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**STATE OF WASHINGTON
DEPARTMENT OF FINANCIAL INSTITUTIONS
SECURITIES DIVISION**

IN THE MATTER OF DETERMINING
whether there has been a violation
of the Securities Act of Washington by:

TERRENCE R. SPRAGUE,

Respondent.

SDO - 048 - 01

Statement of Charges and Notice of Intent to Issue an
Order Suspending Registration and Imposing Fines

Case No. 01 - 04 - 149

THE STATE OF WASHINGTON TO: TERRENCE R. SPRAGUE
9962 Rainier Avenue South
Seattle, Washington 98118

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STATEMENT OF CHARGES

Please take notice that the Securities Administrator of the State of Washington has reason to believe that Respondent, Terrence R. Sprague, has violated the Securities Act of Washington by making material misrepresentations and omissions in the course of offering and/or selling callable certificates of deposit and by recommending unsuitable investments to his customers. The Securities Administrator believes that these violations justify the entry of an order suspending or revoking respondent's securities salesperson registration and imposing fines pursuant to RCW 21.20.110.

The Securities Administrator makes the following Tentative Findings of Fact:

TENTATIVE FINDINGS OF FACT

I. RESPONDENT

1. Terrence R. Sprague ("Sprague") is registered with the State of Washington as a securities salesperson. From June 10, 1998 through October 11, 1999, Sprague was employed as a registered representative of U.S. Bancorp Piper Jaffray, Inc. ("Piper Jaffray"). Piper Jaffray is a wholly owned subsidiary of U.S. Bancorp, the 9th largest financial services holding company in the United States. U.S.

1 Bancorp does business through a number of subsidiary corporations, including U.S. Bank, N.A. Piper
2 Jaffray is a registered broker-dealer of securities, and has its principal place of business in Minneapolis,
3 Minnesota. Sprague left Piper Jaffray in October 1999 and went to work for Prudential Securities in
4 Bellevue, where he is currently employed.

5 II. NATURE OF THE VIOLATIONS

6 2. This case involves the offer and sale of brokered certificates of deposit ("brokered CD's"). Brokered
7 CD's differ from regular certificates of deposit ("regular CD's") in that brokered CD's are issued by banks
8 in very large denominations. Securities broker-dealers fractionalize the brokered CD's and sell them to
9 investors in smaller denominations. Unlike regular CD's, which mature anywhere from six months to five
10 years, brokered CD's have a longer term, maturing anywhere from five years to twenty years. Brokered
11 CD's usually pay a slightly higher rate of interest than regular CD's, and offer a variety of interest rate
12 terms, including fixed, "step-up," and "step-down." With a step-down rate, the most common, a "teaser"
13 rate of interest is paid for the first one year of the CD, dropping down 1% for years two through twenty.
14 Another major difference between brokered CD's and regular CD's is that most brokered CD's are callable
15 only by the issuing bank. With regular CD's an investor can redeem, or "call," the CD at any time before
16 maturity. Most brokered CD's are also "callable CD's," in that only the issuing bank can call the CD
17 before maturity. While investors can liquidate a regular CD at any time, an investor can only liquidate a
18 callable CD before maturity if a secondary market exists. The only other manner most callable CD's can
19 be liquidated before maturity is if the investor dies or is adjudicated incompetent.
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21 3. Between August 28, 1998, and May 24, 1999, Sprague offered and sold brokered certificates of
22 deposit to at least 33 U.S. Bank customers. Eleven of Sprague's 33 customers subsequently filed
23 complaints alleging that Sprague misrepresented and/or omitted to state material facts concerning the
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1 callable CD's. Many of the complaints alleged that Sprague recommended, offered, and sold the 20-year
2 callable CD's without knowing whether the product was suitable for the investor.

3 4. Sprague, in connection with the offer and sale of the callable CD's, misrepresented or failed to
4 disclose the following information: the sales costs and commissions; the risks specific to the offering, such
5 as interest rate risk; the possible absence of a market for the CD's and the potential loss of principal if sold
6 through such market; the extent of liquidity; the frequency of interest payments; the callable feature of the
7 CD's; the fact that only the issuing bank could call the CD; the "step-down" feature of the product; and the
8 fact that early withdrawal was available only in case of the investor's death or adjudicated incompetence.

9 5. The following paragraphs provide representative examples of Sprague's business practices:

10 A. Offers and Sales to WS

11 6. WS and his wife were born in Germany in 1927 and emigrated to Canada in 1955. In 1963, they
12 moved to the United States, living and working in Seattle until 1980, when they retired to Bellingham.
13 WS owned and operated watch repair shops in both Canada and the United States, and retired with
14 pensions from Germany, Canada, and the United States paying approximately \$1,000 per month. Before
15 meeting Sprague, except for one investment in a private placement stock, WS had only invested in U. S.
16 Bank CD's and mutual funds.

17 7. In September 1998, the investment in the private placement was liquidated, returning \$150,000. On
18 or about September 21, 1998, WS, his wife, and a family friend, DS, met with Sprague at the U.S. Bank
19 branch in Bellingham to discuss investing the money. Sprague asked what their investment goals were.
20 WS responded by saying that they wanted safe, income-producing investments. WS was insistent that, in
21 light of WS's serious pre-existing medical condition, the money must be readily accessible.

22 8. Sprague then briefly described an investment in callable CD's. Sprague stated that callable CD's
23 paid a higher rate of return than their existing CD's. He said that they could withdraw their money early
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1 without penalty or difficulty. Sprague told WS that if he needed his money early, all he would need to do
2 was call Sprague, who would then return WS's funds. Sprague failed to disclose the step-down feature or
3 that an "early withdrawal" meant that the CD would have to be sold on the secondary market, entailing a
4 significant risk of loss of principal. Sprague then began to fill out papers and asked that WS sign them
5 before they were completed to "speed up the process." Sprague said that he would send WS information
6 about the investment and left for his Bellevue office with the incomplete paperwork. Sprague did not
7 provide any additional information about the CD's at that time. At the conclusion of the sales presentation,
8 WS did not understand the nature or terms of the investment Sprague had discussed.

9 9. Later that day Sprague completed the sale from his Bellevue office, selling WS two callable CD's.
10 One was a 20-year \$100,000 Provident Bank step-down callable CD first callable September 21, 1999 and
11 maturing September 21, 2018. The interest rate started at 8% interest and stepped down to a lower rate
12 after one year. The second was a 20-year \$50,000 European American Bank callable CD first callable
13 September 22, 1999 and maturing September 22, 2018. The interest rate was fixed at 6.6% interest for the
14 whole term of the investment. Contrary to Sprague's representations, neither callable CD offered a right to
15 early withdrawal except in the case of death or adjudicated incompetence.
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17 10. On WS's "New Account Form" Sprague ranked "Income" as the sole investment objective for WS.
18 Despite WS's insistence on liquidity for his investments due to his failing health, Sprague failed to record
19 liquidity as an investment objective for WS.

20 11. In early 1999, WS's pre-existing medical condition began to worsen. WS contacted Sprague and
21 asked him to sell their CD's because he needed money for medical expenses. During this conversation,
22 Sprague told WS for the first time that the callable CD's did not mature for 20 years, and that there would
23 be a significant loss of principal if WS were to sell at that time. Sprague then proposed that either WS or
24 his wife should claim to be incompetent and seek the return of their money on that basis. In May 1999,
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1 Sprague sent WS form letters addressed to the callable CD issuers seeking withdrawal of funds based on
2 incompetence. WS and his wife refused to sign the form since neither were or are incompetent.

3 12. In December 1999 Sprague asked WS to move his accounts to Prudential Securities ("Prudential"),
4 promising that if WS moved the accounts Sprague would "get them out of" the callable CD's. WS agreed
5 to transfer his accounts because he still needed the money for medical expenses. After WS transferred his
6 accounts, Sprague failed to liquidate the CD's as directed by WS. On December 11, 2000, WS filed a
7 complaint against Sprague with Prudential. Neither Prudential nor Sprague has ever responded.

8 B. Offers and Sales to DB

9 13. DB was born in 1963 in Toronto, Canada, and attended two years of college at Washington State
10 University. In 1987, he began working for Windermere Realty as a real estate agent, and started investing
11 in real property. In 1989, DB opened an Individual Management Account ("IMA") with U.S. Bancorp
12 Investments where he maintained the funds he used in his real estate investments. DB described this
13 account as a "cash savings account used to purchase real estate." Before meeting Sprague, DB's
14 investment experience consisted of investments in real property, a few stock purchases, and mutual funds
15 in his IRA.
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17 14. In early April 1998, Sprague contacted DB and announced that he was DB's new account manager.
18 Sprague asked about DB's investment objectives. By this time, DB had purchased a real estate investment
19 and management company and was working only part time for Windermere. DB explained his business
20 operations and said that he was interested in a decent return with short-term, liquid investments. DB told
21 Sprague that it was critical that the money in his IMA could be accessed within 30 to 60 days for essential
22 business operations. DB then told Sprague that he was happy with the return and liquidity of his IMA, and
23 purchased no investments through Sprague at that time.
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1 15. In the fall of 1998, Sprague called DB again and said that DB could earn a much higher rate of
2 return investing the IMA money in other products. DB reminded Sprague that his primary investment
3 objective was liquidity, and that he could not invest in any long-term instruments. Sprague said that he
4 was aware of DB's investment objectives, and that he had "just the product for him." Sprague then
5 described an investment in CD's.

6 16. Sprague said that the CD's offered a higher rate of return than the IMA, and that the investment
7 was safe, risk-free, with no early withdrawal penalties or sales fees. When BD asked about the liquidity,
8 Sprague stated that DB could liquidate the CD with "no problem," and that with two-weeks notice,
9 Sprague could liquidate the CD with no penalty. Sprague failed to disclose to BD that "liquidation" meant
10 that the CD would have to be sold on the secondary market, entailing a significant risk of loss of principal.
11 Based on Sprague's representations, DB agreed to invest \$100,000 from his IMA in the CD.

12 17. Approximately one week later, on November 27, 1998, Sprague sold DB a 20-year \$100,000
13 Provident Ohio Bank step-down callable CD, first callable by Provident on November 27, 1999, and
14 maturing November 27, 2018. The interest rate for the first year was 7.5%, "stepping down" to 6% for
15 years 2 through 20. Contrary to Sprague's representations, the callable CD did not provide for any right of
16 early withdrawal except in the case of death or adjudicated incompetence.
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18 18. On DB's "New Account Form" Sprague listed DB's investment objectives as "Safety" and
19 "Income," in that order. Sprague failed to rank liquidity at all as an investment objective, despite the fact
20 that DB had repeatedly told Sprague that the liquidity of his investments was his primary concern and
21 critical to the day-to-day operation of his business.
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1 19. DB had the opportunity to invest in an apartment building in January 1999, two months after
2 purchasing the callable CD. DB called Sprague and instructed him to liquidate the CD. Sprague refused,
3 telling DB that he should only liquidate if he needed the money immediately. DB agreed to wait since he
4 had some time before the funds were required. Two months later, in late March 1999, DB needed the
5 funds in order to take advantage of the investment opportunity. He called Sprague again and left a
6 message instructing him to liquidate the CD. DB received no return communication from Sprague and
7 assumed that Sprague was selling the CD. Sprague did not sell the callable CD, and because of the delay,
8 DB missed the investment opportunity.

9 20. On or about April 1, 1999, DB spoke with Sprague about his investment and expressed concern
10 over the lost opportunity. Sprague suggested that DB use his money market funds for real estate
11 investments. DB stated that, as he had previously told Sprague on numerous occasions, the funds that
12 were in the CD were intended for use in his real estate investments. DB then again instructed Sprague to
13 liquidate his investment.. Sprague delayed again, asking for more time to sell the CD. DB reluctantly
14 agreed, instructing Sprague to sell the CD as soon as possible.

15 21. On or about June 1, 1999, Sprague telephoned DB and told him that selling the CD would result in
16 a significant loss of principal. At no time before this conversation did Sprague disclose to DB that
17 liquidation could result in a loss of principal. In response, DB called an assistant manager at Piper Jaffray
18 who confirmed that selling the CD would result in a 15% loss. DB then contacted the manager at the
19 Bellevue branch, David Piper ("Piper"), and filed a complaint against Sprague. On November 8, 1999,
20 U.S. Bank settled with DB for \$86,493, resulting in a loss of \$16,375 to DB.
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22 C. Offers and Sales to AF

23 22. AF is an 84 year-old widow. AF had worked at Boeing before her marriage and, after her
24 husband's death in 1964, she returned to Boeing until her retirement in 1985. AF receives a \$346 in
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1 monthly pension payments from Boeing; \$1,030 in Social Security; and in 1998 was receiving
2 approximately \$300 a month in interest income from investments. Before meeting Sprague, AF had
3 invested in only treasury bills and CD's sold by U.S. Bank.

4 23. In August 1998, Sprague called AF to solicit her investment business. During that telephone call,
5 Sprague told AF that she could earn as much as \$1,000 more per year in interest income by investing in
6 callable CD's. In November 1998, at Sprague's request, AF met with Sprague at the U.S. Bank branch in
7 Seattle on Roosevelt Way. AF told Sprague that she had only invested in CD's and treasury bills, and
8 wanted her investments to generate monthly income and be available for medical bills or emergencies.
9 Sprague told AF that he "had just the thing for her." Sprague stated that a \$70,000 investment in callable
10 CD's would generate up to \$1,000 more in annual interest income for her. AF asked if she would be able
11 to get access to her money in the event of an emergency. Sprague told her that all she had to do was give
12 him three weeks notice and she would be able to get her money without difficulty. Sprague then described
13 the call feature. Sprague stated that the bank could call the certificate after one year, and at that time she
14 would have the option of taking her money out or leaving it invested. Sprague said that if AF left her
15 money in the CD after one year, she would receive a lower interest rate from then on. AF asked if the
16 product would provide monthly income. Sprague said that he could set it up so that she was paid monthly.

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18 24. On January 27, 1999, Sprague sold AF a 20-year \$65,000 LaSalle Bank step-down callable CD
19 first callable by LaSalle on February 5, 2000, and maturing on February 5, 2019. The interest rate for the
20 first year was 7.5%, "stepping down" to 6.0% for years 2 through 20. Contrary to Sprague's
21 representations, the CD provided no right of early withdrawal except in the case of death or adjudicated
22 incompetence. Additionally, contrary to Sprague's representations, the CD paid interest on a semi-annual
23 basis and had no provision for monthly interest payments.

24 25. On AF's "New Account Form" Sprague ranked "Income" as the sole investment objective for AF.
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1 Even though AF had repeatedly identified liquidity of her investments as an important objective due to her
2 health concerns, Sprague failed to rank liquidity at all as an investment objective. The \$65,000 investment
3 represented more than 50% of AF's net worth at that time.

4 26. In January 1999, AF received her account statement from Piper Jaffray. She noticed the maturity
5 date of February 5, 2019, and called Sprague for an explanation. Sprague told AF that if the bank did not
6 call the certificate then the certificate would mature on that date. AF asked if she could get her money out
7 sooner if she needed it, and Sprague repeated that she could always get her money with a few weeks notice
8 to Sprague.

9 27. In February 1999, AF received a document from Piper Jaffray entitled, "Certificates of Deposit
10 Disclosure Statement." The document indicated that she could not withdraw her money except in the case
11 of death or adjudicated incompetence. AF called Sprague for an explanation; he said that while it was true
12 that only LaSalle could call the CD, she could get her money in an emergency. AF asked Sprague why she
13 had not gotten an interest payment that month. Sprague told her that the LaSalle CD only paid interest
14 semi-annually, not monthly as he had represented.

15 28. After her conversation with Sprague, AF read a series of articles describing problems with the
16 marketing of callable CD's, and determined that such an investment was unsuitable for her and elected to
17 liquidate. In October 1999, AF received a letter from Piper Jaffray informing her that Sprague had left
18 Piper Jaffray, and that her account would be handled by John H. Gonnason ("Gonnason"). On or about
19 January 11, 2000, AF called Gonnason and told him that she wanted to take her money out on the call
20 date, February 5, 2001. Gonnason explained that the CD was only callable by LaSalle, and that if she
21 wanted to liquidate the CD it would result in a loss of principal of approximately \$16,000.
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23 29. AF complained to Sprague's supervisor at the Bellevue branch office, David Piper, who referred
24 her to the home office in Minnesota. On March 27, 2000, AF complained in writing to Piper Jaffray. On
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1 February 27, 2001, AF was diagnosed with cancer. In April 2001, in order to pay for her medical
2 expenses, AF sold the LaSalle callable CD at a loss of \$4,550, recovering just \$60,450 of her principal.
3 After paying her medical expenses, AF returned the balance of her money to CD's.
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5 Based upon the foregoing Tentative Findings of Fact, the following Conclusions of Law are made:

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7 **CONCLUSIONS OF LAW**

8 1. The offer and/or sale of callable CD's by Respondent Sprague constitutes the offer and/or sale of
9 securities as defined in RCW 21.20.005 (10) and (12).

10 2. The offer and/or sale of said securities was made in willful violation of RCW 21.20.010 because
11 Respondent made untrue statements of material fact and omitted to state material facts necessary in order
12 to make the statements made, in light of the circumstances under which they were made, not misleading.

13 3. Respondent Sprague has willfully violated RCW 21.20.702 by failing to make reasonable efforts to
14 obtain information from clients necessary to make suitable recommendations, and by recommending the
15 purchase and sale of securities to his customers without reasonable grounds to believe that such
16 transactions were suitable for those customers.

17 4. Willful violations of RCW 21.20.010 and RCW 21.20.702 provide grounds, under RCW
18 21.21.110(1)(b), for the revocation of Respondent Sprague's securities salesperson's license.
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21 **NOTICE OF INTENT TO SUSPEND REGISTRATION**

22 Pursuant to RCW 21.20.110(1), and based upon the above Tentative Findings of Fact and Conclusions
23 of Law, the Securities Administrator intends to order that Respondent Sprague's securities salesperson
24 registration be suspended for six months.
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NOTICE OF INTENT TO IMPOSE FINES

Pursuant to RCW 21.20.110(3), and based upon the above Tentative Findings of Fact and Conclusions of Law, the Securities Administrator intends to order that Respondent Sprague shall be liable for and pay a fine in the amount of Fifty Thousand Dollars (\$50,000).

AUTHORITY AND PROCEDURE

This STATEMENT OF CHARGES AND NOTICE is entered pursuant to the provisions of RCW 21.20.110 and is subject the provisions of RCW 21.20.120 and Chapter 34.05 RCW. Respondent Terrence R. Sprague may make a written request for a hearing as set forth in the NOTICE OF OPPORTUNITY TO DEFEND AND OPPORTUNITY FOR HEARING accompanying this order. If the respondent does not request a hearing, the Securities Administrator will make the foregoing Tentative Findings of Fact and Conclusions of Law permanent and enter an order suspending Sprague's securities salesperson registration for six months and imposing the \$50,000 fine.

DATED this 1st day of August 2001.



DEBORAH R. BORTNER
Securities Administrator

Approved by:

Presented by:

Michael E. Stevenson
Chief of Enforcement

Anthony W. Carter
Securities Examiner