

BEFORE THE NATIONAL ADJUDICATORY COUNCIL

NASD REGULATION, INC.

In the Matter of

Department of Enforcement

Complainant,

vs.

Gordon Kerr
Walnut, CA,

Respondent.

DECISION

Complaint No. C02980051

Dated: December 17, 1999

General securities representative, who was barred from acting as a securities principal, was acting as a securities principal. Held, findings affirmed, sanctions increased to a bar in all capacities, and fine eliminated.

Gordon Kerr ("Kerr") has appealed all aspects of a July 6, 1999 decision of a Hearing Panel. After a review of the entire record in this matter, we affirm the findings of the Hearing Panel that Kerr was functioning as a securities principal while he was barred from acting in that capacity. We increase the sanctions imposed on Kerr to a bar in all capacities, and eliminate his fine.

Background

Kerr entered the securities industry in 1971. From August 1995 through July 1997, the period relevant to the complaint, Kerr was associated with and later was registered with J. Alexander Securities, Inc. ("J. Alexander Securities" or the "Firm") as a general securities representative.¹ Kerr has remained continuously associated with the Firm since 1996 and remains registered as a general securities representative.

¹ We grant the complainant's motion, dated October 21, 1999, to correct statements made at oral argument. The record is clear that the period relevant to this action was August 1995 through July 1997.

In November 1982, the Securities and Exchange Commission ("SEC") instituted an administrative proceeding against Kerr, American Western Securities, the firm at which he was an executive vice-president, and six other individual respondents. On May 23, 1983, Kerr and four other respondents settled the case with the SEC and the SEC issued an order ("SEC Order") in which it found that Kerr willfully aided and abetted violations of Sections 15(c) and 17(a) of the Exchange Act and Rules 15c2-4, 15c3-3, 17a-3, 17a-4, 17a-5, and 17a-11, promulgated thereunder. The SEC Order stated that Kerr was "barred from acting as a principal, financial principal, officer, director, owner, or employee of a broker or dealer other than as a supervised employee."² The SEC Order provided that after 14 months Kerr could apply to the SEC for permission to work in the capacity of a principal, but not in the capacity of a financial principal, and after 18 months Kerr could apply to the SEC for permission to work in the capacity of a financial principal, officer, director, or owner of a broker/dealer.

Kerr became associated with the Firm in August 1995 and registered as a general securities representative in October 1996. Kerr was hired to be the Firm's Compliance Director and, from August 1995 until July 1997, he functioned in that role.

Discussion

At the hearing of this matter before the Hearing Panel, the Department of Enforcement ("Enforcement") attempted to prove, and Kerr attempted to refute, the allegation that Kerr was functioning as a securities principal at J. Alexander Securities. There was no dispute that neither the SEC nor the NASD had approved an application from Kerr to work in a principal capacity. The parties presented evidence concerning five functions: Kerr's supervision of a registered representative; Kerr's approval of new account forms; Kerr's approval of order tickets; Kerr's review of outgoing correspondence; and Kerr's training of registered representatives. We will discuss the facts relating to each area and our conclusion about these facts separately below.

Kerr's Supervision of a Registered Representative. In February 1997, an NASD Regulation compliance examiner sent a letter to the President of J. Alexander Securities that asked a series of questions about a written customer complaint. The customer had written to the NASD that his account representative, M. Blaine Riley ("Riley"), had effected unauthorized trades in his account. The compliance examiner's letter asked who supervised Riley, a registered representative with the Firm. In March 1997, Kerr responded, on behalf of the Firm, that he was Riley's supervisor. In a second letter to Kerr in May 1997, the compliance examiner asked who was responsible for approving transactions executed by Riley and who approved the specific transactions that were the basis of the customer's complaint. Kerr responded to this letter as follows: "Gordon Kerr is responsible for supervising Mr. Riley; [the customer's] account is not a discretionary account. Gordon Kerr approved these trades as he does all trades."

²

In re Harold Junior Morris, Exchange Act Rel. No. 19805 (May 23, 1983).

At the hearing, the Enforcement attorney asked Kerr if he had ever held himself out "as a supervisor of sales representatives." Kerr denied that he had. When confronted with the statement in his letter that he supervised Riley, Kerr conceded that he had written that he was responsible for supervising Riley. In spite of his letter, Kerr testified that he was not responsible for supervising Riley. He stated that he signed the incorrect letters to NASD Regulation "for expediency reasons."

NASD Membership and Registration Rule 1021(a) requires that all persons engaged in the securities business of a member "who are to function as principals shall be registered as such with the Association in the category of registration appropriate to the function to be performed." The rule defines the functions of a principal as being "engaged in the management of the member's investment banking or securities business," including the functions of "supervision, solicitation, conduct of business or the training of persons associated with a member for any of these functions." Membership and Registration Rule 1021(b).

Based, in part, on Kerr's letters to NASD Regulation, we find that he was acting as Riley's supervisor and, therefore, acting as a principal. We find Kerr's written statements in 1997 credible because--at the time--Kerr had no motive to misrepresent the identity of Riley's supervisor. Kerr's testimony at the hearing that he was not Riley's supervisor, on the other hand, was given at a time when he had a motive to disavow his previous statements. Furthermore, Kerr's testimony that his previous, written statements to NASD Regulation were false undermines his credibility. More importantly, the Hearing Panel concluded that Kerr's written statements were "compelling evidence" that he had functioned as a principal. In addition, the Hearing Panel concluded, after considering all the evidence, that Kerr acted as a principal. The Hearing Panel's credibility determinations should be given "considerable weight" when, as happened here, the Hearing Panel observed Kerr testifying and being cross-examined and was able to observe his demeanor. See In re Christopher J. Benz, Exchange Act Release No. 38440 (Mar. 26, 1997).

Kerr's Approval of New Account Forms. Kerr testified that he signed the new account forms that the Firm used on the line that is labeled "Managing Director's/Principal's Signature." The new account forms did not show the signature of any licensed principal of the Firm. The Firm's procedures manual described the Compliance Director's responsibilities: "In the exercise of his compliance responsibilities, the Compliance Director, or his designee, shall: . . . [r]eview and approve the opening of all new accounts."³ The Firm's chief executive, James Alexander ("Alexander"), testified that from August 1995 through July 1997, Kerr was the only person working in compliance.

³ The Hearing Panel found--and we concur--that as Compliance Director, Kerr was responsible for drafting and maintaining the procedures manual. We reject Kerr's contention that the descriptions of the Compliance Director's duties in the procedures manual should be disregarded. On the contrary, we find the written descriptions of the Compliance Director's duties to be probative evidence that Kerr was acting as a principal.

The NASD's books and records rule requires, among other things, that member firms include in new customer account documents the signature of the partner, officer, or manager who accepts the account. Conduct Rule 3110(c)(1). The registration rules, in turn, provide that partners, officers, and managers of Offices of Supervisory Jurisdiction who are actively engaged in the management of a member's securities business must be registered as general securities principals. See Membership and Registration Rule 1021.

We find that Kerr was acting as a principal of the Firm when he signed new account forms during the two years alleged in the complaint.⁴ We reject Kerr's claim that he was reviewing the new account forms as a non-principal for the purpose of ensuring that the registered representatives were licensed in the appropriate states. The Hearing Panel did not credit Kerr's assertion on this point. Moreover, the Firm had no registered principal sign the new account forms; only Kerr signed them.

Kerr's Review of Order Tickets. Kerr testified that he began reviewing order tickets from the first day that he started working at the Firm. He estimated that in 1995 he reviewed approximately 200 tickets a day. During the two years at issue, he was the only Firm employee who initialed order tickets. The Firm's procedures manual stated that the Compliance Director or his designee would: "[r]eview all account transactions, including a daily review of all purchases and sales."

While Kerr admitted that he reviewed order tickets, he maintained that his review was limited to checking for the proper disclosures on the order tickets. In addition, he testified that for "a big trade, [h]e wanted to make sure the money was in." Kerr testified that Alexander, who reviewed the daily commission blotter the day after the trades, fulfilled the Firm's obligation to have a principal review the trades.

Conduct Rule 3010(d)(1) requires that member firms establish procedures for the review and endorsement by a registered general securities principal in writing, on an internal record, of all transactions. The Hearing Panel found that Kerr was performing the function of a principal when he reviewed and approved order tickets. We agree. Kerr's assertion that he was not acting as a principal is contrary to the weight of the evidence. Prior to the hearing in this case, Kerr had responded to a letter from the NASD by stating that he was responsible for approving "all trades" at the Firm. His initials on the order tickets are the only record of anyone's review at the Firm. As the SEC has emphasized "Rule 3010(d) further does not allow for the supervisory duty of review and endorsement of trade tickets to be delegated to a non-principal." In re L.H. Alton & Co., Exchange Act Rel. No. 40886, at 9 (Jan. 6, 1999). We conclude that Kerr was acting as a general securities principal when he reviewed and initialed trade tickets.

⁴ Kerr has explained that from December 1996 until March 1997 he was not working at the Firm because he was recovering from surgery. Our findings that Kerr acted as a principal are limited to the 20 months when Kerr was working for the Firm.

Kerr's Review of Outgoing Correspondence. The Hearing Panel found that Kerr was responsible for reviewing outgoing correspondence and that he was performing a principal function in doing so. We disagree. We find that a preponderance of the evidence does not support the allegation that Kerr reviewed outgoing correspondence.

At the hearing, Alexander testified that he was responsible for reviewing outgoing correspondence. Although Alexander agreed that the Firm's procedures manual identified the Compliance Director as approving outgoing correspondence, Alexander testified that he had actually been performing the review. Enforcement provided no exhibits that showed Kerr's initials on outgoing correspondence. Therefore, we make no finding that Kerr was acting as a principal when he reviewed outgoing correspondence.

Kerr's Other Activities at J. Alexander Securities. The Hearing Panel found that Kerr's training of registered representatives at the Firm did not constitute violative activity. Based on our review of the record, we uphold the Hearing Panel's conclusion because the evidence on this aspect of the case did not support a finding that Kerr was acting as a principal.

Kerr argues that he was not a principal at J. Alexander Securities because his salary was below that of a principal, he received no fringe benefits, and his bonus was not commensurate with a principal's bonus. Although these facts are undisputed, they are irrelevant. We do not find that the Firm openly acknowledged that Kerr was a principal. We conclude, however, that in several important aspects, Kerr was performing the activities of a principal. Kerr's monetary compensation and benefits are not material to these findings.⁵

Based on the evidence contained in the record, we find that Kerr acted as a general securities principal at J. Alexander Securities while not registered as a principal. Accordingly, we find that Kerr violated Article III, Section 3(b) of the NASD's By-Laws, Membership and Registration Rule 1021, and Conduct Rule 2110.

Additional Evidence in Kerr's Reply Brief. Kerr attached to his reply brief four new documents that were not part of the record before the Hearing Panel. In response, Enforcement filed a motion to preclude the introduction of Kerr's new evidence. Kerr did not submit his new evidence within 30 days of his notice of appeal and did not show good cause for failing to introduce the documents before the Hearing Panel. See Procedural Rule 9346(b). In addition, none of the new documents that Kerr submitted with his reply brief are material. Therefore, we preclude the introduction of this new evidence.

⁵ Kerr also argued that the NASD wrongly refused to allow him to reinstate his registration as a principal. We agree with the Hearing Panel, which found Kerr's argument to be irrelevant because he admitted that the SEC Order was still in effect from 1995 through 1997.

Sanctions

The Hearing Panel imposed sanctions of a \$10,000 fine, a bar as a principal, and a 45-day suspension in all capacities. In egregious cases of registration violations, the NASD Sanction Guidelines ("Guidelines") recommend that we consider suspending the individual in any or all capacities for 30 business days to two years, or consider barring the individual.⁶

The Guidelines explain that all adjudicators should consider a respondent's relevant disciplinary history in determining sanctions. We find that Kerr's 1983 settlement with the SEC is relevant because it evidenced disregard for regulatory requirements, particularly because of the serious SEC sanctions imposed on Kerr -- a limited bar with a right to reapply. Accordingly, we view Kerr's misconduct here as more serious because of his disciplinary history with the SEC.

We conclude that Kerr's misconduct in performing several functions of a general securities principal was an egregious violation of the registration rules. Not only was Kerr not qualified to act as a principal, he was barred from doing so. Kerr was fully aware that he was barred as a principal, but he took actions that evidenced the duties of a principal and he failed to ensure that a qualified principal was actually performing all activities that required registration as a general securities principal. Moreover, we find that on the issue of whether Kerr supervised Riley, Kerr fundamentally misrepresented the truth when he claimed at the Hearing Panel hearing that he was not responsible for supervising Riley. We conclude that Kerr's untruthful statements on this issue demonstrate a lack of integrity. Because Kerr's misconduct involved violating an SEC order and because of his untruthful statement made during this case, we conclude that any continued association by Kerr with a member firm would unacceptably risk future violations of the securities laws or NASD rules. We bar Kerr in all capacities in order to protect the public interest and to deter others from violating SEC orders and NASD rules.

Because we are barring Kerr, we consider the NASD's recently announced policy on imposition of monetary sanctions. See Notice To Members 99-86 (Oct. 1999). Pursuant to that policy, we eliminate any fine or costs imposed on Kerr because this case involved no sales practice violations and no customer losses.

⁶ See NASD Sanction Guidelines (1998 ed.) at 43 (Registration Violations).

Accordingly, Kerr is barred in all capacities.⁷ Pursuant to Rule 9360, the bar in all capacities shall be effective upon service of this decision.

On Behalf of the National Adjudicatory Council,

Alden S. Adkins,
Senior Vice President and General Counsel

⁷ 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.