

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS**

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

THOMAS EDMUND CONNORS
(CRD No. 1081185),

Respondent.

Disciplinary Proceeding
No. 2012033362101

Hearing Officer—MJD

HEARING PANEL DECISION

January 15, 2016

Respondent violated FINRA Rules 3270 and 2010 by engaging in undisclosed outside business activities. For this misconduct, Respondent is suspended from associating with any member firm in any capacity for 14 months and fined \$40,000. Respondent is also ordered to pay hearing costs.

Appearances

For the Complainant: Michael J. Newman, Esq., Woodbridge, New Jersey, and Matthew M. Ryan, Esq., Philadelphia, Pennsylvania, Department of Enforcement, Financial Industry Regulatory Authority.

For the Respondent: Joel S. Forman, Esq., and Marc B. Schlesinger, Esq., Vedder Price P.C., New York, New York.

I. Introduction

Respondent Thomas Edmund Connors engaged in undisclosed outside business activities while registered with Prime Capital Services, Inc. (“Prime Capital” or “Firm”). Without Prime Capital’s knowledge, Connors charged customers a fee for opening their managed advisory accounts in addition to the fees they paid under their agreements with the Firm’s advisory affiliate. He also charged customers a tax preparation fee without notifying his Firm, and he sold insurance products for insurance companies that were not on Prime Capital’s approved list. Connors’ undisclosed outside business activities violated FINRA Rules 3270 and 2010.

The Department of Enforcement filed a three-cause Complaint on December 11, 2014. Connors filed an Answer and Affirmative Defenses on January 29, 2015. A hearing was held on October 13-15, 2015, in Woodbridge, New Jersey.

Each cause alleges that Connors failed to disclose an outside business activity and accordingly violated FINRA Rules 3270 and 2010. The first cause alleges that from October

2011 to May 2012 Connors charged 47 customers \$399 each for opening accounts with him through Prime Capital's affiliated investment advisor, Asset & Financial Planning, Ltd. ("AFP"). Connors' fee was in addition to the standard advisory fees that clients agreed to pay AFP. According to the Complaint, Connors received approximately \$18,000 from this undisclosed activity.¹

Cause two alleges that from January 2012 to June 2012 Connors earned approximately \$10,000 by directly charging 32 customers tax preparation fees ranging from \$150 to \$500.²

Cause three alleges that from May 2011 to May 2012 Connors secretly sold insurance products of insurance companies that Prime Capital and its parent company had not approved. According to the Complaint, Connors earned approximately \$18,000 in commissions from the undisclosed sale of insurance policies to clients during this period.³

In his Answer, Connors denies that he violated FINRA Rule 3270. He claims that the services he provided were not outside the scope of his relationship with Prime Capital, and in any case the Firm had notice of and approved his services because they were expressly permitted under his written employment agreement with the Firm's parent company, Gilman Ciocia, Inc. ("Gilman").⁴ Connors also raises a jurisdictional defense. He argues that even assuming he engaged in the activities alleged, they constitute only a breach of the terms of his employment agreement with Gilman and Prime Capital, and therefore his misconduct is beyond FINRA's regulatory reach.⁵

II. Findings of Fact

A. Respondent's Background

Connors first became registered with a FINRA member firm in 1982. He was registered with Prime Capital from 1993 to July 2012, as a General Securities Representative and General Securities Principal. He was also registered with the Firm's advisory affiliate, AFP, beginning in February 2011.⁶ Connors managed Prime Capital's branch office in Toms River, New Jersey, an Office of Supervisory Jurisdiction.⁷ Connors has been registered with another FINRA member firm since September 2012.⁸ He earned an MBA in finance in 1993, and became a Certified

¹ Complaint ("Compl.") ¶¶ 13-16.

² *Id.* ¶¶ 19-24.

³ *Id.* ¶¶ 27-31.

⁴ Answer ("Ans.") at 8.

⁵ *Id.* at 8, 10-11.

⁶ Compl. ¶ 6; Ans. ¶ 6; CX-1, at 6-8; CX-19, at 5, 7.

⁷ Tr. 52-53, 56.

⁸ CX-1, at 6.

Senior Advisor and Certified Financial Planner in 2005 and 2010, respectively. In 2012, Connors was working towards becoming a Chartered Financial Analyst.⁹

On July 19, 2012, Prime Capital filed a Uniform Termination Notice for Securities Industry Registration (“Form U5”) terminating Connors’ registration with the Firm. In the Form U5, Prime Capital disclosed that through an internal review it had determined that Connors had engaged in undisclosed outside business activities relating to his investment advisory, tax preparation, and insurance services.¹⁰

B. Connors’ Relationship with Prime Capital

Most of Prime Capital’s registered representatives were independent contractors, but some registered representatives, including Connors, had employment relationships with the Firm through Gilman. These persons agreed to work for Gilman and its affiliated companies,¹¹ and accordingly entered into employment contracts with Gilman.¹²

Connors signed an “Employment Agreement” with Gilman on April 10, 2000, seven years after registering with Prime Capital. Gilman’s primary business was tax preparation and financial planning.¹³ Gilman wholly owned Prime Capital, AFP, and its insurance affiliate, Prime Financial Services, Inc. (“Prime Financial”). Gilman and each of the affiliates’ headquarters were located in the same offices in Poughkeepsie, New York.¹⁴ Gilman agreed to employ Connors as a registered representative with Prime Capital. Pursuant to the employment agreement, Gilman also agreed to acquire the assets of Connors’ financial services business called Lighthouse Financial Services in exchange for cash and Gilman stock.¹⁵

Unlike independent contractors, employees of Gilman had to conduct all of their business through Gilman and the affiliated entities.¹⁶ Connors’ employment arrangement with Gilman and Prime Capital was renewed annually. Beginning each calendar year, he signed a “Tax Preparer and Accountant Employment Agreement” (“Tax Preparer Agreement”) with Gilman, Prime Capital, Prime Financial, and AFP.¹⁷ There were no separate or additional employment agreements between Connors and Prime Capital.¹⁸ Relevant to this case are the Tax Preparer

⁹ Tr. 500.

¹⁰ CX-1, at 21.

¹¹ Tr. 37.

¹² Tr. 364-65.

¹³ Tr. 38.

¹⁴ Tr. 166.

¹⁵ CX-17, at 2; RX-1; Tr. 501-02.

¹⁶ Tr. 365-66.

¹⁷ RX-3; RX-4; RX-5; RX-6; RX-7; RX-8.

¹⁸ Tr. 280-81.

Agreements that Connors, Gilman, and each of the affiliates executed on January 10, 2011, and January 10, 2012, which in substantive part do not differ from each other or from prior agreements.

The Tax Preparer Agreements obligated Connors to serve the affiliates “exclusively, faithfully, and to the best of [his] abilities and [required that he] devote [his] full working time and efforts to the performance of [his] duties.” They also prohibited Connors from circumventing affiliates’ client relationships by “either directly or indirectly [] knowingly do work for, serve, solicit, or advertise for, any client” of the affiliates.¹⁹

Connors was compensated by Gilman regardless of whether the commissions and fees he earned were derived from securities transactions or his advisory, tax, and insurance services. Under his employment arrangement with Gilman, he received a payout of 47 percent from the revenue he brought to the affiliate companies.²⁰ Gilman paid his branch office overhead, including rent, staff salaries, and all employee benefits.²¹ This payout rate was higher than most other Gilman and Prime Capital employees with a similar contractual arrangement because Connors was a large producer.²²

C. The Investigation That Led to This Disciplinary Proceeding

Prime Capital began an investigation into Connors’ activities after Michael Doherty, Connors’ immediate supervisor and the Firm’s Vice President for Branch Office Development, discovered a photocopy of a customer’s check made payable to Connors during a routine office inspection on June 19, 2012.²³ According to Doherty, the check “immediately raised a red flag.”²⁴ At approximately the same time, Connors, or someone in his branch office, inadvertently forwarded a photocopy of a letter Connors sent to a customer instructing the customer to make a \$399 check directly payable to him. Connors’ letter was included in a package of customer correspondence and application forms for an advisory account the Toms River branch office sent to AFP’s Poughkeepsie headquarters.²⁵

Led by Marshall Baron, the Firm’s Chief Compliance Officer, Prime Capital initiated an investigation into Connors’ activities. On June 20, 2012, the day after Doherty discovered a photocopy of the check among Connors’ customer files, Baron, Doherty, and Glenn McBride, the Firm’s Director of Supervision and former Chief Compliance Officer, conducted an

¹⁹ RX-7, at 1, 3; RX-8, at 1, 3.

²⁰ CX-17, at 15. For tax preparation services, Connors received 30 percent of billings received by Gilman. RX-7, at 1; RX-8, at 1.

²¹ Tr. 375, 433.

²² Tr. 375.

²³ Tr. 295, 315, 342, 349, 358.

²⁴ CX-10.

²⁵ Tr. 58, 359, 378-79, 434-35.

unannounced examination of the Toms River branch office. During the on-site examination, the Firm determined that Connors had received checks for \$399, which he described as a “one-time set up fee” to new customers opening advisory accounts. The Firm then asked Connors to produce copies of his personal tax returns and bank records, which led to the Firm uncovering more outside activities.²⁶

As a result of the audit, the Firm determined that Connors had engaged in “multiple irregularities in all three areas”—investment advisory, tax preparation, and insurance services.²⁷ On June 27, 2012, Prime Capital formally suspended Connors and instructed him not to have contact with any customers.²⁸ On July 11, 2012, Gilman formally terminated Connors’ relationship with Gilman and the affiliate companies.²⁹

After the Firm filed a Form U5 on July 19, 2012, based on Prime Capital’s findings, FINRA initiated an investigation into Connors’ possible misconduct.³⁰ On August 2, 2012, FINRA’s Department of Enforcement sent Prime Capital its first request for the documents and information that led to the Firm’s decision to terminate Connors.³¹ Enforcement also requested and received information and documents from Connors.³²

D. Prime Capital’s Written Supervisory Procedures

Prime Capital maintained written supervisory procedures that required its employees to disclose outside business activities in writing and to obtain the Firm’s approval before engaging in such activity. The procedures provided examples of activities that employees must report to the Firm. Relevant to this proceeding are:

- acting as an independent contractor to an outside party
- receiving compensation or having the reasonable expectation of compensation from any other person as a result of a business activity outside the scope of employment or other relationship with [Prime Capital]³³

Each year, Connors signed Prime Capital’s “Annual RR/IAR Certification” form in which he attested that he understood that he was prohibited from accepting “any check made out

²⁶ CX-7, at 2.

²⁷ CX-10; Tr. 59-61.

²⁸ CX-7, at 3; Tr. 73-75.

²⁹ CX-7, at 6-7.

³⁰ FINRA investigator Jack Litsky testified, “This was a case where the firm did most of the analysis and investigation.” Tr. 494.

³¹ CX-2.

³² CX-13.

³³ CX-12, at 5.

to me personally” for “securities transactions or financial services.”³⁴ He also acknowledged that he would “fully comply with the disclosure requirements of [FINRA Rule 3270].” Further, Connors acknowledged, “I may not engage in any OBA [outside business activity] without first securing written permission from [Prime Capital] to do so. I acknowledge that if [Prime Capital] does not approve an activity, that [sic] I may not engage in it. I will not engage in any OBA absent such written approval.”³⁵

In November 2011, Prime Capital conducted an annual examination of the Toms River branch office. The examination included a questionnaire that asked Connors, among other things, what outside business activities, if any, he was engaged in and whether he had disclosed them to Prime Capital. Connors did not disclose to the Firm that clients were paying him directly for his investment advisory, tax preparation, and insurance services.³⁶

E. Connors’ Outside Business Activities

We discuss below each of Connors’ three outside business activities—investment advisor, tax preparation, and insurance.

1. Connors’ Investment Advisory Fees

After receiving copies of Connors’ correspondence in June 2012 directing a customer to pay him \$399 for the investment advisor service, the Firm learned that Connors had been paid the same amount by 46 other clients. Connors received a total of \$18,753 from the 47 investment advisory clients.

This was not the first time that the Firm had learned that Connors had asked customers for a separate fee for investment advisor services. In December 2011, Connors inadvertently included a copy of a letter to customer JR that Connors submitted to AFP as part of the customer’s account application. The letter instructed JR to pay a fee of \$399 directly to Connors. The fee, Connors explained to JR in the letter, was “for the one-time set up fee of the new managed accounts.”³⁷

In 2011, McBride was Prime Capital’s Chief Compliance Officer. He called Connors for an explanation of the \$399 fee he had requested from customer JR.³⁸ Connors had not sought permission from McBride before deciding to charge customers the \$399 fee.³⁹ Connors told

³⁴ CX-15, at 3.

³⁵ CX-15, at 8.

³⁶ CX-20, at 5. During the Firm’s June 20, 2012 exam of the branch and Connors’ activities, Connors again failed to disclose that he was charging clients for investment advisory, tax preparation, and insurance services. CX-24, at 5.

³⁷ CX-11; CX-18.

³⁸ CX-11.

³⁹ Tr. 544. Connors also testified that he discussed his asset allocation model with Doherty but did not mention to him that he intended to charge customers a separate fee. Tr. 544-45.

McBride that the fee was “for all the planning work he did for the client to this point,” and he had just started charging the fee. McBride told Connors that a fee for preparing a financial plan could be charged if it were disclosed to the customer, but payment had to be made to AFP, the advisory affiliate.⁴⁰ According to Baron, McBride also told Connors that it was “completely improper” to charge a client a fee for opening an account. Baron also testified that such a fee would have to be approved by the Firm, and paid to AFP, not Connors.⁴¹ According to Baron, McBride thought Connors would follow his instructions because they were clear and explicit. As a result, McBride did not follow up with Connors.⁴²

Connors ignored McBride’s directive. In June 2012, Connors inadvertently sent AFP a photocopy of another letter to a customer asking for payment of his \$399 fee to open a managed account. As a result of its investigation of Connors’ activities, Prime Capital found other correspondence from Connors to new investment advisor clients.

For example, in a form he sent to customer CB, and signed by the customer on December 12, 2011, Connors described the \$399 charge as a “one-time set up fee.”⁴³ In a February 7, 2012 letter to customers NM and MM, a married couple, Connors enclosed paperwork for them to complete and submit to open a managed account. He instructed the couple to send him a check for \$399 payable to him for the “one-time set up fee.”⁴⁴ In another form, Connors described the \$399 fee as a “one-time fee [that] is separate and distinct from the AFP [management fee] platform.”⁴⁵ Each of the 47 customers who opened a managed account with AFP also opened corresponding accounts with Prime Capital.⁴⁶ Each customer also signed Connors’ form charging \$399 for the “one-time set up fee.”⁴⁷ The customers were also obligated to pay a management fee for advisory accounts, ranging from a low of 1.125 percent for assets exceeding \$5 million to a high of two percent for assets below \$1 million.⁴⁸ Under the terms of his employment agreement, Connors was entitled to receive 47 percent of the management fees his clients paid AFP.

Connors does not dispute that he charged customers \$399 and that they paid him directly. In a handwritten letter to Baron dated June 27, 2012, the day the Firm suspended him, Connors explained why he believed he was entitled to the money. He wrote that “over the past years,” he had developed a “binary” investment model that tells him if his customers should invest in

⁴⁰ CX-11.

⁴¹ Tr. 87, 142-43, 217.

⁴² CX-18.

⁴³ CX-8, at 2.

⁴⁴ CX-8, at 1.

⁴⁵ CX-8, at 3.

⁴⁶ Tr. 446, 543.

⁴⁷ Tr. 561.

⁴⁸ CX-8, at 2, 3.

certain Fidelity Select Funds or “sit in cash.” Over the previous nine months, according to Connors, he had performed “extensive research, on my own without any monetary reimbursement from [Prime Capital], to modify my model where I can use [it] to help clients manage their growth portion of their portfolio.” He added that “[t]his one time, per family fee is compensation for my additional time, education, additional monies spent & intellectual property.”⁴⁹

Two months later, in a written submission to FINRA in response to a Rule 8210 request for information, Connors elaborated on why he was entitled to the fee. He wrote that he “never collected improper [investment advisory] fees from customers” because the \$399 fee they “paid were for services associated with [his] role as a certified financial planner; services that were rendered with the sole motive of increasing the worth of my customers’ portfolios and achieving their goals as investors.”⁵⁰ He charged the fee “as compensation for the additional time, education and fiscal expense” he incurred in creating his model.⁵¹

Connors claimed that he never intended to hide the \$399 fee from Prime Capital because he kept customers’ signed consent forms in their files at the branch and therefore they were available for anyone to see. Connors noted that, even though he had placed documents evidencing the \$399 fee in customer files, Prime Capital’s compliance department conducted an audit of his branch in November 2011 and found no irregularities.⁵²

At the hearing, Connors acknowledged that he ignored McBride’s December 2011 directive. He claimed that he had “the right to charge for financial planning and investment modeling fees” because he was a certified financial planner.⁵³ Connors testified that he told McBride he “respectfully disagreed with him” because, as a certified financial planner, “it was only fair for me to be compensated for my additional time.”⁵⁴ Accordingly, Connors continued to accept checks for \$399 from new investment advisory clients.

2. Connors Charges Customers Tax Preparation Fees

Connors was permitted to provide tax preparation and consulting services for Gilman clients while he was registered with Prime Capital. Gilman paid Connors 30 percent of the fees it collected from clients for Connors’ tax services.⁵⁵ During its investigation of Connors’ \$399 advisory account fee, Prime Capital discovered that Connors was providing tax services for certain clients and was being paid directly by them. It found that Connors collected a minimum

⁴⁹ CX-7, at 4.

⁵⁰ CX-13, at 8. Connors acknowledged that he began charging customers the \$399 fee in October 2011.

⁵¹ CX-13, at 8.

⁵² CX-13, at 8; RX-14; Tr. 525-26.

⁵³ Tr. 463.

⁵⁴ Tr. 522; RX-7, at 1; RX-8, at 1.

⁵⁵ Tr. 455.

of \$10,035 from 32 tax preparation customers from January to June 2012.⁵⁶ Connors never sought the Firm's approval for the personal tax work. Connors acknowledged that had he disclosed the fees he earned from the outside tax business to Prime Capital and Gilman, he would have been entitled to keep only 30 percent of what customers paid him.⁵⁷

Connors sent tax customers invoices generated by TaxWise, a commercial tax software program used by Gilman. In instances when Connors received payments directly from customers, he usually discounted his fees in the TaxWise system for his tax preparation work before printing an invoice for the customer. He later altered the records in TaxWise to falsely show that he had not charged the customer for his work. As a result, if a Gilman or Prime Capital supervisor reviewed a customer's invoice in TaxWise, it appeared that Connors charged the customer nothing when in fact he had.⁵⁸ Connors admitted that he went into the TaxWise system and altered the invoices to show that they were fully discounted.⁵⁹ Connors did not tell Prime Capital that he was "zeroing" out the tax invoices and receiving payments from customers.⁶⁰

For example, based on the work Connors performed for customer EC, TaxWise generated a \$447 invoice for completing various state and federal tax schedules for 2011. Connors discounted \$247 and invoiced EC \$200. He wrote on the invoice that EC should make her check payable to Connors. EC wrote Connors a check for \$200, dated April 10, 2012.⁶¹

In another instance, Connors did not discount his tax work. He sent customer DM an invoice generated by TaxWise for \$252 for completing her 2011 state and federal returns, with the instruction "pls make check payable to Thomas E. Connors." DM sent Connors a check payable to Gilman instead, dated April 14, 2012; Connors wrote his name over Gilman's and deposited the check in his personal account.⁶²

Years earlier, Gilman had instructed Connors that he could not perform tax work outside of his arrangement with Gilman. In December 2000, shortly after signing his employment agreement with Gilman, Connors asked for permission to perform tax preparation work for elderly persons residing in nursing homes. Gilman denied his request in writing, telling him that such activity would "constitute a breach" of his employment agreement. It reminded him that under his employment agreement he had to "devote [his] full working time and efforts to

⁵⁶ CX-3, at 9. Baron, Prime Capital's Chief Compliance Officer, testified that he stopped looking for more customers who paid Connors directly for tax preparation services once he reached the \$10,000. He believed he would have found additional customers had he continued his search. Tr. 99-101.

⁵⁷ Tr. 455.

⁵⁸ Tr. 69-70, 380-82.

⁵⁹ Tr. 570.

⁶⁰ Tr. 584.

⁶¹ CX-3, at 2.

⁶² CX-3, at 11.

working with and developing clients” for Gilman.⁶³ Connors admitted at the hearing that he ignored the instructions Gilman gave him in December 2000.⁶⁴

In a written response to a request for information pursuant to FINRA Rule 8210, Connors stated that, “for the last ten years,” he prepared tax returns for “my family, close friends and select clients, who paid me directly for the service.” He said he never hid these services from Prime Capital because his practice was to place copies of customer checks in their files, which the Firm audited annually.⁶⁵ He added that documents reflecting his tax work were also located in Prime Capital’s computer system. As a consequence, he “was under the impression for 10 years that charging my customers directly for tax preparation work was permitted by [Prime Capital].”⁶⁶ At the hearing, Connors testified that he felt entitled to keep fees for a portion of his tax services because he worked overtime during tax season.⁶⁷

At the hearing, Connors admitted that in 2012 he accepted approximately \$10,000 from 32 customers for tax preparation services that he did not disclose to Prime Capital.⁶⁸

3. Connors Sold Insurance Policies that Were Not Approved by Prime Capital and the Affiliates

Prime Capital and Gilman allowed Connors to sell insurance products only through the insurance affiliate, Prime Financial. Connors’ 2000 Employment Agreement with Gilman specifically instructed him to engage in insurance services through companies Gilman had approved:

Employee shall submit all business on life/health/disability insurance, and on annuities, for which he renders services through [Gilman’s] corporate license, or through other licensed insurance agents of [Gilman] designated by [Gilman] from time to time in writing. . . . Employee shall not submit any insurance business to an insurance company, directly or indirectly, that [Gilman] has not approved and been licensed with.⁶⁹

Connors does not dispute that he made secret arrangements to sell the products of other insurance carriers. In August 2012, he told FINRA that “for the last 10 years” he had sold

⁶³ CX-9.

⁶⁴ Tr. 454, 510-12.

⁶⁵ CX-13, at 9.

⁶⁶ CX-13, at 9.

⁶⁷ Tr. 453, 456-57.

⁶⁸ Tr. 451-52, 524. Connors also admitted that an unknown number of clients who paid him directly for tax work were also Prime Capital customers. Tr. 448-49. Connors testified that each year, from 2007 to 2012, he received fees from 20 to 30 customers for his tax services. Tr. 584.

⁶⁹ CX-17, at 11. The agreement also warned Connors that he could be terminated if he violated this prohibition. CX-17, at 11.

customer insurance products provided by insurance companies that were not authorized by Prime Capital and the affiliates. (Contrary to what he told FINRA, Connors testified that he had engaged in the outside insurance activity for as many as four years before the activity was detected by the Firm in 2012.⁷⁰)

He explained to FINRA: “Since selling insurance is within the scope of the activities in which I am permitted to engage under various licenses, and is within the scope of my relationship with [Prime Capital], I did not think that this was an outside business activity that required a disclosure.”⁷¹ He claimed that the insurance group at Prime Financial “has been below par for a long time with respect to the products it offers and its level of customer service.”⁷² At the hearing, Connors testified that the insurance department was not up to his “standards” and had high personnel turnover.⁷³ He acknowledged that he could have complained to his supervisors and even the President of the Firm and Prime Financial but he did not.⁷⁴ Connors testified that one of the reasons he engaged in the unapproved and undisclosed insurance business was so he could earn extra money.⁷⁵

Connors reported his commissions from the unapproved insurance companies on his 2010 and 2011 federal tax returns. On the Schedule C (“Profit or Loss From Business (Sole Proprietorship)”) for 2010 and 2011, he reported that he had an “Insurance” business, separate from the earnings he received from Gilman and reported on a Form W-2. On his federal tax return for 2010, Connors reported gross receipts from insurance commissions of \$89,018; on his 2011 federal tax return, he reported gross receipts from insurance commissions of \$34,380.⁷⁶ Connors testified that he considered this money income from his sole proprietorship.⁷⁷

Connors acknowledged that he did not share the commissions he received from unapproved insurance companies with Gilman or Prime Financial. Under his arrangement with Gilman, Connors was paid 47 percent of the total commissions Prime Financial received.⁷⁸

From May 2011 to May 2012, Connors received \$17,696 in commissions from the sale of insurance products through unapproved carriers.⁷⁹

⁷⁰ Tr. 472; CX-13, at 9.

⁷¹ CX-13, at 9.

⁷² CX-13, at 9.

⁷³ Tr. 469.

⁷⁴ Tr. 470-71.

⁷⁵ Tr. 471-72.

⁷⁶ CX-4, at 4-5. Connors’ tax returns for years before 2010 were not offered in evidence.

⁷⁷ Tr. 567.

⁷⁸ CX-17, at 15.

⁷⁹ CX-5, at 15.

III. Conclusions of Law

FINRA Rule 3270 prohibits registered persons from being an employee, independent contractor, sole proprietor, officer, director, or partner of another person or from being compensated or having the reasonable expectation of compensation from any other person as a result of any business activity outside the scope of the relationship with their member firm, unless they have provided prior written notice to the member, in the form specified by the member. The purpose of the Rule “is to ensure that firms receive prompt notification of all outside business activities of their associated persons so that the member’s objections, if any, to such activities could be raised at a meaningful time and so that appropriate supervision could be exercised as necessary under applicable law.”⁸⁰ A registered representative must “disclose outside business activities at the time when steps are taken to commence a business activity unrelated to his relationship with his firm.”⁸¹ The sweep of the Rule is intentionally broad, requiring registered persons “to report *any* kind of business activity engaged in away from their firms,”⁸² not only business activities related to securities.⁸³ A violation of FINRA Rule 3270 constitutes conduct inconsistent with just and equitable principles of trade and therefore violates FINRA Rule 2010.⁸⁴

The outside business activity rule has been described as a “prophylactic rule designed to assure that an employee engages in conduct consistent with his duties to his employer and its clients.”⁸⁵ When registered persons engage in business outside the scope of their relationships with their firm, without notice to the firm, they deprive the public of the protection afforded by the oversight and supervision provided by their firm.⁸⁶

Connors contends that he did not violate FINRA Rule 3270. His argument is disingenuous. First, he claims that his activities were within the scope of his employment

⁸⁰ *Dep’t of Enforcement v. Houston*, No. 2006005318801, 2013 FINRA Discip. LEXIS 3, at *32 (NAC Feb. 22, 2013), *aff’d*, *Kent M. Houston*, Exchange Act Release No. 71589, 2014 SEC LEXIS 614 (Feb. 20, 2014) (quoting Proposed Rule Change by NASD Relating to Outside Business Activities of Associated Person, Exchange Act Release No. 26063, 1988 SEC LEXIS 1841, at *2-3 (Sept. 6, 1988)); *see also* NASD Notice to Members 88-86, 1988 NASD LEXIS 207 (Nov. 1988) (introducing the predecessor to FINRA Rule 3270 and explaining that it is “intended to improve the supervision of registered personnel by providing information to member firms concerning outside business activities of their representatives”).

⁸¹ *Dep’t of Enforcement v. Schneider*, No. C10030088, 2005 NASD Discip. LEXIS 6, at *13-14 (NAC Dec. 7, 2005) (citing *Dep’t of Enforcement v. Abbondante*, No. C10020090, 2005 NASD Discip. LEXIS 43, at *30-31 (NAC Apr. 5, 2005)) (rejecting argument that representative was not required to disclose outside business activity that was formed to conduct future business).

⁸² NASD Notice to Members 01-79, 2001 NASD LEXIS 85, at *7 (Dec. 2001) (emphasis in original).

⁸³ *Dist. Bus. Conduct Comm. v. Cruz*, No. C8A930048, 1997 NASD LEXIS 123, at *101 (NBCC Oct. 31, 1997).

⁸⁴ *See Dep’t of Enforcement v. Moore*, No. 2008015105601, 2012 FINRA Discip. LEXIS 45, at *25 (NAC July 26, 2012).

⁸⁵ *Wanda P. Sears*, Exchange Act Release No. 58075, 2008 SEC LEXIS 1521, at *26 n.38 (quoting *Herbert J. Burns*, 52 S.E.C. 823, 829 (1996)).

⁸⁶ *Id.* at *26 n.39 (citing *Micah C. Douglas*, 52 S.E.C. 1055, 1060 (1996)).

agreement with Prime Capital and Gilman because he was authorized to provide advisory, tax, and insurance services to customers.⁸⁷ Connors argues that if he is liable for anything, it is limited to breaching his employment contract with Gilman, Prime Capital, and the affiliates by performing advisory, tax, and insurance work outside the scope of the agreement. Because Gilman, AFP, and Prime Financial are not FINRA member firms, Connors insists, FINRA has no jurisdiction to regulate Connors' advisory, tax, and insurance work.⁸⁸ This latter argument would undermine the purpose of FINRA's outside business activity rule because a business activity outside the scope of an associated person's relationship with a member firm typically involves activities with a non-registered entity or person.

In any event, Connors' undisclosed outside business activities were not with Gilman, AFP, and Prime Capital. They were with the individual clients whom he charged for the advisory and tax services. With respect to the insurance-related activities he engaged in, Connors' undisclosed outside business activities were with the insurance companies his employer had not placed on its list of approved companies and from whom he received commissions directly. In his 2010 and 2011 federal tax returns, Connors acknowledged that his income from his undisclosed insurance activities was a sole proprietorship,⁸⁹ which is one of the outside business activities specifically identified by FINRA Rule 3270 that must be disclosed.

Connors cites two FINRA Office of Hearing Officers decisions in support of his defense that an associated person's breach of contractual obligations does not constitute a violation of Rule 3270.⁹⁰ The Hearing Panel finds that these cases are inapposite to the facts present here.

In *Department of Enforcement v. Somerindyke*, the hearing panel dismissed a charge that respondents violated NASD Rule 3030 by engaging in outside business activities without notice to their firm.⁹¹ The respondents disclosed in writing their involvement in the operations of a marketing company they formed. Their employer firm permitted them to maintain "passive participation" but not involvement in the daily operations of the company. Despite the restrictions imposed by the firm, respondents continued to be actively, rather than passively, engaged in the company.⁹² The hearing panel concluded that the *Somerindyke* respondents met the requirement of Rule 3030 by providing written notice that they were engaged in outside business activities outside the scope of their employment with the firm even though they exceeded the restrictions the firm imposed.⁹³

⁸⁷ Connors' Pre-Hearing Brief, at 3-5.

⁸⁸ *Id.* at 9.

⁸⁹ CX-4, at 4-5.

⁹⁰ Connors' Pre-Hearing Brief, at 6-8.

⁹¹ *Dep't of Enforcement v. Somerindyke*, No. 2009020081301, 2012 FINRA Discip. LEXIS 69 (OHO Dec. 17, 2012).

⁹² *Id.* at *12.

⁹³ *Id.* at *16.

Connors misunderstands the purpose of FINRA’s outside business activity rule. Unlike Connors, the respondents in *Somerindyke* gave their firm written notice of their outside activities, as Rule 3030 requires, thereby providing the firm with the opportunity to regulate those activities. Also unlike Connors, the *Somerindyke* respondents did not deprive their firm of funds it was due from the outside business activities.

Connors also cites an older case, *Department of Enforcement v. Sahai*,⁹⁴ for a similar proposition: violating a contractual restriction or internal policy of a firm does not constitute a violation of the outside business activity rule.⁹⁵ In *Sahai*, the respondent provided written disclosure that he was engaged in an outside insurance business beyond the scope of his employment with his firm. Enforcement alleged in its complaint that Sahai violated Rule 3030 because he did not submit to his firm for approval his outside business letterhead, fax form, and business card.⁹⁶ The hearing panel dismissed this charge because the respondent had given notice of the outside business in the form the firm required. If he used an unapproved letterhead, fax form, and business card, the hearing panel reasoned, that does not constitute a violation of the outside business activity rule.⁹⁷ Again, unlike Connors, Sahai gave his firm proper written notice of the nature of his outside activities, providing his firm with the opportunity to supervise the activity.

Based on the foregoing, the Hearing Panel finds that Connors engaged in outside business activities. He charged 47 advisory customers a “one-time set up fee” when they opened their accounts. He did so even after being admonished by his supervisor that he could not charge such fees. He also charged 32 customers for his services in preparing their tax returns. And he was paid commissions for selling insurance products for insurance companies that his Firm did not approve.

In each instance, Connors failed to provide Prime Capital written notice of these activities for which he received compensation. Accordingly, the Hearing Panel concludes that Connors violated FINRA Rule 3270, which also constitutes a violation of FINRA Rule 2010.

IV. Sanctions

FINRA’s Sanction Guidelines provide that when the outside business activities do not involve aggravating conduct, the panel should consider a suspension of up to 30 business days. When the outside business activities involve aggravating conduct, the panel should consider a suspension of up to one year. In egregious cases, including those involving a substantial volume

⁹⁴ *Dep’t of Enforcement v. Sahai*, No. C9B020032, 2003 NASD Discip. LEXIS 29 (OHO June 23, 2003), *aff’d and modified on other grounds*, Rooney A. Sahai, Exchange Act Release No. 51549, 2005 SEC LEXIS 864 (Apr. 15, 2005), 2006 NASD Discip. LEXIS 2 (NAC Mar. 2, 2006), Rooney A. Sahai, Exchange Act Release No. 55046, 2007 SEC LEXIS 13 (Jan. 5, 2007).

⁹⁵ Connors’ Pre-Hearing Brief, at 7-8.

⁹⁶ *Sahai*, 2003 NASD Discip. LEXIS 29, at *5-7.

⁹⁷ *Id.* at *28-29.

of activity or significant injury to customers, a longer suspension or a bar is appropriate.⁹⁸ The Guidelines also recommend a fine of \$2,500 to \$73,000 and state that the panel may also order disgorgement.⁹⁹

The principal considerations in determining sanctions for undisclosed outside business activities relevant to this matter include (i) whether the outside activity involved customers of the firm; (ii) the duration of the outside activity, the number of customers, and the dollar volume of sales; (iii) whether the respondent's marketing and sale of the product or service could have created the impression that the employer had approved the product or service; and (iv) whether the respondent misled his employer member firm about the existence of the outside activity or otherwise concealed the activity from the firm.¹⁰⁰

In addition, the relevant generally applicable Principal Considerations in Determining Sanctions include whether Connors (i) accepted responsibility for and acknowledged the misconduct prior to intervention by his Firm or regulator; (ii) engaged in numerous acts and a pattern of misconduct; (iii) engaged in the misconduct over an extended period of time; (iv) attempted to conceal his misconduct or to lull into inactivity, mislead, deceive, or intimidate his Firm; (v) caused injury, directly or indirectly, to others, including his Firm and the investing public; (vi) acted intentionally or negligently; and (vii) was motivated by the potential for monetary or other gain.¹⁰¹

Because of the presence of multiple aggravating factors, the Panel finds that Connors' misconduct is egregious and calls for substantial sanctions. Connors' outside business activities involved Prime Capital's customers. All 47 advisory clients of AFP were also Prime Capital customers, and some of the tax customers, Connors admitted, also were Firm customers. Connors engaged in a pattern of misconduct that was intended to line his pockets at the expense of his employer. He effectively misappropriated money that should have been received by Gilman and shared with Prime Capital and the affiliates.

The Complaint alleges that Connors' misconduct extended for about a year, from May 2011 to June 2012. Connors admitted in writing to FINRA and at the hearing that he had engaged in unapproved and undisclosed private tax preparation and insurance services for many

⁹⁸ FINRA Sanction Guidelines ("Guidelines") at 13 (2015), <http://www.finra.org/sanction-guidelines>.

⁹⁹ Guidelines at 13. The Panel does not order disgorgement because Connors made restitution to Gilman when he bought back his financial services business from Gilman, in August 2012. The purchase price included an adjustment for the money Gilman claimed he owed. RX-21. He also separately disgorged to AFP \$18,354 in fees he earned from charging 46 advisory customers \$399 each. RX-21. AFP then made restitution to the customers. In 2013, a 47th customer came forward who said he had paid Connors \$399 for opening an advisory account. RX-27, at 2; Tr. 81, 220. The Panel does not find that Connors' restitution is mitigating because Connors made payment only after detection and did so in connection with buying back his business from Gilman. Guidelines at 6 (Principal Consideration in Determining Sanctions No. 4).

¹⁰⁰ Guidelines at 13.

¹⁰¹ *Id.* at 6-7 (Principal Considerations in Determining Sanctions Nos. 2, 8, 9, 10, 11, 13, and 17).

years. The Hearing Panel has taken this into account in determining appropriate sanctions to impose on Connors.¹⁰²

Connors misled Prime Capital by failing to disclose his outside business activities. As alleged in the Complaint, Connors earned approximately \$46,000 from his misconduct. But evidence presented at the hearing showed that Connors made considerably more money. His tax records show that in 2011 Connors made \$34,380 from undisclosed insurance commissions. Additionally, Connors does not dispute that he earned \$89,018 in insurance commissions in 2010, which predates the relevant period in this case. The Hearing Panel finds aggravating that Connors tampered with the tax system software to hide from his employer that he had privately invoiced customers for tax preparation services. He also ignored his Firm's clear instructions to cease charging customers \$399 for opening advisory accounts. The Hearing Panel also finds aggravating that Connors accepted checks directly from customers. Each of these acts was designed to conceal his outside business activities from his Firm.

Connors also misled the customers whom he charged for services into assuming that his employer had approved them. Connors' letter to new advisory customers asking \$399 for the one-time set up fee was written on Gilman letterhead, which also identified Prime Capital as a FINRA member firm through which securities were offered.¹⁰³ Connors also generated his tax invoices on a Gilman form.¹⁰⁴

The Panel finds that Connors acted intentionally and that he was solely motivated by the prospect of monetary gain. Prime Capital's President testified that when she informed Connors that he was being terminated, Connors protested that he was entitled to the money he earned from his undisclosed activities because the value of the Gilman stock he was paid in 2000 in exchange for his financial services business had declined.¹⁰⁵

Finally, Connors did not accept responsibility for his misconduct. At the hearing, he admitted that he engaged in the activities alleged and received money directly from customers, but said he was entitled to the money. He denied that his misconduct constituted a violation of

¹⁰² Evidence of misconduct that is not alleged in a complaint, but is similar to the misconduct charged in a complaint, is admissible to determine sanctions. *See Sears*, 2008 SEC LEXIS 1521, at *22 n.33 (in an unauthorized trading case, finding that evidence of unauthorized trading, which was not alleged in the complaint, was admissible in gauging aggravating factors to assess appropriate sanctions); *Gateway Int'l Holdings, Inc.*, Exchange Act Release No. 53907, 2006 SEC LEXIS 1288, at *24 n.30 (May 31, 2006) ("Although we are not finding violations based on [failures to file timely reports], we may consider them, and other matters that fall outside the [Order Instituting Proceedings], in assessing appropriate sanctions.").

¹⁰³ CX-8, at 1.

¹⁰⁴ CX-3, at 3-7, 11.

¹⁰⁵ Tr. 387-88.

FINRA Rule 3270.¹⁰⁶ Connors claimed his misconduct at most constituted a breach of his contract with Prime Capital and Gilman.

When fashioning appropriate sanctions, the Guidelines instruct adjudicators to also consider whether the employer disciplined the respondent before regulatory detection.¹⁰⁷ Prime Capital terminated Connors before FINRA learned of his misconduct. The Hearing Panel finds that Connors' termination by Prime Capital is a mitigating factor in determining sanctions.¹⁰⁸ The Panel also considers that the termination had no long-term effect. Connors registered with another firm in September 2012, within two months of his termination by Prime Capital, and is currently registered. His termination does not overcome the Panel's concern that Connors' egregious misconduct warrants severe sanctions.

After weighing each of the principal considerations in determining sanctions, the Panel finds that Connors' outside business activities involved egregious misconduct. Aside from the fact that he was terminated by Prime Capital, the Panel finds no mitigating circumstances warranting reduced sanctions. Accordingly, the Panel suspends Connors in all capacities from associating with a FINRA member firm for 14 months. The Panel also determines that a fine that falls in the middle of the recommended range of \$2,500 to \$73,000 is appropriate and therefore imposes a fine of \$40,000.¹⁰⁹

V. Order

Respondent Thomas Edmund Connors is suspended from associating with any member firm in any capacity for 14 months for engaging in undisclosed outside business activities, in violation of FINRA Rules 3270 and 2010. He is also fined \$40,000. Connors is ordered to pay the costs of the hearing in the amount of \$6,093.04, which includes a \$750 administrative fee.

¹⁰⁶ Tr. 600 ("I violated my employment agreement with Gilman."). When asked if his admission that he breached his employment agreement with Gilman was an acknowledgment that he also violated Rule 3270, Connors said, "No." Tr. 602.

¹⁰⁷ Guidelines at 7 (Principal Consideration in Determining Sanctions No. 14).

¹⁰⁸ *John M.E. Saad*, Exchange Act Release No. 76118, 2015 SEC LEXIS 4176, at *18-19 (Oct. 8, 2015), *appeal docketed*, No. 15-1430 (D.C. Cir. Nov. 20, 2015) (finding that termination of employment can be a mitigating factor) (citing *Denise M. Olson*, Exchange Act Release No. 75837, 2015 SEC LEXIS 3629, at *18 (Sept. 3, 2015)) (same).

¹⁰⁹ We considered and rejected without discussion all other arguments by the parties.

If this decision becomes FINRA's final disciplinary action, the suspension shall become effective with the opening of business on Monday, March 7, 2016. The fine and assessed costs shall be due on a date set by FINRA, but not less than 30 days after this decision becomes FINRA's final disciplinary action in this proceeding.

Michael J. Dixon
Hearing Officer
For the Hearing Panel