FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. TRACY CHEN (CRD No. 2553295), Respondent.	Disciplinary Proceeding No. 2013036678201 Hearing Officer–MC **EXTENDED HEARING PANEL DECISION** February 12, 2016

Respondent Tracy Chen submitted false expense reports seeking reimbursement from her FINRA member firm employer for expenses she did not incur, and converted firm funds paid to her as a result, in violation of FINRA Rule 2010. Chen's submission of false expense reports constituted falsification of firm documents, causing the Firm to maintain inaccurate books and records, and violated NASD Rule 3110 and FINRA Rules 4511 and 2010. For these violations, Chen is barred from associating with any FINRA member firm in any capacity, and is ordered to pay costs.

Appearances

For the Complainant: Kelly A. McCormick, Esq., Mark Maldonado, Esq., Department of Enforcement, Financial Industry Regulatory Authority.

For the Respondent: Mark Humenik, Esq.

DECISION

I. Introduction

Respondent Tracy Chen exploited her employer's business expense reimbursement system to obtain funds she had attempted unsuccessfully to persuade her employer to pay her, and to which she was not entitled. Over 17 months, Chen ordered hundreds of client gifts, cancelled the orders, and then sought reimbursement for the orders as if they were legitimate business expenses.

The Complaint charges Chen with conversion of firm funds, falsification of firm records, and causing firm books and records to be inaccurate.

Chen admits filing the false expense reports and acknowledges it was wrong but claims that, because she was entitled to the funds, the money was hers and taking it did not constitute conversion. She also denies that her false expense reports caused the Firm's books and records to be inaccurate.

As explained below, the Extended Hearing Panel rejects Chen's defenses, finding the evidence supports the charges, and the seriousness of Chen's misconduct requires the imposition of a bar.

II. Facts

Chen began her career in the financial industry in 1994 and holds Series 7, 31, 63, and 65 registrations.[1] In 1999 she became a financial advisor at Morgan Stanley's Brea, California branch office, where she remained until May 2013 when the Firm terminated her employment.[2] In the period relevant to this case, from November 2011 to her termination, Chen worked with William Yuen, whom she originally hired as an intern, with whom she had a Joint Production Agreement, and who was terminated when she was.[3]

Morgan Stanley calculated Chen's compensation according to a "grid" that determined her share of the revenue she generated.[4] She was a productive financial advisor and her compensation rate increased as her business grew. When Chen started at Morgan Stanley, she received 38 percent of the gross revenue she produced; by 2013 she qualified to receive 42 percent.[5] In 2012, she generated almost $900,000 in gross revenue,[6] earning more than $440,000 in commissions, fees, and bonuses.[7]

A. Morgan Stanley's Business Expense Reimbursement System

While Chen was at Morgan Stanley, the Firm provided its financial advisors with what it considered "necessary" business resources, such as an office, computer, telephone, access to a market quote system, a sales assistant, and business cards.[8] The Firm also reimbursed employees

[1] Hearing Transcript 50-51; Complainant's Exhibit 1, at 8, 11. References to the testimony at the hearing are "Tr." with transcript page numbers. References to exhibits introduced by Enforcement are designated "CX-___." References to exhibits introduced by Chen are designated "RX-___."

[2] Tr. 774-75, 777. Chen is currently employed by another FINRA member firm. Tr. 50.

[3] Tr. 588-92.

[4] Tr. 269.

[5] Tr. 788-89.

[6] Tr. 146-47; CX-20.

[7] Tr. 140-41; CX-40, at 21.

[8] Tr. 272-73, 790-91.

for additional "reasonable business-related out-of-pocket expenses."[9] The reimbursement policy required financial advisors to submit expense reports with itemized receipts for reasonable business-related expenses that were actually incurred.[10]

Morgan Stanley reimbursed Chen for her out-of-pocket business expenses with funds from three sources: Business Development Allowance ("BDA") funds; Automated Flexible Grid ("AFG") funds; and managers' discretionary allowance funds.[11] The largest share came from AFG funds. The smallest share came from managers' discretionary funds, but those reimbursements included the funds the Complaint charges Chen with converting.

1. The Business Development Allowance

The BDA consisted of money Morgan Stanley made available to each financial advisor annually in an amount determined by the level of revenue the advisor generated. Chen's level of revenue production in 2012 qualified her to receive a BDA allocation of $5,000.[12] However, she testified this amount was insufficient to cover her business expenses for a cell phone, consultants, networking, and "client maintenance," including meals, tickets to events, and gifts. She estimated that for these she needed an additional $15,000 to $20,000 per year.[13]

2. The Automated Flexible Grid Program

Morgan Stanley initiated the AFG program in 2010.[14] The AFG program permitted advisors to allocate a percentage of their pre-tax revenue to a reimbursement pool for business development expenses.[15] At the end of each year the financial advisors decided how much to allocate to AFG based upon their business development activity plans for the next year. Near mid-year, the Firm allowed the advisors to adjust their allocations.[16] Unused AFG fund allocations did not carry over from one year to the next; similarly, if an advisor retired or left

[9] CX-23a, at 3.

[10] Tr. 259, 272, 401.

[11] Tr. 664.

[12] Tr. 146, 153-54.

[13] Tr. 791-92.

[14] Tr. 698.

[15] Tr. 396.

[16] CX-21d, at 2, 4.

Morgan Stanley, the advisor forfeited the allocated funds.[17] Chen knew her allocation had to be used by year's end or it would be "lost."[18]

For 2012, Chen allocated 4.5 percent of her revenue to AFG, which meant if her payout totaled $400,000, her available AFG funds would be $18,000. It also meant Chen's net payout fell by 4.5 percent from 42 percent of the gross revenue she generated to 37.5 percent.[19]

At the end of 2012, Chen increased her AFG allocation for 2013 to 10 percent.[20] Morgan Stanley policy required managers to review and approve financial advisors' AFG allocation decisions. Justin Frame, Chen's supervisor at the time,[21] testified that hers was the largest allocation of anyone in the branch; most financial advisors allocated in the range of 2 percent. Although Frame thought Chen's allocation "seemed high," after discussing it with her he concluded that it was reasonable, considering her plans for the upcoming year, and her "very, very active" approach to business development.[22]

3. Managers' Discretionary Funds

Morgan Stanley managers also had discretionary funds to provide advisors with business expense reimbursements.[23] Richman, as manager of Morgan Stanley's North Orange County, California "complex," with oversight of the Brea branch office, testified that his discretionary fund amount varied from year to year, but usually ranged between $20,000 and $40,000.[24] He explained that his discretionary fund enabled him to "make an additional investment" in a financial advisor's business.[25]

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[17] CX-22, at 1; CX-21b, at 3.

[18] Tr. 168. As described by Enforcement's counsel, this "use it or lose it" characteristic of AFG allocations worked similarly to the way a health flexible spending account operates. Tr. 15.

[19] Tr. 142, 308.

[20] Tr. 142-43.

[21] Tr. 242.

[22] Tr. 274.

[23] Tr. 664.

[24] Tr. 652-53. Richman worked at Morgan Stanley from 1996 until December 2012. From 2011 until he left Morgan Stanley, he was an upper-level "complex" manager, in charge of Morgan Stanley's North Orange County complex, directly responsible for one large branch office, and with oversight of four others. Tr. 629-30. He supervised approximately 150 people, including approximately 110 financial advisors, plus support staff and managers. Tr. 631.

[25] Tr. 664-65.

B. Chen's False Expense Reports

The salient facts are undisputed. On 12 separate occasions over a span of 17 months, Chen submitted expense reports seeking payment for what she reported as client gifts.[26] Chen attached receipts she generated by making online orders for purchases of gifts. She then cancelled the orders, so she never actually incurred these expenses. Morgan Stanley reimbursed Chen for purchases she claimed to have made in ten of the reports she submitted from November 2011 to March 21, 2013.[27] In the 12 false claims, Chen sought $43,987.43 in reimbursement. Before discovering they were false, Morgan Stanley paid Chen $28,435.43.[28] Of that sum, $2,781.10 came from Chen's BDA allocation and $24,054.33 came from her AFG allocation.[29] The remaining $1,600, the subject of the Complaint's conversion charge, came from Richman's discretionary allowance, as described below.

The first false expense report illustrates the pattern of Chen's misconduct. On November 16, 2011, Chen used her credit card to order 50 bracelets from Nordstrom. They cost $88 each, for a total of $4,829. The same day she cancelled the order so her credit card would not be charged. But she submitted an expense report seeking reimbursement for the purchase, supported by the Nordstrom receipt. The expense report states that the business purpose of the purchase was "Client Gifts – Xmas." Chen listed the names of 50 customers, each described as a "client, Business Guest."[30] The expense report contains a Morgan Stanley accounting code showing the expenditures were for "Maintenance of existing client relationship."[31] Morgan Stanley approved the request and deposited the money into Chen's account.[32]

In April 2013, Chen submitted her last two expense reports. On April 5 she placed an order with Nordstrom for 62 serving platters for a total of $6,026.40, then cancelled the order by phone, and submitted the receipt for the order.[33] On April 21 Chen ordered 98 candles for a total of $9,525.60, then cancelled the order, and submitted the receipts for reimbursement. Morgan

[26] Enforcement points out that on these 12 occasions Chen actually submitted a total of 14 false receipts, because she submitted three receipts with the request for reimbursement on October 22, 2012. Enforcement's Post-Hr'g Br. at 7, n.44; CX-10, at 14-16.

[27] CX-45–CX-54.

[28] Enforcement's Post-Hr'g Br. at 1, n.1; CX-4–CX-6, CX-8–CX-10, CX-13–CX-17, CX-19.

[29] Tr. 105-07, 260-63; CX-13, CX-20.

[30] CX-4.

[31] CX-30, at 4.

[32] Tr. 71; Stipulations ("Stips.") ¶¶ 3-8.

[33] Stips. ¶¶ 59-62.

Stanley approved but did not pay the April 5 order, and neither approved nor paid the April 21 order.[34]

1. The Discretionary Allowance Award to Chen

In April 2012, a client with a large account called Chen to complain he had received an erroneous monthly Morgan Stanley account report that showed his account value had dropped by 40 percent. The client told her he knew he had not incurred the loss shown in the report, but he felt such a "huge mistake" was "not acceptable," and he decided to move his account from Morgan Stanley to another firm. Chen became upset. She testified that she "panicked" at the prospect of losing this client because of the Firm's "blunder."[35]

Chen and her immediate supervisor, Ruarri Burda, met with the client to apologize for the error. Burda explained that the Firm was consolidating software systems and experienced errors in a number of the reports, and assured the client that it would not happen again. According to Burda, the client said the erroneous report was the "final straw," but he had decided to move his account to another firm for other reasons, including being unhappy with his account's performance at Morgan Stanley.[36]

On April 19, 2012, Chen sent an email to the president of Morgan Stanley, copying her supervisors and others. In it she described the situation as "a shocking matter of incompetence and negligence at our company that has caused us to lose a good client who left [Morgan Stanley] yesterday." She wrote that she had "worked for 2 years to bring this client" to Morgan Stanley, he had invested $1.4 million with her, and he had been "very satisfied" with her performance.[37]

In May, still angry about the loss of her client, from whom she earned commissions and fees of about $12,000 per year, Chen wrote an email to Burda and Richman, the complex manager, complaining that Morgan Stanley had not properly addressed the loss of the client "through absolutely no fault of my own." She declared it a "retention issue." She also insisted that she "was entitled to compensation for this loss," and as compensation, she would accept an increase in her annual expense account.[38]

Retention of financial advisors was a "very important" and "sensitive" issue to Morgan Stanley.[39] In early July, Burda wrote Richman an email stating that he feared Chen was planning

[34] CX-55–CX-56.

[35] Tr. 819-20.

[36] Tr. 458-59.

[37] CX-71.

[38] Tr. 457; CX-63.

[39] Tr. 644.

to leave Morgan Stanley.[40] Richman testified that when disputes arose, Chen "was known to threaten to leave if things [didn't] go her way."[41] Richman met with Chen to address her contention that she was being treated unfairly[42] and to discuss Chen's plans and ideas for growing her business. Richman assured her that he supported her.[43] Richman testified that he wanted Chen to stay at Morgan Stanley, but did not want to reward what he considered unreasonable behavior: writing directly to the president of the Firm, insisting the client's departure was not in any way her fault, and demanding that Morgan Stanley make up for her loss.[44] But he wanted to avoid driving a "wedge" between her and the Firm.[45]

Richman offered to support Chen by providing her with funds from his discretionary account to share the cost of hiring interns who would help generate new clients.[46] Because experience had taught him it was important to be "very, very specific" when dealing with Chen, he wanted to ensure she clearly understood the terms: he would support her effort to use interns to generate new leads to find other good clients, but he would not "replace one client's revenue."[47]

Richman documented his offer in an email. It began, "Recently we discussed the idea of our Complex making an additional investment" to support Chen's efforts to develop her business and generate new leads. "With that in mind," Richman wrote, "we would like to offer . . . $400 of additional T&E [travel and entertainment] each month" starting from June 2012 through the rest of the year "to offset approximately 50%" of the cost of her interns. He asked Chen to submit her "reimbursement request to the Complex directly"[48] because he wanted to show Chen that Morgan Stanley supported her at an upper-management level, and he wanted to relieve Burda from paying the cost from his branch-level budget.[49] Richman was satisfied that Chen understood the specific purpose of the funds was to defray the cost of the interns.[50]

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[40] Tr. 514-15.

[41] Tr. 644, 649.

[42] Tr. 646-47.

[43] Tr. 647.

[44] Tr. 660.

[45] Tr. 649.

[46] Tr. 650-52.

[47] Tr. 647-49, 654-55, 659.

[48] CX-35.

[49] Tr. 651-52.

[50] Tr. 658-59.

Chen responded to Richman's email the same day he sent it, writing, "You are the best! Thank you for your continual support."[51]

2. Chen's False Reimbursement Requests

On June 27, 2012, Chen submitted the first of four $400 reimbursement requests. Instead of claiming funds to compensate her interns as she and Richman had discussed, she submitted a receipt for reimbursement for seven $60 candles from Nordstrom. Chen characterized the business purpose of the expense as "Client Gifts," listing the names of seven clients, and identifying the manager's discretionary allowance as the source for reimbursement. The same day, Chen cancelled the Nordstrom order. The total cost was $456.75, but Chen sought reimbursement only for the $400 she understood Richman agreed to grant her monthly. Morgan Stanley approved and paid this request.[52]

Again in July, September, and October 2012, rather than use the funds for the agreed purpose of defraying the cost of interns, Chen filed expense reports to claim reimbursements for "client gifts" she purportedly purchased from Nordstrom. She cancelled each order on the same day. Morgan Stanley approved and paid all three reimbursement requests.[53]

C. Morgan Stanley's Investigation

Late in April 2013, Chen's then-immediate supervisor, Justin Frame, learned Morgan Stanley was conducting an investigation into Chen's and Yuen's expense reports. Frame instructed Chen to attend a meeting with auditors to answer questions arising from their review.[54]

The meeting was scheduled for May 2, 2013. In the meantime, on May 1, Chen repurchased hundreds of gifts she had earlier bought and cancelled, charging more than $19,000 to her credit card.

Present at the May 2 meeting were Frame, risk officers, a Morgan Stanley investigator, and a new complex manager who had replaced Richman. To explain the cancelled orders, Chen claimed that it had been her practice to sometimes cancel orders after submitting receipts, and then later reorder the same gifts.[55] However, a review of expense reports she had submitted prior to those under investigation did not corroborate her claim.[56] Chen said she would find and

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[51] CX-35a.

[52] Tr. 75-77, 85-86; CX-5, at 1-2. Chen testified that nobody inquired why she submitted receipts for client gifts instead of for interns. Tr. 842.

[53] Stips. ¶¶ 12-28.

[54] Tr. 276-77.

[55] Tr. 278.

[56] Tr. 281-82.

produce the documentation to verify her reorders. She did not disclose she had just reordered many of the items the day before. At the conclusion of the meeting, management placed Chen on administrative leave while the investigation continued, during which time she was to gather the documents she promised to produce.[57]

The next day, Chen's husband, an attorney, sent an email to Morgan Stanley on her behalf. In it, he made a number of representations characterizing what she had told management at the meeting. He claimed that Chen had described using "a particular accounting system for her expense reimbursements" whereby she would order client gifts, change her mind, and cancel the orders. He claimed that Chen intended to renew the orders without seeking reimbursement, but her administrative assistant had refused her requests to prepare the paper work, so the cancelled orders "remained on the expense reports." The email also claimed that Chen had explained that two of her managers encouraged and approved this "accounting system."[58]

However, at the hearing Chen admitted the representations in the email were not entirely truthful. She testified that at the meeting she did not claim to have used a "particular accounting system" approved by two managers.[59] She testified that, contrary to what she said at the meeting, when she cancelled the orders, she did not intend to replace them with new orders. She explained her objective at the May 2 meeting was to "buy time" by promising to produce documents that would explain everything.[60]

Morgan Stanley terminated Chen's and Yuen's employment the week following the meeting.

III. The First Cause of Action: Conversion

FINRA's Sanction Guidelines define conversion as the "intentional and unauthorized taking of and/or exercising of ownership over property by one who neither owns the property nor is entitled to possess it."[61] In this instance, to prove the charge of conversion, Enforcement's burden was to establish that Chen intentionally took funds from Morgan Stanley to which she was not entitled.[62]

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[57] Tr. 278-79.

[58] CX-38, at 1.

[59] Tr. 219-21.

[60] Tr. 879.

[61] FINRA Sanction Guidelines ("Guidelines") at 36, n.2 (2015), https://www.finra.org/industry/sanction-guidelines.

[62] *Dep't of Enforcement v. Olson*, No. 2010023349601, 2014 FINRA Discip. LEXIS 7, at *12 (Bd. of Governors May 9, 2014), *aff'd*, Exchange Act Release No. 75838, 2015 SEC LEXIS 3629 (Sept. 3, 2015).

A. The Original Charge

As noted above, the Complaint charges Chen with converting $1,600 she obtained in reimbursements from discretionary funds Richman authorized.

The Complaint describes the two programs Morgan Stanley established specifically to fund allowable business expenses, as detailed above: BDA, a $5,000 annual allowance provided to Chen; and AFG, the source of the majority of Chen's falsely obtained reimbursements, "funded by Chen's pre-tax compensation."[63] However, Enforcement did not charge Chen with converting the reimbursements Morgan Stanley paid her from BDA or AFG.

Instead, Enforcement charged conversion only for the four $400 reimbursements Morgan Stanley paid Chen from Richman's discretionary funds "to reimburse her for expenses associated with new business development."[64] Enforcement confined the conversion charge to these four payments because it initially determined they were the clearest instances of conversion. The Complaint alleges that Chen: knew these reimbursements came "directly from Morgan Stanley,"[65] not from her own pre-tax compensation; knew she was not entitled to the reimbursements; and by taking the money, knowingly converted $1,600 of Morgan Stanley's funds, in violation of FINRA Rule 2010.[66]

B. Enforcement's Request to Amend the Conversion Charge

Enforcement filed the Complaint on August 13, 2014. On July 9, 2015, approximately five weeks before the hearing, Enforcement filed its pre-hearing brief. Changing course, Enforcement asked the Panel to deem the Complaint amended to charge that Chen converted *all* of the funds Morgan Stanley paid in falsely claimed reimbursements, not just the $1,600 charged in the original Complaint. Enforcement claimed the evidence at the hearing would prove that Chen "converted the entire amount she received." Therefore, Enforcement argued, the Panel should conform the charges to the evidence and hold that Chen converted the entire amount or, alternatively, should "view the entire amount converted as uncharged misconduct relevant to sanctions."[67]

Chen objects to what she characterizes as an unfair, last-minute attempt to amend the Complaint, and urges the Panel not to consider any conversions not charged in the Complaint.[68]

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[63] Compl. ¶¶ 1, 5-7.

[64] *Id.* at ¶ 28.

[65] *Id.* at ¶¶ 27-28.

[66] *Id.* at ¶¶ 31-33.

[67] Enforcement's Pre-Hr'g Br. at 8-9

[68] Respondent's Opening Post-Hr'g Br. at 5-6.

Chen also argues that she cannot be found to have converted funds Morgan Stanley paid her from pre-tax compensation because the funds rightfully belonged to her, not to the Firm.[69]

C. Discussion

FINRA Rule 9212(b) governs amendments to complaints in FINRA proceedings. It permits Enforcement to file an amended complaint without leave before a respondent files an answer. Even after an answer is filed, a hearing officer may allow "amendments so as to make the complaint conform to the evidence presented," after considering whether Enforcement "has shown good cause for the amendment and whether any Respondent will suffer any unfair prejudice if the amendment is allowed." Amendments should be "freely granted when justice so requires."

Enforcement argues that "in similar cases, hearing panels have routinely allowed the charges to be conformed to the evidence."[70] The cases cited by Enforcement support the notion that a hearing officer may permit an amendment during or after a hearing to make the complaint conform to the evidence.[71]

In one case Enforcement cited, the National Adjudicatory Council ("NAC") recently held that a hearing panel in effect amended a complaint to find that a respondent converted money from an investment fund, when the complaint charged him with converting the money from the *investors* in the fund. However, the NAC pointed out the distinction between the charge and the proof "is one without a difference" because "the gravamen of Enforcement's complaint is that [the respondent] took monies invested in the Fund and used those monies for an unauthorized purpose" and the complaint provided the respondent with adequate notice of the charge.[72]

In another case, the NAC held that a hearing panel properly sustained a complaint that failed to specify the exact subsections of the rule allegedly violated because the language of the complaint provided sufficient notice of the charges.[73] Similarly, the NAC upheld another hearing panel decision despite the respondent's objection that the hearing panel had constructively amended the complaint by holding that the respondent had aided and abetted a manipulation scheme when the complaint did not use the terms "aid" or "abet." The NAC held that because the

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[69] Tr. 957-58, 965-66; Respondent's Opening Post-Hr'g Br. at 9, ¶¶ 1, 3, 9.

[70] Enforcement's Post-Hr'g Reply Br. at 5.

[71] *Id.* at 3-5 and nn.12, 14-15, 19.

[72] *Dep't of Enforcement v. Grivas*, No. 2012032997201, 2015 FINRA Discip. LEXIS 16, at *2, n.3 (NAC July 16, 2015), *appeal docketed*, No. 3-16756 (SEC Aug. 14, 2015). *See also Dist. Bus. Conduct Comm. v. Euripides*, No. C9B950014, 1997 NASD Discip. LEXIS 45 (NBCC July 28, 1997) (upholding a charge that respondent made unsuitable recommendations even though the complaint did not cite the suitability rule, because the complaint tracked the language of the rule precisely).

[73] *Dist. Bus. Conduct Comm. v. Podesta & Co.*, No. C8A960040, 1998 NASD Discip. LEXIS 27 (NAC Mar. 23, 1998).

language alleged that the respondent engaged in or, alternatively, assisted the furtherance of the manipulative scheme, it provided sufficient notice that the respondent was charged with aiding and abetting.[74]

Other cases cited by Enforcement declined to permit amendment. In one, the hearing panel rejected Enforcement's attempt to adopt a new theory of liability during closing arguments at the hearing because the theory was not set forth in the complaint. The hearing panel held that Enforcement failed to demonstrate good cause for its belated amendment, when the record showed Enforcement knew the relevant facts and could have amended the complaint earlier, and found that the respondents were placed at an unfair disadvantage because they had focused on defending the charge specified in the complaint.[75] In another, the Securities and Exchange Commission set aside a hearing panel finding that the respondent executed 18 unauthorized trades not mentioned in the complaint, holding that to sustain the finding would be inappropriate. The hearing panel had relied on declarations prepared by a FINRA examiner and signed by four customers who did not testify.[76]

The cases Enforcement cites affirming amendments to conform to the evidence are not materially similar to this case and do not resolve the issue before us. They focus primarily on whether granting amendments deprived respondents of fair notice.

This case is different. Here, the language of the Complaint reflects a deliberate choice by Enforcement not to charge Chen with converting the majority of the reimbursements funded by her pre-tax compensation. Enforcement crafted the Complaint apparently in anticipation of Chen's defense that she was entitled to those funds, and therefore could not convert them because it is legally impossible to convert something one is entitled to possess. Indeed, Chen argues that she sought "reimbursement from funds that she reasonably believed were her own wages";[77] what she '"took' was hers";[78] the source of the reimbursements "was 'her money"';[79] and it "belonged to her and not to Morgan Stanley."[80] Enforcement anticipated Chen's defense

[74] *Dep't of Mkt. Regulation v. Proudian*, No. CMS5040165, 2008 FINRA Discip. LEXIS 21, at *21, n.22 (NAC Aug. 7, 2008).

[75] *Dep't of Enforcement v. Berry-Shino Sec., Inc.*, No. C3A030001, 2003 NASD Discip. LEXIS 61, at *31-33 (OHO Dec. 10, 2003).

[76] *Wanda P. Sears*, Exchange Act Release No. 58075, 2008 SEC LEXIS 1521, at *9, 12 (July 1, 2008).

[77] Respondent's Pre-Hr'g Br. at 1.

[78] *Id.* at 9.

[79] *Id.* at 10.

[80] *Id.* at 11-12.

by charging that Chen intentionally converted only the $1,600 she received directly from Morgan Stanley, knowing that the source was funds from Morgan Stanley.[81]

When asked at the hearing to explain why Enforcement so limited the conversion charge, Enforcement's counsel responded that because Chen considers the funds allocated from her pre-tax compensation to be her money, it was more "clean cut" and "easier to prove" that the $1,600, paid from Morgan Stanley's manager's discretionary allowance "clearly … belonged to the firm" and Chen had no claim of right to the money.[82] Neither during nor after the hearing did Enforcement explain why it sought to amend the Complaint through its pre-hearing brief rather than file a motion to amend the Complaint earlier in the proceeding.

Enforcement's arguments for permitting the amendment are unpersuasive. Enforcement acknowledges that it framed the Complaint to make its burden of proof easier, and then decided to announce its change of course in its pre-hearing brief. Enforcement has made no showing of good cause for permitting the amendment, nor has it explained why justice requires allowing the amendment at the eleventh hour with no prior notice to Chen. For these reasons, Enforcement's request to amend the Complaint is denied.[83]

D. Chen's Defenses to the Conversion Charge

Chen argues that she did not convert the $1,600 because the money "was always intended as compensation" for the loss of her client's account.[84] Chen claims that Richman "disguised" the payments as reimbursements to replace, in her words, "my compensation that I lost."[85] Chen claims further that the email from Richman documenting the offer of the discretionary funds to defray the cost of her interns was a "CYA" memo to hide the fact he was replacing her "earned income."[86] She testified that Richman never told her that the discretionary funds had to be used to pay interns.[87] Thus, Chen argues, a necessary element of conversion is absent: the intent to take something that was not hers.[88]

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[81] Compl. ¶¶ 1, 27-28.

[82] Tr. 946-47.

[83] We also decline Enforcement's alternative request, to consider the "entire amount converted as uncharged misconduct relevant to sanctions."

[84] Respondent's Opening Post-Hr'g Br. at 1, 18.

[85] Tr. 86.

[86] Tr. 209-10.

[87] Tr. 829.

[88] Respondent's Opening Post-Hr'g Br. at 18, 21. Chen argues that if Enforcement is allowed to amend the Complaint to include AFG funds in the conversion charge, Chen cannot be found to have converted the funds because under California's Labor Code AFG funds are wages and Morgan Stanley was prohibited from applying her wages to cover reasonable business operating expenses for which California law makes the employer responsible.

Chen testified that even though the $400 per month was "really, really small" in comparison to the income she lost with the departure of her client, she accepted it because Richman made it clear that he would not offer more.[89] Chen also testified that Richman told her she could use the money however she wished. Finally, Chen argues that despite Richman's memo stating the funds were to be used to defray the cost of interns, her reimbursement requests were for gifts, and Morgan Stanley approved them. This told her "it was okay" to file false receipts and use the money as her own.[90]

Chen claims that her understanding was consistent with Morgan Stanley management's approach to all business expense reimbursements. For example, she testified that managers referred to AFG as "brokers' funds,"[91] described AFG funds as a pre-tax benefit, and "didn't really care"[92] how much advisors allocated to AFG because "it's like tax-free money" for advisors to use as they saw fit.[93] Chen testified that Burda, her immediate supervisor, reinforced this view. As an example, she claimed that when she purchased a painting for her office, she asked Burda if she could seek reimbursement for it as a business expense, and Burda said if she submitted an expense report, he would approve it because "it's your money."[94] Chen testified this supported her view that the business expense reimbursement system was "like a loophole" for obtaining additional compensation.[95]

Chen also claims that Richman compensated her in 2011 for revenue she lost when another advisor, with whom she had a joint commission agreement, "poached" one of her clients, who was that advisor's relative.[96] Chen demanded Burda and Richman take action to replace her lost commissions. Instead, they offered her "a small, small portion" of the "perpetual earnings" she claimed she lost, offering her $800 in T&E reimbursements to "do whatever" she chose with the money.[97] Chen claims this was when Richman, in a September 2011 email, initially suggested that "branch managerial T&E awards could be used to replace 'effective after-tax

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Tr. 961-64; Respondent's Opening Post-Hr'g Br. at 20. Because the Panel declines to grant Enforcement's proposed amendment to the Complaint, we do not need to decide if the California Labor Code applies to this proceeding, whether Morgan Stanley's use of the AFG allocation violated California law, or whether such a violation requires dismissal of the conversion charge.

[89] Tr. 830.

[90] Tr. 895.

[91] Tr. 804.

[92] Tr. 799.

[93] Tr. 794.

[94] Tr. 802.

[95] Tr. 802. Chen testified that she did not seek reimbursement for the painting.

[96] Tr. 806-07.

[97] Tr. 810-12.

income' and lost client commissions."[98] On that occasion, too, although she thought the offer inadequate, she accepted it because it was management's final decision.[99]

E. The Evidence

Richman did not have a clear recollection of Chen's claim that an advisor had poached a client, but acknowledged he awarded Chen additional T&E funds to assuage her by a show of support because the client account had been Chen's before the other advisor joined Morgan Stanley.[100]

Richman denied indicating in any way to Chen that the award of $400 per month in discretionary funds was intended as compensation for the loss of income from the client who left Morgan Stanley.[101] In fact, Richman was determined *not* to replace the lost client revenue because he believed Chen was being unreasonable. He made sure he was "very specific" in his email documenting the purpose for the funds, and he was satisfied Chen understood this.[102] He adamantly denied that the email Chen described as a "CYA" memo was intended to disguise the purpose of his award; rather, the twofold purpose of the email was to document the award of the funds to Chen, and to inform her in writing that "the only thing" the funds were to be used for was to "reimburse [for] the interns."[103]

As for the approval of the reimbursement requests with their false receipts for client gifts, Richman was not responsible for approving Chen's expense reports and did not see them; for low amounts like these, a branch manager's delegate would review them and forward them directly to the accounting department for payment.[104] Furthermore, when Frame became manager of the Brea branch office, a Morgan Stanley auditor asked Frame about one of Chen's $400 reimbursement requests. Frame found nothing improper after learning that Richman, who had left Morgan Stanley by then, had approved the funds to help Chen by providing additional resources for business development.[105]

Other testimony corroborates Richman, and undermines Chen's testimony that Morgan Stanley managers encouraged her and other advisors to treat T&E reimbursements as supplemental income. Burda testified that he never suggested to Chen she could use AFG funds

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[98] Respondent's Opening Post-Hr'g Br. at 2-3.

[99] Tr. 809-10.

[100] Tr. 734-36.

[101] Tr. 649.

[102] Tr. 654, 658-60.

[103] Tr. 759-60.

[104] Tr. 636.

[105] Tr. 358-62.

as her income or that it was acceptable to file false expense receipts, and he had no recollection of discussing a painting she purchased for her office.[106] Frame testified that all T&E funds were intended for business growth, not for compensation. He denied that he told Chen she could spend T&E funds however she wished, or that she could use reimbursements for purposes other than what she claimed they were for.[107] Jamie Kemp, head of Morgan Stanley's Office of Business Management, formerly in charge of the Firm's field finance division,[108] testified that AFG funds were firm funds set aside at the request of advisors to be used for business development purposes, not to be an additional source of compensation for advisors.[109] The Panel finds this testimony credible.

Chen argues that because Richman granted her the funds at a time when he and Burda were concerned she might leave Morgan Stanley, it must have been intended as compensation. But the Panel finds it is more plausible that the award, as Richman, Burda, and Frame testified, was intended to mollify Chen's concern that she was being treated unfairly, and to show Chen that Morgan Stanley would support her efforts to find additional clients to replace the one she lost.

Finally, Chen argues that Morgan Stanley's approval of the four false reimbursement reports, all of which claimed to be for client gifts, not for covering the cost of interns, proves the "obvious" fact that the award "was always intended to compensate Chen" for lost revenue.[110] The Panel disagrees. That the false claims were approved despite being purportedly for expenditures unauthorized by Richman may be evidence of flaws in Morgan Stanley's auditing process, but it does not prove, as Chen claims, that "[e]verybody at the branch and complex levels knew" the purpose was to pay Chen for lost commissions. [111]

F. Credibility

In her defense against the conversion charge, Chen attacks the credibility of the Morgan Stanley witnesses who contradicted her claims. Chen claims that her testimony should be believed because it was "unwavering, consistent and credible" and the testimony of Richman, Frame, and Burda should be rejected because their testimony was "inconsistent and implausible."[112] The Panel disagrees.

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[106] Tr. 453-55.

[107] Tr. 253-55.

[108] Tr. 394.

[109] Tr. 397-99.

[110] Respondent's Opening Post-Hr'g Br. at 4.

[111] *Id.*

[112] *Id.* at 1-2.

First, Chen's attack on Richman's credibility fails. The Panel found no evidence Richman was biased for or against Chen or Morgan Stanley. Richman testified without contradiction that he voluntarily left Morgan Stanley at the end of 2012 when he became "disillusioned" by the direction the Firm was taking.[113] In advance of the hearing, he informed Chen's counsel he "was not really interested in helping either party" in this case.[114]

Second, Chen's claim that Richman first suggested in 2011 that T&E awards could replace lost client commissions misconstrues the evidence. In his email about resolving the conflict between Chen and the advisor who poached her client, Richman simply explained that Chen should find his T&E award fair because it "effectively" came to more than she may have earned through the joint production agreement she claimed had been dishonored by the other advisor.[115] Although Richman did not specify exactly what the T&E award was to be used for, nothing in it can be construed to authorize Chen to submit false expense reports to claim the award.

Third, the testimony of Richman, Burda, and Frame was consistent and corroborated by documentary evidence on the essential point: expense reimbursements were to be used for approved business expenses, not supplemental salary. Chen argues that by granting the discretionary fund award after she lost her client, Richman gave her permission to file the false reimbursement claims to reclaim "her money." The Panel disagrees. Based on the testimony of Richman, Burda, Frame, and Kemp, which we find credible and corroborated by the documentary evidence, Richman clearly communicated, and Chen clearly understood, the discretionary award was to be used for approved business development activities, and was not meant to replace lost commissions. With the award, Morgan Stanley did not supplement her salary, but gave her access to firm money for approved business development efforts to help her find clients to replace the one she had lost.

In contrast, the Panel does not find Chen credible. First, immediately after her meeting with the Morgan Stanley auditors, she admitted she falsely represented that she had followed an approved "particular procedure" and falsely blamed her former administrative assistant for refusing to process paperwork properly. [116]

Second, Chen's testimony at the hearing was transparently self-serving, contradictory, and inconsistent. For example, Chen asserted that her assistant's suggestion about how to recover unused AFG funds was the "genesis" of her filing false expense reports.[117] While claiming not to blame anybody else for what she did, she "figured" the suggestion must have been "kosher"

[113] Tr. 682-84.

[114] Tr. 680-84.

[115] RX-6.

[116] Tr. 219-21.

[117] Tr. 812-13, 897-98.

because her assistant was married to "the compliance officer at a Fortune 100 company." Chen, purportedly relying on the assistant, consented to the procedure, and the assistant obtained approval for the false claims.[118] Yet, Chen admitted, "I knew what I did was wrong." [119]

At several points during the hearing, Chen revealed a sense of entitlement and disregard for the rules governing brokers' conduct. Although conceding the obvious point that filing false expense reports is wrong, she minimized the seriousness of her misconduct, asserting that funds earmarked for business expenses were her money,[120] stating "all I did was [file] a false receipt to get my money back."[121] At another point, Chen testified that she raised her AFG allocation rate to 10 percent for 2013 in part because she felt "wronged" by Morgan Stanley, claiming her grievances justified filing false reports, again in her words, "to get my money back."[122]

G. Conclusion

As the facts set forth above establish, Chen converted $1,600 of Morgan Stanley funds as charged. Chen stipulated and testified that she filed four false expense reports with receipts for Nordstrom orders after cancelling the orders,[123] representing she had made the purchases and had given the gifts to clients when she had not,[124] and consequently received a total of $1,600 from Morgan Stanley funds.[125] Chen intentionally limited the four reimbursement requests to $400 each because Richman had authorized her to be reimbursed only for that amount.[126] Chen knew the reimbursements she received came from Morgan Stanley[127] through a manager's discretionary fund.[128] Chen testified that she knew her actions violated Morgan Stanley policy and, policy aside, she knew "it was wrong because you shouldn't be submitting false expenses."[129] And contrary to Chen's enthusiastic expression of gratitude to Richman in response to his offer of assistance—"You are the best! Thank you …"—she believed Morgan

[118] Tr. 813-14, 897-98.

[119] Tr. 895.

[120] Tr. 892.

[121] Tr. 883.

[122] Tr. 883, 893-94.

[123] Tr. 846; Stips. ¶¶ 9-29.

[124] Tr. 73-78.

[125] Tr. 842.

[126] Tr. 73-74.

[127] Tr. 86-88.

[128] Tr. 209.

[129] Tr. 233, 236.

Stanley had wronged her, Richman's offer of only $400 per month was an insult,[130] and she was entitled to obtain "her" money by filing false reports. Her actions constituted conversion.

IV. The Second Cause of Action: Falsification of Documents and Books and Records

A. The Charge

The Complaint's second cause of action charges that Chen prepared 12 false reimbursement requests, representing that she had incurred legitimate business expenses, in violation of FINRA Rule 2010's ethical mandate to observe just and equitable principles of trade and high standards of commercial honor. Noting that FINRA Rule 4511 and its predecessor NASD Rule 3110 require FINRA members to create and maintain books and records that conform to the Securities Exchange Act of 1934 and Exchange Act rules,[131] the second cause of action further alleges that by submitting the false reimbursement claims, Chen caused Morgan Stanley to maintain inaccurate books and records, in violation of NASD Rule 3110 and FINRA Rules 4511 and 2010.[132]

B. Chen's Defense

As discussed above, Chen acknowledges preparing and submitting the 12 false reimbursement requests.[133] In her post-hearing brief, she "admits, accepts responsibility, and is remorseful for having submitted a dozen false expense reports to recapture compensation or advance payment of her net wages in violation of Morgan Stanley policies."[134] Conceding that she violated FINRA Rule 2010, she nonetheless denies her conduct constituted a books and records violation of NASD Rule 3110 and FINRA Rule 4511. Chen argues that there is no evidence establishing that any Morgan Stanley books and records were falsified; that any erroneous information in the Firm's records were material; or that Morgan Stanley revised any books and records to correct any misinformation they contained. Chen also claims that since Morgan Stanley has not been charged with a books and records violation of Rule 4511, she cannot be charged with that violation. Finally, Chen asserts that "Morgan Stanley's unlawful

[130] Tr. 144.

[131] Section 17(a) of the Exchange Act and SEC Rule 17a-3(a)(2) require broker-dealers to create and maintain current records "reflecting all assets and liabilities, income and expense and capital accounts."

[132] NASD Rule 3110's provision requiring members to maintain books and records pursuant to SEC Rule 17-a3 was superseded by FINRA Rule 4511 on December 5, 2011. Chen first submitted the reimbursement claims at issue in November 2011, when NASD Rule 3110 was in effect. Her subsequent submission of reimbursement claims spanned January 2012 to April 2013, when FINRA Rule 4511 was in effect.

[133] Stips. ¶¶ 3-65.

[134] Respondent's Opening Post-Hr'g Br. at 8.

compensation practices were the root source of any false books and records maintained by the firm."[135]

C. Discussion

Each of Chen's claims fails. First, Chen does not dispute that she filed false expense reports. Once filed, the false expense reports became Morgan Stanley records. FINRA Rule 4511, essentially identical to NASD Rule 3110, requires members to "make and preserve books and records as required" by FINRA rules and the Exchange Act and rules promulgated thereunder. Section 17(a) of the Exchange Act and SEC Rule 17a-3(a)(2) require broker-dealers to create and maintain current records including those "reflecting all assets and liabilities, income and expense."

Second, Chen submitted her false expense reports to Morgan Stanley knowing the Firm would review them and pay her. She listed numerous clients and hundreds of gifts, which became Morgan Stanley's record of client gifts, which the Firm was required to maintain to document compliance with FINRA rules governing the limits on permissible gifts from brokers to their clients.[136] The false reports resulted in expenditures of Morgan Stanley funds, for which the Firm's accounting and reporting of its spending, and calculations of its profit and loss, in compliance with FINRA and SEC regulations, were inaccurate.[137] Neither FINRA nor Exchange Act rules require evidence that inaccuracies are "material" or that a member firm revised and corrected the filed false reports. As Brea branch manager Frame testified, he was responsible for the accuracy of the books and records documenting the business activities under his supervision. Even though the expenditures involved here may be small compared to Morgan Stanley's total income and expenses, Frame testified that their falsity "taints all the numbers."[138] According to Kemp, head of Morgan Stanley's Office of Business Management, Morgan Stanley reimbursed advisors for business expenses with the expectation that the advisors would appropriately use the Firm's resources for the purpose of increasing revenue.[139] Morgan Stanley thus incurred costs that it would not have otherwise paid, to the detriment of the branch, and maintained records that inaccurately showed the receipt of resources the advisor or her customers did not receive,[140] which the Firm had the responsibility to report accurately in its books and records.[141]

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[135] *Id.* at 22.

[136] Tr. 282.

[137] Tr. 283.

[138] Tr. 386.

[139] Tr. 406.

[140] Tr. 409-10.

[141] Tr. 411.

Third, Chen's claim that because Morgan Stanley has not been charged with a books and records violation, she cannot be found culpable of causing the Firm's books and records to be inaccurate, is incorrect. There is no requirement that the Firm must be charged as a precondition to filing such a charge against a broker. Chen relies on two federal appellate court cases, but her reliance on these cases is misplaced. The cases concern the elements required to legally establish a finding of liability under Exchange Act Section 10(b), Rule 10b-5 thereunder, and related misconduct for fraudulently aiding and abetting a violation of the securities laws.[142] In this case, Chen is not charged with being an aider and abettor; rather, she is charged as a principal with filing false expense reports, which became Morgan Stanley records. Whether or not Morgan Stanley was charged has no bearing on Chen's culpability.

Finally, the Panel finds that the record does not support Chen's contention that Morgan Stanley engaged in "unlawful compensation practices" or, even if there were such evidence, that the Firm's practices justified her in filing false expense reports.

For these reasons, the Panel finds that by filing the false expense reports, Chen violated FINRA Rule 2010 by failing to observe just and equitable principles of trade and high standards of commercial honor, [143] and violated NASD Rule 3110 and FINRA Rule 4511, by causing Morgan Stanley to maintain inaccurate records, as charged in the second cause of action.

V. Sanctions

A. The Parties' Recommendations

Describing Chen's misconduct as egregious, Enforcement contends a bar is the appropriate sanction for each of the two violations. Enforcement argues that the following aggravating factors contribute to the degree of egregiousness: Chen's 12 false reports over 17 months constitute a pattern of misconduct; Chen harmed Morgan Stanley because it paid her based on the false expense reports; Chen acted intentionally, not negligently or recklessly, and did so for personal financial gain; Chen failed to accept responsibility, and instead sought to shift responsibility to her managers and her assistant.

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[142] Chen cites *Ponce v. SEC*, 345 F.3d 722 (9th Cir. 2003), and *Dennis v. Gen. Imaging, Inc*., 918 F.2d 496 (5th Cir. 1990). Neither case involves the books and records violations under SEC Rule 17a-3. In *Ponce*, the respondent was a Certified Public Accountant charged with, among other things, fraudulently aiding and abetting his firm's violations of federal securities laws by filing false financial statements on the firm's behalf. *Ponce*, 345 F.3d 722, 725-26. The court employed a traditional aider-abettor analysis requiring a primary violation by the firm, and knowing substantial assistance by the respondent. *Id*. at 737-38. *Dennis* is a private suit alleging fraud in which the trial court granted summary judgment in favor of defendants. *Dennis*, 918 F.2d 499, 508.

[143] *Dep't of Enforcement v. McCartney*, No. 2010023719601, 2012 FINRA Discip. LEXIS 60, at *7-8 (NAC Dec. 10, 2012) (respondent violated NASD Rule 2110 when he prepared and submitted a false expense report, false receipt, false verification letter, and falsified check to obtain monetary reimbursement to which he was not entitled); *Dep't of Enforcement v. Leopold*, No. 2007011489301, 2012 FINRA Discip. LEXIS 2, at *23-25 (NAC Feb. 24, 2012) (respondent violated NASD Rule 2110 when he submitted false expense reports, for which he was not reimbursed, with fictitious hotel invoices and forged signatures of registered representatives and false verification letters to reduce his tax liability).

Chen claims she is remorseful for her wrongdoing and is willing to accept a "serious sanction,"[144] but argues a bar is too harsh. Rather, she argues, a year's suspension and fine would suffice. Chen insists she did not convert Morgan Stanley funds, arguing she "either misunderstood or had a good faith, but mistaken, belief of express or implied authority" from Morgan Stanley that she could use the $1,600 in discretionary funds "however she wanted."[145] She argues that the Panel should consider her remorse; her "otherwise unblemished record"; her cooperation with Enforcement's investigation; the loss of her job at Morgan Stanley; her reasonable belief that Morgan Stanley treated her unfairly; "the illegality of Morgan Stanley's expense reimbursement system under California law"; the testimony of a customer who attested to her good character; the lack of harm to Morgan Stanley; and the absence of harm to the investing public.[146]

B. Discussion

1. Conversion

Recently the SEC reiterated its agreement with the Guidelines' frequently cited statement that the standard sanction for conversion, for any amount of money, is a bar.[147] The Commission affirmed a hearing panel's imposition of a bar in a case involving a single false claim for reimbursement for less money than Chen converted, stating that conversion, by its nature, is an offense "antithetical to the basic requirement that customers and firms must be able to trust securities professionals with their money,"[148] and "renders the violator unfit for employment in the securities industry."[149] Thus, under the Guidelines, even "a single instance of theft provides ample justification to bar an individual from the securities industry, no matter the sum involved."[150]

The Panel concurs with Enforcement's assessment of the principal aggravating factors. Focusing solely on Chen's four $400 conversions, we find a pattern of misconduct perpetrated over an extended period, not an isolated, negligent or impulsive action.[151] Chen filed the fabricated expense reports in June, July, September, and October 2012, exhibiting "flagrant

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[144] Enforcement's Post-Hr'g Br. at 24.

[145] Respondent's Opening Post-Hr'g Br. at 23-24.

[146] *Id.* at 24-25.

[147] Guidelines at 36.

[148] *Denise M. Olson*, Exchange Act Release No. 75837, 2015 SEC LEXIS 3629, at *9 (Sept. 3, 2015).

[149] *Id.*, quoting *Charles C. Fawcett, IV*, Exchange Act Release No. 56770, 2007 SEC LEXIS 2598, at *22, n.27 (Nov. 8, 2007).

[150] *Olson*, 2015 SEC LEXIS 3629, at *20 (quoting *Olson*, 2014 FINRA Discip. LEXIS 7, at *24, n.18).

[151] Guidelines at 6 (Principal Considerations 8-9, 11).

dishonesty,"[152] motivated by a desire for monetary gain to obtain funds she felt Morgan Stanley owed her.[153] By submitting false receipts and fabricating the names of client gift recipients, Chen concealed her misconduct and misled her employer.[154]

Despite her profession of remorse for filing false expense reports, we cannot consider as mitigating her claim to have accepted responsibility for her conduct to her employer.[155] First, Chen did not volunteer information about her misconduct; Morgan Stanley detected it through its investigation. Second, when Morgan Stanley questioned her, Chen falsely claimed she acted with managerial approval and attempted to place blame on her assistant. Third, Chen never conceded she converted Morgan Stanley funds, despite indisputable evidence. Instead, Chen minimized her misconduct by testifying she merely "filed a false receipt to get my money back."[156]

Chen also claims she deserves credit for having an "unblemished record" in her securities industry career and for cooperating with FINRA's investigation. The Panel has considered both claims, and finds them meritless. It is well established that securities industry professionals are expected to conform to high standards of ethical conduct; thus, Chen's lack of a disciplinary record is not a mitigating factor.[157] As for Chen's claim that her cooperation with FINRA's investigation is mitigating, there is no evidence that Chen provided the "substantial assistance to FINRA in its examination and/or investigation of the underlying misconduct" required to establish mitigation.[158]

Chen's other arguments regarding mitigating factors are also without merit. The Panel rejects Chen's assertion that she was motivated to obtain funds by false means because she reasonably believed she had been mistreated by Morgan Stanley. Even if we were convinced that Chen's employer owed her money for the loss of her client and other perceived unfair treatment, it has been held that "securities professionals are not entitled to self-help" to remedy perceived grievances.[159] We also decline to consider as mitigating Chen's claim that Morgan Stanley's reimbursement system violated California Labor law; whether it did is beyond the scope of our authority to decide. Even if Morgan Stanley's reimbursement system was flawed, it would not justify Chen in filing false expense reports.

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[152] *Olson*, 2014 FINRA Discip. LEXIS 7, at *12.

[153] Guidelines at 7 (Principal Consideration 17).

[154] *Id.* at 6 (Principal Consideration 10).

[155] *Id.* (Principal Consideration 2).

[156] Tr. 883.

[157] Guidelines at 6 (Principal Consideration 1 & n.1); *McCartney*, 2012 FINRA Discip. LEXIS 60, at *14, n.12.

[158] Guidelines at 7 (Principal Consideration 12).

[159] *Olson*, 2015 SEC LEXIS 3629, at *16.

Chen's claims that her misconduct did not harm Morgan Stanley or the investing public are also unavailing. Neither a lack of customer harm[160] nor taking funds by deception from a firm, as opposed to a customer, is mitigating.[161] And Chen's assertion that Morgan Stanley incurred no loss is factually inaccurate; the Firm made payments to Chen for reimbursement of purportedly reasonable business expenses—gifts to customers thought to ultimately benefit both Chen and Morgan Stanley. The evidence is clear that Morgan Stanley, as Chen knew, would not have paid the money if it had known it was simply placing cash in Chen's pocket.

Chen asks the Panel to consider the testimony of a customer who testified for her at the hearing as mitigating. He has known Chen for approximately seven years and remained her customer after her termination by Morgan Stanley. He testified he believes her to be "knowledgeable, trustworthy, and competent." He testified that although her termination from Morgan Stanley caused him some concern, he discussed it with Chen and decided to continue to retain her as his financial advisor.[162] However, he also testified that Chen did not disclose the reason she was terminated was that she submitted and received payment for false expense reports.[163] On the basis of this record, the Panel does not find the customer's testimony to be mitigating.

Finally, the Panel notes that the Guidelines call for us to consider whether Morgan Stanley disciplined her for the same misconduct at issue here.[164] The Central Registration Depository records show Morgan Stanley discharged Chen for "requesting and receiving reimbursement from the firm for expenses described as client gifts, when the orders for the gifts were cancelled by the representative."[165] The Panel is required to consider Chen's termination as a mitigating factor if it occurred as a result of the misconduct prior to FINRA's detection and investigation of the matter.[166] Morgan Stanley interviewed Chen about its investigation into her expense reports on May 2, 2013, and terminated her employment on May 6, 2013. There is no evidence in the record FINRA detected or began to investigate Chen's conduct before her termination.[167] Because it appears that Morgan Stanley terminated Chen for the same conduct underlying the conversion charge, prior to FINRA detecting her wrongdoing, the Panel finds her termination to be a mitigating factor.

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[160] *Blair Alexander West*, Exchange Act Release No. 74030, 2015 SEC LEXIS 102, at *45 (Jan. 9, 2015).

[161] *Richard Dale Grafman*, Exchange Act Release No. 21648, 1985 SEC LEXIS 2397, at *4, n.2 (Jan. 14, 1985).

[162] Tr. 769.

[163] Tr. 771.

[164] Guidelines at 7 (Principal Consideration No. 14).

[165] CX-1, at 4.

[166] *Olson*, 2015 SEC LEXIS 3629, at *17-18.

[167] Enforcement represents that Chen's termination "was not prior to regulatory detection," but provides no evidence in support. Enforcement's Post-Hr'g Reply Br. at 13.

However, the presence of this single mitigating factor does not diminish the egregiousness of Chen's misconduct. Chen's multiple false representations and conversions of Morgan Stanley money; her efforts to avoid accepting responsibility; her lack of truthfulness in sworn testimony; and her willingness to disregard her ethical obligations in order to pursue pecuniary self-interest reflect flagrant dishonesty incompatible with the integrity required by high standards of commercial honor and just and equitable principles of trade.

The Panel finds that Chen's misconduct shows her to be unfit to associate with any FINRA member firm or to be entrusted with the money of a firm or customers. On this record, we conclude that Chen poses a threat to the investing public and to FINRA member firms in any situation in which her self-interest might not coincide with the interests of clients or employers. For these reasons, the Panel concludes that to effect the remedial purposes of the Sanction Guidelines, protect the public interest, and deter others from engaging in similar misconduct, the only appropriate sanction is a bar.

2. Falsification of Documents

The Guidelines call for a fine of $5,000 to $146,000 for falsification of records and, when there are no mitigating factors present, consideration of suspension in any or all capacities for up to two years or, in egregious cases, a bar.[168] Two principal considerations are the nature of the documents and whether the respondent acted under a good-faith, though mistaken, belief of authority. For causing a firm's books and records to be inaccurate, the Guidelines recommend a fine from $1,000 to $15,000 and, in egregious cases, consideration of suspension for up to two years and a fine from $10,000 to $146,000, or a bar.[169]

The Panel agrees with Enforcement that Chen's falsification of records and creation of inaccurate books and records are egregious. In a pattern of misconduct, Chen intentionally filed numerous false expense reports for more than a year.[170] The nature of the false records is also an aggravating factor because Morgan Stanley relied on their accuracy to fulfill its regulatory obligations to document business expenses, including gifts to clients.

For the reasons discussed above, the Panel rejects Chen's claim that she acted under a reasonable but mistaken belief that her managers authorized or tacitly approved of her fabrication of the expense reports. We also find that Chen did not accept responsibility or acknowledge her misconduct to her employer or to FINRA prior to Morgan Stanley's discovery of her misconduct, and that her claim of remorse is unconvincing.[171] Chen's admission that she

[168] Guidelines at 37.

[169] Guidelines at 29.

[170] *Id.* at 6-7 (Principal Considerations 8-9, 13).

[171] *Id.* at 6 (Principal Consideration 2).

was motivated by the potential for monetary gain to which she felt entitled is an additional aggravating factor.[172]

We find it is an aggravating factor that Chen counseled Yuen–her junior partner, whom she initially hired as an intern, to whom she was a mentor, role model, and authority figure–to submit false expense reports as she had done for years.[173]

As discussed above, the Panel finds that although it is mitigating that Morgan Stanley fired her before FINRA discovered her wrongdoing, the mitigation is outweighed by the aggravating factors.

Chen argues the Panel should impose a five-month suspension and a fine of $5,000 for filing false expense reports because these are the sanctions Yuen accepted in his settlement with FINRA "for engaging in precisely the same conduct." To bar her, Chen insists, would be unjust and contrary to the Guidelines' express goal of promoting "consistency and uniformity."[174] The Panel disagrees.

The Guidelines do not require uniformity of outcomes in different cases. Indeed, the Guidelines "do not prescribe fixed sanctions" but recommend ranges of sanctions "[b]ased on the facts and circumstances presented in each case."[175] As the SEC stated, "the appropriate sanction to be imposed in a particular case cannot be determined by reference to the facts of other cases."[176] And the Guidelines acknowledge "the broadly recognized principle that settled cases generally result in lower sanctions than fully litigated cases to provide incentives to settle."[177]

Furthermore, although Yuen, like Chen, filed false reimbursement claims for purchases of client gifts he cancelled, his misconduct is materially distinguishable and less egregious. Yuen filed only five false reports claiming expenses of $11,206, compared to Chen's 12 reports

[172] *Id.* at 7 (Principal Consideration 17).

[173] Tr. 572, 588-89.

[174] Respondent's Opening Post-Hr'g Br. at 25, quoting Guidelines at 1.

[175] Guidelines at 1.

[176] *Davrey Financial Services, Inc.*, Exchange Act Release No. 51780, 2005 SEC LEXIS 1288, at *27 (June 2, 2005).

[177] Guidelines at 1; *Raghavan Sathianathan*, Exchange Act Release No. 54722, 2006 SEC LEXIS 2572, at *44-45 (Nov. 8, 2006) ("We have repeatedly stated that pragmatic considerations may justify lesser sanctions in negotiated settlements."); *Dep't of Enforcement v. Nicolas*, No. CAF040052, 2008 FINRA Discip. LEXIS 9, at *80 (NAC Mar. 12, 2008) (rejecting objection of respondents that others received lesser sanctions for related conduct, noting that "[t]he Commission has repeatedly rejected attempts by respondents to compare the sanctions imposed against them to the sanctions imposed against others.").

seeking over $40,000.[178] Based on Yuen's false reports, Morgan Stanley paid him $9,087,[179] mostly from his AFG account, including approximately $1,000 from his BDA account,[180] significantly less than the more than $28,000 paid to Chen. Furthermore, Yuen acted at the suggestion and with the approval of Chen, his trusted senior partner, who dealt with management on his behalf, and who told him that if any question arose about his reimbursement requests, she would deal with it.[181] Thus, the sanctions the parties agreed to in the settlement FINRA and Yuen reached provide no assistance to the Panel in determining the appropriate sanctions to impose here, and we decline to adopt them in this case.

Because of the egregiousness of her misconduct, the Panel finds that it is necessary to impose a bar for Chen's falsification of records and creation of false books and records. Based on the record of this case, the Panel concludes that a suspension and fine would not suffice to effect the remedial purposes of the Sanction Guidelines, protect the public interest, and deter others from engaging in similar misconduct.[182]

VI. Order

For violating FINRA Rule 2010 by converting funds her employer paid her as a result of falsified expense reports, and for violating NASD Rule 3110 and FINRA Rules 4511 and 2010 by submitting false expense reports, thereby causing her firm to maintain inaccurate books and records, Respondent Tracy Chen is barred from associating with any FINRA member firm in any capacity. Chen is ordered to pay costs in the amount of $8,238.65, which includes a $750 administrative fee and the cost of the hearing transcript.

The bars shall become effective immediately if this decision becomes the final disciplinary action of FINRA. The assessed costs shall be due on a date set by FINRA, but not less than 30 days after this decision becomes FINRA's final disciplinary action in this proceeding.

EXTENDED HEARING PANEL

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By: Matthew Campbell
Hearing Officer

[178] RX-49, at 3.

[179] RX-49, at 3.

[180] RX-49, at 3, n.1.

[181] Tr. 572-74, 592.

[182] We considered and rejected without discussion all other arguments by the parties.