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BEFORE THE SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C.

In the Matter of the Application of

NORTH WOODWARD FINANCIAL CORP. and DOUGLAS A. TROSZAK

for Review of Disciplinary Action Taken by FINRA

Admin Proc. File No. 3-15990

BRIEF IN SUPPORT OF APPLICATION FOR REVIEW

Douglas A. Troszak, pro se
Redacted

October 16, 2014

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I. FACTS

At all times relevant to this proceeding, Applicant, Douglas A. Troszak ("Troszak") was the president, chief financial officer, chief compliance officer, financial and operations principal, and sole registered representative of Applicant, North Woodward Financial Corporation ("NWFC"). Troszak is also a certified public accountant ("CPA"). He operates Troszak CPA Group out of the same location as NWFC. Troszak's accounting business is his primary source of income and all of his clients at NWFC are also clients of Troszak CPA Group.

Troszak owns several condominium units in northern Michigan. In early 2009, Troszak was unable to pay the mortgage on one of the units. The mortgage holder foreclosed upon the property and purchased it at a sheriff's sale in June 2009. In November 2009, Troszak obtained loans totaling $200,000 from his personal friends. Those friends wanted to help Troszak redeem the property from foreclosure. Some of those friends had previously used the property for vacation purposes. They were also clients of Troszak CPA Group and NWFC, some of used funds from their IRAs in order to complete the loan transaction. On December 8, 2009, Troszak used the proceeds of those loans to exercise his statutory right of redemption under Michigan law, which required him to pay the sale price plus interest within six months of the sale in order to retain his ownership of the unit. Troszak used $188,689.52 of the loan proceeds to redeem the property from foreclosure. Approximately $14,000 of the $200,000 loaned amount was provided by Troszak CPA Group. Because the interest continued to increase daily, the exact amount that would be required to redeem the property was not apparent prior to the redemption. Troszak CPA Group made its loan in order to ensure that adequate funding existed to redeem the property.

In exchange for the loans, Troszak Capital Corporation, an entity that Troszak had created, issued promissory notes directing payment at an annual interest rate of 10% along with principal and interest payments on the first day of each quarter for six quarters, beginning on February 1, 2010, with the remaining balance due on May 1, 2011, the end of the sixth quarter. Troszak also granted a $200,000 mortgage on the unit in favor of the note holders as security. Repayment of several of the lenders has since been delayed based upon the wishes of the lenders. The process of redeeming the property and distributing funds in connection with the redemption was handled by a local title company, Bayview Title. Aside from arranging for the loans, Troszak was not involved in the redemption transaction at all, Bayview Title handled the entire transaction, and continues to do so. First Southwest sent money directly from the IRAs of certain lenders to Bayview Title. That money never passed through Troszak or any of his associated entities.

In February 2010, acting on a regulatory tip from an undisclosed source, FINRA began investigating the loan transactions. During the course of its investigation, FINRA issued four requests for documents and information, purportedly under FINRA Rule 8210 ("8210 Requests"). Troszak was represented by counsel in responding to the 8210 Requests. Troszak responded in a timely manner to the first of FINRA's 8210 Requests on March 10, 2010, by providing background information and documentation relating to the loans. Specifically, FINRA was provided with a notice of foreclosure sale, the sheriff's deed, an affidavit stating the redemption amount, a letter Troszak sent to his clearing firm prior to the loan transactions to notify it of his intentions, the promissory notes, a redemption certificate showing the redemption amount, a portion of NWFC's supervisory procedures, and a document granting the $200,000 mortgage to the note holders.

FINRA then issued three subsequent 8210 Requests, the first of which was made on April 22, 2010. The final two 8210 Requests asked for the same documents and information that FINRA had asked for on April 22, 2010. Specifically, FINRA asked (1) whether any disclosures about the foreclosure had been made to the lenders; (2) whether the seven NWFC clients who withdrew funds from their IRAs to loan to Troszak had been informed of potential tax consequences resulting from the withdrawals; and (3) whether the loans made by NWFC clients were evident in their NWFC accounts. In addition to those questions, FINRA sought the following documentation: (1) copies of new account forms, account amendments and account statements for 2009 and 2010; (2) evidence that the lenders were being paid in accordance with the terms of the promissory notes; and (3) an accounting, with supporting documentation, of the $11,310.48 difference between the $200,000 total loan amount and the amount paid by Troszak to redeem the condo unit. Lastly, the April 22 8210 Request asked for information about three tax liens against Troszak and an explanation as to why the liens were not disclosed on Troszak's Form U4. In connection with that request, FINRA asked for copies of all correspondence between the Applicants and the IRS.

Applicants, through their counsel, made a timely response to FINRA's April 22 8210 Request and to FINRA's subsequent 8210 Requests. The response answered the questions that FINRA had specifically asked in their April 22 8210 request, and explained why requested documentation would not or could not be provided. In its response, the Applicants stated (1) that the lenders had been told that the condo unit was in foreclosure but that that information had not been provided to the lenders in writing; (2) that the IRA withdrawals made to loan money to Troszak had not created any taxable events; (3) that new account forms and monthly account statements for NWFC clients could not be disclosed because the information was personal and

confidential to the clients, but that the information could be obtained from First Southwest, NWFC's clearing firm; (4) that interest payments for the promissory notes were made according to schedule; (5) that the difference between the $200,000 loan amount and the redemption payment was kept for the payment of taxes and interest in an account held by Troszak Capital Corp., and not in a NWFC account, this information was in fact incorrect, as the remaining money was kept in a Bayview Title account to pay for current and future taxes on the condo unit; and (6) that Troszak knew of only two tax liens, which were both the responsibility of Troszak CPA Group, not NWFC or Troszak personally, and therefore did not need to be disclosed on the Form U4.

On May 25, 2010, FINRA issued an 8210 Request that was virtually identical to its April 22 8210 Request. However, in the May 25 request, FINRA also asked for bank and brokerage account statements for all businesses in which Troszak held a beneficial interest between January 2009 and April 2010. The Applicants reiterated their previous response to the April 22 request. FINRA issued a final Rule 8210 Request on June 10, 2010, which was again virtually identical to its April 22 8210 Request. The Applicants responded on June 18, 2010. The response indicated that no new account forms had been created as a result of the loan transactions. Documentary evidence of principal and interest payments on the notes was not provided due to its confidential nature. In regard to tax liens, the June 18 response stated that the matter was ongoing and consequently may have been resolved in Troszak's favor, and again pointed out that the lien did not involve Troszak personally.

After the Complaint was filed in this matter, Troszak gave an on-the-record interview to FINRA staff and disclosed over 5,000 pages of documents, including Troszak's personal bank account statements and those of his various business entities, his correspondence with the IRS,

litigation records relating to the Applicants' taxes and liens, and NWFC account statements for 2009 and 2010 for those clients who loaned money to Troszak. The need to collect and produce such a massive quantity of documents posed a significant economic burden on the Applicants. Around the same time as the production of those documents, Troszak also amended his Form U4 to reflect a federal tax lien that had originated in his accounting firm but for which the IRS had made Troszak personally liable.

II. PROCEDURAL HISTORY

On May 18, 2011, FINRA's Department of Enforcement filed a complaint in this matter against the Applicants. The Complaint alleged violations of Article V, Section 2 of the FINRA By-Laws, FINRA Rule 2010 and NASD Rule 2110 due to Troszak's failure to disclose a tax lien on question 14M of his Form U4, which requires registered representatives to disclose any unsatisfied judgments or liens against them. The Complaint also alleged that the Applicants violated FINRA Rules 8210 and 2010 by failing to respond completely to requests for information and documentation.

The FINRA Hearing Panel found the Applicants liable for the alleged violations, finding that the Applicants had never produced an accounting of the difference between the amount borrowed and the amount of the redemption payment, evidence of interest and principal payments made to note holders, or 2009 and 2010 securities account statements for Troszak Capital Corporation. In response to the failure to provide information and documentation, the Hearing Panel barred Troszak, expelled NWFC, and stated that it would be appropriate to fine the Applicants $50,000 jointly and severally, although the fine was not imposed due to the bar and the expulsion. The U4 violation resulted in a thirty-day suspension for both Applicants, as

well as a $10,000 fine against them jointly and severally. However, the Hearing Panel did not impose the sanctions for the U4 violations in light of the bar and the expulsion.

The National Adjudicatory Council ("NAC") affirmed the Hearing Panel's findings with respect to whether or not the Applicants had violated FINRA and NASD rules and with respect to the sanctions imposed for the violation of FINRA Rule 8210. However, the NAC modified the sanctions imposed for the Form U4 violation by eliminating the 30-day suspension for NWFC and increasing Troszak's 30-day suspension to 60 days.

III. STANDARD OF REVIEW

In reviewing determinations made by self-regulatory organizations ("SROs") in disciplinary proceedings, the SEC undertakes an independent review of the record and applies a preponderance of the evidence standard. See *David M. Levine*, Exchange Act Release No. 48760, 2003 SEC LEXIS 2678 (2003). When reviewing the sanctions imposed by an SRO, the Securities Exchange Act of 1934 requires the SEC to determine (1) whether the aggrieved person engaged in the conduct found by the SRO; (2) whether such conduct violates the SRO's rules; and (3) whether the SRO rules that were found to be violated are, and were applied in a manner, consistent with the purposes of the Securities Exchange Act of 1934. 15 U.S.C. 78s(e)(1). If the SEC does not make all three findings, it must set aside the sanctions. *Id.*

IV. ARGUMENT

Applicants take exception to the conclusions that they violated FINRA Rules 8210 and 2010 by failing to provide information and documents responsive to 8210 requests. R. at 4987-4989, Pg. 9 of NAC Decision, Dated July 21, 2014 (hereinafter referred to as "NAC decision"); R. at 4875-4946. They also take exception to the conclusion that none of the Applicants' exculpatory arguments diminish their responsibility to comply with FINRA Rule 8210,

particularly, the Applicants take exception to the NAC's rejection of Applicants' arguments (1) that FINRA lacked the authority to investigate Troszak's loan transactions; and (2) that federal law, including SEC Regulation S-P prevents the disclosure of the information requested by FINRA. R. at 4991-4993, Pg. 13 of NAC Decision; R. at 4875-4946, 4493.

With respect to the NAC's determinations regarding federal tax liens and Form U4, the Applicants take exception to the finding that the failure to disclose the IRS tax lien violated Article V, Section 2 of the FINRA By-Laws, FINRA Rule 2010, and NASD Rule 2110. R. at 4986-4988, Pg. 8 of NAC Decision. Applicants also take exception to the finding that Troszak understood that he was personally subject to the IRS tax lien against Troszak CPA Group. R. at 4980-4982, Pg. 2 of NAC Decision; R. at. 4875-4946, 2127-2318.

The Applicants also take exception to the NAC's findings on the issue of sanctions. Specifically, (1) that the Applicants' disregard FINRA rules and requirements, placing the public interest at risk (R. at 4994-4996, Pg. 16 of NAC Decision); (2) that this case involves egregious violations of FINRA Rules 8210 and 2010 (R at 5000-5003, Pgs. 22-23 of NAC Decision); (3) that aggravating factors justify the imposition of a bar and expulsion for the violation of Rule 8210 (R. at 4999-5001, Pg. 21 of NAC Decision); (4) that the Applicants did not provide valid reasons for failing to respond completely to the 8210 requests (R. at 4997-4999, Pg. 19 of NAC Decision; R. at 4875-4946); (5) that mitigating factors do not exist for the alleged rule violations in this matter (R. at 5000-5002, Pg. 22 of NAC Decision); (6) that the Applicants' response to 8210 requests did not amount to substantial compliance (R. at 5000-5002, Pg. 22 of NAC Decision); and (7) that a bar and expulsion are appropriate sanctions in this case (R. at 5003-5005, Pg. 25 of NAC Decision).

The legal and factual basis for the exceptions to the findings and conclusions of the NAC are set forth more fully below.

A. FINRA EXCEEDED THE SCOPE OF ITS REGULATORY AUTHORITY BY ISSUING 8210 REQUESTS FOR DOCUMENTS AND INFORMATION RELATING TO TROSZAK'S LOAN TRANSACTIONS

FINRA has the authority to regulate securities, as well as conduct not involving securities if that conduct is inconsistent with just and equitable principles of trade and involves business-related conduct. See e.g. *Vail v. S.E.C.,* 101 F.3d 37 (5th Cir. 1996); *Ernest A. Cipriani, Jr.*, Release No. 34-33675, 51 S.E.C. 1004 (1994); *William F. Rembert*, Release No. 34-33202, 51 S.E.C. 825 (1993); FINRA Rule 2010. However, securities are not involved in this case. Nor does this case involve the type of non-securities related conduct that FINRA may regulate.

1. The transactions investigated by FINRA did not involve securities

The loan transactions between Troszak and his friends did not involve securities. The U.S. Supreme Court defines a security as an investment of money due to an expectation of profits arising from a common enterprise which depends solely on the efforts of a promoter or third party. *Sec. & Exch. Comm'n v. Howey*, 328 U.S. 293, 298 (1946). The Supreme Court has also stated that a note secured by a mortgage on a home is not properly viewed as a security. *Reves v. Ernst & Young*, 494 U.S. 56, 66 (1990). Furthermore, a note is not likely to be a security when it is exchanged to correct for a seller's cash-flow difficulties, in contrast to when the note holder's primary motivation is the expected profit to be gained from the note. *Id.*

The notes involved in this case were secured by a mortgage on a home and they were made in order to correct Troszak's cash-flow difficulties, allowing him to redeem the property from foreclosure. The note holders were not primarily interested in the profit to be made from

loaning money to Troszak, but were instead motivated by the desire to help a friend in his time of financial difficulty. Because the notes given by Troszak are not properly viewed as securities and there are no other securities involved in this case, FINRA must rely upon its authority to regulate conduct that does not involve securities in order to justify its investigation into the loan transactions.

2. This case does not involve the type of non-securities-related conduct that FINRA may regulate

FINRA Rule 2010 states that "a member, in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade." Consequently, it has been held that FINRA may regulate conduct that does not involve securities only if that conduct is inconsistent with just and equitable principles of trade and involves business-related conduct. See e.g. *Vail v. S.E.C.,* 101 F.3d 37 (1996); *Ernest A. Cipriani, Jr.*, 51 S.E.C. 1004 (1994); *William F. Rembert*, 51 S.E.C. 825 (1993); FINRA Rule 2010. Conduct is inconsistent with just and equitable principles of trade if the conduct reflects negatively on "the associated person's ability to comply with the regulatory requirements of the securities business and to fulfill his fiduciary duties in handling other people's money." *Daniel D. Manoff*, 55 S.E.C. 1155, 1162 (2002). The SEC has previously stated that any violation of Rule 8210 is also a violation of Rule 2010. See *CMG Institutional Trading, LLC,* Exchange Act Release No. 59325, 2009 SEC LEXIS 215 (2009). However, if FINRA was not authorized to request the documents that are the subject of an 8210 request in the first place, or if the Applicants were prevented by federal law from providing them, then surely the Applicants must be excused from the requirement to provide those documents. Therefore, in order for FINRA to be able to regulate the loan transactions in this matter, it must find that the Applicants engaged in conduct unrelated

to the 8210 requests, that negatively reflects on their ability to comply with regulatory requirements or their ability to fulfill their fiduciary duties to their clients.

FINRA never alleged that the loan transactions themselves or any aspect of those transactions violated Rule 2010. That is because the Applicants' conduct surrounding those transactions was clearly consistent with just and equitable principles of trade. The conduct at issue here are a series of private loan transactions between friends. The mortgages granted in exchange for those loans were publicly recorded and the loaned amounts were and continue to be repaid in accordance with the wishes of the lenders. Troszak did not take a commission or impose any charges upon the lenders in the course of the transactions. The Applicants also complied with FINRA Rule 3240, which is the rule that is specifically designed to regulate borrowing from or lending money to customers. Rule 3240 states that registered broker-dealers may not borrow money from customers unless "the lending arrangement is based on a personal relationship with the customer, such that the loan would not have been solicited, offered, or given had the customer and the registered person not maintained a relationship outside of the broker-customer relationship." FINRA Rule 3240(a)(2)(D). Each of the lenders were personal friends of Troszak whom he had known for years prior to the loan transactions. They were all clients of Troszak CPA Group long before Troszak or NWFC became registered with what was then the NASD. Several of the lenders had used the property for vacation purposes. The long-standing personal relationships that Troszak had with the lenders led him to feel comfortable with asking them for the loans and caused them to feel comfortable in issuing those loans. Absent the personal relationships, the loan transactions involved in this case would not have occurred. Ordinarily, a registered person loaning money from a customer must also notify the member that the registered person is associated with, and receive written pre-approval for the

transactions from the member. *Id.* at (b)(1). However in this case, Troszak is the sole registered representative of NWFC, so compliance with the notification and pre-approval portion of Rule 3240 would result in Troszak notifying and pre-approving himself. Troszak did however notify First Southwest, NWFC's clearing firm, on November 16, 2009, prior to entering into the loan transactions. The letter affirmed Troszak's compliance with the requirements of FINRA Rule 3240 and referenced his personal relationship with the lenders.

The Applicants provided FINRA investigators with all of this information in response to their first 8210 request to the Applicants, which would have enabled FINRA to verify that the transactions were not inconsistent with just and equitable principles of trade. Nothing about the loan transactions reflects negatively on the Applicants ability to comply with regulatory requirements. The Applicants complied with the rule that was specifically designed to regulate transactions with clients. In addition, the Applicants did not attempt to hide the transactions, instead, relevant documents were publicly recorded and Troszak even went so far as to notify his clearing firm of the transactions prior to obtaining the loans. The Applicants' response to FINRA's initial 8210 request also showed that the Applicants' ability to fulfill their fiduciary duties to their clients is not impugned as a result of these transactions.

The Applicants provided FINRA with information beyond that requested in FINRA's initial 8210 request when they informed FINRA investigators that many of the documents requested by FINRA did not exist, were not in Troszak's possession, or could not be provided due to the privacy concerns of the lenders. All of the information and documentation provided to FINRA in response to its first 8210 request was sufficient to allow FINRA to conclude that the Applicants' conduct was consistent with just and equitable principles of trade.

Because the conduct at issue was not inconsistent with just and equitable principles of trade, it cannot be regulated by FINRA. FINRA should not be allowed to hand out discipline for a failure to provide information related to transactions which FINRA does not have the authority to regulate, otherwise, FINRA will continue to request information on matters outside the scope of its regulatory authority. The need to limit FINRA's overreaching 8210 requests is especially prevalent in this case because of the countervailing statutes and regulations preventing the Applicants from disclosing the information requested by FINRA.

B. APPLICANTS ARE BEING SANCTIONED FOR FAILING TO PROVIDE DOCUMENTS THAT THEY COULD NOT DISCLOSE UNDER FEDERAL LAW

1. Federal law prohibits the Applicants from providing the documents requested by FINRA

26 U.S.C. 6713 prevents tax preparers from disclosing information given to them to assist them in preparing a tax return by imposing fines on tax preparers who disclose such information. Similarly, 26 U.S.C. 7216 prohibits tax preparers from knowingly or recklessly disclosing information given to them in connection with the preparation of a tax return. If a tax preparer discloses documents covered by those statutes, he subjects himself to criminal punishment, including up to one year in prison, in addition to possible fines. 26 U.S.C. 6713 and 7216. Both statutes include the same exceptions. Those exceptions include disclosures made pursuant to an administrative order or demand by a federal agency, and disclosures made in response to a written request by a professional association ethics committee or board investigating the ethical conduct of the tax return preparer. 26 CFR 301.7216-2(f)(4)(i); 26 CFR 301.7216-2(f)(5). In addition, SEC Regulation S-P includes a similar prohibition on the disclosure of non-public

personal information. See 17 CFR 248.10. Non-public personal information is defined to include personally identifiable financial information. 17 CFR 248.3(t)(1). Personally identifiable financial information includes any information "about a consumer resulting from any transaction involving a financial product or service between you and a consumer." 17 CFR 248.3(u)(1)(ii); see also 17 CFR 248.3(w)(1) (defining "you" to include "any broker or dealer"). Regulation S-P contains an exception for properly authorized regulatory investigations. 17 CFR 248.15(a)(7)(ii). The regulation also has an exception allowing disclosure of non-public personal information in response to government regulatory authorities with jurisdiction for examination or compliance purposes. *Id.* at (iii). The NAC concluded that that exception applied to the 8210 requests in this matter. Disclosure of non-public personal information may also be made in compliance with Regulation S-P to self-regulatory organizations to the extent that disclosure is specifically permitted or required under other provisions of law and in accordance with the Right to Financial Privacy Act of 1978. *Id.* at (a)(4).

FINRA's 8210 Requests do not meet any of the exceptions to 26 U.S.C. 6713 or 26 U.S.C. 7216. As a result, the Applicants cannot provide information given to them to assist in preparing tax returns without violating those statutes. FINRA is not a federal agency, meaning that it does not meet the exception for disclosures made pursuant to an administrative order or demand by a federal agency. See http://www.finra.org/AboutFINRA/ (last accessed October 14, 2014) (stating "FINRA is not part of the government"; *Cf. Richard A. Neaton*, Exchange Act Release No. 65598, 2011 SEC LEXIS 3719 (2011); *Asensio & Co., Inc.*, Exchange Act Release No. 68505, 2012 SEC LEXIS 3954 (2012); *First Jersey Sec. Inc. v. Bergen*, 605 F. 2d 690, 698, 699 n.5 (3d Cir. 1979) (all concluding that FINRA is not a state actor). Another exception that may apply relates to written requests by a professional association ethics committee or board

investigating the ethical conduct of the tax return preparer. 26 CFR 301.7216-2(f)(5). Under the doctrine of *expressio unius est exclusion alterius*, the express provision allowing disclosure to an ethics committee or board investigating the ethical conduct of a tax return preparer, necessarily means that disclosure is not allowed to an ethics committee or board investigating the ethical conduct of a securities broker/dealer. See, e.g. *Tenn. Valley Auth. v. Hill*, 437 U.S. 153, 188 (1993) (applying *expressio unius*). This exception does not apply because it relates to tax preparation, and although Troszak happens to be a CPA, FINRA's duties and responsibilities are not to oversee tax return preparation activities, but rather to regulate and oversee the securities business. Because FINRA does not fit either of those two exceptions, or any other exception under 26 U.S.C. 6713 and 7216, those statutes prohibit the disclosure of information used by Troszak in connection with the preparation of tax returns.

At all times relevant to FINRA's request for evidence of principal and interest payments to the lenders, Troszak was the tax preparer for each of the lenders. Interest payments for the promissory notes would have been disclosed to the IRS on the note holder's tax return. It necessarily follows that all interest payments made on the loans may not be disclosed because those payments are information that Troszak used in preparing the lenders' tax returns. Because payments of principal were sometimes included in the same check as interest payments, it is impossible to provide FINRA with evidence of those particular principal payments that were combined with interest payments, without also providing FINRA with evidence of the interest payments, which would violate 26 U.S.C. 6713 and 26 U.S.C. 7216. The NAC erred by failing to even address the Applicant's arguments about these federal statutes.

In addition, FINRA does not meet any exception to SEC Regulation S-P, preventing the Applicants from providing non-public personal information to FINRA. Despite including a

provision for properly authorized regulatory investigations, FINRA's 8210 Requests in this case do not meet that exception because FINRA exceeded the scope of its regulatory authority in this matter for the reasons set forth above, meaning that its regulatory investigation was unauthorized. The NAC determined that FINRA's 8210 Requests fit within a different exception which allows disclosure of non-public personal information "to respond to judicial process or government regulatory authorities having jurisdiction over you for examination, compliance, or other purposes as authorized by law." 17 CFR 248.15(a)(7)(iii). R. at 4991-4993, Pg. 13 of NAC Decision at FN24. However, in its analysis of the exception, the NAC failed to notice the importance of the word "government" in the language of the regulation. Although FINRA is a regulatory authority, it is not a government regulatory authority. See http://www.finra.org/AboutFINRA/ (accessed October 11, 2014) (stating "FINRA is not part of the government"; *Cf. Richard A. Neaton*, Exchange Act Release No. 65598, 2011 SEC LEXIS 3719 (Oct. 20, 2011); *Asensio & Co., Inc.*, Exchange Act Release No. 68505, 2012 SEC LEXIS 3954 (Dec. 20, 2012); *First Jersey Sec. Inc. v. Bergen*, 605 F. 2d 690, 698, 699 n.5 (3d Cir. 1979) (concluding that FINRA is not a state actor). Because FINRA is not part of the government, it does not meet the exception for government regulatory authorities. FINRA's 8210 requests do not meet any other exception to SEC Regulation S-P's prohibition against the disclosure of non-public personal information. Evidence of principal and interest payments to the note holders resulted from transactions involving a financial product or service offered by Troszak to those note holders. As a result, the payments of principal and interest made to those consumers is non-public personal information about those consumers which cannot be disclosed under SEC Regulation S-P. Consequently, the NAC erred in concluding that the requested documents could be provided under SEC Regulation S-P.

2. The federal laws preventing the Applicants from providing the requested documents justify the Applicants' failure to fully respond to the 8210 requests

FINRA's authority to request documents under Rule 8210 is based upon a contract. See *Kidder, Peabody & Co. v. Zinsmeyer Trusts P'ship*, 41 F.3d 861, 863 (2d Cir. 1994) ("The rules of a securities exchange are contractual in nature."). That contract is the agreement to comply with federal securities laws, including relevant rules and regulations and FINRA rules (hereinafter referred to as "Compliance Agreement"). See Article IV, Section 1 of the FINRA By-Laws. That agreement must be submitted in connection with an application for FINRA membership. *Id.* However, as a matter of contract law, a contract is illegal if it requires an act that is a civil wrong or is contrary to statutory provisions or public policy. See 17A C.J.S. Contracts §254 (2014); *L'Orange v. Medical Protective Co.*, 394 F.2d 57, (6th Cir. 1968); *Measday v. Sweazea*, 78 N.M. 781, 438 P.2d 525 (Ct. App. 1968); *Hazard v. Hazard*, 46 N.C. App. 280, 264 S.E.2d 908 (1980). Contracts are generally voided if performance requires a violation of criminal law. See 17A C.J.S. Contracts §254 (2014); *Beyers v. Roberts*, 199 S.W.3d 354 (Tex. App. Houston 1st Dist. 2006). Contracts that tend to bring about a result that the law seeks to prevent will generally not be enforced. 17A C.J.S. Contracts §254 (2014); *Meek v. Wilson*, 283 Mich. 679, 278 N.W. 731 (1938); *Della Corp. v. Diamond,* 210 A. 2d 847 (Del. 1965).

FINRA has used Rule 8210 to request documents which the Applicants are contractually obligated to provide if it is determined that FINRA's requests did not exceed the scope of its investigatory authority. If the Applicants were to provide FINRA with the documents that it has requested, the Applicants would be in violation of federal law. Therefore, the Compliance Agreement is illegal because violations of criminal law and other statutory provisions would

result from compliance with its terms. In order to prevent that undesirable outcome, the Compliance Agreement, or at least FINRA's 8210 requests which render that agreement illegal, should be voided and held unenforceable.

The Applicants' failure to provide all of the documents requested by FINRA should be excused even if the contractual basis for FINRA's authority to issue 8210 requests to the Applicants is not void or invalid due to the fact that disclosure of the requested information by the Applicants would violate criminal statutes. FINRA, through its 8210 requests, should not be allowed to put the Applicants in the unenviable position of having to choose between exposing themselves to criminal and civil liability by complying with FINRA's requests, or being kicked out of the securities business simply because they chose not to break federal laws designed to protect client confidentiality in order to meet their contractual obligations to FINRA. It is difficult to understand how FINRA's mission of protecting the investing public is served by forcing members of the securities industry to violate laws specifically designed to protect clients and barring those members who refuse to do so. Instead, in situations where disclosing documents requested by FINRA under Rule 8210 would result in the violation of federal law, as is the case here, the failure to provide the requested documents must be excused and the requirements of FINRA Rule 8210 should yield to contrary law.

C. CERTAIN DOCUMENTS REQUESTED BY FINRA EITHER DID NOT EXIST OR WERE NOT IN TROSZAK'S POSSESSION, CUSTODY OR CONTROL

Under FINRA Rule 8210 (a)(2), FINRA has the right to "inspect and copy the books, records, and accounts of such member or person with respect to any matter involved in the investigation...that is in such member's or person's possession, custody or control." The Rule was recently amended to add the reference to "possession, custody or control," however the SEC

recently ruled that the version of 8210 in place at the time of the investigation in this case, also required associated persons to produce documents in their possession, custody or control. See *Gregory Evan Goldstein*, Release No. 34-71970, 2014 WL 1494527 (2014).

FINRA requested an accounting of the difference between the total loan amount of $200,000 and the redemption amount of $188,689.52. The exact amount that would be necessary to redeem the property was unknown, so after arranging for approximately $186,000 in loans from his friends, Troszak, through his accounting firm Troszak CPA Group, submitted the final $14,000 or so, in order to make the total loan amount an even $200,000 and to ensure that there was enough money available to redeem the property. Once Troszak had the funds, he turned them over to Bayview Title, the title company handling the redemption transaction. That company is completely independent of Troszak. Troszak has no control over Bayview Title and no ownership interest in that company. Bayview paid the redemption amount. The amount remaining after the property was redeemed, approximately $11,500, belonged to Troszak CPA Group, which had submitted the final $14,000 or so. Bayview was instructed to keep any amount remaining after the redemption and to use those remaining funds to pay any existing or future taxes on the building. In connection with the loan transactions, Troszak had promised the lenders that he would remain current with the taxes on the building. Neither Troszak, nor any entity that he had an ownership interest in or control over, have ever received any of the approximately $11,500 that was left over after redemption of the property. That amount has remained with Bayview Title. Consequently, Troszak could not possibly complete an accounting on the remaining $11,500 because he does not have all of the necessary information, which is possessed and controlled, not by Troszak or any of his associated entities, but by Bayview Title.

FINRA also requested 2009 and 2010 securities account statements for Troszak Capital Corporation. Troszak Capital Corporation's account statements would have been generated by First Southwest, a company that Troszak has no ownership interest in and no control over. That account rarely, if ever, contained much more than $1,000 and often would have months with no activity. Upon information and belief, First Southwest does not generate account statements when there is no activity in such a small account. As a result, it is possible that no such account statements exist for 2009 and 2010. If those documents do exist, then FINRA should have already received copies of them. Troszak gave all documents in his possession that were responsive to FINRA's 8210 requests to his attorneys. Those attorneys provided FINRA with over 5,000 pages of documents, including Troszak Capital Corporation account statements for years after 2010. If FINRA wishes, Troszak will attempt to obtain Troszak Capital Corporation securities account statements for 2009 and 2010 from First Southwest, if any such statements exist. Of course Troszak has no control over First Southwest and therefore, cannot guarantee that any responsive documents will be provided by First Southwest.

The absence of any ownership interest in First Southwest or Bayview Title, and the lack of possession, custody or control over the information and documentation requested by FINRA justify Troszak's failure to provide an accounting for the difference between the total loaned amount and the redemption price, and any existing Troszak Capital Corporation securities account statements for 2009 and 2010.

D. THE NONDISCLOSURE OF THE IRS TAX LIEN ON TROSZAK'S FORM U4 WAS JUSTIFIABLE

Question 14M of Form U4, the question relating to liens, requires registered representatives to disclose any unsatisfied judgments or liens against them. The relevant IRS

lien was related to a Troszak CPA Group issue. Although Troszak is an officer of both Troszak CPA Group and NWFC, Troszak CPA Group is a separate entity from NWFC, and it is not a FINRA member. Troszak was unaware that officers of Troszak CPA Group such as himself could be held personally liable for the company's payroll tax penalties related to payroll obligations. Furthermore, he was unaware that the IRS had sought to hold him personally liable. Troszak therefore, did not have knowledge of any lien against him personally or against NWFC and as a result, he could not be expected to disclose the lien. Although FINRA told Troszak that he should disclose the lien, he was not aware that the IRS lien was against him personally and it was the position of his counsel that the lien did not need to be disclosed because he was not personally subject to it. As soon as Troszak discovered his personal liability on the lien, he immediately paid it off. Troszak should not be punished for failing to disclose something that he was not aware that he needed to disclose.

E. THE SANCTIONS IMPOSED AGAINST THE APPLICANTS ARE EXCESSIVE

1. The sanctions imposed for the alleged violations of FINRA Rule 8210 are excessive

Section 19(e)(2) of the Securities Exchange Act of 1934 states that FINRA's sanctions should be upheld unless the SEC finds that, having due regard for the public interest and the protection of investors, the sanctions are excessive, oppressive, or impose an unnecessary or inappropriate burden on competition. 15 U.S.C. 78s(e)(2). The SEC also considers aggravating or mitigating factors that may exist, as well as whether the sanctions imposed are remedial rather than punitive. FINRA Sanction Guidelines at 2; *Saad v. SEC*, 718 F. 3d 904, 906 (D.C. Cir. 2013); *Wright v. SEC,* 112, F.2d 89, 94 (2d Cir. 1940); *PAZ Sec., Inc. v. SEC*, 494 DF.3d 1059,

1065; (stating that sanctions must be remedial). A firm's size should be considered in determining whether a sanction is appropriately remedial. FINRA Sanction Guidelines at 2. Ongoing regulatory proceedings prior to a final decision are not relevant when deciding upon sanctions. *Id.* Where, as here, an individual partially responds to 8210 requests, a bar is standard unless the information provided by the person substantially complied with all aspects of the 8210 request. FINRA Sanctions at 33. Expulsion of the firm is appropriate only in egregious cases. *Id.* There are three primary considerations when determining the appropriate sanctions to impose in the case of a partial, but incomplete response to 8210 requests. *Id.* Those considerations are (1) the "importance of the information requested that was not provided as viewed from FINRA's perspective, and whether the information provided was relevant and responsive to the request"; (2) the "number of requests made, the time the respondent took to respond, and the degree of regulatory pressure required to obtain a response"; and (3) "whether the respondent thoroughly explains valid reason(s) for the deficiencies in the response." *Id.* Where mitigation exists, a suspension of up to two years is recommended. *Id.*

The NAC made several errors relating to the principal considerations and general principles applicable to determining sanctions when it decided to impose a bar against Troszak and to expel NWFC. First, in stating that the Applicants place the public interest at risk, the NAC made note of an ongoing regulatory proceeding involving the Applicants. R. at 4994-4997, Pgs. 16 and 17 of NAC Decision at FN 28. Consideration of such proceedings that have not yet reached a final decision are explicitly listed as being irrelevant to sanctions determinations. FINRA Sanction Guidelines at 2. The NAC's consideration of ongoing regulatory matters was erroneous and may have led to an increased sanction for the Applicants.

The NAC also determined that there were several aggravating factors present. The aggravating factors found by the NAC were that Troszak acted intentionally and did not accept responsibility for misconduct. R. at 4999-5001, Pg. 21 of NAC Decision. Those factors are irrelevant to this case. Troszak has not accepted responsibility for misconduct only because he has legitimate legal concerns given the fact that federal law prohibits him from disclosing documents requested by FINRA. He fails to see how complying with those laws constitutes misconduct, and if it does not constitute misconduct, then he has not engaged in any misconduct at all relating to Rule 8210. Troszak acted intentionally in asserting the laws that prevented him from fully responding to the 8210 requests only because there is no way that he could unintentionally assert those laws. He had no choice but to act intentionally in pointing out the legal problems inherent in disclosing the requested documents. The NAC erred in finding that these aggravating factors are present in this case.

The NAC's conclusion that there are no mitigating factors is also erroneous. The Applicants were represented by legal counsel from the time when the first 8210 request was received until the day prior to the initial hearing in this matter before FINRA's hearing panel. His attorneys had experience litigating FINRA disciplinary proceedings and Troszak reasonably trusted the legal advice that he received from them. Throughout the course of that representation, Troszak was advised about the relevant federal laws which prohibited disclosure of the requested documents. He relied upon that advice in responding to FINRA's 8210 requests, and in forming the basis for much of his defense in this disciplinary proceeding against him and his firm. His reasonable reliance on that legal advice is a mitigating factor to be considered in determining sanctions. See FINRA Sanction Guidelines at 6. The NAC's statement that there are no valid reasons for failing to respond completely to FINRA's 8210

requests ignores the numerous reasons set forth in this brief and before the NAC. In fact, the NAC failed to even address several of the statutes that prohibit disclosure of the requested information. The mitigating factor of Troszak's reliance on the advice of legal counsel makes it clear that the NAC's determination that this case involved egregious violations of FINRA rules was an error. Furthermore, Troszak substantially complied with the 8210 requests by providing the information and documents that he could legally provide. As a result, the harsher sanctions imposed due to the finding of egregious violations should be reduced.

The NAC also upheld the Hearing Panel's decision to impose a $50,000 fine against the Applicants, jointly and severally. That fine is the highest recommended amount under the Sanction Guidelines for a violation of Rule 8210. FINRA Sanction Guidelines at 33. This may be due to the fact that the NAC failed to consider the size of NWFC in imposing that fine. The Sanction Guidelines state that firm size should be considered in crafting sanctions in order to ensure that sanctions are remedial rather than punitive. FINRA Sanction Guidelines at 2. Discretion not to consider firm size is given only in egregious cases, which this is not. *Id.* Troszak is the sole registered representative and the only employee of NWFC. NWFC is a small firm with relatively few clients and a low level of trading activity. These facts all point to the conclusion that the amount of the fine is punitive in nature and that a smaller fine is necessary in order to make the fine remedial.

The Applicants have not engaged in fraudulent activity or activity which was harmful to its customers or non-client investors. If the Applicants violated FINRA rules, it was because they tried too hard to protect their clients' confidential information. Troszak's friends that loaned him money to redeem the property, including those friends that are also Troszak's clients at NWFC, are sophisticated and informed businesspeople. They are aware of FINRA's history,

particularly its association with Bernie Madoff when FINRA was known as the National Association of Securities Dealers. They also know that FINRA, although subject to government oversight, is not a government regulator and that information collected during FINRA investigations may be subject to hacking and is not treated confidentially and may be disclosed, as FINRA investigators made clear through their correspondence with the Applicants. For those reasons, the lenders did not want the Applicants to disclose information relating to the loans that they made to Troszak. If it is ultimately found that the Applicants violated FINRA Rule 8210, it will not be because they had no basis for refusing to provide certain documents to FINRA investigators, instead it will be because of the Applicants' legitimate concerns about the confidentiality of the documents and information relating to the lenders and the implications of violating federal law by providing those documents. See e.g. 26 U.S.C. 6713; 26 U.S.C. 7216; 17 CFR 248.10; Mich. Comp. Laws §339.732. Believing that disclosing the documents requested by FINRA would lead to criminal charges against them, the Applicants chose not to provide those documents. The Applicants' actions show that they are mindful of the laws that govern them. If it is found that the Applicants misapplied those laws in this case by refusing to provide documents requested under FINRA Rule 8210, the Commission should feel confident that the Applicants will learn from their honest mistake and impose sanctions less than a bar and expulsion from the securities industry.

2. The sanctions imposed for the alleged Form U4 violation are excessive

The FINRA Sanction Guidelines relating to the alleged Form U4 violation provide a wide range of sanctions depending on a variety of factors. The NAC determined that this matter involved the failure to file an amendment, for which the Guidelines recommend a fine of $2,500 to $50,000 for the responsible individual and $5,000 to $100,000 for the responsible firm.

FINRA Sanction Guidelines at 69-70. In addition, the suspension of the responsible individual for five to 30 business days is recommended. *Id.* at 69. In egregious cases, the responsible individual may be suspended for up to two years or barred, and the firm may be suspended until the filing deficiency is resolved. *Id.* at 70. There are three principal considerations to be used in determining the appropriate sanction for a violation relating to Form U4 filings. *Id.* at 69. Those factors are (1) the "nature and significance of the information at issue"; (2) "whether failure resulted in a statutorily disqualified individual becoming or remaining associated with a firm"; and (3) "whether respondent member firm's misconduct resulted in harm to a registered person, another member firm or any other person or entity." *Id.*

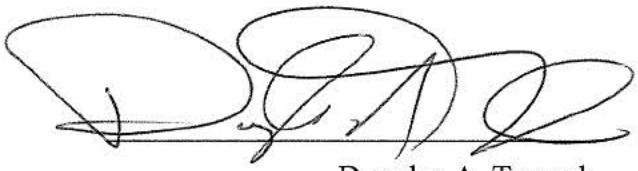
The NAC argued that only one of the three principal considerations, the nature and significance of the information at issue, applied in this case. R. at 5001-5003, Pg. 23 of NAC Decision. The NAC found that an undisclosed tax lien is significant. *Id.* It failed to consider the remaining two factors, both of which support reduced sanctions. First, no statutorily disqualified individual became or remained associated with a firm as a result of the alleged violation. Secondly, no actual harm to any person has been alleged or proven as a result of the alleged violation. In addition, the NAC found the U4 violation to be egregious. *Id.* In support of their conclusion, they rely on three aggravating factors, that Troszak's conduct was intentional, that the alleged violation occurred over an extended time period, and that "Troszak attempted to trivialize his failure to disclose the tax lien." R. at 5002-5004, Pg. 24 of NAC Decision. The premise that Troszak's conduct relating to reporting the tax lien was intentional is simply false. Troszak did not know that he was personally liable. The fact that the alleged violation occurred over several years is only due to the fact that Troszak was not aware of his personal liability during that time period. Furthermore, what the hearing panel viewed as the trivialization of

Troszak's alleged U4 violation, was in fact an argument in support of a mitigating factor, albeit one which the Hearing Panel failed to recognize. The alleged trivialization was Troszak's statement while representing himself before the FINRA Office of Hearing Officers that "I want to establish the fact of who's been harmed here. Eight of my personal friends didn't get a chance to see that I didn't have an exactly correct U4." *Id.* This statement goes directly to a principal consideration in determining sanctions, which is "whether the respondent's misconduct resulted directly or indirectly in injury to such other parties (referring to the investing public, amongst others), and ...the nature and extent of the injury." FINRA Sanction Guidelines at 6, Factor 11. Troszak was expressing the fact that no injury to the investing public or anyone else has been alleged to have resulted from the claimed U4 violation, and if such an injury occurred, it was not very serious in nature. He was not trivializing his alleged U4 violation as the NAC stated, but making a legal argument. The NAC, as was the case with the sanctions imposed for the alleged violation of Rule 8210, failed to consider the mitigating factor of Troszak's reliance upon the advice of legal counsel who advised him that the tax lien was the responsibility of Troszak CPA Group and not him personally. The NAC recognized that Troszak was acting on the advice of his counsel when he amended his U4 but erroneously failed to recognize that he was also acting upon the advice of his attorney during the period when the Form U4 did not reflect the tax lien. Based upon these errors by the NAC in setting the sanctions for the Applicants' alleged U4 violations, those sanctions should be reduced.

V. CONCLUSION

For the reasons set forth above, the Applicants respectfully request that the Commission reverse the NAC's conclusions that the Applicants violated NASD or FINRA rules and by-laws and did so without justification. The Applicants also respectfully request that the Commission

reverse the NAC's decision to impose sanctions against the Applicants and its choice of sanctions.



Douglas A. Troszak,

Personally and on behalf of North Woodward Financial Corporation

Redacted

Date: October 16, 2014