

NYSE AMEX LLC

HEARING BOARD DECISION 09-AMEX-05
WEDBUSH MORGAN SECURITIES
MEMBER ORGANIZATION

April 8, 2009

* * *

Violated Article V, Section 4(e) of Amex Constitution in that its then Compliance Registered Options Principal ("CROP") made misstatements to Amex by representing that it had taken corrective action in response to examination findings when it had not; violated Amex Rule 31 in that its then CROP failed to cooperate and timely comply with specific deadlines set by Amex to provide information responsive to Amex requests made in connection with ongoing Amex investigation; violated Amex Rule 320(c) by failing to implement adequate controls, including a separate system of follow-up and review, to verify that all necessary steps were taken by its then CROP, who was also the Firm's Compliance Director, to comply accurately and within the time frames required to Amex requests for information and/or documentation made in connection with an ongoing Amex investigation – Consent to censure and \$15,000 fine.

Appearances:

For the Division of Enforcement
Robert A. Marchman, Esq.
Kenneth R. Bozza, Esq.
Shawn Mallon, Esq.

For Respondent
Eric Seagall, Esq.

* * *

A Hearing Officer on behalf of the NYSE Amex LLC ("NYSE Amex") considered a Stipulation of Facts and Consent to Penalty entered into between NYSE Regulation, Inc.'s Division of Enforcement ("Enforcement") and Wedbush Morgan Securities ("Respondent" or the "Firm"), an NYSE Amex¹ member organization. Without admitting or denying guilt, Respondent consented to a finding by a Hearing Officer that it:

09-AMEX-05.1

¹ On or about October 1, 2008, the American Stock Exchange ("Amex") was acquired by NYSE Euronext and was renamed NYSE Amex LLC. Thus, while the rules of NYSE Amex govern the procedural aspects of this Stipulation and Consent, because the conduct referred to herein occurred prior to the acquisition date, the violations were of "Amex Rules" or the "Amex Constitution".

- I. Violated Article V, Section 4(e) of the Amex Constitution in that its then Compliance Registered Options Principal ("CROP") made misstatements to the Amex by representing that it had taken corrective action in response to examination findings when in fact Respondent had not taken such corrective action.
- II. Violated Amex Rule 31 in that its then CROP failed to cooperate and timely comply with specific deadlines set by the Amex to provide information responsive to Amex requests made in connection with an ongoing Amex investigation.
- III. Violated Amex Rule 320(c) in that it failed to implement adequate controls, including a separate system of follow-up and review, to verify that all necessary steps were taken by its then CROP, who was also the Firm's Compliance Director, to comply accurately and within the time frames required to Amex requests for information and/or documentation made in connection with an ongoing Amex investigation.

For the sole purpose of settling this disciplinary proceeding, without adjudication of any issues of law or fact, and without admitting or denying any allegations or findings referred to in the Stipulation of Facts and Consent to Penalty, Respondent stipulates to certain facts, the substance of which follows:*

Background and Jurisdiction

1. During all relevant periods herein, Respondent was a Regular Member organization of the American Stock Exchange ("Amex"). Respondent is currently an NYSE Amex Member Firm conducting multiple areas of business that include: retail private client servicing, investment banking, institutional prime brokerage and clearing.
2. Following a referral by the Amex Sales Practice Examination Department, which conducted an initial options sales practice examination of Respondent pursuant to its authority as the Firm's Designated Options Examining Authority ("DOEA"), the Firm was notified of this investigation.
3. On or about July 11, 2008, Respondent was issued a Charging Memorandum in connection with the matters discussed herein, and on or about August 19, 2008 Respondent filed an Answer.

Overview

4. Pursuant to an examination conducted of Respondent by the Amex Sales Practice Examination Department ("SPED"), which detected seven accounts that appeared to permit trading activity that was inconsistent with the parameters established by the

* Hearing Officer Note: The facts, allegations, and conclusions contained in paragraphs 1 to 19 are taken from the executed Stipulation of Facts and Consent to Penalty between Enforcement and Respondent. No changes have been made to the stipulated paragraphs by the Hearing Officer.

Firm's Written Supervisory Procedures ("WSPs"), the Firm made misstatements to the Amex that it took corrective action with respect to the accounts when it failed to do so. Thereafter, the Firm failed to cooperate and timely comply with specific deadlines set by the Amex to provide information with respect to its misstatement. The Firm also failed to implement adequate controls, including a separate system of follow-up and review, to verify that all necessary steps were taken by its then CROP, who was also at the time the Firm's Compliance Director, to comply with the Amex's requests in an accurate and timely manner.

Regulatory Framework

5. During all relevant periods herein, Article V, Section 4(e) of the Amex Constitution provided that a member, member organization or approved person are prohibited from making a misstatement, or submitting a report or statement containing a misstatement upon a material point to the Board, to the Chairman or any officer or representative of the Amex.
6. During all relevant periods herein, Amex Rule 31 provided that a member, member organization, approved person or any employee, partner, trustee or director of a member organization or member shall comply with any request by an authorized representative or committee of the Amex to produce his or its books, papers or records, or to appear and testify as to any matter pertaining to his or its business, within the time specified by the representative or committee of the Amex making the request.
7. During all relevant periods herein, Amex Rule 320(c) provided that the general partners, directors, trustees of each member organization shall provide for appropriate supervisory control and shall designate a general partner, principal executive officer, trustee to assume overall authority and responsibility for internal supervision and control of the organization and compliance with securities laws and regulations. This person shall: (1) delegate to qualified principals or employees responsibility and authority for supervision and control of each office, department or business activity, and provide for appropriate procedures of supervision and control; and (2) establish a separate system of follow-up and review to verify that the delegated authority and responsibility is being properly exercised.

Misstatements to the Amex and Untimely Responses

8. During the period from January 28, 2002 to February 1, 2002, the Amex SPED conducted an initial options sales practice examination of Respondent in which it examined options accounts, including examination for compliance with all option account documentation requirements. In addition, SPED was provided with the Firm's November 2001 WSPs, which were purported to be in effect at the time of the examination.

9. On May 2, 2002, following its examination of the Firm, SPED held a staff exit interview via telephone with the Firm's CROP who was notified by SPED of several deficiencies detected in seven customer accounts that were approved for uncovered options trading contrary to the "Annual Income" and/or "Net Worth" requirements prescribed by the Firm's November 2001 supervisory procedures. SPED observed uncovered options trading in five of these seven accounts and requested that Respondent take corrective action on the accounts where deficiencies were detected.
10. On May 8, 2002, SPED memorialized its May 2, 2002 exit interview in a letter addressed to the Firm's CROP.
11. On June 20, 2002, in a letter signed by the Firm's CROP, Respondent responded to SPED's May 8, 2002 letter indicating that Respondent had taken corrective action regarding the deficiencies. The letter indicated that the accounts were downgraded in that the approved option levels were decreased until Respondent received and approved updated agreements or retrieved required missing information.
12. On December 18, 2002, SPED conducted a follow-up examination at the offices of Respondent to verify that the Firm's corrective action, had in fact been taken, and to also determine whether any additional deficiencies had occurred. During this follow-up examination, SPED determined that Respondent in fact had failed to take any corrective action with respect to the above referenced seven accounts.
13. On December 19, 2002, SPED held a telephone exit interview with the Firm's CROP and another Firm employee to discuss Respondent's continued failure to take corrective action on the seven customer accounts at issue. During the December 19, 2002 conversation, SPED requested that Respondent provide SPED with a written response, by no later than December 31, 2002, as to why the Firm failed to take corrective action with respect to the seven accounts.
14. On January 8, 2003, after not receiving any response from Respondent to its request of December 19, 2002, SPED telephoned the Firm's CROP and left a message. Later that day, SPED received an undated letter via facsimile from the Firm, which merely listed the seven accounts at issue and indicated whether option trading had occurred in those accounts. The letter also represented that the stated annual income and/or net worth on several of the subject accounts which traded options fell "within the parameters established by the Firm at the time the accounts were opened according to the 1999 version of [the Firm's] policy F.13."² Respondent did not provide a copy of its 1999 supervisory procedures as part of this response or as part of any future response.
15. On January 8, 2003, SPED sent an email to the Firm that requested an explanation as to why Respondent represented in its June 20, 2002 letter that the seven accounts at issue were downgraded, when in fact they were not. The email further requested that

² "F.13" refers to the relevant section of the Wedbush Procedures Manual entitled "OPTIONS PROCEDURES FOR EXCHANGE LISTED OPTIONS."

- Respondent provide the Amex with copies of all monthly account statements for the seven accounts at issue, for the period of January 1, 2002 through January 8, 2003, in order to determine the extent of any uncovered options trading in those accounts. SPED requested that Respondent provide the aforementioned information and documentation to the Amex by no later than January 15, 2003. When Respondent failed to provide the documentation, SPED made a subsequent request requiring that the Firm provide the information by February 12, 2003. The Firm again failed to provide the information without an explanation for the failure to cooperate.
16. The Enforcement Department of the Financial Industry Regulatory Authority's ("FINRA's") Amex Regulation Division ("FINRA Enforcement") was subsequently informed by Respondent's former Senior Registered Options Principal ("SROP") that there was no 1999 version of the Firm's supervisory procedures. The SROP further stated that the 1999 procedures referenced in the letter from the Firm sent via facsimile on January 8, 2003 were in fact the 1993 procedures. It was further explained by Respondent that the seven accounts in question were approved for uncovered options trading consistent with options new account procedures set forth in the Firm's 1993 procedures, which Respondent had not previously furnished to the Amex.
 17. Respondent, thereafter provided FINRA Enforcement copies of the 1993 procedures and the account statements previously requested but it never explained why the Firm represented in the June 20, 2002 letter that the accounts in question had been downgraded, when no such action was ever taken. FINRA Enforcement confirmed that the 1993 procedures were in effect at the time of the opening of each of the seven accounts and that the accounts met the requirements for trading uncovered options as set forth in the 1993 procedures. Had Respondent supplied the correct procedures governing these accounts at the time of the initial SPED examination, the subsequent requests for information and delayed responses outlined above would not have occurred.
 18. The conduct described above in paragraphs 11 through 17 constitutes violations by Respondent of Article V, Section 4(e) of the Amex Constitution and Amex Rules 31 and 320(c).

Other Factors Considered

19. Enforcement considered, amongst other factors, that it ultimately was determined that the seven accounts in question were approved for uncovered option trading consistent with 1993 Respondent options new account procedures which were in effect at the time of the opening of each of the seven accounts in question.

DECISION

The Hearing Officer, in accepting the Stipulation of Facts and Consent to Penalty, found that Respondent committed the offenses as set forth above.

PENALTY

In view of the above findings, the Hearing Officer imposed the penalty consented to by Respondent of a censure and a \$15,000 fine.

For the Hearing Board

Peggy Kuo - Chief Hearing Officer