

NASD OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

Respondent.

Expedited Proceeding
No. ARB050016

Hearing Officer—Andrew H. Perkins

DECISION

August 2, 2005

Respondent showed that he had a bona fide inability to pay the award issued against him in an NASD arbitration proceeding. The Hearing Officer therefore dismissed the proceeding.

Appearances

For the Complainant: Jill Jablonow, Regional Attorney, Los Angeles, CA.

For the Respondent: Arthur Lewis Stern, III, Esq., Tallahassee, FL.¹

DECISION

I. Introduction

By letter dated March 18, 2005, NASD’s Office of Dispute Resolution notified the Respondent that his registration would be suspended in accordance with NASD Procedural Rule 9554 because of his failure to pay an arbitration award.² On April 11, 2005, the Respondent

¹ Mr. Stern entered his appearance in this case, but he did not participate in the hearing. The Respondent represented himself at the hearing.

² CX 6. “CX” refers to Enforcement’s exhibits, and “RX” refers to the Respondent’s exhibits.

requested a hearing. The Respondent claimed that he had a *bona fide* inability to pay the arbitration award.³

Pursuant to Procedural Rules 9559(d)(1) and 9559(d)(5), the Hearing Officer conducted a hearing by telephone on June 27, 2005. The Department of Enforcement (“Enforcement”) offered 11 exhibits, and the Respondent offered 36 exhibits. In addition, the Respondent testified at the hearing.⁴

After a review of the entire record, the Hearing Officer finds that the Respondent adequately established his *bona fide* inability to pay the arbitration award. Accordingly, the proceeding is dismissed.

II. Findings of Fact

A. Background

The Respondent, who has been employed in the securities industry since 1992, was associated with NASD member firm Wachovia Securities, LLC (“Wachovia”)⁵ from March 2000 to February 2001.⁶ As part of his compensation package, the Respondent received a \$40,000 advance, secured by an interest-bearing promissory note.⁷ According to the Respondent’s Central Registration Depository record, Wachovia discharged him because he made solicited recommendations of a stock that traded under \$5.00 per share in violation of the firm’s policies and procedures.⁸

³ CX 8.

⁴ The hearing transcript is cited “Tr.” followed by the page number.

⁵ The Respondent was actually employed by Wachovia’s predecessors in interest, First Union Securities, Inc. and First Union Brokerage Services, Inc. For simplicity, the firm is referred to by its current name.

⁶ CX 1, at 5.

⁷ CX 5, at 1.

⁸ CX 1, at 5.

After Wachovia terminated the Respondent's employment, Wachovia demanded repayment from the Respondent of the \$40,000 advance on the ground that he was terminated for cause. The Respondent refused to make the demanded repayment on the grounds that his employment had been terminated as part of a reduction in workforce, not for cause. The Respondent claimed that under the terms of his employment arrangement he was not responsible to repay the advance if his employment unless he was terminated for cause. To resolve the dispute, on May 26, 2002, Wachovia filed an arbitration claim against the Respondent, NASD Arbitration No. 02-01791.⁹

On April 19, 2004, the NASD arbitration panel issued its award, finding the Respondent liable to Wachovia for the \$40,000 advance plus interest.¹⁰ The Respondent then timely filed an application to vacate the Arbitration Award with the United States District Court for the Middle District of Florida.¹¹ On January 24, 2005, the United States District Court denied his application.¹²

The Respondent made no payments to Wachovia. Accordingly, by letter dated March 18, 2005, NASD's Office of Dispute Resolution notified the Respondent that he would be suspended for failing to comply with the award.¹³ On April 11, 2005, the Respondent requested a hearing, asserting his financial inability to pay the award.¹⁴

⁹ CX 2.

¹⁰ *Id.*

¹¹ RX 31.

¹² CX 5.

¹³ CX 6.

¹⁴ CX 8.

B. Respondent's Financial Condition

The Respondent lives in Tallahassee, Florida, with his wife and three children, ages 12, 9, and 6.¹⁵ His children require special schooling and therapy.¹⁶ The State of Florida provides assistance to cover some of his children's special educational needs.¹⁷

After the Respondent left Wachovia, he was employed with A.G. Edwards & Sons, Inc. from February 2001 until January 2003, and with NBC Securities, Inc. from February 2003 until April 2005. In April 2005, he joined his current firm, Infinex Investments, Inc., a broker-dealer owned by Wakulla Bank.¹⁸ The Respondent's current salary is \$60,000 per year.¹⁹

The Respondent is insolvent. He and his wife have no liquid assets whatsoever. He sunk deeply into debt while NBC Securities employed him. The Respondent's total compensation for 2004 was \$23,804,²⁰ and his business expenses that year exceeded \$78,000.²¹ He could not pay his bills as they came due. To stay afloat, he borrowed extensively from family and friends. Finally, he was forced to sell his home to repay these loans and avoid foreclosure. The Respondent had not made any of his mortgage payments after January 2004.²²

The Respondent sold his home to MV, his mother-in-law, on July 1, 2004, for \$360,000, its then current fair market value.²³ MV purchased the home so that the Respondent and his

¹⁵ Tr. 26-28.

¹⁶ Tr. 32.

¹⁷ Tr. 33.

¹⁸ Tr. 19-20

¹⁹ Tr. 21-22. The Respondent's salary arrangement with Wakulla Bank is for 18 months, following which he might be switched to commissions. (Tr. 23.) The Respondent is the sole registered representative at Infinex Securities.

²⁰ RX 3.

²¹ Tr. 24-25.

²² RX 33 (Notice of Foreclosure dated June 25, 2004).

²³ RX 36.

family would not have to move. The Respondent currently pays rent of \$2,250 per month, which equals MV's monthly mortgage expense.²⁴ The Respondent intends to repurchase the home when his economic situation improves.

The Respondent and his wife received \$164,515.08 from the house sale.²⁵ The Respondent used the proceeds to repay a number of loans and to prepay rent to his mother-in-law. He deposited the balance in his investment account at NBC Securities.²⁶ The Respondent then actively traded his account, suffering losses of approximately \$44,000 over the following five months. By the end of 2004, the Respondent had no money left in his investment account.²⁷

The Respondent's current monthly expenses about equal his monthly income.²⁸

III. Discussion

Enforcement contends that the Respondent was obligated to pay the award in July 2004, using the proceeds from the sale of his house. Because he used the proceeds to pay other debts and to engage in risky trading, Enforcement argues the Respondent is not entitled to claim that he now has a *bona fide* inability to pay the award. Enforcement characterizes his current insolvency as a product of his own asset-allocation choices rather than a genuine inability to pay.

Enforcement, however, overlooks the fact that the Respondent's obligation to pay the award was stayed while his application to vacate the award was pending before the federal court.

In NASD Notice to Members 00-55 NASD set forth the five bases an associated person may

²⁴ Tr. 27. Pursuant to the agreement he has with his mother-in-law, the Respondent prepaid the first year's rent from out of the proceeds of the sale. (Tr. 28.)

²⁵ RX 36.

²⁶ RX 11.

²⁷ *Id.*

²⁸ *See* RX 20.

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raise in justification for non-payment of an arbitration award.²⁹ One such basis is a “pending” motion to vacate or modify the arbitration award.³⁰ In the corresponding endnote, the NASD further specified that “[a]n award must be paid immediately when a court denies a motion to vacate or modify the award, absent a court order staying compliance with the award.”³¹ Thus, the Respondent was not obligated to pay Wachovia until January 2005. By that time, the Respondent was unable to pay all or a substantial portion of the award.³²

IV. Conclusion

In summary, the Hearing Officer finds that the Respondent has established adequately his *bona fide* inability to pay the award and that, in light of this showing, his registration should not be suspended. Accordingly, the Hearing Officer dismisses this proceeding without prejudice. This does not mean that the Respondent is free from his obligation to pay the award. Moreover, Enforcement may reopen this proceeding at any time upon a showing that the information the Respondent provided to demonstrate his inability to pay the award was materially inaccurate or incomplete, and misrepresented his true financial condition.³³ Finally, nothing in this Decision shall preclude NASD from suspending or canceling the Respondent’s registration in the future if his financial condition changes and he fails to satisfy the award.³⁴

²⁹ NASD Notice to Members 00-55, 2000 NASD LEXIS 63 (Aug. 2000).

³⁰ *Id.* at *5.

³¹ *Id.* at *6 n.5 (emphasis added).

³² The Hearing Officer further notes that there is no evidence that the Respondent intentionally dissipated his assets to avoid paying Wachovia.

³³ *See, e.g., Brent Duane Green*, Exchange Act Release No. 39210, 1997 SEC LEXIS 2124 (Oct. 7, 1997).

³⁴ The Hearing Officer has considered all of the arguments made by the parties. They are rejected or sustained to the extent they are inconsistent or in accord with the views expressed herein.

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Andrew H. Perkins
Hearing Officer