

**Disciplinary Panel
American Stock Exchange, LLC**

	:	Case No. 01-02
	:	
IN THE MATTER	:	Hearing Officer - JN
OF	:	
ROBERT FAULKNER	:	Disciplinary Panel Decision
	:	
	:	December 15, 2003

Digest

Respondent (1) failed to report a customer complaint to his firm and corresponded with a customer from his home address in contravention of the firm's policies, in violation of Exchange Rule 345(a)(4); (2) effected unauthorized trades, in violation of Exchange Rule 924(a); (3) guaranteed a customer against loss, in violation of Exchange Rule 341, Commentary .08(5)(2); and (4) failed to inform the Exchange or his firm that he had become involved in litigation and an arbitration proceeding, in violation of Exchange Rule 341, Commentary .08(5)(9). For these offenses, he was suspended for 90 calendar days and made subject to a nine-month period of heightened supervision.

DECISION

I. Introduction

On February 27, 2003, the Exchange issued a Statement of Charges, alleging that Respondent failed to report a customer complaint to his firm and corresponded with a customer from his home address in contravention of the firm's policies, in violation of Exchange Rule 345(a)(4); effected unauthorized trades, in violation of Exchange Rule 924(a); guaranteed a customer against loss, in violation of Exchange Rule 341, Commentary .08(5)(2); and failed to inform the Exchange or his firm that he had become involved in litigation and an arbitration proceeding, in violation of Exchange Rule 341, Commentary .08(5)(9). Faulkner filed an Answer that admitted most of the allegations, while asserting various mitigating circumstances.

The parties executed a Stipulation of Facts (“Stip.”) in which Respondent agreed that he had engaged in the conduct alleged in the Statement of Charges. On October 1, 2003, an Exchange Disciplinary Panel conducted a hearing on the question of sanctions. Pages of the transcript of that hearing are cited as “Tr.”

II. Factual Background

Respondent, a broker with twenty-five years of experience and no disciplinary history, was employed by Salomon Smith Barney (“Smith Barney”), where he handled the account of a retired McDonnell Douglas executive. That customer followed an investment strategy consisting of selling “covered calls,” *i.e.*, calls covered by his own McDonnell Douglas shares (Stip., par. 3.1).¹ On two occasions in May of 1995, Respondent sold calls on McDonnell Douglas stock for the customer without his knowledge or authorization and without any prior written discretionary authority from him (*Id.*, at pars. 3.2-3.4). After the customer complained, Faulkner promised to cancel the trades (*Id.*, at par. 3.5), but never did so, explaining that cancellation would have required notification to Smith Barney, which would have then held him responsible (*Id.*, at par. 3.7). Though Smith Barney’s policies required that Faulkner report such customer complaints to the firm, he failed to do so (*Id.*, at par. 6.0). In June of 1995, at Respondent’s suggestion, the customer agreed to allow him to try to recover the losses through future trading (*Id.*, at par. 3.7).

In September of 1995, Respondent sent the customer a letter acknowledging his responsibility for the above unauthorized trades and for any subsequent trading that he would conduct until the customer was at least made whole (*Id.*, at par. 4.0). Faulkner wrote this letter

¹ A “call” is “the right to buy a specific number of shares at a specified price by a fixed date.” NASD, Glossary of Investing Terms, p. 12 (2001).

from his home because correspondence from his business address would have become known to the firm (Id.). Corresponding with a customer from a broker's home address was contrary to Smith Barney's policies (Id., at par. 6.0). In December of 1995, the customer sent Faulkner a memorandum of understanding, which Respondent signed in July of 1996. It stated, inter alia, that Respondent "agreed to reimburse [the customer] for any losses that resulted from [the 1995 unauthorized transactions] and any losses that resulted from the attempt to trade out of the original losses" (Id., at par. 4.1).

In September of 1998, the customer sent Respondent a letter stating his desire that Faulkner discontinue efforts to trade out of the losses and suggesting alternatives for payment of the losses alleged (Id., at par. 5.0). Faulkner failed to respond to that letter and to follow-up letters of November of 1998 and January of 1999. In June of 1999, the customer filed a civil action against Respondent, who did not notify the Exchange or his firm of the filing, although an Exchange Rule and Smith Barney's policies required such reporting (Id., at pars. 2.3, 5.2). The customer later withdrew that litigation and filed an NASD arbitration proceeding against Faulkner and the firm. Again Respondent failed to notify the Exchange or his firm of this arbitration proceeding, although an Exchange Rule and Smith Barney's policies required such notification (Id., at pars. 2.3, 5.3).

The parties agree that the customer sustained losses of at least \$50,000 and that, ultimately (after the arbitration was filed), Faulkner personally made restitution of \$55,000 to the customer and \$7,500 to Smith Barney (Tr. 26-28, 30-31).

In March of 2000, Smith Barney terminated the Respondent's employment, with the Form U-5 reflecting his failure to have reported a customer complaint (Stip., par. 1.0; Tr. 61-62). Since April of 2000, Faulkner has been associated with Huntleigh Securities Corporation, a firm

that hired him after disclosure of the relevant facts, and has endorsed his performance and urged that he be allowed to remain in the industry (Tr. 58-59; letter of April 11, 2003, attached to Respondent's post-hearing memorandum).

III. Liability

In the Stipulation, Faulkner agreed that he had engaged in the misconduct alleged in the Statement of Charges (Stip., pars. 7.0-7.3). The Panel thus concludes that Respondent (1) failed to report a customer complaint to his firm and corresponded with a customer from his home address in contravention of the firm's policies, (2) effected unauthorized trades, (3) guaranteed a customer against loss, and (4) failed to inform the Exchange or his firm that he had become involved in litigation and an arbitration proceeding. This conduct violated Exchange Rules 345(a)(4); 924(a); 341, Commentary .08(5)(2); and 341, Commentary .08(5)(9), respectively.

IV. Penalty

A. Suspension

The parties disagree widely about the length of time for which Respondent should be suspended. Enforcement urges a suspension of at least 18 months, while Respondent argues for a suspension of no more than 10 days (Tr. 51, 53, 64-65, 69).

Faulkner's misconduct centered on the unauthorized transactions, from which, as Enforcement stated, everything else flowed (Tr. 75). In these circumstances, and in the absence of any directly applicable Exchange guideline, the Panel begins by looking to the NASD Sanctions Guidelines ("Guidelines") for suggestions as to unauthorized transactions (at p. 102).² For non-egregious unauthorized transactions, the Guidelines recommend suspensions from ten

² The Panel may appropriately consider the NASD Sanction Guidelines. See David Wong, Exch. Act Rel. No. 45,426, 2002 SEC LEXIS 339 at *22 (February 8, 2002). Indeed, Enforcement referred to this source in the instant case (Tr. 38-41).

days to one year; for egregious unauthorized transactions, they recommend consideration of suspensions of up to two years or a bar (p. 102).

The primary question is whether the unauthorized transactions in this case were egregious. They involved two sales on behalf of one customer and thus were not “quantitatively egregious” (Guidelines, p. 102, fn. 2). Nor does the record show that Faulkner entered into the transactions through improper “motives” or “bad faith,” so as to render them “qualitatively egregious” (Id.). Both transactions generated commissions totaling only \$200 to \$250 (Tr. 44). Respondent claims that the transactions paralleled strategies that he and the customer had previously engaged in and were in effect “accidents” (Tr. 78-79). Enforcement stated that it was not contending that Faulkner made the sales in order to generate commissions or to “hurt the customer” (Tr. 43). Respondent, a successful securities professional for many years, would not deliberately engage in unauthorized transactions and risk his entire career in order to pocket an extra \$250 in commissions.

The Guidelines recognize a third category of egregiousness: “unauthorized trading accompanied by aggravating factors” (Guidelines, p. 102, fn. 2). Enforcement argues that the trades were egregious because Respondent’s guarantee against loss, coupled with his nondisclosures, enabled him to hide the facts and evade regulatory action for over three years (Tr. 41-42, 44, 46, 48, 52).

The Panel agrees that such concealment involves serious misconduct, and, as suggested in the NASD Guidelines, it considered imposing a lengthy suspension, as Enforcement requested. However, the Panel found counterbalancing considerations, which led it to conclude that a shorter suspension would be appropriate. First, Faulkner hid nothing from the customer, who at all times was aware of the unauthorized trades and of Respondent’s efforts to recover the

involved losses.³ Nor was there any “history of similar misconduct,” which would be an aggravating circumstance, according to the Guidelines (at p. 102, fn. 2). Indeed, there was no disciplinary history at all. On this record, the Panel concludes that the instant misconduct was an isolated instance in an otherwise unblemished 25-year career.

Moreover, evidence suggests that Faulkner has qualities that continue to make him an asset to the industry. Respondent’s current firm hired him three years ago, knowing of the customer’s complaint, and has monitored his performance, received no customer complaints, and detected no irregularities. Its compliance director endorsed “his experience, his credibility and his work ethic” and believed that “Mr. Faulkner learned a very difficult, but valuable, lesson from his mistake.” Having observed the Respondent, the Panel credits his statement that:

If I had to do it again, believe me, that error would be reported. I wouldn’t ask the client first how he felt and it would have gone the other way. You know, I have suffered the loss of a good career at Smith Barney. I have suffered the loss of deferred compensation, stock plans, loss of business and it has been a real disaster in my life and unfortunate lesson learned. (Tr. 79).

In addition, the record shows that Respondent “cooperated with the Enforcement Department, once Enforcement was referred the case. There was a telephone deposition that was conducted of Mr. Faulkner, never any problems with that....He has been cooperative, yes” (Tr. 61). Such cooperation is also one of the principal sanctions considerations (Guidelines, p. 10).

Considering all of the circumstances, the Panel concludes, on balance, that Faulkner’s misconduct was serious, requiring a longer suspension than he proposed, but was not so egregious as to justify a suspension as lengthy as Enforcement sought. The parties agreed that

³ Respondent’s counsel emphasized the fact that his client made restitution to the customer (Tr. 57, 68). But that payment arose out of the arbitration proceeding; it did not happen “prior to detection and intervention” and is, therefore, entitled to less weight (Guidelines, p. 9).

the Panel should impose a unitary sanction for the violations, because the misconduct alleged reflects a single course of conduct (Tr. 37-38). The Panel concludes that it is appropriate to suspend Faulkner in all capacities for 90 calendar days.

B. Period of Supervision

Each side suggested that the sanction include a period of “heightened supervision” for Faulkner (Tr. 53, 65). The Panel agrees. Such a requirement, to be imposed for nine months following his return from the suspension, would safeguard against any repeat misconduct and would serve to remind Respondent daily of his past errors.

To implement such supervision, the Panel adopts Enforcement’s suggestion that Faulkner, his counsel, and his current employer (which, as noted, submitted a strong letter of support) submit to Enforcement a draft plan for heightened supervision (Tr. 81). Such a draft shall be submitted within 60 calendar days of the date upon which this Decision becomes final. A plan that is satisfactory to Enforcement shall be put into effect as soon as practicable after Enforcement’s approval.

The Disciplinary Panel further finds that the results of this disciplinary proceeding should be publicly disclosed, as provided in Rule 12 of the Exchange Rules on Disciplinary Proceedings.⁴

V. Conclusion

Based on the foregoing, the Disciplinary Panel, by unanimous vote, finds that Respondent Faulkner (1) failed to report a customer complaint to his firm and corresponded with a customer from his home address in contravention of the firm’s policies, (2) effected unauthorized trades,

⁴ Rule 12 exempts from publicity those cases where the Panel finds that the offense “related solely to minor administrative requirements of the Exchange and does not materially affect the public interest or the interest of investors.” Those exemptions do not apply to the facts of this case.

(3) guaranteed a customer against loss, and (4) failed to inform the Exchange or his firm that he had become involved in litigation and an arbitration proceeding. This conduct violated Exchange Rules 345(a)(4); 924(a); 341, Commentary .08(5)(2); and 341, Commentary .08(5)(9), respectively.

For this misconduct, the Panel orders that Respondent be suspended in all capacities for 90 calendar days and be required to submit to a nine-month period of heightened supervision, as set out above.

FOR THE DISCIPLINARY PANEL

Jerome Nelson, Chair

Dated: December 15, 2003
Washington, DC

Copies to: Leo V. Garvin, Jr., Esq. (*via facsimile and first class mail*)
Eric S. Brown, Esq. (*via facsimile, electronic mail and first class mail*)
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Disciplinary Panel
American Stock Exchange LLC

.....	X	
	X	
IN THE MATTER	X	
OF	X	STATEMENT OF CHARGES
ROBERT FAULKNER	X	Case Number 01-02
.....	X	February 27, 2003

Charges are hereby preferred pursuant to Exchange Rule 345(d) of the Constitution of the American Stock Exchange LLC (the “Exchange”) against ROBERT FAULKNER (“Faulkner”) (CRD # 849152), a former employee of Salomon Smith Barney Inc. (“Salomon”), a Regular Member organization of the Exchange.

STATEMENT OF FACTS:

- 1.0 From 1987 through March 2000, Faulkner was employed as a financial consultant for Salomon Smith Barney (“Salomon” or “the Firm”) and its predecessor firms. Faulkner was terminated from Salomon in March 2000. In April 2000, Faulkner joined Huntleigh Securities Corporation as a financial consultant, and remains in that position today.
- 2.0 During all relevant periods herein, Exchange Rule 345(a)(4) provided that the Exchange may disapprove or suspend or withdraw its approval of the employment of an employee of a member or member organization and the Exchange may, in addition to or in lieu of any such action, (a) censure him; (b) declare him ineligible for employment in specified capacities; and/or (c) assess a fine against

- him if the Exchange determines that such employee has been guilty of any conduct or proceeding inconsistent with just and equitable principles of trade.
- 2.1 During all relevant periods herein, Exchange Rule 924(a) provided that no employee of a member organization shall exercise any discretionary power with respect to trading in options contracts in a customer's account unless such customer has given prior written authorization and the account has been accepted in writing by a Registered Options Principal who is qualified with respect to the category of options trading for which discretionary power is to be exercised (debt or equity).
- 2.2 During all relevant periods herein, Exchange Rule 341, Commentary .08(5)(2) provided that, as a condition of registration of an employee, each prospective registered employee sign an agreement that in consideration of the American Stock Exchange LLC approving an employee's application, the employee submits himself to the jurisdiction of the Exchange and agrees that he will not represent to any customer that he will personally guarantee the account of such customer.
- 2.3 During all relevant periods herein, Exchange Rule 341, Commentary .08(5)(9) provided that, in consideration of the American Stock Exchange LLC approving an employee's application, the employee agrees to notify the Exchange and his employer promptly if, while an employee registered with the Exchange or an officer of a member corporation, he becomes involved in any litigation or in any administrative proceeding or if any judgment is obtained against him.

- 3.0 In 1987, Faulkner inherited the Robert E. Perkins (“Perkins”) Revocable Living Trust Account (“Perkins Trust Account”) from another registered representative at Salomon.
- 3.1 According to Perkins’ Options New Account Form, Perkins was a retired executive from McDonnell Douglas (“MD”) whose investment objectives were “growth” and “aggressive”. A portion of his investment strategy included writing covered calls against his MD stock to generate income and enhance the value of his account.
- 3.2 At no time herein did Faulkner obtain prior written authorization from Perkins to exercise discretion in making trades for the Perkins Trust Account without first speaking to Perkins.
- 3.3 On May 12, 1995, Faulkner, without knowledge or authorization from Perkins, placed an order to sell 15 MD November 55 calls at 13 ½ for the Perkins Trust Account, and the trade was ultimately executed.
- 3.4 On May 19, 1995, Faulkner, again without knowledge or authorization from Perkins, placed an order to sell 15 MD August 46 5/8 calls at 23 1/8 for the Perkins Trust Account, and the trade was ultimately executed.
- 3.5 After receiving confirmation statements from Salomon for each of the trades referred to in above paragraphs 3.3 and 3.4, Perkins verbally complained to Faulkner about each trade, and on each occasion Faulkner indicated that he would promptly cancel the trade.

- 3.6 Upon review of his May 1995 account statement for the Perkins Trust Account, Perkins learned that the trades referred to in above paragraphs 3.3 and 3.4 had not been cancelled by Faulkner despite Faulkner's promises to the contrary.
- 3.7 In or about June 1995, Perkins spoke with Faulkner by telephone to discuss why the trades referred to in above paragraphs 3.3 and 3.4 had not been cancelled. Faulkner explained to Perkins that cancellation of the two trades would require notification to branch management. Faulkner also explained to Perkins that such notification would result in Salomon holding Faulkner responsible for the financial loss associated with the trades.¹ Faulkner alternatively suggested that Perkins allow him to attempt to recover the unrealized loss from the two trades specified in above paragraphs 3.3 and 3.4 through future trading of MD covered calls. Perkins ultimately agreed to this strategy.²
- 4.0 On September 1, 1995, Faulkner sent Perkins a letter, from his home on personal stationery, acknowledging that Faulkner alone was responsible for the trades specified in above paragraphs 3.3 and 3.4, and also indicating that any subsequent trading in Perkins' MD position was Faulkner's responsibility until Perkins was made whole or better. This letter, as well as all future correspondence between Faulkner and Perkins regarding trading in the Perkins Trust Account, was directed to Faulkner's home address after Faulkner explained to Perkins that any

¹ By the time Perkins had received the account statement, each of the positions had moved against Perkins, resulting in an unrealized loss of several thousand dollars.

² The strategy involved Faulkner continuing to write "out of the money" calls against Perkins' MD stock, buying back the calls and "rolling them up" to a higher strike price or "rolling them out" at the same strike price with a more distant expiration date as they neared the current expiration date if they feared that the stock would be called away.

correspondence sent to or from Faulkner's business address would be read by Salomon management at Faulkner's branch office.

- 4.1 In an effort to reduce Faulkner's promise to Perkins to writing, Perkins sent Faulkner a Memorandum of Agreement in December 1995, in which he urged Faulkner to make this situation a priority; according to the Memorandum of Agreement, the losses associated with the two unauthorized trades specified in above paragraphs 3.3 and 3.4 would be resolved by the end of 1996. Faulkner ultimately signed and delivered a notarized copy of the Memorandum of Agreement to Perkins on July 8, 1996. In this agreement, Faulkner agreed to reimburse Perkins for any losses that resulted from the trades referred to in above paragraphs 3.3 and 3.4, and any losses that resulted from the attempt to trade out of the original losses, that remained in the Perkins Trust Account at the end of 1996.
- 4.2 Although Faulkner failed to successfully trade out of the losses that resulted from the trades referred to in above paragraphs 3.3 and 3.4, Perkins allowed the strategy to continue because the value of the account was increasing by the end of 1996. However, by the summer of 1998 Perkins became increasingly frustrated with Faulkner's inability to reduce the unrealized losses that resulted from the unauthorized options trading referred to in above paragraphs 3.3 and 3.4.
- 5.0 In September 1998, Perkins sent to Faulkner, at his home address, a letter indicating his desire to discontinue attempts by Faulkner to trade out of the losses resulting from the trades referred to in above paragraphs 3.3 and 3.4, suggesting several alternatives regarding payment of the trading loss Perkins believed he was

- owed by Faulkner, and requesting that Faulkner respond with an estimate of the balance due for his failure to make Perkins whole or better.
- 5.1 Faulkner failed to respond to Perkins' September 1998 letter. Faulkner also failed to respond to additional follow-up letters sent by Perkins in November 1998 and January 1999.
- 5.2 On February 1, 1999, Perkins sent another letter to Faulkner, claiming that Faulkner's failure to respond left Perkins with no alternative but to seek a remedy. In June 1999, Perkins initiated a civil lawsuit against Faulkner in Missouri state court, seeking damages for common law fraud, breach of fiduciary duty, and conversion of Perkins' property. Faulkner failed to notify the Exchange or his branch office manager, or any other management personnel at Salomon, of the lawsuit, notwithstanding the fact that the Firm's policy was to report such a matter.
- 5.3 Perkins subsequently withdrew the civil lawsuit against Faulkner in November 1999, choosing instead to proceed against Faulkner in an NASD Arbitration proceeding. Faulkner failed to notify the Exchange or Salomon of this pending arbitration proceeding; the Firm ultimately learned of the arbitration proceeding, but only because the firm had also been named as a party.
- 6.0 Despite Salomon's policies to the contrary, Faulkner also failed to inform his branch office manager, or any other management personnel at the Firm, of the trades referred to in above paragraphs 3.3 and 3.4, which he admitted were executed in error, the complaints of Perkins, the outgoing and incoming

correspondence sent to his home address, and his guaranteeing Perkins against losses.

CHARGES PREFERRED:

- 7.0 Faulkner violated Exchange Rule 345(a)(4) in that he failed to report a customer complaint to his employer, and corresponded with a customer from his home address in contravention of the policies of his employer, as stated in above paragraphs 3.4 through 3.7, 4.0 through 4.1, 5.0 through 5.2, and 6.2.
- 7.1 Faulkner violated Exchange Rule 924(a) in that he effected two unauthorized trades in a customer account in May 1995, as stated in above paragraphs 3.0 through 3.4.
- 7.2 Faulkner violated Exchange Rule 341, Commentary .08(5)(2) in that he guaranteed a customer against losses, as stated in above paragraphs 3.7 through 4.2.
- 7.3 Faulkner violated Exchange Rule 341, Commentary .08(5)(9) in that he failed to inform the Exchange or his employer that he became involved in litigation and an administrative proceeding, as stated in above paragraphs 5.2 through 5.3.

* * * * *

Faulkner shall have 20 days from the date of service of this Statement of Charges to answer such Charges in accordance with the provisions of the Exchange Constitution and Rules thereunder. The answer shall specifically indicate which statements, or

portions thereof, are admitted and which are denied. Any statement, or portion thereof, not specifically denied shall be deemed admitted.

AMERICAN STOCK EXCHANGE

By: _____
Glen Barrentine
Senior Vice President