

NASD
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. E8A2005013001

TO: Department of Enforcement
NASD

RE: Lexington Investment Company, Inc.
(CRD No. 27393)

Pursuant to Rule 9216 of NASD Code of Procedure, Lexington Investment Company, Inc. ("Member") submits this Letter of Acceptance, Waiver and Consent ("AWC") for the purpose of proposing a settlement of the alleged rule violations described in Part II below. This AWC is submitted on the condition that, if accepted, NASD will not bring any future actions against the Member alleging violations based on the same factual findings.

The Member understands that:

1. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by NASD's Department of Enforcement and National Adjudicatory Council ("NAC") Review Subcommittee or Office of Disciplinary Affairs ("ODA"), pursuant to NASD Rule 9216;
2. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against the Member; and,
3. If accepted:
 - a. this AWC will become part of the Member's permanent disciplinary record and may be considered in any future actions brought by NASD or any other regulator against it;
 - b. this AWC will be made available through NASD's public disclosure program in response to public inquiries about the Member's disciplinary record;
 - c. NASD may make a public announcement concerning this agreement and the subject matter thereof in accordance with NASD Rule 8310 and IM-8310-2; and,
 - d. the Member 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 allegation in this AWC or create the impression that the AWC is without factual basis. Nothing in

this provision affects the Member's testimonial obligations or right to take legal or factual positions in litigation or other legal proceedings in which NASD is not a party.

The Member also understands that its experience in the securities industry and disciplinary history may be factors that will be considered in deciding whether to accept this AWC. That experience and history are as follows:

Lexington Investment Company, Inc. became a member of NASD on November 19, 1990, and became registered with the Securities and Exchange Commission ("SEC") on November 2, 1990. The Member conducts a general securities business on a fully disclosed basis. The Member's membership with NASD and registration with the SEC remain currently in effect. The Member has no history of disciplinary action.

I.

WAIVER OF PROCEDURAL RIGHTS

The Member specifically and voluntarily waives the following rights granted under NASD's Code of Procedure:

- A. To have a Formal Complaint issued specifying the allegations against it;
- B. To be notified of the Formal Complaint and have the opportunity to answer the allegations in writing;
- 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 NAC and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, the Member specifically and voluntarily waives any right to claim bias or prejudice of the General Counsel, 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 acceptance or rejection of this AWC.

The Member further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of Rule 9143 or the separation of functions prohibitions of 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.

II.

ACCEPTANCE AND CONSENT

- A. The Member hereby accepts and consents, without admitting or denying the allegations or findings, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of NASD, or to which NASD 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 NASD:

**Effecting Securities Transactions while failing to Maintain the
Minimum Required Net Capital, Maintaining Inaccurate Books
and Records and Filing Inaccurate FOCUS Reports, in violation of
SEC Rules 15c3-1, 17a-3(a) and 17a-5 and
NASD Conduct Rules 2110 and 3110(a)**

1. On January 30, 2004, February 27, 2004, March 31, 2004, April 30, 2004, May 28, 2004, June 30, 2004, July 30, 2004, August 31, 2004, September 30, 2004, October 29, 2004, November 30, 2004, December 31, 2004 and January 31, 2005, the Member, failed to comply with SEC Rule 15c3-1, in that it used the mails or other means or instrumentalities of interstate commerce to effect transactions in securities, while the Member failed to maintain the minimum required net capital, as shown on Schedule A attached hereto and incorporated by reference, in violation of SEC Rule 15c3-1 and NASD Conduct Rule 2110 by the Member. On February 7, 2005, the Member's accountants informed the Member that the Member was in net capital violation beginning in January 2004. The reason for this was because the Member had a stock repurchase agreement, which stated that "in the event of the death of a stockholder the Personal Representative of such deceased stockholder shall have the right and option, but not the obligation, to put or sell all of such deceased stockholder's shares to the corporation, and upon exercise of such option the corporation shall be obligated to purchase all of such deceased stockholder's shares" This provision meant that the Member has the obligation to purchase all of the shares held by the deceased shareholder. Pursuant to Financial Accounting Standards Board ("FASB") Statement No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity* ("Statement 150"), the Member was required to reclassify its net equity as a liability, which caused it to eliminate its net worth beginning January 1, 2004. The

deficiencies of the Member's minimum required net capital covered a long period of time because the Member was unaware of the effect of Statement 150 until its accountant informed them of it in February 2005.

2. The Member failed to comply with SEC Rule 17a-3(a), in that it prepared an inaccurate trial balance and net capital computation for January 30, 2004, February 27, 2004, March 31, 2004, April 30, 2004, May 28, 2004, June 30, 2004, July 30, 2004, August 31, 2004, September 30, 2004, October 29, 2004, November 30, 2004, December 31, 2004 and January 31, 2005, in that the Member overstated its net capital by varying amounts as shown on Schedule A, for the reasons stated above, which resulted in a deficiency in the Member's required minimum net capital, in violation of SEC Rule 17a-3(a) and NASD Conduct Rules 2110 and 3110(a) by the Member.
3. The Member failed to comply with SEC Rule 17a-5, in that it filed an NASD FOCUS Part IIA Report for the calendar months ending March 31, 2004, June 30, 2004, September 30, 2004, and December 31, 2004, which were inaccurate in that, among other things, the Report overstated the Member's net capital, as noted above, in violation of SEC Rule 17a-5 and NASD Conduct Rule 2110 by the Member.

**Holding Employee Funds Intended for Deposit in a 401k Plan in
Violation of the Member's Membership Agreement and
SEC Rule 15c3-3(k)(2)(ii) and
NASD Conduct Rule 2110.**

4. On July 14, 2003, the Member entered into a Membership Agreement with NASD, under which it agreed that it will not hold customer funds or safe keep customer securities.
5. From November 24, 2004 to December 1, 2004, the Member deducted a total of \$615.60 from the salaries of four of its employees for deposit in the Member's 401(k) fund and held the funds until they were deposited in the 401(k) fund on December 13, 2004. On December 21, 2004, the Member deducted a total of \$3,247.73 from the salaries of two of its employees for deposit in the Member's 401(k) fund and held the funds until they were deposited in the 401(k) fund on December 28, 2004. On January 12, 2005, the Member deducted a total of \$7,925.82 from the salaries of eight of its employees for deposit in the Member's 401(k) fund and held

the funds until they were deposited in the 401(k) fund on January 13, 2005. Such conduct violates SEC Rules 15c3-3(k)(2)(ii) and 15c3-1 and NASD Conduct Rule 2110, by the Member.

**Failure to Promptly Report Municipal Securities Transactions and
Failure to Establish, Maintain and Enforce Adequate Written
Supervisory Procedures, in Violation of Municipal Securities
Rulemaking Board ("MSRB") Rules G-14 and G-27(c).**

6. During the relevant time period, MSRB Rule G-14 required all brokers, dealers and municipal securities dealers (collectively "dealers") to report trades to MSRB by midnight of the date that the trade was executed. The MSRB published data about all reported municipal securities transactions, including, but not limited to, time of trade, price and volume information. If municipal trade data is unavailable or incorrect because trades were not reported in a timely manner or included erroneous data, dealers and investors alike, experience harm because they cannot obtain an accurate picture of market activity and prices. Late or inaccurate transaction data may hinder a dealer's ability to price municipal securities accurately for customers, and, in turn, interferes with an investor's decision-making process.¹ Additionally, accurate and timely municipal trade reporting forms the primary audit trail for regulators to conduct surveillance for potentially manipulative practices, as well as detect sales practice violations and other violations of the federal securities laws and MSRB rules.
7. The MSRB prepared a Customer Transaction Compliance Report ("Report") during the years 2004 and 2005, which showed the total number of municipal trades effected by the Member on a monthly basis along with a percentage of the number of trades which were reported late. The Report also supplied industry averages for the percentages of late reported trades. This Report shows that for nine months from January

¹ Since 1994, NASD and the MSRB have repeatedly advised dealers of their responsibility to report transactions accurately. See "Enforcement Initiative," *MSRB Reports*, Vol. 14, No. 3 (June 1994) at 35; NASD *Regulatory and Compliance Alert*: "Introducing Firm Responsibility When Reporting Municipal Trades Through Service Bureaus and Clearing Firms" (Winter 2000); NASD *Regulatory and Compliance Alert*: "Municipal Securities Transaction Reporting Compliance Information" (Spring 2001); and NASD *Notice to Members 03-13*: "MSRB Rules G-12 and G-14" jointly issued with the MSRB in March 2003 as MSRB *Notice 2003-7*. The MSRB has also advised dealers of their responsibility to ascertain the market value of municipal securities they trade so their customers receive prices that are reasonably related to the market value of the securities (See MSRB *Notice 2004-3*: "Review of Dealer Pricing Responsibilities," January 26, 2004).

which were reported late were substantially larger than the Industry Average, as shown below.

<u>Month</u>	<u>Number of the Member's Trades</u>	<u>Percentage Reported Late</u>	<u>Industry Average</u>
January 2004	9	33.3%	3.6%
April 2004	14	28.6%	3.3%
May 2004	32	21.9%	3.2%
June 2004	21	9.5%	2.9%
July 2004	20	5.0%	3.2%
September 2004	36	5.6%	3.0%
November 2004	16	6.3%	3.4%
December 2004	9	22.2%	5.8%
January 2005	12	16.7%	3.9%

In addition, on December 17, 2004 and January 4, 2005, the Member executed two municipal securities transactions, which were not timely reported. Such acts, practices, and conduct constitute violations of MSRB Rule G-14 by the Member.

8. From approximately January 2004 through February 2005, 2005, the Member failed to establish, maintain and enforce adequate written supervisory procedures that were reasonably designed to achieve compliance with the applicable MSRB Rules related to the reporting of transactions in municipal securities. Such acts, practices, and conduct constitute a violation of MSRB Rule G-27(c) by the Member.

- B. The Member also consents to the imposition, at a maximum, of the sanctions of a censure and a fine of \$15,000.

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

III.

OTHER MATTERS

- A. The Member understands that it may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. The Member also understands that it 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 NASD, nor does it reflect the views of NASD or its staff.
- B. The Member agrees to pay any monetary sanctions imposed on it upon notice that this AWC has been accepted and that such payments are due and payable and have attached Election of Payment forms showing the method by which it proposes to pay any fine imposed.
- C. The Member specifically and voluntarily waives any right to claim that it is unable to pay, now or at any time hereafter, any monetary sanction imposed in this matter.

The Member certifies that a duly authorized officer of the Member has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it, and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein, has been made to induce the Member to submit it.

Lexington Investment Company, Inc.

6/21/06
Date

Richard S. Schultz
By Richard S. Schultz
Its President

Reviewed by:

N/A
Counsel for Respondent

Accepted by NASD:

6/21/06
Date

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

Richard S. Schultz
Richard S. Schultz
Regional Counsel
NASD Department of Enforcement
55 West Monroe Street, Suite 2700
Chicago, Illinois 60603-5052
(312)899-4330

NASD District Director
Carlotta A. Romano
Senior Vice President and Regional Director
NASD, District 8
55 West Monroe Street, Suite 2700
Chicago, Illinois 60603-5052

Lexington Investment Company, Inc. Net Capital Computation Comparisons for the Period From January 2004 Through January 2005.

	January 30, 2004		February 27, 2004		March 31, 2004	
	<u>Firm</u>	<u>Staff</u>	<u>Firm</u>	<u>Staff</u>	<u>Firm</u>	<u>Staff</u>
Net Worth	\$ 410,049.00	\$ -	(a) \$ 407,055.00	\$ -	(a) \$ 427,340.00	\$ -
Non allowable Assets	\$ 66,820.00	\$ 66,820.00	\$ 60,443.00	\$ 60,443.00	\$ 181,389.00	\$ 181,389.00
Tentative Net Capital	\$ 343,229.00	\$ (66,820.00)	\$ 346,612.00	\$ (60,443.00)	\$ 245,951.00	\$ (181,389.00)
Haircuts	\$ 1,726.00	\$ 1,726.00	\$ 1,739.00	\$ 1,739.00	\$ 2,175.00	\$ 2,175.00
Net Capital	\$ 341,503.00	\$ (68,546.00)	\$ 344,873.00	\$ (62,182.00)	\$ 243,776.00	\$ (183,564.00)
Minimum Requirement	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00
Excess Net Capital	\$ 241,503.00	\$ (168,546.00)	\$ 244,873.00	\$ (162,182.00)	\$ 143,776.00	\$ (283,564.00)

(a) The Member's Net Worth was deemed to be \$0, based on Financial Accounting Standards Board (FASB) released Statement No. 150, and the Member's Shareholder's Agreement. The Shareholder's Agreement stated that shockholder shares were mandatorily redeemable, which under FASB Statement No. 150 reclassified the owner's equity as a liability and reduced the net worth of the Member to \$0.

Lexington Investment Company, Inc. Net Capital Computation Comparisons for the Period From January 2004 Through January 2005.

	April 30, 2004		May 28, 2004		June 30, 2004	
	<u>Firm</u>	<u>Staff</u>	<u>Firm</u>	<u>Staff</u>	<u>Firm</u>	<u>Staff</u>
Net Worth	\$ 444,685.00	\$ -	(a) \$ 485,562.00	\$ -	(a) \$ 514,572.00	\$ -
Non allowable Assets	\$ 179,265.00	\$ 179,265.00	\$ 182,875.00	\$ 182,875.00	\$ 186,846.00	\$ 186,846.00
Tentative Net Capital	\$ 265,420.00	\$ (179,265.00)	\$ 302,687.00	\$ (182,875.00)	\$ 327,726.00	\$ 186,846.00
Haircuts	\$ 1,961.00	\$ 1,961.00	\$ 1,912.00	\$ 1,912.00	\$ 1,229.00	\$ 1,229.00
Net Capital	\$ 263,459.00	\$ (181,226.00)	\$ 300,775.00	\$ (184,787.00)	\$ 326,497.00	\$ (188,075.00)
Minimum Requirement	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00
Excess Net Capital	\$ 163,459.00	\$ (281,226.00)	\$ 200,775.00	\$ (284,787.00)	\$ 226,497.00	\$ (288,075.00)

(a) The Member's Net Worth was deemed to be \$0, based on Financial Accounting Standards Board (FASB) released Statement No. 150, and the Member's Shareholder's Agreement. The Shareholder's Agreement stated that shareholder shares were mandatorily redeemable, which under FASB Statement No. 150 reclassified the owner's equity as a liability and reduced the net worth of the Member to \$0.

Lexington Investment Company, Inc. Net Capital Computation Comparisons for the Period From January 2004 Through January 2005.

	July 30, 2004		August 31, 2004		September 30, 2004	
	<u>Firm</u>	<u>Staff</u>	<u>Firm</u>	<u>Staff</u>	<u>Firm</u>	<u>Staff</u>
Net Worth	\$ 507,069.00	\$ -	(a) \$ 521,834.00	\$ -	(a) \$ 558,214.00	\$ -
Non allowable Assets	\$ 189,907.00	\$ 189,907.00	\$ 190,167.00	\$ 190,167.00	\$ 179,322.00	\$ 179,322.00
Tentative Net Capital	\$ 317,162.00	\$ (189,907.00)	\$ 331,667.00	\$ (190,167.00)	\$ 378,892.00	\$ (179,322.00)
Haircuts	\$ 1,229.00	\$ 1,229.00	\$ 1,203.00	\$ 1,203.00	\$ 1,346.00	\$ 1,346.00
Net Capital	\$ 315,933.00	\$ (191,136.00)	\$ 330,464.00	\$ (191,370.00)	\$ 377,546.00	\$ (180,668.00)
Minimum Requirement	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00
Excess Net Capital	\$ 215,933.00	\$ (291,136.00)	\$ 230,464.00	\$ (291,370.00)	\$ 277,546.00	\$ (280,668.00)

(a) The Member's Net Worth was deemed to be \$0, based on Financial Accounting Standards Board (FASB) released Statement No. 150, and the Member's Shareholder's Agreement. The Shareholder's Agreement stated that stockholder shares were mandatorily redeemable, which under FASB Statement No. 150 reclassified the owner's equity as a liability and reduced the net worth of the Member to \$0.

Lexington Investment Company, Inc. Net Capital Computation Comparisons for the Period From January 2004 Through January 2005.

	October 29, 2004		November 30, 2004		December 31, 2004	
	<u>Firm</u>	<u>Staff</u>	<u>Firm</u>	<u>Staff</u>	<u>Firm</u>	<u>Staff</u>
Net Worth	\$ 596,546.00	\$ -	(a) \$ 593,920.00	\$ -	(a) \$ 412,812.00	\$ -
Non allowable Assets	\$ 184,388.00	\$ 184,388.00	\$ 180,826.00	\$ 180,826.00	\$ 190,577.00	\$ 190,577.00
Tentative Net Capital	\$ 412,158.00	\$ (184,388.00)	\$ 413,094.00	\$ (180,826.00)	\$ 222,235.00	\$ (190,577.00)
Haircuts	\$ 1,326.00	\$ 1,326.00	\$ 1,365.00	\$ 1,365.00	\$ 1,989.00	\$ 1,989.00
Net Capital	\$ 410,832.00	\$ (185,714.00)	\$ 411,729.00	\$ (182,191.00)	\$ 220,246.00	\$ (192,566.00)
Minimum Requirement	\$ 100,000.00	\$ 100,000.00	\$ 100,000.00	\$ 250,000.00	(b) \$ 100,000.00	\$ 250,000.00
Excess Net Capital	\$ 310,832.00	\$ (285,714.00)	\$ 311,729.00	\$ (432,191.00)	\$ 120,246.00	\$ (442,566.00)

(a) The Member's Net Worth was deemed to be \$0, based on Financial Accounting Standards Board (FASB) released Statement No. 150, and the Member's Shareholder's Agreement. The Shareholder's Agreement stated that stockholder shares were mandatorily redeemable, which under FASB Statement No. 150 reclassified the owner's equity as a liability and reduced the net worth of the Member to \$0.

(b) The Member's minimum net capital requirement was increased from \$100,000 to \$250,000 for the months of November 2004, December 2004 and January 2005, because the Member received 89 checks made payable to the Member of the 316 checks received by the Member during these months. This constituted a non-compliance rate of 28%. Of the 89 checks, there appeared to be numerous checks from the same customers.

Lexington Investment Company, Inc. Net Capital Computation Comparisons for the Period From January 2004 Through January 2005.

	January 31, 2005	
	<u>Firm</u>	<u>Staff</u>
Net Worth	\$ -	\$ -
Non allowable Assets	\$ 223,949.00	\$ 223,949.00
Tentative Net Capital	\$ (223,949.00)	\$ (223,949.00)
Haircuts	\$ 2,164.00	\$ 2,164.00
Net Capital	\$ (226,113.00)	\$ (226,113.00)
Minimum Requirement	\$ 100,000.00	\$ 250,000.00 (b)
Excess Net Capital	\$ (326,113.00)	\$ (476,113.00)

(b) The Member's minimum net capital requirement was increased from \$100,000 to \$250,000 for the months of November 2004, December 2004 and January 2005, because the Member received 89 checks made payable to the Member of the 316 checks received by the Member during these months. This constituted a non-compliance rate of 28%. Of the 89 checks, there appeared to be numerous checks from the same customers.

Statement of Corrective Action

Re: Examination No. E8A20050130

This Statement of Corrective Action is submitted by the Respondent. It does not constitute factual or legal findings by NASD, nor does it reflect the views of NASD or its staff.

The following steps have been implemented to correct those deficiencies as outlined in the Letter of Acceptance, Waiver and Consent:

Deficiency: Effecting Securities Transactions while failing to Maintain the Minimum Required Net Capital, Maintaining Inaccurate Books and Records and Filing Inaccurate FOCUS Reports in violation of SEC Rules 15c3-1, 17a-3(a) and 17a-5 and NASD Conduct Rules 2110 and 3110(a)

Corrective Action: Upon recognition of the violation during the course of our 2004 Audit on February 7, 2005, the Board of Directors of the Member agreed to amend its Shareholders Agreement to eliminate all mandatory redemption agreements regarding the repurchase of Lexington Investment Company, Inc. common stock. The amendment became effective on February 7, 2005.

Deficiency: Holding Employee Funds Intended for Deposit in a 401K Plan in Violation of the Member's Membership Agreement and SEC Rule 15c3-3(k)(2)(ii) and NASD Conduct Rule 2110

Corrective Action: All payroll personnel were immediately advised to deposit funds withheld from employee payroll checks as 401K contributions be deposited into the employees self-directed Bear Stearn Securities Corp. accounts on the same day the payroll checks are generated.

Deficiency: Failure to Promptly Report Municipal Securities Transactions and Failure to Establish, Maintain and Enforce Adequate Written Supervisory Procedures, in Violation of Municipal Securities Rulemaking Board ("MSRB") Rules G-14 and G-27(c)

Corrective Action: The Supervisory Procedures have been amended to include instructions for operations personnel responsible for submitting municipal trade reports to our clearing agent to do so within fifteen minutes of the original time of the municipal transaction. In conjunction with this procedure are instructions for all registered personnel to immediately deliver order tickets with all appropriate information to the operations area in such manner to allow the trade to be reported within the fifteen minute requirement.

Submitted by: Stanley S. Kerrick, President

dated: May 25, 2005