**NASD REGULATION, INC.**
**OFFICE OF HEARING OFFICERS**

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| DEPARTMENT OF ENFORCEMENT,<br><br>Complainant,<br><br>v.<br><br>WENDELL D. BELDEN<br>(CRD #1324913),<br>Tulsa, OK<br><br>Respondent. | Disciplinary Proceeding<br>No. C05010012<br><br>Hearing Officer - AWH<br><br>**Hearing Panel Decision**<br><br>November 12, 2001 |

**Respondent, a registered representative and principal, made unsuitable recommendations to a customer in violation of Conduct Rules 2110 and 2310. Respondent fined $40,000, suspended in all capacities for 90 days, ordered to pay restitution of $55,567.03 plus interest, ordered to requalify by examination, and assessed costs.**

Appearances:

Mark P. Dauer, Esq., and Karen E. Whitaker, Esq., for the Department of Enforcement

Mark E. Hardin, Esq., for Wendell D. Belden

# DECISION

## Introduction

On February 20, 2001, the Department of Enforcement ("Enforcement") filed the Complaint in this matter alleging that Wendell D. Belden ("Belden" or "Respondent") made unsuitable recommendations to customer JRB, resulting in that customer's purchase of more than $2.1 million in Class B mutual fund shares. On March 13, 2001, Respondent filed his Answer to the Complaint, admitting that he recommended the purchases, but denying that they were unsuitable. A hearing was

held in Tulsa, Oklahoma, on July 10 and 11, 2001, before a hearing panel composed of the Hearing Officer and two current member of District Committee No. 5. Both parties timely filed post-hearing briefs on August 29, 2001. The crux of the case is whether Respondent should have recommended the purchase of Class A mutual fund shares rather than the purchase of Class B mutual fund shares.

## Findings of Fact

The Purchase of Class B shares

Wendell D. Belden is the sole owner of, and a registered representative and principal associated with, member firm Southmark, Incorporated.[1] Stip. No.1; Tr. 185-86, 223; CX-18. JRB, who was a neighbor of Belden and a retired commercial airline pilot, approached Belden in mid-1997 about investing his retirement savings of about $2.1 million. Stip. No. 3. At the time of the hearing, JRB was deceased. Stip. No. 3. JRB was interested in long-term growth. RX-1. Prior to JRB's investment, Belden met with him regularly and discussed the advantages and disadvantages of diversifying among five different mutual funds as opposed to purchasing just one fund. Tr. 195-97, 227, 253. Belden presented JRB with a plan for him to invest his savings in five different mutual funds within two fund families. Tr. 253; CX-9. As a result of these discussions, Belden made the following sales to JRB in July 1997:

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| MFS Emerging Growth Fund B | $495,000.00 |
| MFS Research Fund B | 310,000.00 |
| MFS Mass. Investors Growth Stock Fund B | 495,000.00 |
| Van Kampen Amer. Capital Enterprise Fund B | 495,189.45 |
| Van Kampen Amer. Capital Pace Fund B | 310,000.00 |
| Total | $2,105,189.45 |

[1] References to the parties' Stipulations are designated as Stip._; Enforcement's exhibits, as CX_; Respondent's exhibits, as RX_; and the Transcript of the hearing, as Tr._.

Stip. Nos. 4, 5; CX 11, 12.

Southmark received a four percent commission on mutual fund purchases. Southmark received commissions totaling $52,000.00 from JRB's purchase of MFS Class B shares, and $32,207.85 on the purchase of Van Kampen Fund Class B shares. Stip. Nos. 6, 7. MFS Class B shares are subject to a Contingent Deferred Sales Charge ("CDSC") of four percent in the first and second years after purchase, three percent in the third and fourth years, two percent in the fifth year, one percent in the sixth year, and none thereafter. Stip. No. 8. Van Kampen Class B shares are subject to a CDSC of five percent in the first year after purchase, four percent in the second year, three percent in the third year, two and one-half percent in the fourth year, one and one-half percent in the fifth year, and none thereafter. Stip. No. 9.

The purchases were made through D. J. Kadagian, an investment advisor who owned Four Seasons Asset Management, an investment management firm in Westport, Connecticut. Kadagian, through Four Seasons, operated a timing service used by many Southmark customers under which money was switched between equity mutual funds and a money market mutual fund at the direction of Kadagian. Tr. 17-19. Under the original agreement with Southmark, Four Seasons gave Southmark access only to the Van Kampen Enterprise Fund and a Van Kampen money market fund. The handling of JRB's investment was an exception for both Kadagian and Belden.[2] Tr. 26, 228. Kadagian did not deal directly with JRB for the investment, and he received no commissions on the sales of the funds. Tr. 24, 30. Four Seasons received a fee of two percent per year for its management of the account by use of its timing service (its half of the

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[2] Belden testified as follows: "It's like he had at least five accounts and his interest in those five accounts, you know, I mean, we never had anything like that before." Tr. 228.

four percent yearly fee charged to the customer by Southmark in addition to the sales commission). Tr. 25.

JRB was also interested in selling to other airline pilots the managed account program that Southmark had with Four Seasons. To that end, JRB negotiated an employment agreement with Southmark, began studying for the NASD Series 6 examination, and eventually filed a U-4 with the NASD to become a Series 6 registered representative. CX-8; Tr. 196. As an employee of Southmark, JRB also hoped to receive $42,000.00 in commissions on his own account. RX-11.

Scott Pilgrim was the employee at Southmark who handled the mechanics of the transactions, including the placing of the trades with Kadagian. In June 1996, Pilgrim, who was a C.P.A., began work with Southmark as an accountant, handling personal and corporate accounting and tax matters. Tr. 79. In April 1997, Pilgrim became the president of Southmark. Tr. 81. While Pilgrim was with Southmark, he held Series 6, 26, and 63 NASD registrations. Tr. 78. He was paid a salary at Southmark; he did not sell securities to customers, nor did he receive any commissions. Tr. 82.

Pilgrim did not deal directly with JRB on the investment of his retirement account because, according to Belden, Pilgrim did not have enough experience to assist customers with their investments:

> Mr. Pilgrim was correct earlier…in saying that he did more of the technical work and less of the basic understanding. Because of his experience and the time at work, he couldn't help. It was like the blind leading the blind if Scott had helped [JRB] with that sort of thing. So when it came to understanding things, I helped [JRB] and, oftentimes, Mr. Pilgrim, at the same time.

Tr. 196.

The Concern Over the Purchase of Class B Shares

In discussing the JRB transaction with Pilgrim, Kadagian told him that an investment as large as JRB's should be placed in Class A shares rather than in Class B shares as Belden proposed. Tr. 24-25. At the inception of the business relationship between Southmark and Four Seasons, Kadagian had advised Belden to use Class A shares for all of Belden's accounts. Kadagian's normal practice was to use Class A shares because, while they generally had initial sales charges, they had lower internal expenses and did not charge a CDSC when the shares were sold. Kadagian was particularly concerned about the CDSC because, as a market timer who continually switched his clients in and out of funds, he knew that there was always a possibility that clients would be forced out of a specific mutual fund, or family of funds, should those funds decide to end their relationships with market timers. Any client forced out of a Class B mutual fund would have to pay the CDSC, which varied with the number of years the client had been in the fund. In fact, in June or July 2000, Kadagian received notice from Van Kampen that it was terminating its market timing relationship with Four Seasons. Accordingly, Belden's clients were forced out of Van Kampen funds for that reason. Tr. 19-23, 33. Kadagian also favored Class A shares because he does such a large volume of business with certain mutual funds that, with rights-of-accumulation privileges, he can offer Class A shares to all his clients without a front-end load, regardless of the amount of the initial investment. Tr. 20. Finally, Kadagian did not like to use Class B shares because he commingled accounts to move them simultaneously between the mutual funds and money market funds. If one client elected to leave a Class B mutual fund, that client would incur a CDSC, but the fund would only see an omnibus account. It would then be difficult for Kadagian properly to identify the account and impose the applicable charge. Tr. 27.

Notwithstanding Kadagian's concerns about Class B shares, Belden's policy was to place his clients in those Class B shares, rather than in Class A shares. RX-21, at 31. All of Belden's clients who invested through Kadagian and Four Seasons were placed in Class B shares. Tr. 84. Belden admitted that Class B shares generally have higher internal expenses and trade at lower net asset value than Class A shares. Answer, ¶¶10, 11. Nevertheless, Belden believed that because of the small size of his client base, he could not stay in business without getting the higher commission fees that were paid on Class B shares. CX-25; Tr. 237. As to JRB's investment, Belden intentionally placed JRB in Class B shares and the order was structured to avoid the fund distributors' $500,000 limits on the size of Class B orders. Tr. 231. Belden placed JRB in Class B shares because he needed to make high commissions on an occasional large sale of Class B shares to make up for the small commissions he earned on the many small accounts he had been handling:

> But where my average accounts are less than a hundred thousand dollars, if I don't have some nice accounts, you know – I mean, you can say that that's, you know, that's soaking the rich to pay for the poor if you want to, but that's the way it is.
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> The rest of the rationale is, if you don't have some larger accounts, then you can't be in business to service the rest of them.

Tr. 232-33.

Scott Pilgrim thought that by putting JRB into B shares instead of A shares, JRB had been "cheated," and he so informed JRB. Tr. 88. Angry and feeling that he had been misled by Belden, JRB ended his involvement with Southmark, became a direct customer of Four Seasons, and, in April 1999, exchanged his B shares for A shares. Tr. 31-32. In making the exchange to A shares, JRB incurred contingent deferred sales charges of $84,412.58. Stip. No. 10; CX-24 at 6-7.

<u>The Alternative to Class B Shares</u>

Consistent with the arrangement Southmark had with Four Seasons, JRB's entire investment could have been placed in the Van Kampen American Capital Enterprise Fund. Had his $2.1 million been so invested, his funds would have been forced into Class A shares because of the magnitude of the investment. RX-25; Tr. 37. Regardless of the size of his investment, Four Seasons had the ability to purchase Class A shares from mutual funds with no front-end load for him, or for any other Southmark client who dealt directly with Four Seasons. Tr. 55, 68, 159, 206-7. However, Belden did not want his clients to deal directly with Four Seasons. He stated: "...they wouldn't be my company's accounts or clients. They would be his [Kadagian's] company's accounts and clients, and I would be just a simple salesman for him." Tr. 206.

*Comparison of Sales Charges and Commissions*

JRB's investment, through Southmark, in Van Kampen funds totaled $805,189.45, not enough to qualify for a waiver of the entire initial sales charge on a purchase of Class A shares. However, it was large enough to exceed the most favorable breakpoint. For Van Kampen funds, the initial sales charge for an investment of less than $500,000 in Class A shares is 5.75 percent; on investments of more than $500,000, it is two percent. Van Kampen Funds Class A shares have no CDSC. Stip. No. 9. Although JRB's investment in Van Kampen Funds Class B shares resulted in commissions to Southmark of $32,207.85, the same investment in Class A shares would have resulted in commissions of $15,640.82 if Southmark had requested a cumulative purchase discount, or $18,116.76 if it had not requested the discount. Stip. No. 7.

Had JRB's funds been invested in Class A shares of the three MFS funds, they would have qualified for investment at net asset value, with no sales charge, because the total value of the investment exceeded $1 million. CX-2, at 9-10; CX-13, at 2; Tr. 258-60. MFS prospectuses provide, below a

table indicating breakpoints for the application of initial sales charges and showing that purchases in excess of $1 million carry no initial sales charge, as follows:

> The sales charge may vary depending on the number of shares of the Fund as well as certain other MFS funds owned or being purchased, the existence of an agreement to purchase additional shares during a 13 month period (or 36 month period for purchases of $1 million or more) or other special purchase programs. A description of the Right of Accumulation, Letter of Intent and Group Purchase privileges by which the sales charge may be reduced is set for in the SAI [Statement of Additional Information].[3]

CX-2, at 9-10. Jeffrey Ranahan, Vice President and Compliance Officer for MFS, testified that JRB's investments in the three MFS funds could have been aggregated to achieve the breakpoint for a $1million net asset value purchase, i.e., purchased without an initial sales charge. Tr. 259-60. Although MFS did not have machinery in place to monitor its policy of firmly encouraging the purchase of A shares by all customers who were eligible to purchase them at net asset value, its written policy provided, in relevant part, that "orders to purchase Class B shares for investors investing $1 million or more may be rejected by [MFS]" and that "any purchaser eligible to purchase shares at [net asset value] <u>should purchase</u> Class A shares"(emphasis in the original). CX-21, at 2. Although Belden concluded from his reading of the prospectuses that the A shares

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[3] Respondent argues that the MFS prospectuses allow a right of accumulation only when purchases made subsequent to an initial investment are combined with the initial investment and add up to $1 million or more ("A shareholder qualifies for cumulative quantity discounts on purchases of Class A shares when his new investment, together with the current offering price value of all holdings of Class A, B and C shares of that shareholder in the MFS funds …reaches a discount level." CX-2, at 15). The Hearing Panel does not find that argument persuasive. It is counter to the express testimony of the Vice President and Compliance Officer of MFS and the policy of MFS that a simultaneous purchase of multiple funds in the MFS family, aggregating in excess of $1 million, would qualify for purchase at net asset value. Tr. 260; CX-21, at 2. If Respondent's argument were correct, the anomalous result would be that, while simultaneous purchases would not qualify for the discounts, one could easily qualify for the discount by first investing only the most minimal amount, paying a nominal sales charge, and almost immediately thereafter, investing the bulk of the million dollar purchase at net asset value.

could not be purchased at net asset value, he never consulted with anyone at MFS to determine whether he was correctly interpreting the language of the prospectuses. Tr. 239, 243. JRB's investment in MFS Class B shares resulted in commissions to Southmark of $52,000, while the same investment in Class A shares would have resulted in commissions totaling $13,000. CX-13, at 2.

*Comparison of Internal Fund Expenses*

NASDR staff completed an analysis of the total internal fund expenses for JRB's investments in all five funds (Van Kampen and MFS), comparing the results for Class A and Class B shares over an eight year period. CX-17. The eight year period was chosen because at the end of eight years, any Class B shares JRB held would be converted to Class A shares, and then the expenses would be the same. Tr. 138-41. Had the investment been placed in Class A shares, total expenses for all five funds would have amounted to $179,315.09. Had the investments been placed in Class B shares of the five funds, total expenses over the eight years would have amounted to $294,723.58[4]. CX-17.

The NASD staff analysis of internal fund expenses over an eight-year period shows that for the Class A shares invested in the two Van Kampen funds, total expenses would have been $79,427.09; and for Class B shares, $115,499.58. *Id.* That analysis shows that for the three MFS Funds, total expenses would have been $99,888[5], had the funds been invested in Class A shares. If the funds had been invested in Class B shares, those expenses would have totaled $179,224. CX 17.

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[4] Respondent takes the position that expenses for Class A shares should be increased by $30,700, an amount he claims would have been charged as initial sales charges on the Class A shares of MFS funds. The Hearing Panel does not accept that assertion because the Panel credits the testimony of Jeffrey Ranahan of MFS that no initial sales charge would have applied to JRB's investment in Class A shares. Tr. 259-60, 263. *See also* CX-13.

[5] The Hearing Panel rejects Respondent's assertion that MFS Class A share expenses should be increased by sales charges in the amount of $30,700. *See* n. 4.

*Comparison of Performance*

Van Kampen Investments, Inc. provided an analysis of JRB's investment in the Enterprise and Pace Funds from July 10, 1997 (the date of JRB's original investment), to April 1, 1999 (the date of JRB's switch to Class A shares), comparing the performance of Class A and Class B shares. Stip. Nos. 7, 9; CX-22. The analysis assumes that the investment in Class A shares would have been net of the $16,263.78 initial sales charge, that the Four Seasons timing service was not employed, and that the Class B share value would be net of the appropriate CDSC. The analysis concluded that, at the end of the period, Class A shares would have a value of $1,075,507.33, while Class B shares would have a value of $1,050,744.49[6]. CX-22.

Enforcement did not introduce any evidence comparing the performance of Class A and Class B shares of the MFS funds. However, Respondent introduced handwritten additions to the projected internal fund expenses over eight years that Enforcement offered (CX-17) RX-35. Those handwritten additions project additional income that would have been received if the amount of the initial sales charges for Class A shares had, instead, been invested at the outset in Class B shares. Respondent contends that JRB would have had $46,804.00 (the amount Respondent contends JRB would have paid in up-front sales charges for Class A shares) to invest

in Class B shares, which would offset the projected higher expenses for those Class B shares.

[6]On brief (p.24), Respondent cites Bates Pages 4 and 6 of CX-22 and contends that the value of the Class B shares as of April 1, 1999, would be $1,082,952. However, the figures on those pages do not take into consideration any CDSC on the sale of the Class B shares. The Van Kampen analysis, which the Hearing Panel finds persuasive, is taken from Bates Pages 7 and 8 which do consider the applicable back-end load.

The Hearing Panel finds Respondent's analysis to be flawed because, as previously noted, no initial sales charges would have been applicable to the purchase of the MFS Class A shares. Tr. 258; CX-1-4, 13. Moreover, even if the Hearing Panel were to assume that a front-end load was applicable to the purchase of MFS Class A shares and that, therefore, the net amount initially invested in Class B shares would be higher than the net amount initially invested in Class A shares, Respondent's analysis is still flawed because it does not take into consideration the applicability of the CDSC to the Class B shares. As shown by Schedule A, attached to Enforcement's Post-Hearing Brief, the hypothetical Class A portfolio exceeds the value of the hypothetical Class B portfolio at the end of each of the projected eight years.

## Discussion and Conclusions

NASD Conduct Rule 2310 imposes an obligation on a broker to make a recommendation to purchase or sell a security to a customer only if the broker has "reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts, if any, disclosed by such customer as to his other security holdings and as to his financial situation and needs." The test is whether the broker "fulfilled the obligation he assumed when he undertook to counsel [the client], of making only such recommendations as would be consistent with [the client's] financial situation and needs." *Eugene J. Erdos*, 47 S.E.C. 985, 1983 SEC LEXIS 332, at *10-11 (1988), *aff'd, Erdos v. SEC*, 742 F.2d 507 (9th Cir. 1984).

It is unsuitable to recommend mutual fund purchases that have the effect of causing a customer to forego reduced sales charges to which the customer would otherwise be entitled. The SEC confirmed this principle in sustaining the NASD's imposition of sanctions against a respondent for failing

to have customers execute letters of intent or to take advantage of their right of accumulation, which resulted in the customers' not receiving sales load discounts on mutual fund purchases to which they were entitled. *Fenocchio*, Exchange Act Rel. No. 12194, 46 SEC 279, 1976 SEC LEXIS 2209, *8-9 (March 11, 1976). In commenting on facts that are similar to those in this case, the SEC stated:

> The NASD is rightly concerned when a broker-dealer and its representatives fail to secure for their customers the benefit of a reduced sales charge in the sale of mutual funds. We concur with the NASD that, where a broker-dealer or representative is aware of large amounts of money being invested in a mutual fund over a relatively short period of time, as in this case, it is incumbent upon them to obtain the lowest possible price for the customer. A failure to do so results not only in the customer being deprived of a benefit to which he or she is entitled, but also in the broker-dealer and representative receiving increased commissions at the customer's expense. As the NASD points out, such conduct is inconsistent with just and equitable principles of trade.

*Id. See also, Krull*, Exchange Act Rel. No. 40768, 1998 SEC LEXIS 2664, *21 (Dec. 10, 1998) *aff'd.*, F.3d _, 2001 U.S. App. LEXIS 7644 (9th Cir. 2001) ("Krull made no effort to obtain discounted sales charges for his customers through the use of breakpoints, letters of intent, or rights of accumulation."); *Den Herder*, Exchange Act Rel. No. 39297 1997 SEC LEXIS 2293 (Nov. 5, 1997) (sustaining NASD's findings of violations and sanctions against broker who failed to aggregate mutual fund purchases and otherwise failed to obtain for customer the benefits of breakpoint discounts).

<u>The Recommendation to Invest More Than $2.1 Million in B Shares Was Unsuitable</u>

Belden's recommendation and sale to JRB of more than $2.1 million in Class B shares, rather than Class A shares were unsuitable and violated Conduct Rules 2310 and 2110. Given the size of the investment, there was no reasonable basis for Belden to believe that recommending the purchase of Class B shares would be suitable for JRB. Putting JRB's investment into Class B shares resulted in

$55,567.03 more in commissions paid to Belden than he would have received had the investment been put into Class A shares. Over a projected eight-year period, the internal fund expenses for Class B shares would have exceeded those for Class A shares by $115,408.49. Finally, over that eight-year period, and taking into consideration the CDSC that applies to Class B shares, an investment in Class A shares would outperform Class B shares at the end of each of those eight years. From JRB's perspective, the investment in Class A shares would be the better alternative.

Belden admits in his Answer to the Complaint that it was Van Kampen's policy "not to accept any order for Class B shares in an amount of $500,000 or more because it ordinarily will be *more advantageous for an investor making such an investment to purchase Class A shares*." (Emphasis added). However, he agreed in his testimony that he intentionally wanted JRB to invest just under $500,000 in Van Kampen funds in order to obtain Class B shares. Tr. 231. His purported reason was that he "determined that because of the up-front cost of A shares that [JRB] would be better off in B shares." Respondent's Brief, at 17. There is no evidence to justify that rationale. To the contrary, as Schedule A to Enforcement's Brief demonstrates, Class A shares outperform Class B shares in each of the projected eight years when the CDSC is appropriately taken into consideration. Belden's testimony at the hearing does nothing to buttress his purported rational for placing JRB's investment in Class B shares:

> Q. Well, tell me in what situation do you think A shares to be appropriate for an investor?
> A. Some very large amount of investing that they might do. It would matter on the business it was providing. I don't have experience with that, Mr. Dauer. I've never addressed -- I have never had occasion to concern myself with that kind of situation.
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> Q. You were saying, though, for large investments, it would be appropriate?
> A. I would think it would.
> Q. And what would be the dollar breakoff?
> A. That's what I'm saying I don't know. I don't know.

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> Q. So it all, then, turns on the investment of what would be the sales charge –
> A. Yes.
> Q --on the A shares?
> A. Yes.
> Q. Okay. Now, so then, if Class A shares then are available at net asset value with no front-end load, based on the amount of the person's investment, then that would be the appropriate choice for the customer, would it not?
> A. It could be.
> Q. It could be? Well, in what situation would it not be?
> A. Well, it wouldn't be in my business if that was a normal, ongoing account.
> Q. I'm not sure I follow that. Could you explain that?
> A. Well, I couldn't stay in business.
> Q. Okay. Because of the lower commission on it?
> A. Well, sure. I mean, I have to make – I have to pay all the expenses of Southmark, every month. And I don't – like I say, I don't have a client base big enough to survive on the fees alone.

Tr. 235-237. Earlier, Belden had testified that he thought he was entitled to make a large commission on JRB's transactions because of the work and time he had spent on the account. Tr. 227-28. The Hearing Panel concludes that Belden's real rationale for recommending the purchase of Class B shares was to maximize the commissions he would earn on the transactions, and not to maximize JRB's return on investment.

On brief, Belden asserts (1) that JRB was a sophisticated investor with 30 years of investing experience; (2) that Belden originally recommended that JRB invest his entire funds in the Van Kampen Enterprise Account, which would have been in Class A shares; (3) that although JRB wanted to diversify his investment among several funds, Belden tried to dissuade him from diversifying; and (4) that Kadagian developed the diversification plan for JRB, "including the allocation between the funds, so that it would be tailor made to allow [JRB] to purchase Class B shares." The Hearing Panel finds none of those assertions to be persuasive.

First, although JRB indicated on a client information form (RX-1) that he had 30 years of investment experience, that form did not indicate anything about the breadth of that experience. Belden's own testimony described the client relationship between JRB and Scott Pilgrim as "the blind leading the blind." Second, the claim that he originally recommended Class A shares of a single fund is inconsistent with Belden's assertion that Class B shares would outperform Class A shares, and with his business philosophy of "soaking the rich to pay for the poor" by maximizing commissions on large accounts. His assertion that he tried to dissuade JRB from diversifying is inconsistent with his written statement to NASDR staff that, after he explained to JRB the pros and cons of diversifying into several funds, he "left the choice entirely up to him." CX-9, at 2. Moreover, once the "choice" was made to diversify, all funds that were presented to JRB were Class B share funds. Belden wrote to the staff: "We never use front load [A share] funds. So regardless of [JRB's] choice he would have gotten the exact same amount invested for him." *Id*. Finally, although the Hearing Panel does not find relevant the question of who developed the diversification plan -- Belden admits he recommended the mutual fund purchases that were made in the execution of that plan -- the assertion that someone else developed the plan, including the specific allocation of funds to be invested in each fund, is inconsistent with Belden's testimony admitting that he intentionally placed JRB in Class B shares and structured the order to avoid the limits on the size of Class B share orders. Tr. 231.

Belden could have obtained MFS Class A shares for JRB with no sales charge and Van Kampen Class A shares at the most favorable breakpoint. "The sale of investment company shares in dollar amounts just below the point at which the sales charge is reduced on quantity transactions so as to share in the higher sales charges applicable on sales below the breakpoint is contrary to just and equitable principles of trade." IM-2830-1. By analogy, a sale made just below the investment limit for

Class B shares, made for the purpose of allowing the broker to earn commissions higher than those paid on Class A shares above that limit, is likewise contrary to just and equitable principles of trade. The sales of Class B shares to JRB worked to his financial detriment, and it was unsuitable for Belden to recommend them. Accordingly, the Hearing Panel finds that Belden violated NASD Conduct Rules 2110 and 2310.

**Sanctions**

The NASD Sanction Guidelines for unsuitable recommendations call for a fine of $2,500 to $75,000 and a suspension for a period of 10 business days to one year. In egregious cases, the guidelines urge consideration of a suspension of up to two years or a bar. NASD Sanction Guidelines 99 (2001 ed.). Enforcement, citing certain aggravating factors discussed below, suggests that this is an egregious case, but, because it involves only one customer, that it may not be deserving of the most severe sanctions. Accordingly, Enforcement seeks a suspension in all capacities for one year, a fine of $30,000, and restitution to the estate of JRB in the amount of $84,412.58, the amount of the CDSC JRB incurred when he exchanged his Class B shares for Class A shares. The Hearing Panel finds that there are aggravating factors in this case, but also that there are other circumstances, unique to the case, which require a balancing of the relevant considerations to craft sanctions that are appropriately remedial and not punitive.

On December 8, 2000, three weeks after Belden received a "Wells" letter from the NASD, which detailed the alleged violations at issue in this proceeding, Belden filed a lawsuit in an Oklahoma state court against JRB and Pilgrim. Enforcement argues that by instituting a suit against JRB, Belden attempted to intimidate him or retaliate against him for filing a complaint with NASD. The relationships between Belden, on the one hand, and JRB, Scott Pilgrim, and D. J. Kadagian, on the other, were

highly complex. JRB's death and consequent unavailability to testify at the hearing significantly made it difficult to understand fully and assess those complexities. What is clear is that JRB expected to earn commissions on his own account at Southmark, that JRB and Pilgrim were interested in forming a joint venture with similarities to Southmark, including a business relationship with Kadagian, and that Belden, through Southmark of Tulsa, Inc., filed suit on December 8, 2000, against JRB and Pilgrim, alleging breach of contract, breach of fiduciary duty, breach of duty to act in good faith, deceit, fraud, tortuous interference with contract, and violations of the Oklahoma Deceptive Trade Practices Act. CX-19. The lawsuit was pending at the time of the instant hearing, and was cited by Pilgrim in refusing to answer certain questions during his testimony. Accordingly, the Hearing Panel cannot make findings concerning the matters asserted in that suit, or the motivation(s) behind its institution. There is insufficient evidence in this case to find, as Enforcement would urge, that the lawsuit was an attempt by Belden to intimidate or retaliate against his customer for filing a complaint against him with the NASD. Moreover, because of that lawsuit, the Hearing Panel has not made findings of fact in this case that rely exclusively on the credibility of Scott Pilgrim. In addition, the Hearing Panel can make no findings that concern any monetary amounts alleged in the lawsuit to be owed to Belden by JRB as a result of their prior employment or customer relationship.

The Hearing Panel agrees with the contention of Enforcement that Belden made the unsuitable recommendations for the purpose of more than doubling his commissions. This variation on a Robin Hood theme was not, as Belden put it, to "soak the rich to pay for the poor"; it was to soak the rich to pay for Belden's expenses. The Hearing Panel can never know what JRB had in mind when he came to expect a sizable commission on his own account from the transactions at issue. Consequently, the Hearing Panel cannot know whether JRB acquiesced to the purchase of Class B shares in some hope of

offsetting any inferior performance by the gain from the commissions he thought he would earn. In any event, this was Belden's first experience with an account of such proportions, and, as Enforcement notes, this is not a case where a single event is so egregious as to warrant a bar.

The Sanction Guidelines direct the adjudicator to consider a respondent's relevant disciplinary history in determining sanctions. "Relevant disciplinary history may include (a) past misconduct similar to that at issue; or (b) past misconduct that, while unrelated to the misconduct as issue, evidences prior disregard for regulatory requirements, investor protection, or commercial integrity." NASD Sanction Guidelines 3. Enforcement cites a 1993 settlement in *DBCC v. Wendell D. Belden*, No. C05920110, which involved a complaint alleging Belden's dissemination of misleading sales literature relating to mutual funds. Belden contends that the Committee determined only that he distributed "unapproved" sales literature. The Hearing Panel does not find it necessary to interpret the decision accepting the offer of settlement and to resolve the question whether the literature was "misleading" or "unapproved." The relevant fact is that the Committee censured Belden and fined him $25,000, stating as follows:

> Although there is no indication that Belden was attempting to defraud his customers or his employers, his actions were reckless and are deserving of severe monetary sanctions. The Committee finds, in deciding not to impose a suspension, that no customer funds were lost and that Respondent Belden has no prior disciplinary history.

CX-16, at 4.

The violations in this case concern only one customer; however, they are intentional and were motivated by Belden's efforts to maximize his own financial benefit. Given the nature of the violation and his past disciplinary history, the Hearing Panel concludes that, to effect appropriate remediation and deterrence, a substantial fine is warranted. Accordingly, the Hearing Panel fines Belden $40,000. However, because Southmark has only two registered representatives and one other employee who has

passed a Series 6 examination (Tr. 223-24), the Hearing Panel has concerns with the effect on the firm, and more importantly its customers, of a lengthy suspension. Accordingly, the Hearing Panel will suspend Belden in all capacities for 90 days and require him to requalify by examination before functioning in any principal capacity. *See Dep't. of Enforcement v. Freedom Investors Corporation*, No. C8A990071 (NAC April 19, 2001)(NAC upheld both Hearing Panel's rejection of recommended suspension for one year because of effect on firm, and it's imposition of 90 day suspension of principal).

As an additional sanction, Enforcement recommends that Belden be ordered to pay restitution to the estate of JRB in the amount of $84,412.58, the amount of the CDSC that JRB incurred upon the exchange of his Class B shares for Class A shares, plus interest. The Hearing Panel declines to order restitution based on the amount of the CDSC incurred because JRB made no attempt to cover, that is, to minimize his damages. Had he waited only a few weeks to exchange his Class B shares, the CDSC would have decreased by one percent. Moreover, by reducing his investments by the amount of the CDSC incurred, he lost any earnings from those funds, had they remained invested. The Hearing Panel will instead order restitution to the estate of JRB in the amount of $55,567.03, plus interest calculated pursuant to 26 U.S.C. § 6621(a)(2),[7] from July 10, 1997 (the date of sale), to the date of payment. The amount of restitution is based on the difference in commissions earned by Belden on the Class B shares and what he should have earned on the sale of Class A shares. That amount deprives Belden of his ill-gotten gains on the transactions, and more closely approximates the damages incurred by JRB because his funds were invested unsuitably. In addition Belden will be assessed $2,231.84 in costs, consisting of a $750 administrative fee and a $1,481.84 transcript fee.

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[7] The interest rate used by the Internal Revenue Service to determine interest due on underpaid taxes. This rate, which is adjusted each quarter, reflects market conditions, and thus approximates the time value of money for each quarter in which the customer lost the use of his funds.

These sanctions shall become effective on a date determined by the Association, but not sooner than 30 days from the date this Decision becomes the final disciplinary action of the Association, except that if this Decision becomes the final disciplinary action of the Association, the suspension shall become effective with the opening of business on January 7, 2002, and end on April 6, 2002.

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Alan W. Heifetz
Hearing Officer
For the Hearing Panel

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