BEFORE THE NATIONAL ADJUDICATORY COUNCIL

FINANCIAL INDUSTRY REGULATORY AUTHORITY

In the Matter of Department of Enforcement, Complainant, vs. Jonathan M. Skiba Frankenmuth, MI, Respondent.	DECISION Complaint No. E8A2004072203 Dated: April 23, 2010

Respondent submitted false and misleading variable annuity applications to his firm and circumvented his firm's variable annuity procedures. Held, findings and sanctions affirmed.

Appearances

For the Complainant: Leo Orenstein, Esq., and Richard S. Schultz, Esq., Department of Enforcement, Financial Industry Regulatory Authority

For the Respondent: Pro Se

Decision

The review subcommittee of FINRA's National Adjudicatory Council ("Review Subcommittee") called this matter for review pursuant to NASD Rule 9312 to examine the sanctions imposed by the Hearing Panel.[1] The Hearing Panel found that Jonathan Skiba

[1] Following the consolidation of NASD and the member regulation, enforcement and arbitration functions of NYSE Regulation into FINRA, FINRA began developing a new "Consolidated Rulebook" of FINRA Rules. The first phase of the new consolidated rules became effective on December 15, 2008. *See FINRA Regulatory Notice 08-57* (Oct. 2008). Because the complaint in this case was filed before December 15, 2008, the procedural rules that

[Footnote continued on next page]

("Skiba") submitted inaccurate variable annuity applications to his firm and failed to submit variable annuity replacement forms to his firm as required by the firm's procedures. For this misconduct, the Hearing Panel fined Skiba $5,000, suspended him in all capacities for one year, and ordered him to pay $14,909.49 in restitution. After a de novo review of the record, we affirm the Hearing Panel's findings of violations and the sanctions imposed.

I. Background

Skiba entered the securities industry in July 1992 as an investment company products and variable contracts limited representative with AXA Advisors, LLC ("AXA Advisors" or "the Firm"). He was terminated from AXA Advisors in May 2005 for making inconsistent statements in connection with the Firm's investigation of replacements of variable annuity contracts. Skiba was registered as an investment company products and variable contracts limited representative with another FINRA member from May 2005 through July 2009. Skiba is not presently registered with a FINRA member firm.

II. Facts

A. Skiba Includes False Answers on Customer Variable Annuity Applications

In 2003, Skiba recommended to four customers (two married couples, RR and MR, and LV and VV) that they replace their existing variable annuity contracts with a new variable annuity contract that he considered to be a better product for his customers. The customers agreed to the replacement transactions. Skiba stated at the hearing that he "went around the [Firm's supervisory] system" applicable to variable annuity replacements by transferring the customers' Equi-Vest variable annuity funds[2] to a Franklin Templeton money market mutual fund ("Franklin Templeton Fund")[3] prior to investing the customers' funds in an Accumulator Plus variable annuity.[4] The customers' funds were held in the Franklin Templeton Fund between

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apply are those that existed on December 14, 2008. The conduct rules that apply are those that existed at the time of the conduct at issue.

2 The Equi-Vest variable annuity was issued by The Equitable Life Assurance Society of the United States ("Equitable"), a Firm affiliate.

3 The Franklin Templeton IRA Transfer Request form included RR's initials approving a change in the amount of funds RR would be transferring to the Franklin Templeton Fund from 100 percent to 99 percent. RR testified that he decided upon the change so that he could maintain the $75,000 life insurance policy he had through his Equi-Vest variable annuity. He denied, however, that he had signed his initials onto the document. Skiba eventually admitted that he had written RR's initials on the document, but only after refuting that fact several times earlier in the hearing.

4 The Accumulator Plus variable annuity was another Equitable investment product.

11 to 26 business days, after which the funds were used to purchase shares for their accounts in an Accumulator Plus variable annuity. Skiba testified that he structured the transactions in this manner because he believed the Firm would not permit a transfer from an Equi-Vest to an Accumulator Plus product and considered the replacements to be in the "best interest" of his customers.

The parties stipulated that RR, MR, LV, and VV incurred surrender charges associated with the sales of their Equi-Vest variable annuities.[5] Skiba testified that he orally advised his customers "[a]t the point of sale" about any surrender charges associated with the sales of their Equi-Vest variable annuities. RR testified, however, that Skiba did not advise him that he would be charged $11,958.70 for selling the Equi-Vest variable annuity, and that he did not learn of the charge until 2008, more than four years after this occurred.[6] RR stated that he thought there was a minimal charge of "less than $1,000 or so," associated with that transaction, and that he would not have sold the Equi-Vest variable annuity had he been aware of the surrender charge. MR testified that she was aware there would be a surrender charge, but that with "what we were supposed to gain [from the Accumulator Plus variable annuity] it would be worth the minimal surrender charge." MR testified that she believed the charge associated with surrendering her Equi-Vest variable annuity would be about $2,000. The actual surrender charge was $2,950.79 on the sale of MR's Equi-Vest variable annuity. Customers LV and VV incurred surrender charges of $6,838.52 and $911.86, respectively, on the sale of their Equi-Vest variable annuities.

In completing the Accumulator Plus variable annuity applications that he submitted to his Firm for customers RR, MR, LV, and VV, Skiba checked "No" to the following questions:

> Will any existing life insurance or annuity be (or has it been) surrendered, withdrawn from, loaned against, changed or otherwise reduced in value, or replaced in connection with this transaction assuming the certificate/contract applied for will be issued?
>
> Do you have reason to believe that any existing life insurance or annuity has been or will be surrendered, withdrawn from, loaned against, changed or otherwise reduced in value, or replaced in connection with the transaction, assuming the certificate/contract applied for will be issued on the life of Annuitant?

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[5] The parties also stipulated that RR and MR received "credit[s]" of $11,093.96 and $2,745.64, respectively, in their Accumulator Plus variable annuity accounts for purchasing that product. The amount of the credit depended upon the level of funds contributed to Accumulator Plus variable annuity contracts. There is no information in the record about any specific amounts of credits that LV and VV might have received in their Accumulator Plus variable annuity accounts.

[6] Customers RR and MR testified at the hearing by telephone. Customers LV and VV did not testify at the hearing.

Skiba admitted at the hearing that his negative responses on the applications were false because he knew the Equi-Vest variable annuity proceeds would be used to purchase shares in an Accumulator Plus variable annuity for each customer.

B. Skiba Circumvents Firm Procedures

In 2003, AXA Advisors' compliance manual stated that a "Replacement Sale" occurred when there was "a purchase of a new . . . annuity contract [and] it was known or should have been known to the [r]epresentative that, by reason of the new purchase, an existing insurance policy or annuity contract has been or will be affected," such as when a contract is surrendered in whole or in part. Skiba received a copy of the compliance manual on February 3, 2003, and acknowledged during the hearing that it defined a "Replacement Sale." The parties stipulated that AXA Advisors' representatives were required to send a fully completed Replacement Acknowledgement Form, signed by the applicant and the representative, to their branch office for suitability review and approval. The Replacement Acknowledgement Form disclosed the amount of any surrender charge that the customer incurred on the replacement of an existing variable annuity policy. Skiba's supervisor testified that he never received any Replacement Acknowledgement Forms from Skiba with respect to the transactions at issue.

Susan Ford ("Ford"), a product manager with AXA Advisors, testified that the Firm permitted customers to sell an Equi-Vest variable annuity and purchase an Accumulator Plus variable annuity even if there was a surrender charge on the sale of the Equi-Vest variable annuity, but that the registered representative would not receive a commission on the replacement transaction. In such cases, in addition to the Replacement Acknowledgement Form that required a supervisor's and customer's signatures, the Firm required the customer to sign a surrender letter acknowledging receipt of written disclosures related to the financial consequences of replacing the Equi-Vest variable annuity with the Accumulator Plus variable annuity. The surrender letter warned the customer that the Firm believed the transfer might not be in the customer's best interests. Ford testified that the Firm included such cautionary language because the customer was incurring a surrender charge for withdrawing funds from the Equi-Vest variable annuity and incurring higher fees for the Accumulator Plus variable annuity.[7]

RR testified that he relied on Skiba to assist him and his wife to invest in products that were best for them. Neither RR, a retired sales marketing manager, nor MR, a retired high

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[7] The surrender letter specifically disclosed that: (1) there would be a surrender charge on the sale of the Equi-Vest variable annuity, and the amount of such charge; (2) the surrender charges for the Accumulator Plus variable annuity were higher than those on the Equi-Vest variable annuity; (3) although the Accumulator Plus variable annuity offered a "credit" . . . depending on the amount contributed to the contract[,] . . . over time the surrender charge incurred under the Equi-Vest contract and the higher fees assessed under the Accumulator Plus contract may more than offset the value of the credit"; and (4) the registered representative "*would not be compensated*" for handling the replacement transaction. (Emphasis added.)

school counselor, had a background in securities or financial matters. RR and MR testified that they withdrew their funds from the Equi-Vest variable annuity and transferred the funds to the Franklin Templeton Fund because Skiba advised them that such an interim step was necessary before they invested in the Accumulator Plus variable annuity, which he advised was a more suitable investment for them. During the hearing, RR and MR reviewed a redacted version of the Firm's surrender letter and stated that they had never received a copy of such letter from Skiba. They testified that had they been aware of the disclosures and warnings in the letter they would not have sold their respective Equi-Vest variable annuities.

Skiba conceded at the hearing that he did not give customers RR, MR, LV, and VV the required Replacement Acknowledgement Forms that disclosed the amount of the surrender charges, and that he did not give the customers the disclosures and warnings set forth in the surrender letter. Skiba testified that he thought it was in his customers' best interests to replace each of their Equi-Vest variable annuities with the Accumulator Plus variable annuity because he considered the Accumulator Plus variable annuity to be a superior variable annuity for their investment purposes. But because he believed the Firm prohibited such replacements when there was a surrender charge involved, he structured the transactions in a "roundabout" manner so he "did not have to submit replacement forms" to the Firm for review. Skiba testified that he knew he would receive full commissions if he structured the transactions as he did, and that he would not have been entitled to those commissions if he handled the transactions as replacement sales.[8] In fact, he received full commissions on the customers' purchases of the Accumulator Plus annuities in the amount of $13,136.96 (out of total commissions of $40,000 to $50,000 that he earned in 2003).[9] Further, Skiba received production credits based upon the $13,136.96 in commissions he generated from the replacement transactions. Such production credits entitled AXA Advisors' representatives to qualify for trips and Firm benefits, including "[h]ealth insurance benefits, life insurance benefits, pension benefits, [and] 401(k) benefits."

III. Procedural History

On January 16, 2008, FINRA's Department of Enforcement ("Enforcement") filed a one-cause complaint against Skiba alleging that he violated NASD Rule 2110. The complaint specifically alleged that Skiba submitted false and misleading variable annuity applications to the Firm by responding, "No," to questions on RR's, MR's, LV's, and VV's Accumulator Plus variable annuity applications about whether their existing annuities would be surrendered or replaced as a result of the purchase of the Accumulator Plus variable annuity. The complaint further alleged that Skiba failed to submit Replacement Acknowledgement Forms to his customers and the Firm, and that he structured the variable annuity transactions so that they

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[8] At the hearing, Skiba initially denied knowing that replacement transactions did not pay full commissions, claiming that the rules were "very gray" on the subject.

[9] Skiba received the following commissions on the customers' purchases of the Accumulator Plus variable annuity: $6,101.68 (RR); $1,510.10 (MR); $3,900.33 (LV); and $1,624.85 (VV).

would not appear to be replacements, in circumvention of the Firm's variable annuity procedures. Skiba denied the allegations. Several days prior to the hearing, Skiba entered into an agreement with Enforcement, in which he stipulated to the facts upon which the allegations in the complaint are based.

The Hearing Panel found that Skiba violated NASD Rule 2110 as charged in the complaint. The Hearing Panel fined Skiba $5,000, suspended him for one year, and ordered that he pay $14,909.49 in restitution to customers RR and MR. On August 18, 2009, the Review Subcommittee called this matter for review to examine the issue of sanctions. Neither party requested a hearing. Thus, the National Adjudicatory Council considered the matter on the basis of the written record, including the briefs filed by the parties following the call for review.

IV. Discussion

Skiba does not dispute that he falsely denied on the variable annuity applications that the existing variable annuities at issue would be surrendered or replaced as a result of the customers' purchases of the Accumulator Plus variable annuity. He also does not dispute that he circumvented the Firm's procedures relating to variable annuities by structuring the variable annuity transactions as he did.

NASD Rule 2110 requires that FINRA members and associated persons "observe high standards of commercial honor and just and equitable principles of trade." A respondent violates the just and equitable principles of NASD Rule 2110 when he engages in unethical conduct. *See Dep't of Enforcement v. Davenport*, Complaint No. C05010017, 2003 NASD Discip. LEXIS 4, at *8 (NASD NAC May 7, 2003).

We previously have determined that the submission of false information on variable annuity applications is a violation of NASD Rule 2110. *See Dep't of Enforcement v. Prout*, Complaint No. C01990014, 2000 NASD Discip. LEXIS 18, at *6 (NASD NAC Dec. 18, 2000). Skiba's submission of four false and misleading variable annuity applications to his Firm therefore violated NASD Rule 2110. In addition, Skiba's failure to structure the transactions as variable annuity replacements and to submit proper documentation to the Firm and customers as required by the Firm constitute unethical misconduct under NASD Rule 2110 because the Firm's supervisory review systems could not flag the transactions as variable annuity replacements and because the customers did not receive information necessary to evaluate the economic impact of such replacements. *Cf. Davenport*, 2003 NASD Discip. LEXIS 4, at *8 (noting that respondent violated his firm's policy against borrowing from customers and tried to conceal his violation by misrepresenting to his firm that he had not borrowed from customers, in violation of the ethical standard under NASD Rule 2110). We therefore affirm the Hearing Panel's findings that Skiba violated NASD Rule 2110.

V. Sanctions

The Hearing Panel fined Skiba $5,000, suspended him in all capacities for one year, and assessed hearing costs in the amount of $3,895.28. The Hearing Panel also ordered him to pay customers RR and MR restitution in the amounts of $11,958.70 and $2,950.79, respectively, for losses that they incurred as a result of the surrender charges that they paid for selling their Equi-Vest variable annuities. For the reasons discussed below, we affirm the Hearing Panel's sanctions.

In assessing sanctions, we have considered the FINRA Sanction Guidelines ("Guidelines") for forgery and/or falsification of records, which recommend a fine of $5,000 to $100,000 and a suspension for up to two years where mitigating factors exist, or a bar in egregious cases.[10] Under these Guidelines, we also consider: (1) the nature of the documents falsified; and (2) whether the respondent had a good-faith, but mistaken, belief of express or implied authority to falsify the records. The facts relevant to these considerations serve to aggravate Skiba's misconduct. The Accumulator Plus applications that Skiba falsified were integral to the Firm's variable annuity replacement review and approval process. By answering "No" to the questions on the applications about whether any variable annuity had been or would be surrendered in connection with the Accumulator Plus applications, Skiba violated Firm procedures by not identifying the transactions as replacement transactions and deprived the Firm of its ability to supervise properly the variable annuity sales and purchases. Given these facts, there can be no finding that Skiba had a good-faith, but mistaken, belief of express or implied authority to falsify the Accumulator Plus applications.

We note that Skiba's failure to submit the Replacement Acknowledgement Forms to the Firm and his transfer of customer funds from one variable annuity product to another through an intermediary investment fund further prevented the Firm from being able to supervise properly the transactions at issue. As a result of these deceitful measures and Skiba's provision of false responses on the Accumulator Purchase Applications, the Firm was unaware of the replacement transactions and thus could not satisfy its critical review function to determine if the transactions were suitable for the customers. Skiba claims that he "never [had] any intent to deceive any party involved." His actions, however, were designed to deceive his Firm. The transactions at issue were plainly variable annuity replacements that Skiba restructured to avoid the Firm's

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[10] FINRA Sanction Guidelines 39 (2007), http://www.finra.org/web/groups/industry/@ip/@enf/@sg/documents/industry/p011038.pdf [hereinafter *Guidelines*].

Skiba argued that the Guidelines for annuity switching, which recommend a fine in the range of $5,000 to $75,000 and a suspension of up to one year, should apply. The Hearing Panel determined that the Guidelines for falsification of records are applicable because the allegations relate to Skiba's submission of inaccurate variable annuity applications and failure to follow firm procedures, not the annuity switches themselves. We agree.

procedures applicable to such transactions. This intentional misconduct is aggravating under the Guidelines.[11]

Although Skiba acknowledged at the hearing that his actions violated Firm procedures, we must weigh that candor against the fact that he was less than truthful at times during the hearing. He initially testified that he had not placed RR's initials on the Franklin Templeton IRA Transfer Request form that enabled RR to keep the death benefit on his Equi-Vest variable annuity. He ultimately admitted later in the hearing that he had affixed RR's initials to the document, but only after repeated questioning on the issue. In addition, Skiba claimed he did not engage in the misconduct as a means to obtain commissions on the transactions. The evidence is to the contrary. Skiba admitted that he knew he would receive full commissions if he structured the transactions so they did not appear to be replacement transactions, and that he would not have received those commissions if he had submitted the transactions as replacements. Indeed, he earned $13,136.96 in commissions from these transactions, which constituted a sizeable portion of the $40,000 to $50,000 in commissions he earned in 2003.[12] As the record reflects, in addition to the direct financial benefit derived from the commissions, such commissions also were important because they allowed registered representatives to earn production credits, which entitled them to qualify for trips and Firm benefits. We consider these facts to be aggravating.[13]

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[11] *Guidelines*, at 7 (Principal Considerations in Determining Sanctions, No. 13).

[12] The Guidelines instruct adjudicators to, where appropriate to remediate misconduct, consider a respondent's ill-gotten gain when determining the amount of fine. *Guidelines*, at 5 (General Principles Applicable to All Sanction Determinations, No. 6). Adjudicators may order disgorgement of such ill-gotten gain by fining away the amount of some or all of the financial benefit, including commissions. *Id.* For the following reasons, disgorgement is not an appropriate sanction in this matter. Although Skiba received $13,136.96 in commissions for the Accumulator Plus purchases that he would not have been entitled to had he submitted the transactions properly as replacements, he subsequently entered into an arrangement with AXA Advisors to pay back the commissions. Skiba testified that he agreed to forfeit the commissions to AXA Advisors, that he had made an initial lump sum payment of $5,000, which was confirmed by the Firm, and that he was paying off the remainder by monthly payments of $250. Enforcement stated in its brief on appeal that "[i]n light of Skiba's testimony that he is already being divested of his unjust enrichment, the Hearing Panel's disposition with respect to these remedies – ordering restitution but not disgorgement – was appropriate." We agree with this reasoning and thus decline to order disgorgement of Skiba's commissions.

[13] The Guidelines instruct us to consider whether the respondent's misconduct resulted in the potential for his monetary or other gain. *Guidelines*, at 7 (Principal Considerations in Determining Sanctions, No. 17).

Skiba argues that we should consider as mitigating that he has no prior disciplinary history. While the existence of a disciplinary history is an aggravating factor when determining appropriate sanctions, its absence is not mitigating. *See Rooms v. SEC*, 444 F.3d 1208, 1214-15 (10th Cir. 2006). Skiba also urges us, in assessing appropriate sanctions, to consider that he incurred costs in connection with this proceeding and unspecified losses of income and employment. We have rejected such unsupported claims as not constituting evidence of mitigation. *See, e.g., Dep't of Enforcement v. Jordan*, Complaint No. 2005001919501, 2009 FINRA Discip. LEXIS 15, *53-54 (FINRA NAC Aug. 21, 2009) (finding that respondent's claim that her "personal and business reputation [had been] besmirched and [her] livelihood threatened by attention seeking reporters and zealous regulators" would not warrant a reduction in sanctions even if supported by evidence other than respondent's own testimony); *Dep't of Enforcement v. Cipriano*, Complaint No. C07050029, 2007 NASD Discip. LEXIS 23, at *40 (NASD NAC July 26, 2007) (concluding that "the impact this matter has had on [the respondent's] career" is not a mitigating factor). We therefore afford no weight to this argument.

The Hearing Panel ordered Skiba to pay restitution to RR and MR in the amount of $14,909.49, representing the surrender charges associated with the sale of their shares in the Equi-Vest variable annuity. Skiba asserts that those surrender charges should be offset by the "bonuses" of $13,839.58 that RR and MR received as credits when they invested in the Accumulator Plus variable annuity. For the following reasons, we disagree with Skiba's method of calculating RR's and MR's losses.

Restitution is an equitable remedy, specifically set forth in the Guidelines,[14] that seeks either to prevent a respondent from being unjustly enriched by his wrongdoing, or requires the respondent to "restore his victim to the status quo ante." *See Toney L. Reed*, 51 S.E.C. 1009, 1013 (1994). Here, customers RR and MR were unsophisticated investors who unwittingly incurred substantial surrender charges when they replaced their Equi-Vest variable annuities. Moreover, they were not fully informed by Skiba about the economic effect of their respective variable annuity replacement transactions, including the fact that the Accumulator Plus variable annuity had higher costs than the Equi-Vest variable annuity. These higher costs would regularly impede the performance of RR and MR's investment and erode the value of the "bonuses." Additionally, Skiba's replacement of the customers' variable annuities subjected them to a new surrender period. RR and MR could have waited until the end of the surrender period to replace their Equi-Vest variable annuities and not been subject to a surrender charge. As a direct result of Skiba's actions, however, they replaced their Equi-Vest variable annuities

[14] The Guidelines recommend that we consider ordering restitution where appropriate to remediate misconduct. *Guidelines*, at 4 (General Principles Applicable to All Sanction Determinations, No. 5). "Adjudicators may order restitution when an identifiable person, member firm or other party has suffered a quantifiable loss as a result of a respondent's misconduct, particularly where a respondent has benefitted from the misconduct." *Id.*

during the surrender period. We therefore reject Skiba's argument that the customers' restitution should be offset by the amount of the bonuses. As between Skiba and the customers, equity favors that Skiba, as the person responsible for the customers having incurred surrender charges, bear the burden of those charges and return the customers to the positions they occupied prior to the replacements.[15] *See id.* at 1013 (stating that "an order of restitution can seek to restore the customer's position"); *David Joseph Dambro*, 51 S.E.C. 513, 518-19 (1993) (finding that the person responsible for the loss should bear its burden and return the customer to the position occupied prior to the improper recommendation).[16] We therefore order Skiba to pay restitution to RR and MR in the full amount of their surrender charges – $11,958.70, and $2,950.79, respectively – for total restitution payments of $14,909.49.[17]

After weighing all of the factors discussed above, we find that the sanctions imposed – a $5,000 fine, one-year suspension in all capacities, and order to pay restitution to customers RR and MR in the amount of $14,909.49 – are appropriately remedial. These sanctions also will serve as a general deterrent, impressing on registered representatives the importance of conducting business in an ethical manner by complying with their firm's procedures.

VI. Conclusion

We find that Skiba violated NASD Rule 2110 by submitting four false and misleading variable annuity applications to his Firm, and by failing to structure the transactions at issue as variable annuity replacements and to submit proper documentation for these transactions to his Firm and customers as required by the Firm. For Skiba's violation we fine him $5,000 and suspend him in all capacities for one year from associating with any member firm in any capacity. We also order Skiba to pay restitution to customers RR and MR in the total amount of

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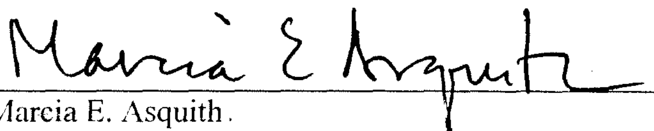
[15] We decline to order restitution with respect to the surrender charges incurred by customers LV and VV, who opted not to testify against Skiba, because there is a dearth of evidence regarding their transactions and dealings with Skiba that prevents us from considering such remedy.

[16] "A person obtains restitution when he is restored to the position he formerly occupied either by the return of something which he formerly had or by the receipt of its equivalent in money." Restatement of Restitution § 1 cmt. a (1937).

[17] We also order the payment of interest on the restitution ordered to customers RR and MR at the rate established for the underpayment of income taxes in Section 6621(a) of the Internal Revenue Code, 26 U.S.C. § 6621(a), calculated from the date of the payment of their surrender charges.

$14,909.49, plus interest from the date that they incurred surrender charges.[18] Skiba also is assessed costs from the proceedings below in the amount of $3,895.28.[19]

On Behalf of the National Adjudicatory Council,



Marcia E. Asquith
Senior Vice President and Corporate Secretary

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[18] The restitution is to be paid in the amounts set forth herein. Skiba shall submit to Enforcement (FINRA District No. 8) proof of payment of restitution within 60 days of the effective date of this decision. In the event that these customers cannot be located, unpaid restitution should be paid to the appropriate escheat, unclaimed-property, or abandoned-property fund for the state of each customer's last known address.

[19] We also have considered and reject without discussion all other arguments advanced by the parties.

Pursuant to FINRA Rule 8320, the registration of any person associated with a 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 revoked for non-payment.