

NASD OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT	:	
	:	Disciplinary Proceeding
Complainant,	:	No. C01040003
	:	
v.	:	Hearing Officer –SNB
	:	
Respondent	:	HEARING PANEL DECISION
	:	
	:	September 17, 2004
	:	
	:	
Respondent.	:	

Respondent engaged in an unauthorized transaction, in violation of Rule 2110, by transferring \$90,000 from one money market fund to another money market fund without the knowledge or consent of the customer. He is censured and fined \$5,000.

Appearances

David A. Watson, Esq. and Mark Graves, Esq., San Francisco, CA, (Rory C. Flynn, Esq., Washington, DC, of Counsel), for Complainant.

JB, Esq., San Diego, California, for Respondent.

DECISION

1. Procedural History

The Department of Enforcement filed a Complaint charging that Respondent engaged in an unauthorized transaction, in violation of Rule 2110, by transferring \$90,000 of a customer’s funds from one money market fund to another money market fund without the customer’s knowledge or consent. Respondent admitted the violation, and a hearing with respect to the issue of sanctions was held in San Francisco, California on July 13, 2004, before a Hearing Panel that included a Hearing Officer and two

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members of the District 1 Committee.¹ The Department of Enforcement made its opening statement and rested, subject to the right to cross-examine Respondent.

Respondent testified on his own behalf, and called JP, the General Counsel of MLS & Co.

2. Facts

The relevant facts are uncontested. The Panel found Respondent's testimony to be direct, forthright and generally consistent with the sworn statement of investor NS. Respondent's testimony was also corroborated by documentary evidence and JP's testimony. The Panel also found JP's testimony to be credible and forthright.

Respondent has been in the securities industry since 1983. (CX-1; RX-45; Tr. at p. 21) Since October 1995 he has been registered with MLS, an NASD member firm. Respondent was at all times relevant to this case registered with the NASD as a General Securities Representative and a Limited Principal, General Securities Sales Supervisor, which registration remains currently in effect. (CX-1) He has no prior disciplinary history and no prior customer complaints. (CX-1; RX-45; Tr. at p. 23)

NS opened an account with Respondent in 1999 to hold the municipal bonds, mutual funds, and money market assets that NS inherited from her father, who previously maintained an account with Respondent. (CX-11; Tr. at pp. 24-27) During the account transfer process in 1998 and 1999, NS spoke with Respondent several times, and several times more after her account was opened until November 2001. (CX-11; Tr. at pp. 25-26)

¹ Enforcement offered Complainant's Exhibits ("CX") 1-11, which were admitted without objection. Respondent offered Respondent's Exhibits ("RX") 1-48, which were admitted without objection. Citations to the Hearing transcript are cited as "Tr. at p.".

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In October 2001 Pacific Life Mutual Funds announced a one-week sales promotion whereby MLS clients could purchase A shares in any Pacific Life Mutual Fund without paying a sales commission or load (CX-5; RX-40; RX-48; Tr. at pp. 27-30, 80-83) This promotion also allowed customers to purchase the Pacific Life Money Market Fund, which could at any time be transferred to any Pacific Life Class A mutual fund without paying a sales commission or load, (RX-48; Tr. at pp. 32, 81-82, 101-103), or a contingent deferred sales charge, as long as they were under \$1 million. (RX-40; Tr. at pp. 31, 84-86, 89) This promotion was associated with the initial launch of the Pacific Life Fund Family, and it had never been offered to MLS customers before, nor has it been offered since. (Tr. at pp. 37, 79)

The promotion was available for purchases between November 5 and November 9, 2001. (CX-5; RX 40; Tr. at pp. 29-30) In late October or early November, Respondent attempted to contact NS to discuss the promotion. In that regard, Respondent left two voicemail messages for NS. (CX-11; Tr. at p. 35) In the first message, he explained the details of the promotion and recommended that NS invest in the Pacific Life Managed Bond Fund (the “Bond Fund”), which he noted had an anticipated yield of 6%. He also expressed to her that this was a conservative, suitable investment that he thought she would like to consider. (Tr. at pp. 35-36) In the second message, Respondent reiterated his earlier message, and suggested that if NS was not yet ready to make a decision on the Managed Bond Fund, she should consider transferring funds from the MLS Money Market Fund to the Pacific Life Money Market Fund, so she could achieve a higher anticipated yield than she was receiving in her current Money Market Fund and the ability to transfer into Class A shares of any Pacific Life Mutual Fund at a later date at net asset value (i.e., without a sales commission or load). (CX-10; Tr. at pp. 37-38)

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As of the deadline for the promotion on November 9, Respondent had not heard from NS. (CX-11; Tr. at p. 37) Respondent believed that NS would want to take advantage of the promotion, and that preserving the option to invest in Pacific Life funds without paying a sales commission or load was in her best interest. (Tr. at pp. 38, 63) He also knew that if he transferred NS's existing money market assets to the Pacific Life Money Market Fund and it turned out that NS did not want this, he would be able to liquidate and transfer the funds back to the MLS Money Market Fund at no cost to NS. Based on this, on November 9, 2001 Respondent transferred the \$90,000 held in the MLS Money Market Fund to the Pacific Life Money Market Fund. (Tr. at pp. 38-39) The total gross commission from the transaction was \$3,600 of which Respondent would receive a net commission of \$1,440, to be paid by Pacific Life.² (CX-8; RX-14; Tr. at pp. 39-40, 63) Consistent with the promotion, NS paid no commission or sales charge. (Tr. at p. 55)

After NS received the confirmation reflecting the money market transfer, she contacted Respondent to call his attention to the error in her account, given that she had never authorized the transfer. (CX-11; Tr. at p. 41) She mistakenly believed that Respondent had invested in the Pacific Life Managed Bond Fund. (CX-11) Respondent explained that he had transferred her existing money market funds into the Pacific Life Money Market Fund, so that she could have the benefit of investing in Class A shares of any Pacific Life Fund, including the Bond Fund, without paying a front end load. (Tr. at p. 41) Respondent again suggested that NS consider the Bond Fund. NS requested a prospectus for the Bond Fund, and indicated that she would consider it and get back to

² The commission for the transaction was not material in relation to Respondent's other income. (Tr. at p. 49)

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Respondent. (Tr. at p. 42) About a week later NS called Respondent and expressed concern about the contingent deferred sales charge. Respondent explained that the charge did not apply to her. (Tr. at p. 67) While NS expressed some concern about investing in the Bond Fund, she was still considering it, and did not request that Respondent reverse the Money Market transfer at that time. (Tr. at pp. 42-43)

Approximately one month later, in late December, NS called Respondent's office and requested that the Money Market transfer be reversed. (CX-11; Tr. at p. 44) Following several conversations with Respondent and others at MLS, the funds were transferred from the Pacific Life Money Market Fund to the MLS Money Market Fund. NS was never charged any load, commission, or contingent deferred sales charge relating to the investment or the subsequent reversal of the investment. (Tr. at pp. 87-88)

Respondent fully cooperated with the NASD's investigation, accepted full responsibility and expressed deep regret for his misconduct. (Tr. at pp. 48, 49, 90-91)

3. Violation

Respondent admitted that he did not have authority for the transaction. (Respondent's Pre-Hearing Brief at p. 1; Tr. at p. 38) The Hearing Panel has also independently considered the charge and finds that it is established by the undisputed facts. It is well settled that unauthorized trading in a customer's account violates the requirement under Rule 2110 that members observe just and equitable principles of trade. See, In re Robert Lester Gardner, 52 S.E.C. 343, 344, (1995) aff'd, 89 F.3d 845 (9th Cir.) (table format). Thus, the only issue for the Panel is to determine an appropriate sanction.

4. Sanctions

The Panel consulted the NASD Sanction Guidelines (2004 ed.) ("Guidelines") to determine the appropriate sanction in this case. As the Overview to the Guidelines notes,

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the Guidelines are not intended to be “absolute.” Rather, they “recommend ranges for sanctions and suggest factors that Adjudicators may consider in determining . . . whether sanctions should be above or below the recommended range.” Guidelines, at p. 3. The Guidelines also acknowledge that the Adjudicator may consider factors in addition to those enumerated, and based upon the facts of a particular case, the Adjudicator may impose sanctions that fall outside the ranges recommended. Id.

The recommended range for unauthorized transactions is a fine of \$5,000 to \$75,000 and a suspension of 10 days to one year, or in egregious cases, a bar. Guidelines at p. 100.³ Enforcement requested that the Respondent be sanctioned at the low end of the range, with a fine of \$5,000 and a 10 day suspension.

The Panel applied the factors or “Principal Considerations” suggested in the Guidelines and found that a \$5,000 fine was appropriate, but determined, in light of the unique facts of this case, that no remedial purpose would be served by imposing a suspension. In this regard, the Panel noted that this case involved only one transaction, which was undertaken with the intent to benefit the customer. In fact, the customer was not disadvantaged, as the transaction was from one money market to another money market with a higher projected interest rate, and unlike an equity investment, there was no risk of loss to principal. Moreover, Respondent had the ability to, and in fact did, unwind the transaction and restore the customer’s account to its original position when, after due consideration, the customer requested it. In addition, Respondent never attempted to conceal his actions, accepted full responsibility, expressed deep regret, and

³ Under the Guidelines, there are three categories of egregious cases: (1) quantitatively egregious unauthorized trading; (2) unauthorized trading accompanied by certain aggravating factors; and (3) qualitatively egregious unauthorized trading, as determined by the strength of evidence that the trades were unauthorized and the Respondent’s motives in effecting the trade. The Panel found that none of these categories were present in this case.

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cooperated fully with the investigation.

Conclusion

Respondent engaged in an unauthorized trade, in violation of Rule 2110, by transferring \$90,000 of a customer's funds from one money market fund to another money market fund without the customer's knowledge or consent. He is censured and fined \$5,000. In addition, he is ordered to pay costs in the amount of \$1,587.18, which includes an administrative fee of \$750 and hearing transcript costs of \$837.18.⁴

The foregoing sanctions shall become effective on a date set by the NASD, but not earlier than 30 days after this Decision becomes the final disciplinary action of the NASD.

HEARING PANEL

/S/

By: Sara Nelson Bloom
Hearing Officer

⁴ 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.