

FINANCIAL INDUSTRY REGULATORY AUTHORITY¹
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

IFTIKHAR UL HAQ
(CRD No. 4212059),

Respondent.

Disciplinary Proceeding
No. ELI2004026701

Hearing Officer – AWH

HEARING PANEL DECISION

November 1, 2007

Registered representative barred from associating with any member firm in any capacity and ordered to make restitution to customer for unauthorized and excessive trading in customer's account, in violation of NASD Conduct Rules 2310 and 2110. Respondent also assessed costs.

Appearances:

Samuel L. Barkin, Esq., and Jon Batterman, Esq., for the Department of Enforcement.

No appearance by or for Iftikhar Ul Haq.

DECISION

Background

On November 30, 2006, the Department of Enforcement filed the Complaint in this proceeding, alleging that Iftikhar Ul Haq (“Haq” or “Respondent”) executed unauthorized transactions and made excessive trades in the account of a public customer.²

On January 4, 2007, Haq filed an Answer to the Complaint, denying the substantive

¹ Effective July 30, 2007, the corporate successor to NASD is the Financial Industry Regulatory Authority (FINRA). The Rules at issue continue to be designated as NASD Rules.

² As an alternative to the charge that Haq executed unauthorized transactions, the Complaint alleged that Haq exercised discretion without written authorization. In light of the evidence that Haq executed unauthorized transactions, the Hearing Panel does not reach the alternative charge.

allegations, and a request for a hearing. During an initial pre-hearing conference, the parties agreed, among other things, that the hearing would be held in New York City on August 21-22, 2007. During the scheduled Final Pre-Hearing Conference on August 14, 2007, Haq announced that he would “try” to attend the scheduled hearing, although, at some unspecified time, he made plans to be in Texas during the week of the hearing. On August 17, 2007, Haq wrote to counsel for Enforcement, stating that he would not attend the hearing, and that he was fully aware that the “decision regarding my case is final and could have a lasting impact on my career in this industry.”

As scheduled, the hearing was held on August 21, 2007, before a Hearing Panel composed of the Hearing Officer and two members of the District 10 Committee. Haq failed to appear at the hearing. Enforcement presented its case, including the testimony of customer KS who traveled from his home in North Carolina to attend the hearing. Enforcement filed a post-hearing brief on October 2, 2007.

Findings of Fact³

Respondent

Iftikhar Ul Haq was first registered with FINRA as a General Securities Representative from September 8, 2000 through March 29, 2007. As pertinent to the Complaint, Haq was registered through GunnAllen Financial, Inc., from October 21, 2002, through November 18, 2005, when GunnAllen terminated his registration. From October 27, 2005 through March 29, 2007, Haq was registered through another FINRA member firm. He is not currently associated with any FINRA member firm.⁴

³ References to the Department of Enforcement’s exhibits are designated as CX-, and the transcript of the hearing, as Tr.-.

⁴ CX-15.

Opening of KS's Account with First Representative

KS is a native of Pakistan who immigrated to the United States in 1980.⁵ KS opened his account at GunnAllen in October 2002. The account was not discretionary.⁶

Initially, KS's registered representative at GunnAllen was Ajmal Mir Shams ("Shams").⁷ When he was at a previous firm, Shams had cold-called KS and solicited him to open an account with Shams as his registered representative.⁸ At the time, KS was co-owner of a motel in Highpoint, North Carolina.⁹ KS told Shams that he had previously lost money investing and that he did not want to put his money at risk.¹⁰ After their conversation, KS opened an account with Shams. In October 2002, Shams joined GunnAllen and KS transferred his account to that firm.¹¹

The GunnAllen new account form, dated October 22, 2002, stated that KS was born in 1961, married, lived in North Carolina, and owned a motel. The "client profile" section of the form stated that his investment objective is "income (quality emphasized)," his risk tolerance is "moderate," his annual income is \$100,000, and that his net worth is 500,000.¹² The information in the "client profile" section was filled in after KS signed and returned his new account form. In fact, KS's annual income at the time he opened his account was approximately \$30,000, and his risk tolerance was low.¹³

⁵ Tr. 7.

⁶ Tr. 76; CX-16, p. 53.

⁷ CX-2, CX-4.

⁸ Tr. 15-16; CX-1.

⁹ Tr. 8-9; CX-2.

¹⁰ Tr. 15-17.

¹¹ Tr. 19-20; CX-2, CX-4.

¹² CX-2.

¹³ Tr. 13-17; CX-13, CX-14.

Soon after opening his account with Shams, KS traveled to Pakistan to take care of his elderly parents.¹⁴ KS stayed in Pakistan from approximately late October/early November 2002 through late March/early April 2003.¹⁵ While KS was in Pakistan, the only transaction in his account was the purchase of shares of Raytheon, which Shams had recommended to him and which KS authorized.¹⁶ After KS returned to North Carolina, he made several purchases and sales of securities in his GunnAllen account based on discussions with Shams.¹⁷

In October 2003, Shams told KS that he was leaving GunnAllen. However, KS decided to keep his account at GunnAllen. On October 21, 2003, KS requested that Haq, who had been introduced to him by Shams, become his account representative at GunnAllen.¹⁸ On that same date, Haq became KS's account representative.¹⁹

Haq's Actions as KS's Account Representative

At the time Haq became his account representative, KS was about to leave again for Pakistan. He told Haq that he was going to Pakistan for several months to take care of his parents, who were both ill, and that for the time being, he wanted to hold the securities in his account until they increased in value and he decided to sell them.²⁰ He gave Haq two telephone numbers where he could be reached in Pakistan: one at his parents' house, and the other at his mother-in-law's house.²¹ On or about October 24, 2003, KS left the United States for Pakistan.²² Haq met KS at LaGuardia Airport, the

¹⁴ Tr. 21-22.

¹⁵ Tr. 21-22.

¹⁶ Tr. 22-23.

¹⁷ Tr. 23-25; CX-4.

¹⁸ Tr. 32-34; CX-11.

¹⁹ CX-11.

²⁰ Tr. 37.

²¹ Tr. 36.

²² Tr. 36-39; CX-5.

terminus of the first leg of Haq's trip. Haq drove KS from LaGuardia to JFK airport where his flight to Pakistan was leaving.²³ KS returned to the United States on April 2, 2004.²⁴

Unauthorized Trades

From the time Haq took over KS's account through the time KS returned from Pakistan, Haq executed 85 trades in KS's account without obtaining KS's authorization and without discussing any of the trades with KS.²⁵ A substantial portion of those trades consisted of securities held for a few days or less.²⁶ Haq marked almost all of the trades as "solicited."²⁷ However, Haq spoke to KS by telephone only three times while KS was in Pakistan.²⁸ The conversations were about personal matters and the stock market in general. At no point during those conversations did Haq tell KS about the trades he had effected in his account, except that during the second conversation, Haq told KS that he had sold two of the securities. KS responded that Haq was not supposed to sell them and Haq was to call him before making any trades.²⁹

KS returned to the United States on April 2, 2004.³⁰ Haq picked up KS at JFK Airport and drove him to LaGuardia Airport for his flight to North Carolina.³¹ Haq told him that there was no problem with his account. After KS arrived in North Carolina, he found confirmations concerning the unauthorized trades that Haq had effected during his

²³ Tr. 36-37; CX-16, pp. 62-63.

²⁴ Tr. 39; CX-5.

²⁵ Tr. 40, 48-54; CX-7, CX-8.

²⁶ Tr. 75; CX-10.

²⁷ Tr. 76; CX-6, CX-16, pp. 55-56.

²⁸ Tr. 41-51. Haq admitted that he called KS only from the GunnAllen office. CX-12, CX-16, pp. 69-70. GunnAllen's phone records show eight calls to KS, five of which lasted less than one minute. Because KS had no telephone conversation with Haq that lasted less than one minute, the five one-minute calls were most likely unsuccessful attempts by Haq to reach KS. Tr. 47.

²⁹ Tr. 40, 48-54.

³⁰ Tr. 39; CX-5.

³¹ Tr. 39-40, 54.

absence. KS called Haq to complain and told him that he did not give him permission to make trades in his absence. Haq replied that he effected the trades to make money for him.³² Notwithstanding KS' complaint and instructions, Haq made 38 more unauthorized trades during May 2004 without discussing any of them with KS.³³ When KS called Haq to object, Haq avoided his calls.³⁴

In response to KS's complaints, GunnAllen reassigned KS's account to another broker.³⁵ Shortly thereafter, KS closed the account.³⁶ As a result of the unauthorized trades made by Haq in his account, KS lost \$66,184.47.³⁷

Excessive Trading in KS's Account

Haq was unaware of KS's financial condition and needs. He never asked KS about his investment objectives, his annual income and net worth, or his risk tolerance.³⁸ He never read KS's new account form. Haq claimed to have reviewed KS's prior trading history at GunnAllen to determine whether the trades he made in KS's account were suitable.³⁹ However, the volume of trading by Haq was inconsistent with KS's previous trading history and his financial objectives and needs.⁴⁰

Haq executed 123 trades in KS's account during the period October 22, 2003, through May 18, 2004, for a total cost of \$2,419,658.05.⁴¹ The average monthly equity in KS's account over that period of time was \$97,864.69.⁴² The turnover rate (total cost of

³² Tr. 56-57.

³³ Tr. 58-59; CX-7.

³⁴ Tr. 58.

³⁵ Tr. 59-60.

³⁶ Tr. 62-63.

³⁷ Tr. 82-85; CX-7, CX-10.

³⁸ Tr. 35.

³⁹ CX-16, pp. 47-50.

⁴⁰ Tr. 76-77; *compare* CX-8 with CX-4.

⁴¹ Tr. 87; CX-6, CX-7, CX-8, CX-9.

⁴² Tr. 72-73; CX-9.

purchases divided by average monthly equity) was 24.725 for the period over which Haq handled the account, or 37.087 on an annualized basis.⁴³

During that same period of time, KS paid commissions, mark-ups, mark-downs, other service and clearing charges, and margin interest totaling \$23,876.15.⁴⁴ The cost-to-equity ratio (the percentage return necessary to make a profit in light of fees associated with the trading activity) was 24.4% or 36.6% on an annualized basis.⁴⁵

Discussion

Unauthorized Trading

Unauthorized trading is a “fundamental betrayal of the duty owed by a salesman to his customers.”⁴⁶ It is “a serious violation of just and equitable principles of trade.”⁴⁷ FINRA has made it clear that it will take disciplinary action against associated persons who have effected unauthorized trades.⁴⁸

The credible evidence adduced at the hearing established that Haq effected 123 unauthorized transactions in KS’s account, both while KS was overseas and upon his return from Pakistan. Based on KS’s demeanor and the consistency of his testimony at the hearing, the Hearing Panel finds credible his statement that he spoke to Haq only three times during the five months he was in Pakistan, and that during those conversations, they never discussed any trades that were contemplated or effected, with

⁴³ Tr. 73-74; CX-9.

⁴⁴ Tr. 72; CX-9.

⁴⁵ Tr. 73-75; CX-9. For the period Haq served as KS’s account representative, the account would have to have returned 24.4% in order to pay the transaction costs.

⁴⁶ *DOE v. Bond*, No. C10000210, 2002 NASD Discip. LEXIS 6, at *12 (NAC Apr. 4, 2002) (citation omitted).

⁴⁷ *Jonathan Garret Ornstein*, Exchange Act Release No. 31557, 1992 SEC LEXIS 2972 (December 3, 1992). See also *Robert Lester Gardner*, Exchange Act Release No. 35899, 1995 SEC LEXIS 1532 (June 27, 1995).

⁴⁸ See IM-2310-2(b)(4)(iii).

the exception of two sales that were not authorized by KS. During his on-the-record testimony, Haq acknowledged that KS's account was not discretionary. Finally, even after KS complained in May 2004 about Haq's unauthorized trading, Haq did not communicate with KS before engaging in 38 unauthorized trades in KS's account over a two-week period in May 2004. By engaging in those unauthorized trades, Haq violated NASD Conduct Rule 2110.

Unsuitable and Excessive Trading

NASD Conduct Rule 2310(a) requires that, in recommending the purchase or sale of a security, a registered person must have "reasonable grounds for believing that the recommendation is suitable for [the] 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."⁴⁹ Moreover, NASD Conduct Rule 2310 encompasses a "fundamental responsibility for fair dealing" that a registered representative has to his or her customers.⁵⁰ A violation of Conduct Rule 2310 is also a violation of Rule 2110, in contravention of just and equitable principles of trade.⁵¹

Rule 2310's suitability requirement can be violated either when the representative's recommendations are unsuitable based on the quality of the recommended transactions, or when the recommendations are quantitatively unsuitable,

⁴⁹ See also *District Bus. Conduct Comm. v. Kunz*, No. C3A96009, 1999 NASD Discip. LEXIS 20, at *62 (NAC July 7, 1999) ("Conduct Rule 2310 provides that a representative may make only such recommendations as would be consistent with a customer's financial situation and needs."), *aff'd*, Exchange Act Release No. 45,290, 2002 SEC LEXIS 104 (Jan. 16, 2002).

⁵⁰ *Larry Ira Klein*, Exchange Act Release No. 37,835, 1996 SEC LEXIS 2922, at **16-17 (Oct. 17, 1996) (citing *John M. Reynolds*, Exchange Act Release No. 30,036, 1991 SEC LEXIS 2725, at *10, n.13 (Dec. 4, 1991)).

⁵¹ *Daniel Richard Holland*, Exchange Act Release No. 46,269, 2002 SEC LEXIS 1909 (July 26, 2002).

i.e., resulting in excessive trading in the account.⁵² As the SEC has stated, “excessive trading, by itself, can violate NASD suitability standards by representing an unsuitable frequency of trading.”⁵³

The SEC has held that excessive trading occurs when (i) a broker has control over trading in an account and (ii) the level of activity in that account is inconsistent with the customer’s objectives and financial situation.⁵⁴ Here, the evidence established both of these elements.

Control

Unauthorized trading constitutes “clear evidence of control” for the purposes of an excessive trading claim.⁵⁵ The evidence clearly demonstrates that all of the trades at issue were unauthorized.

Level of Trading Activity

There is no single, precise formula or method for determining whether an account has been excessively traded.⁵⁶ However, two commonly recognized measures that may be used to determine excessive trading in an account are the cost-to-equity ratio and the turnover rate. As noted above, the cost-to-equity ratio is calculated by dividing total transaction costs incurred in an account by the average equity in the account. The turnover rate measures the number of times during a given period that the securities in the

⁵² *DOE v. Stein*, No. C07000003, 2001 NASD LEXIS 11, *9 (NAC Dec. 3, 2001), *aff’d*, *Jack Stein*, Exchange Act Release No. 47335, 2003 SEC LEXIS 338 (Feb. 10, 2003).

⁵³ *Rafael Pinchas*, Exchange Act Release 41816, 1999 SEC LEXIS 1754, at *22 (Sept. 1, 1999); *see also*, *Harry Glikzman*, Exchange Act Release No. 42255, 1999 SEC LEXIS 2685, n.7 (Dec. 20, 1999).

⁵⁴ *Rafael Pinchas*, 1999 SEC LEXIS 1754, at **11-12.

⁵⁵ *Olde Discount Corp.*, Exchange Act Release No. 40423, 1998 SEC LEXIS 1914 (1998); *Sandra K. Simpson*, Exchange Act Release No. 45923, 2002 SEC LEXIS 1278 (2002) (*de facto* control exists where broker controlled account either because customer relied on broker or because customer was incapable of controlling account due to unauthorized trading); *Leib v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, 461 F. Supp 951 (E.D. Mich. 1978) (courts will often interpret unauthorized trading as a usurpation of control by broker), *aff’d*, 647 F.2d 165 (6th Cir. 1981).

⁵⁶ *Sandra Logay*, Initial Decision Release 159, 2000 SEC LEXIS 119, **52-53 (Jan. 28, 2000), *initial decision final*, Exchange Act Release 42496, 2000 SEC LEXIS 389 (Mar. 6, 2000).

account are replaced by new securities and is calculated by dividing the total cost of purchases by the average equity in the account.

An annualized cost-to-equity ratio in excess of 20% generally indicates that excessive trading has occurred.⁵⁷ The 36.6% annualized cost-to-equity ratio for KS's account is well above that parameter.

Although no turnover rate is universally recognized as indicative of excessive trading, an annual turnover rate in excess of six is generally presumed to reflect excessive trading.⁵⁸ The annualized turnover rate for KS's account was 37.1, far above the rate reflecting excessive trading.

There is no evidence that would justify the quantity of trading in KS's account during the period it was serviced by Haq, given KS's financial situation and investment objective of income. Therefore, Haq engaged in unsuitable excessive trading in KS's account, in violation of Conduct Rules 2110 and 2310.

Sanctions

For unauthorized trading, the FINRA Sanction Guidelines recommend suspending a respondent in any or all capacities for ten business days to one year, and, in egregious cases, a longer suspension up to two years or a bar. The Guidelines also recommend a fine of up to \$75,000.⁵⁹ In addition to the Principal Considerations applicable to all

⁵⁷ *Rafael Pinchas*, 1999 SEC LEXIS 1754, at *18. See also *Peter C. Bucchieri*, Exchange Act Release No. 37218, 1996 SEC LEXIS 1331 (May 14, 1996) (cost-to-equity factors of 21% to 30%); *Michael David Sweeney*, Exchange Act Release No. 29884, 1991 SEC LEXIS 2455 (Oct. 30, 1991) (cost-to-equity factors of 22% to 44%); *Frederick C. Heller*, Exchange Act Release No. 31696, 1993 SEC LEXIS 14 (Jan. 7, 1993) (break-even return was 36%); *Shearson Lehman Hutton Inc.*, Exchange Act Release No. 26766, 1989 SEC LEXIS 778 (Apr. 28, 1989) (break-even return was 50%).

⁵⁸ See *David Wong*, Exchange Act Release 45426, 2002 SEC LEXIS 339, *14, n.18 (Feb. 8, 2002) (turnover rate of 7.3 held to be excessive). See also *Donald A. Roche*, Exchange Act Release 38742, 1997 SEC LEXIS 1283 (June 17, 1997) (turnover rate of 3.3); and *Frederick C. Heller*, 1993 SEC LEXIS 14 (turnover rate of 6.4).

⁵⁹ FINRA SANCTION GUIDELINES at 103.

sanctions determinations, the Guidelines call for the consideration of (1) whether respondent misunderstood his or her authority or the terms of the customer's orders; and (2) whether the unauthorized trading was egregious.

Here, Haq certainly did not misunderstand his trading authority or the instructions that KS gave him. KS specifically told him that he was leaving for Pakistan to care for his elderly parents and that he did not wish to sell anything in his account. When Haq told KS of the only two trades he disclosed to him, KS berated him for not obtaining his authorization to make the sales. When KS returned to the United States, he again complained to Haq who then executed 38 additional unauthorized trades in the account. When KS called to complain about Haq's continued misconduct, Haq avoided his calls.

In determining whether Haq's unauthorized trading was egregious, the Hearing Panel considered the three categories of egregious unauthorized trading that have been recognized by the NAC⁶⁰:

1) quantitatively egregious unauthorized trading, *i.e.*, unauthorized trading that is egregious because of the sheer number of unauthorized trades executed;

2) unauthorized trading accompanied by aggravating factors, such as, efforts to conceal the unauthorized trading, attempts to evade regulatory investigative efforts, customer loss, or a history of similar misconduct (this list is illustrative, not exhaustive); and

3) qualitatively egregious unauthorized trading. Two factors are relevant to a determination as to whether unauthorized trading is qualitatively egregious:

- 1) the strength of the evidence, and
- 2) the respondent's motives; *i.e.*, whether the respondent acted in bad faith or as a result of a reasonable misunderstanding.

⁶⁰ SANCTION GUIDELINES, at 103 (citing *Daniel S. Hellen*, Complaint No. C3A970031, 1999 NASD Discip. LEXIS 22, at **15-24 (NAC June 15, 1999)).

Haq's unauthorized trading was quantitatively egregious. He executed 123 unauthorized trades during a seven month period. His misconduct was not an isolated instance; it constituted a pattern of conduct that was intentional and continued over an extended period of time.

Such quantitatively egregious unauthorized trading also amounts to unsuitable and excessive trading, as charged in the third cause of the Complaint. The Sanction Guidelines for excessive trading also recommend suspending a respondent in any or all capacities for ten business days to one year, and, in egregious cases, a longer suspension up to two years or a bar. The Guidelines also recommend a fine of up to \$75,000.⁶¹ The Hearing Panel takes into consideration the factors that follow in its determination of sanctions to be imposed on Haq for his excessive trading in KS's account.

There were a number of aggravating circumstances that accompanied Haq's misconduct:

(1) Haq's misconduct resulted directly in significant monetary injury to KS, a loss of \$66,184.47 in a little over seven months.⁶²

(2) Haq's misconduct was intentional and reckless and not the result of any inadvertence or mere negligence on his part. He deliberately traded securities in KS's account without authority and excessively traded in the account.⁶³

(3) The number of transactions executed in KS's account is sizeable and should be considered in determining the egregiousness of Haq's excessive trading as well,⁶⁴ and

⁶¹ SANCTION GUIDELINES at 99 (2007 ed.).

⁶² *Id.*, Principal Consideration No. 11.

⁶³ *Id.*, Principal Considerations Nos. 13 and 17.

⁶⁴ *Id.*, Principal Consideration No. 18.

(4) Haq has a prior disciplinary history.⁶⁵ In January 2005, he was censured and fined \$6,000 by the Missouri Secretary of State, Securities Division, for failing to timely amend his Form U-4 disclosing a customer complaint; filing a Form U-4 application for registration through the CRD system that contained a statement that was false and misleading in a material respect; and failing to amend his Form U-4 disclosing the customer complaint therefore making a false or misleading statement in a filing with the Securities Division.⁶⁶

Finally, Haq's unauthorized and excessive trading was qualitatively egregious. The evidence of Haq's misconduct was strong. KS's testimony was credible and uncontradicted. Haq's conduct was intentional and motivated only by selfish interests.

Enforcement requests that the Hearing Panel impose a bar on Haq for both his egregious unauthorized and excessive trading. In addition, Enforcement requests that Haq be ordered to make full restitution to KS. The Hearing Panel agrees that bars and restitution are necessary to protect the investing public. Haq will also be ordered to pay costs.

Conclusion

Iftikhar Ul Haq is barred from associating with any member firm in any capacity and ordered to make restitution to customer KS in the amount of \$66,184.47, plus interest at the rate specified by 26 U.S.C. § 6621(a)(2), calculated from June 30, 2004 (the date of the last unauthorized trade) until paid, for unauthorized and excessive trading, in violation of NASD Conduct Rules 2310 and 2110. He is also assessed costs in the total amount of \$1,546.30, consisting of a \$750 administrative fee and a \$796.30 transcript fee.

⁶⁵ *Id.*, Principal Consideration No. 2.

⁶⁶ CX-15.

The bars shall become effective immediately if this Decision becomes the final disciplinary action of FINRA.

SO ORDERED.

Alan W. Heifetz
Hearing Officer

Iftikhar Ul Haq (Via First Class Mail & Overnight Courier)
Samuel L. Barkin, Esq. (Via First Class & Electronic Mail)
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