

**NASD
OFFICE OF HEARING OFFICERS**

DEPARTMENT OF ENFORCEMENT,

Complainant,

**Disciplinary Proceeding
No. 2005000226001**

v.

Hearing Officer: RH

**David L. McFadden,
General Securities Principal and General
Securities Representative
[CRD No. 2040961]**

**ORDER ACCEPTING
OFFER OF SETTLEMENT**

Date: November 15, 2006

Respondent.

INTRODUCTION

Disciplinary Proceeding No. 2005000226001 was filed on September 14, 2006, by the Department of Enforcement of NASD ("Complainant"). Respondent David L. McFadden submitted an Offer of Settlement ("Offer") to Complainant on November 9, 2006. Pursuant to Code of Procedure Rule 9270(e), the Complainant and the National Adjudicatory Council ("NAC") Review Subcommittee or the Office of Disciplinary Affairs ("ODA") have accepted the uncontested Offer. Accordingly, this Order now is issued pursuant to Code of Procedure Rule 9270(e)(3). The findings, conclusions and sanctions set forth in this Order are those stated in the Offer as accepted by the Complainant and approved by the NAC.

Under the terms of the Offer, Respondent has consented for the purpose of this proceeding only, without admitting or denying the allegations of the Complaint, and solely for the purposes of this

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proceeding and any other proceeding in which NASD is a party, to the entry of findings of facts and violations consistent with the allegations of the Complaint, and to the imposition of the sanctions set forth below, and fully understands that this Order will become part of Respondent's permanent disciplinary record and may be considered in any future actions brought by NASD.

FINDINGS AND CONCLUSIONS

It has been determined that the Offer be accepted and that findings be made as follows:

BACKGROUND

- 1 David L. McFadden entered the securities industry on April 10, 1990 as an Investment Company and Variable Contracts Products Representative of PFS Investments Inc., a member of NASD. David L. McFadden, during all periods mentioned herein, was associated with member firm Securities America, Inc. until his termination on August 31, 2006. McFadden was registered with NASD under Article V of the By-Laws as a General Securities Principal and General Securities Representative. McFadden is not currently associated with a member firm. Although McFadden is not currently registered, he remains subject to the jurisdiction of NASD until August 30, 2008, pursuant to Article V, Section 4 of NASD's ByLaws, which provides for a two-year period of retained jurisdiction over formerly registered persons.

2. Over the course of several years, from 1997 to 2003, McFadden engaged in a course of material misrepresentations and omissions, communicated to a target audience through a variety of media, recommending that the customers withdraw the cash value of their company-sponsored retirement plan to pursue investments styled as a Program of "Managed Money" in Securities America accounts with McFadden. In so doing, he violated the federal anti-fraud rules as well as the rules of the Association.
3. McFadden's target audience consisted of long-term employees of Exxon Corporation, generally between the ages of 50 and 60, who held company sponsored retirement accounts or defined benefit (401K) plans.
4. Through a website operated by McFadden (www.dfsbatonrouge.com) he touted his accounting skills and held himself and an employee out as licensed CPAs although neither was properly licensed in the state.
5. In seminars McFadden conducted, he told the attendees that through his Program, they could retire from their jobs as early as age 55, withdraw the cash value of their company-sponsored retirement accounts (including 401(k) plan and defined benefit plan accounts), deposit the funds in accounts with Securities America managed by McFadden, and by following his investment strategy, would earn them more than they were making by working.
6. McFadden assured the attendees that their salary income could be replaced with systematic monthly withdrawals from their retirement accounts. McFadden also

proposed withdrawals under the provisions of Section 72(t) of the Internal Revenue Code, which allows for withdrawals from qualified retirement plans by persons under the age of 59 ½ without the ordinary ten-percent penalty. Such withdrawals generally must be taken as "substantially equal periodic payments" that must last for five years or until the individual reaches age 59 ½, whichever is longer. The amount of the payments must be calculated according to one of three methods, two of which result in amounts that are fixed for the term of the withdrawals.

7. Seminar materials included a slide showing projections of account values over 20 years at rates of return ranging from 5 percent to 18 percent for a hypothetical customer, "Eddie Exxon," having retirement savings of \$600,000 who made annual withdrawals starting at \$58,000 per year (9.67 percent of the initial balance) after one year. Withdrawals were also shown as increasing by \$6,000 every five years. The slide depicted the investment compounding steadily over time and included no explanation that investments offering the potential for higher rates of return also involve a higher degree of risk to principal.
8. A seminar attendee who expressed interest met individually with McFadden to discuss the application of the program to his or her particular financial situation and objectives. The purpose of the meeting was to determine whether, according to McFadden's calculations, the individual had sufficient retirement funds to stop working and replace salary payments with periodic payments from retirement fund accounts.

9. McFadden represented to these customers that he had sufficient expertise to manage their accounts through variable annuity subaccount switches or mutual fund exchanges, in order to achieve rates of return necessary to permanently sustain the withdrawal amounts at the original levels. He provided customers with individual "Savings Projection of Annual Investment" documents illustrating the performance of a customer's hypothetical retirement portfolio over 33 years with at rates of return ranging from 4 percent to 14 percent and annual withdrawals generally starting at between 7.5 percent and 9 percent of the customer's initial investment with increases at five-year intervals. Most illustrations showed customers running out of money prior to the end of the 33-year period at rates of return less than 11 percent. McFadden referred to his own Program as "Managed Money" for which he illustrated returns of 11 percent to 14 percent—rates that would generally sustain the annual withdrawals over the entire 33-year period. McFadden omitted to disclose to customers the material information that the yield of investment securities would fluctuate with changes in market conditions and that the overall return to the customer investing through a variable annuity would be reduced by various charges, including the mortality and expense risk charge associated with variable annuities.
10. McFadden made the Section 72(t) calculations for the customers and typically recommended withdrawal amounts of between 7.5 percent and 9 percent per year of the individual's total retirement funds at the beginning of the program.

11. As the investment vehicles for his program, McFadden recommended and sold variable annuities, Class B or C mutual fund shares or exchange-traded funds (ETFs). Most of the customers who opted to follow the program entrusted McFadden with the entire cash proceeds of their company-sponsored retirement accounts, and thus forfeited their right to receive a lifetime monthly benefit under the defined benefit plan.
12. As account values declined due to withdrawals and market losses, McFadden continued to represent that withdrawals that now required rates of return ranging from 11.5 percent to 18 percent might be sustainable. In an effort to achieve these returns, McFadden engaged in discretionary, and in some cases unauthorized, subaccount exchanges and mutual fund switches, employing a speculative market-timing strategy.
13. Customers following McFadden's program could not maintain the recommended withdrawal amounts without depleting their retirement accounts to levels that threatened their livelihoods. For example, customer AP deposited cash and securities with McFadden valued at \$414,985.14 on October 2, 1997. He closed his account with McFadden around October 1, 2003, having an account balance at that time of \$77,146.72 after withdrawing about \$3,000 per month for living expenses on Mc Fadden's recommendation.
14. Relying on McFadden's investment advice and recommendation, the 29 customers at issue in this Complaint deposited cash and securities in accounts under his "Managed Money" Program totaling \$19,148,850.24 for the purchase of variable annuities and

mutual funds for their retirement programs. These customers had \$6,186,713.36 in their accounts at the time they stopped doing business with McFadden, after having taken regular withdrawals from their accounts totaling \$7,390,988.39.

FIRST CAUSE OF ACTION

Fraudulent and Unsuitable Sales of Securities, Against Respondent McFadden

15. The Department realleges and incorporates by reference paragraphs 1 through 14 above.
16. In connection with the sales of variable annuities set forth in Exhibit A hereto, with the mutual fund and ETF transactions set forth in Exhibit B hereto, and with the variable annuity subaccount exchange transactions set forth in Exhibit C hereto, McFadden knowingly or recklessly made misstatements and omissions of material facts as described in the preceding paragraphs. In particular, McFadden falsely represented that returns that would be generated by the securities transactions were sufficient to allow customers to retire from their jobs and replace salary payments with regular, sustainable monthly withdrawals from their securities accounts.
17. Sales material and correspondence authored by McFadden containing misstatements and omissions of material facts included the following:
 - a. 5/4/01 letter to customer PS: *"You asked me at your last visit if your withdrawal of \$4,000 a month would last. we have to get 14% return rate to never run out of*

money. I feel you should continue taking the \$4,000 a month and enjoy yourself and let me worry about the market."

- b. 10/1/01 letter to customer WR containing withdrawal scenarios run at 13% and at 15%: *"The 13% 15% on [sic] returns seemed on the high side. However, with the depressed stock market prices this might be achievable in the near future when the market starts to rally.*
- c. 10/10/01 letter to customer GM II containing withdrawal scenarios run at 11.5% and at 14.75%, with 11.5% described as a *"worst case scenario."*
- d. 10/28/02 letter to customer AS containing withdrawal scenario run at 18%: *"We know that return is on the high side, but it is not out of the question. This can be obtained under very favorable circumstances With our tight trading ranges and if we do a very good job, you do have a chance to achieve your goals.*
- e. 3/23/98 "Financial Summary" to customer BS: *"Congratulations, both of you have done a great job of accumulating assets and living within your means. If managed well, the money you have set aside for retirement should be enough for you to maintain the lifestyle you desire.... Since you indicated the need for \$60,000 in today's dollars to retire, we can conclude that everything is OK from a financial perspective if you retire at 55." \$60,000 represented about 8.4% of the customer's estimated \$718,600 in retirement savings.*

- f. 5/27/99 letter to customer GM I suggesting that it might be advisable to make withdrawals greater than about 7.85% of his retirement savings: *"Is your monthly income providing you enough cash to do the things you want?.. If the \$6,000 is enough, I would keep it there, but if things are tight, you should take more since we can't change for 5 years.*

Oral statements containing material omissions and misrepresentations included the following:

- g. Statements to customer WR: *David McFadden told me I was actually losing money by working. David McFadden also told me that he could make more money than I was making in my salary at Exxon.*
- h. Statements to customer KD: *When I first met with David L. McFadden, he told me that unless I liked working, I would be able to make more by staying home and allowing him to handle my investments.*

Statements to customer RR: *When I transferred my retirement funds to David L. McFadden, he told me that my wife and I would need to do some estate planning with him for \$750 because we would eventually have so much money that all of our kids would be fighting over it.*

18. In addition, the variable annuity, mutual fund, ETF and subaccount transactions set forth in Exhibits A, B, and C were unsuitable in view of the customers' financial situations and investment objectives, as described in paragraphs 1 through 17 above.
19. By virtue of such conduct, David L. McFadden violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, and NASD Conduct Rules 2110, 2120 and 2310.

SECOND CAUSE OF ACTION
Advertising Rules Violations, Against Respondent McFadden

20. The Department realleges and incorporates by reference paragraphs 1-19 above.
21. During the period 1997 to 2003, McFadden disseminated false and misleading sales literature, including monthly account statements that contained material omissions, such as the material information that withdrawals could have a significant impact on the value of the annuities in the account.
22. In addition, correspondence sent by McFadden to customers made claims regarding the performance of certain mutual funds, but did not offer a sound basis for evaluating that information.
23. Other sales literature sent to customers by McFadden was misleading in that it promised future positive returns.
24. Also, during 1999-2004, McFadden, in written seminar materials shown and to customers and prospects, touted his accounting skills and referred to himself as a "CPA"

and as having a specific number of years of experience as a CPA despite the fact that he did not have a current, valid, active Louisiana CPA certificate. This conduct violated the Louisiana Accountancy Act.

25. Moreover, McFadden did not submit the sales literature and correspondence that he sent out to customers to his firm for approval in the form that he actually sent it out.
26. Furthermore, the statements set forth in paragraph 17(a) through (f) above are unwarranted, incomplete, and misleading.
27. By virtue of such conduct, David L. McFadden violated NASD Conduct Rules 2210 and 2110.

THIRD CAUSE OF ACTION
Unauthorized Securities Transactions, Against Respondent McFadden

28. The Department realleges and incorporates by reference paragraphs 1-27 above.
29. On or about June 15, 1999, David L. McFadden effected transactions in AST Pimco Total Return Bond, Neuberger Mid Cap Value, Rydex Nova, Rydex OTC, AST Janus Small Cap Growth and Kemper Small Cap Growth variable annuity subaccounts for the account of customer WA without prior authorization, knowledge or consent from the customer.
30. On or about September 17, 2001, David L. McFadden effected transactions in Alger Cap Growth and Alliance Growth annuity subaccounts for the account of customer CS without prior authorization, knowledge or consent from the customer.

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31. By virtue of such conduct, David L. McFadden violated NASD Conduct Rule 2110.

Based on these considerations, the sanctions hereby imposed by the acceptance of the Offer are in the public interest, are sufficiently remedial to deter Respondent from any future misconduct, and represent a proper discharge by NASD, of its regulatory responsibility under the Securities Exchange Act of 1934.

SANCTIONS

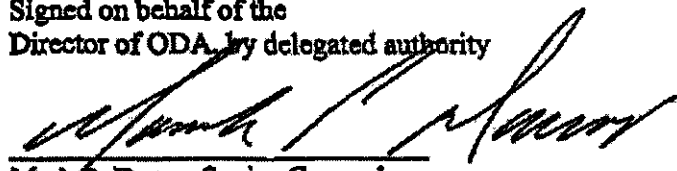
It is ordered that David L. McFadden be barred from association with any NASD member in any capacity.

The sanctions imposed herein shall be effective on a date set by NASD staff. Pursuant to IM-8310-2(f), A bar or expulsion shall become effective upon approval or acceptance of this Order by the NAC.

SO ORDERED.

NASD

Signed on behalf of the
Director of ODA, by delegated authority



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