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

ADMINISTRATIVE PROCEEDINGS RULINGS
Release No. 4013/July 22, 2016

ADMINISTRATIVE PROCEEDING
File No. 3-17070

In the Matter of 3C ADVISORS & ASSOCIATES, INC., STEPHEN JONES, and DAVID PROLMAN	ORDER ON MOTION FOR SUMMARY DISPOSITION

On January 27, 2016, the Securities and Exchange Commission issued an order instituting proceedings (OIP) against Respondents pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934. The OIP alleges that starting in 2013, 3C Advisors & Associates, Inc., willfully violated Section 15(a) of the Exchange Act by engaging in unregistered broker activity, and that Stephen Jones and David Prolman willfully aided and abetted and caused that violation. OIP at 1-2, 5. More specifically, the OIP asserts that 3C acted as a broker by holding itself out as an arranger of private placements and facilitator of capital raises, undertaking extensive responsibilities for customers, and using engagement agreements that provided for performance fees calculated as a percentage of capital raised. *Id.* at 1, 3-4. The OIP further alleges that through 3C, Jones and Prolman solicited small- and medium-sized businesses by marketing these capital advisory services. *Id.* at 1-4.

3C and Jones filed their answer (Answer) on March 1, 2016, denying any violation. *See* Answer at 2; *3C Advisors & Assocs., Inc.*, Admin. Proc. Rulings Release No. 3751, 2016 SEC LEXIS 1201, at *1 n.1 (ALJ Mar. 31, 2016). Prolman filed a separate answer on March 18, also denying any violation. *See* Prolman Answer at 1-2; *3C Advisors & Assocs., Inc.*, 2016 SEC LEXIS 1201, at *1 n.1. On March 31, I issued a scheduling and general prehearing order, which included a briefing schedule for summary disposition motions. *3C Advisors & Assocs., Inc.*, 2016 SEC LEXIS 1201, at *1.

On May 9, the Division filed its motion for summary disposition with a declaration from Division counsel Lynn M. Dean, supported by exhibits 1-49.[1] On May 23, 3C and Jones

[1] After the Division filed its motion for summary disposition, I granted a joint motion by the Division and Prolman to stay the proceeding as to him, given his agreement to a settlement now pending Commission consideration. *See 3C Advisors & Assocs., Inc.*, Admin. Proc. Rulings Release No. 3842, 2016 SEC LEXIS 1733 (ALJ May 13, 2016). Therefore, this order is inapplicable to Prolman, and I construe the Division's motion for summary disposition as

(Respondents) filed their opposition to the Division's motion, with a declaration from Jones, supported by exhibits 1-6. On June 1, the Division filed its reply.

The Division argues that 3C willfully violated Section 15(a) of the Exchange Act, and contends that Jones willfully aided and abetted and caused 3C's violation. Div. Mot. at 10-21. It further requests sanctions against Respondents in the form of cease-and-desist orders, $160,000 in disgorgement, industry bars as to 3C and Jones,[2] and civil penalties of $375,000 and $37,500 as to 3C and Jones, respectively. *Id.* at 21-28. Respondents argue no violation occurred because 3C did not act as a broker, but only "as a finder, connecting interested parties to one another." Opp. at 1.

I. Summary Disposition Standard

A motion for summary disposition may be granted if there is no genuine issue with regard to any material fact and the party making the motion is entitled to summary disposition as a matter of law. 17 C.F.R. § 201.250(b). The facts on summary disposition must be viewed in the light most favorable to the non-moving party. *See Jay T. Comeaux*, Securities Act of 1933 Release No. 9633, 2014 SEC LEXIS 3001, at *8 (Aug. 21, 2014). However, if the moving party establishes that it is entitled to summary disposition on the factual record, the opposing party 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. *See id.* Thus, summary disposition may be appropriate in non-follow-on proceedings. *E.g.*, *S.W. Hatfield, CPA*, Exchange Act Release No. 73763, 2014 WL 6850921, at *9 (Dec. 5, 2014).

In considering the Division's motion for summary disposition, Respondents' Answer has been taken as true, except as modified by stipulations or admissions made by them, by uncontested affidavits, and by facts officially noticed pursuant to Rule of Practice 323, which include any matter in the Commission's public official records. *See* 17 C.F.R. §§ 201.250(a), .323. Thus, the OIP's allegations that were not denied by Respondents' Answer have been deemed true. *See* 17 C.F.R. § 201.220(c). Declarations that state they are made under penalty of perjury and verified as true and correct are equivalent to affidavits. *See Allen v. Potter*, 152 F. App'x 379, 382 (5th Cir. 2005).

A statement by a party, by a party's agent, or that a party agrees is true, constitutes an admission within the meaning of Rule of Practice 250. *See Wheat, First Sec., Inc.*, Exchange Act Release No. 48378, 2003 WL 21990950, at *12 & n.55 (Aug. 20, 2003) (citing Federal Rule of

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relating to 3C and Jones only. *See* Joint Stay Mot. at 1 (requesting the stay so that Prolman "may be relieved of the obligation to oppose" the Division's motion).

[2] The Division states that such bars are authorized "if the respondent willfully violated the federal securities laws while associated with a broker or dealer, and the suspension or bar is in the public interest." Div. Mot. at 23. However, for Jones, who is not alleged to be a primary violator, aiding and abetting liability is a prerequisite for an industry bar as to him. 15 U.S.C. § 78*o*(b)(4)(E), (b)(6)(A)(i).

Evidence 801(d)(2)). Therefore, statements by Respondents or their agent[3] in a presentation, engagement letter, website, email, marketing materials, or investigative testimony, are all admissions and have been considered against Respondents. *See, e.g.*, Div. Exs. 3, 26-30, 34 (3C marketing materials); Div. Ex. 4 (3C website); Div. Exs. 5-8, 10, 18, 41 (3C's engagement letters and agreements); Div. Exs. 11-12 (3C analyses for customer); Div. Exs. 13-14, 22-23, 35 (emails from 3C); Div. Exs. 24, 39 (3C invoice and balance sheet); Div. Ex. 45 (Jones investigative testimony). By contrast, exhibits that do not contain admissions have not been considered as evidence against Respondents (although they have been considered in opposition to the Division's motion). *See, e.g.*, Div. Exs. 15-16, 19-21, 25, 42 (emails from customers and capital sources); Div. Exs. 46-49 (investigative testimony of Prolman and third parties).

The parties' motion papers and all documents and exhibits of record have been fully reviewed and carefully considered. All arguments and proposed findings and conclusions that are inconsistent with this decision were considered and rejected.

II. Factual Background

3C is a California corporation that provides a range of consulting services to small- and mid-sized companies, including the capital advisory services at issue in this action. OIP ¶ 1; Answer at 2. Jones founded 3C in June 2010 and is 3C's senior managing director. OIP ¶ 2; Answer at 2-3. Jones organized 3C as a holding company with the goal of providing comprehensive consulting services through various sub-LLCs, each independently operated. OIP ¶ 4; Answer at 3. 3C has never been registered as a broker-dealer. *See* OIP ¶ 21; Answer at 9; Jones Decl. ¶¶ 37, 42-43, 50.

Jones has never held any securities licenses. OIP ¶ 2; Answer at 2-3. Prior to launching 3C, Jones performed valuation analysis, litigation support, and restructuring consulting for over two decades at several consulting firms, but did not perform any of the transactional and capital advisory services provided by those firms. OIP ¶ 2; Answer at 2-3.

Through 3C, Jones provided valuation services and litigation consulting, and planned to have 3C offer "capital advisory services" under a sub-LLC known as the "Capital Advisory LLC." OIP ¶ 4; Answer at 3. Ultimately, the capital advisory business operated as a segment of 3C rather than as a sub-LLC, and did not commence operations until June 2013, when Prolman joined the firm and became leader of that business segment. OIP ¶¶ 3, 5; Answer at 3-4. Prolman was not a licensed broker-dealer, but had thirty years' experience in finance and business. Jones Decl. ¶ 46; Jones Opp. at 2.

Since Prolman joined 3C, the firm has marketed its capital advisory business and has taken on at least five engagements to perform capital advisory services. OIP ¶ 6; Answer at 4.

[3] As an employee of 3C and head of its capital advisory services business, Prolman spoke for 3C when performing such services. 3C and Jones have acknowledged as much; for example, they admit that statements in engagement letters and agreements prepared and signed by Prolman were made by 3C. *Compare*, *e.g.*, Answer at 5, *with* Div. Ex. 5 at 2-3. However, Prolman often spoke only for himself during his investigative testimony. *See generally* Div. Ex. 46.

3C has solicited customers for those services online, at industry group meetings, and in presentations with prospective customers, and has further marketed those services to law firms that would introduce 3C to potential customers. OIP ¶ 7; Answer at 4; Div. Ex. 45 at 81-82. According to 3C's website and other marketing materials, the capital advisory services that 3C offered included private placement of debt and equity securities, acquisition financing, growth capital, recapitalizations, and restructuring. OIP ¶ 8; Answer at 4; *see also, e.g.*, Div. Ex. 4; Div. Ex. 28 at 20-21.

3C's capital advisory engagement letters and agreements were initially prepared by Prolman at his prior firm and then adopted by 3C. OIP ¶ 9; Answer at 5; Div. Ex. 45 at 90. In these engagements, 3C sought to "[f]ind and introduce [q]ualified [c]apital [s]ources" to the customer and "assist[the customer] in connection with the preparation and dissemination, as appropriate, of confidential materials for any potential or actual [t]ransaction." OIP ¶ 10 (alterations in original, fifth bracket additionally altered); Answer at 5; *see, e.g.*, Div. Ex. 5 at 2-3. The engagements contemplated customers raising millions of dollars through such introductions. OIP ¶ 10; Answer at 5; Div. Ex. 5 at 1; Div. Ex. 6 at 1; Div. Ex. 10 at 1; Div. Ex. 18 at 1; Div. Ex. 41 at 1.

In its engagement documents, 3C further offered to assist customers in identifying and negotiating with capital sources, but stated that 3C would not negotiate with any capital source directly. *E.g.*, Div. Ex. 5 at 2-3; Div. Ex. 6 at 2; Div. Ex. 10 at 2. However, for at least two of its customers, 3C corresponded with the capital sources separately from the customer during negotiations to ascertain the status of pending deals, and shared these updates with the customers. OIP ¶ 19; Answer at 8.

3C required its capital advisory customers to pay a combination of fees. OIP ¶ 12; Answer at 6. In addition to certain hourly fees, customers were required to pay a flat initial fee and fees based on a percentage of financing successfully obtained; those percentages could vary depending on whether the financing was equity versus debt, or whether the debt financing was secured or unsecured. Div. Ex. 5 at 3; Div. Ex. 6 at 3; Div. Ex. 8 at 3; Div. Ex. 10 at 3-4; Div. Ex. 18 at 3-4; Div. Ex. 41 at 2. Certain engagements also included a flat fee to be paid if the customer received a financing offer. Div. Ex. 5 at 3; Div. Ex. 6 at 3; Div. Ex. 18 at 4. For one engagement, where 3C successfully identified a source that provided the customer debt financing, 3C received $125,000 in fees, which included a $90,000 fee based on a percentage of the financing obtained. Div. Ex. 22 at 2-3; Div. Ex. 23 at 1-2; Div. Ex. 24; *see* OIP ¶ 14; Answer at 6 (denying characterization of $90,000 as a "performance fee" but admitting it amounted to a percentage of total funding); Opp. at 5.

Between 2013, when Prolman joined 3C, through 2014, 3C collected roughly $160,000 in fees from five customers for its capital advisory engagements. OIP ¶ 15; Answer at 7. That amount represented over a quarter of the firm's total revenue of $517,420.32 for all its services during that period. OIP ¶ 15; Answer at 7. Practically, however, this percentage may be overstated because other revenue generated in those years may not have been collected until later. *See* Jones Decl. ¶ 44.

In October 2014, after receiving a subpoena from the Commission, 3C removed references to its capital advisory services from its website. OIP ¶ 20; Answer at 9. Thereafter, the firm took on another engagement to perform capital advisory services for a distressed company, which included "looking for capital" and "operational consulting" for that company. OIP ¶ 20; Answer at 9; Div. Ex. 45 at 109.

III. Discussion

Section 15(a)(1) of the Exchange Act makes it unlawful for any broker to effect transactions in securities using interstate commerce without being registered as a broker or associated with a registered broker. 15 U.S.C. § 78*o*(a)(1). "A finding of violation of Section 15(a) does not require proof of scienter." *David F. Bandimere*, Securities Act Release No. 9972, 2015 SEC LEXIS 4472, at *25 (Oct. 29, 2015), *pet. for review docketed*, No. 15-9586 (10th Cir. Dec. 22, 2015).

Neither 3C nor Jones was a registered broker-dealer or associated with one. *See* OIP ¶¶ 2, 21; Answer at 2-3, 9. Moreover, Respondents do not appear to dispute that 3C used means of interstate commerce in connection with the alleged misconduct. *See, e.g.*, *David F. Bandimere*, 2015 SEC LEXIS 4472, at *18-19 & nn.21-22 (stating that the "interstate nexus is de minimis and is satisfied by even tangential mailings or intrastate telephone calls" and further noting that emails and wire transfers suffice (internal quotation marks omitted)); Div. Ex. 14 (Jones communicating with customer via email); Div. Ex. 24 (3C invoice requesting $90,000 wire transfer from customer). However, Respondents dispute the Division's assertion that 3C acted as a "broker," which is defined as "any person engaged in the business of effecting transactions in securities for the account of others." 15 U.S.C. § 78c(a)(4)(A); Answer at 2.

"In determining whether a person is 'engaged in the business' of effecting transactions for others' accounts," a number of factors are relevant. *David F. Bandimere*, 2015 SEC LEXIS 4472, at *26-27. "A primary consideration is whether there has been regular participation in securities transactions at key points in the chain of distribution," as indicated by "[t]he number of customers at issue, the dollar amount of transactions, and the number of transactions effected." *Id.* at *27. Additional factors include whether a person: (1) actively solicits or recruits investors; (2) advises investors as to the merits of an investment, or opines on its merits; (3) receives commissions, transaction-based compensation, or payment other than a salary for selling the investments; (4) is an employee of the issuer of the securities; (5) sells, or previously sold, the securities of other issuers; (6) is involved in negotiations between the issuer and the investor; and (7) handles investor funds and securities. *Id.* at *28-29; *see SEC v. George*, 426 F.3d 786, 797 (6th Cir. 2005). Receiving "transaction-based compensation" is "one of the hallmarks of being a broker-dealer." *SEC v. Kramer*, 778 F. Supp. 2d 1320, 1334 (M.D. Fla. 2011) (internal citations omitted); *see David F. Bandimere*, 2015 SEC LEXIS 4472, at *31-32.

A. Finder's Exception

Before turning to the various factors relevant to broker activity noted above, I address Respondents' argument that 3C was a merely a "finder," Opp. at 13-14, and the Division's argument that no finder's exception exists, *see* Div. Reply at 5-6; Div. Mot. at 15. On the record

as it stands, I agree with the Division, although Respondents may renew their argument on this point in post-hearing briefing.

Some district court cases have identified "a limited, so-called finder's exception that permits a person to perform a narrow scope of activities without triggering the broker/dealer registration requirements." *David F. Bandimere*, Initial Decision Release No. 507, 2013 WL 5553898, at *53 (ALJ Oct. 8, 2013) (internal quotations omitted) (citing district court cases), *on pet. for review*, 2015 SEC LEXIS 4472 (Oct. 29, 2015), *pet. for review docketed*, No. 15-9586 (10th Cir.); *see also David B. Havanich, Jr.*, Initial Decision Release No. 935, 2016 SEC LEXIS 4, at *22 (ALJ Jan. 4, 2016) (citing district court cases), *finality order*, Securities Act Release No. 10045, 2016 SEC LEXIS 668 (Feb. 23, 2016). But neither the Supreme Court nor any federal court of appeals has recognized someone as being exempt from the Exchange Act's broker registration requirement merely by virtue of being a finder. *See David B. Havanich, Jr.*, 2016 SEC LEXIS 4, at *22. This may be explained in part by the fact that, as some of the cases cited by Respondents suggest, the distinction between a finder and a broker is not derived from securities law but from New York state contract law. *See Jones v. Whelan*, No. 99-cv-11743, 2002 WL 485729, at *7 (S.D.N.Y. Mar. 29, 2002) (citing *Train v. Ardshiel Assocs., Inc.*, 635 F. Supp. 274, 278-79 (S.D.N.Y. 1986), *aff'd*, 805 F.2d 391 (2d Cir. 1986)); *Warshay v. Guinness PLC*, 750 F. Supp. 628, 636 (S.D.N.Y. 1990), *aff'd*, 935 F.2d 1278 (2d Cir. 1991); *Ne. Gen. Corp. v. Wellington Advert., Inc.*, 82 N.Y.2d 158, 162-63 (1993); *see also Apex Global Partners, Inc. v. Kaye/Bassman International Corp.*, No. 3:09-cv-637, 2009 WL 2777869, at *3 (N.D. Tex. Aug. 31, 2009) (a finder may need to register if its activities meet certain requirements).

The Commission has never recognized a finder's exception. *See David B. Havanich, Jr.*, 2016 SEC LEXIS 4, at *22. One recent Commission opinion addressing the need for registration under Section 15(a) does not discuss finders as a category distinct from other persons. *See David F. Bandimere*, 2015 SEC LEXIS 4472, at *25-33. The Commission's website includes a page affirmatively stating that a finder "may need to register as a broker, depending on a number of factors." *Guide to Broker-Dealer Registration*, https://www.sec.gov/divisions/marketreg/bdguide.htm#II (last accessed July 15, 2016). Some such factors are pertinent here, including whether the person: finds investors for issuers (even in a "consultant" capacity); finds investors for venture capital or "angel" financings, including private placements; or finds buyers and sellers of businesses, i.e., "activities relating to mergers and acquisitions where securities are involved." *Id.*

One commonly cited treatise uses the term "finder's exemption," but examines at length circumstances in which finders may still be required to register as brokers. *See* 15 David A. Lipton, *Broker-Dealer Regulation*, at § 1.15-.21 (2016) (Lipton). Lipton relies heavily on no-action letters, which do not "have the force of law." *See generally id.*; *Enron Corp.*, 57 S.E.C. 198, 222 n.50 (2003). Lipton nonetheless concludes that four activities in which finders commonly engage, all of which are pertinent here, make it more likely that broker registration will be required: involvement in securities sales negotiations; discussing details of the nature of the securities sold or making recommendations; commissions linked to sales volume; and previous involvement in securities sales. *See* Lipton at § 1.16. If Respondents sufficiently engaged in these or other types of activities indicating 3C was a broker, then even if Respondents were finders, that status is legally meaningless.

Accordingly, there is limited relevance to Respondents' contention, for example, that 3C referred approximately twenty-eight percent of its opportunities to a registered broker-dealer. Jones Decl. ¶ 43; *see* Opp. at 7; Jones Decl. ¶¶ 37-38, 42, 52; Div. Exs. 37-38; Div. Ex. 45 at 54-55. The issue here is whether 3C acted as a broker through the services it *did* provide—whether Respondents referred certain other business to registered brokers is irrelevant to that inquiry. Further, Respondents' argument that certain services or fees "were generated in and from the *non-capital advisory service components of the company*," Opp. at 10-11, is unpersuasive because determining whether an entity acted as a broker requires "evaluat[ing] the totality of [its] activities," *Definition of Terms in and Specific Exemptions for Banks, Savings Associations, and Savings Banks Under Sections 3(a)(4) and 3(a)(5) of the Securities Exchange Act of 1934*, 68 Fed. Reg. 8686, 8689 (Feb. 24, 2003) (to be codified at 17 C.F.R. pt. 240). Not examining this totality would allow an entity to superficially divide various broker functions among its purported business segments to avoid registration. Moreover, though 3C may have categorized its various services and fees differently, it provided them in conjunction with each other and set them out together in its engagement agreements with customers. *See, e.g.*, Div. Exs. 10, 18, 41. As such, I address the totality of 3C's activities below.

B. Factors Relevant to Broker Activity

Customers and Transactions. As to "[t]he number of customers at issue, the dollar amount of transactions, and the number of transactions effected," *David F. Bandimere*, 2015 SEC LEXIS 4472, at *27, the record establishes only that a single 3C engagement led to one transaction, in which the customer raised over $9 million in debt, Div. Ex. 23 at 1-2. 3C did, however, collect fees from four other customers for its capital advisory services, and sought to assist such customers in obtaining many millions of dollars in equity or debt. OIP ¶ 15; Answer at 7; Div. Exs. 6-8, 18, 41.

Soliciting Investors. 3C marketed its capital advisory services on its website, in presentations, and in industry meetings. *See* OIP ¶¶ 6-8; Answer at 4; Div. Ex. 3 at 18; Div. Ex. 4; Div. Exs. 26-27; Div. Ex. 28 at 20-21; Div. Ex. 30 at 10; Div. Ex. 45 at 81-82. 3C advertised its "broad experience in placement of [debt] . . . and equity for the family enterprise and closely held enterprises," listed customers' potential "Purposes [for a] Capital Raise," and stated that "[t]hrough its relationships with institutional and private investors, [3C] has . . . help[ed] clients expand, effect ownership transitions, recapitalize and acquire other companies." *E.g.*, Div. Ex. 3 at 18; Div. Ex. 4. It is undisputed that 3C would actively "[f]ind and introduce" capital sources (i.e., investors) for the customer and would further assist the customer "in connection with the preparation and dissemination, as appropriate, of confidential materials for any potential or actual [t]ransaction." OIP ¶ 10; Answer at 5; Div. Ex. 5 at 2-3; Div. Ex. 6 at 2; *see* Div. Ex. 8 at 2; Div. Ex. 10 at 2; Div. Ex. 41 at 1. Respondents admit to sending "no-name teasers" about possible investments to Prolman's contacts, and subsequently sending non-disclosure agreements to those contacts if they thought they would be interested. Div. Ex. 45 at 85; *see* Opp. at 12. In at least one instance, Prolman sent a marketing book for a "loan request package" to a capital source on behalf of a 3C customer. *See* Div. Ex. 36.

On the other hand, although 3C's marketing materials discuss 3C's ability to assist customer-issuers in raising capital, they are not targeted at *the investors* from whom that capital would come.[4] The Division argues that "3C actively built a base of potential sources of capital who could invest in its customers" by "marketing directly to the capital sources themselves." Div. Mot. at 4. But Respondents dispute this, contending that 3C merely connected customers to capital sources in Prolman's preexisting "Rolodex of contacts," from "his 30 years in the industry" rather than during his time at 3C. Jones Decl. ¶¶ 45-46; *see* Opp. at 8-9; Div. Ex. 45 at 85. And after sending out teasers, Respondents argue they would "step out" of the process. Opp. at 12; Div. Ex. 45 at 85.

Advising or Opining to Investors as to the Merits. The evidence is not definitive on the extent to which 3C offered advice or opinions to investor capital sources regarding the merits of investing in the securities of 3C's customers, or the extent to which 3C touted those merits. The Division relies on 3C's purported creation and dissemination of "marketing books" and shorter "teasers." Div. Mot. at 7; Div. Reply at 4; *see* Div. Ex. 9 (marketing book); Div. Ex. 17 (teaser). Respondents admit to "building the teasers" generally, and for at least one customer, "editing and combining the 'deck' and teaser." Jones Decl. ¶¶ 61-62; *see* Opp. at 12 ("3C's involvement was limited to editing the material with regard to aesthetics, such as layout, and general industry information."); Div. Ex. 45 at 85 (stating that 3C will "critique [the teaser, and] . . . sometimes we help write some if it" or provide edits or suggestions). Indeed, one engagement agreement stated that "3C, with your assistance, will develop a [c]onfidential [i]nformation [m]emorandum . . . and summary sheet (the "Tear Sheet") for distribution to [capital sources]." Div. Ex. 10 at 2.

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[4] It bears mention that the Financial Industry Regulatory Authority (FINRA) has proposed "a separate rule set" for so-called "capital acquisition brokers" that are "solely corporate financing firms that advise companies on mergers and acquisitions, advise issuers on raising debt and equity capital in private placements with institutional investors, or provide advisory services on a consulting basis to companies that need assistance analyzing their strategic and financial alternatives." *Notice of Filing of a Proposed Rule Change To Adopt the Capital Acquisition Broker Rules*, 80 Fed. Reg. 79969, 79969-70 (Dec. 23, 2015). The proposal states that such firms "often are registered as broker-dealers because of their activities and because they may receive transaction-based compensation," even though they "do not engage in many of the types of activities typically associated with traditional broker-dealers" like "handl[ing] customer funds or securities, carry[ing] or act[ing] as an introducing broker with respect to customer accounts, or provid[ing] products and services to retail customers." *Id.* at 79970, 79974. The proposal, therefore, "establishes a separate set of streamlined [FINRA] rules" for these firms that would "reduce the[ir] regulatory burden . . . given their limited activities and institutional business model." *Id.* at 79974. In the proposal, FINRA does not explicitly opine on whether such firms must currently be registered as brokers, but notes that under the new rules, "if a [capital acquisition broker] . . . had engaged in activities [requiring it] to register as a broker or dealer under the Exchange Act . . . FINRA could examine for and enforce all FINRA rules against such a broker." *Id.* at 77971. The Commission is currently determining whether to approve or disapprove these proposed rules. *See Order Instituting Proceedings To Determine Whether To Approve or Disapprove Proposed Rule Change To Adopt FINRA Capital Acquisition Broker Rules*, 81 Fed. Reg. 15588 (Mar. 23, 2016).

Respondents further admit to disseminating these teasers to capital sources, but deny helping create or disseminate the more substantial marketing books, though Prolman sent at least one to a capital source. *See* OIP ¶ 17; Answer at 7-8; Opp. at 12; Jones Decl. ¶¶ 81-82; Div. Ex. 45 at 85; Div. Ex. 36. Moreover, whether 3C substantially helped to create those materials is disputed to a degree, as Respondents assert that "[i]t was the client's responsibility to produce these materials." Opp. at 11; *see* Jones Decl. ¶¶ 81-82; *see also* OIP ¶ 17; Answer at 7-8; Div. Ex. 45 at 84-85 ("Typically it's the responsibility of the client to do that."). The Division also points out that, for at least one customer, 3C "analyzed the customer's funding needs and advised the customer regarding funding options." Div. Mot. at 14; *see* Div. Exs. 11-14, 35. But there is no evidence that this advice and analysis was directed at investors.

3C's Role in Negotiations between the Issuer and Investor. For several engagements, 3C stated that it would assist customers in negotiating with identified capital sources, albeit indirectly. OIP ¶ 11; Answer at 5; Div. Ex. 5 at 3; Div. Ex. 6 at 2; Div. Ex. 10 at 2. This could include assisting the customer "in all phases of the negotiation process, including establishment of price, terms and structure." Div. Ex. 5 at 3. Respondents additionally concede that for at least two customers, 3C corresponded with capital sources separately from the customer during negotiations to ascertain the status of the pending deal and shared updates with the customer.[5] OIP ¶ 19; Answer at 8. However, one of these customers clarified that 3C's role in negotiations was limited, stating that 3C did not "directly [a]ffect negotiations" or "do any negotiations." Div. Ex. 48 at 59-60, 62.

Transaction-Related Compensation. In addition to an initial flat fee and certain hourly fees paid regardless of any transaction, 3C's engagement documents required customers to pay fees based on percentages of successfully obtained financing for the customer, which could vary depending on whether the financing was equity versus debt, or whether the debt financing was secured or unsecured. Div. Ex. 5 at 3; Div. Ex. 6 at 3; Div. Ex. 8 at 3; Div. Ex. 10 at 4; Div. Ex. 18 at 4; Div. Ex. 41 at 2; Div. Ex. 45 at 91 (Jones testifying that percentage-based fees were calculated "off the capital amount that the client used"). Certain of these engagements included an additional flat fee if the customer received a financing offer. Div. Ex. 5 at 3; Div. Ex. 6 at 3; Div. Ex. 18 at 4. Ultimately, however, 3C received transaction-based compensation only once, where 3C successfully identified a source that provided a customer debt financing of approximately $9.4 million; this resulted in a $90,000 fee for 3C, representing about one percent the debt financing obtained for the customer. OIP ¶ 14; Answer at 6; Div. Ex. 22 at 2-3; Div. Ex. 23 at 1-2; Div. Ex. 24. This $90,000 constituted over half of the $160,000 in total fees 3C collected from its five capital advisory customers. *See* OIP ¶ 15; Answer at 7.

Remaining Factors. As noted above, *David F. Bandimere*, 2015 SEC LEXIS 4472, at *28-29, indicates other non-exhaustive factors regarding broker status may include being an employee of the issuer of the securities; selling, or having previously sold, the securities of other

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[5] The Division's additional contentions concerning 3C's role in these negotiations rely on the statements of third parties rather than admissions by 3C or Jones. *See* Div. Mot. at 8 (citing exhibits 15-16 and 19-21, which are emails from customers and capital sources, as well as exhibits 48-49, which are excerpts of investigative testimony taken from 3C customers).

issuers; and handling investor funds and securities. 3C was not an employee of its issuer-customers, but rather was retained as an independent contractor.[6] *See* Div Ex. 10 at 3; Div. Ex. 18 at 2; Div. Ex. 41 at 2. Other than the engagements discussed above, there is no evidence 3C previously sold or attempted to sell the securities of other issuers. Nor is there evidence that 3C handled investor funds and securities.

C. Conclusion as to Alleged Section 15(a) Violation

Viewing the evidence in the light most favorable to Respondents, there remain genuine issues of material fact that make summary disposition inappropriate as to whether 3C acted as an unregistered broker. Respondents genuinely dispute, among other things, the extent to which 3C solicited and advised investors and participated in negotiations. And although Respondents have admitted to much relevant conduct on the part of 3C, including finding investors for its customers and editing and sending certain materials to investors, what weight I accord that evidence is best determined within the broader factual context provided by a hearing. That context is especially important given the multi-factored, non-exhaustive framework for analyzing whether one has acted as a broker. *See, e.g.*, *Sun River Energy, Inc. v. Nelson*, No. 11-CV-198, 2013 WL 1222391, at *5 (D. Colo. Mar. 25, 2013) (denying summary judgment, noting that whether one acted as a broker "is a fact-intensive inquiry" and that the record required more factual specificity to conclude "precisely *what* the Defendants did . . . much less conclude that such activity constitutes 'brokering' as a matter of law"). Even the unequivocal evidence that 3C received substantial transaction-based compensation—which is a strong but not dispositive indicator of brokering activity—is only one factor to consider among many. *See Kramer*, 778 F. Supp. 2d at 1334; *David F. Bandimere*, 2015 SEC LEXIS 4472 at *31-32.

D. State of Mind: Causing and Aiding and Abetting Liability

Causing liability requires proof that: (1) there was a primary violation; (2) an act or omission by the respondent was a cause of the violation; and (3) the respondent knew, or should have known, that his conduct would contribute to the violation, i.e., the respondent was negligent. *Robert M. Fuller*, 56 S.E.C. 976, 984 (2003), *pet. denied*, 95 F. App'x 361 (D.C. Cir. 2004); *KPMG Peat Marwick LLP*, 54 S.E.C. 1135, 1175 & n.100 (2001), *pet. denied*, 289 F.3d

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[6] The majority of courts view being an employee of an issuer as making one less likely to be a broker, while others view it as making one more likely to be a broker. *Compare SEC v. Collyard*, --- F. Supp. 3d ---, 2015 WL 8483258, at *4-5 (D. Minn. Dec. 9, 2015), *Landegger v. Cohen*, 11-cv-1760, 2013 WL 5444052, at *6 (D. Colo. Sept. 30, 2013), *SEC v. Benger*, 697 F. Supp. 2d 932, 944 (N.D. Ill. 2010), *and SEC v. Martino*, 255 F. Supp. 2d 268, 284 (S.D.N.Y. 2003), *with SEC v. George*, 426 F.3d 786, 797 (6th Cir. 2005); *SEC v. Battoo*, --- F. Supp. 3d ---, 2016 WL 302169, at *12 n.15 (N.D. Ill. Jan. 25, 2016). Regardless, status as an independent contractor does not insulate a person from liability under Section 15(a). *See, e.g.*, *Joseph Kemprowski*, Exchange Act Release No. 35058, 1994 WL 684628, at *2 (Dec. 8, 1994) (respondents employed as "independent consultants" for public relations services were brokers where they recommended investments after contacting potential investors directly and through registered representatives).

109 (D.C. Cir. 2002); *see* 15 U.S.C. § 78u-3(a). Aiding and abetting liability requires proof that: (1) there was a primary violation; (2) the alleged aider and abettor provided substantial assistance to the primary violator; and (3) the alleged aider and abettor did so at least recklessly. *E.g.*, *Graham v. SEC*, 222 F.3d 994, 1000 (D.C. Cir. 2000); *Phlo Corp.*, Exchange Act Release No. 55562, 2007 SEC LEXIS 604, at *35 (Mar. 30, 2007). Recklessness is defined as "an extreme departure from the standards of ordinary care . . . to the extent that the danger was either known to the [respondent] or so obvious that the [respondent] must have been aware of it." *Toby G. Scammell*, Investment Advisers Act of 1940 Release No. 3961, 2014 SEC LEXIS 4193, at *26 n.41 (Oct. 29, 2014) (ellipses and alterations in original). Thus, to establish Jones aided and abetted 3C, the Division need not show that Jones intended or knew that 3C was acting as an unregistered broker, *see* Jones Decl. ¶¶ 3, 87, but rather that Jones was or must have been aware of the risk that 3C was acting as an unregistered broker, and disregarded that risk in an extreme departure from the standards of ordinary care.

Having found that summary disposition is inappropriate as to 3C's alleged primary violation, the Division's arguments that Jones caused and aided and abetted such a violation are premature for now. But given that these arguments hinge on Jones' state of mind, I preliminarily address certain assertions by Respondents of potential relevance to that issue,[7] namely:

- Prolman was primarily responsible for capital advisory services and Jones did not carry out such activities, being primarily responsible for litigation services. Opp. at 16-17; Jones Decl. ¶¶ 40, 58.

- Although Jones received from Prolman a 3C business plan identifying six capital advisory firm competitors that were all registered broker-dealers, such firms were identified because 3C was planning to eventually have a broker-dealer component using licensed individuals for such work. OIP ¶ 5; Answer at 3-4; Opp. at 1, 15; Div. Ex. 29 at 4; Div. Ex. 45 at 54-55.

- 3C referred certain business opportunities to a registered broker-dealer rather than take those opportunities itself. *See* Opp. at 7; Jones Decl. ¶¶ 37-38, 42-43, 52; Div. Exs. 37-38.

- If 3C acted as an unregistered broker, Jones did not know or intend it. Opp. at 1-2; Jones Decl. ¶¶ 3, 87.

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[7] These bulleted facts are irrelevant, however, to whether 3C committed a primary violation of Section 15(a)(1), which has no state of mind requirement. 15 U.S.C. § 78*o*(a)(1); *see David F. Bandimere*, 2015 SEC LEXIS 4472, at *25. Regarding Respondents' evidence of threats purportedly made by an embittered former 3C employee, there is no indication why such evidence is of any relevance to this proceeding, as it does not bear on Jones' state of mind or whether Respondents' conduct was violative, but only speaks to how this matter may have been brought to the Division's attention initially. *See* Opp. at 3-4; Jones Decl. ¶¶ 13-20; Resp. Exs. 1-2. Respondents may, however, argue for the introduction of such evidence at the hearing if they still believe it is relevant.

- The lawyers that 3C engaged did not raise the issue of broker registration. Opp. at 4; Jones Decl. ¶¶ 31-33.

- Jones relied on certain legal advice passed on by Prolman from his prior firm concerning engagement materials. *See* Opp. at 16-17; Jones Decl. ¶ 58; Div. Ex. 45 at 90-91.

- A 3C employee who had experience in investment banking and licensing did not raise the issue of broker registration, and 3C consulted another individual for compliance issues. Opp. at 4, 6-7; Jones Decl. ¶¶ 24, 28-30, 34-36.

Even were Jones to establish these facts at a hearing, he still may have been negligent, and perhaps even reckless, if the Division establishes a primary violation on the part of 3C. Although Prolman led the capital advisory business, Jones formed it and founded 3C as senior managing director. OIP ¶¶ 2-5; Answer at 2-4. He also had some role in providing services to capital advisory customers. Div. Exs. 11, 14. Jones had previously worked in other firms' broker-dealer segments and was at least generally aware of the broker registration requirements, although he disclaimed further familiarity with such requirements in his investigative testimony. *See* Div. Ex. 45 at 34-38, 112; Opp. at 2; Div. Ex. 32 (email from Jones, with subject line "FINRA Registration," stating that he was "speaking with a FINRA register BD tomorrow to begin our process"). Indeed, if Respondents were planning to eventually develop a broker-dealer component and knew "they had to get licensed individuals on board first," Opp. at 15, then Jones' awareness of the registration requirements is all the more likely. Further, accepting that 3C had plans to develop a broker component later does not alter the fact that in January 2014, Jones received a 3C business plan identifying six competitor firms, all broker-dealers, "in the markets identified for 2014"—a period during which 3C's capital advisory segment operated and generated transaction-based compensation. OIP ¶ 5; Answer at 3-4; Div. Ex. 29 at 4; *see* Div. Ex. 22 at 2-3; Div. Ex. 23 at 1-2; Div. Ex. 24. Respondents' argument that 3C would "refer [certain] work off" to a registered broker-dealer, and would not have done so if 3C was acting as a broker, does not necessarily help Jones. Opp. at 7 (quoting Div. Ex. 45 at 55); Jones Decl. ¶¶ 37-38, 42-43, 52; *see* Div. Exs. 37-38 (emails from Jones making such referrals). On the one hand, it may further evidence Jones' awareness of the registration issue; on the other hand, it indicates that Jones may have taken precautions to limit the scope of 3C's activities.

Additionally, Respondents' assertions regarding their reliance on the advice of counsel are presently insufficient to constitute a legal defense for Jones. Such assertions are blunted by Jones' admission that 3C did not retain counsel to review its capital advisory engagement materials or the scope of the capital advisory services it could offer. *See* Div. Ex. 45 at 90-91. Indeed, the lawyers that Respondents claim to have engaged were, by Jones' admission, "corporate and tax lawyers" that only advised 3C through "tax and corporate partners," as opposed to directly. Jones Decl. ¶¶ 32, 59. Further, there is no indication that Respondents "(1) made a complete disclosure to counsel; (2) requested counsel's advice as to the legality of the contemplated action; (3) received advice that it was legal; and (4) relied in good faith on that advice." *SEC v. Savoy Indus., Inc.*, 665 F.2d 1310, 1314 n.28 (D.C. Cir. 1981) (listing the required elements of the advice of counsel defense). As to the purported legal advice passed

along by Prolman (who is not an attorney) regarding 3C's engagement materials, such secondhand information does not meet the requirements of an advice of counsel defense. *See id.* Similarly, Jones cannot shield himself by contending that non-lawyers—i.e., a 3C employee and another individual—failed to raise the broker registration issue or were consulted generally for compliance matters, as there is no evidence those individuals provided affirmative advice on broker registration, nor is there evidence concerning "what factors and assumptions underlay" such advice, had it been given. *Scott Mathis*, Exchange Act Release No. 61120, 2009 SEC LEXIS 4376, at *24 (Dec. 7, 2009); *see* Opp. at 4, 6-7; Jones Decl. ¶¶ 24, 28-30, 34-36. Even had Respondents properly retained counsel for compliance with the securities laws and satisfied the elements of an advice of counsel defense, the defense is not a complete one and would be unavailable to Jones with respect to causing liability because it is only available where scienter is an element of the violation. *See David M. Haber*, 52 S.E.C. 201, 206 & n.15 (Apr. 5, 1995) (further noting that the defense is not "automatic" but rather "only one factor to be considered").

IV. Ruling

The Division's motion for summary disposition is DENIED.

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Cameron Elliot
Administrative Law Judge