

State of Missouri  
Office of Secretary of State

Case No. AP-10-11

IN THE MATTER OF:

JAMES E. OTTO,

Respondent.

Serve James E. Otto at:

13425 W. 128th Street  
Overland Park, Kansas 66213

**CONSENT ORDER**

On July 12, 2010, the Enforcement Section of the Securities Division of the Office of Secretary of State (the "Enforcement Section"), through the Securities Division's Assistant Commissioner, Mary Hosmer, submitted a Petition for Order to Cease and Desist and Order to Show Cause Why Civil Penalties and Costs Should Not Be Imposed. After reviewing the petition, the Commissioner issues the following findings of fact, conclusions of law and order:

**SUMMARY OF ENFORCEMENT SECTION'S ALLEGATIONS**

1. The Enforcement Section of the Missouri Securities Division ("Enforcement Section") has alleged that James E. Otto ("Respondent") transacted business as an unregistered securities agent and an unregistered broker-dealer in the State of Missouri and that these activities constitute violations of the Missouri Securities Act and are grounds for the Missouri Commissioner of Securities to issue an order pursuant to Section 409.6-604, RSMo. (Cum. Supp. 2009).
2. In 2004, while working at Bankers Life and Casualty Company ("Bankers"), Otto, with the help of Michael Lees ("Lees"), branch manager at Bankers, formed a transfer business to help Bankers' insurance agents liquidate customer funds held in securities brokerage accounts. Otto assisted customers in opening accounts at two Missouri-registered broker-dealers and in moving the securities held by these customers to these brokerage firms. Each customer gave Otto limited trading authority over this new brokerage account. Otto then assisted customers with liquidating the securities held in the brokerage account and transferring the liquidated funds to Bankers.
3. Insurance agents at Bankers assisted these customers in the purchase of equity indexed annuities or other insurance products with these liquidated funds. Insurance agents of Bankers paid Otto a fee based on the agent's insurance commission for Otto's "in-house brokerage" services ("transfer service"). Otto's transfer services liquidated over seven million dollars (\$7,000,000) from securities in over one hundred eighty (180) customer accounts. During this time Otto was not registered to sell securities in Missouri or to offer investment advice. Otto's transfer service was not registered as a broker-dealer or an investment adviser.
4. Respondent Otto and the Enforcement Section desire to settle the allegations and the matters raised by the Enforcement Section relating to the Respondent's violations of the Missouri Securities Act by transacting business in Missouri as an unregistered agent and as an unregistered broker-dealer.

**CONSENT TO JURISDICTION**

5. Respondent and the Enforcement Section stipulate and agree that the Commissioner has jurisdiction over the Respondent and these matters pursuant to the Missouri Securities Act of 2003, Chapter 409, *et seq.*
6. Respondent and the Enforcement Section stipulate and agree that the Commissioner has authority to enter this Order pursuant to Section 409.6-604(h), RSMo. (Cum. Supp. 2009), which provides:

"The commissioner is authorized to issue administrative consent orders in the settlement of any proceeding in the public interest under this act."

**WAIVER AND EXCEPTION**

7. Respondent waives his right to a hearing with respect to this matter.
8. Respondent waives any right that he may have to seek judicial review or otherwise challenge or contest the terms and conditions of this Order. Respondent specifically forever releases and holds harmless the Missouri Office of Secretary of State, Secretary of State, Commissioner of Securities, and their respective representatives and agents from any and all liability and claims arising out of, pertaining to, or relating to this matter.
9. Respondent stipulates and agrees with the Enforcement Section that, should the facts contained herein prove to be false or

incomplete, the Enforcement Section reserves the right to pursue any and all legal or administrative remedies at its disposal.

### **CONSENT TO COMMISSIONER'S ORDER**

10. Respondent and the Enforcement Section stipulate and 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.
11. Respondent 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 factual basis. Nothing in this paragraph affects Respondent's (a) testimonial obligations; (b) right to take legal or factual position in defense of litigation or in defense of other legal proceedings in which the Commissioner of Securities is not a party; or (c) right to make public statements that are factual.
12. Respondent agrees that Respondent is not the prevailing party in this action since the parties have reached a good faith settlement.
13. Respondent neither admits nor denies the allegations made by the Enforcement Section, but consents to the Commissioner's Findings of Fact, Conclusions of Law, and Order as set forth below solely for the purposes of resolving this proceeding and any proceeding that may be brought to enforce the terms of this Consent Order.

### **COMMISSIONER'S FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER**

#### **A. Respondent and Related Parties**

14. Bankers is a Missouri-licensed insurance company with National Association of Insurance Commissioners ("NAIC") number 61263. Bankers has a main address of 600 West Chicago Avenue, Chicago, Illinois 60654.
15. Otto is an insurance agent and is licensed to sell life and health insurance through the Missouri Department of Insurance, Financial Institutions, and Professional Registration ("Missouri DOI"). Otto was registered as a securities agent in Missouri through the Central Registration Depository System ("CRD") from October 1986 to May 2002 with CRD number 1566081. Otto has not been registered to sell securities in the State of Missouri since May 2002. From June 2004 until August 2006, Otto was an insurance agent with Bankers where he started the transfer service. Otto has an address of 13425 W. 128th Street, Overland Park, Kansas 66213. Otto is not registered as a broker-dealer or investment adviser in the State of Missouri.
16. Brokerage Firm X is a Missouri-registered broker-dealer and has a main address in Nebraska. Brokerage Firm X is one of the broker-dealers Otto used for Otto's transfer service.
17. Brokerage Firm Y is a Missouri-registered broker-dealer and has a main address in Rhode Island. Brokerage Firm Y is one of the broker-dealers Otto used for Otto's transfer service.
18. As used herein, the term "Respondent" refers to Otto.

#### **B. Enforcement Section Investigation**

19. The Enforcement Section opened an investigation and obtained documents and other information that revealed, among other things, the following information.
20. In 2005, Otto approached Bankers' Branch Manager Lees about the possibility of a transfer service for Banker's agents.
21. Otto claimed he could assist insurance agents at Bankers by, among other things:
  - a. Assisting their customers in transferring brokerage accounts to Brokerage Firm X or Brokerage Firm Y;
  - b. Assisting their customers in liquidating securities from the customer's brokerage account at Brokerage Firm X or Brokerage Firm Y; and
  - c. Assisting their customers in requesting the transfer of money from Brokerage Firm X or Brokerage Firm Y to Bankers and other insurance companies.
22. From May 2005 through August 2006, Otto made both group and individual presentations to insurance agents at Bankers regarding Otto's transfer service.
23. During these presentations Otto claimed, among other things, that liquidating a customer's brokerage account through Otto's transfer service:
  - a. was less costly;
  - b. would take a shorter time; and

- c. would involve less paperwork than going through a full service brokerage firm.
24. Packets for Otto's transfer service were maintained at the front of the office at Banker's branch office located in Overland Park, Kansas. These packets, which Otto had developed, contained all the forms needed to open an account with Brokerage Firm X and to transfer securities the customer already held to a new account. Insurance agents of Bankers obtained a packet and assisted their customers with the completion of the forms in the packet. The insurance agents gave the completed forms to Otto, and Otto established the accounts at Brokerage Firm X or Brokerage Firm Y, pursuant to his limited trading authorities.
  25. In an on-the-record statement, Otto stated that thirty to thirty-five (30-35) Bankers insurance agents used Otto's transfer service.
  26. On accounts that Otto set up with Brokerage Firm X or Brokerage Firm Y, Otto obtained limited trading authority on the account, and Otto's email was often listed on Brokerage Firm X forms in order to receive customer statements. These account documents were signed by the customer.
  27. Upon opening the account, Otto also set up an on-line account that allowed Otto to directly access the customer's brokerage account electronically.
  28. Otto used this direct on-line access to sell the securities in the brokerage account and move the money to cash.
  29. Otto executed liquidation orders and had customers sign letters to have the money from the brokerage account sent to Bankers for the purchase of an annuity or other insurance product.
  30. Agents paid Otto ten percent (10%) of the commission they received on the insurance product the customer purchased or a flat fee.
  31. From at least 2005, Otto contacted elderly investors in the Kansas City area and assisted them in selling securities in their brokerage accounts. In addition, Otto recommended to some of these investors that the investor:
    - a. consolidate their accounts at Brokerage Firm X;
    - b. reposition their 401(k)s into annuities;
    - c. liquidate mutual funds;
    - d. retain certain securities; or
    - e. purchase complex equity indexed annuities that had long surrender periods.
  32. In the on-the-record interview, Otto stated, among other things, that:
    - a. while at Bankers, he could only sell Bankers' products; and
    - b. the Bankers' annuity that Otto typically sold to customers had a guaranteed competitive interest rate for one year and then decreased to the minimum interest rate at the end of the first year.
  33. After Otto's resignation from Bankers, Otto and Hayes contacted Bankers' customers and talked to some of these customers about exchanging their Bankers' annuities to a new annuity.
  34. Approximately fifty percent (50%) of the annuities sold by Bankers' agents using Otto's transfer service were surrendered. These Bankers' customers paid surrender fees in excess of two hundred seventy thousand dollars (\$270,000).

#### **Insurance Agent Interviews**

35. The Enforcement Section conducted interviews of insurance agents that used Otto's transfer service. The interviews revealed, among other things that:
  - a. Otto gave a presentation at a branch meeting for the Hutchinson, Kansas, branch office detailing the business; and
  - b. agents in the Hutchinson branch were told that Otto was a registered securities agent at the time he was conducting the service for Bankers.

#### **I. CONCLUSIONS OF LAW**

36. The Commissioner finds Respondent transacted business in Missouri as an unregistered agent and as an unregistered broker-dealer, and that this conduct constitutes grounds to issue an order pursuant to Section 409.6-604, RSMo. (Cum. Supp. 2009).
37. The Commissioner, after consideration of the stipulations set forth above and on the consent of Respondent and the Enforcement Section, finds and concludes that the Commissioner has jurisdiction over Respondent and this matter and that the

following Order is in the public interest, necessary for the protection of public investors and consistent with the purposes intended by Chapter 409, RSMo. (Cum. Supp. 2009).

## II. ORDER

**NOW, THEREFORE**, it is hereby Ordered that:

1. Respondent is prohibited from applying as a securities agent or an Investment Adviser Representative in Missouri for five (5) years;
2. Respondent is prohibited from selling variable annuities, transacting business as an investment adviser representative or transacting business as an investment adviser in Missouri;
3. Respondent is ordered to pay ten thousand dollars (\$10,000) as the cost of this investigation. Nine thousand dollars (\$9,000) of this amount will be suspended provided Respondent is in compliance with the provisions of this Consent Order and with the Missouri Securities Act. Respondent shall send the remaining one thousand dollars (\$1,000) to the Securities Division within ten (10) days of the execution of this Consent Order;
4. For two (2) years from the execution of this document, the suspended payment in paragraph three (3) immediately above shall become payable, under operation of law, upon Respondent's failure to comply with the terms of this Consent Order or the Missouri Securities Act following reasonable notice, and such payments shall be in addition to all other penalties then available under the law;
5. Any payments under this Consent Order shall be mailed to the Enforcement Section at 600 W. Main Street, Jefferson City, Missouri 65101. All penalties will be made payable to the State of Missouri. The Secretary of State shall forward all penalties received to the state treasury for the benefit of county and township school funds as provided in Article IX, Section 7 of the Constitution of Missouri. Any payment for costs will be made payable to the Missouri Secretary of State's Investor Education and Protection Fund;
6. Respondent shall pay their own costs and attorneys' fees with respect to this matter.

### **SO ORDERED:**

WITNESS MY HAND AND OFFICIAL SEAL OF MY OFFICE AT JEFFERSON CITY, MISSOURI THIS 18<sup>TH</sup> DAY OF JANUARY, 2011.

ROBIN CARNAHAN  
SECRETARY OF STATE

(Signed/Sealed)  
MATTHEW D. KITZI  
COMMISSIONER OF SECURITIES

Consented to by:  
MISSOURI SECURITIES DIVISION

Mary S. Hosmer  
Assistant Commissioner of Securities

James E. Otto, Respondent