

Quarterly Disciplinary Review

October 2011

FINRA® publishes this quarterly review to provide firms with a sampling of recent disciplinary actions involving misconduct by registered representatives. The sample includes settled matters and decisions in litigated cases (National Adjudicatory Council decisions and decisions of the SEC in FINRA cases). These summaries call attention to, and remind registered representatives and member firms of, specific conduct that violates FINRA rules and may result in disciplinary action.

FINRA also provides detailed [disciplinary information and decisions](#) and a summary of [monthly disciplinary actions](#) on its website.

Impersonating a Customer

- ▶ FINRA settled a matter involving a registered representative who persuaded an office assistant to impersonate a customer. The representative met with the customer to discuss investments. At that time, the customer provided the representative with information about her investments away from the representative's firm. The representative later asked an office assistant to impersonate the customer on a telephone call. Without the customer's knowledge or consent and in an effort to determine the total amount of the customer's investments away from the firm, the representative contacted the other investment firm and inquired about the customer's investments there. The representative relied on the office assistant to impersonate the customer and, using personal information the customer had provided to the representative, enabled the office assistant to answer personal security questions from the other investment firm.

FINRA found that the registered representative's conduct violated NASD Rule 2110* (ethical standards). FINRA fined the registered representative \$5,000 and suspended him in all capacities for 30 business days.

Private Securities Transactions and Outside Business Activities

- ▶ FINRA settled a matter involving a registered representative who engaged in private securities transactions and unapproved outside business activities, and violated FINRA's advertising rule. Without obtaining prior written approval or acknowledgement from the representative's member firm, between February 2008 and February 2009, the representative participated in customers' securities purchases for more than \$100,000 of interests in a limited liability company that he owned and operated, more than \$160,000 of promissory notes and more than \$60,000 of membership interests in a second limited liability company. Between June 2007 and March 2009, the representative also failed to provide prompt written notice to his member firm of two non-securities outside business activities for which he received, as compensation, more than \$20,000 in salary and rental income from a limited liability company that manages an office building, and approximately \$400 in commissions from his sales of health drinks.

The representative also participated in many sales seminars with customers in 2007 and 2008. At the sales seminars, the representative used sales literature for which he failed to obtain prior written approval from a principal at his firm. He also failed to file the sales literature with FINRA's Advertising Regulation Department, and the sales literature was not fair and balanced, contained exaggerated and unwarranted claims and included predictions of performance.

FINRA found that the registered representative's conduct violated NASD Rules 3030** (outside business activities by an associated person), [3040](#) (private securities transactions by an associated person), [2210](#) (communications with the public) and 2110* (ethical standards), and FINRA Rule [2010](#) (ethical standards). FINRA fined the representative \$10,000 and suspended him from associating with any member firm in any capacity for 12 months.

Inaccurate Information on a Customer Application

- ▶ FINRA settled a matter involving a registered person who provided inaccurate information on customer annuity applications. The representative sold variable annuities to a husband and wife. The customers signed the applications in New York, but the representative misrepresented on the applications that they had been signed in Florida and inserted inaccurate dates on the applications. Because the registered representative indicated that the customers had signed the applications in Florida, not New York, the customers did not receive the benefit of Regulation 60, which would have provided them with the right of rescission of the replacement annuity and reinstatement of the surrendered annuity within 60 days.

FINRA found that the registered person's conduct violated NASD Rule 2110* (ethical standards). As such, FINRA fined the registered person \$5,000 and suspended him in all capacities for one month.

Improper Sharing in a Customer's Losses

- ▶ FINRA settled a matter involving a registered representative who improperly shared in a customer's losses. A customer opened a securities account with the representative at his member firm and chose quarterly automatic rebalancing of her account. This feature caused automated purchases and sales of securities if any asset category in the customer's account deviated from his chosen account allocation by more than 5 percent of the account's value. In September 2008, the customer became concerned with the state of the stock market and ordered the representative to liquidate approximately \$100,000 of his securities positions. The representative executed the customer's request but forgot about the account's automatic rebalancing feature. As a result, the firm automatically reinvested the customer's sales proceeds in October. Thereafter, the registered representative reviewed the customer's account and mistakenly assumed that he had forgotten to process the customer's sales order in September. He contacted the customer and told him that he had not executed his sales request, but promised to "make it up" to the customer. The representative mailed the customer a check for \$15,000, which represented the losses that the representative calculated the customer's account had incurred.

The registered representative failed to inform his firm about the payment until April 2010 when FINRA began an investigation. The registered representative also failed to obtain written authorization from the firm and the customer to share in the customer's losses, and had not previously contributed financially to the customer's account. Under these circumstances, the representative's sharing in the customer's losses violated NASD Rules 2330[†] (customer's securities or funds) and 2110* (ethical standards). As such, FINRA censured the registered person and fined him \$5,000.

Ethical Violation Resulting From Prohibited Campaign Contribution

- ▶ FINRA settled a matter involving a registered representative who violated FINRA's ethics rules by making numerous political contributions to various candidates and parties in a manner contrary to state law. The registered representative made a series of political campaign contributions for local, county, municipal and statewide races in his state. In all, he donated approximately \$120,000 to 19 campaigns, all in the names of his wife and step-children. The representative thereafter admitted that he violated a section of the state code that prohibited political contributions in another person's name. The state's election commission fined the representative \$95,000 and the state department of commerce division of securities suspended his securities license for 45 days based on a finding that the representative was "not of good business repute."

FINRA concluded that the registered representative's conduct violated NASD Rule 2110* (ethical standards). As such, FINRA suspended the representative in all capacities for 60 days and fined him \$10,000.

Improper Borrowing and Misrepresenting Scholarship Fund's Value

- ▶ FINRA settled a matter involving a registered representative who improperly borrowed funds from a customer and misrepresented the value of a corporate scholarship fund to members of the fund's managing board. The representative borrowed \$5,000 from a customer of his firm. The loan was not memorialized in writing and, at the time the loan occurred, the representative's member firm prohibited its registered representatives from borrowing money from customers. The loan also failed to meet the specific limitations outlined in NASD Rule 2370(a)(2). The representative did not obtain firm approval to borrow the funds and did not advise the firm of the loan.

The representative also served as the treasurer and as a board member of an incorporated scholarship fund. As treasurer, the representative received monthly account statements for a securities account that the fund owned at a FINRA member firm and for which he was the representative of record. The representative reported orally and in writing to the fund's management board the most recent month-end total value of the fund's investments. For more than one year, he materially overstated the total value of the fund's investments.

FINRA concluded that the registered representative's conduct violated NASD Rules 2370[‡] (borrowing from or lending to customers) and 2110* (ethical standards), and FINRA Rule [2010](#) (ethical standards). FINRA barred the representative from associating with any member firm in any capacity.

Selling Away

- ▶ FINRA settled a matter involving a registered representative who sold interests in a limited liability company without seeking or obtaining prior firm approval. The representative formed a limited liability company for the purpose of operating a media business focused on financial education for youths. The representative offered and sold interests in the limited liability company to six individuals for total proceeds of \$40,000 without notifying his member firm or obtaining prior firm approval.

FINRA concluded that the representative's conduct violated NASD Rules [3040](#) (private securities transactions by an associated person) and 2110* (ethical standards). As such, FINRA suspended the registered representative from associating with any member firm in any capacity for six months and fined him \$10,000.

Trading on Non-Public Information

- ▶ FINRA settled a matter involving a registered representative who traded on material non-public information and failed to respond to FINRA requests for information. The registered representative learned in February that an issuer was going to be acquired by another company. He knew that the ultimate source of this information was an insider of the issuer and that there had been no public disclosure of the acquisition. In February and March, the representative purchased 73,000 shares of the issuer's stock in five purchases in the two securities accounts he maintained. In April, the issuer published a joint press release with the acquiring company announcing that the company would acquire the issuer for \$3 per share. The issuer's stock price then rose 25 percent. Following the public announcement, the registered representative sold all of his shares in two transactions and realized a profit of more than \$69,000. The registered representative failed to testify truthfully about his actions when FINRA interviewed him. Eventually, the representative told FINRA the truth and also admitted that he had shared the inside information with three other individuals, at least one of whom also purchased the issuer's stock based on the non-public information.

FINRA found that the representative's conduct violated Section 10(b) of the [Securities Exchange Act of 1934](#) and Exchange Act Rule 10b-5 (federal securities fraud), and FINRA Rules [2020](#) (fraud), [8210](#) (requests for information or testimony) and [2010](#) (ethical standards). As such, FINRA barred the representative from associating with any member firm in any capacity and fined him \$69,955 (the amount of his unlawful profits).

Matched Buy-Sell Trades

- ▶ FINRA settled a matter involving a registered representative who executed matched buy-sell trades in collateralized mortgage obligations (CMOs) as part of a scheme to conceal inventory and create illusory trading profits.

Over a period of three years, the registered representative effected more than 450 CMO bond transactions in which one individual, a trader at another member firm, was the contra party. The individual directed and prearranged all of the trades and set the prices. Simultaneously with the sales, the contra party agreed to repurchase the bonds at a specified time, usually the same day, and at an agreed-upon price that provided the registered representative with a profit of 1/32 of one cent per bond. Approximately 50 percent of the compensation the registered representative received during this period resulted from these prearranged CMO bond trades. Over the course of the three-year period, an increasing number of the transactions occurred at prices that were away from the current market.

FINRA concluded that the registered representative's conduct violated NASD Rule 2110* (ethical standards). As such, FINRA suspended the registered representative in all capacities for three months and fined him \$20,000.

* NASD Rule 2110 has been superseded by FINRA Rule [2010](#), effective December 15, 2008.

** NASD Rule 3030 has been superseded by FINRA Rule [3270](#), effective December 15, 2010.

† NASD Rule 2330(a), (e) and (f) have been superseded by FINRA Rule [2150](#), effective December 14, 2009.

‡ NASD Rule 2370 has been superseded by FINRA Rule [3240](#), effective June 14, 2010.