

FILED

OCT 06 2017

**Kansas
Securities Commissioner**

**BEFORE THE SECURITIES COMMISSIONER
OF THE STATE OF KANSAS**

In the Matter of:

NEXT FINANCIAL GROUP, INC. (CRD # 46214)
and JACK MACE SCHWARTZ (CRD # 1027281)

Docket No. **18E07**

KSC No. 2012-5942

Respondents.

Pursuant to K.S.A. 17-12a412

CONSENT ORDER

1. The Staff of the Securities Commissioner of Kansas ("KSC Staff,") alleges that Respondents NEXT Financial Group, Inc. ("NEXT,") and Jack Mace Schwartz ("Schwartz,") engaged in conduct that constitutes violations of the Kansas Uniform Securities Act and that Respondents are subject to discipline pursuant to K.S.A. § 17-12a604.

2. Respondent NEXT and KSC Staff desire to settle the matters raised by KSC Staff relating to Respondents' alleged violations.

3. Respondent Schwartz shall be dealt with in another Order.

I. CONSENT TO JURISDICTION

4. Respondent NEXT and the KSC Staff stipulate and agree that the Securities Commissioner of Kansas ("the Commissioner,") has jurisdiction over Respondents and this matter pursuant to the Kansas Uniform Securities Act, K.S.A. §§ 17-12a101-17-12a703 ("KUSA,)."

5. Respondent NEXT and the KSC Staff stipulate and agree that the Commissioner has authority to enter this Order pursuant to K.S.A. § 17-12a604.

II. WAIVER AND EXCEPTION

6. Respondent NEXT waives its right to a hearing with respect to these matters.

7. Respondent NEXT waives any rights that it may have to seek judicial review or otherwise challenge or contest the terms and conditions of this Order. Respondent NEXT specifically forever releases and holds harmless the Kansas Securities Commissioner, the KSC Staff and their respective representatives and agents from any and all liability and claims arising out of, pertaining to, or relating to this matter.

7. Respondent NEXT stipulates and agrees that, should the facts contained herein prove to be false or incomplete, KSC Staff reserves the right to pursue any and all legal and administrative remedies at its disposal.

III. CONSENT TO COMMISSIONER'S ORDER

8. Respondent NEXT and KSC Staff agree to the issuance of this Consent Order without further proceedings in this matter, agreeing to be fully bound by the terms and conditions specified herein.

9. Respondent NEXT agrees not to take any action or to make or permit to be made any public statement creating the impression that this Order is without a factual basis. Nothing in this Order affects Respondent's: (a) testimonial obligation, or (b) right to take legal or factual positions in defense of litigation or in defense of other legal proceedings in which the Commissioner is not a party.

IV. FINDINGS OF FACT

10. This action is brought by the KSC Staff on behalf of the Office of the Kansas Securities Commissioner (the "KSC,,"), a Division of the Kansas Insurance Department ("KID,,).

11. Respondent Schwartz, CRD # 1027281, is a resident of Kansas. His current address is believed to be [REDACTED] based on his entry in the Central Registration Database (“CRD,,).

12. Respondent NEXT, CRD # 46214, is a corporation formed in Virginia on June 9, 1998 and doing business in Kansas as described herein. The main address for NEXT is 2500 Wilcrest Drive, Ste. 620, Houston, TX 77042 according to the CRD. NEXT is currently registered with the KSC as an investment adviser (“IA,,) and a broker-dealer (“BD,,).

13. Schwartz has been affiliated with NEXT Financial Group from May 24, 2004 to the present. Schwartz is currently registered with the KSC as a broker dealer agent (“BDA,,) and an investment adviser representative (“IAR,,). Schwartz was registered in both capacities during the period relevant in this NOI.

14. Schwartz operated a NEXT branch office, CRD # 173525, under the name JMS Financial Services (“JMS,,). Schwartz operated JMS on behalf of NEXT as a branch supervisor and a principal with supervisory jurisdiction during the time relevant in this NOI. As a principal, the conduct of Schwartz binds NEXT.

15. The following Order is in the public interest and is consistent with the purposes intended by the Kansas Uniform Securities Act.

Lack of Supervision and Oversight

16. In the middle of 2009, Schwartz began purchasing exchange traded fund (“ETF,,) products which were leveraged and/or inverse to an index on behalf of certain clients of NEXT and Schwartz.

17. In particular, Schwartz purchased ProShares UltraShort 20+ Year Treasury Fund (TBT), ProShares Ultra Utilities (“UPW,,), ProShares Short Dow 30 (“DOG,,), Ultra QQQ (“QID,,) on behalf of these clients.

18. Leveraged ETFs and leveraged-inverse ETFs are investments belonging to a category of complex products known as non-traditional ETFs (collectively, “Non-Traditional ETFs,,). Leveraged ETFs seek to deliver a stated multiple of the return of a specified index over a stated time-period. Leveraged-inverse ETFs seek to deliver a stated multiple of the opposite of the return of a specified index over a stated time-period. The majority of Non-Traditional ETFs, including the ones that the Respondent purchased on behalf of his clients are designed to achieve their stated objective on a daily basis.

19. The summary prospectuses for TBT, UPW, DOG, and QQQ all similarly state, “The fund is different from most exchange traded funds in that it seeks inverse leveraged returns and only on a daily basis. The Fund also is riskier than similarly benchmarked exchange-traded funds that do not use leverage. Accordingly, the Fund may not be suitable for all investors and should be used only by knowledgeable investors who understand the potential consequences of seeking daily inverse leveraged investment results. Shareholders should actively monitor their investments., The summary prospectuses go on to explain, “The Fund will lose money if the Index performance is flat over time, and it is possible that the Fund will lose money if the Index’s performance decreases, as a result of daily rebalancing, the Index’s volatility and the effects of compounding.,,

20. In June of 2009, the Financial Industry Regulatory Authority (“FINRA”) issued Regulatory Notice 09-31, “*Non-Traditional ETFs*,” (the “Notice,,) which reminded its members that although Non-Traditional ETFs “may be useful in some sophisticated trading strategies,

they are highly complex financial instruments," and are "typically are unsuitable for retail investors who plan to hold them for longer than one trading session, particularly in volatile markets."

21. The Notice went on to remind firms as to their sales practice obligations in connection with Non-Traditional ETFs. The Notice specifically stated that firms "must have adequate supervisory procedures in place to ensure that these obligations are met.,, Furthermore, the Notice highlighted the need for additional specialized training if registered representative were allowed to recommend these products. In addition, the Notice emphasized that firms should "make every effort to make customers aware of the pertinent information regarding the products.,,

22. Independent of the Notice, BDs and IAs have an ongoing obligation to establish and maintain supervisory procedures reasonably designed to assist in detecting and preventing violations of the KUSA.

23. The nature and complexity of the products and services offered are a factor in determining the reasonableness of procedures used.

24. Non-Traditional ETFs require special care because they are complex products that may not be suitable for the average retail investor, particularly, if the customer holds the product for longer than one day. }

25. Because of their brokerage registrations, both NEXT and Schwartz were put on notice about the nature of leveraged and inverse ETFs by the Notice and were obligated to consider these factors in regard to their duties in their brokerage capacities as well as advisory capacities.

26. Despite their regulatory obligations, the Notice, and the language of the prospectuses, NEXT failed to require any training regarding Non-Traditional ETFs until October 2012 and allowed Schwartz to recommend and invest clients' funds in Non-Traditional ETFs.

27. Similarly, NEXT did not timely establish supervisory structures regarding Non-Traditional ETFs.

28. Additionally, NEXT did not implement s Non-Traditional ETF client disclosure form until October 2012.

29. Despite the abundance of warnings regarding the risks of nontraditional ETFs, Schwartz placed a portion of the assets that he managed into Non-Traditional ETFs.

30. Furthermore, he held the Non-Traditional ETFs for periods much longer than one day (in some instances, they were held for as long as seven years).

Schwartz's Investments as Analyzed by NEXT's own Policy

31. When NEXT finally did put a policy in place on October 10, 2012 (the "NEXT ETF Policy"), and required training regarding the sale and use of Non-Traditional ETFs, the policy stated, "Only customers that have a risk tolerance of High Risk and Speculation may be solicited to purchase Non-Traditional ETFs. No more than 5% of a customer's liquid net worth can be invested in a single Non-Traditional ETF and no more than 10% of a customer's liquid net worth can be invested in Non-Traditional ETFs as a whole."

32. Prior to NEXT putting its Non-Traditional ETF policies in place, Schwartz already had clients who did not meet the policy guidelines. As of December 31, 2011, all of

Schwartz's Non-Traditional ETF clients were invested in amounts that would have exceeded the NEXT ETF Policy guidelines if they had been in place.

33. The transactions described below were unsuitable at the time they were entered and NEXT failed to put a policy in place to prevent such transactions from occurring. These ETF transactions were unsuitable even under the NEXT ETF Policy guidelines subsequently adopted.

Brokerage Client Example

34. Kansas Resident 1 ("KR1,") and KR1's living trust ("KR1 Trust,") were brokerage clients of NEXT and Schwartz.

35. Schwartz invested approximately 16% of the KR1 Trust's identified liquid net worth into TBT, a single Non-Traditional ETF. This investment exceeded the later-adopted NEXT ETF Policy guidelines.

36. The KR1 Trust's first purchase was on May 18, 2011, and the second purchase was on September 16, 2011.

37. Schwartz invested approximately 16% of KR1's identified liquid net worth into TBT on her behalf personally. This investment exceeded the later-adopted NEXT ETF Policy guidelines.

38. KR1's first purchase on her behalf personally was on May 26, 2011, with a second purchase on October 21, 2011.

39. In total, Schwartz invested approximately 32% of KR1's identified liquid net worth into TBT, a single Non-Traditional ETF.

40. As of December 31, 2011, the KR1 Trust had been invested in TBT for 223 days for the first round and 105 days for the second round of purchases. At that time, the KR1 Trust had \$8,417.10 in losses for its investment in TBT.

41. As of December 31, 2011, KR1 had been invested in TBT for 215 days for the first round and 70 days for the second round of purchases. At that time, KR1 had \$8,090.87 in losses for her investment in TBT.

42. As of December 31, 2011, between the KR1 Trust and KR1 personally, the TBT investment had lost \$16,507.97 which accounted for approximately 41% of the amount originally invested in TBT.

Advisory Client Example

43. Kansas Resident 2 ("KR2,") identified his risk tolerance as medium high with an investment objective of achieve strong growth and nominal income.

44. Schwartz invested approximately 44% of KR2's identified liquid net worth in TBT (9% of identified liquid net worth), DOG (25% of identified liquid net worth), and QID (10% of identified liquid net worth), three Non-Traditional ETFs. This investment exceeded the later-adopted NEXT ETF Policy guidelines.

45. On May 14, 2009, Schwartz bought KR2's first position in DOG, representing 1% of his identified liquid net worth.

46. On May 20, 2009, Schwartz increased KR2's position DOG raising it to 5% of KR2's identified liquid net worth. In addition, Schwartz bought a position in TBT on KR2's behalf representing 4% of KR2's net worth.

47. On June 23, 2009, Schwartz increased KR2's position in TBT to represent 9% of his identified liquid net worth as well as buying a position in QID representing 10% of KR2's identified liquid net worth.

48. On September 1, 2009, Schwartz increased KR2's position in DOG by an additional 20% of his identified liquid net worth.

49. On August 3, 2011, Schwartz sold KR2's entire interest in DOG realizing a \$7,857.96 loss which represented approximately 31% of KR2's investment in DOG. KR2 had held his first round position in DOG for 799 days, his second round position for 793 days, and his third round position for 692 days.

50. Additionally on August 3, 2011, Schwartz sold KR2's entire position in QID for a loss of \$7,400.36 representing approximately 71% of KR2's investment in QID.

51. On August 17, 2011, Schwartz bought KR2 a new position in QID representing 10% of KR2's identified liquid net worth. Schwartz sold this position six days later on August 23, 2011 for a gain of \$323.61.

52. On September 7, 2011, Schwartz bought KR2 an additional interest in TBT, representing 6% of KR2's identified liquid net worth, which was sold on September 19, 2011 realizing a loss of \$5,632.96 which represented nearly 3 approximately 7% of KR2's investment in TBT. KR2 held his first round position in TBT for 839 days, his second round position for 806 days, and his third round position for 12 days.

54. In total, KR2 lost \$20,567.67 representing approximately 34% of the money invested in Non-Traditional ETFs.

55. KR2 was an advisory client of Schwartz and NEXT, to which Schwartz and NEXT owed a fiduciary duty.

Inappropriate Disclosure related to Non-Traditional ETFs

56. Prior to October 2012, NEXT did not require that disclosures be made to customers in writing detailing the specialized risks related to Non-Traditional ETFs and describing the nature of the products.

57. On a number of occasions between 2009 and 2011, Schwartz recommended and sold Non-Traditional ETFs to certain customers accompanied by a Mutual Fund Disclosure Form. However, the risks associated with mutual funds differ significantly from Non-Traditional ETFs and many risks associated with Non-Traditional ETFs were not disclosed on Mutual Fund Disclosure Form.

Remedial Efforts

58. Effective as of October 2012, NEXT adopted new procedures, suitability guidelines, and educational and disclosure requirements for leveraged or inverse ETFs.

59. Specifically, NEXT implemented the use of an Exchange Traded Fund (ETF) Disclosure Form and suitability guidelines, including, no more than 5% of a customer's liquid net worth should be in any single Non-Traditional ETF, not more than 10% of a customer's liquid net worth should be in Non-Traditional ETFs, and a customer should have a risk tolerance of High or Speculative to be solicited to purchase non-traditional ETFs.

60. In addition, representatives who wished to solicit Non-Traditional ETFs were required to take certain educational courses.

61. Beginning in April 2014, each Non-Traditional ETF purchase had to be approved by the NEXT compliance department.

62. NEXT provided timely responses and substantial cooperation in connection with the regulatory investigation into this issue.

V. CONCLUSIONS OF LAW

63. Paragraphs 1-62 are incorporated by reference as though fully set forth herein.

64. The Commissioner has jurisdiction over Respondents and this matter.

65. Under K.S.A. 17-12a412(d)(2) and K.A.R. 81-3-7 and 81-14-4, a person may be disciplined under K.S.A. 17-12a412(a)-(c) if the person acting as a BD or BDA or IA or IAR does not maintain proper books and records as provided by law.

66. K.A.R. 81-3-7 requires that BDs must establish and maintain supervisory procedures that are reasonably designed to detect and prevent violations of the KUSA and achieve compliance with the KUSA. In determining whether procedures are reasonably designed, the nature and complexity of the products and services rendered may be taken into account.

62. K.A.R. 81-14-10 requires that IAs must establish and maintain supervisory procedures that are reasonably designed to detect and prevent violations of the KUSA and achieve compliance with the KUSA. In determining whether procedures are reasonably designed, the nature and complexity of the products and services rendered may be taken into account.

63. K.S.A. 17-12a412(d)(9) prohibits the failure “to reasonably supervise [a BDA], [IAR], or other individual, if the [BDA], [IAR], or other individual was subject to supervision and committed a violation of this act or a rule adopted or order issued under this act or the predecessor act within the previous 10 years.,,

64. Pursuant to K.S.A. 17-12a412(c), discipline for violations of K.S.A. 17-12a412(d)(9) and (13) may include: (1) a censure; (2) a bar or suspension from association with an IA registered in this state; (3) a civil penalty of up to \$25,000 for each violation; (4) an order requiring the registrant to pay restitution for any loss or disgorge any profits arising from a violation, including, in the Administrator’s discretion, the assessment of interest from the date of the violation at the rate provided for interest on judgments by K.S.A. 16-204, and amendments thereto; (5) an order charging the registrant with the actual cost of an investigation or proceeding;

or (6) an order requiring the registrant to cease and desist from any action that constitutes a ground for discipline, or to take other action necessary or appropriate to comply with the KUSA.

NEXT's Failure to Institute Proper Procedures

66. Respondent NEXT had an ongoing obligation to establish and maintain supervisory procedures reasonably designed to assist in detecting and preventing violations of the KUSA. Given the nature and complexity of Non-Traditional ETFs, NEXT should have had training requirements and suitability policies in place prior to allowing Schwartz to recommend and invest clients in those products. This is particularly true after FINRA issued the Notice.

67. Failing to put these procedures in place timely constitutes a violation of K.A.R. 81-3-7(a)(2) and is thereby grounds for discipline against NEXT pursuant to K.S.A. 17-14a412(d)(2).

68. Failing to put these procedures in place timely constitutes a violation of K.A.R. 81-14-10(a)(2) and is thereby grounds for discipline against NEXT pursuant to K.S.A. 17-14a412(d)(2).

NEXT's Failure to Supervise Schwartz

69. By not timely maintaining supervisory procedures reasonably designed to assist in detecting and preventing violations of the KUSA instituting and by not enforcing a practice of requiring Non-Traditional ETF Disclosure Forms, NEXT failed to reasonably supervise Schwartz's activities as an IAR in connection with transactions as described above in violation of the KUSA. This constitutes a violation of K.S.A. 17-12a412(d)(9) is grounds for discipline as to NEXT.

72. By not timely maintaining supervisory procedures reasonably designed to assist in detecting and preventing violations of the KUSA instituting and by not enforcing a practice of

requiring Non-Traditional ETF Disclosure Forms, NEXT failed to reasonably supervise Schwartz 's activities as a BDA in connection with transactions as described above in violation of the KUSA. This constitutes a violation of K.S.A. 17-12a412(d)(9) is grounds for discipline as to NEXT.

VI. ORDER

IT IS, THEREFORE ORDERED by the Securities Commissioner of Kansas that:

Respondent NEXT is ordered to pay seventy-five thousand dollars (\$75,000) to the Kansas Investor Education and Protection Fund for violating K.A.R. 81-3-7(a)(2), K.A.R. 81-14-10(a)(2), K.S.A. 17-12a417(d)(2), and K.S.A. 17-12a412(d)(9). Payment shall be made within 30 days after the issuance of this order and delivered to the Office of the Kansas Securities Commissioner, 109 SW 9th St., Ste. 600, Topeka, KS 66612. Such payment shall be in the form of a cashier's check or money order made out to the Office of the Kansas Securities Commissioner.

IT IS SO ORDERED BY THE COMMISSIONER.

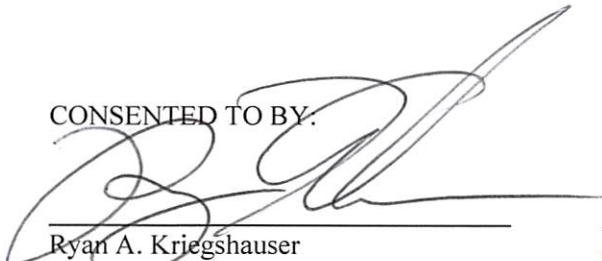
Entered at Topeka, Kansas this 6 day of Oct, 2017.



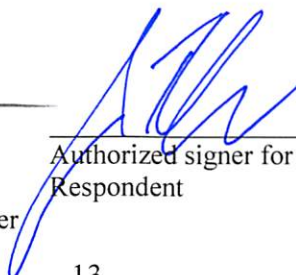
John R. Wine, JR.
Securities Commissioner



CONSENTED TO BY:



Ryan A. Kriegshauser
General Counsel
Office of the Kansas Securities Commissioner



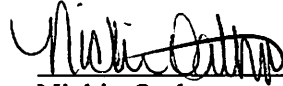
John T. Unger, General Counsel
Authorized signer for NEXT Financial Group, Inc.
Respondent

CERTIFICATE OF SERVICE

I hereby certify that on this 10th day of October, 2017, a copy of the above Consent

Order was sent via Certified Mail to the Following:

Next Financial Group
Attn: John T. Unger
2500 Wilcrest, Suite 620
Houston, TX 77042



Nickie Oathout
Administrative Clerk