

**NASD OFFICE OF HEARING OFFICERS**

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

Respondent.

Expedited Proceeding  
No. ARB040051

Hearing Officer – DRP

**DECISION**

September 26, 2005

**Respondent failed to demonstrate a *bona fide* inability to pay an NASD arbitration award. In accordance with Article VI, Section 3 of NASD By-Laws and NASD Procedural Rules 9554 and 9559(n), Respondent’s registration is hereby suspended.**

*Appearances*

Carole R. Sherman, Regional Attorney, Los Angeles, CA (Rory C. Flynn, Of Counsel) for the Department of Enforcement.

Respondent, *pro se*.

**DECISION**

**I. Introduction**

By letter dated December 8, 2004, NASD’s Office of Dispute Resolution notified Respondent that his registration would be suspended in accordance with NASD Procedural Rule 9554, as a result of his failure to pay the arbitration award rendered in NASD Arbitration No. 03-03389. On December 28, 2004, Respondent requested a hearing.

Pursuant to Rules 9559(d)(1) and 9559(d)(5), the Hearing Officer conducted a hearing by telephone on February 25, 2005. The parties offered ten joint exhibits and a joint stipulation of facts (Stip.).<sup>1</sup> Respondent testified on his own behalf.

Respondent concedes he has not paid the arbitration award. (Stip.) He contends that he is financially unable to do so, while Enforcement argues that Respondent did not establish a *bona fide* inability to pay. After a review of the entire record, the Hearing Officer finds that Respondent failed to demonstrate a *bona fide* inability to pay the arbitration award. Accordingly, his registration shall be suspended.

## **II. Background**

Respondent entered the securities industry in February 1998 and has since been employed by and registered with NASD through various member firms.<sup>2</sup> On May 7, 2003, [Firm N]<sup>3</sup> (Claimant) filed an arbitration case against Respondent. On or about October 26, 2004, a Stipulated Award (Award) was rendered, under which Respondent was held liable to pay \$188,496 to Claimant, plus interest at the rate of 1.81% per year. That same day, NASD Dispute Resolution sent a letter to Respondent to notify him of the Award and to outline his responsibility to pay the award within 30 days. Respondent received that letter. Subsequently, by letter dated December 8, 2004, NASD's Office of Dispute Resolution notified Respondent that he would be suspended for failing to pay the award, and he requested a hearing, as described above. (Stip.; Tr. 35; JX-1; JX-2; JX-3; JX-6; JX-7.)

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<sup>1</sup> JX refers to joint exhibits. Tr. refers to pages of the hearing transcript.

<sup>2</sup> He currently is registered with member firm Stephens Inc. (JX-1).

<sup>3</sup> This company was acquired by SunTrust Capital Mortgage during the course of these proceedings. (Tr. 7).

### III. Discussion

NASD's arbitration process is designed to provide efficient resolution of disputes involving NASD members, their employees and the public.<sup>4</sup> To ensure compliance with arbitration awards, NASD has promulgated rules to allow for expedited suspension proceedings against members and associated persons for failing to abide by such awards.<sup>5</sup>

A respondent may assert certain limited defenses in an expedited suspension proceeding. These include: (1) the award has been paid in full; (2) the parties have agreed to installment payments of the amount awarded or have otherwise agreed to settle the action; (3) the award has been modified or vacated by a court; (4) a motion to vacate or modify the award is pending in a court; (5) the respondent has a bankruptcy petition pending in U.S. Bankruptcy Court pursuant to Title 11, or the award has been discharged by a U.S. Bankruptcy Court.<sup>6</sup> A respondent may also assert a *bona fide* inability to pay the award.<sup>7</sup> Here, Respondent claims a *bona fide* inability to pay.<sup>8</sup>

The burden is on the respondent to establish the alleged inability to pay, "because the scope of his assets is particularly within [his] knowledge."<sup>9</sup> When respondents raise this defense, NASD is entitled to make a searching inquiry into their assertions.<sup>10</sup>

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<sup>4</sup> *Eric M. Diehm*, Exchange Act Release No. 33478, 1994 SEC LEXIS 148, at \*4 (Jan. 14, 1994) (internal citation omitted).

<sup>5</sup> NASD By-Laws, Article VI, Section 3; NASD Procedural Rule 9550, *et seq.* See also Notice to Members 00-55 (August 2000) and 04-36 (May 2004).

<sup>6</sup> NASD By-Laws, Article VI, Section 3; NTM 00-55.

<sup>7</sup> See, e.g., *William J. Gallagher*, Exchange Act Release No. 47501, 2003 SEC LEXIS 599 (Mar. 14, 2003).

<sup>8</sup> Though he has not done so, Respondent considered filing for bankruptcy as a defense to this proceeding and to avoid his responsibility for paying the Award. (Tr. 21-23.)

<sup>9</sup> *Bruce M. Zipper*, Exchange Act Release No. 33376, 1993 SEC LEXIS 3525, at \*8 (Dec. 23, 1993).

<sup>10</sup> *Daniel Joseph Avant*, Exchange Act Release No. 36423, 1995 SEC LEXIS 2816, at \*11 (Oct. 26, 1995); *Zipper*, 1993 SEC LEXIS 3525, at \*8.

Accordingly, by letter dated December 29, 2004, Enforcement asked Respondent to provide specific information and documentation that was necessary to assess his financial condition. Further, on January 4, 2005, the Hearing Officer ordered Respondent to file a standard financial disclosure statement and supporting documentation by February 4, 2005. Respondent supplied Enforcement with some of the requested information by that deadline; he did not, however, comply fully with Enforcement's request. Moreover, he did not file any of the information with the Office of Hearing Officers (OHO), as ordered. His financial information was filed with OHO by joint exhibit submitted by Enforcement. (Tr. 32, 41; JX-8; JX-9.)

Enforcement advised Respondent, by letter dated February 10, 2005, that the information he had provided was deficient. That letter further instructed Respondent about the additional information he needed to produce. Subsequently, Respondent discussed this matter with Enforcement by telephone and promised to supply all missing documents. Nonetheless, Respondent failed to provide additional information or documentation. He explained at the hearing that he did not tender additional information, because he had been trying to work out a settlement agreement with the Claimant and thought it would be final before the hearing.<sup>11</sup> (Tr. 6-8, 13, 20-21, 23-24, 30-31, 41; JX-10.)

The Hearing Officer reviewed all of the documents supplied by Respondent, which included some wage records, a W-2 statement and 1099 form from 2003, a past-due notice from Respondent's mortgage lender, an invoice and bill of sale from Ford Motor Credit Company, a past-due notice for Respondent's escrow account from which his insurance and property taxes

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<sup>11</sup> The Hearing Officer permitted Respondent to supplement the record by filing documents he claimed to have provided to Enforcement regarding a settlement with the Claimant. (Tr. 14.) During the hearing, Respondent offered to submit documents to substantiate other portions of his testimony. (*See, e.g.*, Tr. 77.) Respondent filed no documents after the close of the hearing, however.

are paid, a default notice regarding Respondent's account with Bank of America, and a document related to his initial purchase of his home.

Respondent's greatest asset and source of equity is his home in Tennessee, which he and his wife purchased in December 2002 for \$800,000.<sup>12</sup> It appears that Respondent currently has significant equity in his home, because he made an initial down payment of \$80,000 in December 2002 and an additional \$125,000 payment in March 2003, when he refinanced the home. Respondent neither alleged a decline in the home's value, nor submitted any information as to the home's current market value. The home's initial market value is also unknown, because, despite Enforcement's requests, he also failed to provide a copy of the initial appraisal or copies of the applications for his first or second mortgage. (Tr. 43-44, 61-62, 84; JX-9, pp. 34-35.)

Respondent claimed to be nine months in arrears on his mortgage obligations for his residence. To support this assertion, Respondent tendered a past-due notice from his mortgage lender showing that he and his wife owed \$51,441.18, for failure to make payments from July 1, 2004 through December 1, 2004.<sup>13</sup> The letter stated that failure to pay \$59,824.19 prior to December 30, 2004 will result in sale of the property under foreclosure. Respondent testified that he "continued not to be able to make that payment ... [and his] deficiency has increased." He did not provide any documentation about the status of this debt as of January or February of this year, however, and admitted that no foreclosure proceedings have been initiated. Finally, Respondent testified that he tried, without success, to sell his home to satisfy these and other

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<sup>12</sup> Respondent owns no other real property other than his personal residence. Within the past three years, he owned two other homes, which, according to Respondent, collectively resulted in neither gain nor loss upon sale, though he provided no documentation to support his testimony. (Tr. 50-51, 60-61.)

<sup>13</sup> At the hearing, Respondent pointed to a document that showed, as of December 20, 2004, that he owed \$21,157.32 on an escrow account from which his real estate taxes and insurance premiums are paid. (Tr. 25; JX-9, pp. 27-29.)

past-due financial obligations, but he supplied no documents to corroborate this assertion. (Tr. 24-30; JX-9, pp. 25-26.)

Respondent is the sole wage earner in his family. His wife has never been employed or had any source of income during their marriage. He testified that his annual income for 2004 was approximately \$44,000. He provided wage records from March 1, 2004 through January 31, 2005, establishing that his net income from Stephens Inc. for that eleven-month period was \$42,064.41. Although it is clear Respondent did not use that money to make his mortgage payments in late 2004, he provided no evidence of how that money was spent. In fact, he was asked to list his average monthly expenses and to produce copies of his statements and bills to substantiate his expenses; nonetheless, Respondent did nothing more than turn over evidence of a debt of nearly \$3,000 owed for overdrawing his checking account and point to evidence of wage garnishment for October and November 2004, in the amount of approximately \$1,100 owed to an interior decorator. (Tr. 44-46, 48, 65-66, 68-71; JX-9, pp. 8-18, 33.)

According to Respondent, his 2003 income was approximately the same as in 2004.<sup>14</sup> He testified that he earned approximately \$480,000 in 2002. Respondent offered no copies of his federal tax returns for 2002 and 2003, claiming he neither filed returns with the IRS for those years, nor filed for extensions. While he testified that he intends to submit a settlement offer to the IRS, he has yet to do so, and thus could not provide a copy of that offer to the Hearing Officer. (Tr. 48-49, 59-60, 72-74; JX-9, pp. 5-7.)

Respondent claims he owns no single item of personal property worth \$1,000 or more, though he and his wife jointly own one vehicle, a 2003 Ford Expedition, financed through Ford Motor Company for approximately \$52,000 on March 26, 2003. Respondent failed to provide

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<sup>14</sup> Based on documents Respondent provided, his gross income in 2003 was approximately \$53,500. (Tr. 71-74; JX-9, pp. 5-6.)

any evidence of the vehicle's current market value, but he did show that as of February 10, 2005, the payoff on the loan was \$23,099.72. He also failed to supply the application for the car loan, despite Enforcement's requests to provide it. Respondent pays \$600 per month on that loan, and that account is in good standing. (Tr. 51-52, 63-64, 78-79, 84; JX-9, pp. 21-22.)

Respondent testified that he does not have any investment accounts, aside from his 401(k) retirement account, which currently has a balance of about \$900.00. However, he provided no documentation to confirm that balance. The only evidence pertaining to the account are his 2004 wage statements, which show that approximately 2% of his monthly pay is contributed to the 401(k) account. (Tr. 53, 55; JX-9, pp. 8-18).

Finally, Respondent claims to have no bank accounts as of December 2004. He testified that Bank of America closed his account; however, his pay statement for January 31, 2005 shows that he was paid by direct deposit to a checking account.<sup>15</sup> The account number to which his direct deposits were made differs from the Bank of America account that closed. Respondent's unsubstantiated explanation for that discrepancy was that his earnings are directly deposited to his mother-in-law's bank account. Respondent provided no records from that particular account. (Tr. 80-82; JX-9, pp. 31-32.)

An inability to pay defense may be rejected when the evidence provided by a respondent is insufficient or incomplete,<sup>16</sup> or it appears that the respondent could divert funds from other expenditures to pay the award, or could borrow the funds, or could make some meaningful payment toward the award from available assets or income, even if he is unable to pay the full

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<sup>15</sup> The record discloses that Respondent's paychecks were directly deposited to a checking account (Number \_\_\_\_\_) from April 30, 2004 to January 31, 2005. (JX-9, pp. 9-18.)

<sup>16</sup> *Gallagher*, 2003 SEC LEXIS 599, at \*\*9-12.

award.<sup>17</sup> With these standards in mind, the Hearing Officer finds that Respondent did not meet the burden of proving a *bona fide* inability to pay the award.

Respondent failed to provide many documents bearing on his financial situation, and many of the records he supplied were incomplete. Particularly troubling is Respondent's failure to explain how he spent his income for the past three years. Moreover, he was given an opportunity to supplement the record by Enforcement. In response, he stated he would send additional documentation. He did not. The Hearing Officer also afforded him an opportunity to submit documents post-hearing. He did not. These facts suggest that Respondent provided documents that would maximize his liabilities or financial problems and failed to submit documents that would reveal his assets or creditworthiness or show questionable expenditures.<sup>18</sup>

Without complete information and documentation, the Hearing Officer is unable to ascertain Respondent's true financial situation, and for that reason alone, Respondent has failed to meet his burden of proof. The record nonetheless shows that Respondent has assets he could

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<sup>17</sup> *Dist. Bus. Conduct Comm. v. Escalator Securities, Inc.*, No. C07930034, 1998 NASD Discip. LEXIS 21 (NBCC Feb. 19, 1998); *Dist. Bus. Conduct Comm. v. Cruz*, No. C8A930048, 1997 NASD Discip. LEXIS 62 (NBCC Oct. 31, 1997); *Herbert Garrett Frey*, Exchange Act Release No. 39007, 1997 SEC LEXIS 1796 (Sept. 3, 1997); *Michael H. Novick*, Exchange Act Release No. 37503, 1996 SEC LEXIS 1994 (July 31, 1996); *Dist. Bus. Conduct Comm. v. Zipper*, No. C07910138, 1994 NASD Discip. LEXIS 194 (NBCC Oct. 31, 1994), *aff'd*, Exchange Act Release No. 35606, 1995 SEC LEXIS 981 (Apr. 17, 1995).

<sup>18</sup> Respondent asserted that he did not supply complete documentation because he had reached a settlement with Claimant a week before this proceeding. He was required, however, to provide financial documents to Enforcement and OHO before the purported settlement occurred. For this reason, his explanation lacks merit. It also lacks credibility, as he did not inform OHO of any settlement until the start of the proceeding. According to Enforcement, the sole settlement agreement between the parties occurred in July 2003. Respondent did not comply with the agreement, and the arbitration (and Award) ensued. (Tr. 8-11, 84-88.)

liquidate that would enable him to make at least a meaningful payment towards the arbitration award. For example, he could recapture the equity in his home by selling it.<sup>19</sup>

For these reasons, particularly the lack of adequate and complete documentation regarding Respondent's financial situation, the Hearing Officer finds that Respondent has failed to establish a *bona fide* inability to pay the arbitration award. Furthermore, it appears that Respondent could make some meaningful payment toward the award from available assets, but he has chosen not to do so.

#### **IV. Conclusion**

The Hearing Officer finds, and the parties do not dispute, that Respondent has failed to pay any portion of the arbitration award at issue. The Hearing Officer further finds that Respondent has failed to establish any of the limited defenses permitted by NASD rules or case law and specifically failed to demonstrate the defense he asserted, a *bona fide* inability to pay. Accordingly, Respondent is required to pay the arbitration award.

Pursuant to Article VI, Section 3 of NASD By-Laws and Rule 9559(n), it is hereby ordered that Respondent's registration shall be suspended effective as of the date this Decision is issued, and that such suspension shall continue until he provides documentary evidence to NASD showing that: (1) he has made full payment of the award; or (2) the claimant has agreed to settle the award; or (3) the award has been discharged by a U.S. Bankruptcy Court.

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<sup>19</sup> Respondent's uncorroborated testimony that his attempt to sell his home was unsuccessful is insufficient to demonstrate "that he is incapable of cutting expenses or raising additional capital." *Milton R. Barnes*, Non-Summary Suspension Proceeding, 1998 NASD Discip. LEXIS 55, at \*13 (BOG June 26, 1998).

In addition, a total of \$1,379.25 in costs will be imposed on Respondent, which includes an administrative fee of \$750 and hearing transcript costs of \$629.25.<sup>20</sup>

**SO ORDERED.**

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Dana R. Pisanelli  
Hearing Officer

Dated: September 26, 2005  
Washington, DC

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<sup>20</sup> The Hearing Officer has considered all of the arguments made by the parties. They are rejected or sustained to the extent they are inconsistent or in accord with the views expressed herein.