

**BEFORE THE SECURITIES COMMISSIONER
STATE OF KANSAS**

In the Matter of:

PROFESSIONAL INVESTMENT SERVICES, INC.,
DON H. EHLING, and JOHN J. ORTH,

Docket No. 09E017
KSC Case No. 2009-5517

Respondents.

_____/

A proceeding pursuant to K.S.A. 17-12a412.

**NOTICE OF INTENT TO IMPOSE ADMINISTRATIVE SANCTIONS
UNDER THE KANSAS UNIFORM SECURITIES ACT**

Staff for the Office of the Securities Commissioner of Kansas, by and through Rick A. Fleming, General Counsel, allege that sufficient evidence exists to provide cause under K.S.A. 17-12a412 to invoke administrative sanctions against Respondents Professional Investment Services, Inc., Don H. Ehling, and John J. Orth. If the allegations set forth below are found to be true, through either administrative adjudication, failure of the Respondents to make a timely request for hearing, or default of the Respondents, it is the intention of staff to seek an order from the Commissioner to impose administrative sanctions upon the Respondents under the Kansas Uniform Securities Act, K.S.A. 17-12a412. Such sanctions may include, *inter alia*, a censure, a civil penalty up to \$25,000 per violation, and suspension or revocation of registration.

If the Respondents wish to contest the allegations set forth below, or offer evidence and arguments to mitigate the allegations, then the Respondents must file a request for hearing within 33 days after the date of mailing on the Certificate of Service attached to this notice. The request for hearing must be in the manner and form prescribed by K.A.R. 81-11-3 and 81-11-5, and it must be filed with the Office of the Securities Commissioner, 618 S. Kansas Avenue, Topeka,

Kansas 66603. The request for hearing must be verified under oath by the Respondents, and if the Respondents dispute any of the allegations set forth below, the Respondents shall specifically deny those allegations or the allegations will be deemed admitted by the Respondents. If the allegations are properly disputed, the matter will be set for a hearing to be conducted in accordance with the Kansas Administrative Procedures Act. If a request for hearing is not timely filed, the Commissioner may issue a final order without further proceedings.

In support of such action, staff for the Office of the Securities Commissioner allege and state:

I. Allegations of Fact

1. Respondent Professional Investment Services, Inc., CRD No. 13703, is a business located at 800 Main Place, Suite 301, Winfield, Kansas 67156. The Respondent has been registered as a broker-dealer in the State of Kansas since September 1, 1983. The Respondent is an introducing firm, employing seven registered persons.
2. Respondent Don H. Ehling, CRD No. 76203, is the chief compliance officer and principal for Professional Investment Services, and he has been registered as an agent in association with the firm since 1983. His address is [REDACTED].
3. Respondent John J. Orth, CRD No. 353590, has been registered as an agent in association with Respondent Professional Investment Services since 1984. His addresses as listed on the CRD are [REDACTED] and [REDACTED].
[REDACTED].

A. Prior Deficiencies and Disciplinary History

4. In 1999, the Office of the Securities Commissioner brought an administrative action against Respondents Ehling and Professional Investment Services for employing an unregistered

agent and failure to supervise the agent. The firm was fined \$2,500, Respondent Ehling was censured, and both Respondents were ordered to cease and desist from associating with unregistered agents.

5. On April 18, 2001, staff for the Office of the Securities Commissioner conducted a compliance inspection of Professional Investment Services. As a result of the examination, staff issued a letter on May 23, 2001, which identified the following deficiencies:

- a. The firm's Form BD stated that the firm was a corporation in which a majority of shares were owned by Ehling. However, the firm's corporate status had been forfeited in 1997 and the firm's stock records showed that another individual was the majority owner.
- b. Many discretionary trading authorization forms were several years old, and two accounts lacked proper trading authorization.
- c. The firm was sharing storage space with a CPA firm, which would violate the Gramm-Leach-Bliley Act's (GLBA) safeguarding requirements when they went into effect on July 1, 2003.
- d. The firm's check-writing procedures were inconsistently followed, and the procedures permitted agents to hand deliver checks to customers without obtaining the customers' signatures or to deposit checks directly into customers' bank accounts.
- e. The firm failed to maintain evidence of an annual compliance meeting attended by its agents.
- f. The Form U-4 of at least three agents failed to disclose outside business activities.
- g. Two agents were registered with the firm but were no longer working at the firm.

6. On July 11, 2001, Respondent Ehling responded to the alleged deficiencies as follows:

- a. Ehling stated that a form for reinstatement of the corporate status had been received from the Secretary of State and that the papers were in the process of being completed for reinstatement.
- b. The two agents who possessed discretionary authority were told to obtain new trading authorization forms immediately.
- c. The firm had sent out privacy notices in accordance with GLBA and had moved its files to a storage area that could not be accessed by other businesses.

- d. The check disbursement policies were in the process of being updated to better document the payment of funds to customers.
 - e. The annual compliance meeting records were simply lost.
 - f. All Form U-4's were being reviewed to ensure complete disclosure of outside business activities. Ehling also stated, "It should be noted that certain representatives show multiple employment activities but this information needs to be updated in a timely manner and reviewed and noted on at least an annual basis."
 - g. The firm was processing U-4 terminations for the two inactive agents.
7. A review of CRD records for Respondents Ehling and Professional Investment Services reveals a series of disciplinary actions against the Respondents by NASD/FINRA between 2002 and 2007.
- a. On October 22, 2002, Respondent Professional Investment Services was fined \$5,000 by NASD/FINRA for failing to file an audited annual report for 2001.
 - b. On September 28, 2004, Respondents Ehling and Professional Investment Services were censured and fined \$22,500 (jointly and severally) for failing to file audited annual reports for 2002 and 2003, failing to maintain minimum net capital, and failing to prepare accurate net capital computations.
 - c. On September 2, 2005, Respondents Ehling and Professional Investment Services were censured and fined \$12,500 (jointly and severally) for failing to file an audited annual report for 2004.
 - d. On September 4, 2007, Respondents Ehling and Professional Investment Services were fined \$15,000 (jointly and severally) for failing to file an audited annual report for 2006; in addition, the firm was censured, and Respondent Ehling was suspended from acting in any principal capacity for 10 business days and was required to re-qualify as a financial and operations principal (series 28) within 90 days.
8. In 2006, the United States Securities and Exchange Commission conducted a compliance examination of Professional Investment Services. Based upon the examination, a deficiency letter was issued on December 18, 2006 (revised May 8, 2007), and it noted the following deficiencies:

- a. The firm had failed to adopt adequate safeguarding policies and procedures, and had therefore failed to correct a deficiency identified earlier by the NASD.
 - b. The firm failed to provide some customers a copy of records that contained all of the customers' suitability information and all of the required disclosures.
 - c. The firm failed to maintain suitability information for seven customers.
 - d. The firm failed to comply with the anti-money laundering (AML) requirements by failing to properly verify the identification of customers and failing to check new customers' names against government lists.
 - e. The firm failed to properly update Form U-4 to disclose two agents' outside business activities.
 - f. The firm failed to follow generally accepted accounting principles, which had the effect of overstating its assets by \$6,000.
 - g. The firm failed to establish written supervisory procedures to preserve inter-office communications related to its securities business.
 - h. The firm had policies that prohibited agents from using outside email addresses for business purposes, but the policies were not enforced.
 - i. Ehling's trades were not reviewed or approved by a supervisor.
 - j. The firm failed to update its written supervisory procedures in a timely manner.
9. On January 17, 2007, Respondent Ehling responded to the SEC's deficiency letter as follows:
- a. The firm had adopted numerous safeguarding policies and procedures in March, 2006, but those procedures had not been incorporated into the firm's written supervisory procedures.
 - b. The failure to provide some customers with suitability information and all of the required disclosures was due, in part, to the loss of two employees, and the firm has corrected the problems.
 - c. Ehling recently gave compliance training to his agents and re-emphasized the need to properly record suitability information on new account forms.
 - d. Ehling also covered the AML requirements during his compliance training.

- e. The Form U-4's had been corrected to properly disclose outside business activities. "Also, it is being reviewed at what stage of the process the breakdown occurred as there was information filled out by the representatives as to the disclosure of that information."
- f. An accounting adjustment had been made to bring the firm's financial statements into conformity with generally accepted accounting principles.
- g. The firm "was at the least attempting to comply with the intent of" the rules requiring preservation of inter-office communications.
- h. During the firm's compliance meeting, agents were instructed not to communicate with customers via email and to use only their business email address for business correspondence.
- i. Ehling believed that the NASD examiner had implied during the earlier examination that his trades were not really subject to supervisory review because his activities were reviewed by NASD, but he had corrected this misunderstanding by assigning other agents to review and approve his trades on a daily basis.
- j. The firm challenged the examiner's conclusion that it failed to update its written supervisory procedures in a timely manner.

B. Current Recordkeeping Deficiencies

10. On November 5, 2008, staff for the Office of the Securities Commissioner conducted a compliance inspection of Professional Investment Services. During the on-site examination and later investigation, staff determined that the following facts were true as of November 5, 2008, or as of the dates indicated:

- a. According to the Office of the Secretary of State, Professional Investment Services never filed the required documentation to reinstate its corporate status after it was forfeited in 1997, notwithstanding Respondent Ehling's representations that he would do so after the examination by the Office of the Securities Commissioner in 2001. Furthermore, the firm never filed an amended Form BD to reflect the change in type of business, going from a corporation to a sole proprietorship or partnership.
- b. A one-third owner of the firm, Morlyn Barrett, died over two years ago. Mr. Barrett died without a will and his estate is going through probate. The firm failed to file an amendment to Form BD listing the estate as an owner and removing Mr. Barrett.

- c. Two agents of the firm have outside business activities that are not recorded on the CRD. This includes one agent, Mike Sampson, whose outside business activities were not properly disclosed on the CRD during the examination by the Office of the Securities Commissioner in 2001 and the examination by the SEC in 2006. Respondent Ehling told the examiner for the Office of the Securities Commissioner in 2001 that the problem would be corrected for this individual, and he told the SEC examiner on January 17, 2007 that the problem had been corrected.
- d. A review of the firm's order tickets prepared during August, September, and October of 2008 reveals that the firm has not been recording time of receipt and/or time of entry on any of the order tickets written during the period in question. The firm conducted a preliminary review of this matter and advised that it had not been recording times on its order tickets for at least two years. The firm is able to determine time of entry of an order based on data it can recover from the clearing firm, but it remains unable to document time of receipt. Despite Respondent Ehling's assertions to the NASD on June 2, 2006 that he had taken steps to resolve deficiencies in the firm's order tickets, many of the order tickets in the sampling were found to be incomplete by failing to list items such as date received, client's name and/or account number, the name and/or number of the registered representative that took the order, whether the order was solicited or unsolicited, and whether payment was by cash or margin. The firm's written procedures require (on page 40) that order tickets be completed in full and (on page 119) that Respondent Ehling, as Chief Compliance Officer, review "books and records" daily, but Respondent Ehling failed to conduct such reviews to the extent necessary to identify the ongoing deficient practices.
- e. A sampling of the firm's checks received and forwarded blotter for 2008 revealed that the firm failed to record at least one check on the checks received and forwarded blotter. The sampling also determined that the firm is accepting checks that were made payable solely to the firm instead of the clearing firm. The sampling further revealed that the firm is accepting checks made payable in the client's name which were endorsed and left with the firm for forwarding to the clearing firm. The receipt of client checks made payable to the firm or endorsed in such a way that the firm could obtain possession of the funds constitutes "custody" as defined by K.A.R. 81-14-9.
- f. The firm is not maintaining an up-to-date non-clearing firm trade blotter and does not have written procedures requiring all transactions away from the clearing firm to be listed on the non-clearing firm trade blotter. At the time of the inspection, the firm provided to Reporting Examiner, a copy of a non-clearing firm trade blotter dated "2006." The last entry on that record is March 22, 2006. However, the firm has had numerous transactions since the last entry that should have been listed on the non-clearing firm trade blotter, including transactions entered personally by Respondent Ehling.

- g. The firm has failed to update client information in connection with determining suitability on non-clearing firm accounts at least once every three years. The firm in its arrangement with its clearing firm sends out an annual notice each year requesting that customers review the financial information on file for the given client and return the form or contact the firm regarding items needing changes. However, the firm does not have a written procedure that addresses the manner and timing for providing non-clearing firm clients with an opportunity to update information from which a suitability determination can be made.
- h. The firm's written supervisory procedure manual contains the following errors and omissions:
- Page 7. In the section entitled "Know Your Customer/Customer Account Opening Reviews," the manual does not specifically address a regulatory requirement that the firm contact its clients no less than every 36 months to update account information.
 - Page 19. The manual does not address the ongoing state registration status of its registered representatives or the firm. A preliminary review of the firm's CRD registration shows that the firm is registered in California, Colorado, Kansas, Missouri, and Oklahoma, but the firm is also servicing clients in Arizona and New Mexico. A review of the state registrations associated with the individuals of the firm shows that representatives of the firm are registered in Kansas, Oklahoma, and Missouri, but none of the representatives are registered in California or Colorado. Since the registration requirements can vary state-to-state, the firm should institute a procedure requiring a state-by-state assessment to determine if it and its representatives are subject to registration in a given state.
 - Page 32. The manual states that clients may view the firm's Privacy Notice at www.firstassetfinancial.com. This web address is not that of the firm, but of an unaffiliated broker-dealer.
 - Page 104. The manual does not specifically address the sale of Class C share mutual funds, even though the sale of Class C share mutual funds makes up a sizeable portion of the firm's overall mutual fund activity. Furthermore, the firm does not have any internal disclosure form that addresses the expense difference between that of Class C share mutual funds versus Class A or B share mutual funds.

C. Other Current Violations

11. The firm has written procedures that specifically prohibit a representative from signing a client's name to a document, whether authorized or not. However, during the on-site examination on November 5, 2008, the examiner for the Office of the Securities Commissioner discovered in a client file a set of instructions to photocopy a blank form containing the customer's signature in order to make IRA distributions upon request. According to the agent assigned to the account, the customer needed repeated withdrawals for a remodeling project and lived 40 miles from the firm, so the signed blank form was a convenience that enabled the customer to request funds without coming into the office. The form bearing his signature was used and not copied as instructed, so the agent began manually signing on behalf of the client whenever the customer requested funds.
12. Respondents Professional Investment Services and Ehling failed to detect and prevent the agent's practice of using photocopied and forged signatures.
13. An inspection of the firm's client files revealed that Respondent Orth was the representative for 26 clients who owned 49 accounts that contained mutual funds from Pimco Mutual Funds/Allianz Mutual Funds. These accounts are highly concentrated in Class C share mutual funds. As of September 30, 2008, the total value of the accounts at Allianz was \$2,371,176. A review of the individual mutual fund share classes revealed that 92.53 percent of the total was invested in Class C share mutual funds, 5.81 percent was invested in Class A share mutual funds, and 1.66 percent was invested in Class B share mutual funds.
14. The review of mutual fund holdings by Respondent Orth's customers indicates that some of these accounts may have been eligible for breakpoints (reduced sales charges) had Class A share mutual funds been purchased versus Class C share mutual funds. Additionally, several of the accounts are qualified accounts (IRAs) which by nature require long-term investments

and generally are not suitable for Class C share mutual funds given that Class C was designed for trading less than 3-5 years.

15. On January 9, 2009, an examiner for the Office of the Securities Commissioner spoke with Respondent Orth and Respondent Ehling regarding the use of Class C share mutual funds. Respondent Orth said that approximately twelve to fifteen years ago the firm had him cease charging an ongoing fee of one percent annually based on the assets under management to clients that were invested in no-load mutual funds because he was not properly licensed to charge such a fee. Orth explained that about that time the mutual fund companies began offering Class C shares, and that the compensation for Class C shares was similar to his former arrangement involving no-load mutual funds, so he began offering them instead. He acknowledged, based on the number of years that he has been in the business, that Class C share mutual funds are not suitable for a long-term investor. His recommendation for Class C share mutual funds were not driven by the clients' unwillingness to pay a sales charge at the time of purchase.
16. Respondents Professional Investment Services and Ehling failed to detect the level of Class C share mutual fund sales activity by Respondent Orth or to adopt sufficient written procedures that would have prevented it.

II. Allegations of Law

1. Respondent Professional Investment Services failed to promptly file an amendment to Form BD to disclose a change in its type of business entity, to-wit: changing from a corporation to a sole proprietorship or partnership, in violation of K.A.R. 81-3-1(b)(4).
2. Respondent Professional Investment Services failed to promptly file an amendment to Form BD to disclose a change in its ownership or control, in violation of K.A.R. 81-3-1(b)(4).

3. On two occasions, Respondent Professional Investment Services failed to promptly file an amendment to Form U-4 for its agent when there was a material change in the outside business activities of the agent, in violation of K.A.R. 81-3-1(c)(4).
4. By accepting incomplete order tickets, Respondent Professional Investment Services failed to maintain and preserve records in compliance with SEC rule 17a-3(a)(6)(i), in violation of K.A.R. 81-3-7(c).
5. By failing to record a check on the checks received and forwarded blotter, Respondent Professional Investment Services failed to maintain and preserve records in compliance with SEC rule 17a-3(a)(1), in violation of K.A.R. 81-3-7(c).
6. By failing to maintain an up-to-date non-clearing firm trade blotter, Respondent Professional Investment Services failed to maintain and preserve records in compliance with SEC rule 17a-3(a)(1), in violation of K.A.R. 81-3-7(c).
7. By failing to update client information on non-clearing firm accounts at least once every 36 months, Respondent Professional Investment Services failed to maintain and preserve records in compliance with SEC rule 17a-3(a)(17)(i)(B), in violation of K.A.R. 81-3-7(c).
8. By maintaining an incomplete written supervisory procedure manual, Respondent Professional Investment Services failed to establish or maintain supervisory procedures that are reasonably designed to assist in detecting and preventing violations of and achieving compliance with the Kansas Uniform Securities Act, regulations, and other applicable laws and rules of self-regulatory organizations, in violation of K.A.R. 81-14-10(a)(2).
9. By failing to detect and prevent an agent's unethical practice of using photocopied and forged signatures, Respondents Ehling and Professional Investment Services failed to reasonably supervise the agent, in violation of K.S.A. 17-12a412(d)(9).

10. Respondent Orth recommended to 26 customers the purchase of Class C share mutual funds without reasonable grounds to believe that the transactions or recommendations were suitable for the customers, in violation of K.A.R. 81-3-6(e)(3).
11. By failing to detect and prevent Respondent Orth's unethical practice of making unsuitable recommendations, Respondents Ehling and Professional Investment Services failed to reasonably supervise Orth, in violation of K.S.A. 17-12a412(d)(9).
12. Adequate grounds exist under K.S.A. 17-12a412(d)(2) and (d)(9) to sanction Respondent Professional Investment Services, and such an order is in the public interest.
13. Adequate grounds exist under K.S.A. 17-12a412(d)(9) to sanction Respondent Ehling, and such an order is in the public interest. In addition, Respondent Ehling controls Respondent Professional Investment Services and may be disciplined to the same extent as Respondent Professional Investment Services pursuant to K.S.A. 17-12a412(h).
14. Adequate grounds exist to sanction Respondent Orth under K.S.A. 17-12a412(d)(13), and such an order is in the public interest.

Filed this 26th day of June, 2009.

/s/ Rick Fleming _____
Rick A. Fleming, #17127
General Counsel
Office of the Securities Commissioner
618 S. Kansas Avenue
Topeka KS 66603
(785) 296-5215
(785) 296-5482 (fax)

Certificate of Service

I hereby certify that on this 29th day of June, 2009, copies of the foregoing Notice of Intent to Impose Administrative Sanctions was mailed by certified mail, return receipt requested, properly addressed to the following:

Professional Investment Services, Inc.

800 Main Place, Suite 301
Winfield, Kansas 67156

Don H. Ehling

[REDACTED]

John J. Orth

[REDACTED]

John J. Orth

[REDACTED]

/s/ Michelle Lancaster

Michelle Lancaster

Legal Assistant