

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

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REGISTRATION & DISCLOSURE

Department of Enforcement,

Complainant,

v.

James C. McKelvain,
CRD No. 1565890,

Respondent.

Disciplinary Proceeding
No. 20070088994

Hearing Officer: Maureen A. Delaney

**ORDER ACCEPTING OFFER OF
SETTLEMENT**

Date: January 26, 2010

INTRODUCTION

Disciplinary Proceeding No. 20070088994 was filed on July 8, 2009, by the Department of Enforcement of the Financial Industry Regulatory Authority (FINRA) (Complainant).

Respondent James C. McKelvain submitted an Offer of Settlement (Offer) to Complainant on December 28, 2009. Pursuant to FINRA Rule 9270(e), the Complainant and the National Adjudicatory Council (NAC), a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs (ODA) have accepted the uncontested Offer. Accordingly, this Order now is issued pursuant to FINRA 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, without admitting or denying the allegations of the Complaint, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to which FINRA is a party, to the entry of findings and violations consistent with the allegations of the Complaint, and to the imposition of

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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 FINRA.

BACKGROUND

Respondent entered the securities industry in 1986 as a limited registered representative with Pruco Securities Corp. and remained there until December 1991. From January 1992 through July 2007 Respondent was associated with eight FINRA member firms. Beginning in January 2007 Respondent worked as an independent contractor with Allstate Financial Services, LLC ("Allstate"). He remained in that position until his termination on July 9, 2007. Respondent is not currently employed in the securities industry but remains subject to FINRA jurisdiction pursuant to Article V, Section 4 of the NASD By-laws. Respondent has no prior disciplinary history.

In 1986, Respondent obtained his Series 6 and Series 63 securities licenses. Respondent has never held a Series 7 securities license which would permit him to engage in the solicitation, purchase and/or sale of all securities products.

On or about December 28, 2009, an Offer was executed by Respondent, pursuant to which, Respondent consented, without admitting or denying the allegations, to findings that he violated NASD Rules 3040, 1031 and 2110 by engaging in the sale of securities related to private securities transactions without being properly registered and without providing written notice to and receiving approval from his member firm employer. Additionally, Respondent consented to findings he violated NASD Rule 2110 by making negligent misrepresentations of material fact in connection to above-referenced sales of securities and violated NASD Rules 2210 and 2110 by providing customers with sales materials containing misleading descriptions of a security.

Respondent consented to a sanction consisting of (a) an eight-month suspension in all capacities; (b) a \$35,000 fine; and (c) disgorgement of \$128,177.15.

FINDINGS AND CONCLUSIONS

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

In February and March 2007, Respondent sold installment plan contracts issued by National Foundation of America ("NFOA") to four customers without first providing written notice to and receiving written approval from his member firm employer. The installment plan contracts were securities and Respondent received commissions in connection with their sale.

NFOA represented itself to the public as a charitable organization. In or about January 2006, NFOA submitted its application for Recognition of Exemption under Section 501(c)(3) of the Internal Revenue Code to the Internal Revenue Service (the "Application"). The Application remained pending until in or about December 2007, when it was denied by the Internal Revenue Service.

In connection with the above-referenced sales of the NFOA installment plan contracts, Respondent presented sales materials to the four customers which contained misleading and oversimplified descriptions of the NFOA product and negligently misrepresented to each customer that she would receive a tax deduction in connection with her investment.

Respondent has never held a Series 7 license that would permit him to engage in the solicitation, purchase and/or sale of all securities products including the NFOA product.

Sales of NFOA Installment Plan Contracts

On or about February 7, 2007, Respondent solicited and sold two installment plan contracts issued by NFOA to his customer AB. At the time, customer AB was approximately 87 years old. Pursuant to the terms of the first NFOA Installment Plan Contract signed by customer

AB, she exchanged an existing annuity with a total accumulated value of approximately \$156,873.66 for an NFOA installment plan contract which promised, after a one-year deferral period, 120 monthly installments of \$1,385.42 over a ten-year period and a tax deduction of \$41,438. The total payout over the term of the contract was represented to be approximately \$166,250.01. Pursuant to the terms of the second NFOA Installment Plan Contract signed by customer AB, she exchanged an existing annuity with an accumulated value of approximately \$542,424 for an NFOA installment plan contract which promised, after a five-year deferral period, 240 monthly installments of \$3,332.44 over a 20-year period and a tax deduction of \$199,677. The total payout over the term of the contract was represented to be approximately \$799,784.80.

On or about February 7, 2007, Respondent also solicited and sold an installment plan contract issued by NFOA to his customer VD. At the time, customer VD was approximately 75 years old. Pursuant to the terms of the NFOA Installment Plan Contract signed by customer VD, she exchanged two existing annuities with a total accumulated value of approximately \$367,319.29 for a NFOA installment plan contract which promised, after a 15-year deferral period, 15 annual installments of \$54,707.12 and a tax deduction of \$145,614. The total payout over the term of the contract was represented to be approximately \$820,606.80.

On or about February 12, 2007, Respondent solicited and sold an installment plan contract issued by NFOA to his customer LC. At the time, customer LC was approximately 83 years old. Pursuant to the terms of the NFOA Installment Plan Contract and Agreement signed by customer LC, she exchanged an existing annuity with a total accumulated value of approximately \$517,017 for a NFOA installment plan contract which promised 180 monthly

installments of \$2,424.09 over a 15-year period and a tax deduction of \$298,885. The total payout over the term of the contract was represented to be approximately \$436,336.80.

On or about March 1, 2007, Respondent solicited and sold an installment plan contract issued by NFOA to his customer ST. At the time, customer ST was approximately 70 years old. Pursuant to the terms of the NFOA Installment Plan Contract and Agreement signed by customer ST, she exchanged an existing annuity with a total accumulated value of approximately \$227,092.02 for a NFOA installment plan contract which promised, after a five-year deferral period, 180 monthly installments of \$1,758.86 over a 15-year period and a tax deduction of \$73,912. The total payout over the term of the contract was represented to be approximately \$316,594.11.

After learning of alleged improprieties by NFOA, Respondent contacted NFOA and representatives of the annuity companies who previously held his customers' annuities and attempted to rescind/reverse the transactions.

On or about June 21, 2007, the State of Tennessee placed NFOA in receivership. On or about that date, customers AB, VD, LC, and ST were notified by the State of Tennessee that NFOA had been placed in receivership. In September 2007, NFOA was placed into liquidation. Thereafter, the NFOA receiver arranged for ownership of the originally exchanged annuities to be transferred back to customers AB, LC and ST. Consequently, customers AB, LC and ST did not incur losses related to their purchase of the NFOA installment plan contracts.

The annuity transferred by customer VD had been surrendered by NFOA and thus ownership of the annuity could not be transferred back to customer VD. Customer VD submitted a claim to the Tennessee receiver, seeking the return of the principal of her NFOA investment.

Customer VD's claim was approved in the amount of \$298,237.40¹ and to date she has received disbursements from the Tennessee receiver totaling \$235,607.55 or 79% of the approved amount.²

Respondent received directly from NFOA approximately \$128,177.15 in commissions in connection with the above-referenced sales of NFOA installment plan contracts. The commission amount was consistent with the 9% commissions promised by NFOA to its sales agents.

The NFOA installment plan contracts solicited and sold by Respondent were securities. Respondent participated in the solicitation and sale of the NFOA installment plan contracts listed above without providing prior written notice to and obtaining the written approval from his member firm employer. By the foregoing conduct, Respondent violated NASD Rules 3040 and 2110.

Respondent presented NFOA-prepared illustrations to customers AB, VD, LC and ST in the course of soliciting the sales of NFOA installment plan contracts. The illustrations consisted of a series of documents including a dated cover page identifying Respondent as the presenter, an Installment Plan Flow Chart (the "Flow Chart"), and a NFOA Installment Plan 1099 Statement (the "1099 Statement") (collectively, the "Solicitation Documents"). The Flow Chart Respondent presented to customers AB, VD, LC and ST graphically depicted the terms of each customer's proposed NFOA installment plan contract. Specifically, the Flow Charts Respondent presented to customers AB, VD, LC and ST provided the total payout amount each customer

¹ The amount approved by the NFOA Receiver was based on the surrender value of the annuities as distinct from the accumulated value.

² It is anticipated that the NFOA Receiver will make additional disbursements prior to the close of the Receivership.

would receive over the life of the contract and estimated the allowable tax deduction and allowable tax savings each customer would be entitled to in connection with her investment. The Flow Charts Respondent showed to customers AB, VD and ST also represented that each would receive a total payout in excess of her initial proposed investment over the payment term.

The Flow Charts Respondent presented to customers AB, VD, LC and ST failed to reflect that the total payout amount included a return of principal, did not specify a rate of return and failed to explain the basis for any of its calculations. These omissions provided an oversimplified and exaggerated description of investment returns.

Respondent also presented a 1099 Statement to customers AB, VD, LC and ST which was specific to each customer's proposed investment. The 1099 Statements detailed the number and amount of scheduled payments that each customer would receive in exchange for the transferred asset and listed that portion of the annual payment which was to be "reported as tax free" and that portion which was to be reported as "ordinary income." The 1099 Statement column entitled "reported as tax free" created the false impression that the column represented tax-free income.

Respondent did not present the Solicitation Documents to a registered principal of his member firm employer for review and approval prior to showing them to customers in connection to his sales of the NFOA installment plan contracts. By the conduct described above, Respondent violated NASD Rules 2210(d)1(A), 2210(d)1(B), 2210(b)1 and 2110.

In soliciting the sales of NFOA installment plan contracts to customers AB, VD, LC and ST, Respondent negligently represented to each customer that she would receive a tax deduction in connection with her investment. Respondent lacked an adequate basis to make the above-referenced representations, which were not true in violation of NASD Rule 2110.

By soliciting and selling NFOA installment plan contracts that were securities, in February and March 2007 to customers AB, VD, LC and ST, Respondent acted in a capacity requiring him to be registered with FINRA as a general securities representative. During his solicitation and sales of NFOA installment plan contracts to customers, Respondent held Series 6 and 63 licenses which qualified him to act in the capacity of an Investment Company Products/Variable Products Representative and a State Uniform Securities Agent. However, Respondent has never been registered with FINRA as a general securities representative required for the solicitation, purchase and/or sale of securities products including the NFOA installment plan contracts. By the foregoing, Respondent violated NASD Rules 1031 and 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 FINRA, of its regulatory responsibility under the Securities Exchange Act of 1934.

SANCTIONS

It is ordered that Respondent be (a) suspended in all capacities for a period of eight months; (b) pay a \$35,000 fine; and (c) pay disgorgement in the amount of \$128,177.15.³

³ Payments due in connection with disgorgement of commissions shall be reduced based on proof that Respondent paid all or part of the \$128,177.15 he received in commissions to the NFOA Receiver, Customer VD or the State of Texas.

The sanctions imposed herein shall be effective on a date set by FINRA staff.

SO ORDERED.

FINRA

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

A handwritten signature in cursive script, reading "Susan Light", is written over a horizontal line.

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