

BEFORE THE NATIONAL ADJUDICATORY COUNCIL

NASD

<p>In the Matter of the Continued Association of</p> <p>X</p> <p>as a</p> <p>General Securities Representative</p> <p>with</p> <p>The Sponsoring Firm</p>
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**REDACTED DECISION**

Notice Pursuant to  
Section 19(d)  
Securities Exchange Act  
of 1934

Decision No. SD03007

On April 21, 2003, the Sponsoring Firm<sup>1</sup> (or "the Firm") submitted a Membership Continuance Application ("MC-400" or "the Application") to continue to permit X, a person subject to a statutory disqualification, to associate with the Firm as a general securities representative. In July 2003, a Hearing Panel held a hearing on the matter. X appeared and was accompanied by the president of the Sponsoring Firm. LL appeared on behalf of Member Regulation.

A. X's Statutorily Disqualifying Event

X is subject to a statutory disqualification, under Section 3(a)(39)(F) of the Securities Exchange Act of 1934 ("Exchange Act") and Article III, Section 4(g) of the NASD By-Laws, as a result of his guilty plea in 2001 to the felony charge of conspiracy to commit insurance fraud. X was sentenced in 2002 to three months in prison; two years of supervised probation, including five months of home detention with electronic monitoring; and 200 hours of community service. In addition, X was ordered to pay \$107,699.76 in restitution. X's period of supervised release is scheduled to end in August 2004. X will remain statutorily disqualified until March 2012.

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<sup>1</sup> The names of the Statutorily Disqualified individual, the Sponsoring Firm, the Proposed Supervisor, and other information deemed reasonably necessary to maintain confidentiality have been redacted.

B. Background Information

X became associated with the Sponsoring Firm in 1999 as an investment company and variable contracts products representative and as an investment company and variable contracts products principal. In 2000, X also became registered with the Firm as a general securities representative. He was employed with a previous member firm from 1992 through 1999, as an investment company and variable contracts products representative, and from 1996 to 1999, as an investment company and variable contracts products principal.

Two customer complaints were filed against X for conduct while he was associated with the previous member firm. The first complaint was received in 2000. In that complaint, the customer alleged that X misrepresented facts by not informing the customer of a variable life insurance policy change. The complaint was settled by cancellation of the insurance policy and payment of \$10,122.46 to the customer.<sup>2</sup> We note that X provided a letter at the eligibility hearing from the customer stating that his complaint involved the new agent who had taken over the account when X left the former firm, and had nothing to do with the way in which X handled the account. According to the customer's letter, the new agent had made some changes to the customer's policy and had misinformed him about those changes. The customer further stated that he is still a client of X's.

The second complaint was received in 2001. The customer alleged that X made misrepresentations regarding the flexibility of premium payments during the sale of a variable life insurance policy. After investigating, the previous member firm found no basis for the customer complaint.

C. Proposed Business Activities and Supervision

The Sponsoring Firm has been a member of NASD since 1987. The Firm has five offices of supervisory jurisdiction ("OSJ") and 39 branch offices, and it employs 10 registered principals, 71 registered representatives and 26 employees. The Firm engages in the following types of businesses: the retail sale of over-the-counter equity securities; the retail sale of mutual funds; the sale of tax shelters or limited partnerships in primary distributions; and the sale of variable life insurance or annuities.

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<sup>2</sup> X did not contribute to the settlement amount.

The Sponsoring Firm proposes to continue to employ X as a general securities representative.<sup>3</sup> The Firm originally proposed to have X work out of a branch office in State 1. At the eligibility hearing, however, X's Proposed Supervisor and X testified that they subsequently had decided to have the Proposed Supervisor supervise X onsite at the Firm's State 1 office. X would sell securities, life insurance and annuities, and disability income and Long Term Care ("LTC") products. The Firm expects X to work from his office at least 50 percent of the business day and to be out of the office visiting clients the other part of the business day.

The Proposed Supervisor, the Firm's president, proposes to be X's supervisor.<sup>4</sup> The Proposed Supervisor has been employed with the Firm as a general securities principal since August 1986.

Neither the Sponsoring Firm nor the Proposed Supervisor has any formal or informal regulatory history. The two actions against the Firm that are listed in its MC-400 as pending litigation have been dismissed.

D. Member Regulation's Recommendation

Member Regulation recommended that the Application be denied based on the following factors: the seriousness and recentness of the disqualifying event and the fact that the conduct involved fraud and dishonesty; the fact that X will be on supervised release until 2004; and the inadequacy of the Firm's supervisory plan, given the fact that, as proposed, it failed to provide for daily, onsite supervision. Member Regulation noted that because X was recently convicted for conduct involving deception and dishonesty, offsite supervision was unacceptable. At the eligibility hearing, the Proposed Supervisor acknowledged Member Regulation's concern with the proposal that X be supervised offsite and agreed to revise the Firm's supervisory structure to provide for onsite supervision. Notwithstanding the Proposed Supervisor's agreement to supervise X onsite, Member Regulation did not amend its original recommendation that the Application be denied.

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<sup>3</sup> A person who becomes statutorily disqualified while he or she is employed in the securities industry is permitted to remain in the industry until the MC-400 application process has been completed.

<sup>4</sup> The Proposed Supervisor does not currently supervise other individuals.

E. Discussion

In reviewing this type of application, we have considered whether the particular felony at issue, and other relevant facts and circumstances, create an unreasonable risk of harm to the market or investors.<sup>5</sup> For the reasons set forth below, we conclude that X's continued participation in the securities industry presents an unreasonable risk of harm to the market or investors. We therefore deny the Sponsoring Firm's Application to continue to employ X as a general securities representative.

We find that X's conviction for conspiracy to commit insurance fraud is a serious matter.<sup>6</sup> X admitted in the plea agreement that he negotiated six insurance checks, totaling \$107,699.76, that he knew were fraudulent. X further admitted in the plea agreement that he knowingly participated in the conspiracy through which he obtained the fraudulent checks in the name of his businesses, and that he knew he was not entitled to receive the checks. Because X's conduct involved fraud and dishonesty, we find that his continued employment in the securities industry creates a risk to the investing public.

Further, the short duration of time since X's plea agreement (November 2001) and the pendency of his supervised release militate against allowing X's re-entry into the securities industry at this time. X remains on supervised release until August 2004.

Finally, we have analyzed the Firm's proposed supervisory plan and conclude that the supervision would not qualify as sufficiently heightened supervision given the nature of the conduct that led to X's conviction and the fact that he will be out of the office on a routine basis. Specifically, the proposed plan does not provide the supervision necessary to assure us that the Sponsoring Firm will be capable of effectively preventing and detecting possible misconduct on the part of X, given that the Firm expects X to be out of the office visiting clients 50 percent of the business day.

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<sup>5</sup> See Frank Kufrovich, Exchange Act Rel. No. 45437, 2002 SEC LEXIS 357, at \*16 (Feb. 13, 2002) (upholding NASD's denial of a statutory disqualification applicant who had committed non-securities related felonies "based upon the totality of the circumstances" and NASD's explanation of the bases for its conclusion that the applicant would present an unreasonable risk of harm to the market or investors).

<sup>6</sup> X testified at the eligibility hearing about the circumstances underlying his conviction. We cannot credit any parts of his testimony that differ from the provisions of his plea agreement, because to do so would constitute a collateral attack on the elements supporting his conviction. See Joseph Frymer, 49 S.E.C. 1181, 1182 (1989).

The nature and seriousness of the disqualifying event, the short duration of time since X's plea agreement, the fact that X is still on supervised release, and the inadequate supervisory structure proposed by the Firm lead us to conclude that X's continued association in the securities industry at this time would create an unreasonable risk of harm to the market or investors. We therefore deny the Sponsoring Firm's Application to continue to employ X.

On Behalf of the National Adjudicatory Council,

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Barbara Z. Sweeney  
Senior Vice President and Corporate Secretary