

RECEIVED
2009 JUL 27 P 7 09
STRATEGIC & DISCLOSURE

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2008015730901**

TO: Department of Enforcement
Financial Industry Regulatory Authority ("FINRA")

RE: Kenneth George Neely, Respondent
CRD No. 1586038

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Respondent Kenneth G. Neely, submits this Letter of Acceptance, Waiver and Consent ("AWC") for the purpose of proposing a settlement of the alleged rule violations described below. This AWC is submitted on the condition that, if accepted, FINRA will not bring any future actions against Respondent alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

- A. Respondent hereby accepts and consents, without admitting or denying the findings, 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, prior to a hearing and without an adjudication of any issue of law or fact, to the entry of the following findings by FINRA:

BACKGROUND

Respondent became registered as a General Securities Representative on January 17, 1987 and was registered in that capacity with Merrill Lynch, Pierce, Fenner & Smith, Inc., a FINRA member, until August 24, 1989. From that point forward, Respondent was a registered representative with several FINRA members including Edward D. Jones & Co., Inc. (September 5, 1989 to February 21, 1997), Prudential Securities, Inc. (February 21, 1997 to June 18, 1999), UBS PaineWebber, Inc. (June 18, 1999 to October 4, 2002), Stifel, Nicolaus & Co., Inc. (October 4, 2002 to January 12, 2007), and AXA Advisors, LLC ("AXA") (August 14, 2007 to July 8, 2009). AXA terminated Respondent on July 8, 2009 based upon his admission to FINRA staff that he converted customer funds for his personal use. Respondent currently is not registered with a FINRA member and he has no relevant disciplinary history.

OVERVIEW

From June 2001 to June 2009 (the "relevant period"), Respondent conducted an elaborate Ponzi scheme, fraudulently inducing at least 25 customers, family, friends and fellow church members (the "investors") to participate in a fictitious "St. Louis Investment Club" and to invest in an equally fictitious real estate investment trust, the "St. Charles REIT." To conceal the scheme

000085209 2009

from his employers and federal and state tax authorities, Respondent typically had the investors make payments to his wife or to himself, often in \$2,000 or \$3,000 increments so that Respondent could immediately convert the funds to cash. Respondent promised high rates of return and in some cases falsely assured his investors that their investment would be carefully handled because he was on the investment club's Board of Directors. For most investors, Respondent prepared on his personal computer a document that falsely represented to clients an ownership interest in the St. Louis Investment Club. The document, which was the only written acknowledgment of the investors' contributions, included the legend "invoice" on some versions, but Respondent and customers often referred to the document as a "certificate." Respondent used the invested funds, totaling over \$600,000 during the relevant period, to pay "investment returns" or to make principal payments to other defrauded investors and to pay for his lavish personal lifestyle, including entertainment expenses at his country club, sometimes totaling over \$4,000 a month. Respondent only stopped collecting money for the scheme from his investors when FINRA staff confronted him about the fictitious REIT in July 2009.

Respondent's conduct in furthering his Ponzi scheme constitutes separate and distinct violations of Section 10(b) of the Securities Exchange Act of 1934, SEC Rule 10b-5 and NASD Conduct Rules 2120 (fraudulent misrepresentations and omissions of material fact to customers); 2330(a) (improper use and conversion of customer funds), 2110 (misstatements to his employers concerning his Ponzi scheme), 3040 (private securities transactions without prior written notice and receiving prior written approval), 3030 (engaging in outside business activities without notifying his employers), 3110 (inaccurate books and records) and 2110.

FACTS AND VIOLATIVE CONDUCT

Respondent's Ponzi Scheme – St. Louis Investment Club

By mid-2001, while Respondent was working at UBS PaineWebber, he began to struggle professionally and to experience financial difficulties. His income from brokerage services at UBS PaineWebber dwindled dramatically from approximately \$150,000 in 2000 to approximately \$30,000 in 2002. Accordingly, during this time, it became increasingly difficult for Respondent to cover his personal expenses, including mortgage and credit card debt, country club membership dues and entertainment costs which, in some cases, Respondent incurred by paying for dinners and rounds of drinks for gatherings of clients, friends, guests and acquaintances at his country club and other venues.

It was during this period of personal financial stress that Respondent conceived and effected his Ponzi scheme. He invented the fictitious St. Louis Investment Club intending to lure clients to invest in the equally fictitious St. Charles REIT with the promise of up to 20 percent returns on the strength of the then booming real estate market. Respondent also induced clients to invest by telling them that there were limited opportunities to join the exclusive investment club, and that, as a member of investment club's Board of Directors, he could ensure the success of the investments. Respondent selected \$3,000 as the minimum investment unit in the REIT to avoid scrutiny by the issuing banks when he would cash the investment checks. To avoid detection by employers and tax authorities, Respondent in some cases had his clients pay for the fictitious REIT units in checks made payable to his wife or to himself, which he either deposited in a joint checking account or immediately converted to cash. On at least one occasion in 2005,

Respondent had an investor deliver a check intended for investment in the St. Charles REIT to his office at the broker-dealer, which was intercepted by broker-dealer personnel. When confronted by his Branch Manager, Respondent falsely stated that the check was for the purchase of a car which he had sold to the investor.

To foster the impression that the St. Louis Investment Club and the St. Charles REIT were part of a legitimate enterprise, Respondent prepared false invoices on fictitious St. Louis Investment Club letterhead which he created at home using his personal computer. Most of Respondent's investors received some version of these false REIT invoices. On these invoices, "A.J. O'Brien" is represented as the investment club's President and "Carol Thomas" as the investment club's Secretary, even though neither one of these individuals exists in these positions or any other in the investment club. On the initial invoices, Respondent listed his mother's home address as the address of the St. Louis Investment Club. Respondent later replaced his mother's home address with his own. At no time did Respondent ever disclose any of these activities to any of his employers. Respondent prepared the false REIT invoices using the following format:

<i>St. Louis Investment Club</i>	
St. Charles "REITS"	
Start Date 01/01/1995	End Date 12/31/2008
Unit Value and minimum investment = \$3,000.00 Monthly Income from sales of properties per unit = \$25.00	
<u>(One (1) Year Revision to \$50.00 per unit effective 03/10/2007)</u>	
Member: FB & RB JTWROS Dated December 1, 1998 Member Number [REDACTED]	
Received Last Additional Dues: February 10, 2006 Total \$66,000.00 Total Units Purchased 22	
New Monthly Income Starts March 10, 2006 Ends December 31, 2008 Effective March 1, 2006 New Total per Month = \$550.00	
<u>Taxes and fees will be paid by the St. Louis Investment Club on April 1st of each tax year</u> <u>Meetings on the third Wednesday of each month for all board Members</u> <u>Premature return of dues will be returned via written request, within ninety (90) days after request is received to:</u> <u>Carol Thomas, Secretary, [123 Main St., St. Louis, MO]</u>	
A.J. O'Brien President	
Carol Thomas Secretary	
<i>Invoice</i>	

Throughout the relevant period, Respondent fraudulently induced the investors to invest a total of over \$600,000 in the fictitious St. Charles REIT and converted over half of this amount to his personal use. Respondent used the investors' investment funds to make return payments to existing and subsequent investors, which in every case were made either in cash or cashier's check, and to cover the costs of his lavish personal lifestyle, including mortgage and credit card payments, his country club membership dues and extravagant entertainment bills that sometimes exceeded \$4,000 a month. Respondent did not declare any of the investor's REIT payments on his federal or state income tax returns.

In furthering his Ponzi scheme, Respondent targeted investors who were his customers at the broker-dealers where he worked during the relevant period and for whom he had already provided investment services. The following investors are representative:

Respondent's Cousin

The first victim of Respondent's Ponzi scheme was a member of his family. In mid-2001, Respondent's cousin, LJ, turned to him for advice concerning the disposition of over \$100,000 which she had recently inherited from her father. Respondent recommended that his cousin diversify her investment and helped her place funds in variable annuities, stocks and the fictitious St. Charles REIT. Respondent persuaded his cousin to invest approximately \$30,000 in the St. Charles REIT, promising returns of up to 10 percent on her investments. He did not provide his cousin with an invoice or any other documentation concerning this investment. Respondent converted his cousin's entire investment in the St. Charles REIT for his personal use to pay down his various debts and to support the Ponzi scheme.

Respondent's Fellow Church Members

Respondent also misappropriated funds from fellow church members. Sometime in 2001, when Respondent was working at UBS PaineWebber, Respondent approached FB, a friend and fellow church member, regarding investing in the St. Charles REIT. Respondent promised FB a high rate of return because the St. Louis Investment Club specialized in "flipping properties," which was a lucrative proposition during the then booming real estate market. To further encourage FB to invest in the St. Charles REIT, Respondent misrepresented to FB that he was on the investment club's Board of Directors and from that position could help safeguard FB's investment. To help convince FB that the investment was legitimate, Respondent provided FB with a false "invoice" similar to the example in this document. Based on these representations, Respondent induced FB to invest a total of \$66,000. For a period of time, Respondent paid FB what he represented were small monthly returns of \$100 to \$500 in cash. Respondent, however, eventually converted over \$36,000 of FB's investment for his personal use to pay down debts and to support the Ponzi scheme.

Respondent also misappropriated \$154,000 from RS, a long-time friend and an additional \$10,000 from RS's daughter, LS. Respondent began managing RS's investments in 2002, shortly after RS retired. By mid-2007, Respondent desperately needed funds to pay returns to some of his defrauded clients who were "demanding large chunks of money." Accordingly, Respondent decided to approach RS regarding investing in the St. Charles REIT. Describing the investment as "tax free," Respondent also promised RS a high rate of return on the investment.

Based on these representations, Respondent induced RS to invest a significant percentage of his retirement assets, approximately \$154,000, in the St. Charles REIT. Shortly thereafter, respondent induced LS to invest \$10,000 in the St. Charles REIT that she intended to use for purchasing a home. Over time, Respondent repeatedly failed to provide both RS and LS with requested information concerning the investment. Although Respondent paid back RS a total of \$10,000 and LS a total of \$3,500, he converted the balance of their investments to pay down his various debts, including his extravagant country club and golf expenses.

In another typical case, Respondent defrauded SM, also a long-time friend and fellow church member, misappropriating approximately \$35,000 of SM's retirement funds. Respondent had been managing SM's investments since 2002, shortly after SM retired. Respondent induced SM to invest in the St. Charles REIT by promising a 5 percent rate of return, superior to what SM could hope to receive by investing in a money market account, and by telling SM he could withdraw the funds whenever he liked. Respondent also emphasized the exclusivity of the St. Louis Investment Club, telling SM that it was limited to a discrete number of members. Respondent promised SM that when "openings" in the investment club occurred, he would contact SM and invite him to invest. Over time, whenever Respondent needed ready funds, he would call SM and tell him about new openings. Based on these representations, Respondent induced SM to make incremental investments, usually in the amount of \$3,000 or \$6,000, in the St. Charles REIT. At the outset, Respondent would pay SM small returns of \$100 in cash, usually at SM's home, but these payments began to dwindle until they stopped altogether. Respondent misappropriated approximately \$35,000 of SM's investment, converting the funds to his personal use to pay down his debts and to support the Ponzi scheme.

Accordingly, based on the conduct described above, Respondent willfully made a series of fraudulent misrepresentations to customers to induce these customers to invest in the fictitious St. Charles REIT in violation of Section 10(b) of the Securities Exchange Act of 1934, SEC Rule 10b-5 and NASD Conduct Rule 2120; improperly used and converted customer funds in violation of NASD Conduct Rule 2330(a); made material misstatements to his employers regarding his Ponzi scheme in violation of NASD Conduct Rule 2110; engaged in private securities transactions without prior written notice and receiving prior written approval from his employers in violation of NASD Conduct Rule 3040; engaged in outside business activities without notifying his employers in violation of NASD Conduct Rule 3030; and caused AXA to maintain inaccurate books and records in violation of NASD Conduct Rule 3110. Respondent's violations also constitute a separate violation of NASD Conduct Rule 2110.

- B. Respondent also consents to the imposition of a bar from associating with any FINRA member in all capacities.

Respondent understands that if he is barred or suspended from associating with any FINRA member, he becomes subject to a statutory disqualification as that term is defined in Section 3(a)(39) of the Securities Exchange Act of 1934, as amended. Accordingly, he may not be associated with any FINRA member in any capacity, including clerical or ministerial functions, during the period of the bar or suspension (*see* FINRA Rules 8310 and 8311). The sanctions imposed herein shall be effective on a date set by FINRA staff. Pursuant to FINRA Rule 8313(e), a bar or expulsion shall become effective upon approval or acceptance of this AWC.

II.

WAIVER OF PROCEDURAL RIGHTS

Respondent specifically and voluntarily waives the following rights granted under FINRA's Code of Procedure:

- A. To have a Complaint issued specifying the allegations against him;
- B. To be notified of the Complaint and have the opportunity to answer the allegations in writing;
- C. To defend against the allegations in a disciplinary hearing before a hearing panel, to have a written record of the hearing made and to have a written decision issued; and
- D. To appeal any such decision to the National Adjudicatory Council ("NAC") and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, Respondent specifically and voluntarily waives any right to claim bias or prejudgment of the General Counsel, the NAC, or any member of the NAC, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including acceptance or rejection of this AWC.

Respondent further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of FINRA Rule 9143 or the separation of functions prohibitions of FINRA Rule 9144, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including its acceptance or rejection.

III.

OTHER MATTERS

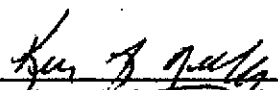
Respondent understands that:

- A. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by the NAC, a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs ("ODA"), pursuant to FINRA Rule 9216;
- B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against Respondent; and
- C. If accepted:

1. This AWC will become part of Respondent's permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against him;
2. This AWC will be made available through FINRA's public disclosure program in response to public inquiries about Respondent's disciplinary record;
3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with FINRA Rule 8313; and
4. Respondent may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. Respondent may not take any position in any proceeding brought by or on behalf of FINRA, or to which FINRA is a party, that is inconsistent with any part of this AWC. Nothing in this provision affects Respondent's right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.

Respondent certifies that he has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that he has agreed to its provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce him to submit it.

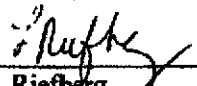
7-21-09
Date


Kenneth G. Neely, Respondent

Accepted by FINRA

7-23-09
Date

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


Linda S. Riefberg
Vice President, Chief Counsel
FINRA Department of Enforcement
14 Wall Street
New York, NY 10005
646-315-7395