**UNITED STATES OF AMERICA**
**Before the**
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES EXCHANGE ACT OF 1934**
**Release No. 101361 / October 16, 2024**

**ADMINISTRATIVE PROCEEDING**
**File No. 3-22259**

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| **In the Matter of**<br><br>**PHX Financial, Inc.**<br><br>**Respondent.** | **ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS, PURSUANT TO SECTIONS 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER** |

## I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act"), against PHX Financial, Inc. ("PHX" or "Respondent").

## II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order"), as set forth below.

## III.

On the basis of this Order and Respondent's Offer, the Commission finds that: [1]

### Summary

1. From January 2019 to October 2021 (the "Relevant Period"), a PHX registered representative ("Representative 1") recommended a short-term, high-volume investment strategy to at least eight of PHX's retail customers without a reasonable basis. As a result of the high volume of recommended transactions and their attendant commissions and fees, it would have been virtually impossible for these customers to achieve positive returns. While these customers each lost money in their PHX brokerage accounts (the "Accounts") during the Relevant Period, PHX and Representative 1 together made over $400,000 in commissions and fees from those Accounts.

2. The Relevant Period encompasses conduct both before and after Regulation Best Interest's ("Reg BI") compliance date, June 30, 2020 (the "Pre-Reg BI Period" and "Reg BI Period," respectively). During the Pre-Reg BI Period, PHX failed reasonably to supervise Representative 1, within the meaning of Section 15(b)(4)(E) of the Exchange Act, with the view to preventing and detecting Representative 1's violations of Section 17(a) of the Securities Act of 1933 ("Securities Act") and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

3. Further, during the Reg BI Period, PHX violated the Reg BI Care Obligation, Exchange Act Rule 15*l*-1(a)(2)(ii), when Representative 1 recommended a series of transactions to retail customers without a reasonable basis to believe that the recommended transactions, even if in the customers' best interests when viewed in isolation, were not excessive and in the customers' best interests when taken together in light of the customers' investment profiles. Additionally, PHX violated the Reg BI Compliance Obligation, Exchange Act Rule 15*l*-1(a)(2)(iv), by failing to establish, maintain and enforce written policies and procedures reasonably designed to achieve compliance with Reg BI's Care Obligation. As a result of PHX's violations of Reg BI's Care and Compliance Obligations, it also violated Reg BI's General Obligation, Exchange Act Rule 15*l*-1(a)(1), which requires compliance with Reg BI's component obligations.

### Respondent

4. **PHX** is a Florida corporation with its main office in New York City and branch offices in Hauppauge, New York and Fort Lauderdale, Florida. It has been registered with the Commission as a broker-dealer since October 31, 2007.

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[1] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

## Facts

### I. Failure to Supervise

#### a. The Underlying Fraud Violations (Pre-Reg BI Period)

5. A broker-dealer has a duty to have a reasonable basis for its trade recommendations. *See SEC v. Hasho*, 784 F. Supp. 1059, 1107 (S.D.N.Y. 1992) ("By making a recommendation, a securities dealer implicitly represents to a buyer of securities that he has an adequate basis for the recommendation."). Under this duty, a registered representative who recommends a particular trading strategy, including a strategy of high-cost in-and-out trading, must have a reasonable basis for believing the strategy is suitable for at least some customers. *See SEC v. Fowler,* 6 F.4th 255, 262-63 (2d Cir. 2021).

6. During the Pre-Reg BI Period, however, Representative 1 began recommending a short-term, high-volume investment strategy to at least five of PHX's retail customers without a reasonable basis. As discussed below, he recommended this strategy to three additional retail customers during the Reg BI Period. Each of the accounts had high cost-to-equity ratios and annual turnover rates, both of which are indicative of excessive trading. The cost-to-equity ratio is the rate of return required for an account to break even, considering the costs, such as commissions and other fees associated with the trading in the account. The annual turnover rate represents the total value of annual purchases made in the account divided by the account's average monthly balance. A cost-to-equity ratio of 20% or higher or an annual turnover rate of six or more is generally indicative of excessive trading.

7. During the Pre-Reg BI Period, the five accounts had cost-to-equity ratios that ranged from almost 37% to 93% and turnover rates that ranged from roughly 11 to 35. Although the four of the five accounts lost money, PHX and Representative 1 made over $60,000 in commissions and fees from those five accounts.

8. Representative 1 did not have a reasonable basis to believe that his recommended short-term, high-volume trading strategy was suitable for any customer given the associated high costs that allowed virtually no chance of profitability. Representative 1 knowingly or recklessly disregarded the fact that the high-cost pattern of frequent trading he recommended for these customer accounts had virtually no chance of generating any profit. As a result of the conduct described above, Representative 1 violated Section 17(a) of the Securities Act, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

#### b. PHX's Supervisory Failures (Pre-Reg BI Period)

9. Representative 1 was subject to PHX's supervision. During the Pre-Reg BI Period, PHX failed reasonably to supervise Representative 1, within the meaning of Section 15(b)(4)(E) of the Exchange Act, with the view to preventing and detecting Representative 1's

violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

10. PHX had policies and procedures addressing excessive trading and suitability, including monitoring procedures to detect excessive trading, as set forth in its written supervisory procedures ("WSPs"). Specifically, its clearing firm generated a Monthly Active Account Report ("MAAR"), which flagged accounts for potentially excessive trading based on, among other things, the number of trades, the cost-to-equity ratio, and the turnover rate in each account. Supervisor 1 reviewed the MAARs each month.

11. PHX did not develop or reasonably implement policies and procedures to prevent and detect Representative 1's unsuitable recommendations. For example, the firm did not have any policies and procedures or a system to implement its policies and procedures to determine whether Representative 1's supervisor or any supervisor at PHX, after having reviewed accounts identified in the MAAR, took reasonable steps to address whether recommendations made by Representative 1 were suitable for the firm's customers, including by carrying out the possible procedures set forth in the WSPs to address the accounts flagged in the MAARs or otherwise acting to address the excessive trading.

12. The firm's WSPs sought to address excessive trading and unsuitable recommendations, in part, through the use of "active trading letters." These letters, among other things, advised a customer of the number of transactions in the customer's account for a three-month period as well as the cost-to-equity ratio. According to PHX's WSPs, if supervisors learned of potentially excessive trading through the review process, they could, but were not required to take steps, including sending an active trading letter to a customer, contacting the customer, or restricting the trading in the account. There were no criteria, however, for determining whether to take any of those steps, particularly where accounts repeatedly appeared on the MAARs. Moreover, the firm's active trading letter procedures were not reasonably designed to prevent violations of reasonable basis suitability obligations. Rather, at best, they sought to alert customers about excessive trading after it had already occurred. Only one of the customers at issue received an active trading letter in the Pre-Reg BI Period even though the five customers' Accounts appeared on the MAARs a total of 13 times during that period.

13. After receiving a customer complaint relating to high commissions and excessive trading in 2019, PHX placed Representative 1 on heightened supervision from May 1, 2019 until May 1, 2020. The terms of Representative 1's heightened supervision were set out in an agreement ("The Heightened Supervisory Agreement") and placed obligations on Representative 1 such as requiring that he review his customers' investment objectives to confirm transactions were suitable and that he adhere to the firm's policies and procedures. The agreement did not further specify how Representative 1 should assess his recommendations to customers to avoid excessive trading or place other obligations or limitations on Representative 1. While Representative 1 was on heightened supervision, a supervisor also had to approve the trades for all of Representative 1's accounts. The Heightened Supervisory Agreement, however, contained no guidance for how the proposed trades in Representative 1's accounts were to be evaluated, particularly to address

excessive trading and suitability. The Heightened Supervisory Agreement did not add any policies and procedures for supervisors to follow with respect to excessive trading and or suitability, and Cabalar continued to engage in excessive trading and make unsuitable recommendations both during and after his heightened supervisory period.

## II. Reg BI Violations

### a. The Care Obligation (PHX's Series of Recommendations With No Reasonable Basis)

14. Reg BI requires that a broker-dealer or its associated person, when recommending securities transactions to a retail customer, "act in the best interest of the retail customer at the time the recommendation is made, without placing the financial or other interest of the broker, dealer, or [associated] person . . . ahead of the interest of the retail customer." Exchange Act Rule 15*l*-1(a)(1). Reg BI's Care Obligation requires a broker-dealer or its associated person, when making a recommendation of any securities transaction or investment strategy involving securities to a retail customer, to have a reasonable basis to believe that a series of recommended transactions, even if in the retail customer's best interest when viewed in isolation, is not excessive and is in the retail customer's best interest when taken together in light of the retail customer's investment profile and does not place the financial or other interest of the broker-dealer or its associated person ahead of the interest of the retail customer. Exchange Act Rule 15*l*-1(a)(2)(ii)(C).

15. During the Reg BI Period, PHX, through Representative 1, recommended a short-term, high-volume investment strategy to eight retail customers without a reasonable basis. The strategy involved frequent trades that placed PHX's and Representative 1's interests in generating commissions and fees ahead of the retail customers' interests. The fact that the account opening documents for the Accounts indicated that the each of the customer's investment objective was "speculation" and that each of their risk tolerance was "maximum" or "speculative" did not relieve Representative 1 or PHX of their obligations under Reg BI. As Reg BI's adopting release explained, "Where a retail customer expresses a desire for 'active trading,' a broker-dealer may take this factor into consideration when evaluating a recommendation; however, the broker-dealer will nevertheless need to reasonably believe that a series of recommended transactions is in the best interest of the retail customer." Regulation Best Interest: The Broker-Dealer Standard of Conduct, Exch. Act Rel. No. 86031, 84 FR 33318, 33384 (June 5, 2019).

16. The cost-to-equity ratios and turnover rates for the Accounts during the Reg BI Period all exceeded the thresholds courts have found to be indicative of excessive trading, with cost-to-equity ratios ranging from approximately 40% to 52% and turnover rates ranging from 7 to 53. During the Reg BI Period, the Accounts all lost money, but PHX and Representative 1 made almost $350,000 in commissions and fees. Given all that, the recommended series of transactions

during the Reg BI Period were not in the customers' best interests because they placed PHX's and Representative 1's interests ahead of the customers' interests.

**b. The Compliance Obligation**

17. Reg BI includes a Compliance Obligation, which requires that a broker-dealer establish, maintain, and enforce written policies and procedures reasonably designed to achieve compliance with Reg BI. *See* Exchange Act Rule 15*l*-1(a)(2)(iv).

18. During the Reg BI Period, PHX failed to establish, maintain, and enforce written policies and procedures reasonably designed to achieve compliance with Reg BI's Care Obligation. Although PHX's WSPs during the Reg BI Period recited Reg BI's Care Obligation and provided for periodic reviews of customer accounts using the MAARs, including actions that supervisors may take to achieve compliance with Reg BI, the WSPs lacked specificity concerning whether and when such additional actions should be taken, if at all.

19. As during the Pre-Reg BI Period, the firm's WSPs during the Reg BI Period sought to address excessive trade recommendations through active trading letters. According to PHX's WSPs, if supervisors learned of active trading through the review process, they could send an active trading letter to a customer, contact a customer, or restrict an account. As before, however, the WSPs did not require any of those steps to be taken and did not have any criteria for determining whether to take them.

20. The Accounts appeared on the MAARs a total of 53 times during the Reg BI Period. Yet, only four of the retail customers received active trading letters for a single three-month period during the Reg BI Period. None of the customers received active trading letters concerning trades executed during any other time in the Reg BI Period. Two of those customers who initially received active trading letters in February 2021 that incorrectly understated their cost to equity ratios. Nine months later, in November 2021, PHX sent revised active trading letters, but the cost-to-equity ratios on those active trading letters were lower than the cost-to-equity ratios as calculated on the MAARs generated by PHX's clearing firm. Despite those active trading letters, Representative 1 continued to recommend a short-term, high-volume strategy that was not in those customers' best interests.

## Supervisory Failures and Violations

### Failure to Supervise

21. As a result of the conduct described above, PHX failed reasonably to supervise Representative 1 during the Pre-Reg BI Period, within the meaning of Section 15(b)(4)(E) of the Exchange Act, with a view to preventing and detecting Representative 1's violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

**Reg BI Violations**

22. As a result of the conduct described above, PHX failed to comply with Rule 15*l*-1(a)(2)(ii)(C) under the Exchange Act, the quantitative prong of Reg BI's Care Obligation, and therefore willfully[2] violated Exchange Act Rule 15*l*-1(a)(2)(ii). The quantitative prong of Reg BI's Care Obligation requires a broker-dealer or its associated person to have a reasonable basis to believe that a series of recommended transactions, even if in a retail customer's best interest when viewed in isolation, is not excessive and is in the retail customer's best interest when taken together in light of the retail customer's investment profile and does not place the financial or other interest of the broker-dealer or its associated person ahead of the interest of the retail customer.

23. As a result of the conduct described above, PHX willfully violated Rule 15*l*-1(a)(2)(iv) under the Exchange Act, which requires a broker-dealer to establish, maintain, and enforce written policies and procedures reasonably designed to achieve compliance with Reg BI.

24. As a result of the conduct described above, PHX willfully violated Rule 15*l*-1(a)(1) under the Exchange Act.

**Disgorgement**

25. The disgorgement and prejudgment interest ordered in paragraph IV.C is consistent with equitable principles and does not exceed Respondent's net profits from its violations, and will be distributed to harmed investors to the extent feasible. The Commission will hold funds paid pursuant to paragraph IV.C in an account at the United States Treasury pending distribution. Upon approval of the distribution final accounting by the Commission, any amounts remaining that are infeasible to return to investors, and any amounts returned to the Commission in the future that are infeasible to return to investors, may be transferred to the general fund of the U.S. Treasury, subject to Section 21F(g)(3) of the Exchange Act.

**IV.**

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent PHX's Offer.

Accordingly, pursuant to Sections 15(b) and 21C of the Exchange Act, it is hereby ORDERED that**:**

A. Respondent PHX cease and desist from committing or causing any violations and any future violations of Exchange Act Rules 15*l*-1(a)(1), 15*l*-1(a)(2)(ii) and 15*l*-1(a)(2)(iv).

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[2] "Willfully," for purposes of imposing relief under Section 15(b) of the Exchange Act, "'means no more than that the person charged with the duty knows what he is doing.'" *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting *Hughes v. SEC*, 174 F.2d 969, 977 (D.C. Cir. 1949)).

B. Respondent PHX is censured.

C. Respondent PHX shall, within 14 days of the entry of this Order, pay disgorgement of $142,995.19, prejudgment interest of $24,993.85, and a civil penalty of $180,000.00 to the Securities and Exchange Commission. If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600 as to disgorgement and pursuant to 31 U.S.C. §3717 as to civil penalties.

Payment must be made in one of the following ways:

(1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;

(2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at http://www.sec.gov/about/offices/ofm.htm; or

(3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying PHX as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Thomas P. Smith, Jr., Division of Enforcement, Securities and Exchange Commission, New York Regional Office, 100 Pearl Street, Suite 20-100, New York, NY 10004.

D. Pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002, a Fair Fund is created for the disgorgement, prejudgment interest, and penalties referenced in paragraph IV.C. above. The Fair Fund may be combined with any other fund established in a parallel proceeding that may arise out of the same facts that the basis of this action. The amount ordered to be paid as a civil money penalty pursuant to this Order shall be treated as a penalty paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondent agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that it shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in

this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

By the Commission.

Vanessa A. Countryman
Secretary