

# Compliance Wars: SEC and FINRA Disciplinary Actions Against Chief Compliance Officers and In-House Counsel in a Galaxy Not Too Far Away (July-December 2014)

By Brian L. Rubin and Irene A. Firippis

## Introduction

*A long time ago, in a galaxy far, far away... It is a period of civil war. Rebel spaceships, striking from a hidden base, have won their first victory against the evil Galactic Empire.<sup>1</sup>*



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In *Star Wars Episode IV: A New Hope* (the first movie from 1977) Princess Leia, a young dissident member of the Imperial Senate and sympathizer to the Rebellion, is intercepted during a covert mission and held hostage by the evil forces of Darth Vader and the Galactic Empire. The fate of Princess Leia and the Rebellion depends on brave Luke Skywalker, daredevil Han Solo and the robotic duo, R2-D2 and C-3PO. Unfortunately, Chief Compliance Officers (CCOs) and in-house counsel for broker-dealers (BDs) or investment advisers (IAs) cannot call on this team of heroes or the sage Jedi Master Obi-Wan Kenobi when serving their roles. CCOs and in-house counsel are tasked with the challenge of advising their colleagues and helping to ensure that their firms comply with securities laws and regulations, without having the authority (or light sabers) to enforce their decisions or advice. The U.S. Securities and Exchange Commission (SEC) and the Financial Industry Regulatory Authority (FINRA) might not watch over the galaxy, but both agencies carefully monitor and scrutinize the conduct of CCOs and in-house counsel. While these advisors to BDs and IAs do not face the danger of being held hostage during a galactic civil war, they are nonetheless targets of SEC and FINRA disciplinary proceedings.

From July through December 2014, the SEC and FINRA brought more than a dozen cases against CCOs (either acting as a compliance officer or acting in another capacity) and one case against an in-house counsel. This article, like its predecessors,<sup>2</sup> analyzes many recent SEC and FINRA actions against CCOs and in-house counsel to gain insight

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on conduct that is likely to attract the attention of—and possibly (light) saber rattling by—the regulators.

## Supervisory Systems and Written Supervisory Procedures

*Darth Vader (uber bad guy in Episode IV): “What have you done with those plans?!”<sup>3</sup>*

While the Rebel Alliance and the evil Galactic Empire were not constrained by specific rules when engaging in high-speed, intergalactic battles, such is not the case for BDs and IAs. Unfortunately, BDs and IAs are subject to FINRA and SEC regulations, not the Jedi Code. Specifically, FINRA requires BDs to establish and maintain supervisory systems “reasonably designed to achieve compliance” with applicable laws, regulations and rules, including written supervisory procedures (WSPs) designed to supervise the business activity of firms.<sup>4</sup> FINRA also requires that the supervisory system “is tailored specifically to the member’s business.”<sup>5</sup> Similarly, IAs must adopt and implement written policies and procedures reasonably designed to prevent violations of applicable laws, regulations and rules.<sup>6</sup> Occasionally, CCOs are responsible for these WSPs and supervisory systems and therefore may be subject to disciplinary actions when the systems or procedures are inadequate.

In December 2014, through a default decision, FINRA disciplined a CCO for not only failing to establish and

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maintain an adequate supervisory system and WSPs, but also for failing to specifically tailor the supervisory system to the member firm’s business.<sup>7</sup> The CCO was solely responsible for establishing and maintaining supervisory systems for the firm, which provided direct access to the U.S. market for an affiliate company. The affiliate company, based abroad, engaged in algorithmic, high-frequency trading through the firm, totaling approximately three billion shares per month through

1,700 to 1,800 traders based in 100 or more locations outside the United States. Between February 2010 and June 2011, FINRA identified more than 6,300 instances of suspicious trading activity involving potential layering, manipulative wash sales, and pre-arranged trading. FINRA sent the firm, in care of the CCO, 11 inquiries requesting documents and information about the 6,300 instances. FINRA found that their notices should have served as red flags and alerted the CCO to the suspicious activity. Despite this notice, the CCO ignored the red flags and did not take action or identify the manipulative trade activity.

The firm relied principally on third-party clearing firms to identify and notify it of manipulative trading. Despite having this system in place, the CCO failed to review the exception reports generated by the clearing firms, implement a system to review the reports, implement a system to review the parameters that each clearing firm used to create the reports, and contribute to the parameters that each clearing firm used to create the exception reports. Additionally, the system was inadequate because it did not monitor or control the issuance of and termination of trader identifications. As a result, the CCO failed to recognize when terminated traders circumvented discipline by creating different trader identifications. FINRA found that even though the firm’s supervisory system included a review for potentially manipulative trading, the system was inadequate. Particularly, “in light of the high volume of trading,” the system was unreasonable because the surveillance was manual and performed for “profit and loss purposes.”

FINRA also found that the CCO failed to establish, maintain, and enforce WSPs that were reasonably designed to supervise the member firm’s trading activity. The WSPs did not have adequate provisions for reviewing and identifying potentially manipulative trading activity. Moreover, the WSPs did not explain how to review for and identify potentially manipulative trading activity and what actions to take if such activity was identified. Despite relying on third-party clearing firms for monitoring the trading activity, the WSPs did not specify that the firm depended on the third-party clearing firms and did not indicate the type of reports relied upon by the firm. Accordingly, FINRA found that the CCO violated NASD Rule 3010(b). The CCO was fined \$30,000 and suspended for two years in all principal capacities.

In December 2014, through a settled Letter of Acceptance, Waiver and Consent (AWC), FINRA disciplined a CCO for his firm's failure to have and enforce an adequate supervisory system and WSPs.<sup>8</sup> The CCO was responsible for the firm's supervisory system, and for drafting and enforcing the WSPs, but relied upon a proprietary data

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system for the supervision of its registered representatives and their securities activities. FINRA found that the data system was insufficient because the trading information that it captured was not "consistently accurate or complete." Despite being aware of the data system's inadequacies, the firm nonetheless relied on the data system. FINRA found that the firm, acting through its CCO, also failed to: (1) supervise a registered representative's public appearance on daily television and radio shows; (2) complete "look backs" for six of its seven registered representatives who previously had been approved for outside business activities (OBAs) before a deadline imposed by Notice to Members 10-49; and (3) accurately and adequately disclose required details of OBAs.

FINRA further found that the firm, acting through its CCO, failed to follow the firm's WSPs by allowing at least one of its producing managers to sign off as the registered representative on his own transaction and to provide the principal approval of the transaction in the data system. Additional allegations included other violations of the firm's WSPs, including the CCO's not following procedures related to reviewing and approving correspondence and approving changes in customer's addresses. Further, the WSPs failed to specify the details of what the CCO's correspondence reviews would entail. The WSPs also lacked detail and guidance on certain procedures such as reviewing and approving producing managers' correspondence and daily review and approval of the daily reports of the approved private securities transactions. Accordingly, FINRA found that the CCO violated numerous NASD, FINRA and MSRB rules. FINRA fined the CCO \$25,000 (joint and several with his firm) and suspended him from associating

with any FINRA registered firm in a principal capacity for three months.

Additionally, in September 2014 the SEC brought a settled administrative action against a CCO and his investment advisory firm for failing to implement written compliance policies and procedures.<sup>9</sup> The CCO, who was also the firm's CEO and 50% owner of the firm and its affiliated BD, was authorized and primarily responsible for developing and implementing the firm's compliance procedures. The firm's policies and procedures manual also required that the CCO conduct an annual review to determine whether the policies

were adequate and effective in detecting and preventing violations of federal securities laws.

During the CCO's tenure, the firm engaged in activity that not only violated federal securities laws but also was directly prohibited in the firm's policies and procedures manual. Specifically, the manual prohibited principal transactions, including those executed through an affiliated BD. Nevertheless, the firm used an affiliated BD, which was under common control of the firm, to execute a majority of transactions for its clients in fixed-income investments. The CCO was an associated person of the affiliated BD, and the firm and the affiliated BD shared a common office. For each of these fixed-income transactions, the affiliated BD purchased bonds from other BDs, marked up the price of the bonds, and then transferred the bonds to another account. The affiliated BD received revenue on the transactions between the different price the affiliated BD paid for the bonds and the higher price the firm sold them to its clients. Not surprisingly, the firm did not disclose to its clients that, through its affiliated BD, it had been acting as a principal in fixed-income trades.

Additionally, the firm did not follow its procedure regarding advertising, which prohibited disseminating advertisements that may be fraudulent, misleading, deceptive, or manipulative. The CCO was responsible for implementing and monitoring this policy. According to the firm's manual, all advertising had to be reviewed, approved, documented, and initialed. Despite this policy, the firm disseminated a company profile that contained performance data that was misleading. For example, the performance results were calculated from multiple sources, but the majority of these sources did not include the firm's

actual performance. Also, some of the model equity investment advertisements did not disclose that results were gross of fees and did not reflect the impact of the firm's advisory fees. This omission caused the advertisement to materially overstate the performance of the firm's model equity portfolio. Given this conduct, the SEC found that the CCO caused the firm's violations of Rule 206(4)-7 of the Advisers Act and Section 206(4) of the Advisers Act (which require written policies and procedures) and Section 207 of the Advisers Act (which prohibits making untrue statements in applications or reports filed with the Commission). The SEC required that the firm disgorge \$368,459. The CCO was ordered to pay a penalty of \$50,000 and was not suspended.

*Takeaways:* CCOs may be sanctioned for their firms' failure to have and maintain procedures relating to, and appropriately tailored to, the business in which their firms are engaged.

## Supervision of Individuals

*Governor Tarkin (evil buddy of Darth Vader): "The regional governors now have direct control over their territories. Fear will keep the local systems in line. Fear of this battle station."<sup>10</sup>*

Death Star commanders relied on fear to keep supporters of the Rebellion in check, but in the securities world, this is generally not an effective tool to supervise individuals. (Although, if supervisors had light sabers, that would be another story.) Even though CCOs (usually) don't invoke fear and don't have light sabers (as far as we know), CCOs may be considered supervisors and face potential liability if they have been delegated specific supervisory responsibility over another person, or have adequate "responsibility, ability, or authority to affect the conduct of the employee whose behavior is at issue."<sup>11</sup> The Securities Exchange Act of 1934 similarly provides a safe harbor from supervisory liability where there are "established procedures and a system for applying such procedures, which would reasonably be expected to prevent and detect" violations.<sup>12</sup> Compliance officers generally do not supervise outside of their direct-line employees. Typical indicia of supervisory authority include hiring, firing (but usually not for supporting the Rebel Alliance), failing to

promote, reassigning with significantly different responsibilities, and making a decision causing a significant change in benefits. *Cf.* Division of Trading and Markets, "Frequently Asked Questions about Liability of Compliance and Legal Personnel at Broker-Dealers under Sections 15(b)(4) and 15(b)(6) of the Exchange Act" (Sept. 30, 2013) at n. 8, available at <http://www.sec.gov/divisions/marketreg/faq-cco-supervision-093013.htm>.

For example, in September 2014, through a settlement, the SEC disciplined a CCO for failing to supervise a registered representative (RR) of the firm who engaged in fraudulent conduct.<sup>13</sup> In the settlement order, the SEC noted that the CCO, who was also the founder and owner of the firm, had supervisory responsibility for the RR. From 2006 to 2011, the RR issued inflated account statements to investors that significantly overstated the value of their investment accounts and concealed the fact that account values were in decline. When the investors discovered the misrepresentations, the RR concealed the fraud by agreeing to pay investors the inflated returns. When the RR could no longer afford to make those payments, he misappropriated funds from unsophisticated and elderly firm clients so that he could cover the payments. On one occasion, the RR caused an elderly customer to redeem mutual funds totaling \$335,000 and deposited the funds into an account that the RR controlled.

Based upon the RR's conduct, the SEC found that the CCO not only failed to develop and implement reasonable supervisory policies and procedures, but also that the CCO failed to reasonably supervise the RR from violating securities laws. The CCO was solely responsible for supervising the RR and failed to follow the firm's procedures that required the CCO to review all incoming and outgoing correspondence, including account statements and cover letters. The SEC found that if the CCO had followed the firm's procedures and properly supervised the RR, the CCO could have prevented the RR's fraudulent conduct and misrepresentations made to the clients. The SEC found that the firm and the CCO failed reasonably to supervise the RR with a view to preventing and detecting his violation of the securities laws. The CCO was ultimately fined \$40,000 and permanently barred from all supervisory capacity.

*Takeaways:* CCOs should generally not supervise registered representatives. If they do (or if they supervise anyone), they should follow their firms' procedures.

## Proper Registration

*Luke Skywalker (hero with stellar light saber skills): "There's nothing for me here now. I want to learn the ways of the Force and become a Jedi like my father."<sup>14</sup>*

When Luke Skywalker wanted to become a Jedi, he faced the challenge of undergoing the rigors of Jedi training.<sup>15</sup> Similarly, when individuals seek to perform certain securities functions, they must become registered with FINRA. CCOs are sometimes responsible for ensuring proper registration of persons at their firm; the failure to do so could result in liability.

For example, in a November 2014 AWC, FINRA disciplined a firm and its CCO (who was also the firm's president) for failing to ensure that all of the firm's registered employees had the proper securities licenses.<sup>16</sup> From November 2012 to January 2013, the CCO allowed an employee to act as the firm's Financial and Operations Principal (FINOP), even though the employee had been suspended in her capacity as FINOP and was ordered to requalify by examination prior to resuming work as a FINOP. The employee carried out duties as a FINOP throughout her suspension and without ever requalifying through examination. For example, the "suspended and disqualified" individual reconciled bank accounts, calculated the firm's net capital, and prepared financial documents for the firm, including the firm's balance sheet, general ledger, and profit and loss statement. Moreover, the suspended individual prepared and submitted monthly and quarterly FINRA filings. FINRA found that the CCO, who was responsible for making sure that each of the firm's associated persons had the requisite securities licenses, violated NASD Membership and Registration Rule 1021, which requires principals to be registered. The CCO was suspended from association with any FINRA member firm in a principal capacity for one month and fined \$10,000.

In another November 2014 AWC, FINRA disciplined a firm and its CCO for failing to ensure that all of the firm's registered employees had the proper securities licenses and also because the CCO represented to FINRA that a suspended and disqualified individual would not carry out any of her prohibited FINOP-related responsibilities prior to requalifying through an examination.<sup>17</sup> Despite this prohibition, the CCO provided the individual with the firm's bank statements and invoices for the individual to review when calculating

the firm's net capital, preparing financial documents, including the firm's balance sheet and profit and loss statement. Moreover, the disqualified individual provided the CCO with information that the firm needed to file with FINRA each month to comply with requirements of the firm's heightened surveillance (the cause of which is not elaborated upon in the AWC). FINRA found that the CCO violated NASD Rule 1021, fined him \$15,000 and suspended him from association with a FINRA member firm in a principal capacity for three months.

*Takeaways:* To avoid potential liability, if the CCO has responsibility for ensuring that all persons associated with their respective firm have their requisite securities licenses, then the CCO should carry out those responsibilities.

## False and Misleading Statements in a Form ADV

*Ben Obi-Wan Kenobi (wise Jedi Master): "These aren't the droids you're looking for."<sup>18</sup>*

Unlike Obi-Wan Kenobi, CCOs are not equipped to (and should not attempt to) "mislead" authority figures, especially regulators, by performing Jedi mind tricks. IAs are, however, required to file Forms ADV, which contain important information and disclosures about the nature of the IA's business. If a CCO is responsible for filing the Form ADV and if it contains inaccurate information, the CCO may incur liability. And the CCO won't be able to say, "These aren't the ADVs you're looking for."

For example, in a July 2014 SEC settlement, a CCO was disciplined for providing false and misleading disclosures in his firm's Forms ADV.<sup>19</sup> The CCO was responsible for drafting and filing the Forms, and for signing the Form, certifying that the provided information was true and correct. One section of the Form ADV requires that an adviser identify every person that "controls" the adviser. Form ADV defines "control" to mean "the power, directly or indirectly, to direct the management or policies of a person." The CCO failed to appropriately identify on the Form ADV the proper individuals who controlled the firm's management and policies. The SEC found that these disclosures, as well as other ones, were false and misleading. The SEC found that the CCO violated Section 207 of the Advisers Act, which makes it unlawful

for any person to make untrue statements of material facts in applications or reports filed under the Advisers Act. The CCO was ordered to pay a penalty of \$35,000 but was not suspended.

In a November 2014 SEC settlement, a CCO was disciplined for making false and misleading disclosures in his firm's Form ADV.<sup>20</sup> The CCO, who was also the IA's executive managing director, was primarily responsible for drafting and signing the firm's periodic filings with the SEC, including the firm's Forms ADV. In 2008, the firm and a third-party broker agreed to a referral-fee, commission-sharing agreement. The agreement, which was partially drafted by the CCO, explicitly required disclosing the fee arrangement to clients who were referred to the third-party broker because the firm would financially benefit from the recommendation. In practice, when the firm referred clients to the broker, it did not disclose that it would benefit financially. Clients were not notified of this conflict of interest or that the broker agreed to provide execution for significantly less than the clients were charged, with the difference going to the firm.

Despite his knowledge of the arrangement, the CCO failed to disclose actual and potential conflicts of interest resulting from the firm's commission-sharing agreement on the firm's Form ADV Part II. In 2009, after the fee arrangement was created, the CCO updated the firm's Form ADV Part II, but did not disclose the arrangement and "what information that was included was materially misleading." The disclosures failed to completely and accurately convey the nature and existence of the conflict of interest created by the commission-sharing arrangement. The settlement also notes that the CCO failed to keep adequate records of the firm's Forms ADV. In 2010, the CCO again updated the Form ADV Part II, providing more information, but overall the form remained "inadequate." Even with the expanded information, the clients still could not "fully appreciate" the fact that by executing trades through the third-party broker, they would be within the "scope" of a commission-sharing arrangement. As a result of his conduct, the CCO was found to have willfully violated Section 207 of the Advisers Act as well as Section 204(a) and Rule 204-2(a) (14), which requires the maintenance of certain books and records. The CCO was suspended from association for 12 months, in addition to other, more specific suspension. The CCO was ordered to pay a penalty of \$150,000.

*Takeaway:* CCOs may be sanctioned if the firm's Form ADV is false.

## Anti-Money Laundering Procedures

*Han Solo (venturesome pilot, friend to Luke Skywalker):  
"Tell Jabba I've got his money."<sup>21</sup>*

Although we can't be sure, our guess is that Jabba the Hutt did not report to the authorities the cash he received from Han Solo, possibly in violation of the GE AML rules (Galactic Empire Anti-Money Laundering Rules, that is). Back here in the United States, under FINRA Rule 3310, BDs are required to implement anti-money laundering (AML) procedures designed to achieve compliance with the Bank Secrecy Act, 31 U.S.C. § 5311 *et seq.* Moreover, federal law mandates that AML procedures be appropriately tailored to the firm's business.<sup>22</sup> AML procedures should reflect the firm's business model and customer base.<sup>23</sup> Additionally, Rule 17a-8 of the Exchange Act requires BDs to comply with reporting obligations under the Bank Secrecy Act. In general, BDs are required to have specific procedures and systems to enable them to detect and respond to suspicious movements of money.

In an October 2014 AWC, FINRA disciplined a CCO, who was also the Anti-Money Laundering Compliance Officer (AMLCO), for failing, among other things, to establish, maintain and enforce the firm's AML compliance program.<sup>24</sup> The AMLCO was also the firm's FINOP, Chief Compliance Officer, and Registered Option and Security Futures Principal. The AMLCO failed to discharge his responsibilities for ensuring that the firm's AML procedures were adequately tailored to the firm's business. In addition, there was trading activity that should have triggered additional due diligence under the existing procedures that the AMLCO failed to properly address. For example, the firm maintained an account for a foreign institutional customer, which was controlled by multiple corporate nominees domiciled outside of the United States. The account began to deposit and liquidate thousands of shares of low-priced securities. The majority of the sale proceeds, \$439,000 in total, were wired to a bank account in Gibraltar, a "known tax haven," without any reinvestment at the firm. FINRA found that the activity should have triggered a review by the AMLCO under the firm's existing WSPs, but no such review occurred. FINRA also found that the AMLCO was put on further notice because the firm's clearing firm raised concerns about the legitimacy of the is-

suers whose securities were being deposited and liquidated through the account, yet no investigation occurred. FINRA found that had additional due diligence been conducted by the AMLCO, he would have discovered additional red flags indicating potentially suspicious activity.

FINRA found that, among other violations, the AMLCO violated NASD Conduct Rule 3011(a) and FINRA Rules 3310(a) and 2010. Under NASD Conduct Rule 3011 and FINRA Rule 3310 (which superseded Rule 3011 as of January 1, 2010), FINRA member firms are required to develop and implement a written AML program reasonably designed to achieve and monitor compliance with the requirements of the Bank Secrecy Act. Under NASD Conduct Rule 3011(a) and FINRA Rule 3310(a) (which superseded it), FINRA member firms are required to establish and implement policies and procedures that can reasonably be expected to detect and cause the reporting of suspicious activity and transactions. The AMLCO was suspended for four months and fined \$11,500.

In December 2014, through a default decision, FINRA disciplined a CCO who was also the firm's AMLCO for failing to implement reasonable AML policies and procedures that were adequately tailored to the firm's business.<sup>25</sup> Despite the firm engaging in high-frequency trading, the AMLCO relied on clearing houses to alert him of any suspicious activity. According to FINRA, the AML procedures did not properly consider the firm's reliance on automated exception reports. Although the AML procedures stated that the firm would monitor for suspicious activity, the AML procedures did not list or describe any exception reports that the firm was supposed to monitor for suspicious activity. The firm relied solely on the clearing house and did not have any reports, automated or otherwise, to flag suspicious activity. The AMLCO never created any monitoring parameters and did not contribute to monitoring parameters created by the clearing firms for their trade surveillance program. As a result, FINRA found that the AMLCO violated FINRA Rule 3310. By failing to establish procedures designed to reasonably detect and report suspicious transactions, as described under 31 U.S.C. § 5318(g), the AMLCO was fined \$20,000 for failing to implement AML procedures and was suspended in all principal capacities for two years.

**Takeaway:** AMLCOs may be found liable if AML policies and procedures are not tailored to ensure that the proper systems are in place to detect and report suspicious trading activity and if red flags are ignored.

## Causing and Aiding and Abetting

*Princess Leia (member of the Imperial Senate, known for her trendsetting hairstyles): "Help me Obi-Wan Kenobi, you're my only hope."*<sup>26</sup>

While helping Princess Leia was a just and noble cause, helping someone (including a Princess) to violate securities law, through causing and aiding and abetting a violation, is not. Liability from aiding and abetting requires an underlying violation, substantial assistance in connection with the primary violation, and scienter, which is satisfied by recklessness (but not the sort commonly associated with poor light saber skills).<sup>27</sup> Similarly, "causing" violations involves a primary violation and an act or omission by the person or entity that causes the violation. Causing liability, however, requires only negligence in some cases.<sup>28</sup>

In July 2014, the U.S. District Court for the Southern District of Florida entered a judgment by consent against an investment adviser's CCO (who was also the IA's general counsel and chief operating officer), providing permanent injunctive relief under Section 10(b) of the Exchange Act and Sections 206(1), 206(2) and 206(4) of the Advisers Act (all antifraud provisions).<sup>29</sup> In that case, the CCO/in-house counsel allegedly aided and abetted fraud committed by his firm and the firm's founder/president. Specifically, the SEC alleged that the firm and the president/founder, "[u]nder a purported swap transaction with a consulting and investment firm," depleted nearly all of the assets of two hedge funds managed by the IA and allowed investors in the hedge funds to receive account statements falsely reflecting that their investments were doing well. The CCO/in-house counsel allegedly "assisted" with the fraudulent activities because the transactions were done with his "knowledge and consent," and he knew the transactions were contrary to the investment strategy laid out in the "Explanatory Memorandum" of one of the funds and contrary to the firm's "Management Agreement." In light of the district court's judgment, in an August 2014 settlement, the SEC barred the CCO/in-house counsel from associating with a registered entity for one year.<sup>30</sup>

**Takeaways:** CCOs (and in-house counsel) may be sanctioned not only for their own violations but also for contributing to another's violation.

## Conclusion

*Darth Vader: "The circle is now complete. When I left you, I was but the learner; now I am the master."*<sup>31</sup>

It takes years to master light saber skills or the ability to use The Force. For some CCOs and in-house counsel, mastery

of securities laws and regulations may also take time. In the meantime, CCOs and in-house counsel should study applicable securities laws and regulations. It may also be helpful to review cases concerning other CCOs and in-house counsel who have faced disciplinary actions. Careful study of these cases may help CCOs and in-house counsel avoid the wrath of the SEC or FINRA, just as training and mastery helped save Princess Leia from the evil Galactic Empire.

### ENDNOTES

- <sup>1</sup> *Star Wars Episode IV: A New Hope* (Lucasfilm 1977) (*Star Wars Episode IV*), available at <http://www.imsdb.com/scripts/Star-Wars-A-New-Hope.html>. (note the use of cool font to emphasize phrases flying through the galaxy).
- <sup>2</sup> See, e.g., Brian L. Rubin & Katherine L. Kelly, *Catching Fire During Regulatory Hunger Games: SEC and FINRA Disciplinary Actions Against Chief Compliance Officers and In-House Counsel (January-June 2014)*, Practical Compliance and Risk Management, November-December 2014 at 13 n.1 (citing prior articles published in the same journal).
- <sup>3</sup> Darth Vader, *Star Wars Episode IV*.
- <sup>4</sup> FINRA Rule 3110 (effective Dec. 1, 2014). Prior to Rule 3110's effective date, NASD Rule 3010 set forth substantially similar requirements for supervisory systems and written procedures.
- <sup>5</sup> *Richard F. Kresge*, SEC Admin. Proc. No. 3-12402, 2007 LEXIS 1407, at \*2 n.24 (June 29, 2007).
- <sup>6</sup> Rule 206(4)-7 promulgated under Section 206(4) of the Investment Adviser's Act of 1940 (Adviser's Act).
- <sup>7</sup> *Department of Enforcement v. Marcus Rodriguez*, Default Decision Proceeding No. 2012033239202 (Dec. 29, 2014), available at <http://disciplinaryactions.finra.org/viewdocument.aspx?DocNB=38366>.
- <sup>8</sup> *Foothill Securities, Inc., & Stephen Guy Shipp*, FINRA AWC No. 20120306704-01 (Dec. 24, 2014), available at <http://disciplinaryactions.finra.org/viewdocument.aspx?DocNB=38370>.
- <sup>9</sup> *Strategic Capital Group, LLC and N. Gary Price*, SEC Admin. Proc. No. 3-16138 (Sept. 18, 2014).
- <sup>10</sup> *Star Wars Episode IV*.
- <sup>11</sup> *George J. Kolar*, SEC Admin. Proc. File No. 3-9570, 55 S.E.C. 1009, 2002 LEXIS 1647, \*13 (June 26, 2002).
- <sup>12</sup> Section 15(b)(4)(E) of the Exchange Act.
- <sup>13</sup> *Rothman Securities Inc. and Theodore Rothman*, SEC Admin. Proc. No. 3-16180 (Sept. 29, 2014).
- <sup>14</sup> *Star Wars Episode IV*.
- <sup>15</sup> As many of you know, Luke did not become a Jedi until *Star Wars Episode V: The Empire Strikes Back* (Lucasfilm 1979). Rumor has it that he will become a Series 24 in a future episode.
- <sup>16</sup> *Larador Becker Securities Corporation & Cindy Hannerhoff*, FINRA AWC No. 2013036030001 (Nov. 19, 2014), available at <http://disciplinaryactions.finra.org/viewdocument.aspx?DocNB=38031>.
- <sup>17</sup> *Michael Allen Stakes*, FINRA AWC No. 2013036030401 (Nov. 5, 2014), available at <http://disciplinaryactions.finra.org/viewdocument.aspx?DocNB=38030>.
- <sup>18</sup> *Star Wars Episode IV*.
- <sup>19</sup> *SignalPoint Asset Management, LLC, John W. Handy, Jonathan Timson, Dennis R. Walker, Michael Orzel*, SEC Admin. Proc. No. 3-15955 (July 2, 2014).
- <sup>20</sup> *Alan Gavornik, Nicholas Mariniello and Lee Argush*, SEC Admin. Proc. No. 3-16286 (Nov. 24, 2014).
- <sup>21</sup> *Star Wars Episode IV*.
- <sup>22</sup> *Dep't of Enforcement v. Domestic Sec., Inc.* Complaint No. 2005001819101, 2008 FINRA Discp. LEXIS 44, at \*23 (FINRA NAC Oct. 2, 2008).
- <sup>23</sup> NASD Notice to Members 02-21, 2002 NASD LEXIS 24, at \*17 (Apr. 2002).
- <sup>24</sup> *Dennis Young*, FINRA AWC No. 2011025544301 (Oct. 30, 2014), available at <http://disciplinaryactions.finra.org/viewdocument.aspx?DocNB=37856>.
- <sup>25</sup> *Department of Enforcement v. Marcus Rodriguez*, Default Decision Proceeding No. 2012033239202 (Dec. 29, 2014).
- <sup>26</sup> *Star Wars Episode IV*.
- <sup>27</sup> Section 15 of the Securities Act of 1933, Section 20(e) of the Exchange Act and Section 209(f) of the Advisers Act provide for aiding and abetting liability for reckless, as well as knowing, conduct. See *MidSouth Capital, Inc. and Mark D. Hill*, Admin. Proc. No. 3-14851, 2012 SEC LEXIS 1254 (April 18, 2012) (finding aiding and abetting liability premised on recklessness).
- <sup>28</sup> *Mark T. Schwetschenau*, Admin. Proc. File. No. 3-13995, 2010 SEC LEXIS 2534 \*9 (Aug. 5, 2010) ("Negligence is sufficient to establish liability for causing a primary violation that does not require scienter").
- <sup>29</sup> *SEC v. Weston Capital Asset Management, LLC*, No. 14-cv-80823 (S.D. Fla. July 7, 2014).
- <sup>30</sup> *Keith Wellner*, SEC Admin. Proc. No. 3-15998 (Aug. 1, 2014).
- <sup>31</sup> *Star Wars Episode IV*.

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