**NASD OFFICE OF HEARING OFFICERS**

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| DEPARTMENT OF ENFORCEMENT,<br><br>Complainant,<br><br>v.<br><br>CHRISTOPHER W. BLACK<br>(CRD No. 1856976),<br><br>Respondent. | : | Disciplinary Proceeding<br>No. CAF040084<br><br>**HEARING PANEL DECISION**<br><br>Hearing Officer - SW<br><br>Dated: December 21, 2005 |

**Respondent violated NASD Conduct Rule 2110 by falsifying firm records when he revised his handwritten notes of conversations with a customer after receiving an arbitration claim. For violating Conduct Rule 2110, Respondent is suspended for three months in all capacities and fined $20,000.**

**Appearances**

Gary M. Lisker, Esq., Regional Counsel, and Brian D. Craig, Esq., Regional Counsel, Washington, DC, for the Department of Enforcement.

Bruce M. Bettigole, Esq., Washington, DC, for Respondent Christopher W. Black.

## DECISION

### I. PROCEDURAL BACKGROUND

On November 19, 2004, the Department of Enforcement ("Enforcement") filed a one-count Complaint against Respondent Christopher W. Black ("Respondent") alleging that Respondent falsified company records in violation of NASD Conduct Rule 2110 when he altered and supplemented his handwritten notes of conversations that he had with customer GS, after receiving an arbitration claim filed by GS.

Respondent admitted that he modified his notes after receiving the arbitration claim. In his defense, Respondent stated that he supplemented his notes of his conversations with

customer GS to create a more complete chronological recollection of the events that had occurred.

The Hearing Panel, consisting of two current members of the District 3 Committee and a Hearing Officer, conducted a Hearing in Seattle, WA, on June 28, 2005, on the issue of sanctions.

## II. FINDINGS OF FACT AND CONCLUSIONS OF LAW

### A. Jurisdiction

Respondent first became associated with an NASD member on June 20, 1988, when he joined Merrill Lynch, Pierce, Fenner & Smith Incorporated ("Merrill Lynch"). (CX-9, p. 3). From August 25, 1988, until February 19, 2003, Respondent was registered with Merrill Lynch as a general securities representative. (Id.). Since March 19, 2003, Respondent has been registered as general securities representative with A.G. Edwards & Sons, Inc. ("A.G. Edwards"). (CX-9, p. 2). Thus, NASD has jurisdiction over Respondent.

### B. Respondent admitted that he revised his client notes after receiving an arbitration complaint from the client

Respondent admitted that he violated NASD Conduct Rule 2110 by both expanding previously drafted notes and drafting additional notes of conversations that he had with customer GS.

#### 1. Background

Respondent and Greg Jensen operated as a team within Merrill Lynch and served as customer GS's financial advisors. (Tr. p. 38; RX-2, pp. 7-8). In October 1999, when customer GS opened his Merrill Lynch account, GS had worked for Microsoft Corporation ("Microsoft") as a marketing manager since 1992, and he intended to retire in the summer of 2000. (CX-1, pp. 2-3).

GS received compensation that included non-qualified stock options to purchase Microsoft common stock. (CX-1, p. 2). In 1999, GS held vested stock options that he could exercise and convert into 83,260 shares of Microsoft common stock with an estimated value of $4.5 million (after taxes and after the cost of exercising the options). (CX-1, pp. 2-3, 6 at n. 1).

In late 1999 and 2000, GS borrowed funds from a Merrill Lynch bank affiliate to exercise his vested stock options, and the Merrill Lynch affiliate held the Microsoft stock as collateral for the loan.[1] (CX-1, pp. 6-7). Instead of immediately selling some of the Microsoft stock to repay the loan, GS held on to the Microsoft stock, which soon began to decline precipitously in value. (CX-1, p. 7). By March 2001, Merrill Lynch had sold all of GS's 83,260 Microsoft shares to meet his margin calls, which GS claimed resulted in his losing approximately $3.6 million.[2] (CX-1, pp. 4, 7 at n. 2).

In the first week of December 2001, customer GS served an arbitration complaint on Respondent, Mr. Jensen, and Merrill Lynch. (Tr. p. 49). In the arbitration complaint, GS claimed that Respondent and Mr. Jensen recommended that GS borrow approximately $3 million

[1] According to the arbitration complaint, the dates, number of shares exercised, price per share, gross proceeds, option price, and taxes owed at exercise of customer GS's stock options are as follows:

| Date | No. of Shares | Price/Share | Gross Proceeds | Option Price | Taxes Owed |
|---|---|---|---|---|---|
| 10/19/99 | 28,800 | $86.31 | $2,485,800.00 | $155,475.01 | $ 686,735.77 |
| 02/16/00 | 50,560 | $97.63 | $4,935,920.00 | $522,655.00 | $1,303,574.42 |
| 09/15/00 | 3,900 | $64.19 | $ 250,331.25 | $107,153.13 | $ 42,165.95 |
| Totals | 83,260 | | $7,672,051.25 | $785,283.14 | $2,032,476.14 |

[2] According to the arbitration complaint, the dates, number of shares sold, price per share, and proceeds from the sale of GS's stock are as follows:

| Date | No. of Shares | Price/Share | Proceeds |
|---|---|---|---|
| 10/04/00 | 2,795 | $55.38 | $ 154,767.97 |
| 10/11/00 | 4,100 | $56.50 | $ 231,390.92 |
| 12/20/00 | 25,306 | $45.81 | $1,158,274.89 |
| 12/27/00 | 5,733 | $45.63 | $ 261,330.09 |
| 03/21/01 | 25,600 | $50.19 | $1,283,727.82 |
| 03/21/01 | 19,726 | $50.19 | $ 989,171.24 |
| Totals | 83,260 | | $4,078,662.93 |

from the Merrill Lynch affiliate and exercise his options to purchase and hold 83,260 shares of Microsoft stock, rather than selling a portion of the stock to fund the purchases. (CX-1, pp. 6-7).

Upon receipt of the arbitration claim, Mr. Jensen and Respondent met and promptly reviewed their handwritten informal notes of their conversations with GS. (Tr. p. 52; RX-2, p. 6). Mr. Jensen and Respondent discussed what information they had provided to GS. (Id.).

At the meeting, both Mr. Jensen and Respondent modified their notes. (Tr. p. 52). Mr. Jensen rewrote a note of a conversation with GS to delete a derogatory comment about GS. (Tr. p. 65). Respondent rewrote his notes not only to remove a similar derogatory comment about GS, but also to include more information about the conversations that he had with GS. (Tr. pp. 48, 52, 129).

Although Respondent had been a broker with Merrill Lynch for approximately 15 years, Respondent had no prior experience with arbitration proceedings or customer complaints, and he did not contact anyone at Merrill Lynch or anyone who had arbitration experience before he altered his notes. (Tr. pp. 49-50, 147, 156). It had always been Respondent's practice to take preliminary notes during a customer meeting and then rewrite the notes in greater detail. (Tr. pp. 140, 147). Neither Mr. Jensen nor Respondent appreciated that their handwritten informal notes constituted official company records.[3] (Tr. p. 52).

**2. The Revised Notes**

Enforcement alleged and Respondent admitted that he altered some of his notes to add statements regarding diversification and hedging strategies. Enforcement argued that Respondent had altered or supplemented his notes in six separate instances: (i) July 28, 1999;

[3] Respondent does not recall Merrill Lynch addressing the issue of books and records in any annual compliance meeting that he attended. (Tr. p. 144). It was Respondent's experience that handwritten informal notes were not reviewed, but simply available for the broker's use. (Tr. p. 46).

(ii) August 5, 1999 and August 5, 1999 loan calculations; (iii) June 2000; (iv) August 25, 2000; (v) September 8, 2000; and (vi) January 8, 2001. (CX-2; CX-3; CX-4; CX-5; CX-6; CX-7). Respondent acknowledged that, in December 2001, he rewrote the notes dated July 28, 1999, and August 5, 1999, to add information; Respondent also acknowledged that he initially drafted the August 5, 1999 loan calculations, the September 8, 2000 notes, and the January 8, 2001 notes, in December 2001. (Tr. pp. 55-57, 65, 69, 96-98). The evidence was less clear as to the June 2000 notes and August 25, 2000 notes.

The June 2000 notes consisted of three items: (i) handwritten notes dated July 2000 written on the preprinted term sheets illustrating collar and prepaid forward contract transactions as hedging strategies, which were presented at a Merrill Lynch seminar that GS attended; (ii) an undated note written on a post-it attached to one of the preprinted term sheets; and (iii) a separate undated handwritten paragraph. (CX-6; Tr. pp. 66-67).

Respondent admitted that he drafted the separate undated handwritten paragraph in December 2001 after receipt of the arbitration claim. (Tr. p. 67). Respondent testified that he believed, but was not positive, that the handwritten notes on the preprinted term sheets and on the post-it were not created after receipt of the arbitration claim. (Tr. pp. 66-67). Other than Respondent's equivocal statement, Enforcement had no evidence to support its allegation that Respondent drafted the handwritten notes dated July 2000 and the undated note written on the post-it in December 2001, after he learned of the arbitration claim.

The Hearing Panel does not find that Enforcement established by a preponderance of the evidence that the post-it note and the handwritten notes on the preprinted term sheets were created after the arbitration claim was served on Respondent. Accordingly, the Hearing Panel

finds that only the separate undated handwritten paragraph of the three June 2000 items constituted a supplemental note.

In an August 25, 2000 letter, Merrill Lynch advised GS of the possibility of renewing his $2,006,229.42 loan. (CX-7). Respondent's undated handwritten notes on the letter mentioned a conversation between Respondent and GS when they discussed the collar strategy and the fact that Microsoft stock had declined from just above $80 around July 4, 2000 to just above $70. (CX-7; Tr. p. 68).

Respondent testified that he believed, but was not positive, that the handwritten notes on the August 25, 2000 letter were created before he received the arbitration claim. (Tr. p. 68). Enforcement presented no evidence, other than Respondent's statement, to prove that the August 25, 2000 notes were drafted after receipt of the arbitration claim.

The Hearing Panel does not find that Enforcement established by a preponderance of the evidence that the handwritten note on a copy of the August 25, 2000 letter to GS was supplemental information drafted after receipt of the arbitration claim.

The Hearing Panel, therefore, finds that the evidence shows that, in December 2001, Respondent supplemented his notes with regard to five separate instances: (i) July 28, 1999;[4] (ii) August 5, 1999[5] and August 5, 1999 loan calculation;[6] (iii) September 8, 2000;[7] and (iv) June 2000;[8] and (v) January 8, 2001.[9] (CX-2; CX-3; CX-4; CX-5; CX-6).

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[4] The July 28, 1999 expanded note stated that GS "will also consider diversifying his [Microsoft stock] after a year or two as things are currently going well at [Microsoft]." (CX-2, p. 1; Tr. pp. 55, 95). This information was consistent with Respondent's original August 5, 1999 note that stated that GS "really wants to wait before he diversifies." (CX-3).

The information in the July 28, 1999 expanded note was also consistent with Mr. Jensen's unaltered August 5, 1999 note which indicated that they talked about how GS "would diversify out of the [Microsoft] stock." (Tr. p. 64; RX-1).

[5] The August 5, 1999 expanded note stated that GS believed the Microsoft stock would go to $140 and indicated that GS had called around to check on interest rates. (CX-3; Tr. pp. 56-57). This information repeated information included in Respondent's original July 28, 1999 note. (CX-2, p. 2; Tr. p. 55). The August 5, 1999 expanded note

The Hearing Panel also finds that most of the information Respondent added, which would have been helpful to Respondent's arbitration defense because it explicitly mentioned diversification and hedging strategies, either repeated or was consistent with information that was in the unaltered notes.[10] Because of this, and in light of the Hearing Panel's assessment of Respondent's credibility and candor in his testimony at the Hearing, the Hearing Panel finds that in revising his notes, Respondent intended to reflect accurately his conversations with GS, as he then recalled them, rather than to concoct evidence to support the defense of the arbitration claim.

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also explicitly stated that GS was aware of the danger of borrowing to exercise stock options and that Respondent had advised GS that borrowing to exercise options and hold increased his risks dramatically. (CX-2, p. 1).

[6] The August 5, 1999 loan calculation note provided an analysis of the costs of GS's loan for exercising his stock options. (CX-4; Tr. p. 97). The August 5, 1999 loan calculation note was a compilation of a number of prior unaltered calculations that had been provided concerning the loan costs for partial exercises of GS's options. (CX-4; Tr. p. 61).

[7] The September 8, 2000 supplemental notes indicated GS's intent to exercise the last of his stock options and referenced the seminar that GS had attended regarding the hedging strategy. (CX-5, p. 1; Tr. p. 69). On September 15, 2000, GS exercised the last of his stock options. (CX-1, p. 6 at n. 1).

[8] The separate paragraph explicitly stated that GS was more concerned about limiting his upside potential than protecting his downside exposure. (CX-6, p. 3). This information was consistent with information in the original July 28, 1999 notes that GS believed that "the upside in Tech is huge!" (CX-2, p. 1).

[9] The January 8, 2001 supplemental note reported GS's concern about the commissions that Merrill Lynch charged to sell GS's stock due to margin calls. (CX-5, p. 2). The January 8, 2001 supplemental note did not mention diversification or hedging strategies. (Id.).

[10] The January 8, 2001 note added information that was not relevant to the issues raised in the arbitration claim. (CX-5, p. 2).

### 3. Respondent failed to timely disclose that he supplemented his notes

In January 2002, Merrill Lynch requested customer GS's file, which Respondent provided. (Tr. p. 93). Respondent provided the file with his notes and without disclosing that he had revised the notes. (Tr. pp. 31, 93).

At a November 2002 mediation, because of contradictory information contained in the notes of Respondent and customer GS, the mediator suggested that notes of Customer GS and Respondent be tested. (Tr. pp. 77-78). Customer GS reported that he did not have access to his former computer and therefore the authenticity of his notes could not be tested. (Tr. p. 78). Merrill Lynch agreed to engage an expert in handwriting to test Respondent's notes. (Tr. p. 83).

During a break at the November 2002 mediation, when a Merrill Lynch employee asked whether the notes were "contemporaneous,"[11] Mr. Jensen stated that they were, which statement Respondent affirmed although neither Mr. Jensen nor Respondent understood the significance of "contemporaneous."[12] (Tr. pp. 105-106).

In January 2003, Merrill Lynch advised Respondent that the handwriting expert could not determine conclusively whether or not the handwritten notes were written contemporaneously. (Tr. pp. 83, 104). Subsequently, at a January 2003 meeting with Merrill Lynch representatives who were assembling documents for production to GS's counsel, in response to a question about how he prepared his notes, Respondent advised Merrill Lynch that he had rewritten the notes. (Tr. pp. 84-85). The Merrill Lynch representatives and Merrill Lynch's outside counsel were shocked. (Tr. p. 85). Respondent also advised Merrill Lynch that he had notes of conversations

[11] The Merrill Lynch employee who asked the question was not a participant in the November 2002 mediation, but had attended the mediation solely to observe a mediation process. (Tr. p. 79).

[12] In a separate subsequent conversation among themselves, Mr. Jensen and Respondent acknowledged that they did not know what "contemporaneous" meant, but neither took the initiative after the meeting to ascertain the meaning of the word, and assumed that there was no problem because the notes were accurate. (Tr. pp. 79-80, 106-107).

with three other customers, who subsequently filed arbitrations, SWH, KK, and TG, which notes were not drafted on the day that he met with the customer. (Tr. pp. 121-122, 133). However, the evidence did not establish that Respondent drafted his notes with the other customers after receipt of an arbitration complaint.[13]

When confronted with Respondent's admission, Mr. Jensen also admitted rewriting his notes.[14] Merrill Lynch subsequently settled the case with customer GS and terminated the employment of Respondent and Mr. Jensen.[15] (Tr. p. 86).

Merrill Lynch filed a Form U-5 that disclosed that Respondent had been terminated because he had represented that certain documents were contemporaneously written original notes of conversations with a Merrill Lynch client when in fact he prepared the notes after he received notice that the client had commenced an arbitration. NASD subsequently began an investigation of Respondent and Mr. Jensen. During the investigation, Respondent fully admitted all of his actions.

**4. Respondent's conduct violated NASD Conduct Rule 2110**

NASD Conduct Rule 2110 provides that "every member, in the conduct of his business, shall observe high standards of commercial honor and just and equitable principles of trade." NASD Conduct Rule 2110 thus allows NASD to regulate broker/dealers under ethical standards as well as legal standards. The SEC has construed Conduct Rule 2110 broadly to apply to all

[13] For example, Respondent drafted the note for customer SWH the day after he met with the customer. (Tr. p. 133).

[14] Subsequently, Mr. Jensen executed an AWC and was fined $5,000 and suspended six weeks for rewriting his notes to exclude a personal comment about customer GS. (RX-5).

[15] As a result of his termination, Respondent forfeited $500,000 in accrued Merrill Lynch retirement benefits. (Tr. pp. 86-87).

business related misconduct, regardless of whether the misconduct involved securities.[16] The principal consideration is whether the misconduct reflects on an associated person's ability to comply with regulatory requirements necessary to the proper function of the securities industry and protection of the public.[17]

It is well established that it is a violation of Rule 2110 for an associated person to falsify firm records.[18] Although Respondent intended to accurately reflect his conversations with customer GS in the supplemental notes, and Respondent did not immediately appreciate the significance of the timing of the drafting of the supplement notes, the Hearing Panel finds that Respondent should have known that it was inappropriate to revise the notes, which were maintained as part of the customer file, after he was aware of the arbitration claim. Accordingly, the Hearing Panel finds that Respondent violated NASD Conduct Rule 2110.

## III. SANCTIONS

For forgery and/or falsification of records, the NASD Sanction Guidelines recommend fines ranging from $5,000 to $100,000.[19] In cases where mitigating factors exist, the adjudicator is to consider suspending a respondent in any or all capacities for up to two years, or, in egregious cases, a bar.[20] The specific considerations for this violation are (i) the nature of the documents forged or falsified, and (ii) whether respondent had a good faith, but mistaken belief

[16] DSW Securities, Corp., 51 S.E.C. 814, 822 (1993) ("[w]e have repeatedly held that a self-regulatory organization's disciplinary authority is broad enough to encompass business-related conduct that is inconsistent with just and equitable principles of trade, even if that activity does not involve a security").

[17] James A. Goetz, 53 S.E.C. 472, 477 (1988) (finding that respondent's false representation that he would not personally benefit from his firm's matching gifts program violated Conduct Rule 2110 because it reflected "directly on [his] ability to comply with regulatory requirements fundamental to the securities business and to fulfill his fiduciary responsibility in handling other people's money").

[18] DBBC v. Sickles, No. C9A950036, 1997 NASD Discip. LEXIS 23 (Jan. 22, 1997) (finding that an associated person acts in contravention of just and equitable principles of trade by falsifying records submitted to his member firm).

[19] NASD Sanction Guidelines, p. 39 (2005).

of express or implied authority.[21] The general considerations in the Guidelines also apply. The Hearing Panel specifically considered whether Respondent acknowledged his misconduct prior to detection, whether Respondent attempted to remedy the misconduct prior to detection, whether Respondent engaged in a pattern of misconduct, and whether the conduct was the result of an intentional, reckless or negligent act.[22]

In this case, the falsified documents were informal notes of conversations with a customer, rather than formal records, and Respondent mistakenly believed that they were not firm records and that he could therefore revise them. As explained above, the Hearing Panel found that Respondent intended his revisions to accurately reflect his conversations with the customer.

Looking to the general considerations, the Hearing Panel noted that Respondent acknowledged his misconduct to Merrill Lynch after questions were raised, but before the firm had discovered that the notes had been revised. In fact, the shocked response of Merrill Lynch to Respondent's admission makes it clear that Merrill Lynch did not doubt the authenticity of the notes prior to Respondent's admission.

The Hearing Panel does not find that Respondent engaged in a pattern of misconduct. Although he freely acknowledged having written his notes of conversations with three other customers after the day the conversations occurred, there was no allegation or evidence that those notes were written after the customers had filed arbitration claims. Instead, it appears that Respondent was simply recording his recollections of the conversations somewhat after the fact.

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[20] Id.

[21] Id.

[22] Id. at pp. 6-7.

The Hearing Panel also finds that Respondent did not deliberately attempt to conceal his misconduct, or to mislead Merrill Lynch. The Hearing Panel found that Respondent did not initially appreciate the significance of his revisions, and did not understand when asked whether the notes were contemporaneous. Respondent's misconduct was negligent, rather than reckless or intentional. When Respondent did realize the importance of the timing of the drafting of the notes, he advised Merrill Lynch.

Enforcement argued that Respondent's actions were analogous to the egregious actions of Mr. Noonan in the Noonan[23] case, and, therefore, recommended that Respondent be barred. As the SEC noted in Noonan, "the appropriate remedies in a disciplinary action depend on the circumstances of each particular case."[24] The circumstances in this case are distinguishable from Noonan in several important respects. Mr. Noonan fabricated a letter, with enclosure, to a customer who had filed an arbitration claim in order to contradict the allegations in the claim, and furnished it to the claimant's attorney during discovery. When his firm investigated, Mr. Noonan lied about the fabrication until the firm confronted him after conducting tests that proved the letter was fabricated. Moreover, during the firm's investigation, Mr. Noonan provided the firm with his calendar, which also contained falsified entries to support his defense in the arbitration.

In contrast, Respondent revised his notes to more fully, but accurately, reflect his recollection of his conversations with the customer; he provided the notes to Merrill Lynch, not the claimant, along with all the rest of the customer's file; and he acknowledged the revisions even after Merrill Lynch's testing failed to establish that the notes had been revised and before the notes were to be provided to the customer's counsel.

[23] John F. Noonan, 1995 SEC LEXIS 1199 (May 18, 1995).

In spite of Respondent's intentions and his voluntary disclosure, the Hearing Panel found that significant sanctions were warranted. Although customer notes are generally informal documents, after Respondent was aware of the arbitration claim he should have realized the notes might be evidence, and needed to be preserved. Further, when casually questioned by Merrill Lynch during the mediation, Respondent failed to explain that he had revised the notes; he should have recognized his obligation to do so even if he did not understand the word "contemporaneous."

Taking all these circumstances into consideration, the Hearing Panel finds that an appropriate sanction for Respondent's conduct is a three-month suspension and $20,000 fine.

## IV. CONCLUSION

Respondent Christopher W. Black violated NASD Conduct Rule 2110 by creating misleading company records because the records did not accurately reflect when certain of the notes were drafted. For violating Conduct Rule 2110, Respondent is suspended for three months in all capacities and fined $20,000.

The Hearing Panel also orders Respondent to pay the $1,960.14 costs of the Hearing, which include an administrative fee of $750 and Hearing transcript costs of $1,210.14. The costs and fines shall be due and payable when, and if, Respondent seeks to return to the securities industry.

The sanctions shall become effective on a date determined by NASD, but not sooner than thirty days from the date this Decision become the final disciplinary action of NASD, except that, if this Decision becomes the final disciplinary action of NASD, Respondent's suspension in

[24] Noonan at fn 9.

all capacities shall commence at the opening of business on Monday, February 20, 2006, and conclude at the close of business on Friday, May 19, 2006.[25]

**HEARING PANEL**

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Sharon Witherspoon
Hearing Officer

Dated: Washington, DC
December 21, 2005

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[25] The Hearing Panel has 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.