BEFORE THE

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C.

In the Matter of the Application of

Shlomo Sharbat

Fore Review of Action Taken by FINRA

File No. 3-19870

SHARBAT'S RESPONSE TO MOTION TO DISMISS APPLICATION FOR REVIEW AND TO STAY BRIEFING SCHEDULE

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Dated: August 11, 2020

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I. INTRODUCTION

Sharbat filed an Application for Review on July 2, 2020 ("Application") after FINRA barred him for life from associating with any FINRA members. On August 4, 2020, FINRA filed its motion to dismiss the Application and asked that the Commission stay the briefing schedule. FINRA asserts two main arguments in support of its motion. First, that Sharbat failed to exhaust his remedies before FINRA, and second, that the Application to the Commission was untimely and contained no allegations of "extraordinary circumstances" that would excuse the untimeliness. It then argues that the Application should therefore be summarily dismissed.

The reasons why the Commission should deny the motion to dismiss are four-fold. First, extraordinary circumstances do exist in this case and these circumstances caused Sharbat to not be able to file his appeal in the time set for it in FINRA's rules. Sharbat should get the opportunity to bring these extraordinary circumstances before the Commission. Second, FINRA's own undue conduct and the ambiguity in the wording in the only documents served by it and actually received

by Sharbat, caused Sharbat to not fully understand the exact nature of the sanctions he was facing and their gravity.

Additionally, the imposition of a lifetime ban on Sharbat by the Hearing Officer involves an exercise of discretion which requires review by this Commission. It was recently held that the Commission "must be particularly careful to address potentially mitigating factors before affirming a permanent bar." *Saad v. SEC*, 718 F3d 904, 913 (D.C. Cir. 2013) citing *Paz Sec. v. SEC*, 494 F.3d 1059 at 1065 (D.C. Cir 2007), as a bar for life by FINRA is the "securities industry equivalent of capital punishment." (Justice Kavanaugh in his concurring opinion in *Saad v. SEC*, 873 F.3d 297, 306 (D.C. Cir. 2017)[1].

Finally, construing the assertions contained in the Application in the light most favorable to Sharbat, should lead to the conclusion that Sharbat has made a reasonable showing that FINRA's departure from its method of service at the end of the proceedings against him, constituted a prejudicial error which militates against a summary dismissal.

II. PROCEDURAL AND FACTUAL BACKGROUND

For a long period throughout the disciplinary procedure FINRA initiated against Sharbat, FINRA effectuated service of process on Sharbat by all of the following methods: (1) via [redacted], Forest Hills, NY, [redacted] ("the CRD address"), (2) via FedEx to [redacted], Tel Aviv, Israel, [redacted] ("the Tel Aviv address"), and most significantly, (3) via email to Sharbat at an email address from which Sharbat regularly communicated with FINRA. In addition, a copy of each document was also sent by first-class mail

[1] The D.C. Circuit Court granted Saad's petition in part and remanded it back to the SEC to determine whether a lifetime bar was "excessive or oppressive" noting that the Commission had an obligation to ensure its sanction was remedial and not punitive. 873 F.3d at 301.

and email to Sharbat's attorney at the time, Irv Einhorn. The only documents that were not sent to Irv Einhorn and Sharbat's email were the default decision and the notice of default decision.

For each of these instances, but for the default decision and the notice of default decision, FINRA carefully noted in its motion that the certified mailing to the CRD address was returned unclaimed, the first-class mailing was not returned, but the FedEx delivery to the Tel Aviv address was signed for by Sharbat. Therefore, FINRA in its motion admits that it realized in real time that Sharbat was receiving notice of its documents *only when* sent to the Tel Aviv address via FedEx or to his email account (since only in these instances Sharbat replied, whether by signature or by responding to an email sent to him).

In each of FINRA's documents that were actually received by Sharbat, the text only generally explained that the relief requested by FINRA was simply that "one or more of the sanctions provided for under FINRA Rule 8310(a) of the FINRA Code of Procedure be imposed." In the motion for default, which was the last document actually received by Sharbat, the text explained that FINRA requests "that the Hearing Officer enter a Default Order barring Respondent Shlomo Sharbat for violating FINRA Rules 8210 and 2010, *and* [emphasis added] suspending him for six months and fining him $25,000 for violating Regulation M and NASD Rule 2110". This text presents the option of a bar for life and the option of a six months suspension as two options that can be imposed together, i.e., that may co-exist, even though there is no way (in reality) to bar someone for life and suspend them at the same time for six months only, as it is only possible to do one or the other. This language is therefore, vague and unclear on its face. It is confusing even for attorneys, and therefore obviously confusing for a layman. This language cannot give

proper and due warning, at the desired level of clarity, before imposing the "securities' industry equivalent of capital punishment"[2].

Therefore, in each of the documents actually received by Sharbat, the text explaining the possible sanctions he was facing was not specific (just a general notice that some sanction may be imposed) or that the text was vague and ambiguous on its face. This caused Sharbat, in fact, to never receive real notice of what he was facing.

Sharbat had come however, to reasonably rely on the service of process methodology that FINRA had established and consistently engaged in in the past, and in particular, on the expectation that he would be receiving any important legal documents from FINRA by email in addition to receiving FedEx delivery to the Tel Aviv address.

Most importantly however, in light of Sharbat's response only to emails or documents received at his Tel Aviv address, FINRA had come to realize that when Sharbat actually receives its documents, he returns acknowledgment of receipt by signing or by responding to FINRA's email. This was not the case with the notice of default decision and the default decision.

Accordingly, at the very least, minimal principles of due process and fairness are applicable to FINRA, a private, self-regulated organization, when it acts in an enforcement role and has the power to impose punitive sanctions. These standards required of FINRA, at the least, to make another attempt of service on a party that clearly did not receive the most important documents it sent, i.e., the only documents that clearly announced the punishment he had received and the right to appeal it. This is especially the case when such an organization abandons a long-used method of service it knew to be effective. In the circumstances known to FINRA at this stage of its correspondence with Sharbat (i.e., that if he receives a document he acknowledges receipt by

[2] *Saad v. SEC*, 873 F.3d 297, 306 (D.C. Cir. 2017).

signature or replies to an email), it was unreasonable of FINRA to assume that Sharbat had received due notice of the default decision.

At the least, FINRA could have attempted to serve those two last most important documents by email (when it realized that they were not received at the Tel Aviv address because Sharbat didn't return an acknowledgment of receipt by signing the documents served), a method FINRA knew by then that Sharbat had come to rely on, and which imposed no significant additional burden on FINRA.

It is for these reasons that Sharbat was unable to exhaust his administrative remedies (either by way of an appeal to FINRA's National Adjudicatory Council ("NAC") within 25 days after service of the default in accord with FINRA Rule 9311(a), or by filing a motion to set aside the default before the same adjudicating Hearing Officer pursuant to FINRA Rule 9269(c) in a timely manner, or appeal FINRA's decision to the Commission within thirty (30) days.

Moreover, further reasons, as described below, justify both Sharbat's delay in filing his application for review as well as a denial of FINRA's motion to dismiss.

III. **ARGUMENT**

Commission Rule of Practice 411(e) provides that "[t]he Commission will decline to grant summary affirmance upon a reasonable showing that a prejudicial error was committed in the conduct of the proceeding or that the decision embodies an exercise of discretion or decision of law or policy that is important and that the Commission should review."

As discussed above, the fact that FINRA established a course of dealing with Sharbat during the course of its entire investigation, on which course of dealing Sharbat reasonably relied, but failed to provide the same method of service when it served him the dispositive documents -

the notice of default and default decision which imposed a lifetime sanction on him - constitutes a reasonable showing that a prejudicial error was committed in the conduct of the proceeding.

Moreover, when a motion is made to dismiss a case summarily, the ruling body, in this case the Commission, must accept the allegations by the applicant as true. Accordingly, Sharbat has to be given the opportunity to convince the Commission that extraordinary circumstances existed in his case, justifying therefore a review of his application (pursuant to 17 C.F.R. §201.420(b)), without precluding this opportunity *ab initio* (by summarily dismissing his application).

In addition, the decision by the Hearing Officer to impose a lifetime bar on Sharbat also involves an exercise in discretion that the Commission should review. As noted in the *Saad v. SEC* cases[3] as well as in the *Destina Mantar*[4] case, this is consistent with the regular practices of the Commission.

Therefore, the Commission should not grant FINRA's motion.

A. FINRA's Conduct Constituted a Prejudicial Error in the Conduct of the Proceeding

The Commission should deny FINRA's motion to dismiss because FINRA failed to comply with its established procedure of providing Sharbat with actual notice of every step in its legal proceeding[5], constituting by that a prejudicial error in the procedure. In addition, FINRA failed to provide Sharbat clear and unambiguous notice of the possible sanctions he was facing

[3] *Saad v SEC*, 718 F.3d 904 (D.C. Cir. 2013); *Saad v. SEC*, 873 F.3d 297 (D.C. Cir. 2017).
[4] *Destina Mantar*, Exchange Act Release No. 79851, 2017 SEC LEXIS 194 at (Jan. 19, 2017).
[5] FINRA's motion to dismiss pg. 8, fn. 4.

(that were eventually imposed), nor a reasonably calculated method of notice to advise him of the outcome of the procedure and his rights to appeal it.

When a private organization is acting in an enforcement role, it must give a respondent the substance of procedural due process. Therefore, if it elects to employ a consistent means of providing notice in an enforcement proceeding, it would be objectively unreasonable, and violative of even minimal due process requirements, for it to abandon that methodology in the middle of a proceeding.

FINRA's unilateral decision to alter its methodology of service resulted in Sharbat's failure to receive its default decision, preventing him from exhausting his administrative remedies or filing a timely appeal. When attempting to take property from a party as a potential punishment, as was the case here, FINRA must clearly disclose the potential penalty in order to meet the requirements of due process. Failure to do so is fundamentally unfair.

When construing the assertions contained in Sharbat's Application in his favor, as is the standard in a motion to dismiss, and in light of FINRA's conduct, which caused Sharbat to remain with the wrong understanding that at most he would be suspended for six months, Sharbat has made a reasonable showing that prejudicial error was committed in the conduct of FINRA's proceedings.

FINRA Rule 9629 provides that "FINRA shall serve the decision [of default] on a Respondent by courier, facsimile or other means *reasonably likely to obtain prompt service* [emphasis added] when the sanction is a bar or an expulsion."

Rule 9629 calls therefore for heightened standards of providing notice with regard to default decisions in general, and with respect to default decisions that impose a bar – the Rule requires standards that are even higher than the heightened ones included in it anyway. Rule

9629(a)(1) requires "due notice" when discussing the possibility of entering a default decision against a party that failed to answer a complaint or appear for a hearing[6], and Rule 9629(d) requires an even higher standard of notice - "reasonably likely to obtain prompt service" - when serving the final decision of default that imposes a bar or an expulsion on a party.

In light of FINRA's experience with Sharbat during the proceedings against him, FINRA was unreasonable when after it learned that Sharbat did not return a signature acknowledging his receipt of the notice of default and the default decision, it decided not to send these documents to his email as well. This conduct did not amount to "due notice" or to a method "reasonably likely to obtain prompt service" as required by FINRA Rule 9629.

At this stage, therefore, it should have been apparent to FINRA that these methods of service were not even reasonably calculated to give Sharbat proper notice of either the sanctions imposed on him, or the time limits in which to challenge those sanctions.

FINRA's conduct was also contrary to Commission case law. In *Destina Mantar*, Exchange Act Release No. 79851, 2017 SEC LEXIS 194, at *11-*13 (Jan. 19, 2017), the Commission specifically ruled that just like the "cases challenging a bar imposed in expedited proceedings *where there is reason to believe* [emphasis added] the applicant did not have actual notice of FINRA's information requests or notices" and where the Commission regularly remanded the matter back to FINRA, it was similarly appropriate to remand the matter back to FINRA when "the record suggests that Mantar, the respondent, may not have had *actual* notice of FINRA's requests or notices" until her bar became effective. This, of course, is consistent with current case law cautioning that the Commission "must be particularly careful to address

[6] FINRA Rule 9269(a)(1) "The Hearing Officer may issue a default decision against a Respondent that fails to answer the complaint within the time afforded under Rule 9215, or a Party that fails to appear at a pre-hearing conference held pursuant to Rule 9241 of which the Party has due notice, or a Party that fails to appear any hearing that a Party is required to attend under the Rule 9200 Series of which the Party has due notice."

potentially mitigating factors before affirming a permanent bar." *Saad v. SEC*, 718 F3d, at 913 (D.C. Cir. 2013), citing *Paz Sec. v. SEC*, 494 F.3d 1059, at 1065 (D.C. Cir 2007).

This situation is thus distinguishable from that presented in *Patrick H. Dowd*, Exchange Act Release No. 83710, 2018 SEC LEXIS 1875, at *23 (July 25, 2018) (a case cited by FINRA in its motion) where the Commission ruled that it was "undisputed that Dowd received mail sent to the CRD address", and further, that Dowd conceded that FINRA provided him with the Bar Notice (*Dowd* at *20).

B. FINRA's Decision Embodied an Exercise of Discretion and there is an Important Issue of Law or Policy that Should be Considered and Which the Commission Should Review

The imposition of a lifetime bar by FINRA obviously embodied an exercise of discretion, in which FINRA did not give sufficient consideration to significant mitigating factors. It is up to the Commission therefore to determine whether or not the sanction imposed by FINRA is "oppressive or excessive." 15 U.S.C. § 78s(e)(2).[7] Among the factors that must be considered is whether there were any personal or professional stressors which might mitigate the penalty that was imposed. *Saad v. SEC*, 873 F.3d, at 299 (D.C. Cir. 2017). As noted in the Application for review, Sharbat's life was threatened because of the possibility he might testify before FINRA. In addition, Sharbat neither received a copy of the default judgment barring him from FINRA nor a written notice of it, as required in FINRA Rule 9629. As a result, Sharbat remained under the impression that at the worst, he would be suspended for six months. As a result of FINRA's

[7] "If the appropriate regulatory agency for a member, participant, or person associated with a member, having due regard for the public interest and the protection of investors, finds after a proceeding in accordance with paragraph (1) of this subsection that a sanction imposed by a self-regulatory organization upon such member, participant, or person associated with a member imposes any burden on competition not necessary or appropriate in furtherance of the purposes of this chapter or is excessive or oppressive, the appropriate regulatory agency may cancel, reduce, or require the remission of such sanction."

decision, Sharbat has been denied of his freedom to be a broker for good, even though he has not engaged in any wrongful actions that would harm investors and despite the Hearing Officer's finding that FINRA had failed to even make a prima facie case that Sharbat had engaged in any wrongdoing. These factors weigh heavily in favor of providing Sharbat an opportunity to be heard and regain his license.

In light of the recent developments in the case law (see, for example, *Saad v. SEC,* 873 F.3d 297), the Commission must not allow FINRA to prevent an applicant the opportunity to have the Commission consider his request to reverse a punitive decision of a lifetime bar, by granting a motion to dismiss. At the least, an applicant that requires the Commission to exercise its authority to review FINRA's discretion when it imposed a lifetime bar should not be denied that summarily.

C. Sharbat Should Be Granted the Opportunity to Present Additional Evidence Demonstrating that Extraordinary Circumstances Existed Which Excuses His Failure to Timely File His Application

In light of all the above, Sharbat should be granted the opportunity to provide evidence to convince the Commission that extraordinary circumstances justify the late filing of his Application. FINRA's attempt, on the one hand, to summarily deny Sharbat the opportunity to provide evidence of the threats he faced, by stating that his application lacks evidence to support his assertions[8], but on the other hand - asking to prevent him from the only chance to bring such evidence (by asking to summarily dismiss his application) - shouldn't be granted. In the interest of justice, Sharbat should be given the opportunity to try to convince the Commission that the threats he received have also amounted to extraordinary circumstances that justified his delay in attempting to appeal the sanctions imposed in the default decision.

[8] FINRA's motion to dismiss pg. 13.

IV. CONCLUSION

Sharbat's application for review should not be dismissed because he never received a copy of the default decision in time to exhaust the administrative remedies made available to him as a result of FINRA's conduct. In addition, Sharbat's appeal to the Commission, although made more than thirty (30) days after the final decision in his matter, should be allowed to move forward by reason of both FINRA's failure to provide him due notice of the default decision from which he appeals, as well as the extraordinary circumstances he was confronted with at the time, which were only recently resolved to the point that he now feels safe to present evidence to the Commission and FINRA.

Respectfully submitted,

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Dated: August 11, 2020