

BEFORE THE NATIONAL ADJUDICATORY COUNCIL

NASD REGULATION, INC.

In the Matter of
the Association of

X

as a

General Securities Representative

with

The Sponsoring Firm

REDACTED DECISION

Notice Pursuant to
Section 19(d)
Securities Exchange Act
of 1934

Decision No. SD010007

On August 4, 2000, the Sponsoring Firm¹ ((or "the Firm") submitted a Membership Continuance Application ("MC-400" or "the Application") to permit X, a person subject to a statutory disqualification, to associate with the Firm as a general securities representative. In February 2001, a subcommittee ("Hearing Panel") of the Statutory Disqualification Committee of NASD Regulation, Inc. ("NASD Regulation") held a hearing on the matter. X appeared and was accompanied by the Proposed Supervisor, President and owner of the Sponsoring Firm, as well as by counsel for the Sponsoring Firm. SC and BA appeared on behalf of NASD Regulation Inc.'s Department of Member Regulation ("Member Regulation").

X's Statutorily Disqualifying Event and Background. X is subject to a statutory disqualification as the result of a 1995 final judgment by consent ("the Consent Judgment") entered against him by a United States District Court for State 1. Without admitting or denying the allegations in the complaint filed against him on the same day by the Securities and Exchange Commission ("the Commission"), X consented to a permanent injunction ("the Permanent Injunction") from future violations of Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act"), and Rule 10b-5 thereunder. The Commission's complaint alleged that from July through August 1990, X had engaged in a scheme to

1 The names of the Statutorily Disqualified individual, the Sponsoring Firm, the Proposed Supervisor, and other information deemed reasonably necessary to maintain confidentiality have been redacted.

defraud 10 brokerage firms, and caused over \$112,000 in losses on behalf of those firms,² by making purchases of stock in Company 1 (of which he was President), without the ability or intent to pay for those purchases in a full and timely manner. The complaint also alleged that X manipulated the price of Company 1 common stock, and made false statements and omissions of material facts concerning, among other things, his lack of ability or intent to pay, and his manipulation of the price of the stock. The complaint asserted that X's purpose was to support the price of the stock in an effort to affect directly the amount of financing that Company 1 would receive in a proposed loan.

X began his career in the securities industry in 1982 as a general securities representative with a member firm. In 1983, he registered with a second member firm, and then registered with a third member firm in 1988. In 1990, he became employed with a fourth firm as an insurance agent. In 1996, he joined Firm 1, an affiliate of the Sponsoring Firm, which is engaged in the business of acquiring mineral rights to properties for oil and gas exploration, drilling, and production operations in the United States. X has been employed at Firm 1 as Vice President of investor customer service, public relations, and corporate marketing. He has no other regulatory or disciplinary history.

The Sponsoring Firm's Background. The Sponsoring Firm became a member of the Association in 2000. Its main office, an Office of Supervisory Jurisdiction, is located in State 1. The Firm has one branch office in State 2. The Sponsoring Firm has two registered principals and five registered representatives. The Firm engages in sales of direct participation programs ("DPPs"), specifically, in oil and gas interests and limited partnerships for one issuer, its operating company Firm 1. At the hearing, the Proposed Supervisor represented his hope that in the future, the Firm would be able to develop deals and sell products for other issuers, as well. The Proposed Supervisor stated that this was the main reason for the creation of the Sponsoring Firm to expand beyond offering only private placements issued by Firm 1.

In 2001, NASD Regulation, Inc. ("NASD Regulation") issued a Letter of Caution ("LOC") to the Sponsoring Firm for failing to prepare and maintain an adequate blotter of checks received and forwarded, and failing to provide written notification to customers at the time of purchase regarding NASD Regulation's Public Disclosure Program. The Sponsoring Firm responded to the LOC advising NASD Regulation staff that procedures had been implemented to rectify the deficiencies.

The record does not show any other complaints, disciplinary proceedings, or arbitrations against the Firm. The Sponsoring Firm does not employ any other individuals subject to statutory disqualification, and it is not a member of any other self-regulatory organization.

² At the hearing, X stated that he had settled with those firms for various amounts and that the required payments had been made.

X's Proposed Duties and the Proposed Supervisor. The Sponsoring Firm proposes that X will be employed as a general securities representative, selling only limited partnership units offered by the Sponsoring Firm. X will be compensated with a percentage of the broker's commission received by the Sponsoring Firm on the sales he makes. He would be employed in the Firm's main office in State 1. X would also continue to be a Vice President of Firm 1.

The Sponsoring Firm proposes that the Proposed Supervisor would be responsible for supervising X. The Proposed Supervisor is the President and owner of the Sponsoring Firm. He is also Co-Chair and Co-Chief Executive Officer of Firm 1. The Proposed Supervisor passed the Series 22 examination (direct participation program representative) in 1995 and again in 2000. He passed the Series 39 examination (direct participation program principal) in 2000. The Proposed Supervisor is qualified to supervise the proposed activities of X because they are limited to direct participation program sales.

The record shows no disciplinary or regulatory proceedings, complaints, or arbitrations against the Proposed Supervisor. The Firm represents that he and X are not related by blood or marriage.

Member Regulation's Recommendation. Member Regulation recommends denial of the Sponsoring Firm's Application to employ X as a direct participation program registered representative, primarily because of the "fact that [X] was found less than six years ago, to have committed [a] serious, securities-related fraud." Member Regulation also notes that the Sponsoring Firm is a new NASD firm that has not had enough time to demonstrate that it and its registered persons have had sufficient experience to supervise a statutorily disqualified person such as X.

Discussion. After careful review of the entire record in this matter, we have determined to deny the Sponsoring Firm's Application to employ X as a registered representative. We find that it would not be in the public interest to permit him to engage in the securities business at this time and that his employment in the industry may create an unreasonable risk of harm to the market and/or investors.

In reaching this conclusion, we, like Member Regulation, note that the incident that resulted in X's statutory disqualification involved serious, securities-related misconduct. The complaint alleged that, from July 1990 through August 1990, X opened cash brokerage accounts at 10 brokerage firms and purchased 106,000 shares of Company 1 common stock in at least 13 transactions in those accounts. The complaint alleged that X made these purchases to support the price of Company 1 common stock, in an effort to affect the amount of financing Company 1 would receive under a proposed loan. X's purchases of the Company 1 stock caused its price to increase from \$1.16 to \$3.35 per share. The complaint further alleged that X made the purchases without either the ability or the intent to pay fully and timely for the stock. Moreover, in connection with the Company 1 purchases, X made untrue statements of material facts and omitted to state material facts to the 10 brokerage firms regarding his manipulation of the price of Company 1 common stock, his intention to support the price of Company 1 common

stock for the purpose of affecting the amount of the proposed loan, his intentions with respect to the delivery of funds to the brokerage firms, and his lack of ability to pay timely and fully for the Company 1 stock. As a result of X's activities, six of the 10 brokerage firms incurred losses totaling approximately \$112,000 from unsecured debit balances in his cash accounts.

X's activities demonstrate a willful disregard for important industry rules, cast doubt on his character, and lead us to question his ability to act in a trustworthy and responsible manner in interactions with the investing public.

We are also very troubled by X's failure to disclose the Consent Judgment on the 2000 Uniform Application for Securities Industry Registration or Transfer ("Form U-4") that he filed with the Sponsoring Firm. At the hearing, X stated that he was "under the impression" that he needed to disclose only events that had occurred within the last five years, but that he did not recall who had told him that.³

Finally, we also share Member Regulation's concern as to the inexperience of the Sponsoring Firm. The Firm is less than one year old, and it has not had sufficient time to demonstrate that it has the ability to supervise a statutorily disqualified person, especially someone like X, who was found to have engaged in serious, securities-related misconduct.

Based on the above, we conclude that it is not in the public interest to allow X to participate in the securities industry through association with the Sponsoring Firm in the capacity of a direct participation program securities representative. Accordingly, the Sponsoring Firm's Application is denied.

On Behalf of the National Adjudicatory Council,

Barbara Z. Sweeney
Senior Vice President and Corporate Secretary

³ The Consent Judgment was entered in 1995, within five years of the May 2000 filing of the Form U-5. In making the statement about his impression with respect to a five-year limit, we assume that X was referring to the underlying activities that led to the Consent Judgment, which activities had occurred between July and August 1990. In any event, X was incorrect, and we find his failure to report accurately on the Form U-4 to be another indication of untrustworthiness and his inability to function with integrity in the securities industry.