The Buck Stops . . . Where? Liability of Presidents And Chief Executive Officers in SEC and FINRA Enforcement Actions

By Brian L. Rubin and Yvonne M. Williams

"The buck stops here."¹

Presidents of the United States are responsible for making certain decisions. They have accountability when they act, when they act unreasonably, and sometimes when they fail to act. President Harry S. Truman² understood these concepts very well, stating:

You know, it's easy for the Monday morning quarterback to say what the coach should have done, after the game is over. But when the decision is up before you—and on my desk I have a motto which says "The Buck Stops Here"—the decision has to be made.

¹ This saying was painted on a sign on the desk in the White House office of President Harry S. Truman. According to the Truman Library, "The saying 'the buck stops here' derives from the slang expression 'pass the buck' which means passing the responsibility on to someone else. The latter expression is said to have originated with the game of poker, in which a marker or counter, frequently in frontier days a knife with a buckhorn handle, was used to indicate the person whose turn it was to deal. If the player did not wish to deal he could pass the responsibility by passing the 'buck,' as the counter came to be called, to the next player." Available at: http://www.trumanlibrary.org/buckstop.htm.

² President Truman’s middle name was actually “S”—a name chosen as a compromise to honor the names of his grandfathers Anderson Shipp Truman and Solomon Young. While no period after the “S” is required when providing President Truman’s full name, the authors have followed the recommendations of the U.S. Government Printing Office Style Manual as well as the Harry S. Truman Presidential Library and Museum in providing the punctuation. See Harry S. Truman Library & Museum, Use of the Period after the “S” in Harry S. Truman’s Name, Available at: http://www.trumanlibrary.org/speriod.htm.
The President—whoever he is—has to decide. He can’t pass the buck to anybody. No one else can do the deciding for him. That’s his job.3

While presidents of financial services firms are not, for the most part, Presidents of the United States4 (although some may act otherwise), they also have certain responsibilities, and if they fail to act properly, they may be disciplined. Top officials from the Securities and Exchange Commission (SEC or Commission) and the Financial Industry Regulatory Authority (FINRA) have recently made it clear that senior officials, including presidents and chief executive officers (CEOs), are in their sights.5 This message of expectation of a strong “tone at the top” is not new. For example, in 2004, following a series of corporate scandals in the early 2000s, Stephen Cutler, the SEC Enforcement Director at the time, stated that the Commission would hold the CEOs and senior management of financial firms accountable because “violations of the securities laws are frequently the product of both individual failings and a deficient corporate culture,” and “we’re hoping that if [the CEO] sees that a failure of corporate culture can result in a fine that significantly exceeds the proverbial ‘cost of doing business’ . . . she may have a little more incentive to pay attention to the environment in which her company’s employees do their jobs.”6

This focus on developing and maintaining a strong culture of compliance from the top down at financial firms is evident from a review of some recent SEC and FINRA enforcement actions brought against presidents and CEOs of broker-dealers and investment advisers. These actions were based on one or more theories of liability, in particular: (1) direct violation of the securities laws or regulatory rules; (2) failure by the president or CEO to follow the firm’s policies and procedures; (3) aiding and abetting or causing an employee’s or the firm’s violations of rules and regulations; and/or (4) failure to supervise firm employees or representatives.

Choosing principle over maximizing profit while building a strong culture of compliance will hopefully endear presidents and CEOs to the hearts of regulators (and possibly to the American people).7 Presidents, CEOs and others who focus on the cases described below may want to model themselves not after the wayward leaders described below, but may want to embody the words of fictional President Josiah “Jed” Bartlet: “I’m victim to my own purity of character.”8

I. Direct Violations of the Law

“I am not a crook.” 9

Richard M. Nixon

Sometimes presidents and CEOs may be “crooks” or rule breakers because they directly violate the law. It is critical that firm leaders follow the rules. Otherwise, they may find themselves barred, suspended, fined, or even jailed, and their firms might be in similar trouble. As Mr. Cutler stated, “If employees see managers bend the rules, they’ll bend the rules.”10

One recent case involved the president of a brokerage-dealer, who not only directly violated the rules but also (like a certain President of the United States) tried to cover up his misdeeds. In October 2010, the National Adjudicatory Council (NAC) affirmed the findings of a FINRA hearing panel and imposed a bar on Mark Alan Uselton, president of Legacy Trading Company, LLC, who, according to the NAC decision, had directly committed several violations of SEC and FINRA rules by effecting impermissible short sales, failing to maintain books and records, providing false information to FINRA and refusing to answer FINRA’s questions.11 The primary substantive rules at issue require member firms to make affirmative determinations of ability to deliver stocks sold short and to document compliance prior to executing sales. According to the NAC, Mr. Uselton himself made more than 1,000 trades that violated those rules.12 He also violated the books and records rules by failing to keep copies of the orders and forms for unsolicited orders submitted to Pink Sheets and by deleting “on a daily basis all firm emails.”13 Once FINRA began investigating Legacy’s activities, Mr. Uselton created further problems for himself by trying to cover up his misdeeds during the investigation.14 The NAC found that he provided false information to

3 Id.
4 Calvin Coolidge was the president of a bank. See http://books.google.com/books? id=89hurH2O2Q&dq=calvin%20coolidge%20nonotuck%20bank&source=bl&ots=h97tuO2xJQC&pg=PA82&lpg=PA82&dq=calvin%20coolidge%20nonotuck%20bank&hl=en&ei=CofBTaqmLOYK4twfQzYzTBA&sa=X&oi=book_result&ct=result&resnum=8&ved=0CDoQ6AEwBw#v=onepage&q=calvin%20coolidge%20nonotuck%20bank&f=false.
5 See Brad Bennett, FINRA Executive Vice President and Chief of Enforcement, FINRA Sanctions Two Firms and Seven Individuals for Selling Private Placements Without Conducting Reasonable Investigation (April 7, 2011) (available at: http://www.finra.org/Newsroom/NewsReleases/2011/P123441) (“senior officials at these firms [one CEO and three presidents] failed to fulfill their responsibilities to customers by not conducting reasonable investigations of these unrelated offerings, especially in light of multiple red flags”); Robert Khuzami, Director, Division of Enforcement, Securities and Exchange Commission, Remarks at SIFMA’s Compliance and Legal So-
7 See, e.g., Warren Buffett and his company Berkshire Hathaway, which “emerged from the global financial crisis as the nation’s most admired company, thanks to its CEO’s ‘humility and sense of accountability.’ ” Available at: http://www.cnbc.com/id/36169712/Warren-Buffett-s-Berkshire-
8 Id. at 11.
9 Id. at 14-15.
10 Id. at 8.
12 Id. at 11.
13 Id. at 11.
14 Id. at 14-15.
15 Id. at 8.
FINRA’s staff while also refusing to answer certain questions during the investigation. Ultimately, Mr. Uselton was fined $50,000, jointly and severally with Legacy, and suspended in all principal capacities for one year for his recordkeeping violations. Trying to cover up his actions made matters worse for this president, who was barred in all capacities for his conduct during the FINRA investigation and for his refusal to provide testimony.

II. Liability for Failing to Follow the Firm’s Own Procedures

“A president’s hardest task is not to do what is right, but to know what is right.”

Lyndon B. Johnson

Presidents of broker-dealers and investment advisers often know what is right by learning about the securities laws and by reviewing their firms’ procedures (assuming those procedures are reasonable, but that would be the subject of another article). If they fail to review their procedures, and end up not knowing what is right, they may be sanctioned.

A settlement from April 2011 illustrates this point. In that case, FINRA fined Robert Alan Vollbrecht, the president of the Workman Securities Corporation, $10,000 and barred him from association with any FINRA member in any principal capacity. According to FINRA’s findings set forth in Mr. Vollbrecht’s Letter of Acceptance, Waiver and Consent, he failed to follow his obligations as set forth in the firm’s Supervisory Procedures Manual. The procedures identified Mr. Vollbrecht as the single individual responsible for Non-Conventional Investments and Private Placements, requiring him “to take affirmative steps to ensure that information in offering documents for private offerings sold through Workman was accurate.” Additionally, Mr. Vollbrecht was required to conduct “all necessary and appropriate due diligence to ensure that Workman and its field sales force understood any product sold through a private offering through Workman, and any associated risks.” FINRA found that he conducted “cursory” and “minimal” due diligence reviews, which were inadequate and inconsistent with the firm’s procedures. Therefore, he was liable under NASD Conduct Rules 2010 and 2110 and FINRA Rule 2010 for his violations relating to Workman’s sales of various private placement offerings.

III. Presidential Liability for Causing or Aiding and Abetting Violations

“Trees cause more pollution than automobiles do.”

Ronald Reagan

While Presidents or candidates for the highest office in the land may have debated the causes of pollution (or global warming) (or where certain presidents were born), there is no question that broker-dealer or investment adviser presidents (as well as other associated persons) may face liability if they are found to have caused or aided and abetted violations of securities laws and regulations. Section 21C of the Securities Exchange Act of 1934 states that a person “causes” a violation through “an act or omission the person knew or should have known would contribute to such violation,” while under Section 20(e) a person “aids and abets” a violation if the person “knowingly provides substantial assistance to another person” in violation of the Exchange Act or any rule promulgated under the Act and will therefore “be deemed to be in violation of such provision to the same extent as the person to whom such assistance is provided.” The Investment Advisers Act of 1940 similarly assigns liability to persons associated with investment adviser firms who either aid and abet or cause a violation of the securities laws, using the same standard as the Exchange Act.

In May 2011, the SEC announced a settlement that illustrates these issues. The SEC found that Wunderlich Securities, Inc. (a broker-dealer and registered investment adviser), Gary K. Wunderlich (the CEO and principal founder) and Tracy L. Wiswall (the CCO) violated numerous rules related to overcharging commissions and transactional fees to advisory clients in more than 6,000 separate transactions. With regard to the CEO, the SEC found that Mr. Wunderlich had willfully aided and abetted and caused violations of the Advisers Act, which requires investment advisers to adopt and implement written policies and procedures as well as maintain and enforce a written code of ethics. The SEC found the firm lacked such policies, procedures and a


27 Id. at 2.
written code of ethics until after April 2008, despite being registered with the SEC as an investment adviser firm in February 2007. The SEC also made findings that Mr. Wunderlich knew about this issue, retained a consultant to review the firm’s advisory operations, but failed to take any actions after receiving the consultant’s report. As a result, the SEC found that Mr. Wunderlich had notice of the violations, knew of the requirements of the Advisers Act, and therefore willfully aided and abetted the firm’s violations of the Act. In determining sanctions, the SEC considered remedial acts promptly undertaken by respondents, as well as their cooperation. As a result of his violations, Mr. Wunderlich was censured and agreed to cease and desist from committing or causing future violations.

Another recent case involving these concepts concerned Frederick O. Kraus, the president of GunnAllen Financial, Inc., a broker-dealer that was going through the process of ending its operations. Through a settlement, the SEC found Mr. Kraus liable for causing and aiding and abetting the firm’s violations of Regulation S-P by allowing GunnAllen to transfer nonpublic information to another broker-dealer through his authorization of the transfer of approximately 16,000 direct application accounts. For his conduct, Mr. Kraus was fined a civil money penalty of $20,000 and ordered to cease and desist from committing or causing any violations of Regulation S-P.

The SEC found that, in early 2010, GunnAllen began preparing to end its operations as a broker-dealer. Since it would no longer be servicing accounts, the sales manager of the firm sent GunnAllen customers a notice explaining the situation and purporting to provide an opportunity for customers to transfer their accounts themselves or to allow their registered representatives (RRs) to transfer the accounts. Mr. Kraus, as president, personally approved this notice. Yet, according to the SEC, two days later—without confirming the lack of customer objections—Mr. Kraus personally authorized the transfer of approximately 16,000 accounts to the company’s sales manager, who then downloaded customer information to his new firm and transferred the accounts.

The SEC alleged that Mr. Kraus “was familiar with Regulation S-P” but he “knowingly placed customer information at substantial risk of unauthorized access” by executing the transfer and allowing the downloading of the account applications. The scienter requirement for aiding and abetting was therefore satisfied, and a primary violation clearly existed that Mr. Kraus ratified. The SEC also found that Mr. Kraus “knowingly placed customer information at substantial risk” when he “authorized the Sales Manager to download customer information” thereby willfully aiding and abetting and causing the Regulation S-P violations.

IV. Liability for Failure to Supervise Firm Employees or Representatives

“You do not lead by hitting people over the head—that’s assault, not leadership. . . . [Leadership is] the art of getting someone else to do something you want done because he wants to do it.”

Dwight D. Eisenhower

President Eisenhower presumably knew something about leading and supervising people. He did, after all, lead the invasion of France and Germany during World War II as Supreme Commander of the Allied Forces before he stepped foot into the White House as leader of the free world. In contrast, supervisory liability is imposed on presidents of broker-dealers and investment advisers through the following sources: the Exchange Act, FINRA Rule 3010 and the Investment Advisers Act.

Leadership and supervisory liability concepts have been applied in numerous cases. For example, in a litigated decision, an SEC Administrative Law Judge (ALJ) found that Guy S. Amico and Scott H. Goldstein, the president and chief executive officer, respectively, of Newbridge Securities Corporation, a broker-dealer, failed to supervise a registered representative who participated in the unregistered distribution of stock and manipulated the market for those securities. Messrs. Amico and Goldstein were specifically made aware by subordinates that the registered representative was “potentially engaging in unlawful conduct and was proving difficult to supervise,” and yet both failed to intervene and specifically take action with respect to these reports.

The ALJ’s decision describes the respondents’ defense as consisting of shifting blame to the transfer agent of the securities at issue, to the representative’s

33 Id. at 2, 6-7.
34 Id. at 6-7.
35 Id. at 8. The CCO of Wunderlich Securities, Inc., was also found to have willfully aided and abetted and caused the firm’s violations, but the SEC found that “as CEO, Wunderlich had overall responsibility for ensuring that WSI complied with regulatory mandates under the Advisers Act.” Id. at 7.
36 Id. at 11-12.
38 Id. at ¶5.
39 Id. at ¶7.
40 Id. at ¶13-14.
intermediate supervisors, and even to NASD and the SEC for approving their firm's market making authority in the first place. The ALJ held that Messrs. Amico and Goldstein were equally responsible for failing to supervise, pointing to the firm's organizational charts, which placed the president and CEO directly in charge of the chief compliance officer and head trader. The ALJ noted that as a result of their positions, they were "routinely addressed or copied on emails and memora-

DID NOT PUNCH IN DESCRIBING HIS VIEW TOWARDS THESE TWO EXECUTIVES, DESCRIBING THEIR "ACTUAL APPROACH TO SUPERVISION [AS] FAR CLOSER TO 'THE BUCK STOPS WITH YOU...'." Ultimately, they were barred from associating in a supervisory capacity for two years and the ALJ imposed $79,000 in civil money penalties against each.

A February 2011 example of a FINRA failure to supervise case, involving Workman Securities president Robert Vollbrecht, is discussed above. Specifically, through the settlement, FINRA found Mr. Vollbrecht failed to supervise two Workman registered representatives whom he had approved to engage in securities transactions without any additional review of their transactions, despite having "red flags" in their history that should have signaled the need for heightened supervision. In his capacity as president, he recom-

mended that Workman hire one of the RRs, despite the RR's history of regulatory violations. Mr. Vollbrecht did little to inquire about the RR's history, "other than accept [his] explanation" regarding the investigation of his sales practices at his prior firm. FINRA cited Mr. Vollbrecht for failing to supervise the RR because "[Mr.] Vollbrecht did not investigate the validity of, or status of, these customer complaints, and instead largely accepted [the RR's] self-serving explanations that the complaints were meritless." The RR went on to become the subject of seven additional customer complaints while at Workman. FINRA also found Mr. Vollbrecht "did not scrutinize [the RR's] transactions in any different substantive fashion than he did the transactions of other representatives," despite having the RR on heightened supervision, and this failure to provide oversight permitted the RR to conduct "questionable" transactions involving 15 of the RR's customers. The allegations involving Vollbrecht's supervision of the other RR also involved Mr. Vollbrecht's failure to dili-

gently supervise the RR with respect to questionable transactions, despite being aware of his limited experi-

ence. For his supervision of both RRs, FINRA found "[Mr.] Vollbrecht's failure to investigate the customer complaints made against [one RR] and scrutinize [the other RR's] transactions are particularly problematic given [Mr.] Vollbrecht's position as President of Work-

man." As such, FINRA found Mr. Vollbrecht in viola-

tion of NASD Conduct Rules 3010 and 2210 and FINRA Rule 2010, and imposed a fine of $10,000 as well as a bar from association with any broker-dealer in a princi-

pal capacity for these violations and for his failure to conduct due diligence discussed above.

Even when a president delegates certain responsibili-

ties to someone else, he or she may still be found liable for failing to supervise the supervisor. In January 2011, FINRA announced that Stuart Gregory Burchard, the former president of Broad Street Securities, Inc., had submitted an offer of settlement, which resulted in a bar from any future association with any FINRA member. Among the charges were that "[Mr.] Burchard failed to reasonably supervise the activities of a registered repre-

sentative to ensure she performed her supervisory responsibilities delegated to her by [Mr.] Burchard." The Investment Advisers Act provides liability similar to that provided by the Exchange Act and allows for the Commission to sanction an individual associated with an investment adviser "for failing reasonably to super-

vise, with a view to preventing violations of the federal securities law, another person who commits such a vio-

lation, if that person is subject to the person's supervi-

sion," even if the violation itself is not in violation of the Investment Advisers Act. Thus, presidents of firms registered both as broker-dealers and investment advisers may be found liable under both the Exchange Act and the Investment Advisers Act.

An example from February 2011 involved Jack C. Smith, who served as the president and CEO of Torrey Pines Securities, Inc., which was a broker-dealer as well as an investment adviser. One of the firm's registered representatives had been permanently enjoined in 2010 for violating various provisions of the Securities Act of 1933 and the Exchange Act for the sale of unregistered offerings. In the settled case against Mr. Smith, the SEC found that as president and CEO of the firm, he had failed to develop an adequate supervisory system and failed to establish a system to implement and enforce policies regarding outside business activities and selling away. As such, he violated Section 15(b)(4)(E) of the Exchange Act and Section 203(f) of the Advisers Act "when he failed to supervise [the RR] with a view to preventing and detecting violations of Section 15(a) of the Exchange Act." Mr. Smith was suspended from supervision associated with any broker-dealer or any investment adviser for nine months and was ordered to pay a civil money penalty of $25,000.
V. The Future

“The lesson of history is rarely learned by the actors themselves.”\(^{6,0}\)

James A. Garfield

The presidents and CEOs cited above probably (and hopefully) learned certain lessons from their cases and experiences. Unfortunately for them, however, they may never have the opportunity to demonstrate their newfound knowledge because it is unlikely that they will return to the securities industry as senior executives. In contrast, current presidents and CEOs may want to review those cases carefully to learn about the issues they discuss.

If you are the president or CEO, you may also want to consider taking the following steps among your other efforts to try to minimize your personal exposure:

- Determine whether you have been assigned particular responsibilities through the firm’s policies and procedures;
- If you have taken on additional job functions, you may want to take steps to ensure that you are fulfilling those responsibilities;
- Periodically review your firm’s written policies and procedures to see whether they are consistent with your job functions and responsibilities;
- If you are supervising an employee with a record of regulatory problems or customer complaints, you may want to provide heightened supervision or document why you have not done so;
- If there are questions about who is supervising a person or a function, you may want to work with others at the firm to determine who is responsible and then document that role or delegation;
- If you learn about “red flags,” work with others at the firm to address them, including possibly investigating what caused the problem, what harm has been caused by the problem, how it will be fixed, who will be working on these issues, and who will be supervising that person;


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- Review the firm’s business growth and determine whether compliance functions and other resources have adequately kept up with that growth; and
- If a serious concern arises about an issue and you have not been able to address it adequately, consider escalating the issue to the board of directors, self-reporting the conduct to a regulator, or resigning.\(^{6,1}\)

In addition to these specific tasks, presidents and CEOs who wish to avoid regulatory scrutiny may want to consider sending a strong message of compliance from the top, evidenced through their words and through actions. As former SEC Enforcement Chief Stephen Cutler has stated, “setting the right tone means letting employees know that no one at the company is above the law; that no matter how important or how senior, someone who has violated an ethical standard will be punished.”\(^{6,2}\) Presumably, no one wants to be in the same position that Messrs. Amico and Goldstein found themselves—listening to a judge tell them that their “actual approach” to supervision is “far closer to ‘the buck stops with you…’”\(^ {6,3}\) We cannot imagine what President Truman would say about such conduct (although we are pretty sure that if we were to quote him, we might have to delete a few expletives).\(^ {6,4}\)

61 Cf. Remarks of Commissioner Mary L. Schapiro at the National Association of Securities Dealers, Inc., Sixth Annual Educational Seminar, Oct. 5, 1993 (“Perhaps the most controversial aspect of the Salomon report is its suggestion that, in some circumstances, where management has been apprised of a wrongdoing but has failed to act, a supervisor knowing of the wrongdoing and the failure to act may need to consider further action, including disclosure to the Board or regulatory authorities, or even resignation. I should say that I think the circumstances requiring such drastic action are rather extraordinary.”) (available at: http://www.sec.gov/news/speech/1993-100595schapiro.pdf).


63 Newbridge Securities Corp., at 57 (initial decision).

64 In addition to his belief in personal responsibility, President Truman was known for his use of colorful language, and is famous for remarking, “I never did give anybody hell. I just told the truth, and they thought it was hell” (See, The Quotations Page, Harry S. Truman, available at: http://www.quotationspage.com/quotes/Harry_S_Truman). This distinctive characteristic of President Truman was captured in the play and movie titled “Give ‘em Hell, Harry,” where the former President explains his choice of words by remarking, “[T]here’s a story going around about me these days. It says that some old party hen is supposed to have cornered Bess at some party, and said, “Mrs. Truman, isn’t there anywhere you can do to get the President to stop using the word ‘manure’?” And Bess is supposed to have replied, “It took me forty years to get him to use that word!”


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