



**STATE OF NEW MEXICO
REGULATION AND LICENSING DEPARTMENT
SECURITIES DIVISION**

In the Matter of:)
)
OPPENHEIMER & CO., INC. (CRD # 249),) Case No. 14-03-0028
ROYCE O. SIMPSON (CRD # 1403356))
)
Respondents.)

NOTICE OF CONTEMPLATED ACTION

The Director of the New Mexico Securities Division (“Director”) after investigation has good reason to believe, and therefore alleges the following:

I. PROPOSED FACTS

A. Persons

1. Oppenheimer & Co., Inc. (“Oppenheimer”) (CRD # 249) is a registered securities broker-dealer, with its principal place of business located at 85 Broad Street, 25th Floor, New York, NY 10004.
2. Royce O. Simpson (“Simpson”) (CRD # 1403356) was a registered broker-dealer representative associated with Oppenheimer from November 10, 2011, to February 12, 2014. While supervised by Oppenheimer, Simpson’s business address was 711 Louisiana Street, 15th Floor, Houston, TX 77002.
3. Oppenheimer terminated Simpson on February 12, 2014, during Oppenheimer’s internal review of Simpson’s servicing of the account for the Bernalillo County Treasurer’s Office (“BCTO” or “the county”).
4. BCTO is the property tax collector for the County of Bernalillo, City of Albuquerque, Albuquerque Public Schools, the State of New Mexico, and other taxing agencies within Bernalillo County, New Mexico. BCTO also collects money for a variety of county services, licenses, and revenues from bond issues and special assessments. It supervises how public money is invested based on the advice and consent of the County Commission. County public services – such as fire, law enforcement, transportation, roads – are paid for with monies handled by BCTO.
5. In 2012, Patrick Padilla (“Padilla”) was the county Treasurer. Padilla became the county’s Investment Officer in January 2013. Padilla has never been licensed in the securities industry.

6. In 2013, Manny Ortiz (“Ortiz”) became the county Treasurer. Ortiz was the Investment Officer to the county during 2012. Ortiz has never been licensed in the securities industry.

B. BCTO’s Investment Policy

7. During 2012-2013, BCTO invested public funds pursuant to an investment policy dated February 14, 2012. Under BCTO’s investment policy, the Treasurer had authority to make investment decisions, subject to certain investment priorities, New Mexico and federal law, and oversight by the Board of Finance.
8. BCTO’s investment policy created a six person Investment Committee. The members are appointed by the Treasurer and serve at the Treasurer’s discretion. The Investment Committee advises the Treasurer in administering BCTO’s investment policy. The Treasurer is both a member and the Chairman of the Investment Committee. The Investment Officer is a member and the Vice Chairman of the Investment Committee. There were no requirements that members of the Investment Committee have investment experience.
9. BCTO’s investment policy’s priorities were “safety, liquidity and yield,” subject to the Prudent Person Rule referenced in § 6-8-10 NMSA 1978. The Prudent Person Rule emphasizes capital preservation while discouraging trading for short-term capital gain.
10. BCTO’s investment policy also contained a competitive bid process for awarding business to broker-dealers that sold securities to the county. Under the policy, broker-dealers were awarded business based on price and service. Broker-dealers had to be approved by the Investment Committee.

C. BCTO’s Investment Portfolio 2012-2013

11. During 2012-2013, BCTO’s investment portfolio contained approximately \$250,000,000 in assets.
 12. Based on an October 8, 2013 review of the portfolio by Slocum, a U.S. Securities and Exchange Commission registered investment adviser, 77% of BCTO’s portfolio was allocated to bonds issued by two U.S. agencies: Federal Home Loan Bank and Fannie Mae. *See Slocum Report.* While the bonds had ratings of AA+, the average maturity was over 11 years. Generally, bonds with a long maturity subject their holders to the risk of changes in interest rates over a longer period of time as compared to short term bonds. Slocum found that BCTO’s long maturity exposed the county to interest rate risk. Bonds with a low coupon rate lose market value if interests go up (sort of like how a dollar bill may lose its purchase power as inflation goes up). Said another way, a long maturity runs the risk that interest rates – which were historically low in 2008-2012 – will rise over a long period.
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13. The Slocum Report indicated that a minor rise of 1% in interest rates will equate to an 8.2% loss in market value of the county’s portfolio. Slocum noted: “stated another way,

interest rates would need to rise only approximately 0.28% to eliminate one year's worth of income." In a practical sense, if rates rose and BCTO had to sell the bonds to meet its cash needs (or to diversify its portfolio to reduce interest rate risk), BCTO would likely get a lower price.

14. The Slocum Report found that BCTO's investment strategy was positioned for yield, which exposed BCTO to "significant mark-to-market factors." This means that the county's portfolio was in danger of losing millions of dollars in value simply because of interest rate increases.
15. To reduce BCTO's exposure to interest rate risk (and thereby reduce its risk of more significant losses in the future), between February and June 2014, BCTO sold 100% of its portfolio. The realized loss to Bernalillo County tax payers is approximately \$16,521,177.

D. BCTO Relationship with Oppenheimer

16. On December 7, 2011, Oppenheimer's Compliance Department approved Simpson to solicit business from BCTO, a government client. *OPCO 0016*.
17. Simpson also serviced BCTO while employed at UBS Financial Services, Inc. ("UBS"). (In November 2011, Simpson resigned from UBS after being accused of overcharging Harris County, Texas for certain bond purchases).
18. Oppenheimer deemed BCTO as an "institutional investor" based solely on its total assets. Such status is not based on the sophistication of the Treasurer or any of BCTO's employees or the Investment Committee.
19. The status of being an institutional investor is important because there is an assumption of sophistication. But, broker-dealers run the risk of falsely assuming an institutional investor can independently evaluate investment risk. In fact, such sophistication is not the case for many local and county agencies that are headed by persons without substantial or even minimal investment experience.
20. No BCTO employee had the investment experience to price the bonds purchased and sold and by the county.
21. In December 2011, Oppenheimer's DVP Account Opening sheet noted BCTO's investment objective was "safety of principal." *OPCO 0001*. (A DVP account is a "direct verses payment" account, which means Oppenheimer delivered the asset to another depository).
22. On or about December 2011, Oppenheimer obtained a copy of BCTO's investment policy. *OPCO 0004-0009*.

E. Recommendations Were Not Suitable

23. To protect investors, registered broker dealers and representatives must:

“have a reasonable basis to believe that a recommended transaction or investment strategy involving a security or securities is suitable for the customer, based on the information obtained through the reasonable diligence of the [firm] or associated person to ascertain the customer’s investment profile.” *See, FINRA Rule 2111(a); NMAC Rule 12.11.4.15.*

The “suitability” rule also covers recommended investment strategies involving securities, including recommendations to “hold” securities. *Id., FINRA RN 12-55.*

24. Institutional investors are protected by the suitability rule. *See FINRA Rule 2111.* A broker dealer and representative fulfills the suitability obligation for an institutional investor if (1) the member has a reasonable basis to believe the institutional customer is capable of evaluating investment risks independently, with regard to particular transactions and investment strategies and (2) the institutional customer affirmatively indicates that it is exercising independent judgment in evaluating the member’s recommendations. *FINRA Rule 2111 (b).*

25. Oppenheimer’s policy on suitability considers the risk its agents undertake by assuming an institutional investor has the sophistication to independently evaluate investment decisions and strategy. Oppenheimer’s suitability policy provides:

“although institutional investors tend to be sophisticated and experienced, sales personnel nevertheless have certain suitability obligations when making recommendations to such customers. FINRA rules require that the sales person determine the customer’s ability to evaluate investment risk independently ... these factors cannot be assumed.” *Oppenheimer Taxable Fixed Income Sales & Trading Policies and Procedures Manual, 32-33.* (emphasis added).

26. Oppenheimer and Simpson lacked a reasonable basis to believe Padilla, Ortiz or the Investment Committee could independently evaluate the risks associated with particular transactions and the county’s overall investment strategy.

27. Between May 2012 and June 2013, Oppenheimer and Simpson recommended that BCTO purchase 15 Government Sponsored Enterprise bonds (“GSEs”). *See Figure 1 (below).* These 15 GSEs were complicated securities to value because they had long-term maturity dates (10 and 20 years) and / or other embedded optionality features, such as “call” options and “step” features.

28. As discussed above, BCTO’s portfolio contained an overconcentration of long-term GSEs. This overconcentration exposed the county to cash management risk and the risk of capital should interest rates rise (since the county must value its portfolio based on mark-to-market accounting).

29. On April 3, 2012, Oppenheimer and Simpson became aware of the county's portfolio when Padilla directed a BCTO employee to email a "snap shot" of the county's portfolio to Simpson:

"Patrick wanted me to send you a snap shot of our portfolio. He wanted your input in whether he should make some changes or hold. I believe this is the information that [name redacted] sends. Let me know if you need anything else." (emphasis added).

Simpson replied: "Got it." *OPCO 0253-0254.*

30. Although BCTO had 11 approved broker-dealers, the sensitive information contained in the April 3, 2012 email was not provided to all approved broker-dealers. Thus, this information could have provided an unfair advantage to Oppenheimer to obtain business from the county.

31. Subsequent to the April 3, 2012, email, Oppenheimer and Simpson recommended the county to purchase 15 long-term GSEs. *See Figure 1 (attached, below).*

32. Between January 5, 2012, and September 27, 2013, Oppenheimer received \$156,563.13 in commissions for BCTO account transactions. The vast majority of transactions occurred after the April 3, 2012, email.

33. The commissions are based on the sale price of the bonds.

34. Oppenheimer and Simpson continued to have knowledge of the county's investment and / or strategy. In another email (undated) an employee of BCTO emailed Simpson and Oppenheimer:

"Patrick asked me to send you a list of agency investment that the county currently holds that have maturities greater than 14 years." *OPCO 0277-0279.*

35. On March 21, 2013, Simpson emailed Padilla an Oppenheimer publication that discussed liquidating 5+ year securities. Simpson wrote:

"Patrick ... Please take the time to read this short OPCO research piece. It illustrates what we've been discussing and makes recommendation for a rising rate environment. I will call further to discuss." *OPCO 0239-0241.*

36. After March 21, 2013, Simpson and Oppenheimer solicited the county to purchase 4 GSEs, each of which had a 10 year maturity.

37. From January 2012 to September 2013, all confirmation sheets Oppenheimer sent to BCTO described its trades as "solicited." (A solicited trade transaction is one where the registered representative contacts the client and initiates the buy or sell transaction).

38. In correspondence with this Division, Oppenheimer stated:

“During Oppenheimer internal review in this matter, Mr. Simpson advised that the purchases in question were not solicited by him, but rather were, for the most part, unsolicited trades selected by BCTO. Through his own oversight he alleged that he failed to properly indicate in Oppenheimer’s records that those purchases were unsolicited.” *Oppenheimer Letter, May 22, 2014.*

If Oppenheimer and Simpson had marked trade transactions “unsolicited,” BCTO may have known that the transactions – and, by implication, the investment strategy – was not suitable.

39. To reduce risk to the county, between February 2014 and June 2014, BCTO sold all investments that were recommended by Oppenheimer and Simpson for a realized loss of \$4,172,686.76. *See Figure 2 (attached, below).*

F. Broker Misconduct

40. With respect to the long-term GSEs referenced in Figure 1, both Oppenheimer and Simpson failed to disclose to BCTO that its recommendations were not suitable for the county’s need to protect capital from interest rate increases.
41. During 2012-2013, Oppenheimer had a set of written supervisory procedures and a system for applying such procedures to detect violations of the rules and laws relevant to suitability and other state and federal securities regulations. However, Oppenheimer’s supervisory system failed to reasonably detect and prevent the alleged violations discussed in Section II.
42. During 2012-2013, Oppenheimer and Simpson did not have a reasonable basis to believe BCTO could independently evaluate investment risk with regard to all transactions and / or investment strategies, nor did BCTO affirmatively indicate to Oppenheimer or Simpson it had such an ability. Oppenheimer and Simpson were well aware of BCTO’s portfolio and written investment policy.

II. PROPOSED CONCLUSIONS OF LAW

1. Section I is incorporated.
2. The Director has jurisdiction over this matter pursuant to §58-13C-601 and § 58-13C-610 NMSA 1978.
3. Oppenheimer and Simpson repeatedly violated NMAC Rule 12.11.4.15(C), Suitability, by recommending to BCTO the purchase of securities without reasonable grounds to believe the recommendations were suitable for BCTO. Given the ongoing professional relationship between Oppenheimer and Simpson with BCTO, and knowledge of BCTO’s portfolio and investment goals, Oppenheimer and Simpson breached their duty to recommend investments and transactions that were suitable. Oppenheimer and Simpson failed to perform the due diligence necessary to make recommendations or provide

options which would be suitable for BCTO, based on all the information available to them as broker-dealers.

4. Oppenheimer violated NMAC Rule 12.11.4.10, Supervision, by failing to adequately supervise Simpson's servicing of the account for BCTO, including the accurate reporting of trade confirmations.
5. Oppenheimer violated NMAC Rule 12.11.3.9(E), Broker Dealer Records, by failing to mark whether a transaction for the BCTO account was unsolicited.

III. PROPOSED ORDER

After administrative hearing or waiver of such hearing by Respondent, the Director proposes to issue a Final Order that:

1. Pursuant to §58-13C-604(A)(2) NMSA 1978, Simpson will be permanently barred from transacting business in New Mexico as a broker dealer representative.
2. Pursuant to §58-13C-604(A)(2) NMSA 1978 and NMAC Rule 12.11.4.10, Oppenheimer's license to transact business in New Mexico as a broker dealer will be suspended pending a sufficient showing that its supervisory system may be reasonably expected to prevent and detect violations of the suitability obligation that the company owes institutional and municipal customers.
3. Pursuant to § 58-13C-604(C) NMSA 1978, the Director will assess a \$10,000 fine against Oppenheimer and Simpson for each violation of the New Mexico Uniform Securities Act and its Rules, taking into consideration the number of Bernalillo County residents adversely affected by Respondents' conduct and the resources of the Respondents committing such violations. The Director will consider the 15 transactions in *Figure 1* and the violations per transaction in determining an appropriate fine.
4. Pursuant to § 58-13C-604(E) NMSA 1978, Oppenheimer and Royce Simpson will each pay \$10,000 towards the costs of this investigation.

NOTICE OF ADMINSTRATIVE HEARING RIGHTS

Each Respondent is hereby notified of its statutory right to request an administrative hearing on the Notice of Contemplated Action in the above referenced matter. Administrative hearings are governed by § 58-13C-604(b)(4)-(11) NMSA 1978. Respondents have fifteen (15) days from receipt of this notice to file a written request for a hearing. The request may be sent by U.S. Mail RRR or via email to the Director at stephanie.varoz@state.nm.us. The Director will set the matter for hearing no more than sixty (60) days nor less than fifteen (15) days from receipt of the hearing request. The Director will promptly notify the Respondent of the time and place for hearing. The Director or an appointee will conduct the hearing. The Director or his appointee will pass upon the admissibility of evidence and may exclude evidence that is incompetent, irrelevant, immaterial or unduly repetitious.

As discussed more fully in 58-13C-604(b) NMSA 1978, any Respondent requesting a hearing is entitled to: appear on its own behalf or may be represented by an attorney; present all relevant evidence; to examine all opposing witnesses who appear on any matter relevant to the issues; request and obtain discovery, including the names and addresses of witnesses.

ENTERED AT Santa Fe, New Mexico this 20th day of November 2014.



Alan R. Wilson, Director
New Mexico Securities Division

Figure 1

BROKER NAME	INVESTMENT TYPE	ACCOUNT NUMBER	BOUGHT @	DATE BOUGHT	MATURITY DATE	INT RATE (%) (COUPON)	PAR AMOUNT (LESS DISCOUNT)	PLUS AMORTIZATION	MARKET VALUE	MARKET GAIN (LOSS)
OPPENHEIMER & CO. INC.	FANNIE MAE	3136GOKK9	99.2950	5/24/2012	5/24/2032	3.000%	5,987,700.00	5,988,376.88	5,711,760.00	(276,616.88)
OPPENHEIMER & CO. INC.	FED HOME LOAN BANK	313379PB9	99.9200	6/14/2012	6/14/2027	3.240%	3,060,516.12	3,060,794.32	2,899,706.44	(161,087.88)
OPPENHEIMER & CO. INC.	FANNIE MAE	3136GOKQ4	99.9300	7/16/2012	7/16/2032	3.000%	4,991,900.00	4,992,286.98	4,675,200.00	(317,036.98)
OPPENHEIMER & CO. INC.	FED HOME LOAN BANK	313380C96	99.9000	8/13/2012	8/13/2027	2.000%	4,995,000.00	4,995,292.99	4,666,300.00	(328,992.99)
OPPENHEIMER & CO. INC.	FANNIE MAE	3136GOKX6	99.2500	8/27/2012	8/27/2027	2.250%	4,987,500.00	4,988,200.53	4,666,780.00	(321,417.53)
OPPENHEIMER & CO. INC.	FED HOME LOAN BANK	3133814T9	99.8500	11/21/2012	10/29/2027	1.750%	2,845,725.00	2,845,912.43	2,697,439.50	(148,477.93)
OPPENHEIMER & CO. INC.	FED HOME LOAN BANK	3133812F1	99.9100	11/14/2012	10/29/2027	2.125%	7,493,250.00	7,493,531.76	7,234,350.00	(259,181.76)
OPPENHEIMER & CO. INC.	FED HOME LOAN BANK	313381EJ5	99.9950	12/14/2012	12/14/2027	1.250%	5,999,700.00	5,999,710.84	5,868,960.00	(130,750.84)
OPPENHEIMER & CO. INC.	FED HOME LOAN BANK	313381W49	99.8500	1/30/2013	1/30/2023	1.000%	5,849,122.50	5,849,158.78	5,699,479.50	(149,679.28)
OPPENHEIMER & CO. INC.	FED HOME LOAN BANK	313382B81	99.6200	2/21/2013	2/21/2023	1.250%	4,983,500.00	4,984,082.83	4,777,550.00	(206,532.83)
OPPENHEIMER & CO. INC.	FANNIE MAE	3136GOK36	99.5000	3/6/2013	10/30/2023	2.100%	4,925,000.00	4,927,236.50	4,670,450.00	(256,786.50)
OPPENHEIMER & CO. INC.	FANNIE MAE	3135GQI3	99.8750	5/6/2013	1/23/2023	2.330%	3,495,625.00	3,495,692.80	3,318,630.00	(177,062.80)
OPPENHEIMER & CO. INC.	FED HOME LOAN BANK	313382T87	99.4400	5/16/2013	5/16/2023	2.300%	4,972,000.00	4,972,345.02	4,730,000.00	(242,345.02)
OPPENHEIMER & CO. INC.	FANNIE MAE	3136GJDT3	99.5500	5/30/2013	3/6/2023	2.550%	4,977,500.00	4,977,695.54	4,790,350.00	(187,345.54)
OPPENHEIMER & CO. INC.	FREDDIE MAE	3134G4553	97.7000	6/12/2013	6/12/2023	2.570%	4,885,000.00	4,885,566.81	4,743,450.00	(142,116.81)

Source: Mark to Market Report as of June 30, 2013

Figure 2

Account	Identifier	Description	Original Broker	Original Units	Current Units	Currency/Compon	Rate/Transaction	Type	Post Date	Final Maturity	Price	Principal	Accrued Interest	Realized Gain/Loss	Amount
BCTO	313379PB9	FEDERAL HOME LOAN BANK	Oppenheimer	(3,060,000.00)	(1,875,483.87)	USD			03/06/2014	06/14/2027	92.726	(1,739,061.17)	(13,841.07)	(134,208.94)	1,752,902.24
BCTO	313380C96	FEDERAL HOME LOAN BANK	Oppenheimer	(1,940,000.00)	(1,169,632.26)	USD			04/09/2014	06/14/2027	93.599	(1,112,922.31)	(12,306.48)	(74,714.37)	1,125,238.79
BCTO	3133812F1	FEDERAL HOME LOAN BANK	Oppenheimer	(5,000,000.00)	(5,000,000.00)	USD			03/06/2014	08/13/2027	90.550	(4,527,500.00)	(6,388.89)	(468,034.93)	4,533,888.89
BCTO	3133814T9	FEDERAL HOME LOAN BANK	Oppenheimer	(7,500,000.00)	(7,500,000.00)	USD			03/04/2014	10/29/2027	91.470	(6,860,250.00)	(55,338.54)	(633,588.34)	6,915,588.54
BCTO	313381EJ5	FEDERAL HOME LOAN BANK	Oppenheimer	(2,850,000.00)	(2,850,000.00)	USD			03/06/2014	10/29/2027	92.050	(2,623,425.00)	(25,135.42)	(222,682.60)	2,648,660.42
BCTO	313381W49	FEDERAL HOME LOAN BANK	Oppenheimer	(6,000,000.00)	(6,000,000.00)	USD			03/06/2014	12/14/2027	95.750	(5,745,000.00)	(47,833.33)	(255,000.00)	5,792,833.33
BCTO	313382B81	FEDERAL HOME LOAN BANK	Oppenheimer	(5,000,000.00)	(5,000,000.00)	USD			03/17/2014	01/30/2023	99.280	(4,808,465.00)	(7,150.00)	(41,017.06)	4,815,615.00
BCTO	3134G4553	FREDDIE MAE	Oppenheimer	(5,000,000.00)	(5,000,000.00)	USD			03/17/2014	02/21/2023	96.450	(4,822,500.00)	(3,993.06)	(162,832.34)	4,826,493.06
BCTO	3136GOKN4	FANNIE MAE	Oppenheimer	(6,000,000.00)	(6,000,000.00)	USD			06/12/2013	06/12/2023	95.200	(4,760,000.00)	(32,838.89)	(137,583.88)	4,792,838.89
BCTO	3136GOKQ4	FANNIE MAE	Oppenheimer	(5,000,000.00)	(5,000,000.00)	USD			02/27/2014	05/24/2032	93.050	(4,583,000.00)	(46,500.00)	(406,071.37)	4,529,528.63
BCTO	3136GOK36	FANNIE MAE	Oppenheimer	(5,000,000.00)	(5,000,000.00)	USD			02/27/2014	07/16/2032	90.440	(4,522,000.00)	(17,083.33)	(520,210.31)	4,539,083.33
BCTO	3136GJDT3	FANNIE MAE	Oppenheimer	(5,000,000.00)	(5,000,000.00)	USD			10/30/2013	10/30/2023	90.560	(4,528,000.00)	(2,333.33)	(403,317.74)	4,530,317.74
BCTO	3136GJDT3	FANNIE MAE	Oppenheimer	(5,000,000.00)	(5,000,000.00)	USD			03/04/2014	08/27/2027	90.500	(4,525,000.00)	(2,187.50)	(520,711.57)	4,527,187.50
									03/14/2014	03/06/2023	95.630	(4,781,500.00)	(2,033.33)	(197,713.31)	4,784,333.33
											\$ (61,938,633.48)	\$ (275,763.17)	\$ (4,172,686.76)	\$ 62,214,386.65	