

NASD OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,

Complainant

v.

LH ROSS & COMPANY, INC.
(BD No. 37920)

Boca Raton, FL

FRANKLYN ROSS MICHELIN
(CRD No. 2459180)

Boca Raton, FL,

Respondents.

Disciplinary Proceeding
No. C07040074

Hearing Officer – DMF

HEARING PANEL DECISION

January 25, 2005

Respondent firm is expelled from NASD membership and Respondent individual is barred from associating with any NASD member in any capacity for failing to provide certain requested information, in violation of Rules 8210 and 2110. Respondents also failed to provide other information in a timely manner, in violation of Rules 8210 and 2110, but in light of the expulsion and bar, no additional sanctions are imposed for that violation.

Appearances

Joel R. Beck, Esq., Atlanta, GA, Roger D. Hogoboom, Esq., Denver, CO, (Rory C. Flynn, Washington, DC, Of Counsel) for Complainant.

Respondents pro se.

DECISION

I. Procedural History

The Department of Enforcement filed a Complaint on August 31, 2004, charging that Respondents LH Ross & Company, Inc. and Franklyn Ross Michelin failed to provide certain information requested by NASD staff and failed to provide other

information in a timely manner, in violation of Rules 8210 and 2110. Respondents filed an Answer in which they contested the charges and requested a hearing.

Enforcement subsequently filed a motion for summary disposition, pursuant to Rule 9264, supported by the affidavits of two NASD staff members and ten Complainant's Exhibits (CX 1-10). Although Respondents had been represented by counsel, on December 23, 2004, after Enforcement filed its motion for summary disposition, Respondent's counsel withdrew, stating that he could "no longer ethically represent[] LH Ross and Mr. Michelin in this case." In withdrawing, Respondents' former counsel requested an indefinite extension of time for Respondents to seek new counsel and to respond to Enforcement's motion. On December 28, 2004, the Hearing Officer issued an order denying the request, which was served on Michelin individually and as president of LH Ross. Respondents did not thereafter file any documents or otherwise contact the Office of Hearing Officers regarding their representation in this matter, and they did not file an opposition to the motion. For the reasons set forth below, the Hearing Panel, including the Hearing Officer and two members of the District 7 Committee, grants Enforcement's motion.

II. Facts

A. Respondents

LH Ross has been a member of NASD since 1995. It conducts a general securities business, with approximately 16 branch office locations and 159 registered representatives, and is headquartered in Boca Raton, Florida. Michelin, LH Ross' president, has been registered with LH Ross since about November 1994. He is currently registered in various capacities, including as a general securities principal and

representative. Both LH Ross and Michelin are subject to NASD jurisdiction for purposes of this proceeding. (Compl. ¶¶ 1-2; Ans. ¶¶ 1-2.)

B. Failure to Respond to Requests for Information

On May 6, 2004, in connection with examinations of certain of LH Ross' branch offices, NASD staff sent a letter to Michelin at LH Ross requesting specified information concerning the sales practices, compensation and supervision of certain registered representatives and associated persons of LH Ross. The request was made pursuant to Rule 8210 and required a response by May 20, 2004. (Compl. ¶¶ 4-5; Ans. ¶¶ 4-5; Kallbreier Aff. ¶¶ 4-6; CX 1.)

On May 20, an LH Ross employee contacted NASD staff, stated that the firm had referred the May 6 request to counsel, and sought and obtained a two week extension of time, to June 4, in which to respond to the May 6 request. On June 4, a representative of the firm's counsel contacted NASD staff and sought and obtained an additional extension of time, to June 9, within which to respond to the May 6 request. (Kallbreier Aff. ¶¶ 7-8.)

On June 3, 2004, NASD staff sent a second letter to Michelin at LH Ross requesting information relating to, among other things, whether a statutorily disqualified individual was associated with the firm, and whether the firm had complied with its obligations to file and update Forms U-4 and U-5 for its associated persons, as well as its reporting obligations under Rule 3070. The request was made pursuant to Rule 8210 and required a response by June 17, 2004. (Compl. ¶¶ 8-9; Ans. ¶¶ 8-9; Kallbreier Aff. ¶¶ 9-10; CX 2.)

On June 7, 2004, NASD staff sent a third letter to Michelin at LH Ross requesting information regarding, among other things, payments by the firm to certain specified

individuals. The request was made pursuant to Rule 8210 and required a response by June 21, 2004. (Compl. ¶ 10; Ans. ¶ 10; Kallbreier Aff. ¶¶ 11-12; CX 3.)

As of June 15, Respondents had provided no information in response to any of the three requests. On that date, the firm's counsel contacted NASD staff and requested and obtained an extension of time, to June 30, within which to respond to all three requests. The firm's counsel confirmed the extension in a June 15 letter to NASD staff, and NASD staff confirmed the extension in a June 18 letter to Michelin at LH Ross. The staff's letter noted that the information had been requested pursuant to Rule 8210, stated that the June 30 extension was the last that would be granted and explained that a failure to respond might result in disciplinary action. The staff received a return receipt showing that LH Ross received the letter. Nevertheless, Respondents failed to provide any of the requested information by the June 30 deadline. (Compl. ¶¶ 11-12; Ans. ¶¶ 11-12; Kallbreier Aff. ¶¶ 13-17; CX 4-5.)

On June 30, the staff received by facsimile a letter from the firm's counsel apologizing for the failure to provide the requested information by the deadline. According to the letter, the firm had "been occupied over the past few weeks meeting other NASD and other regulatory deadlines and has not been able to respond to your requests." The letter stated that the counsel did "not want to set another deadline without knowing that our client will be able to fulfill such deadline. We anticipate contacting you by the close of business Friday [July 2] to propose an appropriate deadline." The firm's counsel did not, however, contact the staff and the firm did not provide any of the requested information. (Kallbreier Aff. ¶¶ 18-20; CX 6.)

On August 9, 2004, NASD staff sent another letter to Michelin at LH Ross and at his residential address, as listed in the Central Registration Depository (CRD). The letter noted that none of the information requested by the May 6, June 3 and June 7 letters (which were enclosed) had been provided, and again requested, pursuant to Rule 8210, that LH Ross and Michelin provide the requested information by August 19, 2004. The letter also noted that failure to provide the requested information by August 19 could subject both LH Ross and Michelin to disciplinary action. Nevertheless, Respondents failed to provide any of the requested information by that date. Indeed, as of December 13, 2004, the date of Enforcement's motion and supporting affidavits, none of the information requested in the May 6, June 3, June 7 and August 9 letters had been provided, and there is no evidence that Respondents have provided any of the information since then. (Kallbreier Aff. ¶¶ 21-27; CX 7.)

C. Failure to Respond to Requests for Information in a Timely Manner

In 2003, NASD staff was investigating a customer complaint that an LH Ross representative had effected an unauthorized purchase of LH Ross stock in the customer's account. On October 21, 2003, in connection with this investigation, NASD staff sent a letter to Michelin at LH Ross requesting information relating to the customer's complaint. The letter was sent pursuant to Rule 8210 and required a response by November 4, 2003. (McKay Aff. ¶¶ 3-5; CX 8.)

Respondents provided no information by the November 4 deadline. On November 5, NASD staff contacted LH Ross and was advised by an employee that the firm would provide the information the following day, but the firm did not do so. Therefore, on November 7, 2003, NASD staff sent a second letter to Michelin at LH Ross

requesting, pursuant to Rule 8210, that the firm provide the information requested in the October 21 letter by November 21. The letter also advised that the failure to provide the information by the deadline could result in disciplinary action against Michelin and the firm. Nevertheless, Respondents did not provide any of the requested information by the November 21 deadline. (McKay Aff. ¶¶ 6-9; CX 9.)

In January 2004, an NASD staff attorney sent a letter to counsel for LH Ross and Michelin citing, among other things, their failure to respond to the October 21 and November 7 requests for information. On February 13, 2004, NASD staff received the information originally requested in the October 21 letter. (McKay Aff. ¶¶ 10-11.)

III. Discussion

Rule 9264 provides that a party may move for summary disposition of any or all of the causes of action set forth in the Complaint, or any affirmative defense asserted in the Answer. The Hearing Panel may grant summary disposition if there is no genuine issue with regard to any material fact and the moving party is entitled to summary disposition as a matter of law. “[T]he moving party bears the burden of demonstrating the absence of a genuine issue of material fact. ... If the moving party meets this burden, the opposing party must come forward with specific facts showing that there is a genuine issue in dispute. ... Absent such a showing, summary disposition is appropriate.”

Department of Enforcement v. Shvarts, No. CAF980029, 2000 NASD Discip. LEXIS 6, at *10 n.11 (NAC June 2, 2000) (citations omitted).

There is no genuine dispute as to the material facts set forth above, and, based on those facts, Enforcement is entitled to summary disposition as a matter of law. The Complaint charges that Respondents violated Rule 8210, which provides:

For the purpose of an investigation ... [NASD] staff shall have the right to ... require ... a member [or] person associated with a member ... to provide information orally, in writing, or electronically... with respect to any matter involved in the investigation

This authority is critically important to NASD's effective performance of its self-regulatory function. To perform that function, NASD must be able to gather information, and because NASD has no subpoena power, it depends on the cooperation of its members and their associated persons to obtain that information. "A failure to provide information fully and promptly undermines the NASD's ability to carry out its regulatory mandate." Department of Enforcement v. Valentino, No. FPI010004, 2003 NASD Discip. LEXIS 15, at *12 (NAC May 21, 2003).

This case involves two distinct failures to comply with Rule 8210. Respondents failed to provide any information in response to the May 6, June 3, June 7 and August 9, 2004 requests. Those requests were properly issued and transmitted to Respondents, and pursuant to Rule 8210(d) they are deemed to have received them. Moreover, the various communications that NASD staff received from LH Ross employees and its counsel show that the requests were delivered, yet, although LH Ross and its counsel repeatedly requested extensions of time and promised to comply, Respondents never provided the information requested.

The October 21 and November 4, 2003 requests were also properly issued and transmitted to Respondents, and they are deemed to have received them. Although Respondents eventually provided the information sought in the requests, they did not do so until February 2004, more than three months after the information was due.

Thus, as to all six of the requests, LH Ross failed to fulfill its obligations, as a member of NASD, to fully and promptly respond to requests for information. Because

the requests were addressed to Michelin, he was responsible for ensuring that the firm properly responded. Richard J. Rouse, 51 S.E.C. 581, 585 (1993).

In their Answer, Respondents offered, as an “affirmative defense” to the charges, the claim that “NASD Enforcement has so inundated [LH Ross] with Rule 8210 requests and other regulatory actions that it cannot run its business and also satisfy the NASD.” That LH Ross may have been the subject of other investigations and regulatory actions, however, does not excuse Respondents’ failure to respond to requests for information, or to respond in a timely manner.

The May 6, June 3, June 7 and August 9, 2004 requests sought specific information concerning LH Ross’s private placement offering of its own stock, and the activities and job responsibilities of three LH Ross employees involved in the private placement sales; an explanation regarding the employment of one of those individuals, who appeared to be statutorily disqualified from association with any NASD member as a result of a conviction for mail and wire fraud; and information regarding the firm’s relationship with, and reasons for paying substantial sums to, several unregistered individuals. Respondents should have been able to provide this information in fairly short order, but even if compiling and transmitting the information to NASD imposed a burden, Respondents had an unqualified obligation to respond. However, more than six months after the May 6 letter, and more than three months after this proceeding was filed, Respondents had yet to provide any of the requested information.

Similarly, the October 21 and November 4, 2003 requests sought information regarding a single customer complaint alleging the unauthorized purchase of LH Ross stock in the customer’s account, an extremely serious allegation. Respondents have

failed to establish any justification for their failure to provide the information for more than three months after it was due.

Therefore, the Hearing Panel finds that the material facts are undisputed and establish, as a matter of law, that Respondents violated Rule 8210 by failing to respond to the May 6, June 3, June 7 and August 9, 2004 requests for information and by failing to respond to the October 21 and November 4, 2003 requests for information in a timely manner. A violation of Rule 8210 is also a violation of Rule 2110. Department of Enforcement v. Hoepfer, No. C02000037, 2001 NASD Discip. LEXIS 37 at *5 (NAC Nov. 2, 2001).

IV. Sanctions

The Sanction Guidelines provide that for a failure to respond to Rule 8210 requests, a bar is the standard sanction for the responsible individual, and in egregious cases the firm should be expelled. NASD Sanction Guidelines at 37 (2004). For failure to respond in a timely manner, the Guidelines recommend suspending the firm and the responsible individual for up to 30 business days, and a fine of \$2,500 to \$25,000. Enforcement requests that LH Ross be expelled and Michelin barred for their violations.

In determining sanctions for failure to respond or failure to respond in a timely manner, the Guidelines instruct the Hearing Panel to consider the nature of the information requested, whether the information was ever provided, and, if so, the number of requests made, the time Respondent took to provide the information and the degree of regulatory pressure required to obtain the information. Here NASD staff requested information about LH Ross' offering of its own stock and the LH Ross employees who were soliciting customers to purchase that stock, as well as information regarding a customer complaint of an unauthorized purchase of LH Ross stock in his account. Much

of the information was never provided; the information regarding the customer complaint was provided only after repeated requests and a delay of several months. There is no evidence of any mitigating facts.

The Hearing Panel, therefore, finds that, under the undisputed facts, it is appropriate to expel LH Ross from NASD membership and to bar Michelin from associating with any NASD member in any capacity for failing to respond to the May 6, June 3, June 7 and August 9, 2004 requests for information. In light of the expulsion and bar, no fines will be imposed for this violation, and although substantial sanctions would also be appropriate for Respondents' failure to respond to the October 21 and November 4, 2003 requests in a timely manner, in light of the expulsion and bar no further sanctions will be imposed for that violation.

V. Conclusion

Respondent LH Ross & Company, Inc. is expelled from NASD membership and Respondent Franklyn Ross Michelin is barred from associating with any NASD member in any capacity for failing to respond to requests for information, in violation of Rules 8210 and 2110. Respondents also failed to respond to other requests for information in a timely manner, in violation of Rules 8210 and 2110, but in light of the expulsion and bar, no additional sanctions are imposed for that violation. If this decision becomes NASD's final disciplinary action in this matter, the expulsion and the bar shall become effective immediately.

HEARING PANEL

By: David M. FitzGerald
Hearing Officer

Copies to: LH Ross & Company, Inc. (*via overnight and first class mail*)
Franklyn Ross Michelin (*via overnight and first class mail*)
Roger D. Hogoboom, Esq. (*electronically and via first class mail*)
Joel R. Beck, Esq. (*electronically and via first class mail*)
Rory C. Flynn, Esq. (*electronically and via first class mail*)