

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C.

SECURITIES EXCHANGE ACT OF 1934  
Rel. No. 59729 / April 8, 2009

INVESTMENT ADVISERS ACT OF 1940  
Rel. No. 2684 / April 8, 2009

Admin. Proc. File No. 3-13009

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In the Matter of

SCOTT B. GANN  
c/o Randall G. Walters  
Walters, Balido & Crain, LLP  
900 Jackson Street  
Suite 600  
Dallas, Texas 75202

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OPINION OF THE COMMISSION

BROKER-DEALER PROCEEDING  
INVESTMENT ADVISER PROCEEDING

Grounds for Remedial Action

Injunction

Former associated person of registered broker-dealer and investment adviser was permanently enjoined from violating antifraud provisions of the federal securities laws. Held, it is in the public interest to bar Respondent from association with any broker, dealer, or investment adviser.

APPEARANCES:

Randall G. Walters, of Walters, Balido & Crain, LLP, for Scott B. Gann.

Jeffrey A. Cohen and Toby M. Galloway, for the Division of Enforcement.

Appeal filed: September 29, 2008  
Last brief received: December 16, 2008

## I.

Scott B. Gann, formerly a senior vice-president and associated person with Southwest Securities, Inc. ("SWS"), a broker-dealer and investment adviser registered with the Commission, appeals from the decision of an administrative law judge. 1/ The law judge barred Gann from association with any broker, dealer, or investment adviser based on Gann's injunction from violation of the antifraud provisions of the federal securities laws. We base our findings on an independent review of the record, except with respect to those findings not challenged on appeal.

## II.

On January 10, 2005, the Commission filed an injunctive complaint ("Injunctive Complaint") in the Northern District of Texas against Gann and George B. Fasciano, another SWS representative, alleging violations of Exchange Act Section 10(b) 2/ and Rule 10b-5 thereunder. 3/ The Injunctive Complaint alleged that, between February and September 2003, Gann and Fasciano used fraudulent devices to facilitate thousands of deceptive market-timing mutual-fund trades on behalf of Haidar Capital Management and Capital Advisor ("HCM"), a hedge-fund client of the firm. 4/

On March 31, 2008, after a three-day bench-trial, the district court entered a Memorandum Opinion and Order finding that Gann violated Exchange Act Section 10(b) and Exchange Act Rule 10b-5. 5/ On April 4, 2008, the district court entered a final judgment

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1/ As of June 5, 2008, Gann was associated with Sanders, Morris, Harris, a Dallas-based broker-dealer, as a registered representative.

2/ 15 U.S.C. § 78j(b).

3/ 17 C.F.R. § 240.10b-5.

4/ "Market timing is a 'trading strategy in which traders rapidly buy and sell mutual fund shares to exploit brief discrepancies between the official stock prices used to determine[] the value of the mutual fund shares, and the prices at which the stocks are actually trading'" Justin F. Ficken, Securities Exchange Act Rel. No. 58802 (Oct. 17, 2008), 94 SEC Docket 10887, 10888 n.1 (quoting SEC v. Druffner, 517 F. Supp.2d 502, 506 (D. Mass. 2007)). Market timing, while not illegal, is strongly disfavored by mutual fund companies because it dilutes the value of the shares held by long-term shareholders, disrupts portfolio management, and increases trading costs.

5/ SEC v. Gann, No. 3:05-CV-0063-L/NDTX (N.D. Tex. Mar. 31, 2008). Fasciano settled with the Commission before trial. The district court entered a final judgment as to Fasciano on April 23, 2007, enjoining him from violations of Exchange Act Section

(continued...)

against Gann permanently enjoining him from further violations of the securities laws, ordering him to pay \$56,640.67 in disgorgement, \$13,568.68 in prejudgment interest, and \$50,000 in civil penalties. <sup>6/</sup> We summarize here the district court's findings, which establish the factual framework within which we consider Gann's appeal.

In or around November 2002, Fasciano introduced Gann to HCM after HCM had approached Fasciano about facilitating its market-timing trades. Gann investigated HCM as a potential customer over several months. Gann knew that mutual fund companies employed compliance monitors, commonly referred to as the "market timing police," tasked with preventing market-timing trades. In his investigation, Gann learned that HCM employed various tactics at other broker-dealer firms such as using multiple accounts and accounts with multiple identification numbers (whether for clients, representatives, or offices, or all three) to circumvent the mutual funds' rules prohibiting market timing. As one witness testified, these tactics enabled brokers to "circumvent block notices and get transactions executed in mutual funds that imposed trading restrictions on market timers." Gann's contact at HCM testified that the use of multiple representative numbers was "designed to basically hide the identity of the investor to be able to continue to trade."

All HCM trades were placed through one SWS trader, Fred Turner, at a central trading desk. Turner "was expected to understand the trading rules of the fund, to enter all orders, and to create and maintain relationships with the funds." Fasciano testified that "it was up to Turner to contact the mutual fund to determine if a given trade was compliant."

Between January 23 and May 6, 2003, Gann and Fasciano opened twenty-one SWS accounts for nine different HCM affiliates. Gann and Fasciano used three registered representative numbers for their HCM trading (one number for each of their names and one joint number for their partnership). Gann's number was listed on nine accounts, Fasciano's on nine, and the partnership's on three.

Gann and Fasciano placed the first market-timing trade for HCM on February 10, 2003. The district court found that, by September 2003, "Gann and Fasciano had executed approximately 2,500 trades on behalf of HCM in fifty-six mutual fund families, and in 165

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<sup>5/</sup> (...continued)  
10(b) and Exchange Act Rule 10b-5, and ordering Fasciano to disgorge \$56,000, plus prejudgment interest, and to pay a \$30,000 civil money penalty. Fasciano subsequently consented to a bar from association with a broker, dealer or investment advisor with a right to reapply in two years. George B. Fasciano, Exchange Act Rel. No. 55763 (May 15, 2007), 90 SEC Docket 1962.

<sup>6/</sup> Gann appealed the district court's decision to the United States Court of Appeals for the Fifth Circuit. SEC v. Gann, No. 08-10404 (5th Cir.). That appeal is pending.

mutual funds, with an aggregate value of \$650 million." Gann was paid \$56,640.67 in pretax commissions for his work on the HCM account.

The district court found that, "[o]f the 2,500 trades executed on behalf of HCM, there were sixty-nine block notices sent from thirty-four mutual fund families." "Block notices" are "communications from a mutual fund company prohibiting market-timing trading" that "typically include a statement of a mutual fund's objection to market timing and a notification of restrictions on market timing trading, including the prohibition of future trades in specific blocked accounts, of trades by a particular broker, or of future trades bearing a particular branch office identification number." Gann and Fasciano received their first block notice on February 25, 2003, fifteen days after they began trading. In the injunctive proceeding, Gann stipulated that he was aware of the block notices. SWS did not permit trading to continue after receipt of a block notice: a block notice was the "final word." The district court found that "[t]here is no evidence in the record that a single mutual fund family gave Gann permission to continue trading in their funds after sending SWS a block notice."

The district court found that Gann made material misrepresentations. The court detailed HCM's trading in six mutual funds and concluded that, after receiving block notices, Gann and Fasciano executed a total of 117 trades in those six mutual funds. "Gann tried to make it appear as if different brokers and clients were making trades" through the "use of multiple accounts and representative numbers, as well as the change in the branch office identifier." The court found these misrepresentations were material to the mutual funds, which had tried to prevent Gann's trading. Gann employed these deceptive devices so that he could continue trading for HCM despite the mutual funds' attempts to prohibit his trades.

The district court also rejected Gann's argument that he had no intent to deceive or defraud the mutual funds. The district court stated that the "overwhelming testimony and evidence, however, undercut Gann's credibility." The district court concluded that Gann had acted with scienter, finding that his "actions were intentionally geared toward evading detection by the mutual fund managers" and that his "continuing behavior in trying to make trades in funds after receiving block notices indicates his intent to deceive the mutual funds." The district court also observed that Gann knew SWS's procedures for mutual funds were not being followed. Further, the court stated that, while Gann and Fasciano "may have contacted the mutual funds before any trades were made [in an attempt to comply with the funds' rules], after trading began, they adopted an entirely new branch number to continue trading after their trades were blocked." <sup>7/</sup> The district court found that injunctive relief was warranted given "the repeated nature of Gann's misrepresentations, the number of mutual funds to which he made such misrepresentations, Gann's continued refusal to recognize that his actions involved deception, and that he continues to act as a stockbroker."

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<sup>7/</sup> Emphasis in original.

On April 17, 2008, we initiated this administrative proceeding. Gann admitted in his answer to the Order Instituting Proceedings that he was associated with SWS and that an injunction had been entered against him in connection with the purchase or sale of securities. The Division of Enforcement moved for summary disposition pursuant to Commission Rule of Practice 250. 8/ Gann attached an affidavit to his brief before the law judge in which he stated that he "will always hold the belief [he] did not have the intent to defraud any mutual fund company" and that "[he] cannot admit that [his] personal actions were wrong when [he] sincerely [does] not believe that [he] had the intent to deceive any person, investor, or fund company."

On September 9, 2008, the law judge granted the Division's motion. The law judge found that barring Gann from association with any broker, dealer, or investment adviser was "necessary and appropriate to protect the public interest." The law judge found that Gann's actions were "egregious and recurrent," that he acted with "a high degree of scienter," and that he has "not admitted the wrongful nature of his conduct." While the law judge found that Gann had provided assurances against future violations, he determined that Gann's continuance in the securities industry would provide him with "additional opportunities to violate securities laws." This appeal followed.

### III.

Exchange Act Sections 15(b)(4) and (6) and Advisers Act Sections 203(e) and (f) allow for imposition of sanctions on a person associated with a broker or dealer or investment adviser, consistent with the public interest, if the person has been permanently enjoined from engaging in any conduct or practice in connection with the purchase or sale of securities. 9/ We find that Gann satisfies the requirements for imposition of sanctions. As Gann admitted before the law judge, at the time of the conduct at issue in this proceeding, Gann was associated with SWS, a broker-dealer and investment adviser registered with the Commission, and he has been permanently enjoined in connection with the purchase or sale of securities. 10/

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8/ 17 C.F.R. § 201.250.

9/ 15 U.S.C. §§ 78o(b)(4) and (6); 15 U.S.C. §§ 80b-3(e) and (f).

10/ Gann has moved pursuant to Commission Rule of Practice 401, 17 C.F.R. § 201.401, for a stay of these proceedings pending the decision of the Fifth Circuit on his appeal, SEC v. Gann, No. 08-10404 (5th Cir.). We deny Gann's motion. It is well established that a pending judicial appeal does not affect the injunction's status as a basis for an administrative proceeding. James E. Franklin, Exchange Act Rel. No. 56649 (Oct. 12, 2007), 91 SEC Docket 2708, 2714 n.15 (collecting cases). To the extent Gann prevails in his appeal, he would be entitled to file a motion to vacate the opinion and order in this matter. Id. (citing Jimmy Dale Swink, 52 S.E.C. 379 (1995) (granting motion to vacate bar upon appellate reversal of criminal conviction that was basis for bar in administrative (continued...))

To determine the appropriate remedial sanction we evaluate the following factors: the egregiousness of respondent's actions; the isolated or recurrent nature of the infraction; the degree of scienter involved; the sincerity of respondent's assurances against future violations; the respondent's recognition of the wrongful nature of his conduct; and the likelihood that respondent's occupation will present opportunities for future violations. 11/ No single factor is dispositive.

We have consistently found that antifraud violations, such as those committed by Gann, are "especially serious and subject to the severest sanctions." 12/ We are responsible for protecting the public interest, and "[f]idelity to the public interest" requires severe sanctions for fraudulent conduct because the "securities business is one in which opportunities for dishonesty recur constantly." 13/ In fact, "ordinarily, and in the absence of evidence to the contrary, it will be in the public interest to . . . bar from participation in the securities industry . . . a respondent who is enjoined from violating the antifraud provisions." 14/ We have found that "an antifraud injunction can, in the first instance, indicate the appropriateness in the public interest of . . . [a] bar from participation in the securities industry." 15/

The district court found that Gann engaged in fraudulent market timing from February until September 2003. 16/ Knowing that the mutual funds intended to halt his market-timing trades by issuing block notices, Gann used deceptive devices to enable him to continue trading. The district court found that "Gann responded to block notices by changing the representative number or account number and by continuing to execute trades to circumvent the mutual funds'

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10/ (...continued proceeding)).

11/ SEC v. Steadman, 603 F.2d 1126, 1140 (5th Cir. 1979).

12/ Jose P. Zollino, Exchange Act Rel. No. 55107 (Jan. 16, 2007), 89 SEC Docket 2598, 2608; Marshall E. Melton, 56 S.E.C. 695, 713 (2003).

13/ Richard C. Spangler, Inc., 46 S.E.C. 238, 252 (1976).

14/ Melton, 56 S.E.C. at 713.

15/ Id. at 710.

16/ We note that, around this time, the Commission and other regulators instituted a series of investigations and injunctive and administrative actions with respect to market timing. See, e.g. Martin J. Druffner, Litigation Rel. No. 18444 (Nov. 4, 2003), 81 SEC Docket 2196 (filing of injunctive complaint alleging fraudulent market timing); SEC v. Sec. Trust Co., Litigation Rel. No. 18479 (Nov. 25, 2003), 81 SEC Docket 2835 (same); SEC v. Mutuals.com, Inc., Litigation Rel. No. 18489 (Dec. 4, 2003), 81 SEC Docket 2932 (same).

attempts to prohibit his trades." The district court also described "the repeated nature of Gann's misrepresentations, [and] the number of mutual funds to which he made such misrepresentations."

Gann argues that, despite the district court's findings, his conduct was not egregious or recurrent. He contends that his actions involved trading for a single client, for a brief period over five years ago, and has not been followed by other violations of the securities laws. Contrary to Gann's assertion, his violative conduct occurred over an eight-month period from February to September, during which Gann facilitated thousands of market-timing trades in fifty-six mutual fund families, and in 165 mutual funds, with an aggregate value of \$650 million. Gann received sixty-nine block notices from thirty-four mutual fund families and used deceptive devices to circumvent these measures taken by the funds to prohibit his trading. With respect to the six mutual funds that the district court discussed in detail, Gann and Fasciano executed a total of 117 trades after receiving block notices. Accordingly, we find that Gann's misconduct was egregious and recurrent.

Gann asserts that he engaged in the 2003 conduct "only after conducting extensive due diligence in an attempt to comply with the mutual funds' rules." The district court stated that there was "some evidence that Gann and Fasciano contacted mutual fund companies . . . in an attempt to comply with the companies' rules." However, the district court also found that Gann "continued to execute trades in mutual funds after those funds had issued block notices . . . ." The court stated that "[s]everal witnesses testified that this in and of itself demonstrates that [Gann] did not intend to comply with the mutual funds' rules . . . ." Moreover, the district court found that Gann's initial attempts to comply were abandoned soon after trading began.

Gann argues that he had no previous experience with mutual fund trading or market timing and that he "relied on others" to ensure that his trading complied with the securities laws. Gann asserts that he "was told by HCM that HCM had lawyers for compliance and its own compliance department and that HCM's legal counsel had done due diligence and approved the market timing business." He also contends that it was the job of Fred Turner, who operated SWS's mutual fund trading desk, to understand the funds' "trading rules" and to "determine if a given trade was compliant." According to Gann, Turner sometimes stated that Gann "could continue trading in a fund even after receiving a block notice." Gann's arguments are without merit. Gann as a participant in the securities industry was responsible for compliance with the applicable regulatory requirements and cannot excuse his conduct by claiming a lack of experience or by reliance on others to ensure his compliance. <sup>17/</sup> To the extent that Gann asserts

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<sup>17/</sup> Vincent M. Uberti, Exchange Act Rel. No. 58917 (Nov. 7, 2008), 94 SEC Docket 11406, 11412 n.11 (inexperience no excuse for violation of NASD Rules); Thomas C. Kocherhans, 52 S.E.C. 528, 531 (1995) (holding that participants in the securities industry are responsible for regulatory compliance and cannot excuse their conduct by lack of knowledge or understanding of the rules or by reliance on a supervisor); Jeffrey  
(continued...)

that he acted on advice of counsel, he has not made the factual showing required by that defense. 18/ Gann has introduced no evidence that he disclosed the mechanics of his market-timing to an attorney and received advice that those trades complied with the securities laws. Moreover, Gann may not rely on counsel for HCM because its counsel could not be relied on to give disinterested advice to Gann. 19/

In any event, Gann's infractions involved a high degree of scienter, and, in the face of this scienter, Gann's assertion that he sought to comply with the federal securities laws cannot survive. The district court found that "Gann's continuing behavior in trying to make trades in [mutual] funds after receiving block notices indicates his intent to deceive the mutual funds." The district court found that Gann used devices to disguise his identity and to continue to trade in response to block notices, and his "actions 'were intentionally geared toward evading detection by the mutual fund managers.'" 20/ Although Gann acknowledges the district court's finding that he committed fraud, he denies that he acted with a "high degree" of scienter. That Gann used deceptive devices to continue trading after receiving block notices undermines his claim that he did not act with a high degree of scienter. He asserts that he never disguised his name, but that is not evidence of a lack of scienter because the funds with which he traded on behalf of HCM identified traders and customers by identification number, not by name.

Gann has provided some assurances that he will not commit further infractions. Gann has not traded mutual funds since 2005, represents that he does not intend to trade mutual funds in the future, and is willing to surrender his Series 65 license, which permits such trading. However, Gann currently works as a registered representative at a Dallas-based brokerage where he maintains an array of licenses that permit him to work in the industry. Gann's occupation will

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17/ (...continued)  
D. Field, 51 S.E.C. 1074, 1076 (1994) (finding that "[p]articipants in the industry must take responsibility for their compliance [with applicable regulatory requirements] and cannot be excused for lack of knowledge, understanding, or appreciation of these requirements") (quoting Kirk A. Knapp, 51 S.E.C. 115, 134 (1992)).

18/ John A. Carley, Securities Act Rel. No. 8888 (Jan. 31, 2008), 92 SEC Docket 1693, 1712 (holding that reliance on advice of counsel requires that respondent "made complete disclosure to counsel, sought advice as to the legality of his conduct, received advice that his conduct was legal and relied on that advice in good faith") (quoting Markowski v. SEC, 34 F.3d 99, 104-05 (2d Cir. 1994)), appeal filed, No. 08-1141 (D.C. Cir. Mar. 31, 2008).

19/ See Carley, 92 SEC Docket at 1734 n.137 (stating "[o]ne cannot rely on the advice of another's counsel because that counsel cannot be relied upon to provide disinterested advice").

20/ See SEC v. Druffner, 517 F. Supp. 2d at 509.



provide future opportunities for violation. 21/ Moreover, Gann's claims that he will "[a]lways hold the belief that [he] did not have the intent to defraud any mutual fund company" and that "[he] cannot admit [his] personal actions were wrong" reveal a fundamental misunderstanding of the duties of a securities industry professional that presents a significant likelihood that he will commit similar violations in the future. Gann's lack of disciplinary history since the conduct at issue is also not a mitigating factor. 22/

Gann also asserts as mitigating his reliance on his employment as a registered representative to pay the disgorgement, interest, and civil penalties imposed by the district court in the injunctive action and that he is the sole support of his wife and two daughters, one of whom is disabled. The need to protect the public given Gann's egregious and repeated misconduct outweighs any increase in the likelihood of Gann's timely payment and his need to fulfill his financial obligations.

Based on a consideration of the relevant factors, and all of the circumstances in this case, we find that the barring Gann from association with any broker, dealer, or investment adviser serves the public interest and is remedial because, as discussed, it will protect the investing public from the significant likelihood that Gann will commit future violations of the federal securities laws.

An appropriate order will issue. 23/

By the Commission (Commissioners CASEY, WALTERS, and PAREDES); Chairman SCHAPIRO and Commissioner AGUILAR not participating.

Elizabeth M. Murphy  
Secretary

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21/ Spangler, 46 S.E.C. at 252 (stating that, in the industry, opportunities for wrongdoing "recur constantly").

22/ John Audifferen, Exchange Act Rel. No. 58230 (July 25, 2008), 93 SEC Docket 8129, 8148 ("[T]he Commission has consistently rejected the argument that a lack of disciplinary history should be considered as a mitigating factor in connection with the imposition of sanctions in FINRA proceedings."); Michael A. Rooms, Exchange Act Rel. No. 51467 (Apr. 1, 2005), 85 SEC Docket 444, 450 (same), aff'd 444 F.3d 1208 (10th Cir. 2006).

23/ We have considered all of the parties' contentions. We have rejected or sustained them to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA  
before the  
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934  
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ORDER IMPOSING REMEDIAL SANCTIONS

On the basis of the Commission's Opinion issued this day, it is

ORDERED that Scott B. Gann be, and he hereby is, barred from association with any broker, dealer, or investment adviser.

By the Commission.

Elizabeth M. Murphy  
Secretary