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ARKANSAS SECURITIES DEPT.

**BEFORE THE ARKANSAS SECURITIES COMMISSIONER**  
**Case No. S-18-0089**  
**Order No. S-18-0089-18-OR01**

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**IN THE MATTER OF**  
**GERALD DONNER, JR. &**  
**AUXARC ASSET MANAGEMENT COMPANY**

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**CONSENT ORDER**

This Consent Order is entered pursuant to the Arkansas Securities Act, codified at Ark. Code Ann. §§ 23-42-101 through 23-42-509 (Act), the Rules of the Arkansas Securities Commissioner promulgated under the Act (Rules), and the Arkansas Administrative Procedures Act, codified at Ark. Code Ann. §§ 25-15-201 through 25-15-219, in accordance with an agreement by and between the Staff of the Arkansas Securities Department (Staff) and Gerald Donner, Jr. (Donner), investment adviser representative and owner of Auxarc Asset Management Company (AAMC), in full settlement of all claims that could be brought against Donner and AAMC by the Staff in the factual situation set out below.

Without admitting or denying the allegations herein, Donner admits jurisdiction of the Act and Arkansas Securities Commissioner (Commissioner), waives his right to formal hearing and consents to the entry of this order and agrees to abide by its terms. Donner has cooperated fully with the Department's investigation and resolution of this matter.

**FINDINGS OF FACT**

1. AAMC, CRD No. 154173, is an entity that has been registered with the Arkansas Securities Department (Department) as an investment adviser firm since June 30, 2010. AAMC has a principal place of business located at 106 W. Tulsa, Siloam Springs, AR

72761. Donner, CRD No. 1856602, is a resident of Siloam Springs, Arkansas. Donner has been registered with the Department as an investment adviser representative in the state of Arkansas since September 12, 1988. Since June 30, 2010, Donner has been registered as the investment adviser representative and owner of AAMC.

2. In April of 2009 and August of 2011, Donner recommended to a number of his clients that they invest in non-traditional exchange traded funds (ETFs), including inverse ETFs, and leveraged inverse ETFs (collectively, Non-traditional ETFs).
3. ETFs are index funds traded as though they are equity stocks. Inverse ETFs are keyed to a particular index or market and designed to fluctuate inversely to that index or market. Leveraged ETFs increase or decrease in value by multiples, usually of two or three. For example, a leveraged ETF keyed to the S & P 500 index will deliver returns of two or three times the change in the S & P 500 index, and an inverse leveraged ETF will deliver the inverse of the change in the index, e.g., a 20% return on a 10% loss in the index. The Non-traditional ETFs Donner recommended to his clients all reset on a daily basis, and were designed to deliver the return promised in one day.
4. Non-traditional ETFs are designed for a one-day performance. Adverse returns could result from holding them for longer periods of time, particularly if the index to which the Non-traditional ETFs is keyed goes in a direction other than the direction anticipated when the Non-traditional ETFs were purchased. These characteristics of Non-traditional ETFs were well known and could be easily ascertained at the time Donner recommended the purchase of the Non-traditional ETFs in question, as shown by the following:
  - a. The Financial Industry Regulatory Authority (FINRA) issued Regulatory Notice 09-31 in June 2009, entitled "Non-Traditional ETFs." It was explained in the

notice that inverse and leveraged ETFs are “highly complex financial instruments that are typically designed to achieve their stated objectives on a daily basis.” Because these Non-traditional ETFs reset daily and compounded any returns or losses, their performance “can differ significantly from their stated daily objective,” the notice stated. On the first page of the notice was a clear warning: “inverse and leveraged ETFs... are unsuitable for retail investors who plan to hold them for longer than one trading session, particularly in volatile markets.” This warning that “inverse and leveraged ETFs are typically not suitable for retail investors who plan to hold them for more than one trading session” was repeated on page three of the notice under the heading, “Suitability.”

- b. The United States Securities and Exchange Commission (SEC) issued an investor alert simultaneously with FINRA Regulatory Notice 09-31. It, too, noted that inverse ETFs were one-day products, stating that the “performance of these ETFs over a period longer than one day can differ significantly from their stated daily performance objectives.”

5. Donner purchased the following Non-traditional ETFs:

<u>Name</u>	<u>Type</u>
Proshares Ultrashort Dow30	Inverse 2X to the Dow
Proshares Short MSCI Emerging Markets	Inverse to MSCI Emerging Markets
Proshares Ultrashort QQQ	Inverse 2X to the QQQ
Proshares Ultrashort Financials	Inverse 2X to the Financials

- 6. The prospectuses of the Non-traditional ETFs Donner purchased state quite clearly that they are to be used for one-day trades, stating “the Fund seeks investment results for a single day only, not for longer periods.” In addition, the prospectuses state that “[f]or

periods longer than a single day, the Fund will lose money when the level of the Index is flat, and it is possible that the Fund will lose money even if the level of the Index falls.”

7. Contrary to the regulatory notice produced by FINRA, the investor alert published by the SEC, and the prospectuses produced by the issuers of these securities, Donner recommended that his clients buy these Non-traditional ETFs and hold them much longer than one day. Donner’s recommendations led to at least four of his clients purchasing non-traditional ETFs. These clients have held Non-traditional ETFs for up to nine years. These Non-traditional ETF holdings make up from 1% to 8% of the value on the accounts. Of the accounts examined by the Staff, the unrealized losses in these securities now come to approximately \$15,519.58.

#### **CONCLUSIONS OF LAW**

8. The Commissioner has jurisdiction over this matter pursuant to Ark. Code Ann. § 23-42-308.
9. Under Rule 308.02 of the Rules, recommending to a client to whom investment supervisory, management or consulting services are provided the purchase, sale or exchange of any security without reasonable grounds to believe that the recommendation is suitable for the client on the basis of information furnished by the client after reasonable inquiry concerning the client’s investment objectives, financial situation and needs, and any other information known or acquired by the investment adviser after reasonable analysis of the client’s information and records provided to the investment adviser shall be considered unethical and grounds for denial, suspension or revocation. Considering the characteristics of the Non-traditional ETFs, Donner and AAMC violated

Rule 308.02 of the Rules by recommending that clients buy and hold these products in client accounts for longer than one day.

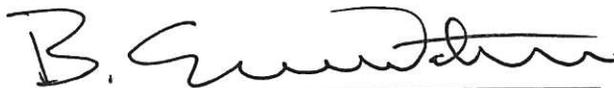
10. Under Ark. Code Ann. § 23-42-308(a)(2)(B) the Commissioner may by order deny, suspend, make conditional or probationary, or revoke any registration if he or she finds that an investment adviser has willfully failed to comply with any of the Rules. As noted above, Donner and AAMC violated Rule 308.02 of the Rules and, thus, violated Ark. Code Ann. § 23-42-308(a)(2)(B) by recommending that clients buy and hold the Non-traditional ETFs for more than one day.

11. Ark. Code Ann. § 23-42-308(h) allows for the informal disposition of a proceeding or allegations which might give rise to a proceeding by consent.

#### **ORDER**

IT IS THEREFORE ORDERED that Donner and AAMC shall jointly pay a fine to the Department in the total amount of \$2,500 upon entry of this Order.

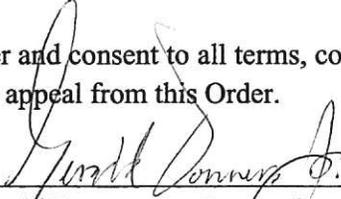
IT IS SO ORDERED this 10<sup>th</sup> day of October, 2018.



**B. EDMOND WATERS**  
Arkansas Securities Commissioner

**CONSENT TO ENTRY OF ORDER**

I hereby agree to the entry of this Consent Order and consent to all terms, conditions, and orders contained therein; and waive any right to appeal from this Order.

  
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Gerald Donner, Jr., Respondent

Approved as to content and form:

  
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Aislinn Andrews, Staff Attorney  
Arkansas Securities Department