

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 5330 / August 26, 2019

ADMINISTRATIVE PROCEEDING
File No. 3-19378

In the Matter of

Laurel Wealth Advisors, Inc.

Respondent.

**ORDER INSTITUTING ADMINISTRATIVE
AND CEASE-AND-DESIST PROCEEDINGS,
PURSUANT TO SECTIONS 203(e) AND
203(k) OF THE INVESTMENT ADVISERS
ACT OF 1940, MAKING FINDINGS, AND
IMPOSING REMEDIAL SANCTIONS AND A
CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) against Laurel Wealth Advisors, Inc. (“Respondent” or “LWA”).

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”), which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order (“Order”), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds¹ that

Summary

1. LWA is an investment adviser registered with the Commission. From at least March 2013 to June 2015 (the "relevant time period"), an investment adviser representative ("IAR") associated with LWA engaged in undisclosed "cherry-picking," a practice of fraudulently allocating profitable trades in an omnibus account to favored accounts.

2. LWA failed reasonably to supervise the IAR who engaged in cherry-picking and failed to implement policies and procedures reasonably designed to prevent violations of the Advisers Act and its rules. More specifically, LWA had a compliance procedure to prevent conflicts of interest that required IARs to pre-clear and obtain written approval before trading in their personal accounts, but LWA did not implement that procedure until January 2015.

3. During the relevant time period, LWA's Code of Ethics as disclosed in its Forms ADV stated that it had a pre-clearance procedure for IARs' personal trading and that the firm required all transactions be carried out in a way that put its clients' interests before its employees' interests. These disclosures were false and misleading because LWA did not implement the pre-clearance procedure until January 2015, and an IAR's misconduct put his personal interests before his clients' interests.

Respondent

4. **Laurel Wealth Advisors, Inc.** is a California corporation with its principal place of business in La Jolla, California. LWA registered with the Commission as an investment adviser in May 2011 and had \$1.16 billion in assets under management as of June 2019.

Other Relevant Person

5. **Joseph C. Buchanan**, age 57, resides in Camarillo, California. Buchanan was an investment adviser representative with LWA from November 2011 until December 2015. On December 20, 2013, FINRA suspended Buchanan until November 23, 2015 for failure to satisfactorily respond to a request for information relating to his time as a registered representative prior to joining LWA.

¹ The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

Facts

The Cherry-Picking Scheme

6. Buchanan was the second IAR to join LWA in 2011. Beginning in May 2012, Buchanan used his omnibus account with LWA's brokerage provider to purchase a number of shares in an omnibus account for subsequent allocation to his client and personal accounts. The personal trading by Buchanan consisted of predominately the same securities as those traded for his clients.

7. During the Relevant Period, Buchanan delayed the allocation of trades from his omnibus account until after the purchases were executed, sometimes waiting until after the market closed or even the subsequent day. Trading positions that became profitable later the same day (e.g., because the share prices of the securities had increased after the purchase was executed) were disproportionately allocated to Buchanan's personal accounts. On the other hand, Buchanan allocated to his clients' accounts a disproportionate number of the positions that became unprofitable later the same day because share prices had decreased after a trade's execution.

8. Profitable trades based on same-day gains in Buchanan's omnibus account were often sold on the same day, before or after allocation to Buchanan's personal or client accounts, and thus amounted to realized day-trading profits. Trades that had unrealized same-day gains or losses could also be held after allocation by Buchanan and his clients as part of a short or long term investment strategy.

9. From at least March 2013 to June 2015, Buchanan's allocations from his omnibus account to his personal account had same-day realized and unrealized gains of 0.89%, or \$56,075 in same-day profits, while allocations to Buchanan's client accounts had same-day realized and unrealized losses of 0.13%, or a combined same-day loss of \$60,821. In February 2015, LWA's brokerage provider suspended for one month Buchanan's use of his omnibus account due to the number of late allocations. Buchanan's access to his omnibus account was suspended indefinitely by LWA in June 2015 and permanently removed by LWA's brokerage provider in August 2015.

10. The realized and unrealized gains for allocations to Buchanan's personal accounts are statistically significant in that the likelihood that these same-day profitable trades were disproportionately allocated to Buchanan's accounts was due to random chance is less than one in one billion.

LWA's Compliance Failures and Misleading Disclosure

11. Registered investment advisers are required to adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules adopted by the Commission under the Act.

12. During the relevant time period, LWA's compliance policies and procedures manual required investment adviser representatives to pre-clear and obtain written pre-approval before buying or selling most securities, such as common stocks or options, in their personal accounts. Although a third party firm that LWA had retained to conduct a risk assessment in July 2014 uncovered that LWA was not observing its preclearance procedure, LWA failed to implement this procedure until January 2015.

LWA's Failure to Supervise Buchanan

13. LWA failed to reasonably supervise Buchanan through its inadequate oversight of Buchanan's omnibus account. Although LWA's brokerage provider alerted LWA of Buchanan's late allocations in written notifications and telephone calls on or about April 2013, LWA did not reasonably address Buchanan's conduct. Despite these warnings and the one-month suspension imposed by LWA's brokerage provider on Buchanan's omnibus account from February 2015 until March 2015, LWA permitted Buchanan to use his omnibus account thereafter until June 2015, when LWA permanently suspended his access.

LWA's Misleading Disclosure

14. Registered investment advisers are required to file Forms ADV with the Commission, and to update them at least annually. Form ADV includes Part 2A, which provides disclosures to advisory clients about the qualifications and business practices of investment advisers. Registered investment advisers are required to deliver Part 2A to their clients at the beginning of the advisory relationship, and to provide clients with an updated Part 2A whenever material changes are made.

15. During the relevant period, LWA's Form ADV Part 2A disclosures represented that the firm would place its clients' interests before those of its employees. For example, LWA represented that the firm requires that all "personal investment transactions of its members and employees ... be carried out in a way that does not endanger the interest of any client." LWA's Form ADV Part 2A also contained a section on "Code of Ethics," which stated in pertinent part: "Therefore, in order to prevent conflicts of interest, we have in place a set of procedures (including a pre-clearing procedure) with respect to transactions effected by our members, officers and employees for their personal accounts." As described in paragraph 12 above, LWA's Code of Ethics and compliance manual, which was attested to by Buchanan, described a pre-clearing procedure; but LWA did not actually implement such a procedure until January 2015.

Violations

16. As a result of the conduct described above, LWA willfully violated Section 206(2) of the Advisers Act, which prohibits an investment adviser from engaging "in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client." Proof of scienter is not required to establish a violation of Section 206(2) of the Advisers

Act, but may rest on a finding of negligence. *SEC v. Steadman*, 967 F.2d 636, 643 n.5 (D.C. Cir. 1992) (citing *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195 (1963)).

17. As a result of the conduct described above, LWA willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder, which require that registered advisers adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules adopted by the Commission under the Act. A violation of Section 206(4) and the rules thereunder does not require scienter. *Steadman*, 967 F.2d at 647.

18. As a result of the conduct described above, LWA failed reasonably to supervise Buchanan within the meaning of Section 203(e)(6) of the Advisers Act.

LWA's Remedial Efforts

19. In determining to accept LWA's offer, the Commission considered the remedial acts undertaken by LWA and its cooperation with the Commission staff in the investigation of this matter. Among other things, LWA hired a new chief compliance officer (effective January 2018), heightened restrictions governing IARs' personal trading, implemented technological preclearance of personal trading, and engaged an outside compliance consultant and counsel for guidance. LWA also revised its Code of Ethics and compliance and procedures manual and provided training focused on personal trading to LWA's IARs.

Undertakings

20. Respondent has undertaken to:

21. **Order Notification.** Within thirty (30) days of the issuance of this Order, LWA shall mail to each of Buchanan's former clients a copy of this Order. LWA shall certify, in writing, compliance with this undertaking. The certification shall provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Commission's staff may make reasonable requests for further evidence of compliance, and LWA agrees to provide such evidence. The certification and supporting material shall be submitted to Diana K. Tani, Assistant Regional Director, Los Angeles Regional Office, Securities and Exchange Commission, 444 South Flower Street, Suite 900, Los Angeles, CA 90071, with a copy to the Office of Chief Counsel in the Enforcement Division, no later than sixty days from the date of completion of this undertaking.

IV.

In view of the foregoing, the Commission deems it appropriate and, in the public interest to impose the sanctions agreed to in Respondent's Offer.

Accordingly, pursuant to Sections 203(e) and 203(k) of the Advisers Act, it is hereby ORDERED that:

A. Respondent LWA cease and desist from committing or causing any violations and any future violations of Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-7 promulgated thereunder.

B. Respondent LWA is censured.

C. Respondent LWA shall, within 21 days of the entry of this Order, pay a civil money penalty in the amount of \$100,000.00 to the Securities and Exchange Commission. The Commission may distribute civil money penalties collected in this proceeding if, in its discretion, the Commission orders the establishment of a Fair Fund pursuant to 15 U.S.C. § 7246, Section 308(a) of the Sarbanes-Oxley Act of 2002. The Commission will hold funds paid pursuant to this paragraph in an account at the United States Treasury pending a decision whether the Commission, in its discretion, will seek to distribute funds or, subject to Section 21F(g)(3) of the Securities Exchange Act of 1934, transfer them to the general fund of the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. § 3717.

Payment must be made in one of the following ways:

- (1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
- (2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or
- (3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying Laurel Wealth Advisors, Inc. as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Diana K. Tani, Assistant Regional Director, Securities and Exchange Commission, Los Angeles Regional Office, 444 South Flower Street, Suite 900, Los Angeles, CA 90071.

D. Regardless of whether the Commission in its discretion orders the creation of a Fair Fund for the penalties ordered in this proceeding, amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all

purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondent agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that it shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

E. Respondent LWA shall comply with the undertakings enumerated in Section III above.

By the Commission.

Vanessa A. Countryman
Secretary