BEFORE THE NATIONAL ADJUDICATORY COUNCIL

FINANCIAL INDUSTRY REGULATORY AUTHORITY

In the Matter of Department of Enforcement, Complainant, Wedbush Securities, Inc. Los Angeles, CA, and Edward William Wedbush Los Angeles, CA, Respondents.	DECISION Complaint No. 20070094044 Dated: December 11, 2014

Member firm committed regulatory reporting failures with respect to Forms U4 and U5, NYSE Forms RE-3, and statistical reporting concerning customer complaints. Member firm and its president failed to reasonably supervise regulatory reporting. Held, findings affirmed and sanctions modified.

Appearances

For the Complainant: Leo F. Orenstein, Esq., Danielle I. Schanz, Esq., Department of Enforcement, Financial Industry Regulatory Authority

For the Respondents: John L. Erikson, Esq.

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Decision

Respondents Wedbush Securities, Inc. ("Wedbush Securities" or the "Firm") and Edward William Wedbush ("Mr. Wedbush" and together, with Wedbush Securities, "Respondents") appeal an August 2, 2012 Extended Hearing Panel decision pursuant to FINRA Rule 9311. The Extended Hearing Panel found that Wedbush Securities failed to file, late filed, and filed inaccurate: Forms RE-3 (Submission of Requested Information), in violation of NYSE Rule 351(a) and NASD Rule 2110; Uniform Applications for Securities Industry Registration or Transfer ("Forms U4") and Uniform Termination Notices for Securities Industry Registration ("Forms U5"), in violation of NASD and FINRA By-Laws, NASD Rule 2110, and FINRA Rule 2010; and statistical reports concerning customer complaints, in violation of NYSE Rule 351(d), NASD Rule 3070(c), NASD Rule 2110, and FINRA Rule 2010. The Extended Hearing Panel also found that the Firm and Mr. Wedbush failed to supervise regulatory filings, in violation of NASD Rule 3010, NASD Rule 2110, and FINRA Rule 2010.[1] For the misconduct, the Extended Hearing Panel fined Wedbush Securities $300,000 and fined Mr. Wedbush $25,000 and suspended him from all supervisory activities, other than the supervision of trading and order entry, for 31 days. After an independent review of the record, we affirm the Extended Hearing Panel's liability findings and modify the sanctions. We impose on Wedbush Securities a $300,000 fine and impose on Mr. Wedbush a 31-day suspension in all principal capacities and a $50,000 fine.

I. Background

Wedbush Securities is a securities brokerage and investment banking firm founded by Mr. Wedbush and another individual in 1955. The Firm registered with NASD in 1955 and NYSE in the early 1970s. The Firm grew substantially during the relevant period,[2] and, as of the hearing, employed approximately 900 employees.

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[1] The conduct rules that apply are those that existed at the time of the conduct at issue. The FINRA rulebook consists of: (1) FINRA Rules; (2) NASD Rules; and (3) rules incorporated from NYSE (Incorporated NYSE Rules). Following the consolidation of NASD and the member regulation, enforcement and arbitration functions of NYSE Regulation into FINRA, FINRA began developing a "Consolidated Rulebook" of FINRA Rules. While NASD Rules generally apply to all FINRA member firms, the Incorporated NYSE Rules apply only to those members of FINRA that are also members of the NYSE (Dual Members). *See FINRA Information Notice* (March 12, 2008), available at http://www.finra.org/web/groups/industry/@ip/@reg/@notice /documents/notices/p038121.pdf. For convenience, the Incorporated NYSE Rules are referred to as NYSE Rules. During the relevant period, Wedbush Securities was a dual member firm, and thus was subject to FINRA, NASD, and NYSE Rules.

[2] The relevant period is January 2005 to July 2010 unless otherwise noted.

Mr. Wedbush joined the securities industry in 1955 when he formed the Firm. He is registered as a general securities principal and representative and has served as the Firm's president since its inception.

II. Procedural History

On October 4, 2010, the Department of Enforcement ("Enforcement") filed the underlying five-cause complaint, which it amended twice thereafter to reduce the number of alleged reporting violations but otherwise not changing the causes of action. In causes one through three, Enforcement alleged that, during various periods between January 2005 and July 2010, Wedbush Securities failed to properly report 81 disclosable events, resulting in 38 Form RE-3 reporting violations, 113 Form U4 and U5 violations, and nine statistical reporting violations concerning customer complaints. In causes four and five, Enforcement alleged that Wedbush Securities (from January 2005 to July 2010) and Mr. Wedbush (from August 2006 to July 2010) failed to supervise the Firm's regulatory reporting.

Of the 160 alleged reporting violations, Respondents stipulated that Wedbush Securities was liable for 115 reporting violations alleged by Enforcement. For the remaining reporting violations for which Respondents did not stipulate, Respondents asserted that the items either did not constitute reporting violations or did constitute reporting violations but were not reporting violations by the Firm.

After presiding over a nine-day hearing, the Extended Hearing Panel issued its decision on August 2, 2012. The Extended Hearing Panel found in favor of Enforcement for all causes of action as alleged in the complaint. The Extended Hearing Panel found that Wedbush Securities was liable for the 115 reporting violations to which respondents stipulated and an additional 43 disputed reporting violations. The Extended Hearing Panel fined Wedbush Securities $300,000 and fined Mr. Wedbush $25,000 and suspended him from all supervisory activities, other than the supervision of trading and order entry, for 31 days. The Extended Hearing Panel also ordered the Respondents to jointly and severally pay costs in the amount of $14,930.95.

Respondents appealed the decision.

III. Facts

A. Business Conduct Department Management and Organization

The Firm's compliance department is known as the Business Conduct Department and, at all relevant times, was responsible for making all regulatory filings, including Forms RE-3, Forms U4 and U5, and statistical reports concerning customer complaints. During the relevant period, the Business Conduct Department was comprised of approximately eight to 10 people.

From January 1, 2005 to August 14, 2005, Marie Eaton was the Business Conduct Manager and a compliance officer, and James Richards was the Firm's Chief Compliance Officer ("CCO"). Eaton reported to the head of the Firm's legal department, who reported to Richards, who in turn reported to Mr. Wedbush.

From August 15, 2005 to August 15, 2006, Charles Huang was the Business Conduct Manager and CCO. Huang reported to the head of the Firm's legal department, who reported to Richards, who in turn reported to Mr. Wedbush.

From August 16, 2006 to September 30, 2007, Mr. Wedbush was the Business Conduct Manager. Mr. Wedbush also served as Chief Compliance Officer from August 16, 2006 until July 2007,[3] at which time, Mr. Wedbush served as the co-CCO with Vincent Moy until October 2007. While Mr. Wedbush served as the Business Conduct Manager, the Business Conduct Department reported directly to him. He remained the Firm's president throughout this time.

On October 1, 2007, Eric Segall took over Mr. Wedbush's role as Business Conduct Manager and co-CCO. Moy reported to Segall and continued to serve as co-CCO. Segall reported directly to Mr. Wedbush.

B. <u>The Firm's Regulatory Reporting Structure</u>

During the relevant period, the Business Conduct Department relied on the cooperation of the Firm's registered representatives, managers, executives, human resources department, and legal department to provide them with documents and information required for timely regulatory filings.

Regulatory reporting at the Firm occurred as follows. If Wedbush Securities received a complaint or information that triggered a disclosable event, branch management or another department at the Firm was supposed to forward the information to the Business Conduct Department. At times, branch management would determine that the complaint or information did not constitute a disclosable event and would not forward the complaint to the Business Conduct Department. After receiving notice of a potentially disclosable event, the Business Conduct Department would make its own determination whether it was disclosable and what filings and disclosures, if any, needed to be made. For an event reportable on a Form RE-3 or a reportable customer complaint, the Business Conduct Department was responsible for submitting the appropriate Form RE-3 or statistical report. For an event reportable on Forms U4 or U5, the Business Conduct Department was responsible for drafting a Form U4 or U5, providing the draft to the appropriate registered representative or manager, notifying the representative's manager of the event, and filing the signed Form U4 or U5 once it was returned by the manager.[4]

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[3] All compliance officers at NYSE firms were required to have Series 14 (Compliance Officer) licenses. Mr. Wedbush did not have a Series 14 license at the time, so he sought an exception from NYSE, which was eventually granted.

[4] A Form U4 is supposed be signed by the registered representative and manager, and a Form U5 is supposed to be signed by the manager who is approving the termination.

According to Respondents, compliance and supervision at the Firm were separate functions. The Business Conduct Department had no authority to suspend or terminate a registered representative or other Firm employee. The Business Conduct Department, however, could, and at times did, make recommendations about taking internal disciplinary action against a registered representative or placing him or her on heightened supervision. Its recommendation was not necessarily followed. Ultimately only the representative's management chain had the authority to implement any recommendation.

C. The Firm's Regulatory Reporting Deficiencies

Respondents admit that the Firm failed to properly and timely make numerous regulatory filings during the relevant period. Of the 160 alleged violations, the parties stipulated that the Firm filed 33 Forms RE-3 late, filed two Forms RE-3 inaccurately, and failed to file three Forms RE-3; filed 40 Forms U4 and 20 Forms U5 late, filed six Forms U4 and four Forms U5 inaccurately, and failed to file one Form U4 and two Forms U5; and filed late four statistical reports concerning customer complaints.

Prior to, during, and after the relevant period, the Firm received several notifications from regulators about regulatory reporting issues. Among other notifications, on March 20, 2007, the Firm submitted a Letter of Acceptance, Waiver and Consent ("AWC"), by which it accepted and consented, without admitting or denying the findings, that the Firm filed untimely 27 Forms U5 and failed to enforce its supervisory procedures with respect to the 27 Forms U5 from January 1, 2003 to August 3, 2005. The Firm was censured and fined $18,000.

Regulators also relayed many of the regulatory reporting issues to the Firm in examination exit meetings and examination reports related to the 2002, 2006, and 2008 examinations. Mr. Wedbush attended every examination exit meeting and required all executive vice presidents to do so as well. In its responses, the Firm admitted that certain Business Conduct Managers were unaware of filing requirements under NYSE Rule 351(a), that Business Conduct Department personnel were not promptly updating information, and that the legal department and branch managers were not promptly providing information and documents to the Business Conduct Department. The Firm represented that it would review its logging procedures to prevent violations, and that it had installed new personnel (including making Mr. Wedbush the Business Conduct Manger and CCO) and provided additional training in late 2007 to address the issues. Despite these assurances, the violations continued.

On December 17, 2008, FINRA staff sent the underlying Wells Notice to Segall, advising him that FINRA staff had made a preliminary determination to recommend disciplinary action be brought against the Firm for the Firm's failure to file, late filing, and filing of inaccurate Forms RE-3 and amended Forms U4 and U5. In response, the Firm admitted that there had been reporting problems, which it attributed to a lack of knowledge of Firm personnel about filing requirements, a lack of communication between the legal department and Business Conduct Department, and a lack of experience and training. Among other things, the Firm acknowledged that previously no one at the Firm was monitoring Form U5 disclosures by other firms of current Firm employees for purposes of updating the employee's Form U4. The Firm represented that it had corrected the problems: it had instituted a new communication process between the legal

department and the Business Conduct Department, and the Business Conduct Department was monitoring Form U5 disclosures daily.

In response to continued regulatory reporting violations, FINRA staff sent a second Wells Notice to Segall on June 22, 2010, advising him that FINRA staff had made a preliminary determination to recommend additional disciplinary action be brought against the Firm for the Firm's continued late filing of amended Forms U4 and U5 for the period April 1, 2008 through March 31, 2010, as reflected in the FINRA Late Disclosure Fee Reports, and the Firm's failures concerning customer complaint reporting and Forms U4 and U5, as reflected in the 2009 and 2010 examinations. In addition, the letter provided that FINRA staff also made a preliminary determination to recommend disciplinary action be brought against Mr. Wedbush for his failure to supervise the Firm's regulatory filings from January 2005 to April 2010.

At the hearing, Respondents attributed the Firm's failure to properly and timely make regulatory filings to Firm personnel outside of the Business Conduct Department who the Department relied on to provide information. Mr. Wedbush, specifically, attributed "practicably 100 percent" of the filing issues alleged in the complaint to management in the Firm's four divisions, from branch and division managers to executive vice presidents, but not to the Business Conduct Department.

IV. Discussion

The Extended Hearing Panel found that Wedbush Securities failed to file, late filed, and filed inaccurate Forms RE-3, Forms U4 and U5, and reports concerning customer complaints. Besides the reporting violations to which Respondents stipulated, the Extended Hearing Panel found that Wedbush Securities was liable for 40 disputed Form U4 and U5 reporting violations and an additional three disputed reporting violations concerning customer complaints. The Extended Hearing Panel further found that Wedbush Securities and Mr. Wedbush failed to supervise regulatory filings.

Despite broadly objecting in their notice of appeal to all of the findings of the Extended Hearing Panel, including findings related to the non-stipulated violations, Respondents thereafter exclusively focused their arguments on appeal on issues not related to the specifics of the non-stipulated violations. We focus our decision on the issues, arguments, and defenses raised by Respondents in their opening brief, reply brief, and oral argument presented to the National Adjudicatory Council ("NAC"). For these reasons and reasons set forth below, we affirm the Extended Hearing Panel's liability findings.

A. Wedbush Securities Failed to File, Late Filed, and Filed Inaccurate Forms RE-3

The Extended Hearing Panel found that Wedbush Securities failed to file, late filed, and filed inaccurate Forms RE-3 from January 2005 to July 2007, in violation of NYSE Rule 351(a) and NASD Rule 2110. We affirm the Extended Hearing Panel's findings.

NYSE Rule 351(a) required each member firm to promptly report whenever the member or any registered or non-registered employee associated with such member:

> (7) is a defendant or respondent in any securities or commodities-related civil litigation or arbitration which has been disposed of by judgment, award, or settlement for an amount exceeding $15,000 . . . [or] when a member organization is the defendant or respondent . . . [then] for an amount exceeding $25,000;
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> (8) is the subject of any claim for damages by a customer, broker, or dealer which is settled for an amount exceeding $15,000. . . [or] when the claim for damages is against a member organization . . . [then] for an amount exceeding $25,000 . . . .

NYSE defined "promptly" as occurring within 30 days of the reportable event. *See NYSE Information Memo 90-17*, 1990 NYSE Info. Memo LEXIS 41, at *1 (Apr. 30, 1990). The Form RE-3 was the mechanism for "reporting [to NYSE] under Rule 351 with respect to all employees who are continuing to work for the firm, and for non-registered persons that are terminated for cause."[5] *NYSE Information Memo 86-11*, 1986 NYSE Info. Memo LEXIS 43, at *5 (Mar. 21, 1986). A violation of NYSE Rule 351 also is a violation of NASD Rule 2110.[6] *See William J. Murphy*, Exchange Act Release No. 69923, 2013 SEC LEXIS 1933, at *26 n.29 (July 2, 2013) (providing that "a violation of another Commission or NASD rule or regulation . . . constitutes a violation of [NASD] Rule 2110").

The parties stipulated to all 38 violations alleged in the complaint with respect to failing to file, late filing, and filing of inaccurate Forms RE-3.[7] Accordingly, we find that Wedbush Securities violated NYSE Rule 351(a) and NASD Rule 2110 by failing to file, late filing, and the filing of inaccurate NYSE Forms RE-3.

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5 If there was a reportable event with respect to a former registered employee, member firms were required to report it on the employee's Form U5, not a Form RE-3. If the member firm also was a respondent or defendant in the same reportable event, the member firm may have been required to file a Form RE-3 as to the member firm. *NYSE Information Memo 90-17*, 1990 NYSE Info. Memo LEXIS 41, at *5.

6 NASD Conduct Rule 2110 (and later FINRA Rule 2010) requires members, "in the conduct of [their] business, [to] observe high standards of commercial honor and just and equitable principles of trade."

7 The parties stipulated that the Firm filed 33 late Forms RE-3, filed two inaccurate Forms RE-3, and never filed three Forms RE-3. With respect to the inaccurate Forms RE-3, the Extended Hearing Panel mistakenly found that the parties stipulated to only one inaccurate Form RE-3. We consider this discrepancy negligible, and it does not affect our findings with respect to liability or sanctions.

B. Wedbush Securities Failed to File, Late Filed, and Filed Inaccurate Forms U4 and U5

The Extended Hearing Panel found that Wedbush Securities failed to file, late filed, and filed inaccurate Forms U4 and U5 from May 2005 to July 2010, in violation of NASD and FINRA By-Laws, NASD Rule 2110, and FINRA Rule 2010. We affirm the Extended Hearing Panel's findings.

Article V, Section 2(c) and Section 3(b) of both NASD and FINRA By-Laws require member firms to report certain disclosable events on Forms U4, if the registered representative is still employed with the member firm, and on Forms U5, if the registered representative is no longer employed by the member firm. The By-Laws further require that reportable events be reported accurately no later than 30 days after the member firm learns of the facts or circumstances giving rise to a reportable event. Filing a misleading Form U4 or U5, or failing to file a timely amendment to a Form U4 or U5 when required, violates the high standards of commercial honor and just and equitable principles of trade to which FINRA holds its members under NASD Rule 2110 and FINRA Rule 2010. *See Jason A. Craig*, Exchange Act Release No. 59137, 2008 SEC LEXIS 2844, at *8 (Dec. 22, 2008).

The Forms U4 are used by all self-regulatory organizations (including FINRA), state regulators, and broker-dealers to determine and monitor the fitness of securities professionals who seek initial or continued registration with a member firm. *See Rosario R. Ruggiero*, 52 S.E.C. 725, 728 (1996). The information on the Form U4 also is important to member firms, when evaluating whether to hire an employment applicant, and the investing public, who have access to certain disclosures on FINRA's BrokerCheck, when evaluating a broker. *See, e.g.*, *Richard A. Neaton*, Exchange Act Release No. 65598, 2011 SEC LEXIS 3719, at *17-18 (Oct. 20, 2011); *Scott Mathis*, Exchange Act Release No. 61120, 2009 SEC LEXIS 4376, at *29 (Dec. 7, 2009), *aff'd*, 671 F.3d 210, 211 (2d Cir. 2012). The Form U5 "serves as a warning mechanism to member firms of the potential risks and accompanying supervisory responsibilities they must assume if they decide to employ an individual with a suspect history." *Dep't of Enforcement v. McCrudden*, Complaint No. 2007008358101, 2010 FINRA Discip. LEXIS 25, at *20 (FINRA NAC Oct. 15, 2010). FINRA also uses the Form U5 when deciding whether to initiate investigations. *Id.* at *19.

The parties stipulated that Wedbush Securities committed 47 Form U4 violations and 26 Form U5 violations.[8] The Extended Hearing Panel found Wedbush Securities was liable for an additional 40 violations, comprised of 38 Form U4 violations and two Form U5 violations. Having independently reviewed the record, we summarily affirm and adopt as our own findings

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[8] The Extended Hearing Panel mistakenly found that the stipulated Form U4 violations totaled only 45 violations. We consider this discrepancy negligible, and it does not affect our overall findings with respect to liability or sanctions.

for purposes of any further review proceedings permitted under the federal securities laws, the Extended Hearing Panel's reasoning and findings concerning the 40 non-stipulated violations. Thus, we find that Wedbush Securities is liable for 113 reporting violations with respect to Forms U4 and U5.[9]

In sum, we find that Wedbush Securities violated NASD and FINRA By-Laws, NASD Rule 2110, and FINRA Rule 2010 by failing to file, late filing, and the filing of inaccurate Forms U4 and U5.

C. Wedbush Securities Failed to File, Late Filed, and Filed Inaccurate Statistical Reports Concerning Customer Complaints

The Extended Hearing Panel found that Wedbush Securities failed to file, late filed, and filed inaccurate statistical reports concerning customer complaints from July 2008 to July 2009 in violation of NYSE Rule 351(d), NASD Rule 3070(c), NASD Rule 2110, and FINRA Rule 2010. We affirm the Extended Hearing Panel's findings.

NYSE Rule 351(d) required NYSE members to file statistical information regarding customer complaints. The information was required to be filed by the 15th calendar day of the month following the quarter's end. *See NYSE Information Memo 03-39*, 2003 NYSE Info. Memo LEXIS 39, at *1 (Sept. 19, 2003). Similarly, NASD Rule 3070(c) required each member firm to file quarterly statistical and summary information with FINRA concerning customer complaints by the 15th day of the month following the calendar quarter in which customer complaints are received by the member. NASD Rule 3070(d) exempted members that were subject to NYSE Rule 351 from the requirements of NASD Rule 3070(c). "Customer complaints" were defined as "any written statement of a customer, or any person acting on behalf of a customer, other than a broker or dealer, alleging a grievance involving the activities of those persons under the control of a member firm."[10] *See FINRA Regulatory Notice 08-64*, 2008 FINRA LEXIS 57, at *13 (Oct. 2008). For convenience, we refer to the quarterly reports as Rule 3070 reports. The failure to file Rule 3070 reports promptly and accurately violates NASD Rule

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[9] While the Extended Hearing Panel's decision recites that it found an additional 39 violations, in actuality, the Extended Hearing Panel found Wedbush Securities was liable for an additional 40 violations, comprised of 38 Form U4 violations and two Form U5 violations. The alleged violations concerning the reporting of an arbitration against J. Rubenstein and Debbie Saleh establish five violations (i.e., three late Forms U4, one inaccurate Form U4, and one Form U5 that was never filed), not four violations, as recited in the decision.

[10] Previously NYSE Rule 351(d) applied to both oral and written complaints. Effective November 11, 2008, NYSE Rule 351(d) was amended to limit the definition of "customer complaint" to written statements, making the definition substantially similar to the definition of NASD Rule 3070(c). *See FINRA Regulatory Notice 08-64*, 2008 FINRA LEXIS 57, at *13 (Oct. 2008).

3070, NYSE Rule 351, NASD Rule 2110, and FINRA Rule 2010. *See Murphy*, 2013 SEC LEXIS 1933, at *26 n.29.

The parties stipulated that Wedbush Securities committed four violations by late filing certain Rule 3070 reports, but Respondents disputed the remaining allegations concerning five alleged violations. We review the five disputed violations below.

1. Customer Complaint Against Wedbush Securities Registered Representative RB

On March 18, 2009, customer TM faxed a letter to Wedbush Securities alleging that Wedbush Securities registered representative RB conducted unauthorized trades in his account. Despite receiving the customer complaint on March 18, 2009, the Firm did not report the complaint until January 15, 2010—275 days after the deadline. Respondents conceded that the complaint was not timely reported, but disputed their responsibility for the late reporting, asserting that the Firm office manager failed to forward the letter to the Business Conduct Department because he did not believe it constituted a customer complaint.[11]

The customer's letter, on its face, undoubtedly was a customer complaint. The office manager's failure does not excuse the late filing or the Firm's responsibility for the late filing. As Segall testified at the hearing, the manager was acting on behalf of the Firm, and the Firm is obligated under the rules to timely report customer complaints. Thus, like the Extended Hearing Panel, we find that this late Rule 3070 report is an additional violation of NASD Rule 3070(c) and NYSE Rule 351(d).

2. Customer Complaint Against Wedbush Securities Registered Representative BH

On June 30, 2008, customer BE hand-delivered a letter to Wedbush Securities registered representative BH with the subject line "My Displeasure," alleging poor investment choices and unsuitable investments in accounts for members of his family, some of which were trusts directed by BE. BE stated that he was moving all of his family's accounts to another firm. At the hearing, Segall admitted that the Firm never disclosed the June 30, 2008 complaint in accordance with the applicable rules.

Nearly a year later, on April 28, 2009, BE sent an e-mail to BH, complaining that a particular investment was unsuitable because of risk and withdrawal penalties, that other investments were generally unsuitable, and that BH failed to disclose material information.

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[11] According to Segall, the Firm emphasized at each annual compliance meeting and thereafter with this particular office manager that anything that resembles a customer complaint should be forwarded to the Business Conduct Department, so it could make the proper determination.

On July 15, 2009, the Firm filed a quarterly Rule 3070 report disclosing the April 28, 2009 complaint. Although the customer complaint was disclosed timely, the Rule 3070 report was inaccurate. The Rule 3070 report erroneously stated that the alleged misconduct took place between June 30, 2008 and April 28, 2009. It is clear, however, from the text of the two customer complaints that all of the activity of which BE complained occurred before June 30, 2008, at which time BE planned to transfer his accounts to another firm.[12] We, like the Extended Hearing Panel, reject Enforcement's contention that the Rule 3070 report is inaccurate because it reported the complaint date as April 28, 2009, instead of the earlier complaint date of June 30, 2008.

Thus, we find two additional violations of NASD Rule 3070(c) and NYSE Rule 351(d) for failing to file a Rule 3070 report to disclose the June 30, 2008 letter and filing an inaccurate Rule 3070 report concerning the April 28, 2009 letter.

3. Customer Complaint By Customer CN

On February 3, 2009, Mr. Wedbush received a handwritten letter from CN, a customer of the Firm, which was largely unintelligible, concerning various issues relating to her divorce and access to her money, and asserting several times that her ex-husband's accountant had no right to access her account. The Firm did not report the letter because it believed that CN was complaining about her ex-husband and his accountant, not Wedbush Securities. We agree with the Extended Hearing Panel that Enforcement did not establish that the letter was reportable because it is not clear that CN was complaining about how her registered representative handled her account. Thus, we do not find a violation for the failure to report the letter as a customer complaint.

* * * *

In sum, we find that Wedbush Securities violated NYSE Rule 351(d), NASD Rule 3070(c), NASD Rule 2110, and FINRA Rule 2010 by failing to file one customer complaint, late filing five customer complaints, and filing one customer complaint inaccurately, resulting in seven violations.[13]

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[12] It is also clear from the text of the April 28, 2009 email that it is not a complaint about BH's failure to respond to the June 30, 2008 letter, as contended by Respondents at the hearing.

[13] At the hearing below, Enforcement presented evidence of the industry average percentage of late Forms U4 and U5, noting that the Firm's late percentage exceeded the industry average and arguing that the Firm's violations were egregious for sanction purposes. On appeal, Respondents argue that Enforcement's failure to introduce evidence of the industry average percentage of late Forms RE-3 and Rule 3070 reports amounts to a failure of proof of liability for causes one and three because there is "no standard of liability." Respondents' argument fails. Enforcement does not need to prove that the Firm's reporting violations exceeded industry averages to prove liability. *See Ko Sec., Inc.*, 56 S.E.C. 1126, 1132 (2003) ("[T]he fact that a

[Footnote continued on next page]

D. Wedbush Securities and Mr. Wedbush Failed to Reasonably Supervise the Firm's Regulatory Filings

The Extended Hearing Panel found that Wedbush Securities failed to supervise the Firm's regulatory filings from January 2005 to July 2010, and that Mr. Wedbush failed to supervise the Firm's regulatory filings from August 2006 to July 2010, in violation of NASD Rule 3010, NASD Rule 2110, and FINRA Rule 2010. We affirm the Extended Hearing Panel's findings.

"Assuring proper supervision is a critical component of broker-dealer operations." *Richard F. Kresge*, Exchange Act Release No. 55988, 2007 SEC LEXIS 1407, at *27 (June 29, 2007). NASD Rule 3010 requires each member firm to establish and maintain a reasonably designed system, including written procedures, to supervise the activities of its registered representatives, principals, and associated persons and achieve compliance with the federal securities laws and FINRA rules. *See* NASD Rules 3010(a), (b)(1); *see also CapWest* , Exchange Act Release No. 71340, 2014 SEC LEXIS 205, at *33 (Jan. 17, 2014). "A supervisor is responsible for reasonable supervision, a standard that is determined based on the particular circumstances of each case." *Dep't of Enforcement v. Pellegrino*, Complaint No. C3B050012, 2008 FINRA Discip. LEXIS 10, at *46-47 (FINRA NAC Jan. 4, 2008), *aff'd*, Exchange Act Release No. 59125, 2008 SEC LEXIS 2843 (Dec. 19, 2008) (internal quotations and citations omitted). "To ensure compliance with this requirement, 'red flags and suggestions of irregularities demand inquiry as well as adequate follow-up and review. When indications of impropriety reach the attention of those in authority, they must act decisively to detect and prevent violations of the securities laws.'" *Midas Sec., LLC*, Exchange Act Release No. 66200, 2012 SEC LEXIS 199 (Jan. 20, 2012) (quoting *John B. Busacca III*, Exchange Act Release No. 63312, 2010 SEC LEXIS 3787, at *35 (Nov. 12, 2010)). "In large organizations, it is especially imperative that those in authority exercise particular vigilance when indications of irregularity reach their attention." *Wedbush Sec., Inc.*, 48 S.E.C. 963, 967 (1988).

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practice is common or widespread in an industry does not make such conduct proper or legal"); *Donald T. Sheldon*, 51 S.E.C. 59, 66 n.32 (1992), *aff'd*, 45 F.3d 1515 (11th Cir. 1995)*; Dep't of Enforcement v. Nouchi*, Complaint No. E102004083704, 2009 FINRA Discip. LEXIS 5, at *15 (FINRA NAC July 30, 2009) (citing *Charles E. Kautz*, 52 S.E.C. 730, 733 (1996)). Enforcement need only show that the Firm failed to file, untimely filed, or inaccurately filed regulatory reports in accordance with the relevant rules to prove a violation.

1. Mr. Wedbush Had Supervisory Authority Over the Firm's Regulatory Filings

As an initial matter, we find Mr. Wedbush had supervisory authority over the Firm's regulatory filings from August 2006 to July 2010. It is undisputed that Mr. Wedbush served as the Firm's president since the Firm's inception, including throughout the relevant period. It is also undisputed that Mr. Wedbush served as Business Conduct Manager from August 2006 to September 2007, CCO from August 2006 to July 2007, and co-CCO from July 2007 to October 2007. The Business Conduct Department, which oversaw the Firm's regulatory filings, reported directly to Mr. Wedbush from August 2006 to October 2007, and thereafter to Segall, who reported to Mr. Wedbush. As the president of Wedbush Securities, Mr. Wedbush "is responsible for the firm's compliance with all applicable requirements unless and until he . . . reasonably delegates a particular function to another person in the firm, and neither knows nor has reason to know that such person is not properly performing his . . . duties." *Kresge*, 2007 SEC LEXIS 1407, at *45.

Respondents argue that Mr. Wedbush had "no responsibility to personally make or directly supervise the filings at issue," and that he operated as a "manager rather than a supervisor" at the Firm.[14] As the president of Wedbush Securities, however, Mr. Wedbush ultimately was responsible.[15] Unless Mr. Wedbush reasonably delegated a particular compliance function to another person in the Firm, and neither knew nor had reason to know that proper supervision was not occurring, the existence of several levels of management between Mr. Wedbush and the person actually making the regulatory filings does not strip Mr. Wedbush of his supervisory obligation at the Firm. Regardless of any delegation, "[i]t is not sufficient for the

[14] The fact that Mr. Wedbush had other responsibilities managing the Firm does not make him any less liable for the Firm's regulatory reporting failures. *Cf. Busacca*, 2010 SEC LEXIS 3787, at *38 (finding the firm's president's focus on generating more clearing business contributed to president's failure to supervise); *Pellegrino*, 2008 SEC LEXIS 2843, at *39 (finding a securities principal's sales efforts exacerbated, rather than alleviated, the risk of additional noncompliance). Respondents' contention that the Firm's unchallenged written supervisory procedures provided that the Firm's president had little involvement in regulatory filings is equally unavailing. The Firm's written supervisory procedures do not need to elucidate Mr. Wedbush's specific responsibilities with respect to regulatory filings for us to conclude that he failed to reasonably supervise.

[15] Contrary to Respondents' assertion, Enforcement's failure to "introduce evidence on the responsibility of broker-dealer presidents for regulatory filings" was not fatal to its allegation that Mr. Wedbush failed to supervise. As recited earlier, established case law supports the legal proposition that broker-dealer presidents are responsible for their firm's compliance obligations unless reasonably delegated. *See, e.g.*, *Dep't of Enforcement v. Busacca*, *III,* Complaint No. E072005017201, 2009 FINRA Discip. LEXIS 38, at *18 (FINRA NAC Dec. 16, 2009), *aff'd*, 2010 SEC LEXIS 3787.

person with overarching supervisory responsibilities to delegate supervisory responsibility to a subordinate, even a capable one, and then simply wash his hands of the matter until a problem is brought to his attention. . . . Implicit is the additional duty to follow up and review that delegated authority to ensure that it is being properly exercised." *Kresge,* 2007 SEC LEXIS 1407, at *35-36.

Respondents do not argue that Mr. Wedbush, during the time he served as the Business Conduct Manager and CCO or co-CCO, ever delegated the task of supervising the filings at issue to anyone else. Indeed, Respondents admit on appeal that Mr. Wedbush did supervise, but not directly, individuals who were responsible for regulatory filings when he was CCO. Respondents also do not argue that Mr. Wedbush delegated the responsibility of supervising the filings at issue to Segall, when Segall became the Business Conduct Manager and co-CCO, or to Moy, when Moy became the co-CCO. We nonetheless considered whether Segall's assumption of the role of Business Conduct Manager and co-CCO or Moy's assumption of the role of co-CCO amounted to a delegation and reasonable supervision by Mr. Wedbush under the circumstances. We find that the numerous regulatory notifications and continued regulatory reporting violations after Segall and Moy joined the Firm provided Mr. Wedbush with ample notice that they were not properly performing their supervisory duties. Accordingly, Mr. Wedbush always retained supervisory responsibility over the Firm's regulatory reporting. *See Midas Sec., LLC*, 2012 SEC LEXIS 199, at *55.

2. Respondents Failed to Effectively and Reasonably Implement the Firm's Supervisory System

The adequacy of the Firm's supervisory system, including the Firm's written supervisory procedures, is not at issue in this case. As Enforcement alleged in the complaint and emphasized throughout the proceeding, it was not challenging the Firm's written supervisory procedures but instead the implementation of those procedures. The Firm adequately designed its supervisory system to ensure compliance with FINRA rules concerning regulatory reporting.[16] Respondents, however, failed to implement effectively the Firm's supervisory system. *See Rita H. Malm*, 52

[16] The Firm's written supervisory procedures, during the relevant period, required customer complaints to be forwarded immediately to the Business Conduct Department in accordance with NYSE Rule 351 and NASD Rule 3070. Specifically, the procedures required the division manager to report the event to the Business Conduct Department, and the Business Conduct Department to identify reportable complaints and other reportable events. The procedures provided that the Business Conduct Department was to complete Rule 3070 reports quarterly, Forms U4 and U5 promptly after receipt of complaint, and NYSE Forms RE-3 within 30 days after receipt of complaint. The procedures further provided that employees were required to notify the Business Conduct Department if they were subject to any event reportable on the Form U4, and the Business Conduct Department would determine if the information was reportable under NYSE Rule 351 or NASD Rule 3070 and on the employee's Form U4 or U5.

S.E.C. 64, 69 n.17 (1994) ("The presence of procedures alone is not enough. Without sufficient implementation, guidelines and strictures do not assure compliance.").

Evidence introduced at the hearing below established that Respondents did not act decisively to detect and prevent future regulatory reporting rule violations. During the relevant period, Wedbush Securities failed to properly report 80 disclosable events, resulting in 158 reporting violations. The regulatory reporting violations occurred for more than five years, during which Wedbush Securities and Mr. Wedbush received several notifications from regulators about regulatory reporting issues, including examination reports, examination exit meetings, an AWC, and two Wells Notices. Unlike some red flags that merely suggest that misconduct may be occurring, the regulators' notifications explicitly detailed the Firm's regulatory reporting failures and put the Firm and Mr. Wedbush on notice about their continued occurrence. Mr. Wedbush attended every examination exit meeting, signed the AWC, drafted the relevant portion of the Firm's response regarding filing deficiencies identified in the 2006 examination report, and signed the Firm's responses regarding filing deficiencies identified in the 2008 examination report.

Respondents attributed various reporting violations to a lack of experience and training among Business Conduct Department personnel, a lack of communication between the Business Conduct Department and the legal department, and the failure of Firm personnel outside the Business Conduct Department to get information or documents to the Business Conduct Department in a timely fashion. Even on appeal, Respondents seemingly contend that the failure of firm personnel outside the Business Conduct Department to get information or documents to the Business Conduct Department somehow insulates Respondents from liability or is otherwise mitigating.

Where employees are failing to abide by internal procedures concerning the firm's reporting obligations, however, a member firm is responsible for taking steps that are reasonably designed to achieve compliance, including providing meaningful training, following-up, and taking actions to remedy continued failures. A member firm and a responsible supervisor cannot be excused from their supervisory responsibility due to the failures of employees to abide by the Firm's written supervisory procedures. Indeed, final responsibility for proper supervision of a member's business rests with the member, and this supervision must be reasonable based on the particular facts of each case. *See* NASD Rule 3010(a); *see also Reynolds & Co.*, 39 S.E.C. 902, 917 (1960) ("The duty of supervision cannot be avoided by pointing to the difficulties involved where facilities are expanding or by placing the blame upon inexperienced personnel . . . . These factors only increase the necessity for vigorous effort.").

We, like the Extended Hearing Panel, find that the Firm's Business Conduct Department functioned without authority or influence to ensure compliance with regulatory reporting, while the supervisors and executives across the Firm took insufficient steps to ensure that regulatory reporting was completed timely and accurately. Neither the Firm nor Mr. Wedbush exerted their power and authority to compel the Firm's personnel to act or took responsibility to ensure compliance with the regulatory reporting rules. The Firm's relegation of the Business Conduct Department to an administrative role that lacked the experience, training, and ability to enforce the written supervisory procedures was unreasonable under the circumstances. Further, the fact

that associated persons, supervisors, and executives suffered no repercussions for failing to report reportable events to the Business Conduct Department also was unreasonable and created a culture of noncompliance concerning regulatory reporting that directly contributed to the 158 reporting violations.[17]

Respondents did not provide the Business Conduct Department with adequate supervision and guidance concerning reporting obligations. *See Kresge*, 2007 SEC LEXIS 1407, at *35 ("Members should determine that supervisors understand and can effectively conduct their requisite responsibilities."); *see also* NASD Rule 3010(a)(6) (stating that FINRA members must undertake "[r]easonable efforts to determine that all supervisory personnel are qualified by virtue of experience or training to carry out their assigned responsibilities"). For example, Respondents admitted that Eaton and Huang were unaware of filing requirements under NYSE Rule 351. Moreover, Huang had never previously worked at an NYSE firm and, despite being the manager of the compliance department at a large dual member firm, only passed the Series 14 examination months after accepting the position at the Firm. *Cf. Kresge*, 2007 SEC LEXIS 1407, at *31 (finding that the firm president did not make "reasonable efforts" to determine that a branch office manager, who only passed his principal examination six months earlier, was qualified). Despite having actual notice of the lack of leadership and experience in the Business Conduct Department, the Firm nonetheless thereafter installed Mr. Wedbush as the Business Conduct Manager and CCO at the Firm, notwithstanding his lack of appropriate licensing, lack of familiarity with compliance obligations, and admitted lack of dedication to day-to-day supervision.[18] Reporting violations continued even after Segall became the co-CCO.[19] The

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[17] On appeal, Respondents argue that the Extended Hearing Panel's conclusion that the Business Conduct Department functioned solely in an administrative capacity is an indictment of the Firm's written supervisory procedures, which were not challenged by Enforcement. We disagree and explicitly find the Firm did not effectively implement its procedures for the reasons stated herein.

[18] As president of the Firm and someone who attended every examination exit meeting, Mr. Wedbush undoubtedly was aware of the Firm's regulatory reporting issues prior to installing himself as the Business Conduct Manager in August 2006, which makes his appointment to Business Conduct Manager and CCO even more unreasonable under the circumstances. *Cf. Busacca*, 2010 SEC LEXIS 3787, at *41 ("His previous involvement underscores the unreasonableness of his supervision. He understood the severity of the operational problems when he became president, yet he failed to act promptly."); *Sec. Planners Assoc., Inc.*, 44 S.E.C. 738, 742 (1971) (finding firm president, who was "generally aware" of the firm's problems before accepting promotion to president, failed to "exercise reasonable supervision to prevent" violations that continued to occur after he became president).

[19] More than half the reporting violations occurred in 2008 or later, after Segall joined the Firm. Even if we were to conclude that Segall, unlike prior Business Conduct Managers, was highly qualified, based on the number of violations that occurred after he joined the Firm, we

[Footnote continued on next page]

sheer amount of violations alone under such leadership supports the conclusion that the Business Conduct Department's personnel was not qualified to carry out their compliance and reporting obligations.

3. Respondents' Corrective Measures Were Untimely and Insufficient to Address the Regulatory Reporting Failures

Respondents contend that the Firm and Mr. Wedbush implemented numerous initiatives to improve the supervision of the Firm's regulatory reporting, including additional training for the Business Conduct Department and legal department personnel, new management, and emphasis on regulatory reporting at the Firm's Saturday management committee meeting among executives led by Mr. Wedbush every other month. Considering that more than half of the Firm's violations occurred after Respondents' delayed efforts, we find that Respondents' corrective efforts lacked vigor and failed to address the inadequate implementation of the written supervisory procedures. *See Busacca,* 2010 SEC LEXIS 3787, at *38 ("Despite the presence of numerous red flags, Busacca failed to direct his prompt and full attention to remedying the Firm's operational breakdowns that arose and to preventing the occurrence of future problems."); *George J. Kolar*, 55 S.E.C. 1009, 1016 (2002) ("Decisive action is necessary whenever supervisors are made aware of suspicious circumstances, particularly those that have an obvious potential for violations."); *Robert Grady*, Exchange Act Release No. 41309, 1999 SEC LEXIS 768, at *7 (Apr. 19, 1999) ("Supervisors have an obligation to respond 'vigorously' and 'with the utmost vigilance' to 'any indication of irregularity.'").

When addressing the Respondents' measures to improve regulatory reporting, the Extended Hearing Panel stated, "It is too soon to know if these measures will be effective, and the evidence at the hearing was inconclusive." We disagree. We considered the individual supervisory steps that Respondents took as well as the cumulative effect of those supervisory efforts, and we find the evidence conclusively supports the finding that Respondents' efforts during the relevant period were ineffective, inadequate, and unreasonable under the circumstances. *Cf. Busacca*, 2010 SEC LEXIS 3787, at *44 (finding respondent's corrective measures, including holding weekly meetings, periodically checking on operations staff and requiring them to review firm procedures, and increasing staff, "were not reasonably designed to address the extensive operational dysfunction"); *Pellegrino*, 2008 FINRA Discip. LEXIS 10, at *53 (finding that respondent's supervisory steps, including training initiatives, staffing and recruitment changes, and amendments to procedures, were insufficient to address the problems at the firm).

[Cont'd]

find that Mr. Wedbush did not discharge his "additional duty to follow up and review that delegated authority to ensure [compliance with his regulatory requirements was] being properly exercised." *Kresge*, 2007 SEC LEXIS 1407, at *35-36 (citing *Malm*, 52 S.E.C. at 73).

Mr. Wedbush, as president, was apathetic about his commitment to resolving the compliance problems, admitting that he took no direct steps to address the reporting problems because he, as a manager as opposed to being a supervisor at the Firm, did not believe it was his responsibility. *See Robert E. Strong*, Exchange Act Release No. 57426, 2008 SEC LEXIS 467, at *29 (Mar. 4, 2008) ("[T]he evidence establishes that Strong's unreasonable inaction effectively nullified the supervisory system related to the Firm's compliance with Rule 2711."). Further, simply emphasizing regulatory reporting obligations and the importance of compliance does not amount to meaningful supervision. Other efforts, such as hiring a co-CCO in July 2007, a new co-CCO in October 2007, and providing additional training, were hardly prompt considering the numerous notifications from regulators that preceded such efforts.[20] And violations continued unabated even after Respondents undertook these corrective measures.

Eventual changes to the Firm's policies, including structural changes in 2010 to the Firm's organization to include business conduct personnel in each of the Firm's divisions, and any resulting regulatory reporting improvement, do not excuse the lack of supervision during the relevant period. *See Dep't of Enforcement v. CapWest Sec., Inc.*, Complaint No. 2007010158001, 2013 FINRA Discip. LEXIS 4, at *29 n.23 (FINRA NAC Feb. 25, 2013), *aff'd*, 2014 SEC LEXIS 205 ("Such after-the-fact efforts to improve CapWest's supervision of the firm's communications with the public, however, do not excuse its lack of supervision of these communications . . . ."); *Busacca*, 2010 SEC LEXIS 3787, at *43 ("Reasonable supervision . . . required Busacca . . . to address known deficiencies promptly . . . not only after regulatory action had commenced."); *Kresge*, 2007 SEC LEXIS 1407, at *37 ("Kresge's [remedial] actions occurred months after the misconduct at issue already had transpired and after [FINRA] began its investigation."); *Dep't of Enforcement v. Murphy*, Complaint No. 20005003610701, 2011 FINRA Discip. LEXIS 42, at *101 (FINRA NAC Oct. 20, 2011) (remedial measures taken by supervisor after violation has persisted for years, FINRA began its investigation, and action by state regulators was "far too late"), *aff'd*, 2013 SEC LEXIS 1933.

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In sum, the evidence established that Respondents failed to effectively and reasonably implement the Firm's supervisory system. Although the Firm had adequate supervisory procedures in place, Respondents did not effectively implement them, which allowed the Firm to commit 158 regulatory reporting violations over a five-year period. Under these circumstances, and given the Firm's continued reporting violations, Mr. Wedbush was obligated to ensure that the Firm had effective staffing and sufficient resources to resolve the Firm's reporting problems.

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[20] To the extent that Respondents are arguing that improvements led to the discovery of prior reportable items that were not filed or previously misfiled, thus skewing the numbers of violations in later years, the evidence belies such an assertion: filings that were due as of 2008 or later comprised more than 100 of the 158 violations.

See Pellegrino, 2008 SEC LEXIS 2843, at *55. He did not discharge this obligation.[21] Thus, we affirm the Extended Hearing Panel's findings that Wedbush Securities violated NASD Rule 3010, NASD Rule 2110, and FINRA Rule 2010, from January 2005 to July 2010, and Mr. Wedbush violated NASD Rule 3010, NASD Rule 2110, and FINRA Rule 2010, from August 2006 to July 2010, by failing to reasonably supervise the Firm's regulatory filings.

E. Respondents Received a Fair Hearing

Respondents contend the disciplinary process and hearing below was fundamentally unfair because Respondents were not notified that Mr. Wedbush could be suspended by the Hearing Panel and, if they had known about the possibility, they would have conducted their defense differently, including stipulating to fewer facts, calling additional witnesses, and presenting additional evidence in mitigation.

Section 15A(b)(8) of the Exchange Act provides that FINRA disciplinary proceedings must be conducted in accordance with fair procedures. *See Scott Epstein*, Exchange Act Release No. 59328, 2009 SEC LEXIS 217, at *51 (Jan. 30, 2009), *aff'd*, 416 F. App'x 412 (3d Cir. Nov. 23, 2010). Section 15A(h)(1) of the Exchange Act requires that FINRA, in a disciplinary proceeding, "bring specific charges, notify such member or person of and give him an opportunity to defend against, such charges, and keep a record." We find that the complaint, which requested any sanction under FINRA Rule 8310(a)[22] and explicitly charged Mr. Wedbush with a failure to supervise registration filings, provided Respondents with sufficient notice that Mr. Wedbush could be suspended. *See William C. Piontek*, 57 S.E.C. 79, 90-91 (2003) (finding that respondent who "'understood the issue[s]' and 'was afforded full opportunity' to litigate . . . had sufficient notice of the charges against him and opportunity to prepare and present his defense"); *Bison Sec., Inc.*, 51 S.E.C. 327, 334 (1993) (holding that Article V, Section 1 of NASD Rules, which was substantially similar to FINRA Rule 8310(a), "provides adequate notice of the possible sanctions a violator may face").

Moreover, the FINRA Sanction Guidelines ("Guidelines") advise adjudicators to consider, in the case of a failure to supervise, a suspension of the "responsible individual in all

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[21] Contrary to Respondents' arguments on appeal, FINRA and the Extended Hearing Panel are not obligated to specify what steps Mr. Wedbush should have taken to address the Firm's regulatory reporting problems. As the Commission has repeatedly stated, "a broker-dealer cannot shift its responsibility for compliance with applicable requirements to [regulators]." *Quest Capital Strategies, Inc.*, 55 S.E.C. 362, 377-78 (2001) (internal quotations omitted).

[22] FINRA Rule 8310(a) provides that, in any disciplinary proceeding, FINRA may impose one or more sanctions on a member or person associated with a member for each violation, including "(2) impose a fine upon a member or person associated with a member; (3) suspend the membership of a member or suspend the registration of a person associated with a member . . . or (7) impose any other fitting sanction."

supervisory capacities for up to 30 business days" or longer in egregious cases. *FINRA Sanction Guidelines*, 103 (2013), http://www.finra.org/web/groups/industry/@ip/@enf/@sg/documents/industry/p011038.pdf [hereinafter *Guidelines*]. FINRA makes the Guidelines publicly available "so that members, associated persons and their counsel may become more familiar with the types of disciplinary sanctions that may be applicable to various violations." *Id.* at 1.

Respondents assert that they devoted very little of their case to the issue of mitigation, and the entire case was about monetary mitigation, which is "vastly different" than mitigation as it applies to a suspension. As an initial matter, we disagree that a distinction exists; the objectives of sanctions in FINRA disciplinary proceedings are the same regardless of what type of sanction ultimately is imposed. *See id.* at 2-3. Further, contrary to Respondents' assertions, Respondents were not prevented from presenting evidence that would have established that a suspension was not warranted. Respondents, who were represented by counsel, fully participated in a nine-day hearing, calling nine witnesses and introducing 50 exhibits. Mr. Wedbush himself testified for three days. Respondents were not prevented from calling any of the 23 potential witnesses they identified. Instead, they made a conscious choice and elected not to call nine witnesses whom they now argue they would have called.[23] Respondents also willingly entered into the stipulations with Enforcement, by which they agreed that 61 disclosable events constituted 115 reporting violations. The fact that Respondents' choice of litigation strategy before the Extended Hearing Panel was unsuccessful does not render the proceeding below unfair.[24] *See Russo Sec., Inc.*, 55 S.E.C. 58, 78 (2001) ("Public policy considerations favor the expeditious disposition of litigation, and a respondent cannot be permitted to gamble on one course of action and, upon an unfavorable decision, to try another course of action.") (internal quotations omitted).

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[23] The Code of Procedure grants the Hearing Officer broad discretion to accept or reject evidence. *See Dep't of Enforcement v. Fiero*, Complaint No. CAF980002, 2002 NASD Discip. LEXIS 16, at *89 (NASD NAC Oct. 28, 2002). Among other things, the Hearing Officer may "exclude all evidence that is irrelevant, immaterial, unduly repetitious, or unduly prejudicial." NASD Rule 9263(a). The Hearing Officer denied Enforcement's motion to preclude testimony of certain witnesses, but nonetheless encouraged Respondents to limit the number of witnesses on the topics of "the Firm's reporting structure and supervision" and Mr. Wedbush's "work ethic and dedication to compliance." Nine of Respondents' witnesses appeared at the hearing, some of who testified as to Mr. Wedbush's work ethic and dedication to compliance. By now arguing on appeal that they would have "elicited significantly more testimony on the issue," Respondents seemingly concede that the additional testimony would have been cumulative and thus excludable by the Hearing Officer. We do not need to reach this issue. Regardless of whether the testimony would have been cumulative, we find no unfairness in the proceeding below.

[24] On appeal, Respondents noted that Enforcement presented evidence pertaining to "cherry picked" stipulated items for sanctions purposes over Respondents' objection, and Respondents had not prepared a defense to these items. We agree with the Extended Hearing Panel that the evidence was relevant for sanctions purposes and properly admitted.

In sum, we conclude that Respondents received a fair hearing in accordance with FINRA rules and the Exchange Act.

F. The Record Does Not Support a Claim for Selective Prosecution

On appeal, Respondents also note that Mr. Wedbush, who was the Business Conduct Manager for only 20 percent of the relevant period, was charged with a failure to supervise while no other Business Conduct Manager was charged. It is well established that FINRA has broad discretion to determine who should be charged with wrongdoing. *See, e.g.*, *Schellenbach v. SEC*, 989 F.2d 907, 912 (7th Cir. 1993) ("[FINRA] disciplinary proceedings are treated as an exercise of prosecutorial discretion."). The record also does not support a claim for selective prosecution. *See Epstein*, 2009 SEC LEXIS 217, at *53 ("To establish [a claim for selective prosecution], a petitioner must demonstrate that he was unfairly singled out for prosecution based on improper considerations such as race, religion, or the desire to prevent the exercise of a constitutionally protected right.").

V. Sanctions

The Extended Hearing Panel fined Wedbush Securities $300,000 and fined Mr. Wedbush $25,000 and suspended him from all supervisory activities, other than the supervision of trading and order entry, for 31 days. After an independent review of the record, we modify these sanctions.

A. The Firm's Failure to File, Late Filing, and Filing of Inaccurate Forms RE-3

The Extended Hearing Panel fined Wedbush Securities $75,000 for its violations of NYSE Rule 351(a) and NASD Rule 2110 with respect to Forms RE-3. We affirm this sanction.

There are no specific Guidelines for Form RE-3 filing violations, so we considered the most closely analogous Guidelines—i.e., the Guidelines for late filing, failing to file, and filing false, misleading, or inaccurate Forms U4 or U5 or amendments.[25] For late filing Forms U4 or U5 or amendments, the Guidelines recommend consideration of a fine of $5,000 to $50,000.[26] For failing to file, or for filing false, misleading, or inaccurate forms or amendments, the Guidelines recommend imposing a fine on the firm between $5,000 and $100,000.[27] In evaluating the appropriate sanctions to impose, the Guidelines provide three principal

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[25] *Guidelines*, at 1.

[26] *Id.* at 69-70.

[27] *Id*. at 70.

considerations specific to Form U4 and U5 violations, two of which are relevant here: the nature and significance of the information at issue and whether the misconduct resulted in harm to a registered person, another member firm, or any other person or entity.[28] These considerations are in addition to the principal considerations of the Guidelines applicable in every disciplinary case.[29]

The Form RE-3 was an important tool for regulators. Enforcement reviewed all Forms RE-3 it received and, where appropriate, conducted a preliminary investigation into the matter reported. *See NYSE Information Memo 2003-55*, 2003 NYSE Info. Memo LEXIS 56, at *1 (Dec. 16, 2003). "Reports of misconduct that [were] late (*i.e.,* submitted more than 30 days after a reportable event), unduly short, vague, or misleading, or that mischaracterize a matter . . . interfere[d] with the Exchange's ability to efficiently make informed decisions as to whether review of a reported matter [was] appropriate." *See NYSE Information Memo 2005-65*, 2005 NYSE Info. Memo LEXIS 67, at *4-5 (Sept. 14, 2005).

From January 2005 to July 2007, Wedbush Securities filed 33 Forms RE-3 late, filed two Forms RE-3 inaccurately, and failed to file three Forms RE-3.[30] Of the 33 late Forms RE-3, one Form RE-3 was nearly three years late. The late Forms RE-3 averaged 231 days late with a median of 86 days late. One inaccuracy involved the Firm incorrectly disclosing a $3.8 million settlement as a $1.4 settlement. The Firm's late, inaccurate, and never-filed Forms RE-3 prevented FINRA from efficiently identifying which reportable events deserved further scrutiny and following up on those events in a timely fashion. The Firm's Form RE-3 violations generally related to the failures to report arbitrations and litigation, and the arbitration awards and settlements ranged from $27,600 to $3.8 million. Such information is significant for regulators attempting to identify sales practice problems, potential fraudulent activity, and other violations of securities laws. The substantial number of violations, gross inaccuracy, extent of the lateness, and the complete failure to file three reports are aggravating factors supporting higher sanctions.

This was not the first time that the Firm was on notice that it failed to properly disclose customer complaints in compliance with NYSE Rule 351(a)(8) and (9). In response to a March 2002 examination report, the Firm represented it would "review its logging procedures to prevent repetitions or omissions." Four years later, in response to the December 2006 examination report providing that the Firm still was not in compliance with NYSE Rule 351(a), Mr. Wedbush represented that the managers of Business Conduct Department, Huang and his predecessor, Eaton, were unaware of the filing requirements under NYSE Rule 351(a). Although the misconduct was not intentional, Huang and Eaton's obliviousness with respect to the applicable

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28 *Id*. at 69.

29 *Id*. at 6-7.

30 *See Guidelines*, at 6-7 (Principal Considerations in Determining Sanctions, Nos. 8, 9, 16).

reporting rules was reckless.[31] The Firm's failure to take appropriate action and its subsequent repeated misconduct notwithstanding regulators' prior warnings are aggravating and demonstrate to us that strong sanctions are needed to deter future regulatory reporting failures at the Firm.[32] *Cf. Dep't of Enforcement v. Fox & Co. Inv., Inc.*, Complaint No. C3A030017, 2005 NASD Discip. LEXIS 5, at *45 (NASD NAC Feb. 24, 2005), *aff'd*, 58 S.E.C. 873 (2005) (finding that a stronger sanction for reporting failures was necessary to deter future misconduct where respondents previously committed the same rule violations).

Under these facts, a sanction toward the upper end of the range provided by the Guidelines strikes an appropriate balance between assessing sanctions that are commensurate with the Firm's misconduct and remediating the specific misconduct. It also serves the public interest by encouraging future compliance with regulatory reporting rules by the Firm and others in the securities industry. Thus, we affirm the sanctions imposed by the Extended Hearing Panel and fine Wedbush Securities $75,000 for failing to file, late filing, and filing of inaccurate Forms RE-3 in violation of violations of NYSE Rule 351(a) and NASD Rule 2110.

B. The Firm's Failure to File, Late Filing, and Filing of Inaccurate Forms U4 and U5

The Extended Hearing Panel fined Wedbush Securities $100,000 for its violations of NASD and FINRA By-Laws, NASD Rule 2110, and FINRA Rule 2010 with respect to Forms U4 and U5. We affirm this sanction.

As noted above, the Guidelines recommend consideration of a fine of $5,000 to $50,000 for late filing and a fine of $5,000 to $100,000 for failing to file, or for filing false, misleading, or inaccurate Forms U4 and U5. The same principal considerations specific to Form U4 and U5 violations—the nature and significance of the information at issue and whether the misconduct resulted in harm to a registered person, another member firm, or any other person or entity—are applicable here.

The Firm's violations are extensive.[33] From May 2005 to July 2010, Wedbush Securities filed 70 Forms U4 late, filed 11 Forms U4 inaccurately, and failed to file four Forms U4. The late Forms U4 ranged from one day to 2,007 days late, averaging 162 days late with a median of 34.5 days late.[34] In addition, from May 2005 to July 2010, Wedbush Securities filed 21 Forms

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[31] *See id.* (Principal Considerations in Determining Sanctions, Nos. 5, 6, 13). Ignorance of FINRA requirements is no excuse for violative behavior. *See Thomas C. Kocherhans*, 52 S.E.C. 528, 531 (1995).

[32] *See Guidelines*, at 7 (Principal Considerations in Determining Sanctions, No. 15).

[33] *See Guidelines*, at 6 (Principal Considerations in Determining Sanctions, Nos. 8, 9).

[34] 23 Forms U4 were less than 10 days late.

U5 late, filed four Forms U5 inaccurately, and failed to file three Forms U5. The late Forms U5 ranged from one to 457 days late, averaging 204 days late with a median of 183 days late. The high number of violations over an extended period of time, in spite of the numerous notices from regulators about regulatory reporting issues, demonstrate the Firm's lack of adequate training, educational initiatives, and general commitment to compliance with respect to Form U4 and U5 filings.[35]

The nature of the information also is highly significant. The Firm's reporting failures included substantial settlements with customers, FINRA and SEC Wells Notices, criminal matters, bankruptcies, customer complaints, and arbitration filings. Among other violations, the Firm failed to file Forms U4 and U5 for settlements, customer complaints, and civil litigation filings. Inaccuracies on Forms U4 and U5 included incorrect resolution dates, inaccurate disposition descriptions, an arbitration claim amount incorrect by more than $500,000, failing to name proper respondents, and naming improper respondents.

This information would not only be important to regulators, which may want to inquire into the details of each matter to determine whether disciplinary actions against the brokers or the Firm would be appropriate, but also to customers seeking information about the Firm and its brokers. *See Neaton*, 2011 SEC LEXIS 3719, at *17-18 ("The duty to provide accurate information and to amend the Form U4 to provide current information assures regulatory organizations, employers, and members of the public that they have all material, current information about the securities professional with whom they are dealing."). The failure to properly file Forms U4 and U5 harmed both FINRA and the investing public by depriving them of material information.[36] *See Dep't of Enforcement v. Knight*, Complaint No. C10020060, 2004 NASD Discip. LEXIS 5, at *13 (NASD NAC Apr. 27, 2004) ("Because of the importance that the industry places on full and accurate disclosure of information required by the Form U4, we presume that essentially all the information that is reportable on the Form U4 is material.").

The evidence established the Firm's rate for late Form U4 and U5 filings exceeded industry average for the relevant period:

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[35] *See id.* at 6-7 (Principal Considerations in Determining Sanctions, Nos. 6, 15, 16)

[36] On appeal, Respondents argued that "[n]o public customer was directly harmed" as a result of the regulatory filing violations, noting that Enforcement presented no evidence of any customer who took any action based on untimely regulatory filings. We disagree for the reasons stated herein. Regardless, the absence of customer harm is not mitigating. *See Edward S. Brokaw*, Exchange Act Release No. 70883, 2013 SEC LEXIS 3583, at *68 (Nov. 15, 2013).

Year	Industry Percentage of Form U4 and U5 Late Disclosure	Firm Percentage of Form U4 and U5 Late Disclosure[37]
2005	23%	42%
2006	22%	33%
2007	21%	42%
2008	19%	30%
2009	20%	35%
Jan. 2010-July 2010	21%	44%

We find the Firm's misconduct, which resulted in a failure rate substantially higher than the industry average, was reckless.[38]

Much of the Firm's misconduct occurred after it was on notice that it previously failed to properly file Forms U4 and U5 in accordance with the applicable rules. As we noted, on March 20, 2007, the Firm submitted an AWC, by which it accepted and consented to a $18,000 fine and censure for filing untimely 27 Forms U5 and failing to enforce its supervisory procedures with respect to Forms U5 from January 1, 2003 to August 3, 2005. Despite the AWC, the Firm continued to engage in repeated violations through 2010. Such recidivism is aggravating.[39] *See Midas Sec., LLC*, 2012 SEC LEXIS 199, at *67 ("Applicants' repeated misconduct underscores the egregiousness of their violations and demonstrates a conscious disregard for their regulatory obligations."). Considering that FINRA previously sanctioned the Firm for the same misconduct, it is obvious that the prior sanction did not provide substantial remediation, and a higher sanction is necessary to deter future regulatory reporting failures at the Firm.[40] *See Fox & Co. Inv., Inc.*, 2005 NASD Discip. LEXIS 5, at *45.

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[37] The percentage of Form U4 and U5 late disclosures was compiled using the FINRA Late Disclosure Fee Reports, by which FINRA tracks late filings for individual firms and industry wide and imposes a $300 fee on each firm for each late filing. In a few instances, a late fee is reversed by FINRA because of an error associated with the filing. To the extent that a late fee is reversed by FINRA after the three to four-week grace period, the late filing is not removed from the Late Disclosure Fee Report. As a result, the percentages are slightly higher than the actual percentage, but only marginally so because of the small amount of times that a fee is reversed after the grace period. We do not need to resolve these minor differences in the calculated averages to conclude that the Firm's failure rate exceeded the industry average during the relevant period.

[38] *See Guidelines*, at 7 (Principal Considerations in Determining Sanctions, No. 13).

[39] *See id.* at 6 (Principal Considerations in Determining Sanctions, No. 1).

[40] *See Guidelines*, at 7 (Principal Considerations in Determining Sanctions, No. 14).

On appeal, Respondents assert that the Firm's reporting rates "improved dramatically," noting that the Firm's Form U5 reporting improved from 27 late filings during the period 2003 to 2005, as noted in the AWC, to zero late filings in 2010. While it may be true that the Firm's reporting with respect to Forms U5 improved, the Firm continued to file Forms U4 late from January to July 2010. Regardless, we do not consider any improvement mitigating because it occurred only after numerous notices by regulators concerning regulatory problems, the commencement of the investigation underlying this disciplinary action, and the threat of disciplinary action.[41] For the same reason, we also do not find it mitigating that the percentage of Form U4 and U5 late disclosures improved to 18 percent for the period September 2010 to August 2011—after the relevant period—while the industry average was 21 percent for the same period.[42]

Based on the foregoing, and in particular the nature and extent of the violations and the prior AWC, we believe a strong sanction within the range provided by the Guidelines is necessary to deter future misconduct by the Firm and others from engaging in similar misconduct.[43] Thus, we affirm the sanctions imposed by the Extended Hearing Panel and fine Wedbush Securities $100,000 for failing to file, late filing, and filing of inaccurate Forms U4 and U5 in violation of NASD and FINRA By-Laws, NASD Rule 2110, and FINRA Rule 2010.

C. The Firm's Failure to File, Late Filing, and Filing of Inaccurate of Statistical Reports

The Extended Hearing Panel fined Wedbush Securities $25,000 for its violations of NYSE Rule 351(d), NASD Rule 3070, NASD Rule 2110, and FINRA Rule 2010 with respect to statistical reporting of customer complaints. We affirm this sanction.

For late reporting under NASD Rule 3070, the Guidelines recommend a fine of $5,000 to $50,000.[44] The principal considerations for late NASD Rule 3070 reporting are: the number and type of incidents not reported and whether the events reported in late reports established a pattern of potential misconduct.[45] For the failure to file or filing false, misleading, or inaccurate reports

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[41] *See Guidelines*, at 6 (Principal Considerations in Determining Sanctions, No. 3) (considering whether member firm voluntarily employed subsequent corrective measures *prior* to detection or intervention by a regulator, to revise general and/or specific procedures to avoid recurrence of misconduct).

[42] *See id.*

[43] *See id.* at 2 (General Principles Applicable to All Sanction Determinations, No. 1).

[44] *Id*. at 74.

[45] *Id.*

under NASD Rule 3070, the Guidelines recommend consideration of a fine of $5,000 to $100,000.[46] The principal considerations for never-filed and inaccurate NASD Rule 3070 reporting are whether the events not reported or reported inaccurately would have established a pattern of potential misconduct and the number and type of incidents not reported or reported inaccurately.[47]

The information reported by members pursuant to NASD Rule 3070 "provides [FINRA] with important regulatory information that assists with the timely identification of problem members, branch offices, and registered representatives to detect and investigate potential sales practice violations." *NASD Notice to Members 96-85*, 1996 NASD LEXIS 107, at *3 (Dec. 1996); *see also NASD Notice to Members 06-34*, 2006 NASD LEXIS 82, at *1 (July 2006) ("The information reported by members provides NASD with important regulatory information that assists with the timely identification of potential sales practice and operational problems."). Here, the complaints concerned, among other things, allegations of unauthorized trading and unsuitable investment strategies. Timely and accurate disclosure of such complaints would have provided FINRA with information to detect and investigate these serious sales practice allegations.

From July 2008 to July 2009, Wedbush Securities committed seven violations with respect to Rule 3070 reports, failing to file one customer complaint, failing to timely report five customer complaints, and also inaccurately reporting one of those customer complaints.[48] Although the number of violations was not large, the untimely Rule 3070 reports were very late—ranging from three months to one year and averaging 253 days overdue. The inaccuracy consisted of describing the allegation period inaccurately by 10 months. The majority of the complaints did not specify damages, but one complainant sought compensation in the amount of $156,000.

The six customer complaints were against six different representatives, all based on different allegations of misconduct, so the late Rule 3070 reports did not necessarily establish a pattern of potential misconduct. The June 30, 2008 complaint against registered representative BH, which the Firm failed to disclose, however, may have established a pattern of potential misconduct by BH. The Firm acknowledged that BH had received numerous complaints prior to joining the Firm, and the June 30, 2008 letter from customer BE explicitly provided that BE's previous email to her was "registered as a customer complaint." Thus, the June 30, 2008 letter should have been at least the second complaint by BE against BH, which could have elicited

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46 *Id.*

47 *Id.*

48 *See Guidelines*, at 6 (Principal Considerations in Determining Sanctions, Nos. 8, 9).

further investigation by regulators, particularly after receiving the third complaint against BH on April 28, 2009.

As with the other violations, we note that the Firm had been cautioned by regulators repeatedly about properly reporting customer complaints, but the Firm nonetheless failed to properly file these Rule 3070 reports. We find the Firm's conduct reckless and its failure to address the misconduct despite prior warnings from FINRA aggravating.[49]

Taking into consideration all the relevant facts, including the smaller number of violations and the possibility that the failure to disclose the BH complaint may have established a pattern of misconduct, we agree with the Extended Hearing Panel that a sanction within the mid-range provided by the Guidelines is appropriate. Thus, we affirm the sanctions imposed by the Extended Hearing Panel and fine Wedbush Securities $25,000 for failing to file, late filing, and filing of inaccurate statistical information in violation of NYSE Rule 351(d), NASD Rule 351(a), NASD Rule 2110, and FINRA Rule 2010.

D. The Firm's Failure to Supervise

The Extended Hearing Panel fined Wedbush Securities $100,000 for its failure to reasonably supervise the Firm's regulatory filings in violation of NASD Rule 3010, NASD Rule 2110, and FINRA Rule 2010. We affirm this sanction.

For a failure to supervise, the FINRA Sanction Guidelines recommend a fine of $5,000 to $50,000.[50] In evaluating the appropriate sanctions to impose, the Guidelines provide three principal considerations, two of which are relevant here: whether respondent ignored "red flag" warnings that should have resulted in additional supervisory scrutiny and the nature, extent, size and character of the underlying misconduct.[51] The Guidelines further instruct adjudicators to consider limiting activities of appropriate branch office or department for up to 30 business days, or longer in egregious cases.[52]

As discussed, the evidence establishes that the Firm's regulatory reporting violations were extensive and widespread. The violations occurred for more than five years, during which time Wedbush Securities received several notifications from regulators—including examination reports, examination exit meetings, an AWC, and two Wells Notices—that explicitly detailed the Firm's regulatory reporting failures. Despite the Firm's senior management repeatedly being

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[49] *See id.* at 7 (Principal Considerations in Determining Sanctions, Nos. 13, 15, 16).

[50] *Id*. at 103.

[51] *Id*.

[52] *Id*.

made aware of the regulatory reporting problems, the Firm continually failed to effectively address its supervision. As we discussed, the Firm failed to provide its personnel adequate leadership, training, and guidance, and, as a result, the Business Conduct Department personnel were unqualified to carry out their compliance and reporting obligations. The Firm's failure to address the underlying misconduct in spite of repeated notifications is highly aggravating.

At the hearing, Respondents testified concerning a number of corrective actions that the Firm undertook to address the issues. But the Firm undertook these corrective actions only after being notified by regulators about the Firm's reporting failures and commencement of the underlying investigation, which is not mitigating for sanctions purposes.[53] Further, as we explained, the evidence conclusively supports the finding that Respondents' corrective efforts were ineffective, inadequate, and unreasonable under the circumstances. Therefore, we give no mitigation for the Firm's corrective actions.

We considered the Firm's extensive disciplinary history with respect to supervision failures. In the past 10 years alone, the Firm has been fined approximately $2,000,000 by FINRA, NASD, and NASDAQ in 16 separate disciplinary actions and settlements involving supervision failures.[54] The Firm's disciplinary history coupled with its failure to remedy regulatory reporting problems despite repeated warnings from regulators present a significant aggravating factor in our determination of sanctions.[55] *See Gregory O. Trautman*, Exchange Act Release No. 61167, 2009 SEC LEXIS 4173, at *79 n.85 (Dec. 15, 2009) (considering orders in both settled and litigated proceedings for sanctions purposes).

The Extended Hearing Panel found that the Firm's failure to supervise its regulatory reporting was egregious. We agree. In egregious cases, the Guidelines advise adjudicators to consider suspending the firm with respect to any or all activities or functions for up to 30

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[53] *See Guidelines*, at 6 (Principal Considerations in Determining Sanctions, No. 3).

[54] For example, in April 2007, NYSE, finding that the Firm's responses to requests for Blue Sheet information were "inadequate, inept, dilatory and systematically deficient," censured the Firm, fined it $200,000, and required it to retain a legal and compliance consultant to evaluate its "Blue Sheet" reporting failures and make recommendation concerning the adequacy of its regulatory and compliance resources. In January 2009, NYSE imposed a censure, fined the Firm $100,000, and required the Firm to hire a consultant to assess the Firm's regulatory and compliance resources for a variety of failures relating to the Firm's Paris branch office, as well as weaknesses in the Firm's anti-money laundering program and failure to maintain adequate funds in the Firm's reserve account. The NYSE Hearing Panel found that "the underlying factor or cause of the violations at issue was the Firm's understaffed legal and compliance departments."

[55] *See id.* at 6 (Principal Considerations in Determining Sanctions, No. 2).

business days, or, in a case against a member firm involving systemic supervision failures, imposing a longer suspension or expelling the firm.[56] Although we explicitly find that the Firm's misconduct was egregious, we decline to impose a suspension on the Firm. Instead of a suspension, we agree with the Extended Hearing Panel that a fine of $100,000—outside the recommended range—better serves to remediate the misconduct and prevent its reoccurrence.

On appeal, Respondents argue that the misconduct underlying a failure to supervise must be egregious to find that the failure to supervise is egregious. This argument is without merit. *Cf. Busacca III*, 2009 FINRA Discip. LEXIS 38, at*43-47 (rejecting argument that underlying violations were "merely technical" and finding president's failure to exercise reasonable supervision over his firm's back-office operations egregious). The regulatory reporting rules exist to protect the investing public, and compliance and adherence to them, along with the supervision thereof, is of the utmost importance. Moreover, Respondents' arguments ignore that the egregiousness of the Firm's conduct is also based on its recidivist nature.

In sum, under the facts in this case, and taking into consideration the numerous and highly aggravating factors, we believe the Firm's egregious misconduct warrants the imposition of a sanction outside the recommended range to deter future misconduct by the Firm, deter others from engaging in similar misconduct, improve supervision of regulatory reporting in the industry, and protect the investing public. Accordingly, we affirm the sanctions imposed by the Extended Hearing Panel and fine Wedbush Securities $100,000 for failing to reasonably supervise regulatory filings in violation of NASD Rule 3010, NASD Rule 2110, and FINRA Rule 2010.

E. Mr. Wedbush's Failure to Supervise

The Extended Hearing Panel fined Mr. Wedbush $25,000 and suspended him from all supervisory activities, other than the supervision of trading and order entry, for 31 days for his failure to reasonably supervise the Firm's regulatory filings in violation of NASD Rule 3010, NASD Rule 2110, and FINRA Rule 2010. We modify this sanction.

As noted above, the Guidelines recommend imposing on a responsible individual a fine of $5,000 to $50,000 for the failure to supervise.[57] In addition to the other two principal considerations applicable to a failure to supervise, the Guidelines provide an additional principal consideration relevant here: the quality and degree of the supervisor's implementation of the firm's supervisory procedures and controls. The Guidelines also instruct the adjudicator to consider independent monetary sanctions for the firm and responsible individuals (i.e., not joint and several) and to consider suspending the responsible individual in all supervisory capacities

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[56] *See Guidelines*, at 103.

[57] *Guidelines*, at 103.

for up to 30 business days. In egregious cases, the Guidelines advise adjudicators to consider imposing a longer suspension in all capacities or barring the responsible individual.

As we discussed, the Firm's regulatory reporting violations were extensive and widespread. In addition to serving as the Firm's president throughout the relevant period, Mr. Wedbush served as the Business Conduct Manager from August 2006 to September 2007, CCO from August 2006 to July 2007, and co-CCO from July 2007 to October 2007. Thirty of the 158 violations occurred while Mr. Wedbush was serving as the Business Conduct Manager and supervising the Business Conduct Department directly. An additional 91 violations occurred thereafter when Segall joined the Firm and reported directly to Mr. Wedbush.

The evidence conclusively established that Mr. Wedbush was aware of the regulatory reporting issues at the Firm. Mr. Wedbush attended every examination exit meeting, signed the AWC concerning the 27 Form U5 failures, drafted the relevant portion of the Firm's response regarding filing deficiencies identified in the 2006 examination report, and signed the Firm's responses regarding filing deficiencies identified in the 2008 examination report.[58] Despite being aware of the regulatory reporting problems, Mr. Wedbush failed to act decisively and reasonably to address the issues. Respondents argue that the Firm's regulatory reporting improved dramatically, and that Mr. Wedbush is responsible for that improvement. We disagree with the underlying premise, and find there was not any meaningful improvement during the relevant period for the reasons we discussed. While the evidence establishes that Mr. Wedbush made some efforts, including emphasizing the importance of regulatory reporting at executive meetings, it also establishes these efforts were delayed and ineffective at addressing the widespread regulatory reporting problems.[59]

Respondents argue that Mr. Wedbush undertook the role as Business Conduct Manager and CCO to investigate the problems in the Business Conduct Department so he could better address the regulatory reporting problems, "not to directly supervise [Form] U4 and U5 filings." But if Mr. Wedbush was not supervising regulatory filings during that time, it begs the question who was. Despite being aware of existing regulatory reporting problems and knowing his general apathy toward compliance supervision, Mr. Wedbush nonetheless thought it was appropriate to install himself as Business Conduct Manager for more than a year. Then, instead of dedicating himself to supervising the Business Conduct Department and resolving the regulatory reporting problems at the Firm, he worked less than 10 hours a week in the Department, and, to this day, contends that he was not responsible for supervision of regulatory reporting at the time. Mr. Wedbush could not shed his supervisory responsibilities, however, by ignoring them.

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[58] *Id.* at 7 (Principal Considerations in Determining Sanctions, No. 15).

[59] *Id.* at 6 (Principal Considerations in Determining Sanctions, No. 2).

We agree with Respondents that Mr. Wedbush's acts were not motivated by fraud or intentional malfeasance. We find, however, that his conduct was reckless,[60] and the quality of Mr. Wedbush's implementation of the firm's supervisory procedures and controls was severely lacking.[61] Mr. Wedbush's own testimony and conduct demonstrate the frivolousness with which he approaches supervisory and regulatory reporting obligations at the Firm. In fact, Mr. Wedbush did not even ensure that his own Form U4 was amended in a compliant manner:

- On October 2, 2007, the Firm filed an untimely and inaccurate amended Form U4 for Mr. Wedbush reporting that a previously-disclosed matter pending in California federal court was "dismissed" on March 15, 1999, and providing that "[t]he matter was resolved is [sic] a court trial including the 9th Circuit appeal court and Mr. W was found not guilty." We agree with the Hearing Panel that the Firm was liable for four Form U4 violations with respect to this Form U4 amendment: the amendment was filed 2,007 days after the deadline; the resolution date was March 5, 2002, not March 15, 1999; the resolution detail should have provided that the matter was "other" rather than "dismissed;" and the disposition detail was inaccurate because there never was a finding that Mr. Wedbush was not liable.[62]

- The Firm also filed 29 days late the amendment to Mr. Wedbush's Form U4 disclosing the second Wells Notice in this case. In the second Wells Notice, FINRA staff advised Segall, among other things, that FINRA staff made a preliminary determination to recommend disciplinary action be brought against Mr. Wedbush for his failure to supervise. Notwithstanding that the Notice explicitly explained that it triggered an obligation to update his Form U4 and that Segall told Mr. Wedbush that he had to update his Form U4, Mr. Wedbush refused to do so. Mr. Wedbush responded to the Wells Notice, stating he was the "[m]anager of the business conduct department for a brief period of time so that [he] could assess the need of resources for business conduct responsibilities going forward," and asked for an explanation of the need to update his Form U4. He later asserted that disclosing the Wells Notice on his Form U4 would harm his reputation. Mr. Wedbush's letters to Enforcement asking for an explanation about

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60 *Id.* at 7 (Principal Considerations in Determining Sanctions, No. 13).

61 *Id.* at 103.

62 These four violations are encompassed in our findings concerning the Firm's 113 violations with respect to Forms U4 and U5. Respondents disputed these violations at the hearing below.

the need to update his Form U4 did not stay the filing requirement for disclosing the Wells Notice.[63]

We consider each instance aggravating by itself, and that aggravation is compounded by the multiple failures.[64] Further, the fact that Mr. Wedbush initially refused to file an amendment to his Form U4 disclosing the second Wells Notice shows a troubling disregard for the regulatory reporting rules, even after serving as the Business Conduct Manager and CCO, and a lack of respect for regulatory reporting rules.[65]

Respondents' attempt to blame others for the regulatory reporting failures does not shield Mr. Wedbush from liability or provide any mitigating value for sanctions purposes. Notwithstanding the conduct of registered representatives, branch managers, and other personnel both in and outside the Business Conduct Department who failed, on their part, to give the Business Conduct Department the proper information or failed to properly file the forms in accordance with the rules, Mr. Wedbush himself is responsible for serious supervisory lapses. *Cf. Wedbush Sec., Inc.*, 48 S.E.C. at 972 (dismissing the Firm's argument for reduced sanctions because the supervisory deficiencies were the immediate responsibility of a branch manager).

Respondents note that Huang, a Business Conduct Manager at the Firm for approximately one year, was issued a letter of caution for his failure to file 12 Forms RE-3 and no other sanction was imposed. And other than Huang, no other CCO was charged or disciplined. Respondents also argue that Mr. Wedbush's sanction was excessive and improper when compared to two settled cases, in which large broker-dealers paid hefty fines for even larger numbers of reporting violations but in which no individual, and in particular no president, was charged with a failure to supervise. It is well established that Enforcement has broad prosecutorial discretion when deciding who and what violation to charge. *See, e.g.*, *Nicholas T. Avello*, 55 S.E.C. 1197, 1209 (2002) (holding NASD has wide discretion in deciding against whom to proceed), *aff'd*, 454 F.3d 619 (7th Cir. 2006); *Schellenbach*, 989 F.2d at 912 (same). It

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63 This additional violation is encompassed in our findings concerning the Firm's 113 violations with respect to Forms U4 and U5. Respondents disputed the violation, but Segall conceded the filing was late at the hearing below.

64 At the hearing below, Enforcement introduced evidence over Respondents' objection about an additional failure by the Firm to update Mr. Wedbush's Form U4 to disclose a judgment lien against Mr. Wedbush and his wife during the pendency of an appeal. Enforcement discovered the failure only weeks before the hearing and did not allege the failure as an additional Form U4 violation by the Firm, but sought to introduce the evidence for sanction purposes. Based upon our findings that the Firm failed to properly file Form U4 amendments in two other instances, we need not consider this additional evidence when assessing the appropriate sanction.

65 *See id.* at 6-7 (Principal Considerations in Determining Sanctions, Nos. 2, 8, 9, 16).

is also well established that "the appropriateness of the sanctions imposed depends on the facts and circumstances of the particular case and cannot be determined precisely by comparison with action taken in other cases." *Dennis S. Kaminski*, Exchange Act Release No. 65347, 2011 SEC LEXIS 3225, at *41 (Sept. 16, 2011). Furthermore, "comparisons to sanctions in settled cases are inappropriate because pragmatic considerations justify the acceptance of lesser sanctions in negotiating a settlement such as the avoidance of time-and-manpower-consuming adversary proceedings." *Kent M. Houston*, Exchange Act Release No. 71589, 2014 SEC LEXIS 614, at *33 (Feb. 20, 2014) (internal quotations omitted).

Respondents' claim of bias is unsupported by the record. *Cf. Epstein*, 2009 SEC LEXIS 217, at *62 (finding no evidence of Hearing Panel bias and holding that adverse rulings generally do not demonstrate improper bias). We see nothing in the record to support Respondents' assertion that Huang received a lighter sanction because he was a former NASD employee. We likewise are not troubled that a FINRA witness at the hearing below who supervised regulatory filings at one of the broker-dealers that settled with FINRA was never charged. Regardless, our de novo review of this matter would cure any prejudice if any had existed. *See Dep't of Enforcement v. Gallagher*, Complaint No. 2008011701203, 2012 FINRA Discip. LEXIS 61, at *37 (Dec. 12, 2012) (holding that the NAC's de novo review cures alleged Hearing Panel prejudice).

Contrary to Respondents' assertions, suspensions imposed on firm presidents for a failure to reasonably supervise effectively are not unprecedented. *Cf. Busacca III*, 2009 FINRA Discip. LEXIS 38, at*44-46 (imposing a $25,000 and six-month suspension on the firm president for his failure to reasonably supervise back-office operations after a software conversion caused operational breakdowns). The fact that Enforcement did not advocate or request a suspension does not bind the Extended Hearing Panel, which is free to impose any sanction it sees fit.[66] *Cf. Caruselle v. New York Mercantile Exch.*, 2005 CFTC LEXIS 64, at *8-9 (June 21, 2005) (NYMEX did not err in imposing lengthier sanction than that recommended by compliance counsel). As the Guidelines make clear, adjudicators have broad discretion when assessing sanctions.[67]

After a thorough and independent review of the record, we find a 31-day suspension in all principal capacities and a $50,000 fine represent sanctions best tailored to remediate the totality

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[66] Other than the complaint's request for any sanction under FINRA Rule 8310(a), it is undisputed that Enforcement did not recommend imposing a suspension on either respondent throughout the proceeding below.

[67] *See Guidelines*, at 2. The NAC also has broad discretion, and "may affirm, modify, reverse, increase, or reduce any sanction, or impose any other fitting sanction" in its de novo review. *See* FINRA Rule 9348.

of the misconduct at issue.[68] We agree with the Extended Hearing Panel that Mr. Wedbush's misconduct is serious and warrants a suspension and a fine. Unlike the Extended Hearing Panel, however, we believe Mr. Wedbush should be suspended in all principal capacities because his misconduct demonstrates a troubling disregard for supervision in general, so a carve out for the supervision of trading and order entry activities is not warranted. A suspension in all supervisory capacities is appropriately tailored to fit Mr. Wedbush's misconduct and his refusal to acknowledge his supervisory responsibility as president of the Firm. It also is consistent with the Guidelines.[69] We also increase the fine to $50,000, which is the highest fine within the range suggested by the Guidelines.

We believe these sanctions will deter Mr. Wedbush and similarly situated individuals from effectively abdicating their obligation to exercise reasonable supervision and will encourage Mr. Wedbush and others to respond vigorously to known issues. *See Busacca*, 2010 SEC LEXIS 3787, at *67. The regulatory reporting rules exist to protect the investing public and provide meaningful and significant information to regulators, broker-dealers, and the investing public itself to further that goal. We are imposing these sanctions, including the suspension, for the purposes provided in the Guidelines, including for the purpose of protecting investors. *See Howard F. Rubin*, 52 S.E.C. 126, 126-27 (1994) ("When we suspend or bar a person, it is to protect the public from future harm at his or her hands."); *Dep't of Enforcement v. Kresge*, Complaint No. CMS030182, 2008 FINRA Discip. LEXIS 46, at *36 n.32 (FINRA NAC Oct. 9, 2008) ("Whether a sanction is punitive or remedial . . . depends on the facts or circumstances of the case."). Thus, taking into consideration the numerous and highly aggravating factors, we impose on Mr. Wedbush a 31-day suspension in all principal capacities and a $50,000 fine for his failure to reasonably supervise regulatory filings in violation of NASD Rule 3010, NASD Rule 2110, and FINRA Rule 2010.

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[68] *See Guidelines*, at 3 (General Principles Applicable to All Sanctions Determinations, No. 3).

[69] *See id*. at 103.

VI. Conclusion

Wedbush Securities failed to file, late filed, and filed inaccurate Forms RE-3, in violation of NYSE Rule 351(a) and NASD Rule 2110; failed to file, late filed, and filed inaccurate Forms U4 and U5, in violation of NASD and FINRA By-Laws, NASD Rule 2110, and FINRA Rule 2010; failed to file, late filed, and filed inaccurate statistical reports concerning customer complaints in violation of NYSE Rule 351(d), NASD Rule 3070(c), NASD Rule 2110, and FINRA Rule 2010; and failed to reasonably supervise regulatory filings, in violation of NASD Rule 3010, NASD Rule 2110, and FINRA Rule 2010. Mr. Wedbush also failed to reasonably supervise regulatory filings, in violation of NASD Rule 2010, NASD Rule 2110, and FINRA Rule 2010. For this misconduct, we impose on Wedbush Securities a $300,000 fine, and we impose on Mr. Wedbush a 31-day suspension in all principal capacities and a $50,000 fine. We also affirm the Extended Hearing Panel's imposition of hearing costs in the amount of $14,930.95 and order that Respondents pay appeal costs in the amount of $1,591.78.[70]

On Behalf of the National Adjudicatory Council,

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Marcia E. Asquith,
Senior Vice President and Corporate Secretary

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[70] Respondents are jointly and severally responsible for costs. Pursuant to FINRA Rule 8320, the registration of any person associated with a member who fails to pay any fine, costs, or other monetary sanction imposed in this decision, after seven days' notice in writing, will summarily be revoked for non-payment.