

BEFORE THE NATIONAL ADJUDICATORY COUNCIL
NASD

<p>In the Matter of the Association of X¹ as a General Securities Representative with The Sponsoring Firm²</p>	<p style="text-align: right;">Redacted Decision</p> <p><u>Notice Pursuant to</u> <u>Rule 19h-1</u> <u>Securities Exchange Act</u> <u>of 1934</u></p> <p><u>Decision No. SD06006</u></p> <p>Date: 2006</p>
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I. Introduction

On September 27, 2005, the Sponsoring Firm (“the Firm”) filed a Membership Continuance Application (“MC-400” or “the Application”) with NASD’s Department of Registration and Disclosure, seeking to permit X, a person subject to a statutory disqualification, to associate with the Firm as a general securities representative. A hearing was not held in this matter. Rather, pursuant to NASD Procedural Rule 9523, NASD’s Department of Member Regulation (“Member Regulation”) recommended that the Chair of the Statutory Disqualification Committee, acting on behalf of the National Adjudicatory Council, approve X’s proposed association with the Sponsoring Firm pursuant to the terms and conditions set forth below.

For the reasons explained below, we approve the Sponsoring Firm’s Application.

II. The Statutorily Disqualifying Event

X is statutorily disqualified because he pled guilty in October 1998, to possession of marijuana, a felony in State 1. A state court judge sentenced X to two years’ probation and 60

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.

² The Sponsoring Firm was formerly known as Firm A. It filed an amended Form BD in March 2006, to change its name.

days in the county jail;³ revoked his driving privileges for six months; and ordered him to undergo urine monitoring and complete a substance abuse evaluation program.

III. Background Information

A. X

X first registered in the securities industry as a general securities representative (Series 7) in October 1996. He requalified as a Series 7 on July 20, 2005. He also passed the uniform securities agent state law examination (Series 63) in February 1997 and qualified as a general securities principal (Series 24) in February 2002.

X was previously employed by Firm One from January 2002 until March 2002, and by Firm Two from January 1998 until October 2001.

X's background includes two other regulatory incidents. In April 1995, he was charged in State 2 with a misdemeanor for personal use of marijuana, criminal/defiant trespass, and disorderly conduct. In November 1995, a State 2 court accepted that case for accelerated rehabilitative disposition and placed X on probation for six months.⁴

In 2002, NASD's Department of Enforcement ("Enforcement") conducted an investigation to determine whether X had failed to disclose his 1998 felony conviction while he was employed in the securities industry by Firms One and Two.⁵ This investigation led to Enforcement's issuance of a Letter of Caution ("LOC") to X in 2002.⁶ In addition, as a result of this investigation, X voluntarily resigned from Firm Two in March 2002. X was employed in the real estate industry from March 2002 until he filed this Application to become employed by the Sponsoring Firm.

B. The Firm

³ X served two days of this sentence in jail and the remainder in a work release program.

⁴ X is not required to disclose this misdemeanor event on a Uniform Application for Securities Industry Registration or Transfer ("Form U4"). NASD's Central Registration Depository ("CRD"[®]) maintains such information for historical purposes only.

⁵ NASD's investigation was triggered by X's filing of a Form U4 when he attempted to transfer his registration from Firm One to Firm Two in January 2002.

⁶ The LOC specifically stated that it would not be included in CRD and that X need not report it on a Form U4. The LOC also stated, however, that "in accordance with long-standing NASD practice, it will be taken into consideration in determining any future matter should violations occur."

The Sponsoring Firm became an NASD member in December 2004. The Firm has no offices of supervisory jurisdiction and no branch offices. As of the fourth quarter of 2005, the Sponsoring Firm employed nine individuals, three of whom are registered principals, and four of whom are registered representatives. The Firm is a full-service broker-dealer that clears through Firm B.

NASD conducted a routine examination of the Sponsoring Firm for 2005 and filed it without action.

The record shows no customer complaints, regulatory proceedings, or arbitrations against the Firm.

IV. X's Proposed Business Activities and Supervision

The Firm proposes to employ X as a general securities representative in its home office in State 3. The Sponsoring Firm will compensate X by "commissioned payout on gross commissions generated."

The Sponsoring Firm proposes that the Proposed Supervisor will be X's primary, responsible supervisor. The Proposed Supervisor has been employed by the Sponsoring Firm since April 2004 and is the Firm's Chief Executive Officer, Chief Financial Officer, and Chief Compliance Officer. He has been employed in the securities industry since 1988, becoming registered as a general securities representative in February 1992, a general securities principal in October 1995, and a financial and operations principal in May 1996.

The Proposed Supervisor has no disciplinary or regulatory proceedings, complaints, or arbitrations against him.

V. Member Regulation's Recommendation

Member Regulation recommends that the Application be approved, subject to the specified terms and conditions of heightened supervision over X set forth below.

VI. Discussion

After carefully reviewing the entire record in this matter, we approve the Firm's Application to employ X as a general securities representative, subject to the supervisory terms and conditions set forth below.

In reviewing this type of application, we have considered whether the particular felony at issue, examined in light of the circumstances related to the felony, and other relevant facts and

circumstances, creates an unreasonable risk of harm to the market or investors.⁷ We assess the totality of the circumstances in reaching a judgment about X's future ability to deal with the public in a manner that comports with NASD's requirements for high standards of commercial honor and just and equitable principles of trade in the conduct of his business.

For the reasons set forth below, we conclude that X's participation in the securities industry will not present an unreasonable risk of harm to the market or investors.

We acknowledge the seriousness of X's criminal conviction. We note, however, that his felony conviction occurred in 1998, more than seven years ago, and that he has not committed any intervening criminal misconduct. We also recognize that X has been punished for his felony offense by a State 1 court, which imposed a prison sentence and placed him on probation for two years. X completed his sentence through a work release program and his probation was terminated in December 2000. X also completed the required substance abuse evaluation. Moreover, X has been employed in the securities industry at various times since 1996 and has an unblemished regulatory record.

Further, we acknowledge that X, as a registered representative, was responsible for knowing the rules of the securities industry and for providing information about his 1998 felony charge and conviction to Firm One on a timely basis to update his Form U4. *See e.g. Robert E. Kauffman*, 51 S.E.C. 838, 840 (1993), *aff'd*, 40 F.3d 1240 (3d Cir. 1994) (table) "Every person submitting registration documents [to NASD] has the obligation to ensure that the information printed therein is true and accurate."). We note, however, that X has consistently maintained that he provided timely oral notice to Firm One of the 1998 criminal matter and that X's contention is corroborated in the record by an affidavit from Employee 1, who was a principal at Firm One during X's employment. Employee 1 states that X provided Firm One with "copies of his court paperwork evidencing his disposition the day following his conviction." Employee 1 also states that the Firm processed this information and provided it to NASD. According to Employee 1, NASD did not inform Firm One that X was statutorily disqualified and instead suggested that Firm One place him on heightened supervision. Thus, the record shows that X provided full disclosure orally to Firm One at the time of the felony event and did not attempt to conceal his criminal record.⁸

X's failure to amend his Form U4 to disclose the felony charge and conviction to Firm

⁷ *See Frank Kufrovich*, Exchange Act Rel. No. 45437, 2002 SEC LEXIS 357, at *16 (Feb. 13, 2002) (upholding NASD's denial of a statutory disqualification applicant who had committed non-securities related felonies "based upon the totality of the circumstances" and NASD's explanation of the bases for its conclusion that the applicant would present an unreasonable risk of harm to the market or investors).

⁸ Further evidence of Firm One's understanding of X's legal situation during the time in question is provided in Employee 1's statement in the affidavit that he provided a character letter on behalf of X in connection with the sentencing proceeding in December 1998.

One has also previously been addressed by Enforcement. In its investigation of the matter with X, Enforcement had a choice as to whether it would proceed against him for a willful violation, or a non-willful violation. The distinction between a willful and non-willful failure to disclose is critical because a willful failure results in a separate, lifetime statutory disqualification under the Securities Exchange Act of 1934 and the NASD By-Laws.⁹ Enforcement evaluated all of the circumstances regarding X's failure to disclose and determined that his violation was non-willful, thereby resulting in an LOC rather than a formal disciplinary action. Enforcement noted X's arguments that he was not aware that his conviction was a felony when it occurred in 1998, and that he relied upon the advice of his counsel¹⁰ and Firm One in determining that he was not required to disclose it on his Form U4.

The proposed supervisor is well qualified and has worked in the securities industry since 1988 with no disciplinary history. As for the Firm, although it is a relatively new member of NASD, we find that its short tenure will not negatively affect its ability to supervise X. The Firm has agreed to a comprehensive supervisory plan to ensure that it will be able to maintain future compliance with the plan of heightened supervision for X.

In sum, given the nature of X's felony offense, his lack of willful intent to conceal it from his employers, and the fact that he previously has been successfully employed in the securities industry, we conclude that the following supervisory conditions agreed to by the Sponsoring Firm will provide the enhanced compliance measures necessary to monitor X's activities:¹¹

1. The Sponsoring Firm will amend its written supervisory procedures to state that the Proposed Supervisor is the primary supervisor responsible for X. When the Proposed Supervisor is out of the office, Employee 2, another principal on-site, will perform the necessary review for the Proposed Supervisor, and when the

⁹ Art. III, Sec. 4(f) of NASD's By-Laws provides that a person is subject to a statutory disqualification if that person: "has willfully made or caused to be made in any application . . . to become associated with a member of a self-regulatory organization, . . . any statement which was at the time, and in light of the circumstances under which it was made, false or misleading with respect to any material fact, or has omitted to state in any such application . . . any material fact which is required to be stated therein."

The language of NASD's By-Laws tracks the language of Sections 15(b)(4) and 3(a)(39) of the Exchange Act.

¹⁰ X's argument that he relied on the advice of his counsel is further corroborated in this Application by a November 2005 letter from his current counsel, stating that X was erroneously advised by his former counsel that the 1998 conviction for possession of marijuana was not a felony and did not have to be disclosed on the Form U4.

¹¹ The items denoted by an asterisk are heightened supervisory conditions and not standard operating procedures of the Firm.

Proposed Supervisor returns to the office, he will complete his review in a timely fashion and evidence his review by counter-signing the documents;

2. *X will not maintain discretionary accounts;
3. *X will not act in a supervisory capacity;
4. The Proposed Supervisor will supervise X on-site;
5. All of X's customer orders will be introduced to the Firm's clearing agent on a fully disclosed basis;
6. The Proposed Supervisor will review all of X's securities transactions on a daily basis;¹²
7. The Proposed Supervisor will review all of X's new account forms on a weekly basis and will evidence his review by signing the forms;
8. *The Proposed Supervisor will review all of X's placed orders, whether executed or still opened, on a daily basis. The Proposed Supervisor will evidence his review by initialing a printout of the Firm's "daily order Inquiry" screen from its clearing firm, Firm B's, order entry system;
9. *All complaints pertaining to X, whether oral or written, will be immediately referred to the Proposed Supervisor for review, and then to the Compliance Department. The Proposed Supervisor will prepare a memorandum to the file as to what measures he took to investigate the merits of the complaint (e.g., contact with the customer) and the resolution of the matter. The Proposed Supervisor will keep all documents pertaining to these complaints segregated for ease of review;
10. *For the duration of X's statutory disqualification, the Sponsoring Firm must obtain prior approval from Member Regulation if it wishes to change X's responsible supervisor from the Proposed Supervisor to another person; and
11. *The Proposed Supervisor must certify quarterly (March 31st, June 30th, September 30th, and December 31st) to the Firm that X and the Proposed

¹² The Firm's MC-400 Application represents that the daily reviews will include order tickets (or a computerized run of transactions); trade confirmations; correspondence; advertising; new accounts and related documentation ensuring that the documentation is submitted for signing within three business days of the opening of an account; customer complaints; extension of time requests; sell-outs and/or buy-ins; prepayments; trade re-billings; error reports; and renegees.

Supervisor are in compliance with all of the above conditions of heightened supervision.

NASD certifies that: 1) X meets all applicable requirements for the proposed employment; 2) the Firm is not a member of any other self-regulatory organization; 3) the Firm has represented that the Proposed Supervisor and X are not related by blood or marriage; and 4) the Firm currently employs no other statutorily disqualified individuals.

Accordingly, we approve the Sponsoring Firm's Application to employ X as a general securities representative. In conformity with the provisions of SEC Rule 19h-1, the association of X as a general securities representative with the Firm will become effective within 30 days of the receipt of this notice by the Commission, unless otherwise notified by the Commission.

On Behalf of the National Adjudicatory Council,

Barbara Z. Sweeney
Senior Vice President and Corporate Secretary