specialists: Registration Specialist 1, who was employed by the Firm from November 1993 until April 1994 and Registration Specialist 2, who was employed by Firm A from March 1992 to March 1995, but was employed in the compliance department of Firm A only from approximately April 1994 to March 1995. Compliance Officer 1 was employed by the Firm from March 1989 to September 1994 and Compliance Officer 2 was employed by the Firm from July 1993 to September 1994.

The job of compliance officer differed from that of the registration specialist in that the compliance officers were required to investigate and resolve the complaints, but were not required to draft the Disclosure Reporting Page(s) ("DRP(s)") (the part of the Form U-4 and U-5 that contains information about the reportable event or proceeding) or to file the amended Forms U-4 and U-5. Compliance Officer 1 and Compliance Officer 2 both testified that it was the job of the registration

² The DBCC decision incorrectly stated that the complaint alleged a total of 30 late filings when, in fact, the complaint alleged a total of 35 late filings. The District staff stipulated to dismiss four of the alleged late filings, and the subcommittee of the DBCC that heard this matter directed that one additional alleged late filing be dismissed.

specialist to prepare language for, and to file, the amended Forms U-4 and U-5 to reflect the customer complaints.

According to Compliance Officer 1, the procedure for handling customer complaints during the time of her employment was that Respondent 1 or Respondent 2 would log in the complaints and then distribute copies of the complaints to the registration specialist (Registration Specialist 2 replaced Registration Specialist 1 in April 1994) and compliance officers for subsequent resolution. Compliance Officer 1 testified that her job consisted of reviewing and determining the merits of the customer complaint. She would investigate the merits of the customer complaint by asking the broker and branch manager for a written statement and would request copies of customer account documents and order tickets. After completing her investigation, she would prepare a response to the customer. Compliance Officer 1 maintained that she was not responsible for the updating of Forms U-4 and U-5, but that in unusual circumstances she would make the determination as to whether a Form U-4 or U-5 had to be updated, and would prepare and sign the DRPs in such cases.

Compliance Officer 2, an attorney, handled complaints originating from a broker in Minneapolis, a broker/dealer that Firm A had acquired in July 1992. Compliance Officer 2 maintained that he had never prepared a DRP form and had never dictated to Registration Specialist 1 or Registration Specialist 2 what should be on a DRP form as a result of a particular customer complaint.

The two registration specialists (Registration Specialist 1 and Registration Specialist 2) maintained that they had no independent authority to amend and file Forms U-4 and U-5 to reflect customer complaints. Their other job responsibilities, however, were not in dispute (e.g., arranging for state registrations and updating Forms U-5 that did not involve customer complaints). Registration Specialist 1 testified that she only updated Forms U-4 and U-5 if she was given specific directions to do so. In the event that a Form U-4 or U-5 had to be updated regarding a customer complaint, Registration Specialist 1 was told what information to enter onto the DRPs. Registration Specialist 1 maintained that, throughout her nine-month tenure at Firm A, Respondent 1 or Respondent 2 would dictate to her the information that would go on the DRPs, and that she was not given copies of complaints. Registration Specialist 1 did not recall ever having been reprimanded by Respondent 1 or Respondent 2 for failing timely to update Forms U-4 and U-5, and neither Respondent 1 nor Respondent 2 claimed that they had reprimanded her with respect to her updating of Forms U-4 and U-5. Registration Specialist 1 stated that when she did receive DRPs, she handled them promptly. Further, Registration Specialist 1 denied having knowledge of any of the customer complaints that she was questioned about in connection with this matter. Registration Specialist 2 testified that Respondent 2 was his supervisor, both before and after the sale of Firm A. After receiving a handwritten copy of the updated Forms U-4 and U-5 from Respondent 1 or the compliance officers, Registration Specialist 2 would type the language onto the DRP form.

The Sale of Firm A. During the weeks preceding the sale of Firm A on August 31, 1994, Firm B attorneys performed due diligence by interviewing Firm A's compliance personnel and reviewing all

customer complaints against Firm A's registered personnel. The due diligence also included a review of the registration files of Firm A's registered personnel. Respondent 2 testified that the due diligence review disrupted the operations of the compliance department because the Firm B attorneys had removed customer complaint and registration files from the compliance department and took the files to another location within the same building. At the conclusion of the due diligence review, the Firm B attorneys did not return the files to Firm A's compliance department. Respondent 1 and Respondent 2 therefore had to search the building for the missing files, which they eventually found in a disheveled state on the floor in a conference room.

August 31, 1994 to December 1994 (Respondent 2's Tenure as Compliance Director). The transfer of Firm A's assets to Firm B caused a large increase in the number of customer complaints beginning in August 1994. Firm A's compliance department received more than 20 complaints per month in August, September, and October 1994, which equaled or exceeded the number of complaints received in all of 1992 or 1993.

When Firm A announced the purchase by Firm B, all of Firm A's compliance officers looked for new employment. Respondent 1 gave a three-week notice of resignation on August 31, 1994, and he accepted a position as compliance director at another member firm. The compliance officers, Compliance Officer 2 and Compliance Officer 1, were hired as compliance officers at Firm B, and then relocated to other offices in the building in which Respondent 2 continued to work.

On August 17, 1994 Respondent 2 accepted an offer to become the compliance director for another member firm. She had planned to begin her new position on September 1, 1994. However, after she had submitted her letter of resignation to Firm A, Firm A's General Counsel pleaded with her to stay to oversee all pending compliance matters during the winding-up phase of Firm A's operations. Respondent 2 testified that out of loyalty to Firm A's General Counsel and to the Firm she agreed to stay at Firm A and become its compliance director. Respondent 2 testified that it was her understanding that, after the sale, Compliance Officer 2 and Compliance Officer 1 would still be available to assist her with the pending customer complaints and that Respondent 1 would be available to work on Firm A compliance matters until his termination on September 21, 1994.

Despite Respondent 2's understanding that Respondent 1 would be available to work on Firm A compliance matters following the sale of Firm A's assets to Firm B, on September 6 she was advised by Firm B's General Counsel that he would require Respondent 1 to dedicate 100 percent of his remaining three weeks to assist with the transition of compliance responsibilities to Firm B's legal and compliance staff. Firm B's General Counsel also advised Respondent 2 that Compliance Officer 2 and Compliance Officer 1 would be required to dedicate 100 percent of their time to Firm B compliance issues and, therefore, would be unable to assist Respondent 2 with any Firm A compliance matters.

After the departure of Respondent 1, Compliance Officer 2, and Compliance Officer 1, Firm A's compliance department consisted of Respondent 2 and Registration Specialist 2. Although

Respondent 2 attempted to hire additional personnel to assist Registration Specialist 2 and her with compliance matters, she had a difficult time finding people willing to take the job. In early September 1994, Respondent 2 hired New Employee 1 to conduct a review of the branch offices and eventually to assist with the day-to-day activities of the compliance department once the branch office reviews were concluded. New Employee 1 had completed eight of the scheduled 29 branch office examinations when she had a serious automobile accident in early October 1994. As a result of the accident, New Employee 1 did not return to her job at Firm A until February 1995.

In approximately early October 1994, Respondent 2 arranged with Firm A Employee 1 who was from one of Firm A's bank service groups, to fly to Chicago from Columbus, Ohio to work part-time in Firm A's compliance department. On his first day of work, however, Curran gave Respondent 2 two weeks' notice. Finally, by about mid-October 1994, Respondent 2 succeeded in hiring two individuals, New Employee 2 and New Employee 3, to assist her and Registration Specialist 2 in the compliance department. Neither New Employee 2 nor New Employee 3 had any previous compliance experience and thus had to be trained by Respondent 2. As a result of these events, Respondent 2 and Registration Specialist 2 were the only full-time employees in Firm A's compliance department from approximately Sept 1 to mid-October 1994 who worked on customer complaint matters.

In addition to working as a registration specialist for Firm A, Registration Specialist 2 also was responsible for maintaining Firm B's "watch list,"³ which demanded a significant amount of his time. Additionally, Hurst, Firm B's General Counsel, made daily demands on Registration Specialist 2 to reproduce all of the registration files for the hundreds of account executives and/or registered staff that had transferred to Firm B. Registration Specialist 2 testified that the procedure he followed with respect to updating the Forms U-4 and U-5 in November and December 1994 was that he would look through the file to find the original complaint, prepare a rough draft of the DRP, and then submit it to Respondent 2 to see if it required any additional language. Registration Specialist 2 testified that once he had all of the relevant information, it would take him a matter of minutes to update the Forms U-4 and U-5. Upon further questioning, however, Registration Specialist 2 admitted that over the entire period that he worked at Firm A, it would typically take him one week to update the Forms U-4 and U-5 after receiving approval of draft language.

After Respondent 2 had assumed the compliance director position at Firm A, she instituted a new procedure to track complaints. Under the new procedure, Respondent 2 was responsible for logging in the customer complaints, and Registration Specialist 2 was responsible for reviewing and making the initial determination whether an amendment was required on the Form U-4 or U-5 to reflect a customer complaint. As part of the new process, Registration Specialist 2 was required to process

³ Before the sale, Firm B did not have any mutual funds. As a result of the sale, Firm A's mutual fund was transferred to Firm B, which generated a need by Firm B to maintain a "watch list," whereby certain securities are singled out for special surveillance in order to spot irregularities.

the Forms U-4 and U-5 (including the preparation of a draft DRP form) and forward the information to the person responsible for responding to the customer. Respondent 2 attached a checklist of the procedures to each customer complaint. Under the new procedure, after Registration Specialist 2 had prepared a DRP form, he was supposed to bring it to Respondent 2 to review its contents. It was undisputed that even under the new procedures, Registration Specialist 2 did not have authority to sign the DRPs or the amended Forms U-4 or U-5.

In early October 1994, the NASD began its annual examination of Firm A. Respondent 2 claimed that the NASD examiner, inadvertently exacerbated the already difficult situation by borrowing complaint files that were necessary for the registration process and by insisting that the old complaints be addressed first, thereby causing delays with respect to the filing of the newer complaints. No other witness, however, corroborated Respondent 2's claim. Deske testified that he had never advised Respondent 2 or Registration Specialist 2 that the old complaints had to be filed before the newer complaints. Additionally, the NASD examiner testified that he had always accommodated Respondent 2's and Registration Specialist 2's requests to return files to them when they were needed to process a customer complaint.

Registration Specialist 2 testified that he had compiled a list of the outstanding customer complaints and obtained the relevant customer complaint files for the NASD examiner. Registration Specialist 2 further testified that prior to compiling the list, he had not been aware that the Forms U-4 and U-5 had not been updated to reflect those customer complaints. Registration Specialist 2 also denied ever having seen the customer complaints at issue prior to his compilation project for the NASD examiner.

Discussion

Respondent 1. We find that Respondent 1 failed promptly to file amendments to nine Forms U-5 and five Forms U-4 to reflect customer complaints (as detailed on the attached Schedule A) as required by Article IV, Sections 2 and 3 of the NASD By-Laws in violation of Conduct Rule 2110.⁴

⁴ Applications for securities industry registration or transfer are made on a Form U-4. Article IV, Section 2(a)(3)(c) of the NASD By-Laws requires every application for registration that is filed with the NASD to be kept "current" at all times by supplementary amendments to the original application. During the relevant time, Section 2(a)(3)(c) did not specify a period of time within which such amendments should be made; however, it was industry practice for firms to file Form U-4 amendments within 30 days of the filing of a customer complaint that was a reportable event or proceeding in accordance with the criteria set forth in Form U-4.

The NASD requires that a Form U-5 be filed with the NASD following the termination of a person associated with a member firm. Article IV, Section 3(a) of the NASD's By-Laws provides that, the member must promptly, but in no event later than 30 calendar days after such termination, file a

Among other things, Forms U-4 and U-5 contain a series of questions that request information about whether the registered representative has been the subject of an investment-related, consumer-initiated, written complaint, that involved one or more sales practice violations and contained a claim for compensatory damages of \$5,000 or more or was settled for \$10,000 or more, or contained an allegation involving forgery, theft, misappropriation or conversion of funds or securities. The forms also request information about whether the registered representative has ever been named as a respondent/defendant in an investment-related, consumer-initiated arbitration or civil litigation which alleged one or more sales practice violations. We further find that Respondent 1 did not effectively delegate to his compliance staff the responsibility for filing these amended Forms U-4 and U-5. We, however, modify the findings of violation made by the DBCC by dismissing certain customer complaints for which we find Respondent 1 cannot be held responsible. Specifically, we find that Respondent 1 is not responsible for the three customer complaints that were filed only days before he stepped down as compliance director, since he did not have 30 days within which to file the relevant amended Forms U-4 and U-5. Accordingly, we dismiss the complaints filed by customers BH, TE, and CP. In addition, we dismiss the complaint filed by DS because it is not clear from the record that any principal of the Firm had received notice of the arbitration action at issue.

It was standard operating procedure for Respondent 1 or the compliance officers sometimes to decide to defer reporting customer complaints on amended Forms U-4 and U-5 based on concerns about the merit of a complaint or possible defamation claims by the registered representatives who were the subject of the complaints. Respondent 1 testified that he had a personal problem placing "frivolous" complaints on amended Forms U-4 and U-5 because of the potential for being sued for defamation.

We find that Respondent 1, in fact, was on notice of his obligation to update all Forms U-4 and U-5 for which there was a reportable event or proceeding, regardless of the merits of the customer complaints.⁵ In September 1993, District No. 8 staff issued a Letter of Caution ("LOC") that was issued to Firm A during Respondent 1's tenure as compliance director for failing to file updates to one Form U-4 and two Forms U-5 in a timely manner. Respondent 1 testified that the reason the Firm received the LOC was because he had determined the complaints at issue had no merit and, therefore, were not reportable.

Form U-5, and concurrently provide a copy to the person whose association has been terminated. Article IV, Section 3(b) of the NASD's By-Laws requires NASD members to file a written amendment to the Form U-5 within 30 days when the members learn of facts or circumstances causing any information set forth in the Form U-5 to become inaccurate or incomplete.

⁵ The Securities and Exchange Commission ("SEC" or "Commission") has recognized that a securities professional's responsibility to ensure compliance with the securities rules is heightened by prior proceedings by the NASD. See Cost Containment Services, Inc. Exchange Act Rel. No. 34-35730 at 770 (May 18, 1995) (finding that respondent's awareness of the accrual problem involving the firm's net capital could only have been heightened by the NASD's prior proceedings).

In a response letter to the NASD regarding the LOC, Respondent 1 stated that the Firm's practice was to investigate a customer complaint and if it was "deemed frivolous or without a reasonable basis . . . the registration would remain unaffected." However, Respondent 1 did acknowledge in his response letter that it was "mandatory that any complaint containing an allegation of fraud, churning, unsuitable recommendations or similar charges requires the amendment of the individual's Form U-4 or U-5 within thirty (30) days of receipt." Even after the Firm had received the LOC and Respondent 1 had assured the NASD in his letter of response that he had "modified [the Firm's] procedures to reflect this rule interpretation," the Firm's procedure for handling customer complaints essentially did not change. The record demonstrates that after receiving the LOC Respondent 1 and the compliance officers continued to investigate the merits of the customer complaints before they would coordinate with the registration specialist regarding the language for inclusion in the DRPs.⁶

Although Respondent 1 argues that he was not required to "ensure" that the amendments to Forms U-4 and U-5 to reflect customer complaints had been made because he had hired competent staff to handle the filings, we find no evidence in the record that Respondent 1 effectively delegated the responsibility for such filings to others on his staff.⁷ It appears that although there were occasions on which the compliance officers prepared and signed the DRPs, their primary responsibility was to investigate customer complaints and to respond to the customers. The compliance officers assumed that the registration specialists handled the updating of the Forms U-4 and U-5 to reflect customer complaints. Although the registration specialists testified that they would prepare the DRPs after guidance from others, they maintained that they could not independently draft, sign, and file the amended Forms U-4 and U-5. Respondent 1 testified that Registration Specialist 1's testimony about not being authorized to sign DRPs was "a lie." He also testified, however, that it was "not a bad idea" for Registration Specialist 1 to let someone review the DRPs before they were filed. We find Respondent 1's testimony on this issue to be inconsistent and therefore not credible.

⁶ Respondent 1 admitted in his testimony that he did not have any follow-up procedures in place to ensure that the registration specialists were preparing the amendments on a timely basis.

⁷ It is undisputed that while Respondent 1 was compliance director there were no written supervisory procedures setting forth whose responsibility it was to prepare and file the amended Forms U-4 and U-5. Although Respondent 1 admitted that he was responsible for clearly letting subordinates know what their job duties were, he testified that he could not, from his personal knowledge, attest to the steps that were followed by Registration Specialist 1 and Registration Specialist 2 after they received a copy of the complaint. Respondent 1 testified that he had not personally trained Registration Specialist 1 and that he was not aware of what she was specifically told about the procedures for handling customer complaints.

We credit Registration Specialist 1's and Registration Specialist 2's testimony that they would obtain the wording for the DRPs from Respondent 1 or the compliance officers before obtaining an authorized signature from Respondent 1 or the compliance officers. We also credit the compliance officers' testimony that, while they were responsible for investigating the customer complaints and responding to the customers, they were not responsible for the timely filing of the DRPs. We also find no evidence in the record that demonstrates that the registration specialists had been delegated the authority to ensure that amendments to Forms U-4 and U-5 reflecting customer complaints would be filed in a timely manner.

We find that Respondent 1's contention that the merit of customer complaints should first be investigated in order to determine whether they are required to be reported is without support. The customer complaints for which we have made findings of violation were reportable events and proceedings, which required that the Forms U-4 and U-5 at issue be timely updated (*i.e.*, within 30 days from the receipt of the customer complaint or notice of arbitration), in accordance with Article IV, Sections 2 and 3 of the NASD By-Laws.⁸ In the event the final disposition is not known at the time the initial reporting of the event or proceeding is made on the Form U-4 or U-5, firms are required to file a subsequent amendment to reflect the outcome, in accordance with the instructions contained in Forms U-4 and U-5.

Respondent 1 also argued that the operations of the compliance department were disrupted by Firm B's due diligence review and that, as a result, customer complaints and registration files were sometimes unavailable. We have reviewed the dates that the customer complaints were received by the Firm and have concluded that almost all of the complaints at issue were received months before Firm B began its review, thus the due diligence review would have had no impact on the amendments to Forms U-4 and U-5 that were required to be filed as a result of those complaints. In any event, the fact that Firm B was performing a due diligence review of the Firm did not absolve Respondent 1 from timely filing Forms U-4 and U-5 as required.⁹

⁸ Item 8 on each of the DRPs requires information about the "current status" of the event or proceeding. In addition, the DRPs request information about the type of proceeding and the date that the proceeding was initiated; a description of the allegations, including the amount of actual or alleged damages; and the result of the event or proceeding.

⁹ We also do not credit Respondent 1's argument that he is being held responsible for the alleged violations simply because the compliance department did not have a computerized "tickler" system in place that would alert him whenever a 30-day period was ending and the amended Forms U-4 and U-5 had to be filed. He argues that the NASD does not require firms to maintain a tracking system to ensure that a registration specialist is reporting customer complaints in a timely manner. Respondent 1's arguments are without merit. Contrary to Respondent 1's argument, we find that the prompt filing of Forms U-4 and U-5 certainly could have been accomplished without the benefit of a computerized system.

Respondent 2. We find that Respondent 2 was responsible for the prompt filing of amendments to Forms U-4 and U-5 to reflect customer complaints. We also find that Respondent 2 should not be held liable for the late filings at issue because she did everything in her power to attempt to carry out her responsibilities as Firm A's compliance director. Accordingly, we dismiss the allegations against Respondent 2. Individuals in Respondent 2's position have to make every reasonable effort to identify compliance problems and to obtain the resources necessary to comply with relevant regulatory obligations. Accordingly, in circumstances such as those faced by Respondent 2, responsible parties must either obtain the necessary additional resources or leave the firm. In this case, Respondent 2 did what was required by seeking to hire additional staff, and shortly thereafter actually hiring additional staff, to assist with the updating of Forms U-4 and U-5 to reflect customer complaints. The record demonstrates that there was an improvement in the timeliness of the filings as a result of Respondent 2's efforts.

When she became compliance director, Respondent 2 was unexpectedly left with no compliance staff, except for Registration Specialist 2. During this period, Firm B's General Counsel constantly inundated Registration Specialist 2 with work that took his time away from the task of updating Forms U-4 and U-5 to reflect customer complaints. In light of Firm B's demands and Registration Specialist 2's mounting workload as a result of the influx of customer complaints in September, Respondent 2 told Registration Specialist 2 in September 1994 to make updating the Form U-4 and U-5 amendments a top priority, even if it meant that he would have to work evenings and weekends, and to ignore the demands being made on him by Firm B. Towards the end of September, Respondent 2 realized that Registration Specialist 2 was not completing the amendments on a timely basis. She spoke to Registration Specialist 2 again and explained that the drafting of the amendments was a priority. Although Respondent 2 had been continuously pressuring Registration Specialist 2 over a period of approximately three weeks to make the amendments a priority, Registration Specialist 2's performance did not improve. Consequently, Respondent 2 spoke to Firm A's chief financial officer and Firm A's General Counsel, and asked them to intervene with Registration Specialist 2 to make the amendments a priority. Firm A's CFO subsequently spoke to Registration Specialist 2 and advised him that he had to make it a priority to complete the amendments to the Forms U-4 and U-5 on a timely basis, after which Registration Specialist 2's performance improved dramatically.¹⁰

During this period, Respondent 2 also realized that she needed more assistance to process the customer complaints so she attempted to hire additional staff. As discussed above, she was unable to find replacements until mid-October 1994.

¹⁰ We do not credit Registration Specialist 2's denial that while he was employed at Firm A he had never been given a written or oral reprimand or a negative evaluation about his job performance. Firm A's CFO and Firm A's General Counsel testified consistent with Respondent 2 that Respondent 2 had complained to them in September about Registration Specialist 2's performance.

After the sale of Firm A, Respondent 2 was responsible for all compliance-related duties. Specifically, her duties included the completion of the filings for the firm, the investigation of all customer complaints, the handling of all regulatory examinations and audits and inquiries, and the completion of the bank service group audits. Although she was also responsible for the updating and filing of the amendments to the Forms U-4 and U-5, she attempted to delegate much of that responsibility to Registration Specialist 2 in light of the fact that she was doing her best to address all of her other compliance-related duties with virtually no compliance staff. Registration Specialist 2, however, initially did not make the filing of the updated Forms U-4 and U-5 a priority. Even after he started amending and filing the Forms U-4 and U-5, his effort was not enough to keep up with the influx of customer complaints.

In addition, Respondent 2 was attempting to handle the work of four compliance officers and was working 12 hour days, seven days a week and commuting at least two hours every day in an effort to comply with her regulatory obligations. In determining that Respondent 2 should not be held responsible for the late filings at issue, we conclude that she did everything humanly possible to comply with her obligation promptly to file amendments to Forms U-4 and U-5 to reflect customer complaints.¹¹ It appears that had Respondent 2 put aside her other compliance duties to concentrate solely on getting the updates to the Forms U-4 and U-5 filed it is entirely likely that she would have faced compliance problems other than those at issue here.

General Defenses.¹² Respondent 1 argues that, although he was not charged with a failure to supervise, the DBCC made findings that he had failed adequately to supervise Registration Specialist 1 and Registration Specialist 2 during his tenure as compliance director. He further argues that because the complaint did not charge him with failure to supervise, he was deprived of due process because he had not prepared or presented a defense on the issue of failure to supervise. We reject these arguments. The threshold issue with respect to Respondent 1 is whether he had effectively delegated the responsibility for the timely filing of amendments to Forms U-4 and U-5 to others on the compliance staff. As discussed above, we find that Respondent 1 had not effectively delegated that responsibility. Unlike the DBCC, however, we do not reach the question of whether a delegation of the duties at issue to Registration Specialist 1 and Registration Specialist 2 would have been appropriate or whether further supervision or guidance was necessary under the facts of this case. In any event, the DBCC did

¹¹ While there may have been some problems accessing Firm A's customer complaint and registration files as a result of the due diligence review and the NASD examiner's examination, our decision to dismiss the allegations against Respondent 2 is not based on that fact.

¹² Although these defenses were offered with respect to both Respondent 2 and Respondent 1, we consider them only as to Respondent 1 in light of our dismissal of the allegations against Respondent 2.

not base its findings on a theory of failure to supervise. On the contrary, the DBCC specifically found that, because Respondent 1 and Respondent 2 had not delegated their responsibilities for the prompt filing of the amendments, they (Respondent 1 and Respondent 2) were the responsible parties with respect to the late filings.

Respondent 1 also argues that the complaint did not put him on notice as to the factual and regulatory basis for the NASD's allegations. The complaint alleged that Firm A, acting through Respondent 1 and Respondent 2, failed promptly to amend and file with the NASD Forms U-4 and U-5 to reflect customer complaints against representatives of the Firm. The Commission has held that respondents are afforded due process if the record demonstrates the respondent understood the issue and was afforded an opportunity to defend. In re Orion Securities, Inc., Exchange Act Rel. No. 35001 (Nov. 23, 1994). With respect to the instant matter, the record demonstrates that Respondent 1 understood that the DBCC had charged him with failing promptly to amend and file Forms U-4 and U-5 to reflect customer complaints. He filed a five-page answer to the complaint within a few weeks of the complaint's filing in which he claimed that he had delegated the responsibility for the filings at issue to others in the compliance department. Further, the schedule attached to the DBCC's complaint contained a list of the late filings for which Respondent 1 was responsible, including the name of the relevant registered representative, the customers' initials, and the number of days between receipt of the customer complaints and submission of the respective Forms U-4 and U-5. In addition, Respondent 1 presented testimony that attempted to show that he had delegated responsibility for the filings to compliance staff personnel. Finally, the record demonstrates that, prior to the hearing, Respondent 1 had never raised the issue that the complaint did not adequately inform him of the charges against him.

Respondent 1 argues that he was denied due process because he was not permitted to question the NASD examiner during the DBCC hearing about the basis for the DBCC's decision to hold him individually responsible, as opposed to the Firm.¹³ We agree with the argument made by Regional Counsel for District No. 8 that questions in that regard were inappropriate because the entire DBCC, and not the NASD examiner, authorized the filing of the complaint and because testimony on the issue could have revealed confidential deliberations by the DBCC. We therefore affirm the determination of the subcommittee of the DBCC that heard this matter, which refused to order the NASD examiner to respond to questions about the basis for the DBCC's decision to file the complaint.

Sanctions

The DBCC imposed a censure and a \$1,000 fine for Respondent 1's failure promptly to file amendments to Forms U-4 and U-5 to reflect customer complaints. In assessing sanctions, the DBCC cited, as mitigating factors, the turmoil that Firm A had experienced as a result of Firm B's due diligence

¹³ We note that Firm A had withdrawn as a member of the NASD in March 1995, which was well before the time that the complaint in this matter was filed.

review, including the fact that files were in a state of disarray and were missing for periods of time. While we acknowledge that there was some disruption to the compliance department during this period, we find that a majority of the customer complaints for which we have made findings of violation had been received by the Firm before Firm B had commenced its due diligence review. Thus, we do not consider the fact that Firm A's registration and compliance files were in disarray as a result of Firm B's due diligence review sufficiently mitigating to justify the imposition of such a low fine (\$1,000).

We believe that Respondent 1's fine should be increased to \$5,000 to reflect the seriousness of the violations. We therefore affirm the censure imposed by the DBCC and impose a fine of \$5,000.¹⁴ We consider the timely updating of Forms U-4 and U-5 to reflect customer complaints to be an essential function of compliance departments in light of the importance of such information to the public. Whether a registered representative has had a number of customer complaints that have resulted in settlements or disciplinary actions is information that should be available to potential investors. In assessing the fine, we also have considered that there were at least 10 instances in which the number of days between receipt of a customer complaint and submission of an amended Form U-4 or U-5 was substantial (ranging from 100 to 321 days). In addition, we find Respondent 1's practice of deferring the filing of so-called "frivolous" complaints because of his concern about defamation suits to be especially irresponsible because he was on special notice, from the Firm's prior LOC, that it is mandatory to disclose promptly customer complaints.¹⁵

¹⁴ When the complaint in this matter was filed, there was no directly applicable Sanction Guideline ("Guidelines") for the late filing of amendments to Forms U-4 and U-5. By analogy, we consulted the Guideline for late reporting of customer complaint information (to the NASD), which recommends a monetary sanction in the range of \$2,500 to \$5,000 for a fifth late filing. See Guidelines (1996 ed.) at 29. The monetary sanction recommended for a fifth late filing of customer complaint information is a useful guideline because of the numerous late filings (14) at issue in this matter.

¹⁵ Respondent 1 also testified that it was his opinion that when a customer complaint had been received by the Firm and subsequently withdrawn, it was not necessary to report the event or proceeding on Forms U-4 and U-5. That view is inconsistent with the requirements of Article IV of the NASD By-Laws, Sections 2 and 3 and with the directions contained in Forms U-4 and U-5.

Accordingly, Respondent 1 is censured, fined \$5,000, and assessed \$4,559 in DBCC costs.¹⁶ Pursuant to NASD Procedural Rule 8320, any member who fails to pay any fine, costs, or other monetary sanction imposed in this decision, after seven days' notice in writing, will summarily be suspended or expelled from membership for non-payment. Similarly, the registration of any person associated with a member who fails to pay any fine, costs, or other monetary sanction, after seven days' notice in writing, will summarily be revoked for non-payment. We dismiss the allegations against Respondent 2 and eliminate the censure, \$1,000 fine, and the \$4,559 in costs imposed by the DBCC.

On Behalf of the National Adjudicatory Council,

Joan C. Conley, Corporate Secretary

¹⁶ We have considered all of the arguments of the parties. They are rejected or sustained to the extent that they are inconsistent or in accord with the views expressed herein.