

NASD OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

DAVID T. KAAGAN
(CRD #2727926),

Beverly Hills, CA,

Respondent.

Disciplinary Proceeding
No. C02030026

Hearing Officer—Andrew H. Perkins

HEARING PANEL DECISION

December 4, 2003

Respondent is barred from the securities industry for refusing to appear for an on-the-record interview, in violation of NASD Procedural Rule 8210 and Conduct Rule 2110.

Appearances

For the Department of Enforcement: Cynthia A. Kittle, Regional Attorney, NASD, Los Angeles, CA, (Rory C. Flynn, Chief Litigation Counsel, of Counsel).

For the Respondent: Michael J. Abbott, JONES, BELL, ABBOTT, FLEMING & FITZGERALD, LLP, Los Angeles, CA.

DECISION

I. INTRODUCTION

The Department of Enforcement (the “Department”) charged David T. Kaagan (“Kaagan” or the “Respondent”), a formerly registered representative, with providing false information to NASD staff and failing to appear for an on-the-record interview in connection with NASD’s

investigation of customer SB's complaint, in violation of NASD Procedural Rule 8210 and NASD Conduct Rule 2110. The Amended Complaint alleges that NASD staff served the Respondent with two written requests that he appear for an on-the-record interview (the "Information Requests") and that in each instance he informed NASD staff that he would not appear until an arbitration brought by SB concluded. In his Amended Answer, the Respondent reiterated his offer to cooperate fully once the arbitration ended.¹ In addition, the Respondent requested a hearing.

The hearing was held in Los Angeles, California, on September 30, 2003, before a Hearing Panel composed of the Hearing Officer and two current members of the NASD District 2 Committee.² At the hearing, the Parties submitted Joint Stipulations of Fact ("Stip."), which cover most of the underlying material facts. In addition, the Department presented the testimony of the Respondent and Gene Horwitz, the investigator assigned to investigate the underlying customer complaint. Kaagan also testified on his own behalf and confirmed that he would not submit to questioning about customer SB's complaint until their arbitration ended.

Upon consideration of the entire record, and for the reasons set forth below, the Hearing Panel finds that the Respondent willfully violated NASD Procedural Rule 8210 and NASD Conduct Rule 2110. Accordingly, the Hearing Panel concludes that the Respondent should be barred from the securities industry.

¹ Amended Ans. ¶ A.

² References to the hearing transcript are cited as "Tr. ___." The Department's exhibits are cited as "CX-," and the Respondent's exhibits are cited as "R-." In addition, the Parties submitted six joint exhibits, which are cited as "JX-."

II. FINDINGS OF FACT

There are no material facts in dispute.

A. The Respondent

Kaagan entered the securities industry in February 1996 in an unregistered capacity with Merrill Lynch, Pierce, Fenner & Smith. In May 1996, he left Merrill Lynch and associated with Dean Witter Reynolds Inc, and on September 10, 1996, he became registered as a General Securities Representative. Kaagan left Dean Witter on October 15, 1999, and joined UBS PaineWebber Inc. (“PaineWebber”). Kaagan was associated with PaineWebber until February 9, 2001, at which time he left to join CIBC World Markets Corp. (“CIBC”), where he was registered as a General Securities Representative until August 16, 2001. Kaagan has not been registered with the NASD or associated with an NASD member firm since he left CIBC.³

B. Kaagan’s Failure to Appear for an On-The-Record Interview

On February 15, 2002, PaineWebber filed an amended Uniform Termination Notice for Securities Industry Registration–Form U-5 (“Amended Form U–5”) with NASD on Kaagan’s behalf. The Amended Form U–5 disclosed that customer SB had filed a Statement of Claim with NASD Dispute Resolution, Arbitration Claim No. 02-01874, concerning her PaineWebber securities account.⁴ In brief, SB claimed that Kaagan and others at PaineWebber had engaged in the following misconduct: (1) excessive trading; (2) in-and-out trading; (3) unauthorized trading;

³ Stip. ¶ 2; Ex. CX–1.

⁴ Stip. ¶ 5; Ex. CX–3.

(4) improper use of margin; and (5) fraud.⁵ In addition, SB claimed that Kaagan, on behalf of PaineWebber, had offered to “make her whole” by bringing her accounts to \$2.5 million in return for her agreement to refrain from any legal action for losses she had suffered in her account due to the trading activities of another PaineWebber registered representative.⁶ SB claimed that Kaagan’s representations were false and that neither he nor PaineWebber ever intended to honor the agreement.

Upon receipt of the Amended Form U-5, NASD staff opened an investigation into SB’s claims. In the course of the investigation, on February 6, 2003, NASD staff interviewed Kaagan about SB’s allegations,⁷ and Kaagan denied them. In particular, Kaagan told the investigator that neither he nor anyone else at PaineWebber had made any statement to SB regarding any agreement to guarantee investment performance or to “make her whole.”⁸ The staff’s memorandum of the February 6 interview (the “Memorandum”) states:

Kaagan has heard that [SB] claims to have tapes of conversations between herself and Kaagan in which she claims that Kaagan made guarantees or assurances to make her whole. Kaagan never made any statement to [SB] suggesting that he agreed in any way to make her whole to any amount. Moreover, Kaagan did not ever understand that [SB] was taping any conversation. Kaagan did not waive or give [SB] permission to tape any conversation.

At no time did Kaagan ever reach any agreement or guarantee to make [SB] whole for any claimed losses, nor did Kaagan ever tell [his] or any other PaineWebber

⁵ See JX-1 (copy of arbitration Statement of Claim); Stip. ¶ 9.

⁶ *Id.*

⁷ Stip. ¶ 15.

⁸ *Id.* ¶ 15.

supervisor that he had reached, or was negotiating, such an agreement. [RG] never would have allowed any such agreement.⁹

On February 10, 2003, NASD staff sent Kaagan and his attorney the Memorandum of the February 6 interview with a request that Kaagan sign the Memorandum after making any edits and corrections to assure that the memorandum is complete and accurate.¹⁰ NASD issued this request under NASD Procedural Rule 8210. NASD staff further instructed Kaagan that should he “wish to make any clarifying statements or correct a statement that [he] made on February 6th [he] should do so by supplemental memorandum.”¹¹

Kaagan did not sign the Memorandum. Instead, on February 21, 2003, Kaagan’s attorney sent NASD staff a letter containing a number of edits and corrections.¹² In addition, he asked NASD staff to add the following language to the Memorandum in two places:¹³

However, on several occasions [SB] talked to me about a deal or guarantee which she wanted from PaineWebber. I feel that [SB] misled me into the topic of a deal or guarantee in an attempt to entrap me or make incriminating statements about [RG’s] knowledge of a deal or guarantee. I should have been more clear that no such deal ever existed.¹⁴

Kaagan’s attorney represented that Kaagan would sign the Memorandum once NASD staff made the requested revisions.

⁹ *Id.* ¶ 16.

¹⁰ Ex. CX-12.

¹¹ Ex. CX-12, at 1.

¹² Ex. CX-13.

¹³ Kaagan’s attorney requested that the language be appended to paragraphs 25 and 47 of the Memorandum.

¹⁴ *Id.*

Horwitz testified that he could not understand the suggested new language because it appeared to be inconsistent with Kaagan's February 6 statements that "there was absolutely no discussions or anything suggesting that [he made a deal with SB]."¹⁵ To clarify Kaagan's requested amendments, Horwitz sent Kaagan's attorney two emails dated February 24¹⁶ and February 27¹⁷ explaining his confusion over the requested amendments and requesting Kaagan's attorney to telephone him.¹⁸ Horwitz, however, was unable to obtain the clarification he desired. Accordingly, Horwitz sent Kaagan two written requests that he appear for an on-the-record interview. In each instance, Kaagan refused to appear.

Horwitz sent the first request to Kaagan on March 18, 2003, which requested Kaagan appear and testify on March 24.¹⁹ In response, Kaagan's attorney sent a letter dated March 21 reiterating his request that NASD postpone Kaagan's on-the-record interview until after the conclusion of the SB arbitration.²⁰ Kaagan's attorney explained that he desired the postponement because the arbitration panel had recently ordered that SB could not introduce into evidence the "illegally taped conversations between [SB] and Mr. Kaagan," and his client was concerned about the "implications" of the interview on the arbitration panel's order.²¹ Kaagan presented evidence that the arbitration panel had excluded the tapes because they had been made without Kaagan's

¹⁵ Tr. 33.

¹⁶ Ex. CX-14.

¹⁷ Ex. CX-15.

¹⁸ Tr. 35; Stip. ¶ 19.

¹⁹ Ex. JX-3.

²⁰ Ex. JX-4.

²¹ Ex. JX-4.

knowledge and consent, in violation of California Penal Code § 632.²² NASD staff denied Kaagan's request for a postponement; Kaagan nevertheless failed to appear on March 24.²³

On March 24, Horwitz sent Kaagan the second request that he appear for an on-the-record interview pursuant to NASD Procedural Rule 8210.²⁴ This request scheduled Kaagan's interview for March 28, 2003, and specifically advised that his failure to appear may subject him to disciplinary action. The following day, Kaagan's attorney renewed his request for a postponement of the on-the-record interview.²⁵ Kaagan failed to appear on March 28, as scheduled.²⁶

III. CONCLUSIONS OF LAW

A. Jurisdiction

Jurisdiction of this proceeding is founded on Article V, Section 4(a) of the NASD's By-Laws, which provides that a person whose association with a member has been terminated and who is no longer associated with any NASD member continues to be subject to the filing of a complaint based upon a failure to provide information requested by NASD for two years after the effective date of the termination. Here, the Department filed the Amended Complaint within two years of the date Kaagan was last registered with NASD, and the Complaint alleges that Kaagan

²² Ex. R-7.

²³ Stip. ¶¶ 28-29.

²⁴ Ex. JX-5.

²⁵ Ex. CX-16.

²⁶ Stip. ¶ 38.

failed to respond to the Information Requests that NASD staff issued during the period of retained jurisdiction under Article V, Section 4 of the NASD By-Laws.

B. Kaagan Violated NASD Procedural Rule 8210 and NASD Conduct Rule 2110

As a general matter, an NASD member firm or associated person who is requested to provide testimony, documents, or other information pursuant to NASD Procedural Rule 8210 has an unqualified obligation to respond fully and promptly to the request. Rule 8210 provides that NASD staff “shall have the right to ... require a ... person subject to [NASD’s] jurisdiction to provide information orally ... with respect to any matter involved in [an] investigation....” The Rule further provides, “No member or person shall fail to provide information or testimony ... pursuant to this Rule.”

Here, there is no dispute that Kaagan placed his economic interests ahead of his professional responsibilities. Kaagan’s concern that NASD’s investigation might adversely affect the SB arbitration does not excuse or mitigate his refusal to appear and testify in connection with NASD’s investigation of SB’s complaint. Moreover, Kaagan had no right to require NASD to delay its investigation.²⁷ In short, Kaagan’s refusal to comply with the Information Requests except on his own schedule is a willful violation of NASD Procedural Rule 8210 and NASD Conduct Rule 2110.

²⁷ *Department of Enforcement v. Valentino*, No. FPI010004, 2003 NASD Discip. LEXIS 15, at *12 (N.A.C. May 21, 2003) (holding that it is well settled that respondents cannot impose conditions on their responses to NASD’s inquiries).

IV. SANCTIONS

Where there is a lack of mitigation, the NASD Sanction Guidelines provide, “[i]f the individual did not respond in any manner, a bar should be standard.”²⁸ Kaagan argues that there are mitigating factors in this case analogous to those the National Adjudicatory Council (“NAC”) found in *Department of Enforcement v. Levitov*, No. CAF980025, 1999 NASD Discip. LEXIS 30 (N.A.C. Nov. 1, 1999). Specifically, Kaagan argues that: (1) a short delay would not have diminished the value of his later testimony; (2) he had cooperated fully up to the point that the arbitration panel issued its order excluding his taped conversations from evidence in the SB arbitration; and (3) he was concerned about the impact his testimony would have on the SB arbitration.²⁹ The Hearing Panel, however, neither finds the *Levitov* decision analogous to the present case nor finds any of the foregoing factors mitigating.

Levitov involved unique circumstances, and the NAC cautioned that its conclusions should not be applied generally to cases involving a respondent’s violation of Procedural Rule 8210.³⁰ In *Levitov*, the NAC found that the staff had “acted rigidly when it denied the respondents’ requests for continuances” following closely their arrest on parallel criminal charges.³¹ Central to this conclusion were the factors that NASD’s investigation had been ongoing for two years at the time the staff requested further information from the respondents and the staff’s admission that a short

²⁸ NASD Sanction Guidelines at 39 (2001 ed.).

²⁹ Respondent’s Pre-Hearing Submission at 5.

³⁰ *Levitov*, 1999 NASD Discip. LEXIS at *21.

³¹ *Id.* at *22.

delay would not have diminished the value of the respondents' testimony.³² In the context of the respondents' previous cooperation, the NAC concluded that a short postponement "might have been appropriate."³³ But the NAC found none of the individual factors cited by the respondents in *Levitov* as mitigating. Moreover, the NAC emphasized:

By concluding that [NASD] staff's refusal to grant respondents' continuance requests should, in this case, be considered as a mitigating factor in our determination of sanctions, we do not intend to depart from the long line of NAC and SEC cases that state that respondents may not second-guess the NASD's need for information and may not impose conditions on their responses. Similarly, we are not departing from our previous holdings that NASD Regulation has no obligation to postpone investigations because of actions taken by other regulators or criminal authorities. To do so would, in our view, severely undercut the usefulness of Procedural Rule 8210.... A registered person's failure to respond to a request for information pursuant to Procedural Rule 8210 compromises the NASD's ability fully to investigate potential wrongdoing....³⁴

None of the unique factors underlying the NAC's decision in *Levitov* is present in this case, and, more importantly, this case does not involve the unique blend of factors present in *Levitov* that led the NAC to conclude that the staff's refusal to grant a limited continuance was a mitigating factor. Here, Kaagan refused to testify because he speculated that any information he might give NASD would be used in some unexplained manner by SB to prosecute her claims against him or would otherwise impair the value of the arbitrator's ruling excluding from evidence the taped conversations between himself and SB.³⁵ However, a respondent may not refuse to

³² *Id.* at *23–24.

³³ *Id.* at 23, n.19.

³⁴ *Id.* at 23–24.

³⁵ Moreover, there is no evidence that NASD staff intended to inquire about the taped conversations. Indeed, Horwitz testified that he had refused to listen to the taped conversations when SB's attorney offered them to him. (Tr. 44–45.)

respond or condition his response because he fears adverse collateral consequences. Otherwise, respondents would be able to delay NASD investigations of customer complaints by citing their concerns regarding their potential civil liability. Accordingly, the Hearing Panel finds no mitigating circumstances that would warrant a sanction less than a bar for Kaagan's violation.

V. ORDER

Therefore, having considered all the evidence,³⁶ the Hearing Panel orders that Respondent David T. Kaagan be barred from association with any member firm in any capacity for refusing to appear for his on-the-record interview, in violation of NASD Procedural Rule 8210 and Conduct Rule 2110. The bar shall become effective immediately if this Decision becomes the final NASD disciplinary action in this matter.

Kaagan also is ordered to pay costs in the total amount of \$1,605.18, which include an administrative fee of \$750 and hearing transcript costs of \$855.18.

Andrew H. Perkins
Hearing Officer
For the Hearing Panel

Copies to:

David T. Kaagan (by overnight courier and first-class mail)
Michael J. Abbott, Esq. (by facsimile and first-class mail)
Cynthia A. Kittle, Esq. (by first-class and electronic mail)
Rory C. Flynn, Esq. (by first-class and electronic mail)

³⁶ The Hearing Panel has considered all of the arguments of the Parties. They are rejected or sustained to the extent they are inconsistent or in accord with the views expressed herein.