

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS**

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

PATRICK F. HARTE, Jr.
(CRD No. 1865650),

Respondent.

Disciplinary Proceeding
No. 2006004666601

Hearing Officer – MAD

DEFAULT DECISION

July 21, 2011

Respondent is barred from associating with any FINRA registered firm in any capacity for violating (1) NASD Conduct Rule 2110 by participating in the sale of unregistered securities in violation of Section 5 of the Securities Act of 1933, and (2) NASD Conduct Rules 3010 and 2110 by failing to reasonably supervise a registered representative in connection with the sale of unregistered securities.

Appearances

Jonathan I. Golomb, Senior Special Counsel, Washington, DC, and David Friedman, Principal Counsel, New York, NY, for the Department of Enforcement.

No appearance by or on behalf of Patrick F. Harte, Jr.

DECISION

I. Background

On March 30, 2010, the Department of Enforcement ("Enforcement") filed the attached Complaint in this matter against Respondents Ryan J. Kirkpatrick ("Kirkpatrick") and Patrick F. Harte, Jr. ("Respondent"). The First Cause of Action alleges that, between April 2005 and April 2006, Respondent participated in the sale of unregistered securities, in violation of Section 5 of

the Securities Act of 1933 ("Securities Act"), and violated Conduct Rule 2110.¹ The Complaint alleges that Respondent and Kirkpatrick sold millions of shares of a thinly-traded penny stock, Sniffex, Inc. ("Sniffex"), resulting in proceeds exceeding \$9.3 million for Barron Moore, Inc. ("Barron Moore") customers. The Second Cause of Action alleges that Respondent failed to supervise Kirkpatrick, the registered representative assigned to the customer accounts at issue, in connection with the sale of the unregistered securities.

Kirkpatrick filed an answer on June 17, 2010, and requested a hearing. A hearing on the allegations against Kirkpatrick was held before a Hearing Panel in Dallas, Texas, on January 11, 2011. On March 28, 2011, the Hearing Panel issued a separate decision on the Complaint against Kirkpatrick. This default decision addresses the charges against Respondent.

Respondent filed an answer on June 2, 2010. However, he failed to appear for the final pre-hearing conference ("Conference") and a subsequent show cause hearing. Accordingly, the Hearing Officer issued an Order holding Respondent in default on January 7, 2011. On May 16, 2011, Enforcement filed a Motion for Entry of Default Decision ("Default Motion") on the charges against Respondent, supported by the Declaration of Jonathan I. Golomb, Esq. ("Golomb Decl.") and three exhibits. Respondent did not file a response to the Default Motion. For the reasons set forth below, Enforcement's Default Motion is granted.²

¹ As of July 30, 2007, NASD consolidated with the member regulation and enforcement functions of NYSE Regulation and began operating under a new corporate name, the Financial Industry Regulatory Authority (FINRA). References in this decision to FINRA include, where appropriate, NASD. Following consolidation, FINRA began developing a new FINRA Consolidated Rulebook. The first phase of the new consolidate rules became effective on December 15, 2008, including certain conduct rules and procedural rules. See Regulatory Notice 08-57 (Oct. 2008). This decision refers to and relies on the NASD Conduct Rules that were in effect at the time of Respondent's alleged misconduct.

² The factual determinations in this Decision are based on the Golomb Declaration, the exhibits filed by Enforcement with its Default Motion ("CX-A, CX-B, and CX-C"), and the evidence admitted at the Hearing, including Hearing exhibits ("CX-1-56") and the transcripts of the sworn testimony ("Tr.").

II. Respondent's Default

On December 9, 2010, the Hearing Officer issued a notice setting the Conference on January 4, 2011. The notice cautioned the parties that a failure to appear at the Conference may be deemed a default. Respondent failed to appear at the Conference in accordance with Rule 9241. On January 5, 2011, the Hearing Officer issued a show cause order, requiring Respondent to appear on January 7, 2011, to show cause why he should not be held in default for failing to appear at the Conference. Respondent failed to appear for the show cause hearing. Accordingly, the Hearing Officer issued an Order, dated January 7, 2011, holding Respondent in default.

III. Origin of the Investigation

FINRA's investigation into the sales of Sniffex stock was triggered by its receipt of a spam e-mail touting the stock in June 2005. FINRA learned that the Sniffex stock was not registered with the Securities and Exchange Commission ("SEC"). In addition, the e-mail revealed that a third party was paid \$22,000 to promote the Sniffex stock. In light of these factors, FINRA initiated an investigation regarding a possible unlawful distribution of unregistered securities.

IV. Findings of Fact and Conclusions of Law

A. Respondent

Respondent was first registered with FINRA in 1989 as a General Securities Representative.³ Between July 2004 and June 2008, Respondent was employed with Barron Moore,⁴ a former FINRA member firm in Dallas, Texas, when the conduct at issue took place.⁵

³ CX-9, at 5.

⁴ Barron Moore was a FINRA member from 2003 to 2008. The firm was expelled on July 23, 2008, for participating in the sale of unregistered securities and failing to supervise in connection with those violations. Its business was comprised largely of receiving and liquidating securities of low priced Pink Sheet or Penny stocks. Tr. 60-62; CX-5, at 3.

⁵ CX-9, at 1.

At Barron Moore, he was registered as a General Securities Representative, General Securities Principal, and an Equity Trader.⁶ Respondent supervised the Barron Moore retail brokers, including Kirkpatrick.⁷ He was also the executive vice-president and part owner of Barron Moore from August 2006 to June 2008.⁸

On June 10, 2008, Barron Moore filed a Uniform Termination Notice for Securities Industry Registration ("Form U5") on Respondent's behalf, terminating his employment as of that date.⁹ Respondent is not currently employed in the securities industry.¹⁰

B. Jurisdiction

FINRA has jurisdiction over this disciplinary proceeding, pursuant to Article V, Section 4 of FINRA's By-Laws, because (1) the Complaint was filed within two years after Respondent's FINRA registration terminated, and (2) the Complaint charges him with misconduct that occurred while he was associated with a FINRA registered firm.¹¹

C. Sale of Unregistered Securities

1. The Issuer: Sniffex

Sniffex was incorporated in Nevada on October 27, 2004, as Snissex, Ltd.¹² On November 1, 2004, the Board of Directors changed the company's name to Sniffex, Inc.¹³ The company claimed that it manufactured and marketed a device that could detect explosives. The

⁶ *Id.*

⁷ CX-1-6; CX-10, at 2-3, 5; Tr. 112.

⁸ Comp. ¶ 5.

⁹ Golomb Decl. ¶ 2; CX-9, at 14.

¹⁰ CX-9, at 1.

¹¹ See Article V, Sec. 4(a), FINRA By-Laws, available at www.finra.org/Rules (then follow "FINRA Manual" hyperlink to "Corporate Organization: By-Laws").

¹² CX-16, at 3.

¹³ *Id.* at 1.

inventor of the device is a Bulgarian national.¹⁴ The inventor's business partner, also a Bulgarian national, is Petar Mihaylov ("Mihaylov"), a stock promoter.¹⁵

Mihaylov controlled Sniffex.¹⁶ He developed a plan for Sniffex to issue 15 million shares of "free-trading" stock.¹⁷ For assistance in executing his plan, Mihaylov approached Mark Lindberg ("Lindberg"), a former stock promoter who had worked on previous deals with Mihaylov, and Lindberg agreed to assist him.¹⁸

2. The Stock Promoter: Mark Lindberg

Lindberg was in the business of taking companies public, following which he would manipulate the stock price through promotional activities and sell the stock into the market.¹⁹ To manipulate the stock price without detection, Lindberg hid the actual participants in the stock distribution through the use of nominees, family members' names, or offshore corporations.²⁰

Barron Moore was one of the brokerage firms that Lindberg used to conduct his business.²¹ Barron Moore would obtain the trading symbols for the securities and would help liquidate the stock for clients, who deposited shares with Barron Moore.²² Lindberg primarily dealt with Respondent and Josh Lankford, another registered representative at Barron Moore and

¹⁴ Tr. 9.

¹⁵ Tr. 33, 36.

¹⁶ Tr. 36-37.

¹⁷ Tr. 36.

¹⁸ Tr. 33. Lindberg participated in numerous reverse mergers with shell companies. Tr. 20-21. Lindberg pled guilty to conspiracy to commit securities fraud and wire fraud in the Northern District of Oklahoma. Tr. 21-22. As part of his plea agreement, he agreed to provide truthful testimony to prosecutors and regulators. Tr. 22.

¹⁹ Tr. 20, 23, 29.

²⁰ Tr. 23.

²¹ Lindberg had utilized Barron Moore to sell the shares for approximately 50-75 shell company merger deals. Tr. 27.

²² Tr. 25-26.

Lindberg's business partner.²³ Respondent assisted Lindberg with his activities, taking directions from Lindberg or others working with Lindberg.²⁴ For example, Lindberg would call Respondent and place orders to sell stock, then later he would call Respondent to allocate the sales to particular customers.²⁵ Lindberg had access to multiple nominee accounts at Barron Moore.²⁶

3. Issuance of Sniffex Stock

In order to obtain the 15 million shares of Sniffex "free-trading" stock, Lindberg utilized a state-qualified registration in Nevada under Federal Rule 504 whereby a registration statement is filed with the state instead of the SEC.²⁷ On February 28, 2005, Sniffex filed a registration statement with the Securities Division of the Nevada Secretary of State for the sale of up to 15 million shares of common stock pursuant to Rule 504 under Regulation D of the Securities Act and Chapter 90.490 of the Nevada Administrative Code.²⁸ In reality, none of the 15 million shares would be "free-trading" because every share had Mihaylov or his nominees designated as the final recipients.²⁹

The registration statement was approved by the state on April 6, 2005.³⁰ It named six different entities that were recipients of the Rule 504 stock.³¹ Each entity was under the control of Mihaylov, Lindberg, or one of Mihaylov's nominees. Two of the six entities were PU

²³ Tr. 26-27, 45, 112.

²⁴ Tr. 28-29.

²⁵ Tr. 29-30.

²⁶ Tr. 29.

²⁷ Tr. 33.

²⁸ CX-24, at 2-28.

²⁹ Tr. 36.

³⁰ CX-24, at 1. On April 22, 2005, Sniffex filed a Form D, Notice of Sale of Securities, with the SEC regarding the sale of the shares issued pursuant to the Nevada Rule 504 offering. CX-25.

³¹ Tr. 36.

Partners, Inc., which received 6.3 million shares, and Interim Capital Corp., which received 3.245 million shares.³² At Mihaylov's direction, those two entities transferred most of their shares to two nominees: YM, the inventor's mother, and AS, the inventor's uncle.³³ Pursuant to Mihaylov's plan, YM and AS each received 3.75 million shares of Sniffex stock.³⁴

4. Opening of Accounts at Barron Moore

On March 23, 2005, Barron Moore opened accounts in the names of YM and AS.³⁵ Kirkpatrick was the registered representative for both of the accounts.³⁶ According to the new account documents, YM was a retired, 72-year-old resident of Sofia, Bulgaria, with no investment experience.³⁷ Her annual income was less than \$25,000, and her liquid net worth was less than \$50,000.³⁸ Her new account form indicated that her risk tolerance was "High Risk," and her investment objective was "Active or Day trading."³⁹ Respondent approved the YM account as principal on behalf of Barron Moore.⁴⁰

The new account form for AS indicated that he was a 47-year-old resident of Sofia, Bulgaria, working as a self-employed consultant, with three years of experience investing in

³² Tr. 63-64.

³³ Tr. 41-42, 64, 72, 109; CX-30.

³⁴ CX-27, at 3-4, 7-8; CX-28, at 2, 6.

³⁵ Tr. 74, 77; CX-34, 39.

³⁶ Tr. 72. The accounts were transferred to Kirkpatrick from Lankford. Tr. 112.

³⁷ CX-34, at 1-2.

³⁸ *Id.* at 2.

³⁹ *Id.*

⁴⁰ CX-34.

stocks.⁴¹ Similar to YM, he had less than \$25,000 in annual income and less than \$50,000 in liquid net worth.⁴² AS's new account form also stated that his risk exposure was "High Risk," and his investment objective was "Active or Day trading."⁴³ Respondent also approved the AS account.⁴⁴

As noted above, YM's and AS's accounts were nominee accounts under Mihaylov's control.⁴⁵ Mihaylov used e-mail accounts created for YM and AS to communicate with Barron Moore regarding the trading in their accounts.⁴⁶

5. Initiation of the Market for Sniffex

Sniffex stock was not publicly traded prior to April 2005.⁴⁷ On April 8, 2005, a Sniffex stock holder requested that Barron Moore sell 5,000 shares of Sniffex at \$.05 per share.⁴⁸ In response, Respondent contacted Nasdaq's Market Data Integrity Symbols group and requested a symbol for Sniffex.⁴⁹ Sniffex was assigned the symbol "SNFX," and its stock became available for quoting on the Pink Sheets system on April 12, 2005.⁵⁰

⁴¹ CX-39, at 1-2. Barron Moore also had a revised new account form for AS. CX-40. That form stated he had 10 years of investment experience; however, another area on the same page stated that his investment experience was "1-5 years." *Id.* at 2. This new account form appears to have been created after the fact because the date on the form, indicating the version of the form, states "Revised on June 7, 2005," yet, the document is signed on May 23, 2005. *Id.*

⁴² CX-39, at 2.

⁴³ *Id.*

⁴⁴ CX-39.

⁴⁵ Tr. 44-45.

⁴⁶ Tr. 46-48.

⁴⁷ Tr. 68-69.

⁴⁸ CX-29; Tr. 68.

⁴⁹ Tr. 68-69; CX-29.

⁵⁰ Tr. 69; CX-29.

6. Sniffex Stock Deposits

On May 12, 2005, YM and AS each deposited 3.75 million shares of Sniffex stock into their accounts at Barron Moore.⁵¹ The certificates, dated May 10, 2005, bore no restricted legend.⁵² Kirkpatrick did not request or review the certificates.⁵³ The shares were not registered with the SEC.⁵⁴

YM and AS also completed "Incoming Stock Questionnaires" ("Questionnaires"), documents used by Barron Moore to obtain information from customers who deposited stock at the firm. YM's Questionnaire indicated that her shares were purchased from a third-party, non-affiliated shareholder, but it did not identify the shareholder.⁵⁵ There were two Questionnaires for AS, both dated August 30, 2005.⁵⁶ The first one stated that he had purchased his shares in a third-party transaction, but it did not indicate from whom his shares were purchased.⁵⁷ The second stated that he had purchased his shares from the Issuer, i.e., Sniffex.⁵⁸ Neither Respondent nor Kirkpatrick reviewed the Questionnaires.⁵⁹ In fact, during the investigation, Respondent testified that it was Barron Moore's practice to file the Questionnaires without review by the broker or supervisor.⁶⁰

⁵¹ CX-35, at 1; CX-41, at 1.

⁵² CX-28, at 5-6.

⁵³ Tr. 108, 115.

⁵⁴ CX-22; Tr. 57.

⁵⁵ CX-36.

⁵⁶ CX-42.

⁵⁷ CX-42, at 1.

⁵⁸ CX-42, at 2.

⁵⁹ Tr. 119, 122, 124; CX-11, at 6, 9.

⁶⁰ CX-12, at 9-10.

7. Sales of Sniffex Stock

Respondent and Kirkpatrick handled the sales of Sniffex for the YM and AS accounts.⁶¹ From mid-May 2005 through April 2006, they sold approximately 3.4 million shares of Sniffex into the public markets on behalf of YM and AS.⁶² During that time, the stock price increased from approximately \$.05 for the initial trade to a high of \$6.00 on July 29, 2005.⁶³ No registration statement covering these sales was ever filed with the SEC.⁶⁴

On May 16, 2005, within days of depositing the Sniffex stock, YM began selling shares of Sniffex through her account at Barron Moore.⁶⁵ Between May 16, 2005 and April 25, 2006, Respondent and Kirkpatrick sold 2,332,542 Sniffex shares on behalf of YM in 55 transactions.⁶⁶ YM realized approximately \$5.8 million in proceeds from these sales, which were periodically wired out of the account to a Swiss bank.⁶⁷

Between August 2, 2005 and January 24, 2006, Respondent and Kirkpatrick sold 1,079,882 Sniffex shares on behalf of AS in 21 transactions.⁶⁸ AS realized approximately \$3.5

⁶¹ CX-11, at 26, 28, 35-36. All orders for the sales were sent to Barron Moore by e-mail or through instant messaging. Generally, the e-mails and instant messages were addressed to Kirkpatrick. Kirkpatrick then forwarded them to Respondent's trading department, printed them and delivered them to the trading department, or prepared order tickets for execution. CX-45-56; CX-B, at 96-97; CX-C, at 172-73. On at least one occasion, AS sent a sell order e-mail directly to Respondent. CX-52.

⁶² CX-31.

⁶³ Tr. 90-91; CX-32. CX-32 reflects the symbol HSFC, which is Sniffex's successor company, Homeland Safety International, Inc. Tr. 90.

⁶⁴ CX-22; Tr. 57.

⁶⁵ CX-37, at 1.

⁶⁶ CX-31.

⁶⁷ *Id.*; CX-35; Tr. 84, 144-45. Respondent approved some of the wire transfer requests from YM's account. CX-11, at 39-40.

⁶⁸ CX-31.

million in proceeds from these sales, which were also periodically wired out of his account to a Swiss bank.⁶⁹

The total commissions generated for these sales were \$481,398.⁷⁰

8. Failure to Conduct Due Diligence

Respondent failed to conduct any due diligence prior to the Sniffex stock sales from the YM and AS accounts.⁷¹ The circumstances surrounding the Sniffex stock and the firm's customers presented numerous "red flags" of a possible unlawful stock distribution.

Sniffex was a little-known development-stage company whose stock had only recently begun trading publicly in April 2005.⁷² The accounts for YM and AS were opened at Barron Moore approximately one month before Sniffex began trading. In addition, both YM and AS deposited substantial amounts of Sniffex shares into their accounts within weeks of Sniffex's initial trade. The Sniffex stock certificates were newly-issued, dated just two days before YM and AS deposited the stock into their accounts.⁷³ Further, the goal of both accounts was to liquidate their Sniffex positions.⁷⁴ YM began liquidating her shares within a few days after depositing them into her Barron Moore account.⁷⁵

While YM and AS each had incomes of less than \$25,000, a liquid net worth of under \$50,000, and limited investment experience, each deposited millions of shares of Sniffex stock that was worth millions of dollars within a year. In addition, despite YM's and AS's stated limited financial resources and lack of investment experience, when communicating with Barron

⁶⁹ *Id.*; CX-41; Tr. 84.

⁷⁰ CX-31.

⁷¹ CX-11, at 6, 9.

⁷² Tr. 84.

⁷³ Tr. 115.

⁷⁴ Tr. 114, 127.

⁷⁵ Compare CX-35, at 1 with CX-37, at 1.

Moore, they used terminology that evidenced familiarity with the operation of the U.S. markets and sophisticated market-related strategies.⁷⁶ For example, YM sent e-mails referring to "Level 2 offers;" market makers, using a four letter identifier for a specific market maker; and the abbreviation "GTC" for "good till canceled" orders.⁷⁷ YM, a 72-year-old Bulgarian national, also sent an instant message using American slang: "you are the man."⁷⁸ Such communications were "red flags" because they strongly suggest that the account was controlled by someone other than YM.

Neither Respondent nor anyone else at Barron Moore made any effort to determine the source of YM's or AS's shares, how much stock they owned, or the nature of their relationship to the issuer.⁷⁹ As stated above, both Respondent and Kirkpatrick failed to review the Questionnaires for the YM and AS accounts or obtain the same information directly from Kirkpatrick's customers.⁸⁰

Notwithstanding these facts and circumstances, Respondent participated in the sale of the Sniffex stock without taking the necessary steps to determine whether the unregistered Sniffex shares could be sold in compliance with Section 5 of the Securities Act. Respondent did not determine if a registration statement was in effect with respect to YM's or AS's Sniffex shares,

⁷⁶ See CX-45-56. The customer e-mails were generally forwarded to Respondent. CX-B, at 2.

⁷⁷ See e.g., CX-45, at 1; CX-47, at 1.

⁷⁸ CX-49.

⁷⁹ CX-11, at 17, 33-34, 48; Tr. 115-22. In an e-mail exchange with YM, Kirkpatrick learned that she received her Sniffex shares from her son, the inventor of the Sniffex device. Tr. 109. However, after receiving this information, he made no effort to determine whether YM was affiliated with Sniffex. Tr. 115-20. He also never questioned AS about how he acquired his shares or whether he was affiliated with Sniffex. Tr. 120-24.

⁸⁰ CX-11, at 24-25, 47; Tr. 115-22.

or if there was an applicable exemption.⁸¹ He relied on transfer agents and clearing firms to determine the tradability of the stock.⁸²

9. Violation of Section 5 of the Securities Act

Securities Act Section 5(a) prohibits any person, directly or indirectly, from selling a security in interstate commerce unless a registration statement is in effect as to the offer and sale of that security or there is an applicable exemption from the registration requirements. Securities Act Section 5(c) prohibits the offer or sale of a security unless a registration statement as to such security has been filed with the SEC, or an exemption is available.⁸³ The purpose of the registration requirements is to "protect investors by promoting full disclosure of information thought necessary to informed investment decisions."⁸⁴ A violation of Section 5 of the Securities Act constitutes a violation of Conduct Rule 2110.⁸⁵

To establish a *prima facie* case of a violation of Sections 5(a) and 5(c) of the Securities Act, Enforcement must show that: (1) no registration statement was in effect as to the securities; (2) Respondent sold or offered to sell these securities; and (3) interstate transportation or communication were used in connection with the sale or offer of sale.⁸⁶ A showing of scienter is

⁸¹ CX-11, at 9.

⁸² CX-11, at 32.

⁸³ 15 U.S.C. § 77e(a) and (c); see also *Jacob Wonsover*, Exchange Act Rel. No. 41123, 1999 SEC LEXIS 430, at *15-16 (Mar. 1, 1999), *aff'd*, 205 F.3d 408 (D.C. Cir. 2000).

⁸⁴ *SEC v. Ralston Purina Co.*, 346 U.S. 119, 124 (1953).

⁸⁵ *Alvin W. Gebhart*, Exchange Act Release No. 53136, 2006 SEC LEXIS 93, at *54 n.75 (Jan. 18, 2006) *rev'd and remanded in part on other grounds sub. nom Gebhart v. SEC*, 2007 U.S. App. LEXIS 27183 (9th Cir. Nov. 21, 2007) ("Further, because we have consistently held that a violation of a Commission or NASD rule or regulation is inconsistent with just and equitable principles of trade, we find that the Gebharts' sale of the unregistered MHP notes also constitutes a violation of NASD Conduct Rule 2110."); *Stephen J. Gluckman*, Exchange Act Release No. 41628, 1999 SEC LEXIS 1395 (July 20, 1999); see *William H. Gerhauser*, Exchange Act Release No. 40639, 1998 SEC LEXIS 2402 (Nov. 4, 1998).

⁸⁶ *Gebhart*, 2006 SEC LEXIS 93, at *52; *SEC v. Cont'l Tobacco Co.*, 463 F.2d 137, 155 (5th Cir. 1972).

not required because “[t]he Securities Act of 1933 imposes strict liability on offerors and sellers of unregistered securities.”⁸⁷

Here, no registration statement was in effect with respect to the Sniffex securities that are the subject of the Complaint. Respondent actively participated in the sale of the Sniffex stock by obtaining the trading symbol, placing the initial quote, and executing trades in the stock. The sales involved interstate activity because the shares were sold into the over-the-counter market, thereby entering interstate commerce. In addition, they were quoted on the Pink Sheets, a national communications medium. Enforcement has established a *prima facie* case.

“Once Enforcement establishes a *prima facie* case, the burden shifts to [Respondent] to show that the transactions were exempt from the Securities Act’s registration requirements.”⁸⁸ Respondent did not present any evidence that the Sniffex shares were exempt from the registration requirements of Section 5 of the Securities Act. Accordingly, the Hearing Officer finds that Respondent violated Section 5 of the Securities Act and thereby violated Conduct Rule 2110.⁸⁹

D. Failure to Supervise

“Assuring proper supervision is a critical component of broker-dealer operations.”⁹⁰ Conduct Rule 3010(a) requires that FINRA members “establish and maintain a system to supervise the activities of each registered representative, registered principal, and other associated person that is reasonably designed to achieve compliance with applicable securities

⁸⁷ Gebhart, 2006 SEC LEXIS 93, at *53 n.73 (quoting *Swenson v. Engelstad*, 626 F.2d 421, 424 (5th Cir. 1980)).

⁸⁸ *Dep’t of Enforcement v. Midas Securities*, No. 2005000075703, slip op. at 6 (N.A.C. Mar. 3, 2011).

⁸⁹ See e.g., *id.* at 9; *Dep’t of Enforcement v. Morgan Keegan & Co.*, No. CAF040073, 2006 NASD Discip. LEXIS 24, at *40 (O.H.O. July 21, 2006).

⁹⁰ *Richard F. Kresge*, Exchange Act Rel. No. 55988, 2007 SEC LEXIS 1407, at *27 (June 29, 2007).

laws and regulations, and with applicable [FINRA] Rules.”⁹¹ The standard of “reasonableness” is determined based on the particular circumstances of each case.⁹²

Here, Respondent failed to undertake adequate efforts to ensure that Kirkpatrick ascertained the information necessary to determine whether the customers’ unregistered Sniffex shares could be sold in compliance with Section 5 of the Securities Act. He did not consider the determination of the free-trading status of shares to be within his supervisory responsibilities.⁹³

Respondent failed to follow up on “red flags.” For example, having approved the opening of the YM and AS accounts, Respondent was on notice of the inconsistencies between their trading experience and the activity in their Barron Moore accounts; yet, he took no action. Respondent also received some of the customer e-mails, which evidenced a greater level of market sophistication than reflected in the YM and AS new account forms;⁹⁴ however, he failed to investigate these discrepancies.

The Hearing Officer finds that Respondent failed to adequately supervise Kirkpatrick in connection with the sale of unregistered securities, as required by Conduct Rule 3010(a). Accordingly, the Hearing officer finds that Respondent violated Conduct Rules 3010(a) and 2110.⁹⁵

⁹¹ NASD Conduct Rule 3010(a).

⁹² See, e.g., *Christopher Benz*, Exchange Act Rel. No. 38440, 1997 SEC LEXIS 672, at *12 (Mar. 26, 1997) (citing *In re Consol. Inv. Servs., Inc.*, Exchange Act Rel. No. 36687, 1996 SEC LEXIS 83 (Jan. 5, 1996)).

⁹³ CX-11, at 32.

⁹⁴ CX-B, at 2-3.

⁹⁵ A violation of Conduct Rule 3110 also is a violation of Conduct Rule 2110, which requires member firms to observe high standards of commercial honor and just and equitable principles of trade. *Kresge*, 2007 SEC LEXIS 1407, at *42.

V. Sanctions

A. Sale of Unregistered Securities

The FINRA Sanction Guidelines (“Guidelines”) for the sale of unregistered securities provide for a fine of \$2,500 to \$50,000 and consideration of a suspension or bar in egregious cases.⁹⁶ The Guidelines further set forth specific considerations for such violations, three of which are applicable to this case: (1) whether the respondent attempted to comply with an exemption from registration; (2) share volume and dollar amount of transactions involved; and (3) whether the respondent disregarded “red flags” suggesting the presence of unregistered distribution.⁹⁷

At no time did Respondent attempt to ascertain if the stock was registered or if an exemption from registration applied. Instead, he relied on the issuer’s transfer agent to clear the stock for sale. Here, a large number of shares were sold to members of the public. In total, YM and AS sold approximately 3.4 million shares, generating sales proceeds greater than \$9.3 million and commissions of \$481,398. Clearly, the volume of sales and the dollar amount involved created the potential for significant harm to investors. In addition, there were a large number of transactions, totaling 76, which is an aggravating factor.⁹⁸

Respondent also failed to conduct any due diligence on the Sniffex stock. There were ample “red flags,” which should have caused a securities professional to inquire further. First,

⁹⁶ FINRA Sanction Guidelines 24 (2011), www.finra.org/sanctionguidelines.

⁹⁷ *Id.*

⁹⁸ *Id.* at 7 (Principal Consideration in Determining Sanctions No. 18)

substantial blocks of Sniffex stock were deposited at Barron Moore within days of being issued.⁹⁹ Second, the issuer of the shares was an unknown, development-stage company with no trading history.¹⁰⁰ Third, after the sales of the unregistered Sniffex stock, the customers wired their proceeds to Swiss banks. Further, the sales greatly exceeded the customers' reported annual income and liquid net worth. Fourth, the customer e-mails communicating the orders were inconsistent with the customers' securities experience as described on their new account forms.

The Hearing Officer finds that Respondent deliberately turned a blind-eye to the registration requirements and willingly assisted Lindberg (a stock promoter who later pled guilty to conspiracy to commit securities fraud and wire fraud) in his business of taking companies public and manipulating their stock. Respondent's assistance included permitting Lindberg to place trades and wire money in customer accounts for which he had no trading authority.¹⁰¹ Such misconduct cannot be tolerated by a securities professional, especially an officer in a brokerage firm.

Taking all of the foregoing factors into consideration, the Hearing Officer finds that Respondent's misconduct was egregious. The Hearing Officer finds that a bar is the appropriate sanction in this case. There are no mitigating factors that would warrant consideration of lesser sanctions. Accordingly, the Hearing Officer will bar Respondent from associating with any FINRA member firm in all capacities.

⁹⁹ See *Steven E. Scott*, Exchange Act Release No. 43656, 2000 SEC LEXIS 2635, at *10 (Dec. 1, 2000) (stating that if a broker is asked to sell a substantial amount of a thinly-traded security, he must take all necessary steps to make sure that controlling persons are not involved); *Distribution by Broker-Dealers of Unregistered Secs.*, Exchange Act Rel. No. 6721, 1962 SEC LEXIS 74, at *4-5 (Feb. 2, 1962) (discussing how it must be assumed that the issuer is the source of unregistered securities appearing in substantial amounts in the market over a short period of time).

¹⁰⁰ See *Charles F. Kirby*, Exchange Act Rel. No. 47149, 2003 SEC LEXIS 46, at *21-22 (Jan. 9, 2003) (discussing how petitioner failed to make an appropriate showing where company at issue had limited assets, limited trading history, and very little public information regarding the company's business).

¹⁰¹ Tr. 29-30.

B. Failure to Supervise

The Guidelines for failing to supervise recommend, in egregious cases, suspending the responsible individual in any and all capacities for up to two years or imposing a bar. The Guidelines further recommend the imposition of a fine between \$5,000 and \$50,000. The specific considerations for failure to supervise are: (1) whether the respondent ignored "red flag" warnings that should have resulted in additional supervisory scrutiny, (2) the nature, extent, size and character of the underlying misconduct, and (3) the quality and degree of the supervisor's implementation of the firm's supervisory procedures and controls.¹⁰²

The Hearing Officer determined that the supervisory violation by Respondent was egregious. He ignored the "red flags" associated with the sale of the unregistered Sniffex securities. As noted above, the volume of the sales was significant and represented a substantial share of the market. Respondent abdicated his supervisory responsibility with respect to the sale of unregistered securities. He relied exclusively on the clearing firm and conducted no independent due diligence to ensure that the stock could be sold in compliance with the registration requirements.

Respondent's misconduct is particularly troubling because he was aware of and assisted with Lindberg's stock promotion activities. With that knowledge, Respondent permitted Kirkpatrick to sell the unregistered Sniffex securities unfettered by supervisory oversight.

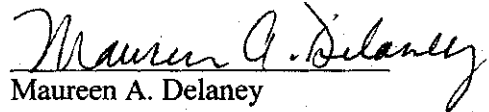
The Hearing Officer also considered Respondent's prior disciplinary history. In 2009, Respondent was suspended for six months in all principal capacities, fined \$10,000, and ordered to requalify before acting in any principal capacity for failing to supervise registered representatives who sold unregistered securities in violation of Section 5.

¹⁰² Sanction Guidelines 105.

In light of the foregoing, and finding no mitigating factors, the Hearing Officer finds that a bar is the appropriate sanction for this violation. Accordingly, the Hearing Officer will bar Respondent from associating with any FINRA member firm in all capacities.

VI. Order

Respondent is barred from associating with any FINRA registered firm in any capacity for: (1) violating NASD Conduct Rule 2110 by participating in the sale of unregistered securities in violation of Section 5 of the Securities Act of 1933; and (2) violating NASD Conduct Rules 3010 and 2110 by failing to reasonably supervise Kirkpatrick in connection with the sale of unregistered securities.


Maureen A. Delaney
Hearing Officer

Copies to: Patrick F. Harte, Jr. (*via e-mail, overnight, and first-class mail*)
David L. Friedman, Esq. (*via e-mail and first-class mail*)
Jonathan I. Golomb, Esq. (*via e-mail and first-class mail*)
David R. Sonnenberg, Esq. (*via e-mail*)

**FINANCIAL INDUSTRY REGULATORY AUTHORITY (FINRA)
OFFICE OF HEARING OFFICERS**

DEPARTMENT OF ENFORCEMENT,

COMPLAINANT,

v.

RYAN KIRKPATRICK (CRD No. 4459488),

and

PATRICK HARTE (CRD No. 1865650),

RESPONDENTS.

**DISCIPLINARY PROCEEDING
No. 2006004666601**

HEARING OFFICER:

MAR 30 2010

COMPLAINT

The Department of Enforcement alleges:

SUMMARY

1. Between April 2005 and April 2006, respondents Ryan Kirkpatrick and Patrick Harte sold millions of unregistered shares of a thinly-traded penny stock, Sniffex, Inc., on behalf of customers, in violation of Section 5 of the Securities Act of 1933 and NASD Conduct Rule 2110. Both Kirkpatrick and Harte were associated with Barron Moore, Inc. at the time. These illicit sales resulted in proceeds of millions of dollars to the customers.

2. Harte was also Kirkpatrick's supervisor at Barron Moore. In that capacity, Harte failed to reasonably supervise the activities of Kirkpatrick in selling Sniffex shares on behalf of customers.

3. As a result of the illicit sales of unregistered securities described herein, Kirkpatrick and Harte violated Section 5 of the Securities Act, thereby violating NASD Conduct

Rule 2110 (now FINRA Rule 2010). By virtue of his supervisory failures, Harte violated NASD Conduct Rules 3010 and 2110.

RESPONDENTS

4. Respondent **Ryan Kirkpatrick** (CRD 4459488) was a registered representative at Barron Moore, a former FINRA member firm in Dallas, Texas, from 2003 to 2008. Kirkpatrick holds a general securities license and is a licensed direct participation limited representative. Kirkpatrick was first registered as a General Securities Representative in 2001. He is currently registered with another FINRA member firm.

5. Respondent **Patrick Francis Harte, Jr.** (CRD 1865650) was employed as the supervisor of the trading desk, executive vice president, and part owner of Barron Moore from August 2006 to June 2008. He is licensed as a General Securities Representative, Equity Trader, and General Securities Principal. Harte was first registered as a General Securities Representative in 1989, as an Equity Trader in 1998, and as a General Securities Principal in 2004. Harte has not been employed in the securities industry since leaving Barron Moore. FINRA retains jurisdiction over Harte pursuant to Article V, Section 4 of the NASD By-Laws, which provides that NASD retains jurisdiction to file a complaint against a former registered person for two years following the effective date of termination of registration.

6. On August 31, 2009, a FINRA Hearing Panel found that Harte had failed to supervise several registered representatives at Barron Moore with respect to the sale of unregistered securities. The Hearing Panel found that Harte was a supervisor at Barron Moore, and specifically that he was the supervisor of Kirkpatrick. As a result of the violations, the Hearing Panel suspended Harte for six months in a principal capacity, fined him \$10,000, and required that he requalify as a principal.

FIRST CAUSE OF ACTION

Sale of Unregistered Securities by Kirkpatrick and Harte (NASD Rule 2110)

7. Paragraphs 1 through 6 are repeated and realleged herein.

The Issuer

8. Sniffex was incorporated in Nevada on October 27, 2004, as Snissex. On November 1, 2004, the Board of Directors changed the company's name to Sniffex.

9. The company's business activities purportedly involved manufacturing and marketing a device which the company claimed could detect explosives.

10. Between December 2004 and April 2005, Sniffex issued convertible promissory notes to a number of parties purportedly domiciled in Nevada, including entities named PU Partners, Inc. and Interim Capital Corp.

11. On February 28, 2005, Sniffex filed a registration statement with the Securities Division of the Nevada Secretary of State for the sale of up to 15 million shares of common stock pursuant to Rule 504 under Regulation D of the Securities Act and Chapter 90.490 of the Nevada Administrative Code. The registration statement was approved by the state on April 6, 2005.

12. Sniffex stock was not publicly traded prior to April 2005. Its stock was not listed on a national securities exchange or quoted in the over-the-counter market prior to that time.

13. On April 8, 2005, an individual who owned Sniffex stock requested that Barron Moore sell 5,000 shares of Sniffex at \$.05 per share. In response, Harte contacted Nasdaq's MDI Symbols group and requested a symbol for Sniffex. Sniffex was assigned the symbol "SNFX" and its stock became available for quoting on the Pink Sheets system on April 12, 2005.

14. On April 22, 2005, Sniffex filed a Form D, Notice of Sale of Securities, with the Securities and Exchange Commission regarding the sale of the shares issued pursuant to the Nevada Rule 504 offering.

15. Sniffex' stock began trading on April 27, 2005. That day, 10,000 shares of Sniffex was traded. No other shares were traded until May 13, 2005, when 800 shares of Sniffex were traded.

16. On April 25, 2005, and May 5, 2005, the note holders referred to in paragraph 10 above received a total of 14,980,000 shares of Sniffex stock, putatively issued under the Nevada Regulation D filing described above, pursuant to the conversion feature of the notes.

17. On May 10, 2005, all of the shares held in the names of Interim Capital and PU Partners were conveyed to two Bulgarian nationals, YM and AS. YM is the mother of the supposed inventor of the device sold by Sniffex, and AS is YM's nephew. YM and AS sold their shares through accounts handled by Kirkpatrick and Harte, as set forth below.

18. Specifically, a total of 3,750,000 shares were transferred to AS and a total of 3,750,000 shares were transferred to YM. The shares transferred to YM included 1,200,000 shares held in the name of Interim Capital and 2,550,000 shares held in the name of PU Partners. The 3,750,000 shares transferred to AS had been held in the name of PU Partners.

The Barron Moore Accounts

19. On March 23, 2005, accounts were opened at Barron Moore in the names of YM and AS. No one at Barron Moore ever met or spoke with either YM or AS.

20. Kirkpatrick served as the registered representative for both of these accounts during the time period in which the misconduct alleged herein took place.

21. Harte accepted both the YM and AS accounts as principal on behalf of Barron Moore.

22. According to the new account documents for her account, YM was a 72 year old resident of Sofia, Bulgaria, was retired, and had less than \$25,000 in annual income, less than \$50,000 in liquid net worth and no investment experience. Her new account form indicated that her risk tolerance was "high risk," and she was interested in "Active or Day trading."

23. AS's new account form indicated that he was a 47 year old resident of Sofia, Bulgaria working as a self-employed consultant with less than \$25,000 in annual income, less than \$50,000 in liquid net worth and three years of experience investing in stocks. AS's new account form indicated interest in "high risk" and "Active or Day trading."

24. Neither Kirkpatrick nor Harte ever met or spoke directly with YM or AS. Instead, both communicated with those customers solely via email and instant message. This was a violation of Barron Moore's written sales practice policy.

25. On May 12, 2005, YM and AS each deposited the 3.75 million shares of Sniffex referred to in paragraph 18 above into their accounts at Barron Moore in the form of unlegended certificates.

Sales of Unregistered Sniffex Stock

26. From mid-May 2005 through April 2006, the Kirkpatrick and Harte sold approximately 3.4 million unregistered shares of Sniffex into the public markets on behalf of YM and AS. These transactions are set out in Attachment A to this Complaint.

27. On May 16, 2005, YM began selling shares of Sniffex through her account at Barron Moore. Between May 16, 2005 and April 25, 2006, Kirkpatrick and Harte sold 2,332,542 Sniffex shares on behalf of YM in 55 transactions. YM realized approximately \$5.8

million in proceeds from these sales, which generated at least \$303,000 in commissions. The proceeds of these sales were periodically wired out of the account to a Swiss bank.

28. During this period, YM purchased 443,489 shares of Sniffex into her account at Barron Moore, costing approximately \$870,000 and generating approximately \$36,000 in additional commissions.

29. On August 2, 2005, AS began selling shares of Sniffex through his account at Barron Moore. Between August 2, 2005 and January 24, 2006, Kirkpatrick and Harte sold 1,079,882 Sniffex shares on behalf of AS in 21 transactions. AS realized approximately \$3.5 million in proceeds from these sales, which generated approximately \$177,000 in commissions. The proceeds of these sales were periodically wired out of the account to a Swiss bank.

30. During this period, AS purchased 190,500 shares of Sniffex, costing approximately \$450,000 and generating approximately \$21,000 in additional commissions.

31. Kirkpatrick and Harte each accepted orders for the sale of Sniffex shares from YM and AS and submitted orders for execution.

32. No registration statement covering these sales was ever filed with the Securities and Exchange Commission. At no time has Sniffex filed a registration statement for the sale of its stock, other than in connection with the Nevada 504 sales described above.

Respondents' Failure to Fulfill Their Obligations in Connection with the Sale of Unregistered Securities

33. Kirkpatrick and Harte were aware, or on notice, of the following facts concerning Sniffex and the firms' customers, YM and AS, that should have alerted them to the need to undertake a searching inquiry with regard to the customers' sales of Sniffex shares:

- a. Sniffex was a little-known development-stage company whose stock was unregistered and had only recently begun trading publicly.

- b. YM and AS each opened an account at Barron Moore and deposited millions of Sniffex shares into those accounts shortly before Sniffex began trading.
- c. YM promptly began liquidating her Sniffex shares a few days after depositing them into her Barron Moore account.
- d. YM and AS were trying to liquidate their Sniffex positions.
- e. Both YM and AS had listed incomes on their new account forms of under \$25,000, net worth of under \$50,000, and limited or no investment experience. However, each purportedly came into possession of millions of shares of stock which, within a year, was worth millions of dollars.
- f. YM and AS each bought shares costing hundreds of thousands of dollars, almost ten times their reported net worth and twenty times their reported net incomes.
- g. Despite YM's and AS's supposedly limited financial resources and lack of investing experience, both used sophisticated financial terminology and evidenced familiarity with the operation of the U.S. markets and with sophisticated market-related strategies. For example, YM sent Kirkpatrick an email referring to "Level 2 offers" and market makers, using a four letter identifier for a specific market maker, and using the abbreviation "GTC" for good 'til cancelled orders.

34. Notwithstanding these facts, Kirkpatrick and Harte sold their clients' stock without taking any steps to ascertain information necessary to determine whether their customers' unregistered Sniffex shares could be sold in compliance with Section 5 of the

Securities Act. Neither Kirkpatrick nor Harte attempted to determine if a registration statement was in effect with respect to YM's or AS's Sniffex shares, or if there was an applicable exception. Harte relied on the clearing firm as well as the issuers' transfer agent to determine if the Sniffex stock deposited by YM and AS could be sold in compliance with the registration requirements. Kirkpatrick relied on the issuers' transfer agent to determine if the Sniffex stock deposited by YM and AS could be sold.

35. Kirkpatrick and Harte also failed to review the "Incoming Stock Questionnaire" for the YM and AS accounts. That document was used by Barron Moore to obtain information from customers who deposited stock at the firm. The questionnaire included information about how, and from whom, stock was acquired, whether the customer was affiliated with the issuer or a control person, and whether or not the stock was restricted.

36. The questionnaires completed by YM and AS stated that each had purchased their shares in third party transactions. The questionnaire completed for AS's shares did not indicate from whom the shares were purchased, although the form called for that information. The questionnaire completed for YM's shares indicated that the shares were purchased from a third party non-affiliated shareholder, but did not identify that shareholder.

37. Kirkpatrick was told by YM, by email, that YM received her shares from her son, the inventor of the Sniffex device. Despite this, he made no effort to determine whether YM was affiliated with Sniffex. He also never asked AS how he acquired his shares, if he paid for the shares, if he owned other shares of Sniffex, or whether he was affiliated with Sniffex.

38. Harte also failed to make any effort to determine the source of YM's or AS's shares.

39. By virtue of the foregoing, Respondent Kirkpatrick and Harte sold unregistered securities in violation of Section 5 of the Securities Act of 1933. By doing so, they violated NASD Conduct Rule 2110 (now FINRA Rule 2010).

SECOND CAUSE OF ACTION

Supervisory Failures by Harte (Rules 3010 and 2110)

40. Paragraphs 1 through 39 are repeated and realleged herein.

41. Pursuant to Barron Moore's Supervisory and Sales Practices Manual, Patrick Harte was designated as the "second principal" of the firm and had supervisory responsibilities over the retail sales force. In addition, Harte had responsibility for accepting new accounts and for approving transactions.

42. Harte knew that Kirkpatrick's clients YM and AS had deposit Sniffex shares into their accounts, that YM had "a lot" of Sniffex shares in her account, and that YM and AS were selling shares of Sniffex. He had approved the opening of the YM and AS accounts, and so was notice of the inconsistency between their trading experience and their activity in their Barron Moore accounts. He also received copies of at least some of the customer emails, which evidenced a much higher degree of market sophistication than indicated in their new account forms.

43. Harte failed to take reasonable supervisory measures to ensure that Kirkpatrick complied with the requirements of Section 5 of the Securities Act in selling unregistered Sniffex stock on behalf of customers. For instance, he failed to take reasonable steps to require that Kirkpatrick ascertain whether the securities being sold were registered, whether the customers for whom the securities were sold had any affiliation with the issuer, how, from whom and under

what circumstances the customers obtained their shares, whether and when the shares were paid for, and whether the transactions were subject to any exemption from registration.

44. By failing to take reasonable steps to supervise Kirkpatrick in the sale of Sniffex shares, Harte violated NASD Conduct Rules 3010(a) and 2110 (now FINRA Rule 2010).

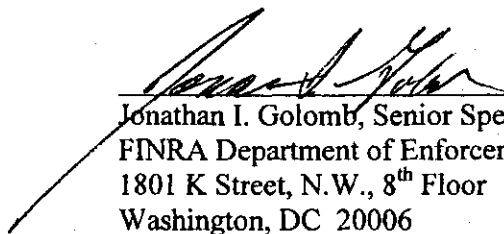
PRAYER FOR RELIEF

WHEREFORE, the Department respectfully requests that the Panel:

- A. order that one or more of the sanctions provided under Rule 8310(a) of the FINRA Procedural Code be imposed; and
- B. order that each respondent bear such costs of proceeding as are deemed fair and appropriate under the circumstances in accordance with Rule 8330 of the FINRA Code of Procedure.

FINRA DEPARTMENT OF ENFORCEMENT

Date: March 30, 2010



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Barron Moore Client	Trade Date	Quantity	Net Amount	Commission
YM	11/14/2005	50,000	\$151,861.48	\$7,995.10
YM	11/15/2005	11,000	\$33,555.20	\$1,767.00
YM	12/6/2005	14,800	\$44,082.34	\$2,321.20
YM	1/10/2006	496,500	\$1,931,406.75	\$101,671.25
YM	1/27/2006	2,000	\$3,523.73	\$186.00
YM	1/31/2006	13,500	\$27,535.77	\$1,450.25
YM	2/1/2006	125,000	\$292,966.88	\$15,424.00
YM	2/1/2006	125,000	\$292,254.38	\$15,386.50
YM	2/2/2006	5,577	\$12,174.79	\$641.36
YM	2/6/2006	4,300	\$8,624.80	\$454.50
YM	2/7/2006	16,600	\$34,123.85	\$1,797.10
YM	4/20/2006	30,000	\$19,303.37	unknown
YM	4/21/2006	40,000	\$28,488.87	unknown
YM	4/24/2006	5,000	\$3,409.51	unknown
YM	4/25/2006	13,012	\$9,187.95	unknown
AS	8/2/2005	34,000	\$80,978.12	\$4,263.75
AS	8/3/2005	52,000	\$172,995.15	\$9,107.50
AS	8/4/2005	5,500	\$20,071.69	\$1,057.00
AS	10/11/2005	1,200	\$2,554.79	\$135.00
AS	10/13/2005	23,000	\$74,951.28	\$3,946.20
AS	10/14/2005	2,000	\$6,529.56	\$340.00
AS	10/18/2005	1,000	\$3,219.78	\$170.00
AS	10/24/2005	5,000	\$14,713.98	\$775.00
AS	10/31/2005	65,100	\$202,850.90	\$10,679.27
AS	11/7/2005	70,450	\$211,896.28	\$11,155.51
AS	11/8/2005	2,000	\$6,012.58	\$317.00
AS	11/21/2005	50,000	\$155,174.04	\$8,169.45
AS	11/22/2005	20,000	\$62,371.75	\$3,284.00
AS	12/5/2005	18,250	\$54,376.58	\$2,863.13
AS	12/12/2005	2,000	\$5,879.59	\$310.00
AS	12/19/2005	20,500	\$60,940.92	\$3,208.71
AS	1/9/2006	166,522	\$521,182.33	\$27,436.96
AS	1/11/2006	199,500	\$922,567.60	\$48,564.30
AS	1/12/2006	150,000	\$503,588.30	\$26,510.48
AS	1/13/2006	6,000	\$19,026.71	\$1,002.00
AS	1/24/2006	150,000	\$320,710.40	\$8,223.75