

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

Department of Enforcement,

Complainant,

v.

David D. Lewis (CRD No. 1004661),

Respondent.

DISCIPLINARY PROCEEDING
No. 2011025633201

Hearing Officer—MAD

**ORDER ACCEPTING OFFER OF
SETTLEMENT**

Date: October 12, 2015

INTRODUCTION

Disciplinary Proceeding No. 2011025633201 was filed on January 16, 2015, by the Department of Enforcement of the Financial Industry Regulatory Authority (“FINRA”) (“Complainant”). Respondent David D. Lewis (“Respondent” or “Lewis”) submitted an Offer of Settlement (“Offer”) to Complainant dated September 18, 2015. Pursuant to FINRA Rule 9270(e), the Complainant and the National Adjudicatory Council (“NAC”), a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs (“ODA”) have accepted the uncontested Offer. Accordingly, this Order now is issued pursuant to FINRA Rule 9270(e)(3). The findings, conclusions and sanctions set forth in this Order are those stated in the Offer as accepted by the Complainant and approved by the NAC.

Under the terms of the Offer, Respondent has consented, without admitting or denying the allegations of the Complaint (as amended by the Offer of Settlement), and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to which FINRA is a party, to the entry of findings and violations consistent with the allegations of

the Complaint (as amended by the Offer of Settlement), and to the imposition of the sanctions set forth below, and fully understands that this Order will become part of Respondent's permanent disciplinary record and may be considered in any future actions brought by FINRA.

BACKGROUND

Lewis entered the securities industry in or around August 1977 as an associated person of a FINRA member firm. He became registered as a General Securities Representative ("GS") in November 1977, a Registered Options Principal ("OP") in January 1978, a Senior Registered Options Principal ("SR") in October 1981, a General Securities Principal ("GP") in July 1989, and an Equity Trader Limited Representative ("ET") in September 2000. In May 2003, Lewis associated with First Washington as a GS, GP, OP, and ET. During the period from April 2010 until December 2010, he was also registered through First Washington as a Limited Representative – Investment Banking ("IB").

During the period from March 2008 until February 2011 (the "Relevant Period"), Lewis was the Chairman, Chief Executive Officer, Chief Compliance Officer ("CCO"), SR and Compliance Registered Options Principal ("CROP") of First Washington. He held primary and overall responsibility for compliance and supervision, with the exception of the roles of AML Compliance Officer, Financial and Operations Principal and Municipal Principal. He was responsible for establishing, maintaining and enforcing First Washington's supervisory system and its WSPs, and he was the principal responsible for supervision of the Firm's public customer options accounts and all options transactions made therein.

First Washington filed a full Form BDW Uniform Request Withdrawal from Broker-Dealer Registration ("Form BDW") with FINRA on or about September 30, 2013. The Form BDW became effective on or about November 29, 2013.

Lewis' registrations with First Washington were terminated without a Form U5 Uniform Termination Notice for Securities Industry Registration filing on or about November 29, 2013. He has not since registered or associated with a FINRA member firm.

Although Respondent Lewis is no longer registered or associated with a FINRA member firm, 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 effective date of termination of Respondent's registration with the Firm, namely, on or about November 29, 2013, and (2) the Complaint charges him with misconduct committed while he was registered or associated with a FINRA member.

FINDINGS AND CONCLUSIONS

It has been determined that the Offer be accepted and that findings be made as follows:

FIRST CAUSE OF ACTION

Failure to Establish, Maintain and Enforce Adequate Supervisory System and Written Supervisory Procedures (NASD Conduct Rules 2110, 2860 and 3010; and FINRA Rules 2010 and 2360)

NASD Conduct Rule 3010(a) requires each member firm to establish and maintain a supervisory system that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA Rules. In addition, Rule 3010(b)(1) requires each member firm to establish, maintain and enforce written procedures to supervise the types of business in which it engages, which are reasonably designed to achieve such compliance. Rule 3010(c)(1) further requires each member to conduct a periodic examination of customer accounts to detect and prevent irregularities or abuses.

NASD Conduct Rule 2860, which was in effect from the beginning of the Relevant Period until February 16, 2009, sets forth the rules on options for member firms. Subsection (b) sets forth the requirements all member firms that engage in an options business must follow.

Paragraph (b)(20) discusses the supervision of options accounts and (b)(20)(A) “Duty to Supervise” states that “[e]ach member that conducts a public customer options business shall ensure that its written supervisory system policies and procedures pursuant to Rules 3010, 3012, and 3013 adequately address the member’s public customer options business.”

FINRA Rule 2360, which became effective February 17, 2009, sets forth the rules on options for member firms. Subsection (b) sets forth the requirements all member firms that engage in an options business must follow. Paragraph (b)(20) discusses the supervision of options accounts and (b)(20)(A) “Duty to Supervise” stated, from February 17, 2009 through the end of the Relevant Period, that “[e]ach member that conducts a public customer options business shall ensure that its written supervisory system policies and procedures pursuant to NASD Rules 3010, 3012, and FINRA Rule 3130 adequately address the member’s public customer options business.”

NASD Conduct Rule 2110, which was superseded by FINRA Rule 2010 on December 15, 2008, both state “[a] member, in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade.”

During the Relevant Period, First Washington conducted a public customer options business and was required to ensure that its written supervisory system policies and procedures adequately addressed that line of business pursuant to the NASD and FINRA Rules described above.

During the Relevant Period, three of First Washington’s customers engaged in a large number of high-risk options transactions, resulting in losses of approximately \$2,853,924.29. The customers paid the Firm approximately \$515,596.48 in commissions for those options

trades. A significant portion of the customers' losses could have been prevented if Lewis had established, maintained and enforced an adequate supervisory system and WSPs.

- During the period from December 2008 to October 2009, customer JRK opened approximately 117 options positions in his options account. During that period, JRK paid the Firm approximately \$232,094.98 in commissions for options trades and suffered losses of approximately \$1,385,447.95 in his options account.
- During the period from April 2008 to December 2010, customer J-MPS opened approximately 245 options positions in his account. Approximately 20 of those positions exposed J-MPS to risk in an amount greater than the Firm had authorized. In connection with these options positions during that period, J-MPS paid the Firm approximately \$244,561.31 in commissions and suffered losses of approximately \$848,906.12 in his account.
- During the period from December 2010 to February 2011, customer AS opened approximately 29 options positions in his account. Approximately 28 of those positions exposed AS to risk in an amount greater than the Firm had authorized. In connection with these options positions during that period, AS paid the Firm approximately \$38,940.19 in commissions and suffered losses of approximately \$619,570.32 in his account.

Lack of Supervision over the Firm's Options Business

The Firm received monthly exception reports from its clearing firm, Pershing LLC, known as the Accounts for Statement Review ("ASR") reports. Those ASR reports identified customer accounts in which multiple trades had occurred, there was a significant decrease in net worth, or large amounts of commissions had been charged. The information contained in the

ASR reports enabled a firm to identify accounts warranting further review for, among other things, qualitatively and quantitatively unsuitable recommendations. First Washington did not generate any other internal reports that contained the same or similar information to the ASR report.

Notwithstanding the Firm's receipt of the ASR reports, its WSPs, maintained by Lewis, were deficient in that: (a) they did not require an options principal to review the ASR reports and determine whether any of the Firm's options accounts required further review, and (b) they did not require documentation of the reasons for any action taken upon such review, or of the decision to take no action. They were also deficient in that they did not state with specificity criteria for identifying options accounts warranting additional review.

The WSPs, maintained by Lewis, were further deficient because they failed to provide for verification that the customer understood and authorized the transactions when multiple options transactions were effected in an account.

Lewis did not establish, maintain or enforce any system or procedure to ensure that customers had sufficient buying power to support their purchases of options or that customers who traded options were not exposed to risks greater than the Firm had authorized.

The Firm's WSPs required that the CROP review, approve and endorse Commission Reports and Trading Blotters concerning options activity. They further required that the CROP document any course of action deemed appropriate, regardless of determination, and that the approval of Option Trading Blotters be evidenced by the signature or initial of the CROP.

As the Firm's CROP throughout the Relevant Period, Lewis failed to implement the requirements described above. Specifically, he failed to endorse Commission Reports or Trading

Blotters concerning options activity to evidence his review and approval of those documents. He further failed to document the course of action, if any, taken upon his review of those documents.

Additionally, the Firm's WSPs required that each prospective options customer's Pershing Options Agreement be completely and accurately filled out.

Lewis failed to enforce the foregoing requirement. The Pershing Options Agreement included spaces for the Firm to designate the dollar amount limitation for a customer's options risk exposure and the maximum number of options contracts. On or about April 2, 2008, Lewis approved an Option Agreement and Approval Form for customer JRK on which neither the dollar amount limitation for the customer's options risk exposure nor the maximum number of options contracts had been filled in.

The Firm's WSPs also stated that an order limit shall be established in the amount of \$10,000 per transaction for a period of one year following the date that an options account is opened where the client has no previous options trading experience.

Lewis failed to implement the foregoing requirement. In or about November 2009, he approved an Option Agreement and Approval Form for customer AS, which stated that AS had zero years of experience trading options. Lewis did not establish an order limit of \$10,000 per transaction for AS. During the one-year period following the approval of his account for options trading, AS's account frequently effected options transactions in amounts greater than \$10,000.

The Firm's WSPs stated that options transactions may not be solicited and that each options ticket must be marked "unsolicited."

Lewis failed to enforce the prohibition of solicited options trading. During the Relevant Period, he approved numerous options transactions, knowing that they had been solicited by one of the Firm's registered representatives and that the order tickets were not marked "unsolicited."

The Firm's WSPs required that the order ticket for any order must be completed in full, including the customer's name or account number. Whenever a customer name or account number was changed, the procedures required that documentation of the reasons for the change be placed on the back of the ticket.

Lewis failed to enforce the foregoing requirement. In September 2009 the Firm's registered representative RAF filled out six order tickets for options transactions in the Firm's average price account. On each ticket, he changed the account numbers or changed the allocation of options contracts among the customers. Lewis approved the trades and did not require that any documentation of the reasons for changing the orders be placed on the back of the tickets.

Lack of Supervision over the Firm's Average Price Account

The Firm maintained an average price account (also known as the allocation account). Its registered representatives entered trades in the average price account and identified on the order tickets the customer accounts to which those trades would be allocated.

When a purchase transaction was entered, Pershing's system was able to detect whether there was adequate equity in the customer's account to permit the purchase. When a purchase transaction was executed in the average price account, however, Pershing was not informed for which customers the trade had been entered. Pershing was therefore unable to detect whether there was adequate equity in the customers' accounts to permit the trade until after the trades were executed and they were allocated to the customers.

The supervisory system and WSPs established and maintained by Lewis were deficient in that they did not include any procedures to ensure there was sufficient equity in customers'

accounts when trades were entered in the average price account, or that the trades were allocated to the accounts identified on the order tickets.

In September 2009, the Firm's registered representative RAF used the average price account to effect options purchase transactions for customers whose accounts lacked sufficient equity to support the purchases.

Lack of Heightened Supervision over Registered Representatives

The Firm's WSPs required that registered representatives with a history of customer complaints, disciplinary actions or arbitrations be placed under heightened supervision.

When a registered representative was placed under heightened supervision, the Firm's WSPs required that a written document be prepared outlining the special supervisory arrangements, including an assessment of the type of supervision needed and specifying the frequency, duration and scope of the review. The WSPs further required that the document be signed by the supervisor and the registered representative subject to the special supervision.

The Firm's WSPs required that all trades effected by the registered representative under heightened supervision be approved by the Firm's Vice-CCO and endorsed by initialing the order memorandum prior to its execution. They further required that a sample of all new accounts opened by the registered representative be contacted to verify that the information contained on the new account form was accurate and complete.

The Firm's WSPs also required that a registered representative under heightened supervision receive training, in addition to the Firm's Continuing Education Firm Element training, covering topics that involve areas for which the registered representative was required to be subject to the special supervision.

Lewis failed to enforce the requirements described above. Specifically, sometime in 2008, Lewis imposed heightened supervision on the Firm's registered representative RAF, who, pursuant to the Firm's WSPs described in above, was required to be placed on heightened supervision because of his prior customer complaints and a regulatory action. A document was prepared stating that Lewis would approve the opening of all option accounts and that he would review all option order tickets before the orders were executed. No other conditions were imposed. The document describing the heightened supervision did not include an assessment of the type of supervision needed and did not specify the frequency, duration or scope of the review. The document was not signed by Lewis or by the registered representative.

Following the imposition of the heightened supervision of RAF, Lewis failed to review all of RAF's options order tickets before the orders were executed. The Firm's Vice-CCO also did not document his approval of RAF's non-option trades by initialing the order memoranda before the orders were executed. Further, RAF did not receive any additional training, other than the Firm's normal Continuing Education Firm Element training.

Lewis's heightened supervision plan for RAF was inadequate. Lewis was aware that two customers had complained to RAF's previous broker-dealer, alleging that RAF had not complied with their instructions to limit their options exposure to \$100,000. Lewis also knew that these customers held uncovered options positions that created millions of dollars of exposure and, in or around August 2008, he became aware that RAF's previous broker-dealer had settled the customers' claims for approximately \$5,675,398.

Lewis's heightened supervision plan for RAF did not establish any requirement that RAF's options trades be reviewed to ensure that the customers' options exposure did not exceed authorized limits. Nor did the heightened supervision plan for RAF prohibit RAF from soliciting

options trades or include any measures to ensure that his customers' options trades were unsolicited.

In September 2009, in trades solicited by RAF, three of RAF's customers sold uncovered calls that created excessive risk exposure for each of them. The customers' accounts had not been approved to write uncovered calls. Although Lewis was aware of this, and despite the similarity to the alleged incidents at RAF's previous broker-dealer, Lewis did not implement any measures to ensure that RAF's customers would not engage in unapproved options strategies or that they would not hold options positions that exposed them to excessive risk.

By failing to establish, maintain, and enforce a supervisory system and written supervisory procedures that were reasonably designed to achieve compliance with applicable securities laws and regulations, and with the applicable rules of NASD and FINRA, Lewis violated NASD Conduct Rules 2110 during the period before December 15, 2008, 2860(b)(20)(A) during the period before February 17, 2009, 3010(a), 3010(b)(1), and 3010(c)(1); and FINRA Rules 2010 during the period on and after December 15, 2008 and 2360(b)(20)(A) during the period on and after February 17, 2009.

SECOND CAUSE OF ACTION

Failure to Amend Form U4 to Disclose IRS Liens (NASD By-Laws, Art. V, § 2(c) and FINRA By-Laws, Art. V, § 2(c); NASD IM-1000-1; NASD Conduct Rule 2110; and FINRA Rules 2010 and 1122)

Article V, Section 2(c) of the NASD By-Laws, during the period before July 30, 2007, and FINRA By-Laws, during the period on and after July 30, 2007, requires that “[e]very application for registration filed with [NASD or FINRA] shall be kept current at all times by supplementary amendments” and that “[s]uch amendment to the application shall be filed with [NASD or FINRA] not later than 30 days after learning of the facts or circumstances giving rise to the amendment.”

During the period from January 19, 2005 through August 16, 2009, NASD Membership & Registration IM-1000-1 stated, “The filing with [NASD or FINRA] of information with respect to membership or registration as a Registered Representative which is incomplete or inaccurate so as to be misleading, or which could in any way tend to mislead, or the failure to correct such filing after notice is given thereof, may be deemed to be conduct inconsistent with just and equitable principles of trade and when discovered may be sufficient cause for appropriate disciplinary action.”

During the period on and after August 17, 2009, FINRA Rule 1122 states, “No 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.”

On or about January 19, 2005, Lewis submitted, or caused to be submitted, an Amended Form U4 in connection with his registration through the Firm.

Question No. 14M of the Form U4 asks, “Do you have any unsatisfied judgments or liens against you?” If an affirmative answer is given to Question No. 14M, the registered person is required to provide details regarding the lien or judgment.

In the Amended Form U4 submitted on or about January 19, 2005, Lewis correctly answered Question No. 14M, “No.”

On or about May 2, 2005, the U.S. Internal Revenue Service (“IRS”) filed a lien in the amount of \$33,984.85 against Lewis for unpaid tax liabilities. The lien remained unsatisfied until it was released on or about May 6, 2009.

On or about November 21, 2006, the IRS filed a lien in the amount of \$133,031.50 against Lewis for unpaid tax liabilities. The lien remained unsatisfied until it was released on or about March 28, 2012.

On or about December 23, 2008, the IRS filed a lien in the amount of \$12,904.05 against Lewis for unpaid tax liabilities. The lien remained unsatisfied until it was released on or about December 23, 2009.

On or about September 9, 2010, the IRS filed a lien in the amount of \$54,940.48 against Lewis for unpaid tax liabilities. The lien remains unsatisfied.

On or about December 22, 2010, the IRS filed a lien in the amount of \$22,992.66 against Lewis for unpaid tax liabilities. The lien remains unsatisfied.

On or about January 18, 2011, the IRS filed a lien in the amount of \$22,992.67 against Lewis for unpaid tax liabilities. The lien remains unsatisfied.

The filing of the IRS lien on or about May 2, 2005, caused Lewis's previous "No" answer to Question No. 14M on the Amended Form U4 submitted on or about January 19, 2005, to become inaccurate; and it gave rise to an obligation to submit an amendment to the Form U4 with a "Yes" answer to Question No. 14M, within 30 days after he became aware of the May 2, 2005 IRS lien and to attach a Disclosure Reporting Page setting forth details pertinent to the "Yes" answer.

Each successive IRS lien described above also required disclosure on Lewis's Form U4, within 30 days after he became aware of each successive IRS lien, through the filing of an amended Form U4 and the completion of a Disclosure Reporting Page.

Although he was aware of each IRS lien described above, Lewis did not, within 30 days after he became aware of the facts and circumstances giving rise to each obligation to amend,

submit a supplementary amendment to his Form U4 changing his answer to Question No. 14M and providing information regarding the IRS liens.

During the period from on or about June 1, 2005, until on or about December 8, 2011, Lewis failed to amend his Form U4 to disclose any of the IRS liens described above.

The IRS liens were material facts, in that a reasonable employer, customer, or prospective customer would have viewed the information as relevant to Lewis's business and employment.

By failing to amend his Form U4 to disclose the IRS liens, Lewis violated Article V, Section 2(c) of the NASD By-Laws, during the period before July 30, 2007, and FINRA By-Laws, during the period on and after July 30, 2007; NASD Membership & Registration IM-1000-1 during the period from January 19, 2005, through August 16, 2009; NASD Conduct Rule 2110 during the period before December 15, 2008; and FINRA Rules 1122, during the period on and after August 17, 2009, and 2010, during the period on and after December 15, 2008.

Based on the foregoing, Respondent violated NASD By-Laws, Article V, Section 2(c); FINRA By-Laws, Article V, Section 2(c); NASD Membership & Registration IM-1000-1; NASD Conduct Rules 2110, 2860(b)(20)(A), 3010(a), 3010(b)(1), and 3010(c)(1); and FINRA Rules 1122, 2010, and 2360(b)(20)(A).

Based on these considerations, the sanctions hereby imposed by the acceptance of the Offer are in the public interest, are sufficiently remedial to deter Respondent from any future misconduct, and represent a proper discharge by FINRA, of its regulatory responsibility under the Securities Exchange Act of 1934.

SANCTIONS

It is ordered that Respondent be

- Suspended from association with all FINRA members in all capacities for two years; and

- Fined \$30,000.

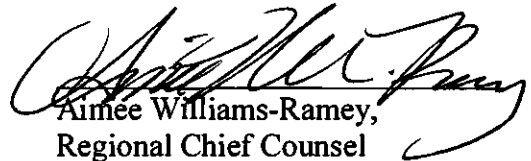
The fine shall be due and payable either immediately upon reassociation with a member firm following the two-year suspension noted above, or prior to any application or request for relief from any statutory disqualification resulting from this or any other event or proceeding, whichever is earlier.

The sanctions imposed herein shall be effective on a date set by FINRA staff.

SO ORDERED.

FINRA

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

A handwritten signature in black ink, appearing to read "Aimee Williams-Ramey", is written over the printed name.

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