Initial Decision Release No. 1360
Administrative Proceeding
File No. 3-18454

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

In the Matter of

Christopher M. Lee, a/k/a Rashid K. Khalfani

Initial Decision
March 4, 2019

Appearance: Amy Jane Longo, Douglas M. Miller, and Junling Ma for the Division of Enforcement, Securities and Exchange Commission

Rashid K. Khalfani, *pro se*

Before: James E. Grimes, Administrative Law Judge

Summary

I grant the Division of Enforcement's motion for summary disposition. Respondent Christopher M. Lee, also known as Rashid K. Khalfani,[1] is barred from associating with an investment adviser, broker, dealer, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization.

Procedural Background

The Securities and Exchange Commission initiated this proceeding in April 2018, when it issued an order instituting proceedings (OIP) under

[1] Respondent used the name Rashid K. Khalfani in his filings in this proceeding, and I will refer to him by that name in this initial decision except when citing judicial proceedings and other documents that refer to Respondent as Christopher M. Lee.

Section 203(f) of the Investment Advisers Act of 1940.[2] This is a follow-on proceeding based on a permanent injunction entered by the United States District Court for the Central District of California in March 2018.[3] The injunction was based on Khalfani's misrepresentations to investors, misappropriation of investor funds, sale of unregistered securities, signing and filing false Forms ADV for Capital Cove Bancorp LLC, and aiding and abetting Capital Cove's improper registration with the Commission as an investment adviser.

A different administrative law judge originally presided over this proceeding, but the matter was reassigned to me following the Supreme Court's decision in *Lucia v. SEC*.[4] Khalfani was directed to propose how further proceedings should be conducted,[5] but he never submitted a proposal. Only the Division of Enforcement participated in the telephonic prehearing conference that I held on October 17, 2018.[6] The Division then filed a motion for summary disposition, supported by eight exhibits.[7] In response, on December 27, 2018, Khalfani updated the brief he filed in response to the prior administrative law judge's order to show cause.[8] Khalfani seeks a hearing, but has not offered evidence sufficient to create a genuine issue as to

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2 OIP at 1; *see* 15 U.S.C. § 80b-3(f).

3 *See SEC v. Capital Cove Bancorp LLC*, No. 8:15-cv-980 (C.D. Cal.).

4 138 S. Ct. 2044 (2018); *see Pending Admin. Proc.*, Securities Act of 1933 Release No. 10536, 2018 SEC LEXIS 2058, at *2–3 (Aug. 22, 2018); *Pending Admin. Proc.*, Admin. Proc. Rulings Release No. 5955, 2018 SEC LEXIS 2264, at *2–3 (ALJ Sept. 12, 2018).

5 *Christopher M. Lee*, Admin. Proc. Rulings Release No. 6003, 2018 SEC LEXIS 2383, at *1 (ALJ Sept. 18, 2018).

6 *Christopher M. Lee*, Admin. Proc. Rulings Release No. 6211, 2018 SEC LEXIS 2880 (ALJ Oct. 18, 2018).

7 The exhibits are cited as "Div. Ex. _" using the documents' internal pagination.

8 This response is cited as "Opp'n." Khalfani raises objections to service of documents in this proceeding. Opp'n at 3–4, 7. I have already found that he was properly served with the OIP. *Christopher M. Lee*, Admin. Proc. Rulings Release No. 6160, 2018 SEC LEXIS 2782, at *1 (ALJ Oct. 10, 2018). Based on Division counsel's declaration on January 9, 2019, I am satisfied that Khalfani has been served with the Division's motion, supporting papers, and reply.

any material fact. In conducting this proceeding and considering the Division's motion, I gave no weight to the opinions, orders, or rulings issued by the prior administrative law judge.[9]

Findings of Fact

The findings and conclusions in this initial decision are based on the record and on facts officially noticed.[10] In making the findings below, I have applied preponderance of the evidence as the standard of proof.[11]

In 2004, Khalfani, under the name Christopher M. Lee, pleaded guilty to six counts of felony grand theft and was ordered to pay more than $1 million in restitution and serve two years in prison.[12] Nine years later—in the midst of the conduct underlying this proceeding—Khalfani, again as Lee, pleaded guilty to misdemeanor forgery, receiving a sentence including jail time, probation, and a fine.[13]

Khalfani incorporated Capital Cove in September 2010.[14] He owned all of the company and was its sole managing member.[15] Capital Cove filed a Form ADV on November 26, 2010, registering it with the Commission as an investment adviser.[16] Khalfani was only able to register Capital Cove under Advisers Act Section 203A because he misstated the amount of assets it had

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9 *See Pending Admin. Proc.*, 2018 SEC LEXIS 2058, at *4.

10 17 C.F.R. § 201.323.

11 *See John Francis D'Acquisto*, Advisers Act Release No. 1696, 1998 WL 34300389, at *2 (Jan. 21, 1998).

12 Div. Ex. 3 at 3. Division Exhibit 3 is an order granting summary judgment against Khalfani in the Commission's civil case against him and Capital Cove. *Capital Cove*, No. 8:15-cv-980, ECF No. 407 (Aug. 31, 2016). The district court's findings on summary judgment are entitled to preclusive effective in this proceeding. *Shreyans Desai*, Advisers Act Release No. 4656, 2017 WL 782152, at *3 (Mar. 1, 2017).

13 Div. Ex. 3 at 3.

14 *Id.* at 2.

15 *Id.*

16 *Id.*

under management by tens of millions of dollars.[17] Capital Cove continued to file Forms ADV annually through 2013.[18] Notably, the forms did not mention Khalfani's alias or his criminal convictions under that alias. In addition, two of the forms contained the signature of Capital Cove's outside counsel, but that counsel stated that she neither signed the forms nor knew her signature was being used.[19]

In 2012, Khalfani founded two funds: the Rittenhouse Square Trust LLC and the Capital Cove REO Opportunities Fund II LLC.[20] Khalfani was listed as key management in the private placement memorandum for the Rittenhouse fund and as managing director and CEO of the REO fund.[21] Capital Cove was a co-manager of the REO fund.[22] Both private placement memoranda stated that money invested would be used to acquire real properties.[23] Capital Cove advertised the REO fund on its website and through a marketing flyer Khalfani handed out to investors.[24] Those materials described the REO fund as having been "vetted, qualified and registered," and described Capital Cove as an "SEC-registered Fund Manager" and "FINRA member."[25] Khalfani also orally represented to potential investors that their money would be used to buy real estate.[26] In 2014, Capital Cove filed a Form D with the Commission, signed by Khalfani, which described the REO fund as an unregistered offering.[27]

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17 *Id.* at 13–14.

18 *Id.* at 2; *see* Capital Cove Bancorp LLC (CRD# 155705), Investment Adviser Public Disclosure, SEC, https://adviserinfo.sec.gov/Firm/155705.

19 Div. Ex. 3 at 3.

20 *Id.*

21 *Id.*

22 *Id.*

23 *Id.*

24 *Id.* at 3–4.

25 *Id.* at 4.

26 *Id.*

27 *Id.* at 5.

From March 2012 to January 2014, at least seventeen investors purchased membership interests worth nearly $2 million in the funds.[28] Khalfani transferred investors' funds from their IRA accounts to accounts in the name of the funds.[29] He had sole control over the funds' and Capital Cove's bank and brokerage accounts—some of which were in the name of Christopher M. Lee—and was the accounts' sole authorized signatory.[30] On multiple occasions, Khalfani altered Capital Cove's books and records to show more cash on hand than it really had.[31] More than ninety percent of the investors' funds were (1) used to purchase real properties, but in the name of Capital Cove, not the Rittenhouse or REO funds; (2) deposited into Capital Cove's bank and brokerage accounts; (3) transferred to Khalfani's other accounts or entities; or (4) used for Capital Cove's business operations.[32] Most of the returns paid to investors came from new money coming in from investors and not the flipping of real properties that was the purported business of the funds.[33]

In December 2014, the Commission notified Khalfani of its preliminary determination to charge him with certain violations of the securities laws.[34] In response to a subpoena, Khalfani stated that the REO fund had not received any subscriptions and was not operative.[35] He repeated similar assertions during his investigative testimony.[36] Throughout the investigation, Khalfani denied being the subject of any past criminal investigation, prosecution, or proceeding.[37]

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28 *Id.* at 4.

29 *Id.*

30 *Id.* at 3–4.

31 *Id.* at 5.

32 *Id.* at 4.

33 *Id.* at 5.

34 *Id.*

35 *Id.*

36 *Id.*

37 *Id.* at 6.

Capital Cove filed for Chapter 11 bankruptcy in May 2015, but Khalfani continued to solicit investors, one of whom was an undercover FBI agent.[38] Khalfani told the agent that a $100,000 investment in the REO fund would yield a twelve percent return and that Capital Cove put one hundred percent of investor funds into real estate.[39] Khalfani continued speaking to investors even after the Commission obtained a temporary restraining order enjoining Capital Cove's operations.[40]

The Commission filed its complaint against Capital Cove and Khalfani on June 8, 2015, alleging multiple violations of the Securities Act of 1933, Securities Exchange Act of 1934, and Advisers Act.[41] The district court entered a final judgment against Khalfani and Capital Cove in March 2018, permanently enjoining both from violating Exchange Act Section 10(b) and Rule 10b-5, Securities Act Sections 5 and 17(a), and Advisers Act Section 207.[42] Khalfani was also enjoined from soliciting, accepting or depositing any monies from actual or prospective investors in connection with any offering of securities and from aiding and abetting violations of Section 203A of the Advisers Act.[43] The court ordered disgorgement and prejudgment interest of more than $2 million jointly and severally against Capital Cove and Khalfani.[44] The court also imposed a civil penalty of $1.8 million against Khalfani.[45]

After this administrative proceeding was initiated, Khalfani was indicted on six counts of wire fraud, in violation of 18 U.S.C. § 1343, for conduct overlapping with the conduct underlying this proceeding.[46]

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38 *Id.*

39 *Id.*

40 *Id.*

41 *Id.* at 6–7.

42 Div. Ex. 4 at 2–4.

43 *Id.* at 4.

44 *Id.* at 5.

45 *Id.* at 6.

46 Div. Ex. 8.

Conclusions of Law

Under Rule 250(b), an administrative law judge may grant a motion for summary disposition if "there is no genuine issue with regard to any material fact and . . . the movant is entitled to summary disposition as a matter of law."[47] The Commission has repeatedly upheld the use of summary disposition in cases such as this one, where the respondent has been enjoined or convicted and the sole determination concerns the appropriate sanction.[48]

Khalfani contests the allegations against him, but only by assertion—he has not provided evidence to rebut the fact of the district court's injunction against him or the facts contained in the district court's summary judgment order.[49] There is thus no genuine issue of material fact, and the record contains sufficient evidence to decide this matter in the Division's favor on the papers.[50]

The Advisers Act gives the Commission authority to impose a collateral bar[51] against Khalfani if, as is relevant here, (1) he was associated with or seeking to become associated with an investment adviser at the time of his misconduct; (2) he was enjoined "from engaging in or continuing any conduct

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47 17 C.F.R. § 201.250(b).

48 *Gary M. Kornman*, Exchange Act Release No. 59403, 2009 WL 367635, at *10 (Feb. 13, 2009), *pet. denied*, 592 F.3d 173 (D.C. Cir. 2010); *Jeffrey L. Gibson*, Exchange Act Release No. 57266, 2008 WL 294717, at *5 & n.21 (Feb. 4, 2008) (collecting cases), *pet. denied*, 561 F.3d 548 (6th Cir. 2009).

49 *See* Div. Exs. 3–4; *Kornman*, 2009 WL 367635, at *8; *James E. Franklin*, Exchange Act Release No. 56649, 2007 WL 2974200, at *4 & nn. 13–14 (Oct. 12, 2007).

50 *See James S. Tagliaferri*, Exchange Act Release No. 80047, 2017 WL 632134, at *7 (Feb. 15, 2017) ("The party opposing summary disposition may not rely on bare allegations or denials but instead must present specific facts showing a genuine issue of material fact for resolution at a hearing." (internal quotation marks omitted)).

51 A collateral bar, also referred to as an industry bar, is a bar that prevents an individual from participating in the securities industry in capacities in addition to those in which the person was participating at the time of his or her misconduct. *See Toby G. Scammell*, Advisers Act Release No. 3961, 2014 WL 5493265, at *1 & n.1 (Oct. 29, 2014).

or practice . . . in connection with the purchase or sale of any security"; and (3) imposing a bar is in the public interest.[52]

The record shows that the first element is satisfied. Khalfani denies that he has ever been an investment adviser, and argues that "according to the SEC's own documentation, no proper SEC registration was ever completed and no actual completed registration took place."[53] But the evidence shows that Capital Cove was registered with the Commission as an investment adviser—albeit improperly—for much of the time of Khalfani's misconduct and that he was associated with Capital Cove. Indeed, he created Capital Cove and was listed as its managing director, control person, and chief compliance officer. And it would be absurd to allow a respondent to disclaim the Advisers Act's applicability to an entity because he registered it as an investment adviser under false pretenses.

As to the second element, Section 203(e)(4) requires that the respondent have been enjoined from "engaging in or continuing any conduct or practice . . . in connection with the purchase or sale of any security."[54] Khalfani asserts that Capital Cove "did not engage in securities activities as any noticeable function of its core businesses," because it was "real estate related, and dealt with real property" as its business model.[55] However, the statute simply requires that the respondent have been enjoined from conduct or practices in connection with the purchase or sale of securities. The terms of the district court's injunction satisfy that requirement.[56]

Having found the first two elements satisfied, I must consider the public-interest factors discussed in *Steadman v. SEC*.[57] The public-interest factors include:

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[52] 15 U.S.C. § 80b-3(e)(4), (f).

[53] Opp'n at 2, 5–6.

[54] 15 U.S.C. § 80b-3(e)(4).

[55] Opp'n at 2, 5.

[56] *See, e.g.*, Div. Ex. 4 at 1–2 (ordering that "Khalfani [is] permanently restrained and enjoined from violating . . . Section 10(b) of the . . . Exchange Act . . . and Rule 10b-5 . . . in connection with the purchase or sale of any security" and "Section 17(a) of the Securities Act . . . in the offer or sale of any security").

[57] 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981); *see Scammell*, 2014 WL 5493265, at *5.

> the egregiousness of the respondent's actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of the respondent's assurances against future violations, the respondent's recognition of the wrongful nature of his conduct, and the likelihood that the respondent's occupation will present opportunities for future violations.[58]

The Commission also considers the deterrent effect of administrative sanctions.[59] This public interest inquiry is "flexible . . . and no one factor is dispositive."[60] Before imposing a bar, an administrative law judge must specifically determine why the Commission's interests in protecting the investing public would be served by imposing an industry bar.[61]

In considering the public interest, I am mindful that "in most" cases involving fraud, the public-interest analysis will weigh in favor of a "severe sanction."[62] And because "[t]he securities industry presents continual opportunities for dishonesty and abuse," it "depends heavily on the integrity

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[58] *David R. Wulf*, Exchange Act Release No. 77411, 2016 WL 1085661, at *4 (Mar. 21, 2016).

[59] *Peter Siris*, Exchange Act Release No. 71068, 2013 WL 6528874, at *11 n.72 (Dec. 12, 2013), *pet. denied*, 773 F.3d 89 (D.C. Cir. 2014). Although relevant, general deterrence is not, by itself, determinative in assessing whether the public interest weighs in favor of imposing a bar. *PAZ Sec., Inc. v. SEC*, 494 F.3d 1059, 1066 (D.C. Cir. 2007).

[60] *Gary M. Kornman*, Exchange Act Release No. 59403, 2009 WL 367635, at *6 (Feb. 13, 2009) (quoting *David Henry Disraeli*, Securities Act Release No. 8880, 2007 WL 4481515, at *15 (Dec. 21, 2007), *pet. denied*, 334 F. App'x 334 (D.C. Cir. 2009)), *pet. denied*, 592 F.3d 173 (D.C. Cir. 2010).

[61] *Mark Feathers*, Exchange Act Release No. 73634, 2014 WL 6449870, at *1 (Nov. 18, 2014); *see Ross Mandell*, Exchange Act Release No. 71668, 2014 WL 907416, at *2 (Mar. 7, 2014), *vacated in part on other grounds*, Exchange Act Release No. 77935, 2016 WL 3030883 (May 26, 2016).

[62] *Siris*, 2013 WL 6528874, at *11 n.71 (quoting *Jeffrey L. Gibson*, Exchange Act Release No. 57266, 2008 WL 294717, at *7 (Feb. 4, 2008), *pet. denied*, 561 F.3d 548 (6th Cir. 2009)).

of its participants and on investors' confidence."[63] Investment advisers, in particular, serve as fiduciaries who owe their clients "an affirmative duty of 'utmost good faith, and full and fair disclosure of all material facts,' as well as an affirmative obligation to employ reasonable care to avoid misleading clients."[64] Given the industry's dependence on the integrity of its participants, the duty investment advisers owe their clients, and the confidence and trust investors necessarily place in investment advisers, the Commission takes a dim view of investment advisers and associated persons who defraud their clients.[65]

The public interest and the Commission's interest in protecting the public weigh in favor of an industry bar. Khalfani's conduct was egregious. He misstated Capital Cove's assets under management so that he could unlawfully register it with the Commission as an investment adviser and promote Capital Cove as being an "SEC-registered Fund Manager" and "FINRA member" to attract investors. His scheme worked, as he misappropriated $1.8 million from at least seventeen investors. That the district court found that a civil penalty matching the $1.8 million that Khalfani was ordered to disgorge was appropriate further demonstrates the egregious nature of his conduct.

Khalfani's conduct was also recurrent, as he solicited investors over nearly two years. And while the record appears to show that the last investor was solicited in January 2014, he continued communicating with investors and attempted to solicit new ones more than a year later, even after Capital Cove filed for bankruptcy and the Commission filed its complaint against it and Khalfani.[66]

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[63] *Feathers*, 2014 WL 6449870, at *3 (alteration in original) (quoting *Tzemach David Netzer Korem*, Exchange Act Release No. 70044, 2013 WL 3864511, at *6 & n.53 (July 26, 2013)).

[64] *Conrad P. Seghers*, Advisers Act Release No. 2656, 2007 WL 2790633, at *7 (Sept. 26, 2007) (quoting *Capital Gains Research Bureau v. SEC*, 375 U.S. 180, 194 (1963)), *pet. denied*, 548 F.3d 129 (D.C. Cir. 2008).

[65] *See James C. Dawson*, Advisers Act Release No. 3057, 2010 WL 2886183, at *4 (July 23, 2010) ("[W]e have consistently viewed misconduct involving a breach of fiduciary duty or dishonest conduct on the part of a fiduciary . . . as egregious.").

[66] *See Gordon Brent Pierce*, Securities Act Release No. 9555, 2014 WL 896757, *23 (Mar. 7, 2014) (considering "numerous sales" over eight months "recurrent and long-lasting"), *pet. denied*, 786 F.3d 1027 (D.C. Cir. 2015).

Khalfani's conduct showed a high degree of scienter. The Forms ADV he submitted for Capital Cove did not disclose his use of an alias, or his criminal convictions under that alias, and inflated the assets under management by an order of magnitude. Some of the forms also contained a forged signature of outside counsel. Khalfani has also admitted that he altered a brokerage statement of Capital Cove to make it appear to have more cash on hand that it actually did, and the record shows that he altered several more statements.

Far from disclaiming any intent to commit future violations or recognizing the wrongful nature of his conduct, Khalfani refers to himself as the "wronged party" in this proceeding, which he calls "unwarranted, unjustified, and a total farce."[67] He accuses Division counsel of having a "personal vendetta" against him.[68] Khalfani's lack of remorse weighs in favor of barring him.

Moreover, allowing Khalfani to remain in the securities industry would present him with future opportunities for further misconduct and would put the investing public at risk.[69]

Finally, imposing a bar will serve the Commission's interest in deterring others from engaging in similar misconduct.

Order

The Division of Enforcement's motion for summary disposition is GRANTED.

Under Section 203(f) of the Investment Advisers Act of 1940, Christopher M. Lee, a/k/a Rashid K. Khalfani, is BARRED from associating with an investment adviser, broker, dealer, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization.

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67 Opp'n at 1–2.

68 *Id.* at 7.

69 *See Warwick Capital Mgmt., Inc.*, Advisers Act Release No. 2694, 2008 WL 149127, at *11 (Jan. 16, 2008) ("The existence of a violation raises an inference that the violation will be repeated, and where the misconduct resulting in the violation is egregious, the inference is justified."); *see also Geiger v. SEC*, 363 F.3d 481, 489 (D.C. Cir. 2004) (holding that a finding of egregiousness "justifies the inference" that misconduct will recur); *Korem*, 2013 WL 3864511, at *6 n.50.

This initial decision will become effective in accordance with and subject to the provisions of Rule 360.[70] Under that rule, a party may file a petition for review of this initial decision within twenty-one days after service of the initial decision. A party may also file a motion to correct a manifest error of fact within ten days of the initial decision, pursuant to Rule 111.[71] If a motion to correct a manifest error of fact is filed by a party, then a party shall have twenty-one days to file a petition for review from the date of the undersigned's order resolving such motion to correct a manifest error of fact.

The initial decision will not become final until the Commission enters an order of finality. The Commission will enter an order of finality unless a party files a petition for review or motion to correct a manifest error of fact or the Commission determines on its own initiative to review the initial decision as to a party. If any of these events occurs, the initial decision shall not become final as to that party.

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James E. Grimes
Administrative Law Judge

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70 *See* 17 C.F.R. § 201.360.

71 *See* 17 C.F.R. § 201.111.