NASD REGULATION, INC.
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,	:	
Complainant,	:	Disciplinary Proceeding No. C3A010009
v.	:	
	:	**HEARING PANEL DECISION**
MARK H. LOVE (CRD #1268245)	:	Hearing Officer - DMF
Tucson, AZ	:	November 20, 2001
Respondent	:	

Respondent violated NASD Rules 3040 and 2110 by participating in private securities transactions, for no compensation, without giving written notice to the member firm with which he was associated. Respondent is suspended from association with any member firm in any capacity for 90 days and fined $25,000.

Appearances

Jacqueline D. Whelan, Esq., Regional Counsel, Denver, CO (Rory Flynn, Esq., Washington, DC, Of Counsel) for the Department of Enforcement.

Otto K. Hilbert, II, Esq., Denver, CO, for respondent.

DECISION

Procedural History

The Department of Enforcement filed a Complaint on March 20, 2001, charging that respondent Mark H. Love violated NASD Rules 3040 and 2110 by participating in private securities transactions without giving prior written notice to the member firm with

which he was associated.[1] Love filed an Answer in which he denied the charges and requested a hearing. A Hearing Panel composed of a Hearing Officer and two current members of the District Committee for District 3 held such a hearing on September 10, 2001, at which two NASD Regulation staff members and Love testified. Enforcement also introduced 16 Complainant's exhibits (CX 1-16) and six joint exhibits (JX 1-6).[2] In addition, prior to the hearing the parties filed extensive stipulations regarding the relevant facts (Stip.).

Facts

1. Love's Background in the Securities Industry

Love has been in the securities industry since 1984. From 1988 to 1995, he was associated with NASD member PaineWebber Incorporated as a general securities representative. The events in question occurred in 1994, while Love was associated with PaineWebber. He is currently associated with another member in the same capacity.[3] (CX 16; Stip. 1.)

During the relevant period, Love was the number one producer in PaineWebber's Tucson, Arizona office; his personal production was approximately $1 million per year. His clients, including a number of famous sports stars, had millions of dollars under management with him. (CX 1, at 20-21, 25; Tr. 108, 160.) According to Love, "the majority of my business is fee based, not commission-based business, where I would help

[1] Enforcement originally filed a Complaint on January 4, 2001 that included charges against another respondent, as well as Love. Love filed a motion asking that the charges against him be severed from those against the other respondent, and on March 5, 2001 the Chief Hearing Officer issued an order granting the motion. Enforcement then filed the March 20 Complaint that included only the charges against Love.

[2] Several of the exhibits included copies of firm records that were barely legible or partly illegible, but Enforcement represented that the exhibits were the best copies available. (Tr. 47-48.)

[3] Because Love was associated with a member at the relevant time, and is still associated with a member, the NASD has jurisdiction over these proceedings.

[customers] find outside money managers throughout the United States. From that I would follow those managers' production, I mean as far as their rates of return and risks, and that's basically what I've done all my career." (CX 1 at 6-7.)

2. The Bryan Foster/Summit West Partners Investments

Among Love's PaineWebber customers in 1994 were WJ Sr. and his son WJ, Jr.; DJ and his wife EJ; and PR and his wife RR. WJ Sr. and WJ Jr. had accounts totaling nearly $400,000; DJ and EJ had accounts worth several million dollars; and PR and RR also had several million dollars invested through PaineWebber accounts. (Tr. 53, 103; Stip. 3-6.)

According to Love, at various times during 1994 these customers independently told him they were seeking investments that would bring a greater rate of return than they were getting through their managed accounts – particularly investments in initial public offerings (IPOs). In each case, Love told the customers that they could invest in IPOs through Bryan Foster. (Stip. 8-9; Tr. 87-89, 96, 98-101.)

Love first learned about Foster in 1993, when another PaineWebber registered representative, Thomas Zirbel, told Love that "a friend of his that he's known for a long time [Foster] has started a partnership [Summit West Partners] that invests in IPO[s] and does day trades and … that type of business and is … making a lot of money for his clients …." (CX 1, at 27.) Initially, Love contacted Foster on his own behalf, in an effort to enlist Foster as a customer. In December 1993, Foster opened a PaineWebber account through Love in the name of Garman Art Supply. Foster effected a few transactions in the Garman account in late 1993 and early 1994, on which Love earned commissions. (Stip. 7, 28-29; Tr. 84-85, 147; CX 15.)

Love said that when the customers approached him about IPO investing, he thought of Foster. According to Love, he was unable to obtain any significant IPO allocations for his customers through PaineWebber, and Foster's operation was the only vehicle he knew through which the customers could invest in IPOs. (Tr. 86, 89, 96, 101, 155.)

The parties stipulated that Love told the customers that he "understood that Summit West Partners, an entity formed and controlled by Bryan Foster, was receiving funds from members of the public and using such funds in an IPO trading program developed and implemented by Bryan Foster," and also told the customers how to contact Foster. (Stip. 9-10, 15-16, 18-19.) In testimony during the investigation, Love said, more specifically, he told the customers that "a guy [Zirbel] that I worked with at PaineWebber … for a period of probably three or four years … knows Foster really well. They're best friends. He has visited him. He knows his operation. As a matter of fact, he's even thinking about going to work for him." (CX 1, at 66-67.) At the hearing, Love confirmed he told the customers "[t]here was a gentleman [Foster] that I was referred to by Tom Zirbel that would help them [invest in IPOs] if they wanted him to." (Tr. 89.)

There was evidence that Love's role was more substantial. Enforcement provided the transcript of a staff interview of WJ Sr. during the investigation. WJ Sr., who was 95 when the interview was conducted in April 1998 and had passed away by the time of the hearing, said that Love initiated the Summit West Partners investment by calling WJ Jr. and suggesting that WJ Sr. and WJ Jr. invest through Foster "who did nothing but buy and sell IPOs and did very well at it." Love "didn't say how well. He just said [Foster] had made a lot of money and that his reputation was very good." According to WJ Sr.,

Love "said he had known Bryan Foster for years … and the only thing was he needed about a half a million dollars in order to expand his business." Love "said if we would invest the $400,000, that he, Mark Love, would invest $100,000 in that." WJ Sr. said that "when we heard that Mark Love would invest $100,000, we were inclined to go along with this darned thing because we had pretty good trust in Mark at that time and we had confidence in his ability, you know, as an investment advisor." According to WJ Sr., however, when he received a confirmation statement from Foster reflecting his investment in Summit West Partners, "to my amazement, there was nothing in here about Mark Love … how much he invested, nothing. So I called Mark. I said, Mark, what the heck happened here? You didn't invest your $100,000. He said, well, I couldn't do it. He says, a conflict of interest." (CX 2, at 5-8, 19.)

Enforcement did not offer any evidence to corroborate WJ Sr.'s testimony that Love approached WJ Jr. about investing in Foster's operation.[4] Love insisted that he discussed Foster with WJ Sr. and WJ Jr. only after they told him they needed "a bunch of money" to pay for renovations to a house they owned in Canada, said they had previously invested in IPOs through a broker in Canada, and asked Love if he could obtain IPO investments for them. According to Love, this led him to bring up Foster, the only vehicle he was aware of through which they could invest in IPOs. (Tr. 98-101.)

Love admitted, however, that he told WJ Sr. that he "would look into whether or not [he] could" invest in Foster's operation, along with WJ Sr. and WJ, Jr., and that he later told WJ. Sr. he "could not do that style of investment." (Tr. 173.) Love said that

[4] Neither WJ Jr. nor any of the other customers testified at the hearing, and Enforcement did not interview any customers other than WJ Sr. during the investigation. (Tr. 37, 80, 82.) Enforcement offered customer DJ's responses to an Investor Questionnaire that NASDR staff sent him in May 1998, but his responses were too summary to shed any significant light on Love's role in the investments. (CX 3.)

when he spoke about investing himself, he was not trying "to entice [WJ, Sr.] to put money in [Foster's operation]." He acknowledged however, "Clients listen to their investment advisors – their language, and what they would do. They trust me. And if I told them, go take $500,000 and put it in a small-[cap] money manager, they would probably do that because of the relationship I have with them." (Tr. 173-74.)

In contrast to his extensive knowledge about the money managers he recommended (CX 1, at 7-10, 12, 14, 17), Love knew very little about Foster's operation or past performance. Love said he was "not sure that I completely understood exactly what [Foster] was doing." (Tr. 89.) He thought that Zirbel "knew him real well and trusted him and that type of thing," but neither Zirbel nor Foster gave Love any specific information about Foster's past performance for his clients. (CX 1, at 28, 30, 85.) Love simply assumed Foster was successful: "I knew the area he was in, and I knew the IPOs. So I knew that he had to be into a lot of the ones that were hot during that time. I'm sure that he was getting involved with them." (Tr. 151-52.)

In spite of this, Love said he felt no responsibility for suggesting Foster to his customers, because he "was very specific with these clients that if the money leaves and goes to Foster, that's their responsibility because it's not something I could check out." (Tr. 91, 101.) The customers were "on [their] own as far as finding out what's going on with [their investments]." (Tr. 97.) Love expected the customers to do their own due diligence with respect to Foster's operation, explaining: "I don't know exactly what they would ask. But, I think, they would put him through the same types of questions that they asked the other money managers that they were working with. I mean, about their strategy, their holding and selling strategy. You know, go through the whole gambit of

questions." (Tr. 150-51.) That is, Love thought that the customers would obtain the sort of information that Love and PaineWebber typically obtained about every money manager they recommended, but that Love did not seek or obtain regarding Foster.

All the customers ultimately entered into "Partnership Agreements" with Foster, through which they invested in Summit West Partners. WJ Sr. and WJ Jr. invested more than $365,000, which they obtained by liquidating their PaineWebber accounts; DJ and EJ invested $100,000, which came from their PaineWebber accounts; and PR and RR invested $225,000, some of which came from their PaineWebber accounts. In each case, the customers completed documents authorizing the transfer of funds from their PaineWebber accounts and provided the documents to Love. (Stip. 11-14, 17, 20-26; CX 6-12.)

Although the Partnership Agreements indicated that the investments involved "partnership interests" in a general partnership, the Agreements also provided that "the investors will contribute a pool of money to an account and the account will be managed by Foster with investors in the aggregat[e] receiving 50% of the profits and losses earned in the account and Foster receiving in the aggregate 50% of the profits and losses earned in the account." The Agreements emphasized that the purpose of the partnership was to fund a securities trading operation; that "Foster will have full discretion to trade the account by buying and selling securities of his selection."; and that "[m]anagement and operation of the Partnership business shall in every respect be the full and exclusive responsibility of [Foster]." The Agreements also provided that the customers' partnership interests were transferable, and that Foster could sell additional partnership interests to any person acceptable to him. (CX 7, 10, 12.)

For some period of time the customers believed their investments were performing well, based on periodic account statements from Summit West Partners showing that the customers had realized substantial "trading gains." But even though the Agreements provided that the customers could withdraw up to $30,000 during any month with no advance notice, the customers found it difficult to do so. When the customers encountered difficulties with Foster and Summit West Partners, they called upon Love to intercede with Foster on their behalf, and he did so. (Tr. 92-95, 97-98; CX 2 at 8-9.)

Ultimately, however, Foster's business collapsed. Although the record does not establish the reasons for the collapse in detail, Love's testimony during the investigation and at the hearing indicated that Foster was engaged in fraud, including using investors' funds to make high risk loans, rather than IPO investments.[5] (Tr. 107; CX 1, at 108-10.) In the end, the customers lost most or all of their investments. WJ Sr. and WJ Jr. and PR and RR filed arbitration claims against PaineWebber, which PaineWebber settled, apparently over Love's objection, paying the customers a portion of their losses. (Tr. 126, CX 2 at 11-12, CX 13; JX 6.) PaineWebber, in turn, filed a claim against Love, who also settled, paying PaineWebber $150,000 toward the $385,000 total that PaineWebber paid to the customers. (Tr. 111-12, 125.)

Discussion

1. Private Securities Transactions

Rule 3040(b) prohibits any person associated with a member firm from "participat[ing] in any manner in a private securities transaction," unless, prior to

[5] The NASDR staff began its investigation after receiving a referral from the Federal Bureau of Investigation concerning another representative who had been involved with Foster. The investigation eventually expanded to include Love, Zirbel and other representatives. (Tr. 33-35.) Foster was apparently convicted and imprisoned for his activities. (Tr. 76.)

participating in the transaction, the associated person provides "written notice to the member with which he is associated describing in detail the proposed transaction and the person's proposed role therein and stating whether he has received or may receive selling compensation in connection with the transaction …." A private securities transaction is defined in Rule 3040(e) as "any securities transaction outside the regular course or scope of an associated person's employment with a member …."

In addition, Rule 3040(c) provides that if the associated person has received or may receive compensation for participating in a private securities transaction, the member firm must advise the associated person, in writing, whether the member approves or disapproves the person's participation. If the firm approves participation, it must record the transaction on the firm's books and records and supervise the associated person's participation "as if the transaction were executed on behalf of the member." In this case, however, Enforcement does not contend that Love received, or might have received, compensation for his customers' investments in Summit West Partners, and Love denies receiving or expecting any compensation.[6] Rule 3040(d), however, provides that, even if the person will not receive compensation, the firm may "require the person to adhere to specified conditions in connection with his participation in the transaction."

Love concedes that the Summit West Partners investments were securities, and that his activities in connection with those investments were outside the regular course of

[6] As noted above, Love received commissions for some trades effected in the Garman Art Supply account that Foster controlled. In addition, in 1995 and 1996, subsequent to the customers' investments, Love made a series of loans to Foster, who repaid some of the loans with substantial interest, but ultimately defaulted. (Tr. 105-06, 122, 138-41.) Enforcement does not contend that the commissions or the returns on the loans amounted to "compensation in connection with the transactions" under Rule 3040(c). As Love pointed out, he lost the management fees he would otherwise have earned on the money that the customers transferred from their PaineWebber accounts to Summit West Partners. (Tr. 104.)

his employment with PaineWebber.[7] (Tr. 19.) He also admits he did not give PaineWebber any written notice of his activities in connection with those investments. (Stip. 27.) But he argues that he was not required to give notice, because he did not "participate in any manner" in the sale of the Summit West Partners investments to his customers.

2. Love Participated in the Summit West Partners Transactions

The SEC and the NASD have interpreted the phrase "participate in any manner" broadly, to further the purposes of Rule 3040. The SEC explained those purposes in Anthony J. Amato, 45 S.E.C. 282, 285 (1973):

> The regulatory scheme under the Exchange Act, in which the NASD is assigned a vital role, imposes on broker/dealer entities and NASD member firms the responsibility to exercise appropriate supervision over their personnel for the protection of investors. Where employees effect transactions for customers outside of the normal channels and without disclosure to the employer, the public is deprived of protection which it is entitled to expect. Moreover, the employer may also thus be exposed to risks to which it should not be exposed. Thus, such conduct is not only potentially harmful to public investors, but inconsistent with the obligation of an employee to serve his employer faithfully . . . . There is always a possibility in these situations that some improper conduct may be involved or that the employer's interests may be adversely affected. At the least, the employer should be enabled to make that determination. (Footnotes omitted.)

[7] General partnership interests are securities where "(1) an agreement among the parties leaves so little power in the hands of the investor that the arrangement in fact distributes power as would a limited partnership; (2) the investor is so dependent on some unique entrepreneurial or managerial ability of the promoter or manager that he or she cannot replace the manager of the enterprise or otherwise exercise meaningful partnership or venture powers; or (3) the investor is so inexperienced and unknowledgeable in business affairs the investor is incapable of intelligently exercising managerial powers." Maxmimo Justo Guevara, Exchange Act Rel. No. 42793 (May 18, 2000). At least the first two of these circumstances clearly apply to the Summit West Partners investments.

In light of these purposes, the SEC and the NAC have found that even very limited involvement by an associated person is sufficient to trigger the requirement that the person give written notice to his or her employer.[8]

In this case, unlike most prior cases, Enforcement does not contend that Love received, or expected to receive, any compensation for his customers' investments in Summit West Partners. But even if he did not expect to be compensated, Love's involvement in these transactions, though limited, was sufficient to require that he give PaineWebber prior written notice.

Love says that he told the customers about Foster and Summit West Partners only after they asked, generally, about investing in IPOs.[9] Love admits, however, that in response to the customers' general inquiries, he brought up Foster and Summit West Partners. Love does not claim that the customers were even aware of their existence until then. And Love did more than mention Foster's name. He admits he told the customers of Foster's former employment with PaineWebber and of Zirbel's acquaintance with and favorable opinion of Foster, and, in the case of WJ Sr., expressed his own desire to

[8] See, e.g., Charles A. Roth, Exch. Act Rel. No. 31085, 52 SEC Docket 1102 (Aug. 25, 1992) ("We have previously held that a registered representative who merely introduces clients seeking to purchase control of a company to company management, and later receives a finder's fee when the transaction is consummated, participates in a securities transaction"; Gilbert M. Hair, Exch. Act Rel. No. 32187, 53 SEC Docket 2439 (April 21, 1993) (representative referred customer to a firm that sold the customer a note, and received a commission on the sale); James L. Owsley, Exch. Act Rel. No. 32491, 54 SEC Docket 739 (June 18, 1993) (representative arranged meeting between a customer and an individual who sold the customer stock in his company, and received a finder's fee); District Bus. Cond. Comm. for Dist. 2 v. Gluckman, No. C02960042 (NAC Jan. 23, 1998), aff'd, Exch. Act Rel. No. 41628 (July 20, 1999) (representative "referred the customers to [the seller], typed the agreements, and received a five percent fee for the transactions"); District Bus. Cond. Comm. for Dist. 8 v. Mohn, No. C8A960063 (NAC Jan. 22, 1999) (representative did not receive compensation, but, among other things, admitted he brought the limited partnership investment to the customers' attention; was considered the "expert" regarding the limited partnership by the customers; completed portions of the subscription documents for the customers; and determined the suitability of the limited partnerships as investments for the customers).

[9] Although WJ Sr's statement calls this into question, the Hearing Panel accepts Love's version for purposes of this decision.

invest. The customers would reasonably have understood Love to be endorsing investments with Foster.

In light of this, Love could not distance himself from the customers' decision to invest merely by telling them that they were on their own and would have to do their own due diligence investigation. As Love admits, based on their past experience with him, the customers would "trust me. And if I told them [to make a particular investment] they would probably do that because of the relationship I have with them." Love also admits that when the customers encountered problems with Foster, they called Love and asked him to intercede with Foster on their behalf, which he did. While Love describes this as an accommodation, it indicates to the Hearing Panel that both the customers and Love behaved as though he bore some responsibility for their investments.

Love's involvement in these investments raised precisely the concerns that Rule 3040 seeks to address. The customers, following the lead of their registered representative, invested in securities without any of the protections normally afforded to those who invest through member firms. Because Love did not give PaineWebber prior notice of his involvement, the firm had no opportunity to impose conditions that might have protected the customers. And when the customers suffered losses, the firm was subjected to customer claims that it might have avoided if Love had given prior notice.

Therefore, the Hearing Panel found that Love "participated" in these securities transactions, within the meaning of Rule 3040. Even if he was not being compensated, Love was required to give written notice to PaineWebber prior to participating, describing the proposed transactions and his proposed role. Love admits he did not give

PaineWebber any such notice. Love thereby violated Rule 3040, and by violating that rule, he also violated Rule 2110.[10]

Sanctions

For private securities transaction violations, the Sanction Guidelines recommend a fine of $5,000 to $50,000 and a suspension for 10 days to one year or, in egregious cases, a longer suspension or a bar. NASD Sanction Guidelines at 19 (2001 ed.) The Guidelines list as principal considerations in setting sanctions: (1) whether the respondent had a proprietary or beneficial interest in or was otherwise affiliated with the issuer; (2) whether the respondent attempted to create the impression that his employer sanctioned the activity; (3) whether the respondent sold away to customers of his employer; (4) whether the respondent gave his employer oral notice of his participation; and (5) whether the respondent sold the investment after he had been told or warned by his employer not to do so. There is no evidence that Love had an interest in Summit West Partners, that he attempted to convey the impression that PaineWebber sanctioned his activities, or that he was involved after being warned by PaineWebber. Love does not claim that he gave PaineWebber oral notice. Thus, the only listed consideration that applies is that the investors were PaineWebber customers, which is an aggravating factor in determining sanctions.

This case is distinguishable from recent reported NASD cases involving private securities transactions in two important respects: first, Enforcement does not claim that Love received or expected to receive compensation for his participation in the transactions; and second, Love's involvement in these investments, while sufficient to

[10] See Jim Newcomb, Exch. Act Rel. No. 44945, 2001 SEC LEXIS 2172 (Oct. 18, 2001), at *1, n. 1.

trigger the notice requirement, was considerably less than that of other respondents.[11] The Hearing Panel found that these circumstances tended to reduce the level of sanctions needed to accomplish the Association's remedial goals.

The Hearing Panel rejected, however, Love's plea that, if the Panel found a violation, it should impose no sanction, or the minimum suspension and fine recommended in the Guidelines. (Tr. 220.) In his testimony at the hearing, Love expressed considerable resentment and unhappiness about his own circumstances, but nothing to suggest that he realizes he made a serious error by failing to give notice to PaineWebber, or that he has any remorse about the losses his customers suffered as a result of investing in Summit West Partners. The violations in this case were not minor or technical. Customers who trusted Love and followed his advice invested in Summit West Partners, suffered substantial losses, and recouped a portion – but only a portion – of their losses from Love's employer. None of this might have happened if Love had given the written notice required by Rule 3040.

In order to ensure that Love appreciates the significance of his misconduct, and to deter Love and others from similar misconduct in the future, more than minimum sanctions are required. The Hearing Panel, therefore, will suspend Love, in all capacities, for 90 days and fine him $25,000.

Conclusion

The Hearing Panel finds that respondent Mark H. Love violated Rules 3040 and 2110 by participating in private securities transaction without giving written notice to the

[11] See, e.g., Department of Enforcement v. Fergus, No. C8A990025 (NAC May 17, 2001); District Business Cond. Comm. No 5 v. Goldsworthy, No. C05940077 (NAC Oct. 16, 2000); Department of Enforcement v. Ansula Pet Hwa Liu, No. C04970050 (NAC Nov. 4, 1999), as well as the cases cited above in footnotes 8 and 10.

member firm with which he was associated. As sanctions, Love is suspended from association with any member firm in any capacity for 90 days and fined $25,000. In addition, he is assessed costs in the amount of $1,879.52, which includes an administrative fee of $750 and hearing transcript costs of $1,129.52. These sanctions shall become effective at a time set by the Association, but not less than 30 days after this decision becomes the final disciplinary action of the Association, except that if this decision becomes the final disciplinary action of the Association, Love's suspension shall commence on January 21, 2002 and end on April 21, 2002.[12]

HEARING PANEL

By: _____
David M. FitzGerald
Hearing Officer

Copies to:

Mark H. Love (via overnight delivery and first class mail)
Otto K. Hilbert, II, Esq. (via facsimile and first class mail)
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[12] The Hearing Panel has considered all of the arguments of the Parties. They are rejected or sustained to the extent they are inconsistent or in accord with the views expressed herein.