

NASD OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

Respondent.

Expedited Proceeding
No. ARB040037

Hearing Officer – DRP

DECISION

March 2, 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.

Richard A. Roth, Esq., The Roth Law Firm, PLLC, New York, NY, for the Respondent.

DECISION

I. Introduction

By letter dated September 24, 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. 02-02310. On October 18, 2004, Respondent requested a hearing.

Pursuant to Rule 9559(d)(1) and 9559(d)(5), the Hearing Officer conducted a hearing by telephone on December 20, 2004. The Department of Enforcement offered

eighteen exhibits and a joint stipulation of facts (Stip.).¹ Respondent testified on his own behalf.²

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 was registered with [his former Firm] from January 1996 through March 2003.³ On or about April 19, 2002, [the claimant] filed an NASD arbitration proceeding against the Firm, Respondent, and his partner, [], for unauthorized trading, breach of fiduciary duty, churning, unsuitability, failure to supervise and negligence. Before the award was rendered, the claimant withdrew the claim against the Firm. On or about December 23, 2003, an NASD arbitration panel issued an award against Respondent and his partner, holding them jointly and severally liable to pay \$49,646.53

¹ CX refers to Enforcement's exhibits, which were originally marked as JX or joint exhibits. Tr. refers to pages of the hearing transcript.

² Pursuant to Rules 9559(i) and 9262, a person subject to NASD jurisdiction shall testify under oath or affirmation. Respondent was instructed to file an affidavit regarding the truthfulness of his hearing testimony by December 23, 2005. (Tr. 4-5, 133, 147.) On January 11, 2005, Respondent filed an affidavit "confirm[ing] that [he] was the person on the telephone during the hearing conducted ... on Monday, December 20, 2004." Though Respondent failed to affirm that his testimony was truthful, the Hearing Officer will nonetheless consider Respondent's testimony and afford it the same weight as if it had been given under oath (*Cf. Dist. Bus. Conduct Comm. v. Columbia*, No. C10970029, 1998 NASD Discip. LEXIS 38 (NAC Sept. 11, 1998) (rule requiring witness testimony to be taken under oath does not render unsworn testimony less reliable)). The Hearing Officer notes, however, that Respondent's testimony was often undermined by documents or by his failure to produce relevant documents. For this reason, the Hearing Officer found that Respondent's testimony often lacked credibility.

³ Respondent is currently registered with Ryan Beck & Co.

plus interest and fees. NASD's Office of Dispute Resolution notified Respondent's attorney of the award by letter dated January 7, 2004. (CX-1; CX-3; CX-4; CX-5; Stip.)

Respondent filed a petition to vacate the award in New York State Supreme Court, which was denied by Justice Emily Jane Goodman on September 7, 2004. By letter dated September 24, 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. (CX-5; CX-7; CX-8; Stip.)

III. Discussion

NASD's arbitration process is designed to provide efficient resolution of disputes involving NASD members, their employees and the public.⁴ 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.⁵

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

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

⁵ 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).

by a U.S. Bankruptcy Court.⁶ A respondent may also assert a *bona fide* inability to pay the award.⁷ Here, Respondent claims a *bona fide* inability to pay.

The burden is on the respondent to establish the alleged inability to pay, “because the scope of his assets is particularly within [his] knowledge.” *Bruce M. Zipper*, Exchange Act Release No. 33376, 1993 SEC LEXIS 3525, at *8 (Dec. 23, 1993). Thus, to prove his inability to pay the award, Respondent supplied Enforcement and the Hearing Officer with financial information and documents and offered testimony at the hearing regarding his assets and liabilities.

The Hearing Officer reviewed all of the documents, which included a copy of Respondent’s and his wife’s 2003 joint federal income tax return, showing adjusted gross income of \$291,623.⁸ Respondent also provided an income statement from Ryan Beck & Co. dated November 5, 2004, showing gross income of \$162,833.59 during the first ten months of 2004.⁹ Respondent testified that this tax return and income statement included money he never received. According to Respondent, a portion of his income from Ryan Beck consists of money the firm paid on his behalf to a third party. He offered no

⁶ NASD By-Laws, Article VI, Section 3; NTM 00-55.

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

⁸ This figure includes \$23,292.87 that Respondent’s wife earned in 2003. With this return, Respondent also filed Schedule E to report income from an S Corporation, which indicated total income of \$171,403 from the Firm. (CX-10, pp. 232-233, 242.)

⁹ Respondent testified that his net income from Ryan Beck in November 2004 was \$1,800 and believes it was approximately the same in September and October 2004. Bank statements show that between September 8 and November 5, 2004, Respondent received net income from Ryan Beck totaling \$13,175.34. (Tr. 17; CX-14, pp. 55, 59, 63.)

documentation regarding this loan or the terms of repayment.¹⁰ As of December 2004, Respondent and his wife owed the IRS \$5,525.44 in unpaid taxes for 2003, including penalty and interest. (Tr. 53-55, 73-79; CX-10, pp. 24, 234-235; CX-13, pp. 4-6.)

Respondent testified that he is currently unable to work due to a severe spinal injury he incurred in March 2003. He has tremendous pain and is not very mobile, though he can drive short distances. He is on medication, consisting of painkillers and antidepressants, and has difficulty concentrating; he cannot sit up or stand for any length of time. Respondent submitted some medical bills but admitted that most of his medical expenses have been covered by insurance. He testified that during the previous 18 months, he has spent most of his time in California for health-related reasons. Respondent resides with friends in La Jolla but travels to upstate New York, where his wife and two children still reside, every eight to ten weeks and for major holidays.¹¹ He was visiting his parents in Florida on the date of the hearing. (Tr. 20-21, 27-30, 62-63, 84, 128-129.)

Respondent testified that due to his medical problems, he has not worked in the office in 18 months and that his income is derived from an associate who handles his book of business at Ryan Beck. He testified that he does not have “any money,” his checking account is overdrawn, and his only assets are two retirement accounts (an IRA

¹⁰ Respondent testified that he and his partner from the Firm went out of business after September 11, 2001, and that Ryan Beck & Co. paid U.S. Clearing \$180,000 on their behalf. Presumably, Respondent is responsible for half of the amount, or \$90,000. He did not provide details regarding what percentage of his “income” from Ryan Beck reflects this loan, or whether he pays any interest. He supplied few pertinent details, other than to say the payments were to end in December 2004. (Tr. 73, 77.)

¹¹ Respondent’s CRD address is _____. (CX-1.)

and a 401(k) account) worth approximately \$75,000 combined, but he provided no documentation regarding the retirement accounts.¹² (Tr. 15-16, 21-22, 42.)

Respondent supplied excerpts from monthly bank statements and from several credit card companies. There were several pages missing from his monthly credit card statements, and Respondent failed to supply account statements or information about several other credit cards that appeared on an Equifax credit report dated November 16, 2004. Moreover, he testified that he has at least 30 credit cards and conceded that he did not supply monthly statements for all of them. According to Respondent, he borrows from one credit card to pay another, or as he put it, “borrow[s] from Peter to pay Paul.” (Tr. 24, 87-89, 113; CX-10, pp. 109-110, 112-171; CX-18, pp. 4-10.)

Respondent testified that in 2000, he and his wife purchased the house [in New York] for \$579,000, but he transferred his ownership interest in the property to his wife in order to comply with a prenuptial agreement.¹³ Respondent did not submit a copy of the prenuptial agreement, nor was he able to provide any details about it when questioned by the Hearing Officer. He further testified that he pays \$4,700 in monthly mortgage payments: he and his wife obtained a \$400,000 mortgage when they bought the house, and they obtained a second mortgage for \$100,000 in 2004. Respondent did not supply any document identifying the current market value of the property and testified that he did not know its current value.¹⁴ (Tr. 57-60, 66-71.)

¹² Respondent provided several overdraft notices from [his Bank]. But for one check, the checks were paid and Respondent’s account was charged a service fee. (CX-10, pp. 25-36, 42-52.)

¹³ The transfer occurred in April 2003. (CX-18, p. 3.)

¹⁴ Respondent submitted mortgage statements evidencing a total monthly payment of \$4804.41. (CX-10, p. 212; CX-14, p. 2.)

Respondent testified that he owns a 1989 Dodge truck and that his wife owns two vehicles, a 2002 Chevrolet Avalanche and a 2002 Cadillac. He failed to provide information regarding their current market value but testified that he and his wife make a monthly payment of \$827 for the two new cars. According to Respondent, all three vehicles are in New York. (Tr. 52-53, 55-56, 98-99; CX-17, p. 6.)

Respondent testified that including mortgage and car payments, his family's monthly expenses exceed \$10,000.¹⁵ According to Respondent, he has borrowed thousands from friends and family members, but he supplied no documents to corroborate this assertion, nor an explanation why he needed these loans. Respondent did provide an invoice from counsel showing that he and his partner at the Firm owed The Roth Law Firm \$121,146.95 for representation in the arbitration and other matters. The invoice is dated November 5, 2004, a few weeks after counsel asserted Respondent's inability to pay as a defense in this proceeding. He also provided a document that appears to evidence a \$45,000 loan to his Firm, and documents that appear to show loans totaling \$239,323.15 (including interest) taken against three life insurance policies. (Tr. 84-87, 104-105, 113, 123; CX-10, pp. 205-211; CX-17, pp. 9-11.)

An inability to pay defense may be rejected if 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,

¹⁵ Respondent provided household bills for heating, water/sewer, waste removal and phone (including bills from two wireless providers). (CX-10, pp. 77-86, 172-201; CX-15 pp. 6-12.)

even if he is unable to pay the full award.¹⁶ 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.

To begin, the Hearing Officer notes that Respondent failed to provide many documents bearing on his financial situation, including account statements for his retirement accounts and investment accounts,¹⁷ and that many of the records he supplied were incomplete. For example, he testified that he has at least 30 credit cards, including an American Express card that he uses for travel to and from California, but he failed to produce those records.¹⁸ Of the credit card records he provided, Respondent submitted only one or two pages per monthly statement and omitted dozens of pages. In most cases, Respondent provided the portion of the statement that showed the balance due (which was usually near the credit limit) and omitted pages listing expenditures. These omissions suggest that Respondent provided documents that would maximize his

¹⁶ *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 (April 17, 1995).

¹⁷ Based on some of the records Respondent provided, it appears that he has or had investment accounts. (CX-10, pp. 3-6, 11-15, 18, 20-23, 236, 239.) Respondent testified that he no longer owns any mutual funds. (Tr. 108-111.)

¹⁸ Tr. 91.

liabilities or financial problems and failed to submit documents that would reveal his assets or creditworthiness or show questionable expenditures.¹⁹

Without complete information and documentation, the Hearing Officer is unable to ascertain Respondent's true financial situation,²⁰ and for that reason alone, Respondent has failed to meet his burden of proof.²¹ The record nonetheless shows that Respondent has made no effort to reduce living expenses and has assets he could liquidate that would enable him to make at least a meaningful payment towards the arbitration award. For example, he testified that he has approximately \$75,000 in his retirement accounts. He also has three vehicles in New York but lives in California with friends who provide transportation for him.²²

Respondent testified that he obtains credit cards with lower interest rates in order to pay other credit card bills. Although Respondent argues this shows his inability to pay the award, it actually evidences his ability to obtain credit and make payments as needed.

¹⁹ Though few credit card statements showed actual charges incurred by Respondent, there were some that seemed questionable for someone who contends he has no money or assets and limited physical abilities. For example, on December 16, 2003, there is a charge for \$2,928.25 at Philippe Charriol Boutique in La Jolla, which the Hearing Officer notes is an upscale watch and jewelry store. On July 24, 2004, there is a charge for \$1,023.03 at Focus Camera; Respondent testified that he incurred this charge to purchase a birthday gift for his brother-in-law but claimed he was reimbursed by family members. On September 29, October 8 and October 15, 2004, there are charges totaling \$582.61 for tools and materials to allow Respondent to repair a dent in his 1989 Dodge. (Tr. 95-97, 116-117; CX-10, pp. 118, 151; CX-16, pp. 37-38.)

²⁰ The Hearing Officer further notes that Respondent failed to supply information regarding his wife's assets or her 2004 income, though he included her monthly living expenses in support of his claimed inability to pay.

²¹ At the Hearing Officer's request, Enforcement filed a post-hearing memorandum outlining financial information and documents that Respondent failed to produce. Despite being afforded an opportunity to reply, Respondent did not file a response, nor did he provide copies of any missing documents.

²² Respondent testified that his friends have five vehicles, and he often takes one of their cars when needed. The Hearing Officer notes, however, that credit card records show that on at least one occasion, Respondent rented a vehicle from Thrifty Car Rental in San Diego. (CX-10, p. 118.)

In light of Respondent's testimony that he "feel[s] the judgment [arbitration award]... is totally ridiculous,"²³ the Hearing Officer believes the true issue is Respondent's unwillingness to pay an award he believes is unjust, rather than his inability to pay the award.

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 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, 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

²³ Tr. 126.

award; or (2) the claimant has agreed to settle the award; or (3) the award has been discharged by a U.S. Bankruptcy Court.

In addition, a total of \$1678.20 in costs will be imposed on Respondent, which includes an administrative fee of \$750 and hearing transcript costs of \$928.20.²⁴

SO ORDERED.

Dana R. Pisanelli
Hearing Officer

Dated: March 2, 2005
Washington, DC

²⁴ 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.