

BEFORE THE NATIONAL ADJUDICATORY COUNCIL

NASD

In the Matter of

X

as a

General Securities Representative

with

The Sponsoring Firm

Redacted Decision

Notice Pursuant to
Rule 19h-1
Securities Exchange Act
of 1934

Decision No. SD06004

Date: 2006

I. Procedural Background

In February 2005, the Securities and Exchange Commission remanded a February 2004 National Adjudicatory Council (“NAC”) decision denying a statutory disqualification application that sought to permit X¹ to associate as a general securities representative with the Sponsoring Firm (“the Firm”). The Commission rejected the NAC’s conclusion not to follow the Commission’s previous decisions in *Paul Edward Van Dusen*, 47 S.E.C. 668 (1981), and *Arthur H. Ross*, 50 S.E.C. 1082 (1992). The Commission stated that the NAC should employ the analysis set forth in *Van Dusen* and *Ross* to X’s application and remanded the matter for further consideration.

In light of the Commission’s instructions, the NAC has considered the Firm’s renewed application and has determined to approve its request for X to return to the securities industry.²

¹ 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.

² A subcommittee of the Statutory Disqualification Committee (“the Remand Subcommittee”) was appointed to consider this matter on remand and make a written recommendation to the Statutory Disqualification Committee. In turn, the Statutory Disqualification Committee considered the Remand Subcommittee’s recommendation and presented a written recommendation to the NAC, in accordance with Procedural Rules 9524(a)(10) and 9524(b)(1).

II. Introduction

The Sponsoring Firm initiated this matter on May 13, 2003 by completing a Membership Continuance Application (“MC-400” or “the Application”) seeking to permit X to associate with the Firm as a general securities representative. In July 2003, a subcommittee (“Hearing Panel”) of the Statutory Disqualification Committee of the NAC held a hearing on the matter. X appeared pro se, accompanied by his Proposed Supervisor, the Sponsoring Firm’s Chief Financial Officer. PL appeared on behalf of NASD’s Department of Member Regulation (“Member Regulation”).

The NAC denied the Sponsoring Firm’s Application in a decision dated February 2004. The Sponsoring Firm appealed the denial to the Commission, which remanded the matter to the NAC in February 2005.

Following the Commission’s remand, the Firm submitted letters dated September 2005 and October 2005, stating that it continues to support X’s return to the securities industry under the same terms it proposed in its earlier Application, including having the Proposed Supervisor serve as X’s supervisor. In letters dated September and October 2005, Member Regulation stated that it supported the Firm’s newly proposed Application.

III. X’s Statutorily Disqualifying Event

X is statutorily disqualified under Art. III, Sec. 4(h) of NASD’s By-Laws because the U.S. District Court for State 1 entered an Order of Permanent Injunction (“Permanent Injunction”) against him in 1999. The court permanently enjoined X from further violating anti-fraud provisions of the federal securities acts and rules of the Municipal Securities Rulemaking Board (“MSRB”). The court also ordered X to disgorge \$600,000 in profits and pay a \$40,000 civil penalty.

The Permanent Injunction was based on a complaint issued by the Commission alleging that: (1) X was the former chairman of Firm 1; (2) in connection with two “pool” municipal bond offerings, X made material misrepresentations and omissions pertaining to the size of the pools and the intended use of the bond proceeds, and advised the pools to purchase unsuitable securities; (3) in connection with three land development municipal bond offerings, X made material misrepresentations and omissions pertaining to the value of the land, developer, and capitalization of the project; and (4) X sold securities in contravention of MSRB rules.

The Commission also brought an administrative proceeding against X based on this misconduct. In 1999, X consented to, and the Commission entered, an Order Instituting Public Administrative Proceedings, Making Findings and Imposing Remedial Sanctions (“Commission Bar Order”). The Commission Bar Order barred X from association with any broker-dealer, municipal securities dealer, investment adviser or investment company, but provided that he could reapply for association with the appropriate self-regulatory organization after three years.

IV. Background Information

A. X

X was employed in the securities industry from 1967 to 1999. He qualified as an investment company products/variable contracts representative and a general securities representative in August 1967, a municipal securities principal in January 1981, and a general securities principal in April 1985. He requalified as a general securities representative in October 2002. He was associated with five different broker-dealers between 1967 and 1995.

NASD's Central Registration Depository ("CRD"®) record shows that X has not been the subject of any additional regulatory action since the imposition of the Commission Bar Order in May 1999.

X's CRD record shows two disciplinary matters prior to the Commission Bar Order. In 1994, NASD accepted a Letter of Acceptance, Waiver and Consent ("AWC") from Firm 1 and X for violating the NASD Board of Governors' Interpretation on Free-Riding and Withholding. NASD censured X and fined him \$2,500.

In March 1998, NASD accepted an Offer of Settlement from Firm 1 and X for failing to complete a training needs analysis and failing to establish and maintain written supervisory procedures regarding continuing education requirements and the review of political contributions. NASD censured X, fined him \$5,000 (jointly and severally with Firm 1), and ordered him to requalify in any principal capacity in which he sought to be registered with NASD.

B. The Firm

The Sponsoring Firm became a member of NASD in May 1967 and the Chicago Stock Exchange in August 1997.³ The Firm's main office is an office of supervisory jurisdiction ("OSJ") located in State 1. The Firm is engaged in a general securities business, has one other OSJ and 30 branch offices, and employs 108 registered representatives, 46 principals, and 23 other employees.

The Firm has five formal disciplinary actions—AWCs—on its CRD record between 1998 and 2004. The 2004 AWC cited the Firm for failing to provide timely updates of disclosures on Uniform Applications for Securities Industry Registration or Transfer ("Forms U4") and Uniform Termination Notices for Securities Industry Registration ("Forms U5"), and failing to have adequate written supervisory procedures regarding such disclosures and imposed a \$37,000

³ In letters dated September 2003, and January 2006, the Chicago Stock Exchange informed Member Regulation that it concurs with Member Regulation's recommendation to approve the Application to permit X to be a general securities representative with the Sponsoring Firm.

fine (\$32,000 of which was joint and several with a principal of the Firm). The 2001 AWC fined the Firm \$7,500 for violations of the order audit trail system (“OATS”). The 2000 AWC cited the Firm for failing to report 19 corporate debt securities transactions and failing to register as a fixed income pricing system participant and imposed a \$6,000 fine. The 1999 AWC censured the Firm and imposed a \$7,500 fine for failing to designate late ACT transactions and failing to have adequate written supervisory procedures relating to trade reporting. The 1998 AWC censured the Firm and imposed a \$15,000 fine for failing to file option position reports and failing to have adequate written supervisory procedures regarding reporting option positions.

The Firm also has two recent informal disciplinary actions. In 2002, NASD issued the Sponsoring Firm a Letter of Caution (“LOC”) for failing to have adequate written supervisory procedures to address the review of discretionary accounts and uncovered short option contracts. The Firm responded to the LOC in writing in January 2003, describing the steps it has taken to ensure future compliance with NASD’s rules in this area. In May 2002, NASD required the Firm to participate in a compliance conference. The Firm subsequently submitted a letter to NASD describing its implementation of changes to ensure that the matters were properly addressed.

V. X’s Proposed Business Activities and Supervision

The Sponsoring Firm proposes to employ X as a general securities representative, with the title of vice president and director of product development, in the Firm’s headquarters in State 1. The Firm states that X will “assess the strengths of the [Firm] and its core competencies and look beyond the traditional lines of business to evaluate business opportunities in new products.”⁴ The Sponsoring Firm asserts that these new business ventures can include, but are not limited to, strategic alliances and joint ventures with trading partners. X will conduct meetings with business prospects outside the State 1 office.

X will propose these new ventures first to the Proposed Supervisor. If the Proposed Supervisor determines that any of these ventures are attractive for the Firm, he will present them to the executive management for consideration. The executive management will have the discretion as to whether these proposed ventures should be pursued. If the Firm’s executive management chooses to move forward with any proposal, they must first submit it to the Sponsoring Firm’s Board of Directors for a vote.

⁴ According to the Firm’s Application, X has been acquainted with the Sponsoring Firm’s CEO since the early 1980s. The CEO is familiar with X’s business activities and would like him to develop new opportunities for the Firm to diversify its business plan.

The Firm proposes that the Proposed Supervisor serve as X's responsible supervisor. The Proposed Supervisor is the Sponsoring Firm's CFO and chief compliance officer. He has been in the securities industry since 1970, and he registered with the Firm in January 1990. He qualified as a registered securities principal in 1970, a financial and operations principal in 1978, a registered options principal in 1979, and an equity trader in 2000.

The Proposed Supervisor has no informal or formal disciplinary or regulatory history.

VI. Member Regulation's Recommendation

In a letter dated September 2005, supplemented by a letter dated October 2005, Member Regulation recommended that the NAC approve the Sponsoring Firm's Application to employ X, subject to heightened supervisory terms and conditions.

VII. Discussion

After carefully reviewing the entire record in this matter, we concur with Member Regulation's recommendation and approve the Sponsoring Firm's Application to employ X as a general securities representative.

A. The Legal Standards

As the Commission stated in its February 2005 decision remanding this matter, the legal standards that govern our review are set forth in *Van Dusen* and *Ross*. *Van Dusen* provides that in situations where the Commission has already addressed an individual's misconduct through its administrative process and has chosen to impose certain sanctions for that misconduct, NASD should not consider the individual's underlying misconduct when it evaluates a statutory disqualification application. The Commission stated that when the period of time specified in its order has passed, in the absence of "new information reflecting adversely on [the applicant's] ability to function in his proposed employment in a manner consonant with the public interest," it is inconsistent with the remedial purposes of the Exchange Act and unfair to deny an application for re-entry. *Van Dusen*, 47 S.E.C. at 671.

The Commission also noted in *Van Dusen*, however, that an applicant's re-entry is not "automatic" after the expiration of a given time period. Instead, the Commission instructed NASD to consider other factors, such as: 1) other misconduct in which the applicant may have engaged; 2) the nature and disciplinary history of the prospective employer; and 3) the supervision to be accorded the applicant. *Van Dusen*, 47 S.E.C. at 671.

B. The Application Meets the *Van Dusen* Analysis

After applying the *Van Dusen* standards to this matter, we have determined to approve X's Application.

First, the record shows that X has no complaints, regulatory actions, or criminal history since the 1999 Commission Bar Order.

Second, we look to the nature and disciplinary history of the Sponsoring Firm. The Firm has been an NASD member since 1967, and it engages in a general securities business. We note that the Firm has entered into five AWCs with NASD between 1998 and 2004, and that NASD has issued one LOC to the Firm and required one compliance conference since 2002. We are concerned about the deficiencies noted on these actions, but we also note that they do not indicate a problem with the Firm's ability to supervise individuals. We are also satisfied that the record shows that the Firm has satisfactorily responded to NASD regarding those deficiencies and has made the necessary corrections to its procedures. We therefore conclude that none of the Firm's disciplinary incidents raise concern that it would not be able to effectively supervise X in his proposed responsibilities in the Firm's State 1 headquarters.

Finally, we consider the Firm's proposed supervisory structure for X. The proposed primary supervisor has been a general securities principal with the Sponsoring Firm since 1990 and has no disciplinary history. Moreover, the Proposed Supervisor has been in the securities industry and has functioned in a principal capacity for more than 30 years. We find that the Firm has demonstrated that the Proposed Supervisor will be an effective supervisor for X.

We also recognize that many of X's activities will be conducted off the Firm's premises, when he visits with potential sources of new business. These off-site efforts, however, will be directed toward obtaining business proposals for the Firm to consider. Moreover, X is unable to finalize business transactions for the Firm on his own—he must present each source of potential business to the Proposed Supervisor, who will then determine whether to take the proposal to the Sponsoring Firm's executive management. Ultimately, the Firm's Board of Directors must vote on a proposal before it becomes integrated into the Firm's business plan. In light of X's history of problems with disclosure documents, we have also provided that he have no responsibility in the writing, reviewing, or editing of any disclosure documents that may be needed for a new business venture. We are therefore satisfied that X's activities away from the Firm will not require the physical presence of the Proposed Supervisor for effective supervision.

The Firm also proposed the beginning of a well-structured plan of heightened supervisory conditions to impose on X. After reviewing the Firm's proposal, we determined to accept it, with the addition of several enhancements, as noted below.

After considering all of the facts, we approve X as a general securities representative with the Sponsoring Firm, supervised by the Proposed Supervisor, and subject to the following terms and conditions of employment:⁵

1. The Sponsoring Firm will rewrite its written supervisory procedures to establish clearly that the Proposed Supervisor is X's primary supervisor;*

⁵ The asterisk denotes heightened supervisory terms and conditions that the Firm will impose only on X. These are not part of the Firm's standard supervisory program. The underlined language indicates our enhancements to the Firm's original proposal.

2. X will work out of the Sponsoring Firm's corporate headquarters located in State 1, at a desk near the Proposed Supervisor, and X will report to this office at least once per week;*
3. X will maintain an activity log. This log will list on a daily basis the names of the people and businesses with which he interacts. The Proposed Supervisor will review this activity log on a monthly basis. The log will include:
 - a. Names of the people with whom X has spoken;
 - b. Names of the companies for which the people work;
 - c. Types of business discussed at the meetings;
 - d. Any follow-up information for X to act on; and
 - e. All other information the Firm and X reasonably believe is necessary to disclose in the interest of ensuring compliance with the securities laws;*
4. X will not maintain any office other than the Sponsoring Firm's office in State 1;*
5. X will work to develop a new business plan and explore new business ventures for the Sponsoring Firm;*
6. The Proposed Supervisor will review all of X's new business proposals. The Proposed Supervisor may present any of these new proposals that he deems worthy to the executive management of the Firm to determine whether the proposed ventures will be pursued. The Firm's Board of Directors will vote on a proposal before it is finally adopted by the Firm. If any of the new proposals involve drafting disclosure documents, X will not have any role in writing, reviewing, or editing such documents;*
7. X will not have the authority to approve or commit the Firm's capital or resources in any municipal bond activities;*
8. X may maintain and solicit retail clients. The Proposed Supervisor will review and pre-approve all of X's new account forms for suitability, prior to accepting the new accounts for the Firm;*
9. The Proposed Supervisor will review and approve all of X's order tickets and blotters;
10. The Proposed Supervisor will review all incoming correspondence to X on a daily basis, and will review all of X's outgoing correspondence prior to use;*
11. The Proposed Supervisor will maintain a written record evidencing review and approval of transactions, the opening of new accounts, and all correspondence generated by X;*
12. X will not have discretionary accounts;

13. The Proposed Supervisor will conduct a compliance meeting with X at least once per month to discuss these terms and conditions, and to conduct a review of all of X's account files. The Proposed Supervisor will maintain a record of these meetings in X's file where it can be easily accessed by NASD examiners;*
14. The Proposed Supervisor will conduct random oral customer contacts on a reasonable basis to discuss activities in accounts and to determine customer satisfaction. The Proposed Supervisor will maintain a record of these customer contacts in X's file where it can be easily accessed by NASD examiners;* and
15. The Firm must obtain prior approval from Member Regulation if it wishes to change X's responsible supervisor from the Proposed Supervisor to another person.*

NASD certifies that: 1) X meets all applicable requirements for employment, and 2) X and the Proposed Supervisor have represented that they are not related by blood or marriage.

Accordingly, in conformity with the provisions of SEC Rule 19h-1, the association of X as a general securities representative with the Sponsoring Firm under the above-referenced supervisory plan will become effective upon the Commission issuing an order that it will not institute proceedings pursuant to Section 15(b) of the Exchange Act and that it will not direct otherwise pursuant to Section 15A(g)(2) of the Exchange Act. This notice shall serve as an application for such an order.

On Behalf of the National Adjudicatory Council,

Barbara Z. Sweeney, Senior Vice President and
Corporate Secretary