FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, **Complainant,** v. RICHARD WILLIAM LUNN MARTIN, (CRD No. 723309), Respondent.	Disciplinary Proceeding No. 2013035817701 Hearing Officer DRS **ORDER ACCEPTING OFFER OF SETTLEMENT** Date: April 24, 2017

INTRODUCTION

Disciplinary Proceeding No. 2013035817701 was filed on June 27, 2016, by the Department of Enforcement of the Financial Industry Regulatory Authority (FINRA) (Complainant). Respondent Richard William Lunn Martin submitted an Offer of Settlement (Offer) to Complainant dated April 20, 2017. Pursuant to FINRA Rule 9270(e), the Complainant and the National Adjudicatory Council (NAC), a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs (ODA) have accepted the uncontested Offer. Accordingly, this Order now is issued pursuant to FINRA Rule 9270(e)(3). The findings, conclusions and sanctions set forth in this Order are those stated in the Offer as accepted by the Complainant and approved by the NAC.

Under the terms of the Offer, Respondent has consented, without admitting or denying the allegations of the Complaint as amended by the Offer of Settlement, 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, to the entry of findings and violations consistent with the allegations of the Complaint as amended by the Offer of Settlement, and to the imposition of the sanctions set forth below, and fully understands that this Order will become part of Respondent's permanent disciplinary record and may be considered in any future actions brought by FINRA.

BACKGROUND

At various times since 1981, Martin was associated with several FINRA members.

During this time period, Martin obtained the following FINRA licenses: Series 4 (Registered Options Principal) and Series 7 (General Securities Representative).

Martin was associated with FINRA Member GF Investment Services, LLC ("GF Investments") from July 17, 2009 through April 10, 2014 and April 24, 2014 through July 7, 2015.

Although Martin is no longer registered or associated with a FINRA member, he remains subject to FINRA's jurisdiction for purposes of this proceeding, pursuant to Article V, Section 4 of FINRA's By-Laws, because (1) the Complaint was filed within two years after the effective date of termination of Respondent's registration with GF Investments, namely, July 7, 2015, and (2) the Complaint charges him with misconduct committed while he was registered or associated with a FINRA member.

FINDINGS AND CONCLUSIONS

It has been determined that the Offer be accepted and that findings be made as follows:

Richard William Lunn Martin ("Martin" or "Respondent") violated NASD Rule 2310 and FINRA Rules 2111 and 2010 by not having a reasonable basis to recommend, for long-term holding, non-traditional exchange traded funds ("Non-traditional ETFs") to his customers. Martin claimed to believe that the world economy was on the precipice of catastrophe and that his customers should invest in and hold Non-traditional ETFs to hedge against the impending catastrophe. As a result of his view, from at least March 2011 through July 2015, Martin recommended to virtually all of his customers that they invest almost exclusively in and hold for lengthy periods of time Non-traditional ETFs, despite the enormous risks associated with holding Non-traditional ETFs for more than one trading session. Therefore, Martin had no reasonable basis to recommend these Non-traditional ETFs to his customers. As a result of the foregoing conduct, Martin violated NASD Rule 2310 for the conduct prior to July 9, 2012, FINRA Rule 2111 for the conduct on and after July 9, 2012, and FINRA Rule 2010.

During the period from June 7, 2014 through October 10, 2014, Martin sent communications to the public that failed to provide a sound basis for evaluating the facts, were misleading, and contained exaggerated and unwarranted language, promissory statements, and projections of future performance. As a result of the foregoing conduct, Martin violated FINRA Rules 2210(d)(1)(A), 2210(d)(1)(B), 2210(d)(1)(F), and 2010.

Reasonable Basis Suitability Relating to Non-Traditional ETFs

Martin believed that there was an ongoing United States monetary crisis and that the debt burden of the United States would cause an imminent depression in the world economy and a catastrophic collapse and reset in the financial markets. As a result, Martin's investment strategy from 2009 through early 2011 was primarily based upon recommending and shorting positions in stocks. In late 2010 and by March 2011, Martin changed his investment strategy from shorting positions in stocks to recommending and purchasing leveraged/inverse Non-traditional ETFs. In late 2010 and by March 2011, Martin recommended and liquidated his customers' short positions into cash, and in turn, he recommended and purchased leveraged/inverse Non-traditional ETFs (the "Investment Strategy").

In recommending his Investment Strategy, Martin focused on one potential risk — namely, his prediction of the impending collapse of the monetary and financial system. In failing to account for any other risks, including the risk that his predictions regarding the collapse of the economy may not come to pass, Martin recommended to virtually all of his customers Non-traditional ETFs. Hence, virtually all of his customers were heavily concentrated, ranging from 75% to 99%, in Non-traditional ETFs by approximately March 2011. Moreover, from at least March 2011 through July 2015, Martin recommended that his customers hold the Non-traditional ETFs in their accounts.

In implementing his Investment Strategy, Martin relied on Non-traditional ETFs. ETFs are typically registered unit investment trusts or open-end investment companies whose shares represent an interest in a portfolio of securities that track an underlying benchmark or index. Shares of ETFs are typically listed on national securities exchanges and trade throughout the day at prices established by the market.

Non-traditional ETFs differ from other ETFs in that they seek to return a multiple of the performance of the underlying index or benchmark (*i.e.*, leveraged ETFs), the inverse of that performance (*i.e.*, inverse ETFs), or both (*i.e.*, leveraged/inverse ETFs). To accomplish their objectives, the portfolios underlying Non-traditional ETFs typically contain very complex investment products, including interest rate swap agreements, futures contracts, and other derivative instruments.

Non-traditional ETFs typically are designed to achieve their stated objectives only over the course of one trading session, *i.e.*, one day. As a result, between one trading session and the next, the fund manager for a Non-traditional ETF generally will rebalance the fund's holdings in order to meet its objective. For most Non-traditional ETFs, this happens on a daily basis, and is known as the "daily reset."

Within a particular day's trading session, a Non-traditional ETF may come close to achieving its intended returns. As a result of the daily reset, however, the correlation between the performance of a Non-traditional ETF and its linked index or benchmark is inexact, and there is typically at least a small difference, or "tracking error." Over longer periods of time, this "tracking error" between a Non-traditional ETF and its benchmark, may be compounded significantly. This potential divergence between the performance of the Non-traditional ETF and its benchmark becomes more pronounced during periods of volatility in the underlying index or benchmark.

FINRA advised its membership in June 2009 through FINRA Regulatory Notice 09-31 concerning Non-traditional ETFs that "[d]ue to the effect of compounding, [Non-traditional ETFs'] performance over longer periods of time can differ significantly from the performance . . . of their underlying index or benchmark during the same period of time."[1] Because of these risks and the inherent complexity of the products, FINRA Regulatory Notice 09-31 advised broker-dealers and their representatives that Non-traditional ETFs "are typically not suitable for retail investors who plan to hold them for more than one trading session, particularly in volatile markets."

FINRA's suitability rules, NASD Rule 2310 and FINRA Rule 2111, require, among other things, that a registered representative have reasonable grounds to believe that a recommendation could be suitable for at least some customers. To make a suitable recommendation, a registered representative must first have an understanding of the potential risks and rewards inherent in that recommendation. A registered representative violates the suitability rule if he or she had no

[1] FINRA Regulatory Notice 09-31.

reasonable basis to make the recommendation to any customer, regardless of the customer's wealth, willingness to bear risk, age, or other individual characteristics.

With respect to Non-traditional ETFs, FINRA Regulatory Notice 09-31 also states that the reasonable basis suitability requirement means that the registered representative must understand the terms and features of the funds, including how they are designed to perform, how they achieve that objective, and the impact that market volatility, the ETF's use of leverage, and the effect the customer's intended holding period will have on their performance.

Despite his reliance on Non-traditional ETFs, Martin exhibited a lack of knowledge regarding several fundamental aspects of these ETFs. For example, while Martin claimed to understand the "tracking errors" with these funds, he did not understand how they affected ETFs. Similarly, Martin did not understand the concept of a "decay factor" that occurs as a result of a Non-traditional ETF rebalancing its assets on a daily basis. In addition, Martin claimed to rely on Non-traditional ETFs as a hedge against a drop in the stock market despite the fact that Non-traditional ETFs are not intended as a long-term hedge against market forces generally.

Given his lack of understanding of Non-traditional ETFs, Martin did not have a reasonable basis to recommend his customers' transactions in Non-traditional ETFs, including the recommendations that they hold the products for more than a day.

In and around March 2011, Martin solicited and recommended to his 44 customers approximately 334 Non-traditional ETF transactions in approximately 15 Non-traditional ETFs, including, but not limited to, ProShares UltraPro Short QQQ (SQQQ), ProShares UltraPro Short Russell 2000 (SRTY), Direxion Daily Gold Miners Bear 2X Shares (DUST), Direxion Daily Large Cap Bear 3X Shares (BGZ), Direxion Daily Small Cap Bear 3X Shares (TZA), Direxion Daily China Bear 3X Shares (CZI), Direxion Daily Emerging Markets 3X Shares (EDZ), Direxion Daily Energy Bear 3X Shares (ERY), Direxion Daily Financial Bear 3X Shares (FAZ), and Direxion Daily Real Estate Bear 3X Shares (DRV).

The prospectuses for these Non-traditional ETFs purchased in these accounts indicate that the funds seek investment results for a single day only. For instance, the Direxion prospectus states:

> The Funds with the word "2X" in their name (collectively, the "2X Funds") and the Funds with the word "3X" in their name (collectively, the "3X Funds") seek *daily leveraged* investment results and are intended to be used as short-term trading vehicles.
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> ***The Fund seeks daily leveraged investment results and does not seek to achieve its stated investment objective over a period of time greater than one day.***

Yet, as part of his Investment Strategy, Martin recommended to his customers they hold the Non-traditional ETFs until an apocalyptic crash in the financial markets, which never occurred. As a consequence of Martin's unsuitable Investment Strategy, Martin's customers sustained significant losses in the approximate amount of $2.4 million, and he benefited from commissions received in the approximate amount of $55,912.

Accordingly, Martin did not have a reasonable basis to believe that the Non-traditional ETF products he recommended for purchases and holds were suitable for any customer, in violation of NASD Rule 2310 for the conduct prior to July 9, 2012, FINRA Rule 2111 for the conduct on and after July 9, 2012, and FINRA Rule 2010.

Misleading Communications with the Public

During the period from June 7, 2014 through October 10, 2014, Martin emailed communications to the public that violated the communications with the public provisions. The communications were emails dated June 7, 2014; June 9, 2014; August 12, 2014; October 8, 2014; and October 10, 2014. They related to his apocalyptic predictions and his unsuitable Investment Strategy to hedge against the demise of the world economy.

The communications contained numerous claims for which no basis was provided, including:

a. "We are looking at a depression which is likely to last many years, if not decades."

b. "The economy is in far worse condition that it was in 1929 and my contention is that given that the market lost 87% of its value from top to bottom, it will lose infinitely more this time."

c. "We are looking at a 90% decline in the value of stocks over the next five years."

The communications contained exaggerated and unwarranted statements and claims, including:

a. "I can only say that we have all been subjected to the most outrageous fraud and corruption at the highest levels of government ever witnessed from anywhere on earth at any time in history."

b. "It's very important that you understand this because this is where your spectacular profits are coming from."

c. "The world economic situation is beyond critical."

d. "The Wall Street hype machine has been in overdrive. Its "analysts" have been forecasting crazy earnings growth estimates for the Stoxx 600 (German) companies in order to rationalise [sic] ever higher stock prices."

The communications contained promissory statements, including:

a. "The nature of our investments allows us to benefit in a highly profitable way from this eventuality."

b. "You are well positioned in your current portfolio to benefit from this coming downturn . . ."

c. "As your positions gain value, remember that they will simultaneously gain by way of compounding so that the value of each percentage move in dollar terms will increase dramatically as the market falls."

The communication that "I had an expert prepare for me a chart of a notional Dow Jones Industrial Average inverse ETF . . ." is misleading because the person who prepared the chart had no expertise in finance and investments, when such communication implied otherwise.

The communications contained projections of future performance, including:

a. "I believe we are looking at gains even great [sic] than that on this occasion, Melanie, and if you add 2,900% to the current value of your equity, you will find you will do fine overall and you will make your money back — and much more besides."

b. "I recently had a retroactive study made on a notional Dow Jones Industrial Average triple inverse ETF following the daily movements of the Dow from September, 1929 high to the July, 1932 low. The gain (including a .75% expense ratio) was 2,900%. I firmly believe that we are due for a decline even sharper than that experienced at that time. Even if the gain was to mirrored [sic] from your current $8,000, adding 2,900% would bring the account to $240,000 and I believe we will do much better than during the period from 1929 to 1932."

c. "I can only say that I have a regression analysis done on a notional Dow Industrial triple inverse ETF, starting at $10 with the stock market (Dow Jones Industrial Average) at its September, 1929 high and ending at its low in July of 1932. The $10 turned into $284.32 including the application of a .75% expense ratio. If you were to extrapolate that to the current value of your accounts, you will see the potential for such a decline from such a move. And given that I believe the current economic fundamentals are far, far worse than those of the late 1920s, I believe that the increased potential for losses over-and-above the 87% decline in the market from 1929 to 1932 is an indicator of the increased gains you could see in your accounts."

As a result of the foregoing conduct, Martin violated FINRA Rules 2210(d)(1)(A), 2210(d)(1)(B), 2210(d)(1)(F), and 2010.

Aligning Testimony and/or Causing Inaccurate or Untruthful Testimony

On April 22, 2014, FINRA sent Martin a FINRA Rule 8210 letter, asking Martin to appear for testimony.

On July 1 and 2, 2014, while associated with GF Investments and registered with FINRA, Martin testified under oath in this matter pursuant to FINRA Rule 8210. During his interview, Martin provided testimony about his Investment Strategy.

Knowing that his supervisor DH would provide testimony soon after his interview, Martin, while associated with GF Investments and registered with FINRA, attempted to align his testimony with DH and/or cause DH to provide inaccurate or untruthful testimony. Martin disclosed his testimony to DH, including questions and subject areas, and he provided DH with a copy of his transcript.

On September 23, 2014, Martin emailed DH with a "Quiz" consisting of questions and answers, and page citations to Martin's transcript. Martin told DH that "[t]his is going to be a fiendishly difficult interview for you since you are going to have to marry up my responses with what you are going to say in answer to questions pertaining to what I was asked and answered." Incredibly, Martin also told DH that "My OTR was easy because I was able to make-it-up-as-I-went-along. Unfortunately, there is now a "trail" which you're going to have to follow. Ideally, we would spend a week together boning up on this and then you'd come away smelling like a rose."

On August 18, 2014, FINRA sent DH a FINRA Rule 8210 letter, asking DH to appear for testimony. On October 20 and 21, 2014, DH testified under oath in this matter pursuant to FINRA Rule 8210.

As a result of the foregoing conduct, Martin improperly attempted to align his testimony and/or cause inaccurate or untruthful testimony of DH, in violation of FINRA Rule 2010.

FIRST CAUSE OF ACTION
Reasonable Basis Suitability Relating to Non-Traditional ETFs
(NASD Rule 2310 and FINRA Rules 2111 and 2010)

FINRA's suitability rules, NASD Rule 2310 and FINRA Rule 2111, require, among other things, that a registered representative have reasonable grounds to believe that a recommendation could be suitable for at least some customers. To make a suitable recommendation, a registered representative must first have an understanding of the potential risks and rewards inherent in that recommendation. A registered representative violates the suitability rule if he or she had no reasonable basis to make the recommendation to any customer, regardless of the customer's wealth, willingness to bear risk, age, or other individual characteristics.

During the period from at least March 2011 through July 2015, Martin solicited, purchased and recommended his customers hold Non-traditional ETFs in his customers' accounts for years. As a result of the above, Martin did not have a reasonable basis to believe that the Non-traditional ETF products he recommended were suitable for any customer, in violation of NASD Rule 2310 for the conduct prior to July 9, 2012, FINRA Rule 2111 for the conduct on and after July 9, 2012, and FINRA Rule 2010.

SECOND CAUSE OF ACTION
Misleading Communications with the Public
(FINRA Rules 2210(d) and 2010)

FINRA Rule 2210(d)(1)(A) provides that: "[a]ll member communications must be based on principles of fair dealing and good faith, must be fair and balanced, and must provide a sound basis for evaluating the facts in regard to any particular security or type of security, industry, or service. No member may omit any material fact or qualification if the omission, in light of the context of the material presented, would cause the communications to be misleading."

FINRA Rule 2210(d)(1)(B) provides that: "[n]o member may make any false, exaggerated, unwarranted, promissory or misleading statement or claim in any communication. No member may publish, circulate or distribute any communication that the member knows or has reason to know contains any untrue statement of a material fact or is otherwise false or misleading."

FINRA Rule 2210(d)(1)(F) provides that: "[c]ommunications may not predict or project performance, imply that past performance will recur or make any exaggerated or unwarranted claim, opinion or forecast ...."

During the period from July 7, 2014 through October 10, 2014, Martin distributed communications to the public that violated the communications with the public provisions.

As a result of the foregoing conduct, Martin violated FINRA Rules 2210(d)(1)(A), 2210(d)(1)(B), 2210(d)(1)(F), and 2010.

THIRD CAUSE OF ACTION
Aligning Testimony and/or Soliciting Inaccurate or Untruthful Testimony
(FINRA Rule 2010)

FINRA Rule 2010 provides that a "member, in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade."

Martin improperly attempted to align his testimony and/or to cause inaccurate or untruthful testimony of DH.

As a result of the foregoing conduct, Martin failed to observe high standards of commercial honor and just and equitable principles of trade, in violation of FINRA Rule 2010.

Based on the foregoing, Respondent violated NASD Rule 2310 for the conduct prior to July 9, 2012, FINRA Rule 2111 for the conduct on and after July 9, 2012, FINRA Rules 2210(d)(1)(A), 2210(d)(1)(B), 2210(d)(1)(F), and FINRA Rule 2010.

Based on these considerations, the sanctions hereby imposed by the acceptance of the Offer are in the public interest, are sufficiently remedial to deter Respondent from any future misconduct, and represent a proper discharge by FINRA, of its regulatory responsibility under the Securities Exchange Act of 1934.

SANCTIONS

It is ordered that Respondent be barred from association with any FINRA member in all capacities.

The sanctions imposed herein shall be effective on a date set by FINRA staff. A bar or expulsion shall become effective upon approval or acceptance of this Order.

SO ORDERED.

FINRA

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

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