

NEW YORK STOCK EXCHANGE, INC.

EXCHANGE HEARING PANEL DECISION 04-133

August 4, 2004

JEFFREY SCOTT LAFFERTY

FORMER REGISTERED REPRESENTATIVE

* * *

Misappropriated customer funds; effected unauthorized transfers of customer funds between accounts; submitted forged Letters of Authorization; issued unapproved correspondence to a customer; caused violations of Exchange Rule 440 and SEC Rules 17a-3 and 17a-4 by submitting forged Letters of Authorization; violated Exchange Rule 352(c)(ii) by reimbursing a customer for losses; caused a violation of Exchange Rule 342.16 by sending unreviewed correspondence to a customer; violated Exchange Rule 476(a)(4) by making material misstatements to the Exchange - Censure and permanent bar.

Appearances:

For the Division of Enforcement

Linda S. Riefberg, Esq.

Anthony Traina, Esq.

Scott M. Andersen, Esq.

For the Respondent:

Robert G. Stevens, Esq.

* * *

An Exchange Hearing Panel conducted a hearing on charges brought by the Exchange's Division of Enforcement against Jeffrey Scott Lafferty, a former registered representative with Prudential Securities Inc. (the "Firm"). Mr. Lafferty was charged with having:

- I. Engaged in conduct inconsistent with just and equitable principles of trade in that on one or more occasions he misappropriated funds and/or securities belonging to a customer of his member organization employer.
- II. Engaged in conduct inconsistent with just and equitable principles of trade in that on one or more occasions he breached his fiduciary duty to one or more customers by effecting an unauthorized transfer of customer funds and/or securities between customer accounts of his member organization.
- III. Engaged in conduct inconsistent with just and equitable principles of trade in that on one or more occasions he submitted, or caused to be submitted, a forged Letter of Authorization to his member organization employer to transfer funds and/or securities between customer accounts.

- IV. Engaged in conduct inconsistent with just and equitable principles of trade in that on one or more occasions he issued correspondence to a customer of his member organization employer that was not reviewed or approved by a supervisor of his member organization employer.
- V. Caused a violation of Exchange Rule 440 and SEC Rules 17a-3 and 17a-4 by submitting a forged Letter of Authorization to effectuate unauthorized transfers of funds and/or securities from a customer's account on one or more occasions.
- VI. Violated Exchange Rule 352(c)(ii) on one or more occasions by reimbursing a customer of his member organization employer for losses.
- VII. Caused a violation of Exchange Rule 342.16 by sending correspondence to a customer without having the correspondence reviewed and approved by his member firm organization.
- VIII. Violated Exchange Rule 345.12 by making a misstatement or an omission of fact on a Form U-4 on one or more occasions.
- IX. Violated Exchange Rule 476(a)(10) by making a misstatement or omission of fact on his application or submission filed with the Exchange on one or more occasions.
- X. Violated Exchange Rule 476(a)(4) in that on one or more occasions he made material misstatements to the Exchange.

Mr. Lafferty, through his attorney, submitted an Answer which denied the factual allegations of misconduct and denied the charges, although he admitted having made a payment to a customer. He claimed, as affirmative defenses, that the allegations were the result of the actions of third parties and were barred by the doctrine of unclean hands; he denied any fraud, misconduct, or other wrongdoing.

Mr. Lafferty appeared at the hearing, with his attorney, and testified. On the basis of the testimony and documentary evidence presented at the hearing, the Hearing Panel found as follows:

Background and Jurisdiction

1. Jeffrey Scott Lafferty ("Lafferty") was born on September 29, 1967. Lafferty entered the securities industry in May 1996 when he joined a non-member firm. Lafferty left that firm to join a member organization and was approved as a General Securities Representative by the Exchange in November 1996.
2. In June 1999, Lafferty left to join the Firm as a Financial Advisor, and was employed at the Firm's branch office located in Red Bank, New Jersey.

3. The Firm terminated Lafferty on September 14, 2000 after initiating an internal review of alleged unauthorized transfer of funds and securities from customer accounts and alleged unauthorized trading.
4. In December 2000, Lafferty joined a non-member firm.
5. On or about October 23, 2000, the Exchange's Division of Enforcement ("Enforcement") received a Uniform Termination Notice for Securities Industry Registration ("Form U-5") from the Firm.
6. On October 31, 2000 and March 27, 2001, the Exchange sent letters notifying Lafferty of its preliminary inquiry of this matter; by letter dated May 22, 2001, Enforcement notified Lafferty that it had opened a formal investigation into Lafferty's conduct while employed at the Firm. Lafferty replied to these letters.

Misappropriation of Customer Funds and Securities

7. From March to May 2000, funds from the accounts of two of Lafferty's customers, Customers A and B, were transferred to a third Lafferty customer, Customer C, who had recently opened an account with Lafferty. In March and April, checks totaling over \$19,000 were written from Customer A to Customer C; a check for \$8,000 was issued from Customer B's account to Customer C on or about May 23, 2000. Shortly thereafter, on or about May 26, 2000, Customer C submitted a Letter of Authorization ("LOA") for \$750, on which a check was written to Customer D, who had claimed a refund for overcharged commissions from Lafferty. These events occasioned a chain of unauthorized transactions in the following weeks, in which funds were transferred from one customer account to another to make up for deficits in these accounts.
8. Lafferty had a personal relationship with Customer C, a relationship which continues. Customer C is currently a partner of Lafferty's, and the business contact, in a limited liability company bearing Lafferty's name. Customer C used most of the funds transferred to her for personal expenses.

Unauthorized Transfers of Funds from Customer E to Customers A and B

9. Customer E opened an account with the Firm on or about July 1999 (the "E account"). Customer E, who was approximately 19 years old when she opened her account at the Firm, granted power of attorney to her father. From on or about July 1999 through September 14, 2000, Lafferty was the Financial Advisor and registered representative assigned to the E account.
10. On or about June 22, 2000, Lafferty misappropriated funds belonging to Customer E by wrongfully causing an LOA dated June 22, 2000, and containing a signature purporting to be that of Customer E, to be submitted to the Firm. This LOA directed that a journal be made from the account of Customer E to the account of Customer B in the amount of \$18,710 and, as a result, this journal was made to Customer B.

11. Lafferty did not have permission or authority from Customer E to journal \$18,710 to Customer B. Customer E's signature on the LOA was a forgery.
12. On or about June 30, 2000, Lafferty misappropriated funds belonging to Customer E by wrongfully causing an LOA containing a signature purporting to be that of Customer E, to be submitted to the Firm. This LOA directed that a journal be made from the account of Customer E to the account of Customer A in the amount of \$13,626.78 and, as a result, this journal was made to Customer A.
13. Lafferty did not have permission or authority from Customer E to journal \$13,626.78 to Customer A. Customer E's signature on the LOA was a forgery.

**Unauthorized Transfer of Funds from Customer F to Customer E –
Unapproved Correspondence**

14. On or about July 5, 2000, Lafferty prepared and provided, or arranged to have prepared and provided, a letter dated July 5, 2000, to Customer E's father, which outlined "corrected journal transfers" and "corrected stock transactions" that the Firm was purportedly making in the E account, and that would result in a "credit adjustment" of \$62,255.71 to the E account. The letter is signed by "Jeffrey Lafferty, Financial Advisor."
15. The Firm and/or its supervisory personnel were not aware of and did not approve Lafferty's July 5, 2000 letter to Customer E's father.
16. The July 5, 2000 letter refers to "corrected journal transfers" and identifies two journals erroneously made from the E account: the first relates to a journal from the E account to Customer B, on June 23, 2000, in the amount of \$18,710; and the second relates to a transfer from the E account to Customer A, on July 3, 2000, in the amount of \$13,626.78. The July 5, 2000 letter indicates that these journal transfers are purportedly being corrected by the Firm.
17. The July 5, 2000 letter, refers to a total credit adjustment to be made in the E account in the amount of \$62,255.71, which includes losses to the account in various stock transactions.
18. Customer F had transferred one or more accounts to the Firm's Red Bank, New Jersey branch office on or about November 1999 (the "F account"). From on or about November 1999 through September 14, 2000, Lafferty was the Financial Advisor and registered representative assigned to the F accounts.
19. On or about July 6, 2000, as Customer F left on a vacation out of the country, Lafferty misappropriated funds belonging to Customer F by wrongfully causing an LOA, containing a signature purporting to be that of Customer F, to be submitted to the Firm. This LOA directed that a check in the amount of \$62,255.71 be issued from

the F account and be payable to Customer E. Thereafter a check was issued to Customer E.

20. Customer F did not know Customer E or Customer E's father at the time the \$62,255.71 check was issued from Customer F's account.
21. Lafferty did not have permission or authority from Customer F to issue a check in the amount of \$62,255.71 made payable to Customer E. In fact, Customer E's signature on the LOA was a forgery.
22. Lafferty caused the \$62,255.71 check to be issued from Customer F's account and payable to Customer E on or about July 6, 2000 in order to conceal from the Firm trading losses, trading improprieties and unauthorized conveyances in or from the E account.

Unauthorized Transfer of Securities from Customer G to Customer H

23. Customer G opened an individual account with Lafferty at the Firm (the "G account") on or about July 15, 1999. From on or about July 1999 through September 14, 2000, Lafferty was the Financial Advisor and registered representative assigned to the G account.
24. On or about July 31, 2000, Lafferty misappropriated securities belonging to Customer G by wrongfully causing an LOA, dated July 31, 2000, and containing a signature purporting to be that of Customer G, to be submitted to the Firm. This LOA directed that 200 shares of a particular stock be journaled from the G account to the account of Customer H and, as a result, the 200 shares were thereafter journaled to Customer H's account.
25. The market value of the transferred stock on July 31, 2000 was approximately \$2,850.
26. Customer H opened an individual account with Lafferty at the Firm on or about August 1999 (the H account"). From on or about August 1999 through September 14, 2000, Lafferty was the Financial Advisor and registered representative assigned to the H account.
27. By June 30, 2000, the H account had a negative total net worth.
28. On July 6, 2000, a purchase of 500 shares of a stock was transacted for the H account. No additional funds or securities were added to the H account prior to the July 6 purchase.
29. A sale for the 500 shares purchased on July 6, 2000 was made on July 17, 2000, resulting in a net trading loss of approximately \$1,030, which immediately increased the negative total net worth in the H account. No additional funds or securities were added to the H account prior to the July 17 sale.

30. On July 31, 2000, Lafferty effectuated the transfer of 200 shares of a different stock from the G account to the H account. As a result of Lafferty's transfer, the total net worth for the H account changed from a negative total net worth of slightly over \$1,000 to a positive total net worth of \$1,793.
31. Lafferty did not have permission or authority from Customer G to transfer 200 shares of stock from his account to the H account. In fact, Customer G's signature on the LOA was a forgery.
32. Customer G did not know Customer H at the time of the transfer of 200 shares of stock from the G account to the H account.
33. Lafferty effected this unauthorized transfer in order to conceal from the Firm trading losses and trading improprieties by Lafferty in the H account. Had there been a negative net worth in the H account at the end of the month, there would have been an investigation by the Firm of the circumstances of these transactions.

End of the Game

34. In the spring of 2000, the operations manager at the branch office noticed that Lafferty would too quickly come up with requested authorizations in customer accounts. The operations manager, at one point, expressed her concern to the branch office manager but, in this instance, the branch office manager, checking with the customer, found that the transaction had been authorized.
35. In the summer of 2000, Lafferty's sales assistant noticed that there were frequent margin calls on Lafferty's customers and that, when operations personnel asked for paperwork on the margin calls, Lafferty would produce signed LOAs within minutes, even when no customers had come in to sign the LOAs. However, she did not express her concerns to supervisory personnel until the end of August, when she was questioned by the branch office manager about the matter.
36. In early August 2000, Customer G called to complain about the incorrect information on his statement. Lafferty was not in his office, and the customer spoke to the branch manager instead. The branch manager then spoke to Lafferty who claimed to have no idea about the matter. Lafferty's response was accepted.
37. When Customer F returned from vacation towards the end of August, she met with Lafferty and was told not to worry; the erroneous transfer of the funds was a computer error and had been corrected. Lafferty did not bring Customer F's complaint of transfer of funds from her account to the branch office manager's attention.
38. Customer F herself telephoned the branch manager; and informed him of the unauthorized transfer of some \$62,000 from her account. Again, when interviewed,

Lafferty claimed no knowledge of what had happened. On September 5, Lafferty was suspended, pending investigation by the Firm.

Sharing in Customer Losses

39. On or about August 30, 2000, the Firm determined that Customer F did not authorize the transfer of funds from her account to the E account and debited \$62,255.71 from the E account, returning the funds to Customer F.
40. On or about September 4, 2000, Customer E contacted the branch office manager to question why \$62,255.71 was transferred from her account to Customer F's account without her authorization.
41. Customer E claimed that she was entitled to the money and provided the Firm with the July 5, 2000 letter that was addressed to her father and sent by Lafferty which indicated the E account would be credited \$62,255.71 for "corrected journal transfers" and "corrected stock transactions."
42. On or about October 31, 2000, Lafferty made payments to Customer E totaling \$74,553.30 to reimburse her for losses.
43. The Firm did not contribute to or authorize Lafferty's payment of \$74,553.30 to Customer E to settle and/or withdraw her complaint.
44. On October 31, 2000, an attorney for Customer E sent a letter to the Firm that restated her allegations against Lafferty and then stated the following:

"You are hereby notified that [Customer E] is formally withdrawing this complaint. You are instructed to amend your records and documents that may have been filed to reflect that [Customer E's] complaint and the allegations made have been withdrawn. You are also advised that [Customer E] is releasing Prudential Securities from any and all claims that she may have against it as a result of these allegations.

Please confirm to me in writing that [Customer E's] complaint has been withdrawn with Prudential and all regulatory agencies."
45. Lafferty received a copy of the October 31, 2000 letter from Customer E's attorney regarding the withdrawal of her complaint.
46. Lafferty's payments to Customer E were made to reimburse for losses in the E account for unauthorized trades and transfers of funds that were transacted by Lafferty without authorization.
47. Lafferty had requested, in return for his reimbursement to Customer E, that her complaint to the Firm be withdrawn.

Misstatements to the Exchange

48. During his on-the-record testimony before the Exchange on June 11, 2003 and June 19, 2003, Lafferty made material misstatements regarding his involvement and knowledge concerning the Exchange's investigation into the unauthorized transfers of fund and securities for the customer accounts that he serviced while employed by the Firm.

DISCUSSION

This matter requires little discussion. The documentary evidence presented was irrefutable. The witnesses against Mr. Lafferty were credible. Mr. Lafferty's own testimony was incredible in every material respect, including his inability to provide his current home address.

This matter was set off by Mr. Lafferty's effort to indirectly provide funds to a woman with whom he was developing a personal relationship. He transferred funds from the accounts of two of his customers to the recently opened account of this woman. Illicit transfers between customer accounts escalated during the spring and summer of 2000, as Mr. Lafferty engaged in a veritable Ponzi scheme, seeking to cover up deficits he had created in customer accounts by transferring funds from other customers. This scheme blew up on him in short order.

Mr. Lafferty's denials of any responsibility, or even of any knowledge, of unauthorized transfers between his customers is plainly incredible. His refusal to face the truth is most blatantly expressed in his assertion that he had no relationship with Customer C, the first customer to whom funds were illicitly transferred, thereby starting a chain of misappropriation. Customer C is currently Mr. Lafferty's partner in a business bearing Mr. Lafferty's name.

Almost as blatant is Mr. Lafferty's testimony with respect to the plight of Customer F. He testified that, when Customer F told him of the unauthorized transfer of some \$62,000 from her account while she was on vacation, he said he would look into it, and promptly reported it to his branch manager. But the customer had been informed by Lafferty, at the time she confronted him, that he already knew of the "error" and it had been corrected. He, of course, never told the branch manager of this problem.

It is similarly impossible to accept his claims of ignorance as to the treatment of Customer E's account, as to which he sent the customer an accounting of "corrected journal transfers," and as to which he reimbursed the customer for losses. It is impossible, in total, to accept his ignorance of this dizzying series of unauthorized Letters of Authorization and transfers that occurred among his unfortunate customers.

At least, Mr. Lafferty did not try to cast responsibility for these misdeeds on others. But his illicit scheme, which grew worse and worse until he was caught; his blatant lies to his customers, to his employer and to the Exchange; his false testimony and refusal to take responsibility – all require that he be permanently barred from the securities industry.

DECISION

The Hearing Panel, by unanimous vote, found Mr. Lafferty guilty of Charges I, II, III, IV, V, VI, VII and X.¹

PENALTY

In view of the above findings, the Hearing Panel, by unanimous vote, determined that Mr. Lafferty be censured and permanently barred from membership, allied membership, approved person status, and from employment or association in any capacity with any member or member organization.

For the Hearing Panel

Milton M. Stein
Hearing Officer

¹ Some of Mr. Lafferty's misconduct occurred after he left the Firm – the reimbursement of a customer for losses, and Mr. Lafferty's misstatements in the course of the Exchange's investigation. But, pursuant to Exchange Rule 477, the Exchange retains jurisdiction over these matters, since Mr. Lafferty had been timely informed of the Exchange's investigation and the misconduct concerned his efforts to cover up matters which had occurred while Mr. Lafferty had been employed at the Firm. However, the Hearing Panel has not considered Charges VIII and IX, concerning alleged misstatements on Form U-4 filings submitted after Mr. Lafferty left the Firm, since these filings were submitted in the course of his employment with a non-member firm and were not submitted to the Exchange. Exchange Rules 345.12 and 476(a)(10) specifically concern submissions to the Exchange.