

Quarterly Disciplinary Review

January 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.

Causing Inaccurate Firm Records

- ▶ FINRA settled a matter involving a registered representative who created inaccurate firm records. Over the course of one year, the representative sold variable universal life policies to 42 customers. He also recommended that the customers use funds from existing variable universal life policies to purchase or pay premiums on the new policies. On the forms that he prepared for the 42 variable universal life sales, the representative inaccurately represented that the transactions were not replacement transactions when, in fact, they were.

FINRA found that the registered representative's conduct violated NASD Rules 2110* (ethical standards) and [3110](#) (books and records). As a result, FINRA fined the registered representative \$5,000 and suspended him from associating with any member firm in any capacity for three months.

Outside Business Activities

- ▶ FINRA settled a matter involving a registered representative who engaged in outside business activities without providing his firm with prompt written notice and provided FINRA with an incomplete response to requests for information. Over several years, the registered representative failed to disclose to his member firm that he owned interests in two construction companies and that he acted as a director of an insurance company. Furthermore, in connection with the work of one of the construction companies, he received payments of nearly \$150,000 from a customer of the broker-dealer. In addition to failing to notify the firm of these business activities, the representative also failed to disclose these outside activities on the firm's compliance questionnaires for two consecutive years.

The registered representative also provided incomplete responses to two FINRA information requests regarding payments that firm customers made to companies in which the registered representative had an ownership interest.

FINRA found that the registered representative's failure to provide his member firm with prompt written notice of outside business activities violated NASD Rule 2110* (ethical standards) for conduct before December 15, 2008, and NASD Rule [3030](#) (outside business activities) and FINRA Rule [2010](#) (ethical standards) for conduct after December 14, 2008. As such, FINRA barred the representative from associating with any member firm in any capacity.

Failure to Disclose Material Information on Multiple Forms U4

- ▶ FINRA's National Adjudicatory Council (NAC) issued a decision involving a registered representative who willfully failed to disclose material information on several Uniform Applications for Securities Industry Registration or Transfer (Forms U4). The NAC found that the registered representative learned in August 2004 that he was named in a civil litigation, but he did not amend his Form U4 to disclose the litigation until October 2006. The registered representative learned in May 2005 that a default judgment for \$286,155 had been entered against him, but he failed to disclose it on his Form U4 until October 2006. The registered representative also learned in October 2005 that a second default judgment for \$18,063 had been entered against him. The representative filed three amendments to his Form U4 between October 2005 and October 2006, and he failed to disclose the default judgment in all of the amendments. The NAC found that the information the registered representative failed to disclose was material and that his failure to disclose the information was willful.

The NAC concluded that the registered representative's conduct violated NASD Rule 2110* (ethical standards) and IM-1000-1[†] (misleading registration information). As a result, the NAC fined the representative \$10,000 and suspended him in all capacities for nine months. Additionally, because the NAC's decision included a finding that the representative willfully failed to disclose material facts, under the [Securities Exchange Act of 1934](#), the representative may be statutorily disqualified from the industry.

Requesting and Receiving Continuing Education Answer Keys

- ▶ FINRA settled a matter involving a registered representative who violated FINRA's ethics rules by requesting and receiving continuing education answer keys on two occasions. The registered representative marketed a universal life insurance policy with long-term care benefits to financial advisors, who then sold the product to customers. Certain states require financial advisors who sell long-term care insurance products to retail customers in those states to take a continuing education course and pass a state exam before selling them. FINRA found that, on two occasions, the registered representative requested and received answers to two long-term care insurance continuing education examinations from two different sources.

Although there was no evidence that the registered representative distributed the answer keys to any financial advisors, FINRA concluded that, by requesting and receiving the answer keys, he violated NASD Rule 2110* (ethical standards). As such, FINRA suspended the representative in all capacities for five days and fined him \$5,000.

Private Securities Transactions and Borrowing From Customers

- ▶ FINRA settled a matter involving a registered representative who borrowed funds from two customers on multiple occasions, against firm policies, and improperly engaged in private securities transactions. In August 2004, the representative borrowed \$50,000 from a customer. At the time, procedures at the representative's firm specifically prohibited registered representatives from borrowing money from customers, and the representative never informed the firm of the loan. FINRA found that this conduct violated NASD Rules 2370[†] (borrowing from/lending to customers) and 2110* (ethical standards).

In September 2006, the registered representative repaid the \$50,000 loan by transferring to the customer a membership interest in a limited liability company formed to invest in real estate projects. The registered representative had purchased the interest for \$50,000 in August 2004. FINRA found that the interest was a security and that, by transferring the interest to the customer, the registered representative engaged in private securities transactions without providing prior notice to, or obtaining prior written approval from, his employer firm. FINRA found that this conduct violated NASD Rules [3040](#) (private securities transactions) and 2110* (ethical standards).

Then in January 2008 and April 2008, the registered representative borrowed \$3,500 and \$5,600 from a firm customer, in violation of firm procedures. The representative did not inform the firm of the loans and, in fact, falsely represented on a firm compliance questionnaire that he had not borrowed funds from firm customers. The representative repaid the loans in August 2009. FINRA found that the representative's conduct violated NASD Rules 2370[†] (borrowing from/lending to customers) and 2110* (ethical standards).

In light of these violations, FINRA suspended the registered representative in all capacities for six months and fined him \$10,000.

Engaging in Private Securities Transactions Without Firm Approval

- ▶ FINRA settled a matter involving a registered representative who sold securities away from his firm without providing prior written notice to, or obtaining prior approval from, the firm. The registered representative sold universal lease programs in resort properties in other countries. The universal lease programs were, in essence, time-share interests coupled with options to contract with third-party management companies to manage and lease the property to others and pay the investor rental income. FINRA concluded that the universal lease programs were securities. During a ten-month period, the representative sold universal lease programs to nine investors in 15 transactions totaling \$482,015, without providing his firm with prior written notice and without obtaining the firm's prior approval. The registered representative received commissions in excess of \$40,000 on the sales.

FINRA concluded that the registered representative's conduct violated NASD Rules 2110* (ethical standards) and [3040](#) (private securities transactions). FINRA also concluded that the representative's misconduct was aggravated by the fact that he submitted a questionnaire to the firm, on which he failed to report that he was selling universal lease programs for compensation. For these violations, FINRA fined the representative \$48,000 and suspended him in all capacities for seven months.

Misappropriating Firm Funds, and Creating and Submitting False Expense Reimbursement Reports

- ▶ FINRA settled a matter involving a registered representative who misappropriated more than \$30,000 from his firm by charging personal expenses to a firm credit card over a four-year period. The representative's job responsibilities included promoting the firm's funds to retail broker-dealers and financial advisors, and his job entailed a significant amount of travel and entertaining. The firm issued the representative a corporate credit card for business-related expenses. Firm policy prohibited use of the corporate credit card for personal expenses. The registered representative created and submitted false expense reimbursement reports for approximately \$30,000, representing expenses that were not related to firm business, including purchases from a garden store, a car dealership and a ski store. The representative received reimbursement on all of the false expense submissions.

FINRA found that the registered representative violated NASD Rule 2110* (ethical standards) by misappropriating firm funds for personal use. FINRA also found that he violated NASD Rules [3110](#) (books and records) and 2110* (ethical standards) by submitting false expense reimbursement reports to his firm and causing the firm's books and records to be inaccurate. FINRA barred the representative in all capacities.

Improperly Using Customer Funds

- ▶ FINRA settled a matter involving an unregistered associated person who used a customer's funds held in a checking account at another firm to pay a personal phone bill. The associated person worked at a member firm in an administrative capacity that allowed him access to voided customer checks provided to the firm to initiate online fund transfers from other institutions. The associated person used a customer's bank account information that he obtained from a voided check to transfer funds and pay a personal cell phone bill for \$450 online.

FINRA found that the associated person's conduct violated NASD Rule 2330[§] (customer securities or funds) and FINRA Rule [2010](#) (ethical standards). As such, FINRA suspended him from associating with any member firm in any capacity for one year. Because the associated person filed a petition for bankruptcy relief, FINRA did not impose a fine.

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

† NASD IM-1000-1 has been superseded by FINRA Rule [1122](#), effective August 17, 2009.

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

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