



North Carolina

Department of the Secretary of State

Securities Division

PO Box 29622 Raleigh, NC 27626-0622 • 919-814-5400 • (800) 688-4507 • www.sosnc.com

JANUARY 2010 NEWSLETTER • Vol. 2, #1

Secretary of State Elaine Marshall Takes Action to Protect North Carolina ARS Investors



NC Secretary of State
Elaine F. Marshall

Under the direction of Secretary of State Elaine F. Marshall, the Securities Division has taken action in the last month to protect North Carolina investors of auction rate securities (ARS) that were sold by **Deutsche Bank Securities, Inc.**

Deutsche Bank Securities, Inc., has agreed to buy back ARS investments from North Carolina investors under a settlement signed by Secretary Marshall on January 13, 2010.

The settlement follows an investigation by securities regulators in the Department of the North Carolina Secretary of State that found Deutsche Bank had failed to adequately supervise its investment salesmen, failed to have adequate internal written procedures and had engaged in dishonest and unethical conduct in the securities business by misrepresenting ARS investments to its clients as short-term, highly liquid holdings.

"This settlement holds Deutsche Bank accountable for selling auction rate securities to its investors without full disclosure of the risks those purchases involved," Secretary of State Elaine F. Marshall said. "Just as we said in the Credit Suisse case, we are telling national firms we will not tolerate this type of behavior."

Under the terms of the settlement, Deutsche Bank agreed to buy back all of the ARS investments it

sold in North Carolina to all individuals, charities, non-profit organizations and small- to medium-sized businesses with assets of \$10 million dollars or less with the bank.

There were a total of 55 North Carolina investors who bought over \$8.6 million in ARS holdings from Deutsche Bank. This settlement required the bank to buy back approximately \$7.8 million of those ARS investments. The remaining approximately \$825,000 in ARS investments are held by major "institutional" investors and the process for providing liquidity to those investments continues.

Secretary Marshall did give credit to Deutsche Bank for its efforts to make ARS buybacks. "We are monitoring the situation, but it looks like this investment firm is doing a good job of getting people their money back, and we are glad to see they put that effort into motion even while the investigation was ongoing."

In addition to the repurchase of all ARS held by its individual investor clients, the order also requires Deutsche Bank to repay the State of North Carolina over \$92,000 for the costs of the investigation. "The good thing here," Marshall said, "is that we got people their money back, and North Carolina got paid back for the work we had to do to make it happen."

The settlement order also allows for affected clients to enter into arbitration with the bank for consequential damages, if it can be shown that those clients suffered additional losses due to their monies being tied up in ARS investments that they

North Carolina Department of the Secretary of State
Securities Division • PO Box 29622 • Raleigh, NC 27626-0622
(919) 733-3924 • (800) 688-4507
secdiv@sosnc.com • www.sosnc.com

could not get out of at the time of the ARS market collapse.

In other news, the North Carolina Division of Securities filed an administrative petition on January 19, 2010, asking that Secretary Marshall revoke or indefinitely suspend **E*Trade Securities, LLC** from selling investments in the state. ([Click here to read the petition.](#))

Attorneys in the Division allege wrongdoing by the company between 2005 through 2008 in respect to its sale of Auction Rate Securities (ARS) to customers in North Carolina.

The petition alleges that E*Trade engaged in a widespread effort to portray the ARS investments as short-term, highly liquid securities that were suitable for short-term cash management practices. The petition also alleges that E*Trade did little to educate its clients to the actual risks of ARS investments and did not supervise its salesmen's conduct properly. Securities officials also state in the petition that the company did not create and preserve records correctly regarding its ARS sales activities.

The petition alleges these misleading practices were commonly used on E*Trade clients even though actual ARS investments are typically financial instruments that mature over long periods. The Auction Rate Securities market suffered a major collapse in 2008 that has left many investors stuck holding ARS investments that they once believed they could cash out at any time.

The petition listed the difficulty many E*Trade clients have had in getting their monies back out of the collapsed ARS market. Division officials believe there was at least \$8,375,000 in ARS investments held by North Carolina E*Trade customers at the time of that market collapse.

Allegations in the administrative petition were based on investigation by the Securities Division on its own and in cooperation with securities regulators from other states as part of the North American Securities Administrators Association (NASAA) ARS Task Force. The NASAA ARS Task Force formed after the ARS market collapse in 2008 and has worked on behalf of investors to reach settlements with investment firms since that time.

However, Division officials say they have been unable to reach a settlement with E*Trade, and that no other state regulator has been able to reach a settlement with the company either.

The North Carolina Securities Act gives E*Trade 30 days in which to request a public hearing before Secretary of State Marshall or her designee on the allegations in the petition.

If, after the hearing, the allegations are found to be correct and relief is warranted, a final administrative order could be issued suspending or revoking E*Trade Securities license to conduct business in North Carolina. The company is a subsidiary of E*Trade Bank. A final order would ban the securities company subsidiary only from doing business in North Carolina.

NC Adopts Rule on Senior Designations

On January 22, 2010, the NC Rules Review Commission approved the Department of the Secretary of State's proposed rule on the use of senior designations by securities dealers, securities salesmen, investment advisers and investment adviser representatives. The rule becomes effective on February 1, 2010.

The rule, based on the [Model Rule](#) that the North American Securities Administrators Association (NASAA) adopted on March 20, 2008, applies only to people registered as securities dealers or salesmen and as investment advisers or investment adviser representatives.

In North Carolina, securities and investment advisers are prohibited by law from engaging in dishonest or unethical conduct. However, in recent years, securities regulators across the nation, including the NC Securities Division, have seen an explosion in the number of professional designations that various financial services professionals use in selling investment products. According to the September 2007 report, [Protecting Senior Investors: Report of Examinations of Securities Firms Providing "Free Lunch" Sales Seminars](#), government and regulatory investigators determined that the use of some of these titles were confusing to many people and served to mislead them into thinking that the certifications were issued by a regulatory authority, when in fact that is not the case. In many cases, the credential serves merely as a

marketing tool designed to convey the impression that the holder has more expertise than perhaps (s)he has. The rule which the Securities Division has adopted, therefore, is intended to prohibit the deceptive and misleading use of such designations in connection with the sale of investment products and services. To read the full notice, click [here](#).

Massey Meets with Charlotte FPA



On January 19, 2010, Deputy NC Securities Administrator David Massey (center), and Senior Financial Investigator Darren Kearns (far right), met in Charlotte with members of the Charlotte Chapter of the Financial Planners Association (FPA). Massey was invited to provide a general overview of the regulatory landscape as it relates to investment advisers. Pictured are (L-R): Harry Greyard, Chia-Li (Jolly) Chien, Bill Gary, Kathy Stanley, Robert Higgins, Diane Willis, Massey, Lynn Davidson, Kris Carroll, Cindy Reninger and Kearns.

Calendar of Upcoming Events



A representative from the Securities Division will be giving an anti-fraud presentation on the following dates and locations. Dates and times are subject to cancellation (although cancellations are rare), so please call the contact number listed to confirm the event is still on before leaving for it. All presentations are free and open to the public unless otherwise indicated. If you would like to schedule a speaker for your church, business, group or organization, please contact [John Maron](#) or [Barbara Bennett](#) at (800) 688-4507.

Date	City	Details
2/12/2010	Goldsboro	Seymour Johnson AFB. 9:00 AM – Noon. Open to airmen and their families. Contact the Airman & Family Readiness Center at (919) 722-1123.
2/17/2010	Shelby	Leona Smith Neal Memorial Senior Center , 100 T.R. Harris Drive. 1:30 PM. Call (704) 482-3488 for more details.
2/23/2010	New River	Marine Corps Air Station. Time: TBA. Open to Marines and their families. Contact the Marine & Family Services Center (910) 449-6110.
2/23/2010	Cherry Point	Marine Corps Air Station. Time: 1:00 PM – 4:30 PM. Open to Marines and their families. Contact the Marine & Family Services Center (252) 466-4401.
2/26/2010	Fayetteville	Fayetteville-Cumberland Senior Center , 739 Blue St. 10:00 AM. Call (910) 433-1574 for more details.

North Carolina Department of the Secretary of State
 Securities Division • PO Box 29622 • Raleigh, NC 27626-0622
 (919) 733-3924 • (800) 688-4507
secdiv@sosnc.com • www.sosnc.com

Recent Enforcement Actions

(For prior administrative and criminal actions, click the badge to the right.)

On **January 25, 2010**, J.V. Huffman, Jr., 46, of Claremont, NC, pleaded guilty in a Catawba County courthouse to 14 counts of obtaining property by false pretense and 14 counts of securities fraud. He was sentenced to serve 30 to 40.5 years in prison. In November 2008, investigators with the NC Securities Division arrested Huffman for violating the North Carolina Securities Act. At the time of his arrest, Huffman was not registered to sell securities, which the Act requires. Between 1991 and 2008, investigators determined that some 500 people had invested about \$25 million with Huffman and his company, Biltmore Financial Group, Inc. Division investigators found that Huffman issued various kinds of promissory notes through Biltmore Financial Group, claiming funds would be used to buy and sell real estate mortgages or deeds of trust. But the funds were instead converted to Huffman's personal use, supporting a lavish lifestyle.



On **January 19, 2010**, the Securities Division filed an Administrative Petition seeking to revoke or suspend the North Carolina security dealer registration of E*Trade Securities, LLC. The Administrative Petition contains allegations of misconduct by E*Trade in the offer and sale of Auction Rate Securities (ARS) to North Carolina residents between 2005 and 2008. E*Trade has a right to an administrative hearing before this matter is concluded. The Division has cooperated with the North American Securities Administrators Association (NASAA) ARS Task Force in its investigation into the collapse of the ARS market in 2008. [Click here to see the Petition.](#)

All investors are strongly encouraged to contact the Securities Division at (919) 733-3924 or toll-free at (800) 688-4507 to check that their investment professional is properly registered **before** transferring any assets to that person's control. One five-minute telephone call to the Securities Division could protect your entire life's savings from being stolen from you. For a wealth of investor education information, please visit our Web site, www.sosnc.com. Click the yellow box entitled "Investment Securities".

This newsletter is produced by the Investor Education Program of the Securities Division of the North Carolina Department of the Secretary of State. If you have questions or comments about this publication, or would like to schedule an investor education presentation with your group or organization, please email [John Maron](mailto:John.Maron@sosnc.com), Director of the Investor Education Program, or call (919) 715-1067.

Please help us publicize the educational information in this mailing by forwarding it to your contacts around the state. If you no longer wish to receive mailings from the Securities Division, please send an email to: jmaron@sosnc.com with "Remove from mailing list" in the subject line.

Remember that if an investment sounds too good to be true, it **probably** is!