BEFORE THE NATIONAL ADJUDICATORY COUNCIL

FINANCIAL INDUSTRY REGULATORY AUTHORITY

In the Matter of Department of Enforcement, Complainant, vs. The Dratel Group, Inc. Southold, NY, and William M. Dratel Southold, NY, Respondents.	DECISION Complaint No. 2009016317701 Dated: May 6, 2015

Respondent William M. Dratel willfully failed to make timely amendments to his Form U4, failed to establish and enforce supervisory control systems, and failed to certify compliance and supervisory processes. Respondent Dratel Group, Inc. failed to report municipal securities trades and executed customer transactions in corporate debt securities without completing a TRACE participation agreement and failed to report transactions to TRACE. Respondents William M. Dratel and The Dratel Group, Inc. willfully failed to make timely amendments to the firm's Form BD, willfully failed to create and preserve order memoranda, failed to preserve e-mail communications, and failed to maintain accurate ledger and trial balances. Respondents William M. Dratel and The Dratel Group, Inc. also shared in the losses in customer accounts, executed municipal securities transactions without being registered with the MSRB, and failed to have a registered municipal securities principal supervise municipal securities activities. Held, findings and sanctions affirmed.

Appearances

For the Complainant: Leo F. Orenstein, Esq., and Samuel Barkin, Esq., Department of Enforcement, Financial Industry Regulatory Authority

For the Respondents: Pro Se

Decision

William M. Dratel ("Dratel"), The Dratel Group, Inc. ("DGI") (together "respondents"), and FINRA's Department of Enforcement ("Enforcement") each appeal a September 19, 2013 Amended Hearing Panel decision pursuant to FINRA Rule 9311. The Hearing Panel found that Dratel willfully failed to make timely amendments to his Uniform Application for Securities Industry Registration or Transfer ("Form U4"), failed to establish and enforce supervisory control systems, and failed to certify compliance and supervisory processes; that DGI failed to report municipal securities trades and executed customer transactions in corporate debt securities without completing a Trade Reporting and Compliance Engine ("TRACE") participation agreement and failed to report transactions to TRACE; and that respondents willfully failed to make timely amendments to DGI's Uniform Application for Broker-Dealer Registration ("Form BD"), willfully failed to create and preserve order memoranda, failed to preserve e-mail communications, failed to maintain accurate ledger and trial balances, shared in customers' losses, executed municipal securities transactions without being registered with the Municipal Securities Rulemaking Board ("MSRB"), and failed to have a registered municipal securities principal supervise municipal securities activities.[1]

After an independent review of the record, we affirm each of the Hearing Panel's findings and sanctions and fine Dratel individually $5,000 and suspend him for a total of 25 business days, fine DGI $2,500, and fine respondents, jointly and severally, a total of $31,000.

I. Background

Dratel's father formed DGI, a FINRA member firm, in 1980. Dratel entered the securities industry in January 1977 and joined DGI in March 1980. Dratel was registered with DGI as a general securities representative and principal, an equity trader limited representative, a financial and operations principal, a registered options principal, an operations professional, and a general securities sales supervisor. Beginning in August 1999, Dratel was the sole owner of DGI, and he has operated the firm under a waiver of the two-principal requirement since 2002. DGI employed two unregistered individuals to assist Dratel and perform administrative and clerical tasks, but Dratel was the sole registered representative.

DGI operated out of two offices. Its main office, where Dratel worked primarily, was originally located in East Hampton, New York, and relocated to Southold, New York in 2009. DGI's only branch office, where the firm's two unregistered staff members worked, was located on Broad Street in New York City until 2012. Neither Dratel nor the firm is currently in the industry.

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[1] The conduct rules that apply in this case are those that existed at the time of the conduct at issue.

II. Procedural History

On October 11, 2011, the Department of Enforcement filed an 11-cause complaint against Dratel and DGI. A hearing was held on August 28-29, 2012. The Hearing Panel issued its amended decision on September 19, 2013, finding that Dratel willfully failed to make timely amendments to his Form U4, failed to establish and enforce supervisory control systems, and failed to certify compliance and supervisory processes; that DGI failed to report municipal securities trades and executed customer transactions in corporate debt securities without completing a TRACE participation agreement and failed to report transactions to TRACE; and that respondents willfully failed to make timely amendments to the firm's Form BD, willfully failed to create and preserve order memoranda, failed to preserve e-mail communications, failed to maintain accurate ledger and trial balances, shared in customers' losses, executed municipal securities transactions without being registered with the MSRB, and failed to have a registered municipal securities principal supervise municipal securities activities.

The Hearing Panel fined Dratel $5,000 and suspended him for a total of 25 business days, fined DGI $2,500, and fined respondents, jointly and severally, a total of $31,000.[2] The Hearing Panel also determined that respondents were subject to statutory disqualification for their willful failures to make timely amendments to Forms U4 (Dratel) and BD (respondents).

Respondents and Enforcement appealed.

III. Findings of Fact and Conclusions of Law

This disciplinary matter arises out of FINRA's findings during DGI's 2009 and 2010 annual examinations. FINRA examiners orally communicated to Dratel, and the examination reports enumerated, numerous exceptions, some of which became the subject of this disciplinary action. Respondents generally stipulate to the facts and acknowledge the deficiencies, but argue that most of the violations were less significant rule violations that should not have been charged in a formal complaint.

A. Causes One and Two – Respondents' Failure to Amend Forms U4 and BD

The Hearing Panel found that Dratel willfully failed to make timely amendments to his Form U4 and respondents collectively failed to make timely amendments DGI's Form BD, in violation of FINRA By-Laws Art. IV § 1(c), Art. V § 2(c), and FINRA Rules 1122 and 2010.[3] The Hearing Panel also determined that respondents are subject to statutory disqualification.

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[2] These amounts represent the total suspension and fines for respondents for all causes of action.

[3] It is well settled that a violation of another FINRA rule is a violation of FINRA Rule 2010. *See William J. Murphy*, Exchange Act Release No. 69923, 2013 SEC LEXIS 1933, at *26

[Footnote continued on next page]

We affirm the Hearing Panel's findings.

1. Facts

a. Federal Tax Liens

On March 23, 2010, the Internal Revenue Service ("IRS") sent Dratel a letter notifying him that it had filed a lien against him for $291,342.41 for unpaid income taxes for 2007 and 2008. Dratel admits that he received the notice, but testified that he could not recall precisely when.[4] While Dratel acknowledged that he looked at the notice, he stated that he did not pay particular attention to it because he believed he was in the process of resolving his lien issues with the IRS. Dratel testified that he hired an accountant to assist him with the resolution of the liens. Dratel claimed that in the discussions with the IRS, the accountant made no mention of tax liens or judgments. Dratel testified that he began making payments to the IRS in June 2010.

On September 13, 2010, the IRS sent Dratel a "Final Notice of Intent to Levy and Notice of Your Right to Hearing" for unpaid income taxes for 2009. Several days later, on September 21, 2010, the IRS filed a second tax lien against Dratel for $123,368.59. Dratel admits he received notice of the lien by at least late September. Nonetheless, he claimed that he did not realize that the second federal tax lien had actually been filed. Dratel contends that he was not aware of the liens until FINRA informed him of their existence in late September 2010.

b. New York State Tax Judgments

On September 10, 2009, the New York State Department of Tax and Finance issued a tax warrant for the entry of a judgment in the amount of $42,487.84 against Dratel for outstanding 2006 and 2007 state taxes. The state sent the warrant to the office address Dratel had maintained in East Hampton until October 2009. Dratel testified that he does not recall when he received the warrant, but believes he first saw it in late 2010 when a FINRA information request prompted him to search through his records. By that time, Dratel had already entered into an installment payment plan with the state. Dratel contends the state employees with whom he negotiated the installment plan never mentioned that the warrant was in fact a judgment, such that it would trigger his reporting obligations.

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(July 2, 2013), *aff'd sub nom. Birkelbach v. SEC*, 751 F.3d 472 (11th Cir. 2014) (noting that the violation of another Commission or FINRA rule or regulation constitutes a violation of FINRA Rule 2010).

[4] During his testimony at the hearing, Dratel identified a notation he made on the envelope containing the notice "4/5/10," which, according to Dratel, could have been April or May of 2010.

On April 19, 2010, New York state tax authorities issued a notice to Dratel of a second state tax warrant, which had been issued on February 22, 2010, in the amount of $31,061.38, for his 2008 taxes. The warrant explicitly stated that it was a money judgment against him that would be in effect for 20 years, unless Dratel paid it in full. The tax authorities sent the notice and warrant to Dratel's East Hampton address, but it was several months after he had moved to Southold. Dratel acknowledged that he eventually received the warrant, but could not recall when.

c. Bank Judgment

On March 13, 2009, American Express filed a civil complaint against Dratel and DGI for failure to pay their credit card bills. An affidavit of service certifies that the complaint was served on a "John Smith," described as Dratel's co-worker, at DGI's East Hampton address on April 13, 2009. Dratel testified that he was not served, and that he had no co-worker named John Smith. The unanswered complaint resulted in a default judgment against respondents jointly in the amount of $85,333.83 on December 14, 2009. Another affidavit of service attests to the mailing of a copy of the judgment to the East Hampton address on January 6, 2010, but this was several months after DGI had moved from East Hampton to Southold. Dratel testified that while he endeavored to enter into a payment plan with American Express, he was not aware that a judgment had been entered against respondents until FINRA provided him copies of the relevant documents.

2. Dratel Updates Forms U4 and BD

Dratel testified that on or around September 22 or 23, 2010, during the 2010 FINRA examination, FINRA examiners gave him a copy of the American Express judgment and informed him orally of the existence of the other judgments and liens. Dratel testified that this was his first notice of the outstanding liens and judgments. He claimed that as soon as he realized FINRA wanted him to disclose them, he did so; however, Dratel did not amend his Form U4 and DGI's Form BD until January 25, 2011— four months later.

3. Discussion

FINRA Rule 1122 provides that "[n]o member or person associated with a member shall file with FINRA information with respect to membership or registration which is incomplete or inaccurate so as to be misleading, or which could in any way tend to mislead, or fail to correct such filing after notice thereof," thereby requiring that members and associated persons keep Forms U4 and BD complete and accurate.

In turn, Article V, Section 2(c) of the FINRA By-Laws requires member firms and associated persons to report certain disclosable events on Forms U4 and to keep the form

updated and accurate. The By-Laws further require that certain reportable events be reported accurately no later than 30 days after the member firm learns of the facts or circumstances giving rise to a reportable event.[5] Filing a misleading Form U4 or failing to file a timely amendment to a Form U4 when required, violates the high standards of commercial honor and just and equitable principles of trade to which FINRA holds its members under FINRA Rule 2010. *See Jason A. Craig*, Exchange Act Release No. 59137, 2008 SEC LEXIS 2844, at *8 (Dec. 22, 2008). Similarly, Article IV, Section 1(c) of the FINRA By-Laws requires that member firms update their membership applications within 30 days of learning of changes required to be disclosed on Form BD.[6]

Dratel argues that because he was negotiating, or had negotiated, payment plans for his outstanding liens and judgments, he reasonably believed he was not required to disclose them. He also notes that he never received a copy of the American Express judgment because it was sent to a former address. Dratel also contends that once FINRA informed him that the judgments and liens needed to be disclosed, he did so. However, it is undisputed that respondents did not update the relevant forms until four months after the FINRA examiner questioned Dratel about the judgments and liens—well in excess of the By-Laws requirements for a timely amendment. Therefore, we find that Dratel failed to amend his Form U4 and DGI, acting through Dratel, failed to amend its Form BD, to disclose the respective liens and judgments, in violation of FINRA Rules 1122 and 2010.

a. Respondents are Statutorily Disqualified

A person is subject to a statutory disqualification under Article III, Section 4 of FINRA's By-Laws and Section 3(a)(39)(F) of the Securities Exchange Act of 1934 ("Exchange Act") if he, among other things:

> has willfully made or caused to be made in any application for membership or participation in, or to become associated with a member of, a self-regulatory organization, report required to be filed with a self-regulatory organization, or proceeding before a self-regulatory organization, any statement which was at the time, and in the light of the circumstances under which it was made, false or misleading with respect to any material fact, or has omitted to state in any such

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5 Question 14M on the Form U4 asked: "Do you have any unsatisfied judgments or liens against you?" The General Instructions for Form U4 state that "[a]n individual is under a continuing obligation to amend and update information required by Form U4 as changes occur."

6 Question 11K on the Form BD asks "Does the applicant have any unsatisfied judgments or liens against it?" The General Instructions for Form BD state that "[b]y law, the applicant must promptly update Form BD information by submitting amendments whenever the information on file becomes incomplete for any reason."

application, report, or proceeding any material fact which is required to be stated therein.

15 U.S.C. § 78c(a)(39)(F).

The Hearing Panel determined that respondents are subject to statutory disqualification for their failures to update Dratel's Form U4 and DGI's Form BD promptly because respondents' failure to disclose the judgments and liens were willful and constituted material information. Respondents argue that while they do not deny the existence of the liens and judgments, their failures to disclose were not willful and that the information was not material. We disagree.

(1) Respondents' Failures to Disclose Were Willful

We agree with the Hearing Panel that respondents' failures to disclose the judgments and liens were willful. In order to find a willful violation of federal securities laws we must find "that the person charged with the duty knows what he is doing." *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000). We need not find that respondents intentionally violated FINRA rules, only that respondents knew what they were doing when they did not timely amend the forms to disclose the judgment and tax liens. *See Mathis v. SEC*, 671 F.3d 210, 216-218 (2d Cir. 2012) (finding that respondent was statutorily disqualified where he voluntarily failed to amend Form U4 to disclose tax liens). Here, the record demonstrates conclusively that respondents knew about the judgment and liens, yet they failed to amend the Forms U4 and BD for at least four months. Thus, our finding that they acted willfully is predicated on respondents' intent to commit the act that constitutes the violation—failing to amend the forms. Dratel acknowledged that he received notice of one of the federal tax liens as early as April 2010. He also discussed the judgments and liens and his duty to amend his Form U4 with a FINRA examiner in September 2010. At best, respondents did not amend these forms for another four months even though they were required to do so within 30 days.

Even though Dratel has made these admissions, respondents argue that their failures to disclose were not willful. Respondents maintain that they did not know of the liens and judgments because Dratel was talking with his accountant and the various creditors, and none of them mentioned that there were any liens or judgments outstanding or perfected. This is belied by the fact that Dratel admits that he was aware of their existence by, at the very latest, September 2010. Furthermore, respondents cannot shift their disclosure obligations to their accountant or their creditors. *See Craig*, 2008 SEC LEXIS 2844, at *15 (noting that respondent could not shift his disclosure responsibility). Respondents had an affirmative responsibility to ensure that they made full, accurate, and timely disclosures of the reportable events on the Forms U4 and BD. Respondents therefore acted willfully.

(2) The Information Was Material

Having found that respondents acted willfully, we turn next to the question of whether the federal and state tax liens and the American Express judgment were material for purposes of disclosure on Dratel's Form U4 and respondents' Form BD respectively. Dratel argues that the judgments and liens were not material because none of his customers called to inquire about them nor did they complain about them or withdraw their accounts once the information was

reported. Therefore, Dratel maintains, the information could not have been material. However, whether customers raised concerns over the information is not the standard for determining materiality.

"[B]ecause of the importance that the industry places on full and accurate disclosure of information required by the Form U4, [it is presumed] that essentially all the information that is reportable on the Form U4 is material." *Dep't of Enforcement v. Tucker*, Complaint No. 2007009981201, 2011 FINRA Discip. LEXIS 66, at *20-21 (FINRA NAC Oct. 4, 2011) (*quoting Dep't of Enforcement v. Knight*, Complaint No. C10020060, 2004 NASD Discip. LEXIS 5, at *13 (NASD NAC Apr. 27, 2004)), *aff'd*, Exchange Act Release No. 68210, 2012 SEC LEXIS 3496 (Nov. 9, 2012), *appeal dismissed*, No. 13-31 (2d Cir. Sept. 24, 2013). Similarly, the Commission notes that:

> The principal purpose of this Form [BD] is to permit the Commission to determine whether the *applicant* meets the statutory requirement to engage in the securities business. The Form also is used by *applicants* to register as broker-dealers with certain *self-regulatory organizations* and all of the states. The Commission and the Financial Industry Regulatory Authority, Inc. maintain the files of the information on this Form and will make the information publicly available.[7]

In this case, the materiality of information about the judgments and liens are particularly evident because the disclosure of such information was required by specific questions on the Form U4 and the Form BD. *See Joseph S. Amundsen*, Exchange Act Release No. 69406, 2013 SEC LEXIS 1148, at *41 (Apr. 18, 2013), *aff'd*, 575 F. App'x 1 (D.C. Cir. 2014). Moreover, "the judgments, bankruptcies, and liens [respondents] failed to disclose . . . constituted serious financial problems critical to evaluating his fitness to associate in the securities industry." *Robert D. Tucker*, Exchange Act Release No. 68210, 2012 SEC LEXIS 3496, at *32 (Nov. 9, 2012). We further find that respondents' failure to disclose the judgment and liens significantly altered the total mix of information available. Therefore, this information constituted material information that should have been disclosed timely on Dratel's Form U4 and DGI's Form BD.

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Because we find that respondents willfully failed to disclose material information on Dratel's Form U4 and DGI's Form BD, respondents are statutorily disqualified.

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[7] *See* Uniform Application for Broker Dealer Registration, https://www.sec.gov/about/forms/formbd.pdf.

B. Cause Three – Respondents' Willful Failure to Create and Preserve Order Memoranda

The Hearing Panel found that respondents failed to create and preserve order memoranda in violation of NASD Rule 3110, FINRA Rule 2010, Exchange Act § 17(a), and Exchange Act Rules 17a-3(a)(6)-(7) and 17a-4(b)(1). The Hearing Panel also found these violations willful. We agree with these findings.

1. Facts

DGI's trade blotter reflected that between January 2009 and December 2010 there were approximately 275 trades with errors that related to trades that Dratel executed in DGI's riskless principal account for his discretionary customers or for his personal account that he then cancelled or rebilled to DGI's error account. FINRA examiners asked Dratel about these trades during the 2010 examination and followed up with a FINRA Rule 8210 request in March 2011, asking DGI to produce all records relating to error account transactions from January 2009 to September 2010. Dratel responded that he was unable to do so because he had thrown away the tickets reflecting the erroneous trades, and neither Dratel nor DGI had maintained any other record of the details of trades placed in the error account. Dratel testified that, relying on customer account statements, he could reconstruct the various reasons the trades were erroneous. He was familiar with the details of many of the trades and offered explanations for the errors. Most involved day trades in which he testified that he exceeded his buying power, buying when he had insufficient funds to pay for the orders. On other occasions, misunderstandings with customers about their instructions caused him to journal purchases from customer accounts into the error account.

2. Discussion

Exchange Act § 17(a)(1) requires members and associated persons to create and maintain records of business operations in conformity with SEC rules.[8] SEC rules mandate that FINRA member firms create and maintain records, including memoranda of orders and purchases and sales for a minimum of three years. *See* Exchange Act Rule 17a-4(b)(1). NASD Rule 3110(a) states that FINRA members must make and preserve books, accounts, records, memoranda, and correspondence in conformity with all rules and regulations, as prescribed by Exchange Act Rule

[8] Exchange Act Rule 17a-3(a)(6) requires members and associated persons to create and maintain a "memorandum of each brokerage order, and of any other instruction, given or received for the purchase or sale of securities, whether executed or unexecuted." Exchange Act Rule 17a-3(a)(7) requires members and associated persons to create and maintain "[a] memorandum of each purchase and sale for the account of the member, broker, or dealer showing the price and, to the extent feasible, the time of execution."

17a-3.[9] NASD Rule 3110(j) requires that before any customer order is executed, the name or designation of the account for which the order is to be executed must be placed on the order ticket. In prior decisions, we have held that associated persons who create inaccurate books violate NASD Rules 3110 and 2110 by causing their firms to violate Exchange Act Rule 17a-3. *See Dep't of Enforcement v. Cohen*, Complaint No. EAF0400630001, 2010 FINRA Discip. LEXIS 12, at *35 (FINRA NAC Aug. 18, 2010), *aff'd sub nom. Dennis S. Kaminsky*, Exchange Act Release No. 65347, 2011 SEC LEXIS 3225 (Sept. 16, 2011). In this respect, we followed Commission precedent. *See Davrey Fin. Servs., Inc.*, 58 S.E.C. 474, 481 (2005). A failure to create and maintain order memoranda constitutes a violation of NASD Rule 3110 and FINRA Rule 2010. *Dep't of Enforcement v. Brokaw*, Complaint No. 2007007792902, 2012 FINRA Discip. LEXIS 53, at *52-53 (FINRA NAC Sept. 14, 2012), *aff'd*, Exchange Act Release No. 70883, 2013 SEC LEXIS 3583 (Nov. 15, 2013); *Dep't of Enforcement v. Correro*, Complaint No. E102004083702, 2008 FINRA Discip. LEXIS 29, at *12-14 (FINRA NAC Aug. 12, 2008).

When FINRA examiners asked Dratel to produce the order memoranda and allocation instructions designating the customers for whom the trades were intended before they were placed in the error account from January 2009 to September 7, 2010, he was unable to do so. Respondents had not maintained any record of the details of trades placed in the error account. Dratel testified that, relying on customer account statements, he could reconstruct the various reasons the trades were erroneous. Dratel argued below and on appeal that the fact that he was able to explain most of the trades in this manner indicates that he "did document essential facts that he relied upon to cancel and rebill." We, like the Hearing Panel, disagree. Dratel's ability to give a post-trade explanation of the record of the error does not satisfy the memoranda requirements of NASD Rules 3110(a) and (j). The record establishes that respondents executed approximately 275 trades and then cancelled and rebilled them to DGI's error account without preparing and preserving order memoranda designating the customer accounts for which the trades were originally intended. Respondents failed to document the essential facts Dratel relied upon to cancel and rebill, in violation of SEC, NASD, and FINRA rules.

We also agree with the Hearing Panel that respondents' misconduct was willful.[10] The term "willful" need not connote that respondents intended to violate FINRA and Commission rules and federal statutes. *See Arthur Lipper Corp. v. SEC*, 547 F.2d 171, 180 (2d Cir. 1976)

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[9] Although NASD Rule 3110 establishes specific requirements for member firms, not registered individuals, FINRA Rule 0140 (formerly NASD Rule 0115) indicates that all of FINRA's rules shall apply equally to members and associated persons and that associated persons shall have the same duties and obligations as member firms.

[10] Although not discussed in the Hearing Panel Decision, respondents' willful violation of the Exchange Act serves as a disqualifying event pursuant to Section 3(a)(39) of the Exchange Act, 15 U.S.C §78c(a)(39), noting that a person or entity is subject to statutory disqualification if he has willfully violated the Exchange Act.

(holding that the term "willfully" does not require proof of evil intent). "A willful violation under the federal securities laws simply means 'that the person charged with the duty knows what he is doing.'" *Tucker*, 2012 SEC LEXIS 3496, at *41 (*citing Wonsover*, 205 F.3d at 414). Dratel was an experienced member of the securities industry and a registered principal. He is presumed to have known and understood the rules and laws that govern this industry. *Carter v. SEC*, 726 F.2d 472, 474 (9th Cir. 1983). Furthermore, Dratel admitted that he did not maintain the order memoranda as required by law. Based on Dratel's conduct, we therefore find that respondents acted willfully.

C. Cause Four – Respondents' Failure to Preserve E-mail Communications

The Hearing Panel found that Dratel failed to preserve e-mail communications, in violation of NASD Rule 3110, FINRA Rule 2010, Exchange Act §17(a), and Exchange Act Rule 17a-4(b)(2), but that this failure was not willful. We affirm the Hearing Panel's findings.

1. Facts

In November 2008, respondents contracted with a third-party provider, Smarsh, Inc., to manage DGI's e-mail services and to archive the firm's e-mail as required by SEC rules. However, because of a malfunction, the system did not archive most of DGI's e-mails. Smarsh notified Dratel of the malfunction on December 22, 2008, by e-mail. The message warned that the failure to archive would result in compliance issues. Dratel testified that when he received this message, he instructed one of his employees to contact Smarsh to resolve the problem. The employee reported back to Dratel that the problem had been corrected. Because Dratel was able to send and receive e-mails as before, continued to be billed for the services, and heard nothing further about the issue from Smarsh, he testified that he assumed the issue had been resolved. However, Dratel did not seek independent confirmation that the system was properly archiving e-mails. When asked if he checked the disks purportedly containing the archived e-mails provided monthly by Smarsh, Dratel answered that he looked at some of them. He noticed that they contained only a few e-mails, but thought nothing of it since he used e-mail infrequently.

On July 27, 2009, Dratel received another message from Smarsh about the problem, with the subject line "e-mails not being archived for dratelgroup.com." Around the same time, in response to a FINRA request for his e-mails, Dratel asked Smarsh to provide him a disk containing all of his e-mails from February 1, 2009, through April 30, 2009. When he reviewed the disk and saw how few e-mails it contained, he realized there was a continuing malfunction. Dratel resolved the problem by early August 2009.

2. Discussion

A member firm's responsibility to retain electronic records such as e-mails relating to its business is well-established. *See NASD Notice to Members 03-33*, 2003 NASD LEXIS 40, at *7 (June 2003); *Dep't of Enforcement v. Legacy Trading Co.*, Complaint No. 2005000879302, 2009 FINRA Discip. LEXIS 12, at *54-55 (FINRA Hearing Panel Mar. 12, 2009), *aff'd*, 2010 FINRA Discip. LEXIS 20 (FINRA NAC Oct. 8, 2010). Section 17(a)(1) of the Exchange Act requires broker-dealers to "make and keep for prescribed periods" such records as the SEC prescribes by

rule as necessary or in the public interest. Under Exchange Act Rule 17a-4(b)(4), broker-dealers are required to "preserve for a period of not less than three years, the first two years in an easily accessible place . . . [o]riginals of all communications received and copies of all communications sent . . . by the member, broker or dealer (including inter-office memoranda and communications) relating to its business as such." NASD Rule 3110, in turn, requires its members to preserve records in accordance with the SEC's rule. Electronic communications fall within the purview of NASD Rule 3110, and failing to preserve e-mails relating to a broker-dealer's business violates the rule. *See Legacy Trading Co.*, 2009 FINRA Discip. LEXIS 12, at *54-55 (failure to preserve e-mails).

Enforcement's complaint alleged that respondents willfully failed to preserve messages sent from and received by DGI's e-mail domain for nine months, from December 2008 through August 2009. We, like the Hearing Panel, find that the undisputed facts instruct us that respondents' failures to preserve e-mails were inadvertent, and therefore not willful. Smarsh alerted Dratel that there was a problem with the e-mail archive system; Dratel was assured by an employee that the issue had been resolved, and there was no apparent evidence that would have indicated that the archiving problem persisted. In addition, it is not clear that even if Dratel would have been more diligent in reviewing each monthly disk he would have been made aware of the problem since he used e-mail so infrequently. Thus, although respondents are liable, their violation was technical in nature and did not rise to a willful failure to preserve e-mail.

D. Cause Five – Respondents Shared Customers' Losses

The Hearing Panel found that respondents shared customers' losses, in violation of NASD Rules 2330 and 2110, and FINRA Rules 2150 and 2010. We affirm the Hearing Panel's findings.

1. Facts

From January 2008 through February 2011, Dratel paid a total of $156,575 to a select group of customers. Dratel admits making the payments, but denies he did so to compensate the customers for losses. While denying that the payments were compensation for his customers' losses, Dratel admitted that, as their money manager, he felt responsible for the losses inflicted upon them by adverse market conditions beginning in 2007. He insisted that he paid them because of their long-standing relationships with both Dratel and his father before him, and because it was the right thing to do.[11] He paid some customers when their accounts shrank to a

[11] From January 2008 until June 30, 2009, Dratel paid 15 customers from DGI's account, with some customers receiving as little as $25 and others receiving as much as $1,000 monthly. All told, the 15 customers received DGI funds totaling $31,075.83. In 2009, according to Dratel, a FINRA examiner informed him that he should not be paying customers through the firm. He then started paying them from his personal checking account. From June 2009 until February

[Footnote continued on next page]

level that would not permit them to make their regular monthly withdrawals; he paid others to cover margin calls. Dratel testified that he did not pay the customers to retain their business because most of their accounts were inactive. Although other customers suffered similar or greater losses during the same period, Dratel testified he did not feel obliged to pay them because he did not manage their money, or they were not accustomed to taking monthly withdrawals, or because they had not been close friends of his father.

2. Discussion

NASD Rule 2330(f) and FINRA Rule 2150 prohibit members from sharing "directly or indirectly in the profits or losses in any account of a customer" except under certain defined circumstances.[12]

Despite Dratel's denial that he shared customer losses, by his own admission respondents paid a small group of elderly customers who suffered a reduction of their profits beginning in 2007 out of a sense of loyalty. Accordingly, we affirm the findings that respondents violated NASD Rules 2330 and 2110 and FINRA Rules 2150 and 2010.

E. Cause Six – Respondents Executed Municipal Securities Transactions Without Being Registered with MSRB and Without a Registered Municipal Securities Principal

The Hearing Panel found that respondents engaged in municipal securities transactions while DGI was not registered with MSRB, and while the firm lacked a registered municipal securities principal, in violation of MSRB Rules G-2 and G-3. We affirm these findings.

1. Facts

Dratel testified that DGI had been registered with MSRB from 1980 to 2000, but he let the registration lapse because he had stopped trading municipal bonds. In February 2009, he resumed purchasing municipal bonds. From February through May 2009, while DGI was not

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2011, Dratel made additional monthly payments to six customers in amounts ranging from $1,000 to $3,000, for a total of $125,500.84.

[12] These defined circumstances include when an associated person obtains prior written authorization from the member firm as well as the customer, and shares in the profits or losses in any account of such customer only in direct proportion to the financial contributions made to such account, or is an immediate family member. Respondents do not maintain that these circumstances are applicable here.

registered with the MSRB and had no registered municipal securities principal, DGI and Dratel executed at least 23 municipal securities transactions.[13] Dratel testified that it initially did not occur to him that DGI's MSRB registration had lapsed, but eventually realized that because he was doing municipal bond trading DGI should again be registered, and that the firm needed to acquire a qualified Series 53 registered municipal securities principal. Dratel testified that he immediately acted to rectify these deficiencies. In April, he arranged for an employee to take the Series 53 qualification examination, which she passed in June 2009. DGI registered with MSRB on May 18, 2009, before its annual FINRA examination.

2. Discussion

MSRB Rule G-2 prohibits any broker or dealer from engaging in any municipal securities transaction without being qualified pursuant to the requirements of the MSRB. MSRB Rule G-3 requires firms with fewer than 11 associated persons to have at least one qualified municipal securities principal.

The Hearing Panel found, and respondents do not dispute, that they executed municipal securities transactions from February through May 2009, when DGI was not registered with the MSRB and had no registered municipal securities principal. Dratel testified that he immediately acted to rectify these deficiencies. Although they self-corrected, respondents engaged in municipal securities transactions while DGI was not registered with MSRB, and while the firm lacked a registered municipal securities principal, in violation of MSRB Rules G-2 and G-3.

F. Cause Seven – DGI Failed to Report Municipal Securities Transactions to MSRB

The Hearing Panel found that DGI violated MSRB Rule G-14 when it failed to report municipal securities transactions as required by the rule, and we affirm.

1. Facts

MSRB Rule G-14 requires that municipal securities dealers report to MSRB information about each purchase and sale transaction effected in municipal securities to the Real Time Transaction Reporting System ("RTRS") in the manner prescribed by the rule's procedures and the RTRS Users Manual. The manual, in turn, requires municipal securities dealers to report transactions to RTRS, in most instances, within 15 minutes of each transaction. Dratel testified that prior to 2000, when DGI had been registered with MSRB, RTRS did not yet exist. He learned of the necessity of acquiring an interface and filing a form with RTRS when he contacted

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[13] Dratel contends that DGI failed to report only five trades. However, we need not resolve the number of trades since Dratel has admitted to the violations and we do not find the number of trades material to our analysis.

the MSRB to register DGI, as discussed above. In July 2009, he satisfied the rule's requirements, prior to the firm's annual examination.

After FINRA's 2009 annual examination, FINRA staff informed Dratel that DGI failed to report the 23 municipal bond trades to MSRB, failed to file a required form with RTRS, and failed to test its ability to interface with RTRS, in violation of MSRB Rule G-14.

2. Discussion

As neither Dratel nor the firm disputes that DGI failed to report municipal bond trades, we affirm the Hearing Panel's findings. Dratel testified that prior to 2000, when DGI had been registered with MSRB, RTRS did not yet exist. He learned of the necessity of acquiring an interface and filing a form with RTRS when he contacted the MSRB to register DGI anew in May 2009. In July 2009, he satisfied these requirements. Therefore, we find that DGI's failures constituted a violation of MSRB Rule G-14.

G. Cause Eight – DGI Failed to Report Corporate Bond Trades to TRACE

The Hearing Panel found that DGI failed to report customer transactions in corporate bonds to TRACE, in violation of FINRA Rules 6720, 6230, and 2010. We affirm.

1. Facts

From March 3 through May 5, 2009, DGI executed 38 customer transactions in corporate bonds that should have been, but were not, reported to TRACE.[14] However, these trades were not reported because DGI had not completed a TRACE participation agreement. Dratel testified that prior to the transactions in March 2009, DGI's last previous corporate bond trade took place in or around 2002 which was, Dratel testified, prior to the implementation of the TRACE program. He was thus unaware that DGI needed to be a TRACE participant and to report corporate bond transactions to TRACE. DGI engaged in corporate bond trades through a number of firms before his clearing firm informed Dratel in or about May 2009 that DGI needed to execute a TRACE participation agreement. He executed an agreement shortly thereafter in June 2009.

2. Discussion

FINRA Rule 6720 states that member participation in TRACE for trade reporting purposes is mandatory and requires members to execute a TRACE participation agreement.

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[14] TRACE is the FINRA-developed vehicle that facilitates the mandatory reporting of over-the-counter secondary market transactions in eligible fixed income securities.

FINRA Rule 6730 requires members to report to TRACE each transaction in TRACE-eligible securities, such as corporate debt securities, within 15 minutes of execution.

Dratel admits that DGI executed 38 customer transactions in corporate bonds that should have been reported to TRACE. He testified that prior to the transactions in March 2009, DGI's last previous corporate bond trade took place in or around 2002, which was before TRACE existed. He engaged in corporate bond trades through a number of firms before his clearing firm informed him that DGI needed to execute a TRACE participation agreement. Dratel testified that he execute a TRACE agreement shortly thereafter, in June 2009. The undisputed facts therefore establish a violation of FINRA Rules 6720, 6230 and 2010.

II. Cause Nine – Respondents' Inaccurate Trial Balances and Ledgers

The Hearing Panel found that respondents willfully violated Exchange Act Section 17(a), Exchange Act Rule 17a-3, NASD Rule 3110, and FINRA Rule 2010 by failing to record the apartment rent arrearage, moving expenses, and security deposit on DGI's trial balance and general ledgers. We agree.[15]

1. Facts

FINRA's 2009 examination report determined that DGI's trial balance and general ledgers for April and May 2009 failed to include three liabilities totaling approximately $40,392, consisting of: (i) overdue rent for an apartment; (ii) moving and storage expenses; and (iii) a security deposit the firm owed for its Broad Street branch office.

a. Rent Arrearage

DGI entered into a lease agreement for an apartment in 1983 and remained the sole tenant on the lease until 2003, when DGI sublet the apartment to a friend of Dratel. Dratel argues that the subtenant was responsible for paying the rent, but had withheld payment because of a dispute with the landlord over maintenance issues. In early 2009, the apartment management obtained a default judgment and warrant of eviction against DGI for non-payment of rent. In April 2009, respondents filed an emergency show cause petition to stay the eviction and vacate the judgment, and Dratel signed an affidavit in support of the emergency petition in which, among other things, he represented that he was willing to make payment to reduce the arrearage. The parties eventually settled the matter, recording the settlement in a stipulation in which DGI acknowledged owing $24,376.84 in unpaid rent through April 2009.

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[15] As with the failure to preserve order memoranda, although not discussed in the Hearing Panel Decision, respondents' willful violation of the Exchange Act serves as a disqualifying event pursuant to Section 3(a)(39) of the Exchange Act, 15 U.S.C § 78c(a)(39), noting that a person or entity is subject to statutory disqualification if he has willfully violated the Exchange Act.

When FINRA inquired about the judgment, respondents claimed they were unaware of any judgment or lien against DGI from the apartment management company. Because the rent was payable by his friend, pursuant to the terms of the sublease, Dratel insists that the arrearage was his friend's responsibility and was not a liability of DGI.

b. Moving and Storage Expenses

In its examination report, FINRA noted that respondents had failed to include a bill for $3,580 for moving and storage expenses owed by DGI as a liability on their trial balance and general ledger in April 2009. Respondents do not contest this assertion and admit that they had not included it as an accrued liability as required in their April trial balance and general ledger, but did so in May 2009.

c. Security Deposit

On February 3, 2009, DGI entered into a lease for office space on Broad Street in New York City. The lease agreement required a security deposit of $9,362.49 in the form of an irrevocable letter of credit. On March 12, 2009, the landlord notified Dratel that the letter of credit had not been provided. Dratel claims that respondents were negotiating with the landlord to reduce the amount of the security deposit. He argues that, in any event, the letter of credit was not a liability, but a receivable. However, respondents did not provide the security deposit to the landlord and did not list it as an accrued expense in April or May. FINRA informed Dratel that it disagreed with his characterization of the security deposit as a receivable. Thereafter, Dratel listed the security deposit as a liability on DGI's trial balance and ledgers.[16]

2. Discussion

Exchange Act Section 17(a), and Exchange Act Rule 17a-3 thereunder, require firms to maintain and keep current books and records reflecting their assets and liabilities. It is well established that such books and records must be accurate.

Dratel argues that he was unaware of any judgments against DGI from the apartment's management company because the apartment had been subleased to Dratel's friend since 2004, who had made every rent payment as well as paid the arrearage. For this reason, Dratel never considered the apartment to be a liability of the firm. On the contrary, even though Dratel's friend may have made all the payments, the evidence shows that Dratel knew that the apartment rent arrearage was a liability that should have appeared on either the trial balance or ledger for

[16] Dratel testified that he did so only because FINRA insisted, and he "didn't want to fight any more," but continues to disagree with FINRA's characterization of the security deposit as a liability.

April and May 2009. Dratel signed an affidavit in support of the emergency petition and DGI and the apartment management company settled the matter, recording the settlement in a stipulation in which the firm acknowledged owing the unpaid rent through April 2009.

Dratel also argues that the security deposit in the form of an irrevocable letter of credit was not a liability. However, respondents did not provide the security deposit to the landlord and did not list it as an accrued expense in April or May.[17] Regardless of how Dratel categorized the letter of credit, the fact remains that respondents did not deliver it to the landlord for several months, during which time respondents owed the landlord the security deposit. Thus, the security deposit constituted a liability that should have been posted on their books.

We therefore find that respondents willfully violated Exchange Act § 17(a), Exchange Act Rule 17a-3, NASD Rule 3110, and FINRA Rule 2010 by failing to record the apartment rent arrearage, moving expenses, and a security deposit on DGI's trial balance and general ledgers.

I. Cause Ten – Dratel Failed to Establish, Maintain and Enforce Supervisory Control Systems

The Hearing Panel found that Dratel failed to provide for supervision over his sales activities, failed to establish and enforce supervisory control systems, failed to detail DGI's system of supervisory controls, and failed to test and verify DGI's supervisory procedures. As a consequence, DGI's annual compliance report for 2009 (the "2009 Report") failed to summarize test findings and changes made to respond to test results, because there were no test findings, in violation of NASD Rule 3012 and FINRA Rule 2010. We affirm parts of the Hearing Panel's findings, as discussed below.

1. Facts

On or about February 22, 2010, Dratel submitted DGI's annual compliance report for 2009. The 2009 Report consisted in large part of sections copied and pasted from annual compliance reports from the previous two years, which FINRA had informed Dratel it viewed as deficient. Regulatory Support Services, a third-party vendor, prepared the 2009 Report using information Dratel provided. Dratel admitted at the hearing that the 2009 Report contains no description of supervisory controls and procedures designed to test and verify DGI's procedures as required by NASD Rule 3012. In addition, the report contained no summary of the results of tests conducted to verify the adequacy of DGI's supervisory policies and procedures, and consequently identified no deficiencies or changes made to correct them.

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[17] Dratel acknowledges that he was mistaken in not accruing his moving and storage expenses in April of 2009 but corrected its accruals for the next month.

2. Discussion

NASD Rule 3012(a)(1) requires that each member designate and identify one or more principals who shall establish, maintain, and enforce a system of supervisory control policies and procedures, and who must submit no less than annually a report detailing its system of supervisory controls, a summary of the test results and exceptions, and any amended supervisory procedures created in response to those results. Rule 3012(a)(2)(A)(i) requires that a person senior to or "otherwise independent" of a producing manager perform day-to day supervisory review of the producing manager's account activity. If however, a member is so limited in size and resources that it cannot comply with this requirement, it may have a knowledgeable principal perform the supervisory review. *See* NASD Rule 3012(a)(2)(A)(ii).

Dratel argues that he is a "one man shop" and maintains that he has asked FINRA multiple times for guidance on to how satisfy the supervision requirement, but FINRA has failed to provide any assistance on the matter. Dratel cannot blame FINRA for his own supervision problems. *See, e.g., Hans N. Beerbaum,* Exchange Act Release No. 55731, 2007 SEC LEXIS 971, at *19 & n.22 (May 9, 2007) (a respondent cannot shift the burden of compliance to FINRA). The Commission has emphasized that "a securities dealer cannot shift its compliance responsibility to [its regulator]. A regulatory authority's failure to take early action neither operates as an estoppel against later action nor cures a violation." *W.N. Whelen & Co.*, 50 S.E.C. 282, 284 (1990); *see also Thomas C. Kocherhans*, 52 S.E.C. 528, 531 (1995) ("[We] have repeatedly held that a respondent cannot shift his or her responsibility for compliance with an applicable requirement to . . . the NASD."); *Lowell H. Listrom & Co.*, 48 S.E.C. 360, 366 (1985) (same), *aff'd*, 803 F.2d 938 (8th Cir. 1986); *Melvin Y. Zucker*, 46 S.E.C. 731, 733-34 (1976) (same).

Dratel also maintains that the 2009 Report is adequate because he was consistently testing, and took immediate corrective actions if he saw a deficiency or violation. However, the limited size and resource exception upon which Dratel relies does not provide an exception from having requisite written supervisory procedures or controls to ensure compliance. The 2009 Report fails to demonstrate what, if anything, DGI did to test and verify that its written supervisory procedures were reasonably designed with respect to DGI's activities and were up-to-date.[18]

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[18] We acknowledge that under NASD Rule 30112(a)(2)(A)(ii), sole proprietors subject to the limited size and resource exception would not violate the rule if they supervised themselves. *See* "Supervising Control Frequently Asked Questions," http://www.finra.org/sites/default/files/p602118.pdf. Our review indicates that DGI's written supervisory procedures were deficient under other provisions of Rule 3012. In light of the numerous violations, however, we view any additional violation of Rule 3012 to be insignificant and therefore we do not affirm a finding of a violation of 3012(a)(2)(A)(ii).

Therefore, we affirm the Hearing Panel's findings that the 2009 Report was inadequate because it did not summarize the results of testing DGI's supervisory procedures, did not describe any changes to the firm's supervisory procedures in response to test findings, and failed to establish procedures and policies reasonably designed to review and supervise Dratel's own sales activities, in violation of NASD Rule 3012 and FINRA Rule 2010.

J. Cause Eleven – Dratel Failed to Certify Compliance and Supervisor Processes

As discussed below, we agree with the Hearing Panel that Dratel failed to provide proper certification of DGI's compliance and supervisory processes in violation of FINRA Rules 3130 and 2010.

1. Facts

Included in the 2009 Report is an "Annual Compliance and Supervision Certification" ("Certification"), dated February 23, 2010, which is a rote recital of the requirements of FINRA Rule 3130.[19] The Certification refers back to the 2009 Report stating that "Dratel's processes . . . are evidenced in a report reviewed by the Chief Executive Officer, Chief Compliance Officer, and such other officers as Dratel may deem necessary . . . and the final report has been submitted to Dratel's board of directors and audit committee." Dratel admitted that DGI does not have a true board of directors or audit committee; rather, Dratel views himself as serving those functions. When asked to point out specifically where these processes mentioned in the annual certification were described in the 2009 Report, Dratel stated that he did not know. Furthermore, Dratel initially failed to sign the certification as required.

2. Discussion

FINRA Rule 3130 requires each FINRA member to prepare a report, not less frequently than annually, that identifies the process that the firm follows to establish, maintain, review, test, and modify its written compliance policies and written supervisory procedures. The rule also requires the firm's chief executive officer to certify annually that the firm has processes in place to establish, maintain, review, test, and modify its written compliance policies and supervisory procedures reasonably designed to achieve compliance with applicable securities rules, regulations, and laws.

While it made a rote recitation of the requirements of FINRA Rule 3130, the Certification did not have any substantive information as to the firm's compliance policies or procedures.

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[19] FINRA Rule 3130 requires each member's chief executive officer to certify annually that the firm has in place processes to establish, maintain, and review policies and procedures reasonably designed to achieve compliance with applicable rules and laws, modify the policies and procedures as needed, and test them periodically. These processes are to be memorialized in a report reviewed by the chief executive officer.

Dratel again invokes the "one-man shop" defense for this violation. However, his status as sole-proprietor does not excuse his failure to document DGI's processes for establishing, maintaining, reviewing, testing and modifying compliance policies reasonably designed to achieve compliance with the applicable securities laws, regulations. We therefore agree with the Hearing Panel that Dratel failed to provide proper certification of DGI's compliance and supervisory processes in violation of FINRA Rules 3130 and 2010.

IV. Respondents' Defense

Respondents' central defense is that, while they admit to many of the violations, most of the causes of action brought by Enforcement are not significant rule violations, some of which Dratel self-corrected, and thus should have been left as an exception on the cycle examination report and not inflated into a formal disciplinary matter. He decries Enforcement's prosecution in this matter as overreaching.

Enforcement's decision to bring formal disciplinary action against respondents is entitled to deference. FINRA disciplinary proceedings are treated as an "exercise of prosecutorial discretion" and, as such, "are given wide latitude." *Schellenbach v. SEC*, 989 F.2d 907, 912 (7th Cir. 1993). Generally, "courts will not inquire into a prosecutor's ill motive unless there is a showing of selective enforcement or an attempt to discriminate by arbitrary classification." *Id.* (citations omitted). Here, there is no evidence of either of these motives. Rather, we note that the minor nature of most of these violations is reflected in the nominal sanctions we impose below for those violations.

V. Sanctions

The Hearing Panel fined Dratel individually $5,000 and suspended him for a total of 25 business days, fined DGI $2,500, and fined respondents, jointly and severally, a total of $31,000. We find the sanctions imposed by the Hearing Panel for these violations appropriately remedial and, as explained in further detail below, we affirm the Hearing Panel's sanction determination.

A. Respondents' Failure to Timely Amend Forms U4 and BD

The Hearing Panel aggregated the sanctions for these interrelated causes of action, suspending Dratel in all capacities for 15 business days and fining respondents jointly and severally $5,000.[20] The Hearing Panel concluded that Dratel's failures to amend his Form U4 in a timely manner, and respondents' failure to amend the firm's Form BD in a timely manner,

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[20] The FINRA Sanction Guidelines approve of aggregating or batching when fashioning sanctions for similar violations. *FINRA Sanction Guidelines* 4 (2013) (General Principles Applicable to All Sanction Determinations, No. 4), http://www.finra.org/sites/default/files/Industry/p011038.pdf [hereinafter *Guidelines*].

were serious, but not egregious. On appeal, Enforcement urges the NAC to set aside the sanctions ordered by the Hearing Panel as to the first two causes of action and to order instead that Dratel be suspended for three months, that Dratel be fined $15,000 for his Form U4 violations, and that the respondents be fined $10,000, jointly and severally, for the Form BD violation. Enforcement maintains that respondents' failures to amend were egregious and the Hearing Panel erred by taking into consideration respondents' statutory disqualification when determining the appropriate sanction for these violations. We agree with Enforcement that the Hearing Panel should not have considered Dratel's status as statutorily disqualified when determining sanctions. In addition, we find that the Hearing Panel misapplied the FINRA Sanction Guidelines ("Guidelines") related to this violation. Nonetheless, we agree with length of the suspension and amount of the fine as appropriately remedial, and thus find no reason to disturb the Hearing Panel's sanctions.[21]

The Guidelines for misconduct involving the late filing of amendments to Form U4 – and which we apply to the misconduct involving a Form BD – recommend a fine of between $2,500 and $25,000, as well as a fine between $5,000 and $50,000 for the firm or the responsible principal.[22] The Guidelines do not recommend a suspension.[23] In egregious cases, such as those involving repeated failures to file, untimely filings, or false, inaccurate, or misleading filings, the Guidelines recommend considering a longer suspension of up to two years or a bar.[24] In evaluating the appropriate sanctions to impose, the Guidelines provide three principal considerations specific to Form U4 violations, only one of which – the nature and significance of the information at issue – is relevant here.[25] These considerations are in addition to the principal considerations contained within the Guidelines that apply in every disciplinary case.[26]

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[21] Respondents' status as statutorily disqualified has no bearing on the appropriateness of the sanction. *See Timothy H. Emerson Jr.*, Exchange Act Release No. 60328, 2009 SEC LEXIS 2417, at *26 (July 17, 2009) (explaining that when FINRA denies a request to continue to associate with a firm notwithstanding a statutory disqualification, it is not imposing a penalty or sanction).

[22] *Id.* at 69.

[23] The Hearing Panel looked to the "Failure to File or Filing False, Misleading or Inaccurate Forms or Amendments" portion of this Guideline. However, the violation at issue here involves untimely or late filings, not failures to file.

[24] *Id.* at 70.

[25] *Id.* at 69 (Principal Considerations in Determining Sanctions, No. 1). Respondents' failures to disclose information in this case do not implicate the other two principal considerations applicable to Form U4 violations: whether the failure resulted in a statutorily disqualified individual becoming or remaining associated with a firm; and whether a firm's misconduct resulted in harm to a registered person, another member firm, or any person or entity.

[Footnote continued on next page]

First, we consider the nature of the information that respondents failed to disclose. The information related to federal and state tax liens and judgments expressly implicates respondents' financial stability, judgment, and ability to manage their finances. Such serious financial issues "raise concerns about whether [respondents] could responsibly manage [their] own financial affairs, and ultimately cast doubt on [their] ability to provide trustworthy financial advice and services to investors relying on [respondents] to act on their behalf." *Tucker*, 2012 SEC LEXIS 3496, at *32 (citing *Scott Mathis*, Exchange Act Release No. 61120, 2009 SEC LEXIS 4376, at *29 (Dec. 7, 2009), *aff'd*, 671 F.3d 210 (2d Cir. 2012)). We conclude that the non-disclosed information, when considered in its totality, is significant.

Next, we consider that Dratel and DGI's failures to amend spanned a period of approximately nine months for the first federal tax lien and at least four months for the remaining liens and judgments—a lengthy period of time.[27] Finally, we note that that Dratel has related disciplinary history.[28]

The Form U4 is used by all self-regulatory organizations (including FINRA), state regulators, and broker-dealers to determine and monitor the fitness of securities professionals who seek initial or continued registration with a member firm. *See Rosario R. Ruggiero*, 52 S.E.C. 725, 728 (1996). The information on the Form U4 also is important to member firms when evaluating whether to hire an employment applicant, and the investing public, who have access to certain disclosures on FINRA's BrokerCheck, when evaluating a broker. *See, e g.*, *Richard A. Neaton*, Exchange Act Release No. 65598, 2011 SEC LEXIS 3719, at *17-18 (Oct. 20, 2011); *Mathis*, 2009 SEC LEXIS 4376, at *29. Forms BD are equally important. This form must be completed and submitted to the SEC in order to apply for registration as a securities broker-dealer.

Therefore, we find that respondents' violations, while not egregious, involved aggravating factors that fully warrant an upward departure from the Guidelines. Because of the absence of mitigating factors and the presence of several aggravating factors, particularly the extended period of time that it took respondents to update the forms, and the importance of the

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[cont'd]

Id. Because these considerations do not apply, we do not consider them either aggravating or mitigating.

26 *Guidelines*, at 6-7.

27 *Guidelines*, at 6 (Principal Considerations in Determining Sanctions, No. 9).

28 *Id.* at 2 (General Principles Applicable to All Sanction Determinations, No. 2).

information that they failed to timely update, we believe that a 15-day suspension for Dratel and a $5,000 fine for respondents, imposed jointly and severally, are appropriately remedial sanctions for these violations.

B. Respondents' Willful Failure to Create and Preserve Order Memoranda

For books and records violations of NASD Rule 3110, FINRA Rule 2010, and Exchange Act Rules 17a-3 and 17a-4, the Guidelines recommend a fine of $1,000 to $10,000, and consideration of a suspension in any or all capacities or functions for up to 30 business days.[29] In egregious cases, the Guidelines recommend considering a suspension for up to two years in any or all capacities or functions, or expulsion of the firm and a bar of the responsible individual, and a fine of $10,000 to $100,000.

The Hearing Panel concluded that, to deter respondents and others from similar willful disregard of the recordkeeping rules, it is appropriate to suspend Dratel from associating with any FINRA member firm in any capacity for five business days and to impose a fine of $10,000 upon respondents jointly and severally. The Hearing Panel credited Dratel's explanations as to the reasons for the errors,[30] but noted that the result was not a de minimis frustration of the purpose of the recordkeeping rules.

We agree with the Hearing Panel. The principal consideration for this violation is the nature and materiality of the inaccurate or missing information. We find that the information was material because without the records, FINRA could not determine why the trades were treated as errors or for whom the trades were intended. Respondents' destruction of the order memoranda rendered regulators incapable of determining the reasons for errors in approximately 275 trades over a period of two years. However, we do not find that respondents' failures to amend were attempts to conceal his account activity from regulators.[31] For these reasons, we conclude the violation was serious, but not egregious. Thus, we affirm the fine and suspension imposed by the Hearing Panel.

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29 *Id.* at 29.

30 We defer to the Hearing Panel's credibility findings. *See Dane S. Faber*, 57 S.E.C. 297, 307 (2004) (stating that, "[c]redibility determinations of an initial fact-finder, which are based on hearing the witnesses' testimony and observing their demeanor, are entitled to considerable weight and deference"); *John Montelbano*, 56 S.E.C. 76, 89 (2003) (noting that credibility determinations of an initial fact-finder can be overcome only where the record contains substantial evidence for doing so).

31 *Guidelines*, at 6 (Principal Considerations in Determining Sanctions, No. 10).

C. Respondents' Failure to Preserve E-mail Communications

The sanctions for failure to preserve e-mail communications, in violation of NASD Rule 3110, FINRA Rule 2010, Exchange Act §17(a), and Exchange Act Rule 17a-4(b)(2), implicate the same recordkeeping Guidelines referenced above.[32] The Hearing Panel found mitigating circumstances applicable to respondents' inadvertent failure to preserve e-mails. After being notified of the issue, Dratel appropriately directed an employee to contact Smarsh, and the employee reported to him that the problem had been remedied. Although Dratel did not follow up to confirm the resolution of the issue, he reasonably concluded that the system had been repaired because he continued to be able to send and receive e-mails, and Smarsh continued to provide reports and bill him for the service. Once Dratel realized there was an archiving failure, however, he took immediate steps to correct the issue.

Therefore, we agree with the Hearing Panel that a fine of $1,000, which is the lowest recommended amount in the applicable Sanctions Guidelines, imposed upon respondents jointly and severally is appropriate, particularly in light of the circumstances surrounding this violation as previously discussed.

D. Respondents Sharing Customer Losses

The Hearing Panel determined that a joint and several fine of $10,000 for respondents' sharing in customer losses was appropriately remedial. While the Guidelines do not address the precise misconduct involved in respondents' violations, the NAC has previously found the Guideline for guaranteeing a customer against loss, which the Hearing Panel applied here, to be the most applicable in similar situations. *See Dep't of Enforcement v. Reynolds*, Complaint No. CAF990018, 2001 NASD Discip. LEXIS 17, at *67 (NASD NAC June 25, 2001). The Guidelines recommends imposing a fine of $2,500 to $25,000, and considering a suspension of up to 30 business days, or, in egregious cases, a suspension of up to two years or expulsion of a firm or a bar of an individual.[33]

Again, the Hearing Panel credited Dratel's testimony and found no motive for the payments other than his professed concern for the welfare of elderly, long-time former customers of his father to whom he felt a special obligation. Respondents' motives, sincere or not, still violated the rules. Therefore, we do not disturb the fine levied by the Hearing Panel.

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32 *Id.* at 29.

33 *Id.* at 86.

E. Respondents' MSRB Violations

The Hearing Panel determined that it was appropriate to aggregate the MSRB violations in the sixth and seventh causes of action for the purpose of imposing sanctions. We agree that aggregation is appropriate.

The Guidelines note that the sanctions for registration violations are appropriate for violations of MSRB Rules G-2 and G-3.[34] The Guidelines call for a fine of $2,500 to $50,000 and consideration, in cases involving individuals, of suspension in any or all capacities for up to six months. For a firm, in egregious cases, they recommend consideration of suspension with respect to any or all activities or functions for up to 30 business days.[35]

The Guidelines state that the sanctions for trade reporting violations are appropriate for violations of MSRB Rule G-14, and call for a fine of $5,000 to $10,000, and a greater fine in egregious cases.[36]

The sixth and seventh causes of action both allege violations of MSRB registration and reporting requirements. The sixth cause of action charges respondents with executing municipal securities transactions without being registered with the MSRB and without a registered municipal securities principal, in violation of MSRB Rules G-2 and G-3. The seventh cause of action charges DGI alone with failing to report municipal securities trades in violation of MSRB Rule G-14, and executing municipal securities without testing its ability to interface with RTRS and without filing a Form RTRS.

The Hearing Panel found that respondents' MSRB violations were inadvertent and careless and imposed a fine of $2,500 jointly and severally upon respondents. We agree with the Hearing Panel's credibility findings as to Dratel's testimony that he had resumed executing some municipal securities transactions after a significant hiatus and simply forgot. Dratel's explanation is consistent with the fact that, once it occurred to him that he needed to register DGI, he did so before FINRA was aware of the violations.

F. DGI's Failure to Report Trades to TRACE

As with the MSRB trade reporting violations, the Guidelines for TRACE reporting violations recommend a fine of $5,000 to $10,000.[37] The Hearing Panel concluded that

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34 *Id.* at 45.

35 *Id.*

36 *Id.* at 64-65.

37 *Id.*

imposing a fine of $2,500 on DGI was appropriate for its violations of FINRA Rules 6720, 6730 and 2010.

DGI engaged in TRACE reporting violations from March to May 2009. The evidence suggests that Dratel's omissions were inadvertent, and we find it mitigating that he took remedial steps before FINRA learned of the violations. As with the MSRB reporting violations discussed above, Dratel was unaware of the existence of TRACE when he resumed trading in debt securities, and once he learned from his clearing firm of the need to do so, he took appropriate steps to complete a TRACE participation agreement. Considering that the duration of the problem was brief and self-corrected, that there were only 38 unreported transactions, and that no customer harm resulted, we affirm the fine of $2,500 and find it sufficient to deter DGI and others from such future violations.

G. Respondents' Inaccurate Trial Balances and Ledgers

The Guidelines recommend a fine of $1,000 to $10,000 and consideration of a suspension for up to 30 business days for recordkeeping violations.[38] The Hearing Panel imposed a fine of $2,500 jointly and severally upon respondents and we affirm.

We look to the principal consideration for this violation, the nature and materiality of the inaccurate or missing information, and find that the improperly unreported liabilities were relatively minor in nature and not fundamental to FINRA's oversight of the firm. Therefore, we find the fine imposed by the Hearing Panel to be appropriately remedial in light of the nature of the violation.

H. Dratel's Supervisory Control Violations

The Guidelines relating to failures to supervise suggest a fine of $5,000 to $50,000 and consideration of a suspension of a responsible individual in all supervisory capacities for up to 30 business days.[39] The Hearing Panel chose to aggregate the sanctions for the two supervision-related causes of action, suspended Dratel from associating with any FINRA member firm in any supervisory capacity for five business days, and imposed a $5,000 fine. We affirm.

The principal considerations for this violation instruct us to look to whether respondent ignored "red flag" warnings, the nature, extent, size and character of the underlying misconduct, and the quality and degree of supervisor's implementation of the firm's supervisory procedures and controls.[40] Viewing Dratel's violations through this lens, we agree with the Hearing Panel

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38 *Id.* at 29.

39 *Id.* at 103.

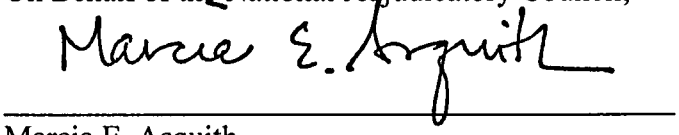
40 *Id.* (Principal Considerations in Determining Sanctions, Nos. 1, 2, and 3).

that sanctions in the lower range are appropriate. While he underlying misconduct was, for the most part, not serious in nature, Dratel's status as a "one-man shop" does not excuse his inability to comply with the supervisory control rules. Therefore, for violating FINRA Rules 3012, 3130, and 2010, we affirm the Hearing Panel's suspension and fine.

VI. Conclusion

Accordingly, Dratel willfully failed to make timely amendments to his Form U4, failed to establish and enforce supervisory control systems, and failed to certify compliance and supervisory processes; DGI failed to report municipal securities trades and executed customer transactions in corporate debt securities without completing a TRACE participation agreement and failed to report transactions to TRACE; and respondents willfully failed to make timely amendments to DGI's Form BD, willfully failed to create and preserve order memoranda, failed to preserve e-mail communications, failed to maintain accurate ledger and trial balances, shared customers' losses, executed municipal securities transactions without being registered with the MSRB, and failed to have a registered municipal securities principal supervise municipal securities activities. For this misconduct, we fine Dratel $5,000 and suspend him for a total of 25 business days, to be served consecutively; fine DGI $2,500; and additionally fine respondents, jointly and severally, a total of $31,000. Respondents are also statutorily disqualified for their willful failures to make timely amendments to the Forms U4 and BD and their willful violations of the Exchange Act. We also affirm the Hearing Panel's imposition of hearing costs in the amount of $4,672 and order that respondents pay appeal costs in the amount of $1,553.96.[41]

On Behalf of the National Adjudicatory Council,



Marcia E. Asquith,
Senior Vice President and Corporate Secretary

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[41] Respondents are jointly and severally responsible for costs. Pursuant to FINRA Rule 8320, the registration of any person associated with a member who fails to pay any fine, costs, or other monetary sanction imposed in this decision, after seven days' notice in writing, will summarily be revoked for non-payment.