ORIGINAL

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-15873

In the Matter of

THOMAS R. DELANEY II and
CHARLES W. YANCEY

Respondents.

POST-HEARING BRIEF OF RESPONDENT THOMAS R. DELANEY II

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

Regulations

Other Authorities

INTRODUCTION

The Division of Enforcement filed this case alleging a grand conspiracy motivated by finances and placing profits ahead of complying with SEC rules and regulations. After two weeks of trial, millions of dollars of experts' time and analysis, and countless hours of attorneys' analysis, presentation and argument, their case against Tom Delaney consist of the dubious theory that he would and did risk his entire career in order to facilitate the Stock Loan department keeping loans out just a few hours longer.

The Division's contention that Delaney even knew of Stock Loan's violations rests entirely on three pieces of evidence: the testimony of Rudy DeLaSierra, the testimony of Brian Gover, and an email on which Delaney was CC'd in which a low-level Stock Loan employee told a low-level Buy-Ins employee that Stock Loan was not to be bought in.

As documented below and demonstrated at the final hearing, DeLaSierra's testimony is unreliable because his original testimony on the matter doesn't support the SEC's theory, and in any event is contradicted by Johnson and Delaney, the two others who he said were parties to the conversations about which he testified. Gover's testimony about a meeting at which the 204 violations were discussed was contradicted by all three of the purported attendees at this meeting who testified at the final hearing: Holly Hasty, Delaney, and Michael Johnson. Both Gover's and DeLaSierra's testimony acquired by promises of leniency against the low-level wrongdoers in exchange for ever-changing testimony against front-office employees. Johnson, who the Division assured the Court would support their version but who did not have a cooperation agreement, did not support the Division and indeed said he did not know whether Delaney knew about Stock Loan's violations. Finally, the email, while speaking for itself, says almost nothing about Delaney's knowledge or intent. This is not the stuff of which cases are made. Because the evidence is thin, contradicted and weak, the Division has failed to meet its burden.

RELEVANT REGULATORY FRAMEWORK

I. Procedural History

The SEC adopted Regulation SHO in 2004 to govern short selling of securities.[1] Initially, Regulation SHO contained delivery requirements and "close-out" obligations only for certain "threshold securities," or securities experiencing a significant number of failures to deliver. During the 2008 financial crisis, the SEC became concerned about the effect of abusive naked short selling[2] on the stability of U.S. securities markets, including "possible unnecessary or artificial price movements stemming" from such activities.[3]

As a result of these concerns, on September 17, 2008, the SEC adopted Rule 204T of Regulation SHO as an "emergency temporary rule."[4] Rule 204T became an "interim final temporary rule" on October 17, 2008.[5] On July 27, 2009, the SEC adopted Rule 204, with an effective date of July 31, 2009.[6]

The close-out requirements of Rule 204T/204 substantially departed from the previous close-out requirements of Regulation SHO, including by applying to all "equity" securities and by imposing significantly compressed time-periods within which close-outs must take place.[7] Notwithstanding the significant changes, Rule 204T and Rule 204 were adopted without the

---

[1] Regulation SHO became effective on September 7, 2004 (Securities Exchange Act Release No. 50103 (July 28, 2004), 69 FR 48008 (August 6, 2004).

[2] In a "naked" short sale, the seller does not borrow or arrange to borrow the securities in time to make delivery to the buyer within the standard three-day settlement period. As a result, the naked short seller often fails to deliver the securities to a buyer when delivery is due.

[3] Release 34-58572, 73 FR 54875 (September 23, 2008) ("September Emergency Order").

[4] *Id.*

[5] Exchange Act Release No. 58733.

[6] Release No. 34-60388.

[7] *See* Paz report, Exhibit 829. The close-out date prior to adoption of Rule 204T/204 was 13 consecutive settlement days after the regular settlement date.

customary notice and comment periods.[8]

II. Requirements and Mechanics of Rule 204T/204

Rule 204T/204 is highly technical rule aimed at reducing "failures to deliver" in equity securities. The Rule requires "participant[s] of a registered clearing agency," such as Penson, to delivery of securities to a "registered clearing agency," such as NSCC, for the settlement of sales. However, the Rule applies to a participant's net settlement obligations in the NSCC's continuous net settlement ("CNS") system, i.e., the net number of shares in a security that Penson needs to deliver to the NSCC as a result of Penson's net position in that security in the CNS system on a given settlement day.[9] As stipulated by the parties:

> Rule 204T/204 requires participants of a registered clearing agency to deliver equity securities to a registered clearing agency when delivery is due; that is, by settlement date. As relevant here, settlement date is generally three days after the trade date ("T+3"). For short sales, if the participant does not deliver securities by T+3 and has a failure-to-deliver position at the clearing agency (also referred to as CNS fails/failures to deliver), at market open on the morning of T+4 it must take affirmative action to close out the failure-to-deliver position by purchasing or borrowing the securities of like kind and quantity by no later than the beginning of regular trading hours on the settlement day following the settlement date ("T+4"). For long sales, if the participant has a failure-to-deliver position at the clearing agency (also referred to as CNS fails/failures to deliver), at market open on the morning of T+6 it must take affirmative action to close out the failure-to-deliver position by purchasing or borrowing securities of like kind and quantity by no later than the beginning of regular trading hours on the third day following the settlement date ("T+6").[10]

Notably, the obligation to purchase or borrow close-out requirements on T+6 only apply

---

[8] *See* Exchange Act Release No. 58733, pp. 35-36; Release No. 34-60388, pp. 47-48.

[9] *See* Exchange Act Release No. 58733, pp.15-16; Release No. 34-60388, pp.20-24; *see also* Sirri Report, ¶46; *see also* Sirri Report, ¶¶10-70, which is incorporated herein in its entirety, for a detailed discussion of the CNS system, and its interplay with and effect on the requirements of Rule 204T(a)/204(a).

[10] (Stipulated COL 1, Tr. 2292:7 – 2293:15.) Permanent Rule 204 closely tracks the requirements of Rule 204T with some exceptions, including the notable addition of the right to "borrow" to close out a failure to deliver position under Rule 204(a). *Compare* 17 C.F.R. § 242.204T(a)(1) *with* 17 C.F.R. § 242.204(a)(1).

"*if* [Penson] has a failure to deliver position at" NSCC as of market open on T+6.[11] As such, anything that affects the clearing member's CNS position on an ongoing or "continuous" basis prior to the applicable close-out date can cure the failure to deliver.[12] This is acknowledged in the adoption release notes to Rule 204(a):

> In determining its close out obligation, a participant may rely on its net delivery obligation as reflected in its notification from NSCC regarding its security delivery and payment obligations, provided such notification is received prior to the beginning of regular trading hours on the applicable close-out date.[13]

Finally, although Rule 204T/204 was adopted "to help further [the] goal of reducing fails to deliver,"[14] persistent failure to delivers can be consistent with Rule 204 compliance.[15] For example, a purchase by Penson or by one of Penson's correspondent clients generates a "receive" in Penson's CNS system three settlement days after the purchase, i.e. a "settlement delay" of three days between execution and settlement of the trade.[16] Thus, a purchase to close out a failure to deliver position in a long sale executed before market open on T+6 generally will not cure a failure to deliver position at CNS until T+9, even though the clearing member is in full compliance with Rule 204T(a)/204(a).[17] Conversely, the return of shares pursuant to a recalled loan, even if not returned until the afternoon of T+6, cures a failure to deliver position on T+6. Indeed, the timing of *when* on T+6 (before market open or in the afternoon) shares are returned

---

[11] *See* Rule 204T(a)/204(a) (emphasis added).

[12] *See id. See also* Sirri Report, ¶¶10-70, which is incorporated herein in its entirety, for a detailed discussion of the CNS system, and its interplay with and effect on the requirements of Rule 204T(a)/204(a).

[13] Release 34-60388, n. 81; Exchange Act Release No. 58733, n. 46.

[14] Release 34-60388, p 1.

[15] *See* Sirri report, ¶¶65-67.

[16] Notably, all of the parties' experts acknowledge and agree on this settlement-delay effect. *See* Sirri Report, ¶¶62-67; Expert Report of Lawrence Harris, ¶115; Expert Report of Marlon Q. Paz (submitted by Yancey), pp. 14-15.

[17] *See* Sirri Report, ¶¶65-67; Paz Report, pp. 14-15. A similar analysis would be true for a purchase on T+4 or T+5, which, due to the settlement delay, would not close out the failure to deliver position until T+7 or T+8, respectively.

pursuant to a recall has no effect on the clearing member's CNS position.[18]

III. Long Sales of Loaned Securities

The Division's claims against Delaney stem solely from purported "systematic" violations of Rule 204T(a)/204(a) with respect to a specific type of transaction, which the Division calls "long sales of loaned securities." The Division does *not* contend that Penson violated Rule 204T(a)/204(a) through "naked" short selling, or other conduct.

According to the Division, a "long sale of a loaned security" occurs in the following situation: (1) a customer of Penson holds shares in a margin account pursuant to a margin agreement with Penson[19]; (2) Penson loans out, or re-hypothecates, those shares to another broker-dealer with whom Penson has entered into a securities lending agreement ("MSLA"); and (3) the margin customer thereafter sells those shares in a long sale. The re-lending of shares by broker-dealers is not improper in any way and is very common. If a customer sells shares that are out on loan, the broker-dealer can issue a recall notice to the borrowing counterparty, and the borrowing counterparty will return the shares. If the borrowing counterparty does not return the shares by market open on T+6, a Rule 204T(a)/204(a) close-out obligation may arise, provided Penson has not closed-out the CNS position in some other manner prior to T+6 market open.

LEGAL STANDARDS OF PROOF

The Division bears the burden of proof on all of its claims against Respondents Delaney and Yancey.[20] Specifically, "the Division has the burden of demonstrating by a preponderance

---

[18] Tr. 1033:3-18.

[19] Penson's customers are largely correspondent brokers. The individual account holder at the correspondent broker is the end customer. For purposes of this brief, and indeed this case, there is no need to make a distinction between Penson's customers (the correspondent brokers) and its customers' customers (the actual owner of the securities).

[20] COL 2, Hearing Transcript, 2533:4-7.

of evidence any wrongdoing by Respondents."[21]

Additionally, "if adjudicated facts are subject to competing inferences, the Division, as the party with the burden of proof, must establish that its inferences are more plausible than the respondent's inferences."[22] "If the record equally supports both innocent and culpable inferences, the Division fails in its burden of proof."[23] Furthermore, "[a]n adverse inference may be employed to complete a chain of reasoning on a point partially established by direct evidence, but it cannot be used to fill a void where there is otherwise no evidence."[24]

ARGUMENT

The Division has alleged that Delaney, "motivated by financial considerations," willfully aided and abetted and caused Penson's "overarching, intentional practice" and policy to "consistently" or "systematically" violate Rule 204T(a)/204(a) related to failures to deliver on long sales of loaned securities.[25] The Division has failed to prove its case.

I. The Division Failed to Prove that Delaney Aided and Abetted.

A. Elements of Aiding and Abetting.

"The 'rules for determining aiding and abetting [securities violations] are unclear, in an area that demands certainty and predictability.'"[26] In general, "[l]iability for aiding and abetting can be established by showing that the defendant joined the specific venture and shared in it, and that his efforts contributed to its success, or, in other words, by showing that the defendant

---

[21] *In the Matter of John J. Kenny & Nicholson/Kenny Capital Mgmt., Inc.*, 1999 WL 587947, *17, Release No. 147 (Aug. 6, 1999) (citing *Steadman v. SEC*, 450 U.S. 91, 102 (1981)).

[22] Stipulated COL 3; *In re H.J. Meyers & Co.*, 2002 WL 1828078 at *29.

[23] Stipulated COL 4, 2534:1-9; *In re H.J. Meyers & Co.*, 2002 WL 1828078 at *29

[24] *See Id.; accord Stanojev v. Ebasco Servs. Inc.*, 643 F.2d 914, 923-24 n.7 (2d Cir. 1981) (holding that an adverse inference cannot supply the missing element of a *prima facie* case).

[25] *See, e.g.*, OIP, ¶¶3-7, 10; Division's Memorandum in Opposition to Delaney's Motion for More Definite Statement, p. 4.

[26] *Howard v. SEC*, 376 F.3d 1136, 1142 (D.C. Cir. 2004) (quoting *Central Bank of Denver v. First Interstate Bank of Denver*, 511 U.S. 164, 188 (1994)).

consciously assisted the commission of the specific crime in some active way."[27] Furthermore, "[t]o establish that one Respondent willfully aided and abetted the violation of another, the Division must show that the aider and abettor acted with scienter."[28]

Specific to securities violations, the Division must prove each of the following three elements to establish aiding and abetting: (1) "a primary or independent securities law violation committed by another party"; (2) "awareness or knowledge by the aider and abettor that his or her role was part of any overall activity that was improper"; and (3) "that the aider and abettor knowingly and substantially assisted the conduct that constitutes the violation."[29] In addition, "willfulness" is shown where a person intends to commit an act that constitutes a violation.[30]

B. The Division has Failed to Adduce Any Evidence of Motive or Intent to Meet the Scienter Requirement.

To prevail on its aiding and abetting claim against Delaney, the Division must establish that Delaney acted with scienter. The Division has attempted to establish scienter by claiming that Delaney, motivated by profit or "financial considerations," intentionally and knowingly participated in a scheme to violate Rule 204T(a)/204(a).[31] As the Division knows, without a motive, none of Delaney's purported acts of concealment or assistance to further the alleged scheme to violate Rule 204T/204 make sense.

The Seventh Circuit Court of Appeal decision in *Barker v. Henderson, Franklin Starnes*

---

[27] *SEC v. DiBella,* 587 F.3d 553, 566 (2d Cir.2009) (quotations and citation omitted).

[28] Stipulated COL 5; *accord In re H.J. Meyers & Co.*, 2002 WL 1828078 at *28 (citing *271*

, 53 S.E.C. 1060, 1070 n.26 (1998)).

[29] *See Graham v. SEC,* 222 F.3d 994, 1000 (D.C. Cir. 2000); *Woods v. Barnett Bank of Ft. Lauderdale*, 765 F.2d 1004, 1009 (11th Cir. 1985) ; *Investors Research Corp. v. SEC*, 628 F.2d 168, 178 (D.C. Cir. 1980); *Woodward v. Metro Bank of Dallas,* 522 F.2d 84, 94-97 (5th Cir. 1975); *Russo Sec. Inc.,* 53 S.E.C. 271, 278 & n.16 (1997).

[30] Stipulated COL 6; *Wonsover v. SEC, 205 F.3d 408, 414* (D.C. Cir. 2000); *Arthur Lipper Corp. v. SEC*, 547 F.2d 171, 180 (2d Cir. 1976).

[31] *See* OIP, ¶¶5, 7.

and Holt is instructive.[32] In *Barker,* the plaintiffs, purchasers of securities, brought claims against a law firm and accounting firm alleging that they aided and abetted an issuer to defraud plaintiffs in the purchase of securities.[33] In affirming summary judgment for the defendant law firm and accounting firm, the Seventh Circuit observed:

> A plaintiff's case against an aider, abettor, or conspirator may not rest on a bare inference that the defendant "must have had" knowledge of the facts. The plaintiff must support the inference ***with some reason to conclude that the defendant has thrown in his lot with the primary violators***.[34]

"[T]he court should ask whether the fraud (or cover-up) was in the interest of the defendants. ***Did they gain*** by bilking the buyers of the securities?"[35] In applying these principles, the Seventh Circuit held:

> In this case the ***Firms did not gain***. They received none of the proceeds from the sales. They did not receive fees for rendering advice in connection with the sales to the plaintiffs. Both Firms billed so little time to the Foundation between 1974 and 1976 (and none after October 1976) that ***it is inconceivable that they joined a venture to feather their nests by defrauding investors. They had nothing to gain and everything to lose***. There is no sound basis, therefore, on which a jury could infer that the Firms joined common cause with other offenders or aided and abetted a scheme with the necessary state of mind.[36]

So it is here. The Division contends that Penson's Stock Loan Department instituted a policy and practice of intentionally and consistently violating Rule 204(a) with respect to closing out long sales of loaned securities for financial gain. The Division has presented no direct evidence of scienter—no written or oral admissions or other such evidence knowing and willful

---

[32] *See Barker v. Henderson, Franklin Starnes and Holt,* 797 F.3d 490 (7th Cir. 1986).

[33] *See id.* at 492

[34] *Id.* at 497 (emphasis added); *accord Howard,* 376 F.3d at 1143 (observing, "aiding and abetting liability cannot rest on the proposition that the person 'should have known' he was assisting violations of the securities laws.").

[35] *Id.* (emphasis added) (citing *Dirks v. SEC,* 463 U.S. 646 (1983)).

[36] *Id.*

participation—to support its claim that Delaney aided and abetted the alleged scheme with the necessary mental state.

As a result, the Division has attempted to invent a role for Delaney in the purported scheme to violate Rule 204T(a)/204(a). Specifically, the Division has attempted to twist the fact that Delaney did not stop the Rule 204 violations into creating an adverse inference that Delaney was a part of the violations. The Division contends Delaney "aided and abetted" Penson to violate Rule 204T/204 by: (a) agreeing with Stock Loan to continue implementing non-compliant procedures; (b) intentionally omitting Stock Loan's "non-compliant" procedures in Penson's WSPs; (c) intentionally concealing the "non-compliant" procedures from regulators and Penson's president/CEO, Yancey; and (d) creating a "Supervisory System" that would allow Johnson to remain unsupervised.[37] Notably, the Division's allegations of Delaney's duplicity are based on Delaney's purported inaction and also exactly what one would expect of a CCO who was unaware of any purported illegal practice or policy.

Furthermore, because Delaney's purported role in the alleged scheme is so complex and involved, the Division knew it needed a motive to tie the disparate acts together and provide "some reason to conclude that [Delaney] has thrown in his lot with the primary violators."[38] The Division thus concocted a theory that Delaney was "motivated by financial considerations" and "consciously chose profits over compliance."[39]

The Division presented no evidence that Delaney directly or indirectly received any personal benefit from the violations at issue. Rather, the Division attempted to establish a motive as to Delaney by asserting a possible financial incentive to Penson. For example,the

---

[37] *See* OIP, ¶¶37-42, 52-53, 60, 64, 68.

[38] *Barker,* 797 F.3d at 497.

[39] *See* OIP, ¶¶7, 39.

Division offered an expert report from Professor Lawrence Harris, which calculated the purported "benefit" and "gain" to Penson from violating Rule 204T(a)/ 204(a) at approximately $6.2 million.[40] Presumably, the Division hoped that if it put a large enough number before the Court, it could justify an inference that Stock Loan and Delaney chose Penson's profits over compliance, even in the total absence of any evidence of personal benefit.

The Division's attempt to use a possible profit motive to Penson to establish a motive or benefit to Delaney confuses the issue. There must be a personal incentive to Delaney himself,[41] particularly where there is no evidence that Delaney has any history of disciplinary actions or violations, and where there is no evidence that his compensation was tied to either Stock Loan's or Penson's revenue.[42] Moreover, the Division has also failed to provide any credible evidence of a financial incentive to *Penson* to violate Rule 204T(a)/204(a), let alone for Delaney. There is no witness testimony to support the existence of a profit motive to violate Rule 204T/204(a). Both Johnson and DeLaSierra confirmed there was no profit motive or economic incentive.[43]

Delaney's expert, Professor Erik Sirri, also conclusively established that the $6.2 million figure resulted from a simple calculation error that caused Professor Harris to overstate the purported benefit by a factor of 100.[44] Professor Harris admitted this error (among others) on the

---

[40] *See* Ex. 239, ¶¶26, 132, and Ex. 1 thereto.

[41] *See Barker,* 797 F.3d at 497; *cf. In re Axis Capital Holdings Ltd. Securities Litig.,* 456 F.Supp.2d 576, 594 (S.D.N.Y.2006) (generalized allegations that can be attributed to any business endeavor, such as the desire to make a profit and maintain business relationships, are insufficient to set forth a motive to aid and abet fraud); In re Bear Stearns Companies, Inc. Sec., Derivative, & ERISA Litig., 763 F. Supp. 2d 423, 499 (S.D.N.Y. 2011) (observing, "[m]otives that are generally possessed by most corporate directors and officers do not suffice; instead, plaintiffs must assert a concrete and personal benefit to the individual defendants resulting from the fraud." (quotation and citations omitted)); *In re PXRE Grp., Ltd., Sec. Litig.,* 600 F.Supp.2d 510, 530–33 (S.D.N.Y.2009) (indicating, that to be indicative of scienter, the allegations must move the desire to raise capital beyond the realm of the generic by illustrating some concrete and personal benefits defendants sought to attain).

[42] *See* Delaney FOF 12.

[43] *See* Delaney FOF 72.

[44] *See* Ex. 454, Sirri Report, ¶¶74-78. In calculating the alleged benefit, Professor Harris treated interest rate percentages as if they were whole numbers, i.e., if one calculated five percent of a number by multiplying the number by the integer 5. In fact, calculating five percent of a number requires multiplying by .05. (*See id.*) This

witness stand, and confirmed the correctness of Professor Sirri's analysis.[45] The Division thereafter conceded that the only specifically quantified benefit to Penson from not timely closing out at market open on T+6 was $59,000, over the entire three-year relevant period.[46] This calculation error undermines the Division's entire case because it defeats any finding of incentive or motive, as against Delaney or Penson.

The Division concedes that the revenue of Penson's Stock Loan Department during the relevant period was approximately $77,000,000, or $100,000 per day.[47] Conversely, the total benefit to Penson from the alleged Rule 204 violations at issue is $77.00/day, [48] or approximately .08% of Stock Loan's total revenue during the relevant period. Indeed, the $59,000 amount is far less than the approximately $500,000 amount the Division paid Professor Harris and his consulting firm to prepare the report.[49] The total financial picture leads to the conclusion that the Division was so desperate to identify some motive that it ignored red flags demonstrating Harris's calculation could not be accurate. [50] Although the Division continues to insist there are other benefits, they are not quantified, and thus there is no proof they actually

---

type of error undermines the reliability of any of the conclusions in Professor Harris's report. *See In re H.J. Meyers & Co.*, SEC Release No. 211; AP File no. 3-10140, 2002 WL 1828078, *45-46 (observing that, while *Daubert v. Merrell Dow Pharm., Inc.*, 509 U.S. 579 (1993); *Kumho Tire Co. v. Charmichael*, 526 U.S. 137 (1999), "were decided in the context of admissibility, [] the principle for which they stand—that all expert testimony must be reliable—should apply with equal force to the weight a[n agency] factfinder accords expert testimony.")

[45] *See* Tr. 1002:1-9, 17-22.

[46] *See* Stipulated FOF 53.

[47] *See* Stipulated FOF 79.

[48] *See* Delaney FOF 92.

[49] *See* Delaney FOF 93.

[50] Stock Loan's total revenue during the relevant period was $77 million. The $6.2 million figure thus represented approximately 8% of Stock Loan's total profits during this period, whereas the number of Rule 204 violations it was based on (less than 1700) is only approximately .7% of all positions related to long sales of loaned securities. This hugely disproportionate ratio of the profit to violation should have been obvious to the Division and its expert. Moreover, the $6.2 million figure was a *single day* calculation. By definition all of those loans had been out at least 6 days, meaning that Penson would have generated approximately $37,200,000, just over 48% of Stock Loan's total revenue, from just the approximately 1,700 positions identified by Professor Harris. These numbers so clearly did not make sense that the Division must have ignored these red flags in their need to establish a motive.

exist.[51]

It strains credulity to believe that anyone at Penson would implement a policy or practice to intentionally violate Rule 204T(a)/204(a) to obtain such a *de minimus* benefit for Penson. It is even more difficult to imagine any incentive for Delaney to conspire with persons, with whom he was not close and with whom he shared no financial interest, to "willfully" and systematically violate the law, mislead regulators and his boss, and doctor WSPs, all to augment the Stock Loan Department's bottom line[52] by eight-one-hundredths of one percent. It is not plausible that Delaney would shape his entire role as Penson's CCO or jeopardize his twenty-year career in the securities industry to perpetuating a scheme from which he would receive no benefit.

The relevant question for scienter is "What did Delaney stand to 'gain' from the primary violation?" As in *Barker,* the evidence establishes that Penson did not materially gain, and that Delaney, who received no portion of the $59,000, "did not gain" at all.[53] Similar to the defendants in *Barker,* Delaney "had nothing to gain and everything to lose."[54] Given this, as in *Barker,* it is simply "inconceivable that [Delaney] joined a venture to feather [his] nest[]" by violating Rule 204T(a)/204(a). [55] Accordingly, there is "no sound basis . . . [to] infer that [Delaney] joined common cause with other offenders or aided and abetted a scheme with the necessary state of mind."[56] The claim should be dismissed.

---

[51] For example, the Division may assert that Penson benefited by avoiding the costs of buying-in shares on the morning of T+6. But there is no evidence to establish what those costs may have been, and thus this assertion is based on pure speculation. Furthermore, the Division has not established that any of the shares at issue did not increase in value during the day, and could not have been sold at a profit the next day to offset any costs. *See* Tr. 427:25-428:7. This type of calculation would be easy to do from the trading records. That the Division did not undertake this effort is compelling evidence that it did not support their position.

[52] Of course given that Stock Loan was just one – and not even the largest – revenue generating department of Penson, the percentage of Penson's combined bottom line would be even smaller.

[53] *See Barker,* 797 F.3d at 497.

[54] *Id.*

[55] *Id.*

[56] *Id.*

C. The Primary Violation

Respondents have stipulated that, after a three-year investigation costing millions of tax-payer dollars, there were 1,500 violations of Rule 204T(a)/204(a) by Penson relating to long sales of loaned securities during the relevant period. However, this does not end the inquiry because the Division's case is not based on isolated technical violations of Rule 204T(a)/204(a), but rather an alleged "systematic, intentional practice of violating Rule 204(a) on failures to deliver related to long sales of loaned securities."[57]

The 1,500 number must therefore be read in context with other evidence. It is undisputed that during the relevant time period, Penson cleared at least one billion securities transactions, or between 3-5 million per day.[58] Of these one billion, there were a total of 83.6 million long sale transactions potentially[59] associated with loaned shares.[60] Stated differently, during the relevant time period, there were approximately 230,000 CNS net sell settling positions associated with long sales of loaned shares.[61] Each of the 230,000 CNS net sell settling positions created close-out obligations that needed to be satisfied under Rule 204T(a)/204(a).[62]

---

[57] Division's Opposition to Delaney's Motion for More Definite Statement, June 19, 2014, p. 5; *see also* Division's Opposition to Delaney's Motion for Postponement, p. 7 (emphasis added); see *also id.* p. 6 ("The Division has alleged that Penson's Stock Loan department instituted a policy and practice of intentionally and consistently violating Rule 204(a) with respect to a particular type of transactions—long sales of loaned securities. (*See, e.g.,* OIP, ¶¶3-5, 22-24.); Division's Opposition to Motion for More Definite Statement, p. 5 ("In sum, Delany does not need detailed trading information to inform him of the charges against him, which are centered on his aiding and abetting Penson's systematic, intentional practice of violating Rule 204(a) on *all* failures to deliver related to long sales of loaned securities."(emphasis added)).

[58] *See* Stipulated FOF 50; *See also* Tr. 165:24-166:7

[59] Dr. Sirri, whose calculations form the basis for this stipulated finding of fact, testified that the term "potentially" is used because the 83.6 million figure was calculated using Professor Harris' methodology. If that methodology was wrong, the number could be different. *See* Tr. 1615:19-1616:2

[60] *See* Stipulated FOF 51.

[61] *See id.*

[62] A "CNS net sell settling position" is a position where Penson owes delivery to CNS of a particular share type, after aggregation (or "netting") of the buying and selling activity in that share type for a particular day. A CNS net sell settling position thus means that Penson processed more sells than buys (or delivers vs. receives from CNS) in that share type for a given day, and thus it owes CNS shares. *See* Tr. 1613:12-1615:18

Out of these numbers, the Division identified only 1,500 negative CNS positions that were Rule 204T(a)/204(a) violations relating to long sales of loaned securities from October 1, 2008 through November 1, 2011, or approximately two per day.[63] The 1,500 violations represent only 0.68% of the total number of Penson's CNS net sell settling positions potentially associated with loaned shares or 0.12% of the 83.6 million long sale transactions during the relevant period.[64] It is thus not disputed that Penson's actual rate of compliance with Rule 204T(a)/204(a) for long sales of loaned securities, during the relevant period, was 99.32% (by CNS net sell settling positions) or 99.88% (by transaction). Where Penson cleared between three to five million shares per day, the number of violations is both tiny and inconsequential.

D. Delaney Was Not Aware of Any Wrongdoing.

Assuming the Court determines that a primary violation occurred, the next question, and the most important issus in this case, is when Delaney discovered that the Stock Loan Department was violating Rule 204T(a)/204(a) with respect to closing-out long sales of loaned securities. Not only is "awareness of the wrongdoing" a separate element of aiding and abetting that must be met, but all of the Division's alleged acts of substantial assistance are premised upon Delaney's purported knowledge of the violations by Stock Loan. Here, the weight of the evidence establishes that Delaney did not know of any consistent "policy" or "practice" by Stock Loan to violate Rule 204T(a)/204(a) until March of 2011—after the February 15, 2011 the date on which the Division concedes that any substantial assistance by Delaney ceased.

1. Legal Standards.

The second element of aiding and abetting requires the Division to establish "awareness or knowledge by the aider and abettor that his or her role was part of any overall activity that was

[63] *See* Stipulated FOF 49, 52

[64] *See* Stipulated FOF 51-52.

improper." [65] "Awareness of wrongdoing means knowledge of wrongdoing."[66] "In analyzing this second element, 'the surrounding circumstances and expectations of the parties are critical. If the alleged aider and abettor conducts what appears to be a transaction in the ordinary course of his business, more evidence of his complicity is essential.'"[67] In addition, "[s]atisfaction of the [knowledge] requirement will ... depend on the theory of primary liability."[68] The "'awareness of wrong-doing requirement' in aiding and abetting disciplinary cases was 'designed to insure that innocent, incidental participants in transactions later found to be illegal are not subjected to harsh . . . administrative penalties.'"[69]

In addition, the Division cannot rely on recklessness (that Delaney "should have known") to establish the awareness. Rather, "[k]nowledge of the wrongdoing must be proven."[70] The D.C. Circuit made this clear in observing,"[w]e are willing to assume that the SEC thought - *incorrectly* - that reckless conduct amounted to a form of awareness of wrongdoing."[71]

2. The Division Produced No Credible Evidence that Delaney Knew About the Allegedly "Systematic" Rule 204T(a)/204(a) Violations At Issue Before Approximately March of 2011.

Delaney and the Division have produced conflicting evidence on the issue of when Delaney became aware of any issues in closing out long sales of loaned securities.[72] The Division claims Delaney knew that Stock Loan was consistently violating Rule 204T(a)/204(a)

---

[65] *See Graham v. SEC,* 222 F.3d 994, 1000 (D.C. Cir. 2000).

[66] *Howard,* 376 F.3d at 1142.

[67] *SEC v. Morris,* (S.D. Texas, 2005)2" \s "WSFTA_14a33d7c670844f48c8437280f6d4a36" \c 3 *SEC v. Morris,* 2005 WL 2000665 *8 (S.D. Texas, 2005) (quoting *Woodward v. Metro Bank of Dallas,* 522 F.2d 84, 95 (5th Cir. 1975).

[68] *SEC v. DiBella,* 587 F.3d 553, 566 (2d Cir. 2009) (quotations and citation omitted).

[69] *Id.* (citation omitted).

[70] *Id.* at 1143.

[71] *Id.* (emphasis added). Moreover, as indicated below, the Division has failed to establish that Delaney acted recklessly.

[72] A timeline of the knowledge element is attached to Delaney Findings of Fact.

with respect to long sales of loaned securities during the entire relevant period. The Division's argument should be rejected as it relies entirely on thin, contradicted, internally inconsistent and unreliable, testimony from cooperating witnesses who hope to gain concessions from the Division as a result of their testimony.

In its prehearing brief, the Division assured the Court that "numerous witnesses will confirm" that "Delaney was told—early and often—that PFSI's Stock Loan group was not closing out fails on long sales of loaned securities by market-open of T+6."[73] The Division then clarified that, by "numerous," it meant three: Michael Johnson, DeLaSierra, and Gover.[74] As demonstrated below, DeLaSierra and Gover are unreliable and Johnson did not support the Division's story.

a. *Johnson did not testify as the Division claimed.*

In its Pre-Hearing Brief, the Division claimed Johnson would testify that he "recalls numerous conversations where he made clear to Delaney that Stock Loan was not closing out by market-open on T+6."[75] Johnson gave no such testimony at the final hearing. For example, the Division had the following colloquy with Johnson after showing him Ex. 89 (Penson's FINRA response from March 18, 2011):

> **Q** **Okay. So, Mr. Johnson, this is a response by Penson in March of 2011 with respect to Rule 204, and it says, "With regards to the timing of long-sale closeouts, the firm does not believe that it is industry practice to close out long sales prior to the market open on T+6."**

[73] *See* Division's Pre-Hearing Brief, p. 13.

[74] *See id.* Delaney further notes that, in its Pre-Hearing Brief, the Division also vaguely indicated that "DeLaSierra *and others in Stock Loan* explained that they were not closing out fails by market-open on T+6." *See id.*, n. 8 (emphasis added). The Division undertook no effort, either in its brief or at the final hearing, to identify these "others in Stock Loan." Certainly, the Division offered no such testimony from the "others" at the final hearing, and the Division knew before the hearing that one possible "other," Hall, directly undermined its story, as the Division indicated this in a Brady letter. That the Division felt the need for "others"—where it must have known they did not exist—to corroborate their story is a telling admission that the Division felt its position was weak.

[75] *See* Division's Pre-Hearing Brief, p. 13.

And a couple of sentences later it says, Thus, the firm executes closeouts versus long sales at the conclusion of the DTCC trading window at approximately 3:00 Eastern Standard Time daily. Is that an accurate description of Stock Lending's practices?

A Yes.

* * *

Q And let me ask you generally, and then we'll talk specifically. Was Mr. Delaney aware that those practices we just saw in Exhibit 89 were how Stock Loan was operated?

A I don't know.

* * *

Q All right. Well, let me ask you this: Did you have any conversations with Mr. Delaney, Mr. Johnson, about Rule 204?

A Yes.

* * *

Q And as you sit here today, in substance, what were the conversations between you and Mr. Delaney? What did you say to him?

A I don't know. They were fast.

Q Okay. And what do you mean by "fast"?

A Hallway conversations, quick conversations. I ran Global; so they were fast in coming, looking for support.

Q In those conversations, did you discuss with Mr. Delaney resistance that Stock Lending was getting to trying to buy in, in the morning of T6?

A I believe so.

Q And what do you believe you discussed with Mr. Delaney on that point?

A I believe we talked about Lindsey Wetzig calling counterparties trying to get a definition of when to do this, and they said it was industry practice, and by us not doing it the old way, we were violating our MSLA agreement.

* * *

Q All right. Do you believe you communicated with Mr. Delaney that your practice was to buy in at the end of market?

A I believe we communicated we had a conflict between those two.

Q Between the rule and the industry practice?

A Yes, sir.

Q And what, as you recall, did Mr. Delaney say in response to you pointing out that conflict?

A I don't know what he said to me specifically. I believe he arranged a meeting with Rudy De La Sierra's staff and Morgan Lewis.[76]

The only evidence in the record of a meeting between Stock Loan, Delaney and Morgan Lewis occurred in February of 2011,[77] at which time the Division has conceded any purported acts of substantial assistance ceased.[78] During cross-examination, when asked whether Stock Loan was getting push back from counterparties, Johnson stated "I don't recall." [79]

Accordingly, Johnson did not testify as the Division claimed he would—that he had "numerous conversations where he made clear to Delaney that Stock Loan was not closing out by market-open on T+6."[80] At most, he testified that he told Delaney Stock Loan's

[76] *See* Tr. 517:5-520:2.

[77] *See* Delaney FOF 87.

[78] *See* Stipulated FOF 58.

[79] *See* Tr. 533:10-20.

[80] *See* Division's Pre-Hearing Brief, p. 13.

counterparties were pushing back on recalls and that Stock Loan believed that industry practice was not consistent with the rule. However, on the key issue — the only issue of consequence to the resolution of this case — Johnson testified that he did not know whether Delaney knew that Stock Loan was not closing out by market open on T+6. Notably, of the three witnesses the Division presented on this issue, only Johnson has both settled with the Division and has no agreement to cooperate.[81]

As the head of Stock Loan, Johnson was also in the best position to take issues directly to Delaney as Penson's CCO for guidance. According to Wetzig, a manager in Stock Loan, Johnson developed Stock Loan's procedures for closing out long sales of loaned securities under Rule 204, and was "the guy who ultimately told us [Stock Loan] what to do."[82]

Moreover, although Johnson is unclear on whether he discussed counterparty resistance to Rule 204 with Delaney, even assuming Johnson did have such conversations with Delaney, they would not put Delaney on notice or raise concerns that Stock Loan was not complying with Rule 204 because as Delaney testified he understood that, "if you're are following the rule, you're getting counterparty pushback."[83]

In sum, Johnson does not support the Division's contention that Delaney knew Stock Loan was not timely closing-out long sales of loaned securities in accordance with Rule 204. Rather, his testimony further confirms that Delaney was not aware of any misconduct.

b. *DeLaSierra's Testimony is Not Credible.*

In its Pre-Hearing Brief, the Division claimed DeLaSierra would testify that "Delaney was told about the practice [of not closing out fails on long sales of loaned securities by market-

[81] *See* Delaney FOF 88.

[82] *See* Tr. 389:11-20.

[83] *See* Tr. 1195:11-12.

open T+6] at around the time Rule 204T was enacted in late 2008."[84] However, DeLaSierra's testimony is inconsistent and has evolved over time and in any event is derivative of Johnson's conversations with Delaney and therefore cannot provide a stronger basis for liability than Johnson's testimony during the hearing. DeLaSierra's testimony became much more favorable and helpful to the Division as he negotiated and executed a cooperation agreement with the Division, in exchange for which the Division agreed to seek "lesser charges and/or remedies," even though DeLaSierra was one of the members in Stock Loan who was directly responsible for any Rule 204T(a)/204(a) violations at issue.[85]

DeLaSierra provided testimony, under oath, three separate times in this matter: (1) investigative testimony in Spring of 2012; (2) investigative testimony in 2013; and (3) at the final hearing.[86] He confirmed that his memory was better closer in time to the events in question, i.e. during his first testimony.[87] During his first testimony, which occurred before his cooperation agreement, DeLaSierra testified that no one in the Stock Loan Department, including himself, consulted with anyone in the Compliance Department at the time Rule 204T came out. DeLaSierra further testified in 2012 that Compliance was not aware of the violative practice until beginning of 2011:

> Q **Now, you -- you were also asked during that testimony if -- if anyone from Compliance was aware of this practice. Is that right?**
>
> A Yes.
>
> * * *

[84] *See* Division's Pre-Hearing Brief, p. 13.

[85] *See* Ex. 446, ¶28.

[86] *See* Tr. 250:10-251:1.

[87] *See* Tr. 251:2-5.

Q **And -- and the meeting you mentioned, you said it was the beginning of last year, which again you were testifying in 2012. Right?**

A Right.

Q **So you mentioned a meeting in the beginning of 2011.**

A Yes.

Q **And -- and that's the meeting that you testified about when you were asked how it was that Compliance was aware, how you knew Compliance was aware of this practice?** [88]

Notably, this testimony is consistent with the accounts of other members of Stock Loan, including Wetzig and Hall, who both indicated that they did not ask Delaney or others in Compliance for help or guidance on Rule 204 prior to 2011.[89]

At his next testimony, however, DeLaSierra testified that he "and/or" Johnson met with Delaney to discuss "severe counterparty pushback" in 2008.[90] At the final hearing, DeLaSierra defined "and/or" to mean both or either; you don't really know.[91]

Subsequently, years later at the final hearing when he acknowledged his memory of events was worse than it had been before, DeLaSierra's story changed again. Now, he suddenly remembered that both he and Johnson were at one or more meetings with Delaney in 2008 to discuss counterparty pushback to executing buy-ins at market open on T+6.[92] Even then, DeLaSierra confirmed that Delaney never told Stock Loan not to comply with Rule 204T/204.[93]

---

[88] Tr. 266:11-267:11

[89] *See* Ex. 446 (indicating "Hall told the Division that he did not ask legal or compliance for help with figuring out a way to comply with Rule 204 until the beginning of 2011"); Tr. 402:4-403:11, 410:21-411:2 (Wetzig).

[90] Tr. 267:15-23, 268:25-270:3.

[91] Tr. 263:13-264:5; *See also* Delaney FOF 34.

[92] Tr. 270:14-271:7.

[93] Tr. 271:19-23; 272:24-273:3.

DeLaSierra's explanation for why he believes that Delaney "knew [Stock Loan] was not buying in at the [market] open" of T+6 is also highly dubious:

> Q **How -- when you say he knew we weren't buying in at the open, what do you mean?**
>
> A Mike had told him already that we -- our counterparties were not accepting morning buy-ins, and we were -- we were going -- we were -- we were the [sic] lost counterparties, and we tried to buy in against the recall letter or the MSLA, the securities loan agreement.
>
> **Q Okay. How does any of that inform [Delaney] that you're -- that you're not buying in at the open?**
>
> A Well, we still have counterparties.
>
> **Q But your counterparties don't stop you from buying in at the open?**
>
> A No, they don't. [94]

Taken at face value it is very difficult to understand how this information should have alerted Delaney that Stock Loan was violating Rule 204T(a)/204(a) with respect to long sales of loaned securities. This is far from direct knowledge and would require Delaney to make a number of inferential leaps that he could not be reasonably expected to make, particularly where DeLaSierra confirmed that counterparty pushback would not have stopped Stock Loan from buying-in at market open to satisfy Rule 204T/204. While DeLaSierra was emphatic in his conclusory testimony that Delaney knew, when asked an open-ended question on cross examination probing the basis for Delaney's alleged knowledge, he provided a non sequitur in lieu of a factual foundation for his conclusion.

Furthermore, DeLaSierra's inferences and testimony at the final hearing are contradicted not only by his own prior testimony but by several other witnesses. For

[94] Tr. 272:10-23.

example, Delaney flatly contradicts DeLaSierra's testimony.[95] In addition, Johnson, who DeLaSierra claimed was present the meetings with DeLaSierra and Delaney, said he did not know if Delaney was aware of Rule 204T/204 violations by Stock Loan.[96]

Finally, Alaniz, the compliance officer who conducted the Rule 3012 testing[97] of Rule 204, impugns DeLaSierra's credibility. For example, DeLaSierra claims that he had never discussed what Rule 204 required with Alaniz in connection with the 3012 audit in 2009.[98] Alaniz, however, said that after he told Hall and DeLaSierra that Rule 204 required long sales to be closed out by market open on T+6, DeLaSierra initially disagreed with Alaniz's interpretation.[99] Alaniz responded to DeLaSierra's refusal to agree with Alaniz's interepretation by telling DeLaSierra to review the Rule again overnight and they would meet again the next day. DeLaSierra ultimately agreed with Alaniz's interpretation of the requirements of the rule.[100] At no point did DeLaSierra, or anyone else from Stock Loan for that matter, ever tell Alaniz Stock Loan's actual practice was different from Alaniz's understanding of the requirements of the rule. [101] And, neither DeLaSierra nor anyone else ever told Alaniz, "Hey, we met with Tom Delaney and he told us that we don't need to comply with your interpretation of the Rule."[102]

Alaniz's testimony is highly credible; he is one of the few purely disinterested witnesses, with no cooperation agreement. It makes no sense that Alaniz would make up

---

[95] *See* Delaney FOF 26.

[96] *See* Delaney FOF 35.

[97] Timeline of Alaniz's 3012 testing is attached to Delaney's Findings of Fact.

[98] Tr. 264:20-265:7; *See also* Delaney FOF 33.

[99] Tr. 750:5-752:10; *see also* Delaney FOF 28-29.

[100] *Id.*

[101] Tr. 752:11-23.

[102] Tr. 752:24-753:5.

the meetings with DeLaSierra. DeLaSierra, however, has a motive to deny meeting with Alaniz because Alaniz contradicts DeLaSierra's story that Delaney knew. If DeLaSierra truly believed that Delaney, and therefore the Compliance department, was aware that Stock Loan was not closing out, DeLaSierra would have had no reason not to have disclosed that practice to Alaniz. Nor would he have had a motive to feign a misunderstanding of the requirements of the rule in his initial meeting with Alaniz related to Rule 3012 testing of Rule 204.

The most plausible understanding of the entire context surrounding DeLaSierra is that he knew that Delaney, and others in Compliance, were not aware of any non-compliant Rule 204 practices by Stock Loan, and that Stock Loan kept them concealed because they knew Compliance would not tolerate rule violations if they knew.[103] As indicated above, there is simply no incentive for Delaney, or anyone in Compliance, to look the other way. Any inconsistent testimony by DeLaSierra at the final hearing is simply not believable.

c. ***Gover's Testimony is Not Reliable.***

The final witness the Division offered to try to prove Delaney knew of Stock Loan's "violative practice," was Gover—the supervisor of Penson's Buy-In Department from approximately mid 2009 through 2011. Similar to DeLaSierra, Gover is a registered person, who claims he knew about Stock Loan's violative practice, but who has not been charged by the Division and who has instead executed a cooperation agreement for favorable treatment.[104]

At the final hearing, Gover testified that he recalled a meeting with Delaney discussing a Rule 204 issue arising from Stock Loan's position that they "don't get bought in," and that he

---

[103] *See* Delaney FOF 56.

[104] *See* Delaney FOF 15; *see also* Ex. 446, ¶28.

believed that to remedy the situation, Stock Loan needed to recall earlier.[105] Gover claimed that he, Delaney, Hasty, Johnson, and potentially DeLaSierra and Hall were present at the meeting.[106] Gover's description of the alleged participants in the meeting must have surprised the Division, who argued in its Pre-Hearing Brief that only Delaney, Johnson and Gover were present.[107] Gover claimed that although he believed Stock Loan's position conflicted with Rule 204, there was no resolution of the conflict at the meeting, and the response was to seek the opinion of outside counsel.[108] Although he was not sure when the purported meeting occurred, he believed it occurred sometime before the email chain in Ex. 91 (July of 2010).[109]

Gover's testimony about this meeting is contradicted by everyone who he said attended the meeting. Delany, Hasty and Johnson all denied that any meeting matching Gover's description occurred.[110] Indeed, Hasty not only denied it, but testified that Delaney's purported response of doing nothing in the face of a violation of a rule was out of character, and she would have expected him to "immediately say, [t]hat's not an acceptable solution, and he would have escalated it further."[111] Further, Gover testified that the outcome of the meeting was a call or meeting with outside counsel to discuss Rule 204 issues, which everyone acknowledges occurred in February of 2011.

Gover's memory of the timing of the purported meeting is also *admittedly* unreliable:

> **Q** **Okay. Let me ask, you're sitting here today. It's been how long since -- since the date of the meetings that you described with Mr. Delaney?**

[105] Tr. 103:6-106:1, 144:1-20.

[106] Tr. 104:9-14; *See* Delaney FOF 16.

[107] *See* Division's Pre-Hearing Brief, p. 13.

[108] Tr. 106:2-6.

[109] *See* Delaney FOF 16.

[110] *See* Delaney FOF 17-19.

[111] Tr. 1757:8-16; *See also* Delaney FOF 13.

A In the range of five years.

Q Okay. And how clear would you say your memory is of the dates of those meetings?

A You know, I think, you know, I can pretty accurately within nine months, but, you know, ***I would not be able to reliably say, yeah, at this point.***[112]

Gover's testimony on the date of the alleged meeting is also contradicted by other evidence. For example, if as he claims, the meeting occurred before the July 2010 email in Ex. 91, it does not make sense that Gover would not have mentioned that he had met with Delaney and Hasty previously, and they were seeking the advice of counsel on the issue. For that matter, it does not make sense that Delaney and Hasty also would not have mentioned Gover's meeting on the very issue being discussed in the July 2010 email exchange. That none of the alleged participants in the meeting mentioned it when faced with an email on the very topic, suggests the meeting never took place, or at the very least did not take place at the time Gover recalls it.

Furthermore, Gover was also present for a 3012 certification meeting on March 31, 2010, to discuss the results of the Compliance Department's 3012 testing of Rule 204.[113] During that meeting, Gover was asked extensively by his supervisor, John Kenny, about the results of, and remediation for the 3012 test results, showing late buy-ins on 112 out of 113 failure positions.[114] Curiously, at the final hearing, Gover did not recall the 3012 meeting, and finds it "hard to speculate" on a "conversation that may or may not have happened five years ago,"[115] but inconsistently claims to recall the details of a purported Rule 204 meeting with Delaney, Hasty and Johnson during that same time frame. Nevertheless, Gover confirmed during the hearing

[112] Tr. 140:14-22; *see also* Delaney FOF 14.

[113] *See* Delaney FOF 20.

[114] *See* Delaney FOF 20.

[115] *See* Tr.154:22-155:16, 156:16-19.

that if he was aware of "the Stock Loan issue" at the time of that meeting, he would mentioned it.[116] He would not "sit back while the person [he] reported to probed him at length about this problem and not report that some it was Stock Loan if he knew some of it was Stock Loan."[117] Yet, this is exactly what Gover did.[118]

In addition, Gover testified that he prepared the November 2010 response to OCIE, which the Division asserts as misrepresentation by Delaney, stating:

> Penson feels that the processes and procedures employed to close out positions that were in violation of Rule 204T were effective and performed as designed. Our current procedures as they relate to 204 are effective and designed to ensure that all short sales and sales not long are covered either through stock borrow or market action prior to the open on S+1.[119]

Gover confirmed at the final hearing that he believed this was accurate when he wrote it.[120]

In sum, Gover's memory, admittedly and demonstrably, is not reliable. His testimony on the timing and content of the Rule 204 meeting is contradicted by everyone else at the purported meeting. Either Gover is making up the Rule 204 meeting to curry favor with the Division pursuant to his cooperation agreement, or the meeting he recalls actually occurred much later — between when he drafted the 2010 response to OCIE and when the Stock Loan issues were escalated to outside counsel, Morgan Lewis & Bacchius, in February of 2011, in which case Gover's testimony adds little to the contention that Delaney knew of Stock Loan's violations.

3. Other factors and evidence further contradict the Division's argument that Delaney knew of Stock Loan's Violative Practice Since 2008.

In addition to the unreliability of the testimonial evidence offered by the Division,

---

[116] Tr. 155:17-22; *see also* Delaney FOF 22.

[117] Tr. 156:20-24.

[118] *See* Delaney FOF 23.

[119] *See* Ex. 86.

[120] Tr. 147:24-148:1; *see also* Delaney FOF 58.

additional factors further contradict its assertions as to Delaney's knowledge of the Rule 204T(a)/204(a) violations at issue.

a. *There is no corroborative documentary evidence.*

The fact that the Division has produced no corroborative documentary evidence showing Delaney knew, despite submitting nearly 300 exhibits, is a glaring hole in its case.[121] It is inconceivable in this day and age, with a purported scheme involving so many people and lasting for three years, that there would be no emails discussing it or Stock Loan's conduct, before the privileged documents from February 2011, which are excluded from evidence.[122] Indeed, where Stock Loan was knowingly violating an SEC rule, it had a strong incentive to create a paper trail demonstrating that it had disclosed its conduct to Compliance who signed off on the practices. Yet, despite this strong incentive, no one in Stock Loan created a single document documenting its disclosure or Compliance's response.[123]

Indeed, the February 2011 emails show that parties were not afraid to put these details in writing. Delaney's immediate response to this February 2011 revelation—escalation to outside counsel and disclosure to regulators—is itself compelling evidence that he did not know previously. If he knew before, his reaction in February 2011 and thereafter makes no sense.

Furthermore, where the Division claims that DeLaSierra, Johnson and Gover—all registered individuals—met with and entered into an agreement with Delaney to violate the law, it is highly dubious that they would not have followed-up in writing to confirm that the CCO knew, to create a paper trail for cover. Similarly, if Stock Loan was uncertain of how to comply

---

[121] *See* Delaney FOF 94. It is worth noting that a centerpiece of the Division's closing arguments against Yancey was the lack of documentary evidence. Measured against the yardstick it used against Yancey the Division's case against Delaney is severely deficient.

[122] Only one exhibit (Ex. 91) even plausibly contains any written record of the alleged policy at issue—the July 26, 2010 email from Erik Alaniz to Summer Poldrack. However, as discussed further below, this email does not establish that Delaney knew or put him on notice of a persistent practice by Stock Loan to violate Rule 204. At the very least, the email is incompetent to establish Delaney's knowledge before July 26, 2010.

[123] *See* Delaney FOF 96.

with Rule 204T/204, why did they never email Delaney, or anyone else in Compliance, for guidance? After all, the number of exhibits in this case shows that at least Johnson was a prolific e-mailer. Instead, Wetzig testified that Stock Loan specifically did not put its practice or policy "in writing."[124] The lack of any such emails or other written evidence showing Delaney knew of Stock Loan's violative policy is compelling evidence that Delaney did not know.

b. *Other witnesses contradict the Division's position.*

The Division's theory that Delaney knew of Stock Loan's violations in 2008 is also contradicted by several other witnesses. First, other members of Stock Loan indicated that they did not have discussions with Delaney. As the Division acknowledged in its disclosure of exculpatory evidence made pursuant to *Brady v. Maryland*, 373 U.S. 83 (1963), "Brian Hall told the Division that he did not ask legal or compliance for help with figuring out a way to comply with Rule 204 until the beginning of 2011."[125] He then met with "Holly Hasty and outside counsel for Penson in early 2011, prior to the response to FINRA, to seek guidance about the non-compliant stock loan procedures that violated Rule 204(a)."[126] Hall was a senior member of Penson's Stock Loan department, junior only to Johnson. If there were issues to report directly to Delaney, as CCO, it is much more likely he would be involved than DeLaSierra. Notably, the Division did not call Hall as a witness.

In addition, Wetzig, who was the manager of recalls for Stock Loan, and who participated in the February 2011 call with outside counsel regarding Rule 204, also confirmed that he "did not have any discussions with Tom Delaney prior to th[at] phone call."[127]

Second, Delaney has adamantly and consistently denied that he knew prior to March of

---

[124] *See* Tr. 389:21-390:7; *see also* Delaney FOF 37.

[125] Ex. 446, ¶3.

[126] *Id.*, ¶5.

[127] *See* Delaney FOF 83.

2011 that Stock Loan had a practice of violating Rule 204T(a)/204(a) for long sales of loaned securities. Delaney testified at length in this proceeding.[128] Numerous witnesses at the hearing testified about Delaney's high moral and honest character and his rigid adherence to the rules and regulations than make him a good compliance officer, including Hasty, Bill Yancey, Alaniz, Phil Pendergraft, Bart McCain, Scott Spiker and Hugh Simpson.[129] None of these individuals had cooperation agreements or other reason for bias towards Delaney and, notably, Spiker and Simpson, Delaney's current employers, think so highly of Delaney's skill and character that they continue to employ him notwithstanding the Division's charges.[130] The Division did not produce any testimony impugning Delaney's character or honesty.

As set forth in more detail in the concurrently filed findings of fact, with respect to Rule 204T/204 issues at bar, Delaney testified that he met with some members of Stock Loan, Johnson and potentially DeLaSierra, around the time that Rule 204T was adopted in the fall of 2008.[131] During the conversation, Johnson "expressed some concern that he was getting counter-party pushback" as a result of Rule 204T.[132] Although Delaney did not recall any further discussions with Johnson or DeLaSierra regarding Rule 204T/204 prior to February of 2011, Delaney testified that he would not have been concerned by additional discussions of counterparty push-back.[133] As indicated, Delaney interpreted counterparty pushback to be an indication that Stock Loan was following the Rule.[134]

Delaney also unequivocally testified that prior to the March 2011 FINRA response (Ex.

[128] *See* Delaney FOF 36.

[129] *See* Delaney FOF 1-4, 8.

[130] *See* Delaney FOF 2.

[131] Tr. 1192:9-15.

[132] Tr. 1192:19-24.

[133] Tr. 1195:5-12

[134] *Id.*

89), he "[n]ever had a conversation with anyone at Penson that left [him] with the understanding that stock loan wasn't closing out long sales of securities they had out on loan."[135] Delaney also testified that no conversation with DeLaSierra left him with "the impression that stock loan wasn't complying with Rule 204."[136] And, as indicated, Delaney denies that the purported meeting with Gover sometime during late 2009 to 2010 ever occurred.[137]

Moreover, despite over four hours of cross-examination by the Division, he was never once directly asked whether he knew about Stock Loan's practices. If the Division had any actual evidence that Delaney knew, surely they would have used it to cross-examine him. Indeed, as Delaney himself said in response to a question about Penson's April 2010 letter to OCIE (Ex. 171), "[i]f he had known, we would have disclosed it long before . . . [o]r we would have remediated it long before. It wouldn't have even been an issue to disclose."[138]

Third, Alaniz's testimony and role in the 3012 testing of Penson's Rule 204 compliance strongly suggests that Delaney did not know. Alaniz testified that Delaney asked him to conduct the 3012 audit of Penson's Rule 204 compliance, but did not tell Alaniz which departments or reports to test or provide the methodology for the test. The Division has never claimed that Alaniz was a part of the alleged conspiracy. But if Delaney knew that Stock Loan was not complying with Rule 204 at this time, and was seeking to aid and abet Stock Loan's violations, it makes no sense that he would send Alaniz out to test Rule 204 compliance without confining Alaniz's testing in some way to make sure Stock Loan's violations were not discovered.

Moreover, the evidence strongly suggests that Stock Loan was actively concealing its practices from Compliance. Alaniz testified that he met with members of both Penson's Buy-In

---

[135] *See* Delaney FOF 36.

[136] *Id.*

[137] *See* Delaney FOF 19.

[138] Tr. 1376:6-14.

and Stock Loan Departments in formulating his test and in conducting follow-up testing. Alaniz met with Stock Loan because they were the experts and knew the area best.[139] Yet, Alaniz was never told that Stock Loan handled close-outs of long sales of loaned securities or that Stock Loan was not complying with Rule 204 in doing so. In addition, Stock Loan received the drafts of the 3012 report (Ex. 70), and even helped draft the remedial sections. Yet, not once during the testing process, including in responding to the draft reports and on-going questions, did Stock Loan distinguish between practices of customer caused fails and Stock Loan fails. Rather, Stock Loan drafted a remedial measure indicating, "The Stock Loan Department borrows for 204 securities daily prior to market open and will monitor those borrows to ensure proper settlement of CNS fails."[140] If the Division's version of facts is true, this response is simply false and was intended to mislead Alaniz.

That Alaniz did not independently discover the violations, despite conducting extensive 3012 testing on Penson's compliance with Rule 204, strongly suggests Stock Loan was concealing any non-compliant practice from Compliance, including Delaney. It also suggests that Delaney did not know of the violations; if Delaney knew, there would be no reason to hide the truth from Alaniz.

c. ***Delaney was candid on much larger issues.***

Penson was the subject of frequent regulatory exams from both FINRA and the SEC. Exhibit 89, the FINRA response from March of 2011 alone sets forth 20 issues. Some of the issues facing Penson were massive, including writing down collateral from $89M due to relationships Phil Pendergraft had with customers of Penson. Delaney spent dramatically more

---

[139] *See* Delaney FOF 38.

[140] *See* Ex. 70; *see also* Ex. 345 (containing an email from Hall to Erik Alaniz and copying DeLaSierra and Summer Poldrack, dated March 11, 2010, indicating "I have updated the remediation document with a manual process that should keep us in compliance with Rule 204 until the development work is complete.").

time on these issues than on anything having to do with Rule 204.[141] It makes no sense that he would conspire to hide Penson's Rule 204 issues, which the evidence has shown were very minor, and yet disclose the large ones.

4. The Division's reliance on Delaney's Wells Submission is misplaced.

It is expected that the Division may rely on Delaney's Wells Submission[142] to try to establish Delaney's awareness of the alleged wrongdoing. Although the Wells Submission is admissible, the Court should give it very little weight. Delaney's Wells Submission is prepared by, and intended to be, argument of counsel. Given the procedural timelines of the administrative process, Wells Submissions are prepared and submitted before respondents and counsel have all the evidence or an opportunity to fully investigate the facts. They should not be given more weight than the live testimony heard at the hearing.

That is the case here. Delaney has consistently represented, during his investigative testimonies and trial, that he did not know of any violative practice by Stock Loan with respect to Rule 204T/204 prior to Spring of 2011. There is nothing in the Well Submission prepared by counsel that is intended to, or does, contradict Delaney's testimony. Indeed, the Wells Submission indicates Delaney was not aware he was playing a role in any wrongdoing.[143] The Division's attempts to pull statements out of context and to ascribe adverse meaning to them to try to impeach Delaney should be given little weight, where the statements at issue were written by counsel, very early in the process, and based on incomplete knowledge.

---

[141] Tr. 1290:18 – 1296:3.

[142] Ex. 157.

[143] Ex. 157, p. 30.

E. Delaney Did Not Knowingly and Substantially Assist.

1. Legal Standards of Substantial Assistance.

To satisfy the knowing and substantial assistance element of aiding and abetting, "the SEC must show that the defendant 'in some sort associated himself with the venture, that he participated in it as something that he wished to bring about, and that he sought by his action to make it succeed."[144] "In other words, the primary violation must be a 'direct or reasonably foreseeable result' of the aider and abettor's conduct."[145] These standards are not met here.

2. Delaney Did Not Knowingly and Substantially Assist Any Violations of Rule 204T/204.

In its OIP, the Division alleged four primary acts of "substantial assistance": (a) agreeing with Stock Loan to continue implementing non-compliant procedures; (b) intentionally omitting Stock Loan's "non-compliant" procedures in Penson's WSPs; (c) intentionally concealing the "non-compliant" procedures from regulators and Penson's president/CEO, Yancey; and (d) creating a "Supervisory System" that would allow Johnson to remain unsupervised so he could continue the practice of intentionally violating Rule 204T(a)/204(a).[146] These theories of substantial assistance fail for both global and specific flaws.

a. *Global Flaws*

The Division's acts of substantial assistance suffer from three global flaws. First, all of these acts are predicated on Delaney having actual knowledge of Stock Loan's non-compliant practices. If Delaney did not know, then he could not act to intentionally "conceal" non-compliant procedures from the WSPs, regulators or Yancey. Similarly, if Delaney did not know

---

[144] Stipulated COL 7.

[145] Stipulated COL 8; *SEC v. Grendys*, 840 F. Supp. 2d 36, 46 (D.D.C. 2012); *accord SEC v. Pentagon Capital Management PLC*, 612 F.Supp.2d 241, 266 (S.D.N.Y.2009) ("The aider and abettor's substantial assistance must be a proximate cause of the primary violation.").

[146] *See* OIP, ¶¶37-42, 52-53, 60, 64, 68.

of the violative practice, he could not agree with Stock Loan to continue it. And, the creation of a purported flawed Supervisory System could not have the required level of conscious intent if Delaney was unaware of any violations; it could be, at best, negligent. As indicated above, Delaney has no such knowledge, rendering the alleged acts of "assistance" meaningless, even if the Division were to try to pursue a recklessness theory.

Second, as indicated above, without some form of motive or incentive, these acts are insufficient to show that Delaney participated in the alleged scheme to violate Rule 204 "as something that he wished to bring about," or "sought by his action to make it succeed." [147] The Division needs the "why" to sustain its charges against Delaney for aiding and abetting. This is the reason it spent half-a-million dollars on Professor Harris to, ultimately unsuccessfully, try to establish a financial incentive.[148]

Third, the Division's theory fails for lack of proximate cause, regardless of whether it is based on conscious intent or recklessness.[149] All of the members of Stock Loan knew at all relevant times that Rule 204T/204 required them to close out all long sale transactions by market open at or before market open on T+6.[150] As Wetzig confirmed during his testimony regarding when he learned about the requirements of the Rule: "The rule came out in 2008. At that point, we had the rule . . . . We looked at the rule and read the rule."[151] Johnson developed Stock Loan's unwritten policy and practice to not timely close-out long sales of loaned securities, [152] and, as indicated above, there is no evidence that Delaney told anyone at Stock Loan they did not

---

[147] Stipulated COL 7.

[148] *See* Delaney FOF 93.

[149] Stipulated COL 8; *accord SEC v. Pentagon Capital,* 612 F.Supp.2d at 266, *supra.*

[150] *See* Stipulated FOF 70.

[151] Tr. 384:8-19.

[152] Tr. 389:10-390:4

need to comply with Rule 204. The evidence also established that Stock Loan continued to violate the Rule even after Delaney learned of the issue in February of 2011, escalated it to counsel, and ultimately left Penson.[153]

Given this, no purported lack of guidance, and no conduct by Delaney could directly, foreseeably or otherwise proximately cause the violations at issue. If Delaney's acts of disclosing the violations and seeking outside legal advice could not stop the violations, it is difficult to imagine that his actions, or lack of actions, ever had any effect on Stock Loan's purported violations. Delaney simply had no role in the violations. There is an unbroken causal chain within Stock Loan itself, and nothing Delaney did or said could have directly caused or contributed to the violations because they continued after the escalation meeting, the disclosure to FINRA, and after Delaney left.

b. *Specific Flaws*

Each of the alleged acts of substantial assistance also fail when considered individually.

i. Delaney did not enter into an agreement to implement non-compliant procedures.

There is no evidence, either through testimony or documentary evidence, that Delaney authorized Stock Loan to violate Rule 204T(a)/204(a). The testimony is actually to the contrary.[154] Nor is there evidence that Delaney rejected any procedures to put Penson into compliance with Rule 204T/204. Again, the members of Stock Loan knew the requirements of the Rule from the time it was adopted, and themselves decided not to comply. Wetzig testified that his supervisors in Stock Loan, "didn't tell me I couldn't close out, but I didn't ask them if I could close out,"[155] even though he admitted he knew he "was violating the rule, as [he]

[153] *See* Stipulated FOF 67-68.

[154] *See* Delaney FOF 68.

[155] Tr. 395:24-25, 411:8-10.

understood the rule."[156]

In fact, any notion that Delaney rejected compliant procedures is a red herring. There is no credible evidence that Stock Loan sought guidance on how to comply with Rule 204 (and all knew the requirements of the Rule), or discussed recalling on T+2 with Delaney. Stock Loan members are the business line experts and are required to know the regulations that are applicable to their practice.[157] They are in the best position to develop their own procedures and are required to conform their procedures and practices to the securities laws.[158] Where Stock Loan knew that long sales needed to be closed out by the morning of T+6 under Rule 204T(a)/204(a), and that recalls generally took three days before the shares were returned, they did not need Delaney to advise them to recall a day earlier, on T+2, to ensure compliance with Rule 204T(a)/204(a).

ii. Delaney did not draft WSPs to conceal non-compliant practices.

The Division next alleges that Delaney created and circulated defective WSPs to hide Stock Loan's practices to not close out, and that forwarding these WSPs to FINRA was substantial compliance. Again, there is no evidence to support this outlandish assertion.

The business units, including stock loan, generated their own WSPs.[159] According to Hasty, the business units are the "experts"; the people doing this "day-to-day," so it is "absolutely necessary to have the business owners be the original people who are drafting those WSPs."[160] No one in the Compliance department had "the level of sophistication with regard to

---

[156] Tr. 411:8-10.

[157] Tr. 391:10-13.

[158] *See* Tr. 391:10-13, 396:15-18.

[159] Tr. 1758:2-12.

[160] Tr. 1758:13-1759:2.

Stock Loan to be able to write Stock Loan substantive WSPs."[161] The business units also had the responsibility to review the WSPs to make sure they reflected actual practices.[162]

Nor were the WSPs misleading or inadequate. Yancey's expert witness, Judith Poppolardo, determined that Penson's Rule 204 procedures were adequate and typical of the industry.[163] The WSPs expressly identify the requirements of Rule 204(a), including the close-out obligations for both long and short sales.[164]

Furthermore, the WSPs also provided procedures for complying with Rule 204 that would have prevented the very issue at bar, had Stock Loan not disregarded them. For example, Penson's WSP Rule 204 procedures for Stock Loan expressly direct Stock Loan to not only buy-in recalls if necessary to satisfy CNS obligations, but to "forward the Buy-In to the customer Buy-In department," when "Stock Loan does not have a counterparty to pass the Buy-In to."[165] Had Stock Loan not willfully disregarded this procedure, the 3012 testing would have caught the close-out issues and they would have been remediated, just as the Division concedes they were when a failure to deliver is caused by a customer. The Division completely ignored these procedures in order to try to buttress their argument that the WSPs were inadequate.

However, even if the Court thought the WSPs sent to FINRA as part of the 1017 application in connection with Penson's acquisition of Ridge Clearing were inadequate, it is worth noting that they were reviewed by counsel.[166] Nor did FINRA find Penson's Rule 204 WSPs inadequate, despite reviewing them with a "fine tooth comb," as it approved the Ridge

---

[161] Tr. 1759:3-8.

[162] *See* Delaney FOF 65.

[163] *See* Delaney FOF 67.

[164] *See* Ex. 66, pp. 396-97; Ex. 183, pp. 337-338.

[165] *See* Ex. 66, pp. 377-78

[166] *See* Ex. 183.

Acquisition.

iii. Delaney did not mislead regulators.

The Division contends that Delaney's most egregious conduct was misleading regulators. The Division has failed to establish that Delaney ever misled a regulator.

As an initial matter, and as indicated, the Division's argument that Delaney misled regulators is entirely based upon its assertion that Delaney had actual knowledge of Stock Loan's Rule 204 violations. Without such knowledge, there is no basis to conclude that Delaney sent any responses or reports to a regulator in furtherance of any underlying misconduct, even if they were erroneous in some manner.

In addition, although the Division insists that misleading regulators was an act of substantial assistance by Delaney, the Division's argument is analytically confused. The primary violation at issue is Rule 204(a). The Division has not explained how an alleged misrepresentation to a regulator substantially assists the alleged practice or policy to violate Rule 204(a). This is particularly true where the evidence here shows that the violations continued unabated even after the disclosure of the practice to FINRA in March of 2011.

Moreover, Delaney did not sign any of the responses at issue.[167] The 3012 Summary Report was prepared by Alaniz and signed by Yancey.[168] The April 10, 2010 Response to OCIE was signed by Doug Gorenflo.[169] The November 2010 Response to OCIE was initially prepared by Gover and signed by Hasty.[170] Thus, he is not "maker" of any of the purported

---

[167] In this regard, the United States Supreme Court's decision in *Janus Capital Group, Inc. v. First Derivative Traders*, 131 S.Ct. 2296 (2011) is instructive. "One who prepares or publishes a statement on behalf of another is not its maker." *Id.* at 2203.

[168] *See* Tr. 825:24-825:21 and Ex. 135.

[169] *See* Ex. 170.

[170] *See* Ex. 101.

misrepresentations.[171] The Division's argument, then, must be that Delaney is aiding and abetting the actual signatory's misrepresentation (without making any effort to demonstrate these individuals had the necessary scienter). However, this is not the charge pleaded by the Division, and it cannot expand its case at this stage of the proceedings, as set forth above.

The Division has also failed to establish that any of the alleged responses are misleading. The 3012 Summary Report (Ex. 135) was not misleading for failure to include the test results from Rule 204. The Summary Report did not include any of the twenty different tests Alaniz conducted. Instead it incorporated an exception and remediation report — which the Division did not attach to the Exhibit it introduced — and made all documentation of all of the 3012 tests available for review by FINRA and OCIE upon request.[172] Furthermore, as contemplated by the Summary Report, a remediation plan was underway at the time the Summary Report was filed.

Moreover, the Division's argument with respect to the 3012 Summary Report is a red herring. The Rule 204 audit only tested Penson's Buy-In Department (although Alaniz's intended to test all of Penson's Rule 204 compliance).[173] Thus, including the test results would not have disclosed anything about the primary violation at issue.

The April 2010 Response to OCIE (Ex. 170) was not misleading in indications that the "manual processes" and "system limitations" were responsible for Penson buying in shortly after market open. The Division has provided no data from April of 2010 to show the representation was false. Rather it relies on data from November 2010, before remediation efforts were underway, as if those results forever governed the reasonableness of representations Penson could make. Indeed, Alaniz's testing a month later showed most buy-ins were taking place

---

[171] *See Janus*, 131 S.Ct. at 2203 ("One 'makes' a statement by stating it.").

[172] *See* Delaney FOF 99; Ex 135.

[173] *See* Delaney FOF 40.

shortly after market open.[174]

Finally, the November 2010 Response to OCIE (Ex. 101) is not misleading. The Response provides, in pertinent part:

> Penson believes that the reasonable processes employed to close out positions that were allegedly in violation of rule 204T were effective and performed as designed. The Firm's current procedures as they relate to Rule 204 are effective and reasonably designed to ensure that all short sales and sales not long are covered either through stock borrow or market action pior to the open on S+1.[175]

The plain language of this response indicates that it is not even addressing long sales at all, so it could not logically substantially assist the violations of Rule 204T(a)/204(a) at issue, even if it were misleading. However, it is not misleading. The fact of the matter is that Penson was closing out over 99.3% of all positions related to long sales of loaned securities during the relevant time period. This indicates that Penson had reasonable processes in place, regardless of the Rule 204T(a)/204(a) violations at issue. This conclusion is in accordance with the expert opinions of both Popplolardo,[176] and the Division's own expert, Paulukaitis, who indicated:

> The standard is reasonableness, with a range of reasonable responses, and the standard doesn't require perfection ... In the context of 10,000 transactions a day, reasonableness must allow some questionable transactions to slip through undetected . . . .[177]

Furthermore, every witness questioned, including Gover, has stood by the accuracy of the language in this response.[178]

Notably absent from the Division's list of allegedly misleading regulatory responses is the March 18, 2011 response to FINRA, where Penson discloses the issues

---

[174] *See* Ex. 85.

[175] *See* Ex. 101.

[176] *See* Delaney FOF 75.

[177] *See* Ex. 238, p 6.

[178] *See* Delaney FOF 5 8.

with long sale close-outs. This is not surprising, as it is a strikingly candid response. However, the Division also misses the point. If Delaney intended to conceal Stock Loan's "violative practice" with respect to Rule 204(a) from regulators, it makes no sense that Delaney would disclose it in March of 2011. That this March of 2011 disclosure was made at all is further compelling evidence that there was no intent to conceal or mislead.

iv. ***Johnson was not unsupervised.***

The final purported act of substantial assistance is by far the weakest. The Court heard a significant amount of evidence at the final hearing from both the Division and Yancey about who supervised Johnson—Phil Pendergraft or Bill Yancey. It is clear, from this evidence, that Johnson was in fact supervised, regardless of who his supervisor was. Phil Pendergraft confirmed this expressly.[179] Pendergraft further confirmed that Delaney would have no reason to be concerned that Johnson was not supervised.[180]

F. Delaney Did Not Act Recklessly.

In light of the weaknesses in its case, the Division may alternatively attempt to establish that Delany substantially assisted the purported scheme by acting recklessly. This argument fails.

In certain circumstances, "'[E]xtreme recklessness" may support aiding and abetting liability."[181] Extreme recklessness' or as many courts of appeals put it, 'severe recklessness' may be found if the alleged aider and abettor encountered 'red flags,' or 'suspicious events creating reasons for doubt' that should have alerted him to the improper conduct of the primary violator, or if there was 'a danger ... so obvious that the actor must have been aware of' the danger."[182] "It is not enough that the accused aider and abettor's action or omission is 'derived from inexcusable

---

[179] *See* Delaney FOF 62-63.

[180] *See* Delaney FOF 61.

[181] *Howard,* 376 F.3d at 114 3 (citations omitted).

[182] *Id.* (internal citations and footnotes omitted).

neglect.'"[183] "'Extreme recklessness' is neither ordinary negligence nor 'merely a heightened form of ordinary negligence.'"[184] "To put the matter in terms of § 21C, aiding and abetting liability cannot rest on the proposition that the person 'should have known' he was assisting violations of the securities laws."[185]

Any effort by the Division to proceed on a recklessness theory fails for both procedural and substantive reasons. Procedurally, the Division has not pursued a recklessness theory in this case. It remains uncertain as to whether the Division intends to argue recklessness._The OIP alleges only "intentional" misconduct against Delaney, not reckless misconduct, and the Division cannot expand its case from the OIP at this late date.[186]

In addition, it unclear—because the Division has not identified them—what the purported "red flags" or obvious dangers were to Delaney. With respect to the claims against Yancey, conversely, the Division clearly identified what it believed were red flags. Delaney should not be forced to guess, at his peril, as to the basis for the Division's new allegations against him. The Administrative Procedures Act specifically requires the Division to provide timely notice of the matters of fact and law asserted. [187] "Hence it is well settled that an agency may not change theories in midstream without giving respondents reasonable notice of the change."[188] Where the Division has not purported to identify how it believes Delaney acted recklessly, or even what

---

[183] *Id.* (citations omitted).

[184] *Id.* (citation and footnote omitted).

[185] *Id.*

[186] *See, e.g., In the Matter of Robert Bruce Lohmann,* Init. Dec. Rel. No. 214 at 13, 17 n.5, 2002 SEC LEXIS 2380 at *33, 46 n.5 (Sept. 19, 2002), *aff'd*, Exchange Act Rel. No. 48092, Investment Advisers Act Rel. No. 2141, 2003 SEC LEXIS 1521 (June 26, 2003); *In the Matter of Richmark Capital Corp.*, Init. Dec. Rel. No. 201 at 25, 2002 SEC LEXIS 601 at *6769 (March 18, 2002), *aff'd*, Securities Act Rel. No. 8333, Exchange Act Rel. No. 48758, 2003 SEC LEXIS 2680 (Nov. 7, 2003);.

[187] *See* 5 U.S.C.A. § 554(b)(3).

[188] *Rodale Press, Inc. v. F.T.C.*, 407 F.2d 1252, 1256 (D.C. Cir. 1968).

the red flags were that he allegedly ignored, the Division has deprived Delaney of the required notice. The Division should not be permitted to proceed on a recklessness theory.

Substantively, the evidence establishes that Delaney has not acted recklessly to aid and abet Stock Loan's alleged practice to violate Rule 204T(a)/204(a). As indicated, all of purported acts of substantial assistance require Delaney to have actual knowledge of the violations. Recklessness, for example, would not show that he agreed with Stock Loan to implement non-compliant procedures, or affirmatively misled regulators.

In addition, the evidence also establishes that there were approximately two violations per day related to long sales of loaned securities. This is not an obvious sign of danger to Delaney where Penson timely cleared millions of transactions a day, and over 99.3% of all positions relating to long sales of loaned securities. Similarly, a financial "gain" of approximately $77/day is not a red flag to non-compliance.

The evidence also shows that Delaney actively worked to ensure Rule 204 compliance. He ordered extensive 3012 testing, and the audit results indicated the issues were being remediated.[189] There is also expert witness testimony indicating that the WSP procedures for 204 compliance are reasonable.[190]

Conversely, there is no credible evidence that any Rule 204T(a)/204(a) issues with respect to Stock Loan were escalated to Delaney before February of 2011, at which time the Division concedes he diligently discharged his duties as CCO. Any evidence that Delaney knew of counter-party push back prior to this time is not a red flag. As indicated, pushback suggests the business units are complying with the Rule.

---

[189] *See* Ex. 70.

[190] *See* Delaney FOF 67, 75.

Moreover, while the Division may claim that the July 26, 2010 email (Ex. 91) was escalation and a significant enough red flag to put Delaney on notice, this argument fails. This email does not give any indication that there was a *persistent* practice by Stock Loan to violate Rule 204. Rather, it is a single email, sent to Delaney only as a courtesy copy. According to Alaniz, it did not purport to escalate a compliance issue to Delaney.[191] The email itself indicates that the issue had been addressed, and resolved, through the responses of two separate compliance officers (Alaniz and Hasty).[192] Even if the email were a red flag, it is only one. A finding of recklessness requires an "abundance of red flags and suggestions of irregularities that demanded inquiry."[193]

Finally, the Division does not claim that Delaney had a duty to affirmatively root out violations of Rule 204, and it has submitted no evidence to support such an assertion. Tellingly, the Division instead submitted an expert report from Mr. Paulukaitis based only on an assumption that Delaney knew of the violations.[194] Accordingly, any effort by the Division to establish Delaney was reckless fails and should be rejected.

II. The Division's Causing Claim Fails.

A respondent who aids and abets a violation also is a cause of the violation under the federal securities laws.[195] However, to establish liability for "causing" in the absence of of aiding and abetting, the Division must prove three elements: (1) "a primary violation"; (2) an act or omission by the respondent that was a cause of the violation"; and (3) that "the respondent knew,

---

[191] *See* Delaney FOF 55.

[192] *See* Ex. 91.

[193] *See Howard,* 376 F.3d at 1149 (quotations and citation omitted).

[194] *See* Ex. 238, p. 15-17.

[195] *See Sharon M. Graham,* 53 S.E.C. 1072, 1085 n.35 (1998), aff'd, 222 F.3d 994 (D.C. Cir. 2000).

or should have known, that his conduct would contribute to the violation."[196] "Negligence is sufficient to establish 'causing' liability under Exchange Act Section 21C(a), at least in cases in which a person is alleged to 'cause' a primary violation that does not require scienter."[197]

Although nominally referencing a "causing" claim in the OIP, the Division did not separately pursued this claim during the hearing nor did the Division reference "causing" in its Pretrial Brief. Similarly, the Division did not use the term "negligent" or any derivative thereof a single time in the OIP, and did not provide any allegations to support a causing claim that is divorced from its aiding and abetting claim. Instead, the Division references causing only in connection with its allegations of willful aiding and abetting; that, "[a]s a result of the conduct described above, Delaney willfully aided and abetted and caused" the alleged primary violation.[198]

Delany therefore believes the Division has not asserted, or has abandoned, a separate claim for "causing." To the extent the Division's aiding and abetting claim fails, its conjoined causing claim fails. And, if the Division intends to now assert a pure "causing" theory, it is procedurally improper for the reasons stated. Delaney reserves further rebuttal for his Reply.

III. The Division is Not Entitled to Remedies Sought.

For the reasons discussed above, the Division's claims against Delaney fail. As such, the Division is entitled to no remedies. In addition, even if the Division does establish liability on its claims against Delaney, the Division is not entitled to the remedies sought.

---

[196] *See In the matter of Mohammed Riad and Kevin Timothy* (June 10, 2014)S" \s "WSFTA_137e5aad5dae4ec6bffc21d48c6a8a31" \c 3 *Mohammed Riad and Kevin Timothy Swanson,* Release No. 590, 2014 WL 1571348 *28 (June 10, 2014)*; see also Robert M. Fuller,* 56 S.E.C. 976, 984 (2003), *pet. for review denied* 95 F. App'x 361 (D.C. Cir. 2004).

[197] *Howard,* 376 F.3d at 1142 (quotations and citation omitted).

[198] *See* OIP, ¶85.

A Division is not Entitled to a Bar under Rule 15(b)(6).

Rule 15(b)(6) provides that an associated person may be barred from association with the securities industry if he willfully aids and abets violations of SEC Rules and it is in the public interest to bar him. The Division has failed to prove that Delaney willfully aided-and-abetted Stock Loans alleged primary violation of Rule 204. As set forth above, he had no profit motive, and had no knowledge of the alleged misconduct before March of 211. The Division has also failed to adduce any evidence that it serves any public interest to bar him from working in the financial services industry. There has been no evidence that Delaney put any member of the public at risk or created any heightened market risk.

It should be noted that the entire group of individuals who the Division claims are the primary violators, including the entire Stock Lending Department, were either granted cooperation agreements and not included in this or any action by the Commission (Hall, Gover), or were allowed to settle for moderate sanctions (Johnson, Wetzig). Indeed, Mr. Wetzig, who admitted at the final hearing to violating Rule 204 as he understood the rule, was not barred.[199]

The Division acts with temperance towards the primary violators who stood to gain from the alleged misconduct and then seeks harsh and aggressive remedies against Delaney who they claim was only an aider and abettor of the actual Rule 204 violations. Based on the evidence in this case, the Court should not allow the Division to selectively reward primary violators in order to sanction those who are on trial for failing to catch the primary violators.

B. A Cease-and-desist Order is Not Warranted

There is also no basis for a cease-and-desist order. The Division stipulated that any claim against Delaney ceased around February 15, 2011 (FOF 58). Thus, the conduct at issue ceased over three years ago and the Division has adduced no evidence to establish any likelihood of

[199] *See* Tr. 404:7-16; 411:3-10.

future violation. The prospect that Mr. Delaney could cause future violations is non-existent and the law is clear that the Division must put forward some evidence to support the need for a cease-and-desist. It cannot rely on speculation that Delaney may cause future violations.

C. Division is not Entitled to the Equitable Remedy of Disgorgement

Disgorgement is unwarranted because Delaney acted lawfully. Furthermore, as stated in the Division's pretrial brief, disgorgement is an "equitable remedy that requires the violator to give up wrongfully obtained profits causally related to the proven wrongdoing."[200] Disgorgement was not sought or ordered against either Johnson or Wetzig, despite their indisputably greater level of culpability. Moreover, the Court should summarily reject the Division's request for disgorgement because – as all witnesses, including the Division's own expert and the alleged primary violators testified – if there were primary violations, they were not for profit motive and the Division has not met its burden to prove an actual profit to Delaney.

Even if this Court determines disgorgement is warranted and Delaney somehow profited, the amount of disgorgement must be limited to a "reasonable approximation of profits causally connected to the violations."[201] As explained above, the actual transactions and dollars at issue are so small that the Division has failed to meet its burden of showing any quantifiable ill-gotten gains specifically to Mr. Delaney from profits causally connected to a primary violation.

Accordingly, this Court should exercise its broad discretion and reject the Division's unsupported claim for disgorgement.[202]

---

[200] Division's Pre-hearing Brief at page 24.

[201] In re Ronald S. Bloomfield, AP File No. 3-3-13871 at 29 (February 27, 2014).

[202] See S.E.C. v. Huffman, 996 F.2d 800, 803 (5th Cir. 1993) (court has "broad discretion" in fashioning equitable remedy of disgorgement); see also In re Gregory M. Dearlove, CPA, AP File No. 3-12064, at *63 (July 27, 2006). It is important to note here that the Division has had relevant data available for several years, along with access to highly skilled accountants, economists and other experts both internally (DERA) and externally, and yet still filed an OIP boldly stating that the violations in this matter by Delany were a conscious choice of "profits over compliance," a statement that has been conceded through stipulation to be incorrect. Generally, Court's consider the SEC the same as any other civil litigant. See SEC v. Collins & Aikman Corp., 256 F.R.D. 403, 414 (S.D.N.Y 2009). An

D. The Division Failed to Establish the Basis for a Civil Penalty.

The Division has failed to establish that any civil penalty is warranted by not producing any evidence to meet the "public interest" test described above, required to impose a monetary penalty. In this case, a penalty would not serve the public interest and the Division has not met its burden to show harm or even potential harm to the public or evidence to support the factors set out in Section 21B of the Exchange Act. The relevant factors to making this determination include (1) whether the act or omission involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement; (2) the harm to other persons resulting either directly or indirectly from the act or omission; (3) the extent to which any person was unjustly enriched; (4) whether the respondent previously had been found by the Commission or another regulatory agency to have violated the securities laws, or the rules of a self-regulatory organization; and (5) the need to deter the respondent and other persons from committing the acts or omissions.[203] Nothing in the record shows harm to other persons from any conduct by Mr. Delaney and the Division has not alleged that he committed fraud in any way. In contrast, the record contains many references to Mr. Delaney's long[204] and unblemished record as a compliance professional with no prior disciplinary history of any sort.

The Division has indicated it believes a third-tier civil penalty is warranted. The statute reserves third-tier monetary penalties if a proven violation involved (1) fraud, and (2) directly or indirectly resulted in substantial losses to other persons or resulted in substantial pecuniary gain

---

ordinary civil litigant filing a complaint without adequate basis could be subject to sanctions under Rule 11 of the Federal Rules of Civil Procedure. This proceeding, however, is governed the SEC's Rules of Practice.

[203] See 15 U.S.C. § 78u-2(c).

[204] Mr. Delaney was has been a securities professional licensed with FINRA for over 15 years.

to the person who committed the act or omission. The Division does not claim Delaney committed fraud and the Division has made no factual showing that the public was harmed in any way or that Delaney received any gain. Certainly the amounts set forth in the FOF's cited above hardly qualify as substantial enough to warrant a finding that the Mr. Delaney "greatly profited" from the alleged scheme.[205] Moreover, several recent administrative decisions indicate that in assessing the amount of a civil penalty, the amount of the penalty must be proportionate and reasonable.[206] This Court should reject the Division's request for civil penalties.

CONCLUSION

For the foregoing reasons, Delaney respectfully requests that the Court rule that (1) Delaney has no liability on the Division's claims for aiding and abetting and causing; (2) dismiss this administrative proceeding; and/or (3) deny one or more of the remedies sought by the Division.

DATED this 19th day of December, 2014.

CLYDE SNOW & SESSIONS

BRENT R. BAKER
ATTORNEYS FOR RESPONDENT THOMAS R. DELANEY II

---

[205] Again, the data necessary to make the actual determination of gain has been available for years and the Division either intentionally elected not to do the analysis or could not do the requisite analysis before being so quick to forcefully allege in its OIP that Delaney violated the law for gain or caused loss to any other person.

[206] In the Matter of Raymond J. Lucia Companies, Inc. and Raymond J. Lucia, Sr., Initial Decision Release No. 540 (Dec. 6, 2013)(The Division in this case sought a one-time, tier-three penalty, and Judge Elliott reduced that by nearly two thirds).

UNITED STATES OF AMERICA

Before the

SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-1587

In the Matter of

THOMAS R. DELANEY II and
CHARLES W. YANCEY

Respondents.

RESPONDENT THOMAS R. DELANEY II'S PROPOSED FINDINGS OF FACT

Tom Delaney Has a Reputation for Honesty and High Moral Character and was a Knowledgeable Chief Compliance Officer.

1. Respondent Tom Delaney is regarded as an honest man of exemplary character, and possessing high integrity by all Penson employees who testified and were asked to express an opinion about his character.

    a. **Tr. 831:8-10** [Alaniz]
    8 Q Do you have an opinion of whether Mr. Delaney
    9 is an honest guy?
    10 A I believe he's an honest guy.

    b. **Tr. 1155:2-4** [Gardner]
    2 Q Do you believe Tom Delaney to be an honest
    3 person?
    4 A Absolutely.

    c. **Tr. 1588:9-14** [Pendergraft]
    9 A I believe that I -- I believe that I did work
    10 closely enough with him to form a view of his
    11 character. And I believe Tom Delaney is a fine man who
    12 is dedicated to doing the right thing.
    13 Q Do you believe he's honest?
    14 A Yes, sir.

    d. **Tr. 1767:11-13** [Hasty]
    11 Q And do you believe Mr. Delaney is an honest
    12 man?
    13 A Yes.

    e. **Tr. 1910:1-5** [Yancey]
    1 Q And how would you describe Mr. Delaney's
    2 character?
    3 A Steeped in value, non compromising, honest
    4 transparent, willing to give and take criticism,
    5 thorough, integrity.

    f. **Tr. 2201:3-13** [McCain]
    3 I take it during the time you worked with him
    4 that you were able to develop some sort of sense of Mr.

5 Delaney's character?
6 A Absolutely.
7 Q How would you describe him?
8 A High ethics, high integrity, just exemplary
9 character. He was about doing things right and
10 correct. He wanted us to be the best we could be in
11 terms of following the rules, and he was very
12 approachable.

2. Delaney's current bosses, who are aware of the Division's allegations against him but have continued to employ him in a compliance-related job, believe that he is honest.

   a. **Tr. 1440:9-10** [Spiker]
   9 Q Is he honest, in your observation?
   10 A Entirely.

   b. **Tr. 1449:16-18** [Simpson]
   16 Q Do you believe that Tom is generally an
   17 honest person?
   18 A I do.

3. Nothing about the Division's allegations, lawsuit, or the evidence in this case changed any witness's opinion of Delaney's character.

   a. **Tr. 1909:18-21** [Yancey]
   18 Q And has anything during this hearing changed
   19 your opinion of who you understood Mr. Delaney to be
   20 when you worked with him?
   21 A No.

   b. **Tr. 2201:12-13** [McCain]
   12 I have nothing but the utmost respect
   13 for Tom.

   c. **Tr. 1453:13-19** [Simpson]
   13 Q Would it change your view of Mr. Delaney's
   14 character if he knew all those facts and did not
   15 communicate to Penson's CEO?
   16 A Honestly, I have a strong positive opinion of
   17 Tom's character. Again, I'd have to look into that

18 matter myself before it changed my opinion of his
19 character.

4. No witness who testified expressed a neutral or negative opinion of Delaney's character for honesty and integrity; all witnesses who were asked expressed only positive opinions of Delaney's Character.

5. Delaney's colleagues and subordinates enjoyed working for and with him because of his industry knowledge, honesty, and collaboration.

    a. **Tr. 724:24 – 725:2** [Alaniz]
    24 A He knew a lot about the industry. I felt I
    25 could learn from him. He just had a lot of the answers.
    1 I mean, he knew the industry very well. I could ask him
    2 a question and he would know.

    b. **Tr. 1767:4-10** [Hasty]
    4 A Tom is a very nice man. I enjoyed working
    5 with him. I never had any reason to believe that he
    6 wasn't forthright with me or honest. We had a good
    7 working relationship. We collaborated on a lot of
    8 projects. We worked on a lot of different initiatives
    9 to try to make the Compliance Department better. And
    10 it was a very good working relationship.

    c. **Tr. 724:21-22** [Alaniz]
    21 Q Did you enjoy working for Mr. Delaney?
    22 A I did.

6. Delaney performed his job as CCO as well as he could based on the available resources he had.

    a. **Tr. 725:8-14** [Alaniz]
    8 Q Okay. If you could, tell us what -- what you
    9 know -- or your opinion of Mr. Delaney's performance in
    10 his job as CCO.
    11 A My opinion, I believe he did the best that he
    12 could. We had a lot of fires to put out. We were always
    13 behind the eight ball. I think with what resources we
    14 had, I believe he did the best.

7. Based on Delaney's colleagues and supervisors' experience with him, Delaney never hid problems from management or regulators and routinely escalated issues up the chain of command or to regulators.

   a. **Tr. 1439:17 – 1440:2** [Spiker]
   17 Q Do you believe, based on anything you've
   18 observed in the years you've known Tom, that he has any
   19 fear of disclosing either good or bad issues up the
   20 chain of command at First Command?
   21 A I've never seen any hesitancy on his part to
   22 disclose everything to me or to others on our team.
   23 Q Have you ever seen any instance where Tom
   24 ever hid anything in his capacity as chief compliance
   25 officer at First Command from anyone, including
   1 supervisors?
   2 A No.

   b. **Tr. 1440:14-16** [Spiker]
   14 Q Do you believe Tom Delaney would ever hide
   15 anything from a regulator?
   16 A I do not.

   c. **Tr. 1441:4-14** [Spiker]
   4 Q Has he ever had any hesitation to provide
   5 negative information to people during that meeting,
   6 even if it was awkward or a great financial or any
   7 financial expense?
   8 A No, he has not. That's the purpose of the
   9 meeting, to air out any of the issues that are
   10 important to us from a compliance perspective.
   11 Q Would you have any hesitation at all to rely
   12 on any information or report that Tom Delaney prepared
   13 and submitted to you?
   14 A No hesitation whatsoever.

   d. **Tr. 1448:23 – 1449:1** [Simpson]
   23 Q Does Tom seem to you to be the kind of CCO
   24 who might hide negative information from you for any
   25 reason?

1 A Not at all. Not at all.

e. **Tr. 1449:6-15** [Simpson]
6 Q In your opinion, is Tom honest with the
7 regulators?
8 A Absolutely.
9 Q Have you ever seen him hide information from
10 a regulator?
11 A Definitely not.
12 Q Would you have any reason to believe that Tom
13 would not include negative information in reports to
14 you or to regulators?
15 A No.

f. **Tr. 2200:6-17** [McCain]
6 Q How would you describe his attitude toward
7 interactions with regulators?
8 A He was -- he was, in my view, based on
9 what -- again, as I mentioned previously, of the
10 attractive parts for me for Tom was his ability to
11 develop relationship with the regulators in California.
12 And I wanted him to be able to do that very same thing
13 here, and he made every effort to do that. Very open,
14 very engaging, very willing to get the material and
15 documents that they requested. And as far as I know, I
16 don't have any reason to believe that he wasn't
17 anything but totally truthful.

g. **Tr. 1766:6-12** [Hasty]
6 Q Did you ever see Mr. Delaney conceal any
7 violations from regulators?
8 A No.
9 Q Did you ever see the opposite, that is
10 disclosing problems to regulators?
11 A Absolutely. We had a regular history of
12 being very transparent with the regulators.

8. Delaney is regarded by his managers and others to whom he reported as a compliance-minded individual and an effective CCO.

   a. **Tr. 1440:3-5** [Spiker]
   3 Q Is he a compliance-minded individual?
   4 A He exudes compliance, that's why we hired him
   5 in that capacity.

   b. **Tr. 1440:17-18** [Spiker]
   17 Q Is he a good chief compliance officer?
   18 A He is.

   c. **Tr. 1450:8-10** [Simpson]
   8 Q Has he been an effective chief compliance
   9 officer?
   10 A Yes, he has.

   d. **Tr. 1834:14-18** [Yancey]
   14 Q Did you think Tom Delaney had the skills
   15 necessary to be the Compliance Officer at Penson?
   16 A Yes, I did.
   17 Q Any reservations or questions about that?
   18 A None.

   e. **Tr. 1908:12-24** [Yancey]
   12 Q Now, during the whole time that he worked
   13 there at Penson, was there ever anything at all that
   14 made you second guess that choice?
   15 A No, there wasn't.
   16 Q What about when Mr. Delaney left? Were you
   17 sad to see him go?
   18 A I was.
   19 Q Why?
   20 A Tom and I had an excellent relationship. Tom
   21 came to his meetings like I wish everybody did, and
   22 most people do. He had a list. He had data. He had
   23 facts. He had observations. He probed me. I probed
   24 him. That's how we worked together.

9. During his tenure at Penson, Delaney worked to improve compliance by doubling the number of compliance personnel.

   a. **Tr. 727:4-16** [Alaniz]
   4 Q Let me ask: At Penson when you started, how
   5 many compliance -- how many people were there in the
   6 Compliance department?
   7 A I would say anywhere from 10 to 12 individuals.
   8 Q Okay.
   9 A Maybe -- no more than 15.
   10 Q And when you left, do you recall how many there
   11 were?
   12 A Over 20. Maybe 20, 25.
   13 Q Okay. So in that time that you were there that
   14 Mr. Delaney was the CCO, the Compliance department
   15 doubled?
   16 A Yes.

   b. **Tr. 1223:16 – 1224:13** [Delaney]
   16 Q Describe for me, if you will, the environment
   17 in the Compliance department at PFSI when you took over
   18 as Chief Compliance Officer.
   19 A The -- the environment at PFSI was a -- it was
   20 a smaller department and working very hard to do the
   21 day's job and -- and try and get things done. There were
   22 A lot of opportunities for them to -- to take on the
   23 challenges of being in a broker-dealer.
   24 Q Did you feel like there were any ways that --
   25 that it could get better?
   1 A Sure.
   2 Q What specifically do you recall -- or what ways
   3 did you think it could get better?
   4 A Well, I think -- I -- I think some of the early
   5 challenges that we wanted to make sure we were getting
   6 the -- well, certainly as the Chief Compliance Officer
   7 that I wanted to address would have been, how do we get
   8 the department to ensure that we're -- we're offering the
   9 best value to the organization that we can. And by that
   10 I mean, how do we make sure we've got staffing and the
   11 right -- the right level of knowledge within the

12 department and -- and -- and really forging the best
13 regulatory relationship we could.

c. **Tr. 1226:16-23** [Delaney]
16 Q What about the size? Did you feel like you had
17 enough people within Compliance to do everything that
18 needed to be done?
19 A Well, I think over time we ended up adding
20 significantly to that. So certainly while I was there
21 and partnering with the Chief Executive Officer, Bill
22 Yancey, really -- really focused on building a robust
23 compliance program.

10. During his tenure at Penson, Delaney worked to improve Compliance by reorganizing the Compliance personnel into three groups, or silos, to handle three significant compliance responsibilities: anti-money laundering; regulatory liaison; and operations.

a. **Tr. 727:17-23** [Alaniz]
17 Q What -- we've heard about a few people in the
18 Compliance department here, but let me ask what
19 functions -- aside from looking at Stock Loan, which has
20 been our main focus here, tell me about -- briefly about
21 the different functions -- or the different groups of
22 compliance at -- at Penson.
23 A We had an AML department.

b. **Tr. 730:5-8** [Alaniz]
5 A Regulatory department.
6 Q And what do you mean by "regulatory
7 department"?
8 A They handle all of the regulatory inquiries.

c. **Tr. 731:12-18** [Alaniz]
12 A We had the operations where I was part of it.
13 Q And what was the operations group's function?
14 A To review operational issues like 3012 testing,
15 answer general questions, come in for our correspondence,
16 help out AML. If they needed any help, they would
17 help -- help the regulatory department. Just a wide --
18 wide swath of testing, answer general questions.

11. When faced with the choice, Delaney did not compromise compliance in order to increase profits.

    a. **Tr. 1440:6-8** [Spiker]
    6 Q Do you believe that he would choose
    7 compliance over profits?
    8 A Always.

    b. **Tr. 1448:15-18** [Simpson]
    15 Q Sure. As CCO, faced with a fact pattern,
    16 would he choose to make money or would he choose to
    17 comply with the law?
    18 A Absolutely to comply with the law.

    c. **Tr. 1766:1-5** [Hasty]
    1 Q In your experience with Mr. Delaney and your
    2 time together at Penson, did you see Mr. Delaney make
    3 any -- take any actions motivated by financial
    4 consideration?
    5 A No.

12. No witness who testified indicated that Delaney's compensation, including salary and bonus, was in any way tied to the profits of Stock Loan or Penson.

13. Delaney has a reputation for escalating compliance issues. If he learned that Stock Loan was choosing to violate the rules, Delaney would not have accepted it and would have escalated the issue immediately.

    a. **Tr. 1757:8-16** [Hasty]
    8 Q All right. Let me ask just assuming
    9 hypothetically that there had been meeting with Mr.
    10 Gover and you and Mr. Delaney where it was discussed
    11 that Stock Loan was deliberately choosing not to comply
    12 with Rule 204. Based on who you know Tom Delaney to
    13 be, what would you expect his response would have been?
    14 A I would have expected him to immediately say,
    15 That's not an acceptable solution, and he would have
    16 escalated that further

Only Two Witnesses Testified that Delaney Knew About Stock Loan's Non-Compliant Processes and Their Testimony is Inconsistent and Contradicted by Other Witnesses.

A. Brian Gover testified regarding meetings with Tom Delaney and others where Stock Loan's practice of not closing out under Rule 204 was discussed but this testimony was contradicted.

14. Brian Gover's memory is neither clear nor reliable.

    a. **Tr. 140:15-22** [Gover]
    15 It's been how long since -- since the date of the
    16 meetings that you described with Mr. Delaney?
    17 A In the range of five years.
    18 Q Okay. And how clear would you say your memory
    19 is of the dates of those meetings?
    20 A You know, I think, you know, I can pretty
    21 accurately within nine months, but, you know, I would not
    22 be able to reliably say, yeah, at this point.

15. Gover entered into a cooperation agreement with the Division.

    a. **Tr. 125:14-18** [Gover]
    14 The last thing I want to ask you about is your
    15 cooperation agreement. You entered into a cooperation
    16 agreement with -- with the Securities and Exchange
    17 Commission; is that correct?
    18 A That's correct.

16. Gover testified that he met with Johnson, Delaney and Hasty regarding Rule 204 sometime between November 2009 and July 2010.

    a. **Tr. 104:9-24** [Gover]
    9 Q And who was involved in that conversation?
    10 A I remember Mike Johnson, Tom Delaney, Holly
    11 Hasty, myself. I believe either Brian Hall and/or Rudy
    12 De La Sierra were present, but I can't conclusively say
    13 that. It's just kind of, I thought they were, but I'm not
    14 positive on that.
    15 Q Okay. And how was the problem presented in
    16 that conversation?
    17 A I am paraphrasing. But it was, okay, Stock

18 Loan is saying they don't get bought in, and then here's
19 me holding 204 and saying I've read the reg, and I don't
20 see anywhere it gives -- where it gives me an out for
21 that. So there were some discussions about, well, in
22 order to have the shares for a loan sale, they should --
23 they would have to be recalled to -- they have to be
24 recalled earlier.

17. Hasty contradicted Gover's testimony: she did not attend a meeting with Gover at which it was discussed that Stock Loan was choosing not to comply with Rule 204's close out requirements.

    a. **Tr. 1756:10-20** [Hasty]
    10 Q Do you recall ever having a meeting with [Gover]
    11 where it was discussed that Stock Loan was choosing not
    12 to close out in accordance with Rule 204?
    13 A No.
    14 Q So you don't recall that meeting ever
    15 happening?
    16 A No.
    17 Q Do you recall ever being in -- in a meeting
    18 with him and Summer Poldrack related to Rule 204 at
    19 all?
    20 A No.

18. Johnson contradicted Gover's testimony: he did not attend a meeting with Gover to discuss the possibility of recalling loans on T+2 to close out 204 fails.

    a. **Tr. 568:14-17** [Johnson]
    14 Q Mr. Johnson, did you ever have a meeting with
    15 Brian Gover where you discussed the possibility of
    16 recalling loans on T+2 to close out to 204 fails?
    17 A Never.

19. Delaney contradicted Gover's testimony: he did not attend any meeting with Gover at which Stock Loan's intentional non-compliance with Rule 204 was discussed.

    a. **Tr. 1308:3 – 1308:11** [Delaney]
    3 Q Do you recall Mr. Gover's testimony that he met
    4 with you?

5 A I do.
6 Q Do you remember ever having a meeting with Mr.
7 Gover where he discussed compliance with Rule 204?
8 Probably I asked that too broadly. Discussed a practice
9 by Stock Loan of not -- of deliberately not closing out
10 long sales of securities they had out on loan?
11 A No.

20. Alaniz described a meeting at which Gover was questioned at length by John Kenny about Rule 204 close-out failures.

    a. **Tr. 790:1-20** [Alaniz]
    1 going to be a peculiar question -- but during this
    2 meeting, was there an interaction between Mr. Kenny and
    3 Mr. Gover that you recall?
    4 A Yes.
    9 Q Okay. What was the interaction that you
    10 recall?
    11 A The interaction from John Kenny was the basic,
    12 simple question of what happened, what were they doing to
    13 remediate it, and Brian Gover replied how he was going to
    14 remediate it.
    15 Q Okay.
    16 A What the issues were and what the remediation
    17 process was.
    18 Q Did that go on for a while, this back and
    19 forth?
    20 A It was probably about 15, 20 minutes.

21. Gover denied that meeting where Kenny asked Gover about the failures in Alaniz's 3012 testing ever happened.

    a. **Tr. 154:23 – 154:16** [Gover]
    22 Q And so is that -- so if that's what you
    23 thought, do you recall there being a meeting about this,
    24 about this 3012 report?
    25 A I don't recall a meeting of it. It's not to
    1 say that there couldn't have been one. I don't recall a
    2 meeting. I don't recall a meeting, though.
    3 Q Do you -- so you don't recall a meeting where

4 Mr. Yancey was there and Mr. Delaney was there.
5 And who's John Kenny?
6 A John Kenny is the COO. I reported to John
7 Kenny.
8 Q So Mr. Kenny was there. You don't remember
9 talking about this 3012 report with -- with that cast of
10 characters? And more, but at least that?
11 A No, I don't.
12 Q And so you don't remember having an extensive
13 discussion with Mr. Kenny where he was asking you
14 about -- about these fails and what buy-ins was going to
15 do to correct the problems in this 3012 report?
16 A No, I don't.

22. Gover testified that if he had known close out failures were a Stock Loan problem he would have mentioned that in a meeting with his supervisor.

    a. **Tr. 156:13 – 157:1** [Gover]
    12 Q But if someone was calling upon you to fix this
    13 problem, you would have identified it as a Stock Loan
    14 problem, right, assuming you knew about the Stock Loan
    15 problem?
    16 A Yeah, I don't -- I don't know. It's hard for
    17 me to speculate what if on something that -- you know, a
    18 conversation that may or may not have happened five years
    19 ago.
    20 Q Well, let's go here. You wouldn't sit back
    21 while the person you reported to probed you at length
    22 about this problem and not report that some of it was
    23 Stock Loan if you knew some of it was Stock Loan?
    24 A No.
    25 Q Would you have just sat back silently?
    1 A Of course not.

23. Gover never told Kenny or anyone else that failures to close out were attributable to Stock Loan.

    a. **Tr. 153:25 – 154:21** [Gover]
    24 Q Do you
    25 attribute that to any particular part of Penson other

than buy-ins?
A Yeah. I mean, at the end of the day Penson is
responsible for the close-outs.
Q I get that. I'm just trying to figure out
if -- if wasn't buy-ins --
A What I think was happening was that Stock Loan
was recalling the shares. So they were coming back and
saying, hey, so let me take a back -- a step back. It
might be helpful to understand the process.
Q Well, let me -- instead, let me go here. So
you think this relates to that Stock Loan's -- whether
they were buying in for market open?
A I think it re- -- I think it relates to, when
Stock Loan was recalling the shares, as to whether those
shares were being recalled in time for the open or if
they were getting recalled and they were coming into the
close.

b. **Tr. 154:22-25** [Gover]
Q And so is that -- so if that's what you
thought, do you recall there being a meeting about this,
about this 3012 report?
A I don't recall a meeting of it.

c. **Tr. 155:18 – 156:1** [Gover]
you don't remember it, as you're sitting here, if you
were asked about that back at the time the 3012 report
came out, I take it you would have mentioned the Stock
Loan issue if you knew about it, right?
A If I were aware of the Stock Loan issue, yeah.
Q You for certain would have brought that up?
A If I were aware and had a belief that Stock
Loan was not doing what they should have been doing, yes,
I would have brought it up.

B. Rudy DeLaSierra was contradicted by other witnesses and testified inconsistent with his investigative testimony when he remembered events more clearly.

24. DeLaSierra entered a cooperation agreement with the Division.

    a. **Tr. 342:8-10** [DeLaSierra]
    8 Q Mr. De La Sierra, you have a cooperation
    9 agreement in this case?
    10 A Yes, I do.

25. During his testimony DeLaSierra was afraid that the Division of enforcement might charge him in the lawsuit as well.

    a. **Tr. 342:11-13** [DeLaSierra]
    11 Q And you still have a fear of being charged in
    12 this case?
    13 A Yes. I don't know what's going to happen.

26. Although DeLaSierra believed Delaney knew about Stock Loan's practice, the only concrete information that he pointed to that would have made Delaney aware of the practice was that Penson's Stock Loan department still had counterparties.

    a. **Tr. 272:1-23** [DeLaSierra]
    1 Q And -- and then, I guess, a couple of weeks
    2 later he kind of followed up with you and asked if you
    3 were getting counter pressure --
    4 A Correct.
    5 Q -- still?
    6 A Correct.
    7 Q And at that meeting did you say, no, and he
    8 said forget the rule then, you're fine?
    9 A No. He knew we weren't buying in at the open.
    10 Q How -- when you say he knew we weren't buying
    11 in at the open, what do you mean?
    12 A Mike had told him already that we -- our
    13 counterparties were not accepting morning buy-ins,
    14 and we were -- we were going -- we were -- we were the
    15 lost counterparties, and we tried to buy in against
    16 the recall letter or the MSLA, the securities loan
    17 agreement.

18 Q Okay. How does any of that inform him that
19 you're -- that you're not buying in at the open?
20 A Well, we still have counterparties.
21 Q But your counterparties don't stop you from
22 buying in at the open?
23 A No, they don't.

27. DeLaSierra's testified that he did not discuss the requirements for Rule 204 with Eric Alaniz.

    a. **Tr. 264:21 – 265:7** [DeLaSierra]
    20 Q So in 2009 during Mr. Alaniz's audit, you
    21 didn't tell him no, our understanding is the rule allows
    22 us to buy in at market close?
    23 A I don't think that came up.
    24 Q You don't think he had that conversation with
    25 you about what was required of Rule 204?
    1 A Correct.
    2 Q Okay. Are you sure of that?
    3 A On the loan sale piece, I never had a
    4 discussion with Eric Alaniz about it.
    5 Q You never had a discussion about when close-out
    6 was required under Rule 204?
    7 A On the long sale portion, no.

28. Alaniz testified that DeLaSierra met with him and discussed Rule 204 and the closeout requirements.

    a. **Tr. 750:6-16** [Alaniz]
    6 when you first met with Stock
    7 Loan, who was there?
    8 A Rudy De La Sierra and Brian Hall.
    9 Q Okay. And in the first meeting with them, did
    10 you discuss the rule?
    11 A I discussed my interpretation of the rule.
    12 Q And what did you tell them that you -- you
    13 understood the rule to require?
    14 A I understood the rule to require if there were
    15 any fails of T+4 or T+6, that the position in question
    16 must be bought in at -- prior or at market open.

29. DeLaSierra acknowledged the Alaniz's understanding of Rule 204, that close-outs must be completed by market open on T+4 or T+6, was correct.

    a. **Tr. 751:13-25** [Alaniz]
    13 A No, they did not. Brian Hall was silent. Rudy
    14 De La Sierra indicated that that was not his
    15 interpretation of the rule.
    16 Q Okay. What did he tell you his interpretation
    17 was?
    18 A He did not. He just stated that my
    19 interpretation was not the correct interpretation. So at
    20 that point, so there wouldn't be any, I guess, head
    21 butting or trying to, I guess, to avoid any type of
    22 confusion, I let them take the rule with them. I told
    23 them to read it, sleep on it, and the next day we would
    24 reconvene and we would decided what -- what they thought
    25 the understanding of the rule was.

    b. **Tr. 752:3-10** [Alaniz]
    3 Q That next day meeting, what happened?
    4 A The next morning, I was called up. I can't
    5 remember who called me up. I met with Brian Hall, Rudy
    6 De La Sierra, and they brought in Matt Butane and I went
    7 over with Doug Gorenflo. And as soon as we arrived, I
    8 asked them if they had time to read the rule. And they
    9 said yes, and they did confirm that my interpretation of
    10 the rule was correct.

30. DeLaSierra understood the requirements of Rule 204 from the very beginning of 204T, that buying in had to occur at market open on T+6.

    a. **Tr. 264:9-15** [DeLaSierra]
    9 You -- you testified that you understood from
    10 the very beginning of 204T, that it required you to buy
    11 in at market open on T+6; is that right?
    12 A Correct.
    13 Q I mean, and you -- you read the rule and -- and
    14 came to that conclusion?
    15 A Correct.

31. In DeLaSierra's first investigative testimony before the SEC, the only meeting that he mentioned that made Penson's Compliance department aware of Stock Loan's practice of not closing out Sales by market open was a meeting in early 2011.

    a. **Tr. 266:15 – 267:11** [DeLaSierra]
    15 Q All right. And when you were asked about that,
    16 you mentioned a meeting. Is that --
    17 A Oh.
    18 Q Is that accurate?
    19 A Yeah.
    20 Q And -- and the meeting you mentioned, you said
    21 it was the beginning of last year, which again you were
    22 testifying in 2012. Right?
    23 A Right.
    24 Q So you mentioned a meeting in the beginning of
    25 2011.
    1 A Yes.
    2 Q And -- and that's the meeting that you
    3 testified about when you were asked how it was that
    4 Compliance was aware, how you knew Compliance was aware
    5 of this practice?
    6 A Oh, I'm sorry. Is that a question?
    7 Q Yeah.
    8 A Yes.
    9 Q And you didn't mention any other meetings with
    10 Compliance?
    11 A Yes.

32. DeLaSierra's memory was better at the time of his first investigative testimony than it was during the final hearing.

    a. **Tr. 250:11 – 251:5** [DeLaSierra]
    10 Q Okay. Mr. De La Sierra, how many times have
    11 you now testified about this topic?
    12 A In court? I'm sorry. I don't understand.
    13 Q In on-the-record testimony or investigative
    14 testimony by --
    15 A This is my third time.
    16 Q Your third time. And the first time you

17 testified was fall of 2012?
18 A I don't believe so. I think it was in the
19 spring.
20 Q You think it was in the spring of what, 2012?
21 A I believe so, yes.
22 Q Okay. So at some point in 2012. And then you
23 testified again in 2013?
24 A Correct.
25 Q And -- and then you're testifying here today?
1 A Yes.
2 Q And tell me: Your memory, I assume, works sort
3 of like mine; that is, the closer I am to an event, the
4 better I remember it.
5 A Yes.

33. In DeLaSierra's first testimony, he said he did not consult with Compliance about Rule 204T when the rule came out.

a. **Tr. 265:15-23** [DeLaSierra]
15 So in the spring of 2012, you testified.
16 And do you recall if you were asked whether Compliance
17 knew about this practice?
18 A Yes.
19 Q Okay. You recall that you were asked that?
20 A I recall that I was asked that, yes.
21 Q And the first thing that you were asked was:
22 At the time that Rule 204T came out, did the Stock Loan
23 department consult with anyone from Compliance?

b. **Tr. 266:1-10** [DeLaSierra]
1 And what did you
2 answer?
3 A I said we did not consult with them.
4 Q Okay. So that was back in 2012. And as we
5 covered earlier, you remembered events a little bit more
6 clearly then?
7 A Yes.
8 Q And you testified that when 204T came out, you
9 didn't consult with anyone from Compliance?
10 A Consult, yes. We did not consult.

34. DeLaSierra's misread his own prior testimony into the record.

    a. **Tr. 269:23 – 270:7** [DeLaSierra]
    23 Q Who did you say attended?
    24 A Myself and Mike Johnson and Tom Delaney.
    25 Q Myself and/or Mike Johnson?
    1 A No, and Mike Johnson.
    2 Q That's -- that's what your transcript says?
    3 A The -- the transcript says "and/or."
    4 Q Okay. Does and/or -- are you saying the
    5 transcript's wrong?
    6 A I'm saying I could have -- could have said
    7 that, yes

No Other Witnesses Who Testified Opined that Delaney Knew About Stock Loan's Non-Compliant Practices.

35. Johnson does not know whether Delaney was aware of Stock Loan's practice of not closing out long sales by market open for stocks out on loan as described in Exhibit 89.

    a. **Tr. 517:19-23** [Johnson]
    19 Q And let me ask you generally, and then we'll
    20 talk specifically. Was Mr. Delaney aware that those
    21 practices we just saw in Exhibit 89 were how Stock Loan
    22 was operated?
    23 A I don't know

36. Delaney was not aware that Stock Loan had been deliberately violating Rule 204 prior to seeing the FINRA exam response in March, 2011.

    a. **Tr. 1307:9-14** [Delaney]
    9 Prior to you seeing that FINRA exam response
    10 that we showed in Exhibit 89 a moment ago, had you ever
    11 had a conversation with anyone at Penson that left you
    12 with the understanding that Stock Loan wasn't closing out
    13 long sales of securities they had out on loan?
    14 A No.

b. **1307:24 – 1308:2** [Delaney]
24 Did any conversation you ever had with Mr. De
25 La Sierra leave you with the impression that Stock Loan
1 wasn't complying with Rule 204?
2 A No.

37. Stock Loan never put any Rule 204 policies or procedures for not closing out until the afternoon of T+6 in writing.

a. **Tr. 389:21 – 390:4** [Wetzig]
21 Q So Mike Johnson developed the procedure by
22 which you would not close out until afternoon of T+6?
23 A Correct.
24 Q And did he communicate that to you in writing
25 ever?
1 A Not that I'm aware of.
2 Q That was just an oral understanding among the
3 Stock Loan folks?
4 A That is correct.

<u>During Eric Alaniz's 3012 Exam Process, No One from Stock Loan Informed Alaniz About the Deliberate Rule 201 Violations.</u>

38. In preparation for testing in 2009 and 2010, Alaniz met with Stock Loan to learn about their Rule 204 process.

a. **Tr. 749:1-20** [Alaniz]
1 to the meetings that you had. What was the purpose of
2 meeting with the Stock Loan department?
3 A The purpose of meeting with any department in
4 this search, under these circumstances with the Stock
5 Loan, was to ensure that I understood the rule
6 completely. Not completely as -- completely as to what I
7 was going to test.
8 Q All right. You've read the rule?
9 A I've read the rule.
10 Q So -- so you said that you met with him to make
11 sure you understood it. How did meeting with him help
12 you understand it?
13 A Well, Reg SHO -- Regulation SHO was new to me.

14 The rule was new at the time. So since they were the
15 business unit that dealt with this rule on a daily basis,
16 I wanted to make sure that I understood it as I read it.
17 As them being the individuals that would be applying this
18 rule, I wanted to make sure we were on the same page so
19 that I wasn't testing one thing when they thought I was
20 testing another.

39. Although he explicitly told them he was testing Rule 204, no one in the Stock Loan department at Penson told Alaniz that their operations were inconsistent with the rule.

    a. **Tr. 752:11-23** [Alaniz]
    11 Q Okay. At any point during that meeting, did
    12 they tell you that they -- that their operations were
    13 inconsistent with your interpretation of the rule?
    14 A No.
    15 Q Would that have affected your testing?
    16 A Yes.
    17 Q How?
    18 A That would have affected my testing in a manner
    19 where I probably would have been a little more alerted.
    20 I probably would have asked them what their procedures
    21 were, although they gave no indication that there was any
    22 other procedures besides my understanding of that.
    23 That's how it would -- what would have alerted me.

40. Stock Loan misled Alaniz by not mentioning their non-compliant procedures with regard to Rule 204.

    a. **Tr. 745:15-23** [Alaniz]
    15 Q What about, did your test focus primarily on
    16 buy-ins -- on the buy-ins function?
    17 A I didn't make -- yes, it did, but at the time,
    18 I didn't make any distinction between what I was going to
    19 focus on. It was just buy-in. The focus was to ensure
    20 that the rule was being adhered to.
    21 Q Okay. And you constructed the test as best you
    22 could to -- to attempt to test that, correct?
    23 A Yes.

41. Both Stock Loan and Buy-Ins knew the Rule 204 close-out requirements.

a. **Tr. 101:17-23** [Gover]
17 Q Who at PFSI knew about Rule 204(a) and the
18 obligations to -- to close out that we just discussed?
19 And I'll just throw it out. Did buy -- did the buy-ins
20 department know that?
21 A Yes.
22 Q Did the Stock Loan department know that?
23 A Yes.

b. **Tr. 202:6-14** [DeLaSierra]
6 Q Mr. De La Sierra, were you aware of when the
7 rule required close-outs of long sales?
8 A When 204T went into place?
9 Q Yes, sir.
10 A Yes.
11 Q What time did the rule require close-outs?
12 A Market open of T6.
13 Q And that wasn't Stock Lending's practice?
14 A Correct.

c. **Tr. 536:3-6** [Johnson]
3 Q And -- and your reading of the rule was that it
4 required close-out by market open on T+6?
5 A My reading of the rule as it pertained to long
6 sales and CNS, yes.

42. During the meeting with Stock Loan, which purportedly occurred after the initial meetings with Delaney related to difficulty of complying with Rule 204, no one indicated that Delaney told them they didn't need to comply with Alaniz's interpretation of Rule 204.

a. **Tr. 752:24 – 753:5** [Alaniz]
24 Q Did -- during this meeting, did either Rudy De
25 La Sierra or Brian Hall tell you, "Hey, we met with Tom
1 Delaney and he told us that we don't need to comply with
2 your interpretation of that rule"?
3 A No.
4 Q Did anyone ever tell you that from Stock Loan?

5 A No.

43. During Alaniz's meeting with Stock Loan, no one discussed contrary industry practice; for example, that in the industry, other firms weren't closing out by market open.

    a. **Tr. 753:6-11** [Alaniz]
    6 Q Did anybody during this meeting mention any
    7 sort of contrary industry practice, that in the industry,
    8 people weren't closing out --
    9 A No.
    10 Q -- by market open?
    11 A No.

44. Following the meeting with Stock Loan, Alaniz had no reason to suspect that Stock Loan wasn't buying in at market open.

    a. **Tr. 753:12-15** [Alaniz]
    12 Q And when you left that meeting, did you have
    13 any reason to suspect that Stock Loan wasn't buying in at
    14 market open?
    15 A No.

45. Alaniz prepared the initial draft of the 3012 summary report (Exhibit 135).

    a. **Tr. 856:22 – 857:5**[Alaniz]
    22 Q Okay. You prepared the initial draft of that,
    23 right?
    24 A Of that, yes.
    25 Q Yes.
    1 Using the template, as you mentioned?
    2 A Correct.
    3 Q And there was the section in that template for
    4 key Compliance items, right?
    5 A I would have to review it. I can't recall.

46. Alaniz included what he thought were key issues on the 3012 summary report. Delaney generally took Alaniz's suggestions on what to include.

    a. **Tr. 858:20-25** [Alaniz]
    20 Q So if you had thought it was an important issue

21 and should have been included, you had the ability to
22 tell him to include it?
23 A Yes.
24 Q Or suggest it anyway?
25 A Suggest it, yes.

47. Alaniz kept testing results and documentation in folders and kept them at Penson. These documents were reviewed by regulators, including FINRA.

    a. **Tr. 804:12 – 805:3** [Alaniz]
    12 Q Let me ask you one quick question. That binder
    13 that we looked at, that 301 in Exhibit 70, those results
    14 from your testing, did you keep that around?
    15 A How so?
    16 Q I mean, did you -- did you shred them as soon
    17 as you were done?
    18 A No, I would put all my documentation in folders
    19 and keep them there.
    20 Q And why -- why is it that you'd keep them
    21 there?
    22 A Well, they were able to be reviewed by the
    23 regulators, FINRA specifically.
    24 Q Okay. So FINRA can come in and ask for it and
    25 you --
    1 A Exactly.
    2 Q Did that ever happen when you were at Penson?
    3 A Yes.

48. By the time of the March 2010 meeting, Alaniz believed the problem with the Buy Ins function was in the process of being remediated.

    a. **Tr. 793:24 – 794:4** [Alaniz]
    24 Q And so while you had a test that showed a
    25 problem with that buy-ins function, I think we saw that
    1 you had already been getting preliminary results back
    2 from, say, Summer Poldrack saying that things were
    3 getting better; is that about right?
    4 A Yes.

b. **Tr. 795:17-21** [Alaniz]
17 Q Okay. So whether they were -- had been in
18 substantial compliance when you did your testing, you
19 understood they were on the road to substantial
20 compliance when you were in this meeting; is that right?
21 A Yes.

49. Stock loan was responsible for carrying out remediation.

a. **Tr. 783:6-17** [Alaniz]
6 Q And why is it that you had the business unit
7 take care of the remediation plan?
8 A Well, since they knew their business better,
9 like Sendero, I don't know what automation they had.
10 There are items that I'm not privy to that they may have
11 some type of system to reconcile. Those were examples of
12 what I wanted to see. How they got to that end really
13 wasn't that concerning to me as far as they got there and
14 they were in compliance with the rule.
15 Q I mean, because you didn't really know their
16 processes as well as they did, right?
17 A Right.

b. **Tr. 784:25 – 785:4** [Alaniz]
25 Was it typical of your experience in -- as a
1 Compliance Officer that you would identify problems and
2 the business units would come up with the most efficient
3 solutions to -- to solve those problems?
4 A It was typical, yes.

The April 2010 Response to OCIE Reflected Remediation Efforts for Buy-In Issues Following the 3012 Testing.

50. The April 2010 OCIE Response indicated that the buy-in issue had been rectified, including specific steps that were being taken to correct the problems.

a. **Tr. 1274:1-15** [Delaney]
1 the OCIE exam. How long had that OCIE exam been going on
2 at the point at which this letter took place?
3 A Since January of 2009.

4 Q So a little over a year?
5 A A year and a quarter, let's -- yeah.
6 Q Let me now direct your attention to that second
7 bolded paragraph. And -- and maybe I'll have you read
8 that into the record.
9 A "This issue has been rectified by advancing the
10 start of the report generation in order to provide the
11 buy-ins department and Stock Loan desk earlier access to
12 the data. The Stock Loan desk has also begun sending
13 partial borrow lists rather than sending the entire
14 borrow list on completion. The earlier timing of Report
15 643 has been in effect since March 22nd, 2010."

51. Remediation efforts following the December 2009 3012 testing were underway by the time the April 2010 OCIE response was drafted.

a. **Tr. 1269:12-20** [Delaney]
Q And after the audit, I think you testified
13 earlier there was some remediation?
14 A There was.
15 Q Or maybe you didn't testify earlier. Maybe I'm
16 misremembering.
17 A I think I recall I did.
18 Q Had the remediation begun by the date of this
19 letter?
20 A It absolutely had begun.

b. **Tr. 1275:19 – 1276:9** [Delaney]
19 A Well, the issue -- we're reporting that the
20 issue had been rectified by advancing the start of the
21 report generation in order to provide the buy-in
22 department and Stock Loan desk earlier access to the
23 data, which ties in here to Summer's e-mail to Eric
24 stating that they've -- that Stock Loan had been going
25 out of their way to either borrow on T+3 or get the
1 report to them earlier on T+4; and that since, they've
2 been able to have the executions to trading by 8:30 in
3 the morning, which is market open.
4 Q Let me ask you the date of this e-mail. And by
5 this e-mail, I mean Exhibit 321.

6 A January 22nd, 2010.
7 Q So that was between the -- Mr. Alaniz's 3012
8 exam and the time you responded back to OCIE?
9 A Yes.

52. At the time of the April 2010 OCIE response, Delaney was not aware of any practice by Stock Loan for not closing out long sales of loaned securities by market open on T+6.

    a. **Tr. 1276:15-20** [Delaney]
    15 Q Were you aware of any practice by the Stock
    16 Loan Department, at the time this letter was sent out in
    17 April of 2010, any practice by the Stock Loan Department
    18 of not closing out long sales of these loaned securities
    19 by -- by market open on T+6?
    20 A No.

Email Correspondence In July 2010 Suggests Compliance Was Not Aware of Stock Loan's Practices.

53. In July 2010, Poldrack sent an email to Hasty, Reilly and Gover (Ex. 91) indicating that Stock Loan stated that "Stock Loan isn't to be bought in…"

    a. **Tr. 818:4-11** [Alaniz]
    4 Q All right. Then do you see the e-mail from
    5 Summer Poldrack that comes just above that on the paper,
    6 but is the next e-mail? I guess it spans Pages 1 and 2;
    7 do you see that?
    8 A Yes.
    9 Q All right. And who did she send that to?
    10 A Holly Hasty, Jerry Reilly and copied Brian
    11 Gover.

54. No one ever informed Alaniz of a policy or practice at Penson that Stock Loan wasn't to be bought in.

    a. **Tr. 818:12 – 819:4** [Alaniz]
    12 Q Okay. Kind of a random question, but at any
    13 point in the process that you went through of looking
    14 into this issue and coming up with a response, did Mr.
    15 Gover mention, "Hey, that's the policy. Stock Loan

16 doesn't get bought in"?
17 A No.
18 Q Brian Gover never volunteered that or anything
19 like that?
20 A No one ever did.
21 Q Okay. No one ever did?
22 A No.
23 Q Not just Mr. Gover? Okay.
24 So let me explore that just a little bit more.
25 You're saying in the whole process of seeing this, other
1 than that e-mail from Marc McCain, nobody ever mentioned,
2 "Hey, that's the process. You don't buy in Stock Loans
3 when they have on recall"?
4 A No, sir.

55. Alaniz did not escalate the issues arising out of the July 2010 emails to Delaney. Rather, he copied Delaney and others on the email simply to ensure he was giving correct advice.

    a. **Tr. 824:25 – 825:11** [Alaniz]
    25 Q Okay. I noticed that you copy Tom Delaney and
    1 Brian Gover and Jerry Reilly and Holly Hasty on this
    2 e-mail. Did you expect any sort of response from any of
    3 those four people?
    4 A If I had been incorrect, then I would hope that
    5 somebody would have corrected my response.
    6 Q But were you -- was this like --
    7 A At the time, I did not.
    8 Q Sorry I keep talking over you.
    9 Was that -- that wasn't to escalate it to Mr.
    10 Delaney because you thought it needed his attention?
    11 A No.

56. Alaniz, Poldrack and Hasty agreed that the penalty box is not an acceptable solution, but rather a violation in and of itself.

    a. **Tr. 819:24 – 820:13** [Alaniz]
    24 A "She is of the opinion that the penalty box is
    25 not an acceptable solution since there are other controls
    820
    1 on the back side that need to be in place to ensure that

2 we do not violate 204T."
3 Q Okay. Do you think the T might be an error
4 given that 204 had been in place for about a year at this
5 point?
6 A Yes.
7 Q Okay. Do you agree -- first of all, the "she"
8 in that sentence you just read, do you understand that to
9 refer to Holly?
10 A Yes.
11 Q All right. Do you agree with Holly's response
12 there?
13 A Yes.

b. **Tr. 822:8-12** [Alaniz]
8 I
9 go, "In that case, I agree with you that what Holly had
10 stated is correct; they should not be using the penalty
11 box as a remediation for fail violations of Reg SHO 204.
12 That is a violation in itself."

57. Alaniz understood that closing out by market open was not an option, but a requirement under Rule 204.

a. **Tr. 823:5-25** [Alaniz]
5 Q All right. And then, "Preferably this should
6 be completed prior to or at market open"; do you see
7 that?
8 A Yes.
9 Q Okay. What -- you're the one who wrote this
10 e-mail. Let's start here. First of all, do you think
11 it's optional to close out by market open?
12 A No, it's a requirement.
13 Q Okay. So this word "preferably" seems to have
14 gotten people hung up a few times. You're shaking your
15 head with a bit of a grin there?
16 A (Nods head.)
17 Q Tell me what you -- what you were trying to
18 communicate there.
19 A I prefer that they closed out these fails prior
20 to market open versus at market open because, in the

21 past, they had issues that placed it at market open and
22 it was over a minute, 30 seconds, two minutes and they
23 knew that was -- they knew, according to me, that would
24 be a violation.
25 Q 30 seconds late is 30 seconds too late –

The November 2010 Response to the OCIE Final Report was Accurate and Not Misleading

58. Every witness who testified on the topic (Gover, Alaniz, and Hasty) stood by the accuracy of the representations made in the OCIE response in November 2010.

a. **Tr. 147:17 – 148:4** [Gover]
17 A And that is the section where it says "Penson
18 feels that the processes and proceedings and options" --
19 Q Yes.
20 A That looks like something I could have written.
21 Q Okay. When you -- when you wrote that, you
22 would have understood that was going to FINRA, right?
23 A Yes.
24 Q And when you wrote that, did you believe it was
25 accurate?
1 A Yes.
2 Q And as you sit here today, is there any reason
3 to think that it's not accurate?
4 A No.

b. **Tr. 828:23 – 829:4** [Alaniz]
23 Q I'll just represent to you that S+1 is
24 settlement plus one, which is the same as T+4.
25 Based on your remediation plans that you had
1 done, did you believe that by November 2010, the firm's
2 programs were effective and reasonably designed to close
3 out short sales in --
4 A Yes.

c. **Tr. 1738:25 – 1739:10** [Hasty]
25 Q Okay. And as you sit here today, Ms. Hasty,
1 do you believe that Mr. Gover's statement that
2 "Penson's processes and procedures were effective and
3 performed as designed," do you believe that was

4 truthful and accurate?
5 A Yes.
6 Q Do you have any reason to believe that Mr.
7 Gover's statement was inaccurate?
8 A No.
9 Q Misleading?
10 A No.

d. **Tr. 1739:11-23** [Hasty]
11 Q Okay. And I believe Michael pulled back up
12 the language from 101. That's the final response.
13 Looking again at the language in the final response,
14 "Penson believes that," do you believe that his -- Mr.
15 Gover's statement that, "Penson believes that the
16 reasonable processes employed to close out positions
17 that were allegedly in violation of Rule 204T were
18 effective and performed as designed." Do you believe
19 that that was truthful and accurate?
20 A Yes.
21 Q Do you have any reason to believe that Mr.
22 Gover's statement was inaccurate or misleading?
23 A No.

e. **Tr. 1739:24 – 1740:7** [Hasty]
24 Q Do you have any reason to believe anything in
25 this final response was inaccurate or misleading?
1 A No.
2 Q If you did believe anything in that response
3 that you signed was inaccurate or misleading, what
4 would you have done?
5 A I would have said something most likely to
6 Tom or would have -- or to the business unit or would
7 have called a meeting and said we need to discuss it.

59. The November, 2010 OCIE Response (Exhibit 101) was not inconsistent with Alaniz's testing results.

a. **Tr. 1792:1-12** [Hasty]
1 Q So when was this letter in relation -- and,
2 again, to the best of your knowledge here today, in

3 time relation to when Mr. Alaniz got it?
4 A This was after.
5 Q How much after?
6 A It would have been nearly a year, 11 months.
7 Q And do you -- what would be your expectation
8 as to whether there was any remediation done between
9 the time of testing and the time of this letter?
10 A I would have expected that there would have
11 been significant remediation done during that time
12 frame.

b. **Tr. 1739:3-19** [Hasty]
3 Q Okay. And What about Rule 204T? When was
4 Rule 204T? When did it go out of -- of effect?
5 A That, I'm not certain. July maybe 2010.
6 Q July 2010 or 2009?
7 A 2009. Sorry.
8 Q No problem.
9 So would Mr. Alaniz' testing in December of
10 2009 tell you anything about what the practices of
11 Penson were related to 204T?
12 A Yes, I would assume they would.
13 I'm sorry. Rephrase your question.
14 Q Sure.
15 204T went out in July of 2009. Would testing
16 that took place six months later tell you anything
17 about what was going on with regard to 204T?
18 A Oh, likely not. Again, modifications were
19 likely to have been made.

60. Delaney relied on information from Penson personnel that remediation was underway and that reasonable processes were in place and, as a result, believed the OCIE response was accurate.

a. **Tr. 1285:5-23** [Delaney]
5 Q Let me do that. Why? Why don't you think this
6 is inconsistent?
7 A Penson -- Eric's testing results were part of a
8 compliance process of testing policies and procedures,
9 and the fact that you find errors in testing -- in

10 testing results is what you expect when you have a good
11 testing regime. I would maybe worry more if he didn't
12 find any errors at that point.
13 And certainly, I had no indicia of any other
14 processes going on beyond what was already being tested
15 and reported back on, and we were remediating and we
16 were -- and there were reports of remediating coming back
17 in. I had business unit leaders telling me, we've got --
18 we've got this -- these -- sorry -- we've got these
19 reasonable processes in place.
20 So there was just no -- there was nothing in
21 that response, where Brian reports in, that would have
22 somehow triggered to me that there was something
23 inconsistent with what Eric was reporting.

Tom Delaney Had No Reason to Suspect that Mike Johnson Was Not Being Supervised.

61. Johnson had a supervisor, and Delaney was reasonable in believing Johnson was in compliance.

    a. **Tr. 1583:13 – 1584:3** [Pendergraft]
    13 Q I want to come back to Mr. Delaney here, but
    14 first I want to -- without regard to who might have
    15 supervised him, it's fair to say Mike Johnson was
    16 supervised during his time at Penson; is that right?
    17 A Yes.
    18 Q And so as chief compliance officer Mr.
    19 Delaney wouldn't have had any reason to be concerned
    20 that Mike Johnson wasn't being supervised?
    21 A Well, I think that Mr. Delaney, when we talk
    22 about broker-dealer supervision of a supervisor of Mr.
    23 Johnson, much of it is around systems and controls and
    24 compliance monitoring. And so I think since Penson
    25 management, including Mr. Delaney, felt like we had
    1 good compliance controls and monitoring of compliance.
    2 I think Mr. Delaney had every right to believe that Mr.
    3 Johnson was in compliance.

62. Delaney believed Johnson was adequately supervised.

a. **Tr. 1219:22 – 1220:2** [Delaney]
22 Q Did you -- well, let me first ask: Was Mr.
23 Johnson supervised?
24 A He was.
25 Q In your observation, was he adequately
1 supervised?
2 A In my observation, he was.

63. There was no ambiguity that Johnson was supervised by Pendergraft.

a. **Tr. 1216:25 – 1217:10** [Delaney]
25 Q And did you have any ambiguity whatsoever about
1 who Mike Johnson reported to?
2 A No.
3 Q And who did Mike Johnson report to?
4 A Phil Pendergraft.
5 Q Were you able to observe any interactions
6 between Mr. Johnson and Mr. Pendergraft?
7 A At times, yes.
8 Q Okay. And were they consistent with a
9 supervisor/supervised relationship?
10 A From my perspective, yes.

Penson's Written Supervisory Procedures Were Written by the Subject Matter Experts in the Business Units and Were Adequate and Typical of the Industry

64. The business units, such as Stock Loan, were considered subject matter experts, and compliance personnel relied on the expertise of the business units for an understanding of the compliance issues associated with each business unit.

a. **Tr. 726:15 – 727:3** [Alaniz]
15 Q And do you rely on those business units for
16 information about what is going on at the firm?
17 A Yes.
18 Q Could you perform your job without kind of an
19 understanding or having information flow from them?
20 A No. They are the product specialist managers
21 of their assigned areas and you do rely on them.

22 Q You said they're the specialists. What do you
23 mean by that?
24 A They're -- they're the owners. They do their
25 job on a daily basis. I guess I'll -- you would assume
1 that they would know how it would work.
2 Q And who knows their job better, you or them?
3 A I would say them.

b. **Tr. 1220:20 – 1221:10** [Delaney]
20 Q Who did you rely on?
21 A Various groups. So I had my own staff, of
22 course, that I would rely on, as well as I would rely on
23 the subject matter experts within the -- within the
24 business.
25 Q When you say "subject matter experts," what
1 does that mean to you?
2 A To me, that would be at Penson, lot of moving
3 parts, a lot of -- a lot of departments with specific
4 processes and procedures and things of that nature. And
5 so those -- those leaders in that business group -- these
6 would be generally the registered principals within those
7 business groups -- would have -- would be those -- that
8 key subject matter. I mean, they would know more --
9 they -- they would forget more about their department and
10 how it operates than -- than I'd ever hope to know.

65. At Penson, creating WSPs was the responsibility of the business units, as was reviewing those WSPs to be certain they accurately reflected the business practices of the business unit.

a. **Tr. 1758:3-10** [Hasty]
3 Who was it who was
4 responsible for generating the WSPs related to a
5 business unit?
6 A So it was a responsibility of the business
7 unit to convey to compliance what they were doing, how
8 they were supervising their business, what documents
9 they were using to evidence supervision of their
10 business.

b. **Tr. 1758:13 – 1759:2** [Hasty]

13 Q Why is it that the business unit originated
14 that?
15 A Well, they're the experts. They are the
16 people who are doing this day to day. As Compliance
17 Officers, we're not experts in every area of the
18 business. We don't sit at someone's desk and process
19 buy-ins or use the reports or, you know, escalate
20 certain items to our supervisors. We're unfamiliar
21 with the process. We're unfamiliar in general with
22 what they're doing on a day-to-day basis. So it's
23 absolutely is necessary to have the business owners be
24 the original people who are drafting those WSPs and
25 providing the information so that we can make sure it's
1 accurate and that it includes what's really being done
2 day to day.

c. **Tr. 807:8-16** [Alaniz]

8 Why is it that the business owner would --
9 would make changes to a WSP?
10 A I would call them preliminary changes. You
11 would want to have them review it to ensure that if it
12 states that they're doing A, when in actuality, they're
13 doing B, you want that to be adjusted. That's why you
14 would want them to review it; so in the event the
15 regulators would come in and they do ask for WSPs, we are
16 doing what we are saying and not –

d. **Exhibit 312**

66. At Penson, the Stock Lending and Buy-Ins groups understood Rule 204 best.

a. **Tr. 749:21 – 750:3** [Alaniz]

21 Q Okay. And who would you say at -- in all of
22 Penson knew Rule 204 best, or who did you -- who was
23 it -- did you expect to know it best?
24 A I expected those business units to know it the
25 best.
1 Q And the business units were the
2 operations/buy-ins group --

3 A And the Securities Lending department.

67. Penson's WSPs were adequate and typical of the industry.

a. **Tr. 1993:16 – 1994:13** [Poppalardo]
16 A Okay. Yes, I did look at PFSI's policies and
17 procedures. And I think what I would say is you start
18 with, you know, as a general matter, you look at all of
19 the key elements of the rule, and you make sure that
20 those are reflected in the policies and procedures and
21 to -- for the Reg SHO, certainly the important things
22 are, you know, that the orders be marked correctly,
23 locate and delivery requirements, close-out
24 requirements and the penalty box restrictions. And I
25 saw all of those elements in the PFSI policies, albeit
1 in not necessarily a single policy because there are
2 separate and distinct responsibilities within different
3 groups in PFSI.
4 Q How did they compare to what you've seen in
5 the industry with respect to policies and procedures?
6 A Relating to Reg SHO, I think their policies
7 and procedures overall were very comprehensive. And
8 we've seen better, but, you know, they're -- they're
9 perfectly adequate. In connection with Reg SHO, it's a
10 really complicated area. I see a lot of policies and
11 procedures and it took me a really long time to parse
12 through them, but I do think that -- I think they were
13 okay.

b. **Tr. 2039:23 – 2040:6** [Poppalardo]
23 Q Can you tell me, did anything in the
24 cross-examination questions that Ms. Atkinson asked
25 change your opinion that PFSI policies and procedures
1 were consistent with what you saw in the industry?
2 MS. ATKINSON: I'm going to object to that as
3 leading.
4 JUDGE PATIL: Overruled.
5 A No, I -- I think they're consistent with --
6 with other policies and procedures that I've seen.

Tom Delaney Did Not Authorize Any Violation of Rule 204 and Violations Persisted After He Escalated the Issue to Outside Counsel and After He Left Penson

68. Delaney never authorized any Penson employee not to comply with Rule 204 or 204T.

    a. **Tr. 1757:23 – 1758:1** [Hasty]
    23 Q Did you ever see
    24 him -- and the "him" here is Tom Delaney. Did you ever
    25 see him accept anyone deliberately violating any rule?
    1 A No.

    b. **Tr. 272:24 – 273:3** [DeLaSierra]
    24 Q Okay. So -- and I just want to be as clear as
    25 I can be on this. Are you -- are you aware of any time
    1 that Mr. Delaney said, don't worry about it, don't comply
    2 with Rule 204T or 204?
    3 A No.

69. Indeed, Delaney circulated an email regarding the adoption of Rule 204 to Penson personnel informing them of the requirements of the Rule (Exhibit 125).

    a. **Tr. 522:4-8** [Johnson]
    4 Q Mr. Johnson, do you recognize Exhibit 125?
    5 A Yes.
    6 Q And what is Exhibit 125?
    7 A It's Tom sending a note out saying the
    8 specifics of Rule 204.

    b. **Tr. 523:13-17** [Johnson]
    13 Q Is that the sort of interpretation you were
    14 referring to --
    15 A Yes, sir.
    16 Q -- earlier from Mr. Delaney?
    17 A Yes, sir.

70. The memo Delaney Circulated Related to Rule 204 was copied almost word-for-word from a bulletin issued by Penson's counsel.

    a. **Tr. 1256:5-17** [Delaney]
    5 Q Have you had a chance to compare the language

6 in Exhibit 425A with the language in Exhibit 125?
7 A I have.
8 Q Are they at all similar?
9 A They're nearly identical.
10 Q Okay. What does that mean to you?
11 A That this was the -- this was the source
12 information for which I took and made the larger
13 distribution in my communication.
14 Q When you say, "they're largely identical," you
15 mean, like, word-for-word you copied large portions of
16 Exhibit 425A?
17 A I did.

71. Following Delaney's call with outside counsel, Penson did not change its practices with respect to Rule 204. In fact, the violations continued after Delaney left Penson.

a. **Tr. 273:25 – 274:5** [DeLaSierra]
25 Q Okay. So -- and -- and Mr. Delaney had talked
1 to outside counsel, it is your understanding, and -- and
2 then Mr. -- Mr. Wetzig and Mr. Hall came back from that
3 meeting. And -- and I -- and I take it at that point
4 that -- that these violations stopped?
5 A No.

b. **Tr .274:22-24** [DeLaSierra]
22 Q And did -- just so we're clear, did this --
23 this pattern, did that persist after he left?
24 A Yes.

c. **Tr. 403:8-11** [Wetzig]
8 Q Did you -- did Stock Loan change of any of its
9 practices after the phone call, with respect to 204
10 closeouts?
11 A No, not that I'm aware of.

72. Penson did not violate Rule 204 for a profit motive.

a. **Tr. 539:23 – 540:11** [Johnson]
23 Q Are you aware, Mr. Johnson, that the SEC
24 alleges in this lawsuit that the reason Penson was

25 violating Rule 204 was for a profit motive? Have you
1 heard that?
2 A Yes.
3 Q What do you think about that?
4 A I think it's bull crap.
5 Q In your view, was there material economic
6 benefit to Penson for the conduct they're alleged to have
7 committed with respect to Rule 204?
8 A I think what you're saying is, was it worth it
9 if we broke the rule. No. We wouldn't -- we didn't do
10 the rule because we didn't understand how to do it. We
11 did not do it for money.

b. **Tr. 256:9-24** [DeLaSierra]
9 Q Okay. Did having these -- these loans out and
10 the potential to make interest, did that have anything to
11 do with whether you were complying with Rule 204?
12 A No.
13 Q So no profit -- you're saying that profit
14 didn't really calculate into it at all?
15 A No.
16 Q Are you aware that -- that the Division of
17 Enforcement here has said that this was about profit,
18 that -- this practice you were undertaking?
19 A I'm not, no.
20 Q Okay. But you told them the exact opposite of
21 that, right? Have you testified that profit didn't
22 come --
23 A The Stock Loan department was not motivated by
24 that.

Compliance with Rule 204 is Complex and the Systems Used by Penson to Comply with the Rule Had Minor Flaws.

73. Compliance with Rule 204 is very complex and difficult and not many firms get it right.

a. **Tr. 138:7-25** [Gover]
7 Q Would you describe Rule 204 -- I guess let's
8 start Reg SHO generally, as -- as simple?
9 A No, it's very complex.

10 Q Okay. When you say "it's very complex," what
11 do you mean?
12 A The implementation of it is -- you know,
13 operationally, it's very difficult, and I think that
14 there's not many firms that really get it right. When
15 you've got -- you know, you're clearing, selling, you
16 know, hundreds of thousands to millions of trades a day,
17 and you've got hundreds of thousands to millions of
18 customer accounts on your books, when you do have a CNS
19 deficit, going in and ascertaining which account or
20 accounts caused that deficit and -- and how the treatment
21 needs to be done on it, it's difficult.
22 I think the rules -- the rules remain the same,
23 but the interpretive guidance that's put out is evolving
24 and, you know, it's -- we spend a lot of our energy on
25 Reg SHO.

74. The Division's expert, Professor Harris, testified that footnote 55, an advisory note to Rule 204, is not at a part of Rule 204(a).

a. **Tr. 1114:19-24** [Harris]
19 Q Were you -- do you know Footnote 55?
20 A I've been exposed to it, yes.
21 Q True or false: It is a violation of Rule 204
22 if you do not recall a long sale loan security on T+2?
23 A The footnote does not require you -- the rule
24 does not require you to recall on T+2.

b. **Tr. 1115:9-11** [Harris]
9 A As I stated before, the rule does not require
10 that you recall on T+2. Accordingly, if you don't recall
11 on T+2, you haven't violated any rule.

75. If Penson had 99 percent compliance with the close-out requirements under Rule 204(a), it would be fair to assume that Penson had a reasonable system in place to ensure compliance.

a. **Tr: 2003:16 – 2004:1** [Poppalardo]
16 If Penson complies with the close-out requirements
17 for Rule 204(a) over 99 percent of the time for long

18 sales of loan securities, would this suggest to you
19 that they have a reasonably designed supervisory system
20 for Rule 204(a)?
21 A I -- I think that might be -- I think that
22 might be fair. It's really -- you know, it's so
23 dependent on the rule and what the rule is trying to
24 accomplish. But I think a 99 percent, you know,
25 compliance rate is a fair assumption that they have a
1 reasonable system.

76. Sendero was built for Penson as a front-end software stock loan system, which would generate reports for failures to deliver.

a. **Tr. 229:14-24** [DeLaSierra]
14 Q What was Sendero?
15 A Sendero started building in 2005. The -- the
16 primary focus of Sendero initially was for locates.
17 We -- we had a large locate volume.
18 Q Did Sendero play any role with respect to the
19 204?
20 A Yes.
21 Q And explain that.
22 A Well, that -- that's what we would query to
23 generate our reports for fails, whether they be versus --
24 long sales versus CNS for short sales.

b. **Tr. 365:9-10** [Wetzig]
9 A So Sendero is essentially a front-end software
10 of a Stock Loan system that was built for Penson.

77. Sendero was heavily relied upon by Stock Loan with regard to timing of recalls.

a. **Tr. 234:23 – 235:4** [DeLaSierra]
23 What was your sense of
24 Sendero's accuracy, reliability?
25 A I felt it was very reliable.
1 Q So if Sendero was telling you there was a fail
2 due to an open Stock Loan, did you have confidence in
3 that?
4 A Yes, we did.

b. **Tr. 365:11-17** [Wetzig]

11 Q And in your experience, did you have experience
12 to work with Sendero?
13 A I did.
14 Q And in your experience, was it -- did it seem
15 to be an accurate system at telling you whose
16 responsibility, whether it was a short or a long?
17 A Yes. Sendero was a very accurate system.

c. **Tr. 372:21-24** [Wetzig]

21 When you talked about the recall on T+3, was that
22 something, again, that -- that Sendero did?
23 A Correct. On T+3, Sendero would tell us what we
24 needed to recall.

d. **Tr. 364:22 – 365:5** [Wetzig]

22 How would you know whether
23 an open obligation was due to a customer's short sale or
24 a -- a long sale, there -- that there was a stock loan
25 outstanding on?
1 A So our system would tell us what to recall and
2 look to see if there was a CNS obligation versus, say, a
3 loan.
4 Q And was there a name for that system?
5 A That system was called Sendero.

e. **Tr. 365:18-25** [Wetzig]

18 Q So on T+3, was there some process to look at
19 Sendero to figure out if there was obligations that Stock
20 Lending would have on an -- on an existing fail to
21 settle?
22 A Yes. So Sendero, we essentially had a recall
23 screen, and we -- it was, I guess, query-based, and it
24 would tell us what we need to recall versus our
25 obligations.

78. Sendero was only 95 percent accurate.

a. **Tr. 374:18-20** [Wetzig]
18 Q Do you have a sense of -- can you put that in a
19 range of accuracy, how accurate it seemed to be?
20 A I would say 95 percent.

Penson's Compliance Personnel were Qualified and Well-Trained.

79. Scott Fertig was co-CCO at Penson until December 2008.

a. **Tr. 1717:16-25** [Hasty]
16 Q And who did you view as having responsibility
17 for Rule 204 compliance?
18 A You know, I don't know that there was a
19 specific person that was assigned to Rule 204
20 compliance. And that was much like a lot of our
21 different areas. It fell within the operational group,
22 and initially at the time that we received the exam
23 notice for this, it was originally assigned to Scott
24 Feretig, who was the head -- one of the co-CCOs and
25 head of the operational group.

b. **Tr. 1700:19-20** [Hasty]
19 A It did. In December of 2008, Scott Fertig
20 left the firm, and Tom took over the majority.

80. Scott Fertig currently works for the Securities and Exchange Commission.

a. **Tr. 833:24-25** [Alaniz]
24 Q Do you know where Scott Fertig works currently?
25 A The SEC.

81. Prior to joining Penson, Gorenflo worked as an examiner at FINRA, and has a reputation as black-and-white, never crossing the foul line.

a. **Tr. 1267:14-18** [Delaney]
14 Did you mention that Mr. Gorenflo had
15 worked at FINRA?
16 A He had previously worked at FINRA, yes.

17 Q Okay. Do you know what his role was at FINRA?
18 A He was an examiner.

b. **Tr. 1268:6-11** [Delaney]
6 Q Did Mr. Gorenflo, in your observation, ever
7 come close to the line, whatever that phrase might mean
8 to you?
9 A Doug Gorenflo is very much a black-and-white
10 kind of guy, and he never -- never came close to crossing
11 the foul line.

82. In its OIP, the Division alleged that Penson systematically violated Rule 204T(a)/204(a) from October 2008 until November 2011.

a. **OIP at 10**
"Penson systematically violated Rule 204T(a)/204(a)'s market-open CNS close-out requirement for long sales of loaned securities from October 2008 until November 2011."

b. **OIP at 18**
"From October 2008 until November 2011, Penson systematically failed to close out CNS failures to deliver resulting from long sales of loaned securities by market open T+6."

83. Wetzig did not have any discussions with Delaney pertaining to Rule 204 prior to the phone call with outside counsel.

a. **Tr. 402:21 – 403:2** [Wetzig]
21 Q Did you have -- did you have discussion -- were
22 the context of your discussions with Mr. Delaney, prior
23 to the phone call with outside counsel, in the context
24 that Stock Loan believed they could opt into the penalty
25 box rather than close out by T+6?
1 A I did not have any discussions with Tom Delaney
2 prior to the phone call.

84. Mike Johnson was the head of Stock Loan, and managed Stock Loan personnel, including DeLaSierra, Hall and Wetzig, among others.

a. **Tr. 93:18-24** [Gover]
18 Q Okay. Who -- who were the main Stock Loan
19 people while you were -- between 2009 and -- and the end
20 of 2011?
21 A Mike Johnson, Rudy De La Sierra, Brian Hall,
22 Lindsey Wetzig.
23 Q Who was the head of Stock Loan at that time?
24 A Mike Johnson.

b. **Tr. 213:9-19** [DeLaSierra]
9 Q All right. So let's talk about -- we just
10 talked for a minute about the mechanics of how stock
11 lending worked and the importance of stock lending to
12 Penson. I want to talk now about the people who were in
13 stock lending at Penson. So between 2008 and 2011, who
14 were the other folks that worked in stock lending at
15 Penson Financial Services?
16 A Mike Johnson.
17 Q Okay. Anyone else?
18 A Brain Hall, Lindsey Wetzig, Terry Ray, Marc
19 McCain, Logan Satterwhite and Dawnia Robertson.

85. Wetzig testified that he knew a lot about the requirements of Rule 204 since the rule first came out.

a. **Tr. 384:5-23** [Wezig]
5 Q So you -- you know a lot about requirements for
6 Rule 204, correct?
7 A Correct.
8 Q And when did you learn about those
9 requirements?
10 A The rule first came out in the financial
11 crisis, so we learned -- started to learn about it then.
12 Q So did -- you -- you were given information you
13 needed, to comply with the rule, when it came out or you
14 learned about it --
15 A The rule came out in 2008. At that point, we
16 had the rule.
17 Q Okay. And how did you -- how did you learn of
18 the rule?

19 A We looked at the rule and read the rule.

86. Wetzig then gave contradictory testimony that he didn't know how to comply with Rule 204.

a. **Tr. 403:23-25** [Wetzig]
23 Q You've admitted here today that you just
24 disregarded the rule; isn't that right?
25 A We didn't know how to comply with the rule.

87. Even after the call with counsel in early 2011, Stock Loan did not change its practices and understood that they were violating Rule 204.

a. **Tr. 410:20-20** [Wetzig]
10 Q And while the requirement of closing out by the
11 morning of T+6 wasn't ambiguous, were you saying that
12 your systems weren't clear on how to accomplish that?
13 What did you mean, "we did not know how to comply?"
14 A We did not know that we were supposed to recall
15 on T+2.
16 Q Was that the only difficulty that you had with
17 complying with the rule?
18 A Yes, sir. That was the main issue with
19 complying with the -- the rule, to close out in the
20 morning of T+6.

b. **Tr. 410:22 – 411:2** [Wetzig]
22 that while the department was violating the rule, at some
23 point in 2011, you participated in a call with outside
24 counsel about what the department was doing, and that
25 after the call, the department did not change its
1 practices?
2 A Yes, sir.

c. **Tr. 411:8-10** [Wetzig]
8 Q Did you believe that you were violating the
9 rule, as you understood the rule?
10 A Yes, we did.

88. Johnson settled with the Division, and was not required to pay disgorgement.

a. **Tr. 562:24 – 563:1** [Johnson]
24 Q Okay. My last question, Mr. Johnson: Did you
25 settle with the SEC in or about March of this year?
1 A Yes.

b. **Tr. 533:4-5** [Johnson]
4 A When -- when -- well, I think it's way off
5 because in my settlement, there was no disgorgement so,

89. Wetzig settled with the Division and agreed to cooperate.

a. **Tr. 403:15-22** [Wetzig]
15 You settled with the Division, in this matter,
16 didn't you?
17 A That is correct.
18 Q And does your settlement agreement identify
19 that you intentionally -- it has facts showing that you
20 intentionally violated Rule 204, correct?
21 A No. I don't believe that it intentionally is
22 in there.

b. **Tr. 404:14-16** [Wetzig]
14 Q And you agreed to cooperate in -- in that
15 settlement agreement, didn't you?
16 A Correct.

90. Wetzig was not ordered to pay any penalties or disgorgement, or to be barred from the industry as part of his settlement with the Division.

a. **Tr. 404:4-13** [Wetzig]
4 You -- you received a relatively light
5 sanction, didn't you?
6 A If that's how you want to interpret it.
7 Q Well, you didn't -- no disgorgement was
8 ordered, correct?
9 A That's correct.
10 Q No penalties, correct?
11 A That's correct.

12 Q No -- no bars, right?
13 A Correct.

91. Poppalardo testified that compliance need not be perfect. In fact, there is an acceptable margin of error, based on supervision and whether the underlying activity was reasonable.

    a. **Tr. 2001:19 – 2002:4** [Poppalardo]
    19 You're not indicating there that compliance
    20 needs to be perfect, are you?
    21 A Compliance doesn't need to be perfect, but
    22 the systems and compliance with the rules, you are
    23 expected to comply with the rules 100 percent. I think
    24 the -- the acceptable margin of error comes in whether,
    25 you know, your supervision of the underlying activity
    1 was reasonable or not. You can't be expected to review
    2 every transaction within a firm. And so it's not
    3 unlikely that there would be a transaction or a few
    4 transactions that might not comply.

92. The Rule 204 violations at issue equal approximately $77.00 per day for the relevant time period (October 2008 – October 2011), based on a total of 252 trading days per year. Based on the date range stipulated for Delaney (see **Stipulated FOF 58**), this daily total is even less.

93. The Division entered into a contract with its expert, Professor Harris, for half a million dollars for work performed in this administrative proceeding.

    a. **Tr. 1099:11-18** [Harris]
    11 Q Do you have any idea how much time or dollar
    12 value of fees Charles River has billed for this
    13 engagement?
    14 A No, I don't. I have some sense of its upper
    15 bound, but I don't know what they've actually billed.
    16 Q And what is your sense of its upper bound?
    17 A I believe that the contract value is for half a
    18 million dollars.

94. The Division did not introduce any documentary evidence indicating that Delaney knew prior to February 2011 that Stock Loan had a practice of violating Rule 204 by failing to close out long sales of loaned securities by T+6 at market open.

95. The Division did not introduce any emails or other documentary evidence suggesting a follow-up of any alleged meetings pertaining to Stock Loan's violative Rule 204 practices where Delaney was purportedly present, prior to February 2011.

96. The Division did not introduce any documentary evidence wherein Stock Loan personnel were seeking guidance or compliance advice from Delaney regarding Rule 204.

97. By January, 2010, Compliance personnel were overseeing remediation of known Rule 204 compliance issues uncovered during Rule 204 testing.

    a. **Exhibit 134** – "Currently the Compliance department has tested, among other areas, SEC Rule 204 and the Transmittal of Funds. These two areas are now the focus of prompt remediation."

98. The Rule 3012 Testing Report presented to Yancey for his signature indicated that documentation of 3012 testing was available in the Compliance department at Penson.

    a. **Exhibit 135** – "2. Execution and documentation of testing (available in the Compliance dept.)"

99. The Rule 3012 Testing report signed by Charles Yancey attached exception and Remediation Reports.

    a. **Exhibit 135** – "3. Exception and remediation tracking (attached)"

100. As part of the remediation efforts arising from Alaniz's 3012 testing of Rule 204, Stock Loan instituted a manual work-around process until the system limitations in Sendero could be updated.

    a. **Exhibit 345** – "I have updated the remediation document with a manual process that should keep us in compliance with Rule 204 until the development work is completed in Sendero."

Timelines

Pursuant to Item 5a of the Court's Post-Hearing Order dated November 13, 2014, attached hereto are two timelines (Exhibit A: Timeline of Tom Delaney's Knowledge of Stock Loan's Rule 204 Violations; and Exhibit B: Timeline of Alaniz's 3012 Testing) to aid the Court in its evaluation of Delaney's position.

DATED this 19th day of December 2014.

CLYDE SNOW & SESSIONS

BRENT R. BAKER
D. LOREN WASHBURN
AARON D. LEBENTA
ATTORNEYS FOR RESPONDENT THOMAS R. DELANEY, II

EXHIBIT A

Timeline of Tom Delaney's Knowledge of Stock Loan's Rule 204 Violations

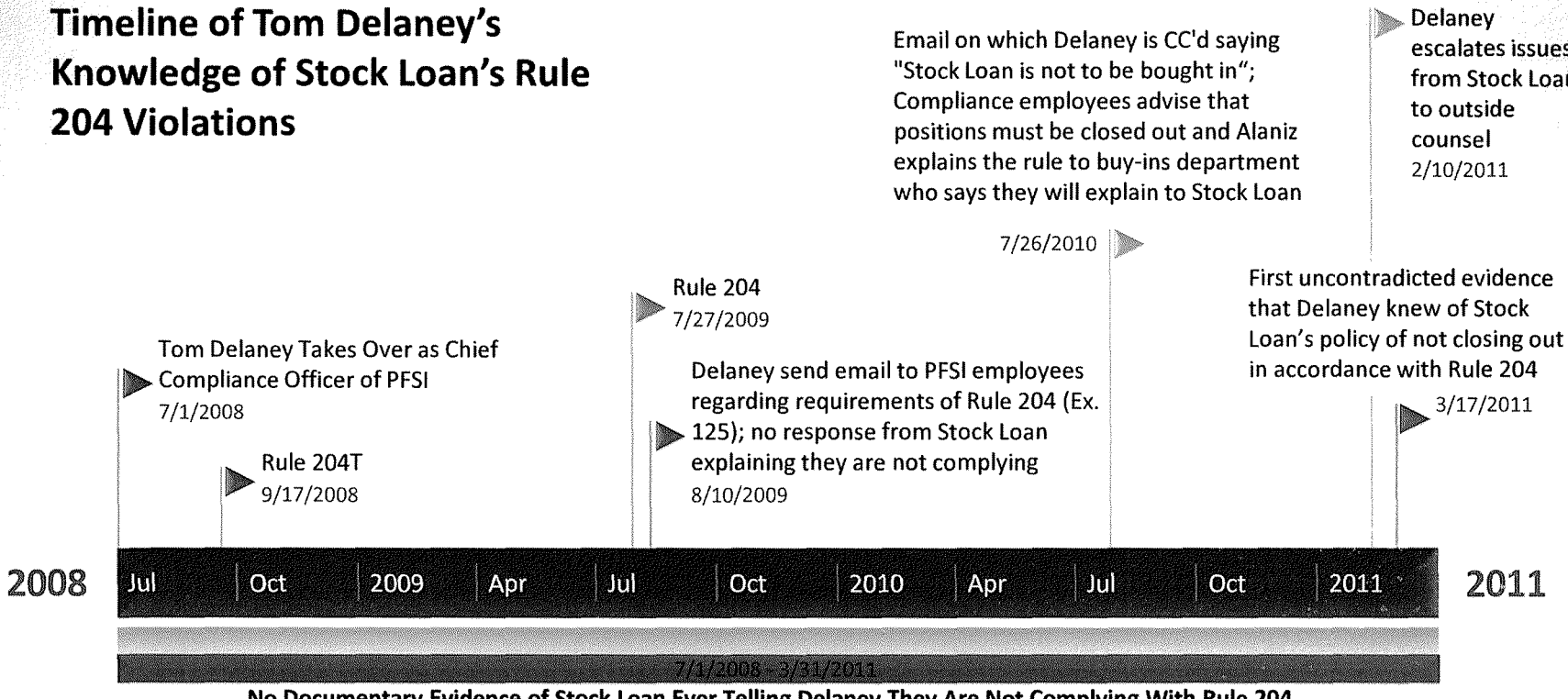
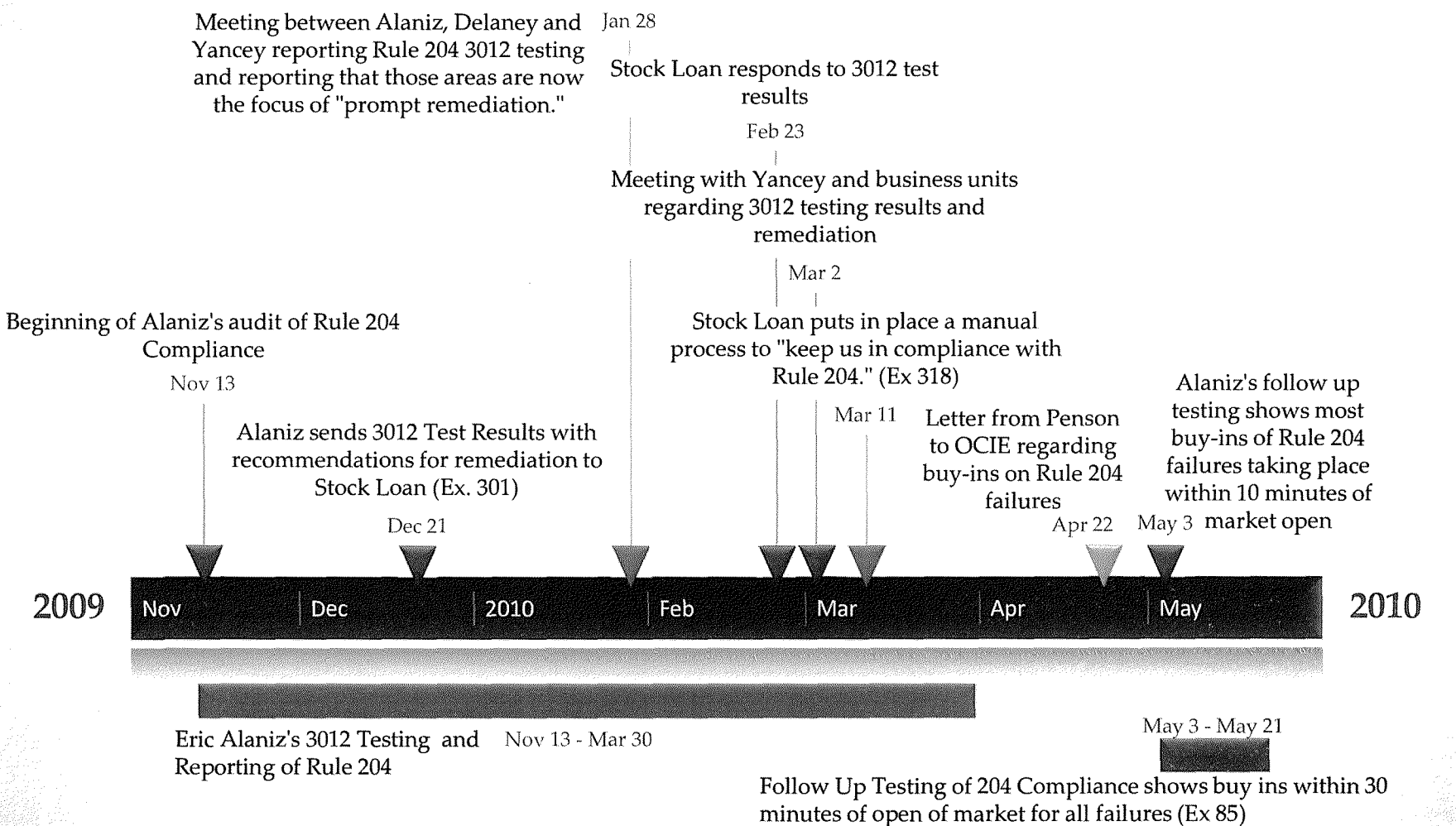


EXHIBIT B

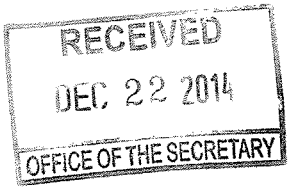
Timeline of Alaniz's 3012 Testing



UNITED STATES OF AMERICA

Before the

SECURITIES AND EXCHANGE COMMISSION



ADMINISTRATIVE PROCEEDING
File No. 3-1587

In the Matter of

THOMAS R. DELANEY II and
CHARLES W. YANCEY

Respondents.

RESPONDENT THOMAS R. DELANEY II'S PROPOSED CONCLUSIONS OF LAW

1. The Division of Enforcement has the "burden of demonstrating by a preponderance of evidence any wrongdoing" by Respondents.

    a. *In the Matter of John J. Kenny & Nicholson/Kenny Capital Mgmt., Inc.,* 1999 WL 587947, *17, Release No. 147 (Aug. 6, 1999) (citing *Steadman v. SEC*, 450 U.S. 91, 102 (1981)).

2. The elements of aiding and abetting are: (1) a primary or independent securities law violation committed by another party; (2) awareness or knowledge by the aider and abettor that his or her role was part of any overall activity that was improper; and (3) that the aider and abettor knowingly and substantially assisted the conduct that constitutes the violation.

    a. *Graham v. SEC,* 222 F.3d 994, 1000 (D.C. Cir. 2000); *Woods v. Barnett Bank of Ft. Lauderdale*, 765 F.2d 1004, 1009 (11th Cir. 1985) ; *Investors Research Corp. v. SEC*, 628 F.2d 168, 178 (D.C. Cir. 1980); *Woodward v. Metro Bank of Dallas,* 522 F.2d 84, 94-97 (5th Cir. 1975); *Russo Sec. Inc.,* 53 S.E.C. 271, 278 & n.16 (1997)

3. "[A]iding and abetting liability cannot rest on the proposition that the person 'should have known' he was assisting violations of the securities laws."

    a. *Howard v. SEC,* 376 F.3d 1136, 1142 (D.C. Cir. 2004)

4. "A plaintiff's case against an aider, abettor, or conspirator may not rest on a bare inference that the defendant 'must have had' knowledge of the facts." The Division "must support the inference with some reason to conclude that the defendant has thrown in his lot with the primary violators."

    a. *Barker v. Henderson, Franklin Starnes and Holt,* 797 F.3d 490, 497 (7th Cir. 1986); *Howard v. SEC,* 376 F.3d 1136, 1142 (D.C. Cir. 2004) (observing, "aiding and abetting liability cannot rest on the proposition that the person 'should have known' he was assisting violations of the securities laws.")

5. To establish the necessary mental state for aiding and abetting, the Division must show a personal incentive to the alleged aider and abettor.

    a. *Barker v. Henderson, Franklin Starnes and Holt,* 797 F.3d 490, 497 (7th Cir. 1986) (observing, in analyzing a claim for aiding and abetting, "the court should ask whether the fraud (or cover-up) was in the interest of the defendants. ***Did they gain*** by bilking the buyers of the securities?") *In re Axis Capital Holdings Ltd. Securities Litig.,* 456 F.Supp.2d 576, 594 (S.D.N.Y.2006) (generalized allegations that can be attributed to any business endeavor, such as the desire to make a profit and maintain business relationships, are insufficient to set forth a motive to aid and abet fraud); In re Bear Stearns Companies, Inc. Sec., Derivative, & ERISA Litig., 763 F. Supp. 2d 423, 499 (S.D.N.Y. 2011) (observing, "[m]otives that are generally possessed by most corporate directors and officers do not suffice; instead, plaintiffs must assert a concrete and personal benefit to the individual defendants resulting from the fraud." (quotation and citations omitted)); *In re PXRE Grp., Ltd., Sec. Litig.,* 600 F.Supp.2d 510, 530–33 (S.D.N.Y.2009) (indicating, that to be indicative of scienter, the allegations must move the desire to raise capital beyond the realm of the generic by illustrating some concrete and personal benefits defendants sought to attain

6. "[A]wareness or knowledge by the aider and abettor that his or her role was part of any overall activity that was improper."

    a. *Graham v. SEC,* 222 F.3d 994, 1000 (D.C. Cir. 2000)

7. For the purposes of aiding and abetting liability, "[a]wareness of wrongdoing means knowledge of wrongdoing."

a. *Howard v. SEC,* 376 F.3d 1136, 1142 (D.C. Cir. 2004) (observing, "aiding and abetting liability cannot rest on the proposition that the person 'should have known' he was assisting violations of the securities laws.")

8. Satisfaction of the knowledge requirement for aiding and abetting depends on the theory of primary liability.

    a. *SEC v. DiBella,* 587 F.3d 553, 566 (2d Cir. 2009) (observing, "[s]atisfaction of the [knowledge] requirement will ... depend on the theory of primary liability.")

9. In analyzing the awareness element, "the surrounding circumstances and expectations of the parties are critical. If the alleged aider and abettor conducts what appears to be a transaction in the ordinary course of his business, more evidence of his complicity is essential."

    a. *SEC v. Morris,* 2005 WL 2000665 *8 (S.D. Texas, 2005) (quoting *Woodward v. Metro Bank of Dallas,* 522 F.2d 84, 95 (5th Cir. 1975)

10. The "awareness of wrong-doing requirement' in aiding and abetting disciplinary cases was designed to insure that innocent, incidental participants in transactions later found to be illegal are not subjected to harsh administrative penalties.

    a. *SEC v. DiBella,* 587 F.3d 553, 566 (2d Cir. 2009).

11. "'Extreme recklessness' is neither ordinary negligence nor 'merely a heightened form of ordinary negligence,'" and cannot be "derived from inexcusable neglect."

    a. *Howard v. SEC,* 376 F.3d 1136, 1143 (D.C. Cir. 2004).

12. Extreme recklessness may be found if the alleged aider and abettor encountered "red flags," or "suspicious events creating reasons for doubt" that should have alerted him to the improper conduct of the primary violator, or if there was a danger so obvious that the actor must have been aware of' the danger.

    a. *Howard v. SEC,* 376 F.3d 1136, 1143 (D.C. Cir. 2004).

13. A finding of recklessness requires an abundance of red flags and suggestions of irregularities that demanded inquiry.

    a. *Howard v. SEC,* 376 F.3d 1136, 1149 (D.C. Cir. 2004) (refusing to find respondent liable for aiding and abetting and distinguishing other authority by observing that a finding of recklessness requires an "abundance of red flags and suggestions of irregularities that demanded inquiry.").

14. The Administrative Procedures Act requires the Division of Enforcement to provide a respondent with timely notice of the matters of fact and law asserted.

    a. 5 U.S.C.A. § 554(b)(3).

15. "[I]t is well settled that an agency may not change theories in midstream without giving respondents reasonable notice of the change."

    a. *Rodale Press, Inc. v. F.T.C.*, 407 F.2d 1252, 1256 (D.C. Cir. 1968).

16. To establish liability for "causing" in the absence of aiding and abetting, the Division must prove three elements: (1) "a primary violation"; (2) an act or omission by the respondent that was a cause of the violation"; and (3) that "the respondent knew, or should have known, that his conduct would contribute to the violation."

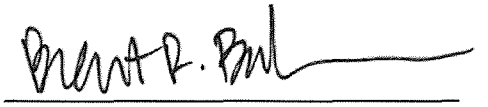
    a. *See In the matter of Mohammed Riad and Kevin Timothy Swanson,* Release No. 590, 2014 WL 1571348 *28 (June 10, 2014)*; see also Robert M. Fuller,* 56 S.E.C. 976, 984 (2003), *pet. for review denied* 95 F. App'x 361 (D.C. Cir. 2004)

17. Negligence is sufficient to establish "causing" liability under Exchange Act Section 21C(a), unless the person is alleged to 'cause' a primary violation that requires scienter.

    a. *Howard v. SEC,* 376 F.3d 1136, 1142 (D.C. Cir. 2004).

DATED this 19th day of December 2014.

CLYDE SNOW & SESSIONS



BRENT R. BAKER
D. LOREN WASHBURN
AARON D. LEBENTA
ATTORNEYS FOR RESPONDENT THOMAS R. DELANEY, II