

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER, AND CONSENT
No. 2018059223501**

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

RE: Frank H. Zito (Respondent)
General Securities Representative
CRD No. 2766336

Pursuant to FINRA Rule 9216, Respondent Frank H. Zito submits this Letter of Acceptance, Waiver, and Consent (AWC) for the purpose of proposing a settlement of the alleged rule violations described below. This AWC is submitted on the condition that, if accepted, FINRA will not bring any future actions against Respondent alleging violations based on the same factual findings described in this AWC.

I.

ACCEPTANCE AND CONSENT

- A. Respondent hereby accepts and consents, without admitting or denying the findings and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to which FINRA is a party, prior to a hearing and without an adjudication of any issue of law or fact, to the entry of the following findings by FINRA:

BACKGROUND

Zito first entered the securities industry in 1996. From March 2010 through July 2018, Zito was registered with FINRA as a general securities representative through an association with Merrill Lynch, Pierce, Fenner & Smith Incorporated. Merrill Lynch discharged Zito for “conduct including failure to adhere to Firm standards regarding selling away and failure to fully disclose participation in an outside business activity.” Zito is currently associated with another FINRA member firm.

Respondent does not have any relevant disciplinary history.

OVERVIEW

Between May 2013 and March 2018, Zito participated in 15 private securities transactions without providing prior written notice to his FINRA member firm, in violation of NASD Rule 3040 and FINRA Rules 3280 and 2010. In addition, between October 2012 and March 2018, Zito received compensation as a result of engaging in an outside business activity without ever disclosing that fact to his FINRA member firm, in violation of FINRA Rules 3270 and 2010.

FACTS AND VIOLATIVE CONDUCT

This matter originated from a June 2018 Form U5 disclosure by Zito's former member firm, Merrill Lynch, that it had terminated Zito's employment. This termination was precipitated by a May 2018 arbitration filing in which a Merrill Lynch customer alleged that he had cumulatively invested a total of \$5 million in Madison Timber Properties, LLC (MTP) promissory notes on Zito's recommendation and that this recommendation was unsuitable.

Madison Timber Properties

In April 2018, the SEC filed a complaint against MTP and its owner alleging that MTP was a Ponzi scheme that bilked at least 150 investors out of \$85 million. In May 2018, MTP's owner pleaded guilty to criminal charges related to his role in the Ponzi scheme.

Zito first learned of MTP in June 2010, when he met with MTP's owner to discuss Zito personally investing in MTP. During that meeting, MTP's owner told Zito that MTP was raising capital from private investors by issuing promissory notes that repaid principal, plus 12% interest. He further explained to Zito that MTP supposedly:

- gave each investor a signed deed to the timber as security for the investment;
- used money raised from investors to purchase timber from Mississippi landowners; and
- "pre-sold" timber to lumber mills before even acquiring rights to harvest it, ostensibly for a significant profit.

MTP also required investors to enter into strict confidentiality agreements that purported to prevent inquiry into the validity of the timber deeds, the company's contractual relationships with lumber mills, its financial records, or any other significant aspect of its operations.

Notwithstanding this lack of transparency, Zito decided to invest in MTP and did so steadily from July 2010 until April 2018. During that time, Zito generally held three promissory notes with staggered maturities simultaneously. As one note matured, he moved the returned principal into a new note.

Zito failed to provide prior written notice to his FINRA member firm before participating in private securities transactions.

FINRA Rule 3280 and its predecessor, NASD Rule 3040,¹ place requirements on persons associated with FINRA members who participate "in any manner in a private securities transaction," which is defined as "any securities transaction outside the regular course or scope of an associated person's employment with a member." Before participating in any

¹ FINRA Rule 3280 superseded NASD Rule 3040 as of September 21, 2015.

such transaction, the associated person must provide his or her member firm with prior written notice “describing in detail the proposed transaction and the person’s proposed role therein” A violation of FINRA Rule 3280 or NASD Rule 3040 constitutes a violation of FINRA Rule 2010, which requires persons associated with FINRA members to “observe high standards of commercial honor and just and equitable principles of trade.”

In May 2013, Zito recommended MTP to RF, one of his customers at Merrill Lynch. Zito told RF about his personal experience as an investor and relayed his understanding of how the investments and the business worked. Shortly afterward, RF began investing in MTP. Zito coordinated RF’s investments in MTP with his own. Zito communicated with RF regularly about the promissory notes, the payments connected to them, and the paperwork related to the investments. Like Zito, RF maintained investments in three promissory notes simultaneously, which accounted for a consistent principal outlay of \$1.0 million. This pattern continued for nearly five years, until the Ponzi scheme unraveled, during which time RF invested in 15 promissory notes totaling \$5 million. Zito received nearly \$100,000 in compensation as commissions on RF’s investments.

Zito did not disclose his participation in these private securities transactions to Merrill Lynch. Moreover, from 2014 through 2017, Zito submitted four annual certifications to Merrill Lynch in which he denied recommending any offerings or private securities transactions that were not offered through Merrill Lynch.

Therefore, Zito violated NASD Rule 3040 (for conduct before September 21, 2015), FINRA Rule 3280 (for conduct on and after September 21, 2015), and FINRA Rule 2010.

Zito failed to provide prior written notice to his FINRA member firm before engaging in outside business activities.

FINRA Rule 3270 requires all persons who are registered with a FINRA member to provide prior written notice to that member before engaging in any outside business activity, which includes anything that results in compensation or “the reasonable expectation of compensation . . . as the result of any business activity outside the scope of the relationship with his or her member firm” A violation of Rule 3270 constitutes a violation of FINRA rule 2010.

During 2011 and 2012, Zito was involved in trying to help MTP’s owner find underwriting for a notional private-placement equity offering related to MTP. Zito inquired of various financial firms about their potential interest in the offering and arranged a meeting between the offering’s backers and representatives of a local business-advisory firm. Although MTP engaged the business-advisory firm, the notional private-placement offering never came to fruition.

Nonetheless, in October 2012, Zito began receiving sporadic payments from MTP as compensation for his efforts. Even though the offering never raised any money, MTP

continued these payments to Zito, in varying amounts and intervals, through March 2018, until they totaled nearly \$130,000.²

Zito failed to provide Merrill Lynch with written notice that he was receiving compensation from MTP as the result of an outside business activity at any time between October 2012 and March 2018. Moreover, during that time Zito submitted five annual certifications to Merrill Lynch in which he denied being paid by any third party for business conducted outside of the firm.

Therefore, Zito violated FINRA Rules 3270 and 2010.

B. Respondent also consents to the imposition of the following sanctions:

- A 16-month suspension from associating with any FINRA member in any capacity and
- a \$10,000 fine.

Respondent agrees to pay the monetary sanction upon notice that this AWC has been accepted and that such payment is due and payable. Respondent has submitted an Election of Payment form showing the method by which he proposes to pay the fine imposed.

Respondent specifically and voluntarily waives any right to claim an inability to pay, now or at any time after the execution of this AWC, the monetary sanction imposed in this matter.

The fine shall be due and payable either immediately upon reassociation with a member firm 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 in this AWC shall be effective on a date set by FINRA.

II.

WAIVER OF PROCEDURAL RIGHTS

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

- A. To have a complaint issued specifying the allegations against him;
- B. To be notified of the complaint and have the opportunity to answer the allegations in writing;

² In November 2018, Zito entered into a consent order with the Securities Division of the Mississippi Secretary of State (Case No. LS-18-3126) pursuant to which he agreed to findings that he engaged in unauthorized private securities transactions and undisclosed outside business activities. He agreed in that consent order to pay \$200,000 to the Receiver for MTP.

- C. To defend against the allegations in a disciplinary hearing before a hearing panel, to have a written record of the hearing made, and to have a written decision issued; and
- D. To appeal any such decision to the National Adjudicatory Council (NAC) and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

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

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

III.

OTHER MATTERS

Respondent understands that:

- A. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by the NAC, a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs (ODA), pursuant to FINRA Rule 9216;
- B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against Respondent; and
- C. If accepted:
 - 1. this AWC will become part of Respondent's permanent disciplinary record and may be considered in any future action brought by FINRA or any other regulator against Respondent;
 - 2. this AWC will be made available through FINRA's public disclosure program in accordance with FINRA Rule 8313;
 - 3. FINRA may make a public announcement concerning this agreement and its subject matter in accordance with FINRA Rule 8313; and
 - 4. Respondent may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying,

directly or indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. Respondent may not take any position in any proceeding brought by or on behalf of FINRA, or to which FINRA is a party, that is inconsistent with any part of this AWC. Nothing in this provision affects Respondent's testimonial obligations or right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.

- D. Respondent may attach a corrective action statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Respondent understands that he may not deny the charges or make any statement that is inconsistent with the AWC in this statement. This statement does not constitute factual or legal findings by FINRA, nor does it reflect the views of FINRA.

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

11/25/2020

Date

Frank H. Zito

Frank H. Zito
Respondent

Reviewed by:

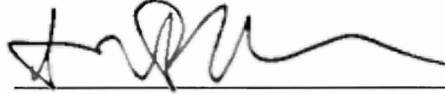
John C. Anjier
Counsel for Respondent
Liskow & Lewis
701 Poydras Street, Suite 5000
New Orleans, LA 70139

Accepted by FINRA:

12/18/2020

Date

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

A handwritten signature in black ink, appearing to read 'Adam B. Walker', written over a horizontal line.

Adam B. Walker
Senior Counsel
FINRA
Department of Enforcement
120 W. 12th St.
Kansas City, Missouri 64105