SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934
Release No. 80314 / March 27, 2017

Admin. Proc. File No. 3-17402

In the Matter of the Application of

BERNARD G. MCGEE

For Review of Disciplinary Action Taken by

FINRA

OPINION OF THE COMMISSION

REGISTERED SECURITIES ASSOCIATION—REVIEW OF DISCIPLINARY PROCEEDINGS

Fraud

Unsuitable Recommendation

Failure to Provide Written Notice to Firm of Outside Business Activities

Failure to Timely Disclose Material Information on Form U4

Conduct Inconsistent with Just and Equitable Principals of Trade

Former registered representative of FINRA member firm appeals from FINRA disciplinary action finding that he induced an investor's securities transaction through a material omission, made an unsuitable recommendation to an investor, engaged in undisclosed outside business activities, failed to disclose material information to his firm, and misrepresented information on compliance questionnaires. *Held*, association's findings of violations and imposition of sanctions are sustained.

APPEARANCES:

Kevin R. Van Duser, of *Sugarman Law Firm, LLP*, for Bernard G. McGee.

Alan Lawhead, *Jennifer Brooks*, and *Jante Turner* for FINRA.

Appeal filed: August 17, 2016

Last brief received: December 7, 2016

Bernard G. McGee, formerly associated with FINRA member firm Cadaret, Grant & Co., Inc., seeks review of FINRA disciplinary action taken against him. FINRA found that McGee induced an investor to engage in a securities transaction through a material omission and made an unsuitable recommendation. Based on these violations, FINRA imposed a bar from association with any FINRA member firm, and ordered McGee to pay restitution, plus interest. FINRA also found that McGee engaged in undisclosed outside business activities, failed to disclose material information to his firm, and misrepresented information on compliance questionnaires. FINRA did not impose sanctions for those additional violations.

McGee contends that he did not recommend the transaction in question, and thus could not have committed fraud or made an unsuitable recommendation. He also argues that any outside business activities fell within a prior disclosure to his firm, that he timely disclosed material information to his firm, and that he was honest on his compliance questionnaires. Based on our independent review of the record, we reject McGee's contentions and sustain all of FINRA's findings of violations and imposition of sanctions.

I. Background

McGee entered the securities industry in 1988 and was registered continuously until 2016. During the period relevant to this case, McGee was registered as a general securities representative and principal with Cadaret. In October 2012, Cadaret permitted McGee to resign due to his failure to disclose outside business activities; it filed a Form U5 with FINRA. The misconduct identified in the Form U5 commenced FINRA's investigation of McGee's handling of investor CF's account. This proceeding followed.

A. McGee recommended that investor CF surrender her variable annuities and use the proceeds to purchase a charitable gift annuity from a company called 54Freedom.

McGee began managing CF's investments in 2007 when he worked at New England Securities, after CF's previous representative left the firm. CF was 67 years old at the time. She had become a customer of New England Securities after a divorce settlement through which she received a Teachers Insurance and Annuity Association ("TIAA") account, a College Retirement Equities Fund ("CREF") account, and cash. CF had minimal employment outside of the home and, until her divorce, had no experience investing or controlling her finances. CF's investment objective was "long term growth" and her risk tolerance was "moderate." New England Securities discharged McGee shortly after he assumed management of CF's investments, and he took CF's account with him when he transferred to Cadaret.

Between 2007 and 2010, CF purchased four variable annuities at McGee's recommendation—two with The Hartford, and two with Pacific Life Insurance Company. In March 2011, CF's holdings with McGee totaled approximately $840,000.[1] Over half of these holdings were invested in The Hartford and Pacific Life variable annuities.

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[1] CF also maintained $258,000 in the TIAA account, which McGee did not manage.

This case stems from CF's surrender of these variable annuities and use of the proceeds to purchase a charitable gift annuity from a company called 54Freedom.

1. McGee had a business relationship with 54Freedom and its CEO.

In 2008 or 2009, McGee met James Griffin, the founder and CEO of 54Freedom, a corporation that offered insurance and a purported charitable gift annuity program. Charitable gift annuities are investment products that allow individuals to transfer securities or cash to charitable organizations. Through administrators, the charitable organizations issue gift annuities to the individuals in exchange for a current income tax deduction and the organization's agreement to make fixed annual payments for life. Upon the annuitant's death, any remaining funds are disbursed to the charitable organization.[2] According to 54Freedom's marketing materials, the corporation's charitable gift annuity program was a "patent pending" investment opportunity that was "unavailable elsewhere."[3] The materials also stated that the company's "generous street level compensation" for sales personnel was eight percent.

In 2010, McGee proposed to enter into a joint venture with Griffin whereby McGee would sell securities and 54Freedom would sell insurance products. McGee developed a business plan for the joint venture and moved his Cadaret business operations to 54Freedom's premises in late 2010 or early 2011. McGee did not update his Form U4 to reflect his updated business address at 54Freedom's premises until December 5, 2011.

2. McGee recommended 54Freedom's charitable gift annuity program to CF.

In late 2010 or early 2011, McGee advised his assistant that he planned to invest a customer's funds with 54Freedom's charitable gift annuity program to determine whether the program worked. McGee indicated that if it did he would recommend the product to his other clients. McGee discussed 54Freedom with CF in December 2010, and followed up on those discussions by giving her 54Freedom's marketing materials about the charitable gift annuity program.

On March 9, 2011, McGee met with CF at her home, and gave her a portfolio summary listing the total value of CF's variable annuities, the cost basis of the annuities, the anticipated gains associated with their surrender, the estimated taxes due because of their surrender, and the surrender charges for surrendering the variable annuities. During this meeting, McGee provided, and CF signed, the surrender forms for her four variable annuities. McGee submitted the surrender documents, at which time the value of CF's annuities totaled $492,642.

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[2] *See NASD Regulatory & Compliance Alert*, Summer 2002 at 26/27, http://www.finra.org/sites/default/files/RCA/p002369.pdf.

[3] We do not decide whether 54Freedom's investment opportunity qualified as a charitable gift annuity or whether a charitable gift annuity can meet the definition of a security.

In anticipation of CF's receipt of the surrender checks, McGee prepared an analysis—which he did not share with CF—showing that he expected compensation from 54Freedom of $49,264. The Hartford and Pacific Life checks actually totaled $454,998.75—the value of the four annuities at the time of surrender minus surrender charges, administrative fees, and taxes. On March 17, 2011, McGee drove CF to the bank and completed the deposit slip for her; CF deposited the surrender checks into her checking account. McGee asked CF to write a check payable to 54Freedom for $454,998.75, which she did. McGee immediately delivered the check to 54Freedom's office. McGee did not provide CF with any documentation of the transaction or ever disclose his expected, or actual, compensation from 54Freedom to CF or Cadaret.

3. 54Freedom paid compensation to McGee for the transaction and used CF's investment to pay several expenses unrelated to a charitable gift annuity.

54Freedom paid McGee $49,264 on March 25, 2011.[4] McGee testified that he knew this money was compensation for CF's purchase of the 54Freedom charitable gift annuity. 54Freedom used CF's funds to pay several expenses unrelated to CF's charitable gift annuity. 54Freedom spent the rest of CF's investment to purchase three Lincoln Financial fixed indexed annuities on CF's behalf and to make donations on her behalf to three charitable organizations, each with connections to 54Freedom or McGee: 54Freedom's call center; "Creative Healing Connections," founded by a customer of McGee's; and 54Freedom Foundation, which subsequently donated a portion of the money to the Blind Children's Center (an organization established by a 54Freedom board member).[5] As finder's fees for its services, 54Freedom received from the charities approximately 40 to 50% of the donation amount.[6]

B. McGee resigned after Cadaret investigated CF's investment with 54Freedom.

CF was unable to get information from McGee regarding her investment with 54Freedom, so she hired an attorney who contacted McGee in June 2012. McGee responded to the attorney by letter on June 18, 2012, stating that he had "introduced [CF] to a local charitable gifting firm, 54Freedom" but that after the introduction he "was no longer involved in any further processing of her donations." Subsequently, the attorney sent a complaint to Cadaret's compliance department, and Cadaret began an internal investigation.

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[4] The record does not contain an explanation as to why 54Freedom paid McGee 10% of the pre-surrender value of the variable annuities.

[5] FINRA found that 54Freedom invested a total of $429,998 for CF: $254,998 in the fixed indexed annuities and $175,000 in the charities. Together with the $49,264 paid to McGee, the amount exceeds CF's proceeds from the variable annuities by $24,263.25. The record, as FINRA noted, does not explain this inconsistency. We note that McGee does not challenge FINRA's findings as to the amounts invested. In any case, the precise amount invested is not relevant to the issue of McGee's failure to disclose to CF his compensation from 54Freedom.

[6] The record does not contain documentation to validate the status of any of these organizations as bona fide charities or as non-profits.

On August 12, 2012, a Cadaret compliance officer made an unannounced visit to McGee's office to discuss CF's account. McGee said that he had done "consulting" work for 54Freedom, but that with regard to CF he had merely "handed her off" to Griffin. Initially, McGee said that he had not received payment in relation to CF's transactions with 54Freedom, but he eventually conceded that he had received a "referral fee" of approximately $50,000. McGee denied that he received the $50,000 for any specific transaction. McGee also told his Cadaret supervisor during the investigation that he did not receive any compensation directly related to the transactions between CF and 54Freedom.

Cadaret permitted McGee to resign following its investigation and noted on McGee's Form U5 terminating his association with the firm that the resignation was related to undisclosed outside business activities. Subsequently, Griffin was prosecuted and found guilty of ten counts of mail fraud, eight counts of wire fraud, and five counts of money laundering for fraudulently inducing investors to purchase 54Freedom's charitable gift annuities and converting their funds to pay personal expenses and 54Freedom's liabilities.[7] The Commission also has a pending federal civil action against Griffin related to his receipt of investor funds through 54Freedom.[8]

Lincoln Financial refunded CF the $254,998 in premiums that 54Freedom had paid on her behalf for the three fixed indexed annuities. CF has not received a refund for the remaining $200,000 that she invested with 54Freedom.

C. FINRA found that McGee committed fraud, made unsuitable recommendations, and violated other FINRA rules in connection with CF's 54Freedom investment.

FINRA's Department of Enforcement charged McGee with: (1) misrepresenting to CF that she faced a tax liability to induce her to sell her variable annuities and invest in a charitable gift annuity, and failing to disclose the fee he would receive in connection with that transaction, in willful violation of Section 10(b) of the Securities Exchange Act of 1934, Exchange Act Rule 10b-5, and FINRA Rules 2020 and 2010; (2) making unsuitable recommendations to CF that she sell her variable annuities and purchase a charitable gift annuity, in violation of NASD Rule 2310[9], NASD IM-2310-2, and FINRA Rule 2010; (3) failing to disclose his relationship with 54Freedom to his employing member firm, in violation of FINRA Rules 3270 and 2010; (4) failing to timely update his Form U4 to reflect his new office address, in violation of FINRA Rules 1122 and 2010 and Article V, Section 2 of FINRA's By-Laws; and (5) making misrepresentations on member firm compliance questionnaires regarding his email address and

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[7] *United States v Griffin*, Criminal Docket No. 5:15-cr-00207-FJS (N.D.N.Y., filed July 22, 2015). Griffin was sentenced to five years imprisonment and ordered to pay $2,153,530.93 in restitution.

[8] *SEC v. Griffin*, Civil Docket No. 5:15-cv-00927-FJS (N.D.N.Y., filed July 30, 2015).

[9] FINRA Rule 2111, effective July 9, 2012, superseded NASD Rule 2310 and NASD IM-2310-2. *See Regulatory Notice 11-25*, 2011 FINRA LEXIS 45, at *2-4 (May 2011).

whether he had processed transactions away from his firm, in violation of NASD Rule 2110[10] and FINRA Rule 2010.

At the ensuing hearing, McGee denied that he recommended to CF that she sell her variable annuities and purchase a charitable gift annuity from 54Freedom. He asserted instead that CF insisted on the liquidations, and that she independently decided to invest in a charitable gift annuity with 54Freedom. He also maintained that the financial products that 54Freedom purchased with CF's charitable gift annuity investment were not securities. McGee further maintained that he had no obligation to disclose his relationship with 54Freedom as an outside business activity and that he properly disclosed his office and email addresses to his firm.

The Hearing Panel's decision found that, with the exception of the alleged misrepresentation concerning the tax liability, Enforcement proved the charged violations. The Hearing Panel barred McGee for the antifraud and unsuitable recommendation violations. It also ordered McGee to pay CF restitution in the amount of $236,202.50, representing the unreturned portion of CF's investment with 54Freedom, the surrender charges from liquidating the variable annuities, and interest. The Hearing Panel further ordered McGee to disgorge his compensation plus interest. In light of the bar, the Hearing Panel declined to impose any additional sanctions for McGee's failure to disclose his outside business activities, failure to timely update his Form U4, and provision of false information to his member firm. The Hearing Panel also ordered McGee to pay hearing costs of $12,325.34.

McGee appealed the Hearing Panel's decision to FINRA's National Adjudicatory Council ("NAC"). The NAC affirmed the Hearing Panel's findings of liability and the sanctions imposed, except that it did not order disgorgement on the ground that it would be duplicative of his obligation to pay restitution. McGee timely filed this appeal.

II. Analysis

Under Exchange Act Section 19(e)(1), we review FINRA disciplinary action to determine whether the associated person engaged in the conduct that FINRA found, whether such conduct violates the statutes and rules that FINRA specified, and whether FINRA's rules are, and were applied in a manner, consistent with the purposes of the Exchange Act.[11]

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[10] FINRA Rule 2010, effective December 15, 2008, superseded NASD Rule 2110. *See Regulatory Notice 08-57*, 2008 FINRA LEXIS 50, at *30-33 (Oct. 2008).

[11] *See* 15 U.S.C. § 78s(e)(1).

A. We sustain FINRA's finding that McGee committed fraud when he induced CF to liquidate her variable annuities in order to purchase a 54Freedom charitable gift annuity without disclosing his compensation from 54Freedom.

We find that McGee recommended that CF surrender her variable annuities in order to purchase the 54Freedom charitable gift annuity as FINRA found. We also find that by doing so without disclosing his compensation from 54Freedom McGee violated Exchange Act Section 10(b) and Rule 10b-5 thereunder and FINRA Rules 2020 and 2010. We find further that FINRA's rules are, and were applied in a manner, consistent with the purposes of the Exchange Act.

1. McGee recommended the 54Freedom transaction.

McGee argues that he did not recommend that CF liquidate her variable annuities or purchase a 54Freedom charitable gift annuity. According to McGee, it was CF's idea to surrender her variable annuities because her relationship with her daughters had deteriorated and they were listed as beneficiaries. McGee testified that he merely suggested that CF contact 54Freedom to discuss charitable giving, as CF had decided to identify alternatives for her estate. McGee also stated that he was unaware that CF wanted to liquidate her variable annuities and purchase a charitable gift annuity until he went to her home on March 9, 2011. He argues that, because she was adamant, he had no choice but to process her request.

We sustain the NAC's finding based on the testimony of McGee's assistant and the documentary evidence that McGee recommended the transaction to CF. McGee's assistant testified that McGee discussed using CF as a case study with him to determine whether 54Freedom's charitable gift annuity program was effective. The Hearing Panel found this testimony credible. Such credibility determinations are entitled to considerable weight and deference and can be overcome only where there is substantial evidence in the record for doing so.[12] Our *de novo* review of the record finds nothing to contradict the Hearing Panel, and we find that the NAC's reliance on the Hearing Panel's determination was appropriate. McGee's determination to use CF as a case study supports the NAC's finding that it was McGee's idea for CF to invest in 54Freedom.

So does the documentary evidence. McGee gave 54Freedom's marketing materials to CF in January or February 2011. On March 9, 2011, he went to CF's home with all of the necessary surrender forms, which she signed. In anticipation of CF's receipt of the surrender checks, McGee prepared an analysis of the compensation he would receive from 54Freedom for CF's transaction. On March 17, 2011, he prepared CF's deposit slip, took her to the bank, and directed CF to write a check to 54Freedom in the amount she had just deposited. McGee then went directly to 54Freedom to drop off CF's check. One week later, McGee received a payment from 54Freedom for $49,264. Indeed, McGee's written response to the Cadaret compliance

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[12] *See The Dratel Grp., Inc.*, Exchange Act Release No. 72293, 2014 WL 2448896, at *4 n.17 (June 2, 2014).

officer admitted that he had "suggested" the charitable gift annuity to CF. Based on these facts, we sustain FINRA's finding that McGee recommended that CF liquidate her variable annuities and purchase a charitable gift annuity from 54Freedom.

2. McGee's failure to disclose his compensation violated Exchange Act Section 10(b) and Exchange Act Rule 10b-5 and FINRA Rules 2020 and 2010.

A respondent violates Section 10(b) of the Exchange Act and Exchange Act Rule 10b-5 when, in connection with the purchase or sale of a security, and acting with scienter, he omits a material fact despite a duty to speak.[13] McGee does not dispute that he did not inform CF that he would receive compensation from 54Freedom for her purchase of the charitable gift annuity. We find that McGee violated Exchange Act Section 10(b) and Exchange Act Rule 10b-5 because his compensation from 54Freedom was a material fact that he had a duty to disclose, he acted recklessly, and his material omission was in connection with the purchase or sale of a security.

a. McGee's compensation was a material fact that he had a duty to disclose.

We find that, having recommended that CF sell the variable annuities and purchase the 54Freedom charitable gift annuity, McGee had a duty to disclose to CF that he would receive compensation from 54Freedom if she did so. When recommending a security to a customer, a representative has a duty to "disclose material adverse facts of which [he] is aware" such as "economic self-interest" because such facts could influence the representative's recommendation.[14]

McGee's compensation from 54Freedom was a material fact that he should have disclosed to CF. A fact is material if there is a substantial likelihood that a reasonable investor would consider the omitted fact important in making an investment decision.[15] When a representative "has a self-interest (other than the regular expectation of a commission) . . . that could influence [his] recommendation, it is material and should be disclosed."[16] McGee's compensation from 54Freedom was "other than the expected commission" because it came from

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[13] *SEC v. First Jersey Secs.*, 101 F.3d 1450, 1467 (2d Cir. 1996). The respondent must also use the means of interstate commerce. 15 U.S.C. § 78j(b). McGee does not dispute that he communicated with CF via telephone, and sent her surrender forms to The Hartford and Pacific Life by U.S. mail and facsimile.

[14] *See, e.g.*, *Richmark Capital Corp.*, Exchange Act Release No. 48758, 2003 WL 22570712, at *3 (Nov. 7, 2003) (internal quotation omitted); *William Scholander*, Exchange Act Release No. 77492, 2016 WL 1255596, at *5 (Mar. 31, 2016) (citing cases).

[15] *Basic, Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988) (quoting *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)).

[16] *Scholander*, 2016 WL 1255596, at *5 (internal quotations omitted).

the issuer, 54Freedom, as opposed to McGee's member firm.[17] A reasonable investor would consider it material that more than 10% of her investment would be paid back as compensation to the broker by the issuer of the recommended security.[18]

b. McGee acted with scienter.

We also find that McGee acted with scienter when he failed to disclose the compensation that he would receive from 54Freedom for CF's purchase of the charitable gift annuity. Scienter is "a mental state embracing intent to deceive, manipulate, or defraud."[19] Recklessness satisfies the scienter requirement, and is defined as conduct that constitutes "an extreme departure from the standards of ordinary care…to the extent that the danger [of deceiving investors] was either known to the [applicant] or so obvious that the [applicant] must have been aware of it."[20]

McGee had an established business relationship with 54Freedom and Griffin at the time of CF's purchase. He was operating his business from 54Freedom's office space, and planning to enter into a joint business venture with Griffin and 54Freedom. He had also seen marketing material promising generous compensation to sales personnel. He had identified CF as a case study for 54Freedom investments, and prior to CF's investment prepared an analysis that assumed he would receive compensation of $49,264 for CF's purchase of the charitable gift annuity. Based on this evidence, we find, like the NAC, that McGee knew of the compensation he would receive from the transaction. The conflict between his being paid such high compensation from the issuer and his recommendation of the issuer to CF was so great that he must have been aware of the danger of misleading CF by omitting this information. Therefore, we find he acted at least recklessly when he failed to disclose his compensation to CF.

McGee argues that he did not act with scienter because New York insurance law does not require him to disclose commissions earned on fixed annuities. New York law does not govern the conduct in this case; Section 10(b) of the Exchange Act, Exchange Act Rule 10b-5, and FINRA rules apply.[21] In any case, McGee knew that 54Freedom based his compensation on the value of CF's variable annuities as opposed to any fixed annuities.

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[17] *Id.* (distinguishing substantial compensation from the issuer of a security from employer compensation, which an associated person is not required to disclose absent a fiduciary duty).

[18] *See United States v. Nouri*, 711 F.3d 129, 142 (2d Cir. 2013) (finding that bribe received in exchange for a broker's recommendation was material because "[a]t the very least it suggests the customer should seriously question the genuineness or reliability of the recommendation").

[19] *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976).

[20] *Scholander*, 2016 WL 1255596, at *6 (internal citations omitted).

[21] *Cf. Jerome v. United States*, 318 U.S. 101, 104 (1943) (absent an indication that Congress intended otherwise, the meaning of a federal statute will not be dependent on state law).

c. McGee's material omission met the "in connection with" requirement.

We find further that McGee's material omission was in connection with the purchase or sale of securities. The Supreme Court has endorsed the Commission's "consistently . . . broad reading of the … 'in connection with'" requirement.[22] When interpreting the "in connection with" requirement, the Supreme Court has held that the material omission need only "coincide" with the purchase or sale of a security.[23] A security need only be involved on one side of the transaction.[24] McGee's material omission was in connection with CF's sale of the variable annuities, and it is well established that variable annuities are securities.[25]

McGee argues that the "in connection with" requirement is not satisfied because the Lincoln Financial fixed indexed annuities that 54Freedom purchased for CF are not securities. He similarly stated in his Notice of Appeal that "FINRA lacked jurisdiction over this matter where McGee's commission…was not from the sale of a security." These arguments ignore the sale of CF's variable annuities. The sale of the variable annuities was a necessary first step to CF's investment in 54Freedom; without McGee inducing those sales, CF would not have had the money for the subsequent investment. And it was the value of the variable annuities prior to their sale that formed the basis for calculating McGee's compensation.

In *SEC v. Zandford*, the Supreme Court held that the "in connection with" requirement is satisfied where a broker "sells customer securities with intent to misappropriate the proceeds."[26] In that case, the "in connection with" requirement was satisfied even though "the sales themselves were perfectly lawful" because the broker's misappropriation "coincided with the sales."[27] We see little difference between a broker inducing the sale of securities so that he can misappropriate the proceeds and a broker inducing the sale of securities so that he can reinvest the proceeds and receive a portion of the reinvested funds for himself as compensation. As in *Zandford*, the sale of the variable annuities that McGee recommended was part of the same fraud as McGee's failure to disclose his compensation from using the proceeds of those sales to invest with 54Freedom.

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22 *SEC v. Zandford*, 535 U.S. 813, 819 (2002) (internal quotations omitted).

23 *Id.* at 822; *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit*, 547 U.S. 81, 85 (2006).

24 *Zandford*, 535 U.S. at 820-22.

25 *See, e.g., SEC v. Variable Annuity Life Ins. Co. of Am.*, 359 U.S. 65, 67-73 (1959); *Lander v. Hartford Life & Annuity Ins. Co.*, 251 F.3d 101, 109 (2d Cir. 2001).

26 *Zandford*, 535 U.S. at 819-20.

27 *Id.* at 820.

McGee argues that the fact that Griffin, and not he, is the subject of criminal and civil proceedings, is evidence that he has not committed fraud. But the criminal and civil proceedings against another individual do not preclude FINRA from taking disciplinary action.[28] McGee also notes that neither Cadaret nor CF's attorney made a finding that he committed fraud. But there is no evidence that either Cadaret or CF's attorney even investigated fraud allegations. Cadaret investigated McGee's outside business activities, and its investigator testified that he "did not attempt to make a conclusion" as to whether McGee committed fraud. CF's attorney sought only to locate CF's investment with 54Freedom.

The record establishes that McGee made a material omission with scienter in connection with the purchase or sale of a security in violation of Exchange Act Section 10(b) and Rule 10b-5. A violation of these provisions also constitutes a violation of FINRA Rule 2020, which prohibits FINRA members from "effect[ing] any transaction in, or induc[ing] the purchase of, any security by means of any manipulative, deceptive, or other fraudulent device or contrivance."[29] Such conduct also violates Rule 2010, which prohibits conduct inconsistent with just and equitable principles of trade.[30] Therefore, we sustain FINRA's finding that McGee's conduct violated Exchange Act Section 10(b) and Rule 10b-5 and FINRA Rules 2020 and 2010.

3. FINRA Rules 2020 and 2010 are, and were applied in a manner, consistent with the purposes of the Exchange Act.

FINRA Rule 2020 protects investors by prohibiting the same conduct as Exchange Act Section 10(b) and Rule 10b-5. It is therefore consistent with the purposes of the Exchange Act. FINRA applied Rule 2020 in a manner consistent with the purposes of the Exchange Act because a preponderance of the evidence supports FINRA's findings that McGee violated Rule 2020.[31]

FINRA Rule 2010 is consistent with the purposes of the Exchange Act because it reflects the mandate of Exchange Act Section 15(b)(6) that FINRA design its rules to "promote just and

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[28] *Cf. Janet Gurley Katz*, Exchange Act Release No. 61449, 2010 WL 358737, *21 (Feb. 1, 2010) (stating that registered representative "cannot shift the blame for her violations to others or claim that others' misconduct somehow excuses her own misdeeds"), *aff'd*, 647 F.3d 1156 (D.C. Cir. 2011).

[29] *See, e.g.*, *Donner Corp. Int'l*, Exchange Act Release No. 55313, 2007 WL 516282, at *13 (Feb. 20, 2007) (finding the same conduct violated Section 10(b) and Rule 2020's predecessor).

[30] *See Kenny Akindemowo*, Exchange Act Release No. 79007, 2016 WL 5571625, at *5 n.3 (Sept. 30, 2016) (stating that it is well established that a violation of a FINRA conduct rule "is conduct inconsistent with just and equitable principles of trade and therefore is also a violation of FINRA Rule 2010").

[31] *Id.* at *7.

equitable principles of trade."[32] The application of Rule 2010 to McGee's conduct furthered the objective of preventing conduct inconsistent with just and equitable principles of trade.[33]

B. We sustain FINRA's finding that McGee's recommendation that CF surrender the variable annuities and purchase a 54Freedom charitable gift annuity was unsuitable.

As discussed above, we find that McGee recommended that CF liquidate her variable annuities and purchase a charitable gift annuity from 54Freedom. We find that by doing so McGee violated NASD Rule 2310 and NASD IM-2310-2—the customer suitability rules—and FINRA Rule 2010. NASD IM-2310-2 stated that "the fundamental responsibility for fair dealing" is implicit in the relationships between customers and registered representatives.[34] NASD Rule 2310 required that registered representatives 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."[35]

A registered representative must have a reasonable basis for recommending a transaction.[36] This test focuses on the particular recommendation, rather than a particular customer, as a broker cannot determine whether a recommendation is suitable for a particular customer unless he has a "reasonable basis" to believe that the recommendation could be suitable for at least some customers.[37] McGee did not have such a reasonable basis here.

McGee knew almost nothing about charitable gift annuities in general or 54Freedom's charitable gift annuity program. Although McGee argues that 54Freedom appeared to be a successful company, he based this judgment on insufficient evidence. He looked at 54Freedom's website, reviewed its marketing materials, and spoke with Griffin, but he did not do any further research. McGee did not know anything about 54Freedom's financial condition and operations, was unaware of whether anyone else had ever purchased a 54Freedom charitable gift annuity, and wondered to his assistant whether charitable gift annuities even worked. Indeed, McGee knew so little about the financial condition of 54Freedom or its charitable gift annuity program that he used CF as a case study to test the program's viability. He therefore lacked an "'adequate

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32 15 U.S.C. 78o-3(b)(6).

33 *Akindemowo*, 2016 WL 5571625, at *7 n.16.

34 NASD IM-2310-2(a)(1).

35 NASD Rule 2310(a); *William J. Murphy*, Exchange Act Release No. 69923, 2013 WL 3327752, *10 (July 2, 2013), *aff'd*, 751 F.3d 472 (7th Cir. 2014).

36 *Michael Frederick Siegel*, Exchange Act Release No. 58737, 2008 WL 4528192, at *8 n.23 (Oct. 6, 2008), *aff'd in relevant part*, 592 F.3d 147 (D.C. Cir. 2010).

37 *Id.*

and reasonable' understanding of [the] investment before recommending" that a customer sell variable annuity securities in order to purchase 54Freedom's charitable gift annuity.[38]

McGee's recommendation also lacked customer specific suitability. Customer specific suitability requires that a recommendation be consistent with the customer's best interests and financial situation.[39] At the time of the transaction, CF was a 71-year-old retiree with an income of approximately $1,000 a month. She intended to rely on her investments to sustain her for the rest of her life. CF's stated investment objective was "long term growth," and her risk tolerance was "moderate." Nonetheless, McGee recommended that CF surrender nearly half of her assets in order to invest in one company, 54Freedom—an extremely high-risk strategy.[40] Moreover, CF incurred expenses worth nearly eight percent of the value of her variable annuities in surrendering them to generate the money to invest in 54Freedom. This meant that the new investment, whose prospects were unknown to McGee, needed to recoup at least an eight percent return simply to put CF in the position she was in before she started. McGee's compensation further reduced the amount of CF's 54Freedom investment. This sort of blind experiment with such a large portion of the assets of an unsophisticated investor of moderate means seeking moderate risk was unsuitable for this customer.[41] We therefore sustain FINRA's finding that McGee did not have a reasonable basis for recommending the transaction to CF in violation of NASD Rule 2310 and NASD IM 2310-2.

NASD Rule 2310 and NASD IM-2310-2 are consistent with the purposes of the Exchange Act, which is meant to protect investors, because they require that registered representatives make suitable recommendations. FINRA applied these rules in a manner consistent with the Exchange Act. A preponderance of the evidence supports FINRA's

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[38] *See Richard G. Cody*, Exchange Act Release No. 64565, 2011 WL 2098202, at *10 n.20 (May 27, 2011), *aff'd*, 693 F.3d 251 (1st Cir. 2012), *citing Hanley v. SEC*, 415 F.2d 589, 597 (2d Cir. 1969) (finding that broker had an independent obligation to ensure that he understood investment before recommending it); *see also* NASD Regulation, Inc., *Regulatory and Compliance Alert Spring 2002*, at 13 (stating that "members must keep in mind that the suitability rule applies to any recommendation to sell a variable annuity . . . including situations where the member recommends using the proceeds to purchase an unregistered product such as an equity-indexed annuity"), *available at* http://www.finra.org/sites/default/files/RCA/p002370.pdf.

[39] NASD Rule 2310(a); *Cody*, 2011 WL 2098202, at *11.

[40] *See George E. Brooks & Assoc., Inc.*, Exchange Act Release No. 23392, 1998 WL 479756, *4 (Aug. 17, 1998) (finding that representative engaged in unsuitable transactions where he placed "large portions of his clients' funds in one or two stock positions" despite the fact that the clients were elderly and had little investment experience).

[41] *See, e.g.*, *Murphy*, 2013 WL 3327752, at *11 (finding that a highly risky investment strategy was unsuitable for an investor "with only moderate risk tolerance and limited understanding of" the recommended investment).

conclusion that McGee's conduct violated NASD Rule 2310, NASD IM-2310-2, and FINRA Rule 2010.

C. We sustain FINRA's finding that McGee engaged in undisclosed outside business activities because he failed to inform Cadaret of the full extent of his relationship with 54Freedom.

We find that McGee failed to disclose his business relationship with 54Freedom to Cadaret, that this failure violated FINRA Rules 3270 and 2010, and that Rules 3270 and 2010 are, and were applied in a manner, consistent with the purposes of the Exchange Act. McGee failed to disclose his business relationship with 54Freedom until August 2012, after Cadaret received a letter from CF's attorney. This conduct violated FINRA Rule 3270 which provides that "[n]o registered person may be . . . compensated, or have the reasonable expectation of compensation, from any other person as a result of any business activity outside the scope of the relationship with his or her member firm, unless he ... has provided prior written notice to the member."

McGee argues that he informed Cadaret in April 2007 that he acted as an independent insurance agent and that because the charitable gift annuity was an "insurance product," his April 2007 advisement was sufficient. As the NAC stated, this argument demonstrates a "profound misunderstanding of FINRA Rule 3270." FINRA explained in adopting Rule 3270 that even if a registered person has provided some prior notice of an outside business activity, such notice is only valid "to the extent that it continues to accurately describe the outside business activity and, thus, it is incumbent on the registered person to provide prior written notice before altering the nature of any outside business activity previously disclosed in writing to the firm."[42] McGee therefore was required to disclose the full nature of his activity with 54Freedom. McGee, Griffin, and 54Freedom were business partners. Beginning in late 2010 or early 2011, McGee ran his business operations, rent-free, from 54Freedom's office space and proposed a joint venture with 54Freedom in which he planned to sell securities. McGee also received compensation of approximately $50,000 from 54Freedom for selling a charitable gift annuity. As the NAC found, McGee's "narrow disclosure" that he was acting as an independent insurance agent was insufficient notification of his ongoing relationship with 54Freedom and his expectation of compensation from that relationship for selling securities.

We find that FINRA Rule 3270 is consistent with the purposes of the Exchange Act because it ensures that member firms may raise objections to an associated person's outside business activities at a meaningful time and exercise appropriate supervision.[43] FINRA applied

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[42] Securities Exchange Act Release No. 62762 (Aug. 23, 2010), 75 Fed. Reg. 53,362 (Aug. 31, 2010) (SR-FINRA-2009-042).

[43] *Proposed Rule Change by NASD Relating to Outside Business Activities of Associated Persons*, Exchange Act Release No. 26063, 1988 WL 902707 (Sept. 6, 1988); *Kent M. Houston*, Exchange Act Release No. 71589, 2014 WL 651953, at *4 (Feb. 20, 2014).

the rules in a manner consistent with the purposes of the Exchange Act here because a preponderance of the evidence supports FINRA's conclusion that McGee violated Rules 3270 and 2010.

D. We sustain FINRA's finding that McGee failed to timely disclose material information on his Form U4.

We find that McGee failed to timely disclose material information on his Form U4, that by doing so he violated Section 2(c) of Article 5 of FINRA's By-Laws and FINRA Rules 1122 and 2010, and that those provisions are, and were applied in a manner, consistent with the purposes of the Exchange Act. McGee failed to update his Form U4 to reflect that he moved his business operations to 54Freedom's office space in late 2010 or early 2011 until about a year later. During his on-the-record testimony in 2012 and 2013, McGee testified that he moved to 54Freedom's premises in late 2010 or early 2011, and was working there when he processed CF's transaction with 54Freedom in March 2011. During the hearing, McGee testified that his earlier testimony was a misstatement and that he moved to 54Freedom's premises in late 2011 or early 2012. We sustain the NAC's reliance on McGee's on-the-record testimony. The on-the-record testimony of McGee's assistant corroborates that testimony,[44] and McGee's on-the-record testimony occurred closer in time to the underlying events and before he was charged.

McGee's failure to update his Form U4 until approximately a year after he moved his business operations to 54Freedom's office space violated FINRA's By-Laws and rules. Section 2(c) of Article 5 of FINRA's By-Laws provides that every application for registration, including the Form U4, must be kept current at all times by filing supplementary amendments within 30 days of learning of the facts or circumstances giving rise to the amendment. Similarly, FINRA Rule 1122 provides that no person associated with a member shall file incomplete or inaccurate information with respect to membership or registration "so as to be misleading, or which could in any way tend to mislead, or fail to correct such filing after notice thereof."

These provisions are consistent with the purposes of the Exchange Act because Form U4 is a "critically important regulatory tool" that assists regulatory agencies in determining and monitoring the fitness of securities professionals.[45] FINRA applied those provisions consistent with the purposes of the Exchange Act because the evidence supports the finding of a violation.

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[44] McGee argues that his assistant's hearing testimony that he purchased business cards in January 2012 demonstrates the timing of the move to 54Freedom's offices. The NAC agreed with the Hearing Panel's determination that the assistant's on-the-record testimony was temporally closer to the underlying events and therefore more reliable, and we sustain that determination.

[45] *Joseph S. Amudsen*, Exchange Act Release No. 69406, 2013 WL 1683914, *6 (April 18, 2013).

E. We sustain FINRA's finding that McGee engaged in conduct inconsistent with the just and ethical principles of trade when he made false statements on compliance questionnaires.

We find that McGee made false statements on compliance questionnaires, that such false statements violated FINRA rules, and that such rules are and were applied in a manner consistent with the Exchange Act. Cadaret asked McGee to disclose on an annual compliance questionnaire all of his business-related email addresses and any involvement in the offer or sale of non-Cadaret processed securities or investments without his firm's approval. From 2007 through 2011, McGee failed to disclose a Yahoo account that he used for securities business. While McGee argues in his brief that he only used the Yahoo account for insurance business, his assistant testified that McGee typically used the Yahoo account to communicate with him about work-related matters. McGee himself testified that, although it was not his "intention" to use his Yahoo email address for securities business, it "ended up happening sometimes." And McGee previously signed an affidavit in which he stated that he used the Yahoo email address for securities business while at Cadaret. In light of this evidence, we sustain the NAC's finding that McGee used his Yahoo email for securities business and failed to disclose it.

McGee also failed to disclose his involvement in the purchase of the charitable gift annuity for CF. McGee sold the charitable gift annuity to CF in March 2011. But he falsely stated on a July 2011 compliance questionnaire that he had not been involved in the offer or sale of any security or investment that was not processed through Cadaret or with Cadaret's written permission.

These false statements violated NASD Rule 2110 and FINRA Rule 2010. As discussed above, FINRA Rule 2010 provides that an associated person must observe high standards of commercial honor and just and equitable principles of trade. The standard applies to all business-related misconduct, regardless of whether the conduct involves securities.[46] We find that McGee's omissions on his compliance questionnaires were inconsistent with just and equitable principles of trade. For the reasons discussed above, we find that Rule 2010 is, and was applied in a manner, consistent with the purposes of the Exchange Act.

III. Sanctions

Pursuant to Exchange Act Section 19(e)(2), we must sustain FINRA's sanctions unless we find, having due regard for the public interest and the protection of investors, that the sanctions are excessive or oppressive or impose an unnecessary or inappropriate burden on competition.[47] Pursuant to this review, we must consider any aggravating or mitigating factors.[48]

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[46] *Vail v. SEC*, 101 F.3d 37, 39 (5th Cir. 1996) (internal citations omitted).

[47] 15 U.S.C. § 78s(e)(2).

[48] *Saad v. SEC*, 718 F.3d 904, 906 (D.C. Cir. 2013) (citing *PAZ Sec., Inc. v. SEC*, 494 F.3d 1059, 1065 (D.C. Cir. 2007)).

The Commission is not bound by FINRA's Sanction Guidelines; however, we use them as a benchmark in conducting our review under Section 19(e)(2).[49]

A. The bar FINRA imposed on McGee is neither excessive nor oppressive.

FINRA's Sanction Guidelines recommend consideration of a bar in particularly egregious situations where an associated person engaged in reckless or intentional misrepresentations.[50] We agree with FINRA that aggravating factors demonstrate that McGee's fraudulent omission and unsuitable recommendation were egregious and justify a bar. McGee persuaded CF to liquidate nearly half of her investment holdings and invest those assets with 54Freedom, even though CF incurred nearly $40,000 in various expenses by doing so and McGee knew almost nothing about 54Freedom's financials or operations. As a result of this transaction, CF lost $200,000.[51] McGee, on the other hand, earned $49,264 in compensation from 54Freedom.[52]

Moreover, even though CF was 71 years old at the time of the transaction, financially unsophisticated, and receiving income of only $1000 a month, McGee chose her to serve as a case study to determine whether 54Freedom's charitable gift annuity program worked.[53] McGee violated his duty as a broker to disclose to CF that he would receive compensation from her investment in 54Freedom. McGee even attempted to conceal his misconduct during Cadaret's investigation.[54]

We agree with FINRA that significant aggravating factors are present in this case. We have also held that violations involving fraud are particularly serious and should be subject to the most severe sanctions.[55] Barring McGee will protect the public by preventing McGee from defrauding other customers. It will also encourage other registered representatives to disclose material information to their customers when they recommend securities transactions. For all of these reasons, we sustain FINRA's imposition of a bar.

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[49] *See, e.g.*, *John Joseph Plunkett*, Exchange Act Release No. 69766, 2013 WL 2898033, at *11 (June 14, 2013).

[50] Guidelines at 87.

[51] *Id.* at 6 (providing that whether the respondent's misconduct resulted in harm to the investing public is a principal consideration in determining the appropriate sanction).

[52] *Id.* at 7 (providing that whether the misconduct resulted in monetary gain for the respondent is a principal consideration in determining the appropriate sanction).

[53] *Id.* (providing that whether the affected customer was sophisticated is a principal consideration in determining the appropriate sanction).

[54] *Id.* (providing that whether the respondent attempted to conceal his misconduct is a principal consideration in determining the appropriate sanction).

[55] *Scholander*, 2016 WL 1255596, at *9.

B. The restitution FINRA ordered is neither excessive nor oppressive.

FINRA's Sanction Guidelines provide that FINRA may order restitution when an identifiable individual has "suffered a quantifiable loss" that was "proximately caused by [the] respondent's misconduct."[56] CF suffered a loss of $237,643.25 as a result of McGee's fraud and unsuitable recommendation—the $200,000 that CF has not recouped from her investment with 54Freedom, the variable annuity surrender charges of $36,202.50, and taxes and administrative fees of $1,440.75. We have held that restitution is appropriate when it is necessary to restore the status quo ante in those situations where a victim would otherwise suffer unjust loss,[57] and we therefore sustain FINRA's imposition of restitution as well.[58]

An appropriate order will issue.[59]

By the Commission (Acting Chairman PIWOWAR and Commissioner STEIN).

Brent J. Fields
Secretary

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[56] Guidelines at 4.

[57] *See Joseph R. Butler*, Exchange Act Release No. 77984, 2016 WL 3087507, at *9.

[58] We also sustain FINRA's imposition of costs, as we find the sanctions FINRA imposed were appropriately tailored to the misconduct. *See Scholander*, 2016 WL 1255596, at n.68.

[59] We have considered all of the parties' contentions. We have rejected or sustained them to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 80314 / March 27, 2017

Admin. Proc. File No. 3-17402

In the Matter of the Application of

BERNARD G. MCGEE

For Review of Disciplinary Action Taken by

FINRA

ORDER SUSTAINING DISCIPLINARY ACTION TAKEN BY FINRA

On the basis of the Commission's opinion issued this day, it is

ORDERED that the disciplinary action taken by FINRA against Bernard G. McGee be, and it hereby is, sustained.

By the Commission.

Brent J. Fields
Secretary