

**FINANCIAL INDUSTRY REGULATORY AUTHORITY<sup>1</sup>**  
**OFFICE OF HEARING OFFICERS**

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

HARVEY M. SCHWARTZ  
(CRD No. 4301325),

Respondent.

Disciplinary Proceeding  
No. E102004083703

Hearing Officer – SNB

**HEARING PANEL DECISION**

November 16, 2007

**Respondent violated Rules 2110 and 3110 by falsely representing in firm records that six customers were disabled, in order to obtain waivers of sales charges that otherwise would be imposed upon their sale of certain Class B mutual fund shares. For these violations, Respondent is suspended from associating with any FINRA member in any capacity for four months and fined \$1,000.**

**Appearances**

Paul Hare, Esq., and Jeff Kern, Esq., New York, NY, for the Department of Enforcement.

Alan M. Wolper, Esq., and Michael Freedman, Esq., Sutherland Asbill & Brennan LLP, Atlanta, GA, for Respondent.

**DECISION**

**I. Procedural History**

On November 9, 2006, the Department of Enforcement (“Enforcement”) filed a one-cause Complaint against Harvey M. Schwartz (“Respondent”). The Complaint alleges that Respondent violated Rule 2110 by falsely representing that six customers were disabled when

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<sup>1</sup> As of July 30, 2007, NASD consolidated with the member firm regulation functions of the NYSE and began operating under a new corporate name, the Financial Industry Regulatory Authority (“FINRA”). References in this decision to FINRA include, where appropriate, NASD.

they were not, in order to obtain waivers of sales charges that otherwise would be imposed upon their sale of certain Class B mutual fund shares. The Complaint also alleges that Respondent's false claims caused the firm's books and records to contain false and misleading information, in violation of Rule 3110. On December 6, 2006, Respondent filed his Answer and requested a hearing. On May 22, 2007, a hearing was held before a hearing panel composed of a Hearing Officer and two current members of the District 7 Committee.<sup>2</sup> Subsequent to the hearing, one panelist withdrew from the matter. Accordingly, this decision is rendered by the Hearing Officer and the remaining panelist.

## **II. Respondent**

Respondent first became registered with FINRA as a General Securities Representative with Citigroup Global Markets/Smith Barney ("Smith Barney"), where he worked from December 2000 through May 2003, when he joined UBS Financial Services, Inc. ("UBS"). He left UBS in August 2004, almost a year after the conduct at issue in the Complaint. In September 2004, he joined the Stanford Group Company (the "Stanford Group"), where he is currently registered. Respondent has no disciplinary history. CX-1.

## **III. Facts**

This case arose from a FINRA cause examination that was opened when UBS made Form U5 filings regarding a number of its registered representatives who either resigned or were terminated because they made false disability claims on behalf of their clients in order to obtain waivers of sales charges for Class B mutual fund shares. Tr. 35-37.

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<sup>2</sup> References to the testimony of the hearing are designated as "Tr\_ ", with the appropriate page number. References to the exhibits provided by Enforcement are designated as "CX-\_\_\_", and references to Respondent's exhibits are designated as "RX-\_\_\_". CX-1-12, and 15-17, and RX-2 and 9 offered and admitted into the record; the remaining exhibits identified by the parties in their pre-hearing submissions were not offered. Tr. 76, 182.

Respondent does not dispute the allegation that he made false entries on a UBS electronic order entry system claiming that six customers were disabled when they were not, in order to obtain waivers of sales charges. The hearing focused on the circumstances surrounding Respondent's actions, and on his subsequent supervision and conduct at the Stanford Group.

While Respondent was with Smith Barney, he worked for a group of senior representatives with approximately \$500 million in accounts. CX-1; Tr. 82. His duties were to answer phones, speak with the senior representatives' customers, send out mailers, cold call, and perform administrative functions to support the senior representatives. Tr. 82-83. Over time, Respondent also opened 10 to 20 accounts for friends and family members. Tr. 84, 93-94. Respondent did no mutual fund business in connection with these accounts. Tr. 85.

In May 2003, Respondent joined UBS, with the plan to build his book of business. CX-4; Tr. 85-87. Approximately 25 customer accounts, including 10 to 15 friend and family accounts, transferred from Smith Barney to stay with him at UBS. Tr. 93-96.

Respondent had never recommended mutual funds for his clients. Tr. 85. However, during the process of transferring client accounts, Respondent learned that some of his customers held a Smith Barney proprietary mutual fund that could not be transferred to UBS. Tr. 96-99. Respondent's customers did not want to maintain separate accounts at Smith Barney. Because the mutual fund shares were Class B, in the event they were liquidated, the customers would be assessed Contingent Deferred Sales Charges ("CDSC").<sup>3</sup> Tr. 98.

Respondent testified that when he joined UBS, the branch manager introduced him to Robert Lieberman ("Lieberman"), who the branch manager characterized as an experienced

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<sup>3</sup> A CDSC is a form of sales charge (or "back-end load") that is paid by a Class B fund investor at the time of redemption, if the redemption occurs within a pre-established holding period. Typically, the CDSC decreases to zero if the investor holds his or her shares long enough. The purpose of the CDSC charge is to reimburse the mutual fund's distributor for commissions paid to dealers at the time the investor purchased fund shares.

broker who could help Respondent. Tr. 91. Lieberman told Respondent that he was an expert in mutual funds, and was the leading seller of mutual funds in the branch. Tr. 92. Lieberman, whose office was adjacent to Respondent's office, visited Respondent's office frequently to see how Respondent was doing and offer advice. Tr. 101-102.

When Respondent encountered difficulties in transferring certain of his customers' Smith Barney Class B mutual fund shares, he discussed the problem with Lieberman. Lieberman suggested that Respondent instruct his clients to request a transfer to another fund within the Smith Barney fund family that could be transferred to UBS. Then, after the transfer, the shares could be liquidated and the proceeds reinvested consistent with the customers' wishes. Tr. 107-108. Lieberman advised Respondent that he could avoid the imposition of CDSCs when the transfer shares were liquidated by using the UBS electronic system to claim that his clients were disabled.<sup>4</sup> Tr. 101-103. Lieberman also showed Respondent how to claim the waiver on the UBS system. Id. Lieberman advised Respondent that it was industry practice to obtain fee waivers in this manner; that he had done it for his clients for many years; and that the mutual fund companies understood and accepted this practice. Tr. 102-103. Respondent trusted Lieberman and did as he suggested, claiming disability waivers for six customers in June and July 2003. Respondent did this without informing his customers or confirming the practice with his branch manager. Tr. 103, 110, 160.

Several months later, Respondent received a copy of a wire from Smith Barney to UBS asking for documentation of his customers' disabilities. Tr. 108-109. Respondent immediately

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<sup>4</sup> UBS had a Mutual Fund Order Entry System that allowed registered representatives to claim CDSC waivers without supervisory approval. Tr. 45, 104. The system default for a CDSC waiver was set to "NO." If a financial advisor elected to claim a waiver, the system required the financial advisor to select CDSC waiver and then select a reason for the waiver from a drop-down menu. The available options were death, disability, mandatory distribution, or systematic withdrawal. When an order was placed through the system, it was electronically transmitted directly to the mutual fund company. CX-10; Tr. 42-45.

realized that he should not have followed Lieberman's advice. Tr. 109. Respondent confessed to his branch manager, who told Respondent to rebook the trades, which Respondent did. Tr. 109-110. Respondent also advised his customers that they would be assessed a CDSC. His customers paid the charge without complaint. Tr. 111. Respondent never advised his customers of his ill-fated attempt to obtain waivers by using false disability claims. Id.

Almost a year later, in August 2004, Respondent was terminated by UBS for making these false disability claims. CX-1. Respondent then joined the Stanford Group, where he is currently registered.

#### **IV. Violations**

Rule 2110 requires members and associated persons to “observe high standards of commercial honor and just and equitable principles of trade.”<sup>5</sup> The Rule articulates a broad ethical principle<sup>6</sup> to promote the “professionalization of the securities industry.”<sup>7</sup> By knowingly submitting false information on mutual fund sales orders, Respondent violated that ethical obligation.<sup>8</sup>

Rule 3110 requires each FINRA member to make and preserve books, accounts, records, memoranda, and correspondence in conformity with applicable rules. By falsely claiming disability waivers for his customers, Respondent caused UBS's books and records to be inaccurate.

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<sup>5</sup> Rule 0115 extends the obligations of Conduct Rule 2110 to associated persons, as well as members.

<sup>6</sup> Timothy L. Burkes, 51 S.E.C. 356 (1993), aff'd mem., 29 F.3d 630 (9th Cir. 1994).

<sup>7</sup> Dep't of Enforcement v. Shvarts, No. CAF980029, 2000 NASD Discip. LEXIS 6, at \*11 (NAC June 2, 2000).

<sup>8</sup> Cf., e.g., Dep't of Enforcement v. Prout, No. C01990014, 2000 NASD Discip. LEXIS 18, at \*6 (NAC Dec. 18, 2000) (submitting false information about customers on variable annuity applications).

Accordingly, the Hearing Panel finds that Respondent violated Rules 2110 and 3110 by knowingly and falsely representing in UBS books and records that six customers were disabled when they were not, in order to obtain CDSC waivers.

**V. Sanctions**

Although the Panel determined that Respondent's conduct violated both Rule 2110 and Rule 3110, the violations arose out of a single action, the entry of false waiver claims, and therefore the Panel will impose a single set of sanctions to address both violations.<sup>9</sup> Moreover, the Panel concluded that the appropriate Sanction Guidelines to apply are those for falsification of records.

For falsification of records, the FINRA Sanction Guidelines ("Guidelines") recommend a fine of \$5,000 to \$100,000 and a suspension of up to two years.<sup>10</sup> In egregious cases, the Guidelines suggest consideration of a bar. Enforcement argued that Respondent's misconduct was egregious and that he should be suspended in all capacities for one year and fined \$5,000. Respondent urged the Hearing Panel to impose no suspension.

The Panel found that Respondent's conduct was serious, but not egregious. Respondent entered information that he knew was false into the UBS system, with the understanding that it would cause mutual funds to waive fees to which his customers were not entitled. The Panel found that it was not reasonable for Respondent to rely upon Lieberman's advice, because the conduct that Lieberman advised was so clearly dishonest.

However, the Panel also considered a number of mitigating factors. First, Respondent acted to benefit his customers' interest. Moreover, the waivers were never processed and the

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<sup>9</sup> See, Dep't of Enforcement v. Cuozzo, No. C9B050011, 2007 NASD Discip. LEXIS 12 at \*\*30-31 (NAC Feb. 27, 2007).

<sup>10</sup> <http://www.finra.org/web/groups/enforcement/documents/enforcement/p011038.pdf>.

mutual fund was not harmed. Respondent also confessed his wrongdoing, expressed regret, and cooperated in the investigation. Moreover, the number of transactions and the amounts involved were small. In addition, the Panel considered Respondent's settlement with the State of Florida which resulted in a \$4,000 fine and heightened supervision.<sup>11</sup> RX-9; Tr. 174-176. The Panel also considered that the Stanford Group imposed heightened supervision beyond that required by Florida. Tr. 177. Finally, the Panel considered the credible testimony of Reginald Ralph Edward Poppel ("Poppel"), the Stanford Group's Director of Compliance responsible for Respondent's heightened supervision. Specifically, the Panel considered Poppel's testimony that Respondent: (i) has been diligent and careful to comply with applicable rules; (ii) has consulted with Poppel in situations where most brokers would not have made the effort; and (iii) in Poppel's opinion, is among the least likely of the Stanford Group's brokers to encounter regulatory issues in the future. Tr. 181.

Based on these factors, the Hearing Panel finds that Respondent should be suspended in all capacities for four months, and, taking into account the \$4,000 fine he has already paid to the State of Florida, fined \$1,000.

## **VI. Conclusion**

Respondent is suspended from associating with any FINRA member in any capacity for four months and fined \$1,000, for violating Rules 2110 and 3110. In addition, he is ordered to pay costs in the amount of \$2,217.70, which include a \$750 administrative fee and the cost of the hearing transcript. The fine and costs shall be payable on a date set by FINRA, but not earlier than 30 days after this decision becomes FINRA's final disciplinary action in this matter. If this decision becomes FINRA's final disciplinary action, the suspension shall begin at the opening of

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<sup>11</sup> See, *Dep't of Enforcement v. Greer*, No. C05990035, 2001 NASD Discip. LEXIS 34, at \*14, n.6 (NAC Aug. 6, 2001) (considering fines paid to another regulator in determining an appropriate fine).

business on January 3, 2008, and end on May 3, 2008.<sup>12</sup>

**HEARING PANEL**

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By: Sara Nelson Bloom  
Hearing Officer

Copies to: Harvey M. Schwartz (*via first-class mail*)  
Alan M. Wolper, Esq. (*via facsimile and first-class mail*)  
Paul Hare, Esq. (*via electronic mail*)  
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Mark P. Dauer, Esq. (*via electronic mail*)

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<sup>12</sup> The Hearing Panel has considered all of the parties' arguments. They are rejected or sustained to the extent that they are inconsistent with the views expressed herein.