

BEFORE THE NATIONAL ADJUDICATORY COUNCIL

FINANCIAL INDUSTRY REGULATORY AUTHORITY

In the Matter of

Department of Enforcement,

Complainant,

vs.

John B. Busacca, III

Orlando, FL,

Respondent.

DECISION

Complaint No. E072005017201

Dated: December 16, 2009

Respondent failed to exercise reasonable supervision and permitted his firm to employ an unregistered chief compliance officer. Held, findings and sanctions affirmed.

Appearances

For the Complainant: Leo F. Orenstein, Esq., Mark P. Dauer, Esq., Department of Enforcement, Financial Industry Regulatory Authority

For the Respondent: Pro Se

Decision

Pursuant to NASD Rule 9311(a), John B. Busacca, III appeals a January 16, 2009 Hearing Panel decision.¹ The Hearing Panel suspended Busacca for six months in all principal capacities and fined him \$25,000 for failing to reasonably supervise the operations of North American Clearing, Inc., f/k/a Advantage Trading Group, Inc. (hereinafter, "North American" or

¹ Following the consolidation of NASD and the member regulation, enforcement, and arbitration functions of NYSE Regulation into FINRA, FINRA began developing a new "Consolidated Rulebook" of FINRA Rules. The first phase of the new consolidated rules became effective on December 15, 2008. *See FINRA Regulatory Notice 08-57* (Oct. 2008). Because the complaint in this case was filed before December 15, 2008, the procedural rules that apply are those that existed on December 14, 2008. The conduct rules that apply are those that existed at the time of the conduct at issue.

the “Firm”), in violation of NASD Rules 3010 and 2110. The Hearing Panel also fined Busacca \$5,000 for permitting North American, as its president, to employ an unregistered chief compliance officer, in violation of NASD Rules 1022 and 2110. After a complete review of the record, we affirm the Hearing Panel’s findings and sanctions.

I. Factual History

A. Busacca’s Background

Busacca entered the securities industry in 1992, registered as a general securities representative in 1993, and as a general securities principal in 1997. In January 2003, Busacca associated with North American in a non-registered capacity. On February 4, 2004, Busacca registered with North American as a general securities representative, general securities principal, equity trader, and options principal. Busacca was officially designated as North American’s president on an amendment to the Firm’s Uniform Application for Broker-Dealer Registration (“Form BD”) dated March 17, 2004, and served in this capacity until May 2007. Busacca resigned from North American in August 2007, and is not currently registered with a FINRA member firm.

B. North American’s Background and Busacca’s Role at the Firm

North American’s principal business was clearing. When Busacca joined North American in January 2003, it was a subsidiary of another member firm. In connection with the settlement of a dispute involving the owners of North American’s parent company, North American was spun off to Richard Goble (a co-owner of North American’s parent company) in November 2003. At that time, Busacca served as an unregistered salesperson for North American and sold the Firm’s clearing services to correspondent firms. Employees were informed, however, that Busacca would be taking a more active role in the Firm. Busacca was bringing in a majority of North American’s business, and Goble agreed that Busacca would become president of the Firm.

Busacca formally registered with North American on February 4, 2004, and was officially designated as the Firm’s president on March 17, 2004. Although Busacca was the Firm’s president, he testified that his primary function at North American was sales and he was the Firm’s “breadwinner.” Busacca traveled extensively during all relevant time periods in his efforts to increase North American’s business.

C. Software Conversion

In November 2003, North American licensed from SIS/ADP a securities-industry software system that allowed the Firm to prepare its books and records and to comply with regulatory filing requirements. This system was used by many other clearing firms. The software, however, was expensive and cost North American a minimum of \$50,000 per month. Goble decided that North American would not renew the license agreement when it expired at

the end of January 2004, and directed that Busacca and others assist him in finding another software system for North American's back office functions.²

Busacca attempted to find another software provider for North American, and investigated a number of vendors. Busacca referred several vendors to Goble, but Goble rejected them because they all were too expensive. Subsequently, Busacca was referred to a small California company that provided a software program to clearing firms. Busacca testified that he performed some diligence on the company and its software, and then referred the company to Goble.³ A FINRA examiner testified that no other clearing firms used this software, but the software cost \$5,000 per month, substantially less than the software North American licensed from SIS/ADP.⁴ Goble decided that North American should utilize the less expensive software, and the Firm entered into a software license agreement with the California company.

On February 9, 2004, North American began operating with the new software system. The Firm, however, did not notify FINRA of this change.⁵ Further, unlike the process followed by most clearing firms that change their software systems, North American did not run parallel systems for any period of time prior to the conversion, and did no testing of the new system.

D. Numerous Problems Develop

It is undisputed that numerous problems occurred in connection with the new software system and conversion to that system. Many of these problems persisted for more than one year after the conversion, and were discovered by FINRA examiners during a routine examination of the Firm in March 2005. The problems generally were attributable to the software's inability to receive and process information from other internal and external software programs. This

² Goble initially suggested that the Firm develop its own software system, but North American's in-house programmers informed him that this was not feasible. Busacca also testified that Goble proposed keeping North American's books and records manually if the Firm could not find a suitable software vendor.

³ A FINRA examiner testified that he found no written record of any diligence on the software company in North American's files.

⁴ Busacca testified that the California company's software was used by some other clearing firms, but "not national clearing firms." Busacca further testified that North American's existing software was "much better" than the new software, and although the software "wasn't bad," "it wasn't the best system, probably should have been tested and everything else like that. It wasn't my call at the time."

⁵ A FINRA examiner testified that the conversion of a clearing firm's software system is very closely monitored by regulators because there are always glitches. NASD Rule 1017(a)(5) requires member firms to seek FINRA's approval for any material change in business operations. Neither Busacca nor North American was charged with violating Rule 1017.

required North American's employees to manually enter a significant amount of information, which led to errors. FINRA staff testified that it was unusual for a firm that cleared for as many correspondent firms as North American to use software that required so much manual input of data and information. FINRA staff further testified that certain of the problems were caused by the lack of training and experience of North American employees. The problems that developed included the following:⁶

1. Inaccurate Box Count

Exchange Act Rule 17a-13 requires that FINRA member firms such as North American perform a "box count." Specifically, a firm must physically examine and count all securities held by the firm at least once per quarter, compare the results against the firm's records, and record unresolved differences in the firm's records within seven business days. During the March 2005 examination, FINRA staff discovered 19 discrepancies between North American's February 28, 2005 box count and staff's box count. A FINRA examiner testified that the erroneous box count was unusual and this was the first box count discrepancy that he had ever seen.

2. Erroneous Records of Customer Securities

Exchange Act Rule 17a-3(a)(5) requires that FINRA member firms such as North American prepare a securities record or ledger, and firms are required to maintain and preserve such records. *See* Exchange Act Rule 17a-3; *see also* NASD Rule 3110(a). During the March 2005 examination, FINRA discovered 17 inaccuracies (of 25 sampled accounts) in North American's records pertaining to customer mutual fund positions dated March 9, 2005. A FINRA examiner testified that the large number of discrepancies in North American's records was unusual.

3. Failure to Timely Validate or Take Exception to Transfer Instructions

During the relevant time periods, NASD Rule 11870(b) required member firms that received broker-to-broker transfer instruction forms to, within three business days⁷ following receipt of the transfer instructions, either validate the transfer instruction or take exception to such instruction. FINRA discovered that from November 2004 through January 2005, North American failed to comply with Rule 11870(b) 20 percent of the time. North American's

⁶ During the 2005 examination, FINRA staff also discovered (among other things) that North American failed to preserve emails and that the Firm's email system and written supervisory procedures ("WSPs") allowed its employees to delete emails, in violation of Exchange Act Rule 17a-4. The Hearing Panel, however, did not find that Busacca's supervision was unreasonable with respect to these violations.

⁷ FINRA amended this rule in 2007 to reduce the time period to one business day. *See FINRA Regulatory Notice 07-50* (Oct. 2007).

failures to comply with Rule 11870(b) comprised the majority of all member firm's failures to comply with this rule during the time period in question. FINRA staff testified that the Firm's failures were caused by the software's inability to process transfers on the Automated Customer Account Transfer Service ("ACATS"),⁸ increased business from correspondent firms, and the Firm having hired inexperienced personnel.

4. Failure to Make Timely Buy-Ins

Exchange Act Rule 15c3-3(d)(2) and NASD Rule 11870(f) require member firms to initiate, within a specified time period, buy-in procedures or to take other steps to obtain possession or control of securities that the firm fails to receive in connection with an account transfer. During the March 2005 examination, FINRA found six failures by North American to make timely buy-ins or obtain possession or control of securities. These failures occurred from June 2004 to January 2005, and three of these six failures involved ACATS transfers.

5. Reg. T Violations

Member firms are required to cancel or otherwise liquidate, within prescribed time periods, purchases in customer cash accounts if customers do not make full cash payment. *See* Section 220.8 of Regulation T of the Federal Reserve Board ("Reg. T"). Further, under certain circumstances, if securities are transferred out of a cash account without the customer having paid for them, the account must be frozen. *Id.* During the March 2005 examination, FINRA reviewed 511 trades in North American customer accounts from January 1, 2004, through February 28, 2005. Staff testified that North American failed to cancel or liquidate purchases in accordance with Reg. T on 71 occasions.⁹ FINRA staff also found 11 instances where North American permitted customers to trade in frozen accounts. A FINRA examiner testified that North American's Reg. T violations were higher than other firms.

⁸ "ACATS is a system administered by the National Securities Clearing Corporation (NSCC) that automates and standardizes procedures for the transfer of assets in a customer account from one firm to another. Rule 11870 mandates the use of ACATS when both the carrying member and the receiving member are participants in a registered clearing agency having automated customer securities account transfer capabilities and are eligible to use such capabilities, and sets forth the procedures for members to use when transferring customer assets between members." *NASD Notice to Members 04-58* (Aug. 2004).

⁹ The summary chart contained in the record documenting such failures, however, shows 54 violations of Reg. T. For purposes of this decision, we do not find material the difference between staff's testimony and the summary chart. Further, all of these failures occurred after Busacca was officially designated as North American's president, with most of the failures occurring in the last few months of 2004.

6. Violation of Margin Requirements

NASD Rule 2520(c) requires that customers maintain specified margins in margin accounts. During the March 2005 examination, FINRA staff discovered 10 instances (7.5 percent of the accounts sampled) from October 2004 through January 2005 in which North American failed to liquidate timely customer accounts that fell below the specified margin requirements.

7. Failure to Report Data

Clearing firms are required to report certain data to FINRA pursuant to NASD Rule 3150.¹⁰ North American failed to report any data from February 2004 through May 2004.

E. Employment of Unregistered Chief Compliance Officer

North American hired Daniel McAuliffe in April 2004, and the Firm designated McAuliffe as its chief compliance officer on its Form BD in July 2004. Busacca introduced McAuliffe to Goble, and Goble made the ultimate decision to hire him. As president of the Firm, Busacca supervised McAuliffe.

McAuliffe had qualified and registered as a general securities principal, and had previously served as a chief compliance officer, with other FINRA member firms. His registration as a principal, however, terminated in March 2001. McAuliffe failed to requalify and did not obtain a waiver of the requirement that he requalify. Both Goble and Busacca believed that McAuliffe had been properly registered, and Busacca did not become aware of McAuliffe's lack of registration until after McAuliffe resigned from North American in February 2005. Busacca testified that he did not have access to FINRA's Central Registration Depository ("CRD"[®]) and trusted that McAuliffe had his registration as a principal reinstated.

II. Procedural History

FINRA's Department of Enforcement filed a 17-cause complaint against North American and Busacca on August 13, 2007. Busacca was charged in two of the 17 causes of action, causes 13 and 17. Cause 13 alleged that Busacca and North American failed to reasonably supervise the Firm's operations system conversion and its operations activities to detect and prevent certain violations, during the period from April 2003 through February 2005, in violation of NASD

¹⁰ This rule implements a program established by FINRA in 2001 called Integrated National Surveillance and Information Technology Enhancements (INSITE). This program was developed to "collect and analyze information about members and produce reports that identify 'exceptions' based on historical and current comparisons of member data. . . . INSITE will permit NASD Regulation to concentrate its examinations on the higher-risk segments of the industry . . . [and] focus the content of each examination on higher-risk topics." *NASD Notice to Members 01-84* (Dec. 2001).

Rules 3010 and 2110. Cause 17 alleged that Busacca and North American employed and designated an unregistered principal as the Firm's chief compliance officer from July 2004 until February 2005, in violation of NASD Rules 1022(a) and 2110. Busacca and North American filed answers denying Enforcement's allegations.

In May 2008, the Commission filed suit against North American and some of its managers (including Goble) seeking the appointment of a receiver for the Firm. A federal court subsequently appointed a receiver for North American, the receiver assumed control of the Firm, and the Firm went out of business. At the request of the Securities Investor Protection Corporation, the court later appointed a trustee to oversee North American's liquidation pursuant to the Securities Investor Protection Act of 1970.

In this case, Enforcement reached a settlement of the complaint against North American with the receiver and trustee pursuant to which FINRA expelled North American from FINRA membership. Enforcement filed a motion to sever the allegations against North American from those against Busacca pursuant to NASD Rule 9214. The Hearing Officer granted Enforcement's request to sever over Busacca's objection.

The Hearing Panel conducted a hearing with respect to the two counts of the complaint for which Busacca was charged on November 10, 2008. Enforcement called five witnesses: two FINRA staff members, Sandra Farr (North American's former operations manager), Goble, and Busacca. Busacca testified on his own behalf. On January 16, 2009, the Hearing Panel issued its decision. The Hearing Panel found that Busacca failed to exercise reasonable supervision over North American's operations, and imposed a six-month suspension in all principal capacities and a \$25,000 fine for this misconduct. The Hearing Panel also found that Busacca, as North American's president, allowed the Firm to employ an unregistered and unqualified person as the Firm's chief compliance officer. The Hearing Panel fined Busacca \$5,000 for this misconduct. The Hearing Panel also assessed \$2,078.60 in costs. Busacca's appeal followed.

III. Discussion

A. Busacca Failed to Reasonably Supervise the Firm's Operations

The Hearing Panel found that Busacca violated NASD Rules 3010 and 2110 by failing to reasonably supervise North American's operations. We affirm the Hearing Panel's findings.

NASD Rule 3010(a) "requires member firms to establish and maintain a supervisory system that is reasonably designed to achieve compliance with the applicable securities laws, rules, and regulations." *Dep't of Enforcement v. Strong*, Complaint No. C04050005, 2007 NASD Discip. LEXIS 10, at *11 (NASD NAC Feb. 23, 2007), *aff'd*, Exchange Act Rel. No. 57426, 2008 SEC LEXIS 467 (Mar. 4, 2008). "A supervisor is responsible for reasonable supervision, a standard that is determined based on the particular circumstances of each case." *Dep't of Enforcement v. Pellegrino*, Complaint No. C3B050012, 2008 FINRA Discip. LEXIS 10, at *46-47 (FINRA NAC Jan. 4, 2008), *aff'd*, Exchange Act Rel. No. 59125, 2008 SEC LEXIS 2843 (Dec. 19, 2008) (internal quotations and citations omitted). The Commission has held that "[t]he duty of supervision includes the responsibility to investigate 'red flags' that

suggest that misconduct may be occurring and to act upon the results of such investigation.” *Pellegrino*, 2008 SEC LEXIS 2843, at *33. A supervisor must respond “vigorously” and with the “utmost vigilance” upon discovering any red flags or irregularities. *See Robert Grady*, Exchange Act Rel. No. 41309, 1999 SEC LEXIS 768, at *7 (Apr. 19, 1999); *see also George J. Kolar*, 55 S.E.C. 1009, 1016 (2002) (holding that “decisive action” is necessary whenever supervisors are made aware of suspicious circumstances); *Quest Capital Strategies, Inc.*, 55 S.E.C. 362, 371 (2002) (same). A failure to supervise is a violation of NASD Rules 3010(a) and 2110. *See Robert J. Prager*, Exchange Act Rel. No. 51974, 2005 SEC LEXIS 1558, at *2 n.3 (July 6, 2005).

To prove that Busacca failed to reasonably supervise North American’s operations in violation of NASD Rules 3010 and 2110, Enforcement must demonstrate that Busacca had supervisory authority over the Firm’s operations and that he failed to reasonably exercise such authority. *See Dep’t of Enforcement v. VMR Capital Mkts. US*, Complaint No. C02020055, 2004 NASD Discip. LEXIS 18, at *16 (NASD NAC Dec. 2, 2004). We address each of these elements in turn.

1. Busacca Supervised the Firm’s Operations

Busacca, as North American’s president, held final responsibility for the Firm’s operations unless and until he reasonably delegated the duties to someone else and had no reason to know that the assigned person was not properly performing the delegated functions. *See Prager*, 2005 SEC LEXIS 1558, at *43 n.45. Busacca never personally delegated responsibility for the Firm’s operations, and all of the violations discovered by FINRA during its March 2005 examination involved the Firm’s operations. *See Part I.D.1-7, supra*.

At the Hearing Panel hearing, Busacca conceded that as North American’s president he was responsible for the Firm’s operations. Busacca now suggests, however, that well before he became North American’s president the Firm had delegated to Sandra Farr responsibility over the Firm’s operations.¹¹ We reject Busacca’s argument that responsibility for North American’s operations was properly delegated to Farr. During all relevant times Farr was registered only as a general securities representative, yet as the Firm’s operations manager she acted in a capacity requiring principal registration.¹² Busacca was Farr’s direct supervisor and knew that Farr was

¹¹ A FINRA examiner explained that typically a firm’s Financial and Operations Principal (“FINOP”) has overall responsibility for the firm’s operations. The examiner testified that North American’s FINOP, however, was responsible only for the Firm’s financial statements, and that the Firm had designated Sandra Farr as the person responsible for the Firm’s operations. The examiner testified that there “wasn’t a lot of typical operational functions happening at North American that I saw in other clearing firms.”

¹² NASD Rule 1021(b) defines a principal as any person associated with a member firm who is “actively engaged in the management of the member’s investment banking or securities business, including supervision, solicitation, conduct of business or the training of persons associated with a member for any of these functions[.]” NASD Rule 1022(b) requires member

not registered as a principal. He also recognized that Farr needed to be registered as a principal. Indeed, Busacca eventually demanded that Farr qualify as a principal, but she did not do so until July 2005. Any previous delegation to Farr, an unregistered principal, of responsibility for the Firm's operations was unreasonable. *See VMR Capital Markets*, 2004 NASD Discip. LEXIS 18, at *25 (holding that general securities representative's lack of registration as a principal made any delegation of supervisory authority to him unreasonable). Moreover, Busacca knew of the numerous problems with the Firm's operations while Farr served in this capacity and thus had reason to know that Farr was not properly performing her duties. *See Prager*, 2005 SEC LEXIS 1558, at *43 (holding that firm president must have no reason to know person he delegated responsibility to is not properly performing delegated duties). Consequently, Busacca held final responsibility for the Firm's operations.¹³ *See Prager*, 2005 SEC LEXIS 1558, at *43 n.45.

2. Busacca Failed to Reasonably Supervise

Having found that Busacca had the responsibility to supervise North American's operations, we must now determine whether his supervision was reasonable. We find that under the circumstances, it was not.

North American's conversion of its software and use of the new software program caused numerous problems that directly and adversely impacted North American's core functions as a clearing firm. Busacca had knowledge of these problems prior to his service as president of the Firm. Busacca acknowledged that the software "wasn't the best system," and described the Firm as a "mess" in March 2004 and the task of correcting the new software's problems as "monstrous." Many of these problems, including the problems discovered by FINRA in March 2005, persisted for at least one year after Busacca was officially designated as North American's president.¹⁴

[cont'd]

firms to designate as a FINOP each person associated with the firm who, among other things, supervises and is responsible for the individuals who are involved in the administration and maintenance of the firm's back office operations. Further, "[a]ll persons engaged or to be engaged in the investment banking or securities business of a member who are to function as principals shall be registered as such[.]" *See* NASD Rule 1021(a).

¹³ Busacca also testified generally that he delegated certain responsibilities to an individual he hired as chief operating officer in late 2005 or early 2006. This alleged delegation, however, occurred after the violations that are the subject of the complaint.

¹⁴ FINRA staff testified that FINRA examined the Firm shortly after the software conversion in 2004, and that "many of the same problems with the conversion were still popping up in February, March of 2005." Staff further testified that the severity of certain of the problems discovered in March 2005 was unusual. However, and with the exception of the Firm's stock records and INSITE reporting, the record generally does not indicate whether there

Busacca argues that he did his best to solve North American's operational problems. We disagree. Busacca testified that both before and after he became North American's president, he was the Firm's primary source of business and the only person at the Firm doing sales. Busacca further testified that "while [he] was trying to grow the firm and travel extensively . . . [he'd] come back from a trip and tackle the problems." North American's serious problems, however, required Busacca's full attention. *See Pellegrino*, 2008 SEC LEXIS 2843, at *22-26 (holding that respondent failed to reasonably supervise when he focused on improving firm's sales rather than responding to red flags). Busacca's travels kept him away from the office at a time when he was directly responsible for the Firm's operations and knew that the Firm lacked adequate personnel to correct the admittedly significant issues at the Firm. Further, Busacca focused on, and succeeded at, increasing the Firm's sales when he knew that the Firm's software could not adequately process data and information for its existing customers.¹⁵

Moreover, Busacca did not act promptly and with the "utmost vigilance" to resolve North American's widespread operational problems. *See Grady*, 1999 SEC LEXIS 768, at *7. Although we acknowledge that Busacca took steps to correct certain of the Firm's operational problems, he took many of these actions well after he became the Firm's president and, in certain instances, after FINRA's March 2005 examination. For example, Busacca testified that he hired someone to perform an audit of North American's systems in 2005, hired a new chief operations officer in 2005 and another in late 2005, forced Farr to qualify as a principal, did "spot checks" of the Firm's operations, strengthened the margin department, made all employees sign the Firm's WSPs, and brought in additional staff so that the Firm grew from approximately 10 employees in 2004 to 40 employees by late 2005 and 2006. Busacca further testified that he conducted weekly manager meetings during which many of the problems with North American's operations were discussed.¹⁶ Busacca did not act promptly to correct North American's

[cont'd]

was improvement in the number and frequency of the problems identified in Part I.D., *supra*, from 2004 to March 2005. With respect to records of customers' securities positions, FINRA staff testified that the Firm's records did improve from 2004 to March 2005. Further, the Firm began reporting INSITE data in or about May 2004.

¹⁵ A supervisor's business development activities do not necessarily, on their own, demonstrate unreasonable supervision under Rule 3010. Under the facts and circumstances of this case, however, Busacca's focus on business development at a time when the Firm was experiencing substantial operational problems is one of several factors that we have considered in finding that he failed to reasonably supervise North American's operations.

¹⁶ Farr testified that she did not recall many manager meetings in 2004, although she did recall generally weekly manager meetings in 2005. In addition, Busacca argues that the Hearing Officer denied him access to numerous documents that demonstrated that he conducted weekly management and compliance meetings to address North American's problems. As set forth in Part III.C., *infra*, we find that the Hearing Officer properly denied Busacca's request to compel

[Footnote continued on next page]

numerous operational problems, as is required under Rule 3010. *See Pellegrino*, 2008 SEC LEXIS 2843, at *53 (finding that reasonable supervision requires supervisor to promptly correct deficiencies); *cf. Dep't of Mkt. Reg. v. Yankee Fin. Group, Inc.*, Complaint No. CMS030182, 2006 NASD Discip. Lexis 21 (NASD NAC Aug. 4, 2006) (finding violation of Rule 3010 where supervisor's corrective actions came after months of inaction and after FINRA began an investigation), *aff'd in rel. part sub nom, Richard F. Kresge*, Exchange Act. Rel. No. 55988, 2007 SEC LEXIS 1407 (June 29, 2007).

Further, to the extent that certain of Busacca's actions were not specifically designed to address problems with the Firm's operations, such actions did not satisfy Busacca's obligations under Rule 3010. *See Pellegrino*, 2008 SEC LEXIS 2843, at *50 ("We must consider, however, whether his supervision was reasonably designed to prevent the violations at issue, not weigh his supervisory performance in other areas against his deficiencies in the area under review.") (internal quotations omitted). Moreover, although Busacca testified that he hired more ACATS staff, the personnel hired to address these problems were inexperienced, and Busacca testified generally that employees were often inexperienced when hired by the Firm. This compounded the problems caused by the Firm's software because the information that was required to be manually entered into the software system often was not entered accurately. Considering Busacca's extensive travel and focus on business development when he had knowledge of the Firm's significant operational problems, the lack of adequate personnel in place to address the Firm's problems, and the failure to diligently and promptly address all of North American's operational issues, we find that Busacca failed to reasonably supervise the Firm's operations.

Busacca argues that Goble hindered his ability to effectively supervise. For example, Busacca alleges that he attempted in 2005 to switch software programs because of the significant number of problems but Goble refused. Busacca also testified that at times Goble would not permit him to hire additional staff, Goble hired young and inexperienced employees, and that Goble was sometimes difficult to work with and the Firm was in constant turmoil because Goble would often fire personnel. Regardless of Goble's lack of cooperation with or support of Busacca's attempts to supervise the Firm and correct problems at the Firm, Busacca had an obligation to reasonably supervise. *See Pellegrino*, 2008 SEC LEXIS 2843, at *46 & n.36 (citing sources); *cf. James Michael Brown*, 50 S.E.C. 1322 (1992) (rejecting defense that president of firm should be excused because he lacked a meaningful role in firm's management), *aff'd*, 21 F.3d 1124 (11th Cir. 1994) (table cite).¹⁷ Busacca failed to satisfy his obligation to reasonably supervise the Firm.

[cont'd]

the production of documents from North American. Regardless, we credit Busacca's un rebutted testimony that he took the actions that he described.

¹⁷ At the hearing, Busacca testified that he remained at North American despite all of its difficulties because of, among other things, a broad non-compete clause contained in his employment agreement. The existence of the non-compete clause, however, does not justify

Finally, Busacca argues that he inherited the problems with North American's operations (which originated with Goble's decision to convert software systems), and that the Hearing Panel held him liable for the software conversion itself, which occurred more than one month before North American officially designated Busacca as the Firm's president. The record is unclear as to whether Busacca assumed responsibility for North American's operations prior to his designation as the Firm's president. It is undisputed, however, that when Busacca was officially designated as North American's president in March 2004 he had knowledge of the problems with the software and resultant problems with North American's operations. Moreover, such problems persisted until well after Busacca was listed as the Firm's president on its Form BD, and Busacca failed to diligently address the problems beginning in March 2004. *See Pellegrino*, 2008 FINRA Discip. LEXIS 10, at *64-65 (holding respondent liable for supervisory violations for problems he inherited because he failed to correct them within a reasonable time); *John A. Chepak*, 54 S.E.C. 502 (2000) (finding respondent failed to reasonably supervise despite knowledge that he was inheriting a firm "in shambles" and "run by crisis management"). Consequently, we find that Busacca failed to reasonably supervise North American's operations, in violation of NASD Rules 3010 and 2110.¹⁸

B. Registration Violation

NASD Rule 1022(a) requires that each person designated as a chief compliance officer on Schedule A of a member firm's Form BD be registered as a general securities principal. North American designated McAuliffe as its chief compliance officer in July 2004. At that time, however, McAuliffe was not properly registered as a principal or in any other capacity. Indeed, although McAuliffe had been registered as a principal with his prior employing firm, McAuliffe's employment with that firm terminated in March 2001, and McAuliffe did not associate with another firm until he joined North American. Pursuant to NASD Rule 1021(c), McAuliffe was required to pass a qualification examination to regain his status as a principal, or to seek a waiver of such requirement pursuant to NASD Rule 1070(d).¹⁹ McAuliffe did neither.

[cont'd]

Busacca's supervisory failures. *See George Lockwood Freeland*, 51 S.E.C. 389, 392 (1993) (finding that supervisor must insist on owner's cooperation and compliance with applicable requirements or resign); *cf. Pellegrino*, 2008 SEC LEXIS 2843, at *68 n.67 (holding that respondent's concern that he would not be able to find employment if he resigned is not mitigating).

¹⁸ NASD Rule 0115 provides that FINRA rules apply to all members and persons associated with a member and that such persons have the same duties and obligations as a member under the rules.

¹⁹ Rule 1021(c) provides that "[a]ny person whose . . . most recent registration as a principal has been terminated for a period of two or more years immediately preceding the date of receipt

Although Goble made the ultimate decision to hire McAuliffe, Busacca, as president of North American, supervised McAuliffe and had the responsibility to ensure that McAuliffe was qualified and registered to serve as the Firm's chief compliance officer. Busacca failed to do so, and violated NASD Rules 1022(a) and 2110. *See Kresge*, 2007 SEC LEXIS 1407, at *50 (affirming FINRA's findings that firm's president violated FINRA's registration rule by permitting non-registered person to act in principal capacity).

C. Procedural Arguments

Busacca raises a number of arguments pertaining to the proceedings before the Hearing Panel. For the reasons set forth below, we reject Busacca's arguments.

1. The Hearing Officer Properly Denied Busacca's Request to Compel Information from North American

Busacca argues that the Hearing Officer improperly denied his request to compel FINRA to issue document requests to North American. Busacca alleges that such documents would have demonstrated his "constant attention to compliance and fixing problems." We reject Busacca's arguments and find that he failed to demonstrate that production of the documents was appropriate pursuant to NASD Rule 9252(b). This rule provides that a request that FINRA compel the production of documents from a member firm shall be granted only if a requesting party demonstrates that the information sought is relevant, material, and non-cumulative and the requesting party has previously attempted in good faith to obtain the documents but has been unsuccessful. Additionally, the Hearing Officer shall consider whether the request is unreasonable, oppressive, excessive in scope, or unduly burdensome. *See* Rule 9252(b).

As an initial matter, Busacca testified that he took a number of actions to address North American's problems. Although Busacca did not act promptly to address the Firm's issues, we have credited his un rebutted testimony that he took the actions that he described. Thus, any documents obtained from North American would have been redundant and cumulative. *See Pellegrino*, 2008 SEC LEXIS 2843, at *60-61 (upholding denial of motion to compel and stating that respondent testified about the information at issue).

Busacca also failed to satisfy the other requirements of Rule 9252. Busacca filed a request seeking certain documents from North American in April 2008. Busacca sought copies of all communications and meetings Busacca had with North American staff from December 2003, copies of all of the Firm's Form BDs and amendments thereto from January 2001 to April 2008, and copies of all WSPs used by North American from January 2001 through May 2007. On May 20, 2008, the Hearing Officer denied Busacca's request. The Hearing Officer found that

[cont'd]

by [FINRA] of a new application shall be required to pass a Qualification Examination for Principals appropriate to the category of registration as specified in Rule 1022 hereof."

Busacca's request failed to state with any specificity why the documents were material, sought broad categories of documents, and failed to describe any prior efforts to obtain the documents from North American. Consequently, the Hearing Officer could not find that the conditions for granting such a request pursuant to Rule 9252 were satisfied. At a prehearing conference in August 2008, Busacca again raised the issue and stated that he expected that he would have a difficult time obtaining documents from the trustee appointed for North American. The Hearing Officer informed Busacca that if there were documents Busacca needed he could still request them from the trustee, that his original April 2008 request was too broad, and that he needed to first request the documents from North American before filing a motion to compel.

On October 27, 2008, Busacca sought a continuance of the November 10, 2008 hearing to allow him more time to obtain his files, emails, and manager meeting minutes from North American that he claimed "will clearly show Respondent was actively involved in day to day supervision of almost every aspect of the operations . . . [and] did everything reasonably possible to solve problems . . ." In support, Busacca produced an unsigned and undated letter to the trustee (which he claimed to have sent on August 20, 2008) requesting all emails attributable to Busacca and copies of minutes from all manager and compliance meetings. Busacca also produced an email to the trustee dated October 22, 2008, containing a copy of the letter, and subsequently produced the trustee's October 28, 2008 response informing Busacca that the trustee would need a subpoena to be issued before he would respond to his request. The Hearing Officer denied Busacca's request to postpone the hearing, and held that Busacca still had not satisfied the requirements of Rule 9252.

We find that the Hearing Officer properly denied Busacca's requests. Busacca's April 2008 request failed to describe in any detail the relevance or materiality of the broad document requests. Busacca also failed to describe any previous good faith attempts to obtain the documents since the issuance of the complaint in August 2007.²⁰ Further, there is no documentation in the record concerning what specific steps (if any) Busacca took to obtain the documents from North American after the Hearing Officer's May 20, 2008 denial. Moreover, even assuming that Busacca sent the requests for information to the North American trustee in late August 2008, he again waited until just two weeks before the hearing to bring the matter to the Hearing Officer's attention. At that time, Busacca again failed to specifically state how the information he sought was material and relevant. For all of these reasons, we reject Busacca's argument that the Hearing Officer improperly denied his request to compel.

²⁰ Busacca states that North American was willing to produce the documents prior to the Hearing Officer's May 20, 2008 order. However, nothing prevented Busacca from continuing to seek the documents from North American subsequent to issuance of the order or attempting to obtain the documents in the 10 months between the issuance of the complaint and the Hearing Officer's order denying Busacca's motion.

2. Busacca Was Not Unfairly Targeted by FINRA

Busacca argues that he was targeted by FINRA because he is a well-known and outspoken critic of FINRA. Busacca's argument is not supported by the record, and there is no evidence that Enforcement had an improper motive in filing the complaint and pursuing disciplinary proceedings against Busacca. *See East/West Secs. Co.*, 54 S.E.C. 947, 954 (2000) (rejecting argument that FINRA brought action against respondent to retaliate against him for criticizing FINRA).²¹ Moreover, even assuming that the record demonstrated that Enforcement had improper motives in investigating Busacca and filing a complaint against him (it does not), "[a]bsent a showing of selective enforcement, the motives behind [Enforcement's decision to initiate an investigation and commence disciplinary proceedings] are irrelevant." *Dep't of Enforcement v. Epstein*, Complaint No. C9B040098, 2007 FINRA Discip. LEXIS 18, at *78 (FINRA NAC Dec. 20, 2007), *aff'd*, Exchange Act Rel. No. 59328, 2009 SEC LEXIS 217, at *62 (Jan. 30, 2009), *appeal pending*, 09-1550 (3d Cir. Feb. 24, 2009); *Frank J. Custable, Jr.*, 51 S.E.C. 855 (1993) (concluding that bias on the part of a FINRA staff member does not mean the FINRA decision is biased). The record is devoid of any evidence that FINRA selectively prosecuted Busacca, and we reject Busacca's argument. *See Terrance Yoshikawa*, Exchange Act Rel. No. 53731, 2006 SEC LEXIS 948, at *28-29 (Apr. 26, 2006) (holding that respondents must demonstrate that they were singled out for enforcement while others similarly situated were not and that such prosecution was motivated by arbitrary or unjust considerations (e.g., race, religion, or the desire to prevent the exercise of a constitutionally protected right)).²²

3. Enforcement's Use of Timeline

Busacca also argues that the Hearing Officer improperly permitted a timeline, which Busacca alleges was inaccurate, to be displayed during the hearing and that this prejudiced Busacca. An Enforcement attorney used the timeline during his opening remarks, after which the Hearing Officer expressly stated that the exhibit was not evidence in the case and could not be given any weight by the Hearing Panel. Enforcement never sought to admit the timeline, and the record does not contain the exhibit. Nonetheless, Busacca argues that the Hearing Panel improperly relied upon the exhibit because it found that he began to supervise Farr in November 2003 and that he never delegated responsibility over operations. The record does not support Busacca's argument, there is no evidence that Busacca was prejudiced by Enforcement's use of

²¹ Busacca alleges that Enforcement's failure to make an offer to settle the charges against him demonstrates an improper motive in bringing the complaint. We disagree. FINRA's rules do not require that Enforcement make a settlement offer before filing a complaint.

²² In addition, the NAC's independent, de novo review of the record is intended to insulate proceedings from procedural unfairness. *See Dist. Bus. Conduct Comm. v. Guevara*, Complaint No. C9A970018, 1999 NASD Discip. LEXIS 1, at *39 n.16 (NASD NAC Jan. 28, 1999), *aff'd*, 54 S.E.C. 655 (2000).

the timeline, and we have not relied upon the timeline in rendering this decision. *See Guevara*, 1999 NASD Discip. LEXIS 1, at *39 n.16.

4. Challenge to Hearing Officer and Composition of Hearing Panel

Finally, Busacca argues that he was prejudiced because the Hearing Officer failed to notify him that he served as the hearing officer in another disciplinary proceeding and that the Hearing Panel did not consist of “a panel of his peers from District 7 of FINRA.” We reject these arguments. First, Busacca has not articulated how he was prejudiced by the Hearing Officer having served in the same capacity in a disciplinary case unrelated to Busacca or these proceedings, and the record does not show that Busacca was prejudiced or that the Hearing Officer was biased. *See Guevara*, 1999 NASD Discip. LEXIS 1, at *39 n.16 (“[U]nsubstantiated assertions of bias are an insufficient basis to invalidate NASD proceedings.”); *see also* Rule 9233(b) (providing that a hearing officer may be disqualified “based upon a reasonable, good faith belief that a conflict of interest or bias exists or circumstances otherwise exist where the Hearing Officer’s fairness might reasonably be questioned”); *Epstein*, 2009 SEC LEXIS 217, at *62 (“[B]ias by a hearing officer is disqualifying only when it stems from an extrajudicial source and results in a decision on the merits based on matters other than those gleaned from participation in a case.”).

Second, we reject Busacca’s challenge to the composition of the Hearing Panel. NASD Rule 9231 provides that the Chief Hearing Officer shall appoint a hearing panel composed of a Hearing Officer and two panelists, and that a panelist must currently serve or have previously served on a FINRA District Committee, the NAC, a disciplinary subcommittee of the NAC or its predecessor, or previously served as a FINRA Director or Governor. Rule 9232 provides, among other things, that the Chief Hearing Officer must also determine from which District Committee the panelists will be selected (the “Primary District Committee”) based upon the facts and circumstances of the case.²³ After designation of the Primary District Committee, the Chief Hearing Officer must select eligible panelists based upon expertise, the absence of any conflicts of interest or bias, availability, and the frequency of prior service on hearing panels. Rule 9232(e), however, further provides that “[d]esignation of the Primary District Committee does not preclude the Chief Hearing Officer from selecting one or more Panelists from other categories of eligible Panelists . . . and the public interest or the administration of [FINRA’s] regulatory and enforcement program would be enhanced by the selection of such Panelists.”

Here, there is no evidence that the Hearing Panel was improperly constituted pursuant to FINRA’s rules. Indeed, in responding to Busacca’s objection to a replacement panelist, the Hearing Officer noted that although the panelist was not a member of FINRA’s District 7, the panelist was qualified, possessed relevant expertise, and that the financial and operational issues

²³ Rule 9232(c) lists a number of non-exclusive factors for the Chief Hearing Officer to consider in designating the Primary District Committee, including the location of a respondent’s principal office at the time of the alleged misconduct and the location of witnesses.

raised by the complaint made it difficult to find qualified individuals to serve as panelists. We find that the Hearing Panel was properly constituted pursuant to FINRA's rules, and reject Busacca's arguments to the contrary. See *Dep't of Enforcement v. Sathianathan*, Complaint No. C9B030076, 2006 NASD Discip. LEXIS 3, at *53-54 (NASD NAC Feb. 21, 2006) (rejecting respondent's challenge to hearing panel and holding that respondents generally can not dictate the qualifications of panelists), *aff'd*, Exchange Act Rel. No. 54722, 2006 SEC LEXIS 2572 (Nov. 8, 2006), *aff'd*, 304 F. App'x 883 (D.C. Cir. 2008); *Dist. Bus. Conduct Comm. v. Gallison*, Complaint No. C02960001, 1999 NASD Discip. LEXIS 8, at *55-56 (NASD NAC Feb. 5, 1999) (rejecting respondent's challenge to composition of hearing panel).

IV. Sanctions

The Hearing Panel suspended Busacca in all principal capacities for six months and fined him \$25,000 for his supervisory failures, in violation of NASD Rules 3010 and 2110. The Hearing Panel fined Busacca \$5,000 for permitting North American to employ an unregistered chief compliance officer, in violation of NASD Rules 1022(a) and 2110, and assessed \$2,078.60 in costs. We affirm the Hearing Panel's sanctions.

A. Failure to Supervise

For failing to supervise, the FINRA Sanction Guidelines ("Guidelines") recommend the imposition of a fine between \$5,000 and \$50,000 and a suspension in all supervisory capacities for up to 30 business days.²⁴ In egregious cases, the Guidelines recommend suspending the responsible individual in any or all capacities for up to two years or imposing a bar.²⁵ The Guidelines also recommend considering, in addition to the General Principles and Principal Considerations in Determining Sanctions applicable to all violations, the nature, extent, and size of the underlying misconduct; whether the respondent ignored red flags; the quality and degree of the supervisor's implementation of the firm's supervisory procedures and controls; and whether the respondent attempted to conceal misconduct.²⁶

After considering the factors set forth in the Guidelines, we affirm the Hearing Panel's six-month suspension in all principal capacities and \$25,000 fine. The numerous problems with North American's operations were not merely technical issues. Rather, North American's extensive operational problems directly and negatively affected important and basic functions of North American as a clearing firm, the duties it owed to its correspondent firms, and endangered customer assets. Busacca accepted the position as North American's president with knowledge of the Firm's extensive operational problems, and described the task of correcting those

²⁴ See *FINRA Sanction Guidelines* 108 (2007), <http://www.finra.org/web/groups/industry/@ip/@enf/@sg/documents/industry/p011038.pdf> [hereinafter *Guidelines*].

²⁵ *Guidelines*, at 108.

²⁶ *Id.*

problems as “monstrous.” Despite this knowledge, Busacca failed to direct his full and immediate attention to correcting these problems and instead traveled extensively to increase North American’s business. Indeed, Busacca successfully increased North American’s business at a time when the Firm was having substantial difficulty servicing its existing customers. North American’s numerous operational problems persisted for at least one year after Busacca became president of the Firm, and FINRA staff testified that the large number of problems at North American was unusual.

The Firm also lacked adequate procedures and controls over the Firm’s operations, and Busacca failed to implement promptly procedures to address the Firm’s problems. Appropriate internal procedures and controls were crucial given the nature and breadth of the Firm’s problems and Goble’s reluctance to expend resources to solve these issues. It was Busacca’s responsibility to establish an adequate supervisory system that would help him resolve these issues, regardless of their magnitude and the lack of ownership’s support. Further, the Firm’s hiring of inexperienced and unqualified staff during Busacca’s tenure as president served to exacerbate, rather than solve, the problems with the Firm’s software. The person designated to supervise the Firm’s operations (Farr) was not properly licensed to do so, and Busacca knew that the Firm’s operational difficulties persisted while she managed North American’s operations. Despite these facts, Farr remained in this position without being properly registered for almost a year while Busacca served as president.²⁷

Under the circumstances and considering all of the facts of this case, we find that Busacca’s failure to address diligently North American’s operational difficulties was egregious. A six-month suspension in all principal capacities and a \$25,000 fine are appropriately remedial considering that Busacca was at all times forthright and never attempted to conceal the Firm’s many problems, and his assistance to FINRA staff in eventually uncovering and resolving problems was substantial.²⁸ We have also considered that Busacca promptly remedied the

²⁷ Busacca argues that the Hearing Panel failed to consider mitigating his lack of a disciplinary record. The fact that Busacca does not have a disciplinary record is not a mitigating factor. *See Rooms v. SEC*, 444 F.3d 1208, 1214 (10th Cir. 2006). In addition, we reject Busacca’s comparison of his sanctions to sanctions imposed in other disciplinary cases. *See Christopher J. Benz*, 52 S.E.C. 1280, 1285 (1997) (“It is well recognized that the appropriate sanction depends upon the facts and circumstances of each particular case and cannot be determined precisely by comparison with actions taken in other proceedings or against other individuals in the same proceeding.”), *pet. for review denied*, 168 F.3d 478 (1998). Finally, we do not consider mitigating that no customer appeared to have suffered any actual harm because of North American’s operational problems. *See Dep’t of Enforcement v. Mizenko*, Complaint No. C8B030012, 2004 NASD Discip. LEXIS 20, at *20 (NASD NAC Dec. 21, 2004) (“[T]here is no authority for the proposition that the absence of harm to customers is mitigating.”), *aff’d*, Exchange Act Rel. No. 52600, 2005 SEC LEXIS 2655 (Oct. 13, 2005).

²⁸ *Guidelines*, at 7 (Principal Considerations in Determining Sanctions, No. 12) and 108.

Firm's failure to retain emails during the relevant time period. Consequently, we affirm the sanctions imposed by the Hearing Panel for Busacca's failure to reasonably supervise North American's operations.

B. Registration Violation

For registration violations, the Guidelines recommend a fine of \$2,500 to \$50,000, and a suspension of up to six months.²⁹ In egregious cases, the Guidelines suggest a lengthier suspension of up to two years or a bar.³⁰ The Guidelines instruct adjudicators to consider, among other things, the nature and extent of the unregistered person's responsibilities.³¹

We affirm the Hearing Panel's imposition of a \$5,000 fine for Busacca having permitted the Firm to employ an unregistered chief compliance officer. Busacca supervised McAuliffe, and although Goble made the ultimate decision to hire McAuliffe, Busacca failed to confirm that McAuliffe was appropriately qualified. McAuliffe, however, had previously registered as a general securities principal and served as a chief compliance officer with other firms, and Enforcement did not allege that McAuliffe failed to perform in his capacity as the Firm's chief compliance officer or that McAuliffe's lack of registration had any connection to the Firm's operational difficulties. Under the circumstances, a \$5,000 fine is appropriate.

V. Conclusion

We affirm the Hearing Panel's finding that Busacca violated NASD Rules 3010 and 2110 by failing to reasonably supervise North American's operations, and violated NASD Rules 1022(a) and 2110 by permitting North American to employ an unregistered individual as its chief

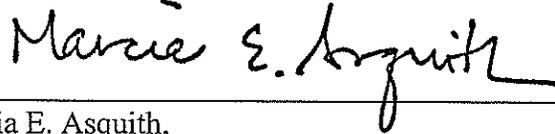
²⁹ *Guidelines*, at 48.

³⁰ *Id.*

³¹ *Id.*

compliance officer. Accordingly, we suspend Busacca in all principal capacities for six months and fine him \$25,000 for his supervisory violation, and impose a \$5,000 fine for the registration violation. We affirm the Hearing Panel's imposition of \$2,078.60 in costs.³²

On behalf of the National Adjudicatory Council,



Marcia E. Asquith,
Senior Vice President and Corporate Secretary

³² Pursuant to FINRA Rule 8320, any member that fails to pay any fine, costs, or other monetary sanction imposed in this decision, after seven days' notice in writing, will summarily be suspended or expelled from membership for non-payment. Similarly, the registration of any person associated with a member who fails to pay any fine, costs or other monetary sanction, after seven days' notice in writing, will summarily be revoked for non-payment.

We also have considered and reject without discussion all other arguments of the parties.