Morgan Lewis

2017 YEAR IN REVIEW: SELECT SEC AND FINRA DEVELOPMENTS AND ENFORCEMENT CASES

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Executive Summary

The Morgan Lewis Year in Review highlights key US Securities and Exchange Commission (the SEC or the Commission) and Financial Industry Regulatory Authority (FINRA) enforcement developments and cases regarding broker-dealers, investment advisers, and investment companies.*

THE SEC

In Fiscal Year 2017 (FY 2017), as well as the months since, there has been significant personnel transition at the SEC, and during this period we also have seen legal developments and changes to technology that are likely to impact how the Agency operates for many years to come.

First, the Commission composition has changed significantly; for much of FY 2017, the Commission operated with fewer than its full five members. The last time we saw this type of transition, in 2013, also resulted in a meaningful reduction in the number of enforcements actions brought, and the Enforcement Division statistics this past year reflect this disruption. Further, in addition to changes at the very top, the churn of personnel changes throughout the organization was remarkable and certainly had to impact the everyday work of the organization.

As noted, for the first time since 2013, in FY 2017, the number of Enforcement Actions brought by the Commission declined from prior years and, for the first time since 2011, the total amount of disgorgement and civil penalties ordered also declined.

The Office of the Whistleblower continues to receive more tips and complaints than ever before; in FY 2017, the Commission received almost 4,500 such tips from all over the country and around the world. However, as we analyzed the data, we found that, over time, even as the numbers of tips has increased, the percentages of those tips that actually led to the opening of an inquiry or an Enforcement investigation has actually declined. Further, with the U.S. Supreme Court's recent decision in *Digital Realty Trust, Inc. v. Somers*, 583 U.S. __ (Feb 21,

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* Morgan Lewis served as counsel in certain actions described herein. Information concerning the matters described in this outline was derived from generally available materials, including information available to the public on the websites of the US SEC and FINRA, and as otherwise expressly noted.

This outline was prepared by partners Amy J. Greer, Ben A. Indek, Jennifer L. Klass, and Christine M. Lombardo, of counsel Russell M. Fecteau, and associates Ariel Gursky, Vineeta Kamath, Olga Kamensky, Eric L. Perelman, and Zoe Phillips; with assistance from partner Michèle A. Coffey, of counsel Mary M. Dunbar, and associates Adam J. Adler, Christina M. Aylward, Kathryn Ball, Matthew T. Bohenek, Bruno Campos, Arcangelo S. Cella, Shannon A. Hayes, Jessica L. Joy, Paul J. Kim, Jonathan E. Maier, John M. Maloy, Devon Minerve, Silki Patel, Anna Sandor, Kathleen H. Shannon, Alexander Starr, Robert Thompson, Lindsey Titus, and John A. Vassallo III; and paralegals Caroline Ball and Victoria Curry. Administrative support was provided by Meredith E. Brooks and Kate Lesko.

2018), which held that, in order to be eligible for the retaliation protections afforded by the Dodd-Frank statutory regime, a putative whistleblower must report his or her concerns to the Commission, we can expect that the numbers of tips reported will increase.

The most significant focuses of the Division of Enforcement this past year have undoubtedly been the protection of Retail or "Main Street" investors and technology, including all "cyber" things, particularly cybersecurity and cryptocurrencies, like Bitcoin and other digital investment offerings. Each of these priorities have echoed throughout the entire Commission. In addition to these priorities being noted in connection with relevant Enforcement proceedings, the Division formed a Retail Strategy Task Force, intended to focus on risks that threaten individual investors, and the Cyber Unit was added to the Enforcement Unit, the first new specialized unit since the Division was reorganized in 2010.

Among the matters that the Commission brought this past year in each of these areas included, on the retail investor side, enforcement actions related to failure to disclose fees and expenses related to investment costs, failure to disclose conflicts of interest, and sales practices concerning complex and structured products; and on the "cyber" side, the Enforcement Staff brought cases concerning Initial Coin Offering (ICO) frauds and the Commission issued its first Report of Investigation Pursuant to Section 21(a) of the Exchange Act in many years, which concluded, among other things, that the digital currency at issue was, in fact, a security subject to the Commission's jurisdiction.

Finally, the Commission has been embroiled in a couple of significant litigation matters that may impact how enforcement cases are brought and the relief available to the SEC in such matters. Specifically, in *Kokesh v. Securities and Exchange Comm'n*, 137 S. Ct. 1635 (2017), the Supreme Court determined that disgorgement, as the remedy was used by the SEC, is a penalty subject to a five-year statute of limitations under 28 U.S.C. § 2462, and not merely an equitable remedy within the discretion of the district court. And the Commission's use of its administrative forum has been challenged as unconstitutional under the Appointments Clause, and that matter is before the Supreme Court for decision in *Lucia v. SEC*, No. 17-130 (U.S. Jan 12, 2018). In Lucia, the challenge relates to the fact that Administrative Law Judges (ALJ) at the Commission have been selected by the chief ALJ through an employment process assisted by the Office of Personnel Management, rather than a process involving the SEC Commissioners. As a result of the challenge to the administrative forum, throughout this past fiscal year and into the present, most unsettled matters are all being filed in federal court.

Looking ahead, we can anticipate that the SEC will continue to focus on "Main Street" investors and on technology, both in the "cyber" context, as noted, and also in how the Agency can use and leverage technology to more fully and efficiently identify violative conduct and mitigate risks in the market as a whole.

FINRA

There were several important developments at FINRA in the last year, including the launch of a new "self-evaluation and organizational improvement" initiative called FINRA360, the consolidation of two enforcement functions, modifications to the Sanctions Guidelines, and changes to the way FINRA uses fine monies.

FINRA360 is an outgrowth of the feedback that FINRA CEO Robert Cook received during his ongoing listening tour. The initiative aims to examine a number of topics, including: (i) the organization and operation of FINRA's regulatory functions; (ii) the use of data and technology; and (iii) the tools and metrics used to evaluate outcomes and successes throughout FINRA. FINRA anticipates that the initiative will be a multiyear project, focused on continuing to improve the organization, but it expects to implement changes on an ongoing basis. The most tangible result of FINRA360 to date has been the announcement in July 2017 that that FINRA would consolidate its two existing enforcement groups, Market Regulation Enforcement and the Department of Enforcement, into one new unified department. At a recent Securities Industry and Financial Markets Association Compliance & Legal Society event, Cook remarked that one of the goals in consolidating the two enforcement groups is to develop a consistent "overall philosophy" throughout Enforcement. Cook said the combination was not merely a "change in reporting lines," but was aimed at creating a unified group with the same set of principles in approaching enforcement outcomes.

In April 2017, FINRA advised firms that its National Adjudicatory Council had made five revisions to its Sanctions Guidelines. The most significant modifications were (i) the addition of a new principal consideration that examines whether a respondent exercised undue influence over a customer; (ii) the creation of a new guideline applicable to systemic supervisory failures and firm-wide supervisory failures, rather than focusing on limited supervisory failures; and (iii) a new general principal addressing potential mitigation where sanctions or corrective action were imposed by another regulator or by a member firm, replacing what was previously Principal Consideration No. 14. FINRA also revised the existing Sanction Guidelines to change the range of sanctions relating to several violations of its rules, including, for example, violations related to the sales of unregistered securities, churning, and unauthorized transactions.

In December 2017, FINRA released its first "Report on FINRA Examination Findings." FINRA issued the report – as it will continue to do on a routine basis – to provide firms with an additional resource for complying with the securities rules and regulations. The report highlights key observations from FINRA's recent examinations, and notes certain effective practices identified by the examination staff. The report includes a section called "Highlighted Observations" in which it provides observations in the following areas: (i) cybersecurity; (ii) outside business activities and private securities transactions; (iii) anti-money laundering compliance programs; (iv) product suitability; (v) best execution; and (vi) market access controls.

In January 2018, FINRA published its first annual budget summary, which described the six Financial Guiding Principles that will inform the organization's financial planning. In explaining one of the principles, "Use Fines to Promote Compliance and Improve Markets," the Budget Summary states that, "[w]hen [FINRA] impose[s] fines, the amounts are based on the facts and circumstances of the misconduct and the principles set forth in our Sanction Guidelines; fines are not based on revenue considerations, and [FINRA] does not establish any minimum amount of fines that must be collected for purposes of [its] annual budget." The Budget Summary also states that the use of fine monies is subject to special procedures and restrictions, and is not considered in determining employee compensation and benefits. The Board's Finance Committee must authorize the use of such funds and will do so for specific purposes: capital or nonrecurring expenditures to promote effective regulatory oversight, education activities, capital or new initiatives required by changes in the law, or to replenish FINRA's reserves if necessary to preserve its ability to continue to fund operations.

Also in January 2018, FINRA published its Annual Regulatory and Examination and Priorities Letter. The 2018 Letter describes the areas FINRA intends to focus on during this year's exams. Those priorities include the by-now-standard list of issues such as financial fraud, high risk firms and advisers, net capital and reserve computations, cybersecurity, anti-money laundering, suitability, best execution, and the market access rules. Potential new areas of concern for firms include (i) business continuity planning; (ii) technology governance; (iii) short sales; (iv) initial coin offerings and cryptocurrencies; (v) use of margin; (vi) securities-backed lines of credit; and (vii) options. Areas that were not addressed in the 2018 Letter but were in prior iterations include (i) social media and electronic communications retention and supervision; (ii) municipal advisor registration; and (iii) FINRA's Audit Trail Reporting Early Remediation Initiative. The 2018 Letter also did not specifically highlight topics such as excessive or short-term trading of long-term products, outside business activities, and supervisory control testing.

As of the date of publication of this Outline, FINRA had not yet announced its 2017 enforcement statistics.

US Securities and Exchange Commission

PERSONNEL CHANGES[1]

The Commission composition changed significantly in fiscal year 2017 and into the beginning of calendar year 2018. From Mary Jo White's departure in January 2017, until the new Chair, Jay Clayton, was sworn in, a little more than three months later, in May 2017, the Commission operated with only two members, then-Acting Chair Michael S. Piwowar and Commissioner Kara M. Stein.

On May 4, 2017, Jay Clayton was sworn into office as the Chairman. Prior to joining the SEC, Mr. Clayton was a partner at Sullivan & Cromwell LLP, where he counseled corporate clients and market participants on corporate transactions, securities offerings and capital raising, mergers and acquisitions, as well as trading matters and corporate governance.

On December 22, 2017, the Senate confirmed Republican Hester Peirce as Commissioner; she was sworn in on January 11, 2018. Ms. Peirce re-joins the Commission from the Mercatus Center at George Mason University, where she has served as a Senior Research Fellow and Director of the Financial Markets Working Group. At the SEC, Commissioner Peirce has experience as a Staff Attorney in the Division of Investment Management and as Senior Counsel to former Commissioner Paul S. Atkins. Following her prior SEC service, Ms. Peirce worked for U.S. Senator Richard Shelby on the Senate Committee on Banking, Housing, and Urban Affairs. Commissioner Peirce's term expires June 5, 2020.

Also On December 22, 2017, the Senate confirmed Democrat Robert J. Jackson Jr. as a Commissioner, and he, too, was sworn in on January 11, 2018. Commissioner Jackson joins the SEC from the NYU School of Law; previously, he had been a professor of law at Columbia Law School. Commissioner Jackson's term will expire June 5, 2019.

As set forth below, there were some changes in key Commission Staff positions during fiscal year 2016.

On May 11, 2017, Lucas Moskowitz was named the Chief of Staff. Previously at the SEC, Mr. Moskowitz served as a counsel to former Commissioner Daniel Gallagher and as an attorney in the Division of Enforcement. Mr. Moskowitz also served as the Chief Investigative Counsel of the U.S. Senate Committee on Banking, Housing, and Urban Affairs and as a counsel on the Financial Services Committee of the U.S. House of Representatives.

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[1] Unless otherwise noted, the information regarding these personnel changes was drawn from SEC Press Releases available on the Commission's website.

On May 15, 2017, Sean Memon was named the Deputy Chief of Staff. Immediately prior to joining the SEC, Mr. Memon practiced law at Sullivan & Cromwell LLP, where he advised clients in regulatory and transactional matters.

On May 15, 2017, Jaime Klima was named Chief Counsel to Chairman Jay Clayton. In her new role, Ms. Klima will be senior legal and policy adviser, and will coordinate the rulemaking agenda of the SEC. She will also serve as the Chairman's representative on the Deputies Committee of the Financial Stability Oversight Council. Ms. Klima previously served as SEC co-Chief of Staff under then-Acting Chairman Michael S. Piwowar and counsel to Commissioner Piwowar and Commissioner Troy A. Paredes.

On May 15, 2017, Robert B. Stebbins was named General Counsel. Mr. Stebbins was a partner at Wilkie Farr & Gallagher LLP, where he focused on corporate transactions, such as mergers and acquisitions, private equity and venture capital, investment funds, and capital market transactions.

On May 25, 2017, Peter Uhlmann was named the Managing Executive in the Office of Chairman Jay Clayton. Mr. Uhlmann will advise Chairman Clayton in matters relating to agency administration, operations, and management, and will serve as the Chairman's primary liaison to divisions and offices on these matters. Mr. Uhlman has served in a variety of senior leadership positions during his tenure at the SEC; most recently, serving as managing executive for then-Acting Chairman Michael S. Piwowar.

On July 18, 2017, the SEC announced that Christopher Hetner will continue to serve as Senior Advisor to Chairman Jay Clayton for Cybersecurity Policy, having previously served in this role under Chair Mary Jo White and Acting Chairman Michael Piwowar. Mr. Hetner will continue to coordinate efforts across the agency to address cybersecurity policy, engage with external shareholders, and help enhance the SEC's mechanisms for assessing cyber-related market risk.

On August 31, 2017, Chairman Jay Clayton named his executive staff:

- John Cook was named Senior Advisor on matters involving the Division of Investment Management, Division of Economic and Risk Analysis, and Office of the Chief Accountant, and on enforcement matters. Mr. Cook has been with the SEC since 2010, in a variety of roles at Division of Economic and Risk Analysis, and Office of the Chief Accountant, and serving as counsel to former Commissioner Gallagher.

- Jeffrey Dinwoodie was named Senior Advisor on matters involving the Division of Trading and Markets, Office of Compliance Inspections and Examinations, Office of Municipal Securities, and Office of Credit Ratings, and on enforcement matters. Mr. Dinwoodie rejoined the SEC, where he had served from 2008-2011 in the Division of Trading and Markets, from Davis Polk & Wardwell LLP, where he advised clients on a variety of regulatory and enforcement issues.

- Raquel Fox was named Senior Advisor on matters involving the Division of Corporation Finance and Office of International Affairs, and on enforcement matters. Ms. Fox joined

the SEC in 2011 and has served as Senior Special Counsel to the Director of the Division of Corporation Finance and an attorney fellow in the offices of Capital Markets Trends and Rulemaking.

- Kristina Littman is the Senior Advisor on matters involving the Division of Enforcement, and other regulatory and policy matters. Ms. Littman joined the SEC in 2010 and has served in the Division of Enforcement as an investigative and trial attorney.

- Alan Cohen is the Senior Policy Advisor on emerging risks and regulatory developments, including Brexit impact and other European Union regulatory matters, as well as domestic and international clearing and settlement of securities and derivatives. Mr. Cohen joins the Commission from Goldman Sachs, where he was, most recently, an advisor to the executive office.

- Christopher Carofine is the Director of Communications, advising on all matters related to communications and media relations. Mr. Carofine most recently served as the Communications Director for House Rep. Scott Garrett.

- Shelby Begany Telle was named Confidential Assistant to Chairman Clayton; prior to joining the SEC, Ms. Telle worked on Capitol Hill.

On December 14, 2017, Kenneth A. Johnson was named the agency's Chief Operating Officer after serving as Acting COO since February 2017. Mr. Johnson previously served as Chief Financial Officer of the SEC and Chief Management Analyst within the former Office of the Executive Director. Before joining the SEC, Mr. Johnson served as an analyst for the Congressional Budget Office.

DIVISION OF ENFORCEMENT

On June 8, 2017, Stephanie Avakian and Steven Peikin were named Co-Directors of the Division of Enforcement, succeeding Andrew J. Ceresney who left the SEC at the end of 2016. Ms. Avakian previously served as Acting Director of the Division of Enforcement and Deputy Director of the Division. Prior to joining the SEC, she was a partner at Wilmer Cutler Pickering Hale & Dorr LLP and the vice chair of their securities practice. Steven Peikin is a former federal prosecutor who, most recently, was Managing Partner of Sullivan & Cromwell's Criminal Defense and Investigations Group.

On September 7, 2017, Bridget Fitzpatrick was named the Chief Litigation Counsel, succeeding Matthew C. Solomon who left the SEC in December 2016. David Gottesman will continue to serve as the Deputy Chief Litigation Counsel. Ms. Fitzpatrick will oversee the SEC's national litigation program and Mr. Gottesman's responsibilities include oversight of all trial lawyers in the SEC's headquarters. Ms. Fitzpatrick and Mr. Gottesman had served as Co-Acting Chief Litigation Counsel and both Ms. Fitzpatrick and Mr. Gottesman previously served as supervisors in the SEC's Enforcement Division.

Other significant personnel changes in the Division of Enforcement include:

On October 14, 2016, Melissa Hodgman was named Associate Director in the SEC's Enforcement Division, succeeding Stephen L. Cohen, who left the SEC in June. Previously, Ms. Hodgman served as Assistant Director of the Market Abuse Unit of the Enforcement Division.

On January 19, 2017, Jennifer A. Diamantis was named Chief of the Enforcement Division's Office of Market Intelligence, replacing Vicente L. Martinez. Ms. Diamantis joined the SEC in September 2016 as Deputy Chief of the Office of Market Intelligence. Prior to that, she served in the CFPB's Division of Research, Markets, and Regulations; the FDIC's Enforcement Section; and the CFTC's Division of Enforcement.

On November 2, 2017, Charles E. Cain was named the Chief of the Enforcement Division's specialized Foreign Corrupt Practices Act Unit after serving as Acting Chief since April 2017. Mr. Cain has over 15 years of experience investigating FCPA matters, most recently as Assistant Director of the FCPA Unit.

On December 7, 2017, Daniel Michael was named the Chief of the Enforcement Division's Complex Financial Instruments Unit. Mr. Michael previously served as an Assistant Director based in the New York Regional Office.

SEC REGIONAL OFFICES

New Senior Staff was appointed in four of the SEC's 11 regional offices:

Atlanta Regional Office:
Richard Best – Regional Director
Donna Esau – Associate Regional Director for Examinations

Chicago Regional Office: Kathryn A. Pyszka – Regional Director

Fort Worth Regional Office: Jessica B. Magee – Regional Director

Los Angeles Regional Office: John W. Berry – Associate Regional Director for Enforcement

New York Regional Office:
Marc P. Berger – Regional Director
Thomas J. Butler – Associate Regional Director for Examinations

Philadelphia Regional Office:
G. Jeffrey Boujoukos – Regional Director
Kelly L. Gibson – Associate Regional Director for Enforcement

DIVISION OF CORPORATION FINANCE

On May 9, 2017, William H. Hinman was named the director of the Division of Corporation Finance, succeeding Keith F. Higgins who left the SEC in January 2017. Previously, Mr. Hinman was a partner at Simpson Thacher & Bartlett LLP, where he advised a wide range of issuers and underwriters on capital-raising transactions and corporate acquisitions.

On June 20, 2017, Robert Evans III was named Deputy Director in the Division of Corporation Finance, where he will join Shelley Parratt, who will also continue in that role. Most recently, Mr. Evans worked as a partner at Shearman & Sterling LLP, in that firm's capital markets practice.

DIVISION OF ECONOMIC RISK ANALYSIS

On August 31, 2017, Dr. Jeffrey H. Harris was named Director of the SEC's Division of Economic and Risk Analysis, succeeding Mark Flannery. Dr. Harris most recently served as professor at Kogod School of Business at American University.

On January 11, 2018, Dr. Timothy Timura was named Deputy Director and Deputy Chief Economist of the Division of Economic and Risk Analysis. Most recently, Dr. Timura was an Executive in Residence at the Kogod School of Business and American University and he has previously taught finance and economics at other institutions. Dr. Timura's initial focus will be economic policy in agency rulemaking.

Previously, on December 12, 2016, Dr. Narahari Phatak was named Associate Director for Policy in the Division of Economic and Risk Analysis. Dr. Phatak has served DERA since 2012 in a variety of roles.

DIVISION OF INVESTMENT MANAGEMENT

On August 31, 2017, Dalia Blass was named Director of the SEC's Division of Investment Management, succeeding David W. Grim. Ms. Blass returns to the SEC after previously serving in a number of leadership roles in the division of Investment Management, including Assistant Chief Counsel. Most recently, Ms. Blass worked at Ropes & Gray LLP where she advised on a broad range of investment fund, private equity, and regulatory matters.

On November 20, 2017, Paul G. Cellupica was named Deputy Director of the SEC's Division of Investment Management. Most recently, Mr. Cellupica was Managing Director and General Counsel for Securities Law at Teachers Insurance and Annuity Association of America. Prior to that he was Chief Counsel for the Americas at MetLife, Inc. He has also served with the SEC in a number of capacities, including as Assistant Director in the Division of Investment Management.

Other significant personnel changes in the Division of Investment Management include:

On December 22, 2016, Sara P. Crovitz was named Deputy Chief Counsel and Associate Director in the Division of Investment Management's Chief Counsel's Office. In her new role, Ms. Crovitz will focus on collaboration between the Chief Counsel's Office and other offices within the Division of Investment Management and in the Commission. Ms. Crovitz first joined the SEC in 1996 and, since that time, has served in a variety of roles, first joining the Division of Investment Management in 1999.

On December 22, 2016, Timothy Husson was named Associate Director in the Division of Investment Management's Risk and Examinations Office. Dr. Husson joined the Commission staff in 2014, bringing his skills as a quantitative analyst and financial analyst, and he has served in a variety of roles.

DIVISION OF TRADING AND MARKETS

On October 18, 2017, Brett Redfearn was named Director of the Division of Trading and Markets. Mr. Redfearn joins the SEC from J.P. Morgan, where he was Global Head of Market Structure for the Corporate & Investment Bank. Earlier in his career, Mr. Redfearn ran Business Strategy and Equity Order Flow at the American Stock Exchange. He has also served on the boards of Bats Global Markets, the Chicago Stock Exchange, BIDS Trading, and the National Organization of Investment Professionals.

Previously, on October 6, 2016, David H. Saltiel was named to head the Office of Analytics and Research in the Division of Trading and Markets. Before joining the SEC, Mr. Saltiel was Chief Economist at the Municipal Securities Rulemaking Board and, prior to that, he served as Chief Financial Economist and Director of Data Management and Analytics at the U.S. Treasury Department's Bureau of the Fiscal Service.

OFFICE OF COMPLIANCE INSPECTIONS AND EXAMINATIONS

On October 26, 2017, Peter B. Driscoll was named Director of the SEC's Office of Compliance Inspections and Examinations (OCIE) after serving as Acting Director since 2017. Previously, Mr. Driscoll served as OCIE's first Chief Risk and Strategy Officer and OCIE's Managing Executive.

On June 15, 2017, Keith E. Cassidy was named Associate Director of the Technology Controls Program in the OCIE. Mr. Cassidy previously served as Director of the office. Earlier in his career, he was Chief of Staff and Counsel at the Department of Justice's Office of Legislative Affairs.

OFFICE OF THE CHIEF ACCOUNTANT

On November 22, 2016, Wesley R. Bricker was named Chief Accountant after serving as Interim Chief Accountant. Prior to joining the SEC, Mr. Bricker was a partner at PricewaterhouseCooperLLP and responsible for audit engagements in the banking, capital markets, financial technology, and investment management sectors.

Other significant personnel changes in the Office of the Chief Accountant include:

On November 2, 2016, Marc A. Panucci was named Deputy Chief Accountant. Mr. Panucci will assist the Commission in its oversight responsibility for the activities of the Public Company Accounting Oversight Board. He previously served at the SEC from 2007-2010 as Senior Associate Chief Accountant and, most recently, was a partner at the national professional services group of PricewaterhouseCoopers LLP.

On March 30, 2017, Sagar S. Teotia was named Deputy Chief Accountant in the SEC's Office of the Chief Accountant. In this role, Mr. Teotia will assist in discharging the Commission's oversight of standard-setting bodies such as the Financial Accounting Standards Board. From 2009-2011, Mr. Teotia served as an SEC Accounting Fellow. He re-joins the agency from Deloitte & Touche LLP's National Office Accounting Consultation Group.

OFFICE OF LEGISLATIVE AND INTERGOVERNMENTAL AFFAIRS

On July 24, 2017, Bryan Wood was named Director of the Office of Legislative and Intergovernmental Affairs. Mr. Wood has spent a decade on Capitol Hill in various roles; most recently, Mr. Wood was Senior Advisor and Counsel at the House Financial Services Committee and he has previously served as Counsel for the Subcommittee on Capital Markets, Securities, and Investment.

ENFORCEMENT STATISTICS[2]

The statistics for the Enforcement Division's Fiscal Year 2017 evidence the significant transition occurring at the agency; the last year when we saw this much transition was 2013, when Mary Jo White brought in her team, and, that year, we also saw a dip in the total enforcement actions. In 2017, the Commission brought a total of 754 enforcement actions, comprised of 446 independent actions for securities laws violations, 196 "follow on" administrative proceedings seeking associational bars against individuals, and 112 deregistration actions against issuers that were delinquent in making required filings. Those cases represented

[2] Unless otherwise noted, the information in this section is drawn from the Commission's Division of Enforcement Annual Report, "A Look Back at Fiscal Year 2017," ("ENF Annual Report") https://www.sec.gov/files/enforcement-annual-report-2017.pdf. The SEC's fiscal year 2017 ended on September 30, 2017.

judgments and orders in excess of $3.7 billion in penalties and disgorgement. According to the Enforcement Division, $1.07 billion was returned to investors in 2017, a significant increase over prior years, but included in that figure were amounts reflecting prior years' efforts. *Id.* at 3.

The Division of Enforcement noted in its Annual Report that included within the total of 754 actions are trading suspensions in 309 companies and bars or suspensions of more than 625 individuals. *Id.* These statistics suggest, perhaps, that, this year, the Division made fewer charging decisions that, on their face, appear solely designed to inflate the end-of-year case statistics. Overall, this would comport with what also appears to be some effort at outward facing transparency, or the appearance of transparency, reflected on the Commission's website and in its overall, redesigned reporting to the public.[3]

In its Annual Report, the Enforcement Division, attributes much of the case decline to the Commission's Municipalities Continuing Disclosure Cooperation (MCDC) program, a voluntary self-reporting program that accounted for 84 of the independent actions in 2016. *Id.* at 6. Interestingly, though, if you compare the one-year drop in enforcement actions in year 2013 (a reduction of 48 cases from 2012) to that in 2017 (a reduction of 114 cases from 2016), the difference is far more significant in 2017, that is, until you consider those 84 MCDC cases.

The chart below reflects the number of cases brought by the SEC over the last decade:

Fiscal Year	Number of Enforcement Actions
2008	671
2009	664
2010	681
2011	735
2012	734
2013	686
2014	755
2015	807
2016	868
2017	754

CATEGORIES OF CASES

The major categories of independent enforcement actions and the number of those cases for fiscal year 2017 within each category follows, and we provide the 2016 numbers, as a reference.

3 *See generally* https://www.sec.gov/.

Type of Case	Number of Actions	Percentage of Total Actions	Number/Percentage in 2016
Issuer Reporting/Audit & Accounting	95	21%	93 cases/17%
Securities Offering	94	21%	90 cases/16%
Investment Advisers/ Investment Companies	82	18%	98 cases/18%
Broker-Dealer	53	12%	61 cases/11%
Market Manipulation	41	9%	30 cases/5%
Insider Trading	41	9%	45 cases/8%
Public Finance Abuse	17	4%	97 cases/18%
FCPA	13	3%	21 cases/4%
Miscellaneous	7	2%	9 cases/2%
Transfer Agent	3	1%	2 cases/0%
National Recognized Statistical Ratings Organization (NRSRO)	0	0%	2 cases/0%
TOTAL	446	100%	548 cases/100%

Given that 2017 was a big year for offering frauds, pump-and-dumps, affinity frauds, Ponzi schemes, and similar enforcement actions affecting retail investors, the fact that 30% of the cases this year are classified by the Division of Enforcement as Securities Offering or Market Manipulation cases is not at all surprising.

Also not a surprise is the continued reduction of Broker-Dealer cases, as the SEC continues to focus on more market-wide or systemic broker-dealer issues, leaving much of the rest of the broker-dealer field to FINRA. However, taken together with the Investment Adviser/Investment Company actions, the matters the SEC categorizes as involving regulated entities totaled 30% of the docket. Of course, as is always the case, broker-dealers, investment advisers, and investment companies are often involved in matters that cross into other categories.

The Enforcement Staff continues to focus on Issuer Reporting and Audit & Accounting cases and on Insider Trading cases, with very consistent results even in a down year overall. One cannot help but wonder whether data analytics hasn't played a part here. Between the DERA Office of Corporation Finance, which assists in all kinds of economic and statistical analysis, and the Enforcement Division's Market Abuse Unit's Analysis and Detection Center, which uses data analysis tools to detect suspicious trading patterns across different securities, these types of cases do play to the numbers and the SEC Staff appears to be figuring out the game.

CIVIL PENALTIES AND DISGORGEMENT ORDERS

In Fiscal Year 2017, the SEC obtained orders requiring the payment of $832 million in civil penalties and $2.957 of disgorgement. In total, this is about a 7% decline from 2016 and the first time since 2013 that the total did not top $4 billion.

Just by way of some context, the five disgorgement orders over $100 million in FY 2017 accounted for 44% of the disgorgement ordered and four of those cases are FCPA actions, with the remaining order having been entered in an offering fraud case. By comparison, in FY 2016, the six disgorgement orders over $100 million accounted for 45% of the total disgorgement ordered and three of those cases were FCPA matters, and two were offering frauds.

Fiscal Year	Penalties and Disgorgement
2008	$1.03 billion
2009	$2.435 billion
2010	$2.85 billion
2011	$2.806 billion
2012	$3.0 billion
2013	$3.4 billion
2014	$4.16 billion
2015	$4.19 billion
2016	$4.082 billion
2017	$3.789 billion

ADDITIONAL STATISTICS

Some additional statistics that may be of interest that were included in the Commission's annual financial report included the fact that the SEC's total staff numbers about 4,600 across the country.[4] According to the SEC's Annual Report, more than half of the agency's budgetary resources are invested in Commission's Enforcement and Examination programs. *Id.* at 16.

Selected Examination Statistics

In fiscal year 2017, OCIE examined 15% of registered investment advisers; 11% of registered investment companies; and, together with SROs, 48% of broker-dealers were examined. *Id.* at 42. These statistics include all types of exams. *Id.* More specific data concerning the nature and breakdown of OCIE exams can be found in the Commission's 2019 Budget request, which is set forth in the table below.[5]

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4 *See* U.S. Securities and Exchange Commission, *"Agency Financial Report, Fiscal Year 2017"* ("2017 SEC Agency Financial Report") at p. 13 (Nov. 14, 2017) https://www.sec.gov/reports-and-publications/annual-reports/sec-2017-agency-financial-report.

5 *See* U.S. Securities and Exchange Commission, *"Fiscal 2019 Congressional Budget Justification and Annual Performance Plan" ("2019 Budget Justification")* at p. 30 (Feb. 12, 2018) https://www.sec.gov/files/secfy19congbudgjust.pdf.

Type of Examination	2017 Total	2018 Estimate
Investment Adviser Exams	2114	2120
Investment Company Exams (including Administrators)	95	100
Broker-Dealer Exams	325	300
Transfer Agent Exams	57	45
Municipal Advisor Exams	83	75
Market Oversight Inspections (*e.g.*, exchanges)	115	128
Technology Controls Oversight Inspections	70	70
Clearing Agency Exams	14	11

Additional Enforcement Statistics

Although, overall, 2017 was a down year for Enforcement statistics, the Division obtained 35 court-ordered asset freezes during the fiscal year, which is up from 33 in fiscal year 2016.[6] This increase is likely a function of the increase in offering fraud, Ponzi scheme, market manipulation, and hacking cases.

Perhaps of more interest to those in the sights of the Division of Enforcement are the statistics related to open and closed investigations. Following is a table comparing data for the last five fiscal years. The Enforcement Staff continues to have a healthy number of open investigations to begin the fiscal year.

Fiscal year	Investigations Opened	Investigations Closed	On-Going Investigations At Close of Fiscal Year
2013	908	1,187	1,444
2014	995	822	1,612
2015	980	821	1,677
2016	1,063	776	1,729
2017[7]	965	*	1,695

6 *See* ENF Annual Report at 12.

7 Statistics for 2017 are drawn from the SEC's 2019 Budget Justification at p. 26. Unfortunately, as of our publication date, the 2017 Select SEC and Market Data report, which usually contains the number of investigations closed, has not yet been issued by the Commission. We will update this information as soon as it becomes available.

OFFICE OF THE WHISTLEBLOWER[8]

The SEC's Whistleblower program was established pursuant to the Dodd-Frank Act, which became effective in July 2010, and the Office of the Whistleblower has been reporting to Congress, as required under the law, since December 2010. In that first report, Congress is advised that the Division of Enforcement "is in the process of establishing a Whistleblower Office." *Id.* at 4.

Now, some seven years later, the Office of the Whistleblower advises that enforcement cases brought based on whistleblower information have resulted in monetary sanctions orders totaling $975 million, and the whistleblower program has awarded about $160 million in awards to 46 individuals. *Id.* at 1.

The program directs the Commission to make whistleblower awards to those eligible individuals who provide information that leads to a successful SEC enforcement action, which results in monetary sanctions over $1 million. *Id.* at 4. The recovery amount can range from 10% to 30% of the sanctions collected, at the discretion of the Commission. The SEC ordered almost $50 million in whistleblower awards in Fiscal Year 2017, including one award of over $20 million. *Id.* at 10-11.

In fiscal year 2017, the SEC's Office of the Whistleblower received 4,484 whistleblower tips, an increase of 266, or 6.3%, which is actually a bit lower than the 7.5% jump in 2016.

Fiscal Year	Total Number Of Tips	Percentage Increase of Tips	Total Investigations Arising from Tips[9]	Percentage of Investigations Arising from Tips
2012	3,001	*	296	9.8%
2013	3,238	7.9%	289	9.2%
2014	3,620	11.8%	291	8.0%
2015	3,923	8.4%	325	8.3%
2016	4,218	7.5%	336	8.0%
2017	4,484	6.3%	307	6.8%

Most notable about the foregoing chart, of course, is that, as tips into the Commission continue to increase significantly, the apparent value of those tips appears to decline. The Supreme

8 *See* "2017 Annual Report to Congress Whistleblower Program" (Nov. 15, 2017), https://www.sec.gov/files/sec-2017-annual-report-whistleblower-program.pdf.

9 These figures are taken from the SEC's 2019 Budget Justification at p. 107.

Court decision discussed below, in *Digital Realty Trust, Inc. v. Somers*,[10] will undoubtedly result in even more tips and complaints being reported to the SEC, but for the purpose of protecting putative whistleblowers and not necessarily identifying issues to which Enforcement resources are appropriately brought to bear. In any case, overwhelming the Office of the Whistleblower with protective complaint reporting will unlikely result in a higher percentage of tips that lead to in the opening of investigations or inquiries by the Division of Enforcement.

In fiscal year 2017, the Office of the Whistleblower received tips from every state and the District of Columbia, with the largest number coming from California, New York, Texas, Florida, and New Jersey. *Id.* at Appendix B and at 25. The Commission also received tips from around the world, with most of the non-US tips coming from the United Kingdom, Canada, and Australia. The Office of the Whistleblower also heard from whistleblowers in China, Russia, and Mexico, just by way of example. *Id.* at 25 and Appendix C.

As in prior years, "Other" is always the largest substantive area for tips, this year accounting for over 25% of the total tips. A tally of the whistleblower tips by substantive allegation area over time, based on the categories offered by the Whistleblower Office, follows. *Id.* at Appendix A.

Allegation Type	Number of Allegations 2017	Number of Allegations 2016	Number of Allegations 2015	Number of Allegations 2014
Corporate Disclosure and Financials	954	938	687	610
Offering Fraud	758	646	613	581
Manipulation	468	472	482	563
Insider Trading	231	262	273	256
Trading and Pricing	271	257	213	144
FCPA	210	238	186	159
Unregistered Offerings	144	143	150	102
Market Event	125	102	192	139
Municipal Securities and Public Pension	58	57	67	67
Other	1,162	996	956	911
Not Reported	94	97	114	97

ENFORCEMENT OF WHISTLEBLOWER PROTECTIONS

Early in this past fiscal year, the Enforcement Staff brought several cases charging violations of Exchange Act Rule 21F-17, which protects individuals' communications with the SEC for the purpose of reporting potential securities laws violations. Although we continue to get questions

10 *See infra*

from clients about their agreements, policies, and procedures, the Enforcement Division has not brought a case in this area since January 2017.

In the *HomeStreet, Inc.* matter, the company was charged with taking punitive steps in attempting to identify the whistleblower allegedly responsible for an SEC investigation and also with requiring separating employees to sign severance agreements waiving any right to whistleblower payments.[11] In settlement, without admitting or denying the conduct, HomeStreet agreed to contact former employees who signed the violative separation agreement, to notify them that the company does not prohibit contact with the SEC to report potential violations or receiving whistleblower awards and to pay a civil penalty of $500,000. *Id.*

Violative separation agreements were also at the heart of the *NeuStar, Inc.*[12] and the *BlackRock, Inc.*[13] matters. In the *NeuStar* matter, the severance agreements precluded former employees from disparaging the company to a regulator, including the SEC; in the *BlackRock* matter, the agreement waived the right to any whistleblower recovery in exchange for the firm's separation payment. Without admitting or denying the conduct, NeuStar paid a civil penalty of $180,000 and BlackRock paid a penalty of $340,000 in settlement. *See id.*

Finally, the Commission charged SandRidge Energy, Inc. with violations of both Rule 21F-17 and the anti-retaliation provisions of Section 21F(h), for the company's alleged termination of an employee who complained about the firm's calculation of its oil and gas reserves, and also for using a separation agreement that did not permit employees to voluntarily contact regulators or cooperate in proceedings involving the company.[14] In settling the matter, without admitting or denying the conduct, SandRidge Energy agreed to pay a penalty of $1.4 million. *Id.*

U.S. SUPREME COURT DECISION NARROWING WHISTLEBLOWER PROTECTIONS

On February 21, 2018, the United States Supreme Court decided *Digital Realty Trust, Inc. v. Somers*,[15] which resolved a split among the Circuit Courts of Appeals, and decided that putative whistleblowers must bring their concerns regarding violations of the securities laws to the Securities and Exchange Commission in order to benefit from the retaliation protections incorporated into the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank).[16]

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11 *In the Matter of HomeStreet, Inc. and Darrell Van Amen*, Exchange Act Rel. No. 79844 (Jan. 19, 2017).

12 *In the Matter of NeuStar, Inc.*, Exchange Act Rel. No. 79593 (Dec. 19, 2016).

13 *In the Matter of BlackRock, Inc.*, Exchange Act Rel. No. 79804 (Jan 17, 2017).

14 *In the Matter of SandRidge Energy, Inc.*, Exchange Act Rel. No. 79607 (Dec. 20, 2016).

15 No. 16-1276, 583 U.S. ___ (2018).

16 *See id.* at pp. 8-9.

The Court concluded that the statutory language of Dodd-Frank was plain and that "whistleblower" was expressly defined under that law as one who provides information to the SEC. *Id.* at p. 9. As a result, the protections from retaliation set forth in the statute are only available to one who reports such concerns to the Commission. *Id.* at p. 12. Further, the Court pointed out that, where Congress intended no such requirement, as in other parts of Dodd-Frank, it did not include this requirement of government reporting; for example, in similar such provisions related to the Consumer Financial Protection Bureau. *Id.* at 10. Finally, the Supreme Court's opinion notes that part of the purpose in incorporating the whistleblower provisions of Dodd-Frank at issue in the case was, in fact, to motivate people to share information with the Commission, so that the SEC could investigate violative conduct. *Id.* at 11. Thus, the regulatory regime was specific and intentionally drafted.

The SEC had joined an amicus brief filed in October 2017 seeking a contrary result.[17]

While a useful decision in connection with some litigated matters, the Supreme Court's decision likely will result in more reports to the SEC in circumstances where employees may otherwise have chosen to report their concerns internally. However, the 2002 Sarbanes-Oxley Act will continue to protect many whistleblowers who chose only to make internal reports. This complicated issue will no doubt be the subject of much discussion in the months to come. For a more complete consideration of the ruling, please see our firm's analysis.[18]

KEY SEC ENFORCEMENT DEVELOPMENTS

Protecting Retail Investors

While it hardly seems like a "key development" that the SEC is focused on protecting retail investors, the Commission and the Division of Enforcement certainly took every opportunity this past year to remind us that this is their "Principle 1."[19] And the year's enforcement actions, 30% of which were comprised of market manipulations and offering frauds, would certainly appear to bear that out. *See supra*. And, in addition to the more garden variety Ponzi schemers, penny stock offerings, boiler room operators, and affinity fraudsters, we also saw the

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[17] *See* Br. for the United States as Amicus Curiae Supporting Respondent, available at https://www.sec.gov/litigation/briefs/2017/digital-realty-trust-1017.pdf.

[18] For more analysis of some of the considerations and issues, please see our Morgan Lewis Law Flash on this topic, *"Supreme Court Holds Dodd-Frank Whistleblower Protection Only Covers Individuals Who 'Tell the SEC,'"* Feb. 23, 2018, available at, https://www.morganlewis.com/pubs/supreme-court-holds-dodd-frank-whistleblower-protection-only-covers-individuals-who-tell-the-sec

[19] *See* ENF Annual Report at 1 ("Principle 1: Focus on the Main Street Investor"). *See also, "Remarks at the Economic Club of New York*, SEC Speech, SEC Chairman Jay Clayton, July 12, 2017 (Principle 1 is the SEC mission "is our touchstone"; Principle 2: "Our analysis starts and ends with the long-term interests of the Main Street investor.") https://www.sec.gov/news/speech/remarks-economic-club-new-york.

Enforcement Division tackle some more creative efforts to defraud retail investors by taking advantage of the potential to make money from newly legalized marijuana in some jurisdictions[20] and from Initial Coin Offering (ICO) frauds[21] (more on those later).
Of course, the "Main Street Investors" priority was also plainly reflected in the enforcement cases brought in the regulated entity space. The SEC's continued focus on overcharges[22] and disclosures of fees and expenses;[23] disclosures of conflicts of interest and, by way of example, the related mutual fund share class selection issues;[24] sales practices in connection with complex and structured products;[25] as well as churning[26] and reverse churning, which directly bear on the Commission's "Retail" mission.

Further to this, the Division of Enforcement recently announced a new self-reporting initiative intended to "protect advisory clients from undisclosed conflicts of interest and return money to investors."[27] Specifically, the Enforcement Division has invited investment advisers to self-report mutual fund share class violations involving Rule 12b-1 fees and, if eligible advisers choose to participate, the Enforcement Staff will recommend that no civil money penalty be sought in connection with the ensuing settled enforcement action. *Id.*

The Commission was clear in its announcement that this program is an important part of its "retail" focus, as Stephanie Avakian, Co-Director of the Division of Enforcement, was quoted in the press release, "This focused initiative reflects our effort to allocate our resources in a way that effectively targets the continued failure by some advisers to disclose conflicts of interest around share class selection and, importantly, is intended to facilitate the prompt return of money to victimized investors." *Id.* For those who participated in the Commission's MCDC initiative, they will already know that these self-reporting initiatives are necessarily far more complex than we can cover here. In addition, it is our view that, although recent enforcement actions and the launch of this initiative might suggest otherwise, the fact remains every

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[20] *See, e.g., "SEC Charges Marijuana-Related Company and Executives With Touting Bogus Revenues,"* SEC Press Release 2017-62 (Mar. 9, 2017) https://www.sec.gov/news/pressrelease/2017-62.html.

[21] *See, e.g., "SEC Exposes Two Initial Coin Offerings Purportedly Backed by Real Estate and Diamonds,"* SEC Press Release 2017-185 (Sept. 29, 2017) https://www.sec.gov/news/press-release/2017-185-0.

[22] *See, e.g., "Barclays to Pay $97 Million for Overcharging Clients,"* SEC Press Release 2017-98 (May 10. 2017) https://www.sec.gov/news/press-release/2017-98.

[23] *See, e.g., In the Matter of Stifel, Nicolaus & Co.*, Inv. Advisers Act Rel. No. 4665 (Mar. 13, 2017) (most recent in the Commission's series of "trading away" matters).

[24] *See, e.g., "SunTrust Charged With Improperly Recommending Higher-Fee Mutual Funds,"* SEC Press Release 2017-165 (Sept. 14, 2017) https://www.sec.gov/news/press-release/2017-165.

[25] *See, e.g., "Morgan Stanley Settles Charges Related to ETF Investments,"* SEC Press Release 2017-46 (Feb. 14, 2017) https://www.sec.gov/news/pressrelease/2017-46.html.

[26] *See, e.g., "SEC Detects Brokers Defrauding Customers,"* SEC Press Release 2017-180 (Sept. 28, 2017) https://www.sec.gov/news/press-release/2017-180.

[27] *See "SEC Launches Share Class Selection Disclosure Initiative to Encourage Self-Reporting and the Prompt Return of Funds to Investors,"* SEC Press Release 2018-15 (Feb. 12, 2018) https://www.sec.gov/news/press-release/2018-15

advisory platform, offerings and disclosure history is different today and, over time.[28] Therefore, we can anticipate much more discussion on this particular initiative during the course of this year.

Even the Commission's formation of a Fixed Income Market Structure Advisory Committee was touted as an event intended to protect retail investors. In the press release announcing the committee, SEC Chairman Jay Clayton said "[i]ndividual investors are highly active in fixed income markets, both directly as retail investors and indirectly through various types of funds."[29] The Chairman continued that he hoped the Committee's work would ensure that regulation in this area meets the needs of retail investors, as well as other fixed income market participants. *Id.*

More specifically, though, at the Division of Enforcement, the formation of a Retail Strategy Task Force was announced in September 2017, with dedicated staff intended to focus strategically on more large-scale risk that threaten individual investors.[30] According to Stephanie Avakian, the Co-Director of Enforcement, the Retail Task Force will build upon prior strategies; work across the agency, with DERA and OCIE; as well as with others within the Enforcement Division, like Market Intelligence and the Center for Risk and Quantitative Analytics, to bring tools, like data analytics and new technologies, to bear on the market data and other information available to the staff to proactively identify misconduct.[31]

Cybersecurity and Cryptocurrency

In a year when it was announced that even the Commission itself had been hacked, cybersecurity became an area of critical focus for the SEC and for the Division of Enforcement.[32] The Division of Enforcement added its first specialized unit since the Division reorganized in 2010 and the specialized units were created, adding the Cyber Unit.[33] Cyber-related frauds have continued to increase in number and sophistication. Some of the cases that involved hacking to obtain information for the purposes of trading are discussed below. In addition to

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28 For more analysis of some of the considerations and issues, please see our Morgan Lewis Law Flash on this topic, *"SEC Launches Self-Reporting Initiative For Mutual Fund Share Classes,"* Feb. 21, 2018, available at https://www.morganlewis.com/pubs/sec-launches-self-reporting-initiative-for-mutual-fund-share-classes.

29 *See "SEC Announces the Formation and First Members of Fixed Income Market Structure Advisory Committee,"* SEC Press Release 2017-209 (Nov. 9, 2017) https://www.sec.gov/news/press-release/2017-209.

30 *See "SEC Announces Enforcement Initiatives to Combat Cyber-Based Threats and Protect Retail Investors,"* SEC Press Release 2017-176 (Sept. 25, 2017) https://www.sec.gov/news/press-release/2017-176.

31 *See "The SEC Enforcement Division's Initiatives Regarding Retail Investor Protection and Cybersecurity,"* SEC Speech, Stephanie Avakian (Oct. 26, 2017) https://www.sec.gov/news/speech/speech-avakian-2017-10-26

32 *See, e.g., "Chairman Clayton Provides Update on Review of 2016 Cyber Intrusion Involving EDGAR System,"* SEC Press Release 2017-186 (Oct. 2, 2017) https://www.sec.gov/news/press-release/2017-18; *and see "Statement on Cybersecurity,"* Statement by SEC Chairman Jay Clayton (Sept. 20, 2017) https://www.sec.gov/news/public-statement/statement-clayton-2017-09-20.

33 *See* notes 17 and 18, *supra*.

those cases, this year saw the rise of ICO fraud,[34] as well as broader concerns at the Commission about the evaluation and regulation of ICOs and cryptocurrencies generally.[35] The Commission is plainly spending a lot of time and energy deciding whether and how to regulate these new products and the Cyber Unit affords the Enforcement Division a "consistent, thoughtful approach," to all of these interrelated issues, including distributed ledger technology, or blockchain.[36]

In terms of enforcement-related matters, the Cyber Unit can be expected to focus on: market manipulations involving false information spread electronically; hacking to obtain material nonpublic information for trading; blockchain and ICO frauds; misconduct effected using the so-called "dark web"; retail brokerage account intrusions; and cyber-related threats to trading platforms and the markets more broadly.[37]

Perhaps it was the novelty of the issues presented, but for whatever reason, it was good to see the Commission and the Division of Enforcement revert to the use of tool not seen since January of 2014, that is the Report of Investigation Pursuant to Section 21(a) of the Exchange Act (21(a) Report), in lieu of bringing an enforcement action in the blockchain/ICO area.[38] These types of reports are particularly useful in new and novel areas to offer guidance to the marketplace and seem much more appropriate and helpful than the more typical "regulation by enforcement."

The 21(a) Report was issued in connection with the Enforcement Division's investigation of "The DAO," an organization that "used blockchain technology to operate as a 'virtual' entity."[39] According to the Commission staff, "The DAO sold tokens representing interests in its enterprise to investors in exchange for payment with virtual currency." *Id.* Based on the findings in the 21(a) Report, the Commission concluded that the tokens sold were, in fact, securities, subject to regulation by the SEC.[40] In addition, the SEC concluded that the organization offering these securities met the Exchange Act definition of an exchange and it operated without an appropriate exemption. *Id.* at 16-17. The SEC Staff and the Commission have continued to

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[34] *See, e.g., "SEC Halts Alleged Initial Coin Offering Scam,"* SEC Press Release 2018-8 (Jan. 30, 2018) https://www.sec.gov/news/press-release/2018-8.

[35] *See "Statement on Cryptocurrencies and Initial Coin Offerings,"* SEC Public Statement, Chairman Jay Clayton, Dec. 11, 2017 https://www.sec.gov/news/public-statement/statement-clayton-2017-12-11.

[36] *See* note 18, *supra* (Avakian speech).

[37] *See* ENF Annual Report at 4.

[38] Section 21(a) does not provide much guidance as to these reports; rather, the section notes that, in connection with investigations, the Commission "is authorized in its discretion, to publish information concerning any such violations . . . ." 15 U.S.C. § 78u.

[39] *See "Statement by the Divisions of Corporation Finance and Enforcement on the Report of Investigation on The DAO," SEC Public Statement*, July 25, 2017 https://www.sec.gov/news/public-statement/corpfin-enforcement-statement-report-investigation-dao.

[40] *See* The DAO 21(a) Report at p. 11, Exchange Act Rel. No. 81207 (July 25, 2017), https://www.sec.gov/litigation/investreport/34-81207.pdf.

issue guidance and alerts in these areas,[41] even as we begin to see fraud cases that appear to be taking advantage of investors, and of the novelty of these products.[42]

The *Kokesh* Decision and the Five-Year Statute of Limitations

In *Kokesh*, a unanimous Supreme Court held that the five-year statute of limitations under 28 U.S.C. § 2462 applies to disgorgement orders sought by the SEC. Previously, the Circuit Courts of Appeal had been split on this issue.[43] The issue was presented to the Supreme Court on appeal by Kokesh, who argued that a trial court's order that he disgorge nearly $35 million for conduct between 1995 and 2009 was in the nature of a penalty or forfeiture, and therefore subject to the five-year statute of limitations under § 2462. The SEC countered that disgorgement is not punitive, but merely an equitable remedy that prevents offenders from reaping ill-gotten gains.

The Court unanimously held that the SEC's disgorgement remedy "bears all the hallmarks of a penalty: It is imposed as a consequence of violating a public law and it is intended to deter, not to compensate." *Id.* at 1644. Thus, "[t]he 5-year statute of limitations in § 2462 therefore applies when the SEC seeks disgorgement." *Id.*

The Kokesh decision represents the second opportunity the Court has taken to narrow the Commission's ability to obtain monetary relief in an enforcement action based on the statute of limitations. Previously, in the *Gabelli* matter, the Court held that the SEC could not use the "discovery rule" to extend the statute of limitations for civil penalties.[44]

The most immediate result of the *Kokesh* decision has been the SEC Enforcement staff's more aggressive requests for tolling agreements, sometimes even at the very beginning of investigations, and we can anticipate that will continue. Further, at least two courts have refused to grant injunctions and related relief based on conduct outside of the five-year limitations period.[45]

In addition, since the Supreme Court has labeled disgorgement as a "penalty," such payments are no longer eligible for tax deduction. In an IRS case from 2016, when the IRS Chief Counsel held that disgorgement payments made to the SEC were a penalty and not tax-deductible, the first doubt was cast on this treatment.[46] At that time, however, the IRS offered a facts-and-

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41 *See "Statement on Potentially Unlawful Promotion of Initial Coin Offerings and Other Investments by Celebrities and Others,"* SEC Public Statement by the Division of Enforcement and OCIE (Nov. 1, 2017) https://www.sec.gov/news/public-statement/statement-potentially-unlawful-promotion-icos.

42 *See* note 21, *supra*.

43 *See Kokesh v. Securities and Exchange Comm'n*, 137 S. Ct. 1635 (2017).

44 *Gabelli v. SEC*, 568 U.S. 442 (2013).

45 *See SEC v. Jones*, Civil Action No. 17-11226 (D. Mass. Jan. 5, 2018); *and see SEC v. Gentile*, Civil Action No. 16-1619 (D.N.J. Nov. 9, 2017).

46 *See* I.R.S. Legal Memorandum 2016-19-008 at 6 (May 6, 2016).

circumstances test to determine whether or not disgorgement was being used as a penalty. *Id.* However, shortly after the Supreme Court had definitively decided the question, the IRS Chief Counsel issued further advice concluding that "as the Supreme Court held, disgorgement payments are penalties and are not compensatory, section 162(f) prohibits a deduction under section 162(a) for an amount paid as disgorgement for violating a federal securities law."[47]

Finally, we can anticipate at least one more swing to be taken at the Commission's authority based on the language of *Kokesh*. Specifically, the Court appears to have opened the door to a challenge to the SEC's authority to seek disgorgement as a remedy *at all*, an issue considered at length at oral argument. Although the Commission expressly has such authority in the context of administrative proceedings, 15 U.S.C. § 78u-2(e), no such authority exists for actions filed in federal court. And, in a footnote, the Supreme Court specified that, in *Kokesh*, it was not deciding "whether courts possess authority to order disgorgement in SEC enforcement proceedings or . . . whether courts have properly applied disgorgement principles in this context."[48]

Given the rather strict statutory approach seen in the whistleblower definition matter, *Digital Realty Trust, Inc. v. Somers*, *see supra*, taken together with the determination here that, in this context, disgorgement is a penalty and not a mere equitable remedy, it will be interesting to see what the Supreme Court might do with a statutorily-based challenge that considers remedies available in federal court enforcement actions, since disgorgement is not among the remedies expressly provided for by Congress.[49]

Significant Challenges to the Commission's Administrative Forum

In January 2018, the Supreme Court granted *certiorari* in the *Lucia* case, in which the appellants asserted that the SEC's administrative law judges (ALJs) have been hired in violation of the Appointments Clause of the Constitution.[50] Challenges to the Commission's administrative forum have been percolating for some time, most notably since Dodd-Frank expanded remedies available to the Commission in that forum and, in turn, the Enforcement Division promised to more liberally use the advantages presented by administrative proceedings in disputed cases.[51] The Appointments Clause challenges are the substantive claims objecting to the administrative forum that actually have gained traction. Essentially, the challenge relates to the fact that ALJs at the Commission have been selected by the chief ALJ through an

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47 See I.R.S. Chief Counsel Legal Advice, C.C.A. 2017-48-008 (Dec. 1, 2017).

48 *Kokesh*, 137 S. Ct. at 1642 n.3.

49 *Compare* 15 U.S.C. § 78u-2(e) (Disgorgement expressly provided for as a remedy in the administrative forum) to 15 U.S.C. § 78u(3) (Money Penalties in Civil Actions) and 15 U.S.C. § 78u(5) (Equitable Relief generally available in civil actions).

50 *Lucia v. SEC*, No. 17-130 (U.S. Jan 12, 2018). The Appointments clause reads, in relevant part, "The Congress may by Law vest the Appointment of such Inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments." U. S. Const. Art. 2 § 2 cl. 2.

51 *See, e.g., "Remarks to the American Bar Association's Business Law Section Fall Meeting,"* SEC Speech, Andrew Ceresney, Nov. 21, 2014, https://www.sec.gov/news/speech/2014-spch112114ac.

employment process assisted by the Office of Personnel Management, rather than a process involving the SEC Commissioners.

The *Lucia* case arrived at the Supreme Court as the result of the split among the Circuit Courts of Appeal, with the D.C. Circuit Court finding in the *Lucia* case that ALJs are not "inferior officers" under the Appointments Clause, who need to be appointed by the President or the head of a department; and the 10th Circuit Court, in the *Bandimere* case, which took a contrary view.[52] And, in a pretty stark example that elections matter, on November 29, 2017, the Solicitor General filed a brief at the Supreme Court effectively switching sides.[53] Until this filing, the Trump Administration had supported the conclusion reached by the D.C. Circuit, but the November 29 brief takes the opposite position: that SEC ALJs must be appointed by the Commission. *Id.* In response, the following day, the SEC issued an order "ratifying" the appointment of the ALJs.[54] In addition, given that the Solicitor General is no longer arguing this matter on the side of the SEC, the Supreme Court was forced to appoint counsel for the agency, which it did.[55]

The result of all of this turmoil has been that, although the Commission routinely has used its administrative forum to conclude settled matters, most disputed matters have been filed in federal court throughout this past fiscal year and into FY 2018. The exception to this practice has been those matters where specific remedies are available against regulated persons only in the administrative forum.[56] We can expect this will continue as uncertainty surrounds the administrative forum.

ADDITIONAL AREAS OF FOCUS FOR THE ENFORCEMENT DIVISION

Financial Reporting and Auditor Misconduct

As is plain from the statistics, this was a significant year for financial reporting and auditor misconduct cases. The Commission continues to look to gatekeepers, and outside auditors in particular, to ensure that the information provided to the investing public is accurate and useful.

Probably the biggest bombshell in this area dropped well after the close of the fiscal year, however, when, in January 2018, the SEC charged six accountants, including former staffers at

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[52] *See Raymond J. Lucia Cos. v. SEC*, 868 F.3d 1021 (D.C. Cir. 2017) (*en banc*) (*per curiam*), *cert. granted sub nom. Lucia v. SEC*, No. 17-130 (U.S. Jan. 12, 2018); *see also Bandimere v. SEC*, 844 F.3d 1168 (10th Cir. 2016), *reh'g denied*, 855 F.3d 1128 (May 3, 2017).

[53] *See* Br. for Respondent, *Lucia v. SEC*, No. 17-130 (U.S. Nov. 29, 2017).

[54] *See In re: Pending Administrative Proceedings*, Sec. Act Rel. No. 10440 (Nov. 30, 2017).

[55] *See Lucia v. SEC*, No. 17-130 (U.S. Jan. 18, 2018) (Order inviting Anton Metlitsky to brief and argue the matter in support of the judgment below.)

[56] *See, e.g., In the Matter of Cynthia Holder, CPA, et al.*, AP File No 3-18346 (Jan. 22, 2018), available at https://www.sec.gov/litigation/admin/2018/34-82556.pdf.

the Public Company Accounting Oversight Compliance Board (PCAOB), in connection with their efforts to use leaked confidential data to assist KPMG in its upcoming PCAOB inspections.[57] This matter is still in litigation and the defendants also were criminally charged.

Insider Trading and Other Fraudulent Trading on Material Nonpublic Information

Insider trading, as well as the electronic stealing and other misuses of material nonpublic information, continued to be significant areas of focus for the Enforcement Staff this year. Among the more high-profile matters included the Commission's cases against Chinese hackers, who stole material nonpublic information about potential corporate deals from two law firms and ran up almost $3 million in trading profits;[58] and a very complex insider trading scheme that originated with an IT employee at a large investment bank, which, according to the SEC, went on for more than three years, and resulted in over $5 million in profits for tippers and tippees involved in three different chains of traders, who profited from advance news on potential mergers, acquisitions, or tender offers.[59] Both matters are still being investigated and litigated and each resulted in criminal charges. *See supra*. In identifying the conduct in each of these cases, the Enforcement Staff noted its sophisticated trading surveillance and data analytics to detect suspicious trading. *Id.* Those same data analytics tools where used in a more standard insider trading case in which Chinese nationals, including a partner at a Chinese private equity firm with advance knowledge that the company was in play, were charged with insider trading ahead of the Dreamworks Animation SKG acquisition by Comcast, and U.S.-based accounts holding $29 million in trading proceeds were frozen.[60]
In an interesting pair of cases, the SEC charged a so-called "political intelligence analyst" with insider trading, for passing along material nonpublic information about Medicare reimbursement rates he obtained from a source inside the government's Centers for Medicare and Medicaid Services to analysts at a hedge fund advisory firm that paid him as a consultant.[61] Shortly thereafter, the Commission charged the hedge fund advisory firm for its lack of adequate controls to prevent insider trading, citing, among other things, certain red flags about the political intelligence analyst's information and sources.[62]

Of course, throughout the year, there were plenty of more standard classical insider trading and

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[57] *See "Six Accountants Charged with Using Leaked Confidential PCAOB Data in Quest to Improve Inspection Results for KPMB,"* SEC Press Release 2018-6, (Jan. 22, 2018) https://www.sec.gov/news/press-release/2018-6; *see also In the Matter of Brian Sweet, CPA*, Exchange Act Rel. No. 82557 (Jan. 22, 2018); *and see In the Matter of Cynthia Holder, CPA, et al.*, Exchange Act Rel. No. 82556 (Jan. 22, 2018).

[58] *See "Chinese Traders Charged With Trading on Hacked Nonpublic Information Stolen From Two Law Firms,"* SEC Press Release 2016-280 (Dec. 27, 2016) https://www.sec.gov/news/pressrelease/2016-280.html.

[59] *See "SEC Uncovers Wide Reaching Insider Trading Scheme"*; SEC Press Release 2017-143 (Aug. 16, 2017) https://www.sec.gov/news/press-release/2017-143.

[60] *See "SEC Charges Chinese Citizens Who Reaped Massive Profits From Insider Trading on Comcast-Dreamworks Acquisition,"* SEC Press Release 2017-44 (Feb. 10, 2017) https://www.sec.gov/news/pressrelease/2017-44.html.

[61] *See "SEC Files Charges in Trading Scheme Involving Confidential Government Information,"* SEC Press Release 2017-109 (May 24, 2017) https://www.sec.gov/news/press-release/2017-109.

[62] *See "Hedge Fund Adviser Charged for Inadequate Controls to Prevent Insider Trading,"* SEC Press Release 2017-146 (Aug. 21, 2017) https://www.sec.gov/news/press-release/2017-146.

tipping cases, which remain the bread-and-butter the Market Abuse Unit of the Enforcement Division. Sometimes, in these matters, the SEC is joined by the Department of Justice in bringing charges against the traders.[63]

Foreign Corrupt Practices Act

As always seems to be the case, some of the largest financial settlements each year come in the FCPA area, and this past year was no different. The top three disgorgement orders, totaling over $1 billion in disgorgement ordered, came in FCPA cases.[64] Given the big numbers, the opportunity to work with international regulatory enforcement organizations, and the incentives for cooperation by respondents, one can expect this trend to continue. In fact, FCPA enforcement by the SEC remains such a high priority that it was the sole focus of the only speech given this year by co-Director of Enforcement Steven R. Peikin.[65] The SEC's website has quite a few resources on FCPA cases, including a page that sets forth many of the more important matters, over quite a few years.[66]

Municipal Securities and Public Pensions

With MCDC behind it, the Public Finance Abuse Unit could focus on more traditional types of pay-to-play, fraud and failures to disclose cases. Early in the year, the Unit brought a very significant pay-to-play case, together with the criminal authorities, against a former official of the nation's third largest public pension fund and two registered representatives at two different broker-dealers, citing racy details of lavish excess.[67] According to the SEC, the gifts and entertainment lavished on the official resulted in his directing $2.5 billion in business to the two brokers. *Id.* In a less sensational, in terms of detail and size, but no less brazen matter, the SEC charged the Town of Oyster Bay, New York, and its former Town Supervisor with fraud for concealing from investors that the Town had indirectly guaranteed some $20 million in private bank loans for the benefit of a private company, which operated restaurants and concessions at

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[63] *See, e.g., "Former Pharma Company Accountant, Three Others Charged With Insider Trading."* SEC Press Release 2017-151 (Aug. 31, 2017) https://www.sec.gov/news/press-release/2017-151; *"SEC Charges Former Employee and Friend with Insider Trading in Securities of International Rectifier Corporation,"* SEC Lit. Rel. No. 24015 (Dec. 14. 2017) https://www.sec.gov/litigation/litreleases/2017/lr24015.htm.

[64] *See "Telecommunications Company Paying $965 Million For FCPA Violations,"* SEC Press Release 2017-171 (Sept. 21, 2017) https://www.sec.gov/news/press-release/2017-171 (disgorgement $457 million); *see also "Petrochemical Manufacturer Braskem S.A. to Pay $957 Million to Settle FCPA Charges,"* SEC Press Release 2017-271 (Dec. 21, 2016) (disgorgement $325 million); *and see "Teva Pharmaceutical Paying $519 Million to Settle FCPA Charges,"* SEC Press Release 2016-277 (Dec. 22, 2017) (disgorgement $236 million).

[65] *See "Reflections on the Past, Present, and Future of the SEC's Enforcement of the Foreign Corrupt Practices Act,"* SEC Speech, Steven R. Peikin, Nov. 9, 2017 https://www.sec.gov/news/speech/speech-peikin-2017-11-09.

[66] *See* SEC Enforcement Actions: FCPA Cases at https://www.sec.gov/spotlight/fcpa/fcpa-cases.shtml.

[67] *See "SEC Charges Former New York Pension Official and Two Brokers in Pay-to-Play Scheme,"* SEC Press Release 2016-272 (Dec. 21, 2016) https://www.sec.gov/news/pressrelease/2016-272.html.

several Town facilities.[68] As a result, the Town's securities offerings were deficient, since they did not fully disclose Oyster Bay's financial condition. *Id.* The Town Supervisor was also criminally charged. *Id.*

In a matter that probably afforded some satisfaction to those who participated in the MCDC initiative, the Enforcement Division charged a municipal financial authority in Beaumont, California and its former executive director with making false statements concerning the authority's compliance with its continuing disclosure obligations in connection with five bond offerings.[69] According to the SEC, these misrepresentations were discovered in a review of municipal issuers and underwriters that did not participate in MCDC. The Commission noted that, had Beaumont authority and its underwriter, which was also charged, chosen to participate in MCDC, they would have been eligible for lesser sanctions.

LOOKING AHEAD

As noted above, we can anticipate that the coming year at the SEC will bring more and continued focus on "retail" and "Main Street" investor protection, as well as the protection of assets saved by retail investors for retirement. This work at the Commission will include potential regulatory action by the Commission on the Fiduciary Rule.[70] The SEC also has prioritized implementation of a consolidated audit trail (CAT) to track and store data of trading activity in the U.S. equity and options markets. *Id.* at 27.

In addition to CAT, the Commission continues to gather more and more market data and to analyze that information using the various data analytics tools the SEC previously has developed and that the Staff has under development, which undoubtedly will result in more interesting and efficient methods for the Staff to identify securities laws violations.[71] This continued leveraging of technology may also assist in the Staff's continued review and analysis of market structure issues, as well as its consideration of more complex trading, including algorithmic and other technology-based strategies and vehicles. *Id.*

All things "Cyber," including cybersecurity and "cyberproducts," like bitcoin and other digital currency and investment products, will continue to be a focus of the SEC, and of the Cyber Unit established at the Division of Enforcement, in the coming year.[72]

Further, we can anticipate that the Commission, through its Fixed Income Market Structure

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[68] *See "Long Island Town and Former Top Official Charged With Defrauding Municipal Investors,"* SEC Press Release 2017-213 (Nov. 21, 2017) https://www.sec.gov/news/press-release/2017-213.

[69] *See "Muni Bond Issuer and Underwriter Charged With Disclosure Failures,"* SEC Press Release 2017-148 (Aug. 23, 2017) https://www.sec.gov/news/press-release/2017-148.

[70] *See* 2017 SEC Agency Financial Report at p. 28.

[71] *See generally id.* at pp. 24-30.

[72] *Id. at pp. 24-26; and see supra.*

Advisory Committee and otherwise, will take a meaningful look at the efficiency and transparency of the fixed income market.[73]

Finally, perhaps the fact that the Division of Enforcement determined that a self-reporting program on the mutual fund share class issue - an area where it was already significantly involved in bringing enforcement actions – suggests some transition from the more prosecutorial Enforcement Division we have seen in the recent past, to a more regulatory mindset. The coming year certainly will tell us a lot on that score.

SEC ENFORCEMENT AND EXAMINATION PRIORITIES

Based on our review of currently available information, we believe that the following list reflects some of the SEC's top enforcement and examination priorities:[74]

Protecting Retail Investors

- Disclosure of Fees and Expenses associated with investing
- Electronic Investment Advice
  - Compliance
  - Marketing
  - Data Protection
  - Conflicts of Interest
- Wrap Fee Programs
  - Dual Registrants
    - Suitability
    - Disclosure
    - Conflicts of Interest
    - Trading away/best execution
- Never-Before Examined Investment Advisers
  - Risk-based

Senior Investors and Investors Saving for Retirement

- Supervision and controls related to products and services directed to senior investors
- Dual registrant offerings to investors saving for retirement
  - Retirement vehicles serving government and nonprofit employees

[73] *See supra; see also* 2017 SEC Agency Financial Report at p. 29.

[74] *See id.* at pp. 24-30; *see also* 2018 National Exam Program Examination Priorities (Feb. 7, 2018) https://www.sec.gov/about/offices/ocie/national-examination-program-priorities-2018.pdf.

- Investment recommendations/products
    - Variable insurance products
    - Target date funds

- Mutual Funds and Exchange Traded Funds (ETFs)
    - Disclosures
    - Suitability
    - Performance and risk
    - Conflicts of interest

- Fixed Income Order Execution

- Cryptocurrency, Initial Coin Offerings
    - Cybersecurity and information controls
    - Risk and volatility disclosure

Market Structure

- National Securities Exchanges
    - Governance
    - Policies, procedures and controls
    - Revenue and expense generation and allocation procedures

- Transfer Agents
    - Transfers, recordkeeping and protection of funds and securities
    - TAs that act as agent for microcap or crowdfunding issuers

- Regulation SCI Entities (exchanges, clearing agencies, certain ATS)
    - Policies, procedures and controls
    - Recording of transaction times and synchronization with other systems
    - Business continuity and risk management programs

FINRA

- Continued review of FINRA's operations and regulatory programs

- Quality of broker-dealer and municipal advisor examinations

MSRB

- Operational and internal policies, procedures and controls

Cybersecurity

- Governance and ongoing risk assessment of cybersecurity programs

- Data protection, including access rights and controls

- Vendor management

- Training

- Incident response

Anti-Money Laundering (AML) Programs

- Continued review of regulated entity AML programs
  - Appropriate ongoing analysis by entities of their AML programs to respond to new risks or changes to businesses
  - Evaluation of AML program monitoring and testing

- Continued review of appropriate filing of Suspicious Activity Reports

SEC ENFORCEMENT ACTIONS[75]

Cases Relating to Broker-Dealer Firms and Their Employees/Affiliated Persons

American Depositary Receipts (ADRs)

In re Banca IMI Securities Corp., Exch. Act Rel. No. 10401, 2017 SEC LEXIS 2544 (Aug. 18, 2017)

The Commission accepted an Offer of Settlement from Banca IMI Securities Corp., a registered broker-dealer. The Commission alleged that from at least 2011 through August 2015, despite its contractual obligation to do so, the Firm obtained and lent prereleased ADRs to other broker-dealers without taking reasonable steps to determine whether the appropriate number of ordinary shares of the foreign company's stock evidenced by the ADRs were owned by and in the custody of either the broker or its customer on whose behalf the prereleased ADRs were obtained. According to the Commission, the Firm also, at times, facilitated short sales and enabled the settlement of trades with ADRs that were not backed by ordinary shares. The Commission noted that the Firm's representatives signed certifications attesting that it was complying with its contractual obligations, and that the Firm's securities lending personnel should have known that the ordinary shares were not properly custodied. The Commission also alleged that the Firm failed to reasonably supervise its employees on its securities lending desk and failed to establish and implement effective policies and procedures. As a result of the foregoing, the Commission alleged that the Firm willfully violated Section 17(a)(3) of the Securities Act of 1933 (the Securities Act) and failed to reasonably fulfill its supervisory responsibilities under Section 15(b)(4)(E) of the Securities Exchange Act of 1934 (the Exchange Act). In connection with this settlement, the Commission imposed sanctions that censured the Firm, ordered it to cease and desist from future violations, and pay disgorgement of $18,048,483, prejudgment interest of $2,362,538, and a $15 million civil monetary penalty. The Commission considered the Firm's cooperation and remedial efforts in reaching this settlement.

In re ITG Inc., Exch. Act Rel. No. 79776, 2017 SEC LEXIS 89 (Jan. 12, 2017)

The Commission accepted a Settlement Offer from ITG Inc., a registered broker-dealer and wholly owned subsidiary of a publicly traded corporation. The Commission alleged that from at least 2011 through September 2014, despite its contractual obligation to do so, the Firm obtained and lent prereleased ADRs to other broker-dealers without taking reasonable steps to determine whether the appropriate number of ordinary shares of the foreign company's stock evidenced by the ADRs were owned by and in the custody of either the broker or its customer on whose behalf the prereleased ADRs were obtained. According to the Commission, the Firm

[75] The cases described herein are settlements in which the respondents neither admitted nor denied the allegations against them, unless the description explicitly states otherwise.

also, at times, facilitated short sales and enabled the settlement of trades with ADRs that were not backed by ordinary shares, in violation of Regulation SHO. The Commission noted that supervisors at the Firm signed certifications attesting that it was complying with its contractual obligations, and that the Firm's securities-lending personnel should have known that the ordinary shares were not properly custodied. The Commission also alleged that the Firm failed to reasonably supervise its employees on its securities-lending desk and failed to establish and implement effective policies and procedures. As a result of the foregoing, the Commission alleged that the Firm willfully violated Section 17(a)(3) of the Securities Act and failed to reasonably fulfill its supervisory responsibilities under Section 15(b)(4)(E) of the Exchange Act. In connection with this settlement, the Commission imposed sanctions that censured the Firm, ordered it to cease and desist from future violations, and pay disgorgement of $15,070,144, prejudgment interest of $1,845.252, and a $7,535,072 civil monetary penalty. The Commission credited the Firm's cooperation and remedial efforts in reaching this settlement.

Anti-Money Laundering/Suspicious Activity Reports

In re Merrill Lynch, Pierce, Fenner & Smith Inc., Exch. Act Rel. No. 82382, 2017 SEC LEXIS 4177 (Dec. 21, 2017)

The Commission accepted an Offer of Settlement from broker-dealer and investment adviser Merrill Lynch, Pierce, Fenner & Smith Inc. in connection with allegations that the Firm's anti-money laundering policies (AML) policies were deficient because they failed to account for the additional risks associated with ATM cash deposits, wires, journal-entry transfers, check writing, ATM withdrawals, cash advances, and ACH transfers. As a result of these policy deficiencies, the Commission found that the Firm failed to file suspicious activity reports (SARs) related to transactions or patterns of transactions in customers' accounts from at least 2011 to 2015. The Commission also stated that Merrill Lynch failed to apply its automated monitoring system to certain accounts, did not investigate and report events that were detected, and failed to adequately monitor continuing suspicious activity. The Commission's Order found that the Firm willfully violated Section 17(a) of the Exchange Act and Rule 17a-8 thereunder. The Commission imposed sanctions that censured the Firm, ordered it to cease and desist from future violations, and required it to pay a $13 million civil monetary penalty. The Commission credited the Firm's subsequent remedial measures in deciding to accept the Offer of Settlement. In a related matter, the Firm also agreed to pay a $13 million fine to FINRA for violations of FINRA Rules 3310(a) and 2010, based on the same conduct.

In re Wells Fargo Advisors, LLC, Exch. Act Rel. No. 82054, 2017 SEC LEXIS 3570 (Nov. 13, 2017)

The Commission accepted an Offer of Settlement from broker-dealer Wells Fargo Advisors, LLC, in connection with allegations that the Firm failed to file or file in a timely manner at least 50 SARs between approximately March 2012 and June 2013. A majority of the SARs related to continuing suspicious activity occurring in accounts held at the Firm's US branch offices that focused on international customers. In most instances, according to the Commission, the Firm failed to file SARs for ongoing suspicious activity after an initial SARs filing had been made. The

Commission attributed the SAR filing deficiencies to "conflicting and confusing directions" from new management of the Firm's AML program starting in approximately March 2012. The SEC also noted that the Firm did not offer new formal training or guidance during the relevant period. As a result of the SAR reporting deficiencies, the Commission found that the Firm willfully violated Section 17(a) of the Exchange Act and Rule 17a-8 thereunder. By the Commission's Order, the Firm was censured, ordered to cease and desist from future violations, and required to pay a $3.5 million civil monetary penalty. According to the SEC, the Firm voluntarily agreed to, among other things, review and update the relevant policies and provide additional training in this area. The Commission credited the Firm's prompt remedial efforts in accepting the Offer of Settlement.

***Windsor Street Capital, L.P. (f/k/a Meyers Associates, L.P.) and John David Telfer*, Exch. Act Rel. No. 81254, 2017 SEC LEXIS 2265 (July 28, 2017)**

The Commission accepted an Offer of Settlement from Windsor Street Capital, L.P., formerly known as Meyers Associates, L.P., based on an Order alleging that the Firm failed to file SARs and facilitated the unregistered sale of penny stock shares without performing reasonable diligence to determine whether those sales had to be registered with the Commission. According to the Commission's Order, the Firm and its Chief Compliance Officer/AML Officer, John Telfer, ignored numerous red flags, including ones raised by Windsor's clearing firm, that customer transactions might have been illegal and failed to properly investigate or report them. The Commission also found that the Firm took at face value its customers' representations that sales were exempt from Section 5 of the Securities Act under the safe harbor provisions of Rule 144, when a reasonable inquiry would have cast doubt on the customers' claims. The Commission determined that the Firm willfully violated Sections 5(a) and 5(c) of the Securities Act, as well as Section 17(a) of the Exchange Act and Rule 17a-8 thereunder. The Firm undertook to not accept customer deposits of stock trading at less than $5.00 a share, unless the orders were on the open market, and to hire an independent consultant to review and monitor the Firm's AML policies and procedures for two years. The Commission's sanctions against the Firm included a censure, an order to cease and desist from committing or causing future violations of securities laws, and a $200,000 civil monetary penalty. Separately, the Commission determined that Telfer willfully aided and abetted and caused Windsor's violations of Section 17(a) of the Exchange Act and Rule 17a-8 thereunder. Telfer agreed to an undertaking to provide additional information to the Commission upon reasonable notice, and he was ordered to cease and desist from future violations; barred from the securities industry; prohibited from acting as an employee, officer or director of an investment advisor, depositor or principal underwriter; and barred from participating in a penny stock offering in any capacity. Finally, the Commission imposed a $10,000 civil monetary fine against him.

Complex and Structured Products

***SEC v. Chan*, Litig. Rel. No. 23848, 2017 SEC LEXIS 1465 (May 26, 2017)**

On May 15, 2017, the Commission filed a complaint in the US District Court for the Southern

District of New York, and a final consent judgment was subsequently entered against Kee Chan, a former head trader on the Commercial Mortgage-Backed Securities (CMBS) Trading Desk at Nomura Securities International, Inc. Chan was alleged to have made material misrepresentations to customers in connection with CMBS transactions. The Commission found that, from 2009 to 2012, Chan provided false information about the prices at which the Firm purchased or sold the securities, bids and offers that the Firm made or received on the securities, the Firm's compensation, and who owned the security, including fabricating communications and negotiations with counterparties when the Firm already owned the securities. According to the Commission, these false representations allowed Chan to manipulate sale and purchase prices and increase the Firm's profits. As a result, the consent judgment found that Chan violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. The district court enjoined Chan from future violations and ordered him to pay $51,965 in disgorgement, $11,758 in prejudgment interest, and a $150,000 civil penalty. The Commission also entered an order that barred Chan from the securities industry and from participating in any capacity in a penny stock offering.

In re Barclays Capital Inc., Exch. Act Rel. No. 80560, 2017 SEC LEXIS 1288 (May 1, 2017)

The Commission accepted Offers of Settlement from Barclays Capital, Inc. and two former traders on its residential mortgage-backed securities (RMBS) trading desk, Yoon Seok Lee and David Wong. According to the Commission, from June 2009 to December 2012, the Firm failed to reasonably supervise Lee and Wong, who allegedly made material misrepresentations to customers and charged excessive markups in RMBS transactions. Lee and Wong conducted nonagency RMBS trades in the secondary market for Firm clients. The Commission found that Lee and Wong made false or misleading statements to the Firm's customers regarding the price of securities, the Firm's profit, and whether the Firm already held the security or the trader was negotiating with a third party. According to the Commission, these misrepresentations induced customers to accept less, or pay more, for securities than they otherwise might have and thereby increased the Firm's profits. The Commission also alleged that the Firm's RMBS desk charged customers excessive and undisclosed markups. The Firm, according to the Commission, did not have reasonable policies and procedures for monitoring communications to customers for misstatements, and its program for flagging excessive markups was not functioning properly during the relevant period due to a technology issue. As a result, the Commission found that Lee and Wong willfully violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder; and the Firm violated Section 15(b)(4)(E) of the Exchange Act by failing to supervise them. The Commission credited the Firm's cooperation and remedial efforts. The Firm also paid $15,561,711 in remediation to its clients. The Commission's ordered sanctions against the Firm included a censure, $9,603,502 in disgorgement, $2,106,541 in prejudgment interest (to be satisfied through the Firm's remediation to clients), and a $1,000,000 civil monetary penalty. Lee and Wong were both ordered to cease and desist from future violations, suspended from the securities industry for 12 months, and prohibited from associating with an investment advisor, depositor or principal underwriter for 12 months. Wong also was ordered to pay a $125,000 civil monetary penalty, and Lee was ordered to pay a $200,000 civil monetary penalty.

***In re Citigroup Global Markets, Inc.; In re Morgan Stanley Smith Barney, LLC*, Sec. Act Rel. No. 10288/10290, 2017 SEC LEXIS 216/218 (Jan. 24, 2017)**

The Commission accepted an Offer of Settlement from Citigroup Global Markets (Citigroup) and Morgan Stanley Smith Barney (MSSB) in connection with allegations that they each made false and misleading statements about the CitiFX Alpha Program, a foreign exchange trading program that was marketed to MSSB customers. At the time of the violations, Citigroup held a 49 percent ownership stake in MSSB. Between August 2010 to July 2011, the Commission found that Citigroup's and MSSB's written and verbal presentations about the CitiFX Alpha Program were based on the program's past performance and risk metrics, and failed to adequately disclose the degree of leverage that would be actually employed. Citigroup and MSSB also allegedly failed to adequately disclose that the brokerage customers and advisory clients would be charged markups on each trade. According to the Commission, the brokerage customers and advisory clients included individuals who had no experience in foreign exchange trading and did not fully appreciate the dynamics of such trading. As a result, the Commission found that Citigroup and MSSB each violated Section 17(a)(2) of the Securities Act. Citigroup and MSSB also each agreed to cease and desist from committing or causing any future violations and to pay disgorgement of $624,458, prejudgment interest of $89,277, and a $2.25 million civil monetary penalty for a total penalty of almost $6 million.

***In re Stifel, Nicolaus & Co., Inc., et al.*, Litig. Rel. No. 23700, 2016 SEC LEXIS 4538 (Dec. 7, 2016)**

The Commission settled allegations of misconduct and obtained admissions from Stifel, Nicolaus & Company, Inc. and its former Senior Vice President, David Noack, in a matter alleging that the Respondents misled five Wisconsin public school districts about the risks and suitability of leveraged collateralized debt obligations (CDOs) that ultimately failed and caused the school districts to lose their full investments. The Firm and Noack admitted to failing to disclose certain material facts to the school districts, including falsely overstating the benefits and downplaying the risks of the leveraged CDOs, particularly the likelihood that the school districts would lose their investment principal. They further admitted that retaining investment principal was particularly important to the school districts, which had no prior experience investing in CDOs, and that Stifel and Noack did not perform any independent suitability assessment of the CDOs. Under the terms of the settlement, the Court enjoined the Firm and Noack from future violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act, ordered the Firm and Noack jointly and severally to pay $1,660,000 in disgorgement and $840,000 in prejudgment interest, ordered the Firm to a pay a $22 million civil monetary penalty split between the Commission and school districts, and ordered Noack to pay a $100,000 civil monetary penalty. Separately, the Commission also entered an order barring Noack from the securities industry and from participating in any penny stock offering in any capacity.

Disclosures – Retirement Plan Customers

In re UBS Financial Services, Inc., Exch. Act. Rel. No. 81974, 2017 SEC LEXIS 3433 (Oct. 27, 2017)

The Commission accepted a Settlement Offer from UBS Financial Services, Inc., a registered broker-dealer and investment adviser. The Commission alleged that from at least January 2010 through June 2015, the Firm failed to ascertain whether certain retirement plan and charitable organization brokerage customers were eligible for less expensive share classes and recommended and sold them more expensive share classes in open-end registered investment companies without disclosing that the Firm would receive greater compensation for these purchases. Specifically, the Firm recommended and sold customers Class A shares with an up-front sales charge, or Class B or Class C shares with a back-end contingent deferred sales charge and higher ongoing fees and expenses, when the customers were eligible to purchase load-waived Class A and/or no-load Class R shares. The Firm has since issued payments with interest to all eligible customers who purchased more expensive shares, and converted all eligible customer holdings to the share class with the lowest expenses for which they are eligible. According to the SEC, by this conduct the Firm willfully violated Sections 17(a)(2) and 17(a)(3) of the Securities Act. In connection with this settlement, the Commission imposed sanctions that censured the Firm and ordered it to cease and desist from future violations and pay a $3.5 million civil monetary penalty. The Commission credited the Firm's cooperation and prompt remedial efforts in reaching this settlement.

Material Nonpublic Information - Supervision

In re LBMZ Securities, Inc., Exch. Act Rel. No. 81719, 2017 SEC LEXIS 3016 (Sept. 26, 2017)

The Commission accepted an Offer of Settlement from LBMZ Securities, Inc. The SEC alleged that the Firm failed to establish, maintain, and enforce policies and procedures to prevent the misuse of material nonpublic information (MNPI) by the Firm and its associated persons. The Firm is a registered broker-dealer that shares its CEO with Zacks Investment Research (ZIR), a division of which, Zacks Small Cap Research (SCR), provides "sponsored research" reports to small-cap issuers. In April 2013, the Firm created an investment banking division that sought to build from SCR's relationships with small-cap companies in need of capital and to refer its own companies to SCR for sponsored research, creating a compliance risk that the Firm's investment banking division would receive MNPI from SCR. According to the Commission, the Firm failed to follow policies and procedures to mitigate risk by inconsistently collecting brokerage statements from employees, reviewing a "trivial amount" of the Firm's interdepartmental emails, and failing to keep a log of reviewed communications. The Firm's information barrier was alleged to be inadequate because the Firm failed to conduct the "minimal elements" described in the Firm's Procedures, including reviews of employee transactions and substantive supervision of interdepartmental communications. As a result, the Commission's Order found that the Firm willfully violated Section 15(g) of the Exchange Act. The Commission's ordered sanctions

included an order to cease and desist from committing or causing any future violations, a censure, and a $240,000 civil monetary penalty. Relatedly, the SEC also settled insider trading charges with Bilal Basrai, the Firm's former Head of Investment Banking; Bryce Stirton, a former employee in the Firm's investment banking division; and Jason Napodano, SCR's former head research analyst. *See SEC v. Napodano, et al.*, Litig. Rel. No. 23943 (Sept. 26, 2017). Separately, Napodano and Basrai also pleaded guilty to criminal charges of securities fraud.

In re Sidoti & Co., LLC, Exch. Act Rel. No. 80027, 2017 SEC LEXIS 448 (Feb. 13, 2017)

The Commission accepted an Offer of Settlement from Sidoti & Company, LLC, a New York–based registered broker-dealer. According to the Commission, the Firm had no written policies or procedures in place to prevent the misuse of MNPI by its employees in connection with an affiliated hedge fund under common control with the Firm and operated by its founder and CEO. The hedge fund, by design, invested in issuers covered by the Firm's research department and some of the issuers for which the Firm provided investment banking services. Although the Firm had written policies preventing the misuse of MNPI by its investment banking and research departments, nothing in the Firm's written polices prevented its CEO and its associated persons from misusing MNPI obtained from these departments when making trading decisions for the hedge fund. The Commission noted that there were 126 instances when the hedge fund traded in a stock despite the fact that it appeared on the Firm's "daily restricted list." In response to concerns raised during a Commission examination, the Firm implemented written procedures that created information barriers to address the CEO's conflicting roles, but the procedures were not reasonably designed to enforce such information barriers. As a result, the Commission found that the Firm willfully violated Section 15(g) of the Exchange Act. The Firm was censured, ordered to cease and desist from further violations, and required to pay a $100,000 civil monetary penalty. The Commission considered the Firm's prompt remedial efforts and cooperation in accepting the Offer of Settlement.

Order-Handling Practices

In re Citadel Securities, LLC, Exch. Act. Rel. No. 79790, 2017 SEC LEXIS 99 (Jan. 13, 2017)

The Commission accepted a Settlement Offer from Citadel Securities LLC (Citadel), a registered broker-dealer. The Firm's wholesale market-maker, Citadel Execution Services (CES), provided a written disclosure to certain retail broker-dealer clients that described a market order as an "[o]rder to buy (sell) at the best offer (bid) price currently available in the marketplace," and made other, similar representations to its clients suggesting that it would either internalize the marketable order at, or seek to obtain through routing, the best bid or offer from the various market data feeds CES referenced. The Commission alleged that from late 2007 through January 2010, CES used proprietary algorithms that did not internalize marketable orders at, or seek to obtain through routing, the best price observed, contrary to its representations.

Citadel's algorithms were triggered when they identified differences in the best prices on market feeds, comparing the consolidated public feeds (known as SIP feeds for the Securities Information Processors that transmit them) to the direct feeds from exchanges. The Commission alleged that one of the algorithms, known as FastFill, immediately internalized orders at the SIP National Best Bid (NBB) or National Best Offer (NBO), without internalizing the order at the better bid or offer from one or more of the depth of book feeds or seeking to obtain that price through routing, resulting in a price to clients that was not the best price observed. The Commission also alleged that the Firm's second algorithm, SmartProvide, delayed the execution of marketable orders, which in some instances resulted in customers receiving a price that was worse than they would have received in the absence of SmartProvide. The Firm discontinued use of these algorithms in January 2010. According to the Commission, by this conduct, Citadel made materially misleading statements in willful violation of Section 17(a)(2) of the Securities Act. In connection with this settlement, the Commission imposed sanctions that censured the Firm, ordered it to cease and desist from future violations and pay disgorgement of $5.2 million, prejudgment interest of $1,465,268, and a $16 million civil monetary penalty.

Regulation SHO

***In re Wilson-Davis & Co., Inc.*, Exch. Act Rel. No. 80533, 2017 SEC LEXIS 1242 (Apr. 26, 2017)**

The Commission accepted a Settlement Offer from Wilson-Davis & Co., a Utah broker-dealer, based on an Order that alleged repeated and willful violations of Rule 203(b)(1) of Regulation SHO and the Market Access Rule, Section 15(c)(3) of the Exchange Act and Rule 15c3-5 thereunder. According to the SEC, from at least November 2011 through May 2013, the Firm's proprietary trading group erroneously relied on the bona fide market-making exception in Rule 203(b)(2) of Regulation SHO, and thereby failed to borrow or locate relevant securities prior to effecting short sales in those securities. The Commission explicitly noted that the Firm engaged in activities that were contrary to the guidance in the Commission's Adopting Release to the 2008 Amendments to Regulation SHO, such as posting quotations that were often not at or near the market on both sides and executing numerous short sales away from the Firm's posted offer quotations, among other examples.

The Commission also alleged that from 2012 through 2014, the Firm failed to have controls and supervisory procedures reasonably designed to prevent the entry of orders that exceeded preset capital thresholds or did not meet preorder regulatory requirements and erroneous orders in violation of the Market Access Rule. The Firm also allegedly failed to establish, maintain, or review the effectiveness of its risk management controls and supervisory procedures, including failing to properly review business activities in connection with market access, as well as failing to execute required CEO certifications. By the SEC's Order, the Firm was censured, ordered to cease and desist from future violations, and required to pay $208,645 in disgorgement, $27,068 in prejudgment interest, and a $75,000 civil monetary penalty. The Commission considered the Firm's remedial acts in determining to accept the Offer of

Settlement. The Commission previously had resolved related administrative proceedings for the same conduct with the Firm's CEO and head trader and one of the Firm's former proprietary traders. *See In re Barkley et al.*, Exch. Act Rel. No. 79578, 2017 SEC LEXIS 4658 (Dec. 16, 2016), and *In re Kerrigone*, Exch. Act Rel. No. 79579, 2017 SEC LEXIS 4659 (Dec. 16, 2016).

Sales Practices Violations

***SEC v. Zachary S. Berkey, et al.*, Litig. Rel. 24004, 2017 SEC Lexis 3903 (Dec. 6, 2017)**

On December 6, 2017, the Commission filed a complaint in the US District Court for the Southern District of New York against Daniel T. Fischer, a former registered representative, alleging that he violated the antifraud provisions of the federal securities laws based on his recommendations to customers, among other things. According to the Commission, Fischer had no reasonable basis to believe that the in-and-out trading strategy he recommended to customers was generally suitable for anyone and specifically suitable for the specific customers at issue. He allegedly churned customer accounts, engaged in unauthorized trading in certain of those accounts, and made material misrepresentations and omissions to customers. In particular, he failed to advise customers that the in-and-out trading strategy, after commissions and fees, likely would not produce gains for the customers. As a result of this conduct, Fischer violated Section 17(a) of the Securities Act, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. Fischer consented to a final judgment pursuant to which he was permanently enjoined from committing similar future violations and was ordered to pay disgorgement of $174,514, prejudgment interest of $13,517, and a $160,000 civil monetary penalty.

***SEC v. Buck*, Litig. Rel. No. 23974, 2017 SEC LEXIS 3458 (Oct. 31, 2017)**

On October 31, 2017, the Commission filed a complaint in the US District Court for the Southern District of Indiana and entered into a consent agreement with Thomas J. Buck, a former financial advisor at Merrill Lynch, Pierce, Fenner and Smith Incorporated, for engaging in a scheme to charge clients excessive fees and commissions. Buck allegedly generated higher commissions than he promised to clients, lied to clients about the amount of commissions he generated, failed to inform clients that fee-based accounts would be less expensive, and traded in client accounts without their authorization. He also allegedly provided misleading statements to his former firm about the commissions he charged in customer accounts. As a result of the conduct, he violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, Section 17(a) of the Securities Act, and Sections 206(1) and 206(2) of the Investment Advisers Act (Advisers Act). The court permanently enjoined Buck from future violations and ordered him to pay $2,561,236 in disgorgement, prejudgment interest of $296,806, and a $2,233,594 civil penalty. In a parallel criminal proceeding, he pleaded guilty to one count of securities fraud.

SEC Judgment Enforcement

SEC v. Hold Brothers On-Line Investment Services, LLC, Litig. Rel. No. 23740, 2017 SEC LEXIS 376 (Feb. 3, 2017)

The US District Court for the District of New Jersey entered a judgment against former broker-dealer Hold Brothers On-Line Investment Services, LLC (Hold Brothers), currently known as Tafferer Trading, LLC, enforcing the Commission's 2012 Consent Order finding that Hold Brothers had enabled and failed to adequately monitor layering or spoofing activities by certain offshore traders who accessed the US markets through the Firm. As a result of the 2012 Consent Order, the Firm was required to pay in five installments approximately $2.5 million in disgorgement, civil penalties, and interest. Hold Brothers made the first installment payment of $503,333, but defaulted on more than $2 million owed under the Commission's Order. In response to the Firm's default, the Commission sought to enforce compliance with the 2012 Consent Order and hold the owners personally liable as control persons for causing Hold Brothers' failure to comply with the Commission's Order. Hold Brothers consented to the Court's January 27, 2017 entry of a judgment enforcing the Commission's Consent Order, finding the Firm liable for the unpaid funds and ordering it to pay $707,764 in partial satisfaction of that judgment. The judgment also provided that the Commission would dismiss its then-pending claims against the individual owners.

Supervision

In re Coastal Equities, Inc. et al., Exch. Act. Rel. No. 82282, 2017 SEC LEXIS 4010 (Dec. 11, 2017)

The Commission accepted a Settlement Offer from Coastal Investment Advisors, Inc. (Coastal IA) and its affiliated broker-dealer, Coastal Equities, Inc. (Coastal Equities). In 2015, Coastal Equities' former President, CEO and COO, Michael Donnelly, pleaded guilty to fraud and was sentenced to 99 months' imprisonment for stealing approximately $1.5 million from his advisory clients and brokerage customers. To conceal his theft, Donnelly manually entered false information about client investments into consolidated financial reports that were provided to the clients. The Commission alleged that from at least 2009 through 2014, neither firm had policies and procedures reasonably designed to prevent and detect Donnelly's misuse of the consolidated reports, which were generated by using an electronic system maintained by Coastal Equities. According to the Commission, both firms knew that financial representatives were able to manually enter information into the reports, yet none of the reports were subject to mandatory review. As a result, the Commission found that Coastal Equities failed reasonably to supervise Donnelly, with a view toward preventing and detecting Donnelly's violations, and that Coastal IA willfully violated Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder. Respondents agreed to a settlement in which the Commission ordered sanctions that censured Coastal Equities and Coastal IA and ordered both firms to pay civil monetary penalties of $40,000. The Commission credited the firms' self-reporting, cooperation, and prompt remedial efforts in reaching this settlement.

Underwriter Due Diligence

***In re Lawson Financial Corp. et al.*, Exch. Act Rel. No. 80376, 2017 SEC LEXIS 1043 (Apr. 5, 2017)**

The Commission accepted a Settlement Offer from Lawson Financial Corporation (LFC), a registered broker-dealer; its former CEO, Robert Lawson (Lawson); and its former underwriter's counsel. The Commission alleged that from 2010 to 2014 LFC failed in its role as a gatekeeper when underwriting conduit bond offerings to purchase and renovate nursing homes and senior living facilities. The bond offerings were later determined to be fraudulent. According to the Commission, LFC and Lawson conducted inadequate due diligence on the bond offerings; in particular, LFC and Lawson conducted only a cursory review of the information provided to them, relied on oral assurances, and failed to investigate numerous red flags. The Commission asserted that these failures deprived buyers and sellers in the secondary market of material information about the offerings and permitted the related fraud to go undetected. LFC also failed to obtain a written continuing disclosure for an April 2013 offering, despite the representation in the official statement that such a disclosure existed.

As a result, the Commission determined that LFC and Lawson willfully violated Sections 17(a)(2) and (3) of the Securities Act. LFC also willfully violated Section 15(c)(2) of the Exchange Act and Rule 15c-12 thereunder, and Lawson aided and abetted and caused the Firm's violations of Section 15(c)(2) of the Exchange Act and Rule 15c-12 thereunder related to his failure to obtain a Continuing Disclosure Agreement for an offering. LFC and Lawson were ordered to cease and desist from future violations and were jointly and severally ordered to pay disgorgement of $178,750, plus prejudgment interest of approximately $20,000. LFC was censured and required to pay a civil monetary penalty of approximately $200,000. The Commission noted that LFC would have been eligible for more lenient remedies had it participated in the Municipalities Continuing Disclosure Cooperation (MCDC) Initiative. Lawson was barred from the securities industry and prohibited from acting as an officer or director. He was ordered to pay a civil monetary penalty of $80,000.

Undisclosed Markups and Markdowns

***In re State Street Global Markets, LLC, State Street Global Advisors Funds Distributors, LLC, and State Street Bank and Trust Co.*, Exch. Act. Rel. No. 81543, 2017 SEC LEXIS 2752 (Sept. 7, 2017)**

The Commission accepted a Settlement Offer from State Street Bank and Trust Company and associated registered broker-dealers, State Street Global Markets, LLC (SSGM), and State Street Global Advisors Funds Distributors, LLC, wholly owned subsidiaries of State Street Corporation (collectively, the Firm). The Commission alleged that from February 2010 to September 2011, the Firm carried out a scheme to defraud customers by charging hidden and unauthorized markups and commissions for transition management services. These services were marketed to institutional customers as a means to help reduce the costs of "transitions," such as a change

in investment advisors or strategies. Specifically, the President and Member of the Executive Management Group for SSGM, Ross I. McLellan, and two former UK employees under his direction charged hidden markups or commissions to six transition management customers. Based on recorded telephone calls and email communications, the Commission alleged that McLellan gave specific instructions to traders in the United States and United Kingdom aimed at keeping these markups and commissions hidden.

As a result of the conduct, the Commission found that there were willful violations of Sections 17(a)(1) and 17(a)(3) of the Securities Act, and Section 10(b) of the Exchange Act and Rules 10b-5(a) and (c) thereunder, and that SSGM willfully violated Section 15(c)(1) of the Exchange Act. After the fraud was discovered, SSGM and State Street Global Markets International contacted the defrauded customers and voluntarily refunded all undisclosed markups and commissions. The Firm also agreed, among other things, to retain a qualified independent ethics and compliance consultant. In addition, the Commission imposed sanctions, including a censure, an order to cease and desist from future violations, and a $32.3 million civil monetary penalty. The Commission has individually charged McClellan with fraud, and that matter is pending.

***In re Louis Capital Markets, LP*, Exch. Act Rel. No. 80332, 2017 SEC LEXIS 981 (Mar. 29, 2017)**

The Commission accepted an Offer of Settlement from Louis Capital Markets, LP, a registered broker-dealer located in New York, based on an Order alleging that the Firm charged customers undisclosed markups and markdowns during times of high volatility. The Firm's cash equity desk operated as an interdealer broker on an agency basis, executing trades on behalf of its customers in exchange for agreed-upon commission rates between $0.01 and $0.03 per share. According to the Commission, the members of the Firm's cash equity desk deceived customers by clandestinely marking share prices up or down when reporting transactions to them. Doing so caused customers to overpay the Firm. Neither the markups and markdowns nor the Firm's secret profits were disclosed to customers, who were provided false prices on thousands of securities transactions. The Commission further alleged that the Firm attempted to conceal the markups and markdowns from customers by making them at times when the customers would be least likely to notice them, such as during times of high market volatility. The cash equity desk ceased operations in 2013 and the individuals associated with the misconduct are no longer employed at the Firm. The Commission's Order found that the Firm willfully violated Section 15(c)(1) of the Exchange Act. The Commission's Order included an order to cease and desist from future violations, a censure, and a $2,500,000 disgorgement payment. The Commission noted that a substantial penalty would have been appropriate based on the evidence, but declined to impose a civil monetary penalty based on the unique circumstances of the Firm, including its financial condition.

Cases Relating to Investment Advisers/Investment Companies and Their Employees/Affiliated Persons[76]

Allocation of Fees and Expenses

In re Paramount Group Real Estate Advisor LLC, Investment Advisers Act Rel. No. 4726, 2017 SEC LEXIS 2037 (July 6, 2017)

The Commission accepted an offer of settlement from Paramount Group Real Estate Advisor LLC (Respondent), a registered investment adviser. The Commission alleged that Respondent caused a garage to be sold by a private fund managed by Respondent (Seller Fund) to another private fund managed by Respondent (Buyer Fund) and failed to cause Buyer Fund to reimburse Seller Fund for certain development expenses that Seller Fund had incurred before the sale despite its obligation to do so. The Commission also alleged that Respondent failed to seek approval from Seller Fund's Investment Advisory Council, or the Limited Partners, to eliminate the reimbursement requirement as a condition of the sale of the garage, or to disclose to them, at the time, its decision not to cause Buyer Fund to make the reimbursement despite its commitment to do so. Respondent had a conflict of interest because it owed a fiduciary duty to both sides of the transaction, and because, at the time, it owned a larger percentage share of Buyer Fund than Seller Fund. As a result of the alleged conduct, the Commission ordered that Respondent cease and desist from committing or causing any violations and any future violations of Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-8 promulgated thereunder. In addition, the Commission censured Respondent. Finally, the Commission ordered that Respondent pay a civil money penalty of $250,000.

In re. Capital Dynamics, Inc., Investment Advisers Act Rel. No. 4746, 2017 SEC LEXIS 2508 (Aug. 16, 2017)

The Commission accepted an offer of settlement from Capital Dynamics, Inc. (Respondent), a registered investment adviser, in connection with Respondent's failure to properly allocate expenses to a private equity fund client. The Commission alleged that Respondent caused the fund to pay $1,273,148 in certain legal, hiring, and consulting expenses that should not have been borne by the fund, according to the fund's organizational documents. The organizational documents allegedly stated that the fund was responsible for paying its own "normal operating expenses," including "all routine, recurring expenses incident to" its own operations, and expenses incurred in connection with the establishment and sale of the fund. However, Respondent allegedly allocated expenses, such as legal expenses, in connection with negotiations of an Umbrella Agreement to the fund. The Commission further alleged that Respondent failed to adopt policies and procedures reasonably designed to prevent such improper expense allocations. As a result, the Commission alleged that Respondent violated

[76] Because of dual registration or multiple parties, a number of the previously discussed cases in the prior section titled "Cases Relating to Broker-Dealer Firms and Their Employees/Affiliated Persons" could be placed in this section as well; however, we have chosen not to repeat them here.

Sections 206(2) and 206(4) of the Advisers Act and Rules 206(4)-7 and 206(4)-8 thereunder. In determining to accept the settlement offer, the Commission considered Respondent's remedial acts, which included retaining additional compliance staff, enhancing employee training, revising policies and procedures, and voluntarily reimbursing the fund $1,405,537 for improperly charged expenses. The Commission ordered Respondent to cease and desist from committing or causing any violations and any future violations of Sections 206(2) and 206(4) of the Advisers Act and Rules 206(4)-7 and 206(4)-8 thereunder. The Commission also ordered Respondent to pay a civil money penalty of $275,000.

***In re Potomac Asset Management Co., Inc. and Goodloe E. Byron, Jr.*, Investment Advisers Act Rel. No. 4766, 2017 SEC LEXIS 2796 (Sept. 11, 2017)**

The Commission accepted an offer of settlement from Potomac Asset Management Company, Inc. (PAMCO) and Byron, its principal (collectively, Respondents), for improperly allocating fees and expenses to two private equity fund clients, Potomac Energy Fund, L.P. (Fund I) and Potomac Energy Fund II, L.P. (Fund II) (collectively, Funds). The Commission specifically alleged that PAMCO, controlled by Byron, improperly charged $2.2 million in fees to Fund I for services that its affiliates provided to a portfolio company of Fund I, despite not being authorized to do so and failing to disclose to the fund's limited partners this use of the fund's assets. The Commission further alleged that PAMCO improperly used the assets of the Funds to pay PAMCO's adviser-related expenses, which, in addition to the Firm's rent and other operational expenses, included compensation to a member of the investment team in order to pay rent and other expenses. This use of the Funds' assets was neither authorized nor disclosed by the Funds' governing documents. The Funds' audited financial statements also failed to disclose that these payments were a related party transaction, causing them to not be prepared in accordance with Generally Accepted Accounting Principles (GAAP). As a result, PAMCO failed to meet the audit exception under Advisers Act Rule 206(4)-2, the Custody Rule, for private funds. Finally, the Commission alleged that PAMCO failed to implement written compliance policies and procedures for the allocation of portfolio company fees and adviser-related expenses between it and the Funds, and further failed to disclose in its Form ADV that PAMCO charged the Funds for the adviser-related costs that it expensed to them. As a result of this alleged conduct, the Commission stated that Respondents violated Sections 206(2), 206(4) and 207 of the Advisers Act and Rules 206(4)-2, 206(4)-7 and 206(4)-8 thereunder. The Commission censured Respondents, and ordered them to cease and desist from committing further violations of the antifraud provisions of the Advisers Act and to jointly and severally pay a civil money penalty of $300,000. The Commission stated that in determining to accept Respondent's offer, it considered the fact that PAMCO hired a new Chief Compliance Officer, constituted a Limited Partner Advisory Board, engaged an independent compliance consultant, and voluntarily reimbursed the Funds for the improper fees and expenses it incurred or otherwise failed to reimburse during the relevant period.

***In re Platinum Equity Advisors, LLC*, Investment Advisers Act Rel. No. 4772, 2017 SEC LEXIS 2943 (Sept. 21, 2017)**

The Commission accepted an offer of settlement from Platinum Equity Advisors (Respondent), a registered investment adviser that managed three private equity funds, for improperly allocating

broken-deal expenses. According to the Commission, from 2004 to 2015 Respondent invested approximately $5,300,000,000 in 85 companies through the funds it managed, while also investing approximately $728,000,000 into the same companies through co-investment vehicles advised and managed by Respondent. The co-investors in these vehicles were affiliates of Respondent, the funds' general partner, and members, officers, directors, and employees of Respondent and its affiliates. The Commission stated that the limited partnership agreements (LPAs) and private placement memoranda (PPMs) for the funds disclosed that the funds were responsible for all expenses of the partnership (other than general partner expenses), including broken-deal expenses for transactions where Respondent incurred expenses to develop, negotiate, and structure potential investment opportunities that ultimately were not consummated. However, the LPAs did not disclose that the funds would also pay the broken-deal expenses for the portion of each investment that would have been allocated to Respondent's co-investors, who participated in and benefited from Respondent's sourcing of private equity transactions. The Commission alleged that this resulted in the funds being improperly subjected to broken-deal expenses without disclosure in the LPAs, including $1,811,501 in such expenses since 2Q 2012. The Commission further alleged that Respondent did not adopt and implement written policies and procedures governing its fund expense allocation practices. As a result, the Commission alleged that Respondent violated Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-7 thereunder. The Commission ordered Respondent to cease and desist from committing further violations of the Advisers Act, and ordered it to pay a civil money penalty of $1,500,000 and disgorgement and prejudgment interest of $1,902,132.

Calculation of Advisory Fees

***In re Morgan Stanley Smith Barney, LLC*, Investment Advisers Act Rel. No. 4607, 2017 SEC LEXIS 107 (Jan. 13, 2017)**

The Commission accepted an offer of settlement from Morgan Stanley Smith Barney, LLC (Respondent). The Commission alleged that Respondent inadvertently erred in calculating advisory client fee billings as a result of the combination between Respondent's subsidiary and a division of another large financial institution. The Commission further alleged that between 2002 and 2016 coding errors in its billing systems and processes caused Respondent and its predecessor to inadvertently charge fees in excess of the fees agreed upon by certain advisory clients, amounting to more than $16,000,000. The Commission further alleged that Respondent failed to maintain certain signed client contracts. The Commission also alleged that Respondent failed to enter into a written agreement for a historic surprise custody examination with an independent accountant to verify client funds and securities for approximately 1 million legacy accounts over which Respondent maintained custody; however, the Commission acknowledged that Respondent engaged an accountant to conduct a supplemental examination the following year. The Commission further alleged that in two separate custody examinations, Respondent provided incorrect universes of advisory accounts for which it maintained custody to its accountants that caused the percentage of custody accounts being examined by the accountant to be skewed. The Commission further alleged that Respondent failed to adopt and implement

written policies and procedures reasonably designed to prevent all of the previously alleged violations from occurring.
As a result of this alleged conduct, the Commission censured Respondent, and ordered that it cease and desist from causing any violations or further violations of Sections 204(a), 206(2) and 206(4) of the Advisers Act and Rules 204-2, 206(4)-2, and 206(4)-7 promulgated thereunder. Respondent was further ordered to pay a civil money penalty of $13,000,000. Further, the Commission ordered that Respondent comply with certain undertakings.

***In re Citigroup Global Markets, Inc.*, Investment Advisers Act Rel. No. 4626, 2017 SEC LEXIS 263 (Jan. 26, 2017)**

The Commission accepted an offer of settlement from Citigroup Global Markets, Inc. (Respondent). The Commission alleged that Respondent erred in calculating advisory client fee billings as a result of the combination of a business division of Respondent and another large financial institution. The Commission alleged that clients were overbilled as a result of Respondent's (A) failure to honor reduced advisory fee rates, (B) coding errors that caused clients moving between advisers at different branch offices to have a standard advisory fee applied when they previously negotiated a reduced advisory fee, and (C) failure to prorate advisory fees for terminated or temporarily suspended client accounts. Further, the Commission alleged that Respondent failed to maintain and preserve executed client contracts in an easily accessible place. The Commission alleged that Respondent failed to adopt and implement written policies and procedures to ensure that advisory fees were appropriately calculated and applied. As a result, the Commission censured Respondent; ordered that it cease and desist from causing any violations or further violations of Sections 204(a), 206(2), and 206(4) of the Advisers Act and Rules 204-2 and 206(4)-7 promulgated thereunder; and ordered it to pay a civil money penalty of $14,300,000, disgorgement of $3,200,000, and prejudgment interest of $800,000. Further, the Commission ordered that Respondent comply with certain undertakings.

***In re Barclays Capital Inc.*, Investment Advisers Act Rel. No. 4705, 2017 SEC LEXIS 1369 (May 10, 2017)**

The Commission accepted an offer of settlement from Barclays Capital, Inc., a registered broker-dealer that during the relevant period was also a registered investment adviser (Respondent). The Commission alleged that from September 2010 to December 2015 Respondent failed to perform, in a manner consistent with its promises to clients, due diligence on certain third-party managers in its wrap-fee programs, and materially misrepresented its due diligence practices in its Form ADV. The Commission further alleged that Respondent charged fees in excess of its express representations to certain advisory clients as a result of inadequate controls relating to valuation, use of disparate systems relying on manual processes, and lack of appropriate oversight; failed to provide, due to a lack of adequate systems or processes, the opportunity for eligible advisory clients to receive fee waivers or less expensive mutual fund share classes; and failed to adopt and implement written policies and procedures reasonably designed to prevent Advisers Act violations. The Commission censured Respondent and ordered it to cease and desist from further violating Sections 17(a)(2) and 17(a)(3) of the Securities Act, and Sections 206(2), 206(4) and 207 of the Advisers Act and Rule 206(4)-7

thereunder, and imposed disgorgement of $49,785,417, prejudgment interest of $13,752,242, and a $30,000,000 civil money penalty on Respondent, with no penalty offset in any Related Investor Action. The Commission further ordered Respondent to comply with an undertaking to pay remediation of $3,504,285 to clients and former clients affected by the underperformance of the strategies whose third-party adviser providers were insufficiently due diligenced, and by the excess share class fees when cheaper share classes were available.

***In re Coachman Energy Partners LLC and Randall D. Kenworthy*, Investment Advisers Act Rel. No. 4743, 2017 SEC LEXIS 2478 (Aug. 14, 2017)**

The Commission accepted an offer of settlement from Coachman Energy Partners LLC (Coachman), a registered investment adviser, and Randall D. Kenworthy (Kenworthy), the sole owner and Chief Executive Officer of Coachman (collectively, Respondents). The Commission alleged that Respondents failed to adequately disclose their methodology for calculating management fees and management-related expenses charged to several funds (the Funds) in Coachman's Form ADV and the Funds' operating documents. The Commission alleged that as a result, Respondents overcharged the Funds approximately $1.1 million in management fees and $449,000 in management-related expenses. The Commission further alleged that Respondents caused one of the Funds to enter into a transaction with an affiliated entity without adequately disclosing or obtaining investor consent to the associated conflicts of interest. The Commission censured Respondents and ordered that they cease and desist from committing or causing any violations and any future violations of Sections 206(2) and 207 of the Advisers Act. The Commission ordered Coachman to pay disgorgement of $2,088,087, plus prejudgment interest of $165,559, offset by $1,362,139 in management fees and expenses owed by the Funds to Coachman resulting in a net payment of $891,507 to a distribution fund. Each Respondent was ordered to pay a civil money penalty of $50,000.

***In re Institutional Investors Advisory Company,* Investment Advisers Act Rel. No. 4747, 2017 SEC LEXIS 2534 (Aug. 16, 2017)**

The Commission accepted an offer of settlement from Institutional Investors Advisory Company (Respondent), a registered investment adviser, in connection with certain failures to make adequate disclosures to clients. The Commission alleged that Respondent advised an investment fund (IIIF) controlled by Respondent's owner and also served as the investment adviser to certain institutions that invested in IIIF though Management Agency Agreements (MAAs). The Commission alleged that the MAAs stated that investors would receive a distribution of all income less expenses earned on investments in IIIF. The Commission alleged that Respondent did not disclose to investors that, contrary to the MAAs, IIIF retained investors' pro rata shares of undistributed earnings held in a reserve fund at the time of investors' withdrawal. Further, the Commission alleged that Respondent did not disclose the conflict of interest resulting from the fact that Respondent's advisory fees were applied to all of IIIF's assets, including investor profits retained in the reserve fund (thereby incentivizing Respondent to retain more of IIIF's income in the reserve fund rather than distributing such earnings to investors). The Commission alleged that, as a result of the conduct above, Respondent violated Section 206(2) of the Advisers Act. The Commission ordered Respondent to cease and desist from committing or causing any violations and any future violations of Section 206(2) of the

Advisers Act. Respondent was ordered to pay disgorgement of $531,680, prejudgment interest thereon of $61,507, and a civil monetary penalty in the amount of $250,000 into a Fair Fund. Respondent also agreed to pay $1,268,536, representing the amount of profits that the MAA investors left upon their withdrawal from IIIF, and prejudgment interest thereon of $146,750, in order to compensate the investors for any harm caused, and the Commission took this undertaking into account in determining whether to accept the offer of settlement.

Conflict of Interest Disclosure

In re Centre Partners Management, LLC, Investment Advisers Act Rel. No. 4604, 2017 SEC LEXIS 68 (Jan. 10, 2017)

The Commission accepted an offer of settlement from Centre Partners Management, LLC (Respondent), a registered investment adviser and the manager of four private equity funds and related parallel entities, for allegedly breaching its fiduciary duties to its fund clients and failing to disclose material conflicts of interests to the funds' investors. The Commission specifically alleged that three of Respondent's principals owned interests in an information technology service provider, controlled its board of directors, and had other close familial relations with the service provider's president and Chief Executive Officer. The Commission alleged that these conflicts of interest were not disclosed, as required by the funds' governing documents, to the advisory committees of the funds that were responsible for reviewing and approving conflicts. The Commission conceded that Respondent disclosed engaging the service provider, but the Commission alleged that Respondent did not disclose the relationships between Respondent's principals and the service provider until it began marketing its sixth fund. The Commission censured Respondent, ordered that it cease and desist from further violations of Section 206(2) and 206(4) of the Advisers Act and Rule 206(4)-8 promulgated thereunder, and ordered it to pay a civil money penalty of $50,000.

In re TPG Capital Advisors, LLC, Investment Advisers Rel. No. 4830, 2017 SEC LEXIS 4189 (Dec. 21, 2017)

The Commission accepted an offer of settlement from TPG Capital Advisers (Respondent), a private equity fund adviser. The Commission alleged that, upon either the private sale or an IPO of a portfolio company, Respondent terminated certain portfolio company monitoring agreements and accelerated the payment of future monitoring fees pursuant to the agreements. The Commission also alleged that Respondent did not disclose future accelerated monitoring fees upon termination of the monitoring agreements to its funds or their investors prior to committing capital, despite disclosing that it may receive monitoring fees from portfolio companies held by funds it advised and the amount of fees that had accelerated. Because receipt of accelerated monitoring fees from four portfolio companies would have been a conflict of interest for Respondent, the Commission alleged that Respondent could not effectively consent to this practice on behalf of the funds it advised and, as a result, the Commission stated that Respondent breached its fiduciary duty to the funds in violation of Section 206(2) of the Advisers Act, and also violated Section 206(4) of the Advisers Act and Rule 206(4)-8 thereunder. The Commission further alleged that Respondent violated Section 206(4) of the

Advisers Act and Rule 206(4)-7 thereunder by failing to adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act arising from the conflicts of interest associated with its undisclosed receipt of fees. Lastly, the Commission alleged that Respondent violated Sections 206(2) and 206(4) of the Advisers Act and Rules 206(4)-8 and 206(4)-7 thereunder as a result of such negligent conduct. The Commission ordered Respondent to cease and desist from current and future violations of the Advisers Act, and ordered it to pay a $3,000,000 civil penalty, disgorgement of $9,487,620, and prejudgment interest of $361,507.

Conflict of Interest Disclosure – Forgivable Loans & Recruitment Benefits

In re TRH Financial LLC, **Investment Advisers Act Rel. No. 4776, 2017 SEC LEXIS 3019 (Sept. 26, 2017)**

The Commission accepted an offer of settlement from registered investment adviser TRH Financial LLC (Respondent) for failure to accurately and completely disclose to clients that it received a forgivable loan of approximately $350,000 from a broker-dealer that provided it with clearing and custodial services for its advisory clients. The Commission specifically alleged that the forgivable loan, which was entered into in connection with the initial agreement between Respondent and the broker-dealer, was structured so that the loan would be forgiven over a five-year period on a straight-line basis, provided that Respondent's owner continued to be associated as a registered representative of the broker-dealer and was otherwise compliant with his contractual obligations with that broker-dealer. The Commission stated that the resulting conflict of interest was not adequately disclosed to clients in Respondent's Form ADV Part 2A brochure and accompanying Part 2B brochure supplements or otherwise. The Commission also alleged that Respondent, in addition to failing to disclose the form of forgiveness of the forgivable loans, did not disclose that the receipt of the loans created a financial incentive for it to select the broker-dealer for clearance and custody of its advisory client accounts. The Commission alleged that as a result of this conduct, Respondent violated Sections 206(2) and 207 of the Advisers Act. The Commission censured Respondent, ordered it to cease and desist from further violations of the Advisers Act, and required that it pay a civil money penalty of $35,000.

In re 360 Financial, Inc., **Investment Advisers Act Rel. No. 4777, 2017 SEC LEXIS 3020 (Sept. 26, 2017)**

The Commission accepted an offer of settlement from registered investment adviser 360 Financial, Inc. (Respondent) for failure to accurately and completely disclose to clients that it received a forgivable loan of approximately $446,356 from a broker-dealer that provided it with clearing and custodial services for its advisory clients. The Commission specifically alleged that the forgivable loan, which was entered into in connection with the initial agreement between Respondent and the broker-dealer, was structured so that the loan would be forgiven over a five-year period on a straight-line basis, provided that Respondent's owner continued to be associated as a registered representative of the broker-dealer and was otherwise compliant with

his contractual obligations with that broker-dealer. The Commission stated that the resulting conflict of interest was not adequately disclosed to clients in Respondent's Form ADV Part 2A brochure and accompanying Part 2B brochure supplements or otherwise. The Commission also alleged that Respondent, in addition to failing to disclose the form of forgiveness of the forgivable loans, did not disclose that the receipt of the loans created a financial incentive for it to select the broker-dealer for clearance and custody of its advisory client accounts. The Commission alleged that as a result of this conduct, Respondent violated Sections 206(2) and 207 of the Advisers Act. The Commission censured Respondent, ordered it to cease and desist from further violations of the Advisers Act, and required that it pay a civil money penalty of $40,000.

***In re VisionPoint Advisory Group, LLC*, Investment Advisers Act Rel. No. 4778, 2017 SEC LEXIS 3021 (Sept. 26, 2017)**

The Commission accepted an offer of settlement from registered investment adviser VisionPoint Advisory Group, LLC (Respondent) for failure to accurately and completely disclose to clients that it received a forgivable loan of more than $1,300,000, and additional nonforgivable loans, from a broker-dealer that provided it with clearing and custodial services for its advisory clients. The Commission specifically alleged that the forgivable and nonforgivable loans, which were entered into in connection with the initial agreement between Respondent and the broker-dealer, was structured so that the forgivable loan would be forgiven over a five-year period on a straight-line basis, provided that Respondent's owner and two of its investment adviser representatives continued to be associated as registered representatives of the broker-dealer and were otherwise compliant with their contractual obligations with that broker-dealer. The Commission stated that the resulting conflict of interest was not adequately disclosed to clients in Respondent's Form ADV Part 2A and accompanying Part 2B brochure supplements or otherwise. The Commission also alleged that Respondent, in addition to failing to disclose the form of forgiveness of the forgivable loans, did not disclose that the receipt of the loans created a financial incentive for it to select the broker-dealer for clearance and custody of its advisory client accounts. The Commission alleged that as a result of this conduct, Respondent violated Sections 206(2) and 207 of the Advisers Act. The Commission censured Respondent, ordered it to cease and desist from further violations of the Advisers Act, and required that it pay a civil money penalty of $45,000.

Conflict of Interest Disclosure – Mutual Fund Share Class Selection

***In re Alison, LLC and Stephen D. Alison*, Investment Advisers Act Rel. No. 4673, 2017 SEC LEXIS 972 (Mar. 29, 2017)**

The Commission accepted an offer of settlement from Alison, LLC (ALLC), a registered investment adviser, and Stephen D. Alison, its principal (collectively, Respondents). The Commission alleged that over a three-year period during which ALLC had escalating financial difficulties, a significant component of its revenue was produced from 12b-1 fee payments that were paid to ALLC out of advisory client assets. The Commission stated that ALLC failed to

disclose to clients that lower cost share classes with identical exposure were available that did not carry such 12b-1 fees, and that Respondents had an undisclosed conflict of interest with their clients given their incentive to choose a mutual fund share class that carried these 12b-1 fees. The Commission stated that Respondents further misrepresented in ALLC's Forms ADV and updating amendments that Alison did not receive 12b-1 fee payments. The Commission additionally alleged that Respondents repeatedly failed to produce required books and records to Commission staff, and failed to disclose to clients that ALLC's distressed financial condition was reasonably likely to impair its ability to meet contractual commitments to clients. The Commission ordered Respondents to cease and desist from further violations of Sections 204(a), 206(2), and 207 of the Advisers Act; barred Alison from association with a right to reapply after three years; and revoked ALLC's registration as an investment adviser.

***In re Credit Suisse Securities USA (LLC)*, Investment Advisers Act Rel. No. 4678, 2017 SEC LEXIS 1033 (Apr. 4, 2017); *In re Sanford Michael Katz*, Investment Advisers Act Rel. No. 4679, 2017 SEC LEXIS 1035 (Apr. 4, 2017)**

The Commission accepted an offer of settlement from Credit Suisse Securities (USA) LLC (Respondent), a dually registered broker-dealer and investment adviser. The Commission alleged that Respondent's investment adviser representatives purchased Class A mutual fund shares (with respect to which shareholders were charged 12b-1 fees) for advisory clients who were eligible to purchase less expensive institutional share classes of the same mutual funds where 12b-1 fees were not imposed, thereby failing to obtain best execution for the relevant transactions. The 12b-1 fees were allegedly passed through to Respondent, which in turn paid a portion of that amount to its investment adviser representatives (IARs), thereby decreasing the value of advisory clients' investments in mutual funds and increasing the compensation paid to Respondent and its IARs. The Commission alleged that Respondent's disclosures, both with respect to Respondent's potential receipt of 12b-1 fees in general and with respect to particular IARs in the applicable brochure supplements, did not sufficiently inform its advisory clients of the resulting conflict of interest. The Commission further alleged that Respondent failed to update its policies and procedures to require IARs to evaluate institutional share classes in comparison to other mutual fund share classes and to address instances where IARs were purchasing and holding Class A shares when less costly institutional share classes were available. The Commission censured Respondent and ordered Respondent to cease and desist from committing or causing any violations and any future violations of Sections 206(2), 206(4), and 207 of the Advisers Act and Rule 206(4)-7 promulgated thereunder and to pay $2,099,624 in disgorgement plus prejudgment interest of $380,090 and a civil money penalty of $3,275,000.

In a related action, the Commission accepted an offer of settlement from Sanford Katz, an IAR at Respondent, who was responsible for managing wrap-fee advisory accounts using his own strategy, which utilized investments in mutual funds to a greater degree than other IARs servicing advisory clients in the same program. The Commission alleged that Katz purchased Class A shares of mutual funds for advisory client accounts despite such clients being eligible for less expensive institutional share classes of the same mutual funds, and that this practice generated approximately $2,500,000 in 12b-1 fees for the Firm, approximately $1,100,000 of which was paid to Katz. As a result of this conduct, the Commission alleged that Katz breached

his fiduciary duty and obligation to achieve best execution for advisory clients. The Commission censured Katz, ordered him to cease and desist from further violations of Section 206(2) of the Advisers Act, and ordered him to pay $1,124,859 in disgorgement, prejudgment interest of $197,587, and a civil money penalty of $850,000.

In re Cadaret, Grant & Co., Inc, Investment Advisers Act Rel. No. 4736, 2017 SEC LEXIS 2308 (Aug. 1, 2017)

The Commission accepted an offer of settlement from Cadaret Grant & Co., Inc. (Respondent), a dually registered investment adviser and broker-dealer, in connection with its role in investing advisory clients in mutual fund share classes with 12b-1 fees. The Commission alleged that Respondent invested advisory clients in mutual fund share classes with 12b-1 fees instead of share classes of the same funds without 12b-1 fees, and, as a result, Respondent received at least $1.93 million in 12b-1 fees and $235,000 in marketing support payments. The Commission alleged that Respondent did not disclose that it had a conflict of interest in connection with the selection of mutual fund share classes. Further, the Commission alleged that these investments were inconsistent with Respondent's Form ADV disclosures that noted that it would seek best execution for Respondent's clients because, by investing clients in mutual fund share classes with higher fees, Respondent failed to comply with its duty to provide best execution, and that as a result the Form ADV disclosures were materially misleading. The Commission also alleged that Respondent failed to disclose that it would retain unearned prepaid advisory fees. As a result, the Commission alleged that Respondent violated Sections 206(2), 206(4), and 207 of the Advisers Act and Rule 206(4)-7 thereunder. The Commission censured Respondent and ordered that Respondent cease and desist from committing or causing any violations and any future violations of Sections 206(2), 206(4), and 207 of the Advisers Act and Rule 206(4)-7 thereunder. The Commission further ordered that Respondent pay a civil penalty of $280,000, disgorgement of $2,591,000, and prejudgment interest of $177,000.

In re Envoy Advisory, Inc., Investment Advisers Act Rel. No. 4764, 2017 SEC LEXIS 2780 (Sept. 8, 2017)

The Commission accepted an offer of settlement from Envoy Advisory, Inc. (Respondent), a registered investment adviser, for breaching its fiduciary duty and various compliance deficiencies in connection with its recommendation to clients of higher-fee mutual fund share classes without sufficient disclosure. The Commission specifically alleged that Respondent failed to adequately inform its advisory clients of the conflicts of interest presented by its recommendations to purchase Class A mutual fund shares, which carried 12b-1 fees of 25 basis points per year that were payable to Respondent's affiliated broker-dealer. Although Respondent disclosed in its Form ADV to retirement plan clients that certain mutual funds "may" pay a "dealer" such 12b-1 fees, the Commission alleged that Respondent failed to disclose to such clients that the "dealer" receiving the 12b-1 fees was Respondent's affiliated broker-dealer, and the conflict this presented. Additionally, the Commission alleged that Respondent failed to disclose anything regarding 12b-1 fees or the conflict of interest associated with its affiliate's receipt of such fees in its Form ADV disclosures to IRA clients. Further, the Commission stated that during the relevant period, Respondent failed to adopt and implement written compliance policies and procedures governing mutual fund share class selection, and

failed to implement the policies and procedures it had adopted regarding conflicts of interest. As a result of this conduct, the Commission alleged that Respondent violated Sections 206(2), 206(4), and 207 of the Advisers Act and Rule 206(4)-7 thereunder. In considering whether to accept the offer of settlement, the Commission considered the remedial acts undertaken by Respondent, which included (1) no longer recommending investments in share classes that carried 12b-1 fees, and transitioning existing advisory client assets in higher-fee share classes to the institutional share class; (2) engaging a compliance consultant to conduct a comprehensive review of Respondent's written policies and procedures, disclosures, and account agreements; and (3) voluntarily rebating certain 12b-1 fees incurred during the relevant period. The Commission censured Respondent, ordered it to cease and desist from further violations of the Advisers Act and, though it did not impose a civil penalty, ordered Respondent to pay total disgorgement of $24,893.26 and prejudgment interest of $2,106.

***In re SunTrust Investment Services, Inc.*, Investment Advisers Act Rel. No. 4769, 2017 SEC LEXIS 2844 (Sept. 14, 2017)**

The Commission accepted an offer of settlement from SunTrust Investment Services (Respondent), a dually registered broker-dealer and investment adviser, for allegedly breaching its fiduciary duty to obtain best execution for wrap-fee advisory clients, making inadequate disclosures about certain conflicts of interest, and having deficient policies and procedures in connection with its mutual fund share class selection process. The Commission specifically alleged that Respondent's investment adviser representatives (IARs) purchased, recommended, or held higher-fee share classes for clients when less expensive institutional share classes were otherwise available. Many of these higher-fee share classes carried ongoing marketing or distribution fees (12b-1 fees) that were passed on as compensation to Respondent as the introducing broker for client accounts, a portion of which was further passed on as compensation to the IARs who were registered representatives of Respondent in its capacity as a registered broker-dealer. The Commission alleged that the Respondent breached its fiduciary duty and violated the Advisers Act as follows. First, the Commission alleged that Respondent did not adequately disclose to clients the conflict of interest posed by its IARs' share class selections and the receipt by Respondent and its IARs of a portion of the 12b-1 fees that Respondent received on investments in share classes that paid a 12b-1 fee. Although Respondent did disclose in its Form ADV Brochure that it "may" receive 12b-1 fees and that receipt of such fees presented a conflict of interest, Respondent did not disclose that many mutual funds offered a variety of share classes, including some that were less expensive and did not charge 12b-1 fees. Further, the Commission noted that although senior management of Respondent was aware during the relevant time frame of the underlying issues, and adopted policies and procedures governing mutual fund share class selection for qualified retirement accounts, they did not adopt comparable policies and procedures to prohibit IARs from recommending or purchasing higher-fee share classes for nonqualified clients when less expensive institutional share classes were available, or converting existing client positions in higher-fee share classes to the lowest eligible share class. The Commission noted that Respondent did eventually begin to convert higher-fee share class positions to the lower-cost share class, but alleged that this conversion "was not pursued in a timely and reasonable manner," and was "unreasonably" limited in scope to only a subset of Respondent's wrap programs. The Commission stated that during the relevant period, Respondent and its IARs received at least $1,148,000 in avoidable

12b-1 fees that would not have been collected had Respondent placed nonqualified advisory client accounts in lower-cost share classes, or converted the holdings in such accounts to the lowest-cost available share class. In addition to these allegations, the Commission also alleged that Respondent breached its duty to seek best execution by investing clients' funds in higher-fee share classes where lower-cost share classes were available. The Commission alleged that as a result of this conduct, Respondent violated Sections 206(2), 206(4) and 207 of the Advisers Act and Rule 206(4)-7 thereunder. Respondent was censured and ordered to cease and desist from further violations of the Advisers Act, and was ordered to pay a $1,148.071 civil penalty and $39,511.59 in disgorgement and prejudgment interest.

***In re Packerland Brokerage Services Inc. and Atlas Capital Management Corp.*, Investment Advisers Rel. No. 4832, 2017 SEC LEXIS 4178 (Dec. 21, 2017)**

The Commission accepted an offer of settlement from Packerland Brokerage Services, Inc., a dually registered investment adviser and broker-dealer, and Atlas Capital Management Corp., an investment adviser (collectively, Respondents). The Commission alleged that in soliciting advisory clients to invest in mutual fund strategies managed by Atlas, Respondent Packerland recommended the purchase of a certain class of mutual fund shares that imposed a 1% annual service fee, which it received in its capacity as a broker-dealer, while failing to disclose the resulting conflict of interest and the fact that a lower-cost but otherwise identical share class was available. The Commission further alleged that Respondent Packerland's Form ADV misrepresented that it would disclose to clients all of its fees and any compensation it received for the sale of securities, whereas in fact it did not disclose its receipt of the annual service fee imposed on the higher-cost mutual fund shares. With respect to Respondent Atlas, the Commission alleged that, although it generally did not directly communicate with the advisory clients solicited by Respondent Packerland, it was aware that it had purchased a costlier mutual fund share class for the clients when a lower-cost share class was available, and thus failed to seek best execution for its clients. The Commission further alleged that both Respondents failed to implement policies and procedures reasonably designed to address mutual fund share class selection and, in the case of Respondent Packerland, the conflict of interest resulting from its receipt of the annual service fee. The Commission censured Respondents, ordered them to cease and desist from further violating Sections 206(2) and 206(4) (and, in the case of Respondent Packerland, 207) of the Advisers Act and Rule 206(4)-7 thereunder, and to pay a total of $616,886.80, consisting of a civil penalty of $80,000 each, and, for Respondent Packerland, disgorgement of $432,949.80 and prejudgment interest of $23,937. The Commission stated that in determining to accept the settlement offer, the Commission considered remedial actions taken by Respondents, including their revision of internal compliance policies and procedures and implementation of new compliance training.

Conflict of Interest Disclosure – Receipt of Undisclosed Compensation

In re Voya Financial Advisors, Inc., Investment Advisers Act Rel. No. 4661, 2017 SEC LEXIS 669 (Mar. 8, 2017)

The Commission accepted an offer of settlement from Voya Financial Advisors, Inc. (Respondent), a dually registered investment adviser and broker-dealer formerly known as ING Financial Partners, Inc. The Commission alleged that Respondent failed to disclose to its advisory clients' compensation it received through an arrangement with a third-party clearing broker (Clearing Firm) and the conflicts of interest arising from that compensation. Specifically, the Commission alleged that the Clearing Firm agreed to share with Respondent certain revenues the Clearing Firm received from mutual funds available in the Clearing Firm's no-transaction-fee mutual fund program, and had a separate arrangement with Respondent in which the Clearing Firm agreed to pay Respondent a percentage of the service fees the Clearing Firm received from the mutual funds in exchange for Respondent performing certain administrative services. The Commission alleged that the compensation under both arrangements created conflicts of interest because it provided a financial incentive for Respondent to favor mutual funds in the program over other investments when giving advice to its clients, and that Respondent failed to disclose its receipt of the compensation to its clients, including in its Form ADV. The Commission censured Respondent; ordered it to cease and desist from committing or causing any violations and any future violations of Sections 206(2), 206(4), and 207 of the Advisers Act, and Rule 206(4)-7 thereunder; and ordered it to pay disgorgement of $2,621,324, prejudgment interest of $174,629.78, and a $300,000 civil money penalty. The Commission further ordered Respondent to provide a notice of the order to its advisory clients and to certify compliance with this undertaking.

SEC v. Momentum Investment Partners LLC (D/B/A Avatar Investment Management) et al., Litig. Rel. No. 23847, 2017 SEC LEXIS 1576 (May 31, 2017)

In a civil action brought by the Commission, the US District Court for the District of Connecticut entered judgment against Momentum Investment Partners LLC (d/b/a Avatar Investment Management) (the Firm) and its CEO, Ronald J. Fernandes (collectively, Respondents). The Commission's complaint alleged that Respondents failed to disclose the material conflicts of interest associated with their practice of moving client assets from individual accounts to new Firm-created and managed mutual funds following the same strategy, thereby causing the relevant clients to pay almost $111,000 in additional fees, $61,000 of which was ultimately paid to the Firm, for no additional services. The Commission further alleged that Respondents failed to provide notice prior to moving client assets to the mutual funds, and that the Firm failed to have policies and procedures in place to address the conflict of interest. Respondents consented to the entry of a permanent injunction enjoining Respondents from violating Sections 206(1) and 206(2) of the Advisers Act, and the Firm from violating, and Fernandes from aiding and abetting the violation of, Sections 204, 206(4) and 207 of the Advisers Act and Rules 204-1 and 206(4)-7 thereunder. The Court further ordered Respondents to disgorge, jointly and severally, $61,276 in ill-gotten gains and $7,401 in prejudgment interest, and imposed civil penalties of $125,000 on the Firm and $40,000 on Fernandes.

In re KMS Financial Services, Inc., Investment Advisers Act Rel. No. 4730, 2017 SEC LEXIS 2119 (July 19, 2017)

The Commission accepted an offer of settlement from KMS Financial Services, Inc. (Respondent). The Commission alleged that Respondent, a dually registered investment adviser and broker-dealer, failed, in its capacity as an investment adviser, to disclose to its advisory clients compensation it received from a third-party broker-dealer (Clearing Broker) for certain investments Respondent selected for its advisory clients. The Commission further alleged that, under this arrangement, the Clearing Broker and Respondent were meant to share in certain revenues the Clearing Broker received from its no-transaction-fee mutual fund program (NTF program). The Commission alleged that these payments created a conflict of interest for Respondent in that they incentivized Respondent to favor the mutual funds in the NTF program over other investments when giving investment advice to clients. The Commission alleged, in addition, that Respondent negotiated a reduction in execution and clearing costs it paid to the Clearing Broker without passing the reduction in brokerage costs to its clients or analyzing whether its clients were obtaining best execution. Finally, the Commission alleged that, in its Form ADV, Respondent made inaccurate statements regarding best execution and omitted disclosure of the compensation received through its NTF program. Respondent consented to the Commission's order that Respondent cease and desist from committing or causing any future violations of Sections 206(2), 206(4) and 207 of the Advisers Act and Rule 206(4)-7 thereunder, that Respondent be censured, and that Respondent pay disgorgement of $382,568.64, prejudgment interest of $69,518.43, and a civil monetary penalty of $100,000. Further, the Commission ordered that Respondent conduct certain undertakings.

SEC v. Westport Capital Markets, LLC and Christopher E. McClure, Litig. Rel. No. 24007, 2017 SEC LEXIS 4024 (Dec. 11, 2017)

The Commission charged Westport Capital Markets, LLC (Westport), a dually registered investment adviser and broker-dealer, and Westport's principal, McClure (collectively, Respondents) with breaching their fiduciary duties and defrauding advisory clients, including by repeatedly purchasing securities that generated significant amounts of undisclosed compensation to Westport. The Commission's complaint, filed in the US District Court for Connecticut, alleged that Respondents repeatedly invested advisory clients' funds in risky securities that generated hundreds of thousands of dollars in undisclosed markups for Westport and resulted in more than $1 million in losses for clients. According to the complaint, Westport purchased securities from underwriters for several years at a discount to the public-offering price and then, acting as a principal for its own account, resold those same securities to its advisory clients at higher prices without disclosing the markup, sometimes holding the securities in client accounts for only a short period before reselling the securities and then investing client funds in another offering with a markup. The complaint further alleged that Respondents defrauded a client by acting contrary to the client's express objectives and instead repeatedly investing the client in risky offerings that generated hidden markups. In addition, the complaint alleged that Westport and McClure made false and misleading representations to clients regarding the compensation that Westport would receive from their accounts. The complaint further alleged that Westport, in its capacity as a broker-dealer, received undisclosed mutual fund distribution fees, known as 12b-1 fees, when the Respondents invested advisory clients in

certain mutual fund share classes. The Respondents allegedly did not disclose to clients the conflict of interest that this created. According to the complaint, in certain instances, the Respondents invested clients in mutual fund shares with 12b-1 fees even when shares of the same funds were available that did not charge 12b-1 fees. The SEC's complaint alleged that Westport's advisory clients paid approximately $780,000 in undisclosed markups and fees on top of the advisory fees they paid the firm. The Commission's complaint charged Westport with violating Sections 206(1), 206(2), 206(3), and 207 of the Advisers Act and McClure with violating Sections 206(1), 206(2), and 207 of the Advisers Act and with aiding and abetting Westport's violation of Section 206(3). The Commission seeks injunctive relief, disgorgement of ill-gotten monetary gains plus interest, and penalties. The matter is pending.

Conflict of Interest Disclosure – Referral Arrangements/Senior Investors

***In re John W. Rafal*, Investment Advisers Act Rel. No. 4601, 2017 SEC LEXIS 52 (Jan. 9, 2017); *In re Peter Hershman, Esq.*, Investment Advisers Act Rel. No. 4602, 2017 SEC LEXIS 53 (Jan. 9, 2017); *In re Essex Financial Services, Inc.*, Investment Advisers Act Rel. No. 4603, 2017 SEC LEXIS 54 (Jan. 9, 2017)**

The Commission accepted an offer of settlement from Essex Financial Services, Inc. (Essex), a dually registered investment adviser and broker-dealer; John W. Rafal, the former President and CEO of Essex; and Peter Hershman, Esq. (collectively, Respondents). The Commission alleged that Rafal agreed to pay Hershman, an attorney, for referring an elderly widow with accounts exceeding $100,000,000 to Essex. According to the order, the referral arrangement was not disclosed to the client. The Commission alleged that Hershman was not properly licensed as an investment adviser agent under the Connecticut Uniform Securities Act and Essex arranged for him to take the examination to become properly registered. The Commission alleged that Hershman never took the examination. The Commission further alleged that Rafal knew that it would be improper for Essex to pay a referral fee, and that Respondents Rafal and Hershman agreed that the payment would be disguised in the form of payments for legal services rendered. According to the order, personnel from within Respondent Essex complained about the payments, and Essex instructed Rafal to stop paying Hershman and arrange for the return of previous payments. The Commission alleged that Rafal sought and received reimbursement from Hershman, but then separately made payments from his own assets without notifying Essex. The Commission alleged that when Rafal became concerned that clients had become aware of the Commission's investigation, he sent numerous emails to clients containing false assurances. In the order, the Commission alleged that during the investigation Rafal had intentionally misled the Commission's staff to believe that Hershman had returned all prior payments when he still retained two payments. The Commission ordered that Respondents each cease and desist from committing or causing any violations and any future violations of the cash solicitation rule, ordered Rafal and Hershman to cease and desist from committing or causing any violations to the antifraud provisions of the Advisers Act, and barred Rafal and Hershman from appearing or practicing before the Commission as attorneys, from association, from serving in any capacity for a registered investment company or affiliated person of an investment adviser, depositor, or principal underwriter, and from participating in penny stock

offerings, with the right to reapply. The Commission further ordered Rafal and Hershman to pay civil penalties of $275,000 and $37,500, respectively, disgorgement of $275,000 and $49,760, respectively, and prejudgment interest of $27,298 and $4,924, respectively. The Commission ordered Essex to pay disgorgement of $170,000 and prejudgment interest of $13,181, but did not impose any civil penalties as a result of its cooperation with the Commission.

Conflict of Interest Disclosure – Undisclosed Related Party Transactions

In re SLRA Inc. as successor entity to Liquid Realty Advisors III, LLC and Scott M. Landress, Investment Advisers Act Rel. No. 4641, 2017 SEC LEXIS 397 (Feb. 7, 2017)

The Commission accepted an offer of settlement from SLRA Inc., a registered investment adviser, and its principal, Scott M. Landress (collectively, Respondents). The Commission alleged that Respondents failed to disclose to SLRA Inc.'s advisory clients, or to the investors of two private equity funds (the Funds) created by Landress for the purpose of investing in real estate trusts with underlying investments in properties throughout the UK, certain related-party transaction service fees and the associated conflicts of interest. SLRA Inc. managed the Funds and earned management fees based on the net asset value of the underlying investments. The Commission alleged that Landress directed SLRA Inc. to withdraw £16,250,000 from the Funds' accounts. Although Landress claimed that the money was withdrawn as payment for fees owed to an affiliate for services provided to the Funds, he allegedly transferred the money to his personal account, and neither SLRA Inc. nor Landress disclosed the related-party transaction until after the money had been withdrawn. After the Commission began its investigation of Respondents, they allegedly returned the withdrawn services fees to the Funds. The Commission ordered Respondents to cease and desist from committing or causing any violations and any future violations of Sections 206(1), 206(2), and 206(4) of the Advisers Act and Rule 206(4)-8 thereunder. Further, the Commission barred Landress from association with any broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization. The Commission also censured SLRA Inc. and ordered Landress to pay a civil penalty of $1,250,000.

In re Resilience Management, LLC, Bassem Mansour and George Ammar, Investment Advisers Act Rel. No. 4721, 2017 SEC LEXIS 1985 (June 29, 2017)

The Commission accepted an offer of settlement from Resilience Management, LLC (Resilience), its co-Chief Executive Officer, Bassem Mansour, and its Chief Financial Officer and Chief Compliance Officer, George Ammar (Respondents). The Commission alleged that the Respondent Resilience, through its co-CEO Mansour, improperly borrowed money from certain private equity fund clients while not being authorized to do so by the funds' limited partnership agreements. The Commission also stated that Respondents did not adequately disclose their borrowing practices to the funds' investors (which included failure to disclose in capital calls to investors that the call was being made for unauthorized expenses), and that Respondent

Ammar made false entries in Respondents' books and records to cover up the misuse and improper advancement of funds that were taken without authorization. In addition, the Commission stated that Respondent Mansour—as co-CEO of Resilience and a member of the funds' general partner—failed to make timely capital contributions to the funds, as he was required to by the funds' governing documents. The Commission also alleged that Respondents' compliance manual did not adequately address the disclosure of material conflicts of interest or acting in the best interests of clients in connection with related-party transactions.
The Commission censured Mansour and Ammar and ordered that Respondents cease and desist from violating Sections 204, 206(2), and 206(4) of the Advisers Act and Rules 204-2, 206(4)-7, and 206(4)-8 thereunder. Respondents Mansour and Resilience were ordered to pay civil penalties of $500,000 and $250,000, respectively, and Respondent Ammar was ordered to pay a civil penalty of $50,000. Respondent Ammar was permanently barred from association, and Mansour was barred from association for a period of three years. Mansour and Resilience further agreed that, for a period of three years, Mansour will not (i) provide instructions or approve any transfer of assets or payment by a client, affiliate, or portfolio company to Resilience or any of its officers, employees, or agents; (ii) supervise any person who provides instructions to or approves any such transfer of assets or payments; or (iii) associate with any registered investment adviser other than Resilience or any of its successors through a business combination. In determining to accept the offer, the Commission considered voluntary remedial acts promptly undertaken by Respondents in connection with this alleged conduct, including (i) repayment of the funds with interest and disclosure regarding borrowing activities and the late capital contributions, and (ii) improvements to Resilience's compliance infrastructure, including retention of an independent compliance consultant, and hiring of a new CFO, CCO, and general counsel.

In re Columbia River Advisors, LLC, Investment Advisers Act Rel. No. 4734, 2017 SEC LEXIS 2270 (July 28, 2017)

The Commission accepted an offer of settlement from Columbia River Advisors, LLC (Columbia River), a registered investment adviser, Benjamin J. Addink (Addink) and Donald A. Foy (Foy) (collectively, Respondents). The Commission alleged that, beginning in June 2012, Respondents caused a fund to which Columbia River was providing investment advisory services to make sizeable investments into another fund that loaned money to Columbia River but failed, until long after making the investments, to inform investors in the investing fund that some of the assets were used to grow Columbia River's advisory business. The Commission also alleged that Columbia River hired an auditor who was not qualified under the Advisers Act Custody Rule, and that the firm did not timely distribute audited financial statements to the funds' investors for the 2012 and 2014 fiscal years as required by the Custody Rule. The Commission ordered that Columbia River and Foy cease and desist from committing or causing any violations or future violations of Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-2 thereunder, and that Addink cease and desist from committing or causing any violations or future violations of Section 206(2) of the Advisers Act. The Commission further ordered that Respondents be censured, that Columbia River pay a civil monetary penalty of $80,000, that Addink pay a civil monetary penalty of $25,000, and that Foy pay a civil monetary penalty of $30,000. Further, the Commission ordered that Columbia River comply with certain undertakings, including the retention of an independent compliance consultant.

***In re Marshall G. Eichenauer, Jr. and Sagent Wealth Management, LLC*, Investment Advisers Act Rel. No. 4773, 2017 SEC LEXIS 2973 (Sept. 22, 2017)**

The Commission accepted an offer of settlement from registered investment adviser Sagent Wealth Management (Sagent) and its sole owner and principal, Eichenauer (collectively, Respondents), for using the assets of a private fund they managed to finance loans that personally benefitted Eichenauer without disclosing the conflict to the fund's investors (many of whom were also advisory clients of Sagent) or obtaining investors' consent to make such loans. The Commission alleged that during the relevant three-year period, Eichenauer caused the fund to loan a total of $326,650 to Sagent, of which Eichenauer personally received approximately half ($166,400). The Commission stated that as a result of failing to disclose Eichenauer's conflict of interest to investors in causing the fund to lend Sagent money, and failing to seek or obtain consent from advisory clients for the loans, Respondents violated Sections 206(2), 206(3), and 206(4) of the Advisers Act and Rule 206(4)-8 thereunder. The Commission ordered Respondents to jointly and severally distribute within 30 days of the order a total disgorgement payment of $16,110.31 to the fund's investors, to retain an independent compliance consultant, and to provide a copy of the order to each of the fund's investors and Sagent's existing advisory clients. The Commission further censured Respondents, ordered them to cease and desist from further violations of the Advisers Act, and ordered that they pay a civil monetary penalty of $165,000.

***In re Augustine Capital Management, LLC*, Investment Advisers Act Rel. No. 4800, 2017 SEC LEXIS 3418 (Oct. 26, 2017)**

The Commission accepted an offer of settlement from Augustine Capital Management, LLC (Augustine), an unregistered investment adviser to a private fund (the Fund), and two of Augustine's three owners, John Porter (Porter) and Thomas Duszynski (Duszynski) (collectively, Respondents). The Commission alleged that Respondents caused the Fund to engage in conflicted transactions, including a personal loan to Duszynski on which he defaulted, and undocumented loans to entities in which Augustine's owners had an interest, without disclosing the conflict to or obtaining consent from Fund investors. The Commission alleged that Respondents also improperly charged investors for Augustine's operating expenses that were not contemplated in the offering documents of the Fund, including salaries, healthcare, and rent, and made direct money transfers to Porter, which resulted in the Fund being overcharged by approximately $950,000 of Augustine's expenses. The Commission further alleged that Respondents provided investors with fraudulent account statements with inflated valuations and omitted material information to conceal losses and bankruptcies. The Commission also alleged that Respondents unilaterally allocated holdings among Fund investors and periodically transferred such holdings without investors' knowledge or consent, which prevented investor exits from the Fund in at least two instances. The Commission ordered Respondents to cease and desist from further violations of Sections 206(1), 206(2), and 206(4) of the Advisers Act and Rule 206(4)-8 promulgated thereunder; censured Augustine; barred Porter and Duszynski from association with the right to reapply after three years; and suspended Duszynski from practicing before the Commission as an accountant. The Commission further ordered the Respondents to pay $685,515 in disgorgement and $42,791 in prejudgment interest and

imposed civil penalties of $150,000 on Augustine, $75,000 on Porter, and $50,000 on Duszynski. Respondents undertook to provide a copy of the order to all Fund investors.

SEC v. Louis G. Mohlman, Mohlman Asset Management, LLC, and Mohlman Asset Management Fund, LLC, Litig. Rel. No. 24011, 2017 SEC LEXIS 4055 (Dec. 14, 2017)

The Commission brought charges in federal district court and agreed to a settlement subject to court approval against Louis G. Mohlman (Mohlman) and two registered investment advisers he owns and controls, Mohlman Asset Management, LLC (MAM) and Mohlman Asset Management Fund, LLC (MAMF) (collectively, Respondents), that manage two private funds. The Commission's complaint alleges that, between 2012 and 2015, Mohlman made payments from the funds in order to satisfy the obligations of third parties, and used assets from one of the funds to make a $150,000 unsecured loan (equivalent to approximately 16% of the fund's portfolio) to third parties, including his wife. Certain of the payments that Mohlman effected from the funds' assets did not benefit the funds, were not legally obligated to be made, and further were not permissible expenses that were authorized by the operating documents of the funds. The Commission further alleged that the funds' investors never consented to these transactions, and in most cases were never disclosed by Mohlman to investors. The Commission alleged that where disclosures were made by Mohlman about these transactions (including the loan), they were incomplete and inaccurate regarding the underlying circumstances and terms of the transaction. The Commission's complaint further alleges that Mohlman misrepresented that tax and legal experts endorsed a strategy he developed to facilitate tax-free transfers between different types of tax-preferred retirement vehicles. However, no such endorsements existed, and the legal and tax experts cited strongly advised against the strategy. Lastly, the Commission alleges that Respondents failed to disclose to investors certain fees that they earned by facilitating the sale of securities from a third party to the private funds, filed materially inaccurate Forms ADV with the Commission, had a deficient compliance program, and did not comply with the provisions of the Advisers Act Custody Rule for the funds.

The Commission alleges that Respondents violated Sections 206(1), 206(2) and 206(4) of the of the Advisers Act; that Mohlman and MAMF violated Section 207 of the Advisers Act; that Mohlman and MAMF violated Rule 206(4)-8 of the Advisers Act; that MAM and MAMF violated Rule 206(4)-7 under the Advisers Act; and MAMF violated Rule 206(4)-2 under the Advisers Act. Without admitting or denying the allegations in the Commission's complaint, Respondents agreed to the entry of permanent injunctions and agreed to pay, on a joint and several basis, a $100,000 civil penalty, $862.03 in disgorgement, and $75.34 in interest. The settlement is subject to court approval.

Custody

In re Southwind Associates of NJ Inc. (d/b/a Villafranco Wealth Management), William Scott Villafranco, and Anthony LaPeruta, Investment Advisers Rel. No. 4834, 2017 SEC LEXIS 4194 (Dec. 22, 2017)

The Commission accepted offers of settlement from Southwind Associates of NJ Inc. (Southwind), a registered investment adviser, William Scott Villafranco, Southwind's president and sole owner, and Anthony LaPeruta, formerly Southwind's CCO (collectively, Respondents). The Commission alleged that Southwind violated the Advisers Act Custody Rule by failing to have surprise examinations conducted with respect to client funds and securities of which it had custody, and by failing to ensure that two private fund clients timely distributed audited financial statements to their investors and that the funds' audits were performed by a qualified independent public accountant. The Commission also alleged that Southwind failed to make and keep records of certain electronic communications required to be maintained, to adopt written policies and procedures reasonably designed to safeguard client records and information as required by Regulation S-P, to adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act and rules thereunder, and to conduct annual reviews of its written policies and procedures. The Commission further alleged that LaPeruta, as Southwind's CCO, willfully aided, abetted, and caused Southwind's violations, having failed to remedy Southwind's deficiencies for several years despite having the responsibility for addressing them, according to Southwind's compliance manual, and despite having been informed of the deficiencies by a compliance consulting firm retained by Southwind in May 2011. The Commission alleged that LaPeruta misrepresented to the compliance consultant the progress that Southwind was making in addressing the deficiencies, and failed to provide certain information to the Commission's Office of Compliance Inspections and Examinations (OCIE) exam staff regarding issues with Southwind's books and records. The Commission further alleged that Villafranco, as Southwind's president and sole owner, caused Southwind's violations by failing to take adequate steps to ensure that the misconduct underlying the violations was addressed after becoming aware of the misconduct. Lastly, the Commission alleged that the Advisers Act violations summarized above were either cited as deficiencies during multiple OCIE examinations or were highlighted in the compliance consultant's recommendations to improve Southwind's compliance program. The Commission censured Southwind, ordered the Respondents to cease and desist from further violations of Sections 204(a) and 206(4) of the Advisers Act and Rules 204-2(a)(7), 206(4)-2, and 206(4)-7 thereunder and Rule 30(a) of Regulation S-P; ordered Southwind and Villafranco to jointly and severally pay a civil penalty of $50,000; and barred LaPeruta from acting in a supervisory or compliance capacity with any broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization. The Commission also ordered Southwind to engage in certain undertakings, including, among other things, to retain an independent compliance consultant (on a nonprivileged basis) to review and report on the adequacy of Southwind's policies, procedures, controls, and systems.

Exchange-Traded Funds (ETFs)

***In re BlackRock Fund Advisors*, Investment Company Act Rel. No. 32613, 2017 SEC LEXIS 1245 (Apr. 25, 2017)**

The Commission accepted an offer of settlement from BlackRock Fund Advisors (Respondent), a registered investment adviser. The Commission alleged that from December 2010 through January 2015, Respondent caused iShares MSCI Russia Capped ETF, Inc. (Russia Fund Company), a registered investment company it advised, to issue securities in the iShares MSCI Russia Capped ETF (Russia Fund ETF) without first obtaining requisite exemptive relief under the Company Act. The SEC order indicated that Respondent had initially mistakenly believed that the Russia Fund ETF was already covered by a previously issued exemptive order that the Commission granted in January 2007. Without exemptive relief from the Commission, the Commission alleged Respondent caused the Russia Fund Company to violate Section 22(e) of the Investment Company Act (Company Act). The Commission ordered Respondent to cease and desist from committing further violations of Sections 22(d) and (e) of the Company Act and Rule 22c-1 thereunder. The Commission further ordered Respondent to pay a civil penalty of $1,500,000.

Investment Adviser Registration

***In re Brian Kimball Case, Bradway Financial, LLC and Bradway Capital Management, LLC*, Investment Advisers Act Rel. No. 4733, 2017 SEC LEXIS 2197 (July 25, 2017)**

The Commission accepted an offer of settlement from Bradway Financial, LLC (Bradway Financial), a registered investment adviser, Bradway Capital Management, LLC (Bradway Capital), an investment adviser that claimed exemption from registration, and Brian Kimball Case, the chief compliance officer for both advisers (collectively, Respondents). The Commission alleged Bradway Capital was not entitled to rely on the private fund adviser exemption in Rule 203(m)-1 under the Advisers Act, since it was under common control and operationally integrated with Bradway Financial, a registered investment adviser. Specifically, the Commission stated that Bradway Financial and Bradway Capital were both owned by Case, shared the same employees, operated in the same office, shared the same technology systems, and failed to maintain policies and procedures addressing registration or exemption from registration as an investment adviser. The Commission further alleged that Bradway Capital provided inflated financial statements to investors for two private funds that it advised and included these values in Forms ADV filed by Bradway Capital and Bradway Financial, both of which were signed by Case. None of Respondents received any fees based on these inflated valuations.

In addition, the Commission alleged that Bradway Capital and Bradway Financial failed to comply with the Advisers Act's custody and compliance rules, improperly used fund assets to pay legal fees incurred in connection with the Commission's investigation of the conduct at issue, and Bradway Financial contracted to earn a performance fee for managing a fund without determining whether that fund's investors were qualified clients. As a result, the Commission

ordered that Case cease and desist from committing or causing any violations or future violations of Sections 203(a), 205(a)(1), 206(2), 206(4), and 207 of the Advisers Act of 1940 and Rules 206(4)-2, 206(4)-7, and 206(4)-8 promulgated thereunder; that Bradway Capital cease and desist from committing or causing any violations and any future violations of Sections 203(a), 206(2), 206(4), and 207 of the Advisers Act and Rules 206(4)-2, 206(4)-7, and 206(4)-8 promulgated thereunder; that Bradway Financial cease and desist from committing or causing any violations and any future violations of Sections 203(a), 205(a)(1), 206(2), 206(4), and 207 of the Advisers Act and Rules 206(4)-2 and 206(4)-7 promulgated thereunder; that Bradway Capital and Bradway Financial be censured; and that Case be barred from acting as a chief compliance officer with the right to reapply in three years. The Commission ordered that Respondents jointly and severally pay a civil monetary penalty of $150,000 and comply with various undertakings.

Investment Company Registration/Misrepresentation

***In re Landwin Management, LLC and Martin Landis*, Investment Advisers Act Rel. No. 4726, 2017 SEC LEXIS 2036 (July 6, 2017)**

The Commission accepted an offer of settlement from Landwin Management, LLC, an unregistered investment adviser, and its principal, Martin Landis (collectively, Respondents). The Commission alleged that Respondents misrepresented the assets of Landwin Partners Fund I, LLC (the Fund), an unregistered proprietary real estate investment fund, by purchasing securities in a manner not authorized in the Fund's operating documents. The Commission alleged that, while the Fund's PPM and other offering documents disclosed that the Fund would seek to acquire a portfolio of real estate and real estate–related investments, Respondents caused the Fund to use approximately $2.4 million in Fund cash to purchase short-term bank, corporate, and sales tax revenue bonds and preferred and common shares of stock unrelated to real estate. The Fund documents neither authorized, nor disclosed the risks associated with, investments other than real estate. Respondents never disclosed to investors that they invested Fund assets in publicly traded bonds unrelated to real estate. The Commission further alleged that the Fund PPM disclosed that Landwin would not cause the Fund to be engaged primarily in the business of selling securities or to invest in securities having a value of 40% of the total assets of the Fund, but that, between January 2011 and September 2015, between 48% and 100% of the Fund's total assets were composed of investment securities as defined under Section 3(a)(2) of the Company Act. As a result, the Commission alleged that the Fund violated Section 7(a) of the Company Act because it did not register with the Commission as an investment company. The Commission censured Respondents; ordered them to cease and desist from committing any future violations of Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-8 promulgated thereunder and Section 7(a) of the Company Act; ordered that they pay jointly and severally a civil money penalty of $75,000; and that they be given no penalty offset in any related investor actions. Further, the Commission ordered that Respondents comply with certain undertakings to, among other things, engage an independent monitor approved by the Commission to oversee the sale of properties underlying the Fund's investments and other aspects related to the wind-down process.

Material Nonpublic Information

In re Deerfield Management Company, L.P., Investment Advisers Act Rel. No. 4749, 2017 SEC LEXIS 2559 (Aug. 21, 2017)

The Commission accepted an offer of settlement from Deerfield Management Company, L.P. (Respondent), a registered investment adviser providing services to funds investing in the healthcare sector. The Commission alleged that Respondent retained research firms, including those focused on political intelligence, to conduct research on the healthcare sector. Political intelligence analysts allegedly communicated material nonpublic information to Respondent analysts, and such analysts traded based on that information on three separate occasions. These trades allegedly resulted in profits of more than $3.9 million for Respondent's hedge fund clients. The Commission alleged that Respondent failed to establish, maintain, and enforce policies and procedures reasonably designed to address the risk that its employees could misuse such material nonpublic information from research firms, and failed to take action despite red flags. The Commission further alleged that Respondent failed to review the policies and procedures of one of the political intelligence analyst's research firms, contrary to its own policies and procedures. The Commission alleged that, as a result, Respondent violated Section 204A of the Advisers Act. In determining to accept the settlement offer, the Commission considered Respondent's remedial acts. Respondent was censured by the Commission and ordered to cease and desist from committing or causing any violations and any future violations of Section 204A of the Advisers Act, and to pay disgorgement of $714,110, prejudgment interest of $97,585, and a civil monetary penalty of $3,946,267.

Misleading Advertising Claims

In re Jeffrey Slocum & Associates, Inc. and Jeffrey C. Slocum, Investment Advisers Act Rel. No. 4647, 2017 SEC LEXIS 419 (Feb. 8, 2017)

The Commission accepted an offer of settlement from Jeffrey Slocum & Associates, Inc. (JSA), a registered investment adviser, and Jeffrey C. Slocum (Slocum), the majority owner and President of JSA (collectively, Respondents). The Commission alleged that JSA disseminated marketing material containing misleading performance data, misstatements regarding JSA's acceptance of items of value from investment managers and misstatements about JSA's enforcement of its Code of Ethics. The Commission specifically alleged that JSA disseminated marketing materials containing representations that JSA had "never, not once, taken even so much as a nickel from an investment manager," even though JSA's gift policy permitted the acceptance of gifts from investment managers under certain circumstances and JSA employees had accepted gifts in the past. Further, the Commission alleged that JSA disseminated misleading marketing materials that included a chart purporting to show the value added by JSA's investment manager recommendations, but which in fact did not include actual performance of JSA but rather hypothetical and back-tested performance. As a result, the

Commission alleged that JSA violated the antifraud provisions of the Advisers Act, failed to adopt and implement compliance policies and procedures with respect to the review of marketing materials and the use of performance data in marketing materials, failed to implement its gift policy, and further failed to keep appropriate books and records regarding the calculation of advertised performance figures. The Commission censured JSA and ordered that JSA cease and desist from committing or causing any violations and any future violations of Sections 204(a), 206(2), and 206(4) of the Advisers Act and Rules 204-2, 206(4)-1, and 206(4)-7 promulgated thereunder. The Commission also ordered that Slocum cease and desist from committing or causing any violations and any future violations of Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-7 promulgated thereunder. The Commission ordered that JSA pay a civil penalty of $300,000 and that Slocum pay a civil penalty of $100,000. The Commission considered the significant remedial acts undertaken by Respondents when imposing penalties.

***SEC v. Navellier & Associates, Inc., and Louis Navellier*, Litig. Rel. No. 23925, 2017 SEC LEXIS 2683 (Aug. 31, 2017)**

The Commission charged Navellier & Associates, Inc. (Navellier), a registered investment adviser, and its founder and chief investment officer, Louis Navellier (collectively, Respondents) with violations of Sections 206(1), 206(2), and 206(4) of the Advisers Act and Rule 206(4)-1(a)(5) promulgated thereunder. The Commission alleged that Respondents misled clients and prospective clients about the performance track record of an investment strategy offered by the Firm, which resulted in materially false advertisements and client communications. The Commission alleged that Respondents ignored and concealed red flags that the performance information was misrepresented. The advertisements allegedly indicated that the client investments had been invested in strategies that had outperformed the S&P 500 Index during a period when, in reality, no client assets had tracked the strategy and, even as a back-test, the claimed performance was overstated. The Commission further alleged that Respondents sold the strategy brand once they became aware of the potential legal risks. The case is pending in the United States District Court for the District of Massachusetts.

***In re Ameriprise Financial Services Inc.*, Investment Advisers Rel. No. 4822, 2017 SEC LEXIS 3983 (Dec. 8, 2017); *In re Horter Investment Management, LLC*, Investment Advisers Rel. No. 4823, 2017 SEC LEXIS 3984 (Dec. 8, 2017)**

The Commission accepted offers of settlement from Ameriprise Financial Services, Inc. (Ameriprise), a dually registered investment adviser and broker-dealer, and Horter Investment Management, LLC (Horter), a registered investment adviser (collectively, Respondents). The Commission alleged that the Respondents had made misstatements to advisory clients and prospective clients concerning F-Squared Investments, Inc. (F-Squared), an unaffiliated investment adviser whose AlphaSector strategies were offered on Respondents' platform, in negligent reliance on F-Squared's false claims about the strategies' exceptional performance over the 2001-2008 period. F-Squared was the subject of a 2016 order from the Commission regarding its use of inflated hypothetical performance figures for an investment strategy available to Institutional Investor Trust's (IIT's) shareholders. *In re F-Squared Investments, Inc.*, Investment Advisers Act Rel. No. 3988 (Dec. 22, 2014). The Commission alleged that

Respondents failed to have a reasonable basis to believe the accuracy of F-Squared's statements regarding the strategies' performance and performance-related claims, having taken insufficient steps to confirm the accuracy of the performance data and not having obtained adequate documentation that would have substantiated F-Squared's assertions. Furthermore, Respondents allegedly failed to maintain adequate books and records necessary to substantiate the calculation of the strategies' advertised performance, and failed to adopt and implement written policies and procedures regarding the accuracy of disseminated performance information and the retention of books and records to support the basis for such performance information. The Commission censured the Respondents and ordered Respondents to cease and desist from committing or causing any violations and any future violations of Sections 204(a), 206(2), and 206(4) of the Advisers Act and Rules 204-2(a)(16), 206(4)-1(a)(5), and 206(4)-7 thereunder. Ameriprise was ordered to pay $1,750,000 in civil penalties and $6,300,000 in disgorgement, with a prejudgment interest of $700,000. The Commission ordered Horter to pay $250,000 in civil penalties and $482,595 in disgorgement, with prejudgment interest of $46,209. The Commission stated that in determining to accept Ameriprise's settlement offer, the Commission considered Respondents' voluntary retention of a compliance consultant to review policies and procedures relating to marketing materials and due diligence of portfolio strategists, among other things.

***In re Institutional Investor Advisers, Inc.*, Investment Advisers Rel. No. 4824, Investment Company Act Rel. No. 32937, 2017 SEC LEXIS 3982 (Dec. 8, 2017)**

The Commission accepted an offer of settlement from Institutional Investor Advisers, Inc. (Respondent), a formerly registered investment adviser that advised IIT, a formerly registered investment company. The Commission alleged that on several occasions, Respondent presented or distributed offering documents for IIT that failed to comply with applicable rules for mutual fund prospectuses and advertisements, and included material misstatements concerning certain inflated hypothetical back-tested performance figures for the AlphaSector Premium strategy provided by IIT's subadviser, F-Squared. F-Squared was the subject of a 2016 order from the Commission regarding its use of inflated hypothetical performance figures for the AlphaSector Premium investment strategy available to IIT's shareholders. *In re F-Squared Investments, Inc.*, Investment Advisers Act Rel. No. 3988 (Dec. 22, 2014). The materials that Respondent provided to shareholders and prospective shareholders of IIT included material misrepresentations regarding the performance of the investment strategy at issue, and referenced important disclosures regarding the performance figures that were not incorporated on the materials, including that certain of the performance figures were back-tested and inflated.

The Commission further alleged that Respondent caused violations of IIT's governance and compliance obligations by failing to (i) enter into a written subadvisory contract with F-Squared for several years, (ii) obtain a vote of IIT's shareholders or its board of directors to approve a subadvisory agreement with F-Squared, and (iii) adopt and implement required compliance policies and procedures prior to 2015, or conduct any annual reviews of Respondent or IIT's required compliance program pursuant to either the Advisers Act or Company Act. The Commission noted that from 2011 to 2016, IIT's board received one-paragraph letters, signed by the president of Respondent, falsely indicating that an annual review of both entities had

been conducted. As a result of this conduct, the Commission alleged that Respondent violated Section 5(b)(1) of the Securities Act, Section 206(4) of the Advisers Act and Rules 206(4)-7 and 206(4)-8 thereunder, and Sections 15(a) and 15(c) of the Company Act and Rule 38a-1 thereunder. The Commission ordered Respondent to pay a civil monetary penalty of $200,000.

Mutual Fund Distribution

In re William Blair & Company, L.L.C., Investment Advisers Act Rel. No. 4695, 2017 SEC LEXIS 1296 (May 1, 2017)

The Commission accepted an offer of settlement from William, Blair & Company, L.L.C., a registered investment adviser and broker-dealer (Respondent). The Commission alleged that Respondent negligently used mutual fund assets to pay for (i) distribution and marketing of fund shares outside of a written, board-approved Rule 12b-1 plan and (ii) subtransfer agent services in excess of board-approved limits. The Commission further alleged that these payments totaled approximately $1,250,000 and rendered certain of Respondent's funds' disclosures concerning payments for such services inaccurate, and that Respondent also failed to fully disclose to the relevant funds' board that Respondent (and not a third-party service provider) would retain a fee for providing shareholder administration services to the funds under a shareholder administration services agreement. The Commission ordered Respondent to cease and desist from further violating and causing violations of Section 206(2) of the Advisers Act and Sections 12(b) and 34(b) of the Company Act and Rule 12b-1 thereunder, and to pay a civil money penalty of $4,500,000, not to be offset by any amounts payable in any related investor action.

In re Calvert Investment Distributors, Inc., et al., Investment Advisers Act Rel. No. 4696, 2017 SEC LEXIS 1309 (May 2, 2017)

The Commission accepted an offer of settlement from Calvert Investment Management, Inc., a registered investment adviser (Calvert), and Calvert Investment Distributors, Inc. (Calvert Distributors), its broker-dealer affiliate (collectively, Respondents). The Commission alleged that instead of paying for distribution-related services out of their own resources, Respondents caused Calvert-advised funds (the Funds) to pay various intermediaries nearly $18,000,000 for such distribution-related services outside of a written, approved 12b-1 plan. The Commission further alleged that the Funds' prospectuses contained material misstatements concerning the Funds' payments for distribution-related services, and that Respondents caused the Funds to incur expenses for subtransfer agent services that exceeded established expense limits. The Commission censured Calvert, ordered Calvert to cease and desist from further violating Section 12(b) of the Company Act and Rule 12b-1 thereunder and Calvert Distributors to cease and desist from further violating Section 206(2) of the Advisers Act and Sections 12(b) and 34(b) of the Company Act and Rule 12b-1 thereunder. The Commission further ordered Respondents to pay, jointly and severally, disgorgement of $17,829,804, prejudgment interest of $3,784,730, and a civil monetary penalty of $1,000,000.

Outsourced Chief Compliance Officer

***In re. David I. Osunkwo*, Investment Advisers Act Rel. No. 4745, 2017 SEC LEXIS 2495 (Aug. 15, 2017); *In re Diane W. Lamm*, Investment Advisers Act Rel. No. 4744, 2017 SEC LEXIS 2496 (Aug. 15, 2017); *In re David I. Osunkwo, Esq.*, Securities Exchange Act Rel. No. 82070, 2017 SEC LEXIS 3581 (Nov. 14, 2017)**

The Commission accepted an offer of settlement from David I. Osunkwo (Osunkwo), an attorney and formerly a principal at SC Consulting who was hired to serve as an outsourced CCO for two registered investment advisers (Registrants). The Commission alleged that Osunkwo was responsible for preparing and filing the Forms ADV for the Registrants but failed to do so correctly. Specifically, the Commission alleged that one Registrant failed to file a Form ADV for the 2010 fiscal year and the other Registrant filed an annual amendment that was intended to reflect a merger between the Registrants, but the filing materially overstated the assets under management (AUM) and total number of client accounts for the Registrants. The filing allegedly overstated the Registrants' combined AUM by more than $119 million and combined number of client accounts by at least 1,000 accounts. The Commission alleged that Osunkwo relied on estimates from the Registrants' Chief Investment Officer but failed to take steps to verify the accuracy of the estimates. As a result, the Commission alleged that Osunkwo caused violations of Sections 204 and 207 of the Advisers Act and Rule 204-1(a)(1) thereunder. The Commission ordered Osunkwo to cease and desist from committing or causing any violations and any future violations of Sections 204 and 207 of the Advisers Act and Rule 204-1(a)(1) thereunder. The Commission suspended Osunkwo for 12 months from association. The Commission also ordered Osunkwo to pay a civil money penalty of $30,000. In a related proceeding, the Commission temporarily suspended Osunkwo from appearing or practicing before the Commission as an attorney, with a right to petition to lift the temporary suspension within 30 days.

In another related action, the Commission also accepted an offer of settlement from Diane W. Lamm (Lamm), the Registrants' Chief Operating Officer and Osunkwo's direct supervisor during the relevant period, in connection with the Registrants' false Form ADV filings described above. In addition, the Commission alleged that the Registrants failed to maintain books and records segregated from affiliated entities, instead aggregating books and records at the level of the Registrants' parent holding company. Furthermore, Lamm admitted that in 2016 she pled guilty to two counts of securities fraud, alleging that she had defrauded investors by means of materially false and misleading statements and omissions and misappropriated investor funds in connection with the purchase or sale of a security. The Commission ordered that Lamm cease and desist from committing or causing any violations and any future violations of Sections 204 and 207 of the Advisers Act and Rule 204-2(a) thereunder. The Commission also barred Lamm from association.

Pay-to-Play

***In re Adams Capital Management, Inc.*, Investment Advisers Act Rel. No. 4617, 2017 SEC LEXIS 132 (Jan. 17, 2017); *In re Aisling Capital LLC*, Investment Advisers Act Rel. No. 4616, 2017 SEC LEXIS 131 (Jan. 17, 2017); *In re Alta Communications, Inc.*, Investment Advisers Act Rel. No. 4614, 2017 SEC LEXIS 129 (Jan. 17, 2017); *In re Commonwealth Venture Management Corp.*, Investment Advisers Act Rel. No. 4615, 2017 SEC LEXIS 130 (Jan. 17, 2017); *In re Cypress Advisors, Inc.*, Investment Advisers Act Rel. No. 4613, 2017 SEC LEXIS 128 (Jan. 17, 2017); *In re FFL Partners*, Investment Advisers Act Rel. No. 4610, 2017 SEC LEXIS 125 (Jan. 17, 2017); *In re Lime Rock Management LP*, Investment Advisers Act Rel. No. 4611, 2017 SEC LEXIS 126 (Jan. 17, 2017); *In re NGN Capital LLC*, Investment Advisers Act Rel. No. 4612, 2017 SEC LEXIS 127 (Jan. 17, 2017); *In re Pershing Square Capital Management, L.P.*, Investment Advisers Act Rel. No. 4608, 2017 SEC LEXIS 123 (Jan. 17, 2017); *In re The Banc Funds Co., L.L.C.*, Investment Advisers Act Rel. No. 4609, 2017 SEC LEXIS 124 (Jan. 17, 2017)**

The Commission accepted offers of settlement from 10 registered investment advisers (collectively, Respondents). The Commission alleged that Respondents permitted certain of its executives or employees that were "covered associates" for purposes of the Advisers Act pay-to-play rule (Rule 206(4)-5) to make campaign contributions to candidates for elected office and to elected officials in various states, which offices had the authority to appoint persons who had influence over selecting the respective Respondent to provide services to a public pension plan (each a Covered Fund and collectively, Covered Funds). Within two years of the contribution by the covered associate to the Covered Fund, each Respondent provided advisory services for compensation to the Covered Fund. In addition, Commonwealth Venture Management Corp. (CVMC) had a covered associate solicit campaign contributions for a candidate for elected office who had the authority to appoint persons who had an influence over selecting CVMC as an investment adviser to a Covered Fund when CVMC was already performing advisory services for compensation for the Covered Fund. The Commission alleged that as a result of this conduct, Respondents violated Advisers Action Section 206(4) and Rule 206(4)-5 thereunder. The Commission censured each Respondent and enjoined each Respondent from further violations of the Adviser's Act's pay-to-play prohibition. The penalties assessed against Respondents ranged from $35,000 (against two of the Respondents) to $100,000 (against NGN Capital LLC).

Scalping/Market Manipulation

***In re Mark A. Gomes*, Investment Advisers Act Rel. No. 4770, 2017 SEC LEXIS 2888 (Sept. 15, 2017)**

The Commission accepted an offer of settlement from Gomes (Respondent), an unregistered investment adviser and independent stock analyst, for a "scalping" scheme in which he provided investors and advisory clients with investment recommendations to purchase specific

securities through stock analysis websites in which he held an ownership interest, while failing to disclose that he was selling stock in his personal brokerage accounts in the same securities. The Commission alleged that on at least five occasions during the relevant period, Respondent sold shares in his personal accounts within days or hours of publicly providing a recommendation to investors or advisory clients to purchase shares of that issuer's stock without ever disclosing to investors that he planned to or was selling his shares. The Commission alleged that Respondent omitted to provide investors and advisory clients with material information necessary in order to make his recommendations not misleading, and consequently violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and Sections 206(1) and 206(2) of the Advisers Act. The Commission ordered that Respondent cease and desist from committing any further violations of the federal securities laws, barred him from association with a right to apply for reentry after five years, and required that he pay disgorgement of $130,669, prejudgment interest of $11,882, and a civil monetary penalty of $130,669.

Sharing of Confidential Information

***In re Brahman Capital Corp.*, Investment Advisers Rel. No. 4819, 2017 SEC LEXIS 3837 (Dec. 5, 2017); *In re Paritosh Gupta, Adi Capital Management LLC, Nehal Chopra, and Ratan Capital Management, LP*, Investment Advisers Rel. No. 4820, 2017 SEC LEXIS 3838 (Dec. 5, 2017)**

The Commission accepted offers of settlement from Paritosh Gupta, formerly a senior research analyst with Brahman Capital Corp., a hedge fund adviser (Brahman); Nehal Chopra, Gupta's spouse and the founder, owner and portfolio manager of Ratan Capital Management LP (Ratan) and Adi Capital Management LLC (Adi); and Ratan and Adi, both investment advisers that competed with each other and with Brahman, and pursued strategies similar to Brahman's. The Commission alleged that Gupta advised Chopra on Ratan's operations and investment strategy, including by providing advice on investing and by helping Gupta draft and edit communications to Ratan investors and prospective investors. The Commission further alleged that Gupta shared Brahman's confidential information with Chopra, including investment analysis, internal trading recommendations, and strategies developed for Brahman's clients, and provided Chopra with access to Brahman's third-party research providers, in contravention of Brahman's policies and procedures, and that Gupta continued to share Brahman's confidential information with Chopra even after Gupta was required to meet with a Brahman principal to discuss his activities and sign a document directing him to stop disclosing the information. The Commission alleged that Ratan's portfolio overlapped significantly with Brahman's portfolio. The Commission further alleged that Gupta's simultaneous work for both Brahman and Ratan, and his role in Ratan's investment strategy and process, was never disclosed to Brahman, Ratan, or their respective clients and prospective clients, and that Adi's February 2014 Form ADV brochure falsely stated that Gupta and Chopra did not discuss any confidential investment-related information. The Commission censured Ratan, Chopra, Gupta, and Adi and ordered Gupta to cease and desist from further violations of Sections 206(2), 206(4), and 207 of the Advisers Act and Rule 206(4)-8 thereunder; Adi to cease and desist from further violations of Section 207 of the Advisers Act;

and Ratan and Chopra to cease and desist from further violations of Sections 206(4) and 207 of the Advisers Act and Rule 206(4)-8 thereunder. The Commission also imposed civil penalties of $250,000 on Gupta, and $200,000 each on Chopra and Rattan.

In a related action, the Commission accepted an offer of settlement from Brahman. The Commission alleged that Brahman failed to supervise Gupta and, upon becoming aware of certain aspects of Gupta's conduct described above, failed to take reasonable steps to prevent its recurrence. The Commission further alleged that Brahman failed to implement policies and procedures reasonably designed to prevent Advisers Act violations, including with respect to safeguarding personal information and the use of personal email (which Gupta had used to share confidential information with Chopra). The Commission censured Brahman, ordered him to cease and desist from further violations of Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder, and to pay a civil penalty of $250,000.

Suitability of Investments

In re Morgan Stanley Smith Barney, LLC, Investment Advisers Act Rel. No. 4649, 2017 SEC LEXIS 456 (Feb. 14, 2017)

The Commission accepted an offer of settlement from Morgan Stanley Smith Barney, LLC (Respondent), a dually registered investment adviser and broker-dealer, in connection with Respondent's recommendations to approximately 600 nondiscretionary advisory clients that they invest in single-inverse ETFs. The Commission alleged that Respondent did not adequately implement its policies and procedures to ensure that clients understood the risks involved with purchasing inverse ETFs. Specifically, the Commission alleged that Respondent failed to obtain from many of these clients a signed client disclosure notice required by policy, which stated that single-inverse ETFs were typically unsuitable for investors planning to hold them longer than one trading session unless used as part of a trading or hedging strategy. The Commission further alleged that Respondent failed to follow through on another key policy requiring that, prior to purchasing a single-inverse ETF in such an account, a supervisor must conduct risk reviews to evaluate the ETFs suitability for the advisory client. As a result of this conduct, the Commission stated that Respondent failed to implement its compliance policies and procedures designed to ensure that recommendations of single-inverse ETFs to nondiscretionary advisory clients were suitable for each individual client.

The Commission alleged that Respondent was aware that the solicitation of the ETFs for advisory client accounts was a concern for regulators following sanctions that it received from FINRA in May 2012 and by the New Jersey Bureau of Securities in July 2013 for lack of compliance policies prior to June 2009 that addressed the sale of nontraditional ETFs, including the single-inverse ETF at issue in this conduct. The Commission further alleged that Respondent was aware of weaknesses and deficiencies in the implementation of its compliance policies and procedures in this area, which were noted by the OCIE in a 2010 exam of Respondent, as well as in internal testing from 2012 to 2014. The Commission censured Respondent and ordered it to cease and desist from committing or causing any violations and any future violations of

Section 206(4) of the Advisers Act and Rule 206(4)-7 promulgated thereunder. The Commission also ordered Respondent to pay a civil penalty of $8,000,000.

In re Gray Financial Group, Inc., **Investment Advisers Act Rel. No. 4812, 2017 SEC LEXIS 3679 (Nov. 22, 2017)**

The Commission accepted offers of settlement from Gray Financial Group, Inc., a former registered investment adviser based in Atlanta, Georgia (Gray Financial); Laurence O. Gray, founder of Gray Financial (Gray); and Robert C. Hubbard, IV, Gray Financial's co-CEO (Hubbard) (collectively, Respondents). The Commission alleged that Respondents breached their fiduciary duty to four Georgia-based public pension clients by recommending and selling investments in a proprietary fund of funds (the Fund) that Respondents knew or were reckless in not knowing were unsuitable because the investments violated the Georgia Investment Act 2012, which authorized eligible large Georgia retirement systems to invest in alternative investments for the first time, subject to certain limitations and restrictions. The Commission further alleged that Gray Financial and Gray made specific material misrepresentations to the board of trustees of one of the clients regarding compliance with Georgia law and the number and identity of prior investors in the Fund. The Commission alleged that, as a result of this conduct, Gray Financial and Gray willfully violated, and Hubbard willfully aided, abetted and caused their violations of, Sections 206(1) and 206(2) of the Advisers Act. In determining whether to accept Gray Financial's offer of settlement, the Commission considered Gray Financial's undertaking to cease acting as an investment adviser as defined in Section 202(a)(11) of the Advisers Act. The Commission censured Gray Financial, ordered Respondents to cease and desist from committing violations of Sections 206(1) and 206(2) of the Advisers Act, barred Gray from association with the right to reapply after two years, and suspended Hubbard for 12 months from association. The Commission further ordered Gray Financial and Gray to pay jointly $224,071 in disgorgement and $27,227.72 in prejudgment interest, and imposed civil penalties of $150,000 on Gray and $75,000 on Hubbard.

Trade Allocation

In re Tellone Management Group, Inc. et al., **Investment Advisers Act Rel. No. 4701, 2017 SEC LEXIS 1340 (May 5, 2017)**

The Commission accepted an offer of settlement from Tellone Management Group, Inc., a registered investment adviser (the Firm), and Tellone, its founder and president (collectively, Respondents). The Commission alleged that from January 2010 to August 2015, Respondents allocated profitable day trades in a manner that was sometimes inconsistent with the Firm's Form ADV disclosure to clients, which stated that the Firm used a rotation method for allocating block trades whereas, in practice, day trades with a profit of $300 or less were allocated to a single client account that had negotiated commission-free trades with a third-party brokerage firm. The Commission further alleged that the Firm's other clients therefore generally paid a higher price for their trades and bore the risk of the account that only received profitable day trades. The Commission censured Respondents, ordered them to cease and desist from further

violating Sections 206(2) and 207 of the Advisers Act, and imposed civil money penalties of $75,000 and $25,000 on the Firm and Tellone, respectively, with no penalty offset in any related investor action.

***In re Laurence I. Balter d/b/a Oracle Investment Research*, Investment Advisers Act Rel. No. 4710, 2017 SEC LEXIS 1578 (May 26, 2017)**

The Commission accepted an offer of settlement from Balter (Respondent), a formerly registered investment adviser and the principal of Oracle Investment Research, a sole proprietorship. The Commission alleged that from January 2011 to April 2014, Respondent, serving as the adviser to a mutual fund (the Fund) and to between 100 and 120 separately managed accounts (SMAs), engaged in three distinct violations. Specifically, the Commission alleged that Respondent fraudulently allocated profitable trades to his own accounts to the detriment of several client accounts; falsely told his SMA clients who invested in the Fund that they would not be subject to two layers of fees (advisory fees and Fund management fees) with respect to the portions of their accounts invested in the Fund; and made trades for the Fund that deviated from two of its fundamental investment limitations, significantly impacting the Fund's performance. The Commission ordered Respondent to cease and desist from further violating Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, Sections 206(1), 206(2), 206(4), and 207 of the Advisers Act and Rule 206(4)-8 thereunder, and Sections 13(a) and 34(b) of the Company Act, and imposed disgorgement of $489,921, prejudgment interest of $10,079, and a civil penalty of $50,000 on Respondent with no penalty offset in any Related Investor Action. The Commission also barred Respondent from association with a right to reapply.

***SEC v. Strategic Capital Management, LLC, and Michael J. Breton*, Litig. Rel. No. 23867, 2017 SEC LEXIS 1942 (June 23, 2017); *SEC v. Strategic Capital Management, LLC and Michael J. Breton*, Litig. Rel. No. 23779, 2017 SEC LEXIS 776 (Mar. 15, 2017); *SEC v. Strategic Capital Management, LLC and Michael J. Breton*, Litig. Rel. No. 23728, 2017 SEC LEXIS 235 (Jan. 25, 2017); *In re Michael J. Breton*, Investment Advisers Act Rel. No. 4663, 2017 SEC LEXIS 747 (Mar. 13, 2017)**

On January 25, 2017, the Commission brought charges against Strategic Capital Management, LLC (SCM) and its principal, Michael J. Breton (Breton) (collectively, Respondents), for allegedly defrauding clients out of approximately $1,300,000 by placing block trades through a master brokerage account and allocating the profitable trades to Breton's account while placing unprofitable trades into clients' accounts, thereby violating the antifraud provisions of the Exchange Act and the Advisers Act. Pending court approval, the Respondents agreed to be permanently enjoined from future violations of the antifraud provisions of the Exchange Act and Advisers Act, and Breton consented to an issuance of a Commission order barring him from association. Civil penalties were to be agreed upon at a later date. Separately, the US Attorney's Office for the District of Massachusetts announced criminal charges against Breton.

On March 3, 2017, Breton pleaded guilty to one count of securities fraud. Breton and SCM consented to the entry of a final judgment permanently enjoining them violating Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and Sections 206(1) and 206(2) of the

Advisers Act. Breton was sentenced by a federal district judge in Massachusetts on June 21, 2017 to two years in prison and two years of supervised release, and ordered to forfeit $1,326,696 and pay restitution in the same amount.

***In re Jeremy A. Licht d/b/a JL Capital Management*, Investment Advisers Act Rel. No. 4767, 2017 SEC LEXIS 2817 (Sept. 12, 2017); *In re Howarth Financial Services, LLC and Gary S. Howarth*, Investment Advisers Act Rel. No. 4768, 2017 SEC LEXIS 2814 (Sept. 12, 2017)**

In two separate actions, the Commission accepted an offer of settlement from Jeremy A. Licht (Licht), a California-registered investment adviser and the sole owner and principal of JL Capital Management, and Howarth Financial Services, LLC and its principal, Gary S. Howarth (Howarth) (collectively, Respondents), for allegedly engaging in fraudulent trade allocation schemes in which a disproportionate number of favorable trades were credited to accounts held for the benefit of Respondents, while a disproportionate number of unfavorable trades were allocated to clients' accounts. The Commission alleged that as a result of these schemes, Respondent Licht realized at least $88,500 in ill-gotten gains over a three-year period, and Respondent Howarth obtained $38,172 (including losses avoided). The Commission further alleged that Respondent Licht made false statements about the Firm's trade allocation practices in his disclosure to clients on his firm's Form ADV Part 2A. The Commission alleged that the Respondents violated Sections 206(1) and 206(2) of the Advisers Act, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. Respondents were each ordered to cease and desist from committing further violations of the securities laws and were barred from the industry. The Commission ordered Respondent Licht to pay disgorgement of $88,504, prejudgment interest of $8,714.34, and a civil penalty of $181,071. Respondent Howarth was ordered to pay a civil monetary penalty of $160,000, disgorgement of $38,172 and prejudgment interest of $5,272.

Unregistered Investment Company

***In re Honeysuckle Research Inc.*, Investment Company Act Rel. No. 32840, 2017 SEC LEXIS 3072 (Sept. 28, 2017)**

The Commission accepted an offer of settlement from Honeysuckle (Respondent), a corporation engaged in the business of investing and trading in hemp and cannabis-related securities, for acting as an unregistered investment company. Specifically, the Commission alleged that Honeysuckle (previously known as Ovation and then Weed Growth Fund, Inc.) acquired noncontrolling interests in various private and over-the-counter (OTC) link (Pink Sheets) issuers in the hemp, medicinal cannabis, and legalized cannabis space. Respondent had limited other assets beyond these investments and had no revenue since at least December 2014. Respondent failed to respond in a timely manner to an inquiry in 2015 from the Division of Corporation Finance and the Division of Investment Management as to whether it was an investment company as defined under the Company Act. Consequently, the Commission alleges that since December 2014, Respondent has been operating as an unregistered investment company as defined by Section 3(a)(1) of the Company Act, and not pursuant to an applicable

exclusion or exemption, as historically 84%-98% of its total assets (exclusive of government securities and cash items) were composed of investment securities. Further, the Commission stated that since December 2014, Respondent arranged for its shares to be quoted in the OTC market while continuing to buy securities for its portfolio and engaging in other business transactions in interstate commerce. The Commission stated that this conduct resulted in a violation of Section 7(a) of the Company Act. Under the terms of the order, Respondent agreed to come into compliance with Section 7(a) of the Company Act by either filing a notification of registration pursuant to Section 8(a) of the Company Act and a subsequent registration statement, or completing steps such that Respondent would no longer be required to register as an investment company. Respondent further agreed to not acquire any investment securities within the meaning of Section 3 of the Company Act until it is registered, or conduct any public offering, and to pay certain agreed-upon delinquency payments in lieu of a civil monetary penalty to the extent that it fails to meet the deadline to file notification of registration, or take steps such that it is not required to register. The Commission further ordered Respondent to cease and desist from further violations of the Company Act.

Valuation

In re Covenant Financial Services, LLC and Stephen Shafer, **Investment Advisers Act Rel. No. 4672, 2017 SEC LEXIS 982 (Mar. 29, 2017)**

The Commission accepted an offer of settlement from Covenant Financial Services, LLC (Covenant) and Stephen Shafer (Shafer), the Vice President, majority owner, portfolio manager, and Chief Investment Officer of Covenant (collectively, Respondents). The Commission alleged that Covenant materially misstated the value of municipal bonds held by five private funds (Funds), resulting in the payment of more than $400,000 in excess management fees. Covenant had engaged a third-party vendor pricing agent to value the municipal bonds held by the Funds beginning in 2009. However, beginning in August 2011 (a period of significant market volatility), the values provided by the third-party pricing agent were not consistent with GAAP fair-value measurements. Among other indications that the Funds overstated the value of these assets, the Funds sold some of the municipal bonds at prices materially less than the amounts recorded. Despite these indications, Covenant continued to use the values provided by the third-party pricing agent through the first quarter of 2013. This approach was inconsistent with Covenant's financial statements, its written valuation policy, and the representations made in the Funds' offering documents. When the valuation issue was discovered by auditors, Covenant refunded $440,000 in excess management fees to the Funds. Covenant also determined that the Funds overpaid about 40 redeeming investors in the Funds a total of more than $3,000,000. Covenant paid approximately $270,000 to the Funds as partial compensation for these overredemptions. The Commission alleged that as a result of this conduct, Covenant and Shafer violated Sections 206(2) and 206(4) of the Advisers Act and Rules 206(4)-7 and 206(4)-8 thereunder. The Commission ordered Respondents to cease and desist from further violations of the Advisers Act, censured both Respondents, and ordered them to pay, on a joint and several basis, a civil penalty of $130,000 and prejudgment interest of $14,845.

In re Enviso Capital, LLC, **Investment Advisers Act Rel. No. 4731, 2017 SEC LEXIS 2122 (July 19, 2017)**

The Commission accepted an offer of settlement from Enviso Capital, LLC, a registered investment adviser, and two of its principals, Ryan Bowers (Bowers) and Jeffrey LaBerge, CPA (LaBerge) (collectively, Respondents). The Commission alleged that between 2012 and 2014 (the Relevant Period), the Respondents materially overstated the value of two private funds advised by Enviso Capital in financial statements sent to investors. The Commission alleged that, in one case, Respondents overvalued the fund's primary asset, private company Bluefin Renewable Energy, LLC (Bluefin), by failing to use reasonable assumptions regarding projected revenues and that, in the other, Respondents failed to properly value a loan despite the fact that it was probable that the full outstanding amount would never be collected. The Commission also alleged that because of the above overstatement, the funds' financial statements were not prepared in accordance with US Generally Accepted Accounting Principles, resulting in Enviso Capital's violating the Custody Rule. In addition, the Commission alleged that Respondents made several misrepresentations regarding Bluefin's progress toward developing a renewable energy project in management discussions and analyses sent to fund investors. LaBerge had a primary role in formulating the valuations and disclosures, which were then approved by Bowers. Finally, the Commission alleged that Enviso Capital falsely disclaimed having custody of client assets in its Form ADV and that Bowers failed to timely conduct annual reviews of Enviso Capital's compliance program. Respondents consented to an order providing that Enviso Capital and Bowers cease and desist from committing or causing any violations or future violations of Sections 206(2), 206(4), and 207 of the Advisers Act and Rules 206(4)-2(b)(4), 206(4)-7, and 206(4)-8 promulgated thereunder, Enviso Capital be censured, and that LaBerge cease and desist from committing or causing any violations and any future violations of Sections 206(2) and 206(4) of the Advisers Act and Rules 206(4)-2 and 206(4)-8 promulgated thereunder. The Commission further ordered that Bowers and LaBerge be barred from association with the right to reapply for reentry after two years. Finally, the Commission ordered that Respondents each pay a civil money penalty of $50,000.

In re Six Financial Information USA Inc., **Investment Advisers Act Rel. No. 4780, 2017 SEC LEXIS 3070 (Sept. 28, 2017)**

The Commission accepted an offer of settlement from Six Financial Information USA (Respondent), an outside valuation agent for investment firms that is not a registered investment adviser, for misleading one of its investment firm clients as to the type of valuation work that it had performed on non-US options agreements. Specifically, the Commission alleged that one of Respondent's valuation experts represented to its investment firm client that Respondent was providing an independent valuation of particular European options at fair value by using a proprietary Black-Scholes-based method that it had developed. In reality, the valuation expert from Respondent calculated a valuation range for the particular options by making purported liquidity adjustments to valuations that were provided by the investment firm. Consequently, Respondent did not either perform an independent valuation of these options or use the proprietary method developed by Respondent, as represented to its client. The Commission alleged that in valuing these options, Respondent was acting as an investment adviser under the Advisers Act since it was engaged in the business of advising others as to the

value of securities (the options) for compensation. The Commission stated that as a result of this conduct, Respondent violated Section 206(2) of the Advisers Act. The Commission ordered Respondent to cease and desist from committing or causing any further violations of the Advisers Act, and to pay disgorgement and prejudgment interest of $32,707 and a civil penalty of $75,000.

In a separate action (*In re Perry H. Beaumont*, Investment Advisers Act Rel. No. 4781), the Commission accepted an offer of settlement under substantially similar allegations and terms from Perry H. Beaumont (Beaumont), Respondent's valuation expert. Beaumont was barred from association with a right to reapply for reentry after one year, and was further ordered to pay a civil monetary penalty of $50,000.

Wrap-Fee Programs – Trading Away

***In re Stifel, Nicolaus & Co., Inc.*, Investment Advisers Act Rel. No. 4665, 2017 SEC LEXIS 757 (Mar. 13, 2017)**

The Commission accepted an offer of settlement from Stifel, Nicolaus & Company, Inc. (Respondent), a dually registered investment adviser and broker-dealer. The Commission alleged that Respondent failed to adopt and implement written policies and procedures to track and disclose the trading-away practices of the subadvisers participating in Respondent's wrap-fee programs. The Commission alleged that Respondent did not track or monitor which subadvisers were trading away from Respondent, how often those subadvisers were trading away, or the specific costs associated with those trades. The Commission further alleged that, in the first quarter of 2015, Respondent began collecting cost information from subadvisers that were trading away, but allegedly failed to adopt or implement policies and procedures designed to provide information to Respondent's clients and financial advisers about the additional costs of trading away. The Commission alleged that, by failing to adopt and implement such policies and procedures, Respondent violated Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder. The Commission ordered Respondent to cease and desist from further violations of Section 206(4) of the Advisers Act and Rule 206(4)-7 thereunder and to pay a civil penalty of $300,000, taking into account Respondent's voluntary remedial efforts to strengthen its compliance function and its undertakings to review and update its policies and procedures related to tracking and disclosing subadviser trading-away practices and associated costs, to design and implement a way to provide clients in its wrap-fee programs and its financial advisors with information related to trading-away practices and associated costs on a periodic basis, and to develop and conduct training for its financial advisors on how to analyze this information in assessing whether an investment is suitable for a particular client.

Financial Industry Regulatory Authority

ENFORCEMENT DEVELOPMENTS

FINRA360

In early 2017, FINRA CEO Robert Cook (Cook) announced the launch of a new "self-evaluation and organizational improvement" initiative, FINRA360. The impetus for the initiative came from feedback Cook received during his ongoing listening tour about ways that FINRA could improve, and he seeks to provide a framework to address it. In particular, FINRA360 aims to examine a number of topics, including (i) the organization and operation of FINRA's regulatory functions; (ii) the use of data and technology; and (iii) the tools and metrics used to evaluate outcomes and successes throughout FINRA. FINRA anticipates that the initiative will be a multiyear project, focused on continuing to improve the organization, but it expects to implement changes on an ongoing basis.

Enforcement Consolidation

On July 26, 2017, FINRA announced that it would consolidate its two existing enforcement groups, Market Regulation Enforcement and the Department of Enforcement, into one unified department. Susan Schroeder, who had been the acting Head of Enforcement since February 2017, was announced to lead the new Enforcement department as Executive Vice President and Head of Enforcement, reporting to Cook. At a Securities Industry and Financial Markets Association (SIFMA) Compliance & Legal Society event on January 24, 2018, Cook remarked that one of the goals in consolidating the two enforcement groups is to develop a consistent "overall philosophy" throughout Enforcement. Cook said the combination was not merely a "change in reporting lines," but was aimed at creating a unified group with the same set of principles in approaching enforcement outcomes. FINRA's announcement credited FINRA 360 for the change.

Changes to Sanctions Guidelines

In April 2017, FINRA released Regulatory Notice 17-13 to advise firms of revisions to FINRA's Sanctions Guidelines. The notice stated that the National Adjudicatory Council made five additions to the Guidelines: (i) a new principal consideration to examine whether a respondent exercised undue influence over a customer; (ii) a new guideline applicable to systemic supervisory failures and firm wide supervisory failures, rather than focusing on limited supervisory failures (involving individuals or a small number of people); (iii) a new guideline for Short Interest Reporting to set forth principal considerations unique to such cases; (iv) a new guideline to address cases involving borrowing and lending arrangements between registered representatives and customers; and (v) a new general principal addressing potential mitigation where sanctions or corrective action were imposed by another regulator or by a member firm, replacing what was previously Principal Consideration No. 14. FINRA also revised the existing Sanction Guidelines to change the range of sanctions relating to what the notice referred to as

"more serious violations of FINRA rules," including, for example, violations related to the sales of unregistered securities, churning and unauthorized transactions. All changes were effective as of the release of the Regulatory Notice.

2018 Annual Budget Summary - Use of Fines Monies

On January 18, 2018, FINRA published its first annual budget summary. The 2018 Annual Budget Summary and the accompanying cover letter describe the six Financial Guiding Principles that will inform the organizations financial planning. In explaining one of the principles, "Use Fines to promote Compliance and Improve Markets," the Budget Summary states that, "[w]hen [FINRA] impose[s] fines, the amounts are based on the facts and circumstances of the misconduct and the principles set forth in our Sanction Guidelines; fines are not based on revenue considerations, and [FINRA] does not establish any minimum amount of fines that must be collected for purposes of [its] annual budget." The Budget Summary goes on to say that the use of fine monies is subject to special procedures and restrictions, and are not considered in determining employee compensation and benefits. The Board of Finance Committee must authorize the use of such funds and will do so for specific purposes: capital or non-recurring expenditures to promote effective regulatory oversight, education activities, capital or new initiatives required by changes in the law, or to replenish FINRA's reserves if necessary to preserve FINRA's ability to continue to fund its operations. FINRA will publish a description of the approved use of fine monies for the prior year on an annual basis.

TARGETED EXAMINATION LETTER

Order Routing Conflicts

In November 2017, FINRA posted a targeted examination letter announcing a review of the impact of the receipt of order routing inducements on firms' order routing practices and decisions. The Staff requested information relating to the quantification of benefits to customers from order routing inducements, such as payment of order flow and maker-taker rebates, as well as the processes for fulfilling best execution duties when routing orders to a market center with materially higher transaction costs than other market centers and the management of the conflict of interest between a firm's best execution duties and its own financial interests when utilizing market centers that offer order routing inducements.

FINRA REPORT ON EXAMINATION FINDINGS

On December 6, 2017 FINRA released its first "Report on FINRA Examination Findings." FINRA issued the report – as it will continue to do on a routine basis – to provide firms with an additional resource for complying with the securities rules and regulations. The report highlights key observations from FINRA's recent examinations, and notes certain effective practices identified by the examination staff. The December 2017 Report includes a section called "Highlighted Observations" in which it discusses what it has seen in the following areas:

(i) cybersecurity; (ii) outside business activities and private securities transactions; (iii) anti-money laundering compliance programs; (iv) product suitability; (v) best execution; and (vi) market access controls. The Report also includes "Additional Observations," other areas FINRA wants to bring to firms' attention. They are: (i) alternative investments held in IRAs; (ii) net capital and credit risk assessments; (iii) order capacity; (iv) Regulation SHO; and (v) trace reporting.

FINRA'S 2018 REGULATORY AND EXAMINATION PRIORITIES

On January 8, 2018, FINRA published its Annual Regulatory and Examination and Priorities Letter (the 2018 Letter). The 2018 Letter describes the areas FINRA intends to focus on during its 2018 exams. To help guide firms' assessment of risk management policies in order to align with FINRA's priorities in the new year, the below discussion highlights priorities outlined in the 2018 Letter, identifying with an asterisk potential new areas of concern for firms, as well as recognizing topics that have fallen off the priority list since 2017.

2018 Priorities

Fraud

FINRA will continue to review activities such as insider trading, issuer fraud, and Ponzi-type schemes, with a specific focus on microcap fraud schemes that target senior investors. FINRA will also review firms' Suspicious Activity Report–filing obligation practices.

High-risk Firms and Brokers

FINRA will continue to prioritize identifying high-risk firms and brokers and will focus on assessing firms' hiring and oversight of brokers. FINRA will closely review the risks posed to senior or unsophisticated investors, and firms' controls on outside business activities of registered persons.

Operational and Financial Risks

- *Business Continuity Planning: FINRA will assess firms' business continuity plans, as required under FINRA Rule 4370 to enable firms to continue to meet existing customer obligations in case of an emergency or business disruption (such as the recent Hurricanes Harvey and Maria).

- Customer Protection and Verification of Assets and Liabilities: FINRA will review firms' net capital and reserve computations for accuracy under Rules 15c3-1 and 15c3-3. FINRA will also examine the adequacy of firms' possession or control supervision and controls, whether firms maintain no-lien letters if necessary, and whether foreign depositories, clearing agencies and custodial banks are good control locations.

- *Technology Governance: FINRA will analyze the adequacy of firms' information and technology change management policies and procedures, and reminds firms that it is important to maintain strong controls over information technology changes (e.g., enhancements or modifications to internal or vendor systems).

- Cybersecurity: FINRA will review firms' cybersecurity programs, specifically as they relate to protecting sensitive and/or personally identifiable information, and notes that firms must have appropriate Suspicious Activity Report policies and procedures. FINRA cross-references the December 6, 2017 Examination Findings Report (the Examination Findings Report), which highlights characteristics of effective cybersecurity programs and notes that some examined firms could improve their cybersecurity programs as they relate to access management, risk assessments, vendor management, branch offices, segregation of duties, and data loss prevention.

- Anti-Money Laundering: FINRA will assess firms' AML programs, including the adequacy of firms' policies and procedures, AML resources and independent testing under FINRA Rule 3310(c). FINRA notes that foreign affiliates could be used to conduct high-risk transactions, and firms should adequately monitor foreign affiliate accounts. FINRA cross-references the Examination Findings Report, which lists select AML program best practices, and highlights failures in the following areas at examined firms: maintaining adequate policies and procedures for suspicious activity, responsibility for AML monitoring, exclusions from data feeds used for AML monitoring, resources for AML monitoring, and independent testing of AML monitoring.

- Liquidity Risk: FINRA will continue to review the adequacy and appropriateness of firms' liquidity plans. FINRA notes that firms should review Regulatory Notice 15-33 for guidance in developing an effective liquidity management plan.

- *Short Sales: FINRA will review firms' policies and procedures for short sale rates and will assess whether firms follow the procedures in place when calculating such rates.

Sales Practice Risks

- Suitability: FINRA will continue to review firms' suitability controls, including firms' processes relating to products such as Unit Investment Trusts (UITs) and multishare class products, and recommendations made to retirement plan participants.

- *Initial Coin Offerings and Cryptocurrencies: FINRA will monitor transactions in digital assets and initial coin offerings, and may review firms' related supervisory, compliance, and operational procedures.

- *Use of Margin: FINRA will review firms' margin loan disclosure and supervisory processes.

- *Securities-Backed Lines of Credit (SBLOC): FINRA will assess firms' compliance with SBLOC sales practice and operational obligations, including firms' SBLOC disclosures, controls, and red-flag procedures.

Market Integrity

- Manipulation: FINRA notes that it may review its market manipulation surveillance programs, including, for example, FINRA's new Cross Market Auction Ramping surveillance pattern launched in August 2017.

- Best Execution: FINRA is expanding its best execution surveillance and will review price improvement when routing customer orders. FINRA is developing a new surveillance pattern to systematically review the frequency of price improvement and the relative amount of that improvement in firms' routing of customer orders. FINRA will also review how firms manage the conflict of interest between their best execution duties and their own financial interests. FINRA cross-references the Examination Findings Report, which cites effective best execution best practices and notes that FINRA observed deficiencies related to failing to compare execution quality between markets, failing to conduct reviews of certain order types, and failing to consider FINRA Rule 5310 when conducting effective reviews.

- Regulation SHO: FINRA will increase its focus on compliance with Rule 201 of Regulation SHO, and firms' reliance on Rule 201 exemptions.

- Fixed Income Data and Integrity: FINRA developed data integrity surveillance patterns to identify instances of late reporting, failing to report interdealer trades, misreporting of interdealer trades, and inaccurate execution time–reporting. Examinations may also include a review of firms' Trade Reporting and Compliance Engine (TRACE) reporting and the accuracy of electronic communications with customers.

- *Options: FINRA developed a surveillance pattern to detect potential options' front-running activities and will also review "marking the close" options activity. FINRA will also review firms' options-related obligations under Rule 14e-4.

- Market Access: FINRA will continue to review compliance with Rule 15c3-5 (the Market Access Rule). FINRA cross-references the Examination Findings Report, which highlights effective market access controls and identifies deficiencies identified in the following areas: establishing pretrade financial thresholds, implementing and monitoring aggregate financial exposures, tailoring erroneous or duplicative order controls, implementing effective fixed-income financial controls, reliance on vendors for fixed-income financial controls, and effective testing for fixed-income financial controls.

- Alternative Trading System Surveillance: FINRA will review alternative trading systems' supervisory systems and assess firms' reviews of potential manipulative activity on alternative trading systems.

Report Cards

FINRA developed the following new report cards and will assess whether firms make effective use of them: (i) Auto Execution Manipulation Report Card, (ii) Alternative Trading System Cross Manipulation Report Card, and (iii) Fixed Income Mark-up Report Card.

New Rules

FINRA emphasizes that certain significant new rules will go into effect in 2018, and FINRA may assess the ways firms are planning to comply with their new obligations under the following rules:

- Financial Exploitation of Specified Adults (FINRA Rule 2165, eff. Feb. 5, 2018)
- Customer Account Information (Amendments to FINRA Rule 4512, eff. Feb. 5, 2018)
- Financial Crimes Enforcement Network's (FinCEN's) Customer Due Diligence Rule (CDD Rule) (firms must comply by May 11, 2018)
- Customer Confirmations (Amendments to FINRA Rule 2232, eff. May 14, 2018)
- Margin Requirements for Covered Agency Transactions (Amendments to FINRA Rule 4210, eff. Dec. 15, 2016)
- Consolidated FINRA Registration Rules (FINRA Rules 1210–1240, eff. Oct. 1, 2018)

Diminished Focus in 2018?

Areas that were not addressed in the 2018 Letter but were in prior iterations include (i) social media and electronic communications retention and supervision; (ii) municipal advisor registration; and (iii) FINRA's Audit Trail Reporting Early Remediation Initiative. The 2018 Letter also did not specifically highlight topics such as excessive or short-term trading of long-term products, outside business activities, and supervisory control testing.

As of the date of publication of this outline, FINRA had not yet announced its 2017 enforcement statistics.

FINRA ENFORCEMENT ACTIONS

Advertised Trading Volumes

HSBC Securities (USA) Inc., FINRA AWC No. 2013035716601 (Jan. 19, 2017)

In a Letter of Acceptance, Waiver and Consent (AWC) with HSBC Securities (USA) Inc. (HSI), FINRA alleged that the firm overadvertised its trade volume executed to Bloomberg on several occasions. According to FINRA, between November 2009 and September 2014, a programming error in one of the firm's order management systems caused HSI to overadvertise the trade volume executed in at least 30 separate affected trading books. FINRA alleged that a sample of HSI's advertised trade volume showed that the programming error caused HSI to overadvertise trade volume executed in 34 securities by approximately 1,272,563 shares between November

2009 and September 2014. FINRA also alleged that, between August 2011 and December 2011, HSI overadvertised trade volume executed in 42 instances by approximately 7,923,300 shares as a result of a trader manually submitting trade volume to Bloomberg, while the firm's Order Management System also automatically sent the trade volume to Bloomberg. FINRA further alleged that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with the relevant rules. HSI consented to a censure, a fine of $575,000, and an undertaking to revise the firm's written supervisory procedures. In determining the sanction, FINRA took into account the firm's cooperation, including that HSI self-reported certain of the overadvertising violations.

J.P. Morgan Securities LLC, **FINRA AWC No. 2012033515001 (Sept. 13, 2017)**

FINRA entered into an AWC with J.P. Morgan Securities LLC (JPMS) in which it alleged that, from June 9, 2010 through July 26, 2012, the firm overstated its trade volume advertisements transmitted to Bloomberg and AutEx by billions of shares. Specifically, FINRA alleged that when the firm implemented a "code-split" designed to create two separate order management systems, the firm failed to account for certain filters that would have ensured that trade volume was not replicated. Instead, according to FINRA, the firm erroneously captured and advertised volume that had already been advertised on a trade date when it later swept for volume to report on trade date plus three (T+3). FINRA alleged that its review uncovered additional instances of overadvertisement prior to the firm's implementation of the "code-split" based on the system's failure to filter out replicated parent-child order volume. FINRA also alleged that the firm did not have adequate written supervisory procedures to ensure the accuracy of its advertised trade volume. As a result of this matter, JPMS voluntarily removed billions of shares it had advertised, but the removal occurred after the relevant trade dates. JPMS consented to a censure, a fine of $1,100,000, and an undertaking to revise the firm's written supervisory procedures with respect to advertising trade volume and to provide a written report to FINRA regarding the implementation and performance of the firm's revised written supervisory procedures. In determining the sanction in this matter, FINRA took into account the firm's self-reporting of the overadvertising that resulted from the failure to account for filters.

Anti-Money Laundering

Merrill Lynch, Pierce, Fenner & Smith Inc., **FINRA AWC No. 2012035224301 (Dec. 21, 2017)**

In an AWC with MLPFS, FINRA alleged that the firm failed to adequately implement its AML systems and procedures. Specifically, FINRA alleged that, between September 2011 and January 2012, while implementing changes to its primary monitoring system because it produced too many "false positives," MLPFS decided to stop reviewing certain activity detected only by that system (as opposed to by other AML monitoring systems). As a result, FINRA found that the firm failed to investigate 1,015 Event Groups (groups of events generated by AML monitoring systems that arose over the last 13 months in the same or related accounts at MLPFS or elsewhere in its parent company) that consisted of only events generated by its primary automated monitoring system during that period. According to FINRA, the firm

reviewed these events in 2014 after the initiation of the investigation that led to the settlement. FINRA further alleged that MLPFS had a deficient system for scoring potentially suspicious activity in its monitoring system, causing it to, for example, not link related accounts and fail to identify customers in high-risk jurisdictions or senior political figures. FINRA also found that, from approximately 2006 through May 2015, MLPFS excluded retirement accounts, certain managed accounts, and certain accounts pledged as collateral to securities-based loans from review by its primary monitoring system. This exclusion, according to FINRA, was known to MLPFS beginning in 2012 and involved millions of accounts. FINRA found that, as a result of these deficiencies, MLPFS also failed to adequately investigate potentially suspicious activity in retail brokerage accounts maintained for nonresident aliens at branches in McAllen, Texas, San Diego, and New York City. MLPFS consented to a censure and a fine of $13 million. In a related matter, the SEC ordered the firm to be censured and pay a fine of $13 million.

Consolidated Reporting

Edward Jones, FINRA AWC No. 2016049783001 (July 13, 2017)

FINRA entered into an AWC with Edward Jones in which FINRA alleged that Edward Jones failed to establish, maintain, and enforce an adequate supervisory system, including written supervisory procedures, concerning the creation and dissemination of consolidated reports from April 2010 through 2014. According to FINRA, Edward Jones lacked any system reasonably designed to mitigate the risk that consolidated reports would communicate inaccurate, confusing, or misleading information, including inaccurately valuing accounts and assets held away from the firm. For example, FINRA found that the firm did not have in place a centralized review process for consolidated reports. FINRA also alleged, for example, that Edward Jones had no policies or procedures to guide its registered representatives on how to create and use consolidated reports. FINRA further alleged that Edward Jones did not provide guidance to registered representatives on how outside information should be included in consolidated reports, whether to verify such information before it was included, or how and when to update it. In addition, FINRA alleged that Edward Jones had no way of determining whether consolidated reports were actually delivered to customers. The AWC notes that, in a review of 65,000 of the 52 million reports created between April 2010 and December 2014, FINRA did not find any instances of reports that were materially inaccurate or misleading. Edward Jones consented to a censure and a fine of $725,000. In determining the sanction, FINRA took into account Edward Jones's comprehensive review of the reports, as well as the extensive remediation implemented to the firms' systems.

Customer Protection Rule

J.P. Morgan Securities LLC, FINRA AWC No. 2015047091401 (Dec. 27, 2017)

FINRA entered into an AWC with J.P. Morgan Securities LLC as successor to J.P. Morgan Clearing Corp. (JPMCC); JPMCC was formerly known as Bear Stearns Securities Corporation (Bear Stearns). In the AWC, FINRA alleged that from March 2008 through June 2016, design

flaws and certain coding and data errors in the legacy Bear Stearns systems resulted in a failure to segregate customers' foreign securities in good control locations as required by Rule 15c3-3. As examples, FINRA alleged that deficits occurred in Italian and Nigerian securities because segregation instructions were not implemented due to coding and data errors. Similar types of technological errors affected securities in Sri Lanka, Turkey, Zambia, Venezuela, and Puerto Rico. FINRA further alleged that design flaws in segregation systems, such as coding that assumed, rather than verified, share movements, or failed to account for canceled instructions, caused deficits in certain international securities. With respect to domestic securities, FINRA alleged that undetected intraday deficits occurred because shares were incorrectly released when a system design flaw treated recalled depository bank loan securities as available to meet segregation requirements. FINRA further alleged that the firm did not reasonably supervise the segregation function, specifically that (a) disparate groups carrying out the function communicated ineffectively and thus there was no comprehensive analysis of root causes, (b) trends were not identified, and (c) periodic independent reviews of the control function across more than 60 countries were not performed. JPMCC was given credit for extraordinary cooperation, which included unilaterally hiring an independent consultant, undertaking a comprehensive review and disclosing new issues to FINRA, creating a new team for overseeing the function, and implementing new monitoring systems. JPMCC was also credited for over-reserving hundreds of millions weekly in cash deposits in order to protect customers. JPMCC agreed to a censure and a fine of $2.8 million.

Exchange-Traded Products

Wells Fargo Clearing Services, LLC, **FINRA AWC No. 2014042465601 (Oct. 16, 2017)**

FINRA settled a matter with Wells Fargo Clearing Services, LLC and Wells Fargo Advisors Financial Network, LLC (collectively, Wells Fargo) in which FINRA alleged that Wells Fargo failed to establish and maintain a reasonably designed supervisory system and procedures related to the sale of volatility exchange-traded products (Volatility ETPs) and, as a result, made unsuitable recommendations of Volatility ETPs. According to FINRA, the firm failed to vet, or restrict to certain risk profiles or investment objectives, Volatility ETPs that became available between early 2009 and May 2012. FINRA alleged that, from July 1, 2010 to May 1, 2012, Wells Fargo and certain Wells Fargo–registered representatives did not perform reasonable diligence to understand the risks and rewards associated with Volatility ETPs before soliciting and effecting Volatility ETP purchases and, therefore, before having a reasonable basis to believe they were suitable. FINRA further alleged that the firm's supervisory system did not provide for supervision or training reasonably designed to achieve compliance with the rules in connection with the sale of Volatility ETPs. Wells Fargo consented to a censure and payment of restitution in the amount of $3,411,478.54. In determining this sanction, FINRA took into account the firm's cooperation, including that Wells Fargo took immediate remedial steps, was previously fined $2.1 million for similar violations relating to ETPs, and provided substantial assistance to FINRA's investigation by, among other things, engaging a consulting firm to determine the appropriate restitution to be provided to affected customers.

Extended Settlement Transactions

***Merrill Lynch, Pierce, Fenner & Smith, Inc.*, FINRA AWC No. 2014041808101 (Dec. 19, 2017)**

In an AWC with Merrill Lynch, Pierce, Fenner & Smith, Inc. (MLPFS), FINRA alleged that, from at least April 2013 through June 2015, the firm did not identify and evaluate certain retail and institutional trades with extended settlement dates (ES Trades). According to FINRA, the firm's computation of margin requirements and net capital deductions was inaccurate for tens of thousands of ES Trades, and the firm improperly extended hundreds of millions of dollars of margin credit in retail customers' cash accounts. As a result, the firm failed to maintain accurate schedules to the general ledger and file accurate FOCUS reports, although FINRA acknowledged that the firm had sufficient net capital during the relevant period. FINRA alleged that MLPFS was made aware of its deficiencies regarding ES Trades during a 2012 Member Regulation examination, but the firm failed to implement timely remedial measures in response to the examination findings. Accordingly, FINRA alleged that the firm failed to establish a reasonable supervisory system and procedures with respect to ES trades. MLPFS consented to a censure and a fine of $1.4 million.

Fingerprinting

***J.P. Morgan Securities LLC*, FINRA AWC No. 2016049305401 (Nov. 21, 2017)**

In an AWC with JPMS, FINRA alleged that from January 2009 to May 2017, the firm failed to fingerprint and screen a significant number of its nonregistered associated persons timely or adequately. Specifically, according to FINRA, the firm failed to fingerprint 2,036 associated persons and screen 8,670 nonregistered associated persons to verify that they were not subject to statutory disqualification prior to their association with the firm. FINRA further alleged that JPMS violated record retention rules by failing to create and maintain records of the four associated persons subject to disqualification and fingerprint records for all eligible associated persons. FINRA also alleged that the firm failed to establish and maintain an adequate supervisory system, including the failure to establish, maintain, and enforce written supervisory procedures for onboarding nonregistered associated persons. JPMS agreed to a censure, a fine of $1.25 million, and an undertaking to review its systems and procedures regarding the identification, fingerprinting, and screening of nonregistered associated persons. FINRA considered the fact that the firm self-reported and undertook to remediate the issue in determining the monetary sanction.

Large Options Position Reporting

***Wells Fargo Securities, LLC*, FINRA AWC No. 2014040326101 (June 21, 2017)**

FINRA entered into an AWC with Wells Fargo Securities, LLC (WFS), alleging that the firm violated certain options rules. Specifically, FINRA alleged that WFS (1) failed to report 60,808

conventional OTC options positions in 18,868,889 instances to the Large Options Positions Report (LOPR) between January 2008 and August 19, 2014; (2) failed to accurately report a significant number of conventional options positions to the LOPR between August 19, 2014 and March 2017, erring in a variety of the required LOPR data fields; (3) exceeded the OTC position limit by 25% for at least 461 trading dates in options relating to one security and by 40% for two trading dates in options related to another security between January 2008 and March 2017; and (4) failed to report a small number of physically settled OTC exercises to the FINRA Trade Reporting Facility with a modifier to denote that the transactions were reported for regulatory transaction fee assessment purposes (i.e., ".RX"). FINRA also alleged that WFS failed to maintain any system of supervision for the reporting of conventional OTC options positions to the LOPR system from January 2008 through 2014, including any relevant written supervisory procedures. FINRA further alleged that, after implementing supervisory systems, the firm still failed to detect errors in numerous conventional OTC options positions reported to the LOPR. FINRA also alleged that the firm did not have an adequate system of supervision related to the exercise of physically settled OTC options. WFS consented to a censure, a fine of $3.25 million, and an undertaking to review its supervisory procedures. In determining the sanction, FINRA considered WFS's provision of extraordinary cooperation, including (a) retaining outside counsel to conduct a review of the firm's options reporting systems, practices, and procedures and sharing that report with FINRA; (b) hiring an independent consultant to conduct a complete review of the LOPR systems, and identify deficiencies and the firm's correction of those deficiencies; and (c) remediating the reporting systems, including the implementation of enhanced reviews and written supervisory procedures for LOPR compliance.

***Goldman, Sachs & Co. LLC*, Bats BZX Exchange AWC No. 2012031318002 (June 26, 2017), NASDAQ PHLX Enforcement No. 2017-12 (July 12, 2017), NASDAQ ISE AWC No. 2012031318003 (July 17, 2017), FINRA AWC No. 2012031318001 (July 17, 2017)**

FINRA and three options exchanges, Bats BZX Exchange, Inc. (BATS), NASDAQ ISE, LLC (ISE), and NASDAQ PHLX LLC (PHLX), entered into settlements with Goldman, Sachs & Co. LLC (Goldman Sachs) alleging that the firm violated various options rules. With regard to reporting to the LOPR, FINRA alleged that (1) between January 19, 2010 and February 19, 2010, Goldman Sachs failed to report more than 16,700 OTC options positions in at least approximately 6.8 million instances to the LOPR, along with an unknown number of intraday positions; (2) between January 19, 2010 and March 18, 2018, the firm failed to report certain OTC options positions in approximately 1.6 million instances because of the firms failure to aggregate positions acting in concert; and (3) between January 1, 2016 and July 7, 2016, Goldman Sachs failed to report OTC positions for a potentially significant, but unknown, number of instances involving 671,080 rejected records and inaccurately reported positions to the LOPR in at least 12.7 million instances for various reasons. FINRA further alleged that Goldman Sachs exceeded position limits on July 31, 2010 for its proprietary account, from April 25, 2016 through April 26, 2016 for the account of a customer, and from at least August 2015 through February 21, 2016 for the account of another customer.

BATS alleged that Goldman Sachs (1) failed to report options positions in 118 accounts of the firm's foreign affiliate in hundreds of thousands of instances to the LOPR between at least

February 19, 2010 and August 31, 2013; (2) inaccurately reported (i.e., invalid or missing address fields) a significant number of positions between at least February 19, 2010 and July 7, 2016; and (3) inaccurately reported options positions with the wrong effective dates for approximately 25,500 positions in the same number of instances.

PHLX alleged that the firm (1) failed to report options positions to the LOPR in 110,220 instances due to a failure to recognize symbols for securities reclassified as units following a corporate action; (2) submitted a "delete" instruction to the LOPR instead of a "modify" instruction, causing the failure to report three options positions; (3) over-reported options positions in 14,166 instances and under-reported options positions in 6,354 instances when the firm inadvertently suppressed "delete" records that should have been reported to the LOPR; and (4) failed to report or inaccurately reported 3,161 options positions in an unknown number of instances due to a technical flaw that caused stale data to be downloaded to the LOPR system.

ISE alleged that the firm (1) failed to report options positions to the LOPR in an unknown number of instances involving approximately 791,940 rejected records that were not resubmitted; (2) reported options positions in an unknown amount of positions and instances that were inaccurate in a variety of fields, including the address, tax number, and tax number type fields; and (3) reported positions with an incorrect account type of customer in an unknown amount of positions and instances.

FINRA and the exchanges also alleged that Goldman Sachs failed to establish and maintain an adequate supervisory system for options reporting and did not have adequate written supervisory procedures. The firm consented to a censure, a total fine of $2.5 million, and an undertaking to address deficiencies and implement controls and procedures for compliance. In determining the settlement, FINRA considered that Goldman Sachs self-reported a number of the violations and cooperated throughout the investigation. FINRA also took into account the firm's remediation.

Market Access Rule

***Deutsche Bank Securities Inc.*, NYSE MKT AWC No. 201309313502 (May 15, 2017), Bats BYX AWC No. 2013039313509, Bats BZE AWC No. 2013039313508, Bats EDGA AWC No. 2013039313510, Bats EDGX AWC No. 2013039313511 (May 18, 2017), NYSE ARCA Dec. No. 20130393135 (May 23, 2017), PHLX Enf. No. 2017-08 (June 2, 2017), FINRA AWC No. 2013039313504, NASDAQ BX AWC No. 2013039313506, NASDAQ AWC No. 2013039313505 (June 28, 2017)**

FINRA and several exchanges entered into AWCs with Deutsche Bank Securities Inc. (DBSI) in which they alleged that DBSI had inadequate Market Access Rule controls. According to FINRA and the exchanges, based on the review of the trade date April 23, 2014, DBSI failed to establish, document, and maintain a system of risk management controls and supervisory procedures to manage risks related to market access, including controls to systematically limit the financial exposure such as blocking orders that exceed preset credit or capital thresholds

and the entry of erroneous orders, as well as controls that restrict access to trading systems. They further alleged that, from March 1 through April 30, 2014, the firm failed to establish, document, and maintain a system of risk management controls and supervisory procedures to manage the risks of its direct market access (DMA) business, particularly by failing to include customer's DMA trading activity in the firm's post-trade market abuse surveillance and thus missing potential layering activity by a customer. FINRA found that an error occurred when the firm changed from one internal system to another, causing certain post-trade market abuse surveillance to not be run over the customer equity DMA business. Specifically, between July 1, 2012 and November 30, 2014, 239,945,894 orders involving 34,453,516,262 shares were excluded from this surveillance. FINRA further alleged that, between March 1, 2012 and December 31, 2014, the firm had a gap in its surveillance of customer DMA activity. DBSI consented to a censure and a total fine of $2.5 million. FINRA stated that the sanction reflected significant consideration to the substantial assistance provided by the firm, which included identifying and self-reporting the gap in its surveillance and providing extraordinary cooperation.

***Interactive Brokers LLC*, Bats BZX AWC No. 2012034773003, Bats EDGA AWC No. 2012034773004, Bats EDGX AWC No. 2012034773005 (May 17, 2017), NASDAQ AWC No. 2012034773002, NYSE ARCA Dec. No. 20120347730010 (May 23, 2017)**

Bats BZX Exchange, Inc., Bats EDGA Exchange, Inc., Bats EDGX Exchange, Inc., NASDAQ Stock Market LLC, and NYSE ARCA (collectively, the exchanges) settled a matter with Interactive Brokers LLC (Interactive) in which they alleged that Interactive had inadequate Market Access Rule controls from July 1, 2013 through at least January 31, 2016. Specifically, the exchanges found that Interactive had inadequate (1) pretrade price controls, such as failing to have controls for orders outside of regular market hours; (2) pretrade size controls, which were too wide; and (3) written supervisory procedures for erroneous orders prior to at least December 31, 2013. The exchanges further alleged that Interactive failed to adequately supervise its customers' trading to detect and prevent potentially violative activity. In particular, at various points during the review period, the firm did not have dedicated surveillance reports or reviews to detect unusual patterns of cancellations or to identify unusual price and/or volume activity in thinly traded securities. Interactive consented to a censure, a total fine of $450,000, and an undertaking requiring the firm to address the deficiencies in the settlement.

***Citigroup Global Markets Inc.*, FINRA AWC No. 2013035462906 (June 9, 2017), Bats BZX Exchange AWC No. 2013035462902 (May 30, 2017), NYSE AWC No. 2013035462905 (June 9, 2017), NASDAQ AWC No. 2013035462904, NYSE ARCA FINRA Proceeding No. 2013035462901 (June 9, 2017), Bats BYX AWC No. 2013035462903 (May 30, 2017)**

FINRA and several exchanges (NASDAQ Stock Market LLC, Bats BZX Exchange, Inc., Bats BYX Exchange, Inc., New York Stock Exchange LLC, and NYSE Arca Equities, Inc. (collectively, the exchanges)) entered into AWCs with Citigroup Global Markets Inc. (CGMI) related to allegations that the firm violated the Market Access Rule between July 2012 and at least December 2016. Specifically, FINRA and the exchanges alleged that CGMI failed to implement reasonable pretrade risk management controls for certain orders and failed to establish and implement

reasonable supervisory procedures to prevent entry of erroneous orders, including sufficient pretrade price and size controls. For example, the firm's controls employed ineffective soft blocks that could be easily overridden by CGMI traders, and the firm did not review or capture the triggering or overriding of the soft blocks. FINRA and the exchanges further alleged that these deficient controls allowed the transmission of erroneous equity orders to the exchanges that caused 12 clearly erroneous events and the filing of eight clearly erroneous execution (CEE) petitions for six of those events. Those errors, in turn, caused a trading halt and several large price change alerts/price movements, including a price movement in one security of approximately 34% that set its 52-week low. According to FINRA and the exchanges, CGMI also failed in certain instances to implement controls that considered individual characteristics of a security and, even when implemented, such controls were often set too high to be effective or employed an excessive minimal share quantity threshold. In certain instances, FINRA and the exchanges found that CGMI pretrade erroneous order controls wholly failed to be applied. In addition to pretrade erroneous order controls, FINRA and the exchanges alleged that, from July 2012 to March 2014, CGMI had at least one trading desk that lacked risk management controls and supervisory procedures to prevent the entry of orders that exceeded appropriate preset capital thresholds by rejecting such orders and, from July 2012 through at least December 2016, failed to configure controls to prevent entry of orders that breached a preset capital threshold. Finally, FINRA and the exchanges found inadequate periodic review of override activity, particularly instances from June 2013 through at least December 2016 in which a soft block for credit limits/capital thresholds were triggered or overridden. The firm consented to a censure and a total fine of $1 million.

***JP Morgan Securities LLC*, Bats BYX AWC No. 2012034829609, Bats BZX AWC No. 2012034829604, Bats EDGX AWC No. 2012034829605, NYSE AWC No. 2012034829602 (June 21, 2017), PHLX Enf. No. 2017-10 (June 26, 2017), ARCA Dec. No. 2012034829601, ARCA Dec. No. 2012034829606 (June 27, 2017), NOM AWC No. 2012034829607, NASDAQ AWC No. 2012034829603 (June 28, 2017)**

Bats BZX Exchange, Inc., Bats EDGX Exchange, Inc., NASDAQ Stock Market LLC, NYSE Arca Equities, Inc., NYSE Arca Options, Inc., NASDAQ Options Market LLC, and NASDAQ PHLX LLC (collectively, the exchanges) settled a matter with JPMS in which they alleged that the firm had inadequate Market Access Rule controls during the period of May 2012 through at least April 2016. Specifically, the exchanges alleged that the thresholds in the commercial nonproprietary third-party surveillance system used by JPMS were set at levels that were unreasonable to detect potentially violative activity, such as layering and spoofing. JPMS agreed to a censure, a total fine of $800,000, and an undertaking to address its Market Access Rule deficiencies.

***Jefferies LLC*, NASDAQ AWC No. 2013037184501 (Dec. 18, 2017)**

On behalf of the NASDAQ Stock Market LLC, FINRA settled a matter with Jefferies LLC (Jefferies) in which it alleged that Jefferies failed to comply with a 2011 undertaking and that the firm's Market Access Rule controls were inadequate between February 2012 and the present. According to FINRA, despite a 2011 undertaking that required Jefferies to revise its supervisory procedures and remediate its pre-order controls by lowering its maximum share quantity control and a representation to FINRA that the change had been made, the firm did

not actually lower the control until August 30, 2013, when contacted by FINRA about an erroneous petition filed with Nasdaq Market Watch. FINRA alleged that the firm did not correct its previous misstatement to FINRA regarding the correction of the control and that the firm provided misleading and/or inaccurate responses to FINRA when asked about its compliance with the 2011 undertaking. As a result, FINRA found that Jefferies failed to comply with the 2011 undertaking. In the AWC, FINRA noted that the firm's senior management cooperated with FINRA during a 2015 review of the conduct, including by voluntarily waiving privileges associated with internal communications. FINRA also alleged that the firm had inadequate pretrade controls for erroneous orders, including deficiencies with pretrade price and size controls and controls to account for the individual trading characteristics of a security, as well as a lack of approval or review of soft-block overrides. FINRA further alleged that the firm had inadequate preset capital thresholds, failing to have any capital thresholds prior to 2014, and only implementing soft capital limits without real-time supervisory reviews of overrides since 2015. FINRA further alleged that, beginning in June 2013, Jefferies defaulted new clients to a credit limit without conducting due diligence and failed to maintain sufficient documentation regarding its credit limit due diligence. FINRA found that Jefferies did not have written supervisory procedures for credit and capital limit breaches. Finally, FINRA alleged that from June 2013 through 2016, the firm's periodic reviews were inadequate, particularly because Jefferies failed to review soft-block overrides on a real-time, post-trade, or periodic basis. In assessing the matter, FINRA considered the firm's voluntary engagement of an outside consultant. Jefferies agreed to a censure, a fine of $1 million, and an undertaking to address the issues in the AWC and implement reasonably designed controls and procedures.

Mutual Fund Sales Charges

***BB&T Investment Services, Inc.*, FINRA AWC No. 2016051183701 (Dec. 5, 2017)**; ***Cetera Advisors, LLC*, FINRA AWC No. 2016050259001 (May 3, 2017)**; ***Cetera Advisor Networks, LLC*, FINRA AWC No. 201605025881 (May 3, 2017)**; ***Cetera Financial Specialists, LLC*, FINRA AWC No. 2016050259101 (Aug. 21, 2017)**; ***Cetera Investment Services LLC*, FINRA AWC No. 2016050259201 (Aug. 21, 2017)**; ***Citizens Securities, Inc.*, FINRA AWC No. 2016049977401 (Mar. 31, 2017)**; ***First Allied Securities, Inc.*, FINRA AWC No. 2016050259301 (Aug. 21, 2017)**; ***FSC Securities Corporation*, FINRA AWC No. 2017054137901 (Dec. 20, 2017)**; ***Girard Securities, Inc.*, FINRA AWC No. 2016050259401 (Aug. 21, 2017)**; ***J.P. Turner & Company, LLC*, FINRA AWC No. 2016050260101 (Dec. 7, 2017)**; ***Invest Financial Corporation*, FINRA AWC No. 2015046036301 (Feb. 22, 2017)**; ***Investacorp Inc.*, FINRA AWC No. 2015047977401 (Dec. 6, 2017)**; ***Investment Centers of America, Inc.*, FINRA AWC No. 2015046688401 (Feb. 22, 2017)**; ***Investors Capital Corporation*, FINRA AWC No. 2016050259601 (Dec. 7, 2017)**; ***Legend Equities Corporation*, FINRA AWC No. 2016050259801 (Apr. 4, 2017)**; ***MSI Financial Services, Inc.*, FINRA AWC No. 2016052332801 (May 12, 2017)**; ***National Planning Corporation*, FINRA AWC No. 2015046915901 (Feb. 22, 2017)**; ***Questar Capital Corp.*, FINRA AWC No. 2016049977801 (Nov. 2, 2017)**; ***Royal Alliance Associates, Inc.*, FINRA AWC No. 2016049977701 (Dec. 20, 2017)**; ***SagePoint Financial, Inc.*, FINRA AWC No. 2017054229301 (Dec. 20, 2017)**; ***SII Investments, Inc.*, FINRA AWC No.**

2015046915601 (Feb. 22, 2017); ***Summit Brokerage Services, Inc.*****, FINRA AWC No. 2016050260001 (Aug. 21, 2017);** ***VSR Financial Services, Inc.*****, FINRA AWC No. 2016050260201 (Dec. 7, 2017);** ***Woodbury Financial Services, Inc.*****, FINRA AWC No. 2016049976501 (Dec. 20, 2017)**

During 2017, 24 firms entered into settlements with FINRA for matters that involved failing to identify and apply sales charge waivers to eligible customers. The eligible customers included certain retirement plans and/or charitable organizations. According to FINRA, the firms failed to apply waivers of up-front sales charges associated with Class A shares made by eligible accounts. FINRA found that the firms either sold the Class A shares with a front-end sales charge or disadvantaged the accounts by selling them Class B or C shares, which had back-end sales charges and higher ongoing fees and expenses. FINRA further alleged that each of the firms had supervisory failures.

Of the 24 firms, 14 self-reported the conduct to FINRA and, in the settlements, FINRA recognized the firms' extraordinary cooperation in initiating their own investigations, remediating the conduct and procedures, and planning for restitution to affected customers. As a result of that activity and consistent with FINRA's recent treatment of these cases, FINRA censured the firms and required remediation to customers, but did not impose a monetary fine. The restitution amounts, inclusive of interest, were as follows:

- BB&T Investment Services, Inc. – approximately $373,134 in restitution;
- Cetera Advisors, LLC – approximately $628,040 in restitution;
- Cetera Advisor Networks, LLC – approximately $1,911,080 in restitution;
- Cetera Financial Specialists, LLC – approximately $572,260 in restitution;
- Cetera Investment Services LLC – approximately $1,391,325 in restitution;
- First Allied Securities, Inc. – approximately $876,915 in restitution;
- Girard Securities, Inc. – approximately $102,765 in restitution;
- J.P. Turner & Company, LLC – approximately $213,137 in restitution;
- Investacorp Inc. – approximately $247,886 in restitution;
- Investors Capital Corporation – approximately $437,674 in restitution;
- Legend Equities Corporation – approximately $2,300,188 in restitution;
- MSI Financial Services, Inc. – approximately $2,200,000 in restitution;
- Summit Brokerage Services, Inc. – approximately $356,915 in restitution; and
- VSR Financial Services, Inc. – approximately $47,801 in restitution.

Three of the firms conducted their own reviews after FINRA initiated an examination of an affiliated firm. These firms then self-reported to FINRA. In determining the sanctions, FINRA similarly took into account the firms' extraordinary cooperation. The fines and restitution amounts, not including interest, for those firms were:

- Investment Centers of America, Inc. – a fine of $60,000 and approximately $154,194 in restitution;
- National Planning Corporation – a fine of $60,000 and approximately $521,370 in restitution; and

- SII Investments, Inc. – a fine of $75,000 and approximately $965,720 in restitution.

Two other firms similarly conducted reviews after FINRA initiated an examination of an affiliated firm, but their AWCs did not reflect credit for extraordinary cooperation or self-reporting. The fines and restitution amounts, inclusive of interest, for those firms were:

- FSC Securities Corporation – a fine of $100,000 and approximately $414,261 in restitution; and
- SagePoint Financial, Inc. – a fine of $75,000 and approximately $196,372 in restitution.

Four firms conducted reviews in response to FINRA's initiation of an examination. The fines and restitution amounts, inclusive of interest, for those firms were:

- Citizens Securities, Inc. – a $50,000 fine and approximately $64,023 in restitution;
- Invest Financial Corporation – a $225,000 fine and approximately $504,722 in restitution;
- Royal Alliance Associates, Inc. – a $150,000 fine and approximately $519,699 in restitution; and
- Woodbury Financial Services, Inc. – a $75,000 fine and approximately $128,583 in restitution.

One firm, Questar Capital Corp., conducted a review in response to FINRA's initiation of an examination, but voluntarily expanded the review period significantly, almost doubling the restitution amount. Recognizing extraordinary cooperation, FINRA did not impose a fine in that matter. The restitution amount was approximately $796,862, inclusive of interest.

All of the firms were censured.

Net Capital

***Royal Alliance Associates, Inc.*, *FSC Securities Corporation*, *SagePoint Financial, Inc.*, *Woodbury Financial Services, Inc.*, *Igner Wilson Fields*, FINRA AWC No. 2016049751001 (May 3, 2017)**

In an AWC, FINRA alleged that Royal Alliance Associates, Inc. (Royal Alliance), FSC Securities Corporation (FSC), SagePoint Financial, Inc. (SagePoint), and Woodbury Financial Services, Inc. (Woodbury) (collectively, the affiliated firms) applied an inaccurate accounting and net capital treatment of investment advisory fees. Specifically, FINRA alleged that the firms booked investment advisory fees on a net basis, offsetting prepayments to financial advisers against related deferred revenue, instead of booking the fees on a gross basis. According to FINRA, this resulted in the firms recognizing only the net difference between fees collected in advance and what was prepaid to financial advisers when the rules require that prepaid expenses be deducted as nonallowable. FINRA found these accounting inaccuracies to cause hindsight net capital deficiencies, books and records violations, and financial reporting inaccuracies. FINRA

alleged that Royal Alliance, FSC, and SagePoint failed to compute their net capital and excess net capital accurately and conducted a general securities business for some period of time between January 2010 through April 2016 without the required net capital. In addition, FINRA alleged that those firms failed to prepare and maintain accurate financial records and filed inaccurate monthly FOCUS reports for 50 months during the same period; according to FINRA, Woodbury failed to do the same for 18 months. Igner Wilson Fields was the Financial and Operations Principal (FINOP) for the firms during the period between January 2010 and April 2015. The firms agreed to a fine of $550,000 ($260,000 for Royal Alliance, $150,000 for FSC, $75,000 for SagePoint, and $65,000 for Woodbury). Fields also agreed to a $5,000 fine and a one-month suspension. In determining the sanctions, FINRA considered the firms' self-reporting of the issues, retention of a new FINOP, and remedial measures.

OATS Reporting

Credit Suisse Securities (USA) LLC, FINRA AWC No. 2014039938101 (Jan. 18, 2017)

FINRA settled a matter with Credit Suisse Securities (USA) LLC (Credit Suisse) that arose from the firm's 2014 Trading and Financial Compliance Examination. According to FINRA, during the course of the examination, it identified a number of issues concerning trade and Order Audit Trail System (OATS) reporting and related supervision. With respect to OATS reporting, FINRA alleged that the firm (1) over-reported 39,047 reports to OATS from 2003 through December 12, 2014; (2) failed to report Combined Order/Route Reports to OATS for 864 orders in July 2014; (3) included incorrect member type codes of "N" on 11 reports; (4) incorrectly submitted Combined Order/Execution Reports for two proprietary orders; and (5) submitted billions of broker dealer orders to OATS with incorrect account type codes of "A" from October 17, 2011 through February 13, 2015. With respect to trade reporting, FINRA found that the firm failed to report the correct symbol indicating whether the transaction was a buy, sell, or sell short for 5,632 transactions to FINRA/Nasdaq Trade Reporting Facility. FINRA also found that 45 transactions were reported as short sales when the firm's position was long on July 15, 2014 and that, from March 21, 2014 through September 11, 2014, 5,587 transactions were reported as long sales when the firm's position was short. FINRA further alleged that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with the relevant rules. Credit Suisse consented to a censure and a total fine of $487,500 (composed of $375,000 for the OATS violations, $100,000 for the supervisory violations, and $12,500 for the trade-reporting violations), and undertook to revise the firm's supervisory system, including, but not limited to, its written supervisory procedures.

Wedbush Securities, Inc., FINRA AWC No. 2011030598001 (Sept. 27, 2017), NYSE Arca AWC No. 20120333282 (Sept. 26, 2017)

In an AWC with Wedbush Securities, Inc. (Wedbush), FINRA alleged that the firm failed to comply with rules related to OATS reporting, Regulation SHO close-out obligations, and short interest position reporting from June 1 to December 31, 2014, as well as related supervisory obligations. Specifically, FINRA found that the firm failed to transmit 548,669,414 Reportable Order Events (ROEs) generated by a sponsored access client to OATS due to a technology issue

in the firm's reporting system. FINRA further alleged that, on 171 occasions, Wedbush accepted a short sale order or effected a short sale for its own account without first either borrowing the security or entering into a bona fide arrangement to borrow the security, and that the firm had a fail-to-deliver position at a registered clearing agency in such a security that was not closed out as required by Rule 204(a) of Regulation SHO. FINRA also found that on 61 days between April and June 2013, Wedbush reported 171 short interest positions totaling 4,706,076 shares when it should have reported 90 short interest positions totaling 747,865 shares due to a coding error. FINRA further alleged that the firm's written supervisory procedures were not enforced as to OATS, were inadequate for close-out obligations because they failed to address certain obligations, and did not provide the steps for supervision of short interest reporting. Wedbush agreed to a censure and a fine of $470,000, $70,000 of which is payable to NYSE Arca Equities Inc. FINRA noted that an undertaking was not required with respect to the written supervisory procedures due to the firm's previous retention of an independent consultant that revised the relevant procedures.

Offering Fraud

Red River Securities, LLC, FINRA Disc. Proc. No. 2013035344201 (Feb. 9, 2017)

A FINRA hearing panel expelled broker-dealer Red River Securities, LLC (Red River) from FINRA membership, barred its CEO Brian Hardwick from association with any FINRA member, and ordered payment of tens of millions of dollars in restitution to investors for various securities violations, including fraud. The panel found that, between January 2010 and July 2013, Red River and Hardwick fraudulently misrepresented and omitted material facts in connection with the sale of interests in five oil and gas joint ventures issued by firm affiliate Regal Energy, LLC. Specifically, the panel found that Red River and Hardwick (1) made misrepresentations that inflated the amount of income distributed to investors in prior well-related ventures; (2) omitted a series of material conflicts of interests; (3) omitted that one of the oil and gas wells at issue was a well without historic production that carries increased investment risk; (4) omitted the significant management fees to be paid by investors; (5) misrepresented as independently authored a geologist report prepared by Hardwick himself; and (6) preyed on two investors for whom the venture was not suitable. The panel noted numerous aggravating factors, including the failure to maintain and enforce an adequate supervisory system and written supervisory procedures, as well as the amount of monetary gain. That is, of the approximately $25 million raised for these ventures from 456 investors, Red River and Hardwick paid themselves more than $10.7 million, while distributing less than $500,000 to investors. In addition to expelling and barring Red River and Hardwick, the panel ordered them to pay restitution totaling $24,615,849 plus interest.

Order Handling

Merrill Lynch, Pierce, Fenner & Smith Inc., FINRA AWC No. 2011028842101 (May 16, 2017)

In a settled matter with MLPFS, FINRA alleged that, from July 1, 2010 through December 31, 2012, the firm failed to adequately review the quality of execution of its customers' nonconvertible preferred securities (NCPS) and OTC convertible preferred securities (CPS) orders. Specifically, according to FINRA, when NCPS orders were manually entered, customers incurred an additional charge that caused the execution price to be inferior to available quotes on automated markets. FINRA also alleged that the manual handling of these transactions caused the firm to record inaccurate order execution times to its books and records, as well as to submit inaccurate trade reports to the FINRA/Nasdaq Trade Reporting Facility (TRF) with the inaccurate timestamp and a mark-up or mark-down in the unit price. Further, FINRA found that MLPFS issued inaccurate confirmations to its customers, failing to disclose the difference between the price reported to the TRF and the price to the customer. Separately, FINRA alleged that from January 1, 2011 through September 30, 2014, the firm failed to adequately review the quality of execution of its customers' OTC CPS orders. According to FINRA, the firm failed to review quotes on automated markets, which led to inferior prices for customers and failed order executions. Finally, FINRA alleged that the firm's written supervisory procedures failed to meet minimum requirements and that the firm failed to demonstrate that it performed the supervisory reviews described in its procedures for OTC CPS executions. MLPFS consented to a censure, a fine of $650,000, and an undertaking to submit a letter acknowledging that the firm revised its written supervisory procedures.

Morgan Stanley Smith Barney LLC, FINRA AWC No. 2012034714701 (Aug. 22, 2017)

In an AWC with MSSB, FINRA alleged that the firm violated rules related to recordkeeping, trade reporting, trading ahead, and best execution of preferred securities orders, along with related supervision rules. Specifically, from January 1, 2012 to September 30, 2013, FINRA found that the firm routinely failed to show the correct order receipt time and/or execution on brokerage memoranda for trades in the National Market System (NMS) stock placed through a process that involved a financial advisor aggregating orders of preferred securities and communicating the aggregated amount verbally to the firm's fixed income sales department, which then liaised with the firm's preferred securities trading desk. FINRA also found that for some or all of these trades, the firm failed to report the trades to the FINRA Trade Reporting Facility (TRF) and that the orders were marked as "not held" even when the customer did not instruct the orders to be handled on a "not held" basis, which removed them from consideration by MSSB's best execution surveillance tool. According to FINRA, between January 1, 2012 and September 30, 2013, the firm also failed to contemporaneously or partially execute 683 customer orders in 66 OTC securities after it traded each subject security for its own market-making account at a price that would have satisfied each customer's limit order because it erroneously marked OTC-preferred securities as exempt from trading-ahead protection (i.e., Manning obligations). FINRA further alleged that, from April 1, 2014 through November 30, 2014, MSSB failed to fulfill its best execution obligations in 74 transactions for or with a customer in preferred securities. In addition, FINRA alleged that, from April 1, 2015 through

September 30, 2015, the firm failed to execute orders in preferred securities fully and promptly and, in 23 of those orders, failed to fulfill its best obligations. FINRA found that, for each alleged violation, the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance. MSSB agreed to a censure and a fine of $500,000, as well as to pay $103,219.25 plus interest in restitution.

Prospectus Delivery

Goldman Sachs & Co. LLC, FINRA AWC No. 2014042582101 (Dec. 1, 2017)

In an AWC with Goldman Sachs, FINRA alleged that, between June 2008 and October 2014, Goldman Sachs Execution and Clearing, L.P. (GSEC), a former affiliate that merged into Goldman Sachs, failed to maintain systems and procedures reasonably designed to achieve compliance with prospectus-delivery requirements for ETF purchases. FINRA alleged that GSEC's procedure for testing whether a prospectus was delivered for an ETF purchase looked only at whether GSEC's vendor had mailed certain prospectuses, and did not test GSEC's overall prospectus-delivery system. According to FINRA, this deficiency allowed at least three system design flaws to remain undetected for nearly five years, resulting in numerous prospectuses not being delivered in connection with more than 100 million ETF purchases cleared during the period. Specifically, FINRA alleged that GSEC (1) failed to deliver ETF prospectuses after taxpayer identification numbers had been removed from the system and no substitute identifier was incorporated to distinguish customers' initial purchases of an ETF security, which required prospectus delivery; (2) did not mail certain prospectuses because an operational error sent mailing labels to the wrong printing queue and no labels were printed; and (3) had a system that did not consider whether a prospectus had been updated since a customer's initial purchase of an ETF and thus failed to deliver updated prospectuses. Goldman Sachs agreed to a censure and a fine of $700,000, as well as an undertaking to certify that its policies, systems, procedures, and training are reasonably designed to ensure delivery of ETF prospectuses.

Research Ratings

Citigroup Global Markets, Inc., FINRA AWC No. 2016048931101 (Dec. 28, 2017)

In an AWC with CGMI, FINRA alleged that from February 2011 to December 2015, the firm displayed inaccurate research ratings for more than 1,800 securities (38% of the equities covered by the firm) due to errors in the electronic feed of ratings data that CGMI provided to its clearing firm. The inaccurate ratings appeared in an internal online platform used by representatives to make securities recommendations, retail customer communications (including account statements, email alerts, and an external online portal), and certain supervisory tools. According to FINRA, as a result of the display of inaccurate research ratings, CGMI brokers solicited thousands of transactions inconsistent with the firm's actual ratings and that violated the portfolio guidelines of certain firm-managed portfolios as well as caused the firm to provide customers with inaccurate ratings. FINRA further alleged that the firm failed to timely correct the inaccurately displayed ratings despite numerous red flags and failed to conduct testing

reasonably designed to verify the accuracy of research ratings data, and, as such, did not have a reasonably designed supervisory system for the dissemination of accurate ratings. In setting the sanction, FINRA credited the firm for cooperation, including self-reporting the issues, engaging outside counsel to conduct a forensic investigation, taking steps to prevent the display of inaccurate information, providing substantial assistance to FINRA by sharing the results of the internal investigation, and proposing and developing a substantial remediation plan to compensate affected customers. CGMI agreed to a censure, a fine of $5.5 million, and to pay at least $6 million in restitution. FINRA considered that the firm discovered and reported certain of these violations to FINRA and provided substantial assistance during FINRA's investigation in determining the sanction in this matter.

Sales Charge Discounts

Purshe Kaplan Sterling Investments, FINRA Disc. Proc. No. 2014042291901 (Feb. 22, 2017)

After bringing charges in a February 2016 complaint, FINRA settled a matter with Purshe Kaplan Sterling Investments (PKS) in which it alleged that a PKS-registered representative, Gopi Vungarala, charged a Native American tribe excessive sales charges on purchases of nontraded Real Estate Investment Trusts (REITs) and Business Development Companies (BDCs), and the firm failed to supervise the sales of those securities. According to FINRA, Vungarala was the tribe's registered representative and Treasury Investment Manager from July 2011 through at least January 15, 2015, and PKS failed to review the risks inherent in the relationship. During that time, Vungarala repeatedly lied to the tribe, including misrepresenting that neither he nor PKS would receive commissions on the tribe's purchases and failing to make the tribe aware of the availability of certain volume discounts. FINRA alleged that Vungarala fraudulently induced the tribe to invest more than $190 million in nontraded REITS and BDCs on which Vungarala received more than $9 million in commissions. FINRA further alleged that PKS failed to identify the fact that more than 200 of the tribe's investments were eligible for discounts based on the volume of the purchases. Although Vungarala represented to PKS that the tribe did not want to receive the discounts, FINRA found that PKS failed to take steps to verify this representation. FINRA also alleged that PKS did not have written supervisory procedures reasonably designed to identify accounts that were eligible for volume discounts, and did not provide guidance to its representatives or supervisors regarding how to ensure that sales volume discounts were applied appropriately. PKS was ordered to be censured, pay a fine of $750,000, and pay restitution in the amount of $3,373,303.68, plus interest. In addition, PKS was ordered to retain an independent consultant.

Supervision

Legend Securities, Inc., FINRA Disc. Proc. No. 2012030422902 (May 25, 2017)

In a FINRA Office of Hearing Officers decision, the hearing officer entered a default judgment against Legend Securities, Inc. (Legend) on a seven-cause complaint filed by FINRA's

Department of Enforcement alleging numerous violations of SEC and FINRA rules. FINRA alleged that Legend failed to establish and maintain an adequate supervisory system and written supervisory procedures to ensure that it (1) reported customer complaints to FINRA; (2) reviewed email communications; (3) timely filed amendments to Forms U4 and Forms U5; and (4) considered whether to place registered representatives on heightened supervision. FINRA also alleged that Legend failed to report or timely report to FINRA 96 written customer complaints involving numerous sales practice violations. In addition, FINRA found that Legend failed to file, or filed late, seven Forms U4 and one Form U5 on behalf of current or former registered representatives alleging various sales practice violations. Finally, the complaint alleged that Legend charged customers an unlawful "handling fee" from January 2013 through May 2014, in addition to a commission or markup/markdown, generating $884,436.24 in revenue. For the causes relating to Legend's alleged failure to exercise reasonable supervision and maintain adequate written supervisory procedures, the hearing officer imposed a unitary fine in the amount of $175,000, as suggested by FINRA's Sanctioning Guidelines for systemic supervisory failures. The hearing officer also imposed fines totaling $475,000, composed of $75,000 for alleged failure to report customer complaints, $25,000 for the late filing of Forms U4 and Forms U5, $200,000 for Legend's alleged charging of unjustified handling fees, as well as restitution in the amount of $884,436.24 for the fees.

NEXT Financial Group, Inc., **FINRA AWC No. 2015043319901 (Dec. 6, 2017)**

In an AWC with NEXT Financial Group, Inc. (NEXT), FINRA alleged that the firm failed to adequately implement new processes to address deficiencies cited in prior FINRA matters, resulting in violations at various times between August 2012 and September 2015. Specifically, FINRA alleged that, between May 2014 and September 2015, NEXT used faulty exception reports to detect excessive trading, such as reports with inappropriate parameters and inaccurate calculations, and failed to review those reports for 14 months, which allowed excessive trading to continue. FINRA also alleged that the firm did not have sufficient or clear supervisory procedures, causing the firm's failure to address certain concerns related to excessive trading that were escalated. FINRA found that, as a result of these supervisory failures, a registered representative was able to excessively trade in a senior investor's accounts, causing losses of approximately $391,893. The AWC stated that NEXT also failed to have a surveillance system to monitor rates of exchange for variable annuities, did not have sufficient variable annuities exception reports, and did not have procedures to address risks associated with multishare class variable annuities. FINRA also alleged that NEXT did not sufficiently monitor the use of consolidated reports by its registered representatives, did not maintain accurate information on its website relating to the firm's financial partners, and did not reasonably supervise noncash compensation received by its registered representatives. NEXT consented to a fine, a censure of $750,000, and an undertaking to retain an independent consultant.

Raymond James Financial Services, Inc., **FINRA AWC No. 2013036343601 (Dec. 21, 2017)**

In an AWC with Raymond James Financial Services, Inc. (Raymond James), FINRA alleged that between December 2007 and September 2017, the firm's email review system was not

reasonably designed to achieve compliance with applicable legal requirements in light of the firm's business model, size, structure, and customers. Raymond James relied primarily on an automated, lexicon-based system that allowed the firm to select from and customize various policies designed to flag emails containing certain words that suggested further review was warranted. Specifically, FINRA alleged that the email system was flawed because the primary lexicon used was not reasonably designed to identify emails suggesting potentially problematic conduct. FINRA also alleged that the firm failed to devote adequate personnel and resources to the team that reviewed emails flagged by the system and failed to apply all of the lexicon policies to the emails of approximately 1,300 registered representatives who worked in branch offices that maintained their own email servers. FINRA alleged that the firm did not periodically test the configuration and effectiveness of the lexicon system and lacked reasonable procedures for doing so. During some of the period, the firm used an additional manual review process whereby representatives self-selected and shared emails with supervisors for review, but there was no effective means of confirming that they provided all required emails, and when branch managers left, records of the review were not retained. According to FINRA, the foregoing allowed millions of emails to evade meaningful review and contributed to the failure by the firm to detect the sale of certain unregistered notes. Raymond James agreed to a censure, a fine of $2 million, and an undertaking to adopt and implement written supervisory procedures that are reasonably designed to address the identified deficiencies, complete a risk-based retrospective review, and comply with reporting obligations for any findings arising from the review.

Survivor Bonds

Department of Enforcement v. C.L. King & Associates, Inc., FINRA Disc. Proc. No. 2014040476901 (Sept. 6, 2017)

After an extended hearing, a FINRA hearing panel determined that C.L. King & Associates, Inc. (C.L. King) made material misrepresentations and omissions related to redemptions of debt securities on behalf of its customers and failed to establish and maintain a supervisory system to oversee that activity and its sales of penny stocks. According to the hearing panel, the firm took on the business of its customer, which involved opening brokerage accounts as joint tenants with rights of survivorship with people who were terminally ill. The accounts were then used to purchase discounted corporate debt securities that contained a survivor option or death put (i.e., survivor bonds). The customer's business required the terminally ill participants to sign agreements forfeiting ownership rights to the assets in the accounts and, after their death, the business could redeem the investments for full principal amount before maturity through C.L. King. The hearing panel found that the firm was obligated to disclose to issuers during the redemption process that the terminally ill account holders lacked beneficial ownership of the survivor bonds. Moreover, the firm failed to establish and maintain a reasonable supervisory system to address survivor bond redemptions. Separately, the hearing panel determined that the firm and its AML compliance officer failed to implement and maintain a sufficient AML program to identify risks presented by the penny stock liquidation business of two customers and to detect certain red flags. In addition, the firm failed to respond to red flags related to the suspicious activity of one of its customers, a foreign financial institution. The hearing panel censured C.L. King and fined it $750,000. The firm's AML compliance officer was suspended in

a principal capacity for six months and fined $20,000. The AML compliance officer was also ordered to requalify as a principal following the suspension.

TRACE Reporting

Deutsche Bank Securities Inc., **FINRA AWC No. 2015044324901 (Dec. 13, 2017)**

In an AWC with Deutsche Bank Securities Inc. (DBSI), FINRA alleged that from October 2014 through December 2016, the firm did not adequately escalate TRACE-reporting deficiencies, including reporting the incorrect time of execution, late reporting, deal-mismatch–reporting issues, and setting up new issues. FINRA also alleged the DBSI did not take sufficient steps to remediate these deficiencies. This was in part because the firm's TRACE-reporting structure was decentralized without clear lines of responsibility. FINRA also considered the firm's "pattern of non-compliance" with regard to TRACE reporting, citing seven prior FINRA matters between November 2012 and March 2016. The AWC states that, through the course of 19 reviews, FINRA found that the firm failed to report, untimely reported, or inaccurately reported transactions to TRACE in a number of instances between October 2014 and December 2016. In addition, for certain quarters during the review period, FINRA alleged that DBSI failed to show the correct time of execution on its brokerage order memorandum, causing a books and records violation. DBSI consented to a censure and a fine of $1.1 million ($450,000 for supervision and $650,000 for TRACE-reporting violations and books and records). In assessing the matter, FINRA considered that following the initiation of FINRA's review, DBSI conducted an internal review and presented its findings to FINRA, retained an independent consultant, and initiated a firmwide remediation plan.

J.P. Morgan Securities, LLC, **FINRA AWC No. 2013038331001 (Feb. 24, 2017)**

In a settlement with JPMS, FINRA alleged that the firm failed to timely report the client side of transactions facilitated by certain trading desks to the TRACE and Real-Time Transaction Reporting System (RTRS). FINRA found that, although JPMS properly reported the street-side transactions (i.e., the transaction between JPMS and the street), the firm did not timely report the offsetting transaction between the client and the firm. Specifically, FINRA alleged that the firm failed to report 147,456 client-side transactions in TRACE-eligible securities to TRACE within 15 minutes and, when reported, failed to report the correct execution time. Similarly, FINRA found that JPMS failed to timely report 132,839 client-side purchase and sale transactions effected in municipal securities to the RTRS Portal within 15 minutes and, when reported, failed to report the correct execution time. FINRA also alleged that JPMS's supervisory system did not provide for supervision reasonably designed to achieve compliance with respect to the applicable securities laws and regulations and FINRA and MSRB rules relating to the TRACE and RTRS reporting. JPMS consented to censure and a fine of $675,000, comprising $287,500 for the TRACE reporting violations, $287,500 for the MSRB Rule G-14 violations, $50,000 for TRACE-related supervision violations, and $50,000 for MSRB-related supervision violations. In determining the sanctions, FINRA considered the firm's self-identification of the conduct, self-reporting of the conduct, extraordinary assistance with the investigation, and remediation efforts.

Unit Investment Trusts

***Morgan Stanley Smith Barney LLC*, FINRA AWC No. 2016048805501 (Sept. 25, 2017)**

In an AWC with MSSB, FINRA alleged that, from January 2012 through June 2015, the firm failed to establish and maintain a supervisory system and written supervisory procedures reasonably designed to detect and prevent unsuitable short-term trading of UIT by its representatives. According to FINRA, MSSB's procedures offered insufficient guidance to supervisors for monitoring and reviewing transactions. In addition, although alerts were sent to supervisors when a UIT was purchased within 60 days of the sale of an open-end mutual fund or UIT, forcing the supervisor to take additional action, UIT rollovers did not generate alerts and thus did not receive the review and approval of supervisors. During the relevant period, FINRA alleged that hundreds of representatives executed short-term UIT rollovers in thousands of customer accounts. MSSB consented to a censure, a fine of $3.25 million, and restitution to 3,020 customer accounts in the amount of $9,786,964.88. In determining the sanction, FINRA considered the firm's cooperation in initiating a firmwide investigation prior to intervention by a regulator, establishing a plan to provide remediation to affected customers, and providing substantial assistance to FINRA in its investigation.

WORM

***Acorns Securities, LLC*, FINRA AWC No. 2016052098301 (July 11, 2017); *Allianz Life Financial Services, LLC and Questar Capital Corporation*, FINRA AWC No. 2016051317701 (June 30, 2017); *HSBC Securities (USA) Inc.*, FINRA AWC No. 20170531337201 (June 30, 2017); *MML Investors Services, LLC, MML Distributors, LLC, MML Strategic Distributors, LLC, and OppenheimerFunds Distributor, Inc.*, FINRA AWC No. 2016052647801 (June 30, 2017); *State Street Global Markets, LLC*, FINRA AWC No. 2016051821601 (July 11, 2017); *Virtu Financial Capital Markets LLC*, FINRA AWC No. 2016051831201 (Sept. 8, 2017)**

Following the first wave of settlements with 12 firms in December 2016, FINRA released a second wave of AWCs with 10 additional firms related to allegations that each firm had deficiencies relating to the preservation of broker-dealer and customer records in "write once, read many" or "WORM" format, which prevents the alteration or destruction of records stored electronically, during the middle of 2017. According to FINRA, each firm's WORM-related deficiencies affected a substantial number of records (in certain cases, tens of millions of records). FINRA also alleged that the firms had procedural and/or supervisory deficiencies related to the WORM-related violations. In settlement, each firm consented to a censure and a fine in the following amounts.

- HSBC Securities (USA) Inc. – $1,500,000;
- State Street Global Markets, LLC – $1,500,000;

- MML Investors Services, LLC, MML Distributors, LLC, MML Strategic Distributors, LLC, and OppenheimerFunds Distributor, Inc. – $750,000, jointly;
- Acorns Securities, LLC – $175,000;
- Virtu Financial Capital Markets LLC – $175,000; and
- Allianz Life Financial Services and Questar Capital Corporation – $150,000, jointly.

FINRA noted in the settlements for Virtu Financial Capital Markets LLC and Acorn Securities, LLC, citing to the General Principals Applicable to all Sanction Determinations contained in the Sanction Guidelines, that it imposed a lower fine after considering, among other things, the firms' revenues and financial resources. HSBC Securities (USA) Inc., State Street Global Markets, LLC, MML Investors Services, LLC, MML Distributors, LLC, MML Strategic Distributors, LLC, OppenheimerFunds Distributor, Inc., and Acorns Securities, LLC also consented to undertakings to adopt and implement policies and procedures reasonably designed to achieve compliance with the federal securities laws and FINRA rules addressed in the AWC.

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