FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. DAVID TRENDE (CRD No. 2725055), Respondent.	Disciplinary Proceeding No. 2007008935010 Hearing Officer – LBB **HEARING PANEL DECISION** Dated: October 4, 2011

Respondent is suspended for three months and fined $10,000 for falsifying Federal Reserve forms, in violation of NASD Conduct Rule 2110, and causing his firm's books and records to be inaccurate by submitting the falsified forms to his firm, in violation of NASD Conduct Rules 3110 and 2110.

Appearances

Jonathan I. Golomb, Esq., Senior Special Counsel, and Thomas Kimbrell, Esq., Principal Counsel, for the Department of Enforcement.

Adam J Davis, Esq. and Andrew J. Dorman, Esq. for Respondent.

DECISION

I. Procedural Background

The Department of Enforcement ("Enforcement") filed the three-cause Complaint in this disciplinary proceeding on December 21, 2010, charging Respondent David Trende ("Respondent") with providing false information on Federal Reserve Forms G-3[1] ("Purpose Statement") with respect to two customers, in violation of Section 7 of the Securities Exchange Act of 1934 ("Exchange Act"), Federal Reserve Regulation T, and NASD Conduct Rule 2110;

[1] The full name of the form is "Statement of Purpose for an Extension of Credit Secured by Margin Stock by a Person Subject to Registration Under Regulation U."

violating NASD Conduct Rule 2110 by engaging in the conduct charged in the First Cause of Action; and causing his firm to maintain false books and records by providing false information on the two Purpose Statements, in violation of NASD Conduct Rules 3110 and 2110.[2] Respondent filed his answer to the Complaint on January 18, 2011, generally denying the allegations of the Complaint.

A hearing was conducted in Cleveland, Ohio, on June 28, 2011, before a hearing panel composed of a Hearing Officer and two former members of the District 8 Committee.

II. Respondent

Respondent entered the securities industry in 1996, and has been associated with five member firms since that time. He was registered with a former member firm, Legacy Financial Services, Inc. ("Legacy"), from October 2001 until July 2007, and is currently registered with another member firm, American Portfolio Advisors, Inc. He has been registered as a Series 7 and 66. Stip. 1.[3] In 2005, Respondent worked in a branch office that operated under the name Legend Financial Group, Ltd. ("Legend"). Stip. 2.

III. Facts

A. Stock to Cash Program

This case concerns Respondent's submission of Purpose Statements for the "Stock to Cash" program, pursuant to which two customers borrowed money, using securities as

[2] As of July 30, 2007, NASD consolidated with the member regulation and enforcement functions of NYSE Regulation and began operating under a new corporate name, the Financial Industry Regulatory Authority (FINRA). References in this decision to FINRA include, where appropriate, NASD. Following consolidation, FINRA began developing a new FINRA Consolidated Rulebook. The first phase of the new consolidated rules became effective on December 15, 2008, including certain conduct rules and procedural rules. *See* Regulatory Notice 08-57 (Oct. 2008). This decision relies on NASD Conduct Rules that were the applicable rules at the time of Respondent's alleged misconduct. The applicable rules are available at www.finra.org/rules.

[3] References to the exhibits provided by Enforcement are designated as "CX-___." References to the exhibits provided by Respondent are designated as "RX-___." Joint exhibits are designated as "JX-___." The parties filed a set of factual stipulations on May 23, 2011, which provided the factual basis for much of this decision. References to the stipulations are designated as "Stip. ___." References to the hearing transcript are designated as "Tr. ___."

collateral.[4] A brochure for the program described it as a "revolutionary … program, allowing investors to receive 90% liquidity from their stock portfolio to fund life insurance and meet their other financial planning objectives, while at the same time protecting those shares against potential market losses." JX-1 at 1. It was designed to be a mechanism to help customers of insurance agents to fund purchases of fixed annuity and fixed life insurance products. Tr. 28.

A participant in the Stock to Cash program transferred stock to Alexander Capital Markets, LLC ("Alexander Capital"), a non-bank independent private lender, as collateral for a loan from Alexander Capital of up to 90% of the value of the stock. Tr. 28-30, 59-60. The program was offered through Emerging Money Corporation, an insurance consulting company. JX-1 at 1; Tr. 32. Emerging Money characterized its role as the licensor of the Stock to Cash program, and obtained its revenue by sharing in the commissions earned by the "licensees," typically insurance agents but sometimes stockbrokers, who received commissions from the sale of insurance products to customers who funded their purchases with the proceeds of the Stock to Cash loans.[5] JX-6; Tr. 41. According to the terms of the Stock to Cash program, Emerging Money was entitled to receive 15% of any commissions received from the purchase of commissionable fixed annuity or life insurance products purchased with the proceeds of the Stock to Cash loans. JX-6; CX-7; Tr. 44-45.

The loans were non-recourse. If the value of the stock at the end of the loan term was below the amount owed to Alexander Capital, including accrued interest, the borrower could "walk away," i.e., forfeit the collateral, keep the money from the loan, and not repay any

[4] FINRA issued an investor alert on June 9, 2011, describing how such programs typically work, and providing information to investors. *See*, "Stock-Based Loan Programs: What Investors Need to Know," available on FINRA's website at www.finra.org/Investors/ProtectYourself/InvestorAlerts/TradingSecurities/P123719.

[5] There is insufficient evidence to determine whether Emerging Money was, as a matter of law, the agent of Alexander Capital, the lender. Regardless of the precise legal classification, it is clear that Emerging Money was the interface between the lender and the insurance agents and brokers who used the Stock to Cash program primarily to finance the purchase of insurance products by their customers.

deficiency.[6] If at the end of the term of the loan, the value of the stock had increased to an amount above the amount owed, the borrower could sell the stock held as collateral and repay the amount owed to the lender while keeping the profit, or repay the loan and recover the pledged securities. JX-1, 2, 4; Tr. 30-32.

The loan documents and federal regulations prohibited investment of the loan proceeds in margin securities. JX-2 at 15, JX-4 at 14.[7] The terms of the program prohibited borrowers from investing in variable annuities. JX-2 at 15, JX-4 at 14; Tr. 36.

As part of the Stock to Cash loan process, Respondent was required to provide a Purpose Statement setting forth the intended use of proceeds, in order to ensure compliance with Federal Reserve Board regulations restricting the extension of margin credit. Stip. 4. The Purpose Statement is a short form required by the Federal Reserve, requiring the borrower to provide the following information:

1) What is the amount of credit being extended?
2) Will the loan be used to purchase or carry margin securities? If the answer is "no," describe the specific purpose of the credit.

B. Respondent's Use of the Stock to Cash Program

Respondent's customers first learned about the Stock to Cash program at a luncheon they attended at Legend. When the customers asked him about the program, he recommended it as a way to invest in more volatile securities than those in which the customers typically invested, but to limit the risk by using the securities as collateral for the Stock to Cash loans. Tr. 134-135, 304-305. During a period of slightly over one month, while employed as a registered

[6] The marketing materials for the program describe the loans as typically for a term of three years. JX-1 at 7. The loans at issue in this case were for terms of two years. JX-2, 4.

[7] See 12 C.F.R. § 221.3; Compliance Guide to Small Entities, Regulation U: Credit by Banks or Persons other than Brokers or Dealers for the Purpose of Purchasing or Carrying Margin Stocks, available at www.federalreserve.gov/bankinforeg/regucg.htm.

representative, Respondent recommended to two of his customers that they participate in the Stock to Cash program. This was the only time Respondent ever used the Stock to Cash program. Stip. 3. He had general discussions with the customers concerning the possible uses of the loan proceeds, but no decisions were made about how to use the funds until after the proceeds were received. Tr. 140, 275-276.[8]

In August 2005, Respondent's customers CK and WK agreed to borrow approximately $180,000 through the Stock to Cash program in the name of the K Family Revocable Living Trust. Stip. 5. Respondent filled out the Purpose Statement before meeting with the Ks. Tr. 287. Respondent wrote the words "real estate" on the Ks' Purpose Statement as the specific purpose of the loan. He also wrote the amount of the loan and the date on the Ks' Purpose Statement. JX-2 at 4; Tr. 138. When the Ks signed the Purpose Statement on August 9, 2005, they had discussed several options for the use of the proceeds with Respondent, but had not determined how they would ultimately use the loan proceeds. Stip. 7; Tr. 140.[9] The Ks did not use the proceeds for the stated purpose of purchasing real estate. On or about September 21, 2005, the Ks used more than 50% of the proceeds of the Stock to Cash loan to purchase a variable annuity from Jackson National Life, with Respondent as their broker. JX-3; CX-10. They used the remainder of the proceeds to purchase an equity-indexed annuity from Equitrust, again through Respondent, and pay some debts. Stip. 8; Tr. 84-85; CX-10. Legacy

[8] Respondent, CK and KR testified that they had discussed real estate as a possible use of the proceeds. The most credible testimony was Respondent's statement that he had general discussions about the use of the proceeds, and that real estate was mentioned as one possible use of the funds. Tr. 93-94, 140, 167, 171, 181, 207, 229-230, 234, 300.

[9] Respondent gave the forms for the two customers who used the Stock to Cash program to two principals at Legend, his branch office, who gave the forms to the branch manager. Tr. 288-289. The FINRA investigator obtained the documents from Legend. Tr. 74-75. The parties stipulated to the authenticity, foundation, and admissibility of the joint exhibits. See Stipulations Regarding Proposed Exhibits, filed May 23, 2011.

received a commission from the annuity sales, and Respondent received a payout from Legacy. CX-10.

In September 2005, Respondent's customer KR agreed to borrow approximately $100,000 through the Stock to Cash program. Stip. 9. In connection with KR's loan, Respondent completed a Purpose Statement for KR's signature. The Purpose Statement stated that the credit was going to be used for real estate. Stip. 10; JX-4 at 4; Tr. 179-180. When KR signed the Purpose Statement on September 7, 2005, he had discussed several options for the use of the proceeds with Respondent, but had not determined how he would ultimately use the loan proceeds. Stip. 11; Tr. 167-168, 207. KR did not use the proceeds to purchase real estate. On or about September 16, 2005, KR signed an application to purchase a variable annuity from Jackson National Life, with Respondent as the broker, with most of the proceeds from the Stock to Cash loan. Stip. 12; JX-5. KR bought the variable annuity from Jackson National Life. CX-10; Tr. 82-84, 176. Legacy received a commission from the annuity sale, and Respondent received a payout from Legacy. CX-10.

Both customers profited on their investments in the securities that they bought for participation in the Stock to Cash program and posted as collateral for their loans. Tr.171-2, 233-234.

IV. Respondent Violated NASD Conduct Rule 2110 by Falsifying Federal Reserve Forms

The Second Cause of Action charges Respondent with violating NASD Rule 2110, which requires a registered representative, "in the conduct of his business," to "observe high standards of commercial honor and just and equitable principles of trade." Unethical conduct violates Rule

2110.[10] A violation of the Rule is based on the ethical implications of a representative's conduct, and does not depend on whether the representative has committed a legally cognizable wrong.[11] Rule 2110 applies broadly to apply to all business-related misconduct.[12] "NASD Rule 2110 reaches beyond legal requirements and, among other things, depends upon general rules of fair dealing, the reasonable expectations of the parties, and marketplace practices."[13]

Respondent prepared the Purpose Statements for the customers' signatures, and accepted the Purpose Statements and submitted them to his firm, knowing that the customers did not have a specific purpose for the loans. Even if there was a possibility that the money would be used in some fashion for real estate, that use was clearly not the specific purpose of the loans. Respondent was well aware that his customers had not decided how to use the money at the time the Purpose Statements were signed. Respondent's conduct was unethical and reflects negatively on his commitment to compliance with the regulatory requirements of the securities industry, and therefore violated NASD Conduct Rule 2110.[14]

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[10] *See Dep't of Enforcement v. Davenport*, No. CO5010017, 2003 NASD Discip. LEXIS 4, at *8 (N.A.C. May 7, 2003).

[11] *See, e.g.*, *Dep't of Enforcement v. Foran*, No. C8A990017, 2000 NASD Discip. LEXIS 8, at *13-14 (N.A.C. Sept. 1, 2000); *Dep't of Enforcement v. Shvarts*, No. CAF980029, 2000 NASD Discip. LEXIS 6, at *12 (N.A.C. June 2, 2000).

[12] *Dep't of Enforcement v. Davenport*, 2003 NASD Discip. LEXIS 4, at *8-9.

[13] *Dep't of Enforcement v. Conway*, No. E102003025201, 2010 FINRA Discip. LEXIS 27, at *29 (N.A.C. Oct. 26, 2010), *appeal filed* (S.E.C. Dec. 2, 2010) (citing *Dep't of Enforcement v. Shvarts*, 2000 NASD Discip. LEXIS 6, at *12) *see also Geoffrey Ortiz*, Exchange Act Rel. No. 58416, 2008 SEC LEXIS 2401, at *22-24 (Aug. 22, 2008) (finding that petitioner violated NASD Rule 2110 by submitting false information to his member firm because such conduct reflected negatively on his ability to comply with regulatory requirements fundamental to the securities industry, and also violated Rule 2110 by submitting false information to FINRA).

[14] Because the Hearing Panel finds that Respondent violated NASD Conduct Rule 2110 by falsifying the Purpose Statements, it is unnecessary to decide whether he also violated Section 7 of the Exchange Act and Federal Reserve Regulation T, as charged in the First Cause of Action.

V. Respondent Violated NASD Conduct Rules 3110 and 2110 by Submitting False Documents to His Firm

NASD Conduct Rule 3110(a) provides, in part:

> Each member shall make and preserve books, accounts, records, memoranda, and correspondence in conformity with all applicable laws, rules, regulations and statements of policy promulgated thereunder and with the Rules of this Association and as prescribed by Exchange Act Rule 17a-3….

Entering inaccurate information in a member firm's books and records violates both the requirement of NASD Conduct Rule 3110 to keep accurate books and records, and of NASD Conduct Rule 2110 that members observe high standards of commercial honor and just and equitable principles of trade.[15]

The Purpose Statements that Respondent submitted to his firm contained inaccurate information concerning the specific purpose for his customers' loans. By submitting inaccurate statements, Respondent violated NASD Conduct Rules 3110 and 2110.[16]

VI. Sanctions

Because Respondent's violations "stem from a single source," it is appropriate to impose a single, unitary sanction.[17] For falsification of records, the FINRA Sanction Guidelines ("Guidelines") recommend consideration of a fine of $5,000 to $100,000. When mitigation is

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[15] *Dep't of Enforcement v. Nouchi*, No. E102004083705, 2009 FINRA Discip. LEXIS 8 (N.A.C. Aug. 7, 2009); *see also*, *Fox & Co. Inv., Inc.*, Exchange Act Rel. No. 52697, 2005 SEC LEXIS 2822, at *30-32 (Oct. 28, 2005); *Geoffrey Ortiz*, Exchange Act Rel. No. 58416, 2008 SEC LEXIS 2401, at *17 (Aug. 22, 2008).

[16] As an associated person of Legend, Respondent was subject to the requirements of NASD Rule 3110 and was prohibited from submitting false information that would make the firm's books and records inaccurate. *See Kirlin Sec., Inc.*, Exchange Act Rel. No. 61135, 2009 SEC LEXIS 4168, at *3 (Dec. 10, 2009) (stating that "NASD General Rule [0]115 (now FINRA Rule [0]140) provides that persons associated with a member have the same duties and obligations as a member"). A violation of NASD Rule 3110 constitutes a separate violation of NASD Rule 2110. *See Stephen J. Gluckman*, Exchange Act Rel. No. 41628, 1999 SEC LEXIS 1395, at *22 (July 20, 1999) ("The NASD's determination that [respondent] violated Conduct Rule 2110 is in accord with our long-standing and judicially-recognized policy that a violation of another Commission or NASD rule or regulation … constitutes a violation of Conduct Rule 2110.").

[17] *Dep't of Enforcement v. Braff*, No. 2007011937001, 2011 FINRA Discip. LEXIS 7 (N.A.C. May 13, 2011), (currently indentified on LEXIS as 2011 NASD Discip. LEXIS 7), *appeal docketed*, SEC Dkt. No. 3-14417 (June 9, 2011).

present, the Guidelines recommend consideration of a suspension in all capacities for up to two years. In egregious cases, they recommend a bar. Principal Considerations include the nature of the falsified document and whether the respondent had a good faith, but mistaken, belief of authority.[18]

The nature of the documents falsified is an important consideration in determining the appropriate sanction in this case. The submission of Purpose Statements is specifically mandated by federal regulations as a tool for monitoring compliance with federal law. The Purpose Statement is intended to ensure that a lender does not extend credit to purchase or carry margin stock in excess of the amount permitted by the Federal Reserve pursuant to Regulation U.[19] Purpose Statements "serve as a compliance tool for the subject lenders and borrowers; … and, if necessary, as an evidentiary or enforcement tool for the Justice Department, the Securities and Exchange Commission, or the self-regulatory agencies charged with ensuring broker-dealer compliance."[20] By falsifying the forms, Respondent interfered with Alexander Capital's ability to comply with federal law, and created records that would mislead regulators that monitor and enforce margin requirements, including the SEC and FINRA, in their examinations of Legacy and Legend.

Respondent's financial gain on the transactions is not a substantial factor. Respondent did not receive any money from the Stock to Cash loans or as commissions on the sale of the securities that his customers used as collateral for their loans. Tr. 135-136. His only financial

[18] *FINRA Sanction Guidelines* at 37 (2011). The Hearing Panel did not consider the existence of express or implied authority to be a relevant factor.

[19] Supporting Statement for the Margin Credit Reports, (FR G-1, FR G-2, FR G-4; OMB No. 7100-0011). (FR G-3; OMB No. 7100-0018), (FR T-4; OMB No. 7100-0019), (FR U-1; OMB No. 7100-0115), available at www.federalreserve.gov/reportforms/formsreview/FRG1_FRG2_FRG3_FRG4_FRT4_20101015_omb.pdf.

[20] FR U-1, *Statement of Purpose for an Extension of Credit Secured by Margin Stock*, available on Federal Reserve website at www.federalreserve.gov/reportforms/ReportDetail.cfm?WhichFormId=FR_U-1&WhichCategory=7.

benefits were the commissions he received on the sales of the annuities to his customers.[21] Enforcement argues that Respondent received a financial benefit by not sharing commissions with Emerging Money, and that his motivation for falsifying the Purpose Statements was to avoid sharing commissions. There is no evidence that Respondent was aware that commissions on fixed annuity and insurance sales were supposed to be shared with Emerging Money at the time his customers entered into their Stock to Cash transactions. At the time the customers signed their Purpose Statements, he had not entered into any agreements to share commissions with Emerging Money.[22] Respondent testified that he did not know that proceeds of Stock to Cash could not be used for variable annuities, although he signed the customers' loan documents that disclosed the restriction.[23] Tr. 284; JX-2 at 15, JX-4 at 14. Respondent likely would have received commissions on the sale of the annuities even if his customers had not participated in the Stock to Cash program. His customers could have purchased the variable annuities directly, without using the Stock to Cash program, and Respondent would have received 10% higher commissions than he received by using the Stock to Cash program to fund the annuity purchases. Tr. 136, 142, 154.

[21] Respondent's firm received a commission of $7,524.75 on the KR investment in a variable annuity. The firm received commissions of $7,920 and $7,545 on the purchase of annuities by the K Family. CX-10 at 3; Tr. 83-84. Summing those numbers, Legend's total commissions were $22,989.75. Respondent's payout for annuity sales was about 30% to 40% of the commissions received by Legend. Tr. 283-284, 318. Thus, Respondent's commissions on the sales of annuities to the K Family and KR were between approximately $6,900 and $9,200.

[22] Respondent signed the agreement with Emerging Money after the loan documents had been submitted for both customers. JX-6.

[23] The Hearing Panel found Respondent's testimony on this issue credible, and consistent with his very limited use of the Stock to Cash program.

Respondent's disciplinary history is an aggravating factor.[24] In September 2004, Respondent submitted a Letter of Acceptance, Waiver and Consent, to settle allegations that he had participated in private securities transactions without providing written notice to his firm. He was fined $5,000 and suspended from October 18, 2004 until April 17, 2005. CX-1 at 10-11, CX-2. Respondent's submission of the false Purpose Statements occurred less than six months after he completed serving his suspension. After serving a substantial suspension for violating FINRA's Rules so soon after entering the industry, Respondent should have been especially careful to follow the Rules precisely. Such repeat misconduct shows a disregard for regulatory requirements.

Having considered all of the foregoing, the Hearing Panel finds that the appropriate sanction is a fine of $10,000, and a suspension of three months.

VII. Conclusion

Respondent David Trende is suspended for three months and fined $10,000 for submitting false falsifying Federal Reserve forms, in violation of NASD Conduct Rule 2110, and causing his firm's books and records to be inaccurate by submitting the falsified forms to his firm, thereby violating in violation of NASD Conduct Rules 3110 and 2110.

If this decision becomes FINRA's final disciplinary action, the suspension shall become effective upon the opening of business on December 5, 2011, and end at the close of business on March 4, 2012. The fine shall be due and payable upon Respondent's return to the securities

[24] "Adjudicators should consider imposing more severe sanctions when a respondent's disciplinary history includes … past misconduct that evidences disregard for regulatory requirements, investor protection, or commercial integrity." "General Principles Applicable to All Sanction Determinations," General Consideration No. 2, *Sanction Guidelines* at 2.

industry. Respondent is also ordered to pay the costs of the hearing in the amount of $3,474.15, which includes an administrative fee of $750 and the cost of the hearing transcripts.[25]

HEARING PANEL

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Lawrence B. Bernard
Hearing Officer

Copies to: David Trende *(via overnight courier and first-class mail)*
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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 they are inconsistent or in accord with the views expressed herein.