

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

DEPARTMENT OF ENFORCEMENT,

COMPLAINANT,

v.

DISCIPLINARY PROCEEDING
No. 20100224056

EDWARD A. SALAZAR,
(CRD 2338244)

RESPONDENT.

COMPLAINT

The Department of Enforcement alleges:

SUMMARY

1. From in or about April 2006 through in or about November 2006, while employed by Countrywide Investment Services, Inc. (the "Firm" or "Countrywide") Respondent participated in the sale to one investor of \$1.1 million in Bonded Life Settlements offered by A&O Resource Management Ltd. ("A&O"). The A&O Bonded Life Settlements Respondent sold are securities. A&O declared bankruptcy in 2009. Consequently, Respondent's customer lost their entire investment.

2. Respondent sold the above-referenced A&O Bonded Life Settlements without first providing written notice to and receiving written approval from his FINRA-registered broker dealer employer. In connection with his sales of the A&O Bonded Life Settlements, Respondent secured \$77,000 in commissions. By the foregoing, Respondent violated NASD Rule 3040 and 2110.

3. Respondent sold the above-referenced A&O Bonded Life Settlements without first conducting an adequate due diligence inquiry. Specifically, Respondent

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failed to exercise reasonable due diligence in researching the A&O product, the financial viability of the company that issued it and the qualifications of its principals to engage in its sales. Respondent thus lacked reasonable grounds to believe that the A&O recommendation was suitable. By the foregoing, Respondent violated NASD Rules 2310 and 2110.

4. Alternatively, Respondent violated NASD Rules 3030 and 2110.

A&O and Its Bonded Life Settlements

5. A&O purchased existing life insurance policies from policy holders at a discount in exchange for the receipt of the death benefit payable upon the death of the insured. A&O then resold these policies to investors in the form of Bonded Life Settlements promising a 10% to 12% return on the investment. In late 2006, A&O's principals began transferring customer funds to a bank account, which they used as a "slush" fund to pay personal expenses, among other things.

6. In 2009, following inquiries by various state securities and insurance regulators concerning A&O's investment offerings, A&O sought Chapter 11 bankruptcy protection. On or about January 7, 2010, the appointed Bankruptcy Trustee filed a 25 count complaint alleging fraud and breach of fiduciary duty against A&O, its related entities and its principals.

7. In 2010 and 2011, three of A&O's principals were convicted in federal district court of securities fraud and conspiracy to commit money laundering, among other things, in connection with their A&O activities.

RESPONDENT AND JURISDICTION

8. Respondent entered the securities industry in 1993 as a Limited Registered Representative for a FINRA-registered broker-dealer. He has since been associated with 12 different FINRA-registered broker-dealers. Respondent obtained his Series 6 and Series 63 securities licenses in February 1993 and October 1993, respectively and his Series 7 securities license in July 1999. These securities licenses were in effect during the time period of the misconduct described herein.

9. From November 2005 through February 2007, Respondent was employed by Countrywide. Countrywide was a FINRA-registered broker dealer during the time of Respondent's association with it.

10. Although Respondent has not been associated with a FINRA member firm since October 9, 2009, he remains subject to FINRA's jurisdiction for purposes of this proceeding, pursuant to Article V, Section 4 of FINRA's By-Laws, because (1) the Complaint was filed within two years after the date upon which he ceased to be associated with a FINRA member and (2) the Complaint charges him with misconduct committed while he was associated with a FINRA member.

FIRST CAUSE OF ACTION Private Securities Transaction (NASD Rules 3040 and 2110)

11. The Department realleges and incorporates by reference paragraphs one through 10 above.

12. NASD Rule 3040 requires an associated person to provide written notice to his FINRA-regulated broker dealer employer prior to participating in any private securities transaction. The notice must describe in detail the proposed transaction and the

person's proposed role therein and state whether he has received or may receive selling compensation in connection with the transaction.

13. NASD Rule 2110 requires members, in the conduct of their business, to observe high standards of commercial honor and just and equitable principles of trade.

Customers JA and AA

14. From in or about April 2006 through in or about November 2006, Respondent participated in the sale of two A&O Bonded Life Settlements to customers JA and AA, a married couple. These customers invested a total of approximately \$1.1 million in two A&O Bonded Life Settlements.

15. Customers JA and AA were not customers of Countrywide. At the time, Customer JA was approximately 40 years old and Customer AA was approximately 42 years old. Spanish was the native language of Customers JA and AA and each had limited knowledge of written and/or spoken English.

16. From in or about April 2006 through in or about November 2006, Respondent spoke with Customers JA and AA on several occasions in the course of soliciting their A&O investment. On each occasion, Respondent spoke with Customers JA and AA in Spanish. On at least two occasions during the solicitation of Customers JA and AA, Respondent was accompanied by KF. KF did not speak Spanish.

17. In the course of soliciting the A&O investment of Customers JA and AA, Respondent advised these customers that A&O procured bonding insurance on the underlying life insurance policies that served as the basis for A&O customer investments from Provident Capital Indemnity, Ltd. ("Provident"), an insurance company located in Costa Rica.

18. On or about November 9, 2006, Customers JA and AA executed various documents in connection with each of their two A&O Bonded Life Settlement investments, including a Line of Credit Loan Agreement ("Loan Agreement") in connection with each investment. Some of the documents prepared and/or executed in connection with these sales identified KF as the agent of record.

A&O Investment No. 1

19. Pursuant to the terms of this Loan Agreement (the "First Loan Agreement"), Customers JA and AA agreed to provide Houston Tanglewood Partners ("Tanglewood Partners") a line of credit up to \$1,116,798 for the purpose of acquiring policies and bonds and authorized Tanglewood Partners to make an initial draw in the amount of \$550,000 to purchase a 18.6133% share in the underlying life insurance policy that was the basis of Customers JA and AA's A&O investment. The First Loan Agreement further indicated that Customers JA and AA's loan to Tanglewood Partners would be documented in the form of a credit note bearing interest at a rate of 12% per annum.

20. Tanglewood Partners is an entity that was given authority by A&O to direct the use of escrowed investor funds to purchase identified life insurance policies underlying customer investments and make the related premium payments, among other things.

21. Customers JA and AA subsequently received a Line of Credit Promissory Note dated November 9, 2006 ("First Promissory Note") and a Security Agreement. According to the First Promissory Note and the Security Agreement, Tanglewood Partners promised to pay Customers JA and AA \$1,116,798 – their fractional interest in

the face value of the life insurance policy underlying the investment based on a 12% rate of return. The First Promissory Note and the Security Agreement also stated that Customers JA and AA would receive both the principal of their investment and accrued interest, payable by the earlier of February 17, 2013 or upon the receipt of funds into the escrow account resulting from proceeds of the underlying insurance policy or from the Provident bond.

A&O Investment No. 2

22. Pursuant to the terms of this Loan Agreement ("Second Loan Agreement"), Customers JA and AA agreed to provide Houston Tanglewood Partners ("Tanglewood Partners") a line of credit up to \$1,117,431 for the purpose of acquiring policies and bonds and authorized Tanglewood Partners to make an initial draw in the amount of \$550,000 to purchase a 74.4954% share in the underlying life insurance policy that was the basis of Customers JA and AA's A&O investment. The Second Loan Agreement further indicated that Customers JA and AA's loan to Tanglewood Partners would be documented in the form of a credit note bearing interest at a rate of 12% per annum.

23. Customers JA and AA subsequently received a Line of Credit Promissory Note dated November 9, 2006 ("Second Promissory Note") and a Security Agreement. According to the First Promissory Note and the Security Agreement, Tanglewood Partners promised to pay Customers JA and AA \$1,117,431 – their fractional interest in the face value of the life insurance policy underlying the investment based on a 12% rate of return. The Second Promissory Note and the Security Agreement also stated that Customers JA and AA would receive both the principal of their investment and accrued

interest, payable by the earlier of February 24, 2013 or upon the receipt of funds into the escrow account resulting from proceeds of the underlying insurance policy or from the Provident bond.

24. Customers JA and AA funded their A&O Bonded Life Settlements investments with the proceeds of an existing annuity that they surrendered. Respondent had previously sold this annuity to Customers JA and AA. They incurred approximately \$40,000 in surrender charges in connection with the transaction.

Commissions

25. Respondent received a payment of approximately \$77,000 in connection with his sales of A&O Bonded Life Settlements to Customers JA and AA. KF received a payment of approximately \$44,000 in connection with the Customer JA and AA investments.

26. During 2009, A&O sought Chapter 11 bankruptcy protection. Customers JA and AA lost their entire investment in A&O Bonded Life Settlements.

27. The A&O Bonded Life Settlements solicited and sold by Respondent were securities.

28. Respondent participated in the solicitation and sale of the A&O Bonded Life Settlements described above without first providing prior written notice to and obtaining written approval from Countrywide, his FINRA-regulated broker dealer employer.

29. The acts, practices and conduct described above constitute separate and distinct violations of NASD Rules 3040 and 2110.

**SECOND CAUSE OF ACTION
(ALTERNATIVE TO FIRST CAUSE OF ACTION)
Outside Business Activities
(NASD Rules 3030 and 2110)**

30. The Department realleges and incorporates by reference paragraphs one through 29 above.

31. NASD Rule 3030 prohibits any person associated with a member in any registered capacity from accepting employment or accepting compensation from any other person as a result of a business activity, other than a passive investment, outside the scope of his relationship with his employer firm, unless he has provided prompt written notice to the member.

32. *Should a determination be made that Respondent did not engage in private securities transactions as set forth above, Complainant states, in the alternative, that from in or about April 2006 through November 2006, Respondent participated in outside business activities without providing notice to his FINRA-registered broker dealer employer through his sales of the A&O Bonded Life Settlements as described above.*

33. Respondent's solicitation and sales of the A&O Bonded Life Settlements were made outside the scope of his relationship with Countrywide, his FINRA-registered broker dealer employer.

34. Respondent received compensation in the amount of \$77,000 as noted above in connection with his sales of the A&O Bonded Life Settlements.

35. The acts, practices and conduct described above constitute violations of NASD Rules 3030 and 2110.

**THIRD CAUSE OF ACTION
Reasonable Basis Suitability
(NASD Rules 2310 and 2110)**

36. The Department realleges and incorporates by reference paragraphs one through 35 above.

37. NASD Rule 2310 requires that in recommending to a customer the purchase, sale or exchange of any security, a member shall have reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts, if any, disclosed by such customer as to his other security holdings and as to his financial situation and needs.

38. NASD Rule 2310 also encompasses "reasonable basis" suitability which requires a broker to have an adequate and reasonable basis for any recommendation that he makes. The "reasonable basis" test relates only to the particular recommendation, rather than to the particular customer.

39. Prior to soliciting and selling the A&O Bonded Life Settlements to Customers JA and AA, Respondent failed to conduct adequate due diligence inquiries regarding Provident, the Costa Rican insurance company that bonded/re-insured the underlying life insurance policies purchased and resold by A&O.

40. Had he done so, Respondent would have learned that in 1992, California's Insurance Commissioner barred Provident from conducting the unlicensed sale of insurance in California based on findings that Provident misrepresented the value of assets on its balance sheet.

41. Prior to soliciting and selling the A&O Bonded Life Settlements to Customers JA and AA, Respondent also failed to conduct adequate due diligence

inquiries regarding Midwest Medical, the company hired by A&O to assess the life expectancies of the insureds of the underlying policies which served as collateral for the A&O Bonded Life Settlement product.

42. Had he done so, Respondent would have learned that in or about November 2003, the owners of Midwest Medical were indicted for 21 counts of violating the criminal provisions of the Federal Food, Drug and Cosmetic Act and that in or about July 2005, the owners of Midwest Medical plead guilty in federal district court to aiding and abetting in the introduction of a misbranded drug into interstate commerce with the intent to mislead.

43. Prior to soliciting and selling the A&O Bonded Life Settlements to Customers JA and AA, Respondent failed to obtain information regarding the qualifications of A&O principals to issue life settlements and to examine reports of A&O's financial status in order to ascertain the economic well-being of the company.

44. Had he conducted reasonable due diligence, Respondent would have learned the facts as identified in paragraphs 39 to 43 above.

45. Based on the foregoing, Respondent lacked a reasonable basis for making the A&O recommendations to his customers.

46. The acts, practices, conduct and omissions described above constitute separate and distinct violations of NASD Rules 2310 and 2110.

RELIEF REQUESTED

WHEREFORE, the Department respectfully requests that the Panel:

- A. order that one or more of the sanctions provided under FINRA Rule 8310(a), including monetary sanctions be imposed, including that Respondent be

required to disgorge fully any and all ill-gotten gains and/or make full and complete restitution, together with interest.

- B. order that the Respondent bear such costs of proceedings as are deemed fair and appropriate under the circumstances in accordance with FINRA Rule 8330.

FINRA DEPARTMENT OF ENFORCEMENT

Date: October 4, 2011

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