

**NASD
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. EAF0301040002**

TO: Department of Enforcement
NASD

RE: John Schaedel, Respondent CRD No. 2833004
Anthony Truman, Respondent CRD No. 2560848

Pursuant to Rule 9216 of NASD Code of Procedure, Anthony Truman ("Truman") and John Schaedel ("Schaedel") (collectively "Respondents") submit 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 Respondents alleging violations based on the same factual findings.

Respondents understand 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 them; and
3. If accepted:
 - a. this AWC will become part of Respondents' permanent disciplinary record and may be considered in any future actions brought by NASD or any other regulator against any of them;
 - b. this AWC will be made available through NASD's public disclosure program in response to public inquiries about Respondents' 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. Respondents 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 Respondents' testimonial obligations or right to take legal or factual positions in litigation or other legal proceedings in which NASD is not a party.

Truman and Schaedel also understand that their 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:

John Schaedel entered the securities industry in 1997 when he became associated with a member firm as a Series 6. He became a general securities representative (Series 7) in 1999 and was associated with HRBFA as a general securities representative from August 2002 to September 2003. Since September 2003, Schaedel has not been associated with any NASD member.

Anthony Truman entered the securities business in 1994 when he became associated with a member firm as a Series 6. He became a general securities representative (Series 7) in 1996 and, from August 2002 to September 2003, he was associated with HRBFA as a general securities representative. Since September 2003, Truman has not been associated with any NASD member.

Neither Truman nor Schaedel has any relevant disciplinary history.

I.

WAIVER OF PROCEDURAL RIGHTS

Respondents specifically and voluntarily waive the following rights granted under NASD's Code of Procedure:

- A. To have a Formal Complaint issued specifying the allegations against either of them;
- 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, Respondents specifically and voluntarily waive any right to claim bias or prejudgment 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.

Respondents further specifically and voluntarily waive 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. Respondents hereby accept and consent, 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:

Summary

From October 2002 to July 2003, John Schaedel and Anthony Truman, two brokers at H&R Block Financial Advisors, Inc. ("HRBFA") facilitated the efforts of their clients to evade mutual fund attempts to block or restrict their clients' market timing transactions, thus allowing their clients to market time mutual funds in violation of valid restrictions imposed by the mutual funds and in violation of NASD rules.

The brokers joined HRBFA in September 2002 intending on opening numerous accounts for hedge funds to market-time mutual funds through HRBFA's fee-based accounts. Nearly all of Schaedel's and Truman's clients at HRBFA market-timed mutual funds. These accounts eventually held approximately \$32 million in assets. Two of their customers, HC and CC, opened accounts for common beneficial owners and engaged in deceptive activities to avoid fund restrictions. HC opened six accounts with Schaedel and Truman for two limited partnerships and CC opened two accounts for the same beneficial owner.

Although the brokers were aware that certain mutual funds discouraged or restricted frequent trading, they immediately began executing market-timing transactions for HC and CC. Schaedel and Truman began receiving letters from mutual funds attempting to block or reject trading soon after HC and CC began market timing mutual funds through the brokers. Schaedel and Truman received over 100 letters blocking or rejecting HC's and CC's market-timing activities.

HC and CC were able to continue market timing mutual funds, evading fund attempts to block such activity, with the knowledge, participation and assistance of Schaedel and Truman. First, when one account was restricted, HC used related accounts to continue

trading in the mutual funds that previously restricted the companion accounts. Second, both HC and CC opened new accounts for the same beneficial owners and used the new accounts to continue to actively trade or market-time funds that had restricted its existing accounts. Finally, Schaedel and Truman changed the broker of record on certain of HC's and CC's accounts (and other customers' accounts as well) to, among other things, hide further market timing transactions from the purview of the mutual funds. As a result of these deceptive practices, HC executed 69 and CC executed 12 roundtrips that violated fund restrictions or limitations, thus earning substantial illicit profits. Schaedel and Truman earned approximately \$40,000 each from the activities of their market timing clients, and each received a check for \$20,000 from HRBFA in January 2003.

Accordingly, Schaedel and Truman violated NASD Conduct Rule 2110.

1. Market Timing Mutual Funds

"Market timing" is the practice of short-term buying and selling of mutual fund shares to exploit inefficiencies in mutual fund pricing. The share price of a mutual fund is determined by the "net asset value" or NAV of the fund. The NAV is typically calculated once per day from the closing price of the securities in the fund's portfolio at 4:00 p.m. E.S.T. This method for determining NAV provides market timers the opportunity to engage in arbitrage based on market information not reflected in that day's net asset value. To do this, market timers typically buy and sell shares in mutual funds on a short-term basis, realizing quick gains and then retreating to the previous market position. Market timing can harm mutual fund shareholders because it can dilute the value of their shares, by, among other things, requiring the fund to keep a larger percentage of highly liquid assets to cover the redemptions, or by increasing the transaction costs for the fund. Long-term fund investors may ultimately bear the burden of paying these costs.

To minimize the negative effects of market timing, many mutual fund companies have policies and procedures, disclosed in their prospectuses and statements of additional information, to detect and prevent market timing. Schaedel and Truman knew that the prospectuses and statements of additional information for the mutual funds at issue here contained explicit restrictions or limitations on market timing. Certain prospectuses stated, among other things, that the funds were not designed for short term trading or market timing, market timing can have an adverse impact on a fund and can harm long term investors, market timing was prohibited, or market timing was limited to a certain number of roundtrip transactions.

Many mutual fund companies monitor trading activity for market timing and attempt to enforce restrictions and limitations on market timing through written and oral communications, or notices ("restriction letter"). Mutual funds also rejected transactions identified as market timing transactions.

As demonstrated by HC's and CC's activities described below, market timers employ a number of strategies to hide their identity or activities, avoid detection, and therefore continue market timing. These strategies include opening and trading in multiple related accounts and using different names, Tax ID numbers, broker numbers, and addresses.

2. Schaedel and Truman Join HRBFA So Their Clients Can Market Time

HRBFA began recruiting Schaedel and Truman to join HRBFA in July 2002. At the time, the brokers had the opportunity to open accounts for hedge funds to market-time mutual funds, but the firm where they worked placed restrictions on turnover in its fee-based account, effectively prohibiting such accounts from being used for market timing. During the recruitment process, Schaedel and Truman told the firm's representatives that they had the opportunity to open accounts for a number of hedge funds that could invest \$30 to \$40 million in assets and would aggressively trade or market-time mutual funds through their accounts at HRBFA.

Schaedel and Truman decided to join HRBFA because, among other things, the firm offered fee-based accounts, called Wealth Management Accounts (WMAs), through which customers could engage in unlimited trading while paying a quarterly fee, rather than a commission on each trade. Moreover, through HRBFA's WMAs, clients had access to a limited roster of mutual funds that they could trade without incurring any load. Schaedel and Truman understood that HRBFA did not have any system in place, such as a limitation on turnover ratios, to inhibit frequent trading or market timing through WMAs.

Schaedel and Truman knew or should have known, however, that WMAs were not intended for entities primarily interested in market timing mutual funds. Each of their clients had to agree to the terms of the WMA Client Guide and Investors Account Agreement when they opened each of their accounts. That Agreement explicitly stated that WMAs were not to designed for market timers:

You understand that the program is designed for investors not primarily interested in purchasing eligible mutual funds or UITs or trading in such investment company shares based on market timing.

Moreover, the brokers understood that mutual funds available through WMAs in fund prospectuses and statements of additional information informed investors they restricted or discouraged market timing, reviewed trading in their funds to detect market timers, and sought to restrict or reject market-timing transactions.

3. HC, CC and Other Clients Commence Market-Timing Mutual Funds, and Schaedel, and Truman Receive Numerous Communications from Funds Blocking or Rejecting Market-Timing Transactions

Schaedel and Truman began working at HRBFA in late September 2002 and began opening accounts for their clients soon thereafter. Schaedel and Truman opened 19

accounts for seven clients that engaged in market timing. Each customer signed a special disclosure document for each account that acknowledged, among other things, that the accounts were going to trade mutual funds "in an aggressive manner." No other account at HRBFA was required to sign a similar disclosure document.

Two customers, HC and CC, opened accounts for common beneficial owners and engaged in the deceptive practices described below to continue their market timing activity. Customer HC opened more accounts with Schaedel and Truman than any of their other market timing customers, engaged in more market timing transactions than any of their other customers, and profited more from market timing mutual funds at HRBFA. Schaedel and Truman opened six HRBFA accounts for HC for two limited partnerships and two HRBFA accounts for CC for one owner.

HC's accounts were purportedly opened for separate legal entities, but Schaedel and Truman knew or should have known that these six accounts had common beneficial owners. In October 2002, Schaedel and Truman opened four accounts for HC (Accounts D, W, F, and H) for two different limited partnerships: one partnership was the beneficial owner for accounts D and W and another partnership was the beneficial owner for accounts F and H. As described more fully below, HC opened two additional accounts in May 2003 (Account NS and NU) after accounts D, W, F, and H had been restricted from market-timing various mutual funds. Account NS had the same beneficial owner as accounts H and F; account NU had the same beneficial owner as accounts D and W. Similarly, two of the four accounts CC opened (CC Global and JMR) had the same beneficial owner.

HC and CC immediately began market timing mutual funds through their HRBFA accounts and the funds began their efforts to prevent such trading by sending letters and electronic communications restricting or rejecting such trading. Schaedel and Truman began receiving these communications from funds in November 2002 either directly or through the firm. By the time HC's and CC's accounts were shut down in July 2003, Schaedel and Truman had received over 100 communications from various fund families restricting or rejecting HC's and CC's accounts.

In restricting or rejecting their clients' market timing transactions, mutual fund companies put Schaedel and Truman on notice that market timing may harm fund shareholders, that the funds discouraged market timing, and that the fund was restricting the account, client, or broker from engaging in future market timing activities. When the account-specific restrictions were ineffective, funds resorted to other, more sweeping restrictions.

4. Schaedel and Truman Assisted HC and Other Clients in Evading Fund Restrictions

After their clients began receiving restriction or rejection letters from mutual funds, Schaedel and Truman established a system to monitor the trading of HC, CC, and their other market timing clients, advised clients when they were close to or had exceeded certain fund's prospectus trading limits, and advised them on what funds to trade. They

used a chart to track investments by HC and their other market-timing clients against fund prospectus trading limits.

Schaedel and Truman knew that HC and CC evaded fund restrictions by using related accounts to continue market timing restricted funds. As Truman stated in a July 28, 2003 e-mail:

If a funds [sic] prospectus states no more than a certain number of round trips per month we try our hardest not to do more than that. If a fund family tells us you have used your limit of round trips, we do not use that fund family for that specific account. We may however use that fund family for other accounts that have not used their limits.

Schaedel and Truman also assisted their clients' market-timing activities by recommending trades that the customer subsequently executed. For example, on June 25, 2003, the person who traded for accounts opened by HC asked Schaedel for his thoughts on "changing the funds" for the six accounts then open. The broker responded the same day with nine suggested trades for Account W, eight for Account H, and nineteen for Account NS. All trades were made the same day. On July 1, 2003 a person with trading authority over Account J for Customer M sent Schaedel a sheet of potential trades. The broker advised that one of the fund families was unavailable through a WMA and another imposed a redemption fee. He suggested trading two other funds and the client agreed. The trades were made the same day.

Through these efforts, HC and CC were able to continue market timing when a fund had prohibited it from doing so and executed transactions beyond the limits placed by the fund families.

Schaedel and Truman's knowledge of their clients' activities is evidenced by e-mails the brokers sent after the firm shut down their clients' accounts. Schaedel and Truman suggested ways to reopen the accounts and, in doing so, acknowledged their desire to hide their clients' trading practices from mutual funds. One device Schaedel and Truman recommended was to have their clients' accounts clear through an omnibus trading account at a third-party clearing firm (HRBFA self-cleared at the time). In arguing for this approach, Schaedel stated in an e-mail to the regional director at HRBFA:

Going through an outside clearing firm . . . would help us In dealing with these huge clearing firms that have the Omnibus Platform, we would literally be a needle in the haystack. Our orders would be mixed in with [] all the major brokerage companies, under the omnibus system. When you self clear, it is not easy to quote unquote "hide." . . . if we can clear through a major clearing house using there [sic] omnibus platform WOULD make all the difference in the world. Why? Our orders would be aggregated with the big brokerage companies around the country. Hence our clients would remain out of sight.

Truman likewise suggested using an omnibus trading platform as a means to hide the market timing done by their clients: In a July 28 e-mail, he stated, "In an omnibus trading platform all orders into a fund are grouped together so the fund family does not know specifically who placed the trade."

5. HC Evaded Fund Restrictions by Trading in Related Accounts and Opening New Accounts

HC used the related accounts it opened in October 2002 to engage in more market timing than it would have had it just opened one account for each beneficial owner. As noted above, Accounts D and W had the same beneficial owner and Accounts F and H had the same beneficial owner. When Account D received restriction notices from certain funds, Account W traded in the funds thereafter; when Account F was restricted, Account H traded in the restricted funds.

By May 2003, HC had fewer funds to market-time through its HRBFA accounts because many of the funds had blocked Accounts D, W, F, and H from engaging in further market timing. To maintain HC's ability to market time, Schaedel and Truman opened two new accounts – Account NU and Account NS – for HC; the new accounts were funded through transfers from Accounts F and H or from a transfer from a common bank account. Neither Schaedel nor Truman disclosed to the mutual funds that had restricted D, W, F, and H the relationship between those accounts and Accounts NU and NS.

Schaedel and Truman executed trades in Accounts NS and NU in funds that had previously restricted Accounts D, W, F, and H. They executed purchases and sales in Account NS in funds that had previously restricted either Account F and/or Account H and executed seven roundtrips in Account NU in funds that had previously restricted Account D and/or Account W. Through this trading, Customer HC made \$112,882 in profits in Account NS and \$26,702 in Account NU.

6. Schaedel and Truman Assist Customer CC to Evade Fund Restrictions

Customer CC opened Account CC Global in October 2002 and began immediately market timing mutual funds through Schaedel and Truman in that account. Several mutual funds began restricting the CC account or rejecting trades because of CC's market timing activities. Customer CC evaded these restrictions and rejections by opening another account that had the same beneficial owner as account CC. In March 2003, customer CC opened Account JMR and began market timing some of the same funds that had restricted its CC account. Schaedel and Truman assisted customer CC in evading fund restrictions. All told, Customer CC executed 12 round trips in Accounts CC and JMR in violation of the funds' legitimate restrictions.

7. Schaedel and Truman Take Other Action In Part to Assist Clients in Avoiding Fund Restrictions

Schaedel and Truman were partners. They each had separate broker numbers at HRBFA, but evenly divided the fees and commissions generated by the accounts under each number regardless of which rep the account was under. In April 2003, Schaedel requested that the firm change the broker-of-record for certain of HC's accounts and CC's accounts, as well as accounts of their other market timing clients, from him to Truman and vice versa. The firm approved the transfers and they occurred on April 24. Thereafter, certain of these accounts market-timed in the same funds they had market-timed before the transfers, without the funds restricting such activity.

In June 2003, Schaedel e-mailed his branch office manager suggesting an "experiment" to change the broker-of-record for Account JB, (which recently had been opened by Customer M), from Schaedel to "OR," which referred to the Orlando branch's house account. The email stated: "I would like to try an experiment. What are the chances of putting [Account JB] into rep OR??" Schaedel admitted that he hoped moving Account JB to the "house account" would improve the chance that Account JB would not receive fund-restriction notices blocking market-timing trades. The firm approved the transfer and on June 23, 2003, Account JB was transferred to the "house account" number – [REDACTED] This scheme failed, however, and Account JB's June 26, 2003 orders totaling approximately \$180,000 were rejected by the mutual fund.

8. Violations

NASD Conduct Rule 2110 requires a member firm and its associated persons to observe high standards of commercial honor and just and equitable principles of trade.

By virtue of the activities described above, Schaedel and Truman violated NASD Conduct Rule 2110.

B. Respondents also consent to the imposition, at a maximum, of the following sanctions:

1. For Schaedel:
 - a. A fine of \$110,000,
 - b. A suspension of one (1) year from associating in any capacity with any member firm.
 - c. Requalification as a general securities representative (Series 7) before being associated with any member firm.

2. For Truman

- a. A suspension of one (1) year from associating in any capacity with any member firm. Truman has asserted an inability to pay and has submitted a sworn financial statement. In light of the financial *status of Truman, the sanctions do not include a monetary fine.*
- b. Requalification as a general securities representative (Series 7) *before being associated with any member firm.*

The sanctions imposed herein shall be effective on a date set by NASD staff. The fine imposed against Schaedel shall be due and payable either immediately upon reassociation with a member firm following the one (1) 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.

III.

OTHER MATTERS

Schaedel and Truman understand that they may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. *They understand that they 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.*

Schaedel agrees to pay any monetary sanction upon reentry as noted above. Schaedel specifically and voluntarily waives any right to claim that he is unable to pay, now or at any time hereafter, any monetary sanction imposed in this matter. Truman has raised the issue of his inability to pay and understands that his assertion of inability to pay has been considered in connection with the monetary sanctions imposed in this matter and specifically and voluntarily waives any right to claim that he is unable to pay at any time hereafter, any monetary sanction imposed in this matter.

Schaedel and Truman also consent to cooperate with NASD in any further proceedings related to this matter as necessary, including but not limited to providing documents and information, participating in interviews, and testifying at any hearing.

Schaedel and Truman understand that if they are barred or suspended from associating with any NASD member, they become subject to a statutory disqualification as that term is defined in Section 3(a)(39) of the Securities Exchange Act of 1934, as amended. Accordingly, they may not be associated with any NASD member in any capacity, including clerical or ministerial functions, during the period of the bar or suspension. (See NASD Rule 8310 and IM-8310-1.)

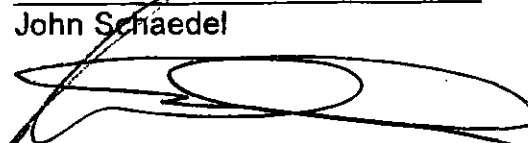
Schaedel and Truman certify that each of them has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it, and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein, has been made to induce Schaedel or Truman to submit it.

Date

9/12/05

Date

John Schaedel



Anthony Truman

Accepted by NASD:

Date

Director, Department of
Enforcement

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

Schaedel and Truman certify that each of them 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 Schaedel or Truman to submit it.

9/12/05
Date


John Schaedel

Date _____

Anthony Truman

Accepted by NASD:

9/21/05
Date


Director, Department of
Enforcement

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