

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

.....X  
Department of Enforcement, :  
Complainant : Disciplinary Proceeding  
2008013429301  
:  
v. : Hearing Officer \_\_\_\_\_  
Kim Edward Elverud :  
[CRD No. 2139216] :  
Respondent :  
.....X

The Department of Enforcement alleges:

**SUMMARY**

1. During the period from 2005 through August 2010, Kim Edward Elverud ("Elverud") was President and Chief Compliance Officer of Sumner Harrington Ltd. ("Sumner Harrington" or "the Firm"), a former FINRA registrant that withdrew its broker-dealer membership on August 5, 2010. Elverud and Sumner Harrington engaged in a broad variety of violations that enticed investors to purchase high-yield subordinated notes, while failing to provide a balanced portrait of these securities' risks. These violations, which were facilitated by extensive failures of supervision, ultimately extended to fraudulent misrepresentations, as set forth more particularly below.

000070273 2010  
000055130 2011

2. During the period from 2005 through 2009, in violation of NASD Rules 2210, 3110, and 2110, and FINRA Rule 2010,<sup>1</sup> Elverud caused the Firm to use internet advertisements, websites, and other public communications that were misleading, did not supply fair and balanced presentations of risks and rewards or failed to give a sound basis for evaluating information. Additionally, Elverud failed to approve or maintain records of public communications issued by the Firm.

3. During the period from July 2008 through December 2008, the Firm distributed a newsletter, written by Elverud about STEN Corporation ("STEN"), a company whose securities the Firm marketed. This newsletter was unduly and excessively positive, and failed to disclose material facts concerning STEN's financial difficulties, which caused the communication to be misleading, in violation of NASD Rules 2210(d)(1)(A) and 2110 and FINRA Rule 2010.

4. In October 2008, in letters on Sumner Harrington letterhead, Elverud made misrepresentations to two investors about securities issued by STEN. These letters misrepresented as a general reinvestment option the individual offers being made to keep these investors from redeeming their holdings in STEN securities, and omitted material information regarding STEN's financial difficulties, in violation of Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5, and NASD Rules 2120, 2210, and 2110.

5. During the period from in or about 2005 through January 2010, Elverud caused Firm books and records identifying personnel holding supervisory and compliance responsibilities to be inaccurate, in violation of NASD Rules 3110 and 2110 and FINRA Rule 2010.

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<sup>1</sup> Effective December 15, 2008, prior NASD Rule 2110, requiring the observance of high standards of commercial honor and just and equitable principles of trade, was renumbered as FINRA Rule 2010. Violations of this obligation, as set forth more particularly below, are charged under NASD Rule 2110 for violations before the renumbering and under FINRA Rule 2010 for violations after the renumbering.

6. In the period from January 2008 to March 2008, inclusive, Elverud caused the Firm to operate on four days – January 25, 2008, January 30, 2008, February 27, 2008, and March 28, 2008 – when it was in violation of its net capital requirements. Based on the foregoing misconduct, Elverud violated NASD Rule 2110.

#### **BACKGROUND AND JURISDICTION**

7. Sumner Harrington Ltd. was a broker-dealer with a single office in Minnetonka, Minnesota, a Minneapolis suburb. First registered in 1999 as Minnesota Investment Services Corporation, in 2001 it was acquired by, and subsequently changed its name to Sumner Harrington Ltd. On August 5, 2010, the Firm filed a Broker-Dealer Withdrawal (“BDW”) form.

8. Elverud entered the securities industry in 1991. In October 2001, he became a principal of Sumner Harrington Ltd. During all periods set forth herein, Elverud was also a principal of the Firm’s affiliates, its parent Sumner Harrington Inc., and its marketing and advertising affiliate Sumner Harrington Agency. At all relevant times, Elverud had responsibility for supervising, monitoring, and ensuring that Sumner Harrington conducted its business in compliance with all securities laws, rules and regulations.

9. Although Elverud has not been associated with a FINRA registered firm since August 5, 2010, when Sumner Harrington made its BDW filing, he remains subject to FINRA’s jurisdiction for purposes of this proceeding, pursuant to Article V, Section 4 of FINRA’s By-Laws, because the Complaint was filed within two years of the date upon which he ceased to be associated with a FINRA registered firm.

10. Sumner Harrington was a limited service broker-dealer, and participated as a best-efforts underwriter in offerings of one form of security, Renewable Subordinated Notes (“Notes”).

11. A Renewable Subordinated Note is a security that represents the promise of the issuing corporation to pay principal and interest on the note to the holder of the note. Notes are not insured, and they are subordinated to all other obligations of the issuing firm. Notes are not negotiable instruments; there is no secondary market for them; they cannot be transferred without the approval of the firm that issued them; and, with very limited exceptions, Notes cannot be redeemed before maturity unless the holder suffers death or permanent disability. Unless the holder redeems a Note upon maturity, it rolls over into a new Note. The Notes were not issued in physical form, but as book-entry obligations, with Sumner Harrington maintaining investment records on behalf of the firms issuing the Notes.

12. During the period from 2005 through 2009, Elverud caused the Firm to market Notes on behalf of four issuers: Zanett Corporation (in an offering that commenced February 7, 2005); Consumer Portfolio Services Inc. ("CPS") (in an offering that commenced May 19, 2005); Winmark Corporation (in an offering that commenced June 14, 2006); and STEN Corporation ("STEN") (in an offering that commenced April 5, 2007 and ceased on or about December 29, 2008).

#### **PRIOR DISCIPLINE**

13. In September 2004, pursuant to a Letter of Acceptance, Waiver and Consent ("AWC"), Sumner Harrington Ltd. and Elverud were disciplined by NASD (which later merged to become FINRA). NASD found that the Firm and Elverud violated several NASD Rules, including NASD Rules 2110 and 2210 cited in this Complaint. With regard to securities issued by Metris Companies ("Metris"), Elverud and the Firm violated NASD's Advertising Rules:

After Metris' senior debt rating was downgraded by Standard & Poor's and other credit agencies in December 2002, Sumner Harrington continued to place newspaper advertisements in major newspapers during the month of January 2003. Sumner Harrington also continued to distribute Investment Kits to prospective customers that

contained sales literature . . . . Neither the newspaper advertisements nor the Frequently Asked Questions portion of the Investment Kits warned the investing public that credit agencies had downgraded Metris's credit rating that the Metris notes carried more risk as a result of the downgrades and events occurring at Metris, in violation of NASD Conduct Rules 2210(d)(1)(A) and 2110.

14. The Firm's sanction included a censure, a fine of \$60,000, joint and several with Elverud, and certain regulatory undertakings, including a requirement that for nine months following the acceptance of the AWC it submit all advertisements and sales literature prepared by itself or its affiliates to the NASD Advertising Regulation Department for approval prior to distribution to the public.

15. Elverud's sanction included a suspension from any NASD registered firm in all capacities for a period of 20 days, a subsequent suspension from acting in an supervisory capacity or as a trainer of personnel with any NASD registered firm for a period of nine months, a fine of \$60,000, joint and several with the Firm, and the requirement that he re-qualify by examination as a Series 24 principal.

**FIRST CAUSE OF ACTION**

**NASD Rules 2210(d)(1)(A) and 2110 and FINRA Rule 2010 –  
Failure to make sufficient disclosure of financial events at STEN Corporation  
(August 2008 - December 2008)**

16. Enforcement realleges and incorporates by reference paragraphs 1-15 above.

17. NASD Rule 2210(d)(1)(A) provides that in all communications with the public, no member may omit any material fact or qualification if this omission would cause the communication to be misleading.

18. During the period from July 2008 through December 2008, inclusive, STEN experienced serious, continuing financial problems. In this period, STEN's main line of business was used-car sales and financing, with its operations based in Arizona.

19. Through Elverud's work in trying to locate financial assistance for STEN, and from Elverud's efforts to obtain timely payment from STEN for obligations due to Sumner Harrington or its affiliates, Elverud was aware of STEN's financial difficulties.

20. On or about August 29, 2008, Elverud approved and caused the Firm to circulate a newsletter relating to STEN. The last date on which this newsletter was distributed to investors was on or about December 20, 2008. The newsletter compared statistics from the period immediately prior to the distribution of the newsletter to statistics from similar periods a year before. These comparisons generally indicated that STEN's performance had improved. The newsletter's discussion of STEN's business prospects concluded on a series of positive notes:

During the quarter, STEN signed an agreement to sell its payday loan and check cashing businesses. That sale closed soon after the quarter ended.

Subsequent to the quarter end, STEN's senior lender increased the Company's line of credit from \$5.50 million to \$8.85 million.

Kenneth W. Brimmer, the Company's Chief Executive Officer, said, "We are pleased with the progress that we are making in all areas of our businesses.

"The continued emphasis on selling used vehicles through our company-owned sales lots will be a positive factor in our performance.

"We expect revenue our fourth quarter of fiscal 2008, ending September 28, to be equal to or greater than the quarter just ended. We also forecasting [sic] positive earnings for our fourth quarter.

"In fiscal 2009, we continue to expect our total revenue to exceed \$25 million and to generate earnings of \$.50 -\$.60 per share."

21. However, this newsletter failed to disclose facts concerning STEN's financial difficulties, which were necessary to give a balanced picture for investors. The newsletter presented insufficient risk disclosures about recent events at STEN, and the newsletter's treatment of STEN's financial state and prospects was unduly and excessively positive.

22. Elverud caused the Firm to distribute the newsletter on STEN to all customers who currently held Notes issued by STEN, who had in the past held Notes issued by STEN, and

to all customers who had previously requested sales kit information regarding STEN, approximately 8,000 investors total.

23. The newsletter omitted material information about recent financial difficulties at STEN and the resulting risks to investors which were or reasonably should have been known by Elverud.

24. By omitting material information necessary to prevent the newsletter from being misleading, Elverud thereby violated NASD Rules 2210(d)(1)(A) and 2110 and FINRA Rule 2010.

**SECOND CAUSE OF ACTION**  
**NASD Rules 2120, 2110, and IM 2310-2, and Securities Exchange Act of 1934**  
**Section 10(b) and SEC Rule 10b-5 – Misrepresentations to Customers**  
**(October 2008)**

25. Enforcement realleges and incorporates by reference paragraphs 1-24 above.

26. Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5 thereunder provide that no person shall knowingly or recklessly (a) employ devices, schemes or artifices to defraud, (b) make untrue statements of material fact or omit to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading or (c) engage in acts, practices and courses of business which operate or would operate as a fraud upon purchasers of securities.

27. NASD Rule 2120 provides that no member shall induce the purchase or sale of any security by means of any manipulative, deceptive, or other fraudulent device or contrivance.

28. NASD Rule IM-2310-2 imposes on FINRA registrants and registered representatives the responsibility for fair dealing with customers.

29. NASD Rule 2110 prohibits FINRA registrants from engaging in conduct inconsistent with just and equitable principles of trade.

30. In October 2008, STEN found that it had insufficient funds available to redeem two Notes presented that month by investors. One Note, with a principal amount of \$100,000, maturing on October 16, 2008, was held by investors EB and JB. The other Note, with a principal value of \$150,000, maturing on October 18, 2008, was held by investors WZ and LG.

31. On or about October 20, 2008, Elverud wrote and sent two letters, one letter to EB and JB and another letter to WZ and LG. On Sumner Harrington letterhead, above Elverud's signature, these letters falsely asserted that "new renewal options" for the Notes that these investors held had been put into effect.

32. Elverud wrote to these customers that "STEN just announced two new renewal options with special bonus interest rates for maturing notes with notes of principal amounts of \$25,000 or more," and set forth further details.

33. Elverud further wrote that "Even though STEN car loans carry high interest rates, loan demand is strong. The company can put to good use every dollar that it raises by selling notes to retail investors. That is why they are offering you and others these two new renewal options. . . . Thank you for your business. I apologize for not informing you about these new renewal options prior to the maturity date of your note. STEN has been crafting them for awhile but just finalized the terms today."

34. In fact, no new renewal option had in fact been announced, and this offer had not been offered to investors other than these two families.

35. Elverud knew at the time that he wrote and sent these letters that no such renewal option had been announced or offered to other investors.

36. Moreover, these letters omitted all reference to the financial difficulties that STEN was experiencing, including but not limited to an inability to meet obligations as they came due.

37. At the time that he wrote and sent these letters, Elverud knew that STEN was experiencing financial difficulties.

38. In distributing these misleading letters, which contained untrue statements of material fact and omitted to state necessary material facts, Elverud violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder.

39. In distributing these letters, which contained false or misleading statements and omissions, Elverud violated the following NASD Rules: NASD Rule 2120, which prohibits FINRA registrants from effecting any transaction in, or inducing the purchase or sale of, any security by means of any manipulative, deceptive or other fraudulent device or contrivance; NASD Rule 2110, which prohibits FINRA registrants from engaging in conduct inconsistent with just and equitable principles of trade; and NASD Rule IM-2310-2, which imposes on FINRA registrants and registered representatives the responsibility for fair dealing with customers.

#### **THIRD CAUSE OF ACTION**

**NASD Rules 2210(d)(1)(A), 2210(d)(1)(B), and 2110; Misrepresentations to Customers (October 2008)**

40. Enforcement realleges and incorporates by reference paragraphs 1-39 above.

41. NASD Rule 2211(a)(1)(A) defines "correspondence" as any written letter or electronic mail message distributed by a member to one or more existing retail customers.

42. NASD Rule 2210(d)(1)(A) provides that all member communications with the public must be based on principles of fair dealing and good faith, must be fair and balanced, and

must provide a sound basis for evaluation the facts in regard to any particular security or type of security, industry, or service, and that no member may omit any material fact or qualification if the omission, in the light of the context of the material presented, would cause the communication to be misleading.

43. NASD Rule 2210(d)(1)(B) provides that no member may make any false, exaggerated, unwarranted or misleading statement or claim in any communication with the public, and that no member may publish, circulate or distribute any public communication that the member knows or has reason to know contains any untrue statement of a material fact or is otherwise false or misleading.

44. The above letters written and sent by Elverud constituted "correspondence," as defined in NASD Rule 2211(a)(1)(A), and were therefore subject to the content standards set forth in NASD Rule 2211(d)(1), which requires compliance with NASD Rule 2210(d)(1).

45. In distributing these letters, which omitted material information regarding STEN's financial difficulties and did not provide a sound basis for evaluating the facts relating to the Notes, Elverud violated NASD Rules 2210(d)(1)(A) and 2110.

46. In distributing these letters, which contained false and misleading statements that new renewal options had been announced, Elverud violated NASD Rules 2210(d)(1)(B) and 2110.

#### **FOURTH CAUSE OF ACTION**

**NASD Rules 2210(d)(1)(A) and 2110 – Omissions of material information;  
failure to be fair and balanced; failure to provide a sound basis for evaluating  
the facts in internet marketing and search engine ads  
(May 2005 – September 2008)**

47. Enforcement realleges and incorporates by reference paragraphs 1-46 above.

48. NASD Rule 2210(d)(1)(A) provides that all member communications with the public must be based on principles of fair dealing and good faith, must be fair and balanced, and must provide a sound basis for evaluation the facts in regard to any particular security or type of security, industry, or service, and that no member may omit any material fact or qualification if the omission, in the light of the context of the material presented, would cause the communication to be misleading.

49. Elverud caused the Firm to advertise Renewable Notes on the internet, using Google ads and maintaining websites for its issuers' Note offerings. These advertisements omitted material information, were not fair and balanced, and failed to provide a sound basis for evaluating the facts with regard to the Notes.

#### Internet Advertisements

50. During the period from about 2006 through May 2008, Elverud caused the Firm to run numerous Google advertisements for Notes issued by Zanett, Winmark, STEN, and CPS. These included approximately 52 ads for Zanett, 54 ads for Winmark, 223 ads for STEN, and 161 ads for CPS.

51. As of May 29, 2008, the Zanett ads had been viewed on 2,666,759 occasions by web users, and on 13,995 occasions web users had clicked on a link in the ad that linked them to the ZanettNotes.com site.

52. As of May 29, 2008, the Winmark ads had been viewed on 713,199 occasions by web users, and on 6,899 occasions web users had clicked on a link in the ad that linked them to the WinmarkNotes.com site.

53. As of May 29, 2008, the STEN ads had been viewed on 62,244,866 occasions by web users, and on 84,962 occasions web users had clicked on a link in the ad that linked them to the StenCorpNotes.com site.

54. As of May 29, 2008, the CPS ads had been viewed on 92,588,856 occasions by web users, and on 225,373 occasions web users had clicked on a link in the ad that linked them to the CPSNotes.com site.

55. These advertisements prominently promoted Zanett, Winmark, STEN and CPS Notes on the basis of their yields (describing the Notes in such terms as "annual yields up to 12.41%", "high yield investments," "high yield notes," and "high annual yields"), but all these advertisements failed to disclose the Notes' risk, which included the potential loss of all principal. This was an omission of material information.

56. Flash advertisements are short advertisements that appear as "sponsored links" in the margin of Google pages in response to Google searches for certain terms, providing links through to advertiser's own websites. Approximately eight Flash advertisements for Notes issued by CPS, prominently promoted CPS Notes on the basis of their specific yields (advertising "Earn Annual Yields Up to 5.92%" to "Earn Annual Yields Up to 9.96%") but failed to disclose the Notes' risk, which included the potential loss of all principal. This was an omission of material information.

#### Websites

57. During the period from about May 2005 through September 2008, Elverud maintained Sumner Harrington's website, [www.sumnerharrington.com](http://www.sumnerharrington.com), that supplied information regarding the Notes marketed by the Firm, as well as identifying the issuers for

which the Firm was currently marketing Notes. As of September 25, 2008, this website stated that these Notes were "typically high yield," "commission-free," and "simple enough to manage without a broker," but failed to provide disclosure of the risks of these Notes, including lack of liquidity and the potential for the total loss of principal. Failure to disclose these risks was an omission of material information.

58. Links from the summerharrington.com website directed users to other websites that supplied information regarding the offerings of Notes issued by Winmark, CPS, STEN, and Zanett. Elverud created and approved each of these offering websites. As of September 25, 2008, these websites failed to balance the emphasis on these Notes' benefits with clear disclosure of their risks.

59. The Google ads and Flash ads that Elverud created, approved, and caused the Firm to distribute, and the Summer Harrington website that Elverud maintained, all omitted material information, and thereby failed to provide a sound basis for evaluating the facts regarding the Notes. The other website presentations that Elverud created, approved, and caused the Firm to distribute by web links were not fair and balanced, and thereby failed to provide a sound basis for evaluating the facts regarding the Notes. These actions by Elverud violated NASD Rules 2210(d)(1)(A) and 2110.

**FIFTH CAUSE OF ACTION**

**NASD Rules 2210(d)(1)(A), 2210(d)(1)(B) and 2110 and FINRA Rule 2010 –  
Omissions of material information; failure to be fair and balanced; failure to provide a  
sound basis for evaluating the facts; making exaggerated or misleading  
statements in printed communications  
(February 2005 – January 2009)**

60. Enforcement realleges and incorporates by reference paragraphs 1-59 above.

61. NASD Rule 2210(d)(1)(A) provides that all member communications with the public must be based on principles of fair dealing and good faith, must be fair and balanced, and must provide a sound basis for evaluation the facts in regard to any particular security or type of security, industry, or service, and that no member may omit any material fact or qualification if the omission, in the light of the context of the material presented, would cause the communication to be misleading.

62. NASD Rule 2210(d)(1)(B) provides that no member may make any false, exaggerated, unwarranted or misleading statement or claim in any communication with the public, and that no member may publish, circulate or distribute any public communication that the member knows or has reason to know contains any untrue statement of a material fact or is otherwise false or misleading.

63. Between about February 2005 through January 2009, numerous advertisements, letters, and other communications created and approved by Elverud and distributed by Sumner Harrington emphasized positive statements about issuers and the high returns offered by Notes, while failing to mention or adequately describe the risks of these investments. As more particularly set forth below, by distributing communications that omitted material information, were not fair and balanced, failed to provide a sound basis for evaluating the facts in regard to the securities, or made exaggerated, unwarranted or misleading statements, Elverud violated NASD Rules 2210 and 2110 and FINRA Rule 2010.

#### **Misleading Sales Kits**

64. During the periods in which issuers' individual offerings were in effect, Elverud caused the Firm to send out sales kits to customers who asked for information on investing in

Renewable Notes. These kits consisted of a self-contained brochure that described the Notes and one-page handouts, which varied by kit. Typically these included "news releases" on the issuer, issuer earnings information, available interest rates, a sheet titled "Do I Pay A Commission?" and a subscription agreement, and were also intended to include a prospectus.

65. In the period from February 7, 2005, through March 5, 2009, sales kits for Notes issued by Zanett were sent to approximately 2,240 persons. In the period from May 19, 2005 through March 5, 2009, sales kits for Notes issued by CPS were sent to approximately 13,800 persons. In the period from June 14, 2006 through March 5, 2009, sales kits for Notes issued by Winmark were sent to approximately 1,250 persons. In the period from April 5, 2007 through on or about December 29, 2009, sales kits for Notes issued by STEN were sent to approximately 8,000 persons.

66. Sales kit brochures created and approved by Elverud and distributed by the Firm for Zanett, CPS, Winmark, and STEN Notes, as of October 8, 2008, omitted material information regarding the risks of the Notes, instead referring the reader to the prospectus for such information.

67. By creating, approving, and causing the distribution of sales kits that omitted material information, Elverud distributed communications that failed to provide a sound basis for evaluating the facts regarding the Notes.

#### **Print Advertisements**

68. Numerous print advertisements for Notes issued by Zanett, STEN, CPS, and Winmark, approved by Elverud and distributed by the Firm during the period from February 2005 to November 2008, prominently presented information on the Notes' benefits, such as their

high yields. However, information on the risks of these Notes was included only as part of a block of other unrelated disclosure and disclaimer language.

69. By creating, approving, and causing the distribution of print advertisements that omitted material information, or presented such information in a way that was not fair and balanced, Elverud distributed communications that failed to provide a sound basis for evaluating the facts regarding the Notes.

#### **Mailers**

70. Mailers written and approved by Elverud and distributed by Elverud through Sumner Harrington in April through August 2008, in communicating with the public with regard to Notes issued by STEN, omitted information regarding the Notes' risk or presented such information in a manner that was not fair and balanced.

71. Two mailers for Notes issued by STEN urged that investors "lock in" a "bonus rate" or "bonus yield" on STEN Notes purchased before a specific date (April 4, 2008, and August 8, 2008, respectively). The first mailer set forth a table in which returns range from a 10.55% bonus rate on a one-year note to a 16.24% bonus yield on a three-year Note, and the second mailer set forth a table in which returns range from a 10.50% bonus rate on a one-year note to a 16.18% bonus yield on a five-year Note. Each mailer also stated that "[i]nvestments of \$25,000 or more can earn higher interest rates than those shown." However, the mailers failed to disclose the risks of these Notes. This was an omission of material information.

72. A mailer for notes issued by STEN, and approved by Elverud on June 11, 2008, offered investors the opportunity to "earn annual yields up to 15.60%." However, information

on the risks of these Notes was only included at the end of the communication, as part of a block of disclosure and disclaimer language. This presentation was not fair and balanced.

73. By creating, approving, and causing the distribution of mailers that omitted material information, or presented it in a manner that was not fair and balanced, Elverud distributed communications that failed to provide a sound basis for evaluating the facts regarding the Notes.

#### **Form Letters**

74. Form letters created and approved by Elverud, and distributed by Elverud through Sumner Harrington, in or about March 2008 and November through December 2008, concerning Notes issued by STEN and Zanett, each began with a positive earnings claim regarding the issuer of the Notes. These statements did not provide a sound basis for evaluating the significance of information contained in these communications.

75. The form letter sent to STEN customers, approved by Elverud on or about March 4, 2008, opened with the statement that "STEN recently announced . . . that it expects to be profitable this fiscal quarter ending March 31, 2008. Current quarter revenues are expected to exceed \$4.2 million, more than double the \$2.1 million in revenue the company generated in the first fiscal quarter." This letter was sent to all individuals whom Sumner Harrington listed as having contacted the Firm about purchasing a note issued by STEN or who had purchased a Note issued by STEN at any time, approximately 8,000 persons total.

76. The form letter sent to Zanett customers, and approved by Elverud on or about October 29, 2008, opened with the statement that "Zanett, Inc. recently released its 3Q 2008 results. The company enjoyed record quarterly revenue, positive net income and improved gross

credit margins. The enclosed press release has more details.” This letter was sent to all individuals who were currently listed by the Firm as having contacted the Firm about purchasing a Note issued by Zanett or who had purchased a Note issued by Zanett at any time, approximately 2,240 persons total.

77. These form letters, which Elverud created, approved, and caused to be distributed, did not provide a sound basis for evaluating the significance of these positive earnings events to an investment in the Notes.

78. Between about March 2005 through about January 2009, form letters communicating with the public with regard to “bonus rate” offers on Notes issued by Zanett, STEN, and CPS, were created and approved by Elverud and distributed by Elverud through the Firm. These form letters prominently promoted the benefits of the Notes and the urgency of the added special limited-time “bonus” rate offers. However, information regarding the risks of these Notes was only included as part of a block of disclosure and disclaimer language at the end of the communication.

79. These form letters, which Elverud created, approved, and caused to be distributed, were not fair and balanced, and thereby failed to provide a sound basis for evaluating the facts regarding the Notes.

#### **Newsletters**

80. Elverud created and approved and caused the Firm to distribute newsletters providing information on Zanett, STEN, and CPS and/or Notes issued by these companies to all individuals who had previously purchased or expressed an interest in purchasing a Note in an offering, to approximately 2,240 persons for Zanett, 8,000 persons for STEN, and 13,800

persons for CPS. These newsletters contained claims regarding the issuers' past payment histories, providing an unwarranted implication that these Notes were safe investments. Such claims are exemplified by, but are not limited, to the following:

81. "During that time the company has never missed a note interest payment or failed to redeem a note upon request at maturity" (Zanett newsletter, "Third Quarter 2008," Page 3).

82. "During that time STEN has never missed an interest payment or failed to redeem a note upon request at maturity" (STEN newsletter, "3d Quarter Fiscal 2008," Page 2).

83. "During that time CPS has never missed an interest payment or failed to redeem a note upon request" (CPS newsletter, "1<sup>st</sup> Quarter 2008 Highlights," Page 2).

84. These newsletter statements conveyed an unwarranted impression of safety.

85. These newsletters emphasized the Notes' benefits, but information on the risks of the Notes was included only as part of a block of disclosure and disclaimer language at the end of the communication.

86. The newsletters written and approved by Elverud and distributed by Sumner Harrington providing information on STEN and/or Notes issued by STEN emphasized the expectation of future positive earnings, but failed to provide the basis for such expectations. As each of these newsletters also reported losses for STEN for the current quarter, the newsletters' failure to provide the basis for predictions of better earnings in the future were omissions of material information.

87. As set forth above, by creating, approving, and distributing sales kits, print advertisements, mailers, form letters and newsletters that omitted material information, were not fair and balanced, or failed to provide a sound basis for evaluating the facts in regard to the securities, and thereby failed to provide a sound basis for evaluating the facts regarding the

Notes, Elverud violated NASD Rules 2210(d)(1)(A) and 2110 and FINRA Rule 2010. By creating, approving, and causing the distribution of newsletters that conveyed an unwarranted impression of safety, Elverud violated NASD Rules 2210(d)(1)(B) and 2110.

**SIXTH CAUSE OF ACTION**  
**NASD Rules 2210(b) and 2110, and FINRA Rule 2010 –**  
**Failure to duly approve and maintain records of public communications**  
**(June 2005 – February 2009)**

88. Enforcement realleges and incorporates by reference paragraphs 1-87 above.

89. Public communications of FINRA registered firms are required to be approved by signature or initial and date by a registered principal of the FINRA registered firm, prior to use, under NASD Rule 2210(b)(1). Under NASD Rule 2210(b)(2), these records must also be maintained in a separate file for a period of three years from the date of last use. Under NASD Rule 2210(b)(2), for each communication, the record of approval must include the name of the registered principal who approved it, the date that approval was granted, and the dates of first and (where applicable) last use. Prior to March 26, 2008, NASD Rule 2210(b)(2) required that the record of approval for each communication include the name of the principal who approved it and the date that approval was given.

90. During the period from in or about June 2005 to February 2009, with regard to public communications for Notes issued by Zanett, STEN, CPS, and Winmark, public communications were not consistently approved and records were not maintained at the Firm in the manner required by NASD Rule 2210(b). For example, certain advertisements lacked the requisite principal's signature or initials, and Elverud did not maintain a separate file containing all successive versions of sales kits and did not maintain a Firm record of the approval and use of Google advertisements. As the Firm's President and Chief Compliance Officer, and as the

individual who created, approved and maintained records regarding these advertisements, Elverud was responsible for their accuracy.

91. By failing to have public communications of the Firm approved by signature or initial by a registered principal of Sumner Harrington, and by failing to maintain records of public communications as required, Elverud violated NASD Rules 2210(b) and Rule 2110 and FINRA Rule 2010.

**SEVENTH CAUSE OF ACTION**

**NASD Rules 3110 and 2110 and FINRA Rule 2010 – Books and records inaccurately identifying personnel holding supervisory and compliance responsibilities (January 2005 – January 2010)**

92. Enforcement realleges and incorporates by reference paragraphs 1-91 above.

93. NASD Rule 3110(a) requires that member firms “make and preserve books, accounts, records, memoranda, and correspondence in conformity with all applicable laws, rules, regulations and statements of policy promulgated thereunder and with the Rules of [FINRA].”

94. NASD Rule 3010(a) provides that a FINRA registrant “shall 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 laws and regulations, and with applicable NASD Rules. Final responsibility for proper supervision shall rest with the member.” NASD Rule 3010(b) provides that a FINRA registrant shall establish, maintain and enforce written procedures to supervise the types of business in which it engages; that these shall include, in relevant part, the title and responsibilities of each supervisory person. NASD Rule 3010(b)(3) provides further that the firm “shall maintain on an internal record the names of all persons who are designated as supervisory personnel and the dates for which such designation is or was effective.”

95. NASD Rules 3013(a) and 3130 provide that each FINRA registrant "shall designate and specifically identify to FINRA on Schedule A of Form BD one or more principals to serve as a chief compliance officer."

96. The Firm's Schedule of Designated Principal Responsibilities (dated July 18, 2008) was inaccurate in that it identified the Firm's second principal, WC, as responsible for "advertising review and approval" and for "annual review of overall supervisory system of broker-dealer." In fact these supervisory functions were carried out by Elverud.

97. Between January 2005 and January 2010, eight Form BD filings made by or for Elverud, on behalf of Sumner Harrington, identified WC as Chief Compliance Officer for Sumner Harrington. These filings were made on the following dates:

- January 3, 2005 (Filing ID #14691758);
- February 14, 2005 (Filing ID #14949909);
- April 11, 2005 (Filing ID #15232164);
- April 14, 2005 (Filing ID #15247028);
- August 24, 2005 (Filing ID #15991272);
- December 22, 2009 (Filing ID #27259902);
- December 22, 2009 (Filing ID #27263192); and
- January 7, 2010 (Filing #27335937).

98. These filings were false or inaccurate in that, in fact, WC never acted as Chief Compliance Officer for the Firm, and in that the title or the responsibilities of Chief Compliance Officer were held by Elverud.

99. Elverud caused the Firm's books and records relating to the identification of personnel holding supervision and compliance responsibilities to be inaccurate, in violation of NASD Rules 3110 and 2110 and FINRA Rule 2010.

**EIGHTH CAUSE OF ACTION**  
**NASD Rule 2110 – Causing Net Capital Deficiencies**  
**(January 2008 – March 2008)**

100. Enforcement realleges and incorporates by reference paragraphs 1-99 above.

101. In the period from January 2008 through March 2008, inclusive, Sumner Harrington's calculation of net capital was inaccurate in that Elverud improperly employed an accounting practice of netting various receivables and payable items from its parent firm, Sumner Harrington, Inc., and its affiliate, Sumner Harrington Agency, in an account titled "Due from SH Inc."

102. When calculating net capital, Elverud treated the "Due from SH Inc." account as a non-allowable asset. When the "Due from SH Inc." account had a negative balance, Elverud, treated the account as a negative non-allowable asset rather than a liability. This had the effect of inaccurately reducing non-allowable items and increasing net capital.

103. SEC Rule 15c3-1 under the Securities Exchange Act of 1934 provides, generally, that every broker or dealer shall at all times have and maintain net capital no less than the greater of the highest minimum requirement applicable to its ratio requirement under paragraph (a)(1) of such section, or to any of its activities under paragraph (a)(2) of such section.

104. At all relevant times, Sumner Harrington's Membership Agreement with FINRA, dated and signed by Elverud on November 16, 2001, provided that the Firm would operate

pursuant to SEC Rule 15c3-1, and provided certain restrictions, including that the Firm would maintain minimum net capital in the amount of \$5,000.

105. Due to the inaccurate calculation of net capital by Elverud, Sumner Harrington failed to maintain adequate net capital under SEC Rule 15c3-1, on four dates between January and March 2008 on which it conducted a securities business, as set forth more particularly below:

106. On January 25, 2008, Sumner Harrington failed to maintain adequate net capital under SEC Rule 15c3-1. On this date, the Firm's computation of excess net capital was \$1,232, while in fact the Firm's excess net capital was a deficiency of \$11,431.

107. On January 30, 2008, Sumner Harrington failed to maintain adequate net capital under SEC Rule 15c3-1. On this date, the Firm's computation of excess net capital was \$14,169, while in fact the Firm's excess net capital was a deficiency of \$11,994.

108. On February 27, 2008, Sumner Harrington failed to maintain adequate net capital under SEC Rule 15c3-1. On this date, the Firm's computation of excess net capital was \$4,902, while in fact the Firm's excess net capital was a deficiency of \$8,289.

109. On March 28, 2008, Sumner Harrington failed to maintain adequate net capital under SEC Rule 15c3-1. On this date, the Firm's computation of excess net capital was a deficiency of \$28, while in fact the Firm's excess net capital was a deficiency of \$3,523.

110. Elverud's failure to prepare accurate net capital calculations caused his Firm's violations and thereby violated NASD Rule 2110.

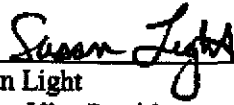
#### **PRAYER FOR RELIEF**

WHEREFORE, the Department respectfully requests that the Panel:

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

**FINRA DEPARTMENT OF ENFORCEMENT**

Date: September 28, 2010



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