NASD OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. JUSTIN E. APGAR (CRD #2770606) Wall Township, NJ, Respondent.	Disciplinary Proceeding No. C9B020046 Hearing Officer - JN **HEARING PANEL DECISION** April 28, 2003

Respondent committed fraud by falsely representing to customer that the interest rate on an investment was guaranteed not to change. Respondent violated NASD Rules 2110 and 2120 and Section 10(b) of the Securities Exchange Act and SEC Rule 10b-5, promulgated thereunder. He was fined $52,000, including disgorgement of commission, suspended for two months, and assessed $2,502.30 in costs.

Appearances

For the Complainant: David B. Klafter, Esq. and Michael J. Newman, Esq.

For the Respondent: Hilary B. Miller, Esq.

Decision

I. Introduction

On July 8, 2002, the Department of Enforcement filed a Complaint against Respondent. The first cause alleged fraud, in violation of NASD Rules 2110 and 2120 and Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5, promulgated thereunder. The second cause alleged forgery, in violation of Rule 2110.

A Hearing Panel composed of an NASD Hearing Officer and two current members of NASD District Committee No. 9 conducted a hearing on January 9, 2003 in Woodbridge, New Jersey. The Department called four witnesses and introduced twelve

exhibits, referred to here with the prefix "CX." Respondent called three witnesses, including himself, and introduced one exhibit, referred to here as "RX." On February 18, 2003, the parties filed post-hearing briefs.

II. Factual Background

Respondent entered the securities industry in 1996 and has no disciplinary history. Between May of 1997 and July of 1998, he was registered as a general securities representative and investment company and variable contracts representative of Fiserv Investor Services, Inc., a member firm. He was also an employee of the Summit Bank, and worked in one of its branch offices (CX-1, ¶¶ 1, 2; CX-2; Tr. 177-178).[1]

While employed by Fiserv and the Bank, Respondent came in contact with Mr. TG, a customer who had several million dollars in CD's held by the bank. On or about December 18, 1997, TG withdrew some $4 million from those CD's and invested the money in the Eaton Vance Prime Rate Reserves mutual fund (CX-1, ¶¶ 14, 15). The customer said that he did so in reliance on various representations by Apgar, including alleged statements that the fund's net asset value would remain fixed and that its rate of return was guaranteed to be 7.1%. Respondent denied having made such guarantees at the time of the investment and suggested that TG had confused the Eaton fund with other recommendations which were discussed.

After becoming concerned that his Eaton fund investment was not earning what Apgar supposedly said it would, he complained angrily to Respondent, who – in order to allay the customer's concerns – wrote a note to TG, which contained a false promise of a guaranteed interest rate (Tr. 192, 203, 210; CX-3). One month later, the customer received a letter purportedly written by Apgar's supervisor, which repeated that promise (CX-4). These letters caused the customer to remain silent for about six months, before

[1] The prefix "Tr." refers to hearing transcript pages.

complaining to the bank, which ultimately settled with him (Tr. 40-41, 45, 68; CX-12). Though he settled, TG nonetheless asserts that the bank should have paid him significantly more money.[2]

III. Fraud

Enforcement alleges that Respondent committed fraud by (1) an oral misrepresentation of a guaranteed rate of return, which induced the customer to invest in the Eaton fund and by (2) a later written reiteration of that guarantee in Respondent's January 2, 1998 letter (Complaint, ¶¶ 9, 10, 12).

A. The alleged oral misrepresentation

Because there were no witnesses to the conversation between TG and the Respondent, Enforcement's case as to the oral guarantee requires that the Panel accept the customer's word over Apgar's. The Panel is not persuaded that it should reach that result. Each party to the conversation had a compelling motive to tell the story his way. The Respondent was, of course, fighting for his continued existence in the securities industry. The customer, believing that the Bank should give him what the investment would have earned under his various allegations, acknowledged that his appearance was partly motivated by financial considerations and that he was contemplating an action against the bank (Tr. 84-87, 89).

Respondent's suggestion that TG had confused the Eaton fund with other investments which did involve guarantees (Tr. 181) was plausible. The customer admitted that Respondent discussed other investments with him, while insisting that they did not carry guarantees (Tr. 56-57). In the Panel's view, TG was an unsophisticated investor who could well have confused one instrument with another. That is especially

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[2] The settlement covered the difference between the actual and promised rates of return, as well as part of the loss attributable to a decline in the Eaton fund's net asset value.

so considering the passage of several years between the conversation and his complaints to NASD. In any event, TG's version – that the guarantees pertained to the Eaton funds and not to other opportunities – was certainly in his own self-interest.

Moreover, the customer's recollections were somewhat uncertain in other respects. After first stating that Apgar had discussed only the Eaton fund as an alterative investment to his CD's, the customer admitted that other investments were discussed (Tr. 56-57). His declaration stated that he received the second letter (the basis for the forgery charge) "about a week after" the first (CX-6, ¶ 3). In fact, the second letter was written more than a month after the first (See CX-3 and CX-4). The same declaration stated that TG never spoke with Lithgow (Apgar's supervisor) and particularly did not do so after receiving the February letter purportedly signed by him (CX-6, ¶ 4). Yet Lithgow testified that TG brought that letter to his attention (Tr. 101). Finally, the customer denied that the signature on the new account form was his (Tr. 48). But the bank's investigator testified that upon showing TG that signed form, the customer said nothing about any irregularity or about not having signed it (Tr. 252).

Considering all of the circumstances, the Panel concludes that TG's testimony failed to persuade it that Respondent more likely than not made the oral misrepresentation. At best, the evidence supporting each version is of equal weight, an equation which dictates that the Department failed to carry its burden of proving liability by a preponderance of the evidence.[3]

[3] See OHO Redacted Decision C07010017 (Nov. 21, 2001), at http://www.nasdr.com/pdf-text/oho1101_02red.pdf; see also Dep't of Enforcement v. Reynolds, 2001 NASD Discip. LEXIS 17, at **54-55 (NAC June 25, 2001) (citing SEC v. Moran, 922 F. Supp. 867, 892 (S.D.N.Y. 1996)); H. J. Meyers & Co., 2002 SEC LEXIS 2175 at *96 (Initial Decision, Aug. 9, 2002); Louis Abrams, 1995 CFTC LEXIS 196 at #15 (July 31, 1995).

B. The January 2, 1998 letter

Apgar acknowledged that on January 2, 1998, he wrote and signed the following note to TG, who received it later that day (Tr. 192; CX-3):[4]

> Mr. [TG]:
>
> It was a pleasure having the oppertunity to conduct buisness with you, and this letter will establish the boundries upon which we have agreed.
>
> The total sum of dollars invested is now and shall continue to earn interest at a rate of no less than 7.1%. We have further come to an agreement in which Summit Financial services division shall not impose any fees or penalties associated with early withdrawal. The early withdrawal option that has been extended to Mr. [TG] shall include no less than his upto date interest and earnings.
>
> These special options extended to Mr. [TG] are to be held in strict confidence and are to be discussed only with your investment counselor.
>
> Sincerly,
>
> Mr. Justice Apgar/AVP
>
> [signature]
>
> Summit Bank

For a violation of the SEC and NASD anti-fraud rules, there must be proof of a material misrepresentation, made with scienter, in connection with the purchase or sale of a security. See, e.g., The PNC Financial Services Group, Inc., Exchange Act Rel. No. 46225, 2002 SEC LEXIS 1847 at *28 (July 18, 2002); Dep't of Enforcement v. Averell Golub, No. C10990024, 2000 NASD Discip. LEXIS 14 at *22 (Nov. 17, 2000). Those elements are present here.

This letter stated that the Eaton Fund would earn a return of "no less than 7.1%," whereas the prospectus contained no statement that the fund would pay any guaranteed rate of return, let alone one of 7.1% (CX-1, ¶ 18). Nor can there be any dispute about the materiality of that falsehood. "The test for materiality is whether the reasonable investor

[4] The following quotation reproduces the misspellings in the actual document.

would consider a fact important" in making an investment decision, or whether disclosure would "significantly alter … the 'total mix' of information made available."[5] Representations as to rate of return are material. See Thomas J. Furnari, Exchange Act Rel. No. 21046, 1984 SEC LEXIS 1358 at *5 (June 14, 1984) ("Furnari made material misrepresentations to customers concerning the anticipated rate of return..."); Dist. Bus. Conduct Committee v. Larry Ira Klein, 1995 NASD Discip. LEXIS 222 (NBCC June 26, 1995), aff'd 1996 SEC LEXIS 2922 (October 17, 1996) (Respondent liable for material misrepresentations that principal and interest were guaranteed by issuer).

As the SEC noted in Klein, "guarantees" are especially misleading where the customer is "a relatively unsophisticated investor" (at *13). Customer TG, though wealthy, was a man of limited education, who testified that he had never before invested in stocks, knew nothing about the market, and would never have transferred his CD money to the Fund without the guarantees (Tr. 32, 36, 56, 58, 83).

There is abundant evidence of scienter, which requires proof that respondent intended to deceive, manipulate, or defraud,[6] or acted "with severe recklessness … involving not merely simple or excusable negligence, but an extreme departure from the standards of ordinary care." A respondent acts with scienter when the fraudulent circumstances "were so obvious … that he must have been aware of them."[7]

Apgar admitted that "there was no way I could do what this guy wanted me to write down [make the guarantee] … I'm not going to try to tell you I didn't know I couldn't do that" (Tr. 192). "[I]n reading the letter, I obviously admit that as a broker …

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[5] In re Martin R. Kaiden, Exchange Act Rel. No. 41629, 1999 SEC LEXIS 1396, at *18 (July 20, 1999)(citing TSC Industries, Inc. v, Northway, Inc., 426 U.S. 438, 444 (1976)); Basic, Inc. v. Levinson, 485 U.S. 224, 231 (1988).

[6] See Aaron v. SEC, 446 U.S. 680, 686-687, fn. 5 (1980); Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 (1976).

[7] Department of Enforcement v. Levitov, No. CAF970011 (NAC June 28, 2000), at slip op. p. 10.

I could not make those types of guaranties [sic] to [TG] or any other client" (Tr. 210). He admittedly knew that the guarantee was inconsistent with the prospectus and that he had no ability to guarantee TG's investment in the Fund (Tr. 212). Respondent repeatedly explained that he wrote the letter in order to "calm" down an angry customer and "diffuse the situation" (Tr. 192, 203), purposes which reflect scienter.[8]

Respondent argues that his January 2, 1998 letter was not fraudulent because TG could not reasonably rely on it and because it did not cause the customer to sustain losses (Br., pp. 22-23).[9] These contentions lack merit. It is well settled that in disciplinary proceedings (unlike private fraud actions) reliance and damage are not required elements of proof. See, e.g., Martin Herer Engelman, Exchange Act Rel. No. 35729, 1995 SEC LEXIS 1197 at *27 (May 18, 1995); Shaw Hooker & Co., Exchange Act Rel. No. 14289, 1977 SEC LEXIS 105 at *13 (December 19, 1977); Dist. Bus. Conduct Committee v. Carol Ann Rhoads, No. C05920027, 1993 SEC Discip. LEXIS at *19, 24 (DBCC June 25, 1993).

IV. Forgery

On February 6, 1998, someone wrote another letter to the customer, which again guaranteed a fixed rate of interest (this time 7.0%) and was purportedly signed by Mr.

[8] Dist. Bus. Conduct Committee v. Cary Daniels Clark, No. C3A030010, 1994 NASD Discip. LEXIS 3 at *26 (NBCC May 18, 1994) (representations made to lull investors into false sense of security). Respondent does not dispute that his January 2, 1998 guarantee was made in connection with the purchase or sale of a security. The letter was written only two weeks after the investment and was made for the specific purpose of trying to lull the customer into inaction. The SEC regularly treats such post-investment lulling as violative of Rule 10b-5. See, e.g., S.E.C. v. Asset Recovery and Management Trust, Litigation Rel. No. 17920, 2003 SEC LEXIS 24 (January 7, 2003); Edward Thomas Jung, Exchange Act Rel. No. 45669, 2002 SEC LEXIS 793 (March 28, 2002); Douglas J. Hopwood, Exchange Act Rel. No. 43353, 2000 SEC LEXIS 2041 (September 26, 2000).

[9] Respondent says that the letter was "expressly conditioned" on his supervisor's approval (Br., p. 23) because Apgar attached a note to it saying "a copy of this letter has been sent to my boss Jim Lithgow. He will sign and return it. I will then forward that to you" (CX-3). By its terms, that note did not make the guarantee contingent upon Lithgow's approval. Indeed, the promise that Lithgow "will sign" added significance to the guarantee. Significantly, Respondent himself acknowledged in his investigative testimony that nothing in the letter would lead the customer to believe that the guarantee depended upon someone else's approval (CX-5, p. 42).

Lithgow, Respondent's supervisor (CX-4). Enforcement alleges that Respondent forged Lithgow's signature. During the hearing, the parties stipulated that the signature on this February letter was not Lithgow's (Tr. 126). The issue is whether Enforcement showed by a preponderance of the evidence that Apgar made the questioned signature.

Respondent acknowledges that the February letter was "substantially identical" to the January 2 letter (Br., p. 7). Though Apgar had access to the stationery and to the several bank typewriters which could have produced the letter, he explained that at least eighteen other employees also had such access (Tr. 195, 198). Lithgow claimed that Respondent admitted the forgery to him. Respondent denied the asserted admission, and the bank's principal investigator testified that Lithgow never mentioned it to him (Tr. 264).

Although Respondent's January 2 letter guaranteed a return of 7.1%, the forged letter guaranteed 7.0%. Reducing the guaranteed return would only upset the customer further, a result totally inconsistent with Apgar's motivation. There is no reason why he would lower the promised rate. Moreover, TG told the bank's investigator that he received the letter in question on a FAX machine, while sitting with Respondent (Tr. 253-254), a circumstance which would make it less likely that Apgar forged the signature. The bank's investigator, with no apparent reason to lie, testified that after comparing relevant signatures and speaking with the customer, Lithgow, and Apgar, he concluded that Respondent had not signed the letter in question (Tr. 264, 265, 276). A handwriting expert testified that he could neither eliminate nor identify Apgar as the author; when asked whether he could state "with any degree of scientific accuracy that Mr. Apgar is the author of the disputed signature" the expert said: "No, I cannot" (Tr. 153).

The Panel concludes that the evidence is, at best, in equal balance on the question whether Apgar committed forgery. Here again, as with the alleged oral misrepresentations, Enforcement has not carried the burden of proving the offense by a preponderance of the evidence (see authorities cited in footnote 3 supra). Accordingly, the Panel is not persuaded that Apgar more likely than not wrote the signature in question.

V. The "Delay" Defense

Respondent argues that this proceeding should be dismissed because of excessive delay, citing Jeffrey Ainley Hayden, Exchange Act Rel. No. 31772, 2000 SEC LEXIS 946 (May 11, 2000) and Dep't of Enforcement v. Morgan Stanley DW Inc., No. CAF000045, 2002 NASD Discip. LEXIS 11 (NAC July 29, 2002), where the SEC and NAC found unfairness due to the passage of time.

In Morgan Stanley, the National Adjudicatory Council looked to four particular time periods as pertinent to the possibility of unfairness through delay. In the instant case, those four periods were markedly less than those in Hayden and Morgan Stanley. Four years and seven months elapsed between the first alleged misconduct (December of 1997) and the filing of the Complaint (July of 2002). In Hayden, that period was nearly fourteen years, while in Morgan Stanley, it was eight years. In this case, four years and five months elapsed between the last alleged misconduct (February of 1998) and the Complaint (July of 2002); in Haley, this period was over six years, and in Morgan Stanley, it was seven years. In the present case, sixteen months elapsed between the first notice of alleged misconduct (March of 2001)[10] and the Complaint (July of 2002). In Hayden, that period was five years, and in Morgan Stanley, it was over five years.

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[10] The NASD investigator testified that TG first complained in March of 2001 and that the NASD began its investigation in July of 2001 (Tr. 156).

Finally, the time from the start of the instant investigation (July of 2001) (Tr. 156) to the issuance of the Complaint (July of 2002) was about one year, as compared to over three years in Hayden and over four years in Morgan Stanley.

Unlike Morgan Stanley, this is not a case where "Enforcement was aware early on of the nature of the allegedly wrongful conduct" (Id., at *37). In the present case, there is no suggestion that Enforcement knew of the 1998 events before March of 2001, when TG came to the NASD office. Thereafter, the Department began its investigation in July of 2001 (Tr. 156) and filed the Complaint in July of 2002. Cf. Robert Tretiak, Exchange Act Rel. No. 47534 (SEC March 19, 2003) (rejecting claim of laches, where NASD received the matter in late 1997, took testimony in February of 1998 and filed a Complaint in July of 1999) (slip op. at 17).

Considering all of the circumstances, the Panel concludes that the delay here did not produce fundamental unfairness and rejects the Respondent's argument for dismissal of the proceeding.

VI. Sanctions

A. The circumstances

Respondent's false representation of a guaranteed rate of return reflected serious misconduct. It involved a $4 million investment, may have lulled the customer into withholding further questions about his investment for six months, and ultimately led the bank to settle with TG. Meanwhile, Respondent netted $27,000 in commissions from the transaction (Tr. 297-298), which money he still retains.

However, there were countervailing considerations. The misconduct consisted of one act directed at one customer (the January 2, 1998 letter to TG). Allegations that Apgar made antecedent oral misrepresentations were not proven. The customer may well have confused the Eaton Fund with other investments, particularly in light of the

customer's acknowledgement that he and Respondent did discuss other investments. The customer's recollection may have been influenced by the passage of several years since the events and by his interest in seeking more money from the bank.

Moreover, Respondent acknowledged his wrongdoing by making an early admission that he had written the January 2, 1998 letter (CX-7, Apgar's September 21, 2001 letter to the staff). At no point did he attempt to hide his authorship of the letter, to delay the investigation, or to conceal information from the staff. Similarly, he repeatedly and candidly admitted to the Panel that he knew it was improper to have made the guarantee.

Respondent had no other difficulty during his service with Fiserv, and the CRD record shows that, even after the customer's allegations, the firm retained him for a brief time, did not terminate him, and reported his voluntary departure (Tr. 118; CX-2., p. 5).[11] A compliance official from another firm, where Respondent worked for over a year, after the events in issue, testified to Respondent's honesty and trustworthiness, noting his care in assuring that particular colleagues were properly registered in certain states, and the absence of customer complaints about him (Tr. 240, 241). The Summit Bank's investigator also had a high opinion of Respondent's ethical and trustworthy character (Tr. 264, 267). These two witnesses appeared voluntarily and had no reason to favor Apgar.

This mix of circumstances requires some balance in selecting the appropriate sanctions, and the Panel strikes that balance here by choosing a serious monetary sanction (which will send an appropriate message for deterrence purposes), while imposing a moderate suspension which, though inflicting an economic penalty upon Apgar, nevertheless stops short of barring him.

[11] Lithgow understood that Respondent had not left voluntarily.

B. The fine

For intentional misrepresentation of material facts, the Sanction Guidelines recommend, inter alia, a fine of $10,000 to $100,000. In addition, they note that in fraud cases, the Panel may "increase the recommended fine by adding the amount of a respondent's financial benefit" (NASD Sanction Guidelines (2001), p. 96, fn. 2). The Panel believes that such an add-on is an appropriate deterrent signal to anyone who might contemplate material misrepresentations in order to lull a customer into false optimism – an especially important consideration in a declining market. The $27,000 in net commissions attributable to the TG transaction should, therefore, be added to the base fine.

As to that latter figure, the Panel notes that, the investment was large and the misconduct lulled the customer into inaction for several months and later forced the firm to settle with him. For these reasons, the fine should be more than the $10,000 which Enforcement recommended as an alternative to a bar (Tr. 299).[12] The Panel concludes that a base fine of $25,000 is appropriate and that the total fine imposed upon Respondent for this material misrepresentation should, therefore, be $52,000.[13]

C. Bar/Suspension

For intentional misrepresentations, the Guidelines recommend suspension from ten business days to two years – or, in egregious cases, a bar. Guidelines, supra, p. 96. In deciding whether Respondent should be barred or suspended for a lengthy period (action which has the same practical impact), the Panel sees Apgar as a person who committed one serious act of misconduct, but who would not likely be a recidivist. In the Panel's

[12] The Department's $10,000 suggestion was an alternative, in the event that the Panel decided against a bar, which was Enforcement's primary recommendation (Tr. 299).

[13] Enforcement argues for disgorgement of $48,886.78 (Br., p. 13). But that number reflects "gross commissions" (CX-1, ¶ 16). Apgar testified, without contradiction, that the firm withheld $26,000 to $28,000 from him (Tr. 207), and the Department's counsel agreed during the hearing that Respondent should be ordered to disgorge $27,000 (Tr. 297-298).

view, excluding him from the securities industry, directly or indirectly through a large suspension, would exact too high a price for that one mistake. The Panel concludes that a two-month suspension would be appropriate.

For these reasons, the Panel concludes that the appropriate sanction requires a substantial monetary penalty – including disgorgement of the commission – and a suspension which, while imposing an economic penalty on Apgar, would nevertheless not operate as the practical equivalent of a bar. The Panel thus concludes that Respondent should pay a fine of $25,000, augmented by the $27,000 in commissions, for a total fine of $52,000. In addition, he should be suspended for two months. Respondent is also assessed a total of $2,502.30 in costs ($1,752.30 for the transcript plus the standard $750 administrative fee).

VII. Conclusion

Pursuant to Article VI, Section 3 of the NASD By-Laws and Rule 9514(g), Respondent Apgar is suspended for two months and fined $52,000 for making a misrepresentation of a material fact, in violation of NASD Rules 2110 and 2120, Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5. Respondent is also responsible for $2,502.30 in costs, reflecting $1,752.30 for the hearing transcript and the standard $750 administrative fee.[14]

These sanctions shall become effective on a date set by NASD, but not earlier than thirty days after this Decision becomes the final disciplinary action of NASD, except that if this Decision becomes the final disciplinary action of NASD, the suspensions shall

[14] The Hearing Panel considered all of the arguments of the parties. They are rejected or sustained to the extent that they are inconsistent or in accord with the views expressed herein.

become effective with the opening of business on June 16, 2003 and end at the close of business on August 15, 2003.

HEARING PANEL

____
Jerome Nelson
Hearing Officer

Dated: Washington, DC
April 28, 2003

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