

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 82954 / March 27, 2018

ADMINISTRATIVE PROCEEDING
File No. 3-18411

In the Matter of

**WEDBUSH SECURITIES,
INC.,**

Respondent.

**ORDER INSTITUTING ADMINISTRATIVE
PROCEEDINGS, PURSUANT TO SECTION
15(b) OF THE SECURITIES EXCHANGE
ACT OF 1934 AND NOTICE OF HEARING**

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Sections 15(b) of the Securities Exchange Act of 1934 (“Exchange Act”) against Wedbush Securities, Inc. (“Wedbush” or “Respondent”).

II.

After an investigation, the Division of Enforcement alleges that:

A. SUMMARY

1. Wedbush failed reasonably to supervise one of its registered representatives, Timary Delorme (“Delorme”), who engaged in manipulative trading activity of penny stocks over multiple years, as detailed below. Wedbush was aware of certain aspects of her activity in 2012 and 2013 but its supervisory policies and implementation systems failed reasonably to guide staff on how to investigate the activity. Specifically, in late 2012 and early 2013, Delorme’s supervisors: (1) reviewed an email outlining her role in fraudulent transactions involving penny stocks; (2) received copies of two FINRA arbitrations filed by her customers outlining serious allegations of her role in their investments in the same penny stock issuers; (3) learned of a FINRA inquiry into her personal trading in one of those penny stock issuers; and (4) learned of a separate FINRA inquiry into the allegations underlying the customer arbitrations. Wedbush had no clear process for how to handle red flags of potential market manipulation.

B. RESPONDENT

2. Wedbush is a California corporation with its headquarters in Los Angeles, California. The firm was founded in 1955 and registered with the NASD as a broker-dealer in 1955, with the Commission as a broker-dealer in 1966, and as an investment adviser in 1970. Wedbush is a wholly-owned subsidiary of Wedbush, Inc., a privately-held company. In June 2014, the Commission charged Wedbush with violating, among other rules, Exchange Act Rule 15c3-5 for providing market access to international traders without proper controls in place. Wedbush settled with the Commission in November 2014, paying a \$2.44 million penalty and agreeing to retain a consultant to conduct a comprehensive review of its system of controls and procedures for compliance with all applicable regulatory requirements relating to its market access business, including but not limited to Exchange Act Rules 15c3-5 and 17a-8; to assess its corporate governance and culture of compliance with respect to its market access business; and to provide recommendations for improvements as may be needed. In February 2018, Wedbush settled with the Commission for violations of Sections 15(c)(3) and 17(a)(1) of the Exchange Act and Rules 15c3-3 and 17a-5(a) thereunder. Wedbush agreed to retain an independent compliance consultant and pay approximately \$250,000 in disgorgement and \$1,000,000 in penalties.

C. OTHER RELEVANT INDIVIDUAL

3. Timary Delorme (“Delorme”) is a registered representative associated with Wedbush since 1981. In 2013, she settled two customer arbitrations without admitting liability. On March 27, 2018, Delorme settled with the Commission for violations of the antifraud provisions of the federal securities related to her involvement in a penny stock market manipulation scheme. In connection with that matter, the Commission issued an order (1) requiring Delorme to cease and desist from committing or causing violations or future violations of Sections 17(a)(1) and (3) of the Securities Act, and Sections 9(a)(2), 10(b) of the Exchange Act and Rules 10b-5(a) and (c) thereunder; (2) barring her from association with any broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization; (3) barring her from participating in any offering of a penny stock; and (4) requiring her to pay \$50,000 in civil penalties.

D. REGULATORY OVERVIEW

4. Broker-dealers registered with the Commission, like other highly-regulated securities market participants, must comply with numerous regulatory requirements that are designed to ensure, among other things, that they operate with adequate capital, protect investors, and maintain high industry standards.

5. One of these regulatory requirements includes broker-dealers developing and maintaining established policies and procedures reasonably designed to prevent and detect securities law violations of associated persons working for them. Broker-dealers must also have systems to implement their supervisory procedures that would reasonably be expected to prevent and detect violations by persons subject to their supervision.

E. WEDBUSH FAILED REASONABLY TO SUPERVISE DELORME

Delorme Violated the Federal Securities Laws

6. From in or around 2008 to 2014, Delorme was involved in a manipulative trading scheme with Izak Zirk Engelbrecht a/k/a Zirk De Maison (“Engelbrecht”). Engelbrecht was charged by the Commission on September 18, 2014 with, among other things, violating the anti-fraud and registration provisions of the federal securities laws. Engelbrecht also pleaded guilty in the Northern District of Ohio to one count of conspiracy to commit securities fraud, two counts of securities fraud, and four counts of wire fraud. He is currently serving a sentence of 151 months in prison for this conduct. Engelbrecht engaged in manipulative trading (*e.g.*, “pump and dumps”) using the stocks of several penny stock issuers that he and his associates controlled. As part of Engelbrecht’s scheme, Delorme bought certain stocks in her customers’ accounts, or encouraged her customers to buy the stocks, in exchange for undisclosed compensation in the form of shares and cash. In addition, Delorme engaged in manipulative trading designed to create a false appearance of volume and increase or stabilize the price of securities.

Wedbush Observed Several Red Flags Concerning Delorme’s Misconduct

7. Wedbush became aware of certain aspects of Delorme’s securities law violations in 2012 but its supervisory policies and implementation systems failed reasonably to guide staff on how to investigate the activity. Specifically, in late 2012 and early 2013, Delorme’s supervisors became aware of the following red flags by: (1) reviewing an email outlining her role in fraudulent transactions involving penny stocks; (2) receiving copies of two FINRA arbitrations filed by her customers outlining serious allegations of her role in their investments in the same penny stock issuers; (3) learning of a FINRA inquiry into her personal trading in one of those penny stock issuers; and (4) learning of a separate FINRA inquiry into the allegations underlying the customer arbitrations. Wedbush failed to develop and implement reasonable policies and procedures and implementation systems to provide guidance to supervisors and other staff on how to reasonably follow-up on red flags of potential market manipulation by registered representatives, including Delorme.¹

8. Despite learning of these red flags, Wedbush continued to allow Delorme to process orders and communicate with customers, including making investment recommendations. During this time period, Delorme continued to act as an accomplice with Engelbrecht’s scheme. Delorme’s violations of the federal securities laws occurred during the period of Wedbush’s deficient supervision.

¹ On September 14, 2017, Wedbush entered into a tolling agreement (and subsequently entered into tolling agreement extensions) tolling the statute of limitations on its conduct from September 11, 2017 to March 31, 2018. Thus, the red flags described herein all fall within the statute of limitations period.

(a) The “Customer A” Email

9. Delorme’s front-line supervisor, Supervisor 1, began working at Wedbush in April 2009, and became Delorme’s supervisor at that time. When he started, he conducted a review of the trading and customer portfolios of each representative he supervised. Based on his experience in the industry, he had general concerns about the quantity of penny stocks in Delorme’s customers’ accounts. He took measures to restrict her trading activity by limiting her trading in the last hour of the day and restricting all customer trading in certain penny stock securities.

10. Because Delorme had been at the firm for 30 years and her business partner was a partial owner of the firm, Supervisor 1 felt he had to “be gentle” in terms of restricting Delorme’s activities and could not take more “draconian action.”

11. On or about November 26, 2012, Supervisor 1 reviewed an email from Delorme to Customer A (“Customer A Email”), a customer of Delorme’s who was substantively involved in Engelbrecht’s penny stock scheme.² The Customer A Email outlined deals between Customer A on one side and Engelbrecht and his associate on the other “confirmed by [Delorme] as she knows them.” This email outlined Customer A’s efforts to assist in inflating the price of penny stocks, many of which were held in Wedbush accounts by Delorme and her customers.

12. The Customer A Email noted that one of the deals had to be handled through a different broker-dealer because Delorme was restricted from any purchases through Wedbush during the last hour of trading – a reference to the restrictions Supervisor 1 had placed on Delorme’s activity.

13. The Customer A Email was escalated internally up to the president of Wedbush, who reviewed and initialed the email on December 17, 2012. Legal and compliance personnel also were aware of the email.

(b) The FINRA Arbitrations

14. Around the same time as the Customer A Email, Delorme and Wedbush were named as respondents in two FINRA arbitration claims submitted by customers of Delorme. Wedbush received the first arbitration claim submitted by four customers on or about October 17, 2012. It was passed along to a number of people, including the president of Wedbush and members of the firm’s legal and compliance staff. The customers alleged that Delorme solicited their investments in certain penny stock issuers, guaranteed no losses, gifted securities, and set up a deal between her customers and an associate of Engelbrecht’s. The customers further alleged, through text message evidence, that Delorme was involved in manipulating the securities in their accounts in order to guarantee them profits.

² As part of its supervision of registered representatives, Wedbush has an email monitoring system that identifies certain emails for manager review based on keywords.

15. Wedbush received a second FINRA arbitration claim against it on or about November 15, 2012. Although Delorme was not personally named in the second claim as a respondent, the underlying allegations were similar to those in the first claim in that they described similar transactions involving Delorme in similar securities. Both arbitrations were settled in the fall of 2013. Delorme was responsible for paying Wedbush half the settlement amounts in both arbitrations because Wedbush deemed her culpable for her behavior.

(c) The FINRA Regulatory Inquiries into Delorme

16. On or about November 9 and 19, 2012, Wedbush received inquiries from FINRA's Office of Fraud Detection and Market Intelligence into trading in a specific penny stock by three accounts held at Wedbush by Delorme and her husband. Delorme's supervisors were aware of the inquiry, as were members of Wedbush's legal and compliance teams.

17. On or about December 6, 2012, Wedbush received a second FINRA inquiry into Delorme. FINRA made numerous requests about the allegations in the customer arbitrations outlined above. During the course of responding to FINRA, Delorme drafted her own responses and sent them to compliance for review. Compliance personnel at Wedbush did not take any steps to investigate or confirm the veracity of Delorme's responses. During the course of this inquiry, in April 2013, FINRA interviewed Delorme. Supervisor 1 and Wedbush compliance personnel attended this interview. Wedbush did not take any steps to follow-up on Delorme's responses given to FINRA during the interview despite the fact that the certain of the responses were inconsistent and contradicted what the firm had already learned from the Customer A Email and customer arbitration filings. This inquiry was resolved September 19, 2014 when FINRA sent a letter of caution finding Delorme to be deficient in failing to comply with Wedbush's policies regarding Regulation S-P by sending emails with customers' names, addresses, and social security numbers "to unaffiliated third parties containing confidential personal information of 20 firm customers without first obtaining approval from the firm or the customers."

Wedbush's Deficient Investigations into Delorme's Conduct

18. Wedbush conducted two flawed investigations into Delorme's activities: one by compliance and one by legal. Wedbush did not document or otherwise clarify the scope of each investigation, and there was no process as to how the results of the investigations were to be documented or reported. The lack of documentation or other reporting mechanism resulted in no coherent response to the red flags outlined above. It is unclear what, if anything, was reported from legal or compliance to Wedbush's management.

19. Delorme was placed on heightened supervision for one year by Wedbush in March 2014. It appears this discipline was instituted in order to resolve the ongoing FINRA matter, rather than in response to any misconduct by Delorme related to the red flags discussed above. For example, Wedbush has no documentation reflecting (1) who decided on Delorme's discipline, (2) why heightened supervision was the appropriate level of discipline, and (3) the timing of the discipline.

20. According to Supervisor 1, if it had been up to him, Delorme would have been on heightened supervision at an earlier time, at least at the point in time of the Customer A Email, which he call “the smoking gun . . . whatever suspicions or worries I had, this confirmed a lot of the worst of them.”

21. In addition, in April 2014, Delorme was approached by the FBI and was interviewed about her role in Engelbrecht’s penny stock scheme. Delorme promptly informed Supervisor 1 about this conversation. Supervisor 1 then contacted his manager and Wedbush’s legal and compliance teams. Delorme and Supervisor 1’s manager spoke about the FBI interview. No one in compliance interviewed Delorme regarding the FBI interview. It does not appear any internal investigation was done in response to the FBI’s interview or the topics that Delorme discussed, and no old investigations were reopened or revisited.

F. WEDBUSH LACKED REASONABLE POLICIES AND PROCEDURES RELATED TO SUPERVISION OF ITS REGISTERED REPRESENTATIVES

22. Wedbush’s policies and supervisory systems lacked any reasonable coherent structure to provide guidance to supervisors and other staff for investigating possible facilitation of market manipulation by registered representatives, including Delorme. This lack of reasonable policies and procedures resulted in Wedbush failing to supervise Delorme.

23. Wedbush lacked reasonable procedures regarding the investigation and handling of red flags. There was substantial confusion as to whose responsibility it is to conduct investigations related to red flags of potential market manipulation by Delorme. According to employees, internal investigations of registered representatives were generally conducted by that representative’s front-line manager or division manager. Those managers would reach out to division managers or executive vice presidents, and legal and compliance as needed. Compliance and legal generally did not conduct internal investigations in the regular course of business. At the time, Wedbush’s policies were silent on this issue.

G. FAILURE REASONABLY TO SUPERVISE

24. As a result of the conduct described above, Wedbush failed reasonably to supervise Delorme, with a view to preventing and detecting Delorme’s violations of Sections 17(a)(1) and (3) of the Securities Act, Sections 9(a)(2) and 10(b) of the Exchange Act and Rule 10b-5(a) and (c) thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate in the public interest that public administrative proceedings be instituted to determine:

A. Whether the allegations set forth in Section II hereof are true and, in connection therewith, to afford Respondent an opportunity to establish any defenses to such allegations;

B. What, if any, remedial action is appropriate in the public interest against Respondent pursuant to Section 15(b) of the Exchange Act including, but not limited to, disgorgement and civil penalties pursuant to Section 21B of the Exchange Act.

IV.

IT IS ORDERED that a public hearing for purposes of taking evidence on the questions set forth in Section III hereof shall be convened not earlier than 30 days and not later than 60 days from service of this Order at a time and place to be fixed and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice, 17 C.F.R. § 201.110.

IT IS FURTHER ORDERED that Respondent shall file an Answer to the allegations contained in this Order within twenty (20) days after service of this Order, as provided by Rule 220 of the Commission's Rules of Practice, 17 C.F.R. § 201.220.

If Respondent fails to file the directed answer, or fails to appear at a hearing after being duly notified, the Respondent may be deemed in default and the proceedings may be determined against him upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f) and 310 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f) and 201.310.

This Order shall be served forthwith upon Respondent as provided for in the Commission's Rules of Practice.

IT IS FURTHER ORDERED that, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice, 17 C.F.R. § 201.360(a)(2), the Administrative Law Judge shall issue an initial decision no later than 120 days from the occurrence of one of the following events: (A) The completion of post-hearing briefing in a proceeding where the hearing has been completed; (B) Where the hearing officer has determined that no hearing is necessary, upon completion of briefing on a motion pursuant to Rule 250 of the Commission's Rules of Practice, 17 C.F.R. § 201.250; or (C) The determination by the hearing officer that a party is deemed to be in default under Rule 155 of the Commission's Rules of Practice, 17 C.F.R. § 201.155 and no hearing is necessary.

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not “rule making” within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Brent J. Fields
Secretary