

NASD OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

STEPHEN NICHOLAS THOMAS
(CRD No. 3236045)
190-07 119th Ave.
Queens, NY 11412,

Respondent.

Disciplinary Proceeding
No. C10030082

PANEL DECISION

Hearing Officer – SW

Dated: June 30, 2004

Respondent is barred from associating with any member firm in any capacity for violating NASD Conduct Rule 2110 through the improper use of his customers' funds.

Appearances

Philip Rothman, Esq., Regional Counsel, and Linda H. Kolodny, Esq., Regional Counsel,
New York, New York, for the Department of Enforcement.

Stephen Nicholas Thomas, pro se.

DECISION

I. Introduction

The NASD Department of Enforcement (“Enforcement”) filed a Complaint against Respondent Stephen Nicholas Thomas (“Respondent”) on October 10, 2003, alleging that Respondent violated NASD Conduct Rule 2110 by converting or misusing the funds of two public customers, when he kept or mishandled \$150 in cash that was to be used to pay his customers’ insurance premiums.

Respondent filed an answer to the Complaint denying that he used the money for his personal use or benefit, but admitting that he had not applied the funds as directed by the customers and had not timely returned the funds.

The Hearing Panel, composed of an NASD Hearing Officer and two current members of the District 10 Committee, held the hearing on this matter in New York, New York, on April 1, 2004.¹

II. Findings of Fact and Conclusions of Law

A. Jurisdiction

Respondent registered as an investment company and variable contracts products representative with NYLife Securities, Inc. (“NYLife”) on June 22, 2001. (CX-1, p. 3).

On October 1, 2002, NYLife terminated Respondent’s registration for “failing to remit a customer’s \$50 traditional whole life insurance premium.” (Id.). Respondent has not been associated with any other member firm since October 1, 2002. (Id.). Article V, Section 4 of NASD’s By-Laws creates a two-year period of retained jurisdiction over formerly associated persons, covering misconduct occurring before the association terminated.

Enforcement filed the Complaint on October 10, 2003, within two years of the October 1, 2002 termination of Respondent’s association with an NASD member firm. The Complaint alleges misconduct that occurred while Respondent was associated with NYLife. NASD thus has jurisdiction over this proceeding.

B. Respondent’s Improper Use of the Funds of Two Customers

The primary facts are not in dispute. On March 25, 2002, customer DJ gave Respondent

¹ References to the testimony set forth in the transcripts of the Hearing will be designated as “Tr. ___”, with the appropriate page number. References to the exhibits provided by Enforcement will be designated as “CX-___”, and Respondent’s exhibits will be designated as “RX-___.”

\$50 in cash, as an initial premium payment on a new whole life insurance policy that Respondent had solicited DJ to purchase.² (Tr. p. 29; CX-4). Respondent never applied the cash as DJ requested, and NYLife did not issue an insurance policy to DJ.³ (Tr. pp. 83, 116-117).

In at least one telephone call in April 2002, Respondent lied to DJ about her insurance policy's effectiveness, by assuring DJ that "everything was okay." (Tr. pp. 33-34, 280-281; CX-5, p. 5). Respondent testified that he accepted DJ's cash, and then misplaced the cash and her contact information.⁴ (Tr. pp. 58, 236). Respondent testified that, when he subsequently found DJ's money, he put it in an envelope with customer HG's cash. (Tr. p. 264). Respondent admitted that he held on to DJ's money for at least five months, without offering to return her money.⁵ (Tr. p. 289). Respondent did not speak with DJ about returning her money until after DJ wrote a complaint letter to NYLife and after NYLife terminated his employment.⁶ (Tr. pp. 40-41, 287; CX-2).

On June 7, 2002, customer HG gave Respondent \$100 in cash as an initial premium payment to switch from a term policy to a whole life insurance policy.⁷ (Tr. p. 167; CX-12). Respondent did not apply the cash for an insurance policy and did not return the funds to HG. (CX-11). Respondent testified that HG contacted him the next day and asked that her insurance application be canceled. (Tr. p. 251). Respondent testified that he did not immediately return

² Respondent and DJ went to school together and knew each other for more than 21 years. (Tr. p. 20).

³ Respondent admitted that he never submitted the application for DJ to NYLife. (Tr. p. 226).

⁴ Respondent testified that the \$50 in cash was a \$50 bill that he had attached to DJ's application and subsequently misplaced. (Tr. pp. 236-237, 244).

⁵ Language in NYLife's handbook, provided to its agents, indicates that cash should be submitted immediately, barring any sort of extenuating circumstances. (Tr. p. 129; CX-15).

⁶ Respondent testified that he had misplaced DJ's contact information and was unsuccessful in reaching her until September 2002 after he searched his office and located her business card. (RX-2; Tr. pp. 287-288). DJ faxed a complaint to NYLife on September 4, 2002. (CX-2). NYLife suspended Respondent on September 4, 2002, and fired him approximately two weeks later. (Tr. pp. 118, 123).

⁷ Respondent also had a prior relationship with HG having dated one of her daughters. (Tr. p. 250).

HG's money because he wanted to talk with HG to see if he could convince her to go forward with converting her term policy to a whole life policy.⁸ (Tr. pp. 256-257, 296). In October 2002, HG wrote to NYLife complaining that she had not received her policy. (CX-11).

NYLife reimbursed DJ and HG on September 10, 2002 and November 6, 2002, respectively. (CX-8; CX-13). DJ ultimately applied her reimbursement to purchase a life insurance policy from NYLife; HG did not purchase a policy. (CX-9; CX-14).

Improper use of a customer's funds occurs when the funds are not used as intended by the customer. Improper use of a customer's funds rises to the level of conversion when a registered representative uses the funds for his own use and benefit, without authorization, and fails to repay the customer.⁹ The National Adjudicatory Council has consistently held that failing to promptly return a customer's funds constitutes misuse of funds and violates NASD Conduct Rule 2110.¹⁰

Respondent failed to make earnest timely efforts to return his customers' funds because he believed that there was no hurry to return the funds of two people who knew him well. However, friendship is no excuse for failing to comply with the high standards of commercial honor. The Hearing Panel finds that Respondent violated NASD Conduct Rule 2110 through the

⁸ Respondent testified that when he subsequently attempted to contact HG, she had moved. (Tr. pp. 17, 256-257).

⁹ Dep't of Enforcement v. Kendzierski, Complaint No. C9A980021 (NAC, Nov. 12, 1999) at http://www.nasdr.com/pdf-text/nac1199_06.pdf.

¹⁰ See Dist. Bus. Conduct Comm. District 2 v. Roach, 1998 NASD Discip. LEXIS 11 (Jan. 20, 1998) (finding respondent violated NASD Conduct Rule 2110 by making improper use of customers funds when she deposited 16 customer checks totaling \$160,000 into an account in her name and funds remained in the account for up to 112 days); see In re Bernard D. Gorniak, Exchange Act Release No. 35,996, 1995 SEC LEXIS 1820 (1995) (finding respondent violated NASD Conduct Rule 2110 when he accepted customer funds and failed to make timely investments with the funds as instructed and failed to promptly return the funds); see Dist. Bus. Conduct Comm. District 4 v. Schimon, Complaint No. C04920066 (NBCC, Nov. 1, 1993) (finding respondent violated NASD Conduct Rule 2110 when respondent's wife deposited the customer's cash in their office account and respondent negligently assured customer that the funds had been applied to purchase an insurance policy).

improper use of the funds of his two customers.¹¹

III. Sanctions

A. Improper Use

The NASD Sanction Guidelines for improper use of funds or securities recommend that the adjudicator consider a bar.¹² The Sanction Guidelines further state that where mitigation exists, the adjudicator is to consider suspending respondent for a period of six months to two years in any and all capacities and thereafter until respondent pays restitution.¹³ Enforcement recommended that Respondent be barred for his misconduct.¹⁴

The Hearing Panel finds that this is an egregious case. On two separate occasions, Respondent accepted cash from a customer without filing the requested insurance application with NYLife, and, thereafter, made no earnest effort to return the funds to the customer until months later.

The Hearing Panel finds that Respondent failed to produce any genuine evidence of mitigating factors. The Hearing Panel did not find Respondent's explanations for the delays in returning DJ's and HG's funds credible. Even assuming that Respondent did misplace DJ's funds and her contact information, Respondent admitted that he waited five months before diligently searching his office in an effort to contact DJ to refund her money. Respondent also admitted that, during the five months that he held DJ's funds, he never attempted to obtain DJ's

¹¹ See Dist. Bus. Conduct Comm. District 8 v. Buenrostro, 1995 NASD Discip. LEXIS 4, *9 (Mar. 7, 1995) (finding respondent misused a customer's funds in violation of NASD Conduct Rule 2110 when he held the money from May 14 until May 29 with no valid explanation).

¹² NASD Sanction Guidelines, p. 42 (2001).

¹³ Id.

¹⁴ Id. at 13. Enforcement does not seek restitution because NYLife reimbursed the customers, and Respondent reimbursed NYLife. (Tr. pp. 39, 237, 260; CX-8; CX-9; CX-13; CX-14; RX-1).

address either through the telephone directory service or a computer search program.¹⁵

With respect to HG, even if the Hearing Panel believed Respondent's testimony that HG decided to cancel her insurance application, there is no excuse for not returning HG's funds in a timely manner. Despite being on notice in September 2002 of the importance of correctly handling a customer's funds, since NYLife had terminated him for failing to return DJ's funds, Respondent did not return HG's funds until after NYLife reimbursed HG in November 2002.

Notwithstanding the modest amounts involved, Respondent's cavalier attitude with regard to his customers' funds convinces the Hearing Panel that there is a danger that Respondent will repeat his misconduct, and therefore Respondent is a danger to the investing public.¹⁶ Accordingly, the Hearing Panel concludes that Respondent should be barred from associating with any member firm in any capacity.

IV. Order

Respondent Stephen Nicholas Thomas is barred from associating with any NASD member firm in any capacity for improper use of customer funds, in violation of NASD Conduct Rule 2110. The bar shall become effective immediately if this Decision becomes the final disciplinary action of NASD.¹⁷

SO ORDERED.

Sharon Witherspoon
Hearing Officer

Dated: Washington, DC
June 30, 2004

¹⁵ The Hearing Panel finds that Respondent's alleged sporadic attempts to contact customers through mutual friends did not constitute earnest efforts to return his customers' funds.

¹⁶ See Dist. Bus. Conduct Comm. for District 7 v. Westberry, 1995 NASD Discip. LEXIS 225 (Aug. 11, 1995) (a bar was imposed because improper use of customer funds is a serious offense which undermines the integrity of the securities industry); See Buenrostro, at *19 (respondent was barred for misusing \$770).

¹⁷ The Hearing Panel 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.

Copies to:

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Philip Rothman, Esq. (via electronic and first class mail)

Linda H. Kolodny, Esq. (via electronic and first class mail)

Rory C. Flynn, Esq. (via electronic and first class mail)