

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS**

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

WALL STREET STRATEGIES, INC.
(CRD No. 31268),

GARRY N. SAVAGE, SR.
(CRD No. 1195330),

and

LOUIS KARL KITTLAUS
(CRD No. 602059),

Respondents.

Disciplinary Proceeding
No. 2012033508702

Hearing Officer–MC

**EXTENDED HEARING PANEL
DECISION**

September 15, 2015

Respondent Louis Karl Kittlaus made false, exaggerated, unwarranted, and misleading statements in a communication he distributed to the public, in violation of NASD Rules 2210(d)(1)(A), (B), and (D), and FINRA Rule 2010. For these violations, he is fined \$25,000, suspended for two years from associating with any FINRA member firm in any capacity, ordered to requalify by examination before again becoming registered in any capacity in the securities industry, and ordered to pay costs.

The remaining charges are dismissed. The Department of Enforcement did not prove by a preponderance of the evidence that Respondents Wall Street Strategies, Inc. and Garry N. Savage, Sr. (i) made recommendations to customers to purchase securities unsuitable for them, in violation of NASD Rule 2310 and FINRA Rules 2111 and 2010; (ii) distributed misleading sales literature with Kittlaus, in violation of NASD Rule 2210(d)(1)(A) and FINRA Rule 2010; or (iii) failed to establish and maintain a system to supervise registered representatives that was reasonably designed to achieve compliance with applicable NASD and FINRA rules, in violation of NASD Rules 3010(a) and (d) and FINRA Rule 2010.

Appearances

Lane A. Thurgood, Esq., and Frank Mazzarelli, Esq., Rockville, MD, for the Department of Enforcement.

Anthony W. Djinis, Esq., and Paul J. Bazil, Esq., Washington, DC, for Respondents Wall Street Strategies, Inc., and Garry N. Savage, Sr.

Brian K. Duncan, Esq., Sunbury, OH, for Respondent Louis Karl Kittlaus.

I. Introduction

In July 2012, RR, President of a FINRA member firm, received a letter, unsigned but with a signature block with “Karl L. Kittlaus” typed underneath and a letterhead reading “ALTERNATIVE INVESTMENTS COMPANY.” The letter contained a pitch for “alternative investments” and invitation to attend “our next dinner meeting.” Attached to the letter were two pages describing “Renewable Secured Debentures” issued by GWG Holdings, Inc.¹

RR forwarded the letter to FINRA’s Department of Enforcement. Upon receipt of the letter, Enforcement began the investigation that led to this disciplinary proceeding.

Enforcement learned that Karl L. Kittlaus was registered with FINRA member firm Wall Street Strategies, Inc. (“WSSI” or the “Firm”). In the ensuing investigation, Enforcement concluded that Kittlaus was responsible for sending the letter to RR. Enforcement also learned that WSSI, through Garry Savage, the Firm’s President, Chief Executive Officer, and Chief Compliance Officer, had recommended a high-risk alternative investment to a number of customers. The recommendations were for registered debt instruments called Renewable Secured Debentures issued by GWG Holdings, Inc. (“GWG”). GWG purchases life insurance policies on the secondary market at a discount, pays the policy premiums, and collects the face value of the policies upon the death of the insured persons, anticipating it will collect more than it spends to buy and maintain the policies. Enforcement undertook a review of the suitability of the recommendations for the WSSI customers who purchased the debentures, considering their ages, investment objectives, and financial profiles. The review focused on customer account documents, the GWG prospectus, and a fact sheet created by GWG and distributed by Respondents.

II. The Complaint and Answers

The Complaint describes the GWG debentures as a “high-risk, illiquid, alternative investment.”² From January to November 2012, the relevant period, the Complaint alleges that WSSI through Savage recommended the GWG debentures to approximately 13 WSSI

¹ Hearing Transcript (“Tr.”) at 47-48; CX-4.

² Complaint (“Compl.”) ¶ 56.

customers.³ Some of the customers agreed to speak to Enforcement investigators; none, however, said that the investments were unsuitable.⁴ Nonetheless, the first cause of action charges that the recommendations Savage made to nine of the customers were unsuitable based on the customers' overall investment profiles, and violated NASD Rule 2310 and FINRA Rules 2111 and 2010.⁵

The second cause of action charges that a Client Fact Sheet distributed by all three Respondents was misleading because it "falsely stated" that the debentures were secured by life insurance policies, without disclosing that the life insurance policies were not collateral for the debentures, and that the investors' secured interests were subordinate to other creditors.⁶ Distribution of the document allegedly violated NASD Rule 2210 and FINRA Rule 2010.

The third cause of action charges that Kittlaus created and sent the letter that RR received, and that it contains exaggerated, unwarranted claims and unfounded predictions of future performance, in violation of various provisions of NASD Rule 2210 and FINRA Rule 2010.

The fourth cause of action charges that WSSI and Savage failed to fulfill their supervisory responsibilities to ensure the suitability of recommendations to customers, failed to reasonably supervise the activities and correspondence of representatives in five branch offices, and failed to reasonably supervise Kittlaus.⁷

In their Answers, Respondents generally deny the charges. In response to the first cause of action, WSSI and Savage assert that (i) Savage properly reviewed the risks disclosed in the GWG debentures prospectus with all customers, (ii) the customers understood the risks, and (iii) the recommendations were suitable for them. Respondents deny that the Client Fact Sheet was misleading, as alleged in the second cause of action. As for the third cause of action, Kittlaus denies all responsibility for the letter RR received. Finally, WSSI and Savage insist that they fulfilled their supervisory responsibilities in a fashion reasonably designed to achieve compliance with the applicable rules.

III. Summary of Findings

The Extended Hearing Panel finds that the evidence establishes that Kittlaus wrote and distributed the letter ("Kittlaus letter") received by RR, and in it made exaggerated and

³ Tr. 203.

⁴ Tr. 158. All of the customers received promised interest payments and repayments of principal on time.

⁵ Compl. ¶¶ 30-31. This decision refers to and relies on the FINRA and NASD Conduct Rules that were in effect at the time of the alleged misconduct. The applicable rules are available at <http://www.finra.org/industry/finra-rules>.

⁶ Compl. ¶ 60.

⁷ Compl. ¶¶ 66-68.

unwarranted claims and improper predictions of future performance. For this violation the Panel fines and suspends Kittlaus in all capacities.

The Hearing Panel concludes that Enforcement did not establish by a preponderance of the evidence that (i) Savage's recommendations were unsuitable for the nine customers; (ii) the fact sheet that Respondents distributed was misleading; or (iii) Savage and WSSI failed to establish and maintain a supervisory system reasonably designed to achieve compliance with applicable NASD and FINRA rules, failed to properly supervise the activities of WSSI representatives and their correspondence, and failed to reasonably supervise Kittlaus. The Hearing Panel therefore dismisses the first, second, and fourth causes of action.

IV. Respondents Wall Street Strategies, Savage, and Kittlaus

A. Savage and WSSI

Savage entered the securities industry in 1967,⁸ after serving six years with the United States Navy.⁹ He obtained licenses in both insurance and securities.¹⁰ Savage formed WSSI in 1993.¹¹ In that year, Savage focused primarily on selling fixed index annuities, insurance products, and only about five securities.¹²

Savage is WSSI's President, Chief Executive Officer, and Chief Compliance Officer.¹³ In these capacities, Savage supervised six representatives registered with FINRA through WSSI during the relevant period.¹⁴ One of these was Karen Geiger, who joined WSSI in January 2012 and worked with another WSSI registered representative at a branch office located in Akron-Canton, Ohio.¹⁵ Kittlaus joined WSSI shortly after Geiger, in April 2012.¹⁶

At the beginning of 2012, WSSI had branch offices in four locations: Huron, Westlake, and Akron-Canton, Ohio, and Bonita Springs, Florida.¹⁷ During 2012, the Firm did not have an

⁸ Tr. 762.

⁹ Tr. 766.

¹⁰ Tr. 762. CRD records in evidence reflect that Savage was first registered in 1983. CX-2, at 10-11. Savage could not explain why the CRD record in evidence does not reflect his licensures in 1967. Tr. 931-32.

¹¹ CX-1, at 4.

¹² Tr. 933.

¹³ CX-1, at 4.

¹⁴ Tr. 773-74.

¹⁵ Tr. 214-18, 847.

¹⁶ Tr. 306-08.

¹⁷ Tr. 845.

e-mail address or an electronic system of e-mail retention and retrieval. Firm policy prohibited representatives from using their personal e-mail addresses to correspond with customers.¹⁸

B. Kittlaus

Kittlaus has more than 30 years of experience in the securities industry. Starting in 1983, he was employed by 11 firms prior to joining WSSI. He holds Series 6, 7, and 25 registrations.¹⁹

Kittlaus has a disciplinary history. In 1997, his employer discharged him for failing to submit advertising and sales literature to the firm for review and approval.²⁰ The incident led FINRA to issue a Letter of Acceptance, Waiver and Consent (“AWC”) in November 1998. Among its findings, the AWC stated that Kittlaus prepared and delivered a flyer containing “exaggerated, unwarranted and/or misleading” claims to the public without the approval of his firm.²¹

The AWC also stated that Kittlaus failed to include the date the flyer was distributed, failed to make the presentation in the flyer fair and balanced, and included projections of investment returns, in violation of NASD Rules 2210(d)(2) and 2110.²² By the terms of the AWC, Kittlaus accepted a censure and a fine of \$7,500. When he signed the AWC, Kittlaus submitted a handwritten note stating, “I have read the NASD rules concerning broker solicitation and now I understand them.”²³

In early 2012, Kittlaus called Savage to ask about associating with WSSI.²⁴ Based on what he had heard from an acquaintance, Kittlaus understood that Savage offered his customers alternative investments, which interested Kittlaus, who believes such investments are suitable for senior citizens.²⁵

Savage described Kittlaus as “an alternative product salesman” and thought he would be useful to WSSI because the Firm had a number of customers who had experienced capital losses and were interested in recouping them.²⁶ But before hiring him, Savage questioned Kittlaus about the AWC.²⁷ In light of Kittlaus’ disciplinary history, Savage told Kittlaus that he would

¹⁸ Tr. 844.

¹⁹ Tr. 294; CX-3, at 3-6.

²⁰ Tr. 298.

²¹ CX-19.

²² CX-19, at 4.

²³ CX-19; Tr. 303-06.

²⁴ Respondent’s Exhibit (“RX-__”) 55, at 31-32.

²⁵ RX-55, at 33-34.

²⁶ Tr. 783-84.

²⁷ Tr. 781-82.

need to submit all correspondence and “every bit of advertising material” to Savage for approval. Furthermore, Savage required Kittlaus to meet with him “every couple weeks or so.”²⁸

Kittlaus joined WSSI in April 2012. At the time he was located in Illinois,²⁹ where he remained through the summer of 2012. In October, he moved to Naples, Florida, near Savage.³⁰

V. WSSI and the GWG Renewable Secured Debentures

A. Background

At WSSI, Savage decided what securities the Firm’s representatives were permitted to recommend.³¹ Savage frequently received informational materials from issuers. His practice was to review these materials, and when he encountered information about a company that interested him, he would contact the company and ask for a due diligence package.³²

In early 2012, he was looking for income-producing investments with specific maturity dates that offered a better rate of return than was available from certificates of deposit.³³ Sometime in January 2012, Savage saw information about GWG’s renewable secured debentures offering, and he contacted a company field representative to ask for a due diligence package.³⁴ Reviewing the package, Savage noted that GWG had a brief operating history and that the offering was a speculative, high-risk investment.³⁵ Nonetheless, he went on to learn that GWG offered debentures with differing maturity dates and interest rates, which Savage thought would fit the needs of some clients.³⁶ In addition, Savage had experience with life insurance and liked the fact that the GWG debentures are “backed by life insurance policies.”³⁷

Savage’s due diligence review included attending a two-day meeting at the company’s headquarters in Minneapolis and meeting with a local GWG representative who came to Savage’s office.³⁸ Savage reviewed the company’s SEC filings and proxy statements and spoke with GWG’s president when he had questions about particular risks.³⁹ Savage informed himself

²⁸ Tr. 782-83.

²⁹ Tr. 845-46.

³⁰ Tr. 362-63.

³¹ Tr. 778.

³² Tr. 779-80.

³³ Tr. 780-81.

³⁴ Tr. 786-87.

³⁵ Tr. 788-89.

³⁶ Tr. 788.

³⁷ Tr. 938.

³⁸ Tr. 790-91.

³⁹ Tr. 792.

of the value of the life insurance policies GWG purchased and determined that the liquidation value of the policies was sufficient to repay investors if the company were to go out of business.⁴⁰ He also reviewed a third-party valuation of the policies⁴¹ and familiarized himself with DZ Bank, which had extended a \$100 million line of credit to GWG.⁴²

B. Underwriting

On March 5, 2012, Savage signed a participating dealer agreement with FINRA member firm Arque Capital, Ltd. (“Arque”) qualifying WSSI to sell GWG Renewable Debentures.⁴³ As a participating dealer, WSSI agreed to distribute only those sales materials that were authorized and provided by Arque and GWG.⁴⁴

GWG Holdings, Inc. is the issuer of the GWG Renewable Secured Debentures.⁴⁵ GWG is publicly listed with the Securities and Exchange Commission (“SEC”); its SEC registration statement for the debentures became effective in January 2012,⁴⁶ and since then it has filed periodic required financial statements with the SEC that are audited by an independent accounting firm.⁴⁷ GWG purchases life insurance policies on the secondary market from seniors who no longer want or need them.⁴⁸

Arque is GWG’s lead underwriter. One of Arque’s responsibilities is to enlist broker-dealers to sell the debentures.⁴⁹ GWG and Arque together assembled the due diligence package for the debentures.⁵⁰ The package included the prospectus, GWG’s audited financials for the prior three years, GWG’s articles of incorporation and by-laws, the customer subscription agreement, outside counsel opinion letters, and the “Client Fact Sheet.”⁵¹

C. The Offering

The debentures marketed by WSSI in 2012 had maturity dates ranging from six months to seven years, with interest rates ranging from 4.75 to 9.5 percent per year for the longest

⁴⁰ Tr. 793-94.

⁴¹ Tr. 795.

⁴² Tr. 796-97.

⁴³ Tr. 630-31, 797.

⁴⁴ Tr. 798-99; RX-13.

⁴⁵ Tr. 623.

⁴⁶ Tr. 623.

⁴⁷ Tr. 623, 627.

⁴⁸ Tr. 625.

⁴⁹ Tr. 631-32.

⁵⁰ RX-9.

⁵¹ Tr. 634-36, 799; RX-9, at 544-46.

maturities.⁵² GWG buys life insurance policies in the secondary market with the goal of earning returns from the policies greater than the costs required to buy, finance, and service the policies to maturity.⁵³ As explained by a FINRA investigator,

In general terms, they make money by selling the debentures and then the debentures assist in paying the premiums on the life insurance policies. And then when the people that hold the life insurance policies pass away, they'll make the value of the life insurance policy.⁵⁴

As described in the prospectus and summarized in a third-party due diligence report, GWG acquires life insurance policies through its wholly owned subsidiary, GWG Life Settlements, LLC, which purchases the policies. The majority of the policies are then held by GWG DLP Funding II, LLC, a direct subsidiary of GWG Life Settlements.⁵⁵

GWG requires a minimum investment of \$25,000.⁵⁶ The prospectus contains multiple risk warnings. It warns that the policies held by GWG are not collateral for its obligations, and that GWG's collateral might be insufficient to repay investors their principal in the event of default. The prospectus also warns that the debentures are junior to the revolving credit facility of the bank funding GWG.⁵⁷

The first page of the prospectus issued in May 2012 contains a section titled "Suitability Standards." It explains that the debentures "are suitable only as a long-term investment for persons of adequate financial means who have no need for liquidity in this investment." It states that "it may be impossible" for an investor to resell the debentures and that to qualify to invest a prospective purchaser must have both a net worth of at least \$70,000 and income of at least \$70,000, or a net worth of at least \$250,000, exclusive of home, furnishings, and automobiles. It warns that potential purchasers must be able to bear the risks, including lack of liquidity and loss of the entire investment.⁵⁸ The prospectus contains a list of "Risks Relating to Forward-Looking Statements" that appear in the prospectus, followed by 14 pages enumerating in detail the risks associated with investing in the debentures.⁵⁹

⁵² CX-10, at 3.

⁵³ CX-10, at 2.

⁵⁴ Tr. 93.

⁵⁵ CX-10, at 2.

⁵⁶ CX-12, at 7.

⁵⁷ Tr. 80-82; CX-10, at 2, 38.

⁵⁸ CX-10, at 7.

⁵⁹ CX-10, at 21-35.

VI. Kittlaus Made False, Exaggerated, Unwarranted, and Misleading Statements in a Public Communication Regarding the GWG Debentures

A. The Kittlaus Letter

RR received the Kittlaus letter with an attachment describing GWG Renewable Secured Debentures in mid-July 2012.⁶⁰ RR had no knowledge of Kittlaus or Alternative Investments Company.⁶¹ On July 18, 2012, RR forwarded the letter to FINRA's Department of Enforcement because he was concerned that it might violate FINRA's advertising rules.⁶²

The letterhead on the Kittlaus letter reads:

ALTERNATIVE INVESTMENTS COMPANY
TREAT YOURSELF TO A 12.86% RETURN IN YOUR RETIREMENT ACCOUNT

The salutation "Dear Mr. [RR]" is followed by the greeting "Hello neighbor!" It goes on to make a pitch for considering an "alternative investment":

If you are like most investors today your retirement dollars are drifting up and down aimlessly without direction. ... Now Warren Buffet [*sic*] and other financial experts think bonds are headed for a bear market

For the last 32 years we have guided investors into alternative investment away from the daily fluctuation of the stock market. ... Alternative investment takes many forms ... and sometimes it can be investing in a portfolio of Senior citizens insurance policies they no longer want. A 7 Year investment reinvested pays 12.86% annually. A \$100,000 investment guaranteed by almost \$500 million of assets becomes \$ 189,000 in 7 years. Would you be happy with that? I have taken the liberty of including more information on this investment.

... 3 things will happen if you switch some money into alternative investments. You will increase your current income, eliminate your risk of daily fluctuation and create a more predictable financial future.

The Kittlaus letter contains an invitation to "attend our next dinner meeting ... on July 10th." It closes "Sincerely ... L. Karl Kittlaus," identifies Kittlaus as "Founder," and provides a telephone number under his name. The letter contains a footer that says, "Securities offered by

⁶⁰ Tr. 47-49; CX-4.

⁶¹ Tr. 49-50.

⁶² Tr. 50-52.

Wall Street Strategies,” gives the Firm’s Huron, Ohio address, and identifies the Firm as a “Member FINRA & SEPC [*sic*].”⁶³

B. Kittlaus’ Testimony Was Not Consistent or Credible

At the hearing Kittlaus admitted that Alternative Investments Company was a name he gave to his “proprietorship” and used as letterhead on other letters.⁶⁴ In a number of other respects, however, his testimony was inconsistent, contradictory, and not credible.

For example, at the hearing, Kittlaus denied that he prepared or sent the letter,⁶⁵ and claimed that the first time he saw the letter was in January 2013 at an on-the-record interview (“OTR”) Enforcement conducted with him during the investigation of this matter.⁶⁶ But at the OTR he seemed familiar with the letter. For example, he explained that in the sentence, “For the last 32 years, we have guided investors,” the “‘we’ is Alternative Investments.”⁶⁷ He later stated that the sentence means, “I have been in the business of guiding investors for 32 years,” and that “‘we’ meant ‘me’ and not Alternative Investments.”⁶⁸

During the OTR he stated that “almost none” of his letters to clients included the subheading promising a “12.86% RETURN.” But he then claimed, “I don’t use that subheading at all” because the “12.86% RETURN” related to GWG, and that “other investments have other criteria.”⁶⁹

As to the letter’s reference to Warren Buffett, at the OTR Kittlaus explained that “Warren Buffett happens to be in the same business that GWG is in, so that’s why I mentioned his name,” and he specified that the nature of the “business” was buying discounted life insurance policies.⁷⁰ At the hearing, though, he claimed that at his OTR he was just “speculating” about “why somebody would use the name Warren Buffett” in the letter,⁷¹ and that he “would never use language like that.”⁷²

⁶³ CX-4, at 2. “SEPC” is apparently a misspelling of “SIPC,” the Securities Investor Protection Corporation, of which WSSI is a member.

⁶⁴ Tr. 311.

⁶⁵ Tr. 365-66, 368.

⁶⁶ Tr. 366.

⁶⁷ RX-55, at 22.

⁶⁸ Emphasis added. RX-55, at 35-36.

⁶⁹ RX-55, at 28-29.

⁷⁰ RX-55, at 38.

⁷¹ Tr. 336-37.

⁷² Tr. 335-36.

Some of his testimony shifted both during the OTR and from the OTR to the hearing. For example, at his OTR Kittlaus testified that the phone number under the signature block was his. Then he said it was a phone number he “was using” at the time RR received the letter. He then stated it was an office number for an office in Northbrook, Illinois. He shifted again, explaining that “[t]here wasn’t an office, it was just an answering service” that he stopped using after a 90-day period.⁷³ At the hearing, although he claimed he did not recognize the phone number under the signature block,⁷⁴ he also testified that it was his “intention” to use the answering service, but he “[did] not believe [he] used that number at all.”⁷⁵

At the OTR, Kittlaus admitted he held a meeting with customers at Francesca’s, the restaurant site for the dinner meeting that the letter invited RR to.⁷⁶ At the hearing, he only acknowledged that the restaurant named as the site for a dinner meeting was one he “may have used” for meetings.⁷⁷

C. The Kittlaus Letter Is Similar to Other Letters Kittlaus Wrote

At the hearing, Kittlaus admitted that Alternative Investments Company was a name he gave to his “proprietorship” and used as letterhead on other letters.⁷⁸ And the Panel noted striking similarities between the Kittlaus letter and other letters that he wrote. First, the Kittlaus letter is not dated. One of the findings in the AWC Kittlaus signed in 1998 was that he failed to include the date in a flyer he circulated to prospective customers.⁷⁹ He claimed that as a result of the AWC, he had “learned [his] lesson” regarding the need to date materials sent to customers. Kittlaus testified that he has “certainly” included the date on all correspondence since then.⁸⁰

Kittlaus insisted at the hearing, “[m]ost every letter that I send out is dated.”⁸¹ However, in response to a January 2013 Enforcement Rule 8210 request, Kittlaus produced a letter he hand-delivered to the customer who purchased GWG debentures on his recommendation while he was employed by WSSI.⁸² The letter is undated and the letterhead reads “ALTERNATIVE INVESTMENTS.” In addition, it has a footer with a first line identical to the footer in the Kittlaus letter. Both read “Securities offered by Wall Street Strategies,” followed by the Firm’s

⁷³ RX-55, at 20, 31.

⁷⁴ Tr. 314-17; RX-55, at 20-31.

⁷⁵ Tr. 327-28.

⁷⁶ RX-55, at 46.

⁷⁷ Tr. 329-30.

⁷⁸ Tr. 311.

⁷⁹ CX-19, at 4.

⁸⁰ Tr. 326.

⁸¹ Tr. 326.

⁸² CX-33, at 1-2; Tr. 387-89, 400.

Huron, Ohio street address, and “Member FINRA & SEPC”—the same misspelling of SIPC.⁸³ During the OTR, he testified that he included the footer references to FINRA and SIPC in letters he sent out because Savage instructed him to do so.⁸⁴

D. Discussion

The evidence clearly points to Kittlaus as the author of the letter. Nonetheless, Kittlaus argues that the third cause of action should be dismissed because Enforcement failed to prove that he *distributed* the Kittlaus letter. In his counsel’s words, “the fundamental requirement to impute liability on Mr. Kittlaus would be an initial finding that Mr. Kittlaus did, in fact, distribute the letter in question.” Kittlaus argues that although the evidence might suggest that Kittlaus “drafted the letter and that [RR] received the letter,” there is insufficient evidence “to essentially bridge the gap between drafting and receipt.”⁸⁵

The Panel rejects these arguments and finds that Kittlaus wrote and sent the letter to RR. Based on the form of the letter and the fact that RR and Kittlaus did not know each other, the Panel concludes that the Kittlaus letter was one of an unknown number of “Hello neighbor!” letters Kittlaus distributed in July 2012.

E. The Applicable Rules

During the relevant period, communications issued by members to the public were governed by NASD Rule 2210, “Communications with the Public.” NASD Rule 2210(d)(1)(A) required that “[a]ll member communications with the public shall be based on principles of fair dealing and good faith and must be fair and balanced,” give the public “a sound basis for evaluating the facts in regard to any particular ... security,” and not be misleading. Rule 2210(d)(1)(B) prohibited members from making “false, exaggerated, unwarranted or misleading” statements or claims, and from distributing any false or misleading communication. Rule 2210(d)(1)(D) forbade members from issuing communications with the public that predicted or projected performance of an investment, and from making “any exaggerated or unwarranted claim, opinion or forecast.” The Complaint’s third cause of action alleges that the Kittlaus letter violated each of these provisions.

⁸³ CX-33, at 5.

⁸⁴ RX-55, at 30.

⁸⁵ Tr. 1103-04.

F. Kittlaus Violated NASD Rule 2210 and FINRA Rule 2010

Clearly, the Kittlaus letter is a communication with the public as defined by NASD Rule 2210(a), which includes “correspondence.”⁸⁶ On its face, the letter is directed to a prospective customer to interest him in investing in the GWG debentures Kittlaus was promoting.

The Kittlaus letter is not “fair and balanced.” It does not, for example, “disclose in a balanced way the risks and rewards of the touted investment”—the GWG debentures—as required by NASD Rule 2210(d)(1)(A).⁸⁷ It promises significant potential gain without disclosing any risks, including possible financial loss. The letter also fails to provide the reader with any basis, much less a sound one, for evaluating the claims it makes. The promised high rate of return and projection of profitability are not accompanied by any explanation of the assumptions underlying the forecasts.

The Kittlaus letter’s promises of increased income, elimination of the “risk of daily fluctuation,” and creation of a “more predictable financial future” with no mention of the risks inherent to balance these rosy representations,⁸⁸ are exaggerated and misleading, implying an unrealistic certainty of these positive outcomes, in violation of NASD Rule 2210(d)(1)(B).⁸⁹

The Kittlaus letter’s projections of a return of 12.86 percent, and the further prediction that an investment of \$100,000 will grow to \$189,000 in seven years, are impermissible performance predictions that violate NASD Rule 2210(d)(1)(D).⁹⁰ The Kittlaus letter violates this Rule because it mentions no risks and predicts returns with specific percentages and dollar figures without “any explanation of the historical basis for these claims or any proviso that past results are no guarantee of future performance.”⁹¹

Because it is not fair and balanced; does not provide a sound basis for evaluating the factual representations it makes about GWG debentures; contains exaggerated and misleading claims; and makes projections of future performance, the Kittlaus letter violates provisions of NASD Rule 2210 and FINRA Rule 2010.⁹²

⁸⁶ NASD Rule 2211(a)(1)(B) further defines correspondence to include a letter distributed by a member to “fewer than 25 prospective retail customers.”

⁸⁷ *CapWest Securities, Inc.*, Exchange Act Release No. 71340, 2014 SEC LEXIS 4604, at *17 (Jan. 17, 2014) (quoting *Jay Michael Fertman*, Exchange Act Release No. 33479, 51 S.E.C. 943, 1994 SEC LEXIS 149, at *17 (Jan. 14, 1994)).

⁸⁸ Claims of “solid growth” and “reliable income” are misleading without disclosure of risks and violate Rule 2210. *Philippe N. Keyes*, Exchange Act Release No. 54723, 2006 SEC LEXIS 2631, at *12 (Nov. 8, 2006).

⁸⁹ *CapWest Securities*, at *24-25.

⁹⁰ *Id.* at *25-26.

⁹¹ *Id.* at *26.

⁹² *Id.* at *13.

VII. Enforcement Failed to Prove that Savage and WSSI Made Unsuitable Recommendations to Nine Customers

Enforcement alleges in the first cause of action that Savage, and the Firm through Savage, made unsuitable recommendations to nine customers by failing to take into account their financial situations and needs, including their investment objectives, investment experience and knowledge, risk tolerance, liquidity needs, age, liquid net worth, and annual income.

A. The Applicable Suitability Rules

Savage made the recommendations at issue in this case between January and November 2012. As noted above, NASD's suitability rule, NASD Rule 2310, was in effect until July 9, 2012; after that, it was replaced by FINRA Rule 2111. Although differing in language, both rules require that a broker's recommendation of an investment in securities must be suitable to the customer based on the customer's financial needs and circumstances. NASD Rule 2310(a) stated:

In recommending to a customer the purchase, sale or exchange of any security, a member shall have *reasonable grounds* for believing that the recommendation is suitable for such 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. (Emphasis supplied.)

The more expansive but substantively similar language of FINRA Rule 2111(a) states:

A member or an associated person must have a *reasonable basis* to believe that a recommended transaction or investment strategy involving a security or securities is suitable for the customer, based on the information obtained through the reasonable diligence of the member or associated person to ascertain the customer's investment profile. A customer's investment profile includes, but is not limited to, the customer's age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, risk tolerance, and any other information the customer may disclose to the member or associated person in connection with such recommendation. (Emphasis supplied.)

The use of the term "reasonable" in both rules is consistent with the long-established principle that implicit in the suitability rule is the "fundamental responsibility for fair dealing" inherent in all members' dealings with customers.⁹³ Essentially, a recommendation must be

⁹³ *Scott Epstein*, Exchange Act Release No. 59328, 2009 SEC LEXIS 217, at *39 (Jan. 30, 2009) (quoting NASD Rule IM-2310-2(a)(1), which states, "Implicit in all member and registered representative relationships with customers and others is the fundamental responsibility for fair dealing. Sales efforts must therefore be undertaken only on a basis that can be judged as being within the ethical standards of the [NASD's] Rules, with particular emphasis on the requirement to deal fairly with the public.").

“consistent with the customer’s financial situation and needs,” and the customer’s best interests.⁹⁴ Thus, a broker should make a recommendation only after considering information provided by the customer and making a “reasonable inquiry concerning the customer’s investment objectives, financial situation, and needs” so that the recommendation is “not unsuitable for the customer.”⁹⁵ He must also “tailor his recommendations to the customer’s financial profile and investment objectives.”⁹⁶

Informing a customer of the risks inherent in an investment is essential, but risk disclosure alone is insufficient. A broker must make sure that a customer *understands* the risks involved in an investment, and must determine that the investment is suitable considering the customer’s needs and circumstances.⁹⁷ Furthermore, “[a] recommendation is not suitable merely because the customer acquiesces in the recommendation.”⁹⁸ Therefore, a broker must expend reasonable effort to learn a customer’s “financial status, tax status, investment objectives, and any other information,” such as a customer’s age and investment experience, reasonably relevant to making a recommendation.⁹⁹ When a broker fails to discuss the risks and speculative nature of a recommended investment, the customer’s objectives, and the advantages and disadvantages of making an investment, and fails to make reasonable attempts to learn about the customer’s financial status, tax status, and investment objectives, the broker fails to comply with fundamental suitability requirements.¹⁰⁰

A violation of the suitability rule is also a violation of FINRA Rule 2010 requiring adherence to high standards of commercial honor and just and equitable principles of trade.¹⁰¹

B. Savage’s Recommendations

Savage, and through him WSSI, recommended GWG renewable debentures to 13 customers during the relevant period. Enforcement, relying primarily on the customers’ account documents describing their ages, investment objectives, and risk tolerances, alleges that the recommendations were unsuitable for nine of these customers. Eight of these customers testified for Savage at the hearing, two in person and the others by telephone. The customers all confirmed Savage’s testimony that he fully informed them of the risks and speculative nature of

⁹⁴ *Epstein*, 2009 SEC LEXIS 217, at *39-40 and n.24 (quoting *Dane S. Faber*, 57 S.E.C. 297, 310-11 (2004)).

⁹⁵ *Rafael Pinchas*, 54 S.E.C. 331, 341 (1999).

⁹⁶ *Epstein*, 2009 SEC LEXIS 217, at *43 (quoting *F.J. Kaufman & Co.*, 50 S.E.C. 164, 168 (1989)).

⁹⁷ *Dep’t of Enforcement v. Chase*, No. C8A990081, 2001 NASD Discip. LEXIS 30, at *16-17 (NAC Aug. 15, 2001).

⁹⁸ *Dane S. Faber*, 57 S.E.C. 297, 310-11 (2004).

⁹⁹ *Epstein*, 2009 SEC LEXIS 217, at *43.

¹⁰⁰ *Id.* at *44-45; *Faber*, 57 S.E.C. at 305; *Charles W. Eye*, Exchange Act Release No. 29572, 50 S.E.C. 655, 658 (1991).

¹⁰¹ *Wendell D. Belden*, 56 S.E.C. 496, 505 (2003).

the debentures. They all also testified that they believed that the recommendations were suitable for them considering their overall financial situations and their then-current investment objectives.

Based upon the tone and substance of their testimony, and the evidence taken as a whole, the Hearing Panel finds the customers and Savage to be credible. The Panel also finds that Savage's recommendations were consistent with his fundamental responsibilities for fair dealing in his relationships with customers, for making reasonable efforts to inform himself of their financial and tax status, investment knowledge and objectives, and for ensuring that his recommendations were consistent with each customer's age, financial situation, needs, and specific investment objectives at the time of the recommendations. After carefully considering the testimony, as well as the customers' account documents, the prospectus, and other information Savage provided to customers, the Hearing Panel concludes that Enforcement has not proven by a preponderance of the evidence that Savage's recommendations were unsuitable.

1. Customers RB and PB

a. RB's Testimony

RB and PB opened accounts with WSSI in 2009, when RB was 70 and his wife was 67 years old.¹⁰² Their new account forms state that both are retired,¹⁰³ but RB testified that he has practiced his profession for 40 years, and continues to operate his own small firm.¹⁰⁴ When RB opened his account, he told Savage that he had 29 years of investment experience with stocks, bonds, mutual funds, and certificates of deposit.¹⁰⁵ Nonetheless, he described his investment knowledge as "limited" on his account opening document because, he explained, "I don't know everything."¹⁰⁶

The couple estimated their net worth at \$7.3 million, their liquid net worth at \$3.1 million, and their total annual income at \$149,000, although RB testified that in 2009 it was actually about \$275,000.¹⁰⁷ They estimated their risk tolerance at five on a scale of one to ten.¹⁰⁸ On their account financial questionnaire, they described their financial goals and ranked asset protection, along with reducing taxes and increasing income, as highly important.¹⁰⁹ Although

¹⁰² CX-20, at 1.

¹⁰³ RX-28, at 1, 4.

¹⁰⁴ Tr. 409-10.

¹⁰⁵ Tr. 412.

¹⁰⁶ RX-28, at 1; Tr. 428.

¹⁰⁷ RX-28, at 1, 3; Tr. 413.

¹⁰⁸ CX-20, at 1.

¹⁰⁹ The form asks the client to number their goals from one to five in order of importance, but RB instead rated the goals on a scale of one to five, assuming five to be high. RB's form shows fives for asset protection, reducing income taxes, and increasing income. RX-28, at 2; Tr. 431.

their financial objectives in 2012 were not identical to their objectives in 2009, when they filled out the documents, RB testified that preservation of principal is always important to him.¹¹⁰

After opening their WSSI account, RB and PB initially invested in fixed annuities, life insurance, and gas and oil.¹¹¹ In 2012, they had profited from their investments, which affected their objectives. RB testified that he “was interested in making the money grow.”¹¹² Thus, although their investment objectives in 2009 were “Growth/with safety of principal,” he testified that because they had made money from their investments, in 2012 they could make a case-by-case determination of whether or not safety of principal was the controlling objective for any particular investment.¹¹³ At that point, he was looking for an investment that would pay interest “similar to what bank CDs used to pay.”¹¹⁴ This led him to become interested in GWG.

In the spring of 2012, when RB was 73 and PB was 70, Savage reviewed the GWG prospectus and discussed the risks with RB. RB testified that Savage pointed out the risks “time and time again.”¹¹⁵ RB read the prospectus carefully and understood the risky nature of the investment.¹¹⁶ RB testified that he did not need the funds and could afford to lose what he invested in GWG.¹¹⁷

In April 2012, RB and PB invested \$75,000¹¹⁸ in GWG renewable debentures for a six-month term at 4.75 percent interest; at the end of six months, they rolled the investment over for another six months. They received all of the interest payments and recouped their principal. RB believes that he should have continued to invest in GWG.¹¹⁹

During the investigation of this case, FINRA staff contacted RB. RB told the staff that he and his wife had invested because they wanted to do so, and would not have invested if they could not afford to lose the entire \$75,000.¹²⁰ Long before the hearing, in March 2013, RB signed a letter that he assumed someone on Savage’s staff had prepared. He testified that it states

¹¹⁰ Tr. 429-30.

¹¹¹ Tr. 413-14.

¹¹² Tr. 429.

¹¹³ CX-20, at 3; Tr. 431-32.

¹¹⁴ Tr. 423.

¹¹⁵ Tr. 423-25, 427.

¹¹⁶ Tr. 417-18.

¹¹⁷ Tr. 420-21.

¹¹⁸ The investment amounted to approximately 2.4 percent of their liquid net worth.

¹¹⁹ Tr. 415-16.

¹²⁰ Tr. 420-21.

accurately that he understood the risks of investing in the GWG debentures and that the investment was suitable for him and his wife.¹²¹

b. Savage's Testimony

Savage testified that he met with RB approximately once each quarter¹²² and “knew his entire financial position.”¹²³ Savage testified that he advised RB fully of the speculative nature and the risks of GWG. Based upon the couple's liquidity, assets, investment objectives and financial condition, Savage believed their investment in GWG was suitable.¹²⁴

c. Discussion

The Complaint alleges that Savage's recommendation to RB and PB was unsuitable because “their account documents listed their investment knowledge as limited, risk tolerance as moderate, and investment objectives as accumulation of retirement capital and preservation of principal.”¹²⁵ Enforcement notes that RB was 73 when he invested. Because his investment objectives were safety of principal and long-term growth, Enforcement argues that the couple sought a safe investment, like a bank CD. Enforcement notes that the GWG debentures “satisfied none of these” objectives and were “inconsistent with [RB's] objectives, investment experience, and risk tolerance.”¹²⁶

RB, however, testified convincingly that he invested in the debentures because he wanted to do so; he would not have invested if he could not afford to lose the entire amount; and he was fully aware that he could lose the funds. He stated: “[I]f I have money that I'm going to invest and I know I can lose all of it and I can afford to lose all of it and I want to invest in it, that's what I do.”¹²⁷

RB's high net worth, substantial liquid net worth, and significant income support RB's testimony that the couple could afford to lose the funds they invested in the debentures. Furthermore, although their account documents indicate that they had limited investment knowledge, RB had a 29-year history of investing in stocks, bonds, and mutual funds.

RB and PB were not unsophisticated investors who were steered into unduly speculative investments that were contrary to their objectives and interests. The evidence establishes that Savage reviewed the prospectus with them at length and disclosed the risks and speculative

¹²¹ Tr. 422; RX-57, at 9.

¹²² Tr. 885.

¹²³ Tr. 888.

¹²⁴ Tr. 887-89.

¹²⁵ Compl. ¶ 32.

¹²⁶ Enforcement's Post-Hr'g Br., at 16-18.

¹²⁷ Tr. 430.

nature of the debentures; they understood the risks when they invested; and they made a reasoned decision that investing in the debentures was consistent with their investment objectives. Investing in GWG was what they wanted to do with a relatively small portion of their available capital.

For these reasons, the Hearing Panel finds that Enforcement failed to establish by a preponderance of the evidence that Savage's recommendation of GWG debentures to RB and PB was unsuitable.

2. Customer EB

a. EB's Testimony

Customer EB opened his account at WSSI in 2005. He is a priest with a Master's degree in theology from the University of Athens. In 2005, he had been retired for seven years.¹²⁸ His account documents identify his investment objectives as asset protection and preservation of principal, and rank his risk tolerance as "conservative."¹²⁹ EB testified that when he opened his account he had more than 20 years of investment experience with stocks, bonds, mutual funds, variable products, and limited partnerships. He described his investment knowledge as extensive.¹³⁰

EB's new account documents reflect that in 2005 he had a net worth of \$1 million, liquid net worth of \$450,000, an annual income of approximately \$55,000, and no dependents. He had a number of investments: \$190,000 in CDs; \$136,000 in stocks; \$88,000 in mutual funds; and \$100,000 in a limited partnership. The account forms identify his investment objectives as safety of principal, income, and long-term growth. At one time he had ranked his risk tolerance as five on a scale of ten, but later, at Savage's suggestion, he changed it to the more conservative ranking of two.¹³¹

Before purchasing GWG debentures, EB had invested over \$1 million with WSSI in nine fixed index annuities and a REIT.¹³² At first, EB made clear to Savage that he wished to remain in conservative investments. Later, as he observed "things being stabilized" and the growing value of his investments, EB adjusted his objectives. By 2012, when he was 80, EB had improved his financial condition and had a higher tolerance for risk than shown on his 2005 new account documents. In his words, he felt that he could "be a steward of God's gifts, ... maybe

¹²⁸ Tr. 462-63.

¹²⁹ CX-21, at 1, 5; RX-29, at 2.

¹³⁰ CX-1, at 1; Tr. 468-70.

¹³¹ Tr. 469-70, 484, 1007-09; RX-29, at 1-2.

¹³² Tr. 472-74, 890.

earn a few dollars more in certain investments to do ... charities and things of that nature,” so he “opted to take some risks.”¹³³

EB made two investments in GWG. In April 2012, he invested \$50,000 for one year and, in June 2012, he invested an additional \$50,000 for two years.¹³⁴ He received all interest payments on time, and at the end of each term, declined to roll the notes over and instead recouped his principal.¹³⁵

EB confirmed that Savage reviewed the prospectus, subscription agreement, and all the risks with him. EB understood those risks, including the risk of losing his principal and all accrued interest payments. He knew that he would not be permitted to withdraw his principal absent the occurrence of a qualifying exigency. EB testified that he carefully reviewed a letter prepared by Savage’s counsel, which he signed to verify that he believed the investment was suitable and that he understood the risks as described in the prospectus and explained by Savage.¹³⁶

b. Savage’s Testimony

Savage testified that he met with EB three to four times yearly to discuss his financial situation.¹³⁷ In the early years of their relationship, EB invested mainly in fixed index annuities.¹³⁸ At an early meeting Savage noticed that EB had rated his risk tolerance at mid-range. Corroborating EB’s testimony, Savage said he suggested it should be more conservative, so EB changed it to two, consistent with his primary objective of asset protection.¹³⁹

With respect to the GWG debentures, Savage testified that he discussed the risks of GWG and that EB understood them. Savage testified that through his discussions with EB over the nine years of their relationship, he knew EB would be able to withstand the loss of the entire principal, and that the investment was consistent with EB’s investment objectives.¹⁴⁰

c. Discussion

The Complaint alleges that Savage’s recommendation to EB was unsuitable because EB’s account documents identified his objectives as asset protection and reduction of risk, and

¹³³ Tr. 473-74.

¹³⁴ RX-29, at 17, 25.

¹³⁵ Tr. 474-75.

¹³⁶ Tr. 480-81; RX-57, at 22.

¹³⁷ Tr. 889-90.

¹³⁸ Tr. 890.

¹³⁹ Tr. 1008-09.

¹⁴⁰ Tr. 890-91.

the investment constituted 22 percent of his liquid net worth.¹⁴¹ Enforcement argues that Savage should not have recommended GWG to EB because EB was 80 years old with a fixed income and conservative risk tolerance.¹⁴²

However, EB explained that even though he wanted to invest conservatively for the most part, he was “willing to take that risk for that one year” to see if he could “earn a few dollars more” for charitable purposes.¹⁴³ He then purchased additional debentures with a two-year maturity, fully aware of the risks.¹⁴⁴

Furthermore, as Savage knew, EB had more than 20 years of experience investing in stocks, bonds, mutual funds, variable products, and limited partnerships, and an extensive knowledge of investing. With GWG, EB undertook risks that he calculated he could tolerate, and decided to make two \$50,000 investments to devote the proceeds to charity.

Based on the evidence that Savage fully informed EB of the speculative nature and risks of GWG debentures, that EB understood those risks, and considering EB’s financial situation, with a net worth of \$1 million and a liquid net worth of \$450,000, a secure annual income, and lack of dependents, the Hearing Panel concludes that Enforcement has failed to prove by a preponderance of the evidence that Savage’s recommendation to EB was unsuitable.

3. Customer RLB

a. Testimony

Ninety-two years old at the time of the hearing, customer RLB did not testify. He and his wife opened accounts with WSSI in February 2011. RLB was retired, and his investment objectives were protection of principal, long-term growth, and income.¹⁴⁵

Savage met with RLB and his wife quarterly through April 2012, often in the kitchen of their home, and got to know them well.¹⁴⁶ RLB owned real estate, a bar, and restaurants. He was in the process of liquidating these assets.¹⁴⁷ Savage prepared RLB’s tax returns and provided him with estate planning services. RLB had decided to leave his funds to his son.¹⁴⁸

¹⁴¹ Compl. ¶ 32.

¹⁴² Enforcement’s Post-Hr’g Br., at 18.

¹⁴³ Tr. 473-74.

¹⁴⁴ Tr. 474-75.

¹⁴⁵ CX-22, at 1, 3.

¹⁴⁶ Tr. 892-94.

¹⁴⁷ Tr. 892-93.

¹⁴⁸ Tr. 902.

RLB's account documents estimate his net worth at \$1 million, his liquid assets at \$300,000, and his risk tolerance as "1-2" and "5-6" on a scale of ten.¹⁴⁹ Savage testified without contradiction that he knew that RLB had additional liquid assets.¹⁵⁰

In February 2011, RLB purchased a \$200,000 fixed index annuity through his wife's account.¹⁵¹ Subsequently, RLB informed Savage that he had sold one of his properties, put the money in a bank, and wanted to invest it to earn higher interest than the bank paid.¹⁵² Savage told RLB that he would do some research on possible investments.¹⁵³

Several months later, Savage suggested that RLB and his wife consider investing in GWG debentures. Savage gave them the prospectus, explained the debentures, and reviewed the prospectus and the risk factors with RLB. They met more than once to discuss GWG. The redemption feature of the debentures was an important consideration for RLB at his advanced age of 90 years. Under that feature, RLB's disability or death would allow the principal to be released directly to RLB's son with no fee assessed.¹⁵⁴ With RLB and his wife, Savage reviewed all of the risk factors associated with investing in GWG.¹⁵⁵ Savage informed RLB and his wife that they could lose their entire investment and any unpaid interest, and that the debentures were illiquid and did not trade in the secondary market.¹⁵⁶

After a time, RLB called Savage to say that he was ready to invest. RLB and his wife had the prospectus out when Savage arrived at their home. RLB asked again about the redemption feature of the debentures. RLB told Savage he wished to proceed. Savage asked RLB if he would need the principal. RLB informed Savage that he had millions of dollars in real estate that he was in the process of selling. RLB had no mortgage and no debts. RLB decided to invest in a seven-year debenture. According to Savage, RLB said that he did not need the money and intended to bequeath the proceeds to his son.¹⁵⁷ Savage did not make a recommendation as to a specific amount for RLB to invest. RLB had already prepared a check for \$200,000 before the meeting. Savage was satisfied from his knowledge of RLB's finances that he did not need the money.¹⁵⁸ RLB assured Savage that he was comfortable with the investment.¹⁵⁹

¹⁴⁹ CX-22, at 1.

¹⁵⁰ Tr. 1026.

¹⁵¹ Tr. 893-94.

¹⁵² Tr. 895.

¹⁵³ Tr. 895.

¹⁵⁴ Tr. 895-99.

¹⁵⁵ Tr. 895-96.

¹⁵⁶ Tr. 903.

¹⁵⁷ Tr. 897, 901-02.

¹⁵⁸ Tr. 899-901.

¹⁵⁹ Tr. 895-99.

b. Discussion

The Complaint alleges that Savage's recommendation to RLB was unsuitable in part because the investment constituted approximately 66 percent of his liquid net worth, estimated at \$300,000 on his account form.¹⁶⁰ Enforcement argues that the investment was unsuitable because of RLB's age; because he identified safety of principal as one of his investment objectives; and because RLB had previously been unfamiliar with debentures.¹⁶¹

However, the Panel finds that Savage testified credibly that he knew RLB's liquid assets exceeded the \$300,000 estimate in the account document, that RLB was selling substantial real estate and business assets, and that RLB's estimated net worth exceeded \$1 million. RLB took into consideration the redemption feature of the debentures, which would facilitate conveying the principal to his son in the event of his death or disability.

Furthermore, like other customers, RLB signed a letter prepared by Savage's counsel confirming that Savage fully informed him of the risks of the investment, and that he believed it was suitable for him.¹⁶²

In sum, the Extended Hearing Panel concludes that Enforcement failed to prove by a preponderance of the evidence that Savage's recommendation was unsuitable, considering RLB's financial situation, his ability to withstand the loss of the principal, the absence of mortgage or other debt obligations, and his desire to take advantage of the redemption feature to bequeath the principal to his son upon his own disability or death.

4. Customer PC

a. PC's Testimony

Customer PC is a retired charter boat captain, a writer for outdoor magazines, and the former owner of a fleet of five fishing boats and several rental cottages on Lake Erie.¹⁶³ When PC opened his account with WSSI in June 2012, Savage became his third financial advisor over a 30-year history of investing.¹⁶⁴ He had invested in REITs, variable and fixed annuities, pension plans, and life insurance products,¹⁶⁵ and characterized his investment knowledge as moderate.¹⁶⁶ At that time, PC was 69 years old and his new account form identified his risk

¹⁶⁰ Tr. 1026; Compl. ¶ 32.

¹⁶¹ Tr. 1026.

¹⁶² RX-57, at 14. Although the letter was prepared by Savage's counsel, no evidence suggested that RLB was unaware of the letter, or that he did not sign it or adopt its contents.

¹⁶³ Tr. 487-88.

¹⁶⁴ Tr. 511-12.

¹⁶⁵ Tr. 489; RX-31, at 1.

¹⁶⁶ Tr. 500-01; RX-31, at 1.

tolerance as three on a scale of ten; his net worth at \$1 million; his monthly income at \$3,100 and expenses at \$1500, leaving a disposable monthly income of \$1,600; and his liquid net worth at \$60,000 but his liquid assets at \$500,000.¹⁶⁷ His new account form identified “safety of principal” as his investment objective.¹⁶⁸

PC first learned of GWG on an ocean cruise from a pilot who owned a financial planning business; they met playing high-stakes poker.¹⁶⁹ In May 2012, PC sold his last boat and had cash available to invest. In June, when speaking with Savage, PC complained about the volatility of the stock market and about the market-indexed annuities he owned.¹⁷⁰ He told Savage he wanted to get out of the stock market and put some of his money where he could earn a better interest rate than he would by depositing the funds in a bank. PC had some money in a bank account earning one percent, and other funds in fixed annuities earning one to two percent. Savage told him about GWG. PC told Savage that he had already heard about the company.¹⁷¹

Savage reviewed the prospectus and the risks. PC understood that the renewable debentures were illiquid, did not trade in the secondary market, and that he ran the risk of losing his entire investment.¹⁷² He wanted to invest long-term to obtain the maximum interest, so he made two purchases of seven-year debentures in October 2012. One of them was for \$35,000 and consisted of funds he did not need and wanted to invest for his grandson’s college education.¹⁷³ The other was for \$130,000.¹⁷⁴ PC did not need this money, either. PC testified that if he lost the principal, he “had a lot of other things to go fall back on,” including “a bunch of REITs” and “guaranteed income” from a mutual fund. PC testified, “Everything I have is bought and paid for. I don’t need anything. All I do is travel. And have a good time. So there is nothing that I need in the future.”¹⁷⁵

b. Savage’s Testimony

Savage testified that he fully informed PC of the speculative nature of the renewable debentures, and reviewed all of the risks. Savage said he asked PC if he would need the funds he

¹⁶⁷ Tr. 488; CX-23, at 1. PC explained that the liquid net worth figure represented funds invested in annuities that he felt were relatively liquid. Tr. 510.

¹⁶⁸ CX-23, at 1.

¹⁶⁹ Tr. 493.

¹⁷⁰ Tr. 494.

¹⁷¹ Tr. 514-15.

¹⁷² Tr. 497-98, 506-08; RX-31, at 13.

¹⁷³ Tr. 496; RX-31, at 23.

¹⁷⁴ RX-31, at 11.

¹⁷⁵ Tr. 508-09.

planned to invest, and PC told him that he would not. Savage, aware of PC's financial situation, agreed with PC's assessment.¹⁷⁶

c. Discussion

The Complaint, based on PC's account documents, alleges that Savage's recommendation to PC was unsuitable in part because PC is retired, described his risk tolerance as conservative, identified his investment objective as safety of principal, and listed his annual income at between \$25,000 and \$49,999, with estimates of his liquid net worth stated variously as between \$500,000 and \$1 million, \$375,000, and \$60,000.¹⁷⁷ Enforcement argues that PC's testimony shows him to be risk-averse and that he mistakenly considered GWG to be safe, because he compared the risk of investing akin to the chance of a hurricane hitting.¹⁷⁸

However, PC considered Savage's recommendation through the lens of extensive investing experience in REITs, variable and fixed annuities, pension plans, and life insurance products. He testified that he asked Savage for ideas when, after selling a property, he had funds to invest that he did not need and could afford to lose. Like some other WSSI customers, PC had disposable income that he did not want to invest in the stock market and he wanted to place funds where they would earn a higher yield than at a bank. PC's testimony confirmed that Savage reviewed with him the prospectus and risks, that PC fully appreciated the risks, and made a reasoned decision to invest a portion of his assets he felt he could afford to lose.

At the time, PC's net worth was over \$1 million, and he calculated his investments in GWG amounted to approximately 25 percent of his net worth,¹⁷⁹ although in reality it was closer to 15 percent. Considering PC's overall financial circumstances, including substantial assets and an absence of obligations, his particular objectives, and his reasoned decision to invest fully aware of the risks, the Panel concludes that Enforcement failed to prove by a preponderance of the evidence that Savage's recommendation was unsuitable for PC.

5. Customer ED

a. ED's Testimony

Customer ED was 72 years old when he opened an account with WSSI in 2011. His account documents describe his investment knowledge as limited and his investment objectives as safety of principal and income. His estimated net worth was \$1,115,000 and his liquid net worth was \$550,000.¹⁸⁰ ED testified that he had been a credit analyst at the Ford Motor

¹⁷⁶ Tr. 1057-58.

¹⁷⁷ Compl. ¶ 32.

¹⁷⁸ Tr. 513; Enforcement's Post-Hr'g Br., at 19.

¹⁷⁹ Tr. 495.

¹⁸⁰ CX-24, at 5.

Company, where he sold Jaguars and Lincolns for the last 15 years of his career prior to retiring in 2002.¹⁸¹

ED's account documents describe his investment objectives as income and growth, and he testified the documents are accurate.¹⁸² ED initially testified that he had invested previously with Wells Fargo, Smith Barney, Edward Jones, and Bank of America.¹⁸³ In November 2011, his annual income was \$109,000.¹⁸⁴ He had a total of 17 years of investment experience, five years more than reflected on his account opening documents.¹⁸⁵ Savage provided tax planning to ED and used information from ED's tax returns to develop a financial plan for him.¹⁸⁶

ED met with Savage on multiple occasions, and they met two or three times specifically to discuss GWG before ED invested, partly because, as ED testified, he was "skeptical" because he previously "got hurt so many times from the other companies."¹⁸⁷

According to ED, Savage advised ED not to invest as much as he wanted to in GWG renewable debentures.¹⁸⁸ ED testified that he understood that the debentures are illiquid, with no public market, unlike a stock or a bond, and that he risked the loss of his entire investment. Savage reviewed the risks with ED, and ED testified, "I understood the risk."¹⁸⁹ As did other customers, ED signed a letter prepared by Savage's counsel stating that he believed GWG was a suitable investment for his needs, that he understood the risks detailed in the prospectus and explained by Savage, and that he could not take his money out before the maturity date.¹⁹⁰

ED testified that he initially invested \$25,000 in GWG renewable debentures in March 2012.¹⁹¹ Then, because he wanted more dividends, he made an additional \$15,000 investment in July. The first investment was for a four-year term; the second was for a seven-year term.¹⁹²

¹⁸¹ Tr. 518-19.

¹⁸² Tr. 524.

¹⁸³ Tr. 519-20, 522.

¹⁸⁴ Tr. 522-23.

¹⁸⁵ Tr. 523-24.

¹⁸⁶ Tr. 524-25.

¹⁸⁷ Tr. 525-26. Savage learned from ED that he had tried a number of different investments with four different brokers, lost money, and sued the brokers as a result. Tr. 1012-13.

¹⁸⁸ Tr. 528.

¹⁸⁹ Tr. 529-30.

¹⁹⁰ Tr. 533. ED, unlike most of the other customers who testified, stated that he had drafted the letter. Tr. 530-31, 534.

¹⁹¹ Tr. 526.

¹⁹² Tr. 527-28; RX-32, at 15, 24.

When cross-examined by Enforcement, ED's testimony was inconsistent with some of his answers to questions on direct examination. He testified that his sole source of income is Social Security,¹⁹³ and that he needs the dividends from his investments to survive.¹⁹⁴ ED testified that he thought there were no risks associated with GWG renewable debentures¹⁹⁵ and that he trusted Savage to withdraw his principal from GWG if Savage discerned any problems with the company.¹⁹⁶

b. Savage's Testimony

Savage, however, testified that ED did not indicate to him that he needed the GWG renewable debentures' dividends to live. According to Savage, ED is interested exclusively in income-generating investments, and had made numerous other income-generating investments with Savage.¹⁹⁷ Savage denied telling ED that he could retrieve ED's principal for him. Savage testified that he explained that GWG had discretion to decline returning his money if he were to try to withdraw it before the maturity date.¹⁹⁸

Savage also testified that he meets with ED regularly, approximately every two weeks, and that they met three or four times to discuss GWG before ED invested. Savage corroborated ED's testimony that he informed ED that GWG was a speculative investment, with risk of loss of principal. Based on his familiarity with all of ED's financial information, Savage believed ED could afford to lose the funds he invested in GWG.¹⁹⁹ Savage said ED was "looking to draw income and be as safe as he can," which "doesn't mean he has to go to the most conservative" investments, like CDs.²⁰⁰ According to Savage, ED was aware of the risks.

c. Discussion

The Complaint alleges that Savage's recommendation to ED was unsuitable on the basis of ED's identification of safety of principal as an investment objective, his limited investment knowledge, and his net worth and liquid net worth, as described in his WSSI account documents.²⁰¹ Enforcement relies on ED's statements under cross-examination that he understood GWG to be an investment for senior citizens to provide monthly dividends, that Savage could retrieve his principal from GWG in the event Savage discerned that the company

¹⁹³ Tr. 539.

¹⁹⁴ Tr. 535.

¹⁹⁵ Tr. 534-35.

¹⁹⁶ Tr. 538-39.

¹⁹⁷ Tr. 1011-12, 1054.

¹⁹⁸ Tr. 1012, 1055-56.

¹⁹⁹ Tr. 1053.

²⁰⁰ Tr. 1012-13.

²⁰¹ Compl. ¶ 32.

was in trouble, and that ED needs the dividends to survive because he has no other sources of income than Social Security.²⁰²

Although ED did make such statements, he initially testified that Savage informed him of the risks and speculative nature of GWG, and that before he invested he fully understood the risks, including the risk of losing his principal, and believed the investment was suitable to his needs and objectives.

It was only when Enforcement repeatedly questioned him about the risks of GWG that ED appeared to react and to become concerned about his investment, asking his own question: “Tell me something ... GWG, are they in trouble?”²⁰³ That was when ED stated that he depended on the interest income, and that he had thought GWG was a safe investment designed to provide monthly dividends to senior citizens at no risk²⁰⁴—the statements Enforcement emphasizes in its argument.

By his own account, ED’s investment experience was extensive. It spanned 17 years, during which ED worked with a number of investment advisors, some of whom, he told Savage, he had successfully sued when he became unhappy with their advice. ED’s testimony and his background suggest that he has a sophisticated grasp of investing and its risks. This experience and sophistication, coupled with the evidence that he met on multiple occasions with Savage about GWG, belie the statements ED made on cross-examination. Finally, ED’s financial circumstances, given his net worth and other investments, do not support his claim that he depended for his survival on GWG’s interest payments.

The Panel found Savage to be credible in his detailed description of carefully reviewing the prospectus with ED in a series of meetings and explaining the risks. Savage’s description of his disclosures of risk and explanation of the nature of the investment is consistent with his testimony of how he presented GWG to his other clients, who corroborated Savage’s testimony. So did the testimony ED gave in his direct examination.

For these reasons, the Panel concludes that Enforcement did not establish by a preponderance of the evidence that Savage’s recommendation to ED was unsuitable, considering his financial situation, investment objectives, and investment sophistication.

²⁰² Enforcement’s Post-Hr’g Br., at 20-21.

²⁰³ Tr. 531.

²⁰⁴ Tr. 534-35.

6. Customer AL

a. AL's Testimony

Customer AL was 81 years old when he opened an account with WSSI in April 2011.²⁰⁵ AL describes himself as the “unofficially retired” owner of two construction companies, one of which does more than \$5 million of business annually, and the other approximately \$30 million.²⁰⁶ His account documents describe his objectives as growth and safety of principal, and estimate his liquid assets at \$5 million, his annual income at \$180,000, and his net worth at \$9 million.²⁰⁷ However, he believes his net worth is “understated” because a portion of his assets consists of real estate that he valued at less than its market value.²⁰⁸

After obtaining financial information from AL, Savage presented him with several investment opportunities. AL invested in some and declined to invest in others.²⁰⁹

AL met with Savage three or four times before investing in GWG. In May 2012, he made two investments totaling approximately \$958,000 in GWG debentures with seven-year terms.²¹⁰

AL testified that Savage provided him with a prospectus and discussed it. AL understood the risk of loss and the speculative nature of the debentures.²¹¹ Indeed, as he put it, AL assumes that “[a]ny investment you make is speculative.”²¹² Savage talked with AL about whether he needed the money, and AL said he did not. That is part of the reason he elected to purchase debentures with a seven-year maturity date.²¹³ In AL’s words, he did “not think that seven or eight percent” of his total net worth invested was inappropriate²¹⁴ because he has “always invested a portion of [his] money any way [he] wanted to.”²¹⁵ AL testified that it was he who decided on the amount invested, based on the fact that he “had the money ... it wasn’t doing [him] any good,” he “did not foresee the need for using this money,” and the seven-year notes could earn substantial interest.²¹⁶

²⁰⁵ RX-33, at 1.

²⁰⁶ Tr. 559-60.

²⁰⁷ CX-25, at 1, 3.

²⁰⁸ Tr. 563.

²⁰⁹ Tr. 564-65.

²¹⁰ RX-33, at 13, 19.

²¹¹ Tr. 567-68.

²¹² Tr. 568.

²¹³ Tr. 569.

²¹⁴ Tr. 569.

²¹⁵ Tr. 577.

²¹⁶ Tr. 566-67.

b. Savage's Testimony

Savage confirmed that he gave AL a copy of the prospectus and told him that GWG was a speculative investment with a high risk of loss. AL took the package of materials home. As a result of reviewing the materials with AL, Savage concluded that the debentures were consistent with AL's risk tolerance and investment objectives, and that AL understood the risks but wanted to make the investment anyway.²¹⁷

c. Discussion

The Complaint alleges that Savage's recommendation to AL was unsuitable because it constituted slightly less than 20 percent of AL's liquid net worth, and AL, an 82-year-old retiree, listed his investment objectives as growth and safety of principal, with investment experience limited to owning stocks and bonds.²¹⁸ Enforcement argues further that AL, who liquidated IRAs to finance his GWG investments, was seeking a safe investment because, when asked how risky he thought it was, AL replied that he thought the risk was "about the same as ... getting run over by a semi when I'm sitting in my car or something like that."²¹⁹

However, in his testimony, AL presented as an astute, successful businessman, with considerable prior investment experience, accustomed to making up his own mind about taking risks and investing a portion of his wealth that he does not need. AL testified that he was unsatisfied with the lack of return of funds in IRAs at other brokerages and, after speaking to Savage, elected to move the money to GWG, fully aware of the risks. AL corroborated Savage's testimony that Savage presented the prospectus to AL and reviewed the risks and speculative nature of the debentures. It is clear that AL could afford to lose the principal. Under these circumstances, the Panel concludes that Enforcement failed to establish by a preponderance of the evidence that Savage's recommendation to AL was unsuitable.

7. Customer DZ

a. Testimony

Customer DZ, a 47-year-old schoolteacher, is AL's daughter. DZ has given her father power of attorney over her funds.²²⁰ As did AL, DZ had an investment account with a Wall Street firm. According to AL, because it was depreciating, he spoke with Savage about investing a portion of those funds in GWG.²²¹

²¹⁷ Tr. 1051-52.

²¹⁸ Compl. ¶ 32; Enforcement's Post-Hr'g Br., at 21.

²¹⁹ Enforcement's Post-Hr'g Br., at 21, quoting Tr. 579-80.

²²⁰ Tr. 570-71. DZ did not testify at the hearing. AL, her father, testified as to his role in her investment.

²²¹ Tr. 570-71.

Savage testified that AL referred DZ to him. She opened her account in July 2012. Savage met with DZ and AL together. According to Savage, DZ needed retirement planning advice, and he spent the meeting reviewing her financial information and discussing her investment goals. At a subsequent meeting, Savage discussed a fixed annuity with her because he felt it was the best retirement investment for her. At AL's request, Savage discussed GWG with her as well. It was during the second meeting that DZ informed Savage that she had approximately \$925,000 to invest. Her father had given her the funds. DZ and AL talked over alternatives, and they informed Savage that they wanted her to invest \$810,000 in a fixed income annuity. AL suggested that DZ purchase GWG debentures with the remaining \$115,000.²²²

DZ's new account form estimates her approximate net worth at \$1.2 million, her liquid net worth at \$810,000, and shows her annual income to be \$80,000. The form characterizes her risk tolerance as conservative, ranking one on a scale of ten, her investment knowledge as limited, and her investment objectives as long-term growth and safety of principal.²²³

Savage gave DZ a GWG prospectus and told her of the illiquidity of the debentures and the risk of loss of interest and principal. He asked about her need for the funds prior to maturity and learned that she "has plenty of money" and that her father planned to give her an additional one million dollars. Savage did not recommend GWG to her.²²⁴ AL did.

AL and DZ discussed GWG with Savage present, and during the discussion DZ asked Savage a number of questions about the debentures.²²⁵ Savage probed DZ about the discrepancy between her conservative risk tolerance—one on a scale of ten—indicated on her new account form, and the level of risk of the debentures. This prompted Savage to tell DZ that the debentures presented a level of risk of ten on a scale of one to ten, not one, where she placed her risk tolerance. Nonetheless, DZ wanted to invest in the debentures. Savage testified that DZ's investment objective changed for this investment.²²⁶ This is reflected on an additional form, "Addendum C – Additional Suitability for Alternative Investments," on which DZ indicated her risk tolerance was moderate, her time frame ten years, and that she had no need for the money.²²⁷

In August 2012, DZ invested \$115,000 in GWG renewable debentures with a maturity date of seven years.²²⁸

²²² Tr. 907-09.

²²³ RX-36, at 1.

²²⁴ Tr. 909-10.

²²⁵ Tr. 1020.

²²⁶ Tr. 1023.

²²⁷ RX-36, at 2.

²²⁸ RX-36, at 7.

b. Discussion

The Complaint alleges that Savage's recommendation to DZ was unsuitable because of her risk tolerance, investment objectives, net worth, and income, and because her \$115,000 investment constituted over 14 percent of her liquid net worth.²²⁹ Enforcement also argues that the investment was inconsistent with DZ's limited investment experience. In addition, her account documents demonstrate that DZ, a schoolteacher, "was seeking safe, conservative investments."²³⁰

The Panel notes that AL, not Savage, recommended the investment to DZ. Nonetheless, once DZ asked questions about GWG, Savage, as established by his testimony and corroborated by AL's testimony, reviewed the prospectus with DZ to ensure that she understood the risks and knew that it was not a conservative investment. She understood that she could lose her principal and the interest, and she indicated that she had no need for the funds.

Considering all of these circumstances, the Panel concludes that Enforcement failed to establish by a preponderance of the evidence that Savage recommended the investment and, even if he had, that it was unsuitable for her.

8. Customer KR

a. Testimony

Customer KR is single with no dependents, and was 48 years old when he opened his account with WSSI in 2005.²³¹ He informed Savage that he had 20 years of investment experience. This included investments in stocks, bonds, mutual funds, REITs, oil and gas partnerships, fixed income investments, insurance, futures contracts, and variable products.²³² KR has several other financial advisors in addition to Savage.²³³ He characterized his knowledge of investing as "good."²³⁴ KR described himself as a detail-oriented engineer, and stated that he made a practice of reading informational materials like the GWG prospectus and subscription agreement and then doing his own additional research.²³⁵

In 2005, KR's net worth, exclusive of his home, was approximately \$1.5 million, his liquid net worth was approximately \$1.25 million, and his annual income was approximately \$280,000. His risk tolerance was seven on a scale of ten. A WSSI account document estimates

²²⁹ Compl. ¶ 32.

²³⁰ Enforcement's Post-Hr'g Br., at 24.

²³¹ Tr. 705; CX-26, at 1.

²³² Tr. 707; CX-26, at 3.

²³³ Tr. 708-09.

²³⁴ Tr. 707.

²³⁵ Tr. 713.

the value of his invested assets at \$1.25 million.²³⁶ His WSSI new account form identifies safety of principal and long-term growth as his investment objectives and estimates his annual disposable income at \$125,000.²³⁷ Other account documentation describes his investment objectives as asset protection, followed by income tax reduction and accumulation of retirement capital.²³⁸ By 2011, his net worth had increased to over \$2 million.²³⁹ KR describes himself as “a moderate investor,” but he added that this does not mean that every investment he makes is moderate or conservative. He explained: “I balance, I have some investments that are considered speculative and those that are considered very safe.”²⁴⁰

In the seven years KR invested with Savage prior to investing in GWG, the two spoke in person and by phone a number of times.²⁴¹ In his first years with WSSI, KR invested in annuities, REITs, and oil and gas partnerships.²⁴² KR shared his tax information with Savage so that he could help reduce KR’s tax liabilities.²⁴³

At a time when KR had funds he did not need,²⁴⁴ he called Savage to tell him that he wanted to invest additional money where it might earn a guaranteed interest rate. He asked Savage if he knew of such an investment. A week or so later, Savage brought GWG to his attention.²⁴⁵ Savage explained what the company did, discussed the interest rates, terms, and some of the risks, and KR decided to pursue it further.²⁴⁶ KR explained to Savage that he was interested in both a short-term investment that would provide better interest than money market rates, and a long-term investment that would pay a return comparable to the stock market, but without the daily fluctuation.²⁴⁷

Savage gave KR the prospectus and told KR what he thought were the major risks, the “pros and cons,” including the illiquidity of the debentures and the risk of loss of principal and accrued interest. KR read the prospectus and understood the risks. He understood that there is risk in any investment, and was aware that the debentures were a speculative investment.²⁴⁸

²³⁶ Tr. 705-06; CX-26, at 1-3.

²³⁷ RX-34, at 3-4.

²³⁸ CX-26, at 1.

²³⁹ Tr. 709.

²⁴⁰ Tr. 730-31.

²⁴¹ Tr. 710.

²⁴² Tr. 708.

²⁴³ Tr. 710.

²⁴⁴ Tr. 722.

²⁴⁵ Tr. 726-27.

²⁴⁶ Tr. 727-28.

²⁴⁷ Tr. 711.

²⁴⁸ Tr. 713-15.

Savage reviewed all of the suitability criteria, KR's income and assets, and although KR does not specifically remember whether Savage asked if he needed the funds, KR testified that he only invests, in his words, "what I know that I can live without should I either lose it or tie it up for long term ... and I would never ... invest in something if I thought I would need the money in the near term."²⁴⁹

KR testified that he was somewhat familiar with the concept of investments linked to life insurance policies²⁵⁰ and that he was not worried about the risks portrayed by the prospectus and Savage. His primary concern was the short period GWG had been in business. In sum, KR was aware of and comfortable with the risks.²⁵¹

In April 2012 KR invested \$50,000 in debentures with a six-month maturity, at 4.75 percent interest, and an additional \$50,000 in debentures with a seven-year maturity, at 9.5 percent interest.²⁵² At the time, KR's liquid net worth was between \$800,000 and \$1 million.²⁵³ These two investments amounted to approximately ten percent of his liquid net worth and five percent of his total net worth. KR testified that he, not Savage, determined the amount of his investments.²⁵⁴

Based on the earnings from his initial investments, on his own initiative, when KR later had additional money to invest, he contacted Savage and told him that he wanted to purchase additional GWG debentures.²⁵⁵ KR has been satisfied with his investments; he has received all interest payments timely, has received notices a month in advance of the rollover dates and has decided to roll some over and has recouped his principal in others. KR signed the letter prepared by Savage's counsel and testified that he agrees with its assertions that he understood the risks of the debentures as explained by Savage, and had concluded that the debentures were suitable for him.²⁵⁶

b. Discussion

The Complaint inaccurately alleges that Savage recommended that KR invest \$380,000 in GWG renewable debentures between April 2012 and August 2012. It also alleges that the recommendations were unsuitable because KR's investment objectives were safety and growth,

²⁴⁹ Tr. 715-16

²⁵⁰ Tr. 727-28.

²⁵¹ Tr. 732.

²⁵² Tr. 710-11; CX-26, at 9, 14.

²⁵³ Tr. 721.

²⁵⁴ Tr. 711-12.

²⁵⁵ Tr. 716-17. KR invested an additional \$280,000: \$100,000 for seven years in May 2012; \$15,000 for six months and \$25,000 for seven years in June 2012; \$60,000 for seven years and another \$80,000 for seven years in August 2012. CX-26, at 17, 32, 48, 72, 93.

²⁵⁶ Tr. 717-19. Like ED, KR testified incorrectly that he drafted the letter. Tr. 723.

his net worth and liquid net worth each were \$1.25 million, and KR's investments in GWG came to 30 percent of his liquid net worth.²⁵⁷ Enforcement argues that KR's testimony "underscores how unsuitable this investment was for his objective of asset protection" and emphasizes that KR sought "less risk than the stock market."²⁵⁸

Savage recommended GWG in response to KR's specific request for ideas for an investment that would provide a fixed rate of interest better than money market rates. However, only KR's initial two \$50,000 purchases of debentures in April 2012 resulted from Savage's recommendation. These investments constituted less than ten percent of KR's liquid net worth. Furthermore, Savage reviewed the GWG prospectus with KR and fully informed KR of the "pros and cons" of GWG, and the risks inherent to GWG as a speculative investment.

KR is a sophisticated, wealthy investor who conducted his own review of the suitability of GWG for his objectives. Fully cognizant of the risks, KR acted on Savage's recommendation initially and invested funds that he did not need, and could afford to lose. Then, based on his own assessment of the performance of the debentures, and understanding the risk of loss, KR made his own decision to invest additional funds. Considering KR's financial situation and needs, the assets at his disposal, and both his and Savage's testimony, the Hearing Panel concludes that Enforcement has failed to prove by a preponderance of the evidence that Savage's recommendation to KR was unsuitable.

9. Customers RW and CW

a. Testimony

RW and his wife CW are retired. He was a schoolteacher and she was a town administrator in the New Jersey community where they lived before retirement.²⁵⁹ They opened their account with WSSI in April 2012 when they were both 66 years old.²⁶⁰ Although their new account form indicates that they had 42 years of investing experience in mutual funds, it characterized their investment knowledge as limited. RW testified that their experience was limited to real estate investments and a mutual fund investment he made when still teaching.²⁶¹

Their new account form estimated their net worth at \$1.2 million and annual income at \$110,000.²⁶² RW testified that their liquid net worth was \$150,000 to \$200,000.²⁶³ On their WSSI personal data form and new account forms, however, they estimated their liquid assets to

²⁵⁷ Compl. ¶ 32.

²⁵⁸ Enforcement's Post-Hr'g Br., at 22.

²⁵⁹ Tr. 436-37.

²⁶⁰ Tr. 439, 444.

²⁶¹ Tr. 445; RX-35, at 1.

²⁶² RX-35, at 1.

²⁶³ Tr. 443.

be \$466,955, identified their investment objectives as safety of principal and long-term growth, characterized their risk tolerance as one to two on a scale of ten, and identified five investment goals in descending order of importance. The goals were reducing income taxes, protecting assets, increasing income, minimizing estate taxes, and accumulating retirement capital.

In 2012, the couple owned two homes, one in New Jersey, the other in Florida, had no mortgage, and were otherwise debt free.²⁶⁴ RW testified that they had full medical coverage from their retirement plans. Their monthly income from pensions and Social Security exceeds their monthly expenses by approximately \$2,000.²⁶⁵

RW's brother-in-law introduced him to Savage.²⁶⁶ When they met, RW and CW provided Savage with their financial information. Savage did not immediately recommend an investment. He told them that he would work up a plan providing options for them to consider.²⁶⁷

According to RW, Savage did not engage in a "hard sell." Rather, Savage told RW and CW about GWG and asked if they were interested. The couple was "tired of doing the CDs" that they had held for five or six years and did not need.²⁶⁸ RW testified that he and his wife reasoned, "it isn't money that we need, it's not going to change our lifestyle if something happens to this \$50,000. We're still going to be able to live the same way we are, we're still going to be able to travel."²⁶⁹

Savage reviewed the prospectus with them. RW did not read it, describing himself as a "lazy investor,"²⁷⁰ but he and his wife initialed pages in the subscription agreement confirming that they had reviewed those parts, knew the risks of the investment, understood that it was illiquid and did not trade in the secondary market, and that they could lose their entire investment.²⁷¹ On May 16, 2012, they invested \$50,000 for seven years at 9.5 percent interest.²⁷² RW testified that he understood that with so high an interest rate, "there had to be risk. Nobody else was offering nine-and-a-half percent."²⁷³ He clearly understood that they could lose all of their investment.²⁷⁴ The investment represented slightly less than four percent of their net worth.

²⁶⁴ Tr. 441; CX-27, at 1, 3; RX-35, at 1.

²⁶⁵ Tr. 437-38.

²⁶⁶ Tr. 439.

²⁶⁷ Tr. 440-41.

²⁶⁸ Tr. 448-49, 458.

²⁶⁹ Tr. 458.

²⁷⁰ Tr. 449.

²⁷¹ Tr. 449-51.

²⁷² RX-35, at 6.

²⁷³ Tr. 450.

²⁷⁴ Tr. 458-59.

RW and CW made other investments with Savage, including approximately \$300,000 in fixed index annuities.²⁷⁵

b. Discussion

The Complaint alleges that Savage's recommendation to RW and CW was unsuitable because RW listed his risk tolerance as very conservative, his investment knowledge as limited, with objectives of asset protection, accumulating retirement capital, and reducing taxes, and because he had a net worth of slightly less than \$1.3 million and liquid net worth of \$467,000, and that the investment constituted over 10 percent of his liquid net worth.²⁷⁶ In addition, Enforcement argues that GWG was RW's first investing experience, that his testimony suggests that his liquid net worth was actually only \$150,000, and that he did not read the GWG prospectus but simply trusted Savage.²⁷⁷

RW's uncontradicted testimony, however, establishes that Savage reviewed the prospectus with him and his wife, and that he and his wife initialed and signed the subscription agreement confirming that they understood the risks as they were detailed in the prospectus and explained by Savage. Furthermore, RW's testimony establishes that he and his wife wanted to invest \$50,000 that they did not need, the loss of which would not affect their lives, to earn a higher rate of return than they were earning on their CDs, fully aware that they risked losing their investment.

Based on their overall financial situation, with substantial assets, no mortgage, and no debt, the Hearing Panel concludes that Enforcement did not prove by a preponderance of the evidence that Savage's recommendation to RW and CW was unsuitable.

VIII. Enforcement Failed to Prove that Respondents Distributed Misleading Sales Literature

The second cause of action charges that Respondents distributed a misleading brochure, the Client Fact Sheet, advertising the GWG debentures in violation of NASD Rule 2210(d)(1)(A) and FINRA Rule 2010. Enforcement asserts that the Client Fact Sheet was materially misleading because (i) it falsely stated that the debentures were secured by life insurance policies and (ii) it failed to state that investors' secured interests were subordinate to other creditors of GWG's subsidiaries.²⁷⁸

²⁷⁵ Tr. 452-53.

²⁷⁶ Compl. ¶ 32.

²⁷⁷ Enforcement's Post-Hr'g Br., at 22-23.

²⁷⁸ Compl. ¶ 60.

A. The Client Fact Sheet

Bo Mayfield, GWG's Chief Compliance Officer,²⁷⁹ testified that GWG's executives prepared the Client Fact Sheet with input from outside counsel and Arque's chief counsel. On GWG's behalf, Arque submitted the Client Fact Sheet to FINRA's advertising department in the fall of 2011 to solicit FINRA's comments and guidance to ensure that it was "fair and reasonable." According to Mayfield, it was "very important" to GWG to ensure that the Client Fact Sheet was fair and balanced, and GWG would not have provided it to members of the selling syndicate unless FINRA issued a "Clean Letter" certifying that FINRA's advertising staff had reviewed the document and determined that it appeared to comply with FINRA's advertising rule.²⁸⁰

Through Arque, GWG submitted several drafts of the Client Fact Sheet to FINRA, received "multiple letters" with comments from FINRA's advertising department staff, and incorporated the comments into the Client Fact Sheet before receiving the Clean Letter.²⁸¹

Mayfield testified that the purpose of the Client Fact Sheet was to provide a brief summary of the prospectus and interest readers in the prospectus.²⁸² The Client Fact Sheet identified risks of the investment in a section titled "Risks Involving Renewable Secured Debentures," where it warned:

An investment in Renewable Secured Debentures involves a high degree of risk. The prospectus provides a comprehensive listing of risks. A summary of those risks includes, but are not limited to: GWG's limited operating history, a continued need to access financing, changes in economic environment including interest rates, subordination to senior debt, actuarial experience, and other factors. Investors should purchase Renewable Secured Debentures only to the extent they are able to bear the risk of loss of their entire investment and have no need for immediate liquidity.²⁸³

The Client Fact Sheet also stated, "Investors must read the entire Prospectus for investment conditions, risk factors, minimum requirements, fees and expenses and other pertinent information with respect to the Renewable Secured Debentures in order to obtain the information essential to making an informed investment decision."²⁸⁴

²⁷⁹ Tr. 621, 623.

²⁸⁰ Tr. 638-39, 661.

²⁸¹ Tr. 642-43.

²⁸² Tr. 661.

²⁸³ CX-7, at 4.

²⁸⁴ CX-7, at 4.

1. FINRA's "Clean Letter"

On February 15, 2012, FINRA issued the "Clean Letter" GWG had been waiting for. It stated that "the [Client Fact Sheet] appears consistent with applicable standards." FINRA's "review" was conditional; it was conducted "with the understanding that the final prospectus for the renewable secured debentures will accompany" the Client Fact Sheet. The letter also included a standard proviso reminding Arque of its "responsibility to ensure that all data reported in the fact sheet is accurate."²⁸⁵

The Clean Letter permitted Arque and GWG to describe the Client Fact Sheet as having been "reviewed by FINRA" or "FINRA Reviewed," but not to state or imply that it was "approved by FINRA."²⁸⁶ GWG understood that the Client Fact Sheet could be provided to prospective investors, but only in conjunction with the prospectus.²⁸⁷

Arque then put the Clean Letter into the due diligence binders it sent to participating broker-dealers and in investor kits, which included the prospectus and supplements and the subscription agreement.²⁸⁸ Mayfield testified that he received a number of calls from members of the broker-dealer selling group to confirm that FINRA had issued the Clean Letter before they distributed the investor kit containing the Client Fact Sheet.²⁸⁹

When WSSI became a participating broker-dealer with Arque and GWG, Savage knew that FINRA's advertising department had reviewed the Client Fact Sheet.²⁹⁰ He had called the "head of Arque" as well as GWG's CEO to ask if the GWG marketing materials had been reviewed by FINRA, and was told that they had.²⁹¹ Savage also understood—and instructed WSSI representatives accordingly—that the Client Fact Sheet had to be distributed together with the prospectus.²⁹²

2. FINRA's Second Review

In October 2012, GWG submitted another document to FINRA, called a Registered Investment Advisor Fact Sheet ("RIA Fact Sheet"). It was similar to the Client Fact Sheet.²⁹³ In a

²⁸⁵ RX-23.

²⁸⁶ Tr. 76; CX-6.

²⁸⁷ Tr. 641.

²⁸⁸ Tr. 643-44, 647.

²⁸⁹ Tr. 647.

²⁹⁰ Tr. 800.

²⁹¹ Tr. 801-03.

²⁹² Tr. 802, 804-08.

²⁹³ Tr. 649.

Review Letter dated November 13, 2012, FINRA’s advertising staff commented on language in two sentences in the RIA Fact Sheet.

The first sentence was identical to the Client Fact Sheet. Under the heading “What are Renewable Secured Debentures?” both documents stated:

Renewable Secured Debentures are secured by the corporate assets of GWG, which consist primarily of investments in life insurance policies purchased in the secondary market.

The second sentence of concern in the RIA Fact Sheet came under the heading “What Backs the Renewable Secured Debentures?” It stated, in relevant part:

GWG’s assets consist primarily of the ownership of life insurance policies purchased in the secondary markets, summarized in the tables below.²⁹⁴

The counterpart to this sentence in the Client Fact Sheet, under the same section title, reads:

Renewable Secured Debentures are secured by all the corporate assets of GWG. GWG’s assets consist primarily of the life insurance policies purchased in the secondary market and are summarized in the tables below.²⁹⁵

Although the Client Fact Sheet had already been reviewed, FINRA’s advertising department staff objected to these two sentences in the RIA Fact Sheet because they did “not explain that the life insurance policies are held by a subsidiary of a subsidiary of the issuer and that the policies are not collateral for the debentures, but rather the debentures are backed by GWG Holdings’ ownership interest in the subsidiary.” The staff stated that these sentences “must be revised to prominently address these material facts.”²⁹⁶

FINRA’s advertising staff apologized for requiring “revisions not previously cited in *similar communications* that contained *comparable language*. We regret the oversight and apologize for any inconvenience this may cause the firm. Nevertheless, the following revisions must be incorporated in this and any similar communications.”²⁹⁷ FINRA informed Arque and GWG in a telephone call that that they did not have to resubmit the Client Fact Sheet for further review. But Mayfield knew that GWG would have to revise the similar sentences in the Client Fact Sheet.²⁹⁸

²⁹⁴ CX-8, at 1-2.

²⁹⁵ CX-5, at 1.

²⁹⁶ RX-27, at 2.

²⁹⁷ RX-27, emphasis supplied.

²⁹⁸ Tr. 649-50.

Mayfield testified that the language FINRA took issue with was “technically accurate.” According to Mayfield, the debentures are secured by GWG’s corporate assets. Those assets consist primarily of the life insurance policies and its cash assets. Although the life insurance policies are not “direct collateral” of the debenture, GWG is vertically integrated; it owns the subsidiary that owns the policies, and there is only one asset class—the life insurance policies. Moreover, according to Mayfield’s un rebutted testimony, the value of the policies has always exceeded GWG’s debt. If GWG were to fail, the primary assets to sell would be the life insurance policies.²⁹⁹

Furthermore, as Mayfield noted, the language at issue in the Client Fact Sheet consisted of two nearly identical sentences in a document containing a lengthy description of the risks of the investment, required to be accompanied by a prospectus that also extensively described the risks involved. Thus, Mayfield stated, given the context of the “total mix of information” GWG provided about the debentures, the questioned language was not material.³⁰⁰

However, Mayfield testified that GWG “wanted to . . . be compliant with FINRA.” Therefore GWG amended the language that concerned the advertising department staff.³⁰¹ The two sentences at issue in both Fact Sheets were changed to read:

Renewable Secured Debentures are secured by the assets owned by GWG. GWG’s primary asset is its wholly-owned subsidiary, GWG Life Settlements, LLC, which owns life insurance policies purchased in the secondary market.³⁰²

Mayfield testified that GWG and Arque submitted the revisions and FINRA reviewed them in February 2013.³⁰³

3. Discussion

Enforcement argues that the Client Fact Sheet is misleading because the two sentences at issue falsely “suggested that the Debentures are secured by life insurance policies.” Enforcement says this is incorrect³⁰⁴ because the “life insurance policies are not collateral for the Debentures and the ‘secured’ interest the Debentures have is subordinate to other creditors of GWG and its subsidiaries.”³⁰⁵ Enforcement argues that WSSI, Savage, and Kittlaus violated NASD Rule

²⁹⁹ Tr. 656-57. Mayfield testified, and the prospectus states, that the life insurance policies are pledged to the senior debt—the hundred million dollar German bank credit facility—and that obligations to investors on default are subordinate to the senior debt. Tr. 659-60.

³⁰⁰ Tr. 656.

³⁰¹ Tr. 657-58.

³⁰² CX-9, at 1-2.

³⁰³ Tr. 654, 685.

³⁰⁴ Enforcement’s Pre-Hr’g Br., at 7.

³⁰⁵ Enforcement’s Post Hr’g Br., at 27.

2210(d)(1)(A), and thereby Rule 2010, when they distributed the Client Fact Sheet in 2012. For doing so, Enforcement seeks to suspend Savage and Kittlaus for two months in all capacities and fine Savage and WSSI jointly \$20,000.³⁰⁶

The Panel notes that the Client Fact Sheet did not expressly claim that the life insurance policies are collateral for the debentures. Rather, it stated that the debentures are secured by “all the corporate assets of GWG,”³⁰⁷ which include, albeit through a wholly owned subsidiary, the life insurance policies.³⁰⁸

As for Enforcement’s argument that the Client Fact Sheet did not disclose that the debentures’ secured interest “is subordinate to other creditors of GWG and its subsidiaries,”³⁰⁹ another section of the Client Fact Sheet, titled “Risks Involving Renewable Secured Debentures,” explicitly identified “subordination to senior debt” as one of the risks to investors. It also reiterated that investors “should purchase Renewable Secured Debentures only to the extent they are able to bear the risk of loss of their entire investment and have no need for immediate liquidity.”³¹⁰

Rule 2210(d)(1)(A) requires communications distributed by members to meet the fundamental test of fairness to customers. The communications must be “based on principles of fair dealing and good faith,” be “fair and balanced,” and thereby give customers a “sound basis for evaluating ... any particular security.” The communications must not “omit any material fact” if doing so causes the communications to be misleading. NASD Rule 2210(d)(1)(B) forbids a member to publish, circulate, or distribute any public communication that the member knows or has reason to know contains any untrue statement of a material fact or is otherwise false or misleading.”

Here, Respondents distributed the Client Fact Sheet—with the prospectus—to customers only after Savage took reasonable steps to assure himself that it was accurate, including carefully reviewing the prospectus and calling responsible persons at Arque and GWG to satisfy himself that FINRA had reviewed the Client Fact Sheet and issued its Clean Letter. As discussed above, FINRA issued the Clean Letter after Arque and GWG had submitted multiple revisions, and the Clean Letter stated that the Client Fact Sheet met the applicable advertising standards of fairness and balance.

The Panel also notes that FINRA’s advertising department required only minor revision to correct the fault it found in its second review. Enforcement argues that the “revised Client Fact Sheet referenced GWG’s complex organizational structure and clarified that the Debentures are

³⁰⁶ Enforcement’s Post-Hr’g Br., at 31.

³⁰⁷ CX-5, at 1; CX-7, at 4.

³⁰⁸ Tr. 656, 824.

³⁰⁹ Enforcement’s Post-Hr’g Br., at 27.

³¹⁰ CX-5, at 2; CX-7, at 4.

not directly secured by life insurance policies.”³¹¹ But the differences between the original and the revised language are minimal.

The allegedly misleading language in the original, FINRA-reviewed Client Fact Sheet stated:

Renewable Secured Debentures are secured by all the corporate assets of GWG. GWG’s assets consist primarily of the ownership of life insurance policies purchased in the secondary markets.³¹²

The revision, which Enforcement concedes is not misleading, states:

Renewable Secured Debentures are secured by the assets owned by GWG. GWG’s primary asset is its wholly-owned subsidiary, GWG Life Settlements, LLC, which owns life insurance policies purchased in the secondary market.³¹³

Enforcement argues that the revisions to the Client Fact Sheet made it “clearer and ... not misleading, because they talk about ... a subsidiary.”³¹⁴ However, the Panel finds that the differences between the original, allegedly misleading language and the revised, not misleading language are not sufficiently significant to support a finding that the original version violated Rule 2210. In the Panel’s view, when taken in context with the total mix of available information, including the express warnings about the risks involved in purchasing the debentures throughout the Client Fact Sheet and the prospectus that always accompanied it, as required, these small edits were not material.

Respondents distributed the Client Fact Sheet in reliance on FINRA’s advertising department’s Clean Letter’s statement that it appeared to be “consistent with applicable standards,” before FINRA’s advertising department revisited the matter. Moreover, after FINRA made its objections to this language known, Respondents did not distribute the original Client Fact Sheet.

Under these circumstances, the Extended Hearing Panel declines to find that Respondents violated FINRA Rules 2210(d)(1)(A) and 2010 by distributing the Client Fact Sheet during the relevant period, prior to FINRA’s advertising staff’s revised assessment of the language in the sentences at issue.

³¹¹ Enforcement’s Pre-Hr’g Br., at 8.

³¹² CX-5, at 1.

³¹³ CX-9, at 1.

³¹⁴ Tr. 1077.

IX. Enforcement Did Not Prove that WSSI and Savage Failed to Establish and Maintain a Reasonable Supervisory System

The fourth cause of action alleges that WSSI and Savage failed to establish and maintain a system to supervise WSSI's registered representatives that was reasonably designed to achieve compliance with NASD Rules 3010(a) and (d), and thereby also violated FINRA Rule 2010. The Complaint alleges several specific failures of supervision. First, it charges that Savage failed to follow up on red flags that should have caught his attention in connection with two recommendations to purchase debentures that registered representative Karen Geiger made to customers. Second, it alleges that Savage failed to supervise branch offices and make onsite supervisory audits. Third, it charges that Savage did not establish a reasonable supervisory system for review and retention of correspondence.

Both Geiger and Kittlaus worked in off-site locations, Kittlaus at his home in the Chicago area through the summer of 2012, and then in Naples, Florida. Geiger worked at an office in Akron, Ohio.³¹⁵

NASD Rule 3010(a) requires generally that a firm establish and maintain a system of supervision of the activities of registered representatives "reasonably designed to achieve compliance with applicable securities laws and regulations." Rule 3010(d) more specifically focuses on supervision of registered representatives, including establishing procedures for a registered principal to review and approve all transactions in writing and review incoming and outgoing correspondence, both electronic and written, with members of the public. Concerning correspondence with the public, the Rule states that a member "shall develop written procedures that are appropriate to its business, size, structure, and customers." That is, a member should craft procedures appropriate to its particular circumstances.

A. Supervision of Karen Geiger

Geiger joined WSSI on January 6, 2012, when she began sharing an office with another WSSI representative.³¹⁶ Geiger places her securities business with WSSI, but she independently conducts business in life insurance, long-term care, annuities, and taxes.³¹⁷

Enforcement faults Savage for approving investments made by Geiger customers who purchased debentures. JB was one.

1. Customer JB

A self-employed architect-contractor, JB was 70 years old when he opened his WSSI account. He estimated his annual income at \$200,000, his net worth at \$2.5 million, and his

³¹⁵ Tr. 214, 362-63.

³¹⁶ Tr. 214, 218.

³¹⁷ Tr. 214-15.

liquid assets at \$1.75 million.³¹⁸ JB's company designs and builds industrial, residential, and commercial buildings.³¹⁹ JB had invested in a variety of high-risk investments including REITs, junk bonds and penny stocks, as well as blue chip stocks over a period of 30 years, including for a time trading stocks on his own account.³²⁰ His personal data form identifies his investment objective as income, and his new account form identifies his investment objectives as income and low risk to principal.³²¹

JB testified that, before investing, he met with Geiger three or four times, for approximately an hour and a half each time.³²² Geiger identified several other possible investments in addition to GWG.³²³ JB testified that Geiger gave him a prospectus to review for each of "probably five different types of investments." He corroborated Geiger's testimony that she did not emphasize GWG or indicate that it was the best, but left it to him to consider each. The investments included, by his description, "waste and fuel," credit unions, annuities, and others.³²⁴

Geiger gave JB the GWG prospectus, and he reviewed it. As he typically did, JB gave the prospectus to his estate planning and corporate attorney and asked him to read it as well.³²⁵ Over the course of several meetings, JB and his attorney "went down all the points of the prospectus."³²⁶ Geiger had not recommended an amount for JB to invest, but after his consultations with her and his attorney, he decided to invest \$900,000.³²⁷

JB understood the risks of investing and particularly the risks of investing in GWG. JB had previously been interested in this type of investment.³²⁸ He testified that he did not consider GWG to be "more risky than stocks bonds and mutual funds" because he knew people who "lost 80 percent of what they had in 2008" and because of his experience with "all the investments" that he has had. As he pointed out: "Look at Detroit. People bought bonds there and have nothing

³¹⁸ Tr. 585; CX-29, at 1.

³¹⁹ Tr. 585.

³²⁰ Tr. 235-37, 241, 590-91, 605.

³²¹ CX-29, at 1, 5.

³²² Tr. 587-88.

³²³ Tr. 591.

³²⁴ Tr. 617

³²⁵ Tr. 247, 592-93.

³²⁶ Tr. 601, 610.

³²⁷ Tr. 244, 594.

³²⁸ Tr. 593-94.

and it was supposed to be a safe investment.” He testified that he does not know that any investments are “rock solid.”³²⁹

He has experienced losing money in investments. In the 1990’s he invested in certificates of deposit in Texas banks that were supposed to be secured by the federal government; he lost a third of his money. Essentially, he does not think “anybody who’s invested anything gets all their money back without any injuries.” He emphasized that his investments in GWG were “[t]otally” his own decision³³⁰ and he understood he could lose all of his invested funds.³³¹ He assured Geiger that he had other funds he could live on.³³²

Geiger was concerned that JB wanted to invest \$900,000 in GWG. She told him she was uncomfortable about the large amount and recommended that he break up the investment into various maturities, but JB declined. She reiterated to JB that GWG was a high-risk, aggressive investment and told him she wanted to discuss it with Savage. She did so on speakerphone so JB could hear.³³³ Savage told JB that he believed his investment was excessive. JB responded that he had looked at this type of investment before and wanted to invest this amount. Reviewing the risk factors, Savage confirmed that Geiger had fully reviewed them with JB. JB told Savage he understood the investment and that he could afford to lose his investment. Savage testified that JB said he had “plenty of money” and “more money coming in.”³³⁴

JB confirmed that he spoke with Savage before investing in GWG. He had four or five conversations with Geiger and Savage that he described as “almost” an “interrogation” of him by them to “make certain” he could afford the investment.³³⁵ He assured Savage that Geiger had not advised him to invest so much, and that she had no idea how much he would invest until he came in with the check. JB described to Savage his review of the prospectus, the time that had elapsed between receiving it and investing, and that he had met several times with his attorney before making his decision. JB told Savage that he thought the investment was a suitable one for him.³³⁶

JB invested \$200,000 in debentures with a seven-year maturity and \$700,000 in debentures with a five-year maturity. He wanted “a longer term for a number of reasons: One, the interest rate was higher,” and he “had intentions to put more money into GWG.”³³⁷ JB, like many of the other investors who testified, signed a letter prepared by Savage’s counsel attesting

³²⁹ Tr. 614.

³³⁰ Tr. 613-14.

³³¹ Tr. 615.

³³² Tr. 600.

³³³ Tr. 245-47.

³³⁴ Tr. 1015-16.

³³⁵ Tr. 615-16.

³³⁶ Tr. 601-03.

³³⁷ Tr. 595-96.

that he believed the debentures were a suitable investment for him, after considering the risks, which Geiger and Savage explained fully.³³⁸

2. Customers RD and BD

Customers RD and BD, a retired married couple, opened their account with WSSI in June 2012.³³⁹ RD, then 64, is a former regional manager for a company that manufactures fire extinguishing systems, and BD, then 62, is a former school teacher.³⁴⁰ They estimated their risk tolerance as four on a scale of ten, their annual income at \$139,000, total net worth at \$1.5 million, and liquid net worth at over \$1 million. They identified long-term growth as their investment objective, and rated his investment knowledge as moderate, and hers as limited.³⁴¹ Both receive pensions and survivor pensions from previous marriages.³⁴² Their monthly income from pensions and Social Security exceeds their living expenses by approximately \$1,400 per month.³⁴³ Geiger described RD as a retired private sector manager who had been investing for over 35 years and was interested in “aggressive type stocks, corporate bonds and mutual funds.”³⁴⁴

RD and Geiger were high school classmates. When they met again at a class reunion in 2012, Geiger gave him her business card. She followed her standard procedure in a series of meetings that followed. She met with RD and BD in April for an introductory meeting so they could inform her about their investments. At this meeting, Geiger gave them forms and instructions on what information to bring to a second meeting, at which they reviewed the couple’s financial situation. This lasted approximately two hours. Geiger reviewed their budget, tax status, income, expenses, insurance assets, and liabilities. The couple had a significant amount of stock in their portfolio. Geiger then reviewed what she had learned before the third meeting, when she first suggested possible investment strategies.

At the third meeting, Geiger presented four investments for them to consider. They were a real estate investment program, annuities, life insurance, and GWG. Geiger reviewed and gave them the investment kit for each company. Geiger reviewed the nature of GWG, informed them that it is a “higher risk,” illiquid investment and went over the Client Fact Sheet and the prospectus, and encouraged them to visit the company website. They did not decide on what investments to make at this meeting.³⁴⁵

³³⁸ Tr. 604; RX-57, at 25.

³³⁹ CX-31, at 1.

³⁴⁰ Tr. 735-36.

³⁴¹ CX-31, at 1.

³⁴² Tr. 737.

³⁴³ Tr. 741-42.

³⁴⁴ Tr. 266.

³⁴⁵ Tr. 257-66.

After considering the various kits, RD and BD met with Geiger again and informed her that they had decided to invest in the real estate investment and GWG. Geiger again explained the risks. They decided to make a joint investment of \$100,000, and BD decided to invest an additional \$30,000 from a money market account she had that was not performing. The couple decided on the maturities they wanted.³⁴⁶

When RD and BD told Geiger that they wished to invest in GWG, Geiger reminded them that it was a higher risk than their stated risk tolerance of four on a scale of ten. She also noted that it was more “aggressive” because it was not publicly traded and there is no secondary market for the debentures. She reviewed the subscription agreement with them, and they initialed the sections acknowledging, after Geiger read them aloud, that they were aware of the risks and that they could lose their entire investment and accrued interest. Geiger submitted the subscription agreement to Savage for approval, filling out a certification that she had fully informed the clients of the risks.³⁴⁷

After reviewing the proposed investment, Savage called RD. He noted that the couple’s total investment amounted to approximately 20 percent of their liquid net worth. He questioned them about their finances and whether they understood that it was highly risky. He then explained the specific risks involved.³⁴⁸

RD confirmed Geiger’s description of their meetings and her review of GWG and its risks. He understood from Geiger that the money invested “had to be money that [they] didn’t need for seven years,” and that they could lose it all. He testified that “this was money that [they] didn’t need.”³⁴⁹ RD also confirmed that Savage called him; he testified that he spoke with Savage several times, and that Savage asked whether Geiger had reviewed the risks and whether he understood them.³⁵⁰

RD and his wife invested a total of \$206,000 in GWG in July and August 2012.³⁵¹ As with other investors who testified, they signed a letter stating that, notwithstanding the risks outlined in the prospectus and explained by Savage, they believed the investment was suitable for them.³⁵²

³⁴⁶ Tr. 267-68.

³⁴⁷ Tr. 269-70.

³⁴⁸ Tr. 1018-19.

³⁴⁹ Tr. 746-49.

³⁵⁰ Tr. 749-50.

³⁵¹ Tr. 754-55; RX-53 at 16, 23, 32, 34, 45.

³⁵² Tr. 750-51.

B. Periodic Inspection of Branch Offices

The Complaint alleges that, during the relevant period, Savage and WSSI failed to supervise the Firm's branch offices properly because they failed to conduct periodic inspections of Kittlaus and Geiger and Savage failed to visit or conduct onsite examinations of Kittlaus's office.³⁵³ Enforcement claims that Savage failed to conduct an onsite visit of either Kittlaus or Geiger until March 2013.³⁵⁴

Enforcement argues that Savage and WSSI had an obligation to supervise Kittlaus "diligently" because of his disciplinary history and because he worked a long distance from Savage's office.³⁵⁵ Kittlaus joined WSSI in April 2012, but Savage did not visit Kittlaus in his office near Chicago. In September 2012, Kittlaus moved and began working from his home in Naples, Florida, not far from WSSI's Bonita Springs, Florida, office, where Savage worked. Then Savage saw Kittlaus weekly and spoke to him on the phone.³⁵⁶ Savage made a visit and audit of Kittlaus' home office on March 27, 2013, before Kittlaus had been with WSSI for a full year.³⁵⁷

Savage visited Geiger's office in January 2012, when she joined the Firm. Savage and an assistant visited the office in June 2012 to conduct an audit and review books and records.³⁵⁸ Savage spoke with Geiger at least monthly to discuss compliance issues, and Geiger called her whenever she had questions or a new prospective customer.³⁵⁹

As Enforcement notes, the determination of whether a firm's supervision meets the reasonableness standard of NASD Rule 3010 depends on the facts and circumstances of each case.³⁶⁰

C. E-mail Review and Outgoing Correspondence

The Complaint alleges that Savage and WSSI failed to implement a supervisory system adequate to review and retain incoming and outgoing written and electronic communications of the firm's registered representatives. Specifically, it points to alleged failures to retain and

³⁵³ Compl. ¶ 68.

³⁵⁴ Enforcement's Post-Hr'g Br., at 29.

³⁵⁵ Enforcement's Pre-Hr'g Br., at 22. (Emphasis in original.)

³⁵⁶ Tr. 850-51.

³⁵⁷ Tr. 197, 878-80.

³⁵⁸ Tr. 218, 254-55, 849.

³⁵⁹ Tr. 217.

³⁶⁰ Enforcement's Pre-Hr'g Br., at 21.

review electronic correspondence, and to require retention of hardcopy correspondence, review correspondence, and maintain a review log.³⁶¹

The only hardcopy correspondence that Enforcement presented at the hearing as an example of a failure to properly supervise correspondence was the Kittlaus letter, which Enforcement claims constitutes “direct evidence” of Savage’s and WSSI’s “lack of supervisory review.”³⁶² As set forth below, however, the evidence demonstrates that Kittlaus sent the letter surreptitiously. There is nothing in the record to support the proposition that reasonable supervision by Savage could have prevented Kittlaus from doing so. As the Complaint asserts, Kittlaus did not inform WSSI of the letter, did not seek or obtain approval, and did not retain a copy of the letter or a distribution list.³⁶³ There were no red flags for Savage to discern and respond to. The Kittlaus letter is not an example of a supervisory failure, but of a representative’s dishonest conduct, successfully designed to avoid detection. When a representative cloaks an act in secrecy under circumstances like these, it is unreasonable to attribute the fault to a supervisory failure. Here, the supervisory system as written and implemented was reasonably designed to monitor and review correspondence. Kittlaus simply evaded it.

Enforcement argues that Geiger used a personal e-mail address for business, putting it on GWG paperwork for three customers, and that Kittlaus used a personal e-mail address to send Savage proposed pieces of sales literatures.³⁶⁴ Enforcement claims that Savage took no supervisory steps to monitor Geiger’s e-mail, and that when Savage made onsite visits to Geiger and Kittlaus, his review of the e-mail on their computers was “woefully inadequate.”³⁶⁵

WSSI’s procedures required that e-mail sent by representatives to more than one customer had to be approved.³⁶⁶ However, Enforcement’s Principal Investigator on this case³⁶⁷ testified that she found no e-mail sent by WSSI registered representatives to customers and no e-mail received from customers.³⁶⁸ Geiger testified that she received no e-mail at her personal e-mail address from clients, but only received account statements from issuers such as GWG, or annuity companies, or from Savage’s office.³⁶⁹ Kittlaus testified that he neither sent nor received customer e-mail on his personal account.³⁷⁰

³⁶¹ Compl. ¶¶ 69-70.

³⁶² Enforcement’s Pre-Hr’g Br., at 12.

³⁶³ Compl. ¶ 37.

³⁶⁴ Enforcement’s Post-Hr’g Br. at 29-30; Tr. 222-24, 309-10.

³⁶⁵ Enforcement’s Post-Hr’g Br. at 30.

³⁶⁶ Tr. 195-96.

³⁶⁷ Tr. 62, 65.

³⁶⁸ Tr. 196.

³⁶⁹ Tr. 279.

³⁷⁰ Tr. 363.

Savage testified that he found no e-mail in either Geiger's or Kittlaus's e-mail accounts when he made his onsite visits to them. Using their computers, he looked at "the entire archives" of their e-mail, and found no evidence they were using their personal e-mail accounts to conduct business.³⁷¹ Furthermore, Savage's un rebutted testimony established that he informed the firm's representatives that WSSI prohibited the use of e-mail for any business activities, and that he had to approve all correspondence.³⁷² In 2012, WSSI had not acquired an e-mail retention system, and thus Savage prohibited the use of e-mail for business. Savage required all representatives to sign an acknowledgement to evidence that they knew and understood this to be the firm's policy and that they would comply with it. He obtained signed acknowledgments from all representatives, including Geiger and Kittlaus.³⁷³

D. Discussion

NASD Rule 3010 requires members to establish and implement supervisory procedures reasonably designed to ensure compliance with applicable rules. The Complaint alleges that Savage and WSSI failed to do so with regard to supervision of branch offices and particularly the activities of Geiger and Kittlaus. The evidence, however, reflects that when notified of Geiger's concern that JB was investing too much in the high-risk debentures, Savage monitored Geiger's recommendations, and he personally contacted and queried the customers to whom she recommended GWG. The record establishes that Savage thoroughly reviewed Geiger's recommendations of GWG and repeated her recitation of the risks to ensure that Geiger had acted properly and that the customers were fully aware of the nature of their investments.

The Hearing Panel also finds that the Complaint's allegation and Enforcement's claim that Savage failed to conduct any onsite examinations of Geiger's office were not borne out by the evidence. The un rebutted evidence is that Savage personally visited Geiger's office the very day she began as a WSSI representative, and made a second onsite visit and audit in June 2012, about six months after the first visit. Although Savage did not visit Kittlaus's Chicago office where he was located from April to September 2012, Savage spoke regularly with Kittlaus by telephone, and met with him at least twice a month, if not weekly, once Kittlaus relocated to Florida in October. Savage also conducted an onsite audit in March 2013, shortly after learning about the Kittlaus letter.³⁷⁴ As Savage points out, NASD Rule 3010 (c)(1)(b) requires a member to inspect branch offices that do not supervise non-branch locations at least every three years. WSSI's procedures tracked the Rule and made the same requirement. Savage's onsite visits met the requirement.

³⁷¹ Tr. 847-53.

³⁷² Tr. 831-32.

³⁷³ Tr. 841-44; RX-39; RX-40.

³⁷⁴ Tr. 852.

As for the supervision of correspondence, the only alleged failure presented was the Kittlaus letter, and Kittlaus simply evaded the system in place to review correspondence and sent it surreptitiously.

For these reasons, the Extended Hearing Panel concludes that Enforcement did not prove by a preponderance of the evidence that Savage and WSSI were responsible for the supervisory failures alleged in the Fourth Cause of Action. It is, therefore, dismissed.

X. Sanctions for Kittlaus' Violation of NASD Rule 2210 and FINRA Rule 2010

FINRA's Sanction Guidelines recommend a fine of \$1,000 to \$29,000 and a suspension for up to 60 days for inadvertently circulating misleading communications. The Principal Consideration cited by the Guidelines is whether the communication was circulated widely.³⁷⁵ For intentionally circulating misleading communications, the Guidelines recommend a fine of \$10,000 to \$146,000 and suspension for up to two years. In more egregious cases, with numerous acts over an extended period, the Guidelines recommend considering a suspension for up to two years or a bar.³⁷⁶

Enforcement argues that Kittlaus' distribution of the letter was intentional. Considering this, as well as Kittlaus' disciplinary history, Enforcement recommends imposing a fine of \$25,000 and suspending him from associating with any member firm in any capacity for six months.³⁷⁷

The Sanction Guidelines call for the Hearing Panel to consider a number of factors in determining sanctions that are relevant to this case. They include: Kittlaus' relevant disciplinary history; whether he has accepted responsibility and acknowledged his misconduct; whether he attempted to conceal his misconduct or to mislead his firm; whether he attempted to conceal information from FINRA or to provide inaccurate or misleading testimony; and whether his misconduct was intentional, negligent, or reckless.³⁷⁸ Specific Guideline provisions relevant here require the Hearing Panel to fashion sanctions designed to "protect the investing public by deterring misconduct and upholding high standards of business conduct"; impose sanctions that are "more severe for recidivists"; and, in appropriate cases, to "require a respondent to requalify in any or all capacities."³⁷⁹

³⁷⁵ FINRA Sanction Guidelines at 79 (2015), <http://www.finra.org/industry/sanction-guidelines> ("Guidelines"). The current Guidelines, issued in March 2015, supersede prior versions. They apply to all disciplinary matters, including matters pending when the current Guidelines were issued, such as this one. *Id.* at 8.

³⁷⁶ Guidelines at 80.

³⁷⁷ Enforcement's Pre-Hr'g Br., at 26. Enforcement's brief was filed prior to the promulgation of the most recent edition of the Guidelines. At that time, the Guidelines recommended a fine for intentional misconduct of \$10,000 to \$100,000 and consideration of a suspension of up to two years.

³⁷⁸ Guidelines at 6-7 (Principal Considerations in Determining Sanctions Nos. 1, 2, 10, 12, 13).

³⁷⁹ Guidelines at 2-5 (General Principles Applicable to All Sanction Determinations Nos. 1, 2, 3, 7).

As discussed above, in late 1998, Kittlaus was sanctioned for distributing a communication to the public similar in nature and violating the same rule, NASD Rule 2210, that he violated by sending the Kittlaus letter to RR. He has failed to accept responsibility and admit his misconduct. Rather, after Enforcement showed Savage the Kittlaus letter in his OTR, Savage asked Kittlaus about it, and Kittlaus “totally” denied that he sent it.³⁸⁰ Kittlaus compounded his misconduct when, under oath at his OTR and at the hearing, he gave misleading testimony designed to persuade FINRA and the Hearing Panel that he did not write and send the letter. Kittlaus’ denials of responsibility have been consistently transparent and untrue. Finally, writing and sending the letter were intentional acts—not negligent or even reckless. Kittlaus is an experienced member of the securities industry whose disciplinary history should have made him especially aware of the requirements of NASD rules governing communications with the public.

Although there is no evidence from which to gauge how widespread Kittlaus’s dissemination of the letter was, based on the content and format of the letter, it would be extremely unreasonable to infer that Kittlaus sent it only to RR. Rather, reason compels the conclusion that Kittlaus sent the letter to other prospective customers, in addition to RR.

Thus, the Extended Hearing Panel concludes that, by distributing a letter so clearly violative of the requirements that communications must be fair and balanced and not misleading, Kittlaus poses a danger to the investing public. His intentional disregard of the requirements imposed by NASD Rule 2210 also violated his obligation to uphold the high standards of business conduct required of associated persons by FINRA Rule 2010. To fulfill the remedial purposes of deterring further such misconduct by Kittlaus and others, protect the investing public, and uphold high standards of business conduct, we conclude it is necessary to impose a fine of \$25,000, a suspension in all capacities for two years, and a requirement that Kittlaus requalify by examination before again becoming registered in any capacity in the securities industry.

XI. Conclusion and Order

For making false, exaggerated, unwarranted, and misleading statements in a communication with the public, in violation of NASD Rules 2210(d)(1)(A), (B), and (D), and FINRA Rule 2010, Respondent Louis Karl Kittlaus is fined \$25,000, suspended for two years from associating with any FINRA member firm in any capacity, and ordered to requalify by examination before again becoming registered in any capacity in the securities industry.³⁸¹ Respondent Kittlaus is also assessed costs of \$3,720.66, including a \$750 administrative fee. If this decision becomes FINRA’s final disciplinary action in this proceeding, the suspension shall begin on November 2, 2015, and end at the close of business on November 1, 2017. The fine and costs shall be payable when Respondent Kittlaus re-enters the securities industry.

³⁸⁰ Tr. 967.

³⁸¹ The Extended Hearing Panel has considered and rejects without discussion any other arguments made by the Parties that are inconsistent with this Decision.

The Department of Enforcement did not prove by a preponderance of the evidence that Respondents Wall Street Strategies, Inc., and Garry N. Savage, Sr. (i) made recommendations to customers to purchase securities unsuitable for them, in violation of NASD Rule 2310 and FINRA Rules 2111 and 2010; (ii) with Respondent Louis Karl Kittlaus, distributed misleading sales literature, in violation of NASD Rule 2210(d)(1)(A) and FINRA Rule 2010; and (iii) failed to establish and maintain a system to supervise registered representatives that was reasonably designed to achieve compliance with applicable NASD and FINRA rules, in violation of NASD Rules 3010(a) and (d) and FINRA Rule 2010. Therefore, the Complaint's first, second, and fourth causes of action are dismissed.

HEARING PANEL.

By: Matthew Campbell
Hearing Officer

Copies to:

Garry N. Savage (by overnight courier and first-class mail)
Louis Karl Kittlaus (by overnight courier and first-class mail)
Anthony W. Djinis, Esq. (by e-mail and first-class mail)
Paul J. Bazil, Esq. (by e-mail)
Brian K. Duncan, Esq. (by e-mail and first-class mail)
Lane A. Thurgood, Esq. (by e-mail and first-class mail)
Frank Mazzaelli, Esq. (by e-mail)
Jeffrey D. Pariser, Esq. (by e-mail)