

BEFORE THE ARKANSAS SECURITIES COMMISSIONER

Case No. S-13-0104

Order No. S-13-0104-13-CO01

IN THE MATTER OF
DAVID ALAN MULLENAX

ARKANSAS SECURITIES DEPT.

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RECEIVED

CONSENT ORDER

This consent order is entered pursuant to the Arkansas Securities Act, codified at Ark. Code Ann. §§ 23-42-101, *et seq.* (Repl. 2000), (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, *et seq.* (Repl. 2002) in accordance with an agreement by and between the Staff of the Arkansas Securities Department (Staff) and David Alan Mullenax in full settlement of all claims that could be brought against Mullenax by the Staff in the factual situation set out below.

Mullenax admits the jurisdiction of the Act and the Arkansas Securities Commissioner (Commissioner), waives his right to a formal hearing and, without admitting or denying the findings of fact made herein, consents to the entry of this order and agrees to abide by its terms.

FINDINGS OF FACT

1. David Alan Mullenax is a resident of Little Rock, Arkansas. His CRD number is 3206327, and since June 28, 2013, he has not been registered in any capacity pursuant to the Act.

Mullenax has been registered with three firms since May 2007.

a. Advisory Services Network (ASN). Until June 28, 2013, Mullenax was registered as an investment adviser representative with ASN. His registration with ASN began in April

2012.

- b. Sowell Management Services (Sowell). Mullenax was registered as an investment adviser representative with Sowell, from June 2011 to May 2012.
 - c. Pacific West Financial Consultants, Inc., an investment adviser, and Pacific West Securities, Inc., a broker-dealer (Pacific West, collectively). Mullenax was registered with Pacific West as both an investment adviser representative and broker-dealer agent from June 2007 to June 2011.
2. From May 27, 2009, to March 24, 2011, when Mullenax was employed by Pacific West, he recommended to some of his clients that they invest in non-traditional exchange traded funds (ETFs), including inverse ETFs, leveraged ETFs and leveraged inverse ETFs (collectively, Non-traditional ETFs). 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 Mullenax recommended to his clients all reset on a daily basis. They were designed to deliver the return promised in one day.
3. 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 Mullenax 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 typically are not suitable for retail investors who plan to hold them for more than one trading session” was repeated on page 3 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 that the “performance of these ETFs over a period longer than one day can differ significantly from their stated daily performance objectives.”
4. The prospectuses of many of the Non-traditional ETFs Mullenax sold state quite clearly that they are to be used for one-day trades. Mullenax sold many Non-traditional ETFs issued by ProShares, listed as follows:

| <u>Name</u> | <u>Type</u> |
|-----------------|-------------------------------|
| Short MidCap400 | Inverse to the S&P MidCap 400 |

| | |
|------------------------|------------------------------------------------|
| Short Dow30 | Inverse to the Dow Jones Industrial Average |
| Short S&P500 | Inverse to the S&P 500 |
| UltraShort Gold | Inverse 2X to the Gold Market |
| UltraShort Russell2000 | Inverse 2X to the Russell 2000 |
| Ultra Dow 30 | Inverse 2X to the Dow Jones Industrial Average |

The prospectuses of all of these Non-traditional ETFs, which are easily accessed on the ProShares website, contain the following statement on the first page of the prospectus,:

This . . . ProShares ETF seeks a return that is [keyed to] . . . an index or other benchmark (target) *for a single day*, as measured from one NAV [net asset value] calculation to the next. Due to the compounding of daily returns, ProShares' returns over periods other than one day will likely differ in amount and possibly direction from the target return for the same period. [Emphasis in original.]

5. 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, Mullenax recommended that his clients buy these Non-traditional ETFs and hold them until the securities markets experience a significant downturn, i.e., much longer than one day. Many of his clients followed Mullenax from Pacific West to Sowell to ASN, and many are invested in Non-traditional ETFs, still, several years later. Fifty-five of his present clients invested in Non-traditional ETFs when he was registered with Pacific West. They purchased these securities for approximately \$1.42 million. The unrealized losses in these securities now come to approximately \$700,000. Although a small part of the total amount of assets Mullenax had under management, these investments and the resultant losses would be significant to a reasonable investor.

CONCLUSIONS OF LAW

6. The Commissioner has jurisdiction over this matter pursuant to Ark. Code Ann. § 23-42-308.
7. Mullenax disregarded the characteristics of the Non-traditional ETFs and the needs of his clients. Mullenax therefore had no reasonable basis for recommending that his clients buy and hold the Non-traditional ETFs for more than one day.
 - a. Each of these recommendations was therefore an unsuitable recommendation, one of the “Unfair, Misleading and Unethical Practices” of a broker-dealer or agent of a broker-dealer listed in Rule 308.01(d), Rules of the Arkansas Securities Commissioner.
 - b. Each of these recommendations was therefore an unsuitable recommendation, one of the “Fraudulent, Deceptive, Dishonest or Unethical Practices” of an investment adviser or representative of an investment adviser listed in Rule 308.02(a), Rules of the Arkansas Securities Commissioner.
 - c. These unsuitable recommendations were “dishonest or unethical practices in the securities business,” violations of Ark. Code Ann. § 23-42-308(a)(2)(G).

UNDERTAKING

In settlement of this matter, Mullenax agrees with the Staff to:

8. Not apply for registration pursuant to the Act in any capacity, including as an investment adviser or representative of an investment adviser or as a broker-dealer or as an agent of a broker-dealer, until
 - a. Mullenax has taken and obtained passing scores on all examinations required by Rule 302.01(c), Rules of the Arkansas Securities Commissioner, and/or Rule 302.01(f), Rules

of the Arkansas Securities Commissioner, and

- b. a period of at least one year from the date of this order has elapsed; and
9. Mullenax will apply for registration only as an agent of a registered broker-dealer or a representative of a registered investment adviser which is
- a) Approved by the Staff and
 - b) Has agreed to on-site, heightened supervision of Mullenax for a period of one year in accordance with a heightened supervision plan approved by the Staff.

OPINION

10. This order is in the public interest. The facts set out in ¶¶ 1 - 5 support the violations of the Act and Rules set out in ¶¶ 6 and 7.

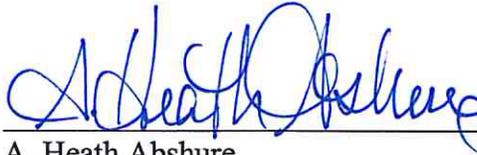
ORDER

IT IS THEREFORE ORDERED that:

11. The registration of Mullenax as an investment adviser representative with ASN is hereby revoked as of June 28, 2013, the last day on which it was effective, for the violations of the Act and Rules set out in ¶ 7 and in accordance with Ark. Code Ann. § 23-42-308(e)(3).
12. In accordance with Mullenax's undertaking, no application for registration pursuant to the Act, including as an investment adviser or investment adviser representative or as a broker-dealer or as a broker-dealer agent, will be accepted or granted until
- a. he has taken and obtained passing scores on all examinations required by Rule 302.01(c), Rules of the Arkansas Securities Commissioner, and/or Rule 302.01(f), Rules of the Arkansas Securities Commissioner, and

- b. a period of one year from the date of this order has elapsed.
13. Should Mullenax apply for registration as either an agent of a broker-dealer or an investment adviser representative, no application will be accepted unless and until
- a. the Staff has approved the broker-dealer or investment adviser and
 - b. the broker-dealer or investment adviser has agreed to heightened supervision of Mullenax for a period of one year in accordance with a heightened supervision plan approved by the Staff.

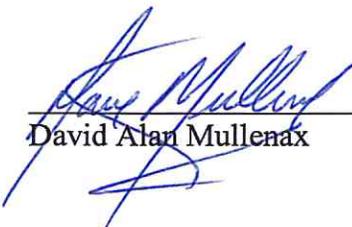
WITNESS MY HAND AND SEAL this 16th day of August, 2013.



A. Heath Abshire
ARKANSAS SECURITIES COMMISSIONER

CONSENT TO ENTRY OF ORDER

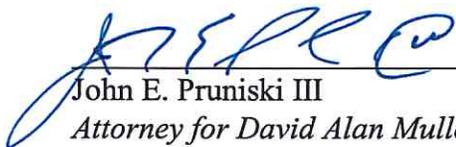
David Alan Mullenax hereby acknowledges that he has been served with a copy of this Order, has read it, is aware of his right to a hearing and has waived that right. He acknowledges that he is consenting to the entry of this order, including the undertaking that is a part of this order, voluntarily after consulting with counsel and that no threats, offers, promises or inducements of any kind have been made by any member of the Staff to induce him to consent to the entry of this order.



David Alan Mullenax

Signed this 16th day of August, 2013.

APPROVED AS TO FORM

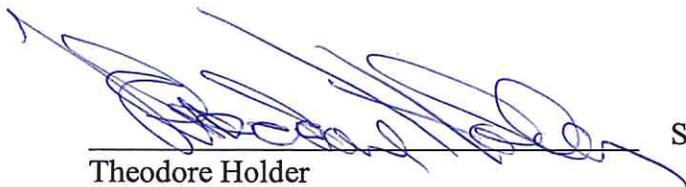


John E. Pruniski III

Attorney for David Alan Mullenax

Signed this 16th day of August, 2013.

APPROVED AS TO FORM



Theodore Holder

Attorney for the Staff

Signed this 16th day of August, 2013.