

Prepared Response of A. Heath Abshire  
Arkansas Securities Commissioner  
before the  
Joint Performance Review Committee  
January 22, 2014

Senator English, Representative Rice, and other Committee members,

I submit this Prepared Response to the allegations of Mr. David Knight and Stephens Inc. (Stephens) as contained in Mr. Knight's prepared remarks and his letter to Senator English and Representative Rice dated January 16, 2014.

I understand that the Committee is concerned with the legality of three consent orders entered into between the Arkansas Securities Department (Department) and parties other than Stephens.<sup>1</sup> The legality of the Three Consent Orders is questioned under the Arkansas Securities Act and under Ark. Code Ann. § 21-8-304(a). The Three Consent Orders predated an unrelated consent order between the Department and Stephens.<sup>2</sup> Stephens' and Mr. Knight's allegations regarding settlement negotiations and the subsequent Stephens Settlement are irrelevant in determining the legality of the Three Consent Orders not involving Stephens. If any violations of the Arkansas Securities Act or Ark. Code Ann. § 21-8-304(a) occurred, they occurred at the time of the particular consent order. I maintain that there were no violations of the law in connection with the Three Consent Orders.

As to the legality of recognizing charitable donations in consent orders under the Arkansas Securities Act, I have cited legal authority authorizing my actions. I also note the news articles in which others agree with my legal analysis. I also point out that recognizing charitable contributions in settled actions is a common practice in many different regulatory areas and has occurred for a number of years. See Exhibits N, Q, and R.

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<sup>1</sup> These three consent orders are In the matter of ProEquities, Inc., Order No. S-12-0135-12-OR01 (Nov. 19, 2012); See Exhibit S; In the Matter of Uvest Financial Service Group, Inc., Order No. S-12-0136-12-OR01 (Dec. 13, 2012); See Exhibit T; and In the Matter of Crews & Associates, Inc., Order No. S-10-006-13-OR03 (July 9, 2013); See Exhibit M. (Exhibits M, S, and T collectively referred to hereafter as the "Three Consent Orders").

A prior consent order, In the Matter of Bankers Life and Casualty Company and BLC Financial Services, Inc., Order No. S-12-0134-12-OR01 (Sep. 18, 2012); See Exhibit EE, is a part of the same multi-state investigation that produced the ProEquities and Uvest consent orders. As can be seen from comparing Bankers Life to ProEquities and Uvest, it is clear Bankers Life involved more extensive findings of fact and remedies.

Contrary to Stephens' allegations in paragraph 19 of its Citizen Complaint, Maine recognized a donation to NASAA of \$20,000 in connection with the Banker's Life settlement executed in Maine.

<sup>2</sup> In the Matter of Stephens Inc., Order No. S-12-0067-13-OR01 (Aug. 22, 2013) (hereinafter, the "Stephens Settlement.")

The next question is whether a common act, legal under the Arkansas Securities Act, was somehow rendered illegal under Ark. Code Ann. § 21-8-304(a) by virtue of my status as President of NASAA during the time of the Three Consent Orders. Stephens and Mr. Knight allege that I improperly profited or benefitted from the contributions recognized in the Three Consent Orders. The Arkansas Ethics Commission is investigating the allegations contained in the Stephens Citizen Complaint and I look forward to the resolution of that proceeding. I am also thankful that this question will be answered based upon actual, real facts rather than speculation, hypotheticals, and unfounded allegations.

As stated before, Stephens' and Mr. Knight's allegations regarding the Stephens Settlement and the negotiations surrounding that settlement are in no way probative on the legality of the Three Consent Orders with other parties. However, Stephens and Mr. Knight devote substantial time to allegations regarding the Stephens Settlement, so I feel obliged to respond briefly.

Although Stephens alleges there was a "deal" in place after our meeting on August 8, 2013, its own evidence proves that there was none. As Stephens and Mr. Knight admit, the amount of the fine was still in dispute. See paragraph 26 of Stephens Citizen Complaint; paragraph 8 of Kim Fowler's Affidavit; and Exhibit BB. All parties were aware that the amount of the fine was dependent on my review of the allegedly similar Morgan Keegan order and consideration of the precise language of the consent order. Further negotiations were to take place. After reviewing the terms of the proposed consent order and determining that the Morgan Keegan order was not sufficiently similar to the Stephens facts, I instructed the Staff to offer \$25,000 as the amount of the fine. This action was wholly justified by the facts and terms of the consent order. See Exhibits X (p.8), BB, and FF.

The fact that no deal was in place on August 8 is further evidenced by an email from Kim Fowler to Scott Freydl on August 21, 2013. This email reads as follows:

I do not want to be irritating or difficult, but please understand that the increase to \$25,000 has put David Knight, Kevin Burns and I, as lawyers, in an awkward situation with Stephens top management. Based on our meeting with the Commissioner, we told them the fine was expected to be \$15,000-\$20,000. We will now have to go back to them and tell them the amount has increased. Would it be appropriate for David to call the Commissioner directly or for us to meet with him again?

See Exhibit BB; page 131 of Stephens Handout from January 8, 2014. This email shows that the Stephens legal team had expectations regarding the range of a fine.

This is proof that there was no deal. Further, it shows the real reason I find myself before this Committee and the Arkansas Ethics Commission. The Stephens legal team promised Stephens management a deal that did not exist. The Stephens Citizen Complaint and this proceeding are the results of that untimely promise.

There are a few other allegations in Mr. Knight's prepared remarks I would like to address. Mr. Knight alleges that the administrative process is "not a level playing field" as the Securities Commissioner often serves as hearing officer in matters that proceed to hearing. Not only is this argument irrelevant in determining the legality of the Three Consent Orders, it ignores years of administrative practice and the appointment of hearing officers under Ark. Code Ann. §§ 23-42-202, 25-15-213, and Rule 601.02 of the Rules of the Arkansas Securities Commissioner. See Exhibit GG.

As Securities Commissioner, I am required to conduct proceedings in a fair and impartial matter. In the few cases in which I am involved during investigation or negotiation, I would consider appointing a hearing officer to preside at any hearing. The parties may also make a Motion for Recusal and request the appointment of a new hearing officer. I was involved in the negotiations with Stephens based on its reputation and community presence. Had this matter gone to hearing, I would have appointed a hearing officer even if I had not received a Motion to Recuse from Stephens or the Staff.

Stephens and Mr. Knight improperly characterize the Department's final settlement offer as a threat. Again, this is irrelevant in determining the legality of the Three Consent Orders. Making a final offer of settlement can hardly be considered a threat. Pointing out the potential adverse consequences of a party's failure to settle is also not a threat. It is in no way a threat to point out that if no settlement is reached, a subsequent legal action may involve additional violations and additional penalties. This is basic aspect of every legal negotiation. Further, it can hardly be considered a threat to engage in a perfectly legal and appropriate legal proceeding if no settlement is reached. Stephens is a sophisticated party. It is the largest investment bank in Arkansas. Stephens' allegations that it felt threatened by reference to a possible legal proceeding by the Department are absurd.

Under the heading "Statutory Issues," Mr. Knight misconstrues my arguments regarding recognition of payments to a third party as part of a settlement. These payments include payments to investors, whether in the form of restitution or otherwise, as well as charitable contributions. Contrary to Mr. Knight's assertions, the Securities Commissioner has no general authority to order restitution. Restitution is provided as an ancillary remedy that the Securities Commissioner may obtain in an action in Pulaski County Circuit Court. See Ark. Code Ann. § 23-42-209(b). If an action against a regulated entity proceeds to

hearing, the available remedies are limited to (i) an order denying, suspending, revoking, or making conditional the regulated entity's license, or (ii) fines of up to \$10,000 per violation, or an amount equal to the amount received by the regulated entity. These amounts are raised to \$20,000 or two times the amount of money received if the victim is 65 or older. See Ark. Code Ann. § 23-42-308.

Restitution or any other remedy that involves something other than a fine or an action against a license is only authorized by Ark. Code Ann. §§ 23-42-209(c) and 23-42-308(h) which reads:

Nothing in this section shall prohibit or restrict the informal disposition of a proceeding or allegations which might give rise to a proceeding by stipulation, consent, or default, in lieu of a formal or informal hearing on the allegations or in lieu of the sanctions authorized by this section.

Any payment to a wronged investor, whether as restitution, disgorgement of profits, or otherwise is only available under this section authorizing negotiation and execution of a consent order in lieu of the sanction authorized under the Securities Act. The Securities Commissioner may recognize payments to third parties, whether contributions or payments to customers, only in a consent order. Those payments, as well as all other remedies, facts, and circumstances, will determine whether the overall remedies negotiated and whether those remedies will include a fine. See Exhibits V, W, and X.

Most of Stephens' and Mr. Knight's proposed legislative reforms are irrelevant in relation to the legality of the Three Consent Orders. I ask that this Committee consider the input of other regulated industries and the interests of Arkansas investors prior to making any changes to the Securities Act. I think many broker-dealers and investment advisers would prefer an administrative action over a circuit court proceeding. Also, I think that many appreciate the breadth of actions that can be considered in consent orders including payments to investors and contributions.

I would also like to briefly respond to Mr. Knight's letter to Senator English and Representative Rice.

The amounts of contributions recognized in the Three Consent Orders are absolutely irrelevant in determining the legality of the Three Consent Orders. The Three Consent Orders were either legal or illegal at the time they were entered. Again, I maintain that the Three Consent Orders were legal.

The data contained in Mr. Knight's letter only covers recognized donations to one organization over a period of five years. It does not provide an overview of

contributions recognized prior to 2009 or recognized contributions to any organization other than NASAA.

The data shows 32 individual contributions to NASAA. Three of those were recognized in Arkansas; the Three Consent Orders. In other words, less than 10% of the consent orders recognizing contributions were Arkansas consent orders. If you take out the Crews consent order, Arkansas-related contributions would total \$22,358. This would make Arkansas seventh on the list.

Stephens alleges that I have contributed a disproportionately large amount of the settlement payments collected through enforcement activities without legislative oversight. Not only does this argument ignore the fact that recognizing a charitable contribution is not the same as collecting a settlement payment, but it also fails to compare the recognized contributions to the fines, fees, and other monies collected by the Department and deposited into the State Treasury. Over the last four fiscal years, the Department had Total Revenues totaling \$62,872,379.36. General revenues totaled \$43,191,203.53. Of this amount \$17,607,214.38 was designated special revenues, an average of \$4,401,803.60 per year. Notwithstanding this amount of designated special revenue, the Department's total appropriation during this period ranged from a low of \$3,195,480.00 to a high of \$3,479,649.00. Revenues from fines as a percentage of total revenues were as follows.

Fiscal Year	% of Fines as Total Revenues	\$ Amount of Fines
2012-2013	1.18%	\$195,537.98
2011-2012	3.13%	\$488,411.01
2010-2011	2.23%	\$343,583.58
2009-2010	10.02%	\$1,528,921.68

See Exhibit Y and Summary Financial Exhibit attached to this response. Stephens' and Mr. Knight's comments regarding changes to Ark Code Ann. § 23-42-213 contained in Mr. Knight's prepared remarks show a misunderstanding regarding the Department as a special revenue agency and the budgeting/appropriation process that is applicable to the Securities Department. The Department does not make its decisions to fine, or the amount of the fine, based on Department budgetary needs. The amount of special revenues in the form of fines pales in comparison to the amount received as fees. Further, an increase in the fine revenue would not benefit the Department as the Department is also subject to Legislative oversight of the budgeting and appropriation process.

In closing, I note that all matters before the Arkansas Ethics Commission are supposed to be confidential at this stage. Not only did Stephens give its Citizen Complaint to the press, it is an exhibit filed before this Committee. If you want to

know why Stephens has taken these actions, you need only look to the email from Kim Fowler to Scott Freydl on August 21. Even though the amount was still in dispute, and I still had to review the Morgan Keegan case and the particular language of the consent order, the Stephens legal team promised its management an expected range of the fine. The difference in the expected range and the actual fine? \$5,000. The actual fine amount, \$25,000, as well as the language of the consent order, were still great deals for Stephens. See Exhibit FF.

By challenging my integrity, Stephens has attacked me personally. In an effort to either save face or retaliate, Stephens has elected to file its Citizen Complaint with the Arkansas Ethics Commission, make that complaint public during the pending investigation, and ensure the action that finds me before this Committee. I stand behind the legality of all actions I have taken as Arkansas Securities Commissioner. While my appearance before this Committee and the Arkansas Ethics Commission are not pleasant experiences, they are necessary. First, to clear my name of the allegations levied against me by Stephens. Second, in hope that future Securities Commissioners do not allow the threat of unwarranted personal attacks deter them from taking appropriate action under the Securities Act.

Senator English and Representative Rice, I respectfully request the opportunity to respond after the regulated industries have been given the opportunity for public comment. Thank you, and thank you Committee members.

Fiscal Year	Total Amount of Securities Fines		Total Revenues	% Fines of Total Revenues	Total General Revenue	Total Special Revenue Designated	Total Appropriation - Operations	Special Revenue limit
	Collected	Total Revenues						
12-13	\$195,537.98	\$16,601,391.13	1.18%	\$10,392,011.33	\$4,587,779.80	\$3,479,649.00	\$2,000,000.00	
11-12	\$488,411.01	\$15,612,071.40	3.13%	\$10,946,436.06	\$4,515,479.94	\$3,426,918.00	\$2,000,000.00	
10-11	\$343,583.58	\$15,400,110.92	2.23%	\$10,789,734.07	\$4,459,331.39	\$3,195,480.00	\$1,000,000.00	
09-10	\$1,528,921.68	\$15,258,756.29	10.02%	\$11,063,022.07	\$4,044,623.25	\$3,437,750.00	\$1,000,000.00	
	\$2,556,454.25	\$62,872,329.74		\$43,191,203.53	\$17,607,214.38			
Investor Education fund limited to \$150,000 per year								
08-09	\$42,510.86	\$14,058,812.31	0.30%	\$9,901,494.42	\$4,101,767.18	\$2,932,688.00	\$1,000,000.00	
07-08	\$64,405.00	\$15,031,985.74	0.43%	\$10,554,630.29	\$4,361,482.32	\$3,252,631.00	\$1,000,000.00	