



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

ADMINISTRATIVE PROCEEDING
FILE NO. 3-18414

In the Matter of

Eugene Terracciano,

Respondent

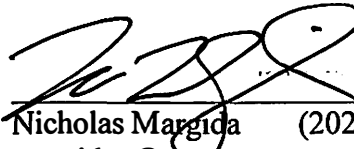
Judge Carol Fox Foelak

DIVISION OF ENFORCEMENT'S FILING OF REDACTED COURT PAPERS

Pursuant to Administrative Law Judge ("ALJ") Carol Fox Foelak's order during the hearing in this matter on March 26, 2019, and ALJ Foelak's corresponding order dated March 28, 2019, the Division of Enforcement (the "Division") hereby files the attached redacted versions of its Motion for Sanctions (and exhibits thereto) filed on December 10, 2018, and its Reply in support of that motion (and exhibit thereto) filed on February 13, 2019. As requested by ALJ Foelak, the Division redacted certain information from the relevant filings and exhibits thereto, including the names of customers and issuers. None of the redacted information constitutes Suspicious Activity Report ("SAR") material or information protected by the Bank Secrecy Act ("BSA"). The Division has not submitted, relied upon, or otherwise used any SAR material or information protected by the BSA during this litigation.

Dated: April 3, 2019

Respectfully submitted,



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In the Matter of Eugene Terracciano
Administrative Proceeding File No. 3-18414
Service List


Pursuant to Commission Rule of Practice 151, 17 C.F.R. § 201.151, I certify that the foregoing was filed with the Office of the Secretary of the Commission and served by email and U.S. Mail, on April 3, 2019, as follows:

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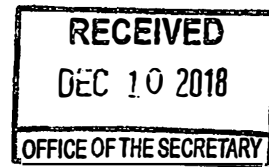
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ADMINISTRATIVE PROCEEDING
FILE NO. 3-18414

In the Matter of
Eugene Terracciano,
Respondent

Judge Carol Fox Foelak



DIVISION OF ENFORCEMENT'S
MOTION FOR SANCTIONS AGAINST RESPONDENT EUGENE TERRACCIANO

December 10, 2018

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I. INTRODUCTION

Respondent Eugene Terracciano (“Terracciano”) concedes that he willfully aided and abetted Aegis Capital Corporation’s (“Aegis’s”) failures to file required Suspicious Activity Reports (“SARs”) on hundreds of transactions, in violation of Section 17(a) of the Securities Exchange Act of 1934 (“Exchange Act”) and Rule 17a-8 thereunder. *See Order Making Findings, Imposing Remedial Sanctions and a Cease-and-Desist Order and Ordering Continuation of Proceedings*, SEC Release No. 4956, 2018 WL 3344228 (July 6, 2018) (hereinafter “Consent Order” or “CO”). As Aegis’s Anti-Money Laundering Compliance Officer (“AML CO”) during the period September 2013 to June 2015, Terracciano knew it was his responsibility to file SARs. Yet, although he had nearly three decades of compliance experience, he failed to file SARs despite being confronted repeatedly with detailed evidence of numerous highly suspicious transactions. In response to these knowing and repeated violations and to protect the public, the Division of Enforcement (“Division”) requests that the Hearing Officer place limitations on Terracciano’s activities, pursuant to Sections 15(b) of the Exchange Act, Section 203(f) of the Investment Advisers Act of 1940 (“Advisers Act”), and Section 9(b) of the Investment Company Act of 1940 (“Investment Company Act”). Specifically, the Division requests that Terracciano be barred from association with any broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization with a right to reapply after a period of two years.

Respondent’s violations are undisputed and egregious. While he served as AML CO, Terracciano permitted suspicious activity in low-priced securities to go completely unreported. He neglected his critical duties as a senior compliance officer and AML CO and displayed a troubling failure to comprehend obvious signs of criminal behavior that posed substantial risk to

market participants. For these and the other reasons set forth below, the requested bar is in the public interest.

II. PROCEDURAL BACKGROUND

On March 28, 2018, the Securities and Exchange Commission (“Commission”) filed an Order Instituting Proceedings (“OIP”) against Terracciano. The OIP alleged that as a result of Terracciano’s failures, from September 2013 through early 2014, Aegis failed to file SARs on hundreds of transactions when it knew, suspected, or had reason to suspect that the transactions involved the use of the broker-dealer to facilitate fraudulent activity or had no business or apparent lawful purpose. (OIP at 1).¹

On May 21, 2018, Terracciano submitted an offer of settlement, which the Commission determined to accept. (CO at 1). In the Consent Order, the Commission required Terracciano to cease and desist from committing or causing any violations of Section 17(a) of the Exchange Act and Rule 17a-8 thereunder and ordered him to pay a civil penalty of \$20,000, pursuant to a payment plan. (*Id.* at 10).

The Consent Order also specified that Terracciano agreed to continued proceedings on the record to determine what remedial action is appropriate in the public interest and that, in

¹ On the same day it filed the OIP, the Commission issued two related Orders. In the first Order, the Commission, *inter alia*, accepted Aegis’s settlement offer and found that Aegis willfully violated Section 17(a) of the Exchange Act and Rule 17a-8 thereunder. *See* Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order, SEC Release No. 82956, 2018 WL 1532091 (Mar. 28, 2018). In the second Order, the Commission accepted the settlement offers of Kevin McKenna, Aegis’s AML CO prior to Terracciano, and Robert Eide, Aegis’s Chief Executive Officer. *See* Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order, SEC Release No. 82957, 2018 WL 1532092 (Mar. 28, 2018). In that Order, the Commission found that McKenna willfully aided and abetted and caused Aegis’s violations, and – among other relief imposed – it barred McKenna from acting as a compliance officer or designated anti-money laundering compliance person for any securities firm, with the right to apply after 18 months. (*Id.*)

connection with those proceedings, the findings of the Consent Order “shall be accepted and deemed true by the hearing officer.” (*Id.* at 9).

III.s FACTS

A.s Aegis’s Low Priced Securities Business

Aegis Capital Corporation, headquartered in New York City, is a dually-registered investment adviser and broker-dealer with multiple branches. (CO at 2). During the relevant period, Aegis had various brokerage customers, including customers of their branch offices, who transacted in low-priced securities. (CO at 3). Several of these customers were foreign financial institutions that effected transactions on behalf of their underlying customers, all of whom were unknown to Aegis. (*Id.*). During the relevant period, Aegis had relationships with various clearing firms that assisted in effecting low-priced securities transactions. (*Id.*).

B.s Aegis’s Anti-Money Laundering Compliance Program – Written Supervisory Procedures Concerning SARs and Specific Red Flags Related to Markets Manipulations^S

During the relevant period, Aegis had specific written supervisory procedures (“WSPs”) governing compliance with its AML responsibilities. Aegis’s WSPs expressly identified Aegis’s AML CO as the individual responsible for deciding whether Aegis was required to file a SAR. (CO at 3; *see also* Aegis WSPs for the period February 27, 2013 to March 25, 2014, submitted herewith in relevant part as Exhibit 1, at 143). Moreover, Aegis’s WSPs stated that all Aegis employees were obligated to “promptly report to the [AML CO] any known or suspected violations of anti-money laundering policies as well as other suspected violations or crimes.” (CO at 3; Exh. 1 at 27).

Pursuant to 31 C.F.R. § 1023.320 (the “SAR Rule”), Aegis was required to file SARs for transactions by, at, or through the firm that involved or aggregated at least \$5,000 if Aegis knew, suspected, or had reason to suspect that, among other things, the transactions involved funds

derived from illegal activity, had no business or apparent lawful purpose, or involved using Aegis to facilitate criminal activity. (CO at 3). Aegis explicitly cited the SAR Rule in its WSPs. (Exh. 1 at 143).

Aegis, in its WSPs, specifically identified certain trading in low-priced securities as suspicious activity that could warrant a SAR filing:

Aegis will file [SARs] for transactions that may be indicative of money laundering activity. Suspicious activities include a wide range of questionable activities; *examples include trading that constitutes a substantial portion of all trading for the day in a particular security . . . [and] heavy trading in low-priced securities.*

(*Id.*, emphasis added).

Aegis's WSPs also identified specific AML red flags associated with low-priced securities transactions. (*Id.* at 182-83, 262). These specific AML red flags included the following:

- i. There is a sudden spike in investor demand for, coupled with a rising price in, a thinly-traded or low-priced security;
- ii. The issuer has been through several recent name changes, business combinations or recapitalizations, or the company's officers are also officers of numerous similar companies;
- iii. The issuer's SEC filings are not current, are incomplete, or nonexistent;
- iv. The customer appears to be acting as an agent for an undisclosed principal, but declines or is reluctant, without legitimate commercial reasons, to provide information or is otherwise evasive regarding that person or entity;
- v. The customer's account has wire transfers that have no apparent business purpose to or from a country identified as a money laundering risk or a bank secrecy haven; and
- vi. The customer, for no apparent reason or in conjunction with other "red flags," engages in transactions involving certain types of securities, such as penny stocks . . . which although legitimate, have been used in connection with fraudulent schemes and money laundering activity.

Many of these red flags identified in Aegis's WSPs tracked or overlapped with the money-laundering red flags contained in FINRA industry notices, including a January 2009 FINRA Notice to Members 09-05 and an April 2002 NASD Notice to Members 02-21, submitted herewith as Exhibits 2 and 3, respectively.

C. a Terracciano Knew Aegis's Policies on SAR Reporting, Including the Fact That a as AML CO, It Was His Responsibility to File SARs.^a

As Director of Compliance and AML CO, Terracciano was thoroughly familiar with Aegis's WSPs. In particular, as AML CO, Terracciano was responsible for updating and did in fact make "adjustments to the WSPs relating to AML procedures" (See Transcript of the Investigative Testimony of Eugene Terracciano, submitted herewith in relevant part as Exhibit 4 and cited hereafter as "Terracciano Tr." at 70:21-71:13). Terracciano also knew that the WSPs placed the responsibility to file SARs solely on him. (*Id.* at 69:23-70:6).

Terracciano acknowledged that for low-priced securities, each of the following is a red a flag: sudden spikes in price and/or trading volume; changes in corporate name or purpose; heavy spending on advertising and promotions and little actual business activity; related party transactions; engaging in a "pump and dump"; or company management with a history of unlawful behavior. (*Id.* at 129:10-130:1; 159:11-23).

D. Terracciano Was Directly Confronted With Clear, Detailed Evidence of Suspicious Activity But Did Not File Any SARs.

Terracciano failed to file SARs on Aegis's behalf on low-priced securities transactions even when he received alerts from Aegis's clearing firm ("AML Alerts") detailing blatantly suspicious transactions. These AML Alerts were sent from Royal Bank of Canada ("RBC"), which Aegis began to use as its clearing firm in December 2012. (CO at 5). Beginning in January 2013, RBC repeatedly identified AML red flags in Aegis's low-priced securities

business and described them in AML Alerts that continued throughout Terracciano's tenure as Aegis's AML CO. (*Id.*)

Terracciano received alerts concerning the following customers:

i. ██████████

In early November 2013, while Terracciano was serving as Aegis's AML CO, RBC sent an AML Alert to Terracciano regarding ██████████, which had an account at Aegis. (*Id.*) That November 1, 2013 AML Alert, (the "November 1 Alert," submitted herewith as Exhibit 5), outlined ██████████' suspicious trading in five low-priced securities, and noted that in about six months ██████████ had sold nearly *1 billion* shares of low-priced securities through Aegis. (Exh. 5 at -20112 (emphasis added); CO at 5).

In the November 1 Alert, RBC also noted that between September 17 and October 31, 2013, ██████████ had sold 31% of ██████████ outstanding shares and that the average daily trading volume had increased by approximately five fold during ██████████' trading while the share price had dropped by approximately 90%. (CO at 6; Exh. 5 at -20113). The AML Alert also explained that ██████████ had experienced a rapid increase in its stock price and trading volume that coincided with a promotional campaign that was inconsistent with the company's financial performance reflected in its SEC filings. (CO at 6; Exh. 5 at -20113).

RBC also noted in the November 1 Alert that ██████████ had reported no revenues and that ██████████ had sold over 60% of the company's outstanding shares in two and a half months while the share price had dropped by approximately 50%. (CO at 6; Exh. 5 at -20113). In addition to its suspicious trading in the low-priced stock of ██████████ and ██████████, RBC identified in the November 1 Alert ██████████' similarly suspicious trading in three other low-priced securities. (CO at 6). For example, the November 1 Alert notified

Terracciano that [REDACTED] had sold more shares of one particular low-priced security in three months than that issuer even had outstanding. (CO at 6; Exh. 5 at -20113).

After detailing in the November 1 Alert [REDACTED]'s suspicious trading in the five low-priced securities, RBC requested that Aegis provide a description of: (i) the due diligence it performed on the customer; (ii) the due diligence it performed on the securities [REDACTED] liquidated in the account; and (iii) how Aegis was comfortable with the activity in the account. (*Id.*).

Although Terracciano recognized the red flags associated with the trading by [REDACTED] [REDACTED] (Terracciano Tr. at 129:10-130:1), and closed the account due to the presence of suspicious activity, Terracciano did not file a SAR on Aegis's behalf. (CO at 6). Terracciano claims to have investigated the information in the November 1, 2013 Alert, but "cannot remember" why he did not file a SAR. (Terracciano Tr. at 134:12-16). Notably, a November 5, 2013 email (submitted herewith as Exhibit 6) indicates that Terracciano had concerns after reviewing "account activity, account opening paperwork . . . etc." with regard to the issues raised in the November 1 Alert. (Exh. 6 at -20680). Yet, despite having the AML Alert and other information indicating potentially criminal – and certainly suspicious – activity in [REDACTED] [REDACTED]'s account, Terracciano did not file a SAR.

Critically, Terracciano knew that closing an account did not "substitute for filing a SAR." (Terracciano Tr. at 152:6-8; CO at 6). Moreover, Terracciano could not provide any written analysis or otherwise demonstrate that he had even considered filing SARs for these transactions. (CO at 6).

ii. [REDACTED]

While Terracciano was the AML CO responsible for filing SARs on behalf of Aegis, another customer – [REDACTED] and [REDACTED],

█████ (collectively ██████) – engaged in suspicious low-priced securities transactions for which he did not file a SAR on Aegis’s behalf. (CO at 6). ██████ was a foreign financial institution that traded on behalf of underlying customers who were unknown to Aegis. (*Id.*) Trading on behalf of an unknown principal is identified by Aegis’s WSPs as a money-laundering red flag. (Exh. 1 at 25).

Between June 11 and 17, 2013, and during a paid promotional campaign, ██████ sold approximately 340,000 shares of ██████ for proceeds of approximately \$248,000. (CO at 6).

Moreover, another Aegis customer, ██████, traded suspiciously in ██████ at the same time as ██████ (CO at 7). In particular, ██████ sold approximately 760,000 shares of ██████ through Aegis during the same promotional campaign, resulting in proceeds of approximately \$840,000. (*Id.*) ██████ was yet another foreign financial institution that traded on behalf of underlying customers who were unknown to Aegis. (*Id.*)

On December 2, 2013, while Terracciano was serving as Aegis’s AML CO, RBC sent an AML Alert (the “December 2 Alert”, submitted herewith as Exhibit 7) to Terracciano, regarding ██████’s trading in ██████ and wrote that the trading “*exhibited characteristics commonly associated with a pump-and-dump scheme*; including paid stock promotion, a significant increase in both price and trading volume, followed by a precipitous drop in price and volume.” (Exh. 7 at -8794; CO at 7) (emphasis added).

In the December 2 Alert, RBC also noted that ██████ had changed both its name and business from an automotive parts manufacturer to a medical device company and that it had no revenue and minimal trading volume before the paid stock promotion began. (*Id.*) The December 2 Alert also notified Terracciano that ██████ trading in ██████ was similar to the

suspicious trading of two other Aegis customers – [REDACTED] and [REDACTED] [REDACTED]² – which had prompted RBC to request that Aegis close those accounts just months earlier in August. (*Id.*).

Terracciano recognized that the information in the December 2 Alert created strong reason to suspect that illegal activity had occurred. (Terracciano Tr. 158:11-159:23). Indeed, in an email sent just 24 minutes after receiving the December 2 Alert, Terracciano ordered that [REDACTED] account be closed and acknowledged that the compliance department did “not have the bandwidth to monitor the account.” (Exh. 7 at -8792). This lack of compliance “bandwidth” was particularly relevant since Terracciano subsequently learned that the Aegis branch manager who supervised the trading had not been conducting required reviews. (Terracciano Tr. 173:6-175:1 (agreeing that the failure to conduct required reviews “makes matters worse”)).

Worse still, Terracciano testified that even if a client engages in a “pump and dump” scheme using its Aegis account, it would not “taint the account forever.” (Terracciano Tr. 212:14-18). Indeed, after receiving the December 2 Alert and initially requesting that the account be closed, Terracciano persuaded RBC to allow the account to continue trading by explaining that it would be restricted to allow trades in only stocks listed on the major exchanges. (*See* December 3, 2013 email thread, submitted herewith as Exhibit 8, at Bates - 8804; Terracciano Tr. at 207:25-208:14).

[REDACTED]’s accounts were ultimately closed because of AML concerns. (CO at 7). But Terracciano did not finally close the account until after he learned that the relevant branch manager had not, in fact, blocked the account from trading in low-priced securities as promised

² The SEC later sued [REDACTED] for violating Section 5 of the Securities Act of 1933. [REDACTED]

or been conducting the requisite reviews of [REDACTED] trading. (*Id.*; *see also* Exh. 7 at -8792; Exh. 8 at -8804; Terracciano Tr. at 167:9-20). Yet despite these red flags associated with the trading in [REDACTED] by [REDACTED] and at least one other Aegis customer, and the fact that a branch manager had not told him the truth or conducted any of the requisite trade reviews, Terracciano still did not file a SAR on Aegis's behalf. As a result, Aegis withheld from the relevant authorities information that strongly indicated Aegis customers were engaged in criminal stock manipulation.

In fact, no regulatory agencies or criminal authorities were ever alerted by Aegis to the clear indicia that [REDACTED] was engaging in market manipulation. [REDACTED] did not face regulatory or criminal scrutiny at that time. A few years later, in March 2018, the Commission sued [REDACTED] in federal district court, alleging it had engaged in a fraudulent "pump and dump" scheme to manipulate the unlisted stock of a different microcap company. *See SEC v. [REDACTED]*. [REDACTED]. Criminal charges were brought against the same defendants and other individuals by the U.S. Attorney's Office for the Eastern District of New York. *See United States v. [REDACTED]*.

In short, after receiving the December 2 Alert, Terracciano conducted only 24 minutes of research. He acknowledged, however, that an average investigation into an issue like the one presented in the December 2 Alert would take a "number of days." (Terracciano Tr. at 163:12-15). Having been presented with strong evidence of illegal conduct and learning that the branch manager did not tell the truth or conduct trade reviews, Terracciano did not produce any written analysis or create any other documents demonstrating that he even considered filing a SAR. (CO 7).

iii. [REDACTED]

[REDACTED], a New York corporation, is a microcap hedge fund and was an Aegis customer during the relevant period. (CO at 8). Between February 10, 2014 and February 20, 2014, [REDACTED] sold 705.9 million shares of [REDACTED] through Aegis for proceeds of approximately \$1.24 million. [REDACTED] is a low-priced security that traded on OTC Link. (*Id.*).

On February 19, 2014, RBC sent an AML Alert (the "February 19 Alert," submitted herewith as Exhibit 9) to Terracciano, explaining that it was going to block [REDACTED]' account at market close because, among other reasons, [REDACTED] had already sold 200 million shares of [REDACTED] that day and 2.7 billion shares of low-priced securities since it opened its account. (Exh. 9 at -17615-16; CO at 8). In addition to the suspicious trading highlighted in the February 19 Alert, RBC also explained that it could "certainly list more concerns with these companies if [Aegis] need[ed] more reasons why [RBC was] concerned." (Exh. 9 at 17615).o

In addition to the suspicious trading, there were numerous other indicia that there was manipulative trading in [REDACTED] (CO at 8). For example, there was a large increase in price and volume of trading in [REDACTED] that coincided with a promotional campaign. (*Id.*). Moreover, the company's name had changed several times before becoming [REDACTED] (*Id.*).

The suspicious information in the February 19 Alert was not, however, limited to the [REDACTED] trades; it also described suspicious trading by [REDACTED] in over 1.6 billion shares of the securities of ten additional microcap issuers, all of whom exhibited red flags – as set forth in Aegis's WSPs – such as numerous stock splits, non-reporting to the SEC, and name changes. (Exh. 9 at -17615-16). RBC also asked Aegis to explain: (i) its due diligence on the customer; (ii) its due diligence on the securities liquidated in the account; and (iii) how Aegis became comfortable with the activity. (*Id.* at -17616-17).

Even after Aegis and Terracciano received the February 19 Alert, Aegis continued to allow [REDACTED] to trade in [REDACTED]. Indeed, on February 19 and 20, 2014, [REDACTED] sold an additional 120 million shares of [REDACTED] (*Id.* at -17615).

Despite the significant trading by [REDACTED] in [REDACTED] and the red flags associated with its trading in other low-priced securities, Terracciano still did not file a SAR on Aegis's behalf. (CO at 9). And once again, there is no evidence that Terracciano even considered filing a SAR.

As a result, despite all the red flags, no regulatory agencies or criminal authorities were alerted by Aegis to the suspicious trading in [REDACTED] account, including clear indicia that it may have been engaging in market manipulation. In 2016, a full two years after Terracciano failed to file a SAR on [REDACTED]' trading in [REDACTED] the SEC filed a complaint against [REDACTED] and its CEO, alleging fraud. *SEC v. [REDACTED]*

E. Terracciano Did Nothing to Verify Why, in Light of These Repeated AML Alerts, Aegis's Trade Review Systems Did Not Flag Low-Price Securities Transactions as Suspicious.

Aegis's trade surveillance system, compliance personnel, and branch managers did not alert Terracciano to any of the suspicious activity described above. (Terracciano Tr. at 173:20-174:21, 186:12-194:14). Although Terracciano testified that he would have wanted to know about the trading as it was occurring, (*id.* at 193:11-25), after he was notified of the suspicious activity by RBC through the AML Alerts, he did nothing to investigate or verify why Aegis's own trade review systems had failed to detect this activity and did nothing to remediate those failures. (*Id.* at 189:18-190:6, explaining that he simply reminded the relevant compliance

personnel that they were supposed to be doing “Google searches” to check for “marketing news”).

Had Terracciano followed up to learn why suspicious transactions were not being brought to his attention through the firm’s own systems, he would have learned that the firm’s trade surveillance system did not even analyze transactions in Delivery Versus Payment/Receive Versus Payment (“DVP/RVP”) account.³ (CO at 5). In DVP/RVP accounts held at Aegis, the customer deposited their shares at another firm in a custodial account, and the sale transactions were effected through Aegis. (*Id.* at 3). All of the suspicious activity described in the AML Alerts and outlined above occurred in DVP/RVP accounts, meaning Aegis’s trade surveillance system did not analyze them at all.

Terracciano claims that he reacted to the AML Alerts by having “subsequent conversations” with the compliance personnel⁴ that monitored the trade surveillance system and general conversations with the branch heads. (Terracciano Tr. at 194:1-195:14). Terracciano also purportedly did “some look-backs,” *id.* 195:19-25, but produced no contemporaneous evidence of what those “look-backs” entailed or found, if they were conducted at all.

³ Aegis personnel testified that, to review trades for suspicious activity, the firm relied heavily on a trade review system provided by RBC called Protegent Surveillance, which they refer to as “ProSurv.” *See, e.g.,* Terracciano Tr. 87:4 – 90:16. The ProSurv system monitored all the firm’s transactions. *See* the Transcript of the Investigative Testimony of Craig Kotash, (“Kotash Tr.”), submitted herewith as Exhibit 10, at 146:12 - 147:18. This system, however, did not analyze DVP/RVP transactions. In July 2013, Aegis upgraded to the ProSurv Enhanced system, but this system’s default setting also did not analyze DVP/RVP transactions and was not adjusted to do so during the Relevant Period. *See* March 10, 2016 email from counsel for RBC, submitted herewith as Exhibit 11; *see also* Kotash Tr. 122:25-123:24 (testifying that nothing changed in his compliance review despite ProSurv upgrade).

⁴ A compliance employee that Terracciano claims he spoke to upon receiving the AML Alerts testified that, in fact, he does not recall ever speaking to Terracciano regarding the AML Alerts specifically or any of the issues RBC raised in them. *See* Kotash Tr. 156:4-158:8.

IV. ARGUMENT

Terracciano's failure to fulfill his important responsibilities as Aegis's AML CO establishes that it is in the public interest to bar him from the industry with a right to reapply after two years. As described above, Terracciano was completely derelict both in filing SARs – particularly after receiving the AML Alerts – and in fulfilling his other obligations as an AML CO. He failed to file SARs when presented with patently suspicious activity, and he failed to address obvious issues in Aegis's compliance and trade surveillance systems for low-priced securities. Moreover, Terracciano showed a basic disregard for the seriousness of the unlawful conduct described in the AML Alerts and the potential harm to investors.

A. Legal Standards

Section 15(b) of the Exchange Act [15 U.S.C. § 78o(b)] and Sections 203(e) and (f) of the Advisers Act [15 U.S.C. § 80b-3(e), (f)] grant the Commission the power to, among other things, place limitations on or bar, in the public interest, any person who is associated with a broker/dealer or investment adviser who “willfully aided [and/or] abetted . . . the violation by any other person of any provision” of the securities laws or rules thereunder. Exchange Act Section 3(a)(18), [15 U.S.C. § 78c(a)(18)] and Advisers Act Section 202(a)(17) [15 U.S.C. § 80b-2(a)(17)] define “officer” and “any employee” to be an “associate” of a broker/dealer and adviser.^{5e}

To determine whether a bar is in the public interest, the Commission typically considers the following factors:

the egregiousness of the [respondent's] actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of the [respondent's] assurances against future violations, the [respondent's] recognition of the wrongful nature of his

⁵ There is no dispute that Terracciano was an officer and employee of Aegis and that he willfully aided and abetted Aegis's violations of Exchange Act Section 17(a) and Rule 17a-8 thereunder. (CO at 1, 2, 9).

conduct, and the likelihood that the [respondent's] occupation will present opportunities for future violations.

Steadman v. SEC, 603 F.2d 1126, 1140 (5th Cir. 2000). Deterrence may also be considered “as a part of the overall remedial inquiry.” *PAZ Securities, Inc. v. SEC*, 494 F.3d 1059, 1066 (D.C. Cir. 2007) (quoting *McCarthy v. SEC*, 406 F.3d 179, 189 (2d Cir. 2005)). The inquiry “into the appropriate sanction to protect the public interest is a flexible one, and no one factor is dispositive.” *In re Conrad P. Seghers*, Advisers Act Rel. No. 2656, 2007 SEC Lexis 2238, at e *13 (Sept. 26, 2007), *aff'd*, 548 F.3d 129 (D.C. Cir. 2008).e

B. It Is in the Public Interest To Bar Terracciano From the Industry for Two Years.

i. Terracciano's Conduct Was Egregious.

Terracciano was repeatedly presented with detailed evidence that gave him a reason to suspect that Aegis clients were engaged in manipulative trading and securities fraud, often in the securities of multiple issuers. The AML Alerts described conduct that Terracciano recognized or at least should have recognized, in light of Aegis's WSPs, FINRA guidance, and his decades of compliance experience, as clearly suspicious. Yet, although he knew it was his responsibility to file SARs, he did nothing. There is no documentary evidence that Terracciano even considered filing any SARs. Terracciano's failure to file SARs when confronted with red flags of illegale activity demonstrates that a bar is necessary to protect the public. *In the Matter of Ronald Se Bloomfield, et al.*, S.E.C. Release No. 9553, 2014 WL 768828, *16 (imposing sanctions,e including a two-year industry bar, on “the designee for making decision on behalf of [brokerage]e about filing SARs . . . [because] he was well aware of many of the red flags necessitating the filing of SARs.”). e

Critically, Terracciano did not discover the suspicious activity described in the AML Alerts, or any other suspicious activity, through his own diligence or from other Aegis personnel. Rather, with respect to the information in AML Alerts, Aegis's clearing firm flagged the conduct as improper and directly questioned how Aegis had allowed it to occur. In other words, another securities firm told Terracciano that it had, at a minimum, a reason to suspect that Aegis was being used by its customers to engage in illegal conduct, and Terracciano's response was to ignore his known responsibility to file SARs. RBC was also clearly exasperated with Aegis; the AML Alerts it sent to Aegis demanded to know what review and analysis Aegis was doing that allowed the subject accounts to remain open and engage in this type of trading.

In short, Terracciano knew the trading was highly suspicious, and he knew that RBC—another securities firm and critical business partner—was alarmed and frustrated that Aegis had allowed it to occur. In that context, his dereliction of his duty to file SARs was egregious and warrants a bar. *Bloomfield*, 2014 WL 768828 at *17 (sanctions appropriate in part because individual responsible for filing SARs did not do so, even though he knew his brokerage's clearing firm had closed accounts and ultimately terminated clearing agreement due to persistent improper activity).

Terracciano's failure to act is even more egregious because, particularly after he received the AML Alerts, he knew that certain Aegis customers were engaged in highly suspicious low-priced securities transactions. Yet, as he testified, no Aegis employee ever reported any suspicious low-priced securities activity to him, and the firm's surveillance system never flagged any such activity either. (Terracciano Tr. at 102:16-21). Thus, he must have known one of two things: no one at Aegis was detecting the activity, or certain employees were simply allowing it to occur. In fact, with respect to ██████'s suspicious trading, Terracciano knew that the

relevant branch manager was not conducting the required trade reviews. Still, Terracciano did not investigate why Aegis's trade surveillance systems or compliance personnel had not flagged this conduct, and he did nothing to ensure that such suspicious activity would be detected in the future. There is also no evidence that, upon receiving the AML Alerts, Terracciano undertook a review of [REDACTED]s, [REDACTED] or [REDACTED] other trading, or trading in the same low-priced securities by other Aegis clients.

ii. Terracciano's Misconduct Was Recurrent.

Terracciano's failures were recurrent. It is undisputed that from September 2013 through early 2014, while Terracciano was serving as Aegis's AML CO, Aegis failed to file SARs on hundreds of transactions. (CO at 2). In that period, Terracciano received at least three AML Alerts detailing blatantly suspicious trading activity by three⁶ Aegis customers in the securities of at least 15 issuers. In the AML Alerts, RBC repeatedly expressed its concern about this potentially unlawful activity and inquired about what, if any, due diligence Aegis had conducted to get comfortable with the activity.

iii. Terracciano Had a High Degree of Scierter.

Terracciano knew that as AML CO it was his duty to file SARs. Terracciano was also familiar with the red flags set forth in Aegis's WSPs and the FINRA guidance indicating that a SAR may need to be filed. Moreover, as his testimony shows, he knew the trading activity described in the AML Alerts was suspicious on its face. In fact, he was sufficiently alarmed in some cases to order the accounts closed. Terracciano also knew, or was reckless in not realizing, that neither Aegis's personnel nor its compliance systems and procedures had flagged the

⁶ The December 2 [REDACTED] Alert also referenced two additional customers -- [REDACTED] and [REDACTED] -- who had engaged in suspicious trading activity.

suspicious activity and brought it to his attention. Terracciano therefore acted with a high degree of scienter, strongly supporting the SEC's requested relief.

iv. Terracciano Does Not Appear To Grasp the Wrongful Nature of His Conduct, Creating a Risk of Future Violations.

In his testimony, Terracciano described taking a flexible approach with regard to customers who are clearly engaging in suspicious activity. For instance, he argued, troublingly, that engaging in a "pump and dump" is *not* by itself sufficient cause to close a client account. Terracciano also failed to display a serious commitment to addressing the fact that Aegis's systems and procedures were not equipped to identify or restrict that activity.

Therefore, notwithstanding Terracciano's bifurcated settlement offer, there is strong reason to doubt that Terracciano fully understands the seriousness of the violations. His reassurances against future violations should be viewed skeptically, especially in the context of his recurrent incompetence and disregard for his AML CO reporting and other obligations. And, because Terracciano intends to return to work as a compliance professional in the securities industry, there is a substantial risk that he will be in a position to commit future violations. As a result, the requested bar is in the public interest. a

v. The Division's Requested Sanction Is Consistent With Precedent and the Goals of Deterrence.

The Division is seeking a bar, with a right to reapply after two years, restricting Terracciano's employment as a compliance or AML professional. Precedent makes clear that the sanction sought by the Division is appropriate. In *Bloomfield*, the Commission imposed a two-year bar in part because the officer responsible for filing SARs "failed to respond to red flags of possible misconduct . . . [and] enabled customers . . . to perpetuate their suspicious activity without detection for a substantial period." 2014 WL 768828, at *19.

Prior settlements for violations of Exchange Act Rule 17a-8 also support a two-year bar. For example, in the settled administrative proceeding, *In the Matter of Park Financial Group, Inc., et al.*, File No. 3-12614 (Order Making Findings, December 5, 2007), the Commission imposed a two-year associational bar against the Respondent, who like Terracciano had been responsible for filing SARs, because he “continued to effect transactions in the securities of [issuer] for the BVI Companies’ account during the relevant time period despite the obvious risks set forth above [including related-party transactions] and the suspicious nature of the transactions.” Similarly, in another settled administrative proceeding, *In the Matter of Jerard Basmagy*, File No. 3-18487 (May 16, 2018), the Commission imposed a three-year bar where the Respondent AML Officer, as here, ignored the red flags set forth in his brokerage’s stated policies regarding suspicious transactions and failed to act on warnings from the clearing firm regarding transactions in low-priced securities. Accordingly, the range of sanctions for analogous conduct strongly supports the imposition of the two-year bar requested by the Division.

Finally, granting the Division’s requested sanction will deter future violations of Rule 17a-8 by sending a message to other AML COs and other broker-dealer compliance officers that the repeated, knowing, and egregious disregard for clear SAR-reporting obligations will not be permitted. AML COs have an essential duty to report suspicious conduct and prevent their firms from being used to perpetrate crimes.

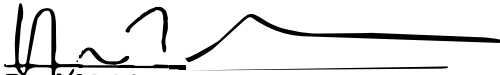
V. **CONCLUSION**

In sum, Terracciano willfully aided and abetted Aegis's violations of Section 17(a) of the Exchange Act and Rule 17a-8 thereunder, and his knowing and egregious conduct readily establishes that the bar requested by the Division is in the public interest. Accordingly, the Division requests that its motion be granted and that Terracciano be barred from the securities industry, with the right to reapply after a period of two years.

Dated: December 10, 2018

Respectfully submitted,

DIVISION OF ENFORCEMENT



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In the Matter of Eugene Terracciano
Administrative Proceeding File No. 3-18414
Service List

Pursuant to Commission Rule of Practice 151, 17 C.F.R. § 201.151, I certify that the foregoing Division of Enforcement's Motion for Sanctions Against Respondent Eugene Terracciano was filed with the Office of the Secretary of the Commission and served by email and U.S. Mail, on December 10, 2018, as follows:

Office of the Secretary (by hand)
Securities and Exchange Commission (original and three copies)
100 F Street, NE, Mail Stop 1090
Washington, DC 20549

Honorable Carol Fox Foelak (by email)
Administrative Law Judge
Securities and Exchange Commission
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Washington, DC 20549
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Counsel for Respondent

Dated: December 10, 2018



Daniel Maher

Exhibit 1

Aegis Capital Corp.

Aegis Capital Corp.

February 27, 2013

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The Firm will promptly report to FINRA (not later than 30 calendar days after the Firm has concluded or reasonably should have concluded) that an associated person of the Firm or the Firm itself has violated any securities-, insurance-, commodities-, financial- or investment-related laws, rules, regulations or standards of conduct of any domestic or foreign regulatory body or self-regulatory organization. Conduct reported will be conduct that has a significant monetary result with respect to the Firm, customers, or markets, or multiple instances of any violative conduct.

Relating to reported events, the Firm will file with FINRA copies of the following. Document filings will not be duplicated if the documents have already been provided to FINRA's Registration and Disclosure staff within 30 days of staff request:

- 1.a any indictment, information or other criminal complaint or plea agreement for conduct reportable under a paragraph (a)(1)(E) of this Rule;a
- 2.a any complaint in which a member is named as a defendant or respondent in any securities- or commodities-related private civil litigation, or is named as a defendant or respondent in any financial-related insurance private civil litigation;a
- 3.a any securities- or commodities-related arbitration claim, or financial-related insurance arbitration claim,a filed against a member in any forum other than the FINRA Dispute Resolution forum;a
- 4.a any indictment, information or other criminal complaint, any plea agreement, or any private civil complaint or arbitration claim against a person associated with a member that is reportable under a question 14 on Form U4, irrespective of any dollar thresholds Form U4 imposes for notification, unless,a in the case of an arbitration claim, the claim has been filed in the FINRA Dispute Resolution forum.a

2.15 Money Laundering

[FINRA Rule 3310; Bank Secrecy Act]

Money laundering is a serious crime potentially related to the funding of terrorist activities. It is the subject of extensive federal regulations that impose requirements on financial institutions, such as broker-dealers and their employees, to detect and prevent potential money laundering activities. This is an obligation of each employee of Aegis.

Money laundering is the movement of criminally derived funds to conceal the true source, ownership, or use of the funds. The funds are filtered through a maze or series of transactions, so the funds are "cleaned" to look like proceeds from legal activities.

In general, money laundering occurs in three stages. Cash first enters the financial system at the "placement" stage, where the cash profits from criminal activity are converted into monetary instruments, such as money orders or traveler's checks, or deposited into accounts at financial institutions. At the "layering" stage, the funds are transferred or moved into other accounts or other financial institutions to separate further the proceeds from their criminal origin. At the "integration" stage, the funds are reintroduced into the economy and used to purchase legitimate assets or to fund further criminal or legitimate activities.

Engaging in money laundering is a federal crime with severe penalties for those engaged in criminal activities and those who facilitate, intentionally or inadvertently, money laundering. It is important that Aegis, as well as all employees, remain diligent and active participants in Aegis's anti-money laundering (AML) program.

2.15.1 Background

The Currency and Foreign Transactions Reporting Act, also known as the Bank Secrecy Act (BSA), and its accompanying regulation, is a tool the U.S. government uses to fight drug trafficking, money laundering, and other crimes. Congress enacted the BSA to prevent financial service providers (such as banks and broker-dealers) from being used as intermediaries for, or to hide the transfer or deposit of, money derived from criminal activity. Money laundering schemes may include the use of wire transfers, cash, bearer instruments, travelers' checks, money orders, cashiers' checks, and other negotiable instruments.

Aegis is required to comply with the reporting, recordkeeping, and record retention requirements of the BSA. The requirements govern the payment, receipt, or transfer of currency within and into and out of the U.S. and foreign financial transactions and accounts.

2.15.2 Shell Companies

[FINCen advisory on shell companies: http://www.fincen.gov/AdvisoryOnShells_FINAL.pdf]

Shell companies may represent potential money laundering risks. "Shell company" refers to non-publicly traded corporations, limited liability companies (LLCs), and trusts that typically have no physical presence (other than a mailing address) and generate little or no independent economic value. It is important for employees to be aware of the risks involved in dealing with shell companies.

Most shell companies are formed for legitimate business purposes such as to hold stock or intangible assets of another business entity or to facilitate domestic and cross-border currency and asset transfers and corporate mergers. Unfortunately, shell companies have become common tools for money laundering and other financial crimes, primarily because they are easy and inexpensive to form and operate, and ownership and transactional information can be concealed from regulatory and law enforcement authorities. Most states do not collect or require disclosure of ownership information at the formation stage or after.

Agents, also known as intermediaries or nominee incorporation services (NIS), can play a central role in the formation and maintenance of shell companies. Agents and NIS firms offer a wide range of services that may include offering an office address, mail-forwarding services, local telephone listings, and other services that may give the appearance of a locally-established business. Some agents and NIS firms also provide nominee services which can preserve a client's anonymity. Some risk indicators of shell companies potentially engaged in money laundering are:

- An inability to obtain (through Internet searches, commercial database searches, or direct inquiries to the company's foreign correspondent bank) information necessary to identify originators or beneficiaries of wire transfers.
- A foreign correspondent bank exceeds the anticipated volume projected in its client profile for wire transfers in a given period or an individual company exhibits a high amount of sporadic activity that is inconsistent with normal business patterns.
- Payments have no stated purpose, do not reference goods or services, or identify only a contract or service number.
- Goods or services of the company do not match the company's profile based on information previously provided.
- Transacting businesses share the same address, provide only a registered agent's address, or raise other address-related inconsistencies.
- An unusually large number and variety of beneficiaries receive wire transfers from one company.
- Frequent involvement of beneficiaries located in high-risk, offshore financial centers.
- Multiple high-value payments or transfers between shell companies with no apparent legitimate business purpose.

2.15.3 Penalties

Participation in a money laundering scheme or the knowing receipt of proceeds from criminal activities is a crime. Aegis and its employees are subject to severe criminal, civil, and regulatory penalties if they facilitate or participate in money laundering activities. Violations by employees may result in internal disciplinary action including termination.

An employee may be deemed to be facilitating or participating in money laundering by engaging in a transaction with a customer (accept a deposit, arrange a withdrawal, effect a trade, *etc.*) when he or she is aware of, or willfully ignores, the fact that the customer is engaged in illegal activities.

2.15.4 Treasury Dept. OFAC List

The U.S. Treasury Department's Office of Foreign Assets Control (OFAC) is responsible for publishing sanctions against persons, corporations, and other entities including foreign governments that have been identified by the U.S. Government as engaging in criminal activities including drug trafficking and terrorist activities. Aegis is obligated to check its accounts against the lists of blockings to ensure it does not engage in prohibited transactions which include securities transactions and transfer of assets out of a blocked account or to a blocked person or entity.

Aegis has procedures to monitor the OFAC lists and comply with requirements to block property and notify OFAC when required. Questions regarding Aegis's program should be referred to the AML Compliance Officer. More information is also available at the OFAC web site at www.treas.gov/ofac.

2.15.5 Preventing Money Laundering

There are a number of ways Aegis and its employees can avoid money laundering schemes.

2.15.5.1 Knowing The Customer

Being familiar with the customer's financial resources, business activities, and sources of funds are avenues for knowing the customer. Knowing the customer occurs at the time an account is opened as well as during the operation of a customer's account.

The identity of customers must be verified when a new account is opened. Procedures for verifying customer ID are explained in the chapter *ACCOUNTS* in the section *New Accounts*.

2.15.5.2 Risk Indicators

[NASD Notice to Members 02-21]

The following are examples of risk indicators (red flags) that may suggest potential money laundering.

Red Flags indicating potential Money Laundering
The customer exhibits unusual concern regarding the Firm's compliance with government reporting requirements and the Firm's AML policies, particularly with respect to his or her identity, type of business and assets, or is reluctant or refuses to reveal any information concerning business activities, or furnishes unusual or suspect identification or business documents.
The customer wishes to engage in transactions that lack business sense or apparent investment strategy, or are inconsistent with the customer's stated business strategy.
The information provided by the customer that identifies a legitimate source for funds is false, misleading, or substantially incorrect.
Upon request, the customer refuses to identify or fails to indicate any legitimate source for his or her funds and other assets.
The customer (or a person publicly associated with the customer) has a questionable background or is the subject of news reports indicating possible criminal, civil, or regulatory violations.
The customer exhibits a lack of concern regarding risks, commissions, or other transaction costs.
The customer appears to be acting as an agent for an undisclosed principal, but declines or is reluctant, without legitimate commercial reasons, to provide information or is otherwise evasive regarding that person or entity.
The customer has difficulty describing the nature of his or her business or lacks general knowledge of his or her industry.

The customer engages in suspicious activity involving the practice of depositing penny stocks, liquidates them, and wires proceeds. A request to liquidate shares may also represent engaging in an unregistered distribution of penny stocks which may also be a red flag. [FINRA Regulatory Notice 09-05]
The customer attempts to make frequent or large deposits of currency, insists on dealing only in cash equivalents, or asks for exemptions from the Firm's policies relating to the deposit of cash and cash equivalents.
The customer engages in transactions involving cash or cash equivalents or other monetary instruments that appear to be structured to avoid the \$10,000 government reporting requirements, especially if the cash or monetary instruments are in an amount just below reporting or recording thresholds.
For no apparent reason, the customer has multiple accounts under a single name or multiple names, with a large number of inter-account or third-party transfers.
The customer is from, or has accounts in, a country identified as a non-cooperative country or territory by the Financial Action Task Force (FATF).
The customer's account has unexplained or sudden extensive wire activity, especially in accounts that had little or no previous activity.
The customer's account shows numerous currency or cashiers check transactions aggregating to significant sums.
The customer's account has a large number of wire transfers to unrelated third parties inconsistent with the customer's legitimate business purpose.
The customer's account has wire transfers that have no apparent business purpose to or from a country identified as a money laundering risk or a bank secrecy haven
The customer's account indicates large or frequent wire transfers, immediately withdrawn by check or debit card without any apparent business purpose.
The customer makes a funds deposit followed by an immediate request that the money be wired out or transferred to a third party, or to another firm, without any apparent business purpose.
The customer makes a funds deposit for the purpose of purchasing a long-term investment followed shortly thereafter by a request to liquidate the position and transfer of the proceeds out of the account.
The customer engages in excessive journal entries between unrelated accounts without any apparent business purpose.
The customer requests that a transaction be processed in such a manner to avoid the Firm's normal documentation requirements.
The customer, for no apparent reason or in conjunction with other "red flags," engages in transactions involving certain types of securities, such as penny stocks, Regulation "S" (Reg S) stocks, and bearer bonds, which although legitimate, have been used in connection with fraudulent schemes and money laundering activity. (Such transactions may warrant further due diligence to ensure the legitimacy of the customer's activity.)
The customer's account shows an unexplained high level of account activity with very low levels of securities transactions.
The customer maintains multiple accounts, or maintains accounts in the names of family members or corporate entities, for no apparent business purpose or other purpose.
The customer's account has inflows of funds or other assets well beyond the known income or resources of the customer.

2.15.6 Cash Deposits Not Accepted

Aegis does not accept cash deposits or cash equivalents (money orders, travelers checks). Customers who attempt to deposit cash should be advised to submit a personal check to his or her account.

2.15.7 Reports Of AML Non-Compliance And Other Potential Crimes

All employees are obligated to promptly report to the AML Compliance Officer any known or suspected violations of anti-money laundering policies as well as other suspected violations or crimes. If the potential violation implicates the AML Officer, it should be reported to a senior officer of Aegis. All reports are confidential and the employee will suffer no retaliation for making them.

What to report: Crimes or suspected crimes by individuals (whether associated with Aegis, a customer, or prospective customer) are required to be reported. This includes suspicion that Aegis is being used as a conduit for criminal activity such as money laundering or structuring transactions (discussed below) to evade the Bank Secrecy Act reporting requirements. There is no clear definition of what constitutes a "crime." If you believe some improper or illegal activity is occurring, it is your obligation to report it.

SAR reports: Broker-dealers are required to file Suspicious Activity Reports (SARs) for transactions that may be indicative of money laundering activity.

By law, Aegis and its employees cannot disclose to the customer or anyone other than authorized regulators that it has filed a SAR. Questions regarding SAR filings should be referred to Compliance.

2.15.8 Currency Transaction Reporting

The Bank Secrecy Act requires broker-dealers to report certain transactions relating to currency transactions, as follows:

- Report cash or currency deposits of more than \$10,000, including multiple deposits on the same day that would total more than \$10,000. A currency Transaction Report (CTR) is filed with the Financial Crimes Enforcement Network (FinCEN), a bureau of the Treasury Department. Some state regulators also require reporting of currency transactions.
- Report currency or bearer instruments over \$10,000 transferred into or out of the U.S. The Currency and Monetary Instrument Transportation Report (CMIR) is filed with the U.S. Customs Service.

2.15.8.1 Prohibition Against Structuring Deposits To Avoid Reporting

Cash or currency deposits or attempted deposits which appear to be part of a deposit structure to avoid IRS or Customs currency reporting requirements or Firm limitations, or are otherwise suspicious, may not be accepted and must be reported to Compliance. Employees are prohibited from:

- aiding or advising a customer in structuring a transaction to avoid reporting requirements
- holding instruments for deposit on succeeding days
- transporting cash or cash equivalents or bearer instruments to a bank on behalf of a customer

2.15.9 Recordkeeping Requirements

In addition to reporting requirements, broker-dealers are subject to requirements to maintain records of transfers of funds (including wire fund transfers) of \$3,000 or more. This includes transfers between accounts that are not for the same owner and transfers to third parties including banks and other financial institutions. Records of transfers are available for inspection by regulators and other appropriate authorities, when requested.

2.15.10 AML Compliance Officer

Aegis has designated an AML Compliance Officer who is responsible for overseeing Aegis's anti-money laundering program. The AML Officer may be contacted whenever an employee has questions about Aegis's program, a current or prospective account, or activities or transactions that raise questions about potential money laundering activities. An employee may also provide information anonymously to the AML Officer. The AML Officer is responsible for investigating suspected money laundering activities and taking corrective action when necessary.

2.15.11 Identity Theft

Identity thieves use someone's personal identifying information to open new accounts and misuse existing accounts. The Firm has established an Identity Theft Prevention Program (ITPP) to help detect and prevent identity theft. Many elements of detecting or preventing identity theft are similar to anti-money laundering (AML) requirements that are included in these policies.

The ITPP is based on identifying "red flags" that indicate identity theft may have occurred. *It is the responsibility of all employees to be alert and report to the AML Compliance Officer any new or existing customers who may be engaged in violations of anti-money laundering regulations or identity theft or who have reported identity theft.*

Following is a list of potential identity theft red flags.

Red Flag
Category: Alerts, Notifications or Warnings from a Consumer Credit Reporting Agency
1. A fraud or active duty alert is included on a consumer credit report. An "active duty" alert is an alert a military person may add to his/her credit report to identify potential identity theft.
2. A notice of credit freeze is given in response to a request for a consumer credit report.
3. A notice of address or other discrepancy is provided by a consumer credit reporting agency.
4. A consumer credit report shows a pattern inconsistent with the person's history, such as a big increase in the volume of inquiries or use of credit, especially on new accounts; an unusual number of recently established credit relationships; or an account closed because of an abuse of account privileges.
Category: Suspicious Documents
5. Identification presented looks altered or forged.
6. The identification presenter does not look like the identification's photograph or physical description.
7. Information on the identification differs from what the identification presenter is saying.
8. Information on the identification does not match other information our firm has on file for the presenter, like the original account application, signature card or a recent check.
9. The application looks like it has been altered, forged or torn up and reassembled.
Category: Suspicious Personal Identifying Information
10. Inconsistencies exist between the information presented and other things we know about the presenter or can find out by checking readily available external sources, such as an address that does not match a consumer credit report, or the Social Security Number (SSN) has not been issued or is listed on the Social Security Administration's (SSA's) Death Master File.
11. Inconsistencies exist in the information that the customer gives us, such as a date of birth that does not fall within the number range on the SSA's issuance tables.
12. Personal identifying information presented has been used on an account our firm knows was fraudulent.
13. Personal identifying information presented suggests fraud, such as an address that is fictitious, a mail drop, or a prison; or a phone number is invalid, or is for a pager or answering service.
14. The SSN presented was used by someone else opening an account or other customers.
15. The address or telephone number presented has been used by many other people opening accounts or other customers.
16. A person who omits required information on an application or other form does not provide it when told it is incomplete.
17. Inconsistencies exist between what is presented and what our firm has on file.

18. A person making an account application or seeking access cannot provide authenticating information beyond what would be found in a wallet or consumer credit report, or cannot answer a challenge question.
Category: Suspicious Account Activity
19. Soon after the Firm gets a change of address request for an account, we are asked to add additional access means (such as debit cards or checks) or authorized users for the account.
20. A new account exhibits fraud patterns, such as where a first payment is not made or only the first payment is made, or the use of credit for cash advances and securities easily converted into cash.
21. An account develops new patterns of activity, such as nonpayment inconsistent with prior history, a material increase in credit use, or a material change in spending or electronic fund transfers.
22. An account that is inactive for a long time is suddenly used again.
23. Mail the Firm sends to a customer is returned repeatedly as undeliverable even though the account remains active.
24. We learn that a customer is not getting his or her paper account statements.
25. We are notified that there are unauthorized charges or transactions to the account.
Category: Notice From Other Sources
26. An outside agency, law enforcement, a clearing firm, or other source notifies the Firm that an account has been opened or used fraudulently.
27. The Firm is notified of potential unauthorized access to customer personal information due to data loss from an outside provider or a breach of an outside provider's data.
28. Notice from a customer of the loss of information (e.g., loss of wallet, birth certificate, etc.).

2.16 Emergency Business Recovery Procedures

[FINRA Rule 4370]

Aegis has a *Business Continuity Plan* that assigns responsibilities and outlines procedures in the event of a disaster or emergency which impacts Aegis's ability to continue conducting business (also termed a "significant business disruption"). Examples of a major disruption include a regional power outage; disruption at another company that provides services critical to Aegis's business; and destruction of an office or other facilities by natural causes or by other means. The Plan designates employees who are responsible for employee safety and protection of firm property, records, and customer assets.

In the event of a disruption, employees will be given instructions by authorized personnel. Depending on the nature of the emergency, it may be necessary to use alternative communication systems; transfer personnel and/or business activities to alternative office space; or transfer Aegis's business to other brokerage firms or financial institutions until normal operations can be resumed.

Aegis has established procedures for contacting employees in the event of an emergency. If Aegis conducts a test of its emergency procedures, all employees are required to participate as if the emergency were real. Past emergencies affecting the securities industry have shown that preparedness and cooperation are key to maximizing the safety of employees and minimizing business interruptions. It is important for all employees to follow instructions from senior management and other authorized key personnel during any drill or when an emergency occurs.

Questions regarding Aegis's Business Continuity Plan may be referred to Compliance.

2.17 Prohibited Activities

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
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security and confidentiality of the shared information; that the information will be used only for the authorized purpose; and the identity of a contact person at the institution.

Aegis will share information about those suspected of terrorist financing and money laundering with other financial institutions for the purpose of identifying and reporting activities that may involve terrorist acts or money laundering activities and to determine whether to establish or maintain an account or engage in a transaction. The AML Compliance Officer will file the required certification with FinCEN and re-certify annually. All information will be treated as confidential and will be maintained in the AML Compliance Officer's files which may either be hard-copy files or password-protected electronic files.

In addition, the AML Officer will verify that any financial institution with which Aegis shares information (including affiliates) has itself filed the requisite certification. A written letter or attestation will be required from the other financial institution and maintained in the AML Officer's files or a list provided by FinCEN will be consulted and a record made that the other institution has filed the required certification.

7.11 Suspicious Activity Reports (SARs)

[Bank Secrecy Act 31 CFR Chapter X Part 1023 Subpart B; USA PATRIOT Act Section 356; FINRA Notice to Members 02-47; FinCEN Guidance on Suspicious Activity Report Supporting Documentation: http://www.fincen.gov/Supporting_Documentation_Guidance.pdf; FinCEN Guidance FIN-2008-G005; FinCEN Guidance regarding sharing SAR information with affiliates: http://www.fincen.gov/news_room/nr/html/20101122.html; FinCEN Advisory FIN-2010-A014 Maintaining the Confidentiality of Suspicious Activity Reports: http://www.fincen.gov/statutes_regs/guidance/html/FIN-2010-A014.html]

Responsibility	<ul style="list-style-type: none"> • AML Compliance Officer
Resources	<ul style="list-style-type: none"> • Reports from employees of crimes or suspected crimes • Suspicious activities detected through ongoing reviews • Other available information
Frequency	<ul style="list-style-type: none"> • As required
Action	<ul style="list-style-type: none"> • Review and investigate suspicious transactions referred by employees • Determine whether Aegis (or its clearing firm, if applicable) will file a SAR • If appropriate, file Form SAR-SF with FinCEN and state authorities • Notify senior management, as appropriate, of forms filed • Provide copy to parent company, if applicable • File SARs jointly with other financial institutions, if applicable
Record	<ul style="list-style-type: none"> • Notes and other documented reviews are retained in a suspicious activity file • Copies of SARs filed by Aegis are retained in the SAR file with notation of when and to whom sent

Aegis will file Suspicious Activity Reports (SARs) for transactions that may be indicative of money laundering activity. Suspicious activities include a wide range of questionable activities; examples include trading that constitutes a substantial portion of all trading for the day in a particular security; trading or journaling between/among accounts, particularly between related owners; late day trading; heavy trading in low-priced securities; unexplained wire transfers, including those to known tax havens; unusually large deposits of funds or securities. For business introduced to a clearing firm, Aegis will rely on the clearing firm to make filings on its behalf and to provide copies to Aegis.

7.11.1 Identifying Potential Suspicious Activity

Aegis uses a number of tools to identify potential suspicious activity including:

- Transaction information including disbursement of funds or securities
- Education of Firm personnel, particularly supervisors in Operations areas
- Employee reports of potential suspicious activity forwarded to the AML Compliance Officer
- Information or reports provided by the clearing firm for business introduced to a clearing firm

7.11.2 When A Report Must Be Filed

A SAR must be filed for any transaction that, alone or in aggregate, involves at least \$5,000 in funds or other assets, if Aegis knows, suspects, or has reason to suspect that the transaction (or a pattern of transactions of which the transaction is part) falls into one of the following categories:

- Transactions involving funds derived from illegal activity or intended or conducted to hide or disguise funds or assets derived from illegal activity.
- Transactions designed, whether through structuring or other means, to evade the requirements of the Bank Secrecy Act (BSA).
- Transactions that appear to serve no business or apparent lawful purpose or are not the sort of transactions in which a particular customer would be expected to engage, and for which Aegis knows of no reasonable explanation after examining the available facts.
- Transactions that involve the use of Aegis to facilitate criminal activity.

Excluded from the filing requirement are violations otherwise reported to law enforcement authorities such as:

- a robbery or burglary that is reported to law enforcement authorities
- lost, missing, counterfeit, or stolen securities reported pursuant to 17f-1
- a violation of federal securities laws or SRO rules by Aegis, its officers, directors, employees, or RRs that are reported to the SEC or SRO, except for violations of Rule 17a-8 (filing of Currency and Transaction Reports) which must be reported on a SAR

7.11.3 Filing A Report And Emergency Notification

If Aegis determines to file a SAR with FinCEN, the AML Compliance Officer will file:

- within 30 days of becoming aware of the suspicious transaction; or
- if no suspect has been identified within 30 calendar days of detection, reporting may be delayed an additional 30 calendar days or until a suspect has been identified, but no later than 60 days from date of initial detection.

In situations involving violations that require immediate attention (such as terrorist financing or ongoing money laundering schemes), the AML Compliance Officer will immediately notify by telephone an appropriate law enforcement agency. Suspicious transactions that may relate to terrorist activity may also be reported to FinCEN's Financial Institutions Hotline. In either event, a SAR will be filed.

7.11.3.1 Emergency Notification

[FINRA Notice to Members 02-21]

When conducting due diligence or opening an account, Federal authorities will be notified immediately by the AML Compliance Officer, when necessary, in the following situations:

- A legal or beneficial account holder or person is engaged in a transaction listed on or located in a country or region listed on the OFAC list.

- An account is held by an entity that is owned or controlled by a person or entity listed on the OFAC list.
- A customer tries to use bribery, coercion, or similar means to open an account or carry out a suspicious activity.
- There is reason to believe a customer is trying to move illicit cash out of the government's reach.
- There is reason to believe the customer is about to use funds to further an act of terrorism.

Emergency contacts include:

- OFAC Hotline
- Financial Institutions Hotline
- Local U.S. Attorney's office
- Local FBI office
- Local SEC office

7.11.4 Retention Of Records

The AML Compliance Officer maintains a file of copies of SARs filed with FinCEN and all related documents for a period of 5 years from the filing date.

7.11.5 Providing SARs Information To SROs

[SEC letter to CEOs: <http://www.sec.gov/about/offices/ocie/brokerdealerletter.htm>]

While SARs are to be treated as confidential, the Firm will provide SARs and supporting documentation available to any self-regulatory organization (SRO) that examines the Firm for compliance with the SAR Rule, upon request of the SEC. The request may be part of a routine examination, an investigation, or part of the SRO's risk assessment effort within its examination program.

7.11.6 Prohibition Against Disclosure

By statute and regulation, Aegis may not inform customers or third parties that a transaction has been reported as suspicious. U.S. Treasury and Federal Reserve Board regulations also require Aegis to decline to produce SARs in response to subpoenas and to report to FinCEN and the Federal Reserve Board the receipt of such requests and Aegis's response. Failure to maintain the confidentiality of SARs may subject an employee to civil and criminal penalties under Federal law. Violations may be enforced through civil penalties of up to \$100,000 for each violation and criminal penalties of up to \$250,000 and/or imprisonment not to exceed five years. The Firm may also be liable for civil money penalties resulting from AML deficiencies that led to improper SAR disclosure up to \$25,000 per day for each day the violation continues.

Procedures to protect the confidentiality of SARs include the following:

- Access to SARs is limited to employees on a "need-to-know" basis
- SARs will be maintained in locked physical or electronic files
- SARs may not be left on desks or on open computer files and must be viewed without access by unauthorized persons
- SARs shared with others will be clearly marked "Confidential"

Compliance (or Aegis's counsel) is responsible for responding to subpoena requests and Compliance will notify FinCEN and the Federal Reserve Bank of any subpoenas for SARs.

9.1.3.7 Non-Documentary Methods Of Verifying Customer Identification

Non-documentary methods of verifying customer ID involve other procedures. Non-documentary methods must be used in the following circumstances:

- An individual is unable to present acceptable photo ID
- The documents presented are unfamiliar
- The account is opened without obtaining documents
- The customer opens the account without appearing in person at Aegis
- Other circumstances, at the discretion of the RR's supervisor, New Accounts; and/or the AML Compliance Officer, where Aegis is unable to verify the customer's identity

In these circumstances, a non-documentary method must be indicated by the RR on the new account application:

- Direct customer contact information

9.1.3.8 Additional Verification For Certain Customers

For the following types of customers, a minimum of TWO forms of customer ID are required in addition to review and approval by the AML Compliance Officer prior to opening the account:

- Accounts for foreign public officials (individuals in high office in other countries, their families and close associates, political party officials)

9.1.3.9 Lack Of Customer ID Verification

For customers presenting unacceptable customer ID at the time of account opening, the account will not be opened.

For customers who fail to provide required ID or documents within 30 days of account opening, the account will be restricted to liquidating transactions only until satisfactory ID verification is received.

For accounts where non-documentary verification results in substantive, unresolved discrepancies (information that is inconsistent such as name, address, taxpayer ID number, etc.), either the account will not be opened or will be immediately closed.

Questions regarding accounts that do not comply with requirements to verify customer ID should be referred to the AML Compliance Officer.

9.1.3.10 Customer Notice

Customers are provided notice, prior to opening an account, that their identification will be verified. This notice may be on Aegis's web site, on new account applications, or in other disclosures provided at the time of account opening.

9.1.4 Identity Theft (FACT Act Red Flags Rule)

[Fair and Accurate Credit Transactions Act (FACT Act) Section 114 and 315]

Responsibility	<ul style="list-style-type: none"> • Designated Supervisor
Resources	<ul style="list-style-type: none"> • New account information

	<ul style="list-style-type: none"> • Order and transactions records (including transfers of funds/securities) • Available reports
Frequency	<ul style="list-style-type: none"> • Daily and ongoing
Action	<ul style="list-style-type: none"> • Identify "red flags" when reviewing new accounts, orders, and transactions • If red flags are identified, contact the AML Compliance Officer to consult regarding further action • Include identity theft in training
Record	<ul style="list-style-type: none"> • New account records • Order and transactions records • Referral of red flags to Compliance and notation of action taken • Records of training including when conducted, subject matter, and who attended

Identity thieves use someone's personal identifying information to open new accounts and misuse existing accounts. The Firm has established an Identity Theft Prevention Program (ITPP) to help detect and prevent identity theft. Many elements of detecting or preventing identity theft are similar to anti-money laundering (AML) requirements that are included in these policies. A more detailed explanation of the Program is included in the section *Identity Theft Prevention Program (FACT Act Red Flags Rule)* in the chapter *ANTI-MONEY LAUNDERING (AML) PROGRAM*.

The ITPP is based on identifying "red flags" that indicate identity theft may have occurred. *It is the responsibility of all employees to be alert and report to the AML Compliance Officer any new or existing customers who may be engaged in violations of anti-money laundering regulations or identity theft or who have reported identity theft.*

9.1.4.1 Red Flags

The following two tables include "red flags" that are possible indicators of identity theft or money laundering.

Red Flags indicating potential Identity Theft	
Category: Alerts, Notifications or Warnings from a Consumer Credit Reporting Agency	
1.	A fraud or active duty alert is included on a consumer credit report. An "active duty" alert is an alert a military person may add to his/her credit report to identify potential identity theft.
2.	A notice of credit freeze is given in response to a request for a consumer credit report.
3.	A notice of address or other discrepancy is provided by a consumer credit reporting agency.
4.	A consumer credit report shows a pattern inconsistent with the person's history, such as a big increase in the volume of inquiries or use of credit, especially on new accounts; an unusual number of recently established credit relationships; or an account closed because of an abuse of account privileges.
Category: Suspicious Documents	
5.	Identification presented looks altered or forged.
6.	The identification presenter does not look like the identification's photograph or physical description.
7.	Information on the identification differs from what the identification presenter is saying.
8.	Information on the identification does not match other information our firm has on file for the presenter, like the original account application, signature card or a recent check.

9. The application looks like it has been altered, forged or torn up and reassembled.
Category: Suspicious Personal Identifying Information
10. Inconsistencies exist between the information presented and other things we know about the presenter or can find out by checking readily available external sources, such as an address that does not match a consumer credit report, or the Social Security Number (SSN) has not been issued or is listed on the Social Security Administration's (SSA's) Death Master File.
11. Inconsistencies exist in the information that the customer gives us, such as a date of birth that does not fall within the number range on the SSA's issuance tables.
12. Personal identifying information presented has been used on an account our firm knows was fraudulent.
13. Personal identifying information presented suggests fraud, such as an address that is fictitious, a mail drop, or a prison; or a phone number is invalid, or is for a pager or answering service.
14. The SSN presented was used by someone else opening an account or other customers.
15. The address or telephone number presented has been used by many other people opening accounts or other customers.
16. A person who omits required information on an application or other form does not provide it when told it is incomplete.
17. Inconsistencies exist between what is presented and what our firm has on file.
18. A person making an account application or seeking access cannot provide authenticating information beyond what would be found in a wallet or consumer credit report, or cannot answer a challenge question.
Category: Suspicious Account Activity
19. Soon after the Firm gets a change of address request for an account, we are asked to add additional access means (such as debit cards or checks) or authorized users for the account.
20. A new account exhibits fraud patterns, such as where a first payment is not made or only the first payment is made, or the use of credit for cash advances and securities easily converted into cash.
21. An account develops new patterns of activity, such as nonpayment inconsistent with prior history, a material increase in credit use, or a material change in spending or electronic fund transfers.
22. An account that is inactive for a long time is suddenly used again.
23. Mail the Firm sends to a customer is returned repeatedly as undeliverable even though the account remains active.
24. We learn that a customer is not getting his or her paper account statements.
25. We are notified that there are unauthorized charges or transactions to the account.
Category: Notice From Other Sources
26. An outside agency, law enforcement, a clearing firm, or other source notifies the Firm that an account has been opened or used fraudulently.
27. The Firm is notified of potential unauthorized access to customer personal information due to data loss from an outside provider or a breach of an outside provider's data.
28. Notice from a customer of the loss of information (e.g., loss of wallet, birth certificate, etc.).

Red Flags indicating potential Money Laundering
The customer exhibits unusual concern regarding the Firm's compliance with government reporting requirements and the Firm's AML policies, particularly with respect to his or her identity, type of business and assets, or is reluctant or refuses to reveal any information concerning business activities, or furnishes unusual or suspect identification or business documents.
The customer wishes to engage in transactions that lack business sense or apparent investment strategy, or are inconsistent with the customer's stated business strategy.

The information provided by the customer that identifies a legitimate source for funds is false, misleading, or substantially incorrect.
Upon request, the customer refuses to identify or fails to indicate any legitimate source for his or her funds and other assets.
The customer (or a person publicly associated with the customer) has a questionable background or is the subject of news reports indicating possible criminal, civil, or regulatory violations.
The customer exhibits a lack of concern regarding risks, commissions, or other transaction costs.
The customer appears to be acting as an agent for an undisclosed principal, but declines or is reluctant, without legitimate commercial reasons, to provide information or is otherwise evasive regarding that person or entity.
The customer has difficulty describing the nature of his or her business or lacks general knowledge of his or her industry.
The customer attempts to make frequent or large deposits of currency, insists on dealing only in cash equivalents, or asks for exemptions from the Firm's policies relating to the deposit of cash and cash equivalents.
The customer engages in transactions involving cash or cash equivalents or other monetary instruments that appear to be structured to avoid the \$10,000 government reporting requirements, especially if the cash or monetary instruments are in an amount just below reporting or recording thresholds.
For no apparent reason, the customer has multiple accounts under a single name or multiple names, with a large number of inter-account or third-party transfers.
The customer is from, or has accounts in, a country identified as a non-cooperative country or territory by the Financial Action Task Force (FATF).
The customer's account has unexplained or sudden extensive wire activity, especially in accounts that had little or no previous activity.
The customer's account shows numerous currency or cashiers check transactions aggregating to significant sums.
The customer's account has a large number of wire transfers to unrelated third parties inconsistent with the customer's legitimate business purpose.
The customer's account has wire transfers that have no apparent business purpose to or from a country identified as a money laundering risk or a bank secrecy haven
The customer's account indicates large or frequent wire transfers, immediately withdrawn by check or debit card without any apparent business purpose.
The customer makes a funds deposit followed by an immediate request that the money be wired out or transferred to a third party, or to another firm, without any apparent business purpose.
The customer makes a funds deposit for the purpose of purchasing a long-term investment followed shortly thereafter by a request to liquidate the position and transfer of the proceeds out of the account.
The customer engages in excessive journal entries between unrelated accounts without any apparent business purpose.
The customer requests that a transaction be processed in such a manner to avoid the Firm's normal documentation requirements.
The customer, for no apparent reason or in conjunction with other "red flags," engages in transactions involving certain types of securities, such as penny stocks, Regulation "S" (Reg S) stocks, and bearer bonds, which although legitimate, have been used in connection with fraudulent schemes and money laundering activity. (Such transactions may warrant further due diligence to ensure the legitimacy of the customer's activity.)
The customer's account shows an unexplained high level of account activity with very low levels of securities transactions.
The customer maintains multiple accounts, or maintains accounts in the names of family members or

Other Notes:

- **Non-affiliate:** to qualify as a non-affiliate, must not have been an affiliate of the issuer for at least 3 months prior to the sale.
- Various staff positions also apply regarding tacking of the holding period; sales by a pledgee; and other staff opinions.
- Rule 144 is not available to sellers of a shell company's securities whether the company is reporting or non-reporting.

10.34.4 New Account Information Regarding Affiliates

Aegis's new account form includes an inquiry whether the customer is an affiliate of an issuer. RRs are responsible for obtaining this information and, if the customer is an affiliate and places an order to sell shares of the issuer, contacting Compliance for instructions on executing the order under Rule 144.

10.34.5 Lending And Option Writing On Control And Restricted Securities

The lending of money, extension of loan value, or use as collateral of restricted securities are subject to specific limitations. Compliance should be contacted prior to any such arrangement.

Covered listed options may be written on underlying control or restricted stock if the stock is saleable when the option is written. Compliance should be contacted to determine the salability of the underlying securities prior to writing covered options.

10.35 Unregistered Resales Of Restricted Securities

[FINRA Regulatory Notice 09-05]

Responsibility	<ul style="list-style-type: none">• Designated Supervisor• Operations personnel
Resources	<ul style="list-style-type: none">• New accounts at opening• Proposed sales of potentially unregistered securities• Order records or transaction reports• Physical certificates
Frequency	<ul style="list-style-type: none">• When new accounts are opened with a potentially questionable transaction• As required - assist RR in evaluating a potential sale• Daily - review of order records/transaction reports• As required - review certificates
Action	<ul style="list-style-type: none">• Review for "red flags" listed in this section• If a red flag is identified, contact the RR for more information about the customer and the block being sold; contact the customer if necessary to confirm the securities are not unregistered or restricted• Operations personnel should refer questionable certificates to the designated supervisor for follow up with the RR or customer
Record	<ul style="list-style-type: none">• Order records/transaction reports• New account records• Records of certificates received• Designated supervisor's record of action taken, if applicable, in a log, on the order

	record, in a daytimer, or in another record
--	---

Broker-dealers are prohibited from selling unregistered securities unless the sale falls within an available exemption such as Rule 144 sales discussed in the prior section. Avoiding such sales is based on knowing the customer and the securities to be sold. The RR should be aware of "red flags" that may indicate a customer is selling unregistered securities, including the following examples:

- A customer opens a new account and delivers physical certificates representing a large block of thinly-traded or low-priced securities.
- A customer has a pattern of depositing physical share certificates, immediately selling the shares and then wiring out the proceeds of the resale.
- A customer deposits share certificates that are recently issued or represent a large percentage of the float for the security.
- Share certificates reference a company or customer name that has been changed or that does not match the name on the account.
- The lack of a restrictive legend on deposited shares seems inconsistent with the date the customer acquired the securities or the nature of the transaction in which the securities were acquired.
- There is a sudden spike in investor demand for, coupled with a rising price in, a thinly-traded or low-priced security.
- The company was a shell company when it issued the shares.
- A customer with limited or no other assets under management at Aegis receives an electronic transfer or journal transactions of large amounts of low-priced, unlisted securities.
- The issuer has been through several recent name changes, business combinations or recapitalizations, or the company's officers are also officers of numerous similar companies.
- The issuer's SEC filings are not current, are incomplete, or nonexistent.

When confronted with a customer wanting to sell a block of stock where there may be a question about the registered status of the stock, the client will be required to complete a questionnaire. The questionnaire will be required to be reviewed and approved by compliance before the stock certificate is deposited. Supporting documentation as to how the shares were received will be requested from the client before it is approved. The following is the questionnaire that the client will be required to fill out before depositing stock into his account;

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 PENSON FINANCIAL SERVICES, INC
 AND/OR BROKER DEALERS
 FOR WHICH IT CLEARS
 DEPOSIT SECURITIES REQUEST
 FOR BULLETIN BOARD, PINK SHEET AND UNREGISTERED SECURITIES
 Indicate Type: Physical Certificate Deposit DWAC/DRS Transfer from Issuer Other Transfer

NOTE: This form must be filled in completely. Failure to complete each line will result in a rejection of the form and/or the certificate. If non-applicable, please enter N/A where needed.

Security Owner Name:
 Account #:
 Shareholder Address:
 Occupation:
 Security Description
 Issuer/Company Name:
 Issuer Address:
 Issuer Phone:
 State of Registration:
 Where are shares traded?
 Certificate No.:
 Ticker Symbol:

No. of Shares:

CUSIP:

Total Shares Outstanding:(most recent public filing)

Approx Value: \$

Total Shares Outstanding: (per Transfer Agent)

Most current trading price:

Date:

Fully reporting: Yes No

Current Filer: Yes No

Security Owner Questionnaire

1

Security Deposit Reason (e.g. safekeeping; resale):

2

How long a client of this correspondent?

3

Has the client or any affiliated accounts deposited shares of this issue within the last 90 days? If yes, please explain:

4

Does the client intend to deposit more shares in the future?

5

If yes to #4, how many?

6

Date Security was Acquired:

7

Were shares acquired thru purchase, as payment for services/compensation, stock offering, employment agreement, debt agreement, or Note/Debt conversion?

Yes No

8

If yes to #7, attach verification.

Verification should include, when applicable, copies of private placement memorandum, offering agreement, certain employee compensation documentation, debt agreement, convertible notes, or employee agreement.

Documentation will be needed to justify question above.

Attached: Yes No

List document attached:

9

Security acquired from (the "Prior Owner")?

Yes No

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10

If Prior Owner and Issuer are not the same, indicate Prior Owner's purchase date, seller's name, and amount/manner of payment:

11

Was the prior owner an officer, director, affiliate, control or 10% holder of the securities at the time, or within 90 days of Owner's receipt of the security?

Yes No

12

If answered yes to #11, please explain.

13

Is client currently selling shares thru any other broker dealer?

Yes No

14

How many shares of the Issuer are owned or controlled, directly or indirectly, by you?

15

How many shares, if any, have been sold by you?

16

How many shares have been issued to, or transferred to, the shareholder within the last year?

17

Is the Security restricted from resale for any reason? If so, what is the basis for the restriction? When does the

restriction end?

Yes No

18

If restricted, may the shares be sold with prospectus before the end of the restrictive period? If so, how soon?

Yes No

19

Was the Security covered by a current registration statement when acquired? If yes, explain, including type of registration e.g. S-1, Form 20, etc.

List type of and date of relevant SEC filing

Yes No

20

Was the Security exempt from SEC registration when you acquired it? If yes, describe exemption relied upon.

Yes No

21

If a non-SEC reporting company, please list Officers and Affiliates.

22

Has the Issuer been through a recent name change? If so, what was (or were) previous name(s)?

Yes No

23

Was Issuer a shell company when shares issued? If so, are the corporate headquarters located in the same state that the shares were issued? In which state were shares issued?

Yes No

24

Are you, or have you been, an officer, director, affiliate, control person or 5% owner of the Issuer? If yes, provide position and dates of duties held.

Yes No

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25

Is client, or any family member, a present or past officer, director, employee, control person, insider or large shareholder (10% or greater)?

Yes No

26

If yes to #25, please explain.

27

Percent of total outstanding shares the shareholder holds?

28

Have you made any payment to any other person in connection with the sale of the security? (e.g. commission)

29

Have you made any arrangements for buy orders in connection with the sale of the security?

30

Are there any stops or restrictions on shares?

Yes No

31

If yes, type of stop or restriction:

32

If restricted, what safe – harbor is being used to resell shares?

33

If Free-trading, are the shares registered?

Yes No

34

If Registered, type of registration (S-1, S-8 etc)

35

Is the registration statement effective?

Yes No

36

List type of and date of relevant SEC filing

37

If not Registered, what safe harbor or exemption was used to create free trading shares or resell shares?

38

Other information regarding security deposit that you would like to provide:

The undersigned hereby represents that the information provided above is true and correct. The undersigned understands that Penson Financial Services, Inc. will be relying on such information in determining whether to accept orders for the sale of the undersigned's securities. As condition to Penson Financial Services, Inc.'s acceptance of any sale, the undersigned hereby agrees to the Terms and Conditions attached hereto:

(Name/Title of Entity) (Security Owner Signature) (Date)

Transfer Agent Verification: (For Broker Use Only)

Transfer Agent:

Address:

Contact Person:

Telephone:

Date Verified:

By:

Is this Issue DTC eligible? If not, are you submitting a request to make eligible?

Notes:

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Broker Approval:

The undersigned Registered Representative, Register Principal, and CCO have carefully reviewed this Deposited Securities Request and the appropriate supporting documents. Each represents to Penson Financial Services, Inc. that to his/her best knowledge the information is true and correct and is made in compliance with all applicable federal and state securities laws and regulations.

Name of Introducing Broker Contact Phone #

(Representative Name) (Representative Signature) (Date)

(Principal Name, other than CCO) (Principal Signature) (Date)

(CCO Name) (CCO Signature) (Date)

TERMS AND CONDITIONS

In consideration of Penson Financial Services, Inc. (PFSI) accepting this Deposited Securities Checklist, the Security Owner understands and agrees to each of the following:

1. The Security Owner agrees to keep the foregoing Questionnaire information up to date and current with PFSI as long as the Security shares are being sold.
2. The Security Owner agrees to indemnify and hold PFSI harmless from and against any and all claims, damages, liabilities and expenses which PFSI incurs as a result of or in connection with any inaccuracy or omission in the Security Owner's responses to the Questionnaire.
3. To cooperate with any internal or external audit or regulatory inquiry relating to this Deposited Securities Checklist by providing any information or documentation reasonably requested by PFSI to support the information provided in the Questionnaire and any Security sale executed in accordance with the Securities Laws (as defined below). This obligation to cooperate will remain in effect before and after the completion of the transfer of the assets.
4. The acceptance of any sale of the related securities are expressly subject to the Security Owner's strict adherence to all applicable federal securities laws, including, without limitation, those described below (the "Securities Laws"):

Selling Unregistered Securities: Federal securities law make it unlawful for a person to make use of any means or instrument of interstate commerce or of the mails to sell a security which has not been registered, or to deliver through the mail a security which has not been registered. Accordingly, unless a person can apply an exemption to its sales of securities, all securities sold are required to be registered pursuant to Section 5 of the Securities Act of 1933 (the "1933 Act").

Securities Fraud: Federal securities law make it unlawful for any person to offer or sell securities by the use of any means of interstate communication or transportation, including the mails, in order to employ a scheme to defraud, to obtain money by omitting material information, or to engage in a course of business that would operate as a fraud on the purchaser.

Insider Trading: Federal securities law prohibits insider trading, which generally refers to buying or selling a security, in breach of a fiduciary duty or other relationship of trust and confidence, while in possession of material, nonpublic information about the security. Insider trading violations may also include "tipping" such information, securities trading by the person "tipped", and securities trading by those who misappropriate such information.

5 of 5

Market Manipulation:

Pools – Agreements, often written, among a group of traders to delegate authority to a single manager to trade in a specific stock for a specific period of time and then to share in the resulting profits or losses. Market manipulation describes a deliberate attempt to interfere with the free and fair operation of the market and create artificial, false or misleading appearances with respect to the price of, or market for, a security, commodity or currency. Market manipulation is prohibited under federal securities law. Market manipulation can occur in multiple ways, including:

Churning – Placing both buy and sell orders at about the same price. The increase in activity is intended to attract additional investors, and increase the price.

Runs – Creating activity or rumors in order to drive the price of a security up. This activity is usually referred to as "Painting the Tape."

Ramping (the market) – Actions designed to artificially raise the market price of listed securities and to give the impression of voluminous trading, in order to make a quick profit.

Wash sale – Selling and repurchasing the same or substantially the same security for the purpose of generating activity and increasing the price.

Bear raid – Attempting to push the price of a stock down by heavy selling or short selling.

Anti-Money Laundering: The Bank Secrecy Act (BSA), and its implementing regulations, is a tool the U.S. government uses to fight drug trafficking, money laundering, and other crimes. Congress enacted the BSA to prevent banks and other financial service providers from being used as intermediaries for, or to hide the transfer or deposit of money derived from, criminal activity. Federal law makes money laundering a criminal act. Money laundering is the criminal practice of filtering ill-gotten gains or "dirty" money through a maze or series of transactions, so the funds are "cleaned" to look like proceeds from legal activities.

Revised 5/2010

10.36 Reporting Of Insider Transactions

[SEC Securities Exchange Act of 1934 Section 16(a); SEC Exchange Act Section 16 and Related rules & Forms (Q & A): <http://www.sec.gov/divisions/corpfin/guidance/sec16interp.htm>]

Under Section 16(a) of the Exchange Act, directors, officers, and >10% holders of equity securities of a publicly-traded company are required to report their purchases and sales of the issuer's securities to the SEC (and, if the security is listed on a national exchange, with the exchange where listed) as follows:

- at the time the security is registered on a national securities exchange or by the effective date of the registration statement
- within 10 days of becoming a 10% beneficial owner, director or officer
- by the end of the second business day following a purchase or sale transaction

Alternate reporting period requirements apply to two categories of transactions in which the insider does not control and may not be able to predict when the transaction will occur:

- Transactions pursuant to a contract, instruction or written plan
- Discretionary transactions pursuant to employee benefit plans such as fund switching transactions

In these instances, the date the executing broker-dealer or plan administrator notifies the insider of the transaction is deemed the date of execution for reporting purposes, as long as the notification is not later than

Exhibit 2

Unregistered Resales of Restricted Securities

FINRA Reminds Firms of Their Obligations to Determine Whether Securities are Eligible for Public Sale

Executive Summary

FINRA reminds firms¹ of their responsibilities to ensure that they comply with the federal securities laws and FINRA rules when participating in unregistered resales of restricted securities. These responsibilities are particularly important in situations where the surrounding circumstances place the firm on notice that it may be participating in illegal, unregistered resales of restricted securities, such as when a customer physically deposits certificates or transfers in large blocks of securities and the firm does not know the source of the securities.

Recent FINRA investigations have revealed instances in which firms failed to recognize certain "red flags" that signaled the possibility of an illegal, unregistered distribution. This *Notice* identifies situations in which firms should conduct a searching inquiry to comply with their regulatory obligations under the federal securities laws and FINRA rules. FINRA also has reviewed procedures provided by a number of large, medium and small firms that are designed to address compliance. This *Notice* describes and discusses those procedures.

Questions concerning this *Notice* should be directed to:

- Gary L. Goldsholle, Vice President and Associate General Counsel, Office of the General Counsel, at (202) 728-8104;
- Joseph E. Price, Vice President, Corporate Financing, at (240) 386-4623; or
- Lisa Jones Toms, Counsel, Corporate Financing, at (240) 386-4661.

January 2009

Notice Type

- Guidance

Suggested Routing

- Compliance
- Registered Representatives
- Trading
- Training

Key Topic(s)

- Unregistered Resale of Restricted Securities
- Unregistered Distributions

Referenced Rules & Notices

- NASD Rule 2710
- NASD Rule 2720
- NASD Rule 2810
- NASD Rule 3010
- SEC Rule 144
- Section 4(1) of the Securities Act
- Section 4(2) of the Securities Act
- Section 4(4) of the Securities Act



Background & Discussion

Firms play a critical role in helping prevent illegal, unregistered resales of restricted securities into the public markets. It is a violation of the federal securities laws for a firm to offer or sell a security without an effective registration statement or an applicable exemption from the Securities Act of 1933 (Securities Act). In addition, such sales may violate NASD Rules 2710 (Corporate Financing Rule – Underwriting Terms and Arrangements)², 2720 (Distribution of Securities and Affiliates – Conflicts of Interest) and 2810 (Direct Participation Programs).³

All firms must have procedures reasonably designed to avoid becoming participants in the potential unregistered distribution of securities. The nature of those procedures and the required level of firm inquiry concerning the customer and the source of the securities will depend on the particular circumstances. In addition, firms may not rely solely on others, such as clearing firms, transfer agents, or issuers' counsel, to fulfill these obligations. Firms' specific obligations are discussed in more detail below.

The Securities Act prohibits the sale of securities unless the sale is made pursuant to an effective registration statement, or falls within an available exemption from registration. Before selling securities in reliance on an exemption, a firm must take reasonable steps to ensure that the transaction qualifies for the exemption, regardless of whether the sale is for its own accounts or on behalf of customers. This includes taking whatever steps necessary to ensure that the sale does not involve an issuer, a person in a control relationship with an issuer, or an underwriter with a view to offer or sell the securities in connection with an unregistered distribution.⁴

Section 4(1) of the Securities Act provides an exemption for the routine trading of already-issued securities. It does not, however, exempt sales by an issuer, or a control person of the issuer, or an underwriter or dealer. Section 4(2) of the Securities Act exempts sales made by an issuer not involving a public offering. Whether a sale is one that involves a public offering, however, is a question of fact which requires an inquiry regarding the surrounding circumstances, including such factors as the relationship between the seller and the issuer, and the nature, scope, size, type and manner of the offering. Section 4(4) of the Securities Act provides an exemption for unsolicited brokers' transactions. However, this exemption is available only if a broker is not aware, after a reasonable inquiry, of circumstances indicating that the selling customer is participating in a distribution of securities.

Recently, FINRA has investigated and brought several enforcement actions concerning unregistered distributions.⁵ A common theme in these cases was that firms resold large amounts of low-priced equity securities in over-the-counter transactions. Among the allegations in these cases are that the inquiries necessary to uncover the facts of the unregistered distribution were not done or were inadequate, and the firms lacked proper supervisory controls to ensure that their written procedures were being followed. More specifically, in some instances, firms failed to take steps to determine when or how their customers had received the share certificates at issue, whether their customers were control persons of the issuers, or what percentage of the outstanding shares of these companies their customers owned. In some instances, physical certificates for shares were repeatedly deposited into accounts and then sold by firms that participated in unregistered distributions.

Red Flags and the Duty to Make an Inquiry

Firms typically serve as the channel of distribution through which issuers, affiliates and promoters can access the public securities markets. Firms that do not adequately supervise or manage their role in such distributions run the risk of participating in an illegal, unregistered distribution. As recent investigations have shown, problems can arise when firms fail to recognize or take appropriate steps when confronted with "red flags" that signal the possibility of an illegal, unregistered distribution.

The following are examples of red flags (these are by no means comprehensive and should not be considered a "roadmap" for compliance purposes):

- ▶ A customer opens a new account and delivers physical certificates representing a large block of thinly traded or low-priced securities;
- ▶ A customer has a pattern of depositing physical share certificates, immediately selling the shares and then wiring out the proceeds of the resale;
- ▶ A customer deposits share certificates that are recently issued or represent a large percentage of the float for the security;
- ▶ Share certificates reference a company or customer name that has been changed or that does not match the name on the account;
- ▶ The lack of a restrictive legend on deposited shares seems inconsistent with the date the customer acquired the securities or the nature of the transaction in which the securities were acquired;
- ▶ There is a sudden spike in investor demand for, coupled with a rising price in, a thinly traded or low-priced security;
- ▶ The company was a shell company when it issued the shares;

- A customer with limited or no other assets under management at the firm receives an electronic transfer or journal transactions of large amounts of low-priced, unlisted securities;
- The issuer has been through several recent name changes, business combinations or recapitalizations, or the company's officers are also officers of numerous similar companies;
- The issuer's SEC filings are not current, are incomplete, or nonexistent.

As noted above, these examples are merely illustrative. There are many other situations that may signal that a firm should take a closer look at the circumstances of a proposed resale transaction.

Regarding the duty of firms to determine whether restricted securities are eligible for public sale, the SEC has said that:

[A] dealer who offers to sell, or is asked to sell a substantial amount of securities must take whatever steps are necessary to be sure that this is a transaction not involving an issuer, person in a control relationship with an issuer or an underwriter. For this purpose, it is not sufficient for him merely to accept "self-serving statements of his sellers and their counsel without reasonably exploring the possibility of contrary facts." (footnote omitted)

The amount of inquiry called for necessarily varies with the circumstances of particular cases. A dealer who is offered a modest amount of a widely traded security by a responsible customer, whose lack of relationship to the issuer is well known to him, may ordinarily proceed with considerable confidence. On the other hand, when a dealer is offered a substantial block of a little-known security, either by persons who appear reluctant to disclose exactly where the securities came from, or where the surrounding circumstances raise a question as to whether or not the ostensible sellers may be merely intermediaries for controlling persons or statutory underwriters, then searching inquiry is called for.

The problem becomes particularly acute where substantial amounts of a previously little known security appear in the trading markets within a fairly short period of time and without the benefit of registration under the Securities Act of 1933. In such situations, it must be assumed that these securities emanate from the issuer or from persons controlling the issuer, unless some other source is known and the fact that the certificates may be registered in the names of various individuals could merely indicate that those responsible for the distribution are attempting to cover their tracks.⁶

Inquiry Obligations under Securities Act Rule 144

A firm that distributes securities for its own account or on behalf of a customer may be considered a statutory underwriter. Securities Act Rule 144 establishes a non-exclusive “safe harbor” from being deemed an underwriter if the securities are sold in compliance with its requirements. Unregistered securities that are not freely transferable are considered “restricted securities” when they are acquired in a private transaction or are acquired by a control person of the issuer.⁷

The SEC recently revised Rule 144 and made substantial changes to the requirements governing resales of restricted securities.⁸ The amendments, which became effective on February 15, 2008, continue to impose a one-year holding period prior to any public resale on restricted securities of companies that are not subject to the Exchange Act reporting requirements. The amendments eliminated the sales volume and manner of sale limitations on resales made by non-affiliates. Revised Rule 144 also includes more stringent restrictions on the resale of shares issued by shell companies. Accordingly, firms should review whether the company that issued the subject shares was a shell company when the shares were issued.

Before reselling restricted securities, firms must take reasonable steps to ensure that the transaction complies with Rule 144 or another available exemption. The factors set forth in the Notes to Rule 144(g) serve as a pragmatic guideline in determining what questions firms should ask their customers before engaging in an unregistered resale of securities:⁹

- How long has the customer held the security?
- How did the customer acquire the securities?
- Does the customer intend to sell additional shares of the same class of securities through other means?
- Has the customer solicited or made any arrangement for the solicitation of buy orders in connection with the proposed resale of unregistered securities?
- Has the customer made any payment to any other person in connection with the proposed resale of the securities? and
- How many shares or other units of the class are outstanding, and what is the relevant trading volume?

Firms should also try to physically inspect share certificates, if possible, as an opportunity to identify red flags and deter risks from forgery and fraudulent certificates.

Supervisory Procedures and Controls for Unregistered Resales of Securities

NASD Rule 3010 (Supervision) requires a firm to establish a supervisory system and corresponding written procedures to supervise its businesses and associated persons' activities. Accordingly, firms that accept delivery of large quantities of low-priced OTC securities, in either certificate form or by electronic transfer, and effect sales in these securities, should have written procedures and controls in place to prevent participation in an illegal, unregistered distribution of securities.

To help firms evaluate their procedures for supervising these resale transactions, FINRA has reviewed the procedures of a number of large, medium and small firms. The procedures noted below are not intended to be a comprehensive roadmap for compliance and supervision with respect to unregistered resales of restricted securities, but rather highlight measures that some firms are using to ensure better compliance with their obligations. While a particular practice may work well for one firm, the same approach may not be effective or economically feasible for another. Firms must adopt procedures and controls that are effective given their size, structure and operations.

The procedures we surveyed varied depending on the firms' business models; nevertheless, the most comprehensive ones tended to include a mandatory, standardized process that requires formal approval of the proposed resale transaction and thorough accompanying documentation that:

- Clearly communicates each step in the review, approval and post-approval process through the various stages of background inquiry, information gathering, required documentation, review, final approval, execution and recordkeeping of the transaction;
- Assigns clear "ownership" of each step of the transaction review, approval and execution process to the responsible representative, principal, legal or compliance specialist, business unit or department; and
- Is easily accessible to the personnel involved in the process, often through internal Web-based applications that are clear, instructive and encourage process standardization.

Standardized procedures should be accompanied by supervisory controls to ensure that a reasonable and meaningful investigation of the surrounding circumstances is conducted and that the information obtained is evaluated to identify whether a proposed resale transaction could amount to an illegal, unregistered distribution of a restricted security on behalf of an underwriter, an issuer, or a control person of the issuer. As a general matter, the procedures and controls should apply to not only proposed resales, but also the transfer of securities from one account to another by journal or book entry.

Among the compliance procedures FINRA reviewed are:

A. Initial Assessment and Review

A number of firms had procedures that required a comprehensive initial review of the proposed resale, which includes gathering information concerning how, when, and under what circumstances a customer obtained the securities; whether the securities are registered pursuant to an effective Securities Act registration statement; how much of the stock is owned by or under the control of the customer; whether the stock was paid for by the customer; what relationship, if any, the customer has with the issuer or its control persons; and how much stock has been sold by the customer. Some procedures also contained brief descriptions of how holders of unregistered securities may acquire them, such as via private placements, corporate reorganizations, business combinations and stock options plans, and explained that the requirements for resales of such securities can vary depending on the nature of the transaction and the status of the seller, *i.e.*, whether the seller is considered an affiliate of the issuer.

Some firms prohibited their representatives from accepting large blocks of securities in certificate form or required supervisory approval before a transfer of restricted securities would be accepted.

Many firms required the results of the initial review to be documented and held the persons performing the review accountable for completion of the fact-gathering and documentation process. As part of this process, firm procedures required the use of questionnaires completed by the selling customer regarding the proposed resale transaction, form letters completed by the customer and registered representative, and other standardized documentation depending on the transaction.

Some firms deferred the documentation requirements to the person or department responsible for approval. Most firms required the completed documentation to be reviewed for any unusual circumstances and for completeness before submitting it for formal approval of the transaction. This assessment may also alert the firm to unusual or suspicious circumstances that may trigger other compliance procedures (such as Anti-Money Laundering (AML) reporting) or additional approvals given the size or nature of the transaction.

B. Formal Review and Approval

Most of the procedures we reviewed required formal approval by a person, unit or department that is independent of the initial assessment and review of the proposed resale transaction. The person or department responsible for such approval was required to document the steps taken and was accountable for the final approval. For many firms, the final approval process is more than a verification of the adequacy of the documentation. It included an investigation of the customer's and issuer's background; a formal process to confirm the seller's affiliation status and the conditions upon which the shares can be resold; verification that the issuer is current in its filings and the issuer's information is publicly available; and a thorough review of the opinion of counsel, restricted stock legend, offering materials or prospectus, and other documents for reasonableness of the information and representations. It also took into account any previous sales by the customer through any accounts at the firm. Approval from a designated principal or legal and compliance specialist generally is required in these instances *before* executing or submitting the trade for execution. The approval document also specifies whether there are any conditions to the resale, such as volume, manner of sale or other applicable requirements.

C. Recordkeeping Obligations and Post-Approval Review

Because of the manner of sale and other requirements that apply to unregistered resales of restricted securities by affiliates, some firms' procedures included steps to monitor executions of approved transactions to ensure they comply with applicable volume or manner of sale requirements. Other firms have a process in place, post-approval of the resale transaction, to examine repeated resales by the same account or accounts under common control and to review and monitor aggregated resales in the same securities.

Some procedures we reviewed did not assign specific recordkeeping obligations. Other procedures designated a registered representative at the firm as the person responsible for retaining all documents related to the resale as opposed to having another entity such as the firm's legal or compliance group or securities transfer unit designated as primarily responsible for document retention or, at least, to receive and retain copies of the documentation related to the resale.

Other Considerations

A. Reliance on Third Parties

In considering their obligations, firms should be aware that there are limitations on their ability to discharge those obligations by relying on others. FINRA, the SEC and the courts have repeatedly held that firms cannot rely on outside counsel, clearing firms, transfer agents, issuers, or issuer's counsel to discharge their obligations to undertake an inquiry. Moreover, the fact that securities have been issued by a transfer agent without a restrictive legend, or have been put into trading status by a clearing firm, does not mean that those securities can be resold immediately and without limitation under the Securities Act.¹⁰

B. AML Compliance

A firm must also ensure that its AML compliance program adequately addresses red flags that may be associated with unregistered resales conducted through the firm.¹¹ In recent investigations, FINRA has found that firms that participated in unregistered resales of restricted securities also may have ignored a number of red flags that indicate not only that the resale was part of an unregistered distribution, but also that action may have been required under AML reporting requirements.¹² Failure to conduct appropriate inquiry and respond to red flags may have consequences under both the federal securities laws and AML requirements.

Conclusion

Firms must have written procedures that are reasonably designed to avoid becoming participants in the illegal, unregistered resale of restricted securities into the public markets. As noted above, these procedures and the required level of firm inquiry depend on the facts and circumstances of the proposed resale. FINRA urges firms to pay careful attention to these obligations and the implementation of these procedures.

Endnotes

- 1 This Notice refers to broker-dealers and their associated persons collectively as "firms" unless otherwise specified.
- 2 NASD Rule 2710 is being re-designated as FINRA Rule 5110. See SR-FINRA-2008-039.
- 3 See, e.g., FINRA's Corporate Financing Rules (NASD Rules 2710, 2720 and 2810), which apply to public offerings, and NASD Rule 2110, which requires firms to act under just and equitable principles of trade. Regulation M under the Exchange Act and other FINRA and SEC rules may also apply to an unregistered public distribution in addition to civil liabilities under the Securities Act.
- 4 The term "underwriter" is broadly defined in the Securities Act to include any person or entity that purchases securities from an issuer with a view to distribute, or offers or sells for an issuer in connection with a distribution, and any person or entity participating, directly or indirectly, in a distribution of securities. The term "issuer" includes any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer. See Sec. 2(a)(11), Securities Act of 1933. Whether a customer is acting as an underwriter, is a control person, or is acting on behalf of an underwriter or control person, depends on the particular facts and circumstances of the transaction.
- 5 See, e.g., *Network 1 Financial Securities, Inc.* NASD AWC No. EAF0400940001, July 11, 2007; *NevWest Securities Corporation*, NASD AWC E0220040112-01, March 21, 2007, and related case *SEC v. CMKM Diamonds, Inc., et. al*, U.S. Dist. Court for the District of Nevada, Civil Action No. 08- CV 0437 (Lit. Rel. No. 20519 / April 7, 2008); and *Cardinal Capital Management, Inc.* NASD AWC E072003004201, July 22, 2005. In addition, FINRA has numerous ongoing investigations involving allegations of unregistered distributions. *Barron Moore, Inc.*, Disc. Proceeding No. 2005000075703, July 21, 2008.
- 6 See, Securities Act Rel. No. 4445, 1962 SEC LEXIS 74 (February 2, 1962); see also Section 21(a) Report, *Transactions in the Securities of Laser Arms Corp. by Certain Broker-Dealers*, 50 S.E.C. 489 (1991).
- 7 See Preliminary Note to Securities Act Rule 144. 17 CFR 230.144. The term "restricted securities" is defined in Rule 144(a)(3), and includes securities acquired directly or indirectly from the issuer or an affiliate of the issuer in a transaction or chain of transactions not involving a public offering.
- 8 Securities Act Release No. 8869, 72 FR 71546 (December 17, 2007).
- 9 Securities Act Rule 144(g). 17 CFR 230.144(g).

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- 10 Recent investigations have uncovered fact patterns in which firms inappropriately relied on stock certificates issued without restrictive legends or certificates accompanied by false attorney opinions, or assumed that their clearing agent had the responsibility to determine if shares could be sold without restriction. FINRA has noted in previous guidance that firms are still responsible for the discharge of their obligations, even if they rely on third parties to perform certain activities and functions related to their business operations and regulatory responsibilities. Additionally, FINRA guidance makes clear that firms may not contract supervisory and compliance activities away from their direct control. *See Notice to Members 05-48 (Members' Responsibilities When Outsourcing Activities to Third-Party Service Providers).*
- 11 *See* NASD Rule 3011 (Anti-Money Laundering Compliance Program) and *Notice to Members 02-21 (Guidance to Member Firms Concerning Anti-Money Laundering Compliance Programs Required by Federal Law).*
- 12 *See, e.g., NevWest Securities Corporation, and related case SEC v. CMKM Diamonds, Inc., et. al, U.S. Dist. Court for the District of Nevada, Civil Action No. 08- CV 0437 (Lit. Rel. No. 20519 / April 7, 2008) (failure to take action in response to the suspicious circumstances surrounding accounts controlled by certain customers, including the practice of depositing penny stocks, liquidating them and wiring the proceeds to bank accounts.) Barron Moore, Inc., Disc. Proceeding No. 2005000075703, July 21, 2008.*

Exhibit 3

INFORMATIONAL

Anti-Money Laundering

NASD Provides Guidance To Member Firms Concerning Anti-Money Laundering Compliance Programs Required By Federal Law

SUGGESTED ROUTING

The Suggested Routing function is meant to aid the reader of this document. Each NASD member firm should consider the appropriate distribution in the context of its own organizational structure.

- Legal & Compliance
- Operation
- Registration
- Senior Management

KEY TOPICS

- Compliance Programs
- Money Laundering

Executive Summary

On October 26, 2001, President Bush signed the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (Patriot Act).¹ Title III of the Patriot Act, referred to as the International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001 (Money Laundering Abatement Act), imposes obligations on broker/dealers under new anti-money laundering (AML) provisions and amendments to the existing Bank Secrecy Act (BSA) requirements.²

Among other things, the Money Laundering Abatement Act requires all financial institutions, including broker/dealers, to establish and implement, by **April 24, 2002**, AML programs designed to achieve compliance with the BSA and the regulations promulgated thereunder. The NASD reminds members that violations of the AML laws could lead to criminal prosecution.

On February 15, 2002, the NASD filed with the Securities and Exchange Commission (SEC) a rule proposal to prescribe the minimum standards required for each member firm's AML compliance program. A copy of this rule filing can be found on the NASD Regulation AML Web Page. (See www.nasdr.com/money.asp.) NASD Regulation's AML Web Page also provides links to other sites and documents to assist members in understanding their obligations under the AML rules and regulations.

On February 25, 2002, the SEC published the proposed rule change in the *Federal Register*. The SEC received four comment letters in response to the *Federal Register* publication. Before

becoming effective, the proposed rule change must be approved by the SEC.

The Securities Industry Association Anti-Money Laundering Committee recently released a preliminary guide for firms to use when developing their AML programs (SIA Guidance). The SIA Guidance generally discusses key elements for broker/dealers to consider in developing effective AML programs. NASD Regulation's AML Web Page provides a link to the SIA Guidance.

The NASD is issuing this *Notice* to provide guidance to assist members in developing AML compliance programs that fit their business models and needs. A table of contents has been provided for readers' convenience.

Because the Department of Treasury (Treasury) is still developing AML rules, the NASD will update its guidance as new rules become final. In the interim, firms must comply with the current requirements of the BSA and the provisions of the Money Laundering Abatement Act that now apply to broker/dealers and should familiarize themselves with the proposed rules that Treasury has issued to date. (For links to Treasury's proposed rules, see www.nasdr.com/money.asp.)

Questions/Further Information

Questions regarding this *Notice to Members* may be directed to Nancy Libin, Assistant General Counsel, Office of General Counsel, NASD Regulation, at (202) 728-8835; Grace Yeh, Assistant General Counsel, at (202) 728-6939; or Kyrae Armstrong, Senior Attorney, Department of Member Regulation, at (202) 728-6962.

Special NASD Notice to Members 02-21

Anti-Money Laundering Notice to Members

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BACKGROUND

The PATRIOT Act is designed to detect, deter, and punish terrorists in the United States and abroad and to enhance law enforcement investigation tools by prescribing, among other things, new surveillance procedures, new immigration laws, as well as new and more stringent AML laws. The Money Laundering Abatement Act expands and strengthens the AML provisions put into place by earlier legislation.

Several provisions of the Money Laundering Abatement Act are relevant to NASD members. Among other things, all broker/dealers must implement an anti-money laundering compliance program by April 24, 2002. The Money Laundering Abatement Act also requires Treasury to promulgate rules requiring broker/dealers to file suspicious activity reports (SARs), which identify and describe transactions that raise suspicions of illegal activity, and to establish certain procedures with regard to "correspondent accounts" maintained for foreign banks.³ In late December 2001, Treasury released proposed rules regarding the filing of SARs by broker/dealers⁴ and the maintenance of "correspondent accounts" for foreign banks.⁵ In late February 2002, Treasury released proposed and final rules governing information sharing among law enforcement authorities, regulatory organizations, and financial institutions.⁶ Treasury will continue to issue proposed and final rules throughout the year governing and providing further guidance with respect to customer identification, "correspondent accounts" with foreign banks, and the application of AML rules to the brokerage industry, among other matters. The NASD will continue to keep members apprised of AML rules and regulations that Treasury proposes and those that Treasury adopts.

INTRODUCTION

Money laundering is generally defined as engaging in acts designed to conceal or disguise the true origin of criminally derived proceeds so that the unlawful proceeds appear to have derived from legitimate origins or constitute legitimate assets. Money laundering occurs in connection with a wide variety of crimes, including, but not limited to, drug trafficking, robbery, fraud, racketeering, and terrorism.

In general, money laundering occurs in three stages. Cash first enters the financial system at the "placement" stage, where the cash profits from criminal activity are converted into monetary instruments, such as money orders or traveler's checks, or deposited into accounts at financial institutions. At the "layering" stage, the funds are transferred or moved into other accounts or other financial institutions to separate further the proceeds from their criminal origin. At the "integration" stage, the funds are reintroduced into the economy and used to purchase legitimate assets or to fund further criminal or legitimate activities.⁷

Broker/Dealers And Existing Anti-Money Laundering Laws

Broker/dealers are subject to most of the existing AML rules as well as the new AML provisions of the Money Laundering Abatement Act, which are discussed in detail later in the document.

Firms should be aware that there are potential severe civil and criminal penalties for violations of AML laws. Under the criminal statutes, a person or entity could be criminally prosecuted for assisting or facilitating a transaction involving money laundering by a customer if the firm (or person) knew or was willfully blind to the fact that the transaction involved illegally obtained funds.⁸

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All broker/dealers have been and will continue to be subject to existing BSA reporting and recordkeeping requirements, as briefly summarized below:

- e **Currency Transaction Report (CTR):** Broker/dealers are required to file CTRs for transactions involving currency that exceed \$10,000. Because structuring is prohibited, multiple transactions are treated as a single transaction if they total more than \$10,000 during any one business day. CTRs are filed with the Financial Crimes Enforcement Network (FinCEN), a bureau of Treasury.
- e **Currency and Monetary Instrument Transportation Report (CMIR):** Any person who physically transports, mails, or ships currency or other monetary instruments into or out of the United States, in aggregated amounts exceeding \$10,000 at one time, must report the event on a CMIR. Any person who receives any transport, mail, or shipment of currency, or other monetary instrument from outside the United States in an aggregate amount exceeding \$10,000 at one time also must report the receipt. CMIRs are filed with the Commissioner of Customs.
- e **Report of Foreign Bank and Financial Accounts (FBAR):** Any person having a financial interest in, or signature or other authority over, financial accounts in a foreign country is required to report the relationship if the aggregate value of the accounts exceeds \$10,000. FBARs are filed with FinCEN.
- e **Funds Transfers and Transmittals:** Broker/dealers effecting transmittals or transfers of funds, including wire fund transfers, of \$3,000 or more must collect, retain and record on the transmittal order certain information regarding the transfer, including the name and address of the transmitter and recipient, the amount of the transmittal order, the identity of the recipient's financial institution, and the account number of the recipient. Broker/dealers also must verify the identity of transmitters and recipients that are not established customers.

In addition, broker/dealers that are subsidiaries of banks or bank holding companies currently are required under the banking regulations to file SARs with FinCEN. Such broker/dealers currently are required to report known or suspected federal criminal offenses, at specified dollar thresholds, or suspicious transactions involving \$5,000 or more that they suspect (1) involve funds derived from illegal activity or an attempt to hide or disguise funds or assets derived from illegal activity, (2) are designed to evade the requirements of the BSA, or (3) have no apparent lawful or business purpose or vary substantially from normal practice. The NASD previously has recommended that members report suspicious transactions and has advised firms that the failure to do so could be construed as aiding and abetting money laundering violations, subjecting the member to civil and criminal liability.⁹ Some firms, in fact, have been submitting SARs on a voluntary basis. As discussed in more detail later in the document, all broker/dealers will soon be required to file SARs.

New And Expanded Anti-Money Laundering Laws Applicable To Broker/Dealers

As noted above, the Money Laundering Abatement Act imposes significant new obligations on broker/dealers through new AML provisions and amendments to the existing provisions of the BSA. A brief summary of the new requirements along with anticipated effective dates is provided below:

- e **Section 312 (Due Diligence Requirements):** Section 312 requires special due diligence for all private banking and "correspondent" bank accounts (accounts established to receive deposits from, make payments on behalf of, or handle other financial transactions for a foreign bank) involving foreign persons, even if opened before Congress passed the PATRIOT Act.¹⁰ Treasury is required to delineate, by regulation, the special due diligence

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policies, procedures, and controls by April 24, 2002. Regardless of whether final regulations have been promulgated, the minimum due diligence requirements set forth in Section 312 (as discussed below in the "Anti-Money Laundering Program Guidance" section) become **effective on July 23, 2002**.

- e **Section 313 (Correspondent Account Prohibitions):** Section 313 prohibits certain financial institutions, including broker/dealers, from maintaining a "correspondent account" for, or on behalf of, a foreign "shell" bank (a foreign bank with no physical presence in any country). Financial institutions are also required to take reasonable steps to ensure that they are not indirectly providing correspondent banking services to foreign shell banks through foreign banks with which they maintain correspondent relationships. Section 313 became **effective on December 26, 2001**. Treasury released proposed regulations defining "correspondent account" in late December 2001.¹¹
- e **Section 314 (Financial Institution Cooperation Provisions):** Section 314 addresses increased cooperation among financial institutions, regulatory authorities, and law enforcement authorities. Treasury published regulations implementing Section 314 in the *Federal Register* on March 4, 2002.¹² Treasury included a proposed rule to establish a communication link between federal law enforcement and financial institutions to better share information relating to suspected terrorists and money launderers. In addition, Treasury issued an interim final rule, **effective March 4, 2002**, requiring financial institutions to file an initial, and annual thereafter, certification (which can be completed online at FinCEN's Web Site at www.treas.gov/fincen) if they wish to share information regarding terrorist financing and money laundering with other financial institutions or associations of financial institutions.¹³
- e **Section 319(b) (Domestic and Foreign Bank Records Production):** Section 319(b) addresses the production of domestic and foreign bank records. A financial institution is required to produce account information relating to foreign bank accounts **within seven days** in response to requests from federal law enforcement. Section 319 became **effective on December 26, 2001**. As mentioned above, Treasury released proposed rules regarding maintaining "correspondent accounts" in late December 2001.¹⁴
- e **Section 326 (Customer Identification Standards):** Section 326 requires Treasury and the SEC, jointly, to issue regulations that set forth minimum standards for customer identification in the account opening process. The regulations will need to require firms, at a minimum, to implement "reasonable procedures" to verify the identity of the customer opening an account, maintain records used to identify the customer, and consult government-provided lists of known or suspected terrorists. Final regulations prescribed under Section 326 will take effect **not later than October 26, 2002**. Treasury and the SEC have not yet released proposed regulations regarding customer identification.
- e **Section 352 (AML Compliance Program Components):** Section 352 requires all financial institutions to develop and implement AML compliance programs **on or before April 24, 2002**. Section 352 requires the compliance programs, at a minimum, to establish (1) the development of internal policies, procedures, and controls, (2) the designation of a compliance officer with responsibility for a firm's anti-money laundering program, (3) an ongoing employee training program, and (4) an independent audit function to test the effectiveness of the anti-money laundering compliance program. Section 352 further requires Treasury by April 24, 2002, to issue regulations that consider the extent to which these requirements correspond to the size, location, and activities of different financial institutions. Section 352 further allows Treasury, at its discretion, to issue additional requirements for AML compliance programs before the April 24, 2002, deadline. As further discussed later in the document, the NASD has proposed a rule setting forth the minimum standards for its members' AML compliance programs.

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- e **Section 356 (Broker/Dealer SAR Regulations):** By *July 1, 2002*, Treasury must publish final regulations requiring broker/dealers to file SARs. Treasury released proposed broker/dealer SAR regulations in late December 2001.¹⁵ Under Treasury's proposed regulations, the suspicious activity reporting requirement would become effective *180 days after the date on which the final broker/dealer SAR regulations are published in the Federal Register*.

NASD ANTI-MONEY LAUNDERING PROGRAM RULE

On February 15, 2002, the NASD filed with the SEC a rule proposal that would set forth minimum standards for broker/dealers' AML compliance programs.¹⁶ As required by the Money Laundering Abatement Act itself, the rule proposal would require firms to develop and implement a written AML compliance program by April 24, 2002. The proposed rule would require the program to be approved in writing by a member of senior management and be reasonably designed to achieve and monitor the member's ongoing compliance with the requirements of the BSA and the implementing regulations promulgated thereunder. The proposed rule change would require firms, at a minimum, to:

- (1) establish and implement policies and procedures that can be reasonably expected to detect and cause the reporting of suspicious transactions;
- (2) establish and implement policies, procedures, and internal controls reasonably designed to achieve compliance with the BSA and implementing regulations;
- (3) provide for independent testing for compliance to be conducted by member personnel or by a qualified outside party;
- (4) designate an individual or individuals responsible for implementing and monitoring the day-to-day operations and internal controls of the program; and
- (5) provide ongoing training for appropriate personnel.

Each firm's AML program must be designed to ensure compliance with the new provisions of the Money Laundering Abatement Act, the earlier provisions of the BSA, and the regulations promulgated thereunder. To be effective, those procedures must reflect the firm's business model and customer base. Further, in developing program criteria, firms should consider the guidelines established by the United States Sentencing Commission in the U.S. Sentencing Commission Guidelines for organizations, as well as the fiduciary responsibilities of officers and directors to ensure that the firm's compliance programs are viable and effective.¹⁷

Regardless of when and in what form the SEC approves the NASD proposed AML compliance rule, all firms are required by federal law (the Money Laundering Abatement Act) to have AML programs in place by **April 24, 2002**.¹⁸ These AML programs must meet the minimum requirements articulated in Section 352 of the Money Laundering Abatement Act.¹⁹

Members should keep in mind that the obligation to develop and implement an AML compliance program is not a "one-size-fits-all" requirement. The general nature of the requirement reflects Congressional intent that each financial institution should have the flexibility to tailor its AML program to fit its business. This flexibility is designed to ensure that all entities covered by the statute, from the very large financial institutions to the small firms, will institute effective and appropriate policies and procedures to monitor for AML compliance.²⁰ In this regard, each broker/dealer, in developing an appropriate AML program that complies with the Money Laundering Abatement Act, should consider factors such as its size, location, business activities, the types of accounts it maintains, and the types of transactions in which its customers engage.

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ANTI-MONEY LAUNDERING PROGRAM GUIDANCE

The required elements of an AML program are discussed in detail below.

Develop Internal Policies, Procedures, And Controls

Broker/dealers must develop internal policies, procedures, and controls to ensure compliance with the AML laws. The AML procedures should contain a statement that sets forth the member's policy of prohibiting money laundering and its overall efforts to detect, deter, and prevent any such violations. Broker/dealers also must establish internal controls to ensure that their AML policies and procedures are being enforced. As with any supervisory procedure, the firm must establish and implement controls and written procedures that explain the procedures that must be followed, the person responsible for carrying out such procedures, how frequently such procedures must be performed, and how compliance with the procedures should be documented and tested.

Firms must determine the manner in which AML procedures that address the following (each of which will be discussed more fully below) will apply to various accounts:

- account opening and maintenance, including verification of the identity of the customer;
- opening and maintaining "correspondent accounts" for foreign banks;
- monitoring of account activities, including but not limited to, trading and the flow of money into and out of the account, the types, amount, and frequency of different financial instruments deposited into and withdrawn from the account, and the origin of such deposits and the destination of withdrawals;
- separating the duties of employees where feasible to ensure a system of checks and balances (for example, firms may want to ensure that persons who handle cash do not open accounts or file CTRs);
- monitoring for, detecting, and responding to "red flags";
- responding to regulatory requests for AML information;
- establishing controls and monitoring employees' trading and financial activity in employee accounts; and
- ensuring that AML compliance programs contain a mechanism or process for the firm's employees to report suspected violations of the firm's AML compliance program procedures and policies to management, confidentially, and without fear of retaliation.

Identification And Verification Of Account Holders

Opening Accounts

Prior to the enactment of the Money Laundering Abatement Act, broker/dealers already had significant obligations to gather information about their customers in order to, among other things, know their customers. NASD Rule 3110 requires member firms to obtain certain information about their customers when opening an account, including the following: the customer's name and residence; whether the customer is of legal age; the signature of the registered representative introducing the account and signature of the member or partner, officer, or manager who accepts the account; and if the customer is a corporation, partnership, or other

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legal entity, the names of any persons authorized to transact business on behalf of the entity. Member firms are also required to make reasonable efforts to obtain the following additional information (for accounts other than institutional accounts and accounts in which investments are limited to transactions in open-end investment company shares not recommended by the member or its associated persons) prior to the settlement of an initial transaction in the account: a customer's tax identification and Social Security number; the customer's occupation and name and address of the employer; and whether the customer is an associated person of another member.

Member firms also are required under NASD Rules 2110 and 2310 to obtain additional customer information. Members are required under NASD Rule 2110 to comply with general "Know Your Customer" requirements. Pursuant to these requirements, members must make reasonable efforts to obtain certain basic financial information from customers so that members can protect themselves and the integrity of the securities markets from customers who do not have the financial means to pay for transactions.²¹ NASD Rule 2310 relates to a member's suitability obligations to its customers and requires each member to use reasonable efforts to obtain information concerning a customer's financial status, tax status, and investment objectives prior to making any recommendations to the customer regarding the purchase, sale, or exchange of securities.

The information required under NASD Rules 3110, 2110, and 2310 is the starting point for new AML customer identification procedures. The Money Laundering Abatement Act imposes additional customer identification requirements on member firms. Effective October 26, 2002 (or earlier, if final customer identification regulations are effective prior to October 26, 2002), broker/dealers are required to implement reasonable procedures for identifying customers and verifying their information.²² These procedures, at a minimum, must require a firm:

- to verify, to the extent reasonable and practicable, the identity of any customer seeking to open an account;²³
- to maintain records of information to verify a customer's identity; and
- to check that a customer does not appear on any list of known or suspected terrorists or terrorist organizations such as those persons and organizations listed on Treasury's Office of Foreign Assets Control (OFAC) Web Site (www.treas.gov/ofac) (and available on www.nasdr.com/money.asp) under "Terrorists" or "Specially Designated Nationals and Blocked Persons" (SDN List), as well as the list of embargoed countries and regions (collectively, the OFAC List).²⁴

Under the new AML customer identification requirements, broker/dealers will be required to make reasonable efforts to obtain and verify information about a customer. If the customer is an individual, a firm will need, to the extent reasonable and practicable, to obtain and verify certain information concerning the individual's identity, such as the individual's name, address, date of birth, and government issued identification number. Possible sources of this information include:

- physical documents, such as a driver's license, passport, government identification, or an alien registration card,²⁵ or, for businesses, a certificate of incorporation, a business license, any partnership agreements, any corporate resolutions, or other similar documents; or
- databases, such as Equifax, Experian, Lexis/Nexis, or other in-house or custom databases.

Firms opening accounts should verify the identification information at the time the account is opened, or within a relatively short time period thereafter (e.g., within five business days after account opening). Because of the unknown risk that the prospective customer could be involved

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in criminal activity, members should consider, depending on the nature of a transaction and an account, not effecting a transaction prior to verifying the information. If a potential customer refuses to provide any of the information described above, or appears to have intentionally provided false or misleading information, a firm should not open the account. If an existing customer fails to provide the requested information, the firm, after considering the known and unknown risks involved, may consider closing the account. Moreover, in either of these situations, the firm's AML compliance personnel should be notified so that a determination can be made as to whether the circumstance should be voluntarily reported to FinCEN or OFAC, as appropriate.

In the context of AML compliance, members should implement procedures that allow the firm to collect and use information concerning the account holder's wealth, net worth, and sources of income to detect and deter possible money laundering activity. Such a review should be integrated into the new accounts supervisor's existing procedures before such supervisor authorizes the opening of an account. Moreover, the supervisor's review should be documented and reviewed to ensure that the account-opening procedures are being conducted properly. Firms should consider using a checklist that lists the types of information required and documents explanations for why an account was opened absent such information.

Online Brokers

Online brokers generally do not meet or speak directly to their prospective or existing clients. These firms must acquire information about customers and, as mentioned earlier, make maximum use of other means of verifying customer identity, such as electronic databases (Equifax, Experian, Lexis/Nexis, or other in-house or custom databases). As is required of all firms, such verification of customer information must take place at the time the account is opened or within a short period thereafter (e.g., five business days). Online firms should also consider conducting computerized surveillance of account activity to detect suspicious transactions and activity. Given the global nature of online brokerage activity, it is essential that online brokers confirm the customer data and review the OFAC List to ensure that customers are not prohibited persons or entities and are not from embargoed countries or regions.

Additional Due Diligence When Opening An Account

Broker/dealers should perform the following additional due diligence when opening an account, depending on the nature of the account, and to the extent reasonable and practicable:

- inquire about the source of the customer's assets and income so that the firm can determine if the inflow and outflow of money and securities is consistent with the customer's financial status;
- gain an understanding of what the customer's likely trading patterns will be, so that any deviations from the patterns can be detected later on, if they occur;
- maintain records that identify the owners of accounts and their respective citizenship;
- require customers to provide street addresses to open an account, and not simply post office addresses, or "mail drop" addresses;
- periodically contact businesses to verify the accuracy of addresses, the place of business, the telephone, and other identifying information; and
- conduct credit history and criminal background checks through available vendor databases.

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Prohibitions On U.S. Correspondent Accounts With Foreign Shell Banks And Special Due Diligence For Correspondent Accounts

Broker/dealers are prohibited from establishing, maintaining, administering, or managing a "correspondent account" (see note 3) in the United States for an unregulated foreign shell bank. Firms should have procedures in place to ensure that this does not occur and should immediately terminate such accounts if they have any. The broker/dealer's AML compliance personnel should be notified upon discovery or suspicion that the firm may be maintaining or establishing a "correspondent account" in the United States for a foreign shell bank.

The Money Laundering Abatement Act requires broker/dealers to maintain records identifying the owners of foreign banks that maintain "correspondent accounts" in the United States and the name and address of an agent residing in the United States authorized to accept service of legal process for such banks.²⁶ Broker/dealers should require their foreign bank account holders to complete model certifications issued by Treasury to the extent possible. U.S. depository institutions and broker/dealers can send the certification forms to their foreign bank account holders for completion. The certification forms generally ask the foreign banks to confirm that they are not shell banks and to provide the necessary ownership and agent information. Use of the certification forms will help firms ensure that they are complying with requirements concerning "correspondent accounts" with foreign banks and can provide a broker/dealer with a safe harbor for purposes of complying with such requirements.²⁷ Firms are required to recertify (if relying on the certification forms) or otherwise verify any information provided by each foreign bank, or otherwise relied upon, at least every two years or at any time the firm has reason to believe that the information is no longer accurate.

In addition, broker/dealers will be required under Section 312 of the Money Laundering Abatement Act to establish appropriate, specific, and, where necessary, enhanced due diligence policies, procedures, and controls that are reasonably designed to detect and report instances of money laundering for any "correspondent account" established, maintained, administered, or managed for a foreign bank. *At a minimum*, in the case of foreign banks licensed by certain high-risk jurisdictions or operating under an offshore banking license, broker/dealers are required to take reasonable steps:

- to determine the ownership of the foreign bank;
- to conduct enhanced scrutiny of the account to detect and report suspicious activity; and
- to determine whether the foreign bank maintains "correspondent accounts" for any other bank, and if so, the identity of those banks.²⁸

Special Due Diligence For Private Banking Accounts

Similarly, the Money Laundering Abatement Act requires broker/dealers, *at a minimum*, to take reasonable steps to determine the identity of the nominal and beneficial account holders of, and the source of funds deposited into, a private banking account maintained by or on behalf of a non-U.S. citizen, and to conduct enhanced scrutiny of accounts requested or maintained by, or on behalf of, a senior foreign political figure,²⁹ or any immediate family member or close associate of a senior foreign political figure. A private bank account is an account (or combination of accounts) that requires an aggregate deposit of funds or other assets of more than \$1,000,000 established on behalf of one or more individuals who have a direct or beneficial ownership interest in the account, and is assigned to, or administered by, in whole or in part, an officer,

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employee, or agent of a financial institution acting as a liaison between the institution and the direct or beneficial owner of the account.³⁰ This enhanced monitoring or scrutiny should be reasonably designed to detect and report transactions that may involve the proceeds of foreign official corruption.³¹ Broker/dealers should monitor future pronouncements from Treasury, while also determining the extent to which they offer "private banking accounts," and ensure that their AML compliance program includes enhanced monitoring and scrutiny of accounts requested or held on behalf of foreign officials who may be involved in corrupt activities. The special due diligence requirements discussed in this section will become effective on July 23, 2002, regardless of whether Treasury has promulgated final regulations.

Monitoring Accounts For Suspicious Activity

The Money Laundering Abatement Act requires Treasury to adopt regulations requiring broker/dealers to file SARs.³² Under Treasury's proposed regulations, SARs would be filed with FinCEN. Broker/dealers would be required to file SARs for:

- any transaction conducted or attempted by, at or through a broker/dealer involving (separately or in the aggregate) funds or assets of \$5,000 or more for which:
 - the broker/dealer detects any known or suspected federal criminal violation involving the broker/dealer, or
 - the broker/dealer knows, suspects, or has reason to suspect that the transaction:
 - involves funds related to illegal activity,³³
 - is designed to evade the regulations, or
 - has no business or apparent lawful purpose and the broker/dealer knows of no reasonable explanation for the transaction after examining the available facts, including the background and possible purpose of the transaction.

Although the reporting threshold begins at \$5,000, in its proposed regulations, Treasury notes that a risk-based approach to developing compliance procedures that can be reasonably expected to promote the detection and reporting of suspicious activity should be the focus of a broker/dealer's AML compliance program. Treasury further notes that a compliance program that allows for the review of only those transactions that are above a set threshold, regardless of whether transactions at a lower dollar threshold may involve money laundering or other risks, would probably not be a satisfactory program.³⁴ Broker/dealers should file a SAR and in some circumstances notify law enforcement authorities of all transactions that arouse articulable suspicion that proceeds of criminal, terrorist, or corrupt activities may be involved.

Treasury could amend its proposed regulations based on comments it receives from interested parties. Treasury is required to issue final SAR regulations by July 1, 2002, and firms will be required to file SARs beginning 180 days after final broker/dealer SAR regulations are published in the *Federal Register*. To demonstrate a strong commitment to compliance with AML principles and goals, broker/dealers should consider filing SARs voluntarily prior to the effective date of the regulations. NASD Regulation will keep members informed as Treasury's proposed regulations are amended and finalized.

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Money Laundering "Red Flags"

Broker/dealers need to look for signs of suspicious activity that suggest money laundering.³⁵ If a broker/dealer detects "red flags," it should perform additional due diligence before proceeding with the transaction. Examples of "red flags" are described below:

- The customer exhibits unusual concern regarding the firm's compliance with government reporting requirements and the firm's AML policies, particularly with respect to his or her identity, type of business and assets, or is reluctant or refuses to reveal any information concerning business activities, or furnishes unusual or suspect identification or business documents.
- The customer wishes to engage in transactions that lack business sense or apparent investment strategy, or are inconsistent with the customer's stated business strategy.
- The information provided by the customer that identifies a legitimate source for funds is false, misleading, or substantially incorrect.
- Upon request, the customer refuses to identify or fails to indicate any legitimate source for his or her funds and other assets.
- The customer (or a person publicly associated with the customer) has a questionable background or is the subject of news reports indicating possible criminal, civil, or regulatory violations.
- The customer exhibits a lack of concern regarding risks, commissions, or other transaction costs.
- The customer appears to be acting as an agent for an undisclosed principal, but declines or is reluctant, without legitimate commercial reasons, to provide information or is otherwise evasive regarding that person or entity.
- The customer has difficulty describing the nature of his or her business or lacks general knowledge of his or her industry.
- The customer attempts to make frequent or large deposits of currency, insists on dealing only in cash equivalents, or asks for exemptions from the firm's policies relating to the deposit of cash and cash equivalents.
- The customer engages in transactions involving cash or cash equivalents or other monetary instruments that appear to be structured to avoid the \$10,000 government reporting requirements, especially if the cash or monetary instruments are in an amount just below reporting or recording thresholds.
- For no apparent reason, the customer has multiple accounts under a single name or multiple names, with a large number of inter-account or third-party transfers.
- The customer is from, or has accounts in, a country identified as a non-cooperative country or territory by the Financial Action Task Force (FATF).³⁶
- The customer's account has unexplained or sudden extensive wire activity, especially in accounts that had little or no previous activity.
- The customer's account shows numerous currency or cashiers check transactions aggregating to significant sums.
- The customer's account has a large number of wire transfers to unrelated third parties inconsistent with the customer's legitimate business purpose.

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- The customer's account has wire transfers that have no apparent business purpose to or from a country identified as a money laundering risk or a bank secrecy haven.
- The customer's account indicates large or frequent wire transfers, immediately withdrawn by check or debit card without any apparent business purpose.
- The customer makes a funds deposit followed by an immediate request that the money be wired out or transferred to a third party, or to another firm, without any apparent business purpose.
- The customer makes a funds deposit for the purpose of purchasing a long-term investment followed shortly thereafter by a request to liquidate the position and transfer of the proceeds out of the account.
- The customer engages in excessive journal entries between unrelated accounts without any apparent business purpose.
- The customer requests that a transaction be processed in such a manner to avoid the firm's normal documentation requirements.
- The customer, for no apparent reason or in conjunction with other "red flags," engages in transactions involving certain types of securities, such as penny stocks, Regulation "S" (Reg S) stocks, and bearer bonds, which although legitimate, have been used in connection with fraudulent schemes and money laundering activity. (Such transactions may warrant further due diligence to ensure the legitimacy of the customer's activity.)
- The customer's account shows an unexplained high level of account activity with very low levels of securities transactions.
- The customer maintains multiple accounts, or maintains accounts in the names of family members or corporate entities, for no apparent business purpose or other purpose.
- The customer's account has inflows of funds or other assets well beyond the known income or resources of the customer.³⁷

The above-listed money laundering "red flags" are not exhaustive; however, an awareness of the "red flags" will help ensure that broker/dealer personnel can identify circumstances warranting further due diligence. Appropriate "red flags" should be described in the written policies and AML compliance procedures of the broker/dealer.

Reporting Procedures

Although final regulations concerning the filing of SARs may not be adopted until July 1, 2002, voluntary reporting is useful to the government and helpful to firms in order to provide a defense to charges of aiding and abetting money laundering violations. Furthermore, in anticipation of the adoption of the final broker/dealer SAR requirements, all broker/dealers should be preparing to establish and implement procedures to detect and report suspicious transactions by means of SARs. Firms should implement systems, preferably automated ones, that would allow firms to monitor trading, wire transfers, and other account activity to allow firms to determine when suspicious activity is occurring. If a firm decides to monitor customer accounts manually, it must review a sufficient amount of account activity to ensure the detection of suspicious activity by allowing the member to identify patterns of activity and more importantly, new patterns or patterns that are inconsistent with the customer's financial status or make no economic sense.

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Exception reports should consider the transaction size, location, type, number, and the nature of the activity. Firms should create guidelines for employees that identify examples of suspicious activity that may involve money laundering and form lists of high-risk clients whose activities may warrant further scrutiny. Firms should develop procedures for following-up on transactions that have been identified as suspicious or high-risk.

Broker/dealers should also develop administrative procedures concerning SARs. The procedures should address the process for filing SARs and reviewing SAR filings and the frequency of filings for continuous suspicious activity. In addition, a broker/dealer should consider requiring that all of its SAR filings be reported periodically to its Board of Directors and/or to senior management. In the event of a high-risk situation, broker/dealers should require that a report be made immediately to the Board of Directors and/or senior management.³⁸

Recordkeeping And Disclosure

Firms should develop procedures to maintain the confidentiality of the SAR filings and to maintain copies of SARs for a five-year period. Firms are prohibited from notifying any person involved in a reported transaction that the transaction has been reported on a SAR. In addition, firms may not disclose SARs or the fact that a SAR was filed, other than to law enforcement agencies or securities regulators. Firms must also have procedures in place to ensure the denial of any subpoena requests for SARs or information in SARs, and for informing FinCEN of any subpoena received. It may be advisable to segregate SAR filings and supporting documentation from other books and records of the firm to avoid violating the prohibitions on disclosure of these records. The broker/dealer should also establish procedures and identify a contact person to handle requests for a subpoena or other requests that call for disclosure of a SAR.

Currency Transaction Reports

Broker/dealers should have procedures to ensure compliance with the BSA provision requiring broker/dealers to file CTRs with FinCEN.

Currency And Monetary Instrument Transportation Reports

Broker/dealers should have procedures to ensure compliance with the BSA provision requiring broker/dealers to file CMIRs with the Commissioner of Customs when any person physically transports, receives, mails, or ships currency or other monetary instruments into or out of the United States, in aggregated amounts exceeding \$10,000 at one time.

Procedures For Sharing Information With And Responding To Requests For Information From Federal Law Enforcement Agencies

Broker/dealers should develop procedures to handle requests for information from FinCEN relating to money laundering or terrorist activity. Under Treasury's *proposed* regulations implementing Section 314, which were published in the *Federal Register* on March 4, 2002, FinCEN may require broker/dealers to search their records to determine whether they maintain or have maintained any account for, or have engaged in any transaction with, each individual, entity, or organization named in FinCEN's request. If a broker/dealer identifies an account or transaction identified by FinCEN, it would be required to report the identity of the individual, entity, or organization, the account number, all identifying information provided by the account holder when the account was established, and the date and type of transaction. Broker/dealers would be required to report the information to FinCEN as soon as possible either by e-mail to patriot@fincen.treas.gov, by calling the Financial Institutions Hotline (1-866-556-3974), or by any other means that FinCEN specifies.

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Broker/dealers also should identify contact persons and have procedures in place for providing information to and handling requests from enforcement authorities about the firms' AML efforts, as well as customers engaged in possible money laundering. This information must be provided to the appropriate agency and made available at a specified location when requested. Firms should establish procedures to provide such information *not later than seven days* after receiving a written enforcement agency request.

Firms should also have procedures in place to terminate a correspondent relationship with a foreign bank *within 10 business days* of receiving written notice from Treasury or the United States Attorney General that the foreign bank failed either to comply with a summons or subpoena or to contest it in United States court.

Finally, in the course of performing due diligence or during the opening of an account, firms should immediately contact Federal law enforcement by telephone in appropriate emergency situations as described below:

- e a customer is listed on the OFAC List;e
- e a customer's legal or beneficial account owner is listed on the OFAC List;e
- e a customer attempts to use bribery, coercion, undue influence, or other inappropriate means to induce a broker/dealer to open an account or proceed with a suspicious or unlawful activity or transaction; ande
- e any other situation that a firm reasonably determines requires immediate government intervention.e

Voluntary Information Sharing Among Financial Institutions

To the extent desired and/or appropriate, broker/dealers should have procedures in place for sharing information with other financial institutions about those suspected of terrorism and money laundering. Under Treasury's *interim rule*, which became effective on March 4, 2002, broker/dealers that share this information must file an annual certification with FinCEN.³⁹ The certification requires broker/dealers to take steps necessary to protect the confidentiality of the information and to use the information only for purposes specified in the rule. The certification can be found at: www.treas.gov/fincen. Broker/dealers should have adequate procedures to protect the security and confidentiality of such information.

Designate Compliance Officer

Every broker/dealer compliance program must designate a compliance officer ("AML Compliance Officer") to help administer the firm's AML compliance program efforts. Broker/dealers should vest this person with full responsibility and authority to make and enforce the firm's policies and procedures related to money laundering. The AML Compliance Officer does not need to be the firm's current compliance officer. Some larger firms have placed this responsibility on the firm's risk manager. Firms may, however, consider incorporating AML compliance requirements into the existing duties of a firm compliance officer. Whomever the firm designates as its AML Compliance Officer should have the authority, knowledge, and training to carry out the duties and responsibilities of his or her position.

The AML Compliance Officer should monitor compliance with the firm's AML program and help to develop communication and training tools for employees. The AML Compliance Officer should also regularly assist in helping to resolve or address heightened due diligence and "red flag" issues.

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The AML Compliance Officer should ensure that AML records are maintained properly and that SARs are filed as required pursuant to the firm's procedures. In short, the AML Compliance Officer should be the primary contact for the firm on AML compliance implementation and oversight.

Finally, to the extent applicable, the AML Compliance Officer should report to a member of the Board of Directors (or other high level executive officer) on AML compliance issues. This senior officer or director should communicate with firm employees on AML issues to further demonstrate the firm's commitment to AML compliance. The firm's senior management should work with the AML Compliance Officer to help ensure that the firm's AML policies, procedures, and programs meet all applicable government standards and that they are effective in detecting, deterring, and punishing or correcting AML misconduct. The firm's senior management also should work with the AML Compliance Officer to ensure that the AML compliance policies, procedures, and programs are updated and reflect current requirements.

Establish An Ongoing Training Program

The Money Laundering Abatement Act requires firms to develop ongoing employee training programs on AML issues. The AML employee training should be developed under the leadership of the AML Compliance Officer or senior management. Educational pamphlets, videos, intranet systems, in-person lectures, and explanatory memos are all appropriate training vehicles for AML training. The training may vary based on the type of firm and its size, its customer base, and its resources. The NASD urges its members to instruct their employees about the following topics, at a minimum:

- how to identify "red flags" and possible signs of money laundering that could arise during the course of their duties;
- what to do once the risk is identified;
- what their roles are in the firm's compliance efforts;
- how to perform their roles;
- the firm's record retention policy; and
- disciplinary consequences, including civil and criminal penalties for non-compliance with the Money Laundering Abatement Act.

The NASD advises its members, *at a minimum*, to implement AML training on an annual basis. Frequent evaluation of training programs may be necessary to ensure that firms are informing employees about any new developments with the rules and regulations. As noted above, firms should update their training materials, as necessary, to reflect new developments in the law. Incorporation of money laundering compliance training into continuing education programs is recommended for both registered representatives and supervisors.

A broker/dealer should scrutinize its operations to determine if there are certain employees who may need additional or specialized training due to their duties and responsibilities. For example, employees in Compliance, Margin, and Corporate Security may need more comprehensive training. The firm should train these employees or have these employees receive the appropriate instruction to ensure compliance with the Money Laundering Abatement Act.

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Establish An Independent Testing Function

In addition to the firm's overall supervisory responsibility to ensure that its procedures are being followed properly, broker/dealers must have an independent testing function to review and assess the adequacy of and level of compliance with the firm's AML compliance program. Either member personnel or a qualified outside party may perform the testing function, depending in part on the firm's size and resources. Smaller firms, for example, may consider using a qualified outside party to complete this function or they may find it more cost effective to use appropriately trained firm personnel. If a firm uses internal personnel, sufficient separation of functions should be maintained to ensure the independence of the internal testing personnel.

The independent testing should be performed annually. After a test is complete, the internal testing personnel or qualified outside party should report its findings to senior management or to an internal audit committee, as appropriate. The firm should ensure that there are procedures for implementation of any of the internal testing personnel's or third party's recommendations and corrective or disciplinary action as the case may warrant.

INTRODUCING BROKERS AND CLEARING BROKERS

The NASD wishes to emphasize that both introducing brokers and clearing brokers have responsibilities under the Money Laundering Abatement Act. All broker/dealers should devote special attention to potentially high-risk areas for money laundering. Both introducing brokers and clearing brokers must establish and implement the appropriate AML procedures identified above to comply with the Money Laundering Abatement Act's requirements.

In order to detect suspicious activity, it is imperative that introducing and clearing brokers work together to achieve compliance with the Money Laundering Abatement Act. For instance, introducing brokers generally are in the best position to "know the customer," and thus to identify potential money laundering concerns at the account opening stage, including verification of the identity of the customer and deciding whether to open an account for a customer.⁴⁰ In essence, introducing brokers should understand that they are the first line of defense in detecting and deterring suspicious activity. Clearing firms, in turn, may be in a better position to monitor customer transaction activity, including but not limited to, trading, wire transfers, and the deposit and withdrawal into and out of accounts of different financial instruments. To assist introducing brokers and, more importantly, satisfy their own obligations under federal law, clearing firms should establish both automated systems to detect suspicious activity and procedures to share AML information and responsibilities with introducing brokers, consistent with the Money Laundering Abatement Act. For example, both the introducing broker and clearing firm may have information concerning a customer relevant to an assessment of whether a wire transfer out of an account to a particular destination raises any AML concerns.

Importantly, introducing brokers must have a basis for assuring themselves that their clearing firms are monitoring customer account activity on their behalf. Similarly, clearing firms must have a basis for assuring themselves that their introducing firms are following appropriate customer identification procedures. Responsibilities relating to AML compliance should be clearly allocated between the parties, and such responsibilities should be specified in the parties' clearing agreements pursuant to NASD Rule 3230. Any such allocation, however, would not relieve either party from its independent obligation to comply with AML laws.

In short, introducing brokers and clearing firms need to work together to allow each firm to meet its obligation to comply with the AML laws.

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CONCLUSION

As stated above, the NASD will update its guidance as new AML rules and regulations become final. In the interim, the NASD reminds members to comply with the provisions of the Money Laundering Abatement Act that currently apply to broker/dealers. Although the obligation to develop and implement an AML compliance program is not a "one-size-fits-all" requirement, all broker/dealers must have an AML compliance program designed to achieve compliance with the BSA and the regulations promulgated thereunder.

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ENDNOTES

- 1 Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, Pub. L. No. 107-56, 115 Stat. 272 (2001).
- 2 31 U.S.C. §§ 5311, *et seq.*
- 3 In its proposed rules released in December 2001, Treasury defines "correspondent account" for purposes of broker/dealers as "an account established to receive deposits from, make payments on behalf of a foreign bank, or handle other financial transactions related to such bank." See 66 Fed. Reg. 67,459 (December 28, 2001). The NASD will keep members apprised of any changes to the definition of "correspondent account" when Treasury releases its final rules in this area. Please also note that Treasury's definition is different from the definition of correspondent brokerage accounts.
- 4 See 66 Fed. Reg. 67,669 (December 31, 2001). NASD Regulation's AML Web Page provides links to Treasury's proposed and final regulations.
- 5 See 66 Fed. Reg. 67,459 (December 28, 2001).
- 6 See 67 Fed. Reg. 9873 (March 4, 2002); 67 Fed. Reg. 9879 (March 4, 2002).
- 7 See generally *Anti-Money Laundering, Efforts in the Securities Industry*, Report to the Chairman, Permanent Subcommittee on Investigations, Committee on Governmental Affairs, U.S. Senate, GAO-02-111 (October 2001).
- 8 Title 18 U.S.C. §§ 1956 and 1957 make knowingly engaging in, or attempting to engage in, financial transactions involving the proceeds of certain unlawful activities a criminal offense. Therefore, under the criminal statutes, a person or entity could be prosecuted for assisting or participating in money laundering perpetrated by its customer if the firm (or person) knew or was willfully blind to the fact that the transaction involved illegal funds. Criminal penalties include fines up to \$500,000 or twice the value of the property involved in the transaction, whichever is greater, and prison sentences as long as 20 years. In addition to criminal penalties, violators may face civil penalties up to the greater of the value of the property, funds, or monetary interests involved in the transaction or \$10,000, as well as forfeiture of any property involved in the transaction. The BSA also imposes criminal and civil penalties for violations of the BSA or its implementing regulations. Generally, a person can be subject to a criminal fine of up to \$250,000 or imprisonment of up to 5 years, or both. A person who violates the BSA while violating another law of the United States, or engaging in a pattern of illegal activity, is subject to a criminal fine of up to \$500,000 or imprisonment of up to 10 years, or both. The Money Laundering Abatement Act adds additional criminal and civil penalties that can be up to two times the amount of the transaction, not to exceed \$1,000,000 for violations of certain BSA provisions.
- 9 See *NASD Notice to Members 89-12, Reporting Suspicious Currency and Other Questionable Transactions to the IRS/Customs Hotline*.
- 10 See note 3.
- 11 See 66 Fed. Reg. 67,459 (December 28, 2001).
- 12 See 67 Fed. Reg. 9873 (March 4, 2002); 67 Fed. Reg. 9879 (March 4, 2002).
- 13 See 67 Fed. Reg. 9873 (March 4, 2002); 67 Fed. Reg. 9879 (March 4, 2002).
- 14 See 66 Fed. Reg. 67,459 (December 28, 2001).
- 15 See 66 Fed. Reg. 67,669 (December 31, 2001).
- 16 See File No. SR-NASD-2002-24.
- 17 The U.S. Sentencing Commission Guidelines for organizations set out the following criteria for an effective corporate compliance program: (1) whether the company's compliance standards and procedures are reasonably capable of reducing the prospect of criminal activity; (2) whether there is oversight of the compliance program by high-level personnel; (3) whether the company exercises due care in delegating substantial authority; (4) whether the company communicates effectively to all levels of employees; (5) whether the company has in place viable systems for monitoring, auditing, and reporting suspected misconduct without fear of reprisal; (6) whether the company enforces compliance standards in a consistent manner using appropriate disciplinary measures; and (7) whether the company has taken reasonable steps to respond to and prevent further similar offenses upon detection of a violation. See also *In Re Caremark International Inc. Derivative Litigation*, 698 A.2d 959 (Del. Ch. 1996); *McCall V. Scott*, 250 F.3d 1997 (9th Cir. 2001).
- 18 The New York Stock Exchange (NYSE) has also proposed Rule 445, which mirrors the NASD's proposed rule. See File No. SR-NYSE-2002-10e (filed with the SEC on February 27, 2002).
- 19 31 U.S.C. § 5318(h) (amended by Section 352 of the Money Laundering Abatement Act).
- 20 See *USA Patriot Act of 2001: Consideration of H.R. 3162 Before the Senate* (October 25, 2001) (statement of Sen. Sarbanes); *Financial Anti-Terrorism Act of 2001: Consideration Under Suspension of Rules of H.R. 3004 Before the House of Representatives* (October 17, 2001) (statement of Rep. Kelly) (provisions of the Financial Anti-Terrorism Act of 2001 were incorporated as Title III in the PATRIOT Act.)
- 21 See *Notice to Members 96-32; Notice to Members 96-70; and Notice to Members 99-11*.

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- 22 Treasury has until October 26, 2002 to promulgate additional customer identification requirements.
- 23 Firms should authenticate customer identity at the time of account opening, and not just when an account shows suspicious activity.
- 24 See *Notice to Members 01-67, Terrorist Activity*. Executive Order 13224 prohibits transactions with those persons and organizations listed on the OFAC Web Site on the SDN List as well as with the listed embargoed countries and regions; See also Section 326 of the Money Laundering Abatement Act. The OFAC Web Site is updated frequently, so members should consult the list on a regular basis. Software programs that allow firms to perform this function in a more user friendly and automated manner are available.
- 25 Note that under the BSA, firms must record a current passport number or other valid government identification number for transfers or transmittals of \$3,000 or more by or for non-resident alien accounts. See 31 C.F.R. 103.33 (2001).
- 26 31 U.S.C. § 5318(k) (amended by Section 319(b) of the Money Laundering Abatement Act).
- 27 31 U.S.C. § 5318(j) (amended by Section 313 of the Money Laundering Abatement Act). Please note that Treasury included a model certification form in its December 2001 rule proposal, available at www.nasdr.com/money.asp.
- 28 31 U.S.C. § 5318(i) (amended by Section 312 of the Money Laundering Abatement Act).
- 29 Treas. Dept., Bd. of Gov. of Fed. Res., Comp. Of the Currency, F.D.I.C., O.T.S. and State Dept., *Guidance on Enhanced Scrutiny for Transactions that May Involve the Proceeds of Foreign Official Corruption*, (Jan. 2001) and at www.ustreas.gov/press/releases/guidance.htm.
- 30 31 U.S.C. § 5318(i) (amended by Section 312(a)(i)(4)(B) of the Money Laundering Abatement Act).
- 31 31 U.S.C. § 5318(i) (amended by Section 312(a)(i)(3) of the Money Laundering Abatement Act).
- 32 31 U.S.C. § 5318(g).
- 33 Evidence that a broker/dealer knows that the property involved in a financial transaction constitutes the proceeds of unlawful activity and nonetheless conducts (or attempts to conduct) the financial transaction with the unlawful proceeds with the intent to promote the unlawful activity or knowing that the transaction is designed to conceal or disguise the nature, source, or ownership of the unlawful proceeds, can subject a broker/dealer to criminal prosecution. See 18 U.S.C. § 1956.
- 34 66 Fed. Reg. 67,669 at 67,674 (Dec. 31, 2001).
- 35 Firms are also reminded to notify self-regulatory organizations and the SEC if they detect indicators of securities laws violations. Firms should note that there are exceptions to the proposed broker/dealer SAR requirements, including that a broker/dealer is not required to file a SAR to report a possible violation of any of the federal securities laws or rules of a self-regulatory organization by the broker/dealer or any of its officers or directors, employees, or other registered representatives, other than certain rules, so long as such violation is properly reported to the SEC or a self-regulatory organization. See 66 Fed. Reg. 67,669 at 67,676-677 (Dec. 31, 2001).
- 36 The FATF is an inter-governmental body whose purpose is the development and promotion of policies, both at national and international levels, to combat money laundering. The FATF monitors members' progress in implementing anti-money laundering measures, reviews money laundering techniques and counter-measures, and promotes the adoption and implementation of anti-money laundering measures globally. See links to the FATF Web Site at www.nasdr.com/money.asp.
- 37 See Speech by Lori Richards, Director of Securities and Exchange Commission's Office of Compliance, Inspections and Examinations, *Money Laundering: It's on the SEC's Radar Screen* (May 8, 2001); See also SIA, *Preliminary Guidance for Detering Money Laundering Activity*, at 12-13e (Feb. 2002); Sarah B. Estes, e Sutherland, Asbill & Brennan LLP, e *Securities Broker-Dealers and Money Laundering: The Obligations of Broker-Dealers Under Money Laundering Laws* at 5-6 (2001).e
- 38 Firms may wish to consult FinCEN's Web Site for more information (see www.treas.gov/fincen), including, annual SAR Activity Review reports and SAR Bulletins, which discuss trends in suspicious activity reporting and give helpful tips.
- 39 See 67 Fed. Reg. 9873 (March 4, 2002).
- 40 All broker/dealers should consider using electronic databases (such as Equifax, Experion, Lexis/Nexis, or other in-house or custom databases) to verify customer identity.

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Exhibit 4

THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION

In the Matter of:)

) File No. [REDACTED]

[REDACTED]

WITNESS: Eugene W. Terracciano

PAGES: 1 through 235

PLACE: Securities and Exchange Commission
100 F Street, N.E.

Washington, D.C. 20549

DATE: Wednesday, September 30, 2015

The above-entitled matter came on for hearing,
pursuant to notice, at 10:10 a.m.

Diversified Reporting Services, Inc.

(202) 467-9200

Page 2

1 APPEARANCES:

2

3 On behalf of the Securities and Exchange Commission:

4 GEORGE BAGNALL, ESQ.

5 DANIEL MAHER, ESQ.

6 Securities and Exchange Commission

7 Division of Enforcement

8 100 F Street, N.E.

9 Washington, D.C. 20549

10 (202) 551-4316o

11

12 On behalf of Financial Crimes Enforcement Network:

13 KATE ZERNES, ESQ.

14 MITCH McINERNEY, ESQ.

15 PO Box 39

16 Vienna, Virginia 22183

17

18

19

20

21

22

23

24

25

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1 CONTENTS

2

3 WITNESS: EXAMINATION

4 Eugene W. Terracciano 7

5

6 EXHIBITS: DESCRIPTION IDENTIFIED:

7 26 Subpoena 7

8 27 U4 Employment History 8

9 28 E-mail from RBC to S. 126

10 Guidetti & K. McKenna

11 29 E-mail from N. DeGidio to 155

12 810 Compliance dtd 12/2/14

13 30 E-mail between E. Terracciano 199

14 & T. Fiorucci

15 31 E-mail between E. Terracciano 206

16 & N. DeGidio

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18

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Page 3

1 APPEARANCES (CONT.):

2

3 On behalf of the Witness:

4 PAUL McCURDY, ESQ.

5 WENDY CLARKE, ESQ.

6 Kelley Drye & Warren LLP

7 400 Atlantic Street

8 Stamford, Connecticut 06901

9 (203) 351-8039

10

11 ALSO PRESENT:

12 Jonathan Walker, SEC Intern

13

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Page 5

1 PROCEEDINGS

2 MR. BAGNALL: We will go on the record at 10:10

3 a.m., using the watch on my wrist, September 30, 2015.

4 Mr. Terracciano, could you please raise your

5 right hand.

6 Do you swear or affirm to tell the truth, the

7 whole truth and nothing but the truth?

8 THE WITNESS: Yes, I do.

9 Whereupon,

10 EUGENE WILLIAM TERRACCIANO

11 was called as a witness and, having been first duly

12 sworn, was examined and testified as follows:

13 EXAMINATION

14 MR. BAGNALL: Can you please state and spell

15 your full name for the record?

16 THE WITNESS: Yes. Eugene, E-u-g-e-n-e,

17 William, W-i-l-l-i-a-n, Terracciano,

18 T-e-r-r-a-c-c-i-a-n-o.

19 MR. BAGNALL: Okay. You can put your hand

20 down. Thanks.

21 So I am George Bagnall and this is Dan Maher.

22 We are members of the staff of the Enforcement Division

23 of the U.S. Securities and Exchange Commission.

24 This is an investigation by the U.S. SEC in the

25 matter of [REDACTED] SEC File No.

1 BY MR. BAGNALL:
 2 Q Did you have any other job responsibilities?
 3 A Training.
 4 Q Okay. Anything else?
 5 A And needs analysis.
 6 Q Okay. Anything else?
 7 A I'm going to say that's it.
 8 Q Okay. How about any responsibilities with
 9 respect to suspicious activity reports? Did you have any
 10 responsibilities in connection with your role as the AML
 11 CO for suspicious activity reports at Aegis?
 12 A Yes.
 13 Q What were those job responsibilities?
 14 A The responsibilities were the actual trade
 15 activity reports were done through branch supervisory
 16 compliance personnel. And issues -- I would periodically
 17 discuss issues or when needed from the branches on
 18 activity.
 19 MR. McCURDY: Excuse me one second. I missed
 20 the first part of your answer.
 21 What was primarily done through branch
 22 supervisory personnel?
 23 THE WITNESS: The trade activity reviews.
 24 MR. McCURDY: Thank you.
 25 BY MR. BAGNALL:

1 Q And the second part was discuss issues with
 2 whom?
 3 A Discuss issues with the supervisors that were
 4 using those systems.
 5 Q And how were the trade activity reviews and
 6 discussions, how were those related to suspicious
 7 activity reports?
 8 A Obviously that captured the trade activity in
 9 accounts. If anything was out of the ordinary, that
 10 would be brought to my attention and the attention of the
 11 previously CCO.
 12 Q And which previous chief compliance officer?
 13 A When Sam Guidetti was there. When Tony Monaco
 14 was there.
 15 Q So whoever was in that role at the time?
 16 A Yes.
 17 Q And what is the "suspicious activity report"?
 18 A What definition are you -- are you asking me a
 19 definition of a --
 20 Q What is a suspicious activity report?
 21 A You know, there's a lot of different activities
 22 that could quite possibly make up a suspicious activity.
 23 MR. McCURDY: He's asking about a suspicious
 24 activity report.
 25 THE WITNESS: Oh, an actual report?

1 BY MR. BAGNALL:
 2 Q Yes, sir.
 3 A Are you saying did I have access to a report?
 4 I'm not sure of your question.
 5 Q Yeah, let me ask it again.
 6 I am asking you if you know what a suspicious
 7 activity report is.
 8 A One that needs to -- one that would be filed,
 9 are you saying?
 10 Q Correct, correct.
 11 A Okay, yes, yes.
 12 Q So what is a suspicious activity report?
 13 A A suspicious activity report is an electronic
 14 report filed through FinCen that outlines activities in
 15 an account in a drop-down box or in additional to that,
 16 and I checked off boxes.
 17 Q And are you describing the boxes and the
 18 drop-down box -- the checked boxed in the drop-down box,
 19 that's an online system?
 20 A Yes, online form, yes.
 21 Q Okay. As the AML CO for Aegis -- in your
 22 capacity as the AML CO for Aegis, what responsibility, if
 23 any, did you have for making suspicious activity reports?
 24 A If an activity was deemed suspicious after
 25 investigation, and a suspicious SAR would be filed.

1 Q Who is responsible for determining whether a
 2 SAR should be filed at Aegis?
 3 A That was a discussion between the CCO and
 4 myself.
 5 Q So was there -- both the chief compliance
 6 officer and the AML CO were responsible for deciding
 7 whether Aegis needed to file a SAR, is that what you're
 8 saying?
 9 A Correct, yes.
 10 Q Was that spelled out somewhere in the firm's
 11 policies and procedures that the responsibility to file a
 12 SAR was both the AML CO and the chief compliance officer?
 13 A I don't know -- I don't know if that was
 14 actually in the memorialized in a WSP.
 15 Q Okay. So is it your testimony then that in
 16 practice it was the responsibility of both the AML CO and
 17 chief compliance officer at Aegis to determine whether a
 18 SAR needed to be filed?
 19 A Correct.
 20 Q Okay. Do you know what the memorialized
 21 practice was at Aegis for who had -- let me start that
 22 over.
 23 Do you know what the WSPs of the firm say about
 24 who has responsibility to determine whether a SAR needs
 25 to be filed?

1 A Yes.

2 Q What do the WSPs say?

3 A I believe that said that the AML CO has that

4 responsibility.

5 Q The AML CO alone?

6 A Yes, correct.

7 Q Again, in connection with your role as the AML

8 CO at Aegis, were there any other job responsibilities

9 you had with respect to SARs that you haven't already

10 mentioned?

11 A I'm not entirely sure what you mean by that.

12 Q So I think you testified that you had the

13 responsibility to determine, after an investigation,

14 whether a SAR needed to be filed in conversations with

15 the chief compliance officer, correct?

16 A Uh-huh.

17 Q And that was in response to my questions about

18 what job responsibilities you had as the AML CO in

19 connection with SAR, correct?

20 A Correct.

21 Q Okay. Did you have any other job

22 responsibilities as the AML CO at Aegis that are related

23 to SARs?

24 A No.

25 Q Okay. Did you have any responsibility as the

d d d d d d d d

1 enhanced procedure for that specific function.

2 Q Was there a precipitating event that led Aegis

3 to update the DVP/RVP procedures?

4 A Not that I know of.

5 Q In what ways did the enhanced procedures for

6 DVP/RVP accounts affect AML compliance at Aegis?

7 A It entailed a number of additional

8 documentation that needed to be filled out and a number

9 of websites that needed to be looked at to check

10 information.

11 Q Do you know why those procedures weren't in

12 place for DVP/RVP accounts initially?

13 A No.

14 Q Did Aegis, during your time at the time, did

15 Aegis have a low-priced securities business?

16 A I'd like you to clarify that a little more.

17 Q What is a low-priced securities business, do

18 you know?

19 A Yes, I do know.

20 Q What is it?

21 A A low-priced securities business is anything --

22 a security that trades under \$5 a share. Could even be

23 on an exchange, but usually on a Bulletin Board

24 transaction or security.

25 Q Okay. With that in mind did Aegis have a

d d d d d d d d

1 AML CO for drafting the AML compliance policies and

2 procedures at Aegis?

3 A Yes.

4 Q Okay. Can you please describe those

5 responsibilities?

6 A Making adjustments to the WSPs relating to AML

7 procedures, putting in enhancements to what was already

8 in the compliance manual.

9 Q Did you do those things during your time at

10 Aegis?

11 A Correct.

12 Q Yes, you did?

13 A Yes.

14 Q What changes did you make to the AML policies

15 and procedures while you were at Aegis?

16 A One in particular was the enhanced procedures

17 for DVP/RVP accounts for low-price securities.

18 Q And what was your role in connection with the

19 enhanced procedure for DVP/RVP accounts?

20 A I worked with senior management to put together

21 an updated procedure.

22 Q Why did you need to update the procedure for

23 DVP/RVP accounts?

24 A In discussions with our outside counsel and

25 senior management, it was determined that we needed an

1d low-priced securities business during the time you were

2 employed by the firm?

3 A You know, I'm still not sure what you mean by a

4 "low-priced securities business."

5 Q Let me try again, okay?

6 A Yeah.

7 Q During the time you were employed by Aegis, did

8 Aegis have customers who traded low-priced securities?

9 A Yes.

10 Q Okay. When I say the "low-priced securities

11 business," I mean that, that Aegis had customers that

12 engaged in transactions with low-priced securities, okay?

13 A Could I just ask you a question?

14 Q Sure. Well -- go ahead.

15 A I'd like to just clarify because when you say

16 "business," I'm thinking of the organization and a line

17 of business.

18 When you characterized that word, you're saying

19 do you transact in stocks, bonds, and low-priced

20 securities, is that part of the firm's business line?

21 And I would say that that is not part of the firm's

22 business ~~only~~ all.

23 Q Why isn't it part of the firm's business

24 overall? Why isn't the low-priced securities -- the

25 trading in low-priced securities by Aegis customers part

1 Q And was that process documented anywhere?
2 A If it was an e-mail, it would be documented.
3 If I had conversations, you know, with additional people,
4 I might have put that into a document, yes.

5 Q Okay. And where would that be maintained?

6 A In a file, SharePoint file.

7 Q Okay. Thank you.

8 BY MR. BAGNALL:

9 Q Did the individuals in the branches that were
10 responsible for conducting the review-- the trade
11 activity reviews, or conducting the trade activity
12 reviews -- did they receive training on how to identify
13 suspicious activity?

14 A Yes.

15 Q When did they receive the training?

16 A The training received on an ongoing basis
17 through discussions, through operations, through the
18 centralized compliance function.

19 Q Were the individuals conducting the trade
20 activity reviews provided with examples of suspicious
21 activity that they should be on the lookout for during
22 the reviews?

23 A No.

24 Q Was there anywhere where the individuals
25 responsible for conducting the trade activity reviews

1 could look to find a set of examples of suspicious
2 activity that they should be on the lookout for?

3 A Yes.

4 Q And what were those resources?

5 A Well, there was within the system itself, the
6 Proserve system, which is an ongoing evolution, the
7 actual system, there were flags and the resources were at
8 RBC and at Aegis to discuss what those flags were, you
9 know, and if the flags were tripped or triggered, what
10 should be done with it.

11 Q Who was responsible for creating the flags in
12 the Proserve system?

13 A Those were I believe a default system.

14 Q When you say a "default system," you mean that
15 when the Proserve system was deployed at Aegis, it came
16 with flags already included in it?

17 A Correct.

18 Q Did Aegis modify those flags at all?

19 A Yes.

20 Q How did Aegis modify the flags?

21 A The modification was done to decrease false
22 positives that came up on the system.

23 Q Did Aegis add any additional flags to the
24 Proserve system that didn't come in the default?

25 A Yes, possibly -- yes, I believe so, yes.

1 Q What flags did Aegis add?

2 A There was an enhanced version that came out
3 that was rolled out through RBC and Kevin McKenna, and
4 that had an enhanced version of the actual system.

5 Q Okay. Did Aegis monitor for suspicious
6 activity in any ways other than the trade activity
7 reviews?

8 A There's -- on the work flow system, requests
9 for journaling securities or requests for wiring out
10 funds, requests for check requests, and things of that
11 nature.

12 In reviewing and processing those, there would
13 be a look-back into the account to see what activity
14 triggered the request to send out the funds or journal
15 securities or anything of that nature.

16 Q I'm sorry. Was that a manual process what you
17 just described?

18 A It was a web-based process. But it was manual
19 in a sense that to look back onto the account activity
20 system, and to look through activity and whatnot, that
21 part was -- that part was electronic but it was manual in
22 the sense that you went back and did a separate step to
23 look into the actual account.

24 Q Okay. Was there anything else?

25 A Spot checks of trade activity through the

1 supervisor in the home office.

2 Q So the person who conducted the spot checks, is
3 that person in the compliance department?

4 A That person is a supervisory person.

5 Q With compliance responsibilities?

6 A With compliance responsibilities in the sense
7 that they have a direct contact with home office
8 compliance on a daily basis.

9 Q For the purposes of conducting the spot checks,
10 were the supervisors responsible for actually the spot
11 checks, were they provided with examples of suspicious
12 activity that they should be on the lookout for?

13 A No.

14 Q Do you know -- specifically now with respect to
15 transactions in low-priced securities, were there any
16 flags in the Proserve system that monitored those sorts
17 of transactions?

18 A Yes, there were flags that did monitor those
19 transactions, yes.

20 Q What did those flags monitor for?

21 A Low-priced security transactions, securities
22 that traded \$5 and under.

23 Q Maybe you could describe for us how a flag
24 worked in the Proserve system.

25 A When a trade was transacted, a sell, let's say,

1 or a purchase, it didn't matter, a flag would be tripped
2 if a security traded under \$5 a share.

3 Q And so every single transaction for a security
4 under \$5 would be flagged in the system?

5 A Yes.

6 Q And so somebody reviewed every single
7 transaction?

8 A Yes.

9 Q What were they reviewing for?

10 A They would review to see if it was a listed
11 security or a security they traded to a market Bulletin
12 Board, that kind of thing.

13 Q Who were the individuals who conducted that
14 review?

15 A One of the hubs was 40 Wall Street. At 40 Wall
16 Street, Todd Golden and Craig Kotash.

17 Q And were Mr. Golden and Mr. Kotash provided
18 with examples of suspicious activity related to
19 low-priced securities transaction that they should be on
20 the lookout for during their review?

21 A In one of the compliance alerts I sent out as
22 part of the training, I believe I had -- I believe I had
23 three Notice to Members that actually outlined suspicious
24 activity or potential suspicious activity.

25 Q Did you disseminate that to Mr. Kotash and Mr.

1 entails?

2 Q Well, you've testified a couple of times today
3 about the different types of training that Aegis offered
4 to its employees.

5 A Uh-huh.

6 Q Any of those types of trainings, did you
7 receive any training about suspicious activity reports?

8 A I administered the training, so the Notice to
9 Members that went out. The annual compliance training,
10 that had modules in it about AML.

11 Q So I'm asking if you received, you personally,
12 received training on suspicious activity reports from
13 Aegis?

14 A No.

15 Q Do you know what circumstances require Aegis to
16 file a suspicious activity report?

17 A Yes.

18 Q What are those circumstances?

19 A There is a number of circumstances that
20 comprise potential suspicious activity.

21 MR. McCURDY: Make sure you're on the right --

22 Are you asking him for examples or are you

23 asking him --

24 MR. BAGNALL: I am asking Mr. Terracciano to

25 tell me what circumstances require Aegis to file a SAR.

1 Golden?

2 A That was disseminated to every single employee
3 at the firm.

4 Q Considering that Mr. Kotash and Mr. Golden had
5 responsibility for reviewing transactions in low-priced
6 securities, did they receive any training unique to that
7 job role that would have provided them guidance on what
8 suspicious activity they should be on the lookout for?

9 A I'm not entirely sure what you mean by that.

10 Q So did Mr. Kotash and Mr. Golden, separate from
11 training that went firm-wide, did they receive specific
12 training that would aid them in their duty to review all
13 low-priced securities transactions?

14 A No.

15 Q For example, did Mr. Kotash and Mr. Golden
16 receive specific training unique to them on what
17 suspicious activity they should be on the lookout for in
18 their review of low-priced securities transactions?

19 A No.

20 Q Did you ever -- you personally, did you ever
21 personally receive any training from Aegis with respect
22 to suspicious activity reports?

23 A I had discussions with one of the previous CCOs
24 about activity, but actual training --

25 Could you just define what training actually

1 THE WITNESS: I don't think that is the
2 question you had originally asked me.

3 MR. McCURDY: That's fine. Just answer the
4 question he just asked.

5 THE WITNESS: Could you --

6 BY MR. BAGNALL:

7 Q What circumstances require Aegis to file a SAR?

8 A When there is no doubt that there is -- that a
9 suspicious activity took place.

10 Q So the standard is when there's no doubt that a
11 suspicious activity took place?

12 A Or when it was deemed that suspicious activity
13 did in fact take place.

14 Q So is it your testimony that Aegis had a duty
15 to file a SAR when it was aware that suspicious activity
16 had taken place?

17 A When suspicious activity was detected.

18 Q Okay. And what type of suspicious activity
19 would require Aegis to file a SAR?

20 A I don't believe that there's any one type of
21 activity. I'd have to look at the whole situation and
22 review it and check documentation and come to a decision.

23 Q Can you provide some examples of suspicious
24 activity that would require Aegis to file a SAR?

25 A Are you asking me if I know of an example? I'm

1 break for lunch if that's okay with you.

2 THE WITNESS: Yeah, that's fine.

3 BY MR. BAGNALL:

4 Q During your time at Aegis, were you ever aware
5 of any suspicious activity related to low-priced
6 securities transactions?

7 A Yes.

8 Q What was the suspicious activity that you were
9 aware of?

10 A I would just like to clarify. I would -- or
11 the department would get -- it would come to maybe 810
12 compliance or maybe sometimes it would be sent to the
13 individual in the compliance department, myself or the
14 CEO or whoever was there at the time -- activity would
15 come or a notice of activity would come from RBC.

16 Q Okay. Were there other -- let me think about
17 the right way to say this.

18 Other than communications from RBC, were you
19 aware of any suspicious activity related to low-priced
20 securities at Aegis?

21 A No, not that was brought to my attention.

22 Q Did any Aegis employees ever report to you any
23 suspicious activity that they had observed in connection
24 with low-priced securities transactions?

25 A On occasion. Yes.

1 And that request would generally -- that would
2 be directed to our operations department and start
3 vetting it that way.

4 If the person gave -- if the registered rep
5 gave the name of the security to the compliance
6 department or to myself, I would -- or the department
7 itself would do a review of that actual security. They
8 would call up on different OTC, maybe trading databases
9 and things like that, and see if there was scull and
10 crossbones, or whatever the case may be, anything that
11 could come up that would be a warning.

12 And that would also be a way to detect activity
13 in person.

14 Q So did that actually happen? Through that
15 review, you became aware of suspicious activity related
16 to a low-priced securities transaction?

17 A I became aware of requests that came to either
18 myself or to the compliance area, or to the operations
19 area, to deposit securities.

20 Q And that was indicative of suspicious activity?

21 A Not necessarily, no.

22 Q So what I was asking you all the methods by
23 which you became aware of suspicious activity at Aegis
24 that was related to transactions in low-priced
25 securities.

1 Q And so with that in mind, is there now two sort
2 of types of -- in addition then, is it fair to say that
3 in addition to communications with RBC, you also became
4 aware of suspicious activity related to low-priced
5 securities from reports from Aegis employees?

6 A Correct.

7 Q Other than those two instances, communications
8 with RBC or reports from Aegis employees, were there any
9 other instances through which you became aware of
10 suspicious activity related to low-priced securities
11 transactions at Aegis?

12 MR. McCURDY: Any other instances, or any other
13 methods?

14 MR. BAGNALL: Methods. Thank you.

15 THE WITNESS: Yes.

16 BY MR. BAGNALL:

17 Q What were they?

18 A There's the direct method. The direct method

19 --

20 Q What do you mean by the "direct method"?

21 A The direct method would be a registered rep
22 would come to the compliance office and say, "I have a
23 client that is a founder of a company and they would like
24 to deposit some shares, to trade those shares
25 eventually."

1 So you mentioned the communications with RBC.
2 You mentioned the reports from Aegis employees.

3 A Right.

4 Q And then you were just describing the third
5 method.

6 A Right.

7 Q So through that direct method, there were times
8 when you identified suspicious activity related to
9 low-priced securities?

10 A There were times when that was one of the
11 factors in an analysis if activity could be suspicious.
12 As I said earlier, if the rep wanted to deposit a
13 security from founder stock, from a CEO or an
14 entrepreneur that started a company. They held that
15 stock for a number of years and now they were looking to,
16 you know, sell that stock.

17 I could do a precursor review of that security
18 and determine if that security should be deposited or not
19 into the account.

20 Q At any time during your employment at Aegis,
21 when you were conducting the direct method that you just
22 testified to, did you ever become aware of suspicious
23 activity related to a low-priced security transaction?

24 It's just yes or no.

25 A I'm not entirely sure. I'd like you to clarify

1 through.

2 Q Did you tell anyone at Aegis why you were

3 leaving?

4 A No.

5 Q Who did you tell that you were leaving?

6 A I told George Kott.

7 Q And what did you tell him?

8 A I told George I had a better opportunity and

9 I'm leaving.

10 Q So you never told anybody at Aegis that a part

11 of the reason you were leaving was because of the lack of

12 resources in the compliance department?

13 A No, no.

14 MR. BAGNALL: Would you mark this next please.

15 (SEC Exhibit No. 28 was marked

16 for identification.)

17 BY MR. BAGNALL:

18 Q Can you take a look at that please and let me

19 know when you're done?

20 A Yes.

21 (The witness reviewed the document.)

22 A Okay.

23 Q Do you recognize this document?

24 A Yes, I do.

25 Q What is it?

1 A It's a -- the document starts from a request

2 from RBC compliance to Sam Guidetti, at that time the

3 CCO, and to Kevin McKenna.

4 Q And who is Michael Heiser?

5 A Michael Heiser is a compliance officer that

6 covers correspondence.

7 Q Sorry. Who is he a compliance officer for?

8 A For RBC.

9 Q Okay. And at the time, November 1, 2013, what

10 role did Mr. McKenna serve at Aegis?

11 A At that time Kevin had transitioned to

12 operations.

13 Q And who is Nicholas DeGidio?

14 A Nick DeGidio is -- I don't know his actual

15 title but he's another employee of RBC.

16 Q Okay. And do you know why Mr. McKenna

17 forwarded you Mr. Heiser's e-mail?

18 A No, no.

19 Q On November 1, 2013, what roles were you

20 serving at Aegis?

21 A Director of compliance and AML officer.

22 Q You were the AML CO at the time?

23 A Right.

24 Q When you received the e-mail, the forward from

25 Mr. McKenna, what responsibility did you have with

1 respect to the e-mail?

2 A To gather information.

3 Q Anything else?

4 A To speak with the individuals involved, to

5 verify information within the e-mail, and to follow up

6 with discussions with Michael Heiser.

7 Q Did you recognize any AML red flags in this

8 e-mail?

9 A I see potential red flags, yes.

10 Q Did you recognize them at the time you received

11 it?

12 A Yes.

13 Q What red flags did you recognize?

14 A Right here -- it starts at the top, "As of

15 7/29/13, the company reported shares outstanding and sold

16 more shares than they reported outstanding."

17 Q Anything else?

18 A Yes. There's a number of issues here that are

19 questionable.

20 Q If you focus specifically on the bottom of the

21 first page -- and I should point out to you, Mr.

22 Terracciano, do you see on the bottom right-hand corner

23 of the page, there's a marking "SEC-Aegis-E" and then a

24 string of numbers?

25 A Right.

1 Q That's called the Bates stamp. And so just for

2 ease of our discussion, when I'm talking about a

3 particular page, I'll refer to the last three numbers of

4 the Bates stamp.

5 A Okay.

6 Q So on the first page of Exhibit 28, the page

7 ending 094, do you see at the bottom, the third bullet

8 from the bottom, [REDACTED]?

9 A Yes.

10 Q Do you see any AML red flags in the two bullets

11 that follow the [REDACTED]?

12 A Yes.

13 Q What red flags do you see?

14 A "The company reported 231.7 million shares

15 outstanding. They sold 31 percent of the outstanding

16 shares." And then it goes on to talk about the average

17 daily volume.

18 Q Okay. Does the average daily volume bullet

19 also include AML red flags?

20 A Yes.

21 Q Or is it multiple red flags or just one?

22 A No, there's multiple red flags.

23 Q All right. Are there any bullets on either

24 page 094 or 095 that aren't an AML red flag?

25 A No. They are all -- I would all consider them

1 a red flag.

2 Q When you received this e-mail, did you consider
3 filing a SAR?

4 A First I gathered the facts of the --

5 MR. McCURDY: That's a yes or no.

6 THE WITNESS: No.

7 BY MR. BAGNALL:

8 Q Why not?

9 A This is a snapshot of information. This
10 information needs to be vetted and verified.

11 Q Okay. At any time after you received this
12 e-mail, did you consider filing a SAR?

13 A Yes.

14 Q When?

15 A Some of the information I believe at the time
16 was inconsistent.

17 MR. McCURDY: He's asking when.

18 THE WITNESS: Oh, when? I don't know -- I
19 don't know that.

20 BY MR. BAGNALL:

21 Q Did you take some steps after receiving this
22 e-mail before you considered whether you should file a
23 SAR?

24 A Yes.

25 Q What steps did you take?

1 A I believe I just outlined those. I gathered
2 the facts. For example, reached out to the reps that
3 covered the account. Pulled out documentation from RBC.
4 That's in the postage system. Had conversations with
5 RBC, with the reps, with Kevin McKenna, that I believe at
6 that time prepared the documentation for the
7 certificates.

8 Q And after you completed those steps, you
9 considered whether to file a SAR?

10 A Yes.

11 Q Did anybody else take part in that
12 consideration?

13 A Sam Guidetti and Kevin McKenna.

14 Q Did you ultimately decide to file a SAR?

15 A I don't know if I actually filed on this one.

16 Q Did you record the deliberative process that
17 you undertook for whether or not you should file a SAR
18 for this e-mail?

19 A Yes. Yes.

20 Q Where did you record it?

21 A In an e-mail back to Michael Heiser.

22 Q You drafted an e-mail to Michael Heiser?

23 A That was -- I believe the e-mail was drafted by
24 a number of -- pulling together all different
25 information, either I sent it or it was sent by someone

1 else. I don't remember exactly.

2 Q Sorry. And that e-mail that you just testified
3 to would memorialize the deliberative process you
4 undertook as to whether or not you would file a SAR for
5 the information contained in this e-mail?

6 A It would answer the facts. It would answer the
7 questions too. We would supply facts to the questions
8 answered.

9 Q How is that a memorialization of the
10 deliberative process over whether you would file a SAR
11 describing the content of this e-mail?

12 A That was a subsequent discussion with Michael
13 Heiser also.

14 Q So you discussed with Michael Heiser whether
15 Aegis would file a SAR on this, on the content of this
16 e-mail?

17 A Well, we discussed the actual information,
18 whether it was -- where this information came from. In
19 some instances previous or during the time that these
20 were sent over, sometimes the information would not be
21 totally factual. It might represent different
22 individuals or different circumstances.

23 So there would be discussion about what we
24 found and what we -- what Mike had thought of the
25 information also. Because he would have to go present

1 that to his AML department.

2 Q It sounds -- and correct me if I'm wrong -- but
3 it sounds like what you are describing is the
4 investigation that you did into answering the questions
5 that RBC presented to you, is that correct?

6 A Yes, correct.

7 Q And then conversations or communications with
8 Mr. Heiser about the results of that investigation, is
9 that right?

10 A Yes, correct.

11 Q I am asking you -- trying to ask you something
12 different. I am trying to ask you whether you documented
13 the deliberative process that you undertook about whether
14 you would file a SAR on the content of this e-mail on
15 Exhibit 28.

16 A No, I did not document the deliberative
17 process.

18 Q Did you ever document the deliberative process
19 of whether or not you would file a SAR other than with
20 respect to Exhibit 28?

21 A I can't say. I don't -- every circumstance
22 would be different.

23 Q Okay. Did you discover anything in your
24 investigation into the facts outlined in Exhibit 28 that
25 led you to conclude that you did not -- that Aegis did

1 not need to file a SAR?
 2 A It was multiple documentation outlining --
 3 multiple documentation outlining in the enhanced
 4 procedure completed that led me to believe that that
 5 sufficed as far as an explanation of what occurred in my
 6 conversation when I went back in addition to Mike Heiser.

7 Q I'm not sure I understood that, Mr.
 8 Terracciano.

9 Could I ask it again --

10 A Yeah, sure.

11 Q -- to make sure we're on the same page.

12 Did you find anything in the investigation that
 13 was conducted into the content of the e-mail in Exhibit
 14 28 that led you to determine that you did not need to file a
 15 SAR on behalf of Aegis?

16 A I cannot remember at that time.

17 Q Okay. Do you know the customer [REDACTED]?

18 A No.

19 MR. BAGNALL: Anybody?

20 Okay. I'll take back Exhibit 28.

21 BY MR. BAGNALL:

22 Q I am going to band you what's been previously
 23 marked as Exhibit 16.

24 Could you let me know when you've had an
 25 opportunity to review it?

1 (The witness reviewed the document.)

2 A Okay.

3 Q Do you recognize this document, Mr.
 4 Terracciano?

5 A No.

6 Q Do you agree that it appears to be a
 7 continuation of the thread that we just looked at in
 8 Exhibit 28?

9 A Yes, I do.

10 Q Okay. Do you have any reason to believe -- do
 11 you see also that the second e-mail down from the top on
 12 the first page of Exhibit 16, page 112, there's an e-mail
 13 at November 4, 2013, at 4:39 p.m., from Mr. Guidetti to
 14 Mr. McKenna, cc'ing Ms. Capara and you.

15 Do you see that?

16 A Uh-huh.

17 Q Do you have any reason to believe that you
 18 didn't receive that e-mail?

19 A No.

20 Q In the most recent e-mail in the thread, at the
 21 very top of the same page, do you see that that's an
 22 e-mail from Mr. McKenna to Mr. Guidetti, cc'ing Ms.
 23 Capara and you.

24 Do you see that?

25 A Yes, I do.

1 Q Do you have any reason to believe that you
 2 didn't receive that e-mail?

3 A No.

4 Q Directing you to the content of the second
 5 e-mail from the top that Mr. Guidetti wrote, "Kevin,
 6 please see us when you get in tomorrow morning."

7 Did Mr. McKenna come and -- let me back up.

8 Do you know who Mr. Guidetti was referring to
 9 when he wrote, "see us"?

10 A No.

11 Q After this e-mail in the November 4, 2013, time
 12 frame, did Mr. McKenna come and see you and Mr. Guidetti
 13 and Ms. Capara about the [REDACTED] inquiry from RBC?

14 A Yes.

15 Q When did he come to see you?

16 A I don't know.

17 Q Did you have an in-person meeting about the [REDACTED]
 18 [REDACTED] inquiry from RBC?

19 A I'm not sure. Could you state that again?

20 Q Yes. I asked you if Mr. McKenna came to see
 21 you and Mr. Guidetti and Ms. Capara after this November
 22 4th time frame about the [REDACTED] inquiry from
 23 RBC?

24 A Yes, he did.

25 Q Okay. Did you have an in-person meeting with

1 Mr. McKenna?

2 A Yes.

3 Q What did you discuss at the in-person meeting?

4 A We discussed the facts surrounding the issues
 5 within the e-mail, the documentation that was supplied by
 6 operations, and that was within the compliance -- excuse
 7 me, within RBC postage.

8 Q Why was Mr. McKenna involved in the meeting?

9 A Mr. McKenna was the point person for -- or the
 10 employee that was involved in the initiation process of
 11 anything to do with requests for certificates or --

12 Q Okay. Did that meeting with Mr. McKenna
 13 include a discussion as to whether or not a SAR needed to
 14 be filed?

15 A I don't remember that.

16 Q Is there anything else about the discussion
 17 with Mr. McKenna that you haven't already testified to?

18 A I do happen to remember that I had stated that
 19 this type of account stretches the bandwidth of
 20 compliance, and that was also -- that was also agreed up
 21 by Sam. We had stretched our bandwidth and we just don't
 22 have the -- we just don't have the time to do all of the
 23 surveillance behind these accounts.

24 And I think at the time Mike Heiser was asking
 25 us how we would be comfortable with the account.

1 Q Okay.

2 MR. BAGNALL: Anybody else?

3 I'll take it back.

4 BY MR. BAGNALL:

5 Q I'm going to hand you what's been previously

6 marked as Exhibit 22.

7 Take a look at it please and let me know when

8 you've had an opportunity to do so, Mr. Terracciano.

9 And as you are looking at it, I'll represent to

10 you that you don't appear to be a recipient or a sender

11 of any of the e-mails included, okay.

12 A Right.

13 (The witness reviewed the document.)

14 A Okay.

15 Q So if I could direct your attention to the

16 middle of the first page of Exhibit 22, the page ending

17 680, do you see the e-mail from Mr. Heiser to Jennifer

18 McGeary, Brittany Mathias and cc'ing Samuel Guidetti.

19 A Right.

20 Q Do you see in the body of that e-mail, it says,

21 "Sam Guidetti and Eugene Terracciano, of Aegis

22 compliance, called me in response to the concerns listed

23 below about five minutes ago."

24 Do you see that?

25 A Uh-huh.

1 Q Do you recall in the November 5, 2013, time

2 frame having a call with Mr. Guidetti and RBC about the

3 [REDACTED] account?

4 A No.

5 Q If you read the second paragraph there, "Per

6 Sam and Eugene, the account predates them. Based on our

7 concerns, they reviewed the account activity, account

8 opening paperwork, spoke to the rep, et cetera.

9 "Based on that review and the concerns brought

10 to their attention by RBC, Aegis will be closing the

11 account."

12 Does that jog your memory as to whether you had

13 a conversation, a telephone call, with Mr. Heiser about

14 the [REDACTED] account?

15 A We had many conversations --

16 MR. McCURDY: It's a yes or no.

17 THE WITNESS: No, no.

18 BY MR. BAGNALL:

19 Q Okay. So let me ask you --

20 A Sure.

21 Q Does that jog your memory as to whether or not

22 Aegis closed the [REDACTED] account?

23 A It says "Aegis will be closing the account."

24 Q Right. What I'm asking is, after reading that,

25 does it prompt you to remember whether the [REDACTED]

1 account was actually closed?

2 A No.

3 Q Okay. Let me give you this back.

4 Assume for a moment that the account was indeed

5 closed, okay.

6 Does closing the account substitute for filing

7 a SAR?

8 A No.

9 Q Do you know what concerns -- strike that. I'll

10 take it back.

11 BY MS. ZERNES:

12 Q If there was an AML concern and an account was

13 closed, who ultimately had final authority to close the

14 account?

15 A Compliance.

16 Q If the sales side wanted to keep it open and

17 compliance did not, was there an arbitration process?

18 MR. McCURDY: Did you say sell side? You mean

19 the salespeople?

20 BY MS. ZERNES:

21 Q Excuse me. The account representation.

22 A No.

23 Q Who physically closed the account?

24 A A GSR, which is an administrative wire would be

25 sent from operations to close the account.

1 Q Okay. Were there any instances in which there

2 was debate on account closure outside of compliance?

3 A Yes.

4 Q And can you describe these situations?

5 A Yes.

6 Q Will you please describe the situation?

7 A Yes, I will. Yes, I will.

8 MR. McCURDY: So just to be clear, when you are

9 saying outside of compliance, in which he participated?

10 MS. ZERNES: Correct.

11 MR. McCURDY: Okay.

12 THE WITNESS: There were instances where we

13 mandated an account be closed. The reps would go to

14 senior management and make a case to keep the account

15 open.

16 BY MS. ZERNES:

17 Q Uh-huh. And at that point, there is still a

18 question, so the reps have gone to management. They

19 said, "We don't want to close the account." Compliance

20 says, "Yes, there are AML concerns."

21 What happens next?

22 A There would be a further discussion at that

23 time. If Sam was there as the CCO, we would both be

24 brought in to Bob's office to discuss the issues and why

25 we believed the account should be closed out.

1t closed as well."t
 2 Do you see that?
 3 A Yes.
 4 Q What, if any, responsibilities did you have
 5 with respect to this e-mail?
 6 A The responsibility was to follow up with
 7 conversations at the branch level. Standard procedure to
 8 contact the branch manager, the rep, the compliance
 9 coverage at the branch level, and, you know, discuss the
 10 activity and how the account is conducted or operates.
 11 Q Okay. Do you identify any AML red flags in the
 12 e-mail from Mr. DeGidio sent December 2, 2013? The one
 13 that I just read through, the one on the page ending 794.
 14 A Yes. He lists -- starting from [REDACTED] down to
 15 [REDACTED]
 16 Q So you are saying the three paragraphs that
 17 follow the colon?
 18 A Yes.
 19 Q Okay. What AML red flags do you see?
 20 A In this snapshot, I see "pump and dump" first
 21 off. Stock promotion and trading volume increases. And
 22 then a drop in the price and volume.
 23 Q Did you consider filing a SAR on the content of
 24 the information in Exhibit 29?
 25 A I don't remember the exact circumstance behind

1t that at that time.t
 2 Q So that's a no?
 3 A I'm just saying I don't remember the exact
 4 circumstance behind that time.
 5 Q So you don't recall whether you --
 6 A I don't recall.
 7 Q Sorry, let me finish the question.
 8 You don't recall whether you considered filing
 9 a SAR?
 10 A Yes, I don't.
 11 Q Okay. Does the content of the e-mail that Mr.
 12 DeGidio sent December 2nd on its face provide a reason to
 13 suspect that illegal activity had been occurring through
 14 Aegis?
 15 A The activity is concerning, what he wrote here,
 16 and would be investigated.
 17 Q That's not what I asked you. I asked if the
 18 information in this e-mail, on its face, gave Aegis a
 19 reason to suspect that illegal activity had occurred
 20 through the firm?
 21 A Correct.
 22 Q Yes?
 23 A Yes.
 24 Q Okay. Do you specifically remember conducting
 25 the investigative steps you just testified to a moment

1 ago for this e-mail?
 2 A No, I don't.
 3t Q Can you flip the page one forward to the page
 4 ending 793...
 5 A Uh-huh.
 6 Q The very bottom of that page, an e-mail from
 7 Eugene Terracciano to Mr. DeGidio, 810 Compliance, Mr.
 8 Kott, Mr. McKenna and Mr. Ferri.
 9 Do you see that?
 10 A Uh-huh.
 11 Q Who is Mr. Ferri? Who is David Ferri, sorry?
 12 A Yes. Dave Ferri is the branch manager of
 13 Maitland office.
 14 Q So do you see what time you sent that e-mail?
 15 A December 2, 2013, at 3:04 p.m.
 16 Q Okay. Flip back one page. The page ending
 17 794.
 18 A Uh-huh.
 19 Q What time did Mr. DeGidio send his inquiry to
 20 you?
 21 Excuse me. To 810 Compliance.
 22 A December 2, 2013, at 2:40 p.m.
 23 Q How much time passed between the time Mr.
 24 DeGidio sent his e-mail and the time you sent your
 25 e-mail?

1 A A little over 20 minutes.
 2 Q Is that enough time to complete the
 3 investigation that you just described a moment ago?
 4 A Yes, yes.
 5 Q So you could conduct an investigation into this
 6 e-mail in 24 minutes?
 7 A Yes.
 8 Q How is that possible?
 9 A By looking at different websites, collecting
 10 the information, news stories, promotion "pump and dump"
 11 is a simple Google search. In name changes --
 12 Q Well, one of the things you mentioned I think
 13 --
 14 MR. McCURDY: Let him finish his answer.
 15 THE WITNESS: I'm not done.
 16 MR. BAGNALL: I'm sorry. I thought you were
 17 done.
 18 THE WITNESS: Yeah. There's name changes that
 19 are easily -- a Google search. I searched [REDACTED]
 20 [REDACTED] and [REDACTED] Those were both closed in
 21 August.
 22 So Kevin McKenna was probably -- since he's on
 23 here, he was probably consulted as to what that activity
 24 was at that time.
 25 That is a quick way of finding out what

1 actually transpired.
 2 BY MR. BAGNALL:
 3 Q Okay. And what about contacting the registered
 4 rep?
 5 A Yes.
 6 Q That could have happened in that amount of time
 7 as well?
 8 A Absolutely.
 9 Q Okay. What about gathering and reviewing
 10 trading data?
 11 A That's all on Proserve.
 12 Q So all of those things you mentioned, including
 13 gathering trading data, talking to the rep, that could
 14 all be done in 24 minutes?
 15 A Yes.
 16 Q Okay. Is that typically how long it took the
 17 compliance department to conduct the investigations into
 18 the inquiries it received from RBC?
 19 A No.
 20 Q How long did the investigations typically take?
 21 A Each one is different.
 22 Q I'm asking you about how long they typically
 23 took.
 24 A You are talking about an average?
 25 Q Sure, yes.

1 MR. McCURDY: So that's a different question.
 2 You said "average" or "typical"? Which one do
 3 you want?
 4 MR. BAGNALL: Let's start with typical.
 5 MR. McCURDY: And he said there isn't a
 6 typical.
 7 BY MR. BAGNALL:
 8 Q Okay. So what's the average?
 9 Well, let me back up.
 10 You agree there's no typical.
 11 A No.
 12 Q What would you say is the average amount of
 13 time it takes to complete an investigation into an RBC
 14 inquiry?
 15 A A number of days.
 16 Q Okay. How out of the ordinary would it be to
 17 complete an investigation in 24 minutes?
 18 A It is out of the ordinary.
 19 Q Okay. Is it possible that no investigation was
 20 conducted and you just instructed that the account be
 21 closed without an investigation?
 22 A No.
 23 Q It's not possible?
 24 A No. It's not possible.
 25 Q Where would the investigation into the [REDACTED]

1 [REDACTED] trading in [REDACTED] where would
 2 that investigation be documented?
 3 A That would be documented in SharePoint.
 4 Q Okay. So reading up the chain -- sorry, are
 5 you still on the second page ending 793?
 6 A 793, yeah.
 7 Q Okay. Do you see, after your e-mail from 3:04
 8 p.m., there's an e-mail from Mr. McKenna at 5:41 p.m.,
 9 that same day, asking Teressa Fiorucci to close the
 10 accounts?
 11 A Uh-huh. Right.
 12 Q Okay. And right above that, Ms. Fiorucci
 13 responds, "One of the accounts, the account ending 28349,
 14 has trades from the day prior."
 15 Do you see that? Ms. Fiorucci responded on
 16 December 3rd, so she points out that there were trades
 17 from December 2nd. Do you see that?
 18 A I'm sorry.
 19 MR. BAGNALL: Let the record reflect I am
 20 pointing to the exhibit in front of Mr. Terracciano.
 21 Do you see that?
 22 THE WITNESS: Okay. I see it now, yes.
 23 BY MR. BAGNALL:
 24 Q Okay. And then you responded to Ms. Fiorucci
 25 -- what is that -- 16 minutes later saying, "Did they

1 traded listed stock?"
 2 Do you see that?
 3 A Uh-huh, yes.
 4 Q Why did you ask her if [REDACTED] had traded
 5 listed stock?
 6 A I don't remember -- I don't remember now.
 7 Q Can you look at the next e-mail up in the
 8 thread, which actually starts on the first page of the
 9 exhibit, the page ending 792? It says, "Below are the
 10 trades." And then there's a table.
 11 Do you see that?
 12 A Uh-huh. Right.
 13 Q Do you recognize the issuers that are included
 14 in the table?
 15 A No, I do not recognize them all. No.
 16 Q Okay. Do you know whether the issuers included
 17 in the trade are listed stocks?
 18 A No, I'd have to do further research on that. I
 19 wouldn't know.
 20 Q All right. Do you see that the next e-mail up
 21 in the thread from Mr. McKenna? "Didn't compliance
 22 request this account to be closed?" On the first page,
 23 Mr. Terracciano. The page ending 792.
 24 A Yes, I see it, yes.
 25 Q And then you responded to Mr. McKenna saying,

1 "Please block the account for sales only and close the
2 account. Dave Ferri said the accounts were only trading
3 in listed securities. Obviously not true."
4 Do you see that?
5 A Yes, I do.
6 Q Does that refresh your recollection as to
7 whether Mr. Ferri asserted to you that the account was
8 not trading in anything other than listed securities?
9 A It refreshes my memory just by looking at this, it
10 refreshes my memory to their -- I had a prior
11 conversation with Mr. Ferri about the accounts and
12 whether or not -- what the trading activity was or was
13 not. And he said, "Oh, they are trading listed
14 securities."
15 Q Okay. But that wasn't true?
16 A That was not true.
17 Q So does that refresh your recollection as to
18 whether the issuers that are included in the table on
19 this exhibit are listed securities?
20 A I would have to do further research. No.
21 Q So when you wrote, "Obviously not true," were
22 you referring to some securities other than those
23 included in the table on this exhibit?
24 A I don't recall from this time period.
25 Q Okay. The most recent e-mail in the thread,

1 the first e-mail at the very top of the page, "George" --
2 this is from you, December 3, 2013, do you see that?
3 A Uh-huh.
4 Q "George, the accounts will be blocked for sales
5 only and close the account. We do not have the bandwidth
6 to monitor. Thank you."
7 Do you see that?
8 A Yes.
9 Q So when you write, "We do not have the
10 bandwidth to monitor," what do you mean when you -- what
11 did you mean when you wrote that?
12 A Reading this -- reading the e-mail now,
13 obviously there was a statement made from Dave Ferri that
14 this account was only going to be trading listed
15 securities.
16 That proved not correct. When Dave Ferri, the
17 branch manager in Maitland, Florida, was interviewed, he
18 did not tell me the truth, right?
19 So that's why the account would be blocked and
20 closed.
21 Q Did Mr. Ferri suffer any consequences for not
22 telling you the truth in an interview?
23 A What do you mean by "consequences"?
24 Q Was he reprimanded?
25 A I did not reprimand him.

1 Q Was he disciplined?
2 A That I don't know.
3 Q You said that you did not reprimand him.
4 Do you know if someone else at Aegis
5 reprimanded Mr. Ferri?
6 A I don't know that.
7 BY MR. MAHER:
8 Q Did you ask that he be reprimanded?
9 A In this case --
10 MR. McCURDY: It's a yes or no.
11 THE WITNESS: This case, no.
12 BY MR. MAHER:
13 Q I'm sorry. You said, "In this case, no."
14 Were there other situations where you felt Mr.
15 Ferri misled you?
16 A Excuse me.
17 Q Were there other situations in which you felt
18 Mr. Ferri misled you?
19 A Oh, no, absolutely not.
20 Q Okay. Were there other interactions you had
21 with Mr. Ferri?
22 A Yes, just phone interactions, yes.
23 Q Okay. And is it your recollection that this is
24 the only situation in which you felt he told you
25 something that was not true?

1 A Correct, yes.
2 BY MR. BAGNALL:
3 Q So when Mr. Maher asked you if you requested
4 that Mr. Ferri be reprimanded, you said, "Not in this
5 case."
6 Where there other cases when you requested that
7 Mr. Ferri be reprimanded?
8 A Absolutely not.
9 Q Okay. When we first started talking about this
10 exhibit, I asked you if it was problematic that somebody
11 had asserted to you that an account had been blocked for
12 trading other than in listed securities, and you
13 testified that it wasn't problematic.
14 After reading it more closely, do you still
15 agree with that statement?
16 A This is a snapshot of activity, and of e-mail
17 activity and correspondence. A full analysis would need
18 to be done. It's not -- it's not -- it's not, you know,
19 easy for me to quickly say yes or no. So I would need
20 to, you know, look into it further.
21 Q So there are instances when an employee of the
22 firm made a misrepresentation to you that are not
23 problematic?
24 A That would always be problematic.
25 Q Okay. So isn't this problematic? Isn't the

1 content of Exhibit 39 problematic?
 2 A I'd like to clarify that.
 3 Q Please. Please do.
 4 A Yes. Okay. Mr. Ferri made a statement to me.
 5 That statement did not hold true. I never had a problem
 6 with Mr. Ferri in the past. There was no reason for me
 7 or maybe the firm - I can't say on behalf of the firm -
 8 but there's no reason to actually reprimand the person at
 9 this time.
 10 To look at this and to try to piece back all of
 11 the activities based upon a snapshot from 2013 is quite
 12 difficult.
 13 BY MR. MAHER:
 14 Q Mr. Terracciano, you received an e-mail in
 15 which RBC raised the threat of criminal misconduct. In
 16 the course of investigating the e-mail, you were lied to
 17 by Mr. Ferri.
 18 That didn't raise any serious concerns to you?
 19 MR. McCURDY: There's no evidence that he was
 20 lied to.
 21 MR. MAHER: Didn't he just testify -
 22 MR. McCURDY: He said there was information
 23 which turned out to be not true.
 24 MR. MAHER: That's not evidence that he was
 25 lied to?

1 MR. McCURDY: Absolutely not. People can be
 2 wrong. Just like that question is wrong.
 3 BY MR. MAHER:
 4 Q So the information Mr. Ferri provided you
 5 turned out not to be true.
 6 In the course of you investigating a clear
 7 threat of criminal misconduct and conducted through
 8 Aegis, it didn't raise any -
 9 MR. McCURDY: Where is the language about a
 10 threat of criminal misconduct?
 11 MR. MAHER: Isn't a "pump and dump" scheme
 12 another word for criminal misconduct?
 13 MS. CLARKE: "Exhibited characteristics -"
 14 MR. McCURDY: But there's no question. What's
 15 the question?
 16 BY MR. BAGNALL:
 17 Q Mr. Terracciano, is a "pump and dump" market
 18 manipulation criminal activity?
 19 A In and of itself -
 20 MR. McCURDY: It's a yes or no.
 21 THE WITNESS: Yes.
 22 BY MR. BAGNALL:
 23 Q Okay. Thank you. And so in the course of
 24 investigating something that exhibited the
 25 characteristics commonly associated with a "pump and

1 dump" scheme, which you understood to be criminal
 2 activity, you were misled by Mr. Ferri, correct?
 3 A Correct.
 4 Q -Okay. And that didn't raise any serious
 5 concerns for you?
 6 A Oh, it absolutely raised concerns for me. And
 7 the fact that this says, "exhibited characteristics of
 8 pump and dump," I'm not entirely sure what that really
 9 means.
 10 And there were cases when I would go back to
 11 Mike Heiser and Nick DeGidio to get further clarification
 12 on that, they would say, "Oh, that's something my AML
 13 department gave me. I'll try to find out," and then I
 14 would never - I wouldn't hear back from them.
 15 Q Okay. And while you didn't ask that Mr. Ferri
 16 to be reprimanded in this situation, did you have any
 17 subsequent conversations with him regarding the
 18 information he provided you?
 19 A Could you state that again? I'm sorry.
 20 Q I said even though in this particular case you
 21 did not ask that Mr. Ferri be reprimanded, did you have
 22 any conversations with Mr. Ferri subsequent to this
 23 regarding the information he provided you?
 24 A I had subsequent conversations with Mr. Ferri
 25 about being careful of what he tells me and what he says

1 he's going to enforce.
 2 Q And what did he say in response?
 3 A He said, "I apologize greatly. I will in the
 4 future make every effort to comply with what you tell
 5 me."
 6 Q Did he explain to you how he came to provide
 7 you incorrect information?
 8 A I'm not sure what that means.
 9 Q Did he tell you how he got it wrong?
 10 A No.
 11 Q Did you ask him?
 12 A Yes, I did.
 13 Q And he did not tell you?
 14 A It wasn't substantial. It was not substantial
 15 what he told me.
 16 Q Can you explain what you mean by "substantial"?
 17 A Substantial meaning he was not monitoring -- he
 18 was not monitoring the account himself directly on an
 19 every-single-transaction basis.
 20 Q Wasn't he required to do that as the branch
 21 manager?
 22 A He was -- yes, as the branch manager, that was
 23 one of my subsequent conversations with him, that he had
 24 the responsibility to uphold that procedure.
 25 Q Doesn't that fact make the matter worse here?

1 So now you've received an e-mail that describes trading
2 through the firm that exhibits the characteristics of
3 criminal activity.

4 Mr. Ferri told you information that turned out
5 to be inaccurate. And when you spoke to him about it
6 further, you learned that he wasn't doing the things that
7 he was supposed to be doing by way of monitoring the
8 trades, correct?

9 A The trades - right, correct.

10 Q So doesn't that make matters worse?

11 A In this little snapshot, I would say - I would
12 say it does not necessarily make matters worse because in
13 my subsequent conversations with him, the trading
14 activity was monitored from another location, from 40
15 Wall Street.

16 Q That's besides the point, isn't it? Mr. Ferri
17 himself had a personal obligation to monitor that
18 trading, correct?

19 A Right, right.

20 Q And he did not do it, right?

21 A Yes, that's correct.

22 Q So he just got lucky that 40 Wall happened to
23 be monitoring it too, right?

24 A Right.

25 Q So that makes matters worse, doesn't it?

1 A Yes. What number is that? I'm sorry.

2 Q Ending 792.

3 A Okay.

4 Q Of Exhibit 29. I just want to go back to the...
5 "We do not have the bandwidth to monitor."

6 Do you see that?

7 A Yes.

8 Q Why were you telling that to Mr. Kott and Mr.
9 McKenna?

10 A They are senior members of Aegis Capital Corp.

11a Q Okay. So does that mean that you didn't
12 monitor the account before December 3, 2013?

13 A No, that does not mean that.

14 Q So does it mean that you're no longer going to
15 monitor?

16 A No, it does not mean that either.

17 Q What does it mean then?

18 A No, it just means that there was not enough -
19 there was not enough - there was not enough - we were
20 stretched quite thin and there was not enough resources
21 to monitor an account on a daily basis, and keep an
22 override on it.

23 Q So does that mean that you did monitor it? Did
24 you monitor it before December 3, 2013? And when I say
25 "it," I mean did you monitor [REDACTED]

1 A Yes.

2 Q Okay. What, if anything, did Mr. Ferri say
3 about the trading that [REDACTED] engaged in in [REDACTED]
4 [REDACTED] that exhibited these characteristics of a
5 "pump and dump"?

6 A I don't remember that - I don't remember that
7 exact specific response.

8 Q Did you ask him about it?

9 A I asked him about every single one of these
10 points.

11 Q But you don't recall his responses?

12 A I don't recall the responses.

13 I'd like - can I just say one official thing?

14 Q Yes, absolutely. Please do.

15 A We never had a problem with Mr. Ferri
16 personally with upholding what he said he would do and
17 whatnot, so this was a situation where he didn't have a
18 repeat - he didn't have a second violation. This was
19 the first time it was actually caught.

20 Q So you're not aware of Mr. Ferri having other
21 issues for the clients that he was responsible for in the
22 Maitland, Florida, branch?

23 A To my knowledge, no.

24 Q Can you turn back to the first page of this
25 exhibit please, Mr. Terracciano?

1 [REDACTED] accounts before
2 December 3, 2013?

3 A Are you asking did I monitor it?

4 Q Yes.

5 A Did I? No, I did not monitor it myself, no.

6 Q Did the compliance department monitor it?

7 A The branch compliance monitored the account.

8 Q That's Mr. Ferri?

9 A No. That's Todd Golden, 40 Wall Street.

10 Q Okay. So when you said, "We do not have the
11 bandwidth to monitor," does that mean you're not going to
12 monitor it going forward?

13 Let me ask that -

14 MR. McCURDY: It says the account is closed.

15 The first part of this e-mail says, "Close the account."

16 So I just want to make sure -

17 THE WITNESS: Yes. That's correct.

18 MR. BAGNALL: The first part of the e-mail is
19 RBC asking for the account to be closed, right?

20 MR. McCURDY: No, the first part of the e-mail
21 that you're referring to says, "The account will be
22 blocked for sales only and close the account."

23 BY MR. BAGNALL:

24 Q But that means at this moment, it is not
25 closed, correct?

1 occurring in the account?
 2 A Yes.
 3 Q And what did they say?
 4 A This is going back to 2013. I don't remember
 5 every conversation I had with them.
 6 Q Well, you made a good point, right, that
 7 there's a lot more than what's in this snapshot.
 8 A Yes.
 9 Q Okay. So I'd like to give you an opportunity
 10 to tell us about that, okay.
 11 A Yes.
 12 Q So how many accounts were Mr. Golden and Mr.
 13 Kotash and responsible for monitoring?
 14 A They were -- well, you mean for this branch or
 15 just for overall?
 16 Q Their job everyday.
 17 A Their job overall was to cover a number of
 18 different branches.
 19 Q My question was how many accounts were Mr.
 20 Golden and Mr. Kotash responsible for monitoring?
 21 A That number I don't know offhand.
 22 Q Was it more than 10?
 23 A Absolutely.
 24 Q Was it more than 100?
 25 A Absolutely, yes.

1 Q Was it more than a thousand?
 2 A Yes.
 3 Q Was it more than two thousand?
 4 A I don't know. You are trying to give me some
 5 numbers and I can't --
 6 Q It's more than a thousand is all you can say.
 7 A Yes.
 8 Q So Mr. Golden and Mr. Kotash were responsible
 9 for monitoring over a thousand accounts and you just made
 10 a phone call to them to tell them that the account was
 11 going to be closed because of "pump and dump" activity --
 12 what is the word -- characteristics commonly associated
 13 with "pump and dump" activity, the misrepresentation or
 14 the misstatement about what type of trading was going to
 15 be done, and the fact that Mr. Ferri wasn't completing
 16 the review that he was supposed to be doing, did they
 17 respond to that information at all?
 18 A Yes, they did.
 19 Q And what did they say?
 20 A In those conversations with them, they were
 21 covering -- they were covering the Proserve system for
 22 Dave Ferri. That was I believe delegated to them from
 23 Dave.
 24 Q Were Mr. Golden and Mr. Kotash concerned with
 25 the information you relayed to them?

1 A Yes, absolutely.
 2 Q Did they say anything to you that indicated
 3 that they were concerned?
 4 A Yeah, when I mentioned "pump and dump," they
 5 were very concerned.
 6 Q And what did they say?
 7 A They said they weren't aware of that, or
 8 whatnot. I said, "Well, you know, you need to be aware
 9 of those issues."
 10 But like I'm saying, this is a snapshot of what
 11 transpired.
 12 Q Okay. So Mr. Golden and Mr. Kotash were
 13 responsible for monitoring these accounts, correct?
 14 A Uh-huh.
 15 Q Did they say whether they had observed trading
 16 in the accounts that exhibited characteristics
 17 commonly associated with "pump and dumps"?
 18 A I'm not sure what you mean by that.
 19 Q I'm asking you, did you Mr. Golden and Mr.
 20 Kotash tell you that in their monitoring activities of
 21 the two accounts, they too had observed the
 22 trading with characteristics commonly associated with a
 23 "pump and dump"?
 24 A They didn't tell me that.
 25 Q Did that concern you?

1 A That they didn't tell me that?
 2 Q Correct.
 3 A Yes, it's a concern.
 4 Q And why was that concerning to you?
 5 A Because that activity is deemed unlawful.
 6 Q Right. And the two individuals that are
 7 responsible for monitoring it didn't notice it, correct?
 8 A Correct.
 9 Q So that's concerning, right?
 10 A Yes.
 11 Q Did that weigh into your determination as to
 12 whether or not changes needed to be made with Aegis's
 13 monitoring protocol?
 14 A The monitoring protocol was an evolving
 15 process. As I stated previously --
 16 Q It was a yes or no question, Mr. Terracciano.
 17 A Yes, yes.
 18 Q Okay. Did you make any changes to the
 19 monitoring protocol after the conversation you had with
 20 Mr. Golden and Mr. Kotash?
 21 A The changes were instructional.
 22 Q What does that mean?
 23 A "Instructional" means you need to check the --
 24 you've got to do Google searches in this immediately as
 25 soon as you see it. And look up all the relevant points.

1 If you do a Google search on -- see a lot of activity on
2 the stock, volume is up, volume is down, do a Google --
3 make sure that a Google search is done and then see if
4 there's any marketing news on the company.

5 Q Weren't they supposed to be doing that already?
6 A Yes.

7 Q And did they tell you that they had not been
8 doing that?

9 A No, I don't remember if they actually told me
10 that.

11 Q Did you ever follow up with Mr. Golden and Mr.
12 Kotash to ensure that they -- after you had given them
13 that direction, that they were following through on it?

14 A Yes.

15 Q How did you do that?

16 A I did that by them coming to the office and we
17 actually went through some situations and did some Google
18 searches at the 810 Compliance office.

19 Q After that time, did Mr. Golden and Mr. Kotash
20 report to you that they had identified any suspicious
21 activity in their monitoring responsibilities?

22 A Not that I remember, no.

23 Q Was that concerning to you?

24 A Not at the time, no.

25 Q Why not?

1 A Because if they didn't see -- if they saw
2 something they would have reported to me directly.

3 Q Well, that's what I'm asking is concerning,
4 that potentially they didn't see it.

5 A Right.

6 Q So isn't that concerning to you?

7 A Well, after additional instruction, if they
8 didn't see anything, then it did not come to my
9 attention. I took it the -- would show it, and then if
10 it wasn't brought to my attention, then obviously it was
11 an issue.

12 Q Were Mr. Golden and Mr. Kotash responsible for
13 monitoring the [redacted] account?

14 A Not -- when you say "monitoring the account,"
15 yes, they were monitoring -- they were monitoring the
16 account, not on an individual basis, but through the
17 actual Proserve system for alerts.

18 Q Okay. Did the Proserve system flag [redacted]
19 [redacted]s
20 trading in [redacted]?

21 A I believe it did, yes.

22 Q Was that brought to your attention?

23 A No.

24 Q How do you know that?

25 A I believe it did because on --

1 MR. McCURDY: Do you know?

2 THE WITNESS: Do I --

3 MR. McCURDY: Know.

4 THE WITNESS: Do I know? No, I don't actually
5 know.

6 BY MR. BAGNALL:

7 Q How do you know that the Proserve system
8 flagged the trading in [redacted] in the [redacted]
9 accounts?

10 A I didn't actually see it so I don't know.

11 Q Okay. Did the Proserve system flag any of the
12 trading that occurred in the [redacted] account?

13 A I don't remember at that time.

14 Q Before receiving the inquiries from RBC, did
15 anyone at Aegis make you aware about the trading in [redacted]
16 [redacted] in the [redacted] accounts?

17 A No.

18 Q Prior to receiving the RBC inquiry regarding
19 the [redacted] account that we discussed earlier, did
20 anybody at Aegis bring to your attention the trading that
21 was going on in that account?

22 A No.

23 Q Okay. And you don't know whether -- correct me
24 I'm wrong, but I think you just testified that you don't
25 know whether the Proserve system flagged the trading in

1 either of the two [redacted] accounts or the [redacted]
2 account, correct?

3 A Correct.

4 Q Did you do anything after you received the RBC
5 inquiries to ensure that going forward you would get
6 notification from the Proserve flags on trading like that
7 described in the RBC alerts?

8 MR. McCURDY: That he would get it himself?

9 MR. BAGNALL: Correct.

10 BY MR. BAGNALL:

11 Q Let me back up. Let me ask you a different
12 question first.

13 As the AML compliance office of Aegis, would
14 you want to know about the type of trading occurring at
15 the firm that's described in Exhibit 29?

16 A Yes, yes.

17 Q Okay. Would you, as the AML CO of Aegis, would
18 you want to know about the type of trading that was
19 occurring in the [redacted] account that we discussed
20 earlier?

21 A Yes.

22 Q Okay. And you just testified a moment ago that
23 you didn't know about that trading until you received the
24 RBC inquiry, correct?

25 A Correct.

1 Q So did you do anything after receiving the RBC
2 inquiries to ensure that you personally would find out
3 about that type of trading? And when I say "that type of
4 trading," I mean the trading like that described here in
5 Exhibit 29.

6 A I had subsequent conversations with the
7 individuals that do the review off of the Proserve
8 system.

9 Q And that's Mr. Golden and Mr. Kotash?

10 A Yes.

11 Q Okay. But then after you had that conversation
12 with them, you never heard from them about any other
13 trading like that described in Exhibit 29, correct?

14 A No, correct.

15 Q So wasn't that concerning to you? So you had
16 this conversation with them about ensuring that you would
17 be aware of this type of trading activity and you never
18 heard about any type of trading activity like this after
19 that.

20 A Correct.

21 Q That wasn't concerning?

22 A No, that is concerning, yes.

23 Q Okay. What did you do about it?

24 A Well, I had -- I would go to the branch and
25 discuss accounts with them and whatnot, and, you know, e

1 Q After you received the RBC inquiries about the
2 [REDACTED] accounts and the [REDACTED] accounts, did
3 you undertake any effort to identify all the accounts at
4 Aegis that were trading in low-priced securities?

5 A That was an ongoing process. Yes, that was an
6 ongoing process.

7 Q Okay. After identifying all the accounts that
8 were trading in low-priced securities, did you subject
9 those accounts to any heightened scrutiny?

10 A Full review was -- at that time conducting a
11 full review on the accounts and whatnot, I don't know
12 offhand what accounts were on --

13 MR. McCURDY: He didn't ask you what accounts.
14 He asked you if you did the review.

15 THE WITNESS: Yes, we did the review.

16 BY MR. BAGNALL:

17 Q So you undertook a review to identify all the
18 accounts that were trading in low-priced securities and
19 then began subjecting all of those accounts to heightened
20 scrutiny?

21 A I'm sorry. When you say "all accounts" --

22 Q All the accounts you identified through your
23 review.

24 A Yes.

25 Q Did you subject all of them to heightened

1 talk to them over the phone about it on a regular basis,
2 and if there was an issue, that would be brought up at
3 that time.

4 Q And were issues brought to you?

5 A There were some issues that were brought, yeah.

6 Q Issues that included trading like that
7 described here in Exhibit 29?

8 A Yeah, yeah.

9 Q How many issues were brought to your attention
10 after you had this conversation with Mr. Kotash and Mr.
11 Golden?

12 A Yeah, I don't know the number, but in
13 conversations, you know, we talked about some trading and
14 some activity. But, yeah, don't know the number.

15 Q Do you think that the steps you took to ensure
16 that you heard about this type of trading going forward
17 were effective?

18 A I think they were effective, yeah.

19 Q Did you conduct or direct anyone to conduct a
20 review of accounts at the firm to see if any other
21 clients had traded over a billion shares of OTC stocks?

22 A I had an individual who was in a supervisory
23 role through Kevin McKenna, and we did -- we did some
24 look-backs on things to try to find some low-priced
25 securities that were traded.

1 scrutiny?

2 A When you say "heightened scrutiny," what
3 specifically are we talking about?

4 Q I'm talking about what you described as
5 "heightened scrutiny" earlier today.

6 A Right. That -- that's one of the issues that I
7 discussed. There's not a bandwidth for --

8 MR. McCURDY: It's a yes or no question.

9 THE WITNESS: No.

10 BY MR. BAGNALL:

11 Q Did you instruct all of those accounts to be
12 closed then because you didn't have the bandwidth to
13 subject them to heightened scrutiny?

14 A There were a number of accounts that were
15 closed.

16 Q Did you instruct that all of the accounts he
17 closed because you didn't have the bandwidth to subject
18 them to heightened scrutiny?

19 A I don't think all of them.

20 Q Why not?

21 A I don't think all of them. There were -- there
22 were over 250 accounts that were actually -- that were
23 actually closed.

24 Q How many remained open?

25 A I don't know that total number, but that was in

1 Q But you don't know whether you did that or not
2 now?

3 A I don't know now, no.

4 Q Okay. I'll take back Exhibit 30. Thank you.

5 MR. BAGNALL: Could you please mark this next
6 in line?

7 (SEC Exhibit No. 31 was marked
8 for identification.)

9 BY MR. BAGNALL:

10 Q Before I hand you this, Mr. Terracciano, do you
11 know whether anybody at Aegis made Mr. Eide aware of
12 RBC's inquiries into the [REDACTED] account?

13 A Yes.

14 Q Did anybody make Mr. Eide aware?

15 A George Kott did.

16 Q How do you know that?

17 A In conversation -- I'm sorry, I just feel I
18 need to say again. As I said previously, the e-mail was
19 only one part. In conversations, in person and on the
20 telephone, all these issues were discussed with senior
21 management, and that was presented to Bob.

22 Q And is that true too of the two [REDACTED]
23 accounts?

24 A Correct.

25 Q And is that true of every RBC inquiry that came

1 31, the oldest e-mail in the thread is from you to Mr.

2 DeGidio cc'ing Mr. McKenna?

3 A Uh-huh.

4 Q At December 2, 2013, at 3:46 p.m.

5 Do you see that?

6 A Yes.

7 Q And in that e-mail, you asked whether RBC would
8 be okay with Aegis keeping the [REDACTED] accounts open,
9 correct?

10 A Uh-huh.

11 Q And you are asking if they'd be okay with it if
12 the accounts are limited to trading in U.S.
13 exchange-listed stocks only, right?

14 A Correct, yes.

15 Q Do you recall whether you received this e-mail
16 after the RBC inquiry indicating that the two [REDACTED]
17 accounts engaged in trading that exhibited
18 characteristics common to a "pump and dump"?

19 A No.

20 Q Okay. Let me hand you back then Exhibit 30.

21 If you'd turn in Exhibit 30 to the page marked
22 773. The e-mail at the bottom of that page from Mr.
23 DeGidio to the 810 Compliance, December 2, 2013, 2:40
24 p.m.

25 Do you see that?

1 to Aegis?

2 A Not -- that I don't know.

3 Q What determined whether an RBC inquiry would be
4 made known to Mr. Eide or not?

5 A By him.

6 Q At the firm, at the firm generally.

7 A That I don't know.

8 Q Do you know how many RBC inquiries Mr. Eide was
9 informed about?

10 A No, I wouldn't know that.

11 Q I am going to hand you what's been marked as
12 Exhibit 31.

13 Could you please take a look at that and let me
14 know when you're done?

15 (The witness reviewed the document.)

16 A Okay.

17 Q Do you recognize this document, Mr.
18 Terracciano?

19 A I recognize it now.

20 Q What is it?

21 A It's a correspondence between myself, all the
22 relevant parties, back to Nick DeGidio over at RBC.

23 Q Related to the two [REDACTED] accounts?

24 A Correct.

25 Q All right. Do you see at the bottom of Exhibit

1 A Uh-huh.

2 Q And then if you look back at Exhibit 31, do you
3 see that your e-mail requesting that the account remain
4 open with certain conditions was sent at 3:46 p.m.?

5 A Right.

6 Q So you had received RBC's inquiry first, is
7 that correct?

8 A Yes, it appears that way, yes.

9 Q Okay. Why would you be -- as the AML CO of
10 Aegis, why would you be comfortable keeping the two
11 [REDACTED] accounts open when you'd been told that they had
12 engaged in trading that exhibited characteristics
13 commonly associated with a "pump and dump"?

14 A I feel the need to go back again and explain --

15 Q Okay, one moment. Could you just answer that
16 question?

17 A Ask me that question again.

18 Q Why, after you had received the e-mail from RBC
19 indicating that the two [REDACTED] accounts had engaged in
20 trading that had characteristics commonly associated with
21 the "pump and dump," why would you be okay with those
22 accounts remaining open at Aegis under any circumstances?

23 A There were conversations preceding this about
24 the accounts.

25 Q And what about those conversations gave you

1 comfort that the accounts could stay open when they had
2 engaged in trading with characteristics commonly
3 associated with a "pump and dump" scheme?

4 A In conversations with everyone listed on this
5 e-mail --

6 Q I'm sorry. Which e-mail? Exhibit 30 or 31?

7 A Both of them. In conversations with myself,
8 Sam, Teresa, Nick DeGidio, Mike Heiser, who was also in
9 some discussion, and Kevin McKenna, we talked about the
10 account and the activity and whatnot, and it wasn't my
11 idea to keep the account open, based upon if they were
12 going to do listed stock or not.

13 The discussion was from RBC, "Why does it look
14 like it's" -- if I remember correctly, "Why does it look
15 like it's predominately low-price security activity?"

16 And in those conversations, it went around and
17 around to the fact that, you know, if the account did
18 some kind of other business besides low-priced
19 securities, RBC might be comfortable with keeping the
20 account open.

21 Q So as an AML CO, if a customer's account
22 engaged in 90 percent trades on listed stock and 10
23 percent in exhibited characteristics of a "pump and
24 dump," you would be okay keeping that account open?

25 A No, I wouldn't be.

1 trading that exhibited the signs of a "pump and dump" so
2 long as that trading was only a small portion of the
3 trading that occurred in the account?

4 A No...No, and let me preface that...

5 The account would need to -- the account would
6 no longer -- it was understood the account would no
7 longer trade any low-priced securities. It would only be
8 listed securities.

9 Q But the bell can't be un-rung, right? What
10 about the trading that it had already done that exhibited
11 the characteristics of a "pump and dump" scheme?

12 MR. McCURDY: What about it?

13 MR. BAGNALL: What weight --

14 MR. McCURDY: Do you mean does that taint the
15 account forever? Is that what you're asking?

16 MR. BAGNALL: That's right. Yes.

17 THE WITNESS: You know, I don't think that
18 taints the account forever.

19 BY MR. BAGNALL:

20 Q Why not?

21 A Well, if it's determined that it is a "pump and
22 dump" scheme, and how you actually determine that, was
23 there any enforcement action taken against the security
24 or the account or the account holders?

25 Q The questions go only one way, Mr. Terracciano.

1 Q Okay. Why then would it matter if the account
2 in question here, the two [REDACTED] accounts, only had a
3 small portion of the trading that exhibited
4 characteristics of a "pump and dump" scheme?

5 A It was --

6 MR. McCURDY: I'm sorry. Can I hear that
7 question again?

8 BY MR. BAGNALL:

9 Q Did you understand the question, Mr.
10 Terracciano?

11 A I would like to hear it again myself.

12 Q Okay. Maybe I misunderstood you, right. I
13 thought you said that the conversation -- I asked you why
14 you would be comfortable keeping this account open under
15 any circumstances, whatever the conditions are.

16 I thought you then said, "Well, we had a
17 conversation with RBC and they indicated that maybe this
18 account only had a small portion of the trading that
19 exhibited the signs of a "pump and dump" and that they
20 would be okay going forward if they focused only on the
21 trading that didn't exhibit those characteristics.

22 Is that what you'd said?

23 A Yes, that's what he said.

24 Q And now what I am asking you is, as the AML CO,
25 you would be okay keeping an account open that engaged in

1 A Yes. Well, there wasn't any.

2 Q How do you know?

3 A I did Google searches. We looked into it. And
4 I don't remember at that time seeing anything about an
5 actual confirmation of a "pump and dump" scheme.

6 BY MR. MAHER:

7 Q Is that your standard test? As long as there's
8 no regulatory action that's been filed?

9 A No, that's not. In this case, that was what --
10 that was what was uncovered.

11 Now, if I can move forward just one moment.

12 In discussions with RBC, it was brought up on
13 that level that if this client was not engaging in that
14 kind of activity, then they might be okay with keeping
15 the account open.

16 MR. McCURDY: They, RBC?

17 THE WITNESS: RBC.

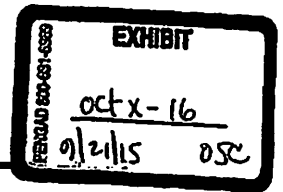
18 BY MR. BAGNALL:

19 Q But I'm not asking you about RBC. I am asking
20 you about your view as the AML CO for Aegls.

21 A Uh-huh.

22 Q Do you agree that you had an independent
23 obligation, and I mean independent from RBC, as the AML
24 CO for Aegis, to make determinations about the accounts
25 at the firm where you were AML CO?

Exhibit 5



From: Kevin McKenna [kmckenna@aegiscap.com]
Sent: Monday, November 04, 2013 4:44 PM
To: Samuel Guidetti
Cc: Melissa Scaparro; Eugene Terracciano
Subject: Re: AML Surveillance Request for xxx-26164 / 12HC / [REDACTED]

Who is the rep ?? Don't think there sd be much discussion

From: Samuel Guidetti
Sent: Monday, November 04, 2013 04:39 PM Eastern Standard Time
To: Kevin McKenna
Cc: Melissa Scaparro; Eugene Terracciano
Subject: FW: AML Surveillance Request for xxx-26164 / 12HC / [REDACTED]

Kevin,

Please see us when you get in tomorrow morning. The attached is an urgent matter from RBC. They were looking for a response today but since you are out of office and I do not recall seeing it, Mike will give us till tomorrow to get back.

Sam

From: Heiser, Michael [mailto:michael.heiser@rbc.com]
Sent: Monday, November 04, 2013 4:32 PM
To: Samuel Guidetti
Subject: FW: AML Surveillance Request for xxx-26164 / 12HC / [REDACTED]
Importance: High

Heiser, Michael
November 01, 2013 12:01 PM
Samuel Guidetti; Kevin McKenna
Siddio, Nicholas
FW: AML Surveillance Request for xxx-26164 / 12HC / [REDACTED]
Importance: High

Good afternoon,

I received the following request from our AML Department. Based on the volume of activity, RBC CS requests a response by the end of day Monday, November 4.

Through our AML surveillance processes, the following account was identified for additional review:

Account Number: xxx-26164
Account Name: [REDACTED]

Please be advised that we require written or electronic confirmation that you have reviewed the account and found the client and activity reasonable under your AML program. Specifically, please address each of the following:

Since the account was opened in February, the client has liquidated nearly one billion shares of OTC stocks, which are covered via shares received via RVP from State Street Bank (DTC #0987). Patterns/concerns RBC CS identified during a preliminary review of a few of the securities include:

- [REDACTED]
- As of 7/29/13, the company reported to have 240M shares outstanding. Between 7/17 and 10/8, the client sold 245.74M shares – more shares than were last reported outstanding.
- a On 9/20, there were 690M shares traded, meaning the company issued at least 750M shares in seven weeks.a
- a On 11/1/13, the number of outstanding shares decreased by 1:500.a
- a The company has generated no revenues and its only asset is a \$350,000 deposit towards the acquisition of a mine.a
- a The company spent \$652,500 on consulting fees in the six months ended 6/30/13.a

- [REDACTED]
- On 8/15/13, the company reported to have 231.7M shares outstanding. Between 9/17 and 10/31, the client sold 71.8M shares, or 31% of the outstanding shares.
- a The average daily trading volume has increased by nearly five times since the client started selling shares, accompanied by a 90% decrease in price.

- [REDACTED]
- As of 7/15, the company reported to have 702.7M shares outstanding. Between 8/15 and 10/30, the client sold 422.4M shares, or 60% of the outstanding shares.
- a During the period the client has been selling, the price has dropped by 50%.a
- a The company has generated no revenues.a

- [REDACTED]
- The company is not reporting with the SEC.
- a The company last reported to have 8.819B shares outstanding. The client sold 217M shares between 6/4 and 7/24 for proceeds of \$21,500.a
- a The company has generated no revenues and has less than \$43,000 in assets.a

- [REDACTED] concerns are from review earlier this year of related account held for [REDACTED]
- a The company has a history of issuing a large amount of shares, followed by multiple reverse splits.a
- a Following a reverse split, the company doubled the amount of shares outstanding in one month, jumping from 11.637M shares outstanding on 10/8/12 to 23.805M shares on 11/14/12. Since then, the price has dropped from \$0.21 to \$0.02.a Less than six months ago, it was trading at over \$2.40.a
- a The company filed with the SEC a document stating its intent to issue 249M shares of common stock and authorize the board of directors to increase or decrease the number of shares of common stock on the company without stockholder approval. It also authorized a revision of the Stock Incentive Plan to be able to issue 15M shares instead of only 71,429.a
- a As of the last 10Q in November 2012, Tripod had \$260,000 of debt which was convertible into over 15 million shares of a the company's common stock (nearly 40% of the outstanding shares assuming the only shares the company has issued since 11/14/12 were to the client).a
- a The issuer's CEO, Peter M. Hoffman, has been investigated by the government on four counts of felony tax fraud charges. Although he ended up only pleading guilty to a misdemeanor charge based on a mistrial, the charges are noteworthy, especially in light of the U.S. Attorney in New Orleans' current investigation into tax credits claimed by an affiliate of the issuer, Seven Arts Pictures Louisiana.a
- a The company's former chairman, Bruce McNall, was convicted of bilking six banks out of \$236 million. He pleaded guilty to five felony charges of conspiracy and fraud and was sentenced to 70 months in prison.a

Questions for the Compliance Officer:

- What due diligence has the firm performed on the client?
- What due diligence has the firm performed on the securities liquidated in the account?
- How is the firm comfortable with this activity?

Any additional information provided in your response would be helpful to determine if the above activity is reasonable.

*** Please note that this inquiry is confidential and is not to be shared with the client. Although the client may be contacted directly to address the questions within this inquiry, informing clients that they are subjects of an Anti-Money Laundering (AML) inquiry is prohibited. ***

Please respond by email to the above inquiry within five business days of receipt. Note that a lack of response will result in the account being blocked for further activity. Based upon the initial answers provided, RBC CS may follow up with additional questions in order to better understand the client.

Due to the risk posed by certain clients, RBC CS may ask that the correspondent closely monitor an account and may even request that the account be closed. If an account is subject to monitoring, RBC CS may periodically request the results of this review from the correspondent.

Correspondents are reminded that under the USA PATRIOT Act, each firm must have its own AML Program. For questions about your AML Program or the AML inquiry process, please contact your Relationship Manager.

Thank you,

AML Compliance

Michael K. Helser | Compliance and Risk Manager
RBC Correspondent Services | RBC Advisor Services | RBC Capital Markets, LLC
60 South 6th St. | Minneapolis, MN 55402
Phone: 612-371-2363 | Fax: 612-313-1194
michael.helser@rbc.com | www.rbc-cs.com | www.rbc-as.com

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Exhibit 6

From: George Kott [gkott@aegiscap.com]
Sent: Wednesday, November 06, 2013 8:03 AM
To: Samuel Guidetti
Subject: Re: AML Surveillance Request for xxx-26164 / 12HC / [REDACTED]

Nicely done

Sent from my HTC

— Reply message —

From: "Samuel Guidetti" <SGuidetti@aegiscap.com>
To: "George Kott" <gkott@aegiscap.com>
Subject: AML Surveillance Request for xxx-26164 / 12HC / [REDACTED]
Date: Tue, Nov 5, 2013 4:39 PM

FYI

From: Helser, Michael [mailto:michael.helser@rbc.com]
Sent: Tuesday, November 05, 2013 4:14 PM
To: McGarry, Jennifer; Matthies, Brittany (RBC Wealth Mgmt)
Cc: Samuel Guidetti
Subject: RE: AML Surveillance Request for xxx-26164 / 12HC / [REDACTED]

Sam Guidetti and Eugene Terantino of Aegis Compliance called me in response to the concerns listed below about five minutes ago.

Per Sam and Eugene, the account predates them. Based on our concerns they reviewed the account activity, account opening paperwork, spoke to the rep etc. Based on that review and the concerns brought to their attention by RBC, Aegis will be closing the account.

Michael K. Helser | Compliance and Risk Manager
RBC Correspondent Services | RBC Advisor Services | RBC Capital Markets, LLC
60 South 6th St. | Minneapolis, MN 55402
Phone: 612-371-2383 | Fax: 612-313-1194
michael.helser@rbc.com | www.rbc-cs.com | www.rbc-as.com

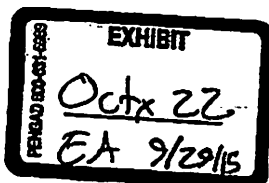
Helser, Michael
November 04, 2013 3:33 PM
Garry, Jennifer
FW: AML Surveillance Request for xxx-26164 / 12HC / [REDACTED]
Priority: High

Kevin is out and Sam hadn't seen it. I told him to get it back to me end of day tomorrow.

Helser, Michael
November 01, 2013 12:01 PM
Samuel Guidetti; Kevin McKenna
Siddio, Nicholas
FW: AML Surveillance Request for xxx-26164 / 12HC / [REDACTED]
Priority: High

Good afternoon,

1



SEC-Aegis-E-0020680

I received the following request from our AML Department. Based on the volume of activity, RBC CS requests a response by the end of day Monday, November 4.

Through our AML surveillance processes, the following account was identified for additional review:

Account Number: xxx-26164

Account Name: [REDACTED]

Please be advised that we require written or electronic confirmation that you have reviewed the account and found the client and activity reasonable under your AML program. Specifically, please address each of the following:

Since the account was opened in February, the client has liquidated nearly one billion shares of OTC stocks, which are covered via shares received via RVP from State Street Bank (DTC #0987). Patterns/concerns RBC CS identified during a preliminary review of a few of the securities include:

- [REDACTED]
- *As of 7/29/13, the company reported to have 240M shares outstanding. Between 7/17 and 10/8, the client sold 245.74M shares – more shares than were last reported outstanding.*
- *On 9/20, there were 690M shares traded, meaning the company issued at least 750M shares in seven weeks.e*
- *On 11/1/13, the number of outstanding shares decreased by 1:500.e*
- *The company has generated no revenues and its only asset is a \$350,000 deposit towards the acquisition of a mine.e*
- *The company spent \$652,500 on consulting fees in the six months ended 6/30/13.e*
- [REDACTED]
- *On 8/15/13, the company reported to have 231.7M shares outstanding. Between 9/17 and 10/31, the client sold 71.8M shares, or 31% of the outstanding shares.*
- *The average daily trading volume has increased by nearly five times since the client started selling shares, accompanied by a 90% decrease in price.*
- [REDACTED]
- *As of 7/15, the company reported to have 702.7M shares outstanding. Between 8/15 and 10/30, the client sold 422.4M shares, or 60% of the outstanding shares.*
- *During the period the client has been selling, the price has dropped by 50%.e*
- *The company has generated no revenues.e*
- [REDACTED]
- *The company is not reporting with the SEC.*
- *The company last reported to have 8.819B shares outstanding. The client sold 217M shares between 6/4 and 7/24 for proceeds of \$21,500.*
- *The company has generated no revenues and has less than \$43,000 in assets.e*
- [REDACTED] *concerns are from review earlier this year of related account held for [REDACTED]*
- *The company has a history of issuing a large amount of shares, followed by multiple reverse splits.e*
- *Following a reverse split, the company doubled the amount of shares outstanding in one month, jumping from 11.637Me shares outstanding on 10/8/12 to 23.805M shares on 11/14/12. Since then, the price has dropped from \$0.21 to \$0.02. Less than six months ago, it was trading at over \$2.40.e*
- *The company filed with the SEC a document stating its intent to issue 249M shares of common stock and authorize the board of directors to increase or decrease the number of shares of common stock on the company without stockholder approval. It also authorized a revision of the Stock Incentive Plan to be able to issue 15M shares instead of only 71,429.*
- *As of the last 10Q in November 2012, Tripod had \$260,000 of debt which was convertible into over 15 million shares of the company's common stock (nearly 40% of the outstanding shares assuming the only shares the company has issued since 11/14/12 were to the client).*
- *The issuer's CEO, Peter M. Hoffman, has been investigated by the government on four counts of felony tax fraude charges. Although he ended up only pleading guilty to a misdemeanor charge based on a mistrial, the charges are noteworthy, especially in light of the U.S. Attorney in New Orleans' current investigation into tax credits claimed by an affiliate of the Issuer, Seven Arts Pictures Louisiana.*
- *The company's former chairman, Bruce McNail, was convicted of bilking six banks out of \$236 million. He pleaded guilty to five felony charges of conspiracy and fraud and was sentenced to 70 months in prison.*

Questions for the Compliance Officer:

- a What due diligence has the firm performed on the client?a
- a What due diligence has the firm performed on the securities liquidated in the account?a
- a How is the firm comfortable with this activity?a

Any additional information provided in your response would be helpful to determine if the above activity is reasonable.a

*** Please note that this inquiry is confidential and is not to be shared with the client. Although the client may be contacted directly to address the questions within this inquiry, informing clients that they are subjects of an Anti-Money Laundering (AML) inquiry is prohibited. ***a

Please respond by email to the above inquiry within five business days of receipt. Note that a lack of response will result in the account being blocked for further activity. Based upon the initial answers provided, RBC CS may follow up with additional questions in order to better understand the client.a

Due to the risk posed by certain clients, RBC CS may ask that the correspondent closely monitor an account and may even request that the account be closed. If an account is subject to monitoring, RBC CS may periodically request the results of this review from the correspondent.a

Correspondents are reminded that under the USA PATRIOT Act, each firm must have its own AML Program. For questions about your AML Program or the AML inquiry process, please contact your Relationship Manager.a

Thank you.

AML Compliance

Michael K. Heiser | Compliance and Risk Manager
RBC Correspondent Services | RBC Advisor Services | RBC Capital Markets, LLCa
60 South 6th St. | Minneapolis, MN 55402
Phone: 612-371-2383 | Fax: 612-313-1194a
michael.heiser@rbc.com | www.rbc-cs.com | www.rbc-as.com

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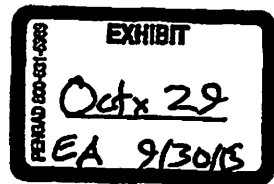
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Exhibit 7



From: Eugene Terracciano <ETerracciano@aeqiscap.com>
 Sent: Tuesday, December 3, 2013 2:48 PM
 To: George Kott <gkott@aeqiscap.com>
 Cc: Kevin McKenna <kmckenna@aeqiscap.com>
 Subject: FW: [REDACTED] (12HC) XXX-19060 and XXX-28349

George,

The accounts will be blocked for sales only and close the account. We do not have the bandwidth to monitor. Thank you,

From: Eugene Terracciano
 Sent: Tuesday, December 03, 2013 9:03 AM
 To: Kevin McKenna; Teresa Fiorucci
 Cc: Samuel Guidetti
 Subject: RE: [REDACTED] (12HC) XXX-19060 and XXX-28349

Teresa,

Please block the accounts for sales only and close the accounts. Dave Ferri said the accounts were only trading in listed securities. Obviously, not true.

Thank you,

Eugene Terracciano
 Director of Compliance
 Aegis Capital Corp.
 810 7th Avenue, 18th Floor
 New York, NY 10019
 646-557-3497 X 693

From: Kevin McKenna
 Sent: Tuesday, December 03, 2013 8:54 AM
 To: Teresa Fiorucci; Eugene Terracciano
 Cc: Samuel Guidetti
 Subject: RE: [REDACTED] (12HC) XXX-19060 and XXX-28349

Didn't compliance request this account be closed ??

Kevin C. McKenna
 Aegis Capital Corp.
 810 7th Avenue 18th Floor
 New York, N.Y. 10019
 212-813-1010 X436

From: Teresa Fiorucci
 Sent: Tuesday, December 03, 2013 8:52 AM
 To: Eugene Terracciano
 Cc: Kevin McKenna
 Subject: RE: [REDACTED] (12HC) XXX-19060 and XXX-28349

Below are the trades.

Date	Quantity	Symbol	Description	Source	Type	Price	Net Amount	Settle Date	Comm Amt	Sales Credit
12/2/2013	-10,000	[REDACTED]	[REDACTED]	BSEL	9	2.39705	23,820.08	12/5/2013	150	
12/2/2013	9,400	[REDACTED]	[REDACTED]	BBUY	9	1.52	14,430.88	12/5/2013	142.88	
12/2/2013	79,500	[REDACTED]	[REDACTED]	BBUY	9	0.674648	53,634.52	12/5/2013		532.65
12/2/2013	2,000	[REDACTED]	[REDACTED]	BBUY	9	1.48015	-3,010.30	12/5/2013	50	
12/2/2013	3,490	[REDACTED]	[REDACTED]	BBUY	9	0.24	-877.6	12/5/2013	40	
12/2/2013	600	[REDACTED]	[REDACTED]	BBUY	9	6.59	-3,954.00	12/5/2013		54
12/2/2013	20,000	[REDACTED]	[REDACTED]	BBUY	9	0.697	14,079.40	12/5/2013	139.4	

12/2/2013	5,000			RVP	9	12,425.19			
12/2/2013	-5,700			DVP	9	33,146.32			

Teresa Fiorucci-Alviz
Aegis Capital Corp
Phone: 646-290-7899
Fax: 646-355-1993
tfiorucci@aegiscap.com

From: Eugene Terracciano
Sent: Tuesday, December 03, 2013 8:40 AM
To: Teresa Fiorucci
Cc: Kevin McKenna
Subject: RE: [REDACTED] (12HC) XXX-19060 and XXX-28349

Teresa,

Did they trade listed stock?

From: Teresa Fiorucci
Sent: Tuesday, December 03, 2013 8:24 AM
To: Kevin McKenna; Eugene Terracciano; 810 Compliance
Cc: George Kott; David Ferri
Subject: RE: [REDACTED] (12HC) XXX-19060 and XXX-28349

898-28349 has trades from 12/2.

Teresa Fiorucci-Alviz
Aegis Capital Corp
Phone: 646-290-7899
Fax: 646-355-1993
tfiorucci@aegiscap.com

From: Kevin McKenna
Sent: Monday, December 02, 2013 5:41 PM
To: Eugene Terracciano; DeGidio, Nicholas; 810 Compliance; Teresa Fiorucci
Cc: George Kott; David Ferri
Subject: RE: [REDACTED] (12HC) XXX-19060 and XXX-28349

Teresa,

Please have these accounts closed.

Tnx
Kevin

Kevin C. McKenna
Aegis Capital Corp.
810 7th Avenue 18th Floor
New York, N.Y. 10019
212-813-1010 X436

From: Eugene Terracciano
Sent: Monday, December 02, 2013 3:04 PM
To: DeGidio, Nicholas; 810 Compliance
Cc: George Kott; Kevin McKenna; David Ferri
Subject: RE: [REDACTED] (12HC) XXX-19060 and XXX-28349

Nick,

(12HC) XXX-19060 and XXX-28349 will be closed.

Kevin, can a member of your team send a request to RBC to close the above referenced accounts.

Thank you,

Eugene Terracciano
Director of Compliance
Aegis Capital Corp.
810 7th Avenue, 18th Floor
New York, NY 10019
646-557-3497 X 693

From: DeGidio, Nicholas (mailto:nicholas.degidio@rbc.com)
Sent: Monday, December 02, 2013 2:40 PM
To: 810 Compliance
Cc: George Kott
Subject: [REDACTED] (12HC) XXX-19060 and XXX-28349
Importance: High

Good Afternoon,

Please see the email below from AML.

The above referenced accounts for client [REDACTED] traded in [REDACTED] (OTCQB [REDACTED]) in June and July 2013. These trades are of concern for the following reasons:

[REDACTED] exhibited characteristics commonly associated with a pump and dump scheme; including paid stock promotion, a significant increase in both price and trading volume, followed by a precipitous drop in price and volume.

[REDACTED] a medical device company, was formerly known as [REDACTED] an auto parts manufacturer.

[REDACTED] had minimal trading volume and zero revenue, and trading volume did not increase until the name was changed to [REDACTED] and the promotions began.

The [REDACTED] transactions resemble activity in the accounts of [REDACTED] (XXX-26454) and [REDACTED] (XXX-26774), which were both closed in August at the request of AML for similar trading of low-priced securities engaged in promotional activity.

We are not comfortable with this activity, and request that accounts owned by the [REDACTED] entity be closed as well.

Nicholas DeGidio | Relationship Manager, RBC Correspondent & Advisor Services | RBC Capital Markets, LLC | 60 South 6th St P18 | Minneapolis | MN | 55402 | T:612-371-2839 | C: 612-387-6295 | F:866-635-3573

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Exhibit 8

From: Eugene Terracciano <ETerracciano@aegiscap.com>
 Sent: Tuesday, December 3, 2013 2:42 PM
 To: Kevin McKenna <kmckenna@aegiscap.com>; Samuel Guidetti <SGuidetti@aegiscap.com>
 Cc: Teresa Fiorucci <TFiorucci@aegiscap.com>
 Subject: FW: XXX-19060 and XXX-28349: [REDACTED]



Gentleman,

As you can see Dave Ferri is incorrect when he states only listed securities for both accounts. Teresa please move forward with closing the accounts. Thank you,

Date	Quantity	Symbol	Description	Source	Type	Price	Net Amount	Settle Date	Comm Amt	Sales Credit
12/2/2013	-10,000	[REDACTED]	[REDACTED]	BSEL	9	2.39705	23,820.08	12/5/2013	150	
12/2/2013	9,400	[REDACTED]	[REDACTED]	BBUY	9	1.52	14,430.88	12/5/2013	142.88	
12/2/2013	79,500	[REDACTED]	[REDACTED]	BBUY	9	0.674648	53,634.52	12/5/2013		532.65
12/2/2013	2,000	[REDACTED]	[REDACTED]	BBUY	9	1.48015	-3,010.30	12/5/2013	50	
12/2/2013	3,490	[REDACTED]	[REDACTED]	BBUY	9	0.24	-877.6	12/5/2013	40	
12/2/2013	600	[REDACTED]	[REDACTED]	BBUY	9	6.59	-3,954.00	12/5/2013		54
12/2/2013	20,000	[REDACTED]	[REDACTED]	BBUY	9	0.697	14,079.40	12/5/2013	139.4	
12/2/2013	5,000	[REDACTED]	[REDACTED]	RVP	9		12,425.19			
12/2/2013	-5,700	[REDACTED]	[REDACTED]	DVP	9		33,146.32			

From: DeGidio, Nicholas [mailto:nicholas.degidio@rbc.com]
 Sent: Tuesday, December 03, 2013 9:28 AM
 To: Eugene Terracciano
 Cc: Kevin McKenna
 Subject: RE: XXX-19060 and XXX-28349: [REDACTED]

Hi Eugene.

As long as the Aegis continues to monitor the accounts to make sure the client is only trading in US exchange Listed Stocks, our AML would be comfortable with that.

Thanks,
 Nick

Nicholas DeGidio | Relationship Manager, RBC Correspondent & Advisor Services | RBC Capital Markets, LLC | 60 South 6th St P18 | Minneapolis | MN | 55402 | T:612-371-2839 | C: 612-387-6295 | F:866-635-3573

From: Eugene Terracciano [mailto:ETerracciano@aegiscap.com]
 Sent: December 02, 2013 3:46 PM
 To: DeGidio, Nicholas
 Cc: Kevin McKenna
 Subject: XXX-19060 and XXX-28349: [REDACTED]

Nick,

We've limited this customer to US exchange Listed Stocks Only. There will not be any bulletin board stocks traded going forward. Are you ok with keeping the accounts open or are you still requesting to close. Please let me know.

Thanks,

Eugene Terracciano
 Director of Compliance
 Aegis Capital Corp.

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810 7th Avenue, 18th Floor
New York, NY 10019
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Exhibit 9

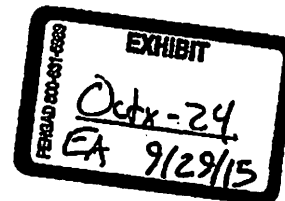
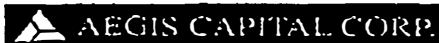
From: Samuel Guidetti [SGuidetti@aegiscap.com]
Sent: Wednesday, February 19, 2014 11:24 AM
To: George Kott; 810 Compliance
Subject: RE: AML Surveillance Request for xxx-18791 / 12HC / [REDACTED]
Attachments: image001.jpg

Shut the account down!

From: George Kott
Sent: Wednesday, February 19, 2014 11:19 AM
To: 810 Compliance
Subject: FW: AML Surveillance Request for xxx-18791 / 12HC / [REDACTED]
Importance: High

This is Drucker. If there are red flags this guy shouldn't be allowed to sell it. At least not thru Aegis.

George Kott
Chief Operating Officer
Aegis Capital Corp.
810 Seventh Avenue, 18th Floor
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From: DeGidio, Nicholas [mailto:nicholas.degidio@rbc.com]
Sent: Wednesday, February 19, 2014 11:13 AM
To: 810 Compliance
Cc: George Kott; Helser, Michael
Subject: AML Surveillance Request for xxx-18791 / 12HC / [REDACTED]
Importance: High

Good Morning,

Please see the email below from AML.

Can you ask them to provide a response for this? Since yesterday, the client has sold an additional 200 million shares of [REDACTED] and more than 1 million shares of [REDACTED] both of which are companies that exhibit a number of red flags. I can certainly list more concerns with these companies if they need more reasons why RBC is concerned with this.

Trading will be blocked at market close today.

Good afternoon,

I received the following request from our AML Department. Based on the volume of activity, RBC CS requests a response by the end of day Tuesday, February 18, 2014.

Through our AML surveillance processes, the following account was identified for additional review:

Account Number: xxx-18791e

Account Name: [REDACTED]

Please be advised that we require written or electronic confirmation that you have reviewed the account and found the client and activity reasonable under your AML program. Specifically, please address each of the following:

Since the account began trading last year, **2.7 billion** shares of OTC stocks have been liquidated, which is 85% of the account's total trading activity. Patterns/concerns RBC CS identified during a preliminary review of a few of the securities include:

- [REDACTED]
- e Multiple large reverse splits (1:20 on 6/27/08 and 1:250 on 6/20/11)e
- e Company not reporting with the SEC
- e The client liquidated 35 million shares on 10/30/13, 10/31/13 and 11/1/13, which account for 30% of the day's volume.
- e The company and CEO were issued a cease and desist order in 2010 by the Alabama Securities Commission for the sale of unregistered securities. <http://www.asc.state.al.us/Orders/2010/CD-2010-0046.pdf>
- [REDACTED]
- e Yield Sign
- e The client liquidated 28 million shares on 10/17/13 and 10/18/13 which accounted for 19% of the day's volume. A stock promotion had been run on 10/7.
- 1:500 reverse split on 7/6/12
- [REDACTED]
- e Stop Sign
- e Split history includes a 5:1 forward split on 10/28/04 and a 1:15 reverse split on 12/1/08.e
- Company deregistered from filing with the SEC on 6/27/08.
- The company has authorized 10 billion shares.
- The client sold a total of 495.5 million shares of which 300 million have been sold in February 2014.
- [REDACTED]
- e Not reporting to the SEC
- e Split history includes a 1.9:1 forward split on 1/29/01 and a 1:50 reverse split on 10/10/06.e
- e The company has changed their name six times since it was formed in 2001.
- e The client sold over 2 million shares on 6/19/13 which accounted for 41% of the day's volume.e
- [REDACTED]
- e The company deregistered from filing with the SEC on 1/22/13.
- e Split history consists of a 1:20 reverse split on 10/19/09 and a 1.02:1 split on 9/16/13.
- e The client has liquidated over 1 billion shares since last April which is a fourth of the 4 billion shares that are authorized.e
- e The company has a history of recent paid promotions from 5/17/13, 6/20/13 and 8/8/13.e
- The company is a food and beverage company that focuses edible marijuana products.
- [REDACTED]
- e Not reporting to the SEC.
- The client has liquidated more than 31 million shares, or about 15% of the total reported shares outstanding.e
- [REDACTED]
- Not reporting to the SEC.
- e Split history consists of 1:40 reverse split on 5/23/07, 1:100 on 11/5/08, 1:300 on 6/15/09, a 20:1 forward split on 1/12/10,e and a 1:2,233 split on 1/30/13.
- The company has changed their name 6 times since 2000.
- [REDACTED]
- Stop Sign
- e The client sold 10 million shares on 6/12/13 which accounted for almost 25% of the day's volume.e
- [REDACTED]
- e Not reporting to the SEC.
- e Split history includes 2:1 forward split on 12/5/02, 1:150 reverse split on 11/9/06, and 1:400 reverse split on 12/7/07.
- e The company changed its name from [REDACTED] to [REDACTED] in April 2013, and before that it was a biotech company.
- [REDACTED]
- Stop Sign
- e The client sold 29 million shares during April 2013
- e The number of authorized shares is not being reported.e

Questions for the Compliance Officer:

- a What due diligence has the firm performed on the client?a
- a What due diligence has the firm performed on the securities liquidated in the account?a
- a How is the firm comfortable with this activity?a

Any additional information provided in your response would be helpful to determine if the above activity is reasonable.

***** Please note that this inquiry is confidential and is not to be shared with the client. Although the client may be contacted directly to address the questions within this inquiry, informing clients that they are subjects of an Anti-Money Laundering (AML) inquiry is prohibited. *****

Please respond by email to the above inquiry within five business days of receipt. Note that a lack of response will result in the account being blocked for further activity. Based upon the initial answers provided, RBC CS may follow up with additional questions in order to better understand the client.

Due to the risk posed by certain clients, RBC CS may ask that the correspondent closely monitor an account and may even request that the account be closed. If an account is subject to monitoring, RBC CS may periodically request the results of this review from the correspondent.

Correspondents are reminded that under the USA PATRIOT Act, each firm must have its own AML Program. For questions about your AML Program or the AML inquiry process, please contact your Relationship Manager.

Thank you,

AML Compliance

This e-mail may be privileged and/or confidential, and the sender does not waive any related rights and obligations. Any distribution, use, or copying of this e-mail or the information it contains by other than an intended recipient is unauthorized. If you receive this e-mail in error, please advise me immediately (by return e-mail or otherwise).

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RBC Capital Markets, LLC
Member NYSE/FINRA/SIPC

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Exhibit 10

THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION

In the Matter of:)

) File No. [REDACTED]

WITNESS: Craig Kotash

PAGES: 1 through 184

PLACE: Securities and Exchange Commission
100 F Street, N.E.,
Washington, D.C. 20549

DATE: Wednesday, January 13, 2016

The above-entitled matter came on for hearing,
pursuant to notice, at 10:14 a.m.

Diversified Reporting Services, Inc.

(202) 467-9200

1 APPEARANCES:
 2
 3 On behalf of the Securities and Exchange Commission:
 4 GEORGE BAGNALL, ESQ., Staff Attorney
 5 DANIEL MAHER, ESQ., Staff Attorney
 6 RICKY SACHAR, ESQ., Staff Attorney
 7 Securities and Exchange Commission
 8 Division of Enforcement
 9 100 F Street, N.E.
 10 Washington, D.C. 20549
 11
 12 On behalf of the Witness:
 13 PAUL McCURDY, ESQ.
 14 WENDY CLARKE, ESQ.
 15 Kelley, Drye & Warren, LLP
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 17 201 Broad Street
 18 Stamford, Connecticut 06901
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 21
 22 ALSO PRESENT:
 23 Kate Zemes, FinCEN
 24 Evelyn Nicholas, FinCEN
 25

1 P R O C E E D I N G S
 2 MR. BAGNALL: We will go on the record at
 3 10:14 a.m., January 13, 2016. Mr. Kotash, could you
 4 please raise your right hand. Do your swear or affirm to
 5 tell the truth, the whole truth, and nothing but the
 6 truth?
 7 THE WITNESS: do.
 8 Whereupon,
 9 CRAIG KOTASH
 10 was called as a witness and, having been first duly
 11 sworn, was examined and testified as follows:
 12 EXAMINATION
 13 BY MR. BAGNALL:
 14 Q Could you please state and spell your
 15 full name for the record?
 16 A Craig Kotash, C-R-A-I-G; K-O-T-A-S-H.
 17 Q Do you have a middle name?
 18 A John.
 19 Q Normal spelling?
 20 A J-O-H-N.
 21 Q I am George Bagnall. And this is Dan
 22 Maher. Later today for a brief time, we will be
 23 joined by another of our colleagues from the SEC
 24 named Ricky Sachar. We are members of the Staff in
 25 the Enforcement Division of the U.S. Securities and

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1 Exchange Commission. Also with us today is Evelyn
 2 Nicholas from FinCEN. And we will be joined later
 3 by one of Evelyn's colleagues from FinCEN named Kate
 4 Zemes.
 5 Could you please confirm that you consent
 6 to FinCEN being here today?
 7 A Yes.
 8 MR. BAGNALL: And, Mr. McCurdy, can you
 9 put on the record that you consent to their presence
 10 as well, please?
 11 MR. McCURDY: Agreed.
 12 MR. BAGNALL: This is an investigation by
 13 the U.S. SEC in the matter of [REDACTED]
 14 Inc., SEC File No. [REDACTED] to determine whether
 15 there have been violations of certain provisions of
 16 the federal securities laws. However, the facts
 17 developed in this investigation might constitute
 18 violations of other federal or state, civil or
 19 criminal laws.
 20 Prior to the opening of the record, you
 21 were provided with a copy of the Formal Order of
 22 Investigation in this matter as well as its
 23 supplements and amendments. It will be available
 24 for your examination during the course of this
 25 proceeding.

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1 version?

2 A Uh-huh.

3 Q Prior to July 2013 when the upgrade

4 occurred, were flags in DVP RVP accounts being

5 suppressed?

6 A I can't say one way or another. I don't

7 know.

8 Q Did you review any DVP RVP accounts prior

9 to July 2013?

10 A Not to my recall. Again, we are talking

11 several years out, though.

12 Q Okay. The description you gave us

13 earlier in your testimony about the flags,

14 specifically with the low-priced securities, you

15 gave us three flags that existed in the system. Is

16 that a description of the flags as they exist after

17 July 2013 or before July 2013? Excuse me. 2013.

18 A Right. And this relates to -- you are

19 gearing this question towards the enhanced and

20 whether that affected any change in --

21 Q Yeah, that's right. I want to know did

22 the three flags that you described for us earlier,

23 did those exist before the enhancement?

24 A Yes, they did.

25 Q So after the enhancement in July 2013

Page 123

1 how, if at all, did those flags change?

2 A I don't know of any material change to

3 those particular flags that I have noticed.

4 Q Do you see also in this response it says

5 -- it describes the upgrade, which is a more

6 powerful and feature-filled version. ProSurv

7 enhanced provides Aegis with an even greater series

8 of suspicious activity and anti-money laundering

9 alerts. Do you see that?

10 A Yes.

11 Q In your experience using the ProSurv

12 service, is that true?

13 A Again, I can't speak to that, because in

14 my role I have not seen any difference in what I am

15 getting back. It is possible there are other flags

16 being generated that is not part of my role in

17 looking at transactional.

18 Q Thank you for making that distinction.

19 Let me just ask that question again. In the way

20 that you personally use ProSurv in connection with

21 your job, did the ProSurv enhanced version provide

22 you with an even greater series of suspicious

23 activity in anti-money laundering alerts?

24 A No, I can't say that.

25 Q Can you turn again Exhibit 55? Turn to

Page 124

1 page five, please. And this time, I would like you

2 to focus on Item 11 when you get there, please.

3 A Okay.

4 Q And you see in accordance -- I am going

5 to read Item 11. "In accordance with the

6 description of the process on page four of the

7 December 23 letter for all potential violations of

8 Aegis policies related to the relevant securities

9 that were found during a daily review. Documents

10 sufficient to identify the potential policy

11 violations were referred to Aegis' AML compliance

12 office." Do you see that?

13 A Yes.

14 Q And then if you read Response 11, it

15 says, "Please be advised that no potential

16 violations of Aegis' policies related to activity in

17 the relevant securities were identified. As a

18 result, there were no referrals to Aegis' AML

19 compliance officer." Do you see that?

20 A Yes.

21 Q Does that refresh your recollection as to

22 whether or not -- when I asked you earlier if you

23 had ever referred anything related to the relevant

24 securities to the AML office, I think you said you

25 didn't recall?

Page 125

1 A Right.

2 Q Does this refresh your recollection as to

3 whether or not you did?

4 A It certainly doesn't bring to mind a case

5 where I did, I will say.

6 Q Okay. Just bear with me here. Can you

7 look on the same page of the same Exhibit 55 at the

8 bottom, Item 16, documents sufficient to identify

9 the Aegis personnel responsible for conducting the

10 daily unregistered securities review for all trades

11 related to the relevant securities, including name,

12 title, and which of the trades in the relevant

13 securities they were responsible for reviewing. And

14 the response is on the following page, page six. It

15 says, not applicable. Please be advised that none

16 of the relevant securities were restricted at the

17 time the shares were deposited and/or received into

18 Aegis' accounts. As a result, the relevant

19 securities were not identified and/or flagged as

20 unregistered.

21 Do you see that?

22 A Yes.

23 Q Was one of your responsibilities to make

24 a determination as to whether or not securities were

25 restricted?

1 trading activity that RBC's AML Group identified at e
2 Aegis?

3 A I can't speak to the nature of the
4 e-mails that have come. I do know there have been
5 questions related to AML that have been sent and
6 required follow-up. Now, whether they represented
7 transactions or account setup, I don't know
8 specifically the nature of the e-mails.e

9 Q Could you look at your Exhibit 54 again,e
10 please, and turn to page nine of Exhibit 54. And e
11 you see subparagraph U when you get there at the top e
12 of the page. It says USGT. Do you see, looking
13 back at Exhibit 10 now, see the subject the account e
14 number there?

15 A Right.

16 Q And then if you match that account number
17 with what you see under U in Exhibit 54, do you see
18e that's what's listed in paragraph one, right?

19e A Not the 898 but the 19059.

20e Q And you are listed there as a trade
21e reviewer for trades in USGT, right, for that
22e account, which is [redacted]'s account?

23e A Yes.

24 MR. McCURDY: Again, he has testified and
25e it is important that he understand the account

1 review responsibility is not driven by the issue or e
2 the symbol.e

3 BY MR. BAGNALL:

4 Q Let me follow-up. Did you review [redacted]
5 [redacted] trading in [redacted]?

6 A I can't recall.

7 Q If you look at the top of the page ending
8 859 of Exhibit 10 and read between 12/12/2012 and
9 3/4/2013, the client received a total of 9,932,077
10 shares of USA Graphite, Inc. After having read
11e that, do you recall whether you saw an amount of
12e shares like that in USA Graphite, Inc in the Bank
13e Gutenberg account?

14 A I can't recall.

15 Q Does it jog your memory at all about any
16 trading in USA Graphite that Bank Gutenberg engaged
17e in that you reviewed?

18 A No.

19 Q Can you turn to the last page of Exhibit
20e 10, please. Can you -- this is -- I am sorry to do
21e this to you. Can you look at the front page? You
22e see the e-mail at the very top of Exhibit 10 is from
23 David Ferri to Kevin McKenna copying George Kott and
24 Stacy Kishpaugh. And he writes, Please see e
25e attached. And then the attachments at the top in

1 the e-mail header it says [redacted] and all response e
2 dot PDF. By the way these documents were produced e
3 to us, we understand that to be the last page, the e
4 page ending 861 on the attachment.

5 A Okay.e

6 Q Can you please read that attachment, page e
7 861 of Exhibit 10, and tell me if that refreshes e
8 your recollection as to whether or not you reviewed
9 any of the [redacted] trading.

10e A Again, I don't recall specifically that
11e issue.e

12e Q And do you believe that it is the case e
13e that there were no flags for the U.S. -- [redacted]
14e [redacted] trading because it was a DVP RVP account
15e and those flags were suppressed?

16e A I think that's likely.

17e MR. MCCURDY: Well, he said where there
18e were no flags.e

19e THE WITNESS: Oh, you said low-priced
20e securities, though, right?

21 BY MR. BAGNALL:

22 Q Let me ask it again. So we asked for the e
23 production of all reports that were related to
24 trading in [redacted] between October 2011 and March of
25 2013?e

1 A Uh-huh.

2 Q And there were none for [redacted]?

3 A Okay.

4 Q So we don't have any flags that were
5 produced. So my question wasn't limited to
6 low-priced securities. It was a question whether e
7 there were no flags for [redacted]'s trading in
8 [redacted] because those flags were being suppressed
9 because [redacted]'s account was to be in the RVP
10e account?

11e A On some levels it could have been. But
12 we have already seen an example of this potential e
13 that it may have flagged for other commission-based
14 items like that. But the likelihood is right. It
15 would not have been produced, particularly if we are
16 talking about the low-priced securities flag.

17 Q All right. I will take back Exhibit 10?

18 MR. BAGNALL: Do you want to ask
19 something?

20 MR. McCURDY: Yeah, maybe we should take
21 another quick break.e

22 MR. BAGNALL: We will go off the record
23 at 2:33 p.m., January 13, 2016.

24 (A recess was held.)

25 BY MR. BAGNALL:

1 A Yeah, I am still unsure of the question
2 when you say do you typically see this. It sounds
3 like you are saying it's a common occurrence.

4 Q I am asking you if it is a common
5 occurrence.

6 A I don't believe it to be, no, not to my
7 recall.

8 Q If you had seen it, would it be something
9 you would likely remember?

10 A I can't say. I mean, the last couple of
11 years since we have changed our guidelines, if it
12 was something that I needed to do some due diligencet
13t on because it had yellow or red flags, then I
14t probably would have some recall. Again, given that
15 amount of time that has passed, I can't account for
16 that as well.

17 Q And I put back in front of you here
18 Exhibit 57. And you will see that there is not
19 exception report for [REDACTED] Did you see that here on
20 Exhibit 57?

21 A Right.

22 Q Do you believe that's likely because the
23 [REDACTED] account was a DVP RVP account? t

24 A I think that's a reasonable conclusion.

25 Q Could you turn to the page ending 095 of

1 listed in paragraphs one and two. And you are
2 identified as a trade reviewer, right?

3 A Yes.

4 Q So if you could look at the page now back
5 to Exhibit 29 ending 794 and see the e-mail from Mr.
6 DeGidio to 810 compliance copying George Kott.
7 Could you read the E-mail that Mr. DeGidio sent,
8 please, and tell me if that refreshes your
9 recollection as to whether or not you reviewed

10t [REDACTED] trading to [REDACTED]

11 A Okay.

12 Q Does it refresh your recollection as to
13 whether or not you reviewed [REDACTED] trading in [REDACTED]
14 [REDACTED]?

15 A No, it does not.

16 Q Okay. Did you discuss [REDACTED] trading
17 in [REDACTED] with Mr. Terracciano?

18 A I don't recall doing so.

19t Q And, again, if you recall, if you look at
20 Exhibit 57 there is only one file for [REDACTED] which is
21 [REDACTED] And we looked at that earlier. And it didn't
22 mention anything low-priced securities as you
23 recall. It was -- I believe it was a commission
24 exception report, right?

25 A Yes.

1 Exhibit 28, please. At the very top of the page,
2 the first bullet says, [REDACTED]

3 A Yes.

4 Q And under that it says as of 7/15 the
5 company reported to have 702.7 million shares
6 outstanding. Between 8/15 and 10/30, the client
7 sold 422.4 million shares or 60 percent of the
8 outstanding shares. During the period the client
9 has been selling, the price has dropped by 50
10 percent. The company has generated no revenues.

11t Does reading that refresh your recollection as tot
12t whether or not reviewed [REDACTED] trading int
13 [REDACTED]?

14t A No, it is not.t

15t Q Okay. I will take back Exhibit 28. I amt
16 going to hand you what has been marked previously as
17 Exhibit 29. If you can look that over and let me
18 know when you are done. Again, I will represent to
19 you that you do not appear to be a sender or
20 recipient to any of the E-mails in this thread?

21 A Okay.

22 Q If you could look, please, at -- this is
23 Exhibit 54. And I will refer you to page one. This
24 is the trading in [REDACTED] You see the accounts for
25 [REDACTED] 19 -- that ends 19060 and 28349 are both

1 Q Did Mr. Terracciano ask you whether you
2 had identified [REDACTED] trading in [REDACTED]
3 [REDACTED]

4 A Not that I can recall.

5 Q Did Mr. Terracciano tell you that
6 [REDACTED] -- that Aegis had received an e-mail from RBC
7 indicating that [REDACTED] trading in [REDACTED]
8 [REDACTED] exhibited characterized commonly
9 associated with a pump and dump scheme?

10 A Not that I can recall.

11 Q As a result of receiving RBC's alert
12 regarding [REDACTED] trading in [REDACTED] did
13 Mr. Terracciano visit you and Mr. Golden and give
14 you instruction on how to investigate trading liket
15 this?

16 A I don't recall.

17 Q So you don't recall specific
18 conversations with Mr. Terracciano about [REDACTED]
19 trading in [REDACTED]? Do you recall generally
20 conversations with Mr. Terracciano in which he would
21 relay to you the substance of alerts from RBC?

22 A I do not recall that type of conversation
23 with him.

24 Q Were there general instances, again, not
25 specific to this, but general instances of

Exhibit 11

To: Bagnall, George[BagnallG@SEC.GOV]
Cc: Maher, Daniel[MaherD@SEC.GOV]; Sachar, Ricky[SACHARR@SEC.GOV]
From: Jackson, J@dorsey.com
Sent: Thur 3/31/2016 9:36:47 AM
Importance: Normal
Subject: RE: In the Matter of [REDACTED] -- ProSurv Settings

George-- Set forth below are the answers you posed with RBC's responses. Also, RBC informed us that it received the attached document from Aegis on November 18, 2013. RBC was not aware of whether it had previously produced this document to the SEC in connection with this matter.

RBC's Responses to the SEC's Questions Set Forth in George Bagnall's Email of March 10, 2016

Q1.e "How it informed Aegis, specifically, of the ProSurv Enhanced functions, particularly the function related to analyzing DVP/RVP accounts."e

Response: General ProSurv Enhanced functions: One WebEx training session to show how to access alert parameters, how to look at and change parameters, and turn alerts on/off. The WebEx did not specifically address DVP/RVP functions. The WebEx and discussion lasted about 20 minutes.

Q2.e "To produce copies of any documents it provided to, or communications it had with, Aegis regarding the ProSurv Enhanced function for analyzing DVP/RVP accounts, including any emails, brochures, manuals, instructions, or any other document on the topic?"e

Response: Aegis called and asked how to turn on DVP/RVP trades in Enhanced. RBC located the function and told Aegis where to access the function and turn it on. These conversations occurred just before Aegis turned on the DVP/RVP in ProSurv, as previously communicated.

SEC-RBC-E-0084684

Q2a. "We are particularly interested in any documents or communications that explained to Aegis the fact that DVP/RVP accounts were not analyzed by default in ProSurv Enhanced, but that such analysis could be enabled if Aegis desired."

Response: There are no such documents or communications.

Q3. "Whether correspondent firms are informed that ProSurv Basic does not analyze DVP/RVP accounts."

Response: RBC is not aware of any such communications.

Q4.e "If the answer to 3 is "yes," how it informed Aegis, specifically, of that fact."e

Response: NA.

Q5.e "If the answer to 3 is "yes," to produce copies of any documents provided to, or communications it had with, Aegis regarding the fact that ProSurv Basic did not analyze DVP/RVP accounts, including any emails, brochures, manuals, instructions, or any other document on the topic?"e

Response: NA.

Please let me know if you have any further questions. J

SEC-RBC-E-0094885

J Jackson

Partner



Description: cid:736091019@03082011-0D5D

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From: Bagnall, George [mailto:BagnallG@SEC.GOV]
Sent: Thursday, March 10, 2016 7:23 PM
To: Jackson, J
Cc: Maher, Daniel; Sachar, Ricky
Subject: RE: In the Matter of [REDACTED] – ProSurv Settings

J:

SEC-RBC-E-0084888

Thank you for getting back to us so quickly. We really appreciate it.

By way of follow-up, could you please ask RBC:

1.o How it informed Aegis, specifically, of the ProSurv Enhanced functions, particularly the function related to analyzing DVP/RVP accounts.o

2.o To produce copies of any documents it provided to, or communications it had with, Aegis regarding the ProSurv Enhanced function for analyzing DVP/RVP accounts, including any emails, brochures, manuals, instructions, or any other document on the topic?o

a.o We are particularly interested in any documents or communications that explained to Aegis the fact that DVP/RVP accounts were not analyzed by default in ProSurv Enhanced, but that such analysis could be enabled if Aegis desired.o

3.o Whether correspondent firms are informed that ProSurv Basic does not analyze DVP/RVP accounts.o

4.o If the answer to 3 is "yes," how it informed Aegis, specifically, of that fact.o

5.o If the answer to 3 is "yes," to produce copies of any documents provided to, or communications it had with, Aegis regarding the fact that ProSurv Basic did not analyze DVP/RVP accounts, including any emails, brochures, manuals, instructions, or any other document on the topic?o

Thank you again.

SEC-RBC-E-0094687

George

From: Jackson.J@dorsey.com [mailto:Jackson.J@dorsey.com]
Sent: Thursday, March 10, 2016 11:36 AM
To: Bagnall, George
Cc: Maher, Daniel; Sachar, Ricky
Subject: RE: In the Matter of [REDACTED] – ProSurv Settings e

George– Set forth below are your question and RBC's response. J

Question: Can you please contact RBC and ask them why the ProSurv Basic system, and the default settings in the ProSurv Enhanced system, are not set to analyze DVP/RVP accounts?

Response: To turn on the DVP/RVP review function in ProSurv Basic would meaningfully affect ProSurv system performance. Making DVP/RVP review the default setting in Basic would require that active review for all firms using Basic. As approximately 155 firms use ProSurv Basic, the volume of DVP/RVP trades that pass through the ProSurv analysis engine would severely degrade the speed and performance of the entire ProSurv system, causing slow performance and occasional ProSurv system crashes. Under the current settings, where DVP/RVP review is not activated as the default, firms using ProSurv Enhanced may still elect to activate DVP/RVP review if management believes that review is important to its compliance function.

When a firm moves to ProSurv Enhanced, the then-current settings are maintained. In other words, if a firm using ProSurv Basic, which has kept the default settings, moves from Basic to Enhanced, those Basic settings will remain the defaults for Enhanced. That firm may enter ProSurv system parameters to turn on the DVP/RVP review function at any time. RBC views function selection decisions to be the firm's, as each firm is in a better position to decide which functions are necessary for its business. RBC informs the firms of the available ProSurv functions they may wish to select.

SEC-RBC-E-0064888

Please let me know if you have any further questions. J

J Jackson

Partner



Description: cid:736091019@03082011-0D5D

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From: Bagnall, George [<mailto:BagnallG@SEC.GOV>]
Sent: Wednesday, March 09, 2016 2:45 PM
To: Jackson, J
Cc: Maher, Daniel; Sachar, Ricky
Subject: In the Matter of [REDACTED] – ProSurv

SEC-RBC-E-0064689

Settings

J:

I'm writing to follow-up the voice mail I left for you a moment ago. Can you please contact RBC and ask them why the ProSurv Basic system, and the default settings in the ProSurv Enhanced system, are not set to analyze DVP/RVP accounts?

Thank you.

George

George Bagnall
Senior Counsel
Division of Enforcement

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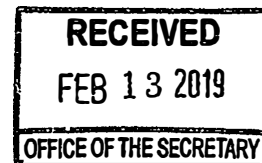
SEC-RBC-E-0084890

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SEC-RBC-E-0084891

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
FILE NO. 3-18414



In the Matter of

Eugene Terracciano,

Respondent

Judge Carol Fox Foelak

DIVISION OF ENFORCEMENT'S
REPLY BRIEF IN SUPPORT OF ITS MOTION FOR SANCTIONS

The Division of Enforcement ("Division") writes in reply to Respondent Eugene Terracciano's Opposition to the Division's Motion for Sanctions ("Opposition," cited as "Opp."). In the Opposition, Terracciano mischaracterizes the record, the law and the nature of the Division's requested relief. Contrary to Terracciano's argument, and as explained below and in the Division's Motion for Sanctions (the "Motion"), the requested two-year associational bar is an appropriate sanction to address Terracciano's egregious misconduct and is necessary to protect the public interest.

ARGUMENT

I. The Division Has Not Requested a Permanent Bar

The Division has sought only a two-year bar, with a right to re-apply. Terracciano casts that as a permanent bar, on the basis that it is "much more likely" his re-application would be unsuccessful. (Opp. at 3-4). But that is pure speculation; if Terracciano's record is as lengthy and pristine as he claims, the Securities and Exchange Commission ("Commission") and/or

FINRA may very well approve his re-application after the required two-year timeout from the industry. Terracciano's strained interpretation of the remedy framework would render the difference between a two-year associational bar and a five-year or lifetime bar meaningless.

As a result, the standards Terracciano cites (Opp. at 6-7) in *Steadman v. SEC*, 603 F.2d 1126 (5th Cir. 1979) and *SEC v. Bengier*, 64 F. Supp. 3d 1136 (N.D. Ill. 2014), both of which concern permanent bars, do not apply here. The Division's proposed relief is neither "drastic" nor "extraordinary." (Opp. at 6-7, quoting *Steadman* and *Bengier*). The Division could have sought a longer, or even permanent, bar, but instead requested relief that is consistent with precedent and proportionate to Terracciano's serious, consequential¹ violations. Terracciano's attempt to suggest otherwise should be disregarded.

II. Terracciano's Conduct Was Egregious

Terracciano argues that his conduct was not egregious. (Opp. at 7-9). But after attacking the Division for referring to the actual record (Opp. at 4), Terracciano invents a story about his conduct that has no basis in fact and contradicts the Consent Order.² Specifically:

A. *Terracciano Did Not "Detect" Red Flags and Did Not Take "Prompt, Effective Action"*

Nothing in the Consent Order or the record supports Terracciano's argument that he "did detect 'red flags' . . . and took prompt, effective action to address those concerns." (Opp. at 7).

¹ In the Opposition, Terracciano declines to address the fact that the Commission eventually sued a number of the entities involved in the improper trading. (Motion at 10-11, 13). Had Terracciano acted properly, their misconduct may have been detected earlier.

² That Terracciano now hopes to divorce the remedy determination from the actual "underlying facts and circumstances" of the case and the "findings to which Mr. Terracciano . . . consented" (Opp. at 4) is telling. Contrary to what Terracciano implies, those facts are directly relevant to the factors the Hearing Officer is to consider in making any remedy determination. (Motion at 3, 15).

As the Division explained in the Motion, it was Aegis's clearing firm, Royal Bank of Canada ("RBC"), that alerted Terracciano to what was plainly manipulative trading. (Motion at 6-13, 16). Worse, having been repeatedly confronted with evidence that Aegis's systems – and its registered representatives – were systematically incapable of flagging suspicious low-priced securities trading, Terracciano did virtually nothing to improve the system. (*Id.* at 13-14, 16, 17). Terracciano did not "detect" anything relevant.

Terracciano also falsely claims that he took "prompt, effective action" after receiving the AML Alerts. (Opp. at 7). As a basic matter, his failures to file SARs demonstrate that he was not "effective" in alerting regulators about blatantly improper trading. (Motion at 10). Nor was he "effective" in assessing why Aegis's systems failed to detect suspicious low-priced trading. Worse, Terracciano was far from "prompt." For example, with regard to ██████████'s suspicious trading in ██████████, Terracciano hesitated to close the account and even asked RBC to permit it to stay open on a limited basis. (Motion at 9-10 and Exhibit 8 thereto). And, after receiving the ██████████ AML Alert in February 2014, ██████████ was permitted to sell an additional 120 million shares of the stock before the account was closed. (Motion at 11-12 and Exhibit 9 thereto).

In sum, Terracciano falsely depicts himself as an effective and decisive compliance officer who was merely naïve about technical reporting requirements. In fact, the record reveals a halting, incomplete response to the AML Alerts and a complete failure to file SARs or address the obvious compliance issues the AML Alerts raised.

B. Terracciano's Failures Involve Far More Than the Three AML Alerts

Terracciano argues that his misconduct was "relatively isolated, especially when considered against the many thousands of accounts maintained at Aegis . . ." (Opp. at 9-10).

But as the Consent Order makes clear, the three AML Alerts are merely illustrations of broader failures both to file SARs on “numerous” suspicious transactions and to address Aegis’s systemic deficiencies. (Consent Order, cited as “CO”, at ¶¶ 7-8, 13). What’s more, while serving as Aegis’s AML CO, Terracciano willfully aided and abetted Aegis’s failures to file SARs on “hundreds of transactions.” (*Id.* at 2). Terracciano’s misconduct was widespread, not isolated.

C.e Terracciano Demonstrated a High Degree of Scienter

Terracciano argues that he lacks scienter. (Opp. at 10). But as the Consent Order states: “Terracciano *willfully* aided and abetted and caused Aegis’ violation of Section 17(a) of the Exchange Act and Rule 17a-8 thereunder.” (CO at ¶ 46, emphasis added). As a fallback, Terracciano argues that his scienter is “significantly ameliorated” by “the fact that he did detect and act on the underlying activity.” (Opp. at 10). But as discussed above, Terracciano did not “detect” anything, while his actions after receiving the AML Alerts represented both aiding and abetting Aegis’s violation of Exchange Section 17(a) and Rule 17a-8 thereunder, and also a failure to address Aegis’s systemic problems.

Although Terracciano emphasizes that he eventually closed certain accounts (Opp. at 7, 9), he did so only after he was explicitly told by RBC that the accounts were engaged in unlawful conduct. Indeed, the fact that he eventually closed certain accounts is itself evidence of his scienter. He knew the trading identified in the AML Alerts was suspicious (after being told); he knew, based on Aegis policies and his experience, that he should have filed SARs for those transactions; he knew closing an account is not a substitute for filing a SAR (Opp. at 10-11); but he nonetheless failed to file any SARs.

Terracciano also exaggerates the decisiveness and worth of the actions he did take. The record and the Consent Order demonstrate, however, that Terracciano actually hesitated to take action on ██████'s suspicious activity, allowed ██████ to continue trading, and did nothing to explore why no system or person at Aegis had alerted him to the suspicious trading that was the basis of the AML Alerts.

In short, his conduct does not “ameliorate” his scienter. Rather, it shows, at best, extreme recklessness. For that and the other reasons described above and in the Motion, Terracciano’s conduct was egregious.

III. Legal Precedent Supports a Two-Year Bar

A. Terracciano Fails To Distinguish In re Bloomfield

Terracciano fails to meaningfully distinguish his failures from the misconduct in *In re Bloomfield*. In that case, the Commission imposed a two-year bar and \$335,000 in penalties on Robert Gorgia, the AML officer for Leeb Brokerage Services (“Leeb”), for his failures to supervise and file SARs. *Bloomfield*, 2014 WL 768828 at *16-17 (Feb. 27, 2014). Gorgia’s failures are nearly identical to those here. He received multiple indications that certain Leeb customers engaged in suspicious trading of low-priced securities. Specifically, like Terracciano, he knew that Leeb’s clearing firm had raised concerns and halted trading in certain accounts. *Id.* at **11-14, 16-17. Yet, like Terracciano, he did little to follow-up and never filed SARs. *Id.* at **14, 16-17; *see also* Motion at 16-17.

Terracciano attempts to distinguish *Bloomfield* in two ways: by suggesting that Gorgia was more senior than Terracciano (Opp. at 8), and by arguing that, in contrast to Gorgia, Terracciano “follow[ed] up on suspicious activity, took prompt action to restrict and close accounts, and implemented enhanced procedures.” (*Id.* at 8-9). Neither argument is valid.

Seniority was not an issue in Terracciano's failures to file SARs. (*See* Transcript of the Investigative Testimony of Eugene Terracciano at 99:23-100:23, attached hereto as Exhibit 12 (explaining that Aegis's CEO did not have the authority to overrule a decision to file a SAR)). And, as described above, Terracciano did not "follow up" properly to ascertain why Aegis's systems and personnel had failed to alert him to the improper trading.³ (CO at ¶ 13). Hiso decision to close certain accounts and circulate a new requirement for DVP/RVP accounts⁴ did not meaningfully address Aegis's systematic inability to flag – or report – suspicious trading.

Accordingly, as in *Bloomfield*, a two-year associational bar is appropriate and in the public interest here.

B. In re Gilford Securities and In re Elizabeth Pagliarini Do Not Support Terracciano's Position

Terracciano cites *In re Gilford Securities, et al.*, Exchange Act Release No. 65450 (Sep. 30, 2011) and *In re Elizabeth Pagliarini*, Exchange Act Release No. 63964 (Feb. 24, 2011), as examples of more limited sanctions for willfully aiding and abetting violations of Exchange Act Section 17(a) and Rule 17a-8 thereunder. (Opp. at 13-15). But those settlements did not involve the kind of egregious conduct found here. Accordingly, Terracciano's sanction should be more severe.

³ Terracciano tries to distinguish *In re Jerard Basmagy* and *In re Park Financial* (discussed in the Motion at 19) on similar grounds, arguing that Terracciano was not comparably senior and did "follow up" properly. (Opp. at 13). For the reasons discussed above, neither argument is availing.

⁴ While Terracciano, in response to deficiencies identified by the Commission's Office of Compliance Inspections and Examinations, did send one email on November 18, 2013 regarding additional compliance procedures to be followed for trading in DVP/RVP accounts (CO at ¶ 31-33), the screening process did not improve. In fact, the February 2014 suspicious trading in [REDACTED]' account was allowed to occur despite the fact that the additional compliance procedures had not been completed. (Motion at 11-13; CO at ¶¶ 34-42).

In *Gilford Securities*, the AML officer (“Granahan”) “was responsible for daily reviews of employee and customer transactions, monthly customer account reviews, and filing SARs on behalf of Gilford.” (*Gilford Securities* OIP at ¶ 27). That is where the similarities between that case and Terracciano’s end. The *Gilford Securities* OIP states only that Granahan “knew, or should have known” that his firm was not filing SARs on certain suspicious activity. (*Id.* at ¶ 28). The settlement lacks any reference to the kind of egregious conduct found here: the repeated AML Alerts Terracciano received explicitly describing market manipulation; the fact that ██████████ was able to sell another 120 million shares after Terracciano had been alerted to its suspicious trading; Terracciano’s willingness to allow ██████████ to continue modified trading after being informed that ██████████ was likely engaging in a pump-and-dump scheme; and Terracciano’s failure to address the systemic failures that allowed Aegis’s customers to engage in this kind of activity. The facts here are more akin to those in *Bloomfield*, not *Gilford Securities*.

Similarly, in *Pagliarini*, the settlement order does not describe the repeated, egregious conduct found here. While Pagliarini “reviewed and approved all order tickets,” (*Pagliarini* OIP at ¶ 7), there is nothing in the settlement order to suggest that Pagliarini actually knew of the improper trading, much less that she repeatedly received emails explaining precisely why the trading was improper. At most, Pagliarini “fail[ed] to follow-up” on the suspect transactions. (*Id.* at ¶ 8). Terracciano, in contrast, was repeatedly presented with explicit information that multiple clients were engaged in manipulative trading, recognized that the trading was improper, but did not file any SARs or attempt to meaningfully address the systemic monitoring and reporting issues at Aegis.

Accordingly, Terracciano should receive a stronger sanction than the settling defendants in *Gilford Securities* and *Pagliarini*.

IV. A Two-Year Bar Is Necessary to Protect the Public Interest

The Division's requested relief is consistent with precedent and proportionate to Terracciano's egregious conduct. Terracciano argues, however, that it would be against the public interest to punish a well-intentioned compliance officer. (Opp. at 16-19). This argument again mischaracterizes Terracciano's systematic failure to fulfill his important role in detecting, stopping, and reporting ongoing fraudulent activity as simply a minor mistake. As demonstrated by the cases Terracciano cites and discusses in the Opposition, the Commission has recognized that failures by AML officers to file SARs are extremely serious breaches of their duties. Where, as here, a compliance professional has repeatedly and egregiously failed to fulfill his professional obligations to act to report illegal activity, a multi-year bar is appropriate.

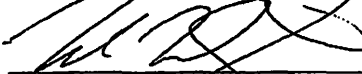
CONCLUSION

In sum, as described above and in the Motion and Consent Order, Terracciano willfully aided and abetted Aegis's violations of Exchange Act Section 17(a) and Rule 17a-8 thereunder, and his knowing and egregious conduct readily establishes that the bar requested by the Division is in the public interest. Accordingly, the Division requests that its motion be granted and that Terracciano be barred from the securities industry, with the right to reapply after a period of two years.

Dated: February 13, 2019

Respectfully submitted,

DIVISION OF ENFORCEMENT



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Counsel for the Division of Enforcement

In the Matter of Eugene Terracciano
Administrative Proceeding File No. 3-18414
Service List

Pursuant to Commission Rule of Practice 151, 17 C.F.R. § 201.151, I certify that the foregoing Division of Enforcement's Reply Brief in Support of its Motion for Sanctions Against Respondent Eugene Terracciano was filed with the Office of the Secretary of the Commission and served by email and UPS, on February 13, 2019, as follows:

Office of the Secretary
Securities and Exchange Commission
100 F Street, NE, Mail Stop 1090
Washington, DC 20549

(by hand)
(original and three copies)


Honorable Carol Fox Foelak
Administrative Law Judge
Securities and Exchange Commission
100 F Street, NE, Mail Stop 2585
Washington, DC 20549
Email: alj@sec.gov

(by Email)

Gregg Breitbart, Esq.
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Fort Lauderdale, FL 33394
Email: gbreitbart@kdvlaw.com
Counsel for Respondent

(by UPS and email)

Dated: February 13, 2019



Nicholas Margida
Counsel for Division of Enforcement

Exhibit 12

1 Is that simply because you can't remember since
2 time has passed, or because it was fuzzy when you started
3 and when you left? "Fuzzy" meaning Aegis did not
4 specifically put you in a position that was sort of a
5 roll-on type position.
6 A That's correct.
7 Q The latter?
8 A Yes.
9 Q Okay. What percent of your job as director of
10 compliance would you say was dedicated to AML CO
11 responsibilities?
12 A I would say 20 percent.
13 Q Okay. Were low-priced securities addressed in
14 the training modules?
15 A Yes.
16 Q Was AML monitoring for low-priced securities
17 addressed in the training module?
18 A Yes.
19 Q Of the branch employees, the 12 that we
20 discussed, who had supervisory and compliance
21 responsibilities, what percent of the responsibilities
22 were dedicated to compliance?
23 A Seventy-five percent.
24 Q Okay. What percent would you say was dedicated
25 to AML of the 100 percent, not of the 75?

1e A For those individuals in the branch you're
2 saying?
3 Q Yes, sir.
4 A I couldn't - I don't know
5 Q And what were their roles and responsibilities
6 outside of compliance?
7 A Those individuals did not report in to me at
8 the branch level, so I really can't opine on that. If
9 you are asking me do I know what else they did on a
10 regular basis, I really can't - I really wouldn't know.
11 Q Okay. In practice, who was ultimately
12 responsible for the decision whether or not to file a
13 SAR?
14 A In practice -
15 Q Yes.
16 A In practice, it was a joint decision
17 Q Between whom?
18 A Between members of the central compliance
19 function, the CCO, myself and whoever else in our
20 department had worked on gathering information
21 Q And by the "department," you mean the four -
22 A Yes, correct
23 Q Okay. Was Mr. Eide ever involved in SAR - let
24 me rephrase.
25 If suspicious activity was uncovered and the

1 group of compliance professions were discussing whether
2 or not to file a SAR, was Mr. Eide ever informed or part
3 of these discussions?
4 A No.
5 Q At what point would Mr. Eide become aware that
6 a SAR was filed or not?
7 A It depends - I would say that informing Mr.
8 Eide of filing SARs or me to file a SAR, would not be
9 predicated upon him saying yes or no. So we didn't need
10 his say-so to actually do that.
11 And I don't know if that answers your question.
12 Q Would he be informed if a SAR was filed or not
13 filed?
14 A Not necessarily, no.
15 Q Okay.
16 BY MR. BAGNALL:
17 Q Okay. Did Mr. Eide have the authority to
18 overrule a decision to file a SAR?
19 A No.
20 Q Was there ever a time when you were employed at
21 Aegis where you recommended that a SAR be filed but you
22 were overruled?
23 A No.
24 BY MS. ZERNES:
25 Q Who was responsible for the 314(a) request, for

1 compliance 314(a) request?
2 A I believe I had stated that I did the actual
3 review.
4 BY MR. BAGNALL:
5 Q For the record, Mr. Terracciano, can you tell
6 us what a 314(a) request is?
7e A If we're all on the same page, the 314(a), I
8 would actually go on the FinCen website and I would be
9 notified by e-mail through FinCen of the various accounts
10 or individuals, individuals' businesses or individual,
11 that showed up on that list. And then I would check the
12 database to make sure that those individuals were not on
13 our database. If we're talking about the same thing
14 BY MS. ZERNES:
15 Q Yes.
16 A Okay
17 Q And what would your next step be after you
18 checked the system?
19 A I would check the system. I would memorialize
20 that with the time and date when I did that, and then I
21 would enter that into a shared file in SharePoint
22 Q Okay. Thank you.
23 MR. BAGNALL: Let the record reflect that Ms
24 Zemes is stepping out of the room.
25 Give me a few more minutes and then we can