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**FIA Law and Compliance Division Conference  
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## **FINRA's CONTINUED FOCUS ON ANTI-MONEY LAUNDERING COMPLIANCE\***

Anti-Money Laundering ("AML") compliance remains a top regulatory priority for FINRA. Along with the watchful and proactive eye of the SEC, FINRA examinations and enforcement actions put the broker-dealer community to the test of having an effective, "risk-based" AML compliance program.

FINRA's recently issued examination priorities letter for the coming year confirms that AML remains an important focus. FINRA emphasizes that its letter, issued March 10, 2010, goes beyond the focus of FINRA's Market Regulation Department to also include topics that are of heightened importance to FINRA's Enforcement Department.

Through its letter, FINRA cautioned that its examiners will continue to closely review firms' systems for monitoring, detecting and reporting suspicious activity: "[R]obust anti-money laundering monitoring systems can assist in deterring possible illegal customer conduct such as unregistered stock distributions . . . ." It noted that in 2009, FINRA took action against firms for failing to establish and/or implement procedures to detect and report suspicious securities transactions in the face of red flags that went undetected.

FINRA also noted that it updated its AML small firm template as of January 1, 2010 ([www.finra.org/am](http://www.finra.org/am)) ("Template") to include new red flags related to securities transactions, deposits of physical certificates and penny stock companies. FINRA recommended that "firms of all sizes should consider incorporating these red flags into their AML programs."

Citing its recent enforcement action against E\*Trade, discussed below, FINRA warned that firms using automated monitoring that does not focus on manipulative trading, or focuses only on suspicious trading accompanied by a suspicious money movement, may not have adequate systems.

This paper summarizes the AML regulatory framework facing the broker-dealer community at this time of heightened scrutiny and highlights twenty-one SEC/FINRA AML-related enforcement actions in the last two years.

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## **Overview of Statutory and Regulatory Requirements**

The Bank Secrecy Act, 31 U.S.C. § 5311, *et seq* (“BSA”), and regulations promulgated thereunder, impose AML obligations directly on broker-dealers. Such obligations include: AML compliance programs; customer identification programs; monitoring and detecting suspicious activity by looking for “red flags;” filing suspicious activity reports relevant to a possible violation of law, and conducting due diligence on private banking and foreign correspondent accounts. FINRA Rule 3310 is the regulatory vehicle by which FINRA members are required to meet minimum standards to comply with the BSA. FINRA, through various notices to members, Frequently Asked Questions (FAQs) and templates, has provided various examples of “red flags,” as discussed below.

### **Know Your Customer**

A key aspect of AML compliance is its own form of the “know your customer” rule to assess the risks your customers present. Section 17(a) of the Securities Exchange Act and Rule 17a-8 thereunder require a broker-dealer to comply with the reporting and recordkeeping requirements under the BSA, including the Customer Identification Program (“CIP”) rule. The CIP rule requires a broker-dealer to have procedures for verifying the identity of customers. 31 CFR § 103.122. Procedures to document and verify the identity of customers who open new accounts are routinely reviewed by the SEC and FINRA examiners and, when not properly executed, form the basis for an enforcement proceeding.

An unexpired government-issued identification evidencing nationality or residence and bearing a photograph or similar safeguard, such as a driver's license or passport, is deemed appropriate for documenting the identity of an individual. A broker-dealer may rely on a government-issued identification as verification of a customer's identity and is not required to take steps to determine whether the driver's license was validly issued. Treasury/SEC Joint Final Rule on Section 326 of USA Patriot Act (“Joint Final Rule”); 68 Fed. Reg. 25, 113 (May 9, 2003). However, FINRA cautions that due to the “prevalence of identity theft, and because identification documents may be obtained illegally or be fraudulent, firms are encouraged to use non-documentary methods even when a customer has provided identification documents.” Notice to Members (“NtM”) 03-34 at 354.

With respect to a customer who is not an individual, appropriate documents are those “showing the existence of the entity, such as certified articles of incorporation, a government-issued business license, a partnership agreement or a trust agreement.” NtM 03-34 at 353. FINRA, echoing the Joint Final Rule, emphasizes the verification of the named accountholder with respect to trust and omnibus accounts.

The release explains that a broker-dealer is not required to look through a trust or similar account to its beneficiaries, and is required only to verify the identity of the named accountholder.

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Similarly, with respect to an omnibus account established by an intermediary, a broker-dealer is not required to look through the intermediary to the underlying beneficial owners, if the intermediary is identified as the accountholder.<sup>1</sup>

While opening account procedures are important, as described below they pale in comparison with the duties imposed on broker-dealers after the accounts are open to conduct diligence and detect “red flags” of suspicious activity and report same via the filing of Suspicious Activity Reports (“SARs”) with the Treasury.

On top of the required documentation for opening accounts, FINRA mandates “customer due diligence,” depending on the nature of the account. Specifically, NtM 02-21 enumerates several steps, including inquiring about the source of the customer’s assets and income so the firm can determine if the inflow and outflow of money and securities is consistent with customer’s financial status; gaining an understanding of what the customer’s likely trading patterns will be, so that any deviations from the patterns can be detected later on; and conducting credit history and criminal background checks through various databases.

Just last month, The Financial Crimes Network (FinCEN) at Treasury along with the SEC and in consultation with the staff of the CFTC issued guidance for obtaining beneficial ownership information for certain accounts and customers and reiterated the importance of customer due diligence. FIN-2010-G001, Guidance on Obtaining and Retaining Beneficial Ownership Information (March 5, 2010) (“March 5 Release”). Broker-dealers are to evaluate risks pertaining to an account and, based on the risk evaluation, employ procedures including:

- “Determining whether the customer is acting as an agent for or on behalf of another, and if so, obtaining information regarding the capacity in which and on whose behalf the customer is acting.
- Where the customer is a legal entity that is not publicly traded in the United States, . . . obtaining information about the structure or ownership of the entity so as to allow the broker-dealer to determine whether the account poses heightened risk.
- Where the customer is a trustee, obtaining information about the trust structure to allow the broker-dealer to establish a reasonable understanding of the trust structure and to determine the provider of funds and any persons or entities that have control over the funds or have the power to remove the trustees.”

March 5 Release at 5.

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<sup>1</sup> NtM 03-34 at 349. “However, a broker-dealer, based on its risk-assessment of a new account, may need to take additional steps to verify the identity of a customer that is not an individual, such as obtaining information about persons with control over the account.” *Id.* at 358 n.9.

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The March 5 Release also reiterated the requirements for special due diligence for foreign correspondent accounts<sup>2</sup> and foreign private banking accounts.<sup>3</sup> For correspondent accounts managed in the United States for foreign banks that operate under an offshore banking license or a banking license issued by certain high-risk jurisdictions, broker-dealers are required to take reasonable steps to determine the ownership of the foreign bank; to conduct enhanced security of the account to detect and report suspicious activity and to determine whether the foreign bank maintains “correspondent accounts” for any other bank, and if so, the identity of those banks.<sup>4</sup> Similarly, broker-dealers are required to determine the identity of the account holders of, and the source of funds deposited into, a private banking account maintained by a non-U.S. citizen, and to establish procedures to determine whether the nominal or beneficial owners are senior political figures. March 5 Release at 3-5; 31 CFR 103.178.

## **Red Flags and the Filing of SARs**

As discussed above, FINRA Rule 3310(a) requires FINRA members to establish and implement policies and procedures “that can be reasonably expected to detect and cause the reporting of” suspicious transactions.

Broker-dealers must establish risk-based procedures reasonably designed to detect and report suspicious transactions in order to comply with the BSA and FINRA Rule 3310. The risk of suspicious activity will vary for each firm depending on its size and location and based on its business model and the products and services it offers. Your firm can identify that risk by looking at the type of customers its serves, where its customers are located, and the types of products and services its offers.

Template at 31.

All broker-dealers are required to file with the Treasury Department “a report of any suspicious transaction relevant to a possible violation of law or regulation.” 31 CFR 103.19(a)(1). Broker-dealers should determine whether activities and transactions raise suspicions by looking for “red flags.” FINRA notes that the types of suspicious activity that are reportable on the Suspicious Activity Report (SAR-SF) are very broad and include securities fraud. Template at 31. With respect to “red flags,” FINRA, via notices to members and other means, has provided its members with numerous examples to consider given the particular risks and circumstances, including:

- For no apparent reason, the customer has multiple accounts under a single name or multiple names, with a large number of inter-account or third-party transfers.

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<sup>2</sup> A “correspondent account” is an account established for a foreign financial institution to receive deposits from, or to make payments or handle other financial transactions on behalf of, the foreign financial institution. 31 CFR 103.175(d).

<sup>3</sup> Among other features, a “private banking account” requires a minimum aggregate of funds of not less than \$1,000,000 and is established on behalf of a non-U.S. person. 31 CFR 103-175(o).

<sup>4</sup> See 31 CFR 103.176(a)-(c).

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- The customer's account has a large number of wire transfers to unrelated third parties inconsistent with the customer's legitimate business purpose.
- The customer makes a funds deposit for the purpose of purchasing a long-term investment followed shortly thereafter by a request to liquidate the position and transfer the proceeds out of the account.
- The customer's account has wire transfers that have no apparent business purpose to or from a country identified as a money laundering risk or a bank secrecy haven.
- The customer has difficulty describing the nature of his or her business or lacks general knowledge of his or her industry.
- The customer has no concern regarding the cost of transactions or fees, *i.e.*, surrender fees or higher than necessary commissions.
- Funds are deposited for purchase of a long-term investment followed shortly by a request to liquidate the position and transfer the proceeds out of the account.

In addition, FINRA, via its March 10, 2010 examination priorities letter, advised firms "of all sizes" to consider new red flags included in its AML small firm template that pertain to deposits or dispositions of physical certificates and transactions involving penny stock companies.<sup>5</sup>

## **Relationship Between Introducing and Clearing Firms**

The SEC and FINRA have made it clear that an introducing or clearing firm cannot be relieved of AML obligations to the extent the other is monitoring for suspicious activities. (FINRA Frequently Asked Questions: all broker-dealers have an independent responsibility to comply with the suspicious activity reporting requirement; introducing and clearing firms are both responsible for filing SARs.)

This is an area routinely covered by examinations:

Another important focus area for SEC and SRO examinations is the relationship between introducing and clearing firms. In many ways, clearing firms are some of the biggest players in the fight against money laundering and terrorist financing. They typically have the most resources and sophisticated systems. They see the highest volume of securities transactions and money flowing through accounts. They file the most SARs. On the other hand, introducing brokers may have the most direct contact with customers on a day-to-day basis. Examiners have in some instances found a lack of communication between introducing and clearing firms, and this is the area where we see the most finger pointing occurring . . . . Broker-dealers can expect that examiners will ask about the introducing-clearing relationship

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<sup>5</sup> These include when the physical certificate is titled differently than the account, the physical certificate does not bear a restrictive legend, but based on history of the stock and/or volume of shares trading, it should have a legend and when the company has been the subject of a prior trading suspension.

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. . . . The message in the area should be clear - - an introducing and clearing firm that *together* effect securities transactions - - need to work *together* to meet their AML obligations.<sup>6</sup>

Where the regulators find an inappropriate delegation of AML responsibility, enforcement actions may follow. For example, as published by FINRA, Mesirow Financial, Inc. submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$75,000. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that its clearing agreement with correspondent firms impermissibly allocated the detection and reporting of suspicious activity with respect to trading activities of introduced customer securities accounts to the introducing correspondent firms. The findings stated that because the BSA imposes an independent obligation to detect and report suspicious activity on all broker-dealers, the firm's AML program was not reasonably designed to detect and cause the reporting of suspicious trading activity in customer accounts. (FINRA Case #2008012747801).

## Case Summaries

### Recent AML-Related Enforcement Actions

***In the Matter of Ferris, Baker Watts***, SEC Admin. Proceeding, File No. 3-13364 (February 10, 2009)

The Commission found the following: a registered representative ("rep") and a customer participated in a scheme to manipulate the market for a stock and that the rep engaged in suspicious trades in another stock. The rep received a stock tip that positive news would soon be released about a company. The rep bought a total of 500,000 shares for himself and for certain customers' accounts without their authorization. At the end of the day, he allocated 480,000 shares among six customers' accounts, and allocated 20,000 to his personal account. He subsequently purchased an additional 480,000 shares for his customers' accounts. Although no positive news was released about the company, the purchases moved up the price of the stock. The rep subsequently sold his 20,000 shares at a profit, but did not sell the remaining 960,000 shares that he purchased without authorization for his customers' accounts.

Ferris's AML Officer noticed these trades and raised the issue with a senior executive whether the trades "could create the appearance of manipulative market practices." The AML Officer later asked if the trades were suspicious because, if so, he was obligated to file a SAR. The firm did not file a SAR.

The Commission found that the information available to Ferris regarding the manipulative practices involving a stock and the AML Officer's observations regarding the trading of the other stock, should have suggested to Ferris that it was required to file SARs. The Commission found that Ferris failed to reasonably supervise the rep with a view to detecting and preventing the rep's violations of Section 17(a) of the Securities Exchange Act and Rule 17-8 thereunder by failing to file SARs.

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<sup>6</sup> Speech by Director, SEC Office of Compliance Inspections and Examinations, before Sixth Annual Anti-Money Laundering Conference, Securities Industry Association, March 29, 2006.

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Without admitting or denying the Commission's findings, Ferris consented to a cease and desist order and paid a \$500,000 civil penalty and \$222,183 in disgorgement.

***In the Matter of E\*Trade Clearing LLC and E\*Trade Securities LLC***, SEC Admin. Proceeding, File No.3-13106 (July 30, 2008)

The Commission found that E\*Trade violated Section 17(a) of the Securities Exchange Act and Rule 17a-18 thereunder.<sup>7</sup> The CIP rule generally requires a broker-dealer to maintain procedures for identifying customers and verifying their identities. E\*Trade established a CIP that specified it would verify all accountholders in a joint account. The Commission found that E\*Trade failed to verify the identities of 65,442 secondary accountholders in joint accounts.

The Commission found that E\*Trade's systems did not verify the names of secondary accountholders in newly opened accounts and that E\*Trade did not "fix the problem" after the non-compliance was reported to three top executives. E\*Trade settled, without admitting or denying the Commission's findings, by paying a total of \$1 million in penalties and engaging a consultant to review and assess whether E\*Trade was in substantial compliance with its CIP obligations.

***E\*Trade Securities, LLC and E\*Trade Clearing, LLC***, FINRA AWC 2006004297301 (December 31, 2008)

In an action unrelated to the SEC proceeding described above, FINRA imposed a \$1 million fine for failing to establish and implement AML policies and procedures that could reasonably be expected to detect and cause the reporting of suspicious securities transactions. E\*Trade processed on average, more than 110,000 customer orders daily with little or no human intervention. FINRA found that E\*Trade did not have an adequate AML program based upon its business model. E\*Trade primarily relied on an automated AML system to review accounts for money laundering. Because the AML system alerts were triggered by money movements, FINRA alleged that it was unlikely that E\*Trade personnel reviewed the alerts for suspicious trading activity in the absence of any money movement. Therefore, according to FINRA, the system did not flag and cause the review of accounts for suspicious trading activity, such as matched trading. FINRA determined that, given E\*Trade's business model, its AML procedures could not reasonably be expected to detect and cause the reporting of suspicious securities transactions, in violation of FINRA Rule 3011. E\*Trade consented to the fine and entry of FINRA's findings without admitting or denying FINRA's findings.

***Scottrade Inc.***, FINRA AWC 200709026302 (October 26, 2009)

FINRA imposed a \$600,000 fine for failing to establish and implement an adequate AML program to detect and trigger reporting of suspicious transactions from April 2003 to April 2008. FINRA found that between April 2003 and January 2005, Scottrade's monitoring procedures were manual and relied exclusively on external and internal sources to refer potentially suspicious transactions to its AML officer. Despite the high volume of on-line trading at the firm,

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<sup>7</sup> The provisions require a broker-dealer to comply with the reporting, recordkeeping and record retention requirements of the BSA, including the requirements in the CIP rule applicable to broker-dealers.

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Scottrade had no systematic or automated processes to monitor for potentially suspicious transactions and generate referrals to the risk management department.

In 2005 and 2006, the firm implemented a proprietary automated filter-based system to monitor for suspicious transactions and a proprietary volume exception report designed to detect pump-and-dump account intrusions and unauthorized trading activity resulting from such account intrusions. However, the systems were not designed to detect and cause the reporting of suspicious trading activity, unless such activity was accompanied by money movement. As a result, the firm's AML policies were inadequate to achieve compliance with the BSA because they were not reasonably designed to detect and cause the reporting of suspicious securities transactions. Scottrade consented to the fine and entry of FINRA's findings without admitting or denying FINRA's findings.

## **OTHER RECENT AML-RELATED FINRA ACTIONS<sup>8</sup>**

**Regal Securities, Inc.** submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$50,000. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to develop and implement an adequate supervisory system and written procedures for detecting and reporting suspicious activity. The findings stated that the firm failed to provide adequate AML training for its designated AML officers and firm employees, and failed to conduct adequate independent testing of its AML compliance program for two years. (FINRA Case #2007007344801)

**Brockington Securities, Inc.** submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$24,000 and required to conduct eight hours of AML training for all employees within six months after issuance of this AWC. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to develop and implement an AML program reasonably designed to achieve and monitor compliance with BSA requirements. The findings stated that the firm's AML program had inadequate procedures regarding the detection and reporting of suspicious activity, and the firm did not receive FinCEN requests pursuant to the BSA. The findings also stated that the firm failed to timely detect, investigate and report multiple instances of suspicious activity in customer accounts. The findings also included that the firm failed to conduct an independent AML test one year, failed to satisfy its supervisory control system requirements under NASD Rule 3012, and failed to prepare an adequate NASD Rule 3012 report detailing its system of supervisory controls and the summary of test results, which made its statement that "no other modification of the written supervisory procedure (WSP) was deemed necessary" baseless. (FINRA Case #2008011660901)

**thinkorswim, Inc.** submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$50,000. Without admitting or denying the findings that it failed to implement a written AML program reasonably designed to achieve compliance with the requirements imposed by the BSA and the regulations promulgated thereunder. The findings stated that the firm failed to create records detailing a description of the resolution of each

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<sup>8</sup> From FINRA's monthly and quarterly "Disciplinary Actions" web page. See <http://www.finra.org/Industry/Enforcement/DisciplinaryActions/MonthlyActions/>

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substantive discrepancy discovered with regard the verification of customers' identifying information. (FINRA Case #2008011800501)

**Westrock Advisors, Inc.** submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$100,000. Without admitting or denying the findings, the firm consented to entry of findings, including that the firm failed to develop and implement an AML program reasonably designed to achieve and monitor its compliance with the requirements of the BSA; the firm's AML program had inadequate procedures governing the testing of its AML program; and the firm's testing of its AML procedures was inadequate and not independent one year, and not tested another year. (FINRA Case #2007008162201)

**George Ernest Reilly** was fined \$50,000 and suspended from association with any FINRA member in any principal capacity for two years. The fine is due and payable if and when Reilly re-enters the securities industry. The findings stated that Reilly failed to develop and implement an AML compliance program, as required by the BSA, reasonably designed to detect suspicious money movements and trading activities in corporate customers' accounts, investigate the activity and make the appropriate SAR filing. The findings also stated that the firm's AML program lacked procedures on monitoring and preventing money laundering and did not explain what follow-up would be required if a money laundering "red flag" was detected or when a SAR must be filed.

**Hudson Securities, Inc.** submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$10,000. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that its AML procedures were not tailored to reflect its business model, but instead used procedures designed for retail firms although it was not a retail brokerage firm. The findings stated that the section identifying "red flags" of suspicious activity copied examples in NASD *Notice to Members* 02-21 and were not modified to reflect issues that might arise in its wholesale trading business. The findings also stated that the firm's supervisory procedures and compliance manual were not cross-referenced to the AML procedures, and failed to give employees guidance on what action to take in an AML context if suspicious activity was detected. The findings also included that the firm's failure to customize its AML procedures to its business left employees to devise their own red flags to address the firm's market-making activities and to determine how to apply AML procedures. (FINRA Case #2007008732901)

**Domestic Securities, Inc.** was fined \$10,000 and ordered to revise its AML policies and procedures and certify its compliance to FINRA within 30 days of the final decision, and quarterly for one year thereafter. FINRA's National Adjudicatory Council ("NAC") imposed the sanctions following a call for review of an Office of Hearing Officers decision. The sanctions were based on findings that the firm failed to develop and implement written AML policies and procedures reasonably designed to achieve and monitor compliance with the requirements of the BSA. The findings stated that, while the firm had AML policies and procedures in effect for retail transactions, it did not have the requisite AML policies and procedures in effect for its market-marking activities. (FINRA Case #2005001819101)

**TerraNova Financial, LLC** submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$100,000. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that, among other violations, the firm failed to evidence that it had conducted an expeditious search of its records to

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determine if it had any accounts for any individual or entity in FinCEN requests, failed to evidence that it conducted an independent annual test of its AML Compliance Program for one year, and failed to assess the adequacy of its AML program and its degree of compliance with written procedures. FINRA also found that the firm's written AML CIP was deficient in its design and failed to address responses to 314(a) requests from FinCEN, failed to maintain documentary evidence that it conducted reviews outlined in its AML CIP necessary for adequate implementation of its procedures for suspicious activity detection and reporting, the firm conducted no specialized or additional training for members of its Treasury Department regarding screening of transactions for AML purposes, reviews conducted by its Treasury Department were done manually rather than by an automated process, and the firm classified accounts based on risk during the account opening process but failed to maintain these classifications going forward for the purpose of due diligence. In addition, FINRA determined that the firm was at a heightened responsibility for AML review because of the large number of securities accounts it serviced and the fact that many accounts were owned by foreign entities or individuals, but failed to conduct an adequate review of transactions for AML purposes. (FINRA Case #2007007328101)

**Chicago Investment Group, LLC** submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$150,000, and required to certify to FINRA that its AML policies and procedures are in compliance with NASD Rules 3011(a) and 3011(b), and that its system and procedures for trading and market making are reasonably designed to achieve compliance with applicable federal securities laws and FINRA rules; thereafter, the firm was required to certify its compliance quarterly for one year. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to establish and maintain an adequate supervisory system, including written procedures, to supervise the firm's trading and market making. The findings stated that the firm failed to reasonably supervise individuals to detect their manipulations of the price of a thinly traded common stock. The findings also stated that the firm failed to establish and implement AML policies and procedures that could reasonably be expected to detect and cause the reporting of suspicious securities transactions, and internal controls reasonably designed to achieve compliance with the BSA and the implementing regulations thereunder. (FINRA Case #2006006518903)

**Synergy Investment Group LLC** submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$75,000. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to establish and implement policies and procedures reasonably designed to detect and cause the reporting of suspicious customer activity; failed to detect, investigate and conduct due diligence when red flags associated with suspicious activity were present; failed to file SARs when red flags associated with suspicious activity were present; and failed to follow its written supervisory procedures, in that it failed to conduct appropriate risk-based due diligence for correspondent accounts of foreign financial institutions customers owned, and failed to implement adequate supervisory procedures to monitor the suspicious activity in those accounts. The findings stated that the firm failed to perform AML customer identification reviews for customers, as required by its procedures, which would have revealed that several accounts appeared to be shell vehicles for possible securities fraud; the firm failed to file SARs on individuals possibly engaged in insider trading; the firm did not adequately test its AML compliance program and, during a two-year period, failed to conduct or document AML training. (FINRA Case #2007007139501)

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***Martinez-Ayme Securities and Alfredo Francisco Ayme***, (Registered Principal) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$21,000. Ayme was fined \$10,000 and suspended from association with any FINRA member in any principal capacity for three months. Without admitting or denying the findings, the firm and Ayme consented to the described sanctions and to the entry of findings that the firm's AML program required the firm and Ayme to monitor for potentially suspicious activity and AML red flags, investigate potentially suspicious activity and report suspicious activity by filing a Form SAR-SF with the U.S. Department of the Treasury's Financial Crimes Network. The findings stated that the firm and Ayme failed to adequately implement or enforce its AML program and to otherwise comply with their AML obligations since they did not identify and analyze numerous transactions to determine if they were in fact suspicious, which would require them to be reported on a Form SAR-SF. The findings also stated that the firm and Ayme permitted suspicious activities to occur undetected and unchecked and failed to file SAR-SFs as appropriate. The findings also stated that the firm conducted tests for compliance with applicable AML laws, rules and regulations, but these tests were not independent since they were conducted by a firm employee who performed AML functions as part of his regular job responsibilities. The findings also included that the firm acted as the placement agent for contingency securities offerings and failed to establish escrow or separate bank accounts in connection with the offerings, and investors were directed to transmit their funds directly to the issuers prior to the contingency being satisfied. (FINRA Case #2009016159201)

***Perrin, Holden and Davenport Capital Corporation, dba PHD Capital*** submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$30,000 and required to have its registered representatives register for three hours of AML training within 60 days of issuance of this AWC, and complete such training within six months of issuance of this AWC. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that, although it had an established a CIP, its internal controls for ensuring compliance were not sufficient to detect or prevent multiple failures to obtain and verify required customer identification information. The findings stated that the firm failed to obtain required customer identification information for certain accounts, failed to confirm that sufficient documentary and/or non-documentary verification information was obtained prior to approving the accounts, and failed to restrict transactions in certain deficient accounts 30 days or more after opening. (FINRA Case #2007008158601)

***ViewTrade Securities, Inc.*** submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$50,000. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to properly implement its AML compliance program, insofar as it did not monitor corporate accounts brought to the firm from a defunct broker-dealer by registered representatives for red flags and did not identify potentially suspicious activity for further due diligence. The findings stated that a registered representative at the firm sent business-related emails from a non-firm email address that were not maintained on the firm's server in a non-writable, non-erasable format, but were obtained from the representative's computer, where they could have been deleted or lost. (FINRA Case #2008011725001)

***WFG Investments, Inc. and Wilson Henry Williams*** submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$30,000, \$25,000 of which was jointly and severally with Williams. Without admitting or denying the findings, the firm and Williams consented to the described sanctions and to the entry of findings that, among other violations

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the firm, acting through Williams, failed to develop and implement an AML program reasonably designed to achieve and monitor compliance with the requirements of the BSA and implementing regulations. The findings also included that the firm's AML program was deficient, in that senior management had not approved the AML program in writing; its AML written procedures did not provide for on-going training of appropriate personnel; its written procedures did not provide for independent testing; its written procedures did not identify a specific individual as an AML compliance officer; its AML written procedures did not address recordkeeping requirements; and the firm had inadequate internal controls to detect an attempt to open or maintain correspondent accounts for foreign banks, or regarding freezing accounts and prohibiting transactions with persons suspected of terrorist activities and for filing relevant reports. (FINRA Case #E062003014607)



## NEWS RELEASE

**For Release:** Thursday, June 4, 2009  
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### **FINRA Fines Three Firms Over \$1.25 Million for Failing to Detect, Investigate and Report Suspicious Transactions in Penny Stocks**

#### **J.P. Turner, Park Financial, Legent Clearing Ignored Indications Customers May Have Been Engaged in Illegal Conduct**

#### **Two Individuals Barred from Securities Industry, One Suspended and Fined**

**Washington, DC** — The Financial Industry Regulatory Authority (FINRA) announced today that it has fined three broker-dealers — J.P. Turner & Co., of Atlanta, Park Financial Group, Inc., of Maitland, FL, and Legent Clearing, LLC, of Omaha — for failing to implement reasonable anti-money laundering (AML) compliance programs, including the failure to detect, investigate and report instances of potentially suspicious transactions in low-priced stocks.

J.P. Turner was fined \$525,000, Park Financial was fined \$400,000 and Legent Clearing was fined \$350,000. In addition, two individuals — Park Financial's former CEO and AML compliance officer Gordon Charles Cantley and J.P. Turner equity trader John McFarland — were barred permanently from the securities industry. David Farber, a Park Financial equity trader, was fined \$25,000 and suspended in all capacities for 30 days. S. Cheryl Bauman, J.P. Turner's former AML compliance officer, was fined \$30,000 and suspended from acting as a principal in a securities firm for 18 months, while Robert Meyer, a former J.P. Turner branch manager, was fined \$5,000 and suspended as a principal for one month.

"It is critical that firms promptly and fully investigate and report suspicious transactions - because law enforcement agencies and the Securities and Exchange Commission use Suspicious Activity Reports to investigate and prosecute money laundering, securities fraud and other financial crimes," said Susan L. Merrill, FINRA Executive Vice President and Chief of Enforcement. "Each of these firms had inadequate AML procedures and each of these firms processed suspicious trades without adequately following up on red flags — such as deposits and liquidations of large quantities of penny stocks by customers or the principals of the issuing firms that had a history of securities fraud or stock manipulation."

The Bank Secrecy Act and FINRA rules require all broker-dealers to design and implement programs to detect and report suspicious transactions at, by or through the firm. The program must be tailored to the risks of the firm's business. For such transactions to be reportable, the firm does not need actual knowledge that the customer is in fact committing a crime or that the funds are the proceeds of a crime.

In each of the three cases announced today, the firms failed to establish and/or implement reasonable procedures to detect and report suspicious trading in low-priced securities. Certain trading in low-priced securities, or "penny stocks," creates a risk that these securities can be used by unscrupulous issuers of the stock, stock promoters and others affiliated with the issuers for money laundering or to commit securities fraud or market manipulation. These firms failed to detect and investigate potentially suspicious transactions. Many of the transactions in these cases presented sufficient red flags that the firms should have had reason to suspect that the customers may have been engaged in unregistered distributions, market manipulation or securities fraud.

In the case against Park Financial, FINRA found that during the period from September 2004 through April 2008, the firm's clientele included several stock promoters and other individuals and entities with regulatory histories of securities-related violations such as stock fraud and manipulation. Many of these customers engaged in high-risk activities, such as depositing millions of shares of low-priced securities, generating millions of dollars in proceeds by liquidating the shares and wiring out the proceeds to offshore and domestic bank accounts. Other Park Financial customers had inflows of funds or other assets into their accounts that were well beyond their known income or financial resources. Park Financial, acting through Cantley, failed to establish and/or implement reasonable procedures to detect and report suspicious trading, failed to investigate any of the potentially suspicious transactions and failed to file Suspicious Activity Reports, as appropriate.

FINRA also found that Park Financial, acting through broker Farber, had engaged in the unregistered distribution of the securities of two issuers. In addition to imposing a fine, FINRA ordered the firm to retain an independent AML consultant to review its AML compliance program.

In a second action, FINRA found that J.P. Turner failed to detect, investigate and file Suspicious Activity Reports as appropriate for numerous potentially suspicious transactions. The suspicious activity included: multiple accounts under a single name or multiple names maintained by customers for no apparent business reason; and numerous transactions where large blocks of low-priced securities of companies with higher risk operating and financial histories were transferred into accounts, sold and the proceeds wired from the accounts. In several cases, the principals of these companies were the subjects of pending SEC actions alleging fraud and other securities law violations.

FINRA also named J.P. Turner's former equity trader, McFarland, for failing to report to his firm suspicious transactions. Former Staten Island Branch Manager Meyer was named along with Bauman for their failures to adequately monitor and enforce special supervisory arrangements for the Staten Island branch.

In the third action, FINRA found that Legent Clearing's AML program was not tailored to the firm's business risks in that it did not adequately consider the money laundering risks posed by correspondent firms for which Legent provided securities clearing services. FINRA found that Legent failed to consider, among other things, that some of the correspondent or introducing firms had lengthy disciplinary histories and were conducting high-risk business activities such as significant penny-stock liquidations.

Even more problematic, Legent processed transactions for individual customers of its correspondent firms with red flags of suspicious activity, without fully investigating the transactions or filing a Suspicious Activity Report as appropriate. For instance, Legent processed transactions involving millions of shares of stock owned by company insiders or known penny stock promoters who had no evident legitimate business purpose for engaging in those transactions. Notably, Legent provided clearing services to introducing broker-dealers that FINRA has expelled from the securities industry for their own AML violations — Salomon Grey Financial in 2006 and Franklin Ross in 2007.

In settling these matters, J.P. Turner, Park Financial, Legent Clearing, Gordon Charles Cantley, John McFarland, David Farber, S. Cheryl Bauman and Robert Meyer neither admitted nor denied the charges, but consented to the entry of FINRA's findings.

Investors can obtain more information about, and the disciplinary record of, any FINRA-registered broker or brokerage firm by using FINRA's BrokerCheck. FINRA makes BrokerCheck available at no charge. In 2008, members of the public used this service to conduct 11.6 million reviews of broker or firm records. Investors can access BrokerCheck at [www.finra.org/brokercheck](http://www.finra.org/brokercheck) or by calling (800) 289-9999.

FINRA, the Financial Industry Regulatory Authority, is the largest independent regulator for all securities firms doing business in the United States. FINRA is dedicated to investor protection and market integrity through comprehensive regulation. FINRA touches virtually every aspect of the securities business - from registering and educating all industry participants to examining securities firms; writing and enforcing rules and the federal securities laws; informing and educating the investing public; providing trade reporting and other industry utilities; and administering the largest dispute resolution forum for investors and firms.

For more information, please visit our Web site at [www.finra.org](http://www.finra.org).



## NEWS RELEASE

**For Release:** Tuesday, January 13, 2009  
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### **FINRA Fines Leonard & Co. for Sale of Unregistered Securities, Bars Broker for Unregistered Penny Stock Sales, Other Violations**

#### **FINRA Issues Regulatory Notice Regarding Sales of Unregistered Securities**

**Washington, D.C.** — The Financial Industry Regulatory Authority (FINRA) announced today that it has fined Leonard & Co. of Troy, MI, \$225,000 for numerous violations, including the illegal sale of more than two million shares of penny stock on behalf of customers. FINRA also required the firm to retain an independent consultant to review its supervisory systems and procedures.

In addition, FINRA has barred Robert J. Cole, formerly a registered representative with Leonard & Co., for his role in the illegal sales.

In a related action, FINRA today issued Regulatory Notice 09-05, *Unregistered Resales of Restricted Securities*, to remind firms and brokers of their obligations to determine whether securities are eligible for public sale before participating in what may be illegal distributions. It also discusses the importance of recognizing "red flags" of possible illegal, unregistered distributions and reiterates firms' obligations to conduct searching inquiries in certain circumstances to avoid participating in illegal distributions.

"This action, and the accompanying Regulatory Notice, demonstrate FINRA's continuing commitment to ensuring that brokerage firms live up to their responsibilities as gatekeepers to the securities markets," said Susan L. Merrill, Executive Vice President and Chief of Enforcement. "FINRA will aggressively pursue firms and individuals who ignore those responsibilities and participate in illegal sales of unregistered securities."

FINRA found that Leonard & Co. and Cole participated in an illegal distribution of a penny stock, Shallbetter Industries, by selling over 2.2 million unregistered shares of the stock into the public markets from three related customer accounts. Cole, who handled the accounts, was aware that trading in the accounts was directed by a "control person" of Shallbetter. A control person is generally an individual who owns 10 percent or more of the stock of a company and can influence its policies and decision-making.

Most of the shares were deposited into the accounts in certificate form with restrictive legends attached to the certificates. Although the sales were made on behalf of a control person of Shallbetter, Cole arranged to have the restrictive legends removed from the stock certificates so the unregistered shares could be sold into the public markets.

Shallbetter is a thinly-traded penny stock. During the time of the sales activity, the company claimed in public filings with the Securities and Exchange Commission (SEC) that it owned mineral exploration licenses and interests in Outer Mongolia. The sales from the Leonard & Co. accounts occurred between August and November 2006 and generated over \$3.1 million in proceeds for the accounts.

FINRA found that the sales coincided with a campaign by third parties to promote Shallbetter through widespread spam e-mail and the issuance of numerous press releases. The campaign resulted in significant increases in the price and trading volume of Shallbetter stock. During five days of the period, sales of Shallbetter from the accounts at Leonard & Co. accounted for more than 20 percent of the stock's total trading volume.

FINRA found that Cole had been told about the promotional campaign in advance by Shallbetter insiders. While in possession of this information, Cole purchased 15,000 Shallbetter shares for his own account and solicited purchases of 10,000 Shallbetter shares for two customers. He also acted to support the price of Shallbetter stock in advance of the promotional campaign by placing trades and by soliciting purchases of Shallbetter stock.

FINRA found that by selling more than two million shares of unregistered Shallbetter stock into the public markets for control persons of Shallbetter, Cole and Leonard & Co. violated the registration provisions of federal securities laws. FINRA also found that Cole and Leonard & Co. failed to conduct an adequate review of Shallbetter before recommending its purchase to customers of the firm. FINRA further found that Cole participated in a scheme to manipulate the price of Shallbetter stock, purchased and recommended purchases of Shallbetter stock while in possession of material nonpublic information and sent numerous emails to customers that inappropriately touted various stocks, including Shallbetter.

In addition, FINRA found that Leonard & Co. was aware of numerous red flags indicating that an illegal distribution might be underway, but failed to conduct a reasonable inquiry into them. In fact, the firm failed to conduct an adequate inquiry even after FINRA's Market Regulation Department inquired about the unusually high volume of trading in Shallbetter stock. FINRA found that the facts available to Leonard & Co had it conducted a reasonable inquiry included:

- That the accountholder/control person who had deposited over two million Shallbetter shares into accounts at Leonard & Co. had the same address as Shallbetter, was closely associated with Shallbetter's management and controlled over 10% of Shallbetter's outstanding stock.
- That the accountholder/control person used shares in the account, or proceeds from shares in the account, to pay legal and auditing expenses for Shallbetter.
- That a former president and director of Shallbetter - who at the time was living with the accountholder/control person - directed the trading and transfers in the account.

FINRA found that Leonard & Co. failed to maintain a supervisory system reasonably designed to comply with the registration requirements, but instead relied on its clearing firm to provide such a review. FINRA, the SEC and the courts have repeatedly held that firms cannot rely on outside counsel, clearing firms, transfer agents, issuers, or issuer's counsel to discharge their obligations to undertake an inquiry into circumstances such as those present in this case. FINRA also found that Leonard & Co. failed to reasonably supervise Cole and ignored numerous red flags that he was engaging in activity that violated securities laws and regulations.

Other violations found by FINRA include the firm's failure to implement an adequate anti-money laundering (AML) program and failure to timely file suspicious activity reports in connection with certain activities, including liquidation of a large position of a thinly-traded unregistered penny stock at the direction of a corporate insider; the wiring of proceeds to third parties, some of whom were overseas; and, the accountholder's refusal to provide requested information about an entity to which he proposed to transfer funds.

Leonard & Co. also failed to retain email for 23 accounts, including the firm's executive management, registered operations staff and non-registered administrative staff, and allowed its Chief Operating Officer to act as a principal before he had requalified to act in that capacity as required by a prior settlement with FINRA.

In settling these matters, neither Leonard & Co. nor Cole admitted or denied the charges, but consented to the entry of FINRA's findings.

Investors can obtain more information about, and the disciplinary record of, any FINRA-registered broker or brokerage firm by using FINRA's BrokerCheck. FINRA makes BrokerCheck available at no charge. In 2007, members of the public used this service to conduct 6.7 million reviews of broker or firm records. Investors can access BrokerCheck at [www.finra.org/brokercheck](http://www.finra.org/brokercheck) or by calling (800) 289-9999.

FINRA is the largest non-governmental regulator for all securities firms doing business in the United States. FINRA is dedicated to investor protection and market integrity through effective and efficient regulation and complementary compliance and technology-based services. FINRA touches virtually every aspect of the securities business - from registering and educating industry participants to examining securities firms; writing rules; enforcing those rules and the federal securities laws; informing and educating the investing public; providing trade reporting and other industry utilities; and administering the largest dispute resolution forum for investors and registered firms.

For more information, please visit our Web site at [www.finra.org](http://www.finra.org).