

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

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

MALLESWARA RAO TUTHIKA
(CRD No. 5131117),

Respondent.

Disciplinary Proceeding
No. 2008014242401

Hearing Officer – LBB

DEFAULT DECISION

Dated: July 26, 2011

Respondent exercised discretion in customers' accounts without written customer authorization, and without approval of the account as discretionary by his firm, in violation of NASD Conduct Rules 2510 and 2110. Respondent also recommended and executed unsuitable mutual fund switch transactions, in violation of NASD Conduct Rules 2310 and 2110, and IM-2310-2. For these violations, Respondent is barred from associating with any member firm in any capacity.

Appearances

Richard S. Schultz, Esq., Senior Regional Counsel, Chicago, Illinois, for the Department of Enforcement.

Malleswara Rao Tuthika, *pro se*.

DECISION

On September 14, 2010, the Department of Enforcement ("Enforcement") filed the three-cause Complaint in this disciplinary proceeding against Respondent Malleswara Rao Tuthika ("Respondent"). The First Cause of Action charges Respondent with exercising discretion in a customer's account without written customer authorization or approval by his firm, in violation of NASD Conduct Rules 2510 and 2110. The Second and Third Causes of Action charge

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Respondent with recommending unsuitable mutual fund switching transactions in customer accounts, in violation of NASD Conduct Rules 2310 and 2110, and IM-2310-2(b)(3).¹

After failing to file a timely answer the Complaint, Respondent sent an e-mail to the Office of Hearing Officers, asserting that he did not have sufficient information to admit or deny the allegations in the Complaint. Respondent subsequently failed to appear for several pre-hearing conferences and failed to respond to an Order to Show Cause. Accordingly, at the final pre-hearing conference of May 24, 2011, the Hearing Officer held that Respondent was in default, and directed Enforcement to file documentation supporting the entry of a default decision.

The Department of Enforcement filed a Motion for Entry of Default Decision on June 29, 2011, to which Respondent did not respond. Pursuant to FINRA Procedural Rules 9241 and 9269, Respondent has defaulted, and the allegations of the Complaint are deemed admitted.

I. Respondent

Respondent was registered as a general securities representative with FINRA member firm Ameriprise Financial Services, Inc. ("Ameriprise") from October 2006 until his employment was terminated on June 24, 2008. On September 18, 2008, Ameriprise filed an amended Form U5, disclosing a customer complaint. Complaint ¶ 2; Decl. 5; CX-4.² Although Respondent was not registered with a FINRA member firm at the time of the filing of the

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 consolidated 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, which were in effect at the time of each alleged violation. The applicable rules are available at www.finra.org/rules.

² The factual determinations in this decision are based on the allegations of the attached Complaint and the materials Enforcement filed with its default motion, which included the Declaration Supporting a Motion for the Entry of a Default Decision, and supporting documentation that was attached to counsel's declaration. Counsel's declaration was marked by Enforcement as CX-1, and is cited herein as "Decl. ¶ ____."

Complaint, he is subject to FINRA's jurisdiction for purposes of this proceeding, pursuant to Article V, Section 4(a)(i) of FINRA's By-Laws, because the Complaint was filed within two years after the filing of an amended Form U5 that discloses that Respondent may have engaged in conduct actionable under applicable statutes, rules, or regulations.

II. Procedural History and Respondent's Default

On September 14, 2010, Enforcement filed the Complaint, and served the Notice of Complaint and Complaint on Respondent at his residential address as listed in the Central Registration Depository ("CRD address"). Respondent failed to answer, and Enforcement served the Notice of Complaint, Complaint, and Second Notice of Complaint on Respondent on October 13, 2010. Apparently in response, Respondent sent a letter to Enforcement dated November 11, 2010, explaining why he would not agree to resolve the matter by consenting to a letter of Acceptance, Waiver and Consent. Enforcement filed the letter with the Office of Hearing Officers on November 18, 2010.

Pursuant to order, a pre-hearing conference was conducted on December 2, 2010, at which Respondent represented that he was seeking counsel and requested an extension of time to answer the Complaint. Enforcement consented to the request, which was granted by Order of December 6, 2010. The Order directed Respondent to file an answer that conformed to the requirements of FINRA Procedural Rule 9215 on or before January 3, 2011. On January 3, 2011, Respondent, continuing to appear *pro se*, submitted a brief e-mail response to the Complaint to the Office of Hearing Officers, stating that he had not retained counsel and that he did not have sufficient information to admit or deny the allegations of the Complaint.

A pre-hearing conference was held on January 20, 2011, at which Respondent failed to appear. A second pre-hearing conference was held on January 28, 2011, at which the parties

agreed upon a hearing schedule. The Hearing Officer issued a Scheduling and Procedures Order on February 7, 2011. On March 17, 2011, the Hearing Officer issued an Order Setting Pre-Hearing Conference for March 24. This order was served on Respondent at his CRD address by first-class mail, and was also served by e-mail. The pre-hearing conference was held on March 24, 2011, at which Respondent failed to appear. On March 25, 2011, the Hearing Officer issued an Order Setting Pre-Hearing Conference, setting a pre-hearing conference for April 1. This order was sent to the Respondent's CRD address by first-class mail, and was served by e-mail. A pre-hearing conference was held on April 1, 2011, at which Respondent failed to appear.³

An Order to Show Cause was issued on May 6, 2011, directing Respondent to show cause, by May 23, 2011, why he should not be defaulted. Also on May 6, 2011, the Hearing Officer issued an order notifying the parties of the final pre-hearing conference on May 24, 2011, as set forth in the Scheduling and Procedures Order. Respondent failed to respond to the Order to Show Cause, and failed to appear at the final pre-hearing conference on May 24. At the pre-hearing conference, the Hearing Officer cancelled the hearing and held that Respondent was in default. By Order of May 25, 2011, the Hearing Officer directed Enforcement to file supporting documentation for the entry of a default decision by June 30, 2011.

On June 29, 2011, Enforcement filed a Motion for Entry of Default Decision. Due to Respondent's repeated failures to attend pre-hearing conferences despite receiving constructive notice, including failure to attend the final pre-hearing conference despite receiving actual notice, and failure to respond to the Order to Show Cause, Respondent has defaulted, pursuant to

³ The Case Administrator and counsel for Enforcement made multiple unsuccessful attempts to contact Respondent by e-mail, voicemail, telephone, and mail. Respondent did not respond to any of these attempts after January 28, 2011.

FINRA Procedural Rules 9241 and 9269. Pursuant to Procedural Rule 9269, the allegations of the Complaint are deemed admitted.

III. First Cause of Action: Respondent Violated NASD Conduct Rules 2510 and 2110 by Exercising Discretion in Customers' Accounts Without Written Customer Authorization or Acceptance of the Account as Discretionary by Respondent's Firm

NASD Conduct Rule 2510(b) provides:

No member or registered representative shall exercise any discretionary power in a customer's account unless such customer has given prior written authorization to a stated individual or individuals and the account has been accepted by the member, as evidenced in writing by the member or the partner, officer or manager, duly designated by the member, in accordance with Rule 3010.

From approximately October 2007 until December 2007, Respondent effected approximately 150 discretionary transactions in equity securities in the account of customer J.B. without obtaining prior written authorization from J.B. or prior written acceptance of the account as discretionary by Ameriprise. Complaint ¶ 4; Decl. ¶ 7. Ameriprise did not permit the exercise of discretion in customer accounts. Decl. ¶ 7(a).

From approximately January 2008 until March 2008, Respondent exercised discretion in the account of customer B.I., investing \$284,000 in 27 mutual funds from 13 different fund families. Respondent executed these transactions without obtaining prior written authorization for discretionary trading from B.I. or prior acceptance of the account by Ameriprise as discretionary. Complaint ¶ 5; Decl. ¶ 7.

In February and March 2008, Respondent executed discretionary transactions in the account of N.B., investing \$74,000 in 34 mutual funds from 16 mutual fund families. Respondent executed these transactions without obtaining prior written authorization for discretionary trading from N.B. or prior acceptance of the account by Ameriprise as discretionary. Complaint ¶ 6; Decl. ¶ 7.

The allegations of the Complaint, which are deemed admitted, are sufficient to establish, for the purposes of this Default Decision, that Respondent violated NASD Conduct Rules 2510 and 2110 by exercising discretion in customers' accounts without receiving prior written authorization from the customers or prior approval of the accounts as discretionary by his firm.⁴

IV. Second and Third Causes of Action: Respondent Violated NASD Conduct Rules 2310 and 2110, and IM-2310-2, by Recommending and Executing Unsuitable Mutual Fund Switches in Customer Accounts

A. A Pattern of Mutual Fund Switch Transactions May Violate NASD Conduct Rules 2310 and 2110, and IM-2310-2

NASD Conduct Rule 2310 requires that, before making a recommendation to a customer, a representative "shall have reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts, if any, disclosed by such customer as to his other security holdings and as to his financial situation and needs." In IM-2310-2, the Board of Governors made it clear that mutual fund shares "normally ... are not proper trading vehicles" and that trading in mutual fund shares "on its face may raise the question of Rule violation."

A pattern of mutual fund switching is a presumptive violation of NASD Rules.⁵ "'A pattern of switches from one fund to another by several customers of a registered representative, where there is no indication of a change in the investment objectives of the customers and where new sales loads are incurred, is not reconcilable with the concept of suitability.' Where such a pattern is established, it is incumbent upon the registered representative that recommended such

⁴ A violation of NASD Conduct Rule 2510 is also a violation of NASD Conduct Rule 2110. *Dep't of Enforcement v. Merhi*, No. E072004044201, 2007 NASD Discip. LEXIS 9, at *33, n.20 (N.A.C. Feb. 16, 2007); *see also*, *Kirlin Sec.*, Exchange Act Rel. No. 61135, 2009 SEC LEXIS 4168, at *59-60, n.81 (Dec. 10, 2009).

⁵ *Dep't of Enforcement v. Respondent*, No. C07010037, 2003 NASD Discip. LEXIS 16, at *22-23 (N.A.C. May 13, 2003).

switches to demonstrate the unusual circumstances which justified what is a clear departure from the manner in which mutual fund investments are normally made.”⁶

B. Second Cause of Action: Respondent Violated NASD Conduct Rules 2310 and 2110, and IM-2310-2, by Recommending and Executing Unsuitable Mutual Fund Switches in Customer B.I.’s Account

From January 2008 until March 2008, Respondent liquidated Class A mutual fund shares in the account of B.I., and invested \$284,000 from B.I.’s account in Class B shares of 27 mutual funds from 13 mutual fund families. Complaint ¶ 10; Decl. ¶ 9. Respondent executed the transactions in B.I.’s account without having reasonable grounds to believe that the transactions were suitable for B.I., in view of the nature of the recommended transactions, and in light of B.I.’s financial situation, investment objectives, circumstances and needs. The purchase of Class B mutual fund shares in B.I.’s account deprived B.I. of savings in fees and expenses that B.I. could have obtained if Respondent had purchased Class A shares of mutual funds within the same family of funds or from fewer fund families. Complaint ¶ 11; Decl. ¶ 9.

The allegations in the Complaint, which are deemed admitted, are sufficient to establish that Respondent violated NASD Conduct Rules 2310 and 2110, and IM-2310-2 by recommending and executing unsuitable mutual fund switches in the account of customer B.I.

C. Third Cause of Action: Respondent Violated NASD Conduct Rules 2310 and 2110, and IM-2310-2, by Recommending and Executing Unsuitable Mutual Fund Switches in Customer N.B.’s Account

In February 2008 and March 2008, Respondent executed transactions in the account of N.B., selling Class A shares of mutual funds and subsequently investing approximately \$74,000 in Class B shares of 34 different mutual funds from 16 fund families. Respondent executed the transactions in N.B.’s account without having reasonable grounds to believe that the transactions

⁶ *Dep’t of Enforcement v. Epstein*, No. C9B040098, 2007 FINRA Discip. LEXIS 18, at *67 (N.A.C. Dec. 20, 2007), *aff’d*, 2009 SEC LEXIS 217 (Jan. 30, 2009).

were suitable for N.B., in view of the nature of the recommended transactions, and in light of N.B.'s financial situation, investment objectives, circumstances, and needs. The purchase of Class B shares of mutual funds deprived N.B. of savings in fees and expenses that N.B. could have obtained if he had purchased Class A shares within the same family of funds or from fewer fund families. Complaint ¶ 16; Decl. ¶ 12.

The allegations in the Complaint, which are deemed admitted, are sufficient to establish that Respondent violated NASD Conduct Rules 2310 and 2110, and IM-2310-2 by recommending and executing unsuitable mutual fund switches in the account of customer N.B.

V. Sanctions

Enforcement argues for a bar for the unsuitable trading, and a separate bar for the exercise of discretion without written authority. Respondent's violations are interrelated – he exercised discretion without written authority in order to execute the unsuitable mutual fund switch transactions and make other trades in the accounts of three customers. Because Respondent's violations "stem from a single source," it is appropriate to impose a "single, unitary sanction."⁷ A bar is imposed as the sanction for the three causes of action.

For unsuitable recommendations, the Sanction Guidelines recommend a fine of \$2,500 to \$75,000, and a suspension for a period of 10 business days to one year. In egregious cases, the Guidelines recommend consideration of a longer suspension or a bar.⁸

This is an egregious case. Respondent engaged in a pattern of switches.⁹ Respondent's clients were injured by the switches, which caused his clients to incur unnecessary fees and

⁷ *Dep't of Enforcement v. Braff*, No. 2007011937001, 2011 FINRA Discip. LEXIS 7 (N.A.C. May 13, 2011), (currently identified on LEXIS as 2011 NASD Discip. LEXIS 7), *appeal docketed*, SEC Dkt. No. 3-14417 (June 9, 2011).

⁸ *FINRA Sanction Guidelines* at 96 (2011) ("Guidelines").

⁹ *Sanction Guidelines*, Principal Consideration No. 8.

expenses.¹⁰ Respondent profited from his improper trading, receiving \$9,344 in total commissions. Decl. ¶ 7(j).

Respondent has never accepted responsibility for his violations.¹¹ While Respondent admits that he recommended all of the switching transactions, he has not acknowledged that the transactions might have been improper. Rather, he has cited the decline in the stock market as a whole as the cause of customer dissatisfaction and frustration. Decl. ¶ 13; CX-2, CX-3.

The fact that the switches were done on a discretionary basis without authorization from the customers or approval of the accounts as discretionary by Respondent's firm, and Respondent's improper exercises of discretion in trading equities in the account of customer J.B., supports the imposition of a substantial sanction.¹² The principal considerations for improper exercises of discretion are: 1) "Whether customer's grant of discretion was express or implied;" and 2) "Whether firm's policies and/or procedures prohibited discretionary trading and/or whether the firm prohibited the respondent from exercising discretion in customer accounts."

Respondent's improper exercise of discretion was egregious. He had not received an express or implied grant of discretion for any of the accounts. See Decl. ¶ 7(c). There were a large number of discretionary trades. As noted above, Respondent executed approximately 150 discretionary trades in equities, in addition to the discretionary mutual fund switch transactions. Ameriprise's policies prohibited discretionary trading, and Respondent did not notify Ameriprise that he was engaging in discretionary trading.

¹⁰ *Sanction Guidelines*, Principal Consideration No. 11.

¹¹ *Sanction Guidelines*, Principal Consideration No. 2.

¹² For exercising discretion without a customer's written authorization, the *Sanction Guidelines* recommend a fine of \$2,500 to \$10,000. The *Guidelines* recommend consideration of a suspension in any or all capacities for 10 to 30 business days in egregious cases. *Sanction Guidelines* at 87.

Respondent's conduct was egregious. A bar is the appropriate sanction.¹³

VI. Conclusion

For exercising discretion in customer accounts without written customer authorization or approval of the account as discretionary by Respondent's firm, in violation of NASD Conduct Rules 2510 and 2110, and recommending and executing unsuitable mutual fund switch transactions, in violation of NASD Conduct Rules 2310 and 2110, and IM-2310-2, Respondent Malleswara Rao Tuthika is barred from associating with any member firm in any capacity.

The bar will become effective immediately if this decision becomes FINRA's final disciplinary action in this proceeding.



Lawrence B. Bernard
Hearing Officer

Copies to: Malleswara Rao Tuthika (*via overnight courier and first-class mail*)
Pamela Shu, Esq. (*via e-mail and first-class mail*)
Richard Schultz, Esq. (*via e-mail and first-class mail*)
Mark P. Dauer, Esq. (*via e-mail*)
David R. Sonnenberg, Esq. (*via e-mail*)

¹³ Enforcement does not seek restitution, and restitution is not appropriate because Ameriprise has settled with the customers. Motion at 4; Decl. ¶ 7(i).