FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. JONATHAN M. SKIBA (CRD No. 2265023), Respondent.	Disciplinary Proceeding No. E8A2004072203 Hearing Officer – SNB **HEARING PANEL DECISION** July 6, 2009

For submitting inaccurate annuity applications and failing to submit required annuity replacement forms to his firm in circumvention of firm procedures regarding annuity replacements in four customer accounts, in violation of Rule 2110, Respondent is suspended in all capacities for one year, fined $5,000, required to pay restitution of $14,909.49, and assessed costs.

Appearances

Richard S. Schultz, Esq. and UnBo Chung, Esq., Chicago, IL, for the Department of Enforcement.

Gary M. Saretsky, Esq. and Jonathan M. Sterling, Esq., Birmingham, MI, for Respondent.

DECISION

I. Procedural History

On January 16, 2008, the Department of Enforcement ("Enforcement") filed a one-count Complaint against Jonathan M. Skiba ("Respondent"). The Complaint alleged that Respondent violated Rule 2110 by submitting inaccurate annuity applications and failing to submit required forms to his firm, resulting in the circumvention of firm procedures regarding annuity replacements in four customer accounts. On March 10, 2008, Respondent filed an answer denying the allegations, and requesting a hearing. The hearing was held on September 9 and 10, 2008, in Chicago, Illinois, before a Hearing Panel

composed of the Hearing Officer and two members of the District 8 Committee.[1] On November 5 and 19, 2008, respectively, Enforcement and Respondent filed post-hearing submissions.

II. Respondent

From July 1992 through May 2005, Respondent was registered as an Investment Company and Variable Contracts Products Representative with AXA Advisors, LLC ("AXA" or "Firm"). CX-1, Stip. 1. Since May 2005, Respondent has been registered in the same capacity with SIGMA Financial Corporation. Id. Respondent has no prior disciplinary history.

III. Facts

This case involves annuity replacements occurring in four accounts held by two married couples, MR and RR, and LV and VV. The Complaint charges, and Respondent does not dispute, that he submitted inaccurate annuity applications and failed to submit required documentation to his firm, in circumvention of firm procedures. The Complaint does not charge that these replacements were unsuitable or unauthorized.

A. Respondent Submitted Inaccurate Information on Annuity Applications

In early 2003, Respondent's customers, MR, RR, LV and VV, owned shares in Equi-Vest variable annuities ("Equi-Vest"). Stip. 3, 6, 8, 11, 13, 22. During 2003, all or a large portion of these Equi-Vest holdings were sold and the proceeds were deposited in a Franklin Templeton money market mutual fund held in the customers' accounts. Stip. 6, 11, 17, 20, 27, 30. Between 11 to 26 business days thereafter, Respondent liquidated these money market mutual funds and invested the proceeds in another variable annuity, Accumulator Plus ("Accumulator"). Stip. 7, 12, 21, 31.

[1] Enforcement offered Complainant's Exhibits ("CX") 1-67, which were admitted without objection. Tr. 355. Respondent did not offer any exhibits. The hearing transcript is referred to as "Tr." Stipulations are referred to as "Stip. __."

Respondent used the extra step of placing the funds in a money market mutual fund so that it would appear that the source of the Accumulator annuity purchase was a money market fund, not another annuity. Tr. 390. He was thus able to replace his customers' Equi-Vest annuities with Accumulator annuities without discovery by his firm. Tr. 389-90, 395; CX-49 p. 7.

Consistent with his efforts to conceal the transactions from AXA, Respondent completed the Accumulator Purchase Applications for the purchases described above, and answered "No" to the following questions:

> Will any existing life insurance or annuity by (or has it been) surrendered, withdrawn from, loaned against, changed or otherwise reduced in value, or replaced in connection with the this transaction assuming the certificate/contract applied for will be issued?
>
> Do you have reason to believe that any existing life insurance or annuity has been or will be surrendered, withdrawn from, loaned against, changed or otherwise reduced in value, or replaced in connection with the transaction, assuming the certificate/contract applied for will be issued on the life of Annuitant?
> CX-3, CX-15, CX-24, CX-34.

Respondent admitted that these "No" answers were false. He knew that the proceeds from the sale of the Equi-Vest annuities would be used to purchase the Accumulator annuities. Tr. 388-89, 403.

B. Respondent Failed to Submit Replacement Forms in Circumvention of Firm Procedures

In 2003 when the activities at issue took place, AXA had special procedures for a "Replacement Sale," a transaction where a customer sold all or a portion of an existing variable annuity and used the proceeds to purchase another variable annuity. CX-53 p. 3, 19; CX-54 p. 3; CX-55 p. 3. The Firm's Compliance Manual defined a Replacement Sale as the purchase of a new annuity contract when a representative knows or has reason to know that by reason of the new purchase, an existing annuity contract was or would be affected, such as the termination of the initial contract in whole or in part. Stip. 32. The

procedures also stated that a Replacement Sale occurs when a new variable annuity is purchased and, within 60 days before and up to 13 months after its issue date, an existing policy is lapsed or surrendered. CX-56 p. 6. Applying the Compliance Manual's definition to the facts of this case, the purchases of the Accumulator annuities, occurring within 26 days of the surrender of the Equi-Vest annuities, constituted a Replacement Sale.

The Firm required all Replacement Sales to be documented. Specifically, representatives were required to complete a replacement form, signed by the customer and approved by a supervisor. CX-53 p. 13; Tr. 282; Stip. 33. The form disclosed the surrender charges, the new sales charges and expenses, and the withdrawal charge on the new annuity. The form also disclosed that the representative would not receive a commission for the transaction, and that the replacement might not be in the customer's best interest. CX-52 p. 2; Tr. 138. A supervisor would then review the form and determine whether the transfer was suitable for the customer, and, if it was, he or she would sign the form to approve the transaction. Tr. 178-79.

Respondent was aware of these procedures and had followed them in the past. CX-62; Tr. 357-58. However, in this case, Respondent believed that his firm would not approve the replacements, so he did not follow the Firm's procedures. Tr. 451-52. As a result, Respondent's customers did not sign replacement forms, which would have informed them of the surrender charges, that such charges would be less if they held on to their Equi-Vest annuity longer, and that the costs associated with the Accumulator annuity were greater than the Equi-Vest annuity. Tr. 392-93.

Moreover, AXA did not have the opportunity to review the replacements to determine whether they were suitable. Further, because the transactions were not treated as replacements, Respondent received substantial commissions on the purchase of the Accumulator annuities. Respondent received total commissions of $13,136.96 for

Accumulator annuity purchases. Stip 7, 12, 21, 31. He was aware that he would not have received these full commissions if the transactions had been disclosed as replacements. Tr. 359-60, 390. In addition, based upon the commissions he generated on these transactions, Respondent received production credits ("PCs") that entitled him to benefits including health insurance, life insurance, pension benefits, 401(k) benefits or trips. Tr. 275-76. For 2003, Respondent's commissions were between $40,000 and $50,000, so the $13,136.96 in commissions and associated PCs he received for the Accumulator purchases by MR, RR, LV and VV, was a substantial part of the total commissions and PCs he earned that year. Tr. 437-38.

On the other hand, Respondent's customers incurred surrender charges on the sale of the Equi-Vest annuities. MR incurred a charge of $2,950.79, RR incurred a charge of $11,958.70; LV incurred a charge of $6,838.52; and VV incurred a charge of $911.86. Stip. 5, 11, 17, 27.

IV. Violation

Rule 2110 provides that, "[a] member, in the conduct of his [or her] business, shall observe high standards of commercial honor and just and equitable principles of trade."[2] It is well established that falsification of documents and the failure to follow firm procedures, particularly those designed to protect customers, are not consistent with the high standards of commercial honor and just and equitable principles of trade required by Rule 2110. See, e.g., Donald M. Bickerstaff, Exch. Act Rel. No. 35,607, 1995 SEC LEXIS 982 (Apr. 17, 1995).

Here, Respondent does not dispute that he submitted inaccurate annuity applications and failed to submit annuity forms to AXA, in circumvention of its procedures

[2] Rule 2110 is applicable to associated persons pursuant to Rule 0115(a), which provides, "These Rules shall apply to all members and persons associated with a member. Persons associated with a member shall have the same duties and obligations as a member under these Rules."

regarding annuity replacements. Respondent argues, however, that he did so because customers wanted to replace their annuities, and he thought that the Firm would prohibit it. However, a respondent may not disregard a firm's policies and procedures, regardless of his personal views or the wishes of his customers. See Dep't of Enforcement v. Zenke, No. 2006004377701at 5 (OHO May 2, 2008) (appeal pending).[3]

Moreover, although Respondent's customers acknowledged that they wanted to replace their existing annuities with better performing ones, the Panel found that MR and RR, customers who testified at the hearing, had limited investment experience, deferred to Respondent's recommendations, and did not fully appreciate the ramifications of replacing their annuities. Tr. 45-46, 49-53, 58-59, 72, 96-98. This is precisely the issue that the Firm's procedures were designed to address. The Panel found that, by failing to follow the Firm's procedures, Respondent received commissions to which he was not entitled, and deprived his customers of full disclosure about the nature of the new annuities in which they planned to invest, as well as the added protection of a Firm's review of the transaction for suitability.

Accordingly, the Panel finds that by submitting inaccurate annuity applications and failing to submit required forms to his firm, in circumvention of firm procedures regarding annuity replacements in four customer accounts, Respondent violated Rule 2110.

V. Sanctions

The FINRA Sanction Guidelines ("Guidelines") for the falsification of records recommend a fine of $5,000 to $100,000 and a suspension for up to two years where mitigating factors exist, or a bar in egregious cases. Guidelines at 39 (2007 ed.). Applying these guidelines, Enforcement urged that the Panel impose a one-year suspension and a $5,000 fine. Respondent argued that the Guidelines for annuity switching, which provide

[3] This decision is available at www.finra.org/Industry/Enforcement/Adjudication/OHO/index.htm.

for a fine of $5,000 to $75,000 and a suspension of up to one year, should apply. Guidelines at 82. Applying these guidelines, Respondent argued for a suspension of three to six months.[4]

In this case, the charges relate to Respondent's submission of inaccurate applications and failure to follow firm procedures, not the annuity switches themselves. Therefore, the Panel has determined to apply the Guidelines for falsification of records.

The Guidelines' principal considerations for falsification of records include the nature of the falsified document and whether the respondent had a good-faith, but mistaken, belief of express or implied authority. Id. at 39. Here, the falsified documents were significant. If correctly completed, they would have triggered disclosure of the precise ramifications of the replacements to customers, including costs. Moreover, Respondent falsified documents in order to deceive his firm. He also deprived his firm of the opportunity to review the transactions for suitability and reduce or eliminate his commissions.

The Panel also considered that Respondent profited from his misconduct, receiving over $13,000 in commissions; a substantial part of his commissions that year. The Panel also considered that Respondent ultimately acknowledged and regretted his actions, paid a fine of $2,000 to the Firm, agreed to repay commissions to the Firm over time, and was placed on heightened supervision.

However, the Panel was concerned that, although Respondent ultimately acknowledged that he engaged in unauthorized annuity replacements, his earlier testimony at the hearing suggested that it was only a possibility, which exhibited to the Panel a lack of candor and acceptance of responsibility. Compare, Tr. 362-64, 371, 375, 383, 386, 389,

[4] Although the Panel did not apply these guidelines, the one-year suspension that the Panel determined to impose fits within it.

with, Tr. 403. Moreover, Respondent was initially dishonest in denying that he placed RR's initials on an annuity application, only admitting that he did so after repeated questioning.[5] Compare, Tr. 370-71, with, Tr. 435.

Respondent argued that he should not be required to pay restitution in the amount of the surrender charges of $2,950.79 and $11,958.70 paid by MR and RR, respectively, because the customers received a bonus payment for purchasing the Accumulator annuities that almost covered the Equi-Vest surrender charge. However, the Panel found that MR and RR did not consent to the offset of the Accumulator annuity bonus against the Equi-Vest surrender charge. Accordingly, the Panel determined that the bonus was for the customers to keep.

After weighing the evidence, the Panel finds that it is appropriate to suspend Respondent in all capacities for one year. In addition, the Panel finds that a fine of $5,000, payable upon re-entry into the industry, is appropriately remedial. Further, the Panel orders Respondent to pay customers MR and RR restitution of $2950.79 and $11,958.70, respectively. Respondent is also assessed costs.

VI. Conclusion

For submitting inaccurate annuity applications and failing to submit required annuity replacement forms to his firm in circumvention of firm procedures in four customer accounts, in violation of Rule 2110, Respondent is suspended in all capacities for one year, fined $5,000, and required to pay restitution of $14,909.49. In addition, he is ordered to pay costs in the amount of $3,895.28, which includes an administrative fee of $750 and the cost of the hearing transcript. [6] If this Decision becomes the final disciplinary

[5] The change in the terms of the form requiring RR's initials were to the customer's benefit; it permitted him to retain 1% of the Equi-Vest annuity so he would be entitled to a death benefit. Tr. 421-22.

[6] The Hearing Panel has considered all of the arguments of the parties. They are rejected or sustained to the extent they are inconsistent or in accord with the views expressed herein.

action of FINRA, the suspension shall become effective with the opening of business on Tuesday, September 8, 2009, and end with the close of business on Tuesday, September 7, 2010. The fine and costs shall become due and payable when Respondent returns to the industry.

HEARING PANEL

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By: Sara Nelson Bloom
Hearing Officer

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