

BEFORE THE NATIONAL ADJUDICATORY COUNCIL

NASD

In the Matter of the Continued Association of  X  as a  Supervising General Securities Principal (without heightened supervision)  with  The Sponsoring Firm. <sup>1</sup>	<u>Redacted Decision</u>  <u>Notice Pursuant to</u> <u>Rule 19h-1</u> <u>Securities Exchange Act</u> <u>of 1934</u>  <u>SD06007</u>  Date: 2006
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**I. Introduction**

In June 2005, the Sponsoring Firm<sup>2</sup> completed a Membership Continuance Application (“MC-400” or “the Application”), seeking to permit X, a person subject to a statutory disqualification, to associate with the Sponsoring Firm as a supervising general securities principal, without heightened supervision. 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 continued association with the Sponsoring Firm.

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

**II. The Statutorily Disqualifying Event**

X is statutorily disqualified because on May 20, 1993, the Securities and Exchange Commission entered an administrative order (“SEC Order”) against him that barred him from association in a supervisory capacity for three years. The Order also provided that after three years, X could apply to become associated in a supervisory capacity other than that of

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<sup>1</sup> The Sponsoring Firm was formerly known as Firm 1.

<sup>2</sup> 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.

chairperson, chief executive officer, or president. The SEC Order stemmed from X's failure to reasonably supervise Employee 1 from 1985 until 1986, while X was CEO of Firm 2. [CASE REDACTED] Employee 1 was formerly the manager of Firm 2's high yield and convertible bond department and he was found to have engaged in manipulative trading and caused misrepresentations in connection with 18 new issues of securities that Firm 2 underwrote and distributed.<sup>3</sup>

X is also statutorily disqualified because the New York Stock Exchange conducted a disciplinary action against him based on the same underlying misconduct. In October 1991, the NYSE issued a decision that barred X from association in any supervisory or controlling ownership capacity for two years ("NYSE Decision").

### III. Background Information

#### A. X's Background and Prior SEC Rule 19h-1 Notices

X first registered in the securities industry as a general securities representative (Series 7)<sup>4</sup> in February 1964. He subsequently qualified as a general securities principal (Series 24)<sup>5</sup> in June 1968 and as a uniform securities agent state law (Series 63) in May 1994.

Firm 2 employed X from January 1977 until December 1991. From December 1991 to December 1993, X was self-employed as a consultant. From December 1993 until July 1996, X was registered as a general securities representative with Firm 3. In 1996, Firm 4 acquired Firm 3 and X was associated with Firm 4 as a general securities representative.

In December 1996, Firm 4 submitted an MC-400 application seeking approval for X to continue to associate with Firm 4, but in the capacity of a general securities principal. In June 1997, NASD filed a notice pursuant to SEC Rule 19h-1 for approval of Firm 4's application. While the Commission was still reviewing NASD's June 1997 Rule 19h-1 notice, however, X voluntarily terminated his employment with Firm 4 in 1998 to join Firm 5, an NYSE member firm. NASD therefore withdrew the June 1997 Rule 19h-1 notice regarding Firm 4.

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<sup>3</sup> The activities of Employee 1 and other Firm 2 employees led to the institution of numerous civil enforcement actions and criminal proceedings. As a result of some of these proceedings, Employee 1 was convicted in 1990 of criminal violations involving securities transactions. [CASE REDACTED]. The Commission also barred Employee 1 from association in the securities industry in all capacities in 1991. [CASE REDACTED].

<sup>4</sup> The general securities representative qualification examination, now known as the Series 7, was formerly known as the Series 1.

<sup>5</sup> X requalified as a general securities principal in October 1996.

Firm 5 filed an application with the NYSE, requesting approval for X to act in a supervisory capacity with responsibility for directing and overseeing investment banking professionals working on corporate finance and investment banking matters. In July 1999, following a concurrence by NASD, the NYSE filed a notice pursuant to SEC Rule 19h-1 recommending approval. In January 2000, the Commission issued an order approving X to be associated in a supervisory capacity with Firm 5.

In May 2001, X joined Firm 1. In December 2001, NASD filed a notice pursuant to SEC Rule 19h-1, recommending approval of X's association with Firm 1 as a supervising general securities principal. The SEC issued an order in April 2002, approving X's association with Firm 1 in this capacity. Pursuant to the SEC's April 2002 order, the Sponsoring Firm has since supervised X in accordance with the following representations that it made to the Commission:

1. X has not been the subject of any disciplinary action since the Commission's May 1993 Order. X has also complied fully with the terms of the May 1993 Order;
2. X will function at the Sponsoring Firm in a supervisory capacity, directing and overseeing investment-banking professionals, and he will report to Proposed Supervisor 1 and Proposed Supervisor 2. He will be a Managing Director of the Sponsoring Firm, but not CEO, President or Chairperson. X will act as Co-Head of the Sponsoring Firm's Corporate Finance Department with Employee 2, a Managing Director of the Sponsoring Firm. X will work out of the City 1, State 1 office of the Sponsoring Firm while Employee 2 will work out of the City 2, State 2 office of the Sponsoring Firm;
3. Proposed Supervisor 1 will be the primary supervisor for X, and will be assisted in his supervision of X by Proposed Supervisor 2. Both Proposed Supervisor 1 and Proposed Supervisor 2 are Managing Directors at the Sponsoring Firm, and both work out of the Sponsoring Firm's City 1 office;
4. X will not handle securities accounts for retail or institutional clients, or supervise individuals who are handling such accounts. X will not conduct proprietary trading on behalf of the Sponsoring Firm, or supervise individuals who are conducting such trading;
5. Upon assuming a supervisory role, X will meet in person with Proposed Supervisor 1 and Proposed Supervisor 2 to review the Sponsoring Firm's supervisory policies and procedures and X's duties and responsibilities relating to those policies and procedures. A written record of this meeting will be maintained;
6. Proposed Supervisor 1 will oversee the day-to-day performance of X's supervisory responsibilities. Proposed Supervisor 1 acknowledges that he, as X's primary supervisor, is ultimately responsible for the supervision of X. Proposed Supervisor 2 will assist when Proposed Supervisor 1 is out of town or unavailable;

7. On a weekly basis, Proposed Supervisor 1 will speak with X to discuss any business or compliance-related issues that have arisen in the course of X performing his supervisory duties. A written record of these meetings will be maintained;
8. On a quarterly basis, Proposed Supervisor 1 will meet with X to review more extensively the matters over which X functions in a supervisory capacity and any business- or compliance-related issues that arise in the course of X performing his supervisory duties. A written record of these meetings will be maintained;
9. X will not assume any of the duties of the positions of Chairman, Chief Executive Officer, or President of the Sponsoring Firm. X may, however, participate in the the Sponsoring Firm management team, if any, which oversees the City 1 operations of the Sponsoring Firm. Absent extraordinary circumstances, Proposed Supervisor 1 and/or Proposed Supervisor 2 will be present for the management team meetings, telephone conferences, and other such events in which X participates. If X becomes a member of the management team, Proposed Supervisor 1 will review X's performance in that function with him at the same time that they discuss X's performance of his other supervisory duties;
10. X's current ownership in Company 1, the sole shareholder of the Sponsoring Firm stock, consists of a direct 4.36% interest and a 1.77% interest held in X's IRA Account (combined 6.13%) and does not currently represent a controlling interest in Company 1. X does not and will not own any stock in the Sponsoring Firm. X's IRA and non-IRA ownership interest in Company 1 will increase slowly during the next six months to one year, but this increase will not exceed 10% of the outstanding stock of Company 1. Any increase in X's ownership interest in the Sponsoring Firm will only occur through an increase in his holdings of stock in Company 1. Moreover, X's ownership interest will not be increased in the future to represent a controlling interest in Company 1;
11. The Sponsoring Firm will continue this supervisory plan until it applies to the NASD for approval of a modified supervisory structure, including any proposed increase in X's ownership interest above 10% in Company 1, and the Commission issues an order consistent with that request;
12. X will not make subordinated loans to the Sponsoring Firm;
13. The proposed supervisors for X, Proposed Supervisor 1 and Proposed Supervisor 2, have no disciplinary history and are not related to X; and
14. X meets all applicable requirements for the proposed employment.

## B. The Sponsoring Firm

The Sponsoring Firm became a member of NASD in November 1982. The Sponsoring Firm engages in a general securities business, has six offices of supervisory jurisdiction (“OSJs”) and six branch offices, and employs 25 registered principals and 86 registered representatives.

The Sponsoring Firm represents that X has contributed capital to Company 2. (Company 2, f/k/a Company 1), the Sponsoring Firm’s parent company. The Sponsoring Firm further represents that it has treated the capital invested by X as equity and that X’s current holdings comprise less than a 6% equity interest in Company 2.

NASD conducted routine examinations of the Sponsoring Firm in 2002 and 2004. Following the 2002 examination, NASD issued the Sponsoring Firm a Letter of Caution (“LOC”) for inaccurate reporting of transactions in Nasdaq National Market securities. The Sponsoring Firm responded to the LOC in a letter dated March 2003, stating that it had corrected the deficiencies.

NASD issued the Sponsoring Firm a citation for a Minor Rule Violation (“MRV”) following the 2004 examination. The MRV fined the Sponsoring Firm \$2,500 for order ticket inaccuracies.

Additionally, in 2005 NASD conducted an options examination of the Sponsoring Firm and issued it an LOC for written supervisory procedure violations and inaccurate options disclosure documentation. The Sponsoring Firm responded in a letter dated June 2005, stating that it had corrected the deficiencies.

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

## **IV. X’s Proposed Business Activities and Supervision**

The Sponsoring Firm proposes that X will continue to act as Co-Head of Corporate Finance in the Sponsoring Firm’s home office, located on Street 1, City 1. The Sponsoring Firm represents that, in accordance with the 1993 SEC Order, it will not permit X to become the Sponsoring Firm’s Chairman, CEO, or President. The Sponsoring Firm will compensate X by a salary and a discretionary bonus.

The Sponsoring Firm also proposes that Proposed Supervisor 1 and Proposed Supervisor 2 will continue to supervise X pursuant to the Sponsoring Firm’s standard supervisory procedures. Proposed Supervisor 1 is the Sponsoring Firm’s Vice Chairman and has been employed by the Sponsoring Firm since May 2001. He has been a general securities principal (Series 24) since November 1985.

Proposed Supervisor 2 is the Sponsoring Firm’s Chairman and has been employed with the Sponsoring Firm since August 1982. He has been registered as a general securities

representative since December 1958 and was grandfathered as a general securities principal in January 1968.

NASD's Central Registration Depository ("CRD"<sup>®</sup>) shows no disciplinary or regulatory proceedings, complaints, or arbitrations against Proposed Supervisor 1 or Proposed Supervisor 2.

## **V. Member Regulation's Recommendation**

Member Regulation recommends approval of the Sponsoring Firm's request to be relieved of the continuing special supervisory procedures for X.

## **VI. Discussion**

After carefully reviewing the entire record in this matter, we approve the Sponsoring Firm's Application to continue to employ X as a supervising general securities principal, without having to observe the special supervisory procedures that were imposed on the Sponsoring Firm in the SEC's April 2002 Order, approving X's initial association with the Sponsoring Firm.

In reaching this determination, we have considered that the underlying activity that led to X's statutorily disqualifying event occurred more than 20 years ago and that the NYSE and SEC Orders that imposed qualified bars on X were entered more than 10 years ago. The time periods contained in those qualified bars have expired, and we are not aware of any intervening misconduct by X.

X re-entered the securities industry in 1993 as a general securities representative. Thereafter, the SEC approved X's re-entry as a supervisor with Firm 5 in January 2000, and as a supervising general securities principal with the Sponsoring Firm in April 2002. CRD shows no reportable incidents for X during this time. Moreover, NASD has conducted numerous statutory disqualification examinations of X and has filed satisfactory reports in all instances.

We have also considered that X will continue to report to Proposed Supervisor 1 and Proposed Supervisor 2, who have successfully supervised X since 2002. Proposed Supervisor 1 and Proposed Supervisor 2 have been in the securities industry for 39 years and 49 years, respectively, and both have no disciplinary history.

Given the standard supervisory procedures in place at the Sponsoring Firm, we conclude that X will be effectively supervised without continuing to impose a heightened plan of supervision.

For these reasons, we conclude that the public interest will not be harmed by X continuing to associate with the Sponsoring Firm as a supervising general securities principal without special supervision.

NASD certifies that: 1) X meets all applicable requirements for the proposed employment; 2) the Sponsoring Firm is a member of the Pacific Stock Exchange, which, in

accordance with regulatory practices, will be sent a copy of this notice; 3) the Sponsoring Firm represents that X, Proposed Supervisor 1, and Proposed Supervisor 2 are not related by blood or marriage; and 4) the Sponsoring Firm does not employ any other statutorily disqualified individuals.

Accordingly, in conformity with the provisions of SEC Rule 19h-1, the continued association of X with the Sponsoring Firm as a supervising general securities principal, without special supervisory procedures, will become effective upon the issuance of an order by the Commission that it will not institute proceedings pursuant to Section 15(b) of the Exchange Act and that it will not direct otherwise pursuant to Section 15A(g)(2) of the Exchange Act. This notice shall serve as an application for such an order.

On Behalf of the National Adjudicatory Council,

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Barbara Z. Sweeney  
Senior Vice President and Corporate Secretary