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B-D, execs who allegedly preyed on seniors hit with $2.6M in fines, restitution

Brookstone socked by Finra for sale of CMOs to the elderly; brokerage to appeal nonfinal decision

By Bruce Kelly

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In a decision rendered last week, a Finra hearing panel fined a midsize independent broker-dealer $1 million over the sale of risky tranches of collateralized mortgage obligations. The panel also ordered the firm, its chief executive and majority owner, along with a broker, to pay a total of $1.62 million in restitution to clients.

Brookstone Securities Inc. made “fraudulent misrepresentation and omissions of material fact in selling complex, esoteric and risky tranches of [CMOs] to unsophisticated, elderly and retired investors,” according to the decision by the Financial Industry Regulatory Authority Inc. The executive, Brookstone's owner, Antony Lee Turbeville, and a broker, Christopher Dean Kline, were barred from working with a Finra-registered B-D.

Brookstone and Mr. Turbeville were jointly ordered to pay clients restitution of $440,600, while the firm and Mr. Kline were jointly ordered to pay $1,179,500 in restitution.

Another Brookstone executive and minority owner, former chief compliance officer David Locy, was suspended from the securities industry for two years, barred in the future from working as a supervisor and fined $25,000 in the matter.

Brookstone has 198 registered representatives and last year had total revenue of $27.3 million, according to a filing with the Securities and Exchange Commission. Finra filed its complaint against the firm in 2009, and Brookstone and its executives denied the allegations. A 16-day hearing was held over last year and this year to decide the matter.

Brookstone will appeal Finra's decision."This is a nonfinal decision by the Finra hearing officer," said the firm's current CEO, Paul Richardson. "We are appealing the decision and refuting the underlying allegations."

According to the decision, Mr. Turbeville and Mr. Kline "preyed on their elderly customers' greatest fears," such as losing their assets to nursing homes and becoming destitute during their retirement and old age, in order to induce them to purchase unsuitable CMOs.

By 2005, interest rates were increasing, and the negative effect on CMOs was evident to Mr. Turbeville and Mr. Kline, yet they did not explain the changing conditions to their customers, according to the Finra panel's decision.

Brookstone, Mr. Turbeville and Mr. Kline intentionally or recklessly misrepresented the CMO investments to their customers as a safe way, through government-backed bonds, to obtain a high rate of return on their investments," according to the decision. "In reality, the CMOs the brokers purchased for the customers were high-risk investments whose returns were not assured, but instead, because of interest rate changes, were subject to dramatic changes in maturity, cash flow and value."

According to the decision, Brookstone, Mr. Turbeville, who has also worked as a rep, and Mr. Kline bought $63.5 million in CMO bonds between July 2005 and July 2007, and sold $62.3 million of CMOs. Brookstone earned $492,500 in commissions over that time, and investors lost $1.62 million, according to Finra.

Ten years ago, both Mr. Turbeville and Mr. Kline worked at the same broker-dealers as Cliff Popper, a broker known for his high living and a prominent seller of CMOs. Those firms include the defunct GunnAllen Financial Inc. Mr. Popper committed suicide this year.

Mr. Turbeville testified for an entire day, according to the decision. "While he displayed an understanding of the CMOs, the hearing panel did not believe his claims that he fully explained the strategy to his clients so that they understood all of the risks involved in trading CMOs or the risks of trading on margin," according to the decision. "His testimony that his customers' account forms accurately reflected their investment objectives was contradicted by each of his customer's testimony and sworn declarations. He showed no remorse for his customers' losses, and insisted that they understood the CMO strategy, despite their claims that they did not."

The seven clients, who were between 61 and 91, never understood how the CMOs worked and were unsophisticated investors, according to the Finra decision. Mr. Turbeville told one client that if he allowed the use of margin, he could reasonably expect an annual return of 15%, according to the regulator.

Finra has a long-standing warning to firms and advisers about selling CMOs, dating back to 1993, when the CMO market collapsed due to rising interest rates. At the time, Finra, formerly NASD, warned that "in light of the complexity and the varying risk characteristics of CMOs, member must be conversant in all of the characteristics of CMOs to assess adequately the suitability of CMOs for their customers. Moreover, members must ensure that their customers understand the characteristics and risks associated with CMOs."