

UNITED STATES OF AMERICA
Before The
SECURITIES AND EXCHANGE COMMISSION
April 8, 2022

ADMINISTRATIVE PROCEEDING

File No. 3-20808

In the Matter of the Application of
LEK SECURITIES CORPORATION

OPPOSITION OF NSCC AND DTC TO
LEK SECURITIES CORPORATION'S MOTION TO STAY AND INCORPORATED
MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT

TABLE OF CONTENTS

	<u>Page</u>
PRELIMINARY STATEMENT	1
BACKGROUND	3
A. DTCC and Risk Management	3
B. Lek Securities Corporation	5
C. DTCC’s Determinations and the Hearing Panel’s Affirmance.....	6
D. Lek’s Application and Stay Motion	7
ARGUMENT	8
I. Lek has not established a strong likelihood of success on the merits.	8
A. The Decision addressed the appropriate substantive and procedural factors.	9
B. The Cease to Act is necessary to protect DTCC.....	11
C. Lek received a fair procedure.	13
D. The Hearing Panel properly found Lek made misstatements and omissions of material fact.	15
II. Lek has not established that it will suffer irreparable harm absent a stay.	15
III. A stay would have a substantial negative impact on DTCC, its members, and other third parties.	17
IV. A stay is not in the public interest.....	19
V. There is no basis to stay the imposition of a censure and fine for Lek’s violations of the Activity Cap.	20
CONCLUSION.....	22

TABLE OF AUTHORITIES

	Page(s)
 CASES	
<i>Bloomberg L.P.</i> , Exchange Act Release No. 83755, 2018 WL 3640780 (July 31, 2018)	8
<i>Citigroup Glob. Mkts., Inc. v. VCG Special Opportunities Master Fund Ltd.</i> , 598 F.3d 30 (2d Cir. 2010).....	8
<i>Dawson James Sec., Inc.</i> , Exchange Act Release No. 76440, 2015 WL 7074282 (Nov. 13, 2015).....	16, 19
<i>In re Revel AC, Inc.</i> , 802 F.3d 558 (3d Cir. 2015).....	8
<i>In the Matter of the Application of Alpine Sec. Corp. for Rev. of Action Taken by the Nat’l Sec. Clearing Corp.</i> , Release No. 87599 (Nov. 22, 2019).....	16
<i>In the Matter of the Application of Bruce Zipper for Rev. of Action Taken by FINRA</i> , 2017 WL 5712555	8, 16, 17
<i>In the Matter of the Application of International Power Group, Ltd. for Rev. of Action Taken by The Depository Trust Company</i> , Admin. Proc. File No. 3-13687 (Apr. 9, 2010) (decided Mar. 15, 2012), 2012 WL 892229	8
<i>In the Matter of the Application of KJM Sec., Inc. for Rev. of Disciplinary Action Taken by FINRA</i> , Release No. 88053, 2020 WL 416696 (Jan. 27, 2020)	8
<i>In the Matter of the Application of Paul H. Giles for Rev. of Action Taken by FINRA</i> , Release No. 92177 (June 14, 2021)	19
<i>In the Matter of the Application of Potomac Cap. Markets, LLC for Rev. of Action Taken by FINRA</i> , Release No. 91172, 2021 WL 666510 (Feb. 19, 2021)	17
<i>In the Matter of the Application of Robbi J. Jones & Kipling Jones & Co., Ltd., for Rev. of Disciplinary Action Taken by FINRA</i> , Release No. 91045 (Feb. 2, 2021).....	16

<i>In the Matter of the Application of Se. Invs., N.C., Inc. & Frank Harmon Black for Rev. of Disciplinary Action Taken by FINRA, Release No. 86097 (June 12, 2019)</i>	<i>16</i>
<i>Mitchell H. Fillet, Exchange Act Rel. No. 75054, 2015 WL 3397780 (May 27, 2015)</i>	<i>5</i>
<i>Nken v. Holder, 556 U.S. 418 (2009).....</i>	<i>8</i>
<i>Peter W. Schellenbach, Exchange Act Rel. No. 30030, 1991 WL 288493, *4 (Dec. 4, 1991) aff’d, 989 F.2d 907 (7th Cir. 1993)</i>	<i>5</i>
<i>Tex. E&P Partners, FINRA Disciplinary Proc. No. 2014040501801, at 33–34 (Dec. 13, 2016).....</i>	<i>5</i>
<i>Trevor M. Saliba, Exchange Act Rel. No. 91527, 2021 WL 1336324 (Apr. 9, 2021)</i>	<i>5</i>

STATUTES

17 C.F.R.	
§ 201.401.....	8
§ 240.17Ad-22(a)(13)	4
§ 240.17Ad-22(e)(4)(i)	5, 12
§ 240.17Ad-22(e)(6)(iii)	4
15 U.S.C. § 78q–1(b)(5)(A) and (B).....	13

OTHER AUTHORITIES

DTC

Rule 10.....	6
Rule 10, § 1(iv)(A) and (B).....	13
Rule 2	4, 13
Rule 22.....	7
Rule 9A	13

NSCC

Addendum B	13
Rule 15	13
Rule 2A	4, 13
Rule 2A.G	15
Rule 2A, § 1.G.ii	6
Rules 2B.....	4, 13
Rule 2B, § 2.B(b).....	15
Rule 37	6, 7
Rule 4	5
Rule 46	6, 11, 13
Rule 46, § 1	6, 12
Rule 46, § 1(G)	13
Rule 48.....	7

National Securities Clearing Corporation (“NSCC”) and The Depository Trust Company (“DTC”) (collectively, as appropriate “DTCC”), submit this opposition in response to the *Motion to Stay and Incorporated Memorandum of Points and Authorities in Support* (the “Motion”), served by Lek Securities Corporation (“Lek”) on Sunday, April 3, 2022.

PRELIMINARY STATEMENT

The Motion seeks a stay pending appeal of the decisions by NSCC and DTC to cease to act for Lek in spite of the fact that on March 10, 2022—after considering hundreds of pages of written testimony and argument, thousands of pages of exhibits, and two days’ worth of live testimony and argument—the Hearing Panel not only found Lek’s capital and liquidity to be inadequate but also identified numerous examples of false and misleading statements of material fact on Lek’s part. For example, Lek made “self-serving determinations of materiality and non-materiality” about what information it would provide in response to DTCC reporting requirements and information requests, which the Hearing Panel characterized as “evidence of an intentional act to mislead.”¹ The Hearing Panel also found that Lek made “knowing” and “material” “affirmative misrepresentations” to DTCC regarding the status of its sources of bank liquidity.² Lek demonstrated a habit of “[s]tretching facts and law to fit [it]’s needs of the moment” and “showed a repeated pattern of hair splitting and tortured interpretations in what was plainly an affirmative attempt to avoid providing DTCC with material information that LSC thought would put LSC in an unfavorable light and possibly lead to unfavorable determinations by DTCC.”³ Most seriously, the Hearing Panel found that Lek had engaged in “a pattern of deliberate obfuscation designed to mislead DTCC.”⁴

¹ Ex. 1, Decision at 16.

² *Id.* at 13-14.

³ *Id.* at 16, 19.

⁴ *Id.* at 19.

Thus, while Lek argues that the Hearing Panel was incorrect in concluding that Lek's liquidity is "highly suspect and unreliable,"⁵ Lek ignores the Hearing Panel's conclusion that dishonesty pervaded Lek's entire business such that Lek "presents an unacceptable risk" to DTCC, its membership, and the financial system as a whole.⁶ Under the circumstances, there is no lesser remedial action that can be taken other than to cease to act for Lek.

Lek cannot satisfy any of the four factors necessary to demonstrate that a stay pending appeal is warranted.

Lek does not have a substantial likelihood of prevailing on appeal. Lek's assertions that the Decision has no basis in the Rules and that it fails to consider aspects of its unsecured sources of financing are false. The Motion ignores the many material deficiencies the Hearing Panel identified in the Lek Holdings Note Program, which Lek has admitted is its primary source of funding for its NSCC Clearing Fund requirement, and the fact that NSCC and DTC Rules require members to have sufficient liquidity to support their risk activity. Lek also adopts a self-serving and narrow interpretation of NSCC and DTC Rules regarding reporting obligations in an effort to excuse the plainly material misrepresentations and omissions it made to DTCC.

The Motion fails to demonstrate that Lek will suffer irreparable harm in the absence of a stay. Lek's insinuation that it will go out of business as a result of DTCC's actions are completely unsubstantiated, supported only by conclusory statements from its CEO, Charles Lek. At most, it may be expected that Lek would experience ordinary effects of transitioning to a new "manner of conducting business,"⁷ which might include some loss of business, but no irreparable harm that would not be of its own making.

⁵ *Id.* at 12.

⁶ Motion at 11.

⁷ Motion at 15.

Meanwhile, a stay would present a significant risk of harm for DTCC and its members that would be subject to significant economic loss in the event Lek were to default on its obligations. Lek contends that the credit risk it poses is insignificant and that there is no risk of harm even if Lek defaulted, because DTCC's *other* members are financially sound and make their required Clearing Fund deposits. But this is not how DTCC's comprehensive risk management scheme works—the only way DTCC can protect against the risks of default to the extremely high level of confidence mandated by statute is by requiring *all* of its members to comply with their *own* financial requirements.

The public interest is not served by a stay pending extensive proceedings that jeopardize the financial position of DTCC, its members, and the public. It is better served by the orderly transition of the clearing functions Lek performs to a more financially responsible clearing member.

Lek's request for a stay should be denied.

BACKGROUND

A. DTCC and Risk Management

NSCC and DTC are wholly owned subsidiaries of The Depository Trust and Clearing Corporation. They are clearing agencies registered with the Securities Exchange Commission ("SEC" or the "Commission") pursuant to Section 17A of the Exchange Act, and are required to comply with Rule 17Ad-22 thereunder. NSCC provides central counter-party clearance, guaranteeing completion of each NSCC member's unsettled transactions in the event of a default. DTC is a central securities depository for U.S. transactions in equity and other securities. Both NSCC and DTC face significant credit risks associated with their activities—NSCC with the risk of completing unsettled trades in the event of a default and DTC with the risks associated with member's end-of-day net funds settlement of securities transactions on each

business day. Each must manage that credit risk with a high degree of confidence. NSCC, in particular, must have a “risk-based margin system” designed “to cover its potential future exposure to participants in the interval between the last margin collection and the close out of positions following a participant default” to a level of assurance exceeding 99 percent.⁸ NSCC and DTC have been designated as Systemically Important Financial Market Utilities (“SIFMUs”) because a failure or a disruption to either agency could increase the risk of significant liquidity problems spreading among financial institutions or markets and thereby threaten the stability of the U.S. financial system. As SIFMUs, NSCC and DTC must place a special emphasis on risk management.⁹

NSCC and DTC manage credit and market risk through their membership admission criteria¹⁰ and through ongoing monitoring of each of their members.¹¹ NSCC’s and DTC’s ability to monitor members’ financial and operational activity relies on each member providing complete and accurate information in a timely manner in response to affirmative reporting requirements and requests for information under NSCC and DTC Rules. Honesty and compliance with these obligations is the cornerstone of self-regulation and proper enforcement under the Exchange Act.¹²

⁸ See 17 C.F.R. §§ 240.17Ad-22(e)(6)(iii); 240.17Ad-22(a)(13) (defining “potential future exposure” to mean “maximum exposure estimated to occur at a future point in time with an established single-tailed confidence level of at least 99 percent with respect to the estimated distribution of future exposure”).

⁹ Ex. 7, Leibrock Hearing Aff. I ¶ 6.

¹⁰ See NSCC Rule 2A; DTC Rule 2.

¹¹ See NSCC Rules 2A, 2B; DTC Rule 2.

¹² See, e.g., *Mitchell H. Fillet*, Exchange Act Rel. No. 75054, 2015 WL 3397780, *14-15 (May 27, 2015); *Peter W. Schellenbach*, Exchange Act Rel. No. 30030, 1991 WL 288493, *4 (Dec. 4, 1991) *aff’d*, 989 F.2d 907 (7th Cir. 1993) (“[D]eliberate deception” of “regulatory authorities” “reflects strongly on the perpetrator’s fitness to serve in any capacity in the securities business.”); *Trevor M. Saliba*, Exchange Act Rel. No. 91527, 2021 WL 1336324, *26 (Apr. 9, 2021) (affirming full bar of individual investor for providing backdated compliance forms to FINRA); *Tex. E&P Partners*, FINRA Disciplinary Proc. No. 2014040501801, at 33–34 (Dec. 13, 2016) (upholding expulsion for backdating documents).

NSCC also manages credit risk through the collection of a required Clearing Fund deposit from each of its members. The Clearing Fund reflects the daily risks associated with each member's trading activities and is intended to provide sufficient funds for NSCC to draw upon to close out the member's unsettled positions in the event it defaults on its obligations to NSCC. The objective, as required by Rule 17Ad-22(e)(4)(i),¹³ is to cover any loss from default by a member with the member's required Clearing Fund deposit, *without* mutualizing the risk of a member default among any other members.¹⁴

B. Lek Securities Corporation

Lek is a broker-dealer registered with the SEC and the Financial Industry Regulatory Authority ("FINRA") and is a wholly-owned subsidiary of Lek Securities Holdings Limited ("Lek Holdings"). Lek became a member of DTCC in 1999.

While DTCC has always closely monitored the risks posed by Lek, concern over whether Lek could meet its financial obligations as a member increased significantly over the past two years after a substantial increase in its required Clearing Fund deposits in February 2021 and its loss over the same timeframe of a majority of its bank credit.¹⁵ These events seriously called into question Lek's ability to meet its Clearing Fund obligations. At the same time, Lek deliberately failed to report material developments in its financial condition, including the impending loss of its reliable bank financing and the replacement of that financing with a much less reliable promissory note from its parent, and failed to respond to DTCC's request for

¹³ See 17 C.F.R. § 240.17Ad-22(e)(4)(i).

¹⁴ See NSCC Rule 4 and Procedure XV; Disclosure Framework for Covered Clearing Agencies and Financial Market Infrastructures, NSCC ("NSCC Disclosure Framework").

¹⁵ Ex. 7, Leibrock Hearing Aff. I ¶¶ 16, 18, 20; Ex. 9, Leibrock Hearing Aff. II (Reply) ¶¶ 11-22.

information on its finances. The failures constituted the most serious breaches of its membership obligations.¹⁶

C. DTCC's Determinations and the Hearing Panel's Affirmance

On October 26, 2021, NSCC sent Lek a notice of NSCC's determinations to (i) cease to act for Lek pursuant to NSCC Rule 46, Section 1, and NSCC Rule 2A, Section 1.G.ii, subject to a hearing pursuant to NSCC Rule 37, and (ii) summarily limit Lek's clearing activity by imposing a cap of \$300 million (subsequently increased to \$400 million) of aggregate unsettled clearing activity as measured by the gross market value ("GMV") of its unsettled portfolio each business day coinciding with the approval of Lek's start-of-day margin call ("Activity Cap"), pursuant to NSCC Rule 46.¹⁷ The same day, DTC sent Lek a notice of DTC's determination to cease to act for Lek pursuant to DTC Rule 10, subject to a hearing under DTC Rule 22.¹⁸ NSCC and DTC's determinations were based on (1) Lek's weak capital and liquidity, particularly in relation to the level of its risk activity, (2) significant deficiencies in Lek's internal controls and its misrepresentations relating thereto, and (3) Lek's failures to report material changes in financial and business condition and its pattern of providing incomplete, misleading or inaccurate information in non-compliance with reporting requirements and DTCC requests. The Activity Cap was imposed to protect NSCC, its members, and investors during the pendency of any hearing Lek requested on the cease to act determinations.¹⁹

¹⁶ Ex. 8, Cuddihy Hearing Aff. I ¶¶ 13, 19-20; Ex. 10, Cuddihy Hearing Aff. II (Reply) ¶ 12.

¹⁷ Ex. 3, October 26, 2021 NSCC Notice.

¹⁸ Ex. 4, October 26, 2021 DTC Notice.

¹⁹ Ex. 8, Cuddihy Hearing Aff. I ¶¶ 31-32.

Lek does not dispute that it violated the Activity Cap six times between November 1 and 7, 2021.²⁰ NSCC notified Lek of its intention to censure and fine it \$20,000 for each violation pursuant to NSCC Rule 48 on November 5 and 7, 2021.²¹

Lek timely requested a Hearing, which was conducted over two days on February 17 and 24, 2022, in accordance with NSCC Rule 37 and DTC Rule 22. On March 10, 2022, the Hearing Panel issued the Decision upholding DTCC's determinations to cease to act, to impose the Activity Cap and to censure and fine Lek.

On Wednesday, March 30, 2022, DTCC, through counsel, informed Lek's counsel that NSCC intends to stop accepting trades for Lek on May 4, 2022 and the cease to act for Lek will become effective a week later on May 11, 2022. Lek was also informed that DTC intends to cease to act for Lek effective June 9, 2022.²² Though Lek now claims that it "to date has received no written notice of the dates upon which the Clearing Agencies intend to cease to act,"²³ in an April 4, 2022 email, DTCC's counsel plainly and unambiguously reiterated NSCC and DTC's intention to cease to act on the aforementioned dates that had been discussed verbally on March 30, 2022.

D. Lek's Application and Stay Motion

On Sunday, April 3, 2022, Lek served the Application, which seeks review of DTCC's determinations to cease to act for Lek and NSCC's determinations to impose the Activity Cap and censure and fine Lek. Concurrently, Lek filed the Motion to stay these actions.

²⁰ *Id.* ¶¶ 33, 35.

²¹ Exs. 5, 6.

²² Ex. 11, April 4, 2022 Email Counsel for DTCC to Counsel for Lek.

²³ *Lek Securities Corporation Supplement to Motion to Stay* ("Motion Supplement"), at 2.

ARGUMENT

A stay pending appeal is an “‘extraordinary remedy,’” and the movant bears the burden of establishing that relief is warranted.²⁴ The Commission considers four factors in determining whether to stay an SRO’s action: whether (1) the movant has established a strong likelihood of success on the merits; (2) the movant will suffer irreparable harm without a stay; (3) there is likelihood that another party will suffer substantial harm as a result of the stay; and (4) the stay is in the public interest.²⁵

“[E]ven if a movant demonstrates irreparable harm that decidedly outweighs any potential harm to the [stay opponent] if a stay is granted, [it] is still required to show, at a minimum, ‘serious questions going to the merits.’”²⁶ “Because the moving party must not only show that there are ‘serious questions’ going to the merits, but must additionally establish that ‘the balance of hardships tips *decidedly*’ in its favor, its overall burden is no lighter than the one it bears under the ‘likelihood of success’ standard.”²⁷

Here, each of the four factors weighs against granting Lek’s Motion.

I. Lek has not established a strong likelihood of success on the merits.

Lek’s argument regarding success on the merits rests on four grounds: (1) the Decision suffers from procedural and substantive flaws (pages 7-8); (2) a cease to act is not necessary to

²⁴ *Bloomberg L.P.*, Exchange Act Release No. 83755, 2018 WL 3640780, at *7 (July 31, 2018) (quoting *Nken v. Holder*, 556 U.S. 418, 432-34 (2009)).

²⁵ See Rule 401(d) of the Commission’s Rules of Practice, 17 C.F.R. § 201.401; *Order Denying Stay, In the Matter of the Application of International Power Group, Ltd. for Rev. of Action Taken by The Depository Trust Company*, Admin. Proc. File No. 3-13687 (Apr. 9, 2010) (decided Mar. 15, 2012), 2012 WL 892229, at *3.

²⁶ *In the Matter of the Application of KJM Sec., Inc. for Rev. of Disciplinary Action Taken by FINRA*, Release No. 88053, 2020 WL 416696, at *2 (Jan. 27, 2020) (quoting *In re Revel AC, Inc.*, 802 F.3d 558, 570 (3d Cir. 2015)).

²⁷ *Bruce Zipper*, Exchange Act Release No. 82158, 2017 WL 5712555, at *6 (Nov. 27, 2017) (quoting *Citigroup Glob. Mkts., Inc. v. VCG Special Opportunities Master Fund Ltd.*, 598 F.3d 30, 35 (2d Cir. 2010) (emphasis in original) (internal quotation marks and citation omitted)).

protect NSCC (pages 9-11); (3) DTCC failed to provide a fair procedure (pages 11-13); and (4) the Decision’s findings regarding Lek’s material misrepresentations and omissions do not comply with NSCC Rules (pages 13-14). As discussed below, all of the grounds are baseless, and Lek’s argument is unlikely to succeed on any of them.

A. The Decision addressed the appropriate substantive and procedural factors.

Lek argues that it is likely to prevail on appeal because the Decision suffers from “substantive and procedural” deficiencies, but none of these withstands scrutiny.

Lek claims that it “actually has *more* access to unsecured financing to fund NSCC funding requirements as of Oct. 26, 2021 than it did in January 2021.”²⁸ The “critical facts” Lek cites in support of its statement are that in January 2021, it had as unsecured financing “only \$8 million of the BMOH line of credit,” and as of October 26, 2021, it had “established a line of credit of [unsecured] \$10 million with Lakeside Bank” that “can be used to meet the NSCC margin call,” representing an increase in its unsecured bank financing.²⁹ However, that is directly contradicted by Mr. Lek’s sworn testimony that Lek had an additional \$7.5 million unsecured line of credit from Lakeside in January 2021 (totaling \$15.5 million) meaning it had *less* access to bank financing to support its NSCC funding requirements on October 26, 2021.³⁰ The Decision, Lek says, is “silent” on this issue; that is so because Lek’s claim is not true.

Lek also claims that the Decision “is stunningly silent about the amounts of volatility margin requirements (as opposed to initial margin requirements that LSC requires investors to pre-pay) and how those amounts compare to the combined amounts of the cash cushion, line of credit and LSC’s own equity.”³¹ But there is ample evidence in the record about the unknown or

²⁸ Motion at 7 (emphasis in original).

²⁹ *Id.*

³⁰ Ex. 12, Lek Hearing Affm. ¶ 110.

³¹ Motion at 8.

partly known components in the methodology Lek uses to anticipate its end-of-day Clearing Fund requirement. Lek's own expert testified about components of the Clearing Fund deposit requirement that cannot be calculated prior to accepting customer trades, as well as about the magnitude of the volatility margin.³² The Hearing Panel obviously considered the heightened credit risk posed by volatility margin requirements, which is substantial, and incorporated that into its Decision.³³

Lek also refers to its \$27 million minimum Clearing Fund requirement as something the Hearing Panel did not consider.³⁴ However, the Hearing Panel decided that the minimum requirement was not properly the subject of the Hearing.³⁵

In any event, Lek made same point to the Hearing Panel it makes in its Motion: that it has met its daily Clearing Fund requirements, including the \$27 million minimum, *in the past*. But the fact that Lek has posted \$27 million in Clearing Fund deposits previously does not assure its ability to continue to meet requirements that have been as high as \$85 million. Accordingly, the Decision correctly found that Lek's history of posting its margin "[w]hile true, [] is also simply not determinative, or even particularly relevant, to DTCC's determination to cease to act for [Lek]. While [Lek] is looking to the past, DTCC's mission is to look prospectively and must guard against what may happen."³⁶

³² Ex. 13, Affidavit of Dr. Emre Carr, ¶ 30. In addition, there is a mark-to-market component of Lek's end-of-day clearing fund requirement that cannot be assessed in advance. *Id.* ¶ 56 & n.44 (noting Lek cannot "substantially determine" the mark-to-market component of its Clearing Fund deposit requirement prior to a trade). Indeed, the Decision recognized that "Dr. Carr[] conceded[] NSCC is exposed to losses because securities prices can fluctuate between trade and settlement," and that "[g]iven L[ek]'s customers' heavy trading in illiquid and microcap securities, margin swings for L[ek] are even more likely to happen and be material. NSCC members must be able to account for potential swings as well as an initial margin estimate." Decision at 10-11.

³³ Decision at 7-8, 11 & n.8

³⁴ Motion at 8.

³⁵ Ex. 2, December 8, 2021 Hearing Panel Decision on Scope of Hearing.

³⁶ Decision at 11.

Ultimately, the Hearing Panel considered whether Lek had adequate liquidity sources to cover its Clearing Fund obligations going forward. The record showed that since February 2021, Lek's Clearing Fund requirements increased at times to almost \$85 million, against which Lek had only \$10 million in unsecured bank credit, cash of only about \$5-6 million and the Lek Holdings Note Program to meet those obligations.³⁷ The Hearing Panel, supported by ample evidence, found the Note Program is unreliable and "presents numerous disqualifying features" because, among other things: the funds were provided by customers who were not obligated to finance Lek's clearing fund requirements and Lek "has advanced no evidence that gives us any confidence it can adequately control its own processes."³⁸

B. The Cease to Act is necessary to protect DTCC.

In the Motion, Lek suggests that NSCC and DTC can cease to act for Lek only if it fails to meet the minimum excess net capital requirements or fails to meet a margin call.³⁹ That is not true. While NSCC could cease to act for a member if it failed to meet the minimum net capital requirement,⁴⁰ it is not the exclusive circumstance in which NSCC could cease to act. The risk management framework in NSCC and DTC Rules goes well beyond that requirement. Under Rule 46, NSCC can "prohibit or limit [a] participant's access to services" where, among other things:

(c) the participant is in such financial or operating difficulty, that the Corporation determined, in its discretion, that such action is necessary for the protection of the Corporation, the participants, creditors or investors . . .

(f) such participant has failed to comply with any financial or operational requirement of the Corporation . . .

³⁷ *Id.* at 11 n.6.

³⁸ *Id.* at 8-9.

³⁹ Motion at 9-10.

⁴⁰ *See id.* at 9 (citing Addendum B of NSCC's Rules).

(g) in any circumstances in which, in the discretion of the Corporation, adequate cause exists to do so.⁴¹

The Hearing Panel's Decision to uphold DTCC's determination to cease to act for Lek on each of these bases was firmly grounded and fully supported by the Rules and the evidence.

Lek, in its Motion, says the Decision "cites no evidence as to how the unlikely failure of a small firm like [Lek] would generate the type of dire consequences the DTCC claims justifies its conclusion."⁴² As discussed above, DTCC's and the Hearing Panel's position was that a member poses a greater risk where the member has substantially less reliable liquidity than its anticipated Clearing Fund requirement. As for the consequences, Lek suggests that even if it failed, NSCC collects enough margin from *other* members that DTCC, its members and the investing public are protected.⁴³ However, the Clearing Fund requirement is such that each member must deposit funds sufficient to cover fully *its own* risk posed to the clearance and settlement on default.⁴⁴ It is not designed for a member to have its risk subsidized by other members. NSCC simply cannot ignore the clearance and settlement risks posed to NSCC and its members by an individual member like Lek. If it did, NSCC would not be complying with its mandate to manage risk posed to the system by *each member* with the high level of confidence required by law.⁴⁵

⁴¹ NSCC Rule 46, Section 1; *see also* DTC Rule 10.

⁴² Motion at 9.

⁴³ *Id.* at 9-10.

⁴⁴ 17 C.F.R. §240.17Ad-22(e)(4)(i).

⁴⁵ The Staff Report concerning trading activity in "meme" stocks in January 2021, cited at page 10 of the Motion, has no application here. NSCC's decision to waive certain ECP charges in a unique circumstance of unprecedented levels of volatility was made in view of the unprecedented and isolated circumstances. NSCC carefully considered the market forces at play and adjusted the margin requirements in that limited situation accordingly. Unlike the limited exception in that circumstance, Lek is essentially asking NSCC here to make an exception for Lek every day, on an ongoing basis, on the financial strength of all of DTCC's other members. The Commission should not countenance Lek's request to do so.

Lek's Motion, like its dealings with DTCC are full of contradictions: On the one hand, it says its potential default will have no impact on DTCC, its members and the market;⁴⁶ on the other, it says "the repercussions to customers and the market would be significant."⁴⁷ It is more proof of Lek's indifference to the truth, and its tendency to say whatever it needs to in order to evade responsibility for its actions.⁴⁸

C. Lek received a fair procedure.

Lek states that "the actions taken by the Clearing Agencies were not based on any articulated, reasoned analysis but rather on an unfettered exercise of discretion."⁴⁹ Nothing could be further from the truth.

Each of NSCC and DTC identified the Rules under which it was taking action against Lek and the facts on which those actions were based, as required by statute.⁵⁰ NSCC's and DTC's October 26 Notices to Lek outlined in detail the conduct Lek engaged in and how that conduct violated NSCC and DTC Rules. The October 26 NSCC Notice explained that Lek's conduct violated NSCC Rules 2B, 15, and Addendum B, which warranted NSCC's determination to cease to act for Lek under NSCC Rules 46 and 2A, Section 1(G), and to impose the Activity Cap under NSCC Rule 46.⁵¹ The October 26 DTC Notice explained that Lek's conduct violated DTC Rules 2 and 9A, which warranted DTC's determination to cease to act for Lek under DTC Rule 10, Section 1(iv)(A) and (B).⁵² In the Decision, the Hearing Panel presented a well-reasoned application of the Rules to the facts.

⁴⁶ Motion at 9.

⁴⁷ *Id.* at 3.

⁴⁸ Decision at 16 (Lek "repeatedly made self-serving determinations of materiality and non-materiality, as well as simply hoping all would turn out well.").

⁴⁹ Motion at 11-12.

⁵⁰ 15 U.S.C. § 78q-1(b)(5)(A) and (B).

⁵¹ Ex. 3.

⁵² Ex. 4.

As noted above, NSCC and DTC Rules unambiguously provide that members must have sufficient resources to meet their financial obligations. Throughout the course of its dealings with Lek, DTCC made abundantly clear that it expected Lek to have sufficient liquidity to meet its Clearing Fund obligations on an ongoing basis.⁵³ Lek knew what its Clearing Fund obligations were. Accordingly, Lek's assertion that it "requested an amount of capital and level of credit facilities it would need to have," and that "NSCC refused,"⁵⁴ is simply untrue.

Lek says "there does not appear to be any precedent for issuing a cease to act directive to a fully-functioning and liquid broker-dealer like L[ek] (and DTCC cited no such authority in the DTCC Decision)."⁵⁵ NSCC and DTC Rules clearly provide that NSCC and DTC may cease to act for a member where the member is in financial or operational difficulty, and in their discretion they determine such action is necessary to protect DTCC, its members, and the public. For obvious reasons, those rules do not require that the member first become insolvent or default on its obligations before NSCC or DTC cease to act. And Lek's suggestion that its situation is unprecedented is simply incorrect. On a number of occasions, NSCC and DTC have been prepared to cease to act for firms that demonstrated financial or operational difficulty that could jeopardize DTCC, its members, or the public. With respect to firms for which DTCC has not proceeded with a formal cease to act, those firms took steps to increase capital and liquidity levels sufficient to meet their Clearing Fund obligations, merged with entities that had additional financial resources, or decided voluntarily to wind down their operations at DTCC. DTCC worked with those firms to do so in an orderly process.⁵⁶

⁵³ *E.g.*, Exs 14-17.

⁵⁴ Motion at 12.

⁵⁵ *Id.* at 3.

⁵⁶ Ex. 18, Cuddihy Decl. ¶¶ 4-5.

Finally, Lek asserts that DTCC “ha[s] the burden to show with particularity” why a different remedy, short of a cease to act, would not be appropriate. The Decision, however, expressly states that “DTCC’s determination that, were it to continue as a member, L[ek] could not be trusted . . . was supported by the evidence and proper.”⁵⁷ The Hearing Panel determined that because of Lek’s many failings “L[ek] presents an unacceptable risk” to DTCC, its membership, and the financial system as a whole.⁵⁸ The Decision clearly recognized that no lesser sanction is appropriate.

D. The Hearing Panel properly found Lek made misstatements and omissions of material fact.

In arguing the Decision improperly considered Lek’s failure to advise DTCC of adverse developments in its settlement bank and financing arrangements, Lek wrongly implies the exemplary events in NSCC Rule 2B, Section 2.B(b) are the only ones that can be considered material under NSCC’s Rules.⁵⁹ But the Rule clearly states that members must report events that “could have a material impact on such participant’s business and/or financial condition, *including but not limited to*” the ones listed. The Rule in no way limits the events that would have a material impact on a member’s financial condition that must be reported honestly and completely (whether affirmatively or in response to DTCC inquiries) under NSCC Rule 2A.G.⁶⁰

II. Lek has not established that it will suffer irreparable harm absent a stay.

The Motion falls well short of establishing that Lek will suffer irreparable harm absent a stay. To meet its burden on this issue, the movant must provide specific factual information

⁵⁷ Decision at 19.

⁵⁸ Motion at 11.

⁵⁹ *Id.* at 13-14.

⁶⁰ Stating that NSCC may cease to act “when such participant or its Controlling Management has a record that reflects . . . the applicant or its Controlling Management is responsible for [] making a misstatement of a material fact or has omitted to state a material fact to the Corporation in connection with application to become a member or thereafter.” NSCC Rule 2A.G.

demonstrating that the impact, absent a stay, would result in the destruction of its business.⁶¹

“[M]ere injuries, however substantial, in terms of money, time, and energy necessarily expended in the absence of a stay, are not enough to constitute irreparable harm.”⁶² Clearly, Lek has not met its burden.

Lek offers only two conclusory paragraphs from Mr. Lek in support of its claim that it will suffer irreparable harm.⁶³ He testifies that, upon implementation of the cease to act, Lek “will be required to notify its clients to make arrangements to transition L[ek]’s customers,” which “will cause a ‘run on the bank’ and result in immeasurable damage to L[ek]’s business and reputation in the market,”⁶⁴ and he states that Lek may need to downsize after implementation of the cease to act.⁶⁵ None of these speculative events rises to the level of a destruction of business sufficient to show irreparable harm. The Motion argues only that Lek will be “forced out of its **current manner of conducting business**” absent a stay.⁶⁶ Lek does not say it will be put out of business entirely and suggests the existence of a path forward even if the cease to act is implemented.

⁶¹ See *In the Matter of the Application of Robbi J. Jones & Kipling Jones & Co., Ltd., for Rev. of Disciplinary Action Taken by FINRA*, Release No. 91045 (Feb. 2, 2021) (“Without submitting evidence about an inability to meet financial obligations or continue in business because of the bars, we cannot find that Applicants have established they will suffer irreparable harm.”); *In the Matter of the Application of Alpine Sec. Corp. for Rev. of Action Taken by the Nat’l Sec. Clearing Corp.*, Release No. 87599 (Nov. 22, 2019) (suggesting failure to submit “information regarding, among other things, its expenses, level of profitability, or exhaustion of available resources” prevented SEC from determining a likelihood applicant is “likely to cease operations”).

⁶² *In the Matter of the Application of Bruce Zipper for Rev. of Action Taken by FINRA*, 2017 WL 5712555, at *4 (quoting *Dawson James Sec., Inc.*, Exchange Act Release No. 76440, 2015 WL 7074282, at *3 (Nov. 13, 2015) (internal quotation marks omitted) (collecting cases)); see, e.g., *In the Matter of the Application of Se. Invs., N.C., Inc. & Frank Harmon Black for Rev. of Disciplinary Action Taken by FINRA*, Release No. 86097 (June 12, 2019) (finding a claim that impact, absent a stay, will “severely hamper” operations is not irreparable injury.)

⁶³ Lek Ex. P, ¶¶ 10-11.

⁶⁴ *Id.* ¶ 10.

⁶⁵ *Id.* ¶ 11.

⁶⁶ Motion at 15 (emphasis added).

Similarly, Lek claims that “being able to self-clear” is Lek’s “key service differentiator” that will be lost in the event the cease to act is implemented.⁶⁷ But Mr. Lek’s affirmation in support of the Motion makes no mention of self-clearing as a “differentiator” and there is otherwise no support for this claim in the record. In its Motion and throughout the proceedings, Lek identified its primary business as being agency brokerage. That business can be performed by Lek without membership in DTCC, as an introducing broker clearing through another DTCC member.⁶⁸

Even where a movant alleges it “will be forced to cease operations absent a stay,” the other stay factors can outweigh the irreparable injury prong. For example, in *In the Matter of the Application of Bruce Zipper for Rev. of Action Taken by FINRA*, the Commission denied a stay where the movant “failed to show that his appeal raises a substantial question on the merits, let alone that he is likely to succeed” and where “the public interest and risk of harm to others decidedly outweigh any irreparable harm to [the movant].”⁶⁹ The Commission denied the stay despite finding the firm’s statements it would be forced out of business “do not appear entirely speculative.”⁷⁰

III. A stay would have a substantial negative impact on DTCC, its members, and other third parties.

NSCC and DTC Rules reflect a risk management framework designed to protect DTCC, its members, and the market from the risk of default and other financial and operational issues

⁶⁷ *Id.* at 16.

⁶⁸ Ex. 18, Cuddihy Decl. ¶ 5.

⁶⁹ Release No. 82158 (Nov. 27, 2017), at *6.

⁷⁰ *Id.* at *4-5 (relying on uncontested statements that FINRA communicated it intended to “shut down” business); see also *In the Matter of the Application of Potomac Cap. Markets, LLC for Rev. of Action Taken by FINRA*, Release No. 91172, 2021 WL 666510, at *1, *4 (Feb. 19, 2021) (denying stay for broker-dealer that failed to file audit report where “the other factors such as the fact that it has not raised a serious question on the merits” outweighed any harm Potomac might suffer).

suffered by its members. NSCC and DTC made the determinations to cease to act for Lek because it failed to meet DTCC's financial standards and repeatedly and willfully violated its reporting obligations. For the Commission to stay such actions would undermine the comprehensive risk management scheme set out by the Rules and place DTCC, its members and the market at risk.

In support of its claim that a stay would not harm third parties, Lek reiterates its argument that "NSCC is already required to require deposits from member firms that protect itself to a 99% level of confidence" and that Lek "has never missed a required margin payment."⁷¹ This argument fails because, under the statutory scheme, DTCC's *other* members should not have to cover for Lek's credit risk, especially where the Hearing Panel—on a fully-developed evidentiary record—finally determined that Lek "presents an unacceptable risk."⁷²

Lek claims its "pre-trade payments from investors to cover initial margin requirements under the Lek Holdings Note Program" are protective of DTCC, investors, and the market.⁷³ But again, Lek ignores the Hearing Panel's determination that the Lek Holdings Note Program "presents numerous disqualifying features" and that Lek "has advanced no evidence that gives us any confidence it can adequately control its own processes."⁷⁴ And, with regard to Lek's arguments concerning its access to unsecured financing and its current levels of excess net

⁷¹ Motion at 17.

⁷² Decision at 11; *see also id.* ("DTCC has an obligation to itself, its entire membership, and the financial system as a whole, to find and eliminate potential problems before they happen. And it must do so to a greater than 99 per cent confidence level.").

⁷³ Motion at 17.

⁷⁴ Decision at 8-9.

capital,⁷⁵ Lek cannot contest that its “reported capital and bank lines of credit do not meet L[ek]’s NSCC margin requirements.”⁷⁶

Finally, Lek suggests that the determinations to cease to act amount to a “corporate death penalty” that will have “repercussion to customers and the market.”⁷⁷ While harm to customers is commonly raised by movants to justify a stay, the Commission often has found that the risk of future harm to customers and others outweighs any potential benefit they might realize from a stay.⁷⁸ If a stay is granted and Lek defaults during the pendency of its review before the Commission, which could take some time, Lek’s customers and others undoubtedly will be harmed by the less orderly transition that would result.⁷⁹

IV. A stay is not in the public interest.

Lek’s argument that a stay would serve the public interest because it provides clearing and custody services to “Small Firms,”⁸⁰ does not withstand scrutiny. Lek’s speculative assertion that some small firms “might otherwise struggle to find a broker willing and able to clear their securities transactions”⁸¹ is conclusory and wholly unsupported. On the contrary, in DTCC’s experience, those firms should have many options for continuing their business with minimal or no interruption, including clearing through another DTCC member firm (or through

⁷⁵ Motion at 17.

⁷⁶ Decision at 7; *see also id.* n.10 (“Indeed, it appears that L[ek] has, or at least would need to, use cash obtained through the Lek Holdings Note Program just to meet its minimum Required Fund Deposit at NSCC.”).

⁷⁷ Motion at 3.

⁷⁸ *See Dawson James Sec.*, Exchange Act Release No. 76440, 2015 WL 7074282, at *3 (Nov. 13, 2015) (any potential harm to customers outweighed by FINRA’s concerns about movant’s ability to comply with securities laws and the threat movant posed to investors); *In the Matter of the Application of Paul H. Giles for Rev. of Action Taken by FINRA*, Release No. 92177 (June 14, 2021) (“[A]ssertions that [broker’s] clients could be harmed in some unspecified way are insufficient to meet his burden of demonstrating irreparable harm. . . . [Broker] has not produced any evidence or even alleged that his clients would be unable to find another comparable broker pending this appeal.”).

⁷⁹ Ex. 18, Cuddihy Decl. ¶ 7.

⁸⁰ Motion at 17.

⁸¹ *Id.* (citing Lek Ex. P, ¶ 6).

Lek under an arrangement in which Lek clears through another DTCC member).⁸² Lek's assertion that these "small firms" might have nowhere else to go is belied by Lek's contention that it may lose business as a result of a "run on the bank" where its clients flee to other firms.⁸³ Its claim demonstrates that even Lek knows there are other readily-available options for its clients,⁸⁴ and the public interest is better served by those customers and other broker-dealers having their trades cleared and settled by a more financially responsible broker-dealer.

NSCC and DTC Rules function to set up a robust risk management framework that is intended to protect the public. The public interest requires that the Rules be enforced to protect against the risk of default by a member. A stay, especially in view of the Hearing Panel's findings, does not serve this goal.

V. There is no basis to stay the imposition of a censure and fine for Lek's violations of the Activity Cap.

In a footnote, Lek purports to seek a stay of NSCC's determination to censure and fine Lek for its violations of the Activity Cap. Motion at 1 n.1. NSCC informed Lek in letters dated November 5 and November 7, 2021 that it intended to censure and fine Lek \$20,000 for each of its violations of the Activity Cap.⁸⁵ In the Decision, the Hearing Panel upheld NSCC's determination to impose the censure and fine on Lek.

Lek makes no effort in the Motion to explain why the Hearing Panel's decision to uphold the censure and fine should be stayed. Contrary to Lek's claim, the Hearing Panel did *not* uphold the censure and fines based on "the same . . . rationale for upholding the 'cease to act'

⁸² Ex. 18, Cuddihy Decl. ¶ 6.

⁸³ Motion at 15.

⁸⁴ Lek admits there are other "agency-only self-clearing broker dealers," including "other clearing brokers [that] will provide clearing services" to small firms. *Id.* at 1, 4.

⁸⁵ Exs. 5, 6.

determinations.”⁸⁶ Rather, the Hearing Panel found that “[o]ther than questioning whether imposition of the Activity Cap itself was warranted, a position we reject for reasons stated above, [Lek] offered no argument that it had not violated the Activity Cap,” and, therefore, “f[ound] as a factual matter that [Lek] did violate the Activity Cap.”⁸⁷

It is *undisputed* that Lek violated the Activity Cap on six occasions on November 1-5 and 7, 2021, and that the censure and fines were imposed for those violations. And the Motion includes no discussion whatsoever concerning whether Lek would be irreparably harmed by the imposition of the censure and fine, or any other factors in support of a stay of those actions.

⁸⁶ Motion at 1 n.1.

⁸⁷ Decision at 20.

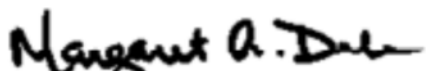
CONCLUSION

For the foregoing reasons, Lek's request for an interim stay should be denied.

Respectfully submitted,

PROSKAUER ROSE LLP

New York, New York
April 8, 2022

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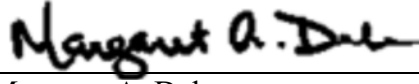
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ATTORNEY CERTIFICATION

Pursuant to Rule 154(c) of the Commission's Rules of Practice, I hereby certify that the foregoing document contains 6,736 words, exclusive of the tables of contents and authorities.

Dated: April 8, 2022

A handwritten signature in black ink, appearing to read "Margaret A. Dale", written over a horizontal line.


Margaret A. Dale

CERTIFICATE OF SERVICE

Pursuant to Rule 151(d) of the Commission's Rules of Practice, on April 8, 2022, the undersigned caused a true and accurate copy of this *Opposition of NSCC and DTC to Lek Securities Corporation Motion to Stay and Incorporated Memorandum of Points and Authorities in Support*, as well as the accompanying Index of Attachments and Attachments 1-18, to be served by electronic mail on the following persons:

DTCC Corporate Secretary (corporatesecretary@dtcc.com)
Kevin J. Harnisch (kevin.harnish@nortonrosefulbright.com)
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Dated: April 8, 2022



Margaret A. Dale

UNITED STATES OF AMERICA
Before The
SECURITIES AND EXCHANGE COMMISSION
April 8, 2022

ADMINISTRATIVE PROCEEDING

File No. 3-20808

<p>In the Matter of the Application of</p> <p>LEK SECURITIES CORPORATION</p>
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NSCC's AND DTC's INDEX OF ATTACHMENTS

<u>Exhibit</u>	<u>Description</u>
1	Hearing Panel Decision, dated March 10, 2022
2	Hearing Panel Decision on Scope of Hearing, December 8, 2021
3	October 26, 2021 NSCC Notice
4	October 26, 2021 DTC Notice
5	November 5, 2021 NSCC Notice
6	November 7, 2021 NSCC Notice
7	Leibrock Hearing Affidavit I
8	Cuddihy Hearing Affidavit I
9	Leibrock Hearing Affidavit II (Reply)
10	Cuddihy Hearing Affidavit II (Reply)
11	April 4, 2022 Email Counsel for DTCC to Counsel for Lek
12	Lek Hearing Affirmation
13	Affidavit of Dr. Emre Carr

- 14 July 21, 2021 DTCC Letter to Lek
- 15 July 28, 2021 Letter DTCC to Lek
- 16 August 3, 2021 Letter DTCC to Lek
- 17 September 13, 2021 Letter DTCC to Lek
- 18 Cuddihy Declaration in support of Motion to Stay

DTCC Attachment 1

Before a Hearing Panel of The Depository Trust & Clearing Corporation

-----X

In the matter of

LEK SECURITIES CORPORATION.

-----X

This Hearing Panel of the Depository Trust & Clearing Corporation (“DTCC”) has been duly constituted pursuant to the rules applicable to DTCC, including the Rules of the National Securities Clearing Corporation (“NSCC”)¹ and The Depository Trust Company (“DTC”).² This constitutes the Hearing Panel’s decision with regard to the appeal by Lek Securities Corp. (“LSC”) of certain determinations made by NSCC, DTC, and/or DTCC, regarding LSC, as identified particularly below.

As discussed herein, we find that the cease to act determinations by NSCC and DTC regarding LSC were appropriate and supported by the evidence. We also find that the activity cap, financial penalties and censures applied to LSC were also appropriate and supported by the evidence.

I. BACKGROUND AND PROCEDURAL HISTORY

DTCC, through its several subsidiaries, serves as the leading post-trade market infrastructure in the securities industry. It stands at the center of global trading activity, daily processing trillions of dollars of securities transactions. Through its subsidiaries, DTCC offers services in clearance, settlement, asset servicing, global data management and information services for equities, corporate and municipal bonds, government and mortgage-backed securities, derivatives, money market instruments, syndicated loans, mutual funds, alternative investment products and insurance transactions. DTCC is owned and governed by its user members, also known as participants, all of whom commit capital as owners, pay fees for its services and ultimately benefit from the safeguards, efficiencies and risk mitigation that DTCC provides to all its members.

NSCC provides central counter-party clearance and settlement services, guaranteeing payment and delivery of securities for counterparties through its Continuous Net Settlement system for virtually all transactions in equities and other types of securities in the United States. Because NSCC guarantees completion of each member’s unsettled transactions in the event of a default, it is potentially exposed to substantial credit risk. DTC is a central securities depository for U.S. transactions in equity and other securities. As such, DTC is faced with the credit risks associated with each participant’s end-of-day net funds settlement of securities transactions on each business day. (Affidavit of Timothy J. Cuddihy, sworn to December 23, 2021 (“Cuddihy Aff.”), at ¶ 6.)

¹ See NSCC Rules 37 and 46.

² See DTC Rule 22.

Each of NSCC and DTC has been named a “Systemically Important Financial Market Utility,” or “SIFMU,” by the Federal Financial Stability Oversight Council, two of only eight financial institutions functioning as Financial Market Utilities, or FMUs, in the United States to be named SIFMUs. A SIFMU is systemically important because the failure of or a disruption to a FMU that is so designated as a SIFMU could create, or increase, the risk of significant liquidity or credit problems spreading among financial institutions or markets and thereby threaten the stability of the entire United States financial system. Among other things, SIFMUs face heightened standards for their Boards of Directors, comprehensive and broader risk management expectations, and expanded rules and procedures requirements concerning liquidity risks.

To help fulfill its obligations, DTCC maintains robust risk management systems, including groups devoted to analyzing and managing Counterparty Credit Risk and Systemic Risk functions. Both NSCC and DTC are clearing agencies registered with the United States Securities and Exchange Commission (“SEC”) and are subject to strict requirements by the SEC and other regulatory bodies. DTCC’s risk management functions identify and monitor potential threats to NSCC, DTC, their respective members and participants, and the securities marketplace generally, from risks of a member’s default in its settlement obligations.

LSC is a wholly owned subsidiary of Lek Securities Holdings Limited. (Affirmation of Charles F. Lek, dated December 27, 2021 (“Lek Aff.”), at ¶ 13.) LSC has been a member of NSCC and a participant in the DTC system since 1999. (Lek Aff. ¶ 20.)

On October 26, 2021, DTCC sent two separate letters to LSC, each informing LSC of a cease to act determination regarding LSC by each of NSCC and DTC. Each letter was sent by Andrew I. Gray, Managing Director and Group Chief Risk Officer of DTCC.

By letter dated October 26, 2021, Mr. Gray provided to LSC a certain “Notice of NSCC’s Determination to Cease to Act for Lek Securities Corp. (“Lek”) and Summary Limitation of Clearing Activity” (the “October 26 NSCC Cease to Act Notice”). The cease to act determination was made pursuant to two separate NSCC Rules: Rule 46, Section 1, and Rule 2A, Section 1.g.ii.

As stated in the October 26 NSCC Cease to Act Notice, NSCC Rule 46, Section 1, provides in relevant part:

The Board of Directors may suspend a Member ... or prohibit or limit such participant’s access to services offered by the Corporation in the event that ... (c) the participant is in such financial or operating difficulty, that the Corporation determined, in its discretion, that such action is necessary for the protection of the Corporation, the participants, creditors or investors ... (f) such participant has failed to comply with any financial or operational requirement of the Corporation, or (g) in any circumstances in which, in the discretion of the Corporation, adequate cause exists to do so.

Also as stated in the October 26 NSCC Cease to Act Notice, with respect to the cease to act, NSCC Rule 2A, Section 1.G.ii, provides in relevant part:

The Corporation may cease to act for any participant when such participant or its Controlling Management has a record that reflects . . . the applicant or its Controlling Management is responsible for . . . making a misstatement of a material fact or has omitted to state a material fact to the Corporation in connection with its application to become a Member or thereafter . . .

The October 26 NSCC Cease to Act Notice informed LSC that the determination to cease to act for LSC was based upon three separate grounds, which are discussed below. Under this cease to act determination, once fully implemented, LSC will be restricted from access to the NSCC system.

In addition to the cease to act determination, the October 26 NSCC Cease to Act Notice also imposed an “Activity Cap” on LSC. Pursuant to the Activity Cap, LSC’s “aggregate unsettled clearing activity as measured by the gross market value of its unsettled portfolio each business day coinciding with the approval of Lek’s start-of-day margin call” was limited to \$300 million. The Activity Cap was imposed, like the cease to act, pursuant to NSCC Rule 46, Section 1, and was to remain in place pending any hearing and final determination regarding the cease to act determination.

The October 26 NSCC Cease to Act Notice stated, among other things, that LSC had a right to request a Hearing pursuant to NSCC Rules 37 and 46 for the purpose of objecting to NSCC’s cease to act determination and Activity Cap. The October 26 NSCC Cease to Act Notice further provided instructions to LSC on the procedures required to request such a hearing, should LSC wish to do so.

By separate letter dated October 26, 2021, Mr. Gray also provided to LSC a “Notice of DTC’s Determination to Cease to Act for Lek Securities Corp.” (the “October 26 DTC Cease to Act Notice”; the October 26 DTC Cease to Act Notice and the October 26 NSCC Cease to Act Notice are sometimes referred to herein collectively as the “October 26 Cease to Act Notices”). According to the October 26 DTC Cease to Act Notice, the cease to act determination was based on DTC Rule 10, which the letter stated provided in relevant part:

Based on its judgment that adequate cause exists to do so, the Corporation may at any time (a) cease to act for a Participant with respect to . . . transactions generally . . . Adequate cause for ceasing to act for a Participant or terminating a Participant’s right to act as a Settling Bank shall be deemed to exist if: . . . (vi) the Board of Directors, or a committee authorized thereby, shall have reasonable grounds to believe (A) that the Participant or its Controlling Management to be responsible for . . . (2) making a misstatement of a material fact or omitting to state a material fact to the Corporation in connection with its application to become a Participant or thereafter . . . or (B) that such ceasing to act is necessary for the protection of the Corporation, other Participants or Pledgees or to facilitate the orderly and continuous performance of the Corporation’s services . . .”.

The October 26 DTC Cease to Act Notice cited as its basis the same three grounds as in the October 26 NSCC Cease to Act Notice. Under this cease to act determination, once fully implemented, LSC will be restricted from access to the DTC system.

The October 26 DTC Cease to Act Notice informed LSC that it had a right to a hearing pursuant to DTC Rule 22.

By letter dated November 5, 2021 (the “November 5 NSCC Notice”), Mr. Gray informed LSC that NSCC had determined, in response to LSC’s request, to increase the Activity Cap applicable to LSC unsettled daily clearing activity to \$400 million. However, the November 5 NSCC Notice also noted that LSC had violated the \$300 million Activity Cap on each of November 1, 2, 3, 4, and 5, 2021. The November 5 NSCC Notice informed LSC that, pursuant to NSCC Rule 48, NSCC had determined to impose a \$20,000 penalty on LSC for each violation, for an aggregate penalty of \$100,000. The November 5 NSCC Notice also informed LSC that in addition to the financial penalty, LSC was being censured via publication to the NSCC membership. Like the two notices on October 26, 2021, the November 5 NSCC Notice informed LSC of its right to request a hearing regarding the imposition of these penalties.

By letter dated November 7, 2021 (the “November 7 NSCC Notice”), Mr. Gray informed LSC that because LSC had violated the Activity Cap (under both the \$300 million and \$400 million limit) on November 8, 2021, NSCC was imposing an additional censure and fine of \$20,000 on LSC. Like the other letters, the November 7 NSCC Notice informed LSC of its right to request a hearing regarding the imposition of the censure and fine.

By letter dated October 29, 2021, counsel for LSC formally objected to DTCC’s determinations as conveyed in the October 26 NSCC Cease to Act Notice and the October 26 DTC Cease to Act Notice and requested a hearing regarding each of NSCC’s and DTC’s determinations to cease to act for LSC and the Activity Cap. In addition, by letter dated November 8, 2021, counsel for LSC objected to the determinations in the November 5 NSCC Notice and the November 7 NSCC Notice modifying the Activity Cap and imposing fines and censures on LSC.³

Pursuant to NSCC Rules and DTC Rules, which are identical in this regard, a hearing panel (the “Hearing Panel”) was duly appointed to hear LSC’s appeal of the referenced determinations by NSCC and DTC. The undersigned members of the Hearing Panel are all members of the DTCC Board of Directors. As provided for in the NSCC Rules and DTC Rules, which are substantively identical in this regard, each of LSC and DTCC appeared before this panel, submitted written testimony and documents, and participated in a live hearing held over an electronic platform on February 17, 2022, and February 24, 2022, to hear further testimony of the witnesses who had submitted written testimony.

³ In its November 8, 2021, letter, LSC also objected to NSCC’s determination to increase LSC’s minimum Required Fund Deposit, as communicated in the November 5 NSCC Notice. In a written opinion dated December 8, 2021, this Hearing Panel ruled that NSCC’s determination to increase LSC’s minimum Required Fund Deposit was not subject to review under NSCC Rules by a Hearing Panel.

In total, LSC submitted affirmations or affidavits from three witnesses and a total of 87 documents or other exhibits. DTCC submitted three affidavits and a total of 61 documents or other exhibits. In addition to evidence, each party also submitted opening and reply memoranda of law and demonstrative exhibits used during closing arguments, which are included in the record. Also included in the record are various letters submitted by the parties on discrete issues, on their own initiative or at the request of the Hearing Panel. Finally, the record includes transcripts of the proceedings on each hearing day.

Following closing arguments on February 24, 2022, the Hearing Panel closed the record. The Hearing Panel read and considered all parts of the record in reaching its decision, whether or not specifically referenced herein. This opinion constitutes the decision of the Hearing Panel.

II. THE DETERMINATIONS TO CEASE TO ACT

As noted above, each of the NSCC and DTC determinations to cease to act for LSC were based on the same three grounds: (i) LSC's weak capital and liquidity position; (ii) LSC's deficient internal controls; and (iii) LSC's inadequate responses, failures to respond, and misleading representations, all in connection with communications with DTCC's risk management staff. We will address each in turn.

A. LSC's Weak Capital and Liquidity Position

The first, and in our view principal, reason for the October 26 Cease to Act Notices was that LSC's liquidity position, including its capital position, was so weak as to present an unacceptable settlement risk to NSCC and NSCC's members other than LSC.

Under both DTC and NSCC rules, membership can only be granted or maintained by a member that has the capability, in DTCC's judgment, to meet its financial obligations to DTCC.⁴

In the financial industry, settlement is the term applied to the exchange of payment to the seller and the transfer of securities to the buyer of a trade. It's the final step in a securities transaction. DTC is the central securities depository for equity securities, such as common stock and debt securities. DTC also processes other types of securities movements such as institutional deliveries, stock loans and financing transactions, including the pledging of securities to the Federal Reserve, commercial banks or the Options Clearing Corporation.

⁴ DTC Rule 2 provides, in part: "The Corporation shall approve applications only upon a determination by the Corporation that the applicant meets the standards of financial condition . . . (a) the applicant has demonstrated that it has sufficient financial ability to make any Required Participants Fund Deposit and Required Preferred Stock Investment and meet all of its anticipated obligations to the Corporation . . ."

NSCC Rule 1 provides, in part: "In furtherance of the Corporation's rights and authority to establish standards for membership, the Corporation shall establish, as it deems necessary or appropriate, standards of financial responsibility, operational capability, experience and competence for membership applicable to Members and to Limited Members."

NSCC Rule 46, section 1, provides, in part, "The Board of Directors may . . . prohibit or limit such participant's access to services offered by the Corporation in the event that . . . (c) the participant is in such financial or operating difficulty, that the Corporation determined, in its discretion, that such action is necessary for the protection of the Corporation, the participants, creditors, or investors . . ."

Settlement is the exchange of money and securities between the parties of a trade. Stock trades are settled in 2 business days (T+2), while government bonds and options are settled the next business day (T+1). Because it takes time to settle a trade and to protect the financial integrity of the market, NSCC requires collateral from its member firms. Because trading volume and risk changes every day, firms must adjust their collateral at NSCC daily. Brokers such as LSC must post collateral with NSCC because of the substantial financial risk between the time the securities are purchased to when they are settled.

In the settlement process, NSCC operates as a seller for every buyer, and buyer for every seller. This means that NSCC assumes the responsibility and the risk for receiving, delivering, and paying for the securities. A failure of this system could cause default after default, with the effect of jeopardizing the entire financial system. As Timothy Cuddihy, a Managing Director for Financial Risk Management for DTCC, testified at the hearing, it is through risk management assessments that DTCC seeks “not just to protect the clearing agencies themselves, but also to protect the members, because the clearing agencies mutualize risk among the members, and the market and as the Exchange Act requires.” (Tr. 2.24.22 at 490.⁵) NSCC is required to ensure to a confidence level that exceeds 99 percent that its risk-based margin system will cover its potential exposure to default by a member. (Affidavit of Michael Leibrock, sworn to December 23, 2021 (“Leibrock Aff.”) ¶ 7.)

LSC, like every NSCC member, is subject to stringent requirements to post margin collateral, and moreover to have available additional sources of liquidity and capital to meet its margin requirements. This is a particularly sensitive requirement in LSC’s specific case because a material aspect of LSC’s business involves transactions in microcap and illiquid securities⁶ that are subject to substantially higher margin requirements compared to other securities due to their limited liquidity and related price volatility. This issue became more critical in February 2021. At that time, an SEC-approved rule change significantly increased the effective NSCC margin requirements applicable to such securities. (See Lek Aff. ¶¶ 42-43; testimony of Timothy Cuddihy, Tr. 2.24.22 pp. 434-35; Affirmation of Emre Carr, Ph.D.,⁷ dated 27, 2021, (“Carr Aff.”) ¶ 48.) LSC has generated elevated NSCC clearing fund margin requirements several times due to its trading activity that includes microcap and illiquid securities. (See testimony of Timothy Cuddihy, Tr. 2.24.22 pp. 434-35; Carr Aff. ¶¶ 44-49; Leibrock Aff. ¶ 10.)

DTCC constantly monitors its members’ financial and liquidity conditions applicable to their margin requirements. This includes assignment of a credit rating, or “CRRM.” Over the past several years, LSC’s CRRM rating was within the range of what DTCC considers to be its riskiest members. LSC has been on DTCC “Watch List” since 2006 and has been under “Enhanced Surveillance” as an enhanced credit risk ever since DTCC created this separate category in 2013. (Leibrock Aff. ¶ 11.) LSC has been required to provide daily reporting on its capital since 2017 and its liquidity since 2021. (*Id.*) LSC’s available non-segregated cash (the cash and cash equivalents that are not already segregated in other accounts and may be accessed to meet LSC’s obligations to DTCC) ordinarily is a low percentage of its assets. LSC’s cash-to-

⁵ Citations to the transcript of the hearing held in this matter are in the form ‘Tr., date of hearing, and page.’

⁶ Microcap and illiquid securities represented 15-20% of Lek’s revenues during early- to mid-2021. (See Leibrock Aff. ¶ 10.)

⁷ Dr. Carr’s direct testimony is labelled “Affidavit” but actually is in the form of an Affirmation.

assets ratio has ranged between approximately 7% to a low of approximately 1% over the period from December 31, 2020, through September 30, 2021. (*Id.* at ¶ 14.)

As noted above, LSC's margin needs increased substantially in February 2021 due to a change in its margin requirements. However, this occurred at the same time LSC was suffering a substantial diminution in its reliably available sources of liquidity.⁸

At the end of 2020, LSC had \$100 million in bank financing from two reputable financial institutions: a \$75 million line of credit from Bank of Montreal Harris ("BMOH") and a \$25 million line from Texas Capital Bank ("Texas Capital"). Both lines were terminated in 2021. By October 2021, the only bank financing available (only in part) to LSC to meet NSCC margin requirements were two lines of credit with Lakeside Bank totaling \$30 million, of which the \$20 million line, at least, was secured by LSC's customer securities accounts.⁹

In an attempt to meet its liquidity needs, LSC implemented what it calls the "Lek Holdings Note Program." Under the Lek Holdings Note Program, as it was explained by Mr. Lek at the hearing in this matter, a customer of LSC who wishes to place a trade through LSC, acting as an "investor," loans money on an unsecured basis in an amount necessary to cover what LSC calculates to be the initial required margin on the trade to Lek Securities Holdings Limited ("Lek Holdings"), LSC's parent company, which then loans the money to LSC, which uses it to post the required margin at NSCC. The Lek Holdings Note Program in February 2021 was initially set at \$50 million, and then increased to \$100 million in April 2021. (Leibrock Aff. ¶ 25.) Mr. Lek testified that while anyone could loan money to Lek Holdings under this program, in practice only LSC customers who wished to place trades have done so. (Testimony of Charles Lek, Tr. 2.17.22 p. 86.)

LSC recognized that by February 2021 its bank financing was inadequate to meet its liquidity needs at NSCC. Mr. Lek conceded in his Affirmation that the new rule in February 2021 resulted in increased margin requirements for LSC that could not be met by LSC's existing or contemplated bank lines of credit. (*See* Lek Aff. at ¶¶ 42-43.)

LSC's own capital, while exceeding the regulatory minimum, is plainly inadequate to meet its liquidity needs. LSC's capital, as reported to DTCC, falls well short of its usual margin requirements. (*See* Leibrock Aff. ¶¶ 14-16.) The addition of the Lakeside lines of credit do not change this; together, LSC's reported capital and bank lines of credit do not meet LSC's NSCC margin requirements.¹⁰ Thus, even aside from movements in securities' values or other post-

⁸ LSC's failure to inform DTCC in a timely and forthright fashion in 2021 of the changes in its sources of liquidity is discussed in more detail below. However, for purposes of this Section, how and when DTCC learned of LSC's liquidity sources is not the issue; the issue is whether or not LSC's liquidity sources as they stood on October 26, 2021, were sufficient to allow LSC to remain a member of NSCC and a participant in DTC.

⁹ There appears to be some dispute as to whether the \$10 million line of credit was secured or unsecured. *Compare* Leibrock Aff. at ¶ 24 ("a secured \$10 million line of credit, collateralized by 20% of Lek's securities at DTCC") with Lek Aff. at ¶ 30 ("an additional unsecured loan facility with Lakeside in the amount of \$10 million"). We note the disagreement, but further note that the distinction makes no difference to our ultimate conclusion that LSC's sources of liquidity are inadequate to satisfy DTCC's needs.

¹⁰ Indeed, it appears that LSC has, or at least would need to, use cash obtained through the Lek Holdings Note Program just to meet its minimum Required Fund Deposit at NSCC. On November 5, 2021, NSCC increased LSC's

trade changes in margin requirements, LSC is dependent on the Lek Holdings Note Program to meet its basic margin requirements at NSCC.

Judged as to whether the Lek Holdings Note Program qualifies as a reliable source of margin funding, we find that it presents numerous disqualifying features.

First, while the Lek Holdings Note Program is certainly novel and inventive, there is no assurance whatsoever that it necessarily will work correctly. Even to fund an initial margin deposit,¹¹ the program depends on several steps that are not required to happen. As described by LSC, the first step is that when a customer orders a trade, LSC will calculate the NSCC margin requirement for that trade. Mr. Lek stated that this is done through its “Q6” risk management software platform. (*See, generally*, 2.17.22 Tr. at 157, *et seq.*) Then, as described by LSC, the customer is required to become an “investor” in Lek Holdings by loaning cash in the amount of the margin requirement to Lek Holdings (LSC’s parent company), which in turn loans the cash to LSC, which then uses it to post the required margin at NSCC. Not a single one of these steps (other than LSC’s requirement to post margin at NSCC) is required through any contract, rule, or other legally binding requirement. Customers may have note agreements with Lek Holdings, but they are not contractually obligated to loan money. Lek Holdings may have a note agreement with LSC, but it is not contractually obligated to loan money. Indeed, as far as we can tell, LSC itself is not actually required even by its own internal procedures to ask that its customers actually loan anything to Lek Holding before being allowed to trade.¹² While we are mindful of LSC’s argument that it has a strong incentive to make the program work properly, that is not the same as everyone involved, some of whom may not share LSC’s incentive, being legally obligated to fulfill their part in the arrangement.¹³

We note as well that DTCC has asserted a finding that LSC’s deficient internal controls warrant the cease to act determinations. As an independent basis for the cease to act

minimum Required Fund Deposit from \$20 million (already a heightened number due to LSC’s risk profile) to \$27 million. Mr. Lek testified that LSC does not use secured lines of credit to fund NSCC margin requirements (2.17.22 Tr. at 65). Even assuming that the \$10 million Lakeside line of credit is unsecured, even with its reported capital LSC does not have sufficient liquidity to fund its minimum Required Fund Deposit. Therefore, even if there was no trading activity at all, LSC would still have to utilize the Lek Holdings Note Program to obtain sufficient cash to fund its required Minimum Fund Deposit. Even assuming all other factors working perfectly, it is not clear that any of LSC’s customers would be willing to loan money to Lek Holdings under this program without making a corresponding trade.

¹¹ As discussed below, a fundamental problem with the Lek Holdings Note Program is it has no provisions for covering market swings or other changes in margin requirements between trade and settlement.

¹² LSC proffers two documents as governing its Q6 risk management platform. (*See* LSC Exs. 64 and 65 and Lek Aff. ¶ 37.) LSC Ex. 64 is dated February 2018, three years before the Lek Holdings Note Program was even instituted. LSC Ex. 65 is undated but makes no reference to the Lek Holdings Note Program. Thus, LSC has offered no evidence establishing any internal procedures at all governing how the Lek Holdings Note Program works.

¹³ There is also a stark difference between customer loans in the Lek Holdings Note Program and bank lines of credit, either committed or uncommitted. Established financial institutions such as banks are in the business of lending money. They have the reliable sources of capital to lend and the infrastructure to assure that lines of credit work effectively, reliably, and on short notice. DTCC cannot rely on any of the actors in the Lek Holdings Note Program the same way. DTCC’s risk management staff found that LSC presented no evidence to it regarding the reliability of the Lek Holdings Note Program prior to the October 26 Cease to Act Notices, and LSC also presented no evidence in this proceeding showing that the program was a reliable source of funds.

determinations, this is discussed and rejected below. However, concerns about LSC's internal controls are a significant factor in our liquidity determination. Certainly, LSC has advanced no evidence that gives us any confidence it can adequately control its own processes. Certain facts such as the outdated risk management controls that on their face do not involve the Lek Holdings Note Program, yet are advanced as part of it, are certainly important. Also important, as discussed below, are the repeated instances of LSC making misleading statements to DTCC, including statements regarding its internal controls.

Regarding an independent consultant's report by BRG (defined below), LSC made representations to DTCC to persuade DTCC to return a portion of an adequate assurance deposit to LSC. Following the filing of an SEC complaint against LSC in 2017, NSCC requested and received a \$1.9 million additional adequate assurance deposit from LSC. (*See* DTCC Ex. 59; Leibrock Aff. ¶ 69.) FINRA filed a complaint against LSC in 2018. (*See* DTCC Ex. 59.) LSC settled both lawsuits. (*Id.*) At LSC's request, NSCC returned half of the additional deposit (\$950,000) in May 2020, but retained the other half pending LSC's certification that it had complied with several components of LSC's settlements with the SEC and FINRA. (*Id.*) In June 2020, LSC made all the necessary certifications to DTCC, including that it had fully complied with the BRG report, and NSCC returned the remaining \$950,000 of the additional deposit. (*See* Leibrock Aff. ¶ 69; DTCC Ex. 50.) This certification to DTCC was false: LSC had not fully implemented all of the recommendations of the BRG report. That LSC had concerns with the BRG report, legitimate or not, is simply beside the point, as is whether or not LSC had a report from another independent consultant that did not make findings similar to BRG. The point is, LSC made certain representations to DTCC regarding its internal controls that it knew were false.

Also troubling in this regard are statements made by Mr. Lek in his testimony in this proceeding concerning FINRA's statements regarding the Lek Holdings Note Program. In his Affirmation, Mr. Lek, the chief executive officer of LSC, indicated that information provided by LSC had "answered FINRA's questions about the Lek Holdings Note Program and alleviated any concerns it had." (Lek Aff. ¶ 130.) Mr. Lek further testified in his Affirmation that in a telephone call Brian Kowalski, FINRA's Senior Director of Risk Monitoring, "acknowledged that FINRA now believes that the Lek Holdings Note Program adequately addresses any liquidity risks associated with NSCC funding requirements." (*Id.*) These statements were knowingly false. In reply to this Affirmation, DTCC submitted an Affidavit from Mr. Kowalski in which Mr. Kowalski testified that Mr. Lek's statements regarding what FINRA had told LSC about the Lek Holdings Note Program were incorrect and that FINRA "continues to have concerns on the subject of whether the Lek Holding Promissory Note Program adequately addresses liquidity risks associated with NSCC funding requirements." (Affidavit of Brian C. Kowalski, sworn to January 15, 2022, at ¶4.)

During the live cross-examination of Mr. Kowalski by LSC's counsel on February 24, 2022, LSC used a transcript of a video conference involving LSC and FINRA representatives on December 10, 2021. In response to a request from DTCC's counsel during the hearing, LSC was required to produce both the transcript and a recording of the audio portion of that video conference. (*See* LSC Exs. 87 and 86, respectively.) DTCC moved that the transcript be admitted into evidence; LSC objected on the basis that the recording of the video conference,

rather than the transcript, was the true evidence of the video conference. The Panel accepted both the recording and the transcript into the record. *See* Tr. 2.24.22 at pp. 394-401. We note that we find no material difference between the transcript and recording and cite to the transcript as an accurate reflection of the audio portion of the video conference.

The evidence of the call proves unequivocally that Mr. Lek's statements were not accurate. Indeed, the divergence is so great that the conclusion is inescapable that the divergence could not be the result of a mere misunderstanding but must be knowing. The evidence of the call shows that, among many other statements, Mr. Kowalski said, "And so where I would agree is that we have an understanding, again, I don't think we're completely comfortable . . ." (LSC Ex. 87 at p. 2.) Moreover, Ornella Bergeron, a FINRA Senior Vice President and in an even more senior risk management position at FINRA than Mr. Kowalski,¹⁴ also took part in the December 10, 2021, call and was unmistakable in stating FINRA's position. "The way with the current lines that you have, we're definitely not comfortable with the liquidity." (LSC Ex. 87 at p. 13.) In light of having participated in this call and having access to the recording and transcript prior to his written testimony, Mr. Lek could not have reasonably believed that his testimony to this Panel regarding FINRA stating that the Lek Holdings Note Program adequately addressed LSC's NSCC liquidity risks was accurate.

This is not a trivial point, or simply a "gotcha" moment. As discussed above, the Lek Holdings Note Program is not based on legally enforceable obligations – at virtually every step it is based on optional acts that may or may not be done in the course of future actual trading. LSC is asking DTCC to accept on faith that because LSC has an incentive not to go out of business, it will ensure that the Lek Holdings Note Program always works perfectly and DTCC and the financial system are not put at risk. However, as demonstrated by the factors just discussed, as well by the numerous concerns regarding DTCC's many attempts to obtain information from LSC discussed in Section II.C. below, DTCC cannot be expected to take LSC's representations at face value. In the course of its dealings with DTCC's risk management staff and in the course of these proceedings, LSC has failed to demonstrate the candor and openness necessary for DTCC to accept its representations.

The participants in the note program as well are an unknown to DTCC and to the extent known, insufficient. (*See* Leibrock Aff. ¶¶ 27-29; Cuddihy Aff. ¶ 29.) Lek Holdings itself has no audited financial statements, but it does not appear that that entity itself has sufficient assets to fund the program on its own. (Leibrock Aff. ¶ 27.) The customer/investors who are to be the ultimate source of cash have also not been vetted as to whether they are reliable sources of capital and are, at any rate, not established financial institutions. DTCC simply does not know who or what they are and whether or not they can be relied on as dependable lenders.

Furthermore, even if working at its ideal, the Lek Holdings Note Program only deals with the initial margin requirement at the time of the trade.¹⁵ Settlement occurs days after the trade. There can be fails. And the value of the trade can vary greatly after it is put on. As LSC's expert

¹⁴ *See* Testimony of Brian Kowalski, 2.24.22 Tr. at 377-78.

¹⁵ Even calculating the initial margin requirement at the time of the trade is something of a hope, not an exact science. There are multiple components involved and there can be no assurance a calculation in advance will be accurate.

witness Dr. Carr, conceded, NSCC is exposed to losses because securities prices can fluctuate between trade and settlement. (Carr Aff. ¶ 30.) Simply put, in the two days between a trade and settlement, a securities' value can change significantly, and the margin required to cover a potential failed trade would change significantly with it. Given LSC's customers' heavy trading in illiquid and microcap securities, margin swings for LSC are even more likely to happen and be material. NSCC members must be able to account for potential swings as well as an initial margin estimate.

LSC has essentially no liquidity sources, and certainly no reasonably assured liquidity sources, to compensate for significant moves in margin requirements in the time between trade and settlement. The two most likely sources for NSCC members for increased margin requirements are a firm's own capital and bank lines of credit. LSC has little capital of its own with which to work, and extremely small lines of credit with Lakeside as compared to its margin requirements.¹⁶

LSC argues that it is purely an "agency" broker acting for customers and does not engage in proprietary trading. In LSC's view, this means that it presents a lower risk profile for DTCC. We disagree. From a settlement risk perspective, the distinction is irrelevant. A trade on NSCC's books presents the same settlement risk profile to NSCC regardless of whether the NSCC member put the trade into the DTCC system acting as a broker or a principal.¹⁷

LSC also emphasizes that it has never failed to meet a NSCC margin call or other material DTCC obligation. While true, it is also simply not determinative, or even particularly relevant, to DTCC's determination to cease to act for LSC. While LSC is looking to the past, DTCC's mission is to look prospectively and must guard against what may happen. With that in mind, even LSC conceded that were it to fail even once it would be out of business. Unfortunately, a failure by LSC would not be a failure for LSC alone. It would cause harm to DTCC and potentially the entire financial system. That is why DTCC maintains a risk management department and engages in extensive analyses of its members to find potential risks. If it were enough to remain a member to have never caused a default, DTCC would not need a risk management function at all. But it is not enough. DTCC has an obligation to itself, its entire membership, and the financial system as a whole, to find and eliminate potential problems before they happen. And it must do so to a greater than 99 per cent confidence level. Looked at prospectively, as DTCC must, and not just retrospectively, as LSC urges, LSC presents an unacceptable risk.

¹⁶ LSC's balance sheet shows only \$5,270,685.80 in total current assets as of June 30, 2021 (DTCC Ex. 36) and its lines of credit with Lakeside Bank are only a \$20 million secured line and a \$10 million line that may be either secured or unsecured, while its margin requirements have at times exceeded \$80 million. (*See, e.g.*, Carr Aff. ¶ 44; Leibrock Aff. ¶ 16.)

¹⁷ There is also the possibility of trades being placed into the DTCC system not subject to LSC's purported internal risk management controls. A "correspondent clearing relationship" is one in which trades may be placed through a member by a party other than the member. During his testimony, Mr. Cuddihy stated that it appeared to him from LSC's trading activity that LSC may have correspondent clearing relationships with firms that have the ability to place trades through LSC, and that these may not be subject to review under LSC's internal risk management controls at all. (2.24.22 Tr. 438-441.) If true, this could present another serious risk to DTCC. However, consideration of this factor, while interesting, is not part of our decision.

Were the Lek Holdings Note Program just one part of a comprehensive set of liquidity sources, it might prove acceptable as part of a robust set. However, as the primary source it is completely inadequate. It is simply not sufficiently reliable or robust. Essentially, LSC has a “single threaded” source of liquidity, and that single thread is itself highly suspect and unreliable.

Accordingly, we find that DTCC’s determinations in the October 26, 2021 Cease to Act Notices on the grounds that LSC’s capital and liquidity are inadequate was supported by the record, and we affirm it. We stress that we find this basis, independent of the other two bases stated by DTCC in the October 26 Cease to Act Notices, as more than sufficient grounds alone to support the cease to act determinations.

We also find that NSCC’s determinations on October 26, 2021, and November 5, 2021,¹⁸ to impose on LSC an Activity Cap restricting the aggregate unsettled activity as measured by the gross market value of its unsettled portfolio each business day was appropriate during the pendency of this action given the risks presented by LSC’s capital and liquidity position, was also appropriate and we affirm that as well.

B. LSC’S DEFICIENT INTERNAL CONTROLS

Each of the October 26 Cease to Act Notices included as one of its three bases that LSC had “deficient internal controls.” The factual basis for this conclusion concerned a certain report by an independent consultant retained by LSC under a FINRA order of settlement. (*See* DTCC Exs. 1 and 2, each at p. 3.)

Pursuant to a FINRA settlement in December 2019, LSC retained an independent consultant, Berkeley Research Group LLC (“BRG”). BRG submitted a report to LSC that included a number of recommendations regarding LSC’s internal controls, many of which BRG later concluded LSC had not in fact implemented. On this basis, DTCC concluded that LSC’s internal controls were deficient, warranting the cease to act notices.

LSC argues that the BRG report was flawed and biased, that LSC has appealed BRG’s findings to FINRA, and that a different independent consultant, Optima, retained pursuant to a SEC settlement did not find deficiencies in LSC’s internal controls. LSC also argued that BRG’s findings concerned controls in LSC’s client onboarding and anti-money laundering functions and not anything that touched on DTCC margin requirements. LSC noted that DTCC has not conducted any analysis of its own regarding LSC’s internal controls or concluded based on its own analysis that LSC’s internal controls are inadequate.

We believe that DTCC’s risk management staff could have conducted a more fulsome analysis of LSC’s internal controls, including possible flaws in the BRG report and possible countervailing opinions in the Optima report. According to the October 26 Cease to Act Notices, DTCC’s conclusions that deficient internal controls were one of three grounds for the determinations to cease to act were based entirely on the findings of the BRG report. We note that it is not clear whether DTCC’s risk management staff considered, or even knew of, some of

¹⁸ DTCC imposed an Activity Cap of \$300 million on October 26, 2021, and raised the Activity Cap to \$400 million on November 5, 2021.

the additional evidence presented in the course of this proceeding tending to indicate that LSC's internal controls are deficient, such as the seriously outdated internal LSC risk management guidelines that do not have any reference to the Lek Holdings Note Program. However, simply reviewing the conclusions of the October 26 Cease to Act Notices, based as they are solely on the findings of the BRG report and without any independent analysis or review, are insufficient to support a determination as draconian as a cease to act notice.

We would like to emphasize that our finding on this point is limited to the facts of this particular case and we do not mean to imply that DTCC cannot, in an appropriate case, base its finding and sanction on a single data source if sufficiently reliable.

C. LSC'S INADEQUATE RESPONSES, FAILURES TO RESPOND, AND INACCURATE AND MISLEADING REPRESENTATIONS

The third ground stated in each of the October 26 Cease to Act Notices was that LSC failed to inform DTCC properly regarding changes in its financial condition and indeed had affirmatively misrepresented or willfully omitted certain material information when responding to DTCC requests. Each of the October 26 Cease to Act Notices cited twelve instances of such failures by LSC to meet its obligations. When examining them, several of these failings can be grouped together.

As an initial matter, it is unquestionable that LSC had a duty as a NSCC member and DTC participant to provide all material information in a full and fair manner to DTCC, both in response to DTCC's requests and on its own initiative when warranted.¹⁹ While every instance cited by DTCC in the October 26 Cease to Act Notices is not of the same weight or importance, it is clear that, taken as a whole, LSC failed to meet its obligations.

Broadly speaking, nearly all of LSC's misrepresentations and omissions closely relate to the subject of the first ground for the cease to act determinations: the sources and adequacy of LSC's capital and liquidity. DTCC in each of the October 26 Cease to Act Notices identified twelve representations, omissions, or responses as the basis for DTCC's determinations. These may be grouped into three subjects. The first is comprised of the disclosures concerning the termination of the BMOH or Texas Capital lines of credit in 2021. The second is comprised of disclosures concerning the Lek Holdings Note Program and LSC's liquidity plans generally. These first two groups may be discussed together, as they relate to the sufficiency of LSC's liquidity. As such, given that we have found as DTCC's risk management department did that LSC's liquidity is inadequate to continue as a NSCC member and DTC participant, these misrepresentations and omissions are material. The third group of disclosure violations concern LSC's failure to provide copies of the BRG final report in a timely fashion.

1. The Liquidity Related Disclosure Violations

As noted, LSC at one point had a line of credit with Texas Capital that was used, among other things, to provide liquidity to post cash for margin requirements at NSCC. The Texas Capital line of credit expired on March 31, 2021. (Leibrock Aff. ¶ 40.) Regardless of why it

¹⁹ See NSCC Rules 2A, 2B. Sec. 2, and 15; DTC Rules 2, 9A.

expired, or whether or not LSC thought it mattered that it had expired,²⁰ LSC does not question that it expired on March 31, 2021. However, LSC did not inform DTCC in a timely manner that it had expired. To the contrary, even after its expiration, LSC represented to DTCC that it was still in place.

In LSC's April 7, 2021, responses to DTCC's due diligence requests for documents and information, LSC stated that the Texas Capital line of credit was still available to it as a source of liquidity. (*See* Leibrock Aff. ¶ 40; DTCC Ex. 40.) Furthermore, in the April 7, 2021, responses LSC affirmatively represented: "There have been no changes in the terms of the Company's credit facilities." (DTCC Ex. 40 at p. 4.) By April 7, 2021, before making a representation to DTCC regarding the Texas Capital line of credit, LSC certainly knew, or should have known, that it had expired. Therefore, these were knowing misrepresentations.

LSC made additional misrepresentations to DTCC regarding Texas Capital in writing on May 3, 2021. In response to DTCC's due diligence inquiries, LSC again stated that the Texas Capital line of credit was still in place as an "available line[] of credit" (though, like in the April 7, 2021, responses LSC stated that it had a March 31, 2021, expiration date). (*See* Leibrock Aff. ¶ 41; DTCC Ex. 42 at p. 2.) LSC specially referred to Texas Capital as among its lines of credit. (DTCC Ex. 42 at p. 2.) LSC did note that "Texas Capital has made substantial changes in its lending division, and has exited the relationships with many broker dealers in the industry." (*Id.*) It is unclear exactly what LSC meant by this representation. Perhaps, LSC was trying to suggest that it is not one of those broker dealers with which Texas Capital has exited its relationship. At any rate, LSC could have plainly stated that Texas Capital had ended its line of credit with LSC, but it did not so state. In sum, we find that LSC made several material misrepresentations to DTCC regarding the status of the Texas Capital line of credit in April and May 2021. LSC also omitted to state the true facts regarding the Texas Capital line of credit, which even in the absence of affirmative misrepresentations should have been reported. It was not until May 13, 2021, in responding to direct questions by DTCC staff during a virtual site visit, that LSC informed DTCC of the expiration of the Texas Capital line of credit. (*See* Leibrock Aff. ¶ 42.)

LSC also made affirmative misrepresentations to DTCC regarding its line of credit with BMOH and the status of its overall relationship with BMOH. On or about July 8, 2021, LSC's counsel received a letter from BMOH's counsel reciting a long history of BMOH telling LSC that BMOH intended to scale back and ultimately discontinue its relationship with LSC. This recitation included stating that BMOH had earlier reduced the portion of LSC's line of credit available for use for LSC's "NSCC sublimit" on two occasions, September 8, 2020, and November 9, 2020. The letter also reaffirmed what the letter described as BMOH's previous statements to LSC that BMOH intended to terminate its entire relationship with LSC in 2021. (*See* DTCC Ex. 16; *see also* Leibrock Aff. ¶ 44; Lek Aff. ¶¶ 62-63 (acknowledging that BMOH reduced the NSCC sublimit in the line of credit).) LSC does not deny that it did not inform DTCC of any potential changes to its relationship with BMOH until after mid-July 2021, when DTCC, which had heard of issues in the LSC-BMOH relationship from FINRA, made a specific request to LSC for information about BMOH. (*See* Leibrock Aff. ¶¶ 43-44; Lek Aff. ¶72.)

²⁰ As discussed elsewhere in this opinion, we believe that the expiration of one of only two bank lines of credit that LSC had was material and that their replacement with the Lek Holdings Note Program was a material change.

Then, some two and a half weeks after it had received the BMOH July 8, 2021, letter (DTCC Ex. 16), LSC forwarded it to DTCC. (*See* DTCC Ex. 10.)

While LSC does not deny that it did not notify DTCC of changes in the BMOH line of credit until DTCC asked about it, LSC states that a reduction in the BMOH line of credit was not material to LSC because LSC had or was in the process of obtaining other sources of liquidity, and because LSC did not actually believe that BMOH intended to terminate the relationship until the July 8, 2021, letter. (*See* DTCC Ex. 10; Lek Aff. ¶¶ 61, 73.)

To take LSC's latter justification first, it is hard to accept on face value the credibility of LSC's argument that it thought BMOH was bluffing when it told LSC it was going to terminate the relationship. What remains unexplained is why LSC believed a responsible corporate actor like BMOH would tell LSC something it had no intention of doing. Even if LSC truly believed BMOH did not mean what it said, LSC still was required to disclose to DTCC that BMOH had made the statement. Given that LSC concedes that long before July 8, 2021, BMOH had informed it that BMOH was both reducing credit limits and ultimately terminating the relationship, and in fact reduced the NSCC sublimit on two occasions, we believe BMOH's statements are ones LSC necessarily should have taken seriously.

Moreover, it is worth noting that LSC took BMOH's statements seriously enough to have its counsel send a demand letter on May 14, 2021, in which, among other things, LSC's counsel states that if BMOH closed LSC's settlement account with BMOH, "immediate and irreparable harm to LSC would result." (*See* DTCC Ex. 17; *see also* Leibrock Aff. ¶¶ 50-51 and further exhibits cited therein.) LSC offers two explanations in this proceeding for the statements in its counsel's demand letter. One is that LSC's concern regarding the BMOH relationship was limited to BMOH acting as its settlement bank, and not related to LSC's line of credit. (*See* Lek Aff. ¶ 72²¹.) This is not credible. Given that BMOH had made repeated statements to LSC concerning BMOH's intention to terminate the entire relationship and had actually reduced the NSCC sublimit on two occasions, LSC could not have reasonably thought that termination of the line of credit was anything other than at least a serious possibility, if not probability. As such, it should have been reported to DTCC.

LSC's other position on the materiality of its communications with BMOH is that there was no material need to immediately inform DTCC about the potential loss of this bank line of credit because LSC believed that this line as well as the Texas Capital line of credit were immaterial because LSC could fully meet its NSCC liquidity needs from other sources such as the Lek Holdings Note Program.²² This position must be rejected, for reasons beyond those discussed above concerning the misplaced reliance on the Lek Holdings Note Program to satisfy LSC's liquidity needs. For purposes of disclosure to DTCC, it is not enough that LSC thought

²¹ "Until the Firm got clarity about BMOH's actual intentions and timetable, and LSC had the opportunity to consider an appropriate transition plan, I did not believe there was a reason to alert other parties and cause any undue and premature alarm." (Lek Aff. ¶ 72.)

²² *See, e.g.*, DTCC Ex. 12 (letter of July 30, 2021 from Charles Lek to Michael Leibrock); Transcript of February 17, 2022 proceedings at 11 (argument of counsel that losses of bank lines of credit were not material), 95 (testimony of Charles Lek concerning BMOH statements regarding future termination of services), 108 (same), 134 (testimony of Charles Lek that losses of credit lines were not material in light of other sources), and 143 (testimony of Charles Lek that loss of Texas Capital line of credit was not material).

the bank lines of credit were not necessary or that the Lek Holdings Note Program was sufficient to cover NSCC liquidity needs or that it thought DTCC would (or should) be satisfied with the program if it was fully informed about it. DTCC needed to be fully informed so that DTCC could make its own determination of what was necessary for the protection of DTCC and all its members.

LSC had previously told DTCC that its only bank lines of credit for its liquidity needs included the BMOH and Texas Capital lines of credit. A change in these lines was material. The fact that LSC was beginning in February 2021 to rely on the Lek Holdings Note Program as its liquidity source (*see* Tr. 2.17.22 at 14; *see also* DTCC Ex. 12 at p. 2, where Mr. Lek writes to Mr. Leibrock that the Lek Holdings Note Program “serves to replace the BMOH line of credit” – though this statement was only made some five months after it began replacing it) was also material, and made disclosure about these developments mandatory. NSCC Rule 2B and DTC Rule 2 both make timely notification to DTCC by members of changes to their financial condition mandatory. But instead of full and fair disclosure to DTCC, LSC made less than full disclosures based on its own determination of materiality – a determination that was both self-serving in favor of non-disclosure and materially misleading to DTCC in DTCC’s efforts to determine the adequacy of LSC’s changing capital and liquidity position.

Mr. Lek’s testimony that statements in LSC’s counsel’s letters to BMOH of May 14, 2021 and June 23, 2021 (DTCC Exs. 17 and 19, respectively) concerning LSC’s statements to BMOH that termination of the banking relationship would cause irreparable harm to LSC were just “embellishments” designed to induce (or possibly threaten) BMOH to “[j]ust continue to do business and provide us with OCC clearing services” (Tr. 2.17.22 pp. 99-100) is troubling for multiple reasons. First, that a responsible business would “embellish,” *i.e.*, intentionally mislead, a federally regulated banking institution for the purpose of inducing it to extend credit or a banking relationship is in and of itself problematic. Moreover, when viewed in light of LSC’s less than forthcoming statement to DTCC regarding its liquidity sources it merely confirms a pattern of behavior. Stretching facts and law to fit LSC’s needs of the moment appears to have become a habit at LSC. To avoid making disclosures, LSC repeatedly made self-serving determinations of materiality and non-materiality, as well as simply hoping all would turn out well. These are not the appropriate criteria to apply when determining what should be disclosed to DTCC. To the contrary, they are evidence of an intentional act to mislead. The conclusion that LSC delayed disclosing the losses of its bank lines of credit and details regarding the highly unusual and ultimately inadequate Lek Holdings Note Program to DTCC intentionally in order to avoid the risk of DTCC fairly evaluating or even questioning the adequacy of its liquidity, is inescapable.²³

As just noted, this behavior by LSC is part of a pattern of obfuscation and non-cooperation with DTCC. For example, in its letter of July 26, 2021, responding to DTCC’s requests for information regarding the BMOH lines of credit (*see* DTCC Ex. 10), rather than making forthright disclosures of all facts that could be relevant to DTCC and working

²³ LSC’s behavior is reminiscent of the concession by the sanctioned respondent in the case of *In the Matter of the Application of Peter W. Schellenbach*, 50 S.E.C. 798 (1991), at *2-3, where the respondent conceded that the firm avoided telling FINRA about its net capital problem because it believed that if it had disclosed the problem, FINRA would have shut it down.

cooperatively with DTCC to address any issues, LSC took a highly adversarial approach. Mr. Lek in his letter on behalf of LSC accuses DTCC of stating “material inaccuracies” regarding the LSC-BMOH relationship and the Lek Holdings Note Program, but provides no real information or descriptions of his firm’s liquidity to address DTCC’s legitimate concerns. Mr. Lek concedes that “[w]e agree that it is important to keep DTCC apprised of all developments that could impact our ability to remain a member in good standing at NSCC and DTC.” (*Id.* at p. 2.) For a member to keep DTCC apprised of such developments is beyond being merely “important,” it is an absolute duty. Mr. Lek tries to justify breaching that duty through a self-serving and objectively flawed determination of materiality.

After conceding LSC should keep DTCC informed, Mr. Lek goes on immediately to conclude: “However, the issues surrounding our sources of funding is not such a development.” (*Id.*) We could not disagree more fundamentally with this statement. These issues of LSC’s capital and liquidity were fundamental to LSC’s ability to remain a member in good standing at NSCC and DTC. However, rather than address them, LSC continued to make unilateral determinations of materiality that cannot be supported objectively and clearly were designed to justify non-disclosure.

DTCC continued to impress upon LSC the seriousness of the issue. For example, in his letter to Mr. Lek dated August 3, 2021 (DTCC Ex. 13), Mr. Leibrock specifically informs LSC that in DTCC’s judgment LSC had up to that point failed “to fully address the DTCC requests and questions” and “to adequately demonstrate that LSC had sufficient and reliable liquidity.” (*Id.* at p. 1.) Despite this clear warning, LSC continued to fail to provide full and fair information to DTCC regarding the Lek Holdings Note Program. We note that LSC never provided DTCC with, among other things, a narrative explanation of the operation of the Lek Holdings Note Program, how it fit into LSC’s risk management system, or full and sufficient financial information regarding all participants in the Lek Holdings Note Program.²⁴

2. LSC’s Failure To Provide the BRG Report

As described above, following a litigation settlement with FINRA, LSC engaged an “Independent Consultant” called BRG. (*See* DTCC Ex. 39 at p. 2; Leibrock Aff. ¶¶ 13, 65-66; Lek Aff. ¶ 91.) Also as described above, following litigation with the SEC, LSC engaged an “Independent Monitor” called Optima. (*See* Lek Aff. ¶¶ 83-84; LSC Ex. 4.) Each was engaged to evaluate certain of LSC’s internal processes and operations. (*See* LSC Exs. 4 and 6.) On April 14, 2021, in advance of a virtual site visit in May, DTCC sent a set of due diligence

²⁴ Among the violations found by DTCC were that LSC failed to respond to DTCC’s September 13, 2021, request for information until after the October 26 Cease to Act Notices were delivered. Whether LSC did in fact attempt to send a response to DTCC on September 23, 2021, was addressed in detail during the course of the hearing on this matter. We find that it appears that Ms. Jessie Quintana, a LSC employee, did make a good faith attempt to electronically transmit a response to DTCC on September 23, 2021, but that for unknown reasons it was never received by DTCC. Thus, we do not find that a failure by LSC to respond to this request is among LSC’s violations of its duties to provide information on request or on its own initiative to DTCC. Given the breadth of LSC’s other violations, however, this makes no difference to our final determination. We also note that LSC could have, but chose not to, follow up with DTCC after September 23, 2021, to inquire whether LSC had answered all of DTCC’s questions.

questions to LSC. (See DTCC Ex. 41; Leibrock Aff. ¶ 65.) Questions 9 and 10 were related these reports.²⁵

Among LSC's failures to provide documents cited by DTCC in the October 26 Cease to Act Notices was LSC's failure to provide a copy of the BRG Independent Consultant report (DTCC Ex. 39) when it was issued and instead delaying providing it until June 2021, after DTCC had asked for it several times. (See DTCC Ex. 1 at p. 5; DTCC Ex. 2 at p.4.) That LSC did not provide the report until June 2021 is uncontested.

In his affirmation, Mr. Lek testified that "LSC appears to have first received a request from DTCC for the BRG Final Report on June 2, 2021 and provided a copy of the report to it on June 10, 2021." (Lek Aff. ¶ 177.) However, besides the April 14, 2021, requests, there were also the "Annual Site Visit (05/13/2021) Follow Up Questions" submitted by DTCC to LSC on May 13, 2021, and repeated on May 19, 2021, and among these was the request: "Please provide all available reports delivered by the Independent Consultant (Berkeley Research Group) produced after February 4, 2020 (date of the report available in our records)." (See DTCC Exs. 47 and 48; Leibrock Aff. ¶ 66.) Therefore, it appears that Mr. Lek's statement in his Affirmation is incorrect and that the Report had been requested both generally and specifically earlier and that LSC failed to respond until June 2021.

When asked about this during cross-examination, Mr. Lek justified LSC's failure to produce the BRG report in response to the April 14, 2021 due diligence questions (DTCC Ex. 41) on the grounds that DTCC's request for it was ambiguous and that LSC interpreted the request for the report of the Independent Monitor Optima, because the request included in parentheses "three-year engagement," and only Optima, and not BRG, was subject to a three-year engagement. (See Tr. 2.17.22 pp. 118-21.) It is certainly true that DTCC's requests, in this instance, were ambiguous, and that the reference to a three-year engagement should not have been included in Request number 10. However, Mr. Lek's testimony on this point is not credible and does not justify LSC's failure to provide the BRG report to DTCC in a timely fashion.

What Mr. Lek's testimony evidences is that LSC was not acting in good faith in responding to the request. Only a tortured reading of the request in context could lead to the conclusion advanced by Mr. Lek. This conclusion would mean that requests 9 and 10 both were seeking the same report, by Optima (as Optima was the one acting under a three-year engagement). This reading, while independently making no sense because it reads one of the requests out of any meaning whatsoever, also fails to account for the fact that the requests, while both making the three-year reference, are not otherwise identical. One asks for the Independent Monitor report and the other for the Independent Consultant report. Independent Monitor was the term applied to Optima, and Independent Consultant was the term applied to BRG. (See Lek Aff. ¶¶ 83, 85, 91, 93.) The only objectively fair interpretation of this pair of requests is that one sought reports by Optima and the other reports by BRG. LSC's reading could only be motivated

²⁵ "9) Please provide updates on the latest Independent Monitor Compliance Reports and status regarding the recommendations presented by the Independent Compliance Monitor (three-year engagement.)

10) Please provide updates on the latest Independent Consultant Reports and status regarding the recommendations presented by the Independent Consultant (three-year engagement.)" (DTCC Ex. 41.)

by a desire to avoid producing the unfavorable BRG report. Also, if the interpretation advanced by LSC at the hearing in this matter was the one genuinely held by LSC at the time it responded to these requests, LSC would have responded to both the same way by referring to Optima. LSC instead chose not to respond to either request. (*See* DTCC Ex. 42, LSC Ex. 70.)

We understand that LSC disagreed with the BRG report and believed there were numerous problems with its preparation and conclusion.²⁶ Perhaps LSC's concerns have some merit, particularly in light of the much more favorable Optima Report, though we make no findings on the question. Whether or not LSC had a good faith basis for questioning the BRG report is not the point. The point is that, regardless of what LSC thought of the Report, it should have complied with DTCC's request and promptly provided a copy. A report by an independent consultant commissioned pursuant to a FINRA settlement had been completed questioning a DTCC member's internal processes and controls. DTCC had a right – indeed, the obligation – to ask for the report and LSC had an obligation to provide it. *See* NSCC Rule 2B; DTC Rules 2 and 9(A). LSC could have provided whatever commentary it wished to DTCC along with delivery of a copy of the BRG report, as it did when it objected to FINRA and as it did in Mr. Lek's Affirmation in this proceeding.

Standing alone, the failure to deliver this report for a month or two is not a violation justifying a cease to act determination. We are, however, troubled by it in the context of LSC's repeated failures to provide material information to DTCC. LSC showed a repeated pattern of hair splitting and tortured interpretations in what was plainly an affirmative attempt to avoid providing DTCC with material information that LSC thought would put LSC in an unfavorable light and possibly lead to unfavorable determinations by DTCC.

Moreover, LSC's communications with DTCC risk management were untimely, materially incomplete, and materially misleading. We also find that LSC's failures were not, in most cases, innocent. Rather, LSC's failures were part of a pattern of deliberate obfuscation designed to mislead DTCC. NSCC members and DTC participants have an ongoing duty to provide full, complete, and truthful information about all material aspects touching upon their part in the DTCC system. *See* NSCC Rule 2B; DTC Rules 2 and 9(A). This includes information requested by DTCC. *Id.* DTCC's risk management can only be as good as the information its members provide. Under these circumstances, DTCC's determination that, were it to continue as a member, LSC could not be trusted and relied upon to comply with its ongoing obligations to provide material information to DTCC as required by NSCC and DTC Rules, was supported by the evidence and proper.

Thus, we find that the repeated, knowing, misrepresentations, omissions, and failures to provide information in a timely manner justify and support NSCC's and DTC's determinations to cease to act for LSC.

III. THE ACTIVITY CAP SANCTIONS

By letter dated October 26, 2021, along with the cease to act notice, NSCC informed LSC that NSCC was imposing an "Activity Cap" limiting LSC's unsettled clearing activity to \$300

²⁶ Mr. Lek discusses issues LSC had with the BRG report extensively in his Affirmation. (*See* Lek Aff. ¶¶ 89-99.)

million. (See DTCC Ex. 1.) The Activity Cap was modified upward to \$400 million by letter dated November 5, 2021. (See DTCC Ex. 3.) Also in the letter dated November 5, 2021, DTCC gave notice that it found that LSC violated the Activity Cap by exceeding the \$300 million maximum allowed unsettled clearing activity on five days, each of November 1-5, 2021. (See DTCC Ex. 3 at p. 3.) By the November 5, 2021, letter, NSCC informed LSC that NSCC was imposing a fine on LSC of \$20,000 for each day that the Activity Cap had been exceeded, for a total fine of \$100,000. NSCC also informed LSC that it had determined to censure LSC via publication to the NSCC membership for LSC's violations of the Activity Cap. By letter dated November 7, 2021 (a Sunday), DTCC informed LSC that NSCC had determined that LSC violated the \$400 million Activity Cap by having aggregate unsettled clearing activity with a start-of-day gross market value of \$418.3 million for November 8, 2021, which exceeded the \$400 million Activity Cap imposed by the November 5, 2021, letter.

Other than questioning whether imposition of the Activity Cap itself was warranted, a position we reject for reasons stated above, LSC offered no argument that it had not violated the Activity Cap of which it had been notified by DTCC's letters of November 26, 2021, and November 5, 2021. Therefore, we find as a factual matter that LSC did violate the Activity Cap on November 1, 2021, November 2, 2021, November 3, 2021, November 4, 2021, November 5, 2021, and November 8, 2021. We also affirm the sanctions imposed by NSCC of a fine of \$20,000 for each day of violation, for a total fine of \$120,000, and that LSC be censured in the manner indicated in DTCC's letters of November 5, 2021 and November 7, 2021.

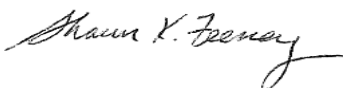
IV. CONCLUSION

For the reasons stated above and based on all the evidence presented in the course of this proceeding, we find that the cease to act determinations made by each of NSCC and DTC as communicated in the October 26 NSCC Cease to Act Notice and October 26 DTC Cease to Act Notice, respectively, were proper and supported by the evidence. They are affirmed.

For the reasons stated above and based on all the evidence presented in the course of this proceeding, we find that the fines and censures determined by NSCC for LSC's violations of the Activity Cap imposed on LSCC on each of November 1, 2021, November 2, 2021, November 3, 2021, November 4, 2021, November 5, 2021, and November 8, 2021, were proper and supported by the evidence. They are affirmed.

This constitutes the unanimous decision of this duly formed Hearing Panel of DTCC.

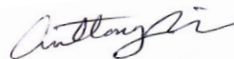
March 10, 2022



Shawn K. Feeney



Pinar Kip



Anthony Miller

DTCC Attachment 2

Before a Hearing Panel of The Depository Trust & Clearing Corporation

-----X

In the matter of

LEK SECURITIES CORPORATION.

-----X

This Hearing Panel of the Depository Trust & Clearing Corporation ("DTCC") has been duly constituted pursuant to the rules applicable to DTCC, including the Rules of the National Securities Clearing Corporation ("NSCC") and The Depository Trust Company ("DTC"). This constitutes the Hearing Panel's decision concerning whether the subject matter for the hearing before this Hearing Panel includes the determination by NSCC to increase the minimum Required Fund Deposit of Lek Securities Corp. ("Lek"), as conveyed to Lek by letter dated November 5, 2021. It does not.

By letter dated October 26, 2021, Andrew I. Gray, Managing Director and Group Chief Risk Officer of the Depository Trust and Clearing Corporation, provided to Lek a certain "Notice of NSCC's Determination to Cease to Act for Lek Securities Corp. ("Lek") and Summary Limitation of Clearing Activity" (the "October 26 NSCC Notice").¹ The October 26 NSCC Notice stated, among other things, that Lek had a right to request a Hearing pursuant to NSCC Rules 37 and 46 to object to NSCC's cease to act determination and Activity Cap. The October 26 NSCC Notice further provided instructions to Lek on required procedures to request such a hearing, should Lek wish to do so.

By letter dated October 29, 2021, counsel for Lek formally objected to NSCC's determinations as conveyed in the October 26 NSCC Notice and requested a hearing regarding "the NSCC's determination to cease to act for Lek and to summarily limit Lek's clearing activity . . . as described in the October 26, 2021 letter of Andrew I. Gray . . ."

On November 5, 2021, Mr. Gray sent another letter to Lek (the "November 5 NSCC Notice"), informing Lek that NSCC had determined to modify Lek's Activity Cap and to sanction and fine Lek for violations of the then-existing Activity Cap on five occasions in early November 2021. The November 5 NSCC Notice informed Lek that Lek could object to and request a hearing regarding the determinations regarding ceasing to act and the Activity Cap pursuant to NSCC Rules 37 and 46, and regarding the sanctions and fines pursuant to NSCC Rules 37 and 48. The November 5 NSCC Notice also stated that as Lek had already requested a hearing regarding the Activity Cap determination communicated in the October 26 NSCC

¹ By separate letter dated October 26, 2021, Mr. Gray also provided to Lek the "Notice of DTC's Determination to Cease to Act for Lek Securities Corp. ("Lek")", which is not relevant to the present question of whether NSCC's determination regarding increasing Lek's minimum Required Fund Deposit is properly part of this proceeding.

Notice, this would be deemed a request for a hearing regarding the modification of the Activity Cap.

Mr. Gray's letter of November 5, 2021, also informed Lek that NSCC had determined to increase Lek's minimum Required Fund Deposit pursuant to Rule 15, effective November 8, 2022. Mr. Gray's letter did not state that Lek could seek a hearing regarding this determination.

On November 7, 2021, Mr. Gray sent a letter to Lek (the "November 7 NSCC Notice"), informing Lek that NSCC had determined to censure and impose fine on Lek for violation of a limitation on Lek's clearing activity. The November 7 NSCC Notice further informed Lek that pursuant to Rules 37 and 48, Lek could request a hearing regarding imposition of this censure and fine.

On November 8, 2021, Lek's counsel sent a letter to the Secretary of the Corporation at DTCC stating that, pursuant to NSCC Rules 3, 46, and 48, Lek objected to and requested a hearing regarding NSCC's determinations regarding the Activity Cap for Lek as imposed in the October 26 NSCC Notice and modified in the November 5 NSCC Notice, the fines and other sanctions imposed on Lek in the November 5 NSCC Notice, and to increase Lek's minimum Required Fund Deposit. Lek's letter of November 8, 2021 also referenced Lek's previous letter of October 29, 2021 that requested a hearing regarding NSCC's determination to cease to act for Lek. Finally, Lek's letter of November 8, 2021 also requested a hearing pursuant to Rules 37 and 48 regarding the censure and fine communicated in the November 7 NSCC Notice.

By email on November 30, 2021, counsel for NSCC (and DTC) wrote to counsel for the Hearing Panel and objected to Lek's inclusion of NSCC's determination to increase Lek's minimum Required Fund Deposit among the issues to be addressed by the Hearing Panel. By later email on November 30, 2021, in response to an inquiry from Panel counsel, counsel for Lek contested NSCC's objection regarding whether NSCC's determination to increase Lek's minimum Required Fund Deposit was properly before the Hearing Panel. Following a preliminary conference held by the Hearing Panel with counsel for both parties on December 1, 2021, the Hearing Panel, through counsel, directed that each of NSCC and Lek submit a written memorandum no later than December 6, 2021, addressing whether NSCC's determination to increase Lek's minimum Required Fund Deposit was properly before the Hearing Panel. Each of NSCC and Lek submitted a written memorandum on December 6, 2021, as directed, and the Hearing Panel has read and considered them.

* * *

This Panel's jurisdiction in this matter is strictly limited by what is provided in the Rules of the NSCC or, as applicable, the Rules of DTC. On this issue regarding determinations made by NSCC, the Rules of NSCC control.

Analysis of this issue is straightforward. The question is whether the NSCC Rules convey a right to an affected Member² to object to a determination by NSCC pursuant to NSCC

² Lek is defined as a "Member" under the NSCC Rules. See Rule 1, "Member."

Rule 15 to modify a Member's minimum Required Fund Deposit and request a hearing by a hearing panel of the Depository Trust & Clearing Corporation to review that determination.

NSCC Rule 37 provides that, when NSCC takes an action regarding a Member that the affected Member "may, *when permitted by these Rules*, request a hearing . . ." NSCC Rule 37, Sec. 1 (emphasis added). There is no provision in Rule 37 or any other NSCC Rule for a Member to request a hearing except where such a request is specifically permitted under the Rules.

NSCC Rule 46, Section 1, gives the NSCC the right and ability to restrict a Member's access to NSCC's services, and such a determination includes a determination to cease to act for a particular Member or to impose a cap on the activity in which a particular Member may engage. Rule 46, Section 2, further expressly incorporates Rule 45, Section 5, and requires NSCC to give notice as provided for in Rule 46, Section 2, to any Member affected by determination by NSCC pursuant to Rule 46. Rule 45, Section 5, in turn, requires that a notice given under Rule 46, Section 2, both set forth the specific grounds for the charges against the Member and inform the Member that the Member has the right to request a hearing on such a determination.

Similarly, Rule 48, which in Section 1 confers on NSCC the right to sanction a Member for a violation or violations of the Rules through fine or censure, also expressly requires Members so sanctioned to be given notice of the charges and provides for the right to a hearing on them. Rule 48, Section 2, provides that before imposing a disciplinary sanction on a Member, the NSCC must give notice to the Member (referred to as a "participant" in this Section) pursuant to Rule 45, Section 6, of the charges against the Member and the Member's right to a hearing. Rule 45, Section 6, expressly incorporates Rule 37 and the Hearing Procedures outlined therein. Thus, determinations pursuant to NSCC Rule 48, Section 1 are subject to review by a hearing panel properly constituted under Rule 37.

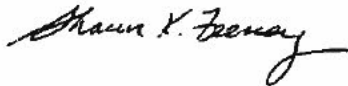
A Member's minimum Required Fund Deposit, initially set in an amount determined by NSCC, as provided for in Rule 4, Section 1, may be modified at any time pursuant to Rule 15. However, in contrast to Rules 46 and 48, Rule 15 confers no right to a hearing on Members affected by modifications to a minimum Required Fund Deposit. Rule 15 conveys no such right, but when such a right is intended, as seen in Rules 46 and 48, it is plainly expressed.

Lek argues that the NSCC's determination regarding Lek's minimum Required Fund Deposit pursuant to Rule 15 and its determinations to cease to act for Lek and to place an Activity Cap on Lek pursuant to Rule 46 arise from the same nucleus of common facts. While this may or may not be true, and at this time prior to a full hearing the Hearing Panel expresses no view on the underlying facts of this matter, whether or not the facts alleged to underpin NSCC's determinations pursuant to Rule 46 are common to those upon which a determination pursuant to Rule 15 are based is irrelevant to the determination of whether Lek has the right to request a hearing on the question of NSCC's determination pursuant to Rule 15. If Rule 15 itself confers no right on a Member to a hearing, this Hearing Panel can neither infer nor create such a right. The Hearing Panel's present decision is based solely on the Hearing Panel's reading of the

NSCC Rules, and the plain text of the Rules does not provide Lek with a right to a hearing on the issue of modifying Lek's minimum Required Fund Deposit pursuant to Rule 15.

THEREFORE, the Hearing Panel concludes that the objection raised by Lek in its November 8, 2021 letter regarding NSCC's determination to increase Lek's minimum Required Fund Deposit is not before this Hearing Panel and shall not be addressed as part of this proceeding.

December 8, 2021



Shawn K. Feeney



Pinar Kip



Anthony Miller

DTCC Attachment 3

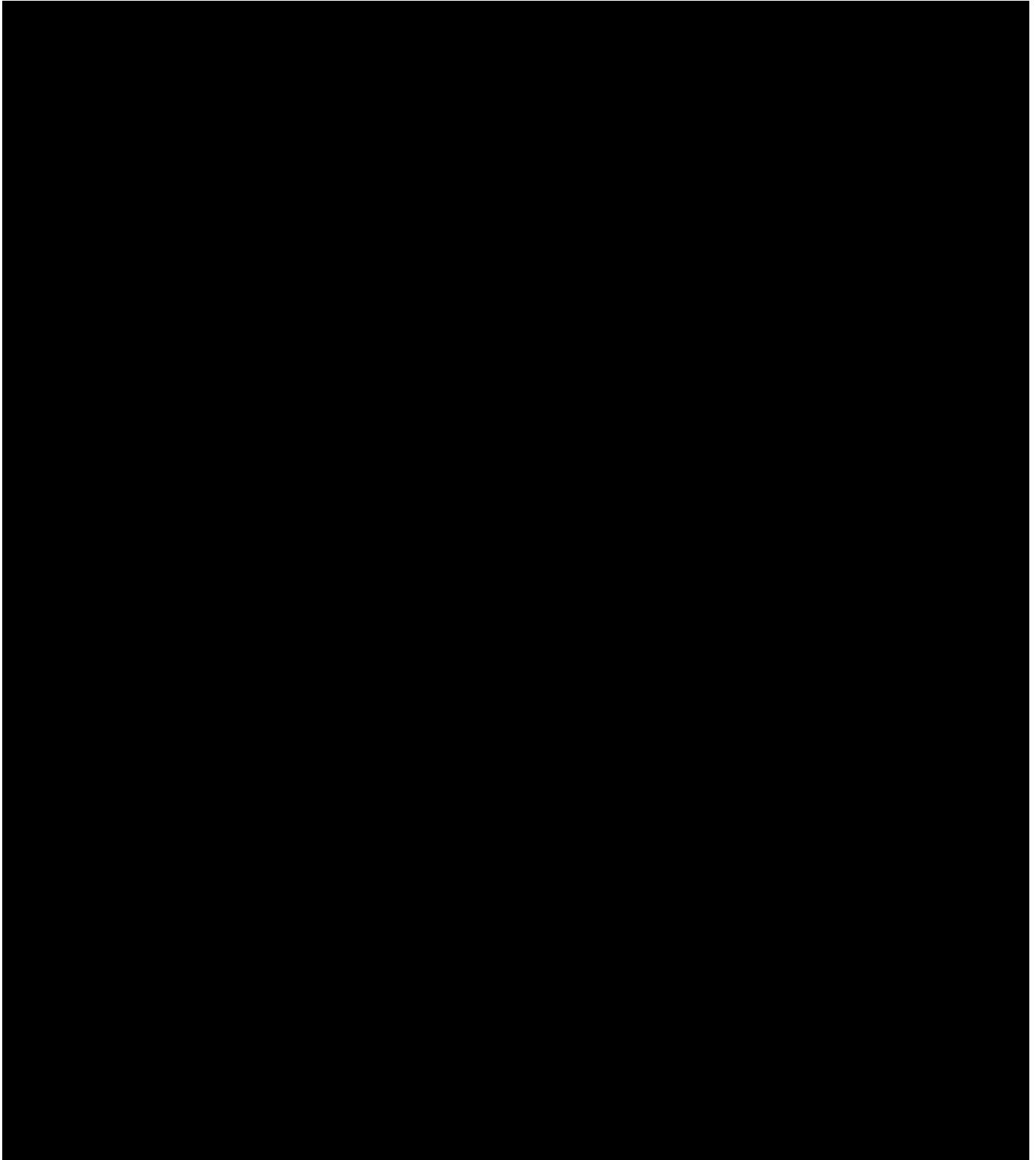


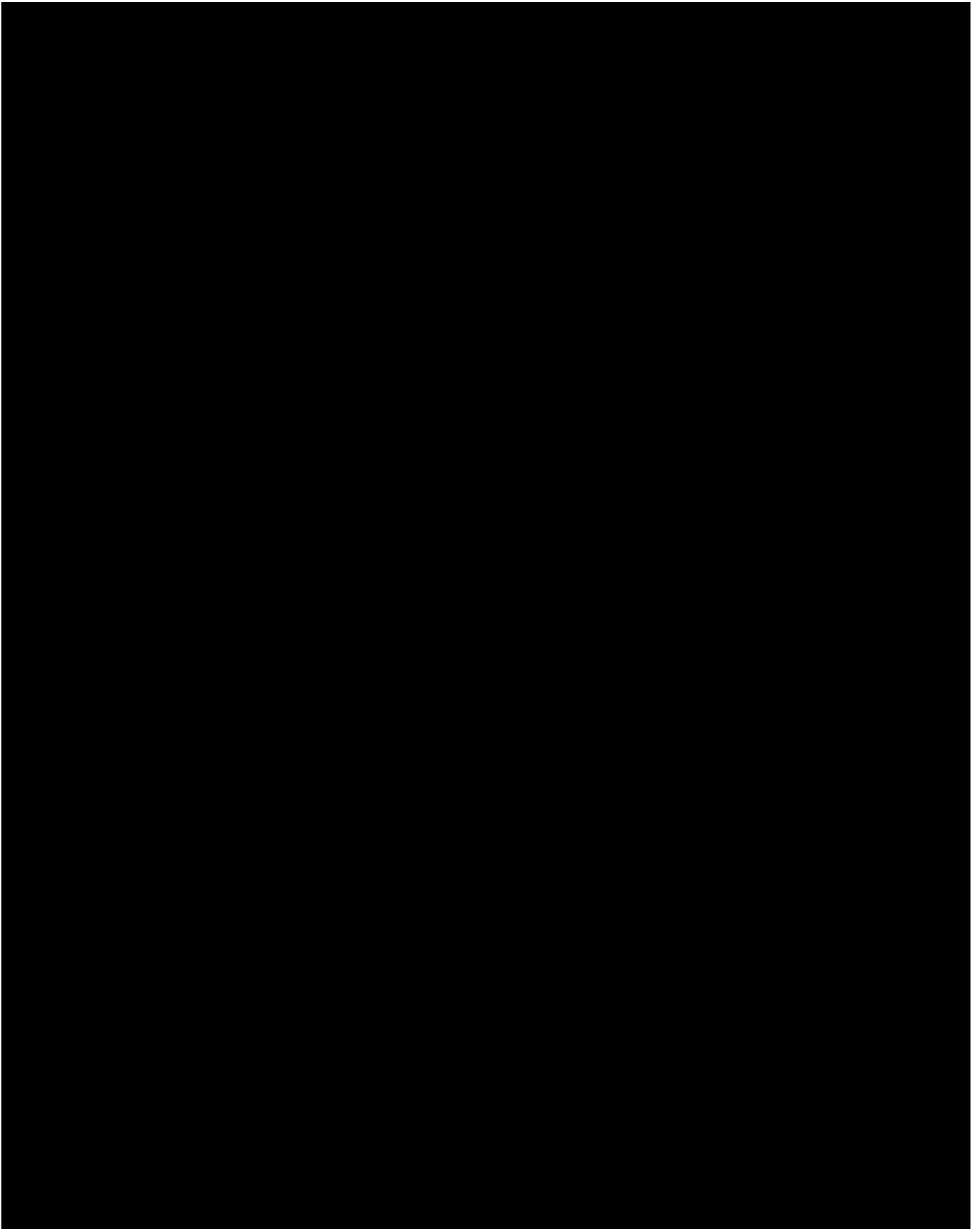
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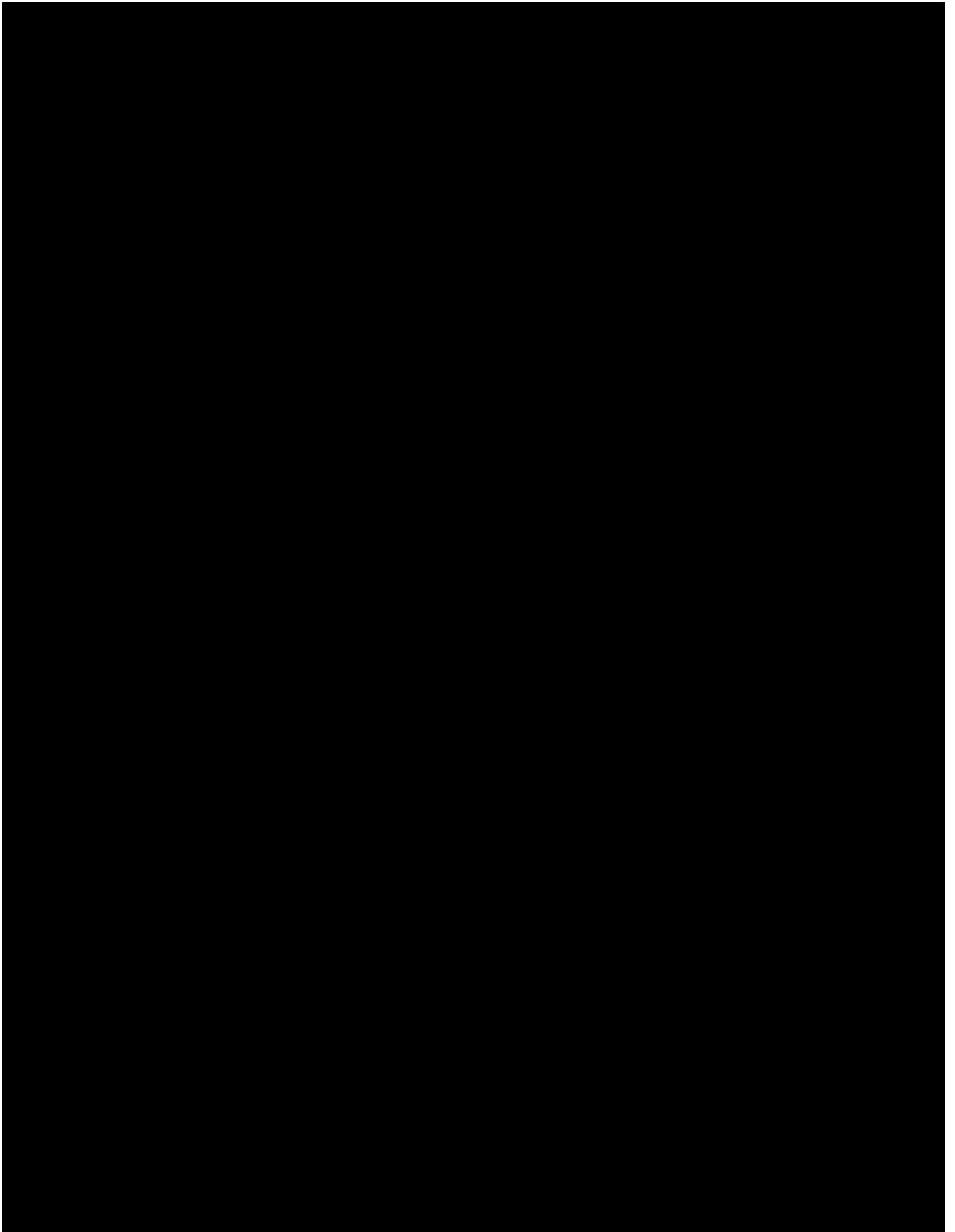
Andrew I. Gray
Managing Director, Group Chief Risk Officer

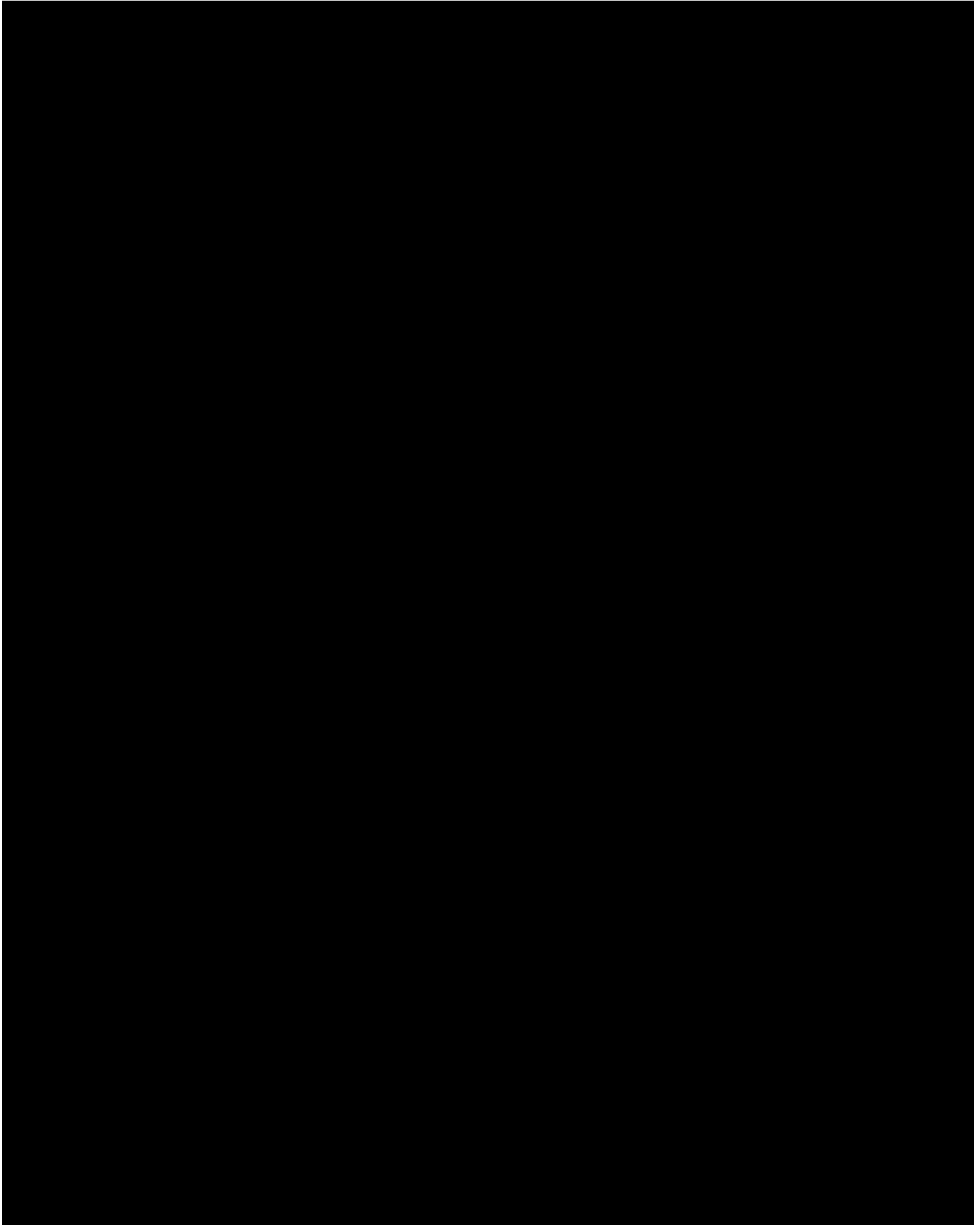
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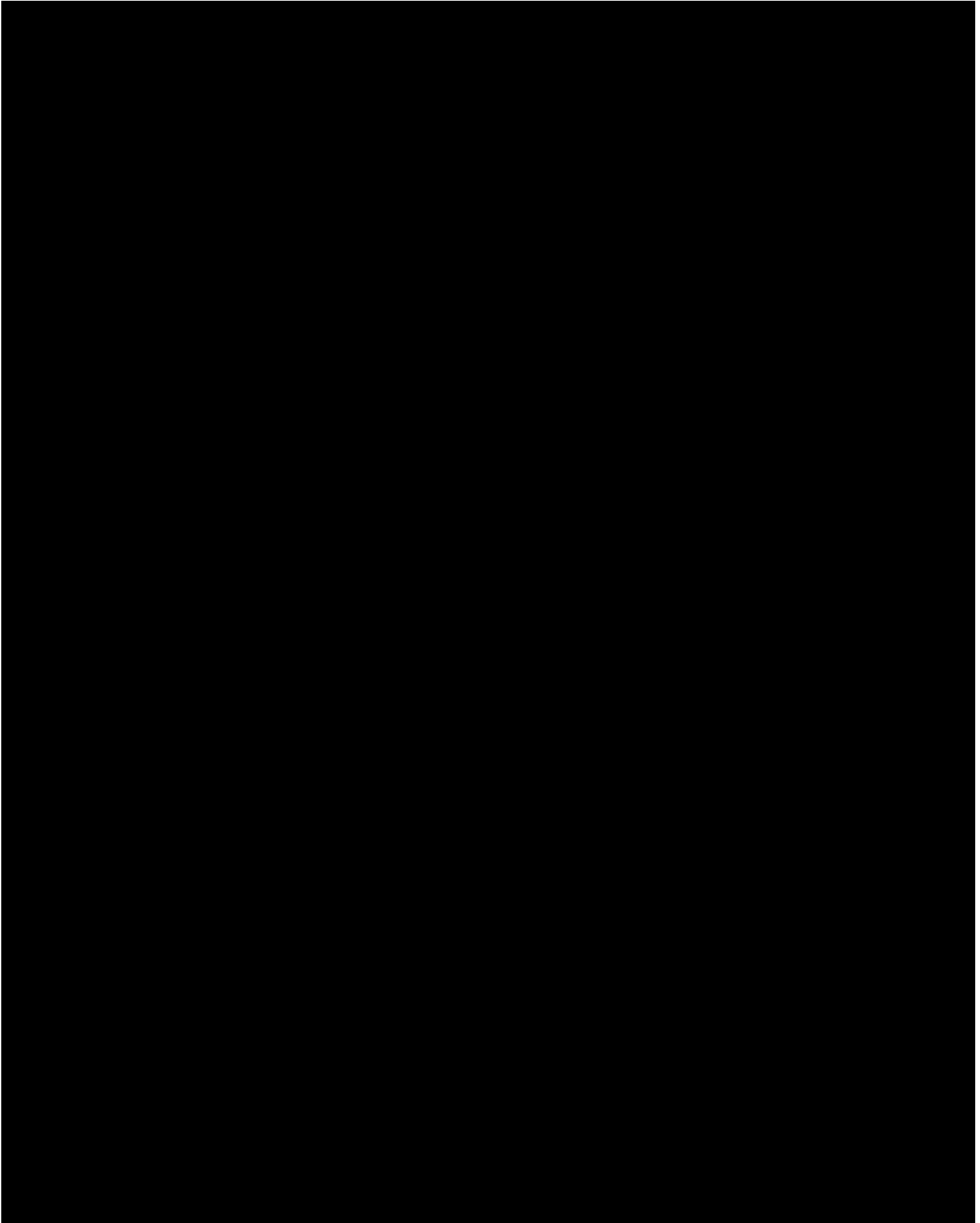
Tel: 212.855.1100
agray@dtcc.com

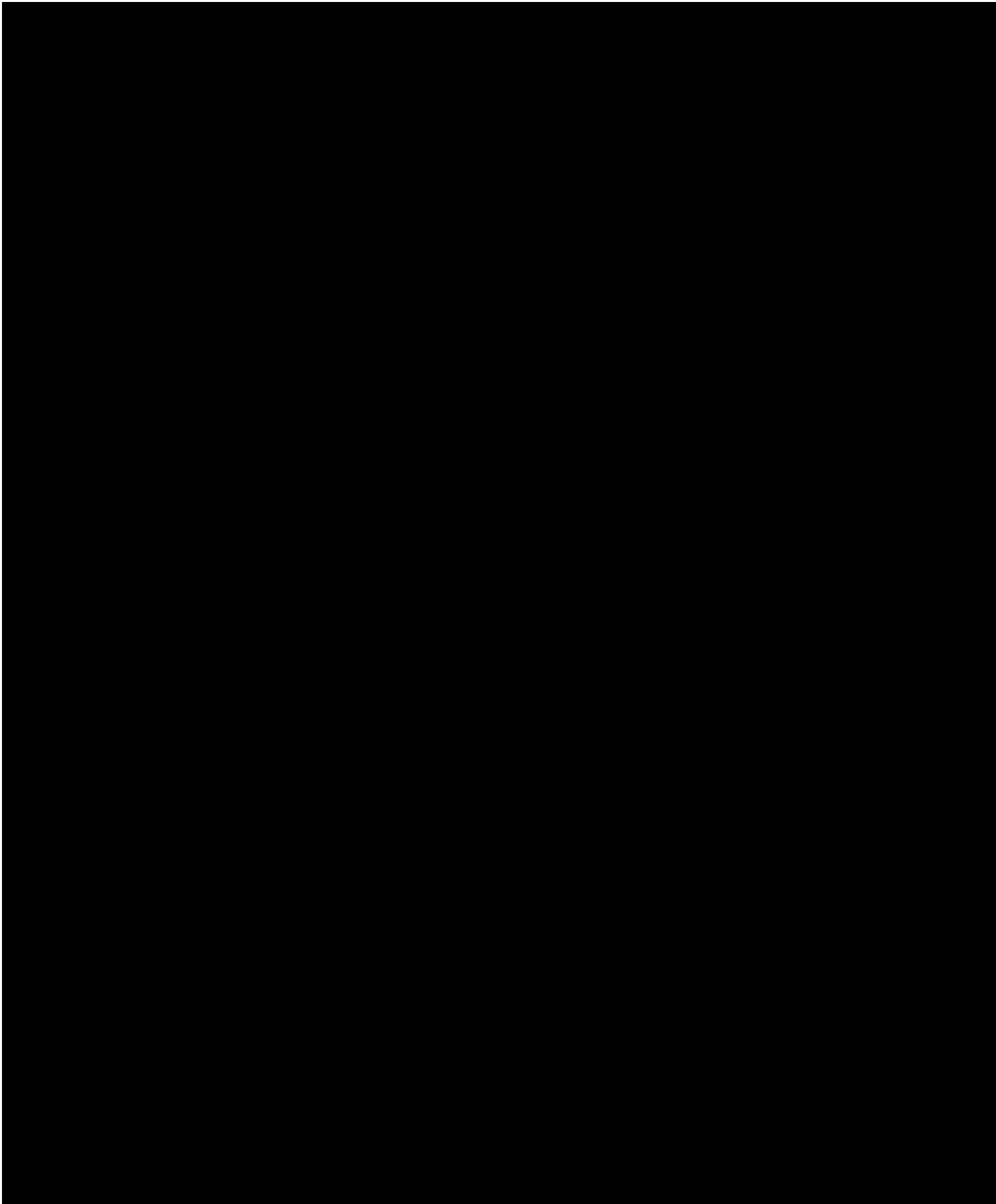












DTCC Attachment 4



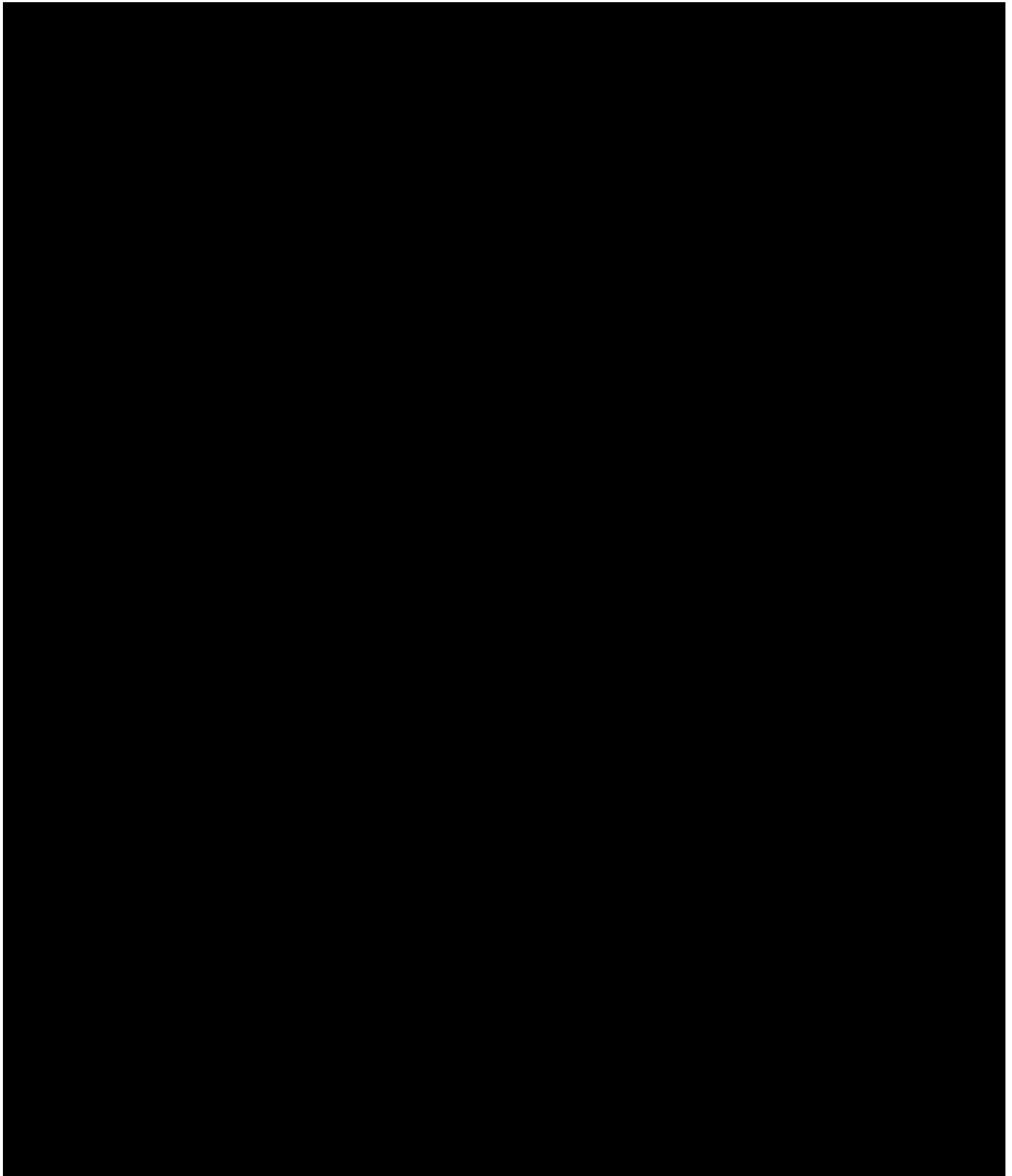
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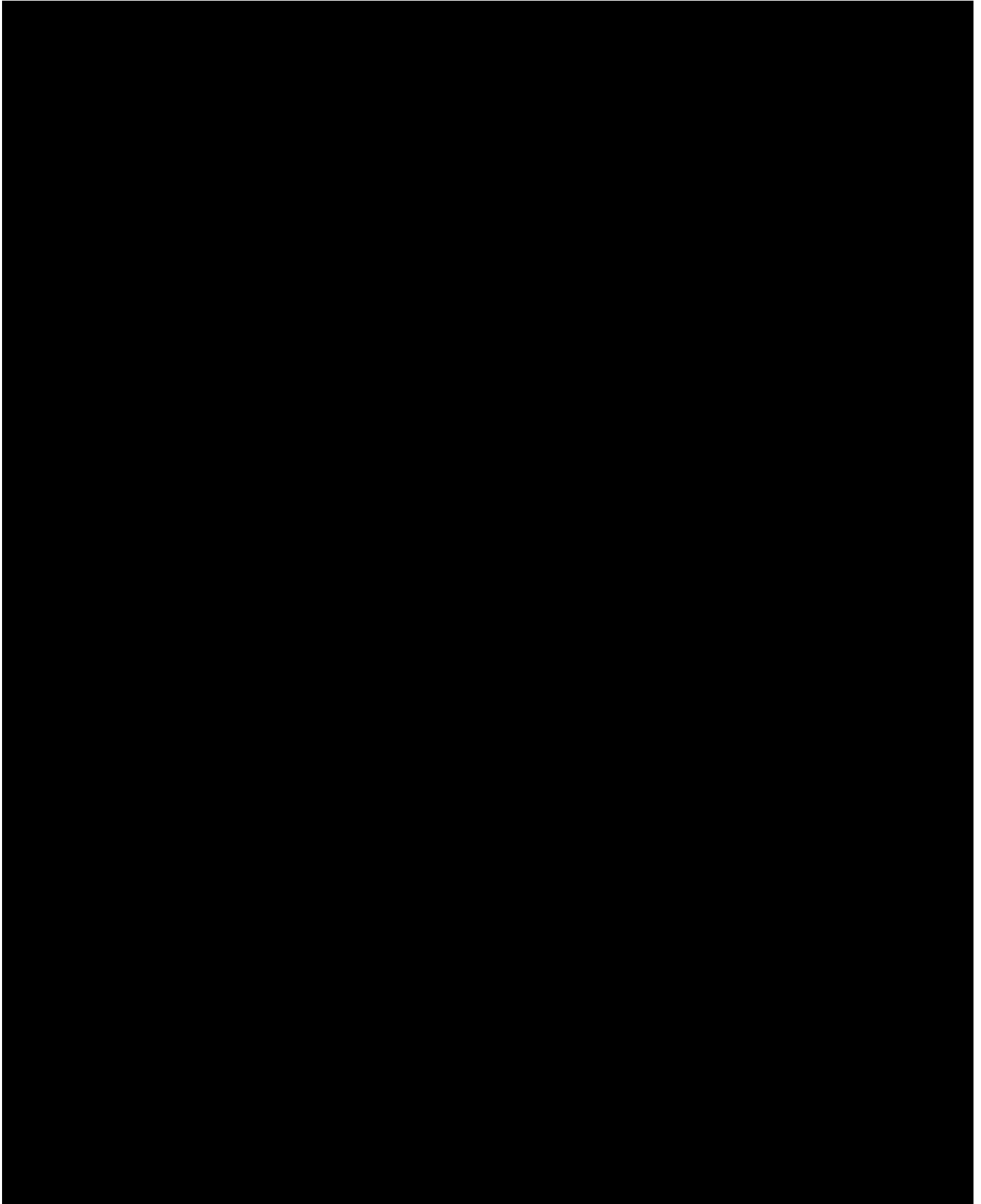
Andrew I. Gray

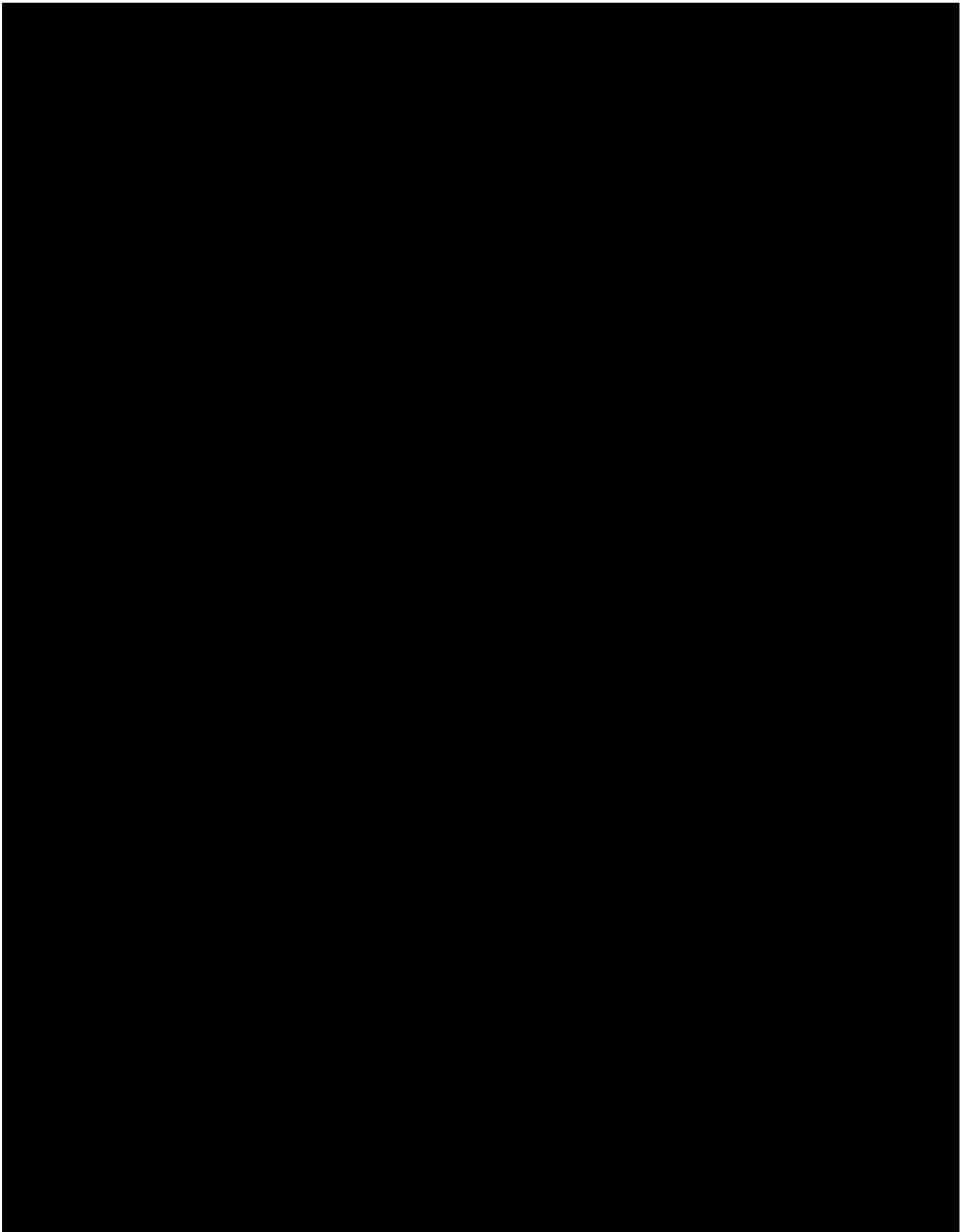
Managing Director, Group Chief Risk Officer

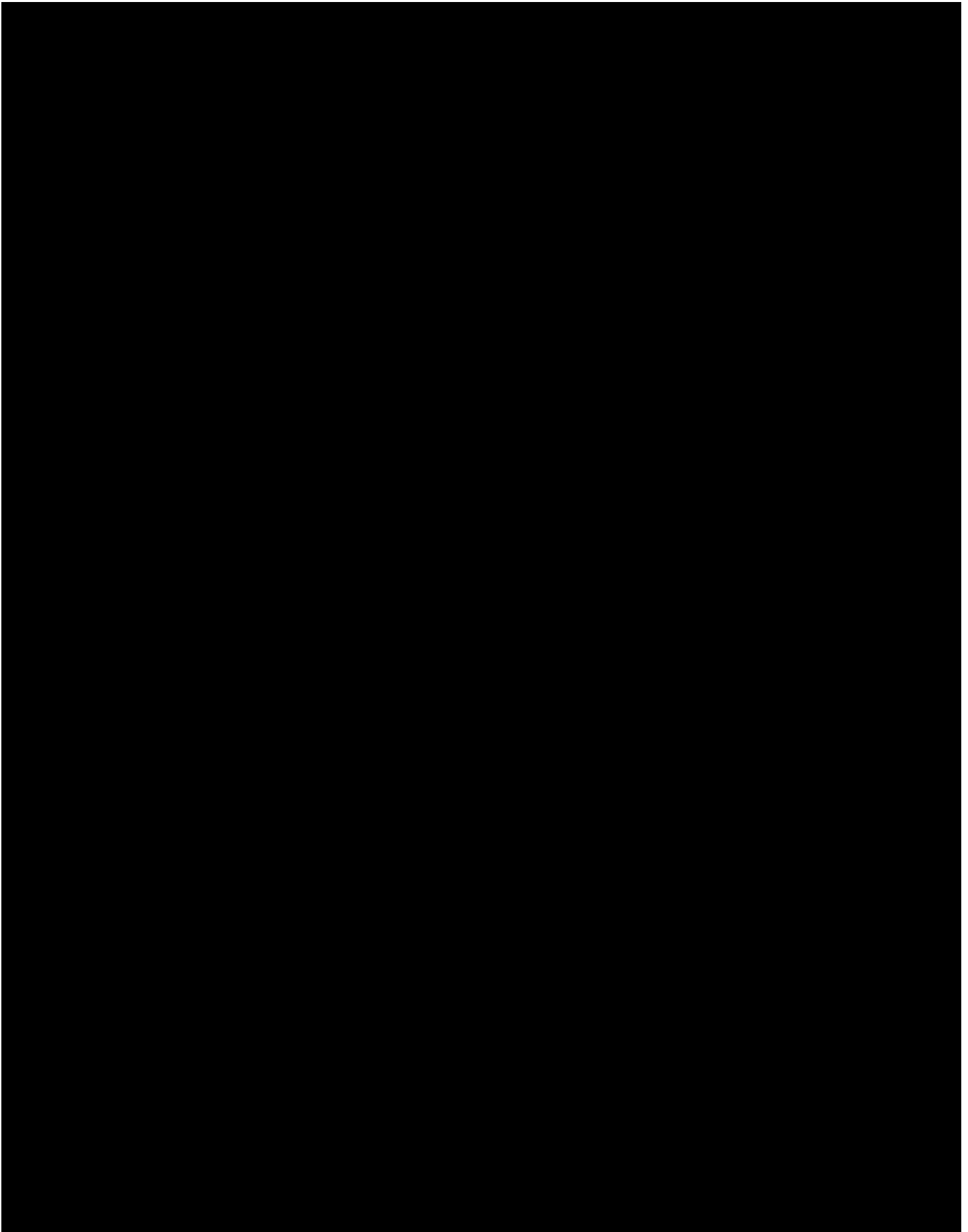
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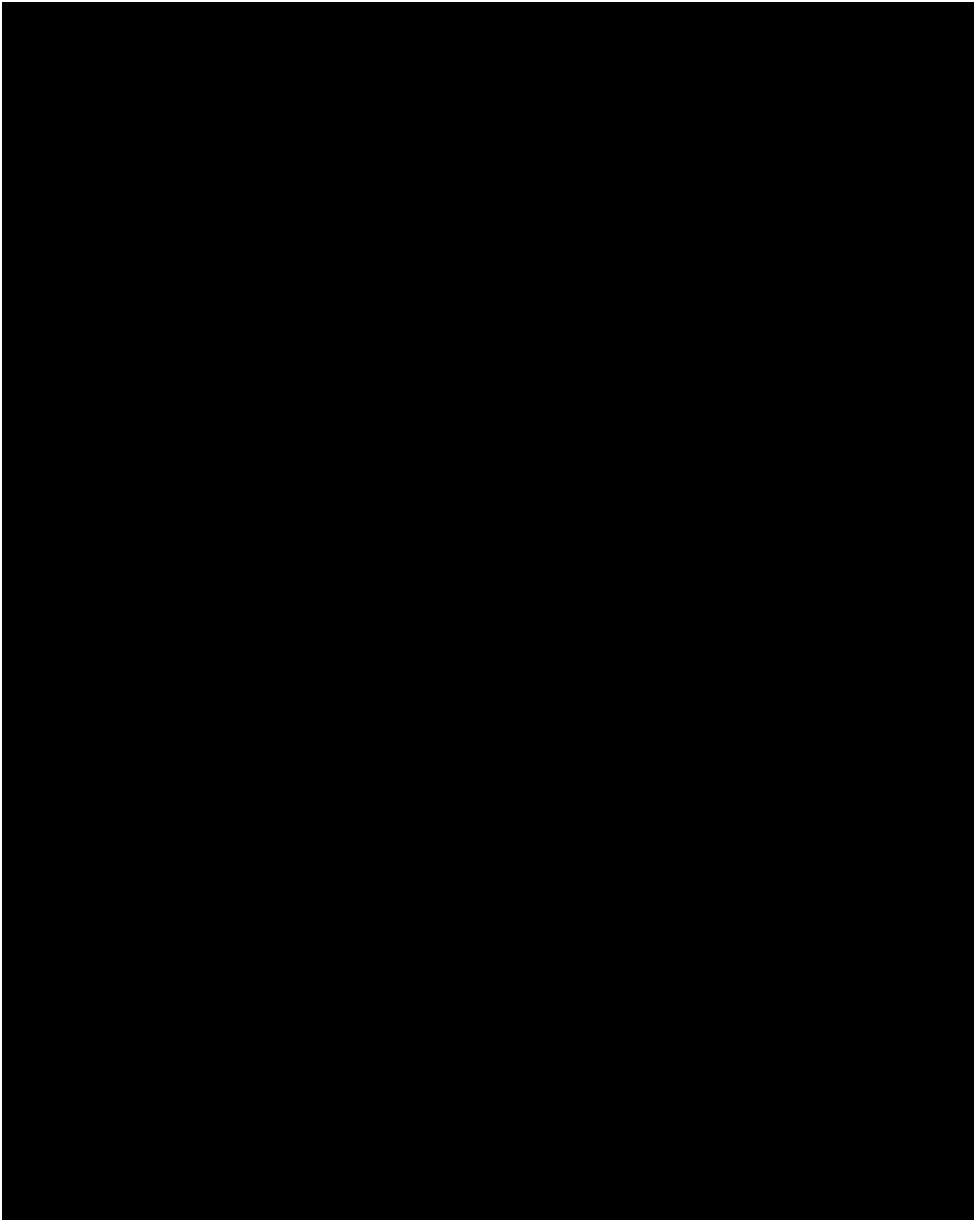
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agray@dtcc.com

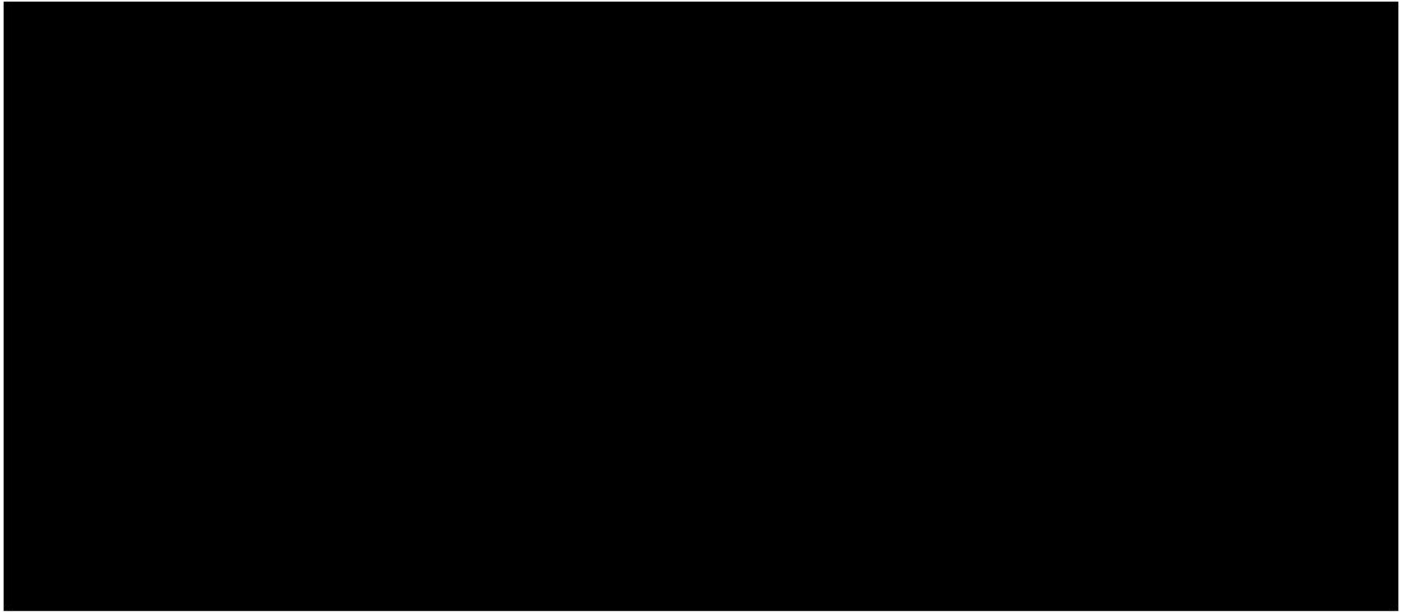












DTCC Attachment 5

November 5, 2021

VIA EMAIL

Lek Securities Corp.
4 World Trade Center, 44th Floor
New York, NY 10007
Attn: Charles Lek

Re: Notice of Modified Activity Cap and the Imposition of Censure and Fines for Violations of Prior Activity Cap

Dear Mr. Lek,

The National Securities Clearing Corporation (“NSCC”) is providing this notice (“Notice”) to inform Lek Securities Corp. (“Lek”) that NSCC has determined (i) pursuant to NSCC Rule 46, to modify its existing Activity Cap (as defined below) on Lek’s unsettled clearing activity, and (ii) pursuant to NSCC Rule 48, to censure and fine Lek for each instance on which it has violated the existing Activity Cap. In addition, NSCC is advising Lek that, pursuant to Rule 15, NSCC is increasing Lek’s minimum Required Fund Deposit from \$20 million to \$27 million, effective November 8, 2021, with such amount subject to upward adjustments as described below.

Activity Cap Modification

On October 26, 2021, NSCC provided Lek notice that NSCC imposed a \$300 million cap on Lek’s aggregate unsettled clearing activity as measured by the gross market value (GMV) of unsettled activity in Lek’s portfolio each business day that coincides with the approval of Lek’s start-of-day margin call (“Activity Cap”). NSCC has determined, pursuant to NSCC Rule 46, to modify the cap by increasing it to \$400 million. The increased Activity Cap will be effective for unsettled activity in Lek’s portfolio following the close of business today, as measured by the portfolio used to calculate Lek’s start-of-day margin call for Monday, November 8, 2021.

This modification responds to Lek’s insistence, as expressed by telephone to Tim Cuddihy, Managing Director, Financial Risk Management, that Lek believed that it could not limit its clients within the \$300 million Activity Cap, and that it was concerned about limiting clients’ ability to sell securities. Lek made these representations after being informed by NSCC that Lek had already breached the Activity Cap twice.

As an accommodation to Lek's representations to NSCC about its clients and in conjunction with NSCC's decision to increase Lek's minimum Required Fund Deposit (as described below), NSCC has determined to increase the Activity Cap to \$400 million GMV. NSCC has observed that the GMV of unsettled activity in Lek's portfolio has only exceeded \$400 million (calculated using Lek's unsettled portfolio each business day coinciding with the approval of Lek's start-of-day margin call) on two prior occasions in the past year.

We remind you that Lek is expected to have appropriate controls in place to manage the risks presented to it, and by extension to NSCC, from its clients' activity. FINRA has recently reiterated that "[m]ember firms are not obligated to receive or accept orders from customers where the firms believe that the associated compliance or legal risks are unacceptable, and there may be situations where firms determine that they must change their order handling procedures to restrict the entry or acceptance of customer orders to limit the firm's exposure to extraordinary market risk."¹ Additionally, SEC Rule 15c3-5 requires Lek to "maintain a system of risk management controls and supervisory procedures" that is "reasonably designed to: (1) systematically limit the financial exposure of [Lek] that could arise as a result of [providing] market access, and (2) ensure compliance with all regulatory requirements that are applicable in connection with [providing] market access."² Lek has previously represented to NSCC in connection with formal due diligence that Lek has "automated controls" on which it may rely "to ensure that [customers] stay within acceptable trading limits ... Our customers do not have 'unfiltered' access. All their orders are routed through our systems and undergo all required checks before being forwarded to the market."³

In view of NSCC's pending decision to cease to act for Lek, and the underlying reasons for that decision, continued growth in the amount of Lek's clearing activity presents unreasonable risk to NSCC. Accordingly, NSCC wishes to reiterate that NSCC expects that Lek will employ whatever risk management tools are necessary to limit the GMV of its unsettled portfolio at NSCC, with an appropriate buffer to protect against the impact of post-trade price changes, to ensure that Lek does not exceed the \$400 million Activity Cap. If Lek exceeds the revised cap, NSCC will immediately pursue the required procedures for imposing further summary restrictions on Lek, up to and including a potential summary cease to act.

Adequate Assurances: Increased Minimum Required Fund Deposit

In the context of Lek's continued use of NSCC's services, NSCC has also determined to increase the minimum Required Fund Deposit that it imposed on Lek as of August 2, 2021, pursuant to NSCC Rule 15. NSCC is increasing Lek's minimum Required Fund Deposit from

¹ See FINRA Regulatory Notice 21-12, issued March 18, 2021, available at <https://www.finra.org/rules-guidance/notices/21-12>.

² See SEC Guidance available at: <https://www.sec.gov/rules/final/2010/34-63241-secg.htm>.

³ Lek Securities Corporation Automated Risk Controls, dated February 2019, at p.2 (provided to NSCC on June 17, 2021).

\$20 million to \$27 million beginning with the start-of-day clearing fund requirement for Monday, November 8, 2021.

Additionally, Lek is informed that if the calculated amount of its start-of-day Required Fund Deposit, exclusive of any Excess Net Capital Premium Charges, exceeds \$27 million on any date after Monday, November 8, Lek's minimum Required Clearing Fund will automatically be re-set to such greater amount as the new minimum. NSCC reminds Lek that it can monitor its estimated clearing fund requirements in the NSCC risk portal.

The foregoing shall not be construed as a waiver of any Excess Net Capital Premium Charges that Lek incurs.

Sanction and Fines

Lek violated the existing \$300 million Activity Cap on multiple occasions since it was imposed, including yesterday:

November 1, 2021 – GMV of \$302.9 million
November 2, 2021 – GMV of \$373.1 million
November 3, 2021 – GMV of \$358.7 million
November 4, 2021 – GMV of \$314.8 million
November 5, 2021 – GMV of \$347.1 million

Notwithstanding NSCC's decision to increase the cap as an accommodation, Lek has repeatedly and materially violated a limitation on Lek's clearing activity that was properly imposed by NSCC and clearly communicated to Lek in writing. Accordingly, NSCC has determined to impose an aggregate fine of \$100,000 on Lek, assessing the maximum \$20,000 penalty permitted for each violation under NSCC Rule 48. NSCC has also determined to censure Lek via publication to the NSCC membership, citing in general terms the above-referenced violations and NSCC's determination to impose the maximum fine permitted for each violation.

Right to a Hearing

Pursuant to NSCC Rules 37 and 46, Lek may request a hearing on the revised Activity Cap. Because Lek has already requested a hearing on the original Activity Cap, NSCC will deem such request as already made.

Under Rules 37 and 48, Lek may also request a hearing concerning NSCC's decision to impose the fines and censure set forth above. If Lek wants to request a hearing with respect to the fine and censure, Lek's request must be in writing and filed with the Secretary of NSCC within five (5) business days from the date of this letter. Within seven (7) business days after the filing of such written request, or such later date as NSCC may specify in writing to Lek following the review of disputed fines required under Section 2 of Rule 37 (unless, with respect to any disputed fines, NSCC determines to waive such fines upon review), Lek must then submit to NSCC a clear and concise written statement setting forth the basis for its objection to the fines and/or censure, whether Lek intends to attend the hearing and whether Lek chooses to be represented by counsel at the hearing. If Lek fails to file the written request and/or written statement within the time periods specified above, Lek will be deemed to have waived its right to

a hearing concerning the fines and the censure, and NSCC will promptly bill Lek for the fines in accordance with NSCC procedures.

Nothing in the foregoing is intended to modify or otherwise impact NSCC's determination to cease-to-act for Lek nor the timeline for the pending hearing process with respect to the cease-to-act or the Activity Cap.

This letter is without waiver of any of NSCC's, DTC's, and DTCC's legal or equitable rights, all of which are hereby expressly reserved.

Sincerely,

A handwritten signature in black ink, appearing to read "Andrew", with a stylized flourish at the end.

DTCC Attachment 6

November 7, 2021

VIA EMAIL

Lek Securities Corp.
4 World Trade Center, 44th Floor
New York, NY 10007
Attn: Charles Lek

Re: Notice of Violation of Activity Cap, Imposition of Censure and Fine, and Request for Information

Dear Mr. Lek,

On October 26, 2021, NSCC provided Lek Securities Corp. (“Lek”) notice that NSCC imposed a \$300 million cap on Lek’s aggregate unsettled clearing activity as measured by the gross market value (GMV) of unsettled activity in Lek’s portfolio each business day that coincides with the approval of Lek’s start-of-day margin call (“Activity Cap”). In response to a request by Lek, and based upon its representations to NSCC, on November 5, 2021, NSCC increased the Activity Cap to \$400 million (“Increased Activity Cap”) effective for Lek’s start-of-day margin call for Monday, November 8, 2021. Lek’s GMV for start-of-day Monday November 8, 2021 is **\$418.3 million**, exceeding the Activity Cap by \$118.3 million, and exceeding the Increased Activity Cap by \$18.3 million.

Fine and Censure

Pursuant to Rule 48, NSCC has determined to impose a fine of \$20,000 on Lek for this violation of a limitation on Lek’s clearing activity that was properly imposed by NSCC and clearly communicated to Lek in writing. NSCC has also determined to censure Lek via publication to the NSCC membership, citing in general terms the above-referenced violation and NSCC’s determination to impose the maximum fine permitted for this violation.

Right to a Hearing

Under Rules 37 and 48, Lek may request a hearing concerning NSCC’s decision to impose the fine and censure set forth above. In view of the fines for prior violations that were communicated to Lek on Friday, for administrative convenience NSCC will consolidate any appeal of this additional fine and censure and extend by one business day the deadline for Lek to object. Lek’s request for a hearing with respect to all fines and censure assessed up to and

including the above must therefore be filed with the Secretary of NSCC no later than the close of business on Monday, November 15.

Request for Information

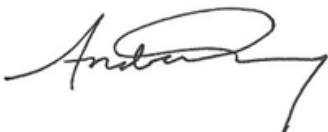
SEC Rule 15c3-5 requires Lek to “maintain a system of risk management controls and supervisory procedures” that is “reasonably designed to: (1) systematically limit the financial exposure of [Lek] that could arise as a result of [providing] market access, and (2) ensure compliance with all regulatory requirements that are applicable in connection with [providing] market access.”¹ Lek has previously represented to NSCC in connection with formal due diligence that Lek has “automated controls” on which it may rely “to ensure that [customers] stay within acceptable trading limits ... Our customers do not have ‘unfiltered’ access. All their orders are routed through our systems and undergo all required checks before being forwarded to the market.”²

We are instructing Lek to advise NSCC, in writing (which may be by email), **no later than the close of business Monday, November 8, 2021**, what specific risk management controls and supervisory procedures Lek has implemented to comply with the Increased Activity Cap. Lek’s response should detail the dates any such controls were implemented and identify the names and positions of the individuals responsible for monitoring the effectiveness of the identified controls.

Nothing in the foregoing is intended to modify or otherwise impact NSCC’s determination to cease-to-act for Lek nor the timeline for the pending hearing process with respect to the cease-to-act or the Activity Cap.

This letter is without waiver of any of NSCC’s, DTC’s, and DTCC’s legal or equitable rights, all of which are hereby expressly reserved.

Sincerely,

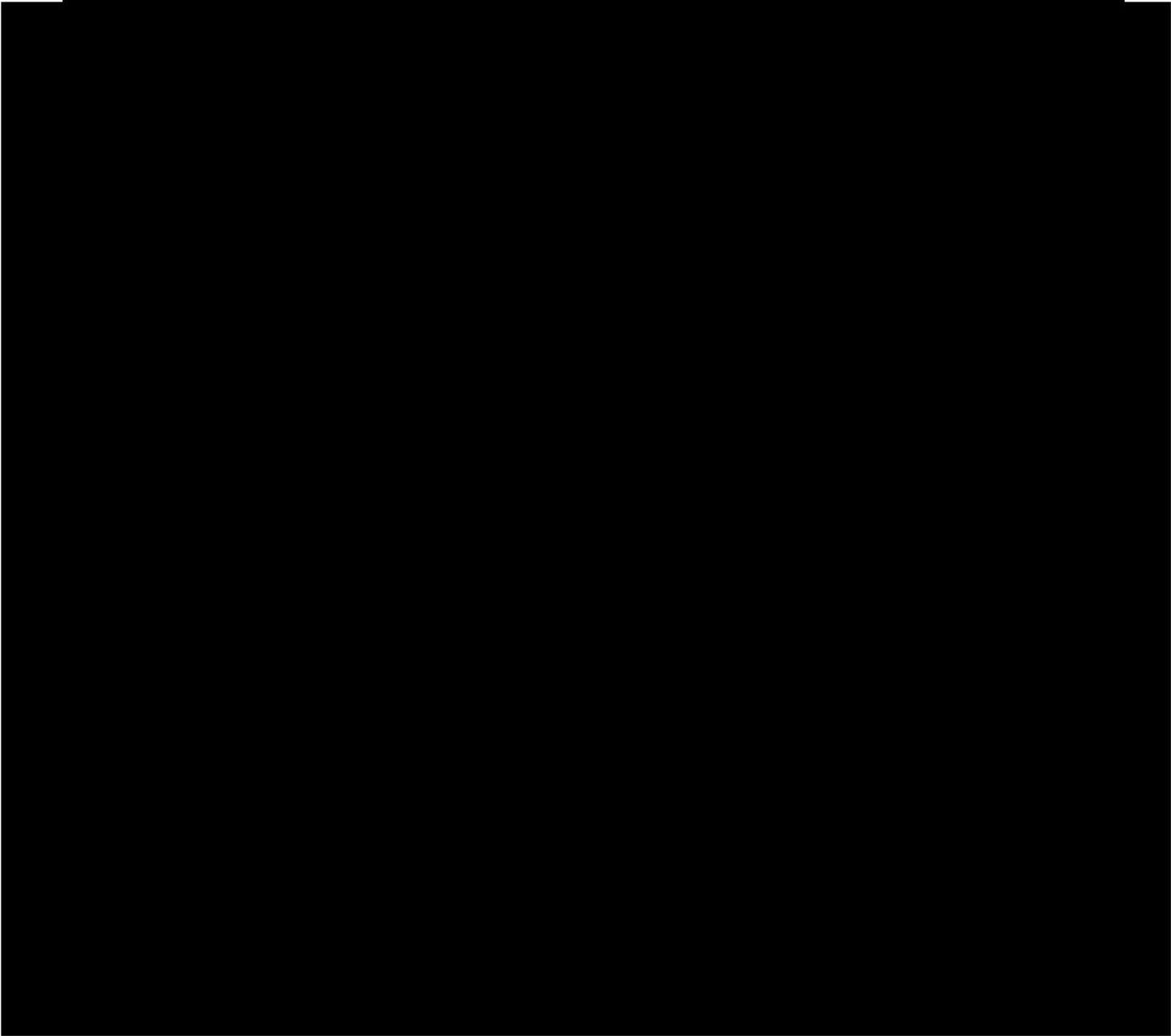
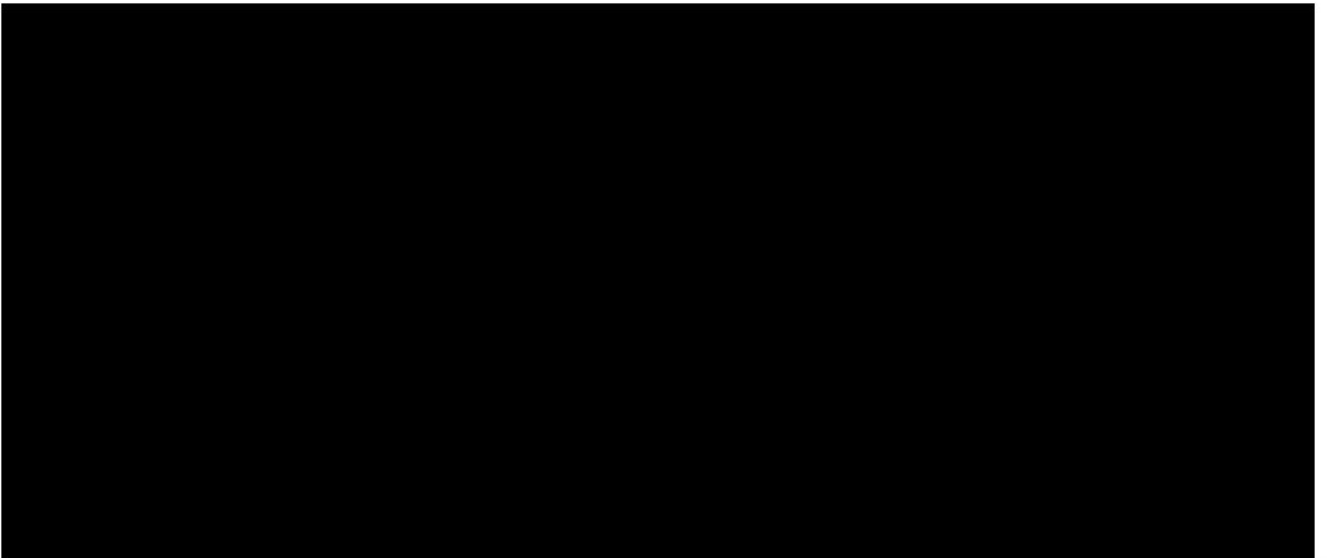


cc: Jeffrey Tabak, Lek Securities Corp.

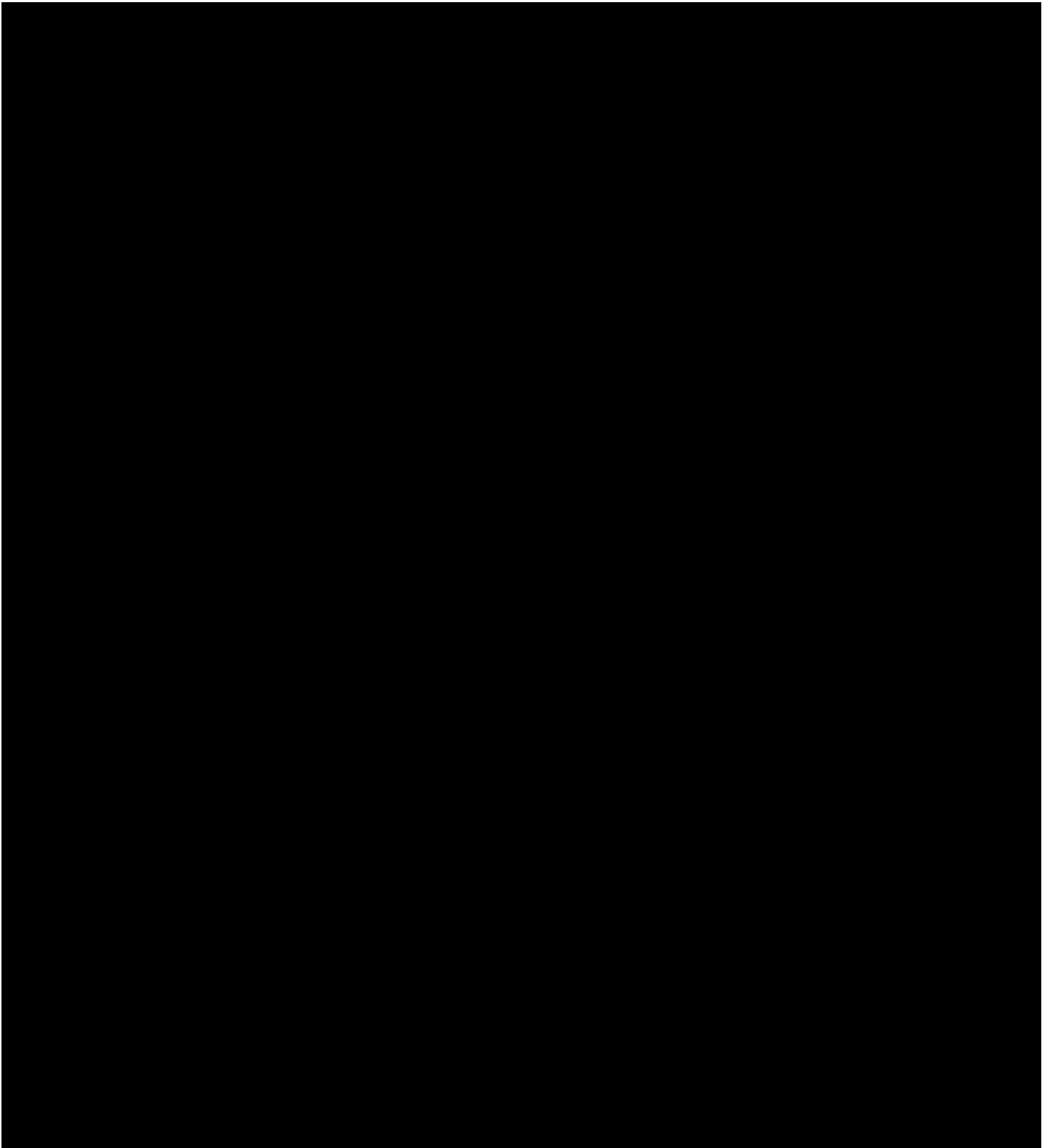
¹ See SEC Guidance available at: <https://www.sec.gov/rules/final/2010/34-63241-secg.htm>.

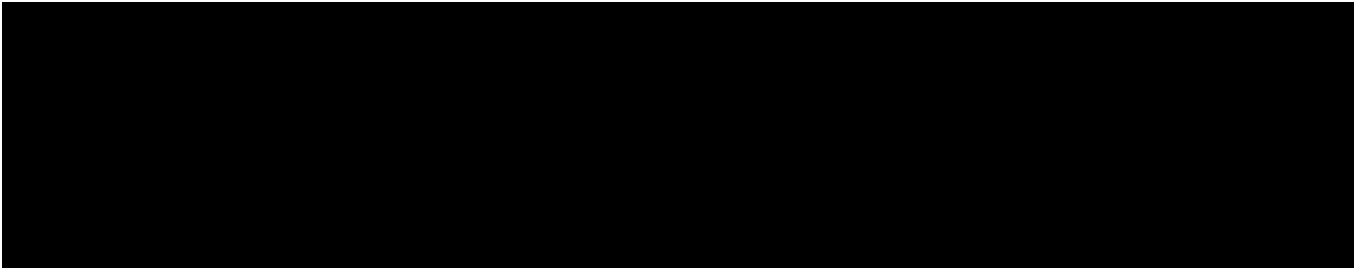
² Lek Securities Corporation Automated Risk Controls, dated February 2019, at p.2 (provided to NSCC on June 17, 2021).

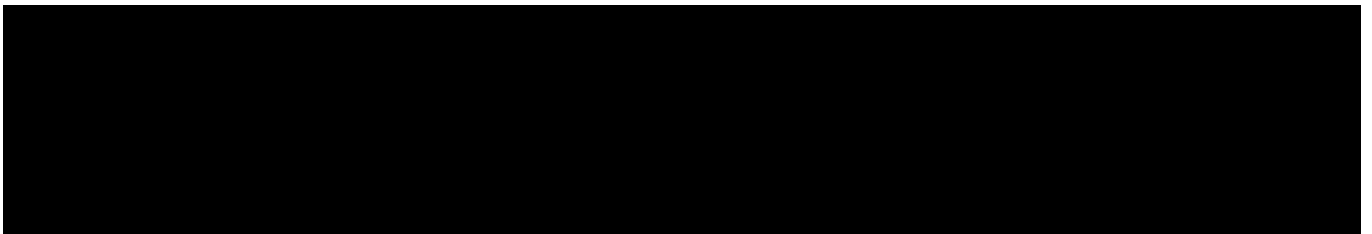
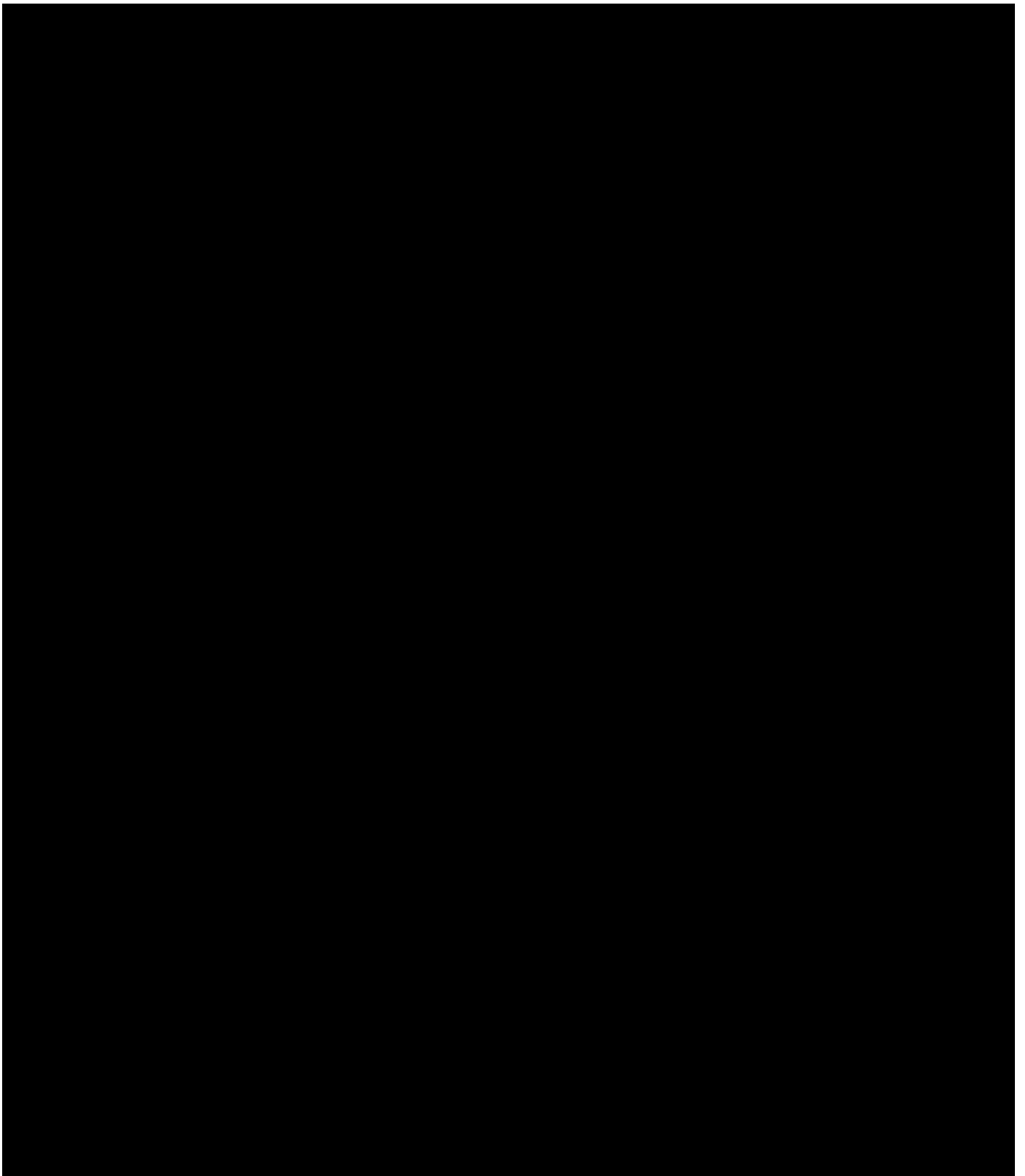
DTCC Attachment 7

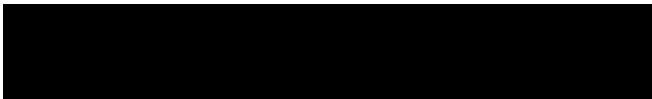
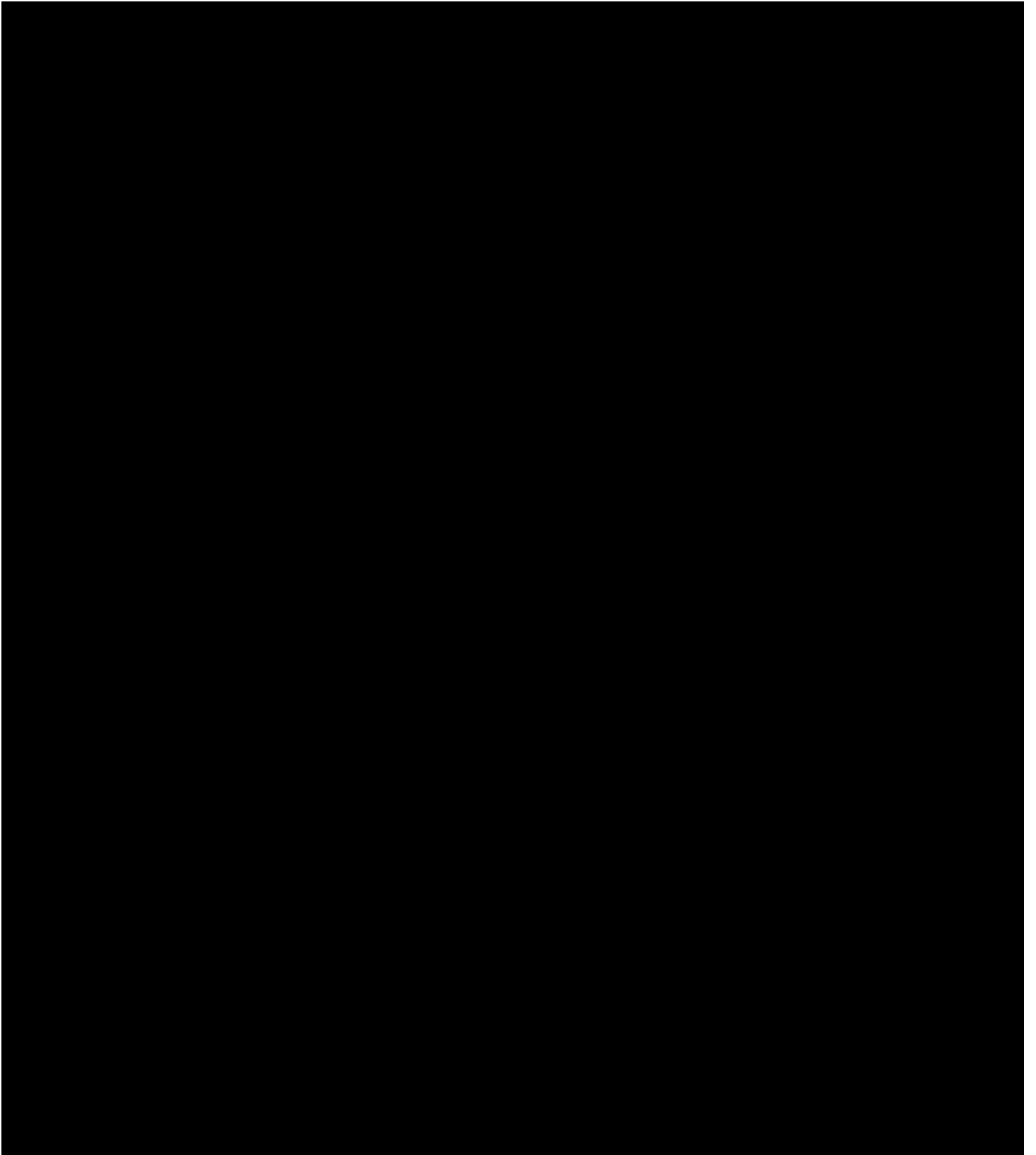


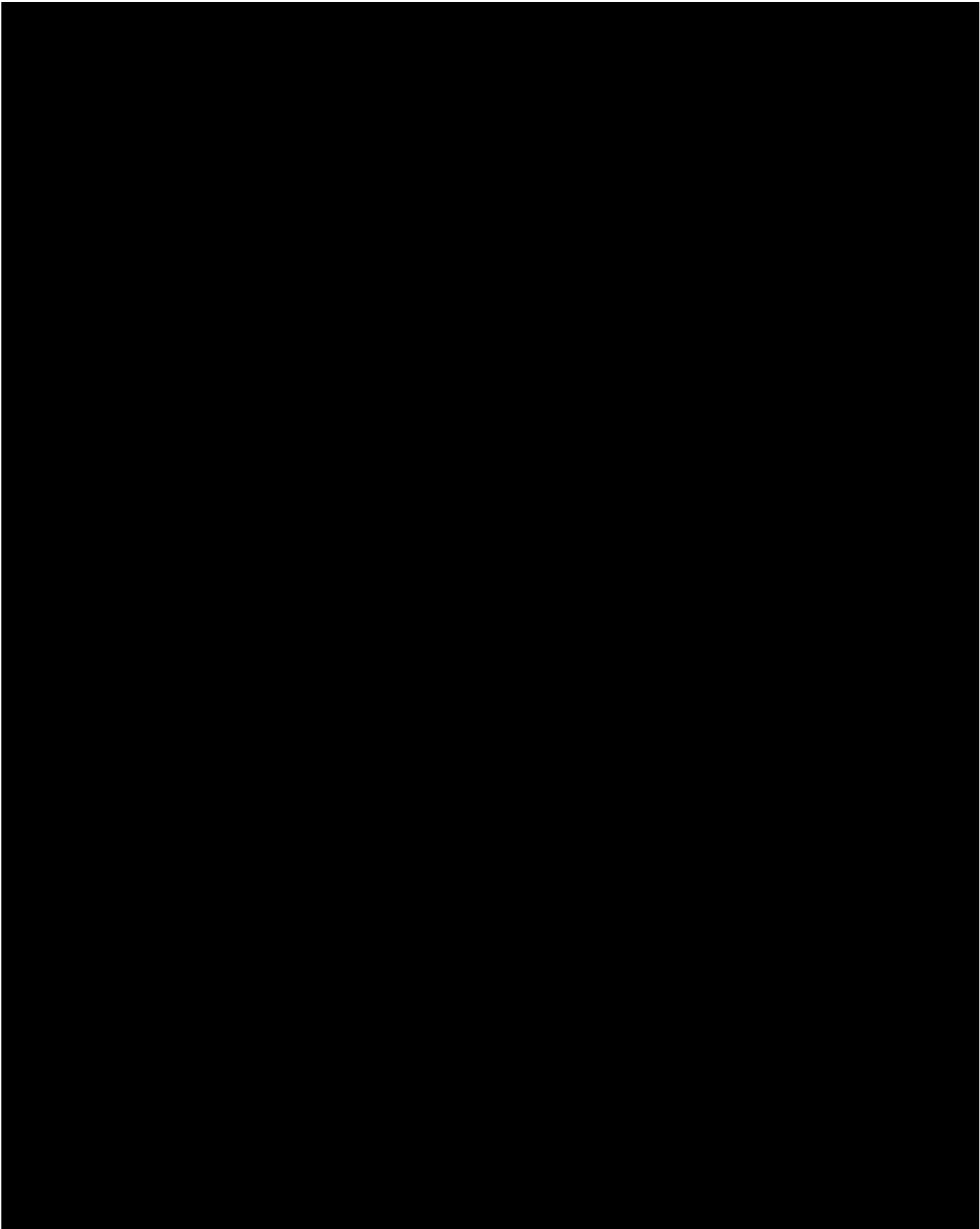
¹ References to exhibits (“Ex.”) refer to the exhibits as numbered in DTCC’s Compendium of Exhibits, which I understand is being submitted concurrently herewith.

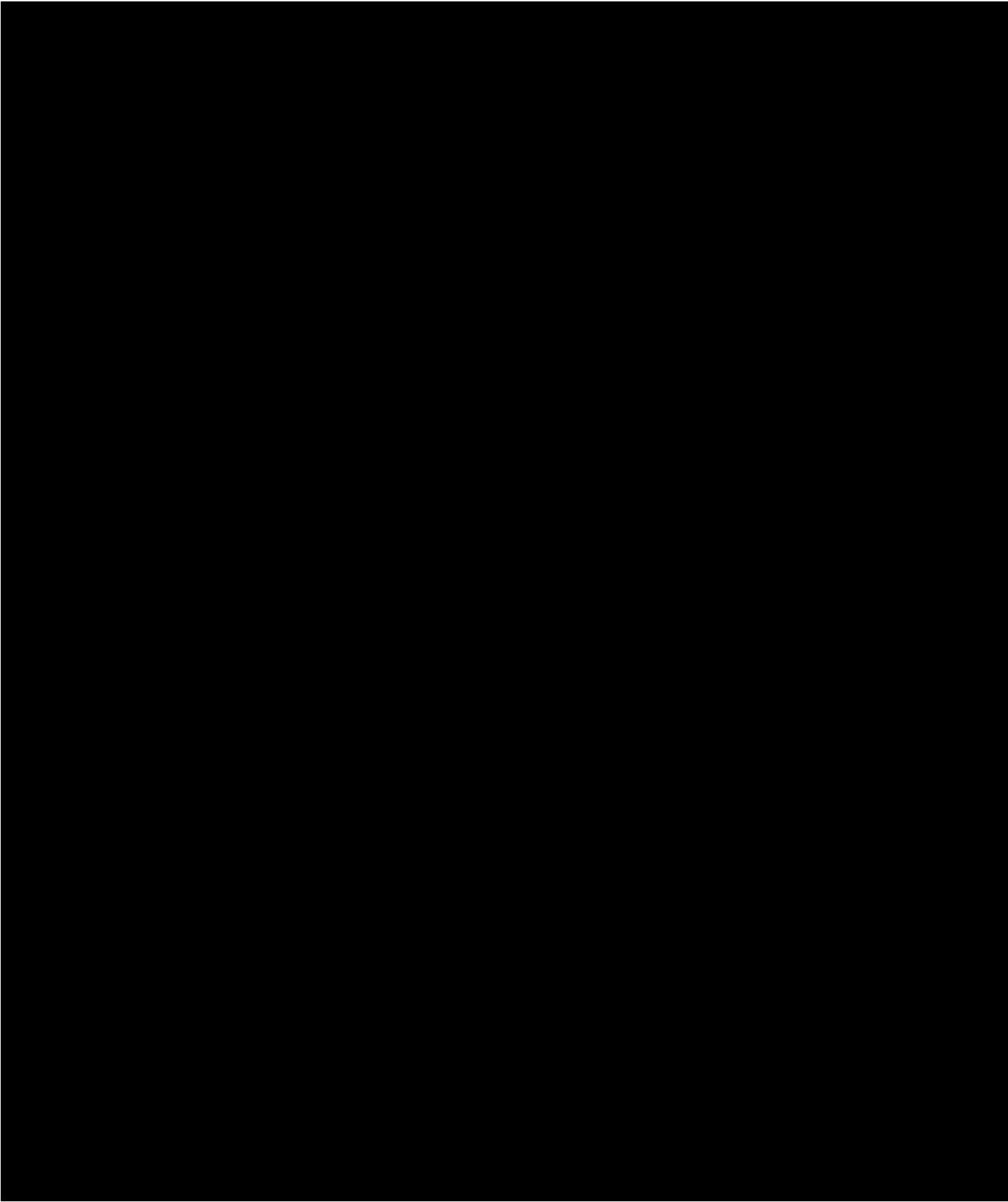


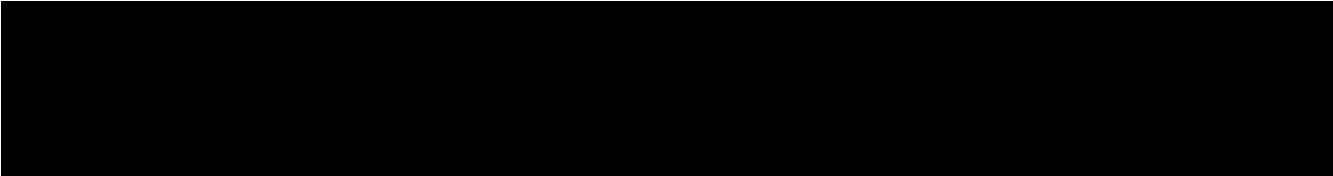


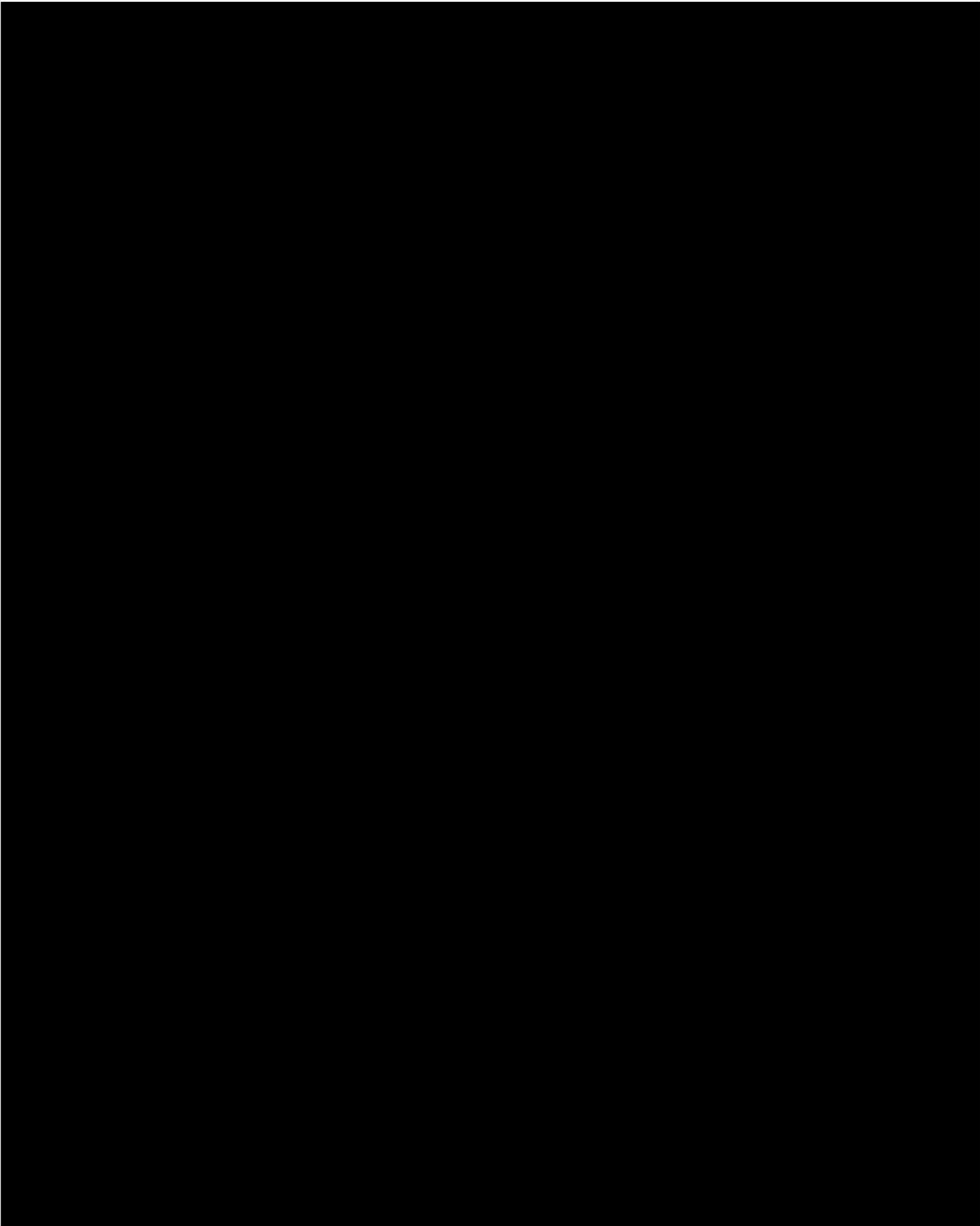




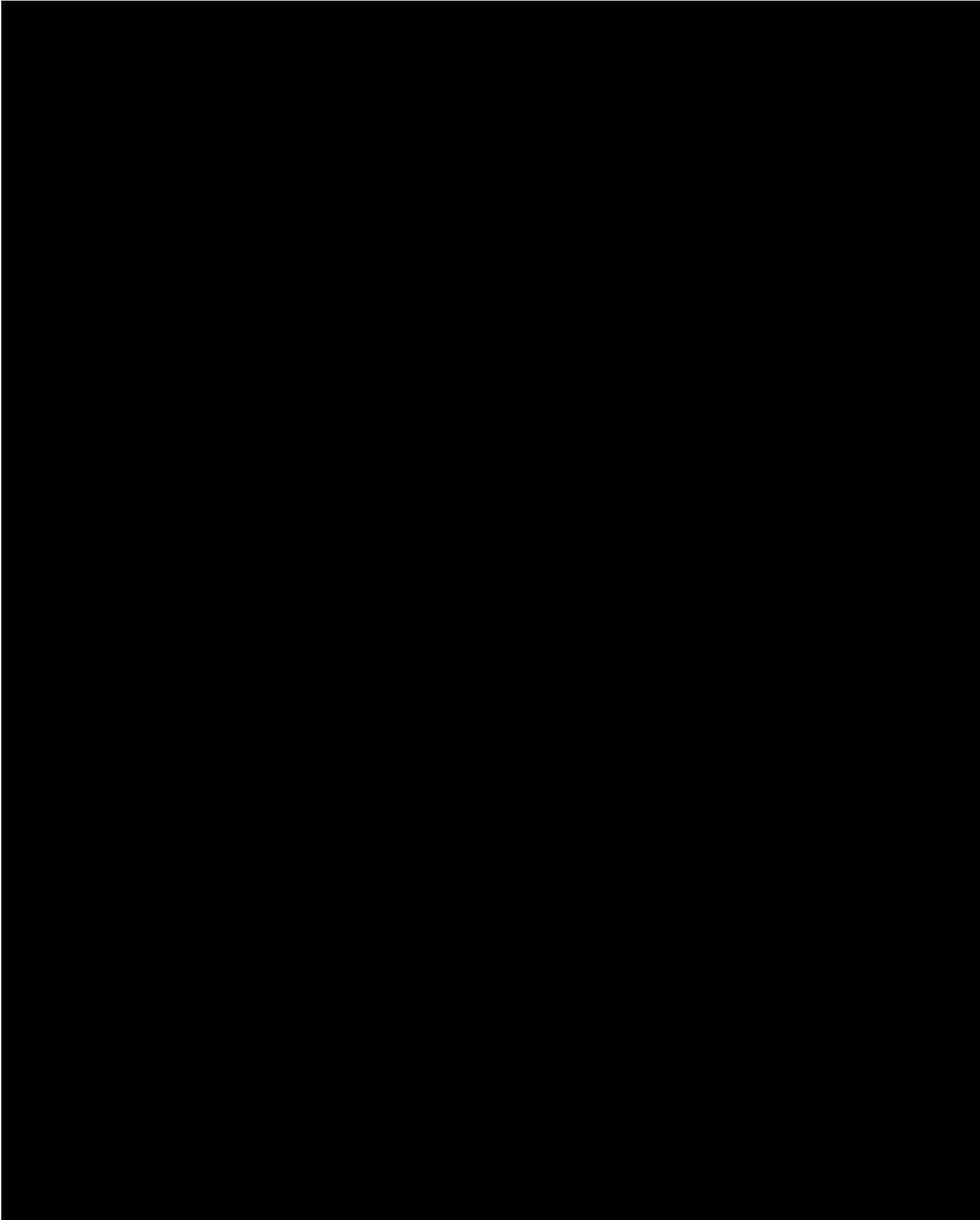


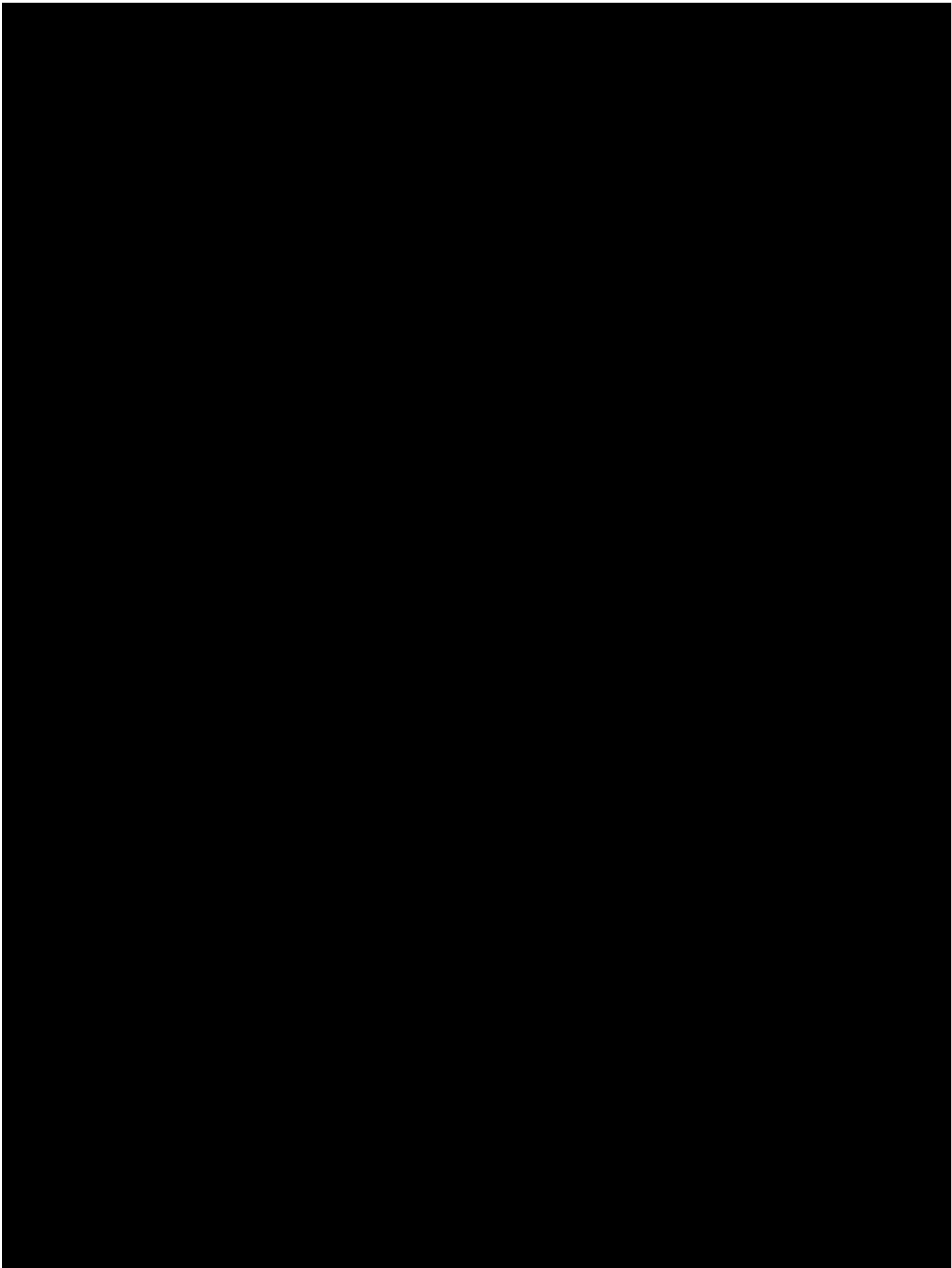






¹¹ See NSCC Rule 4 and Procedure XV.

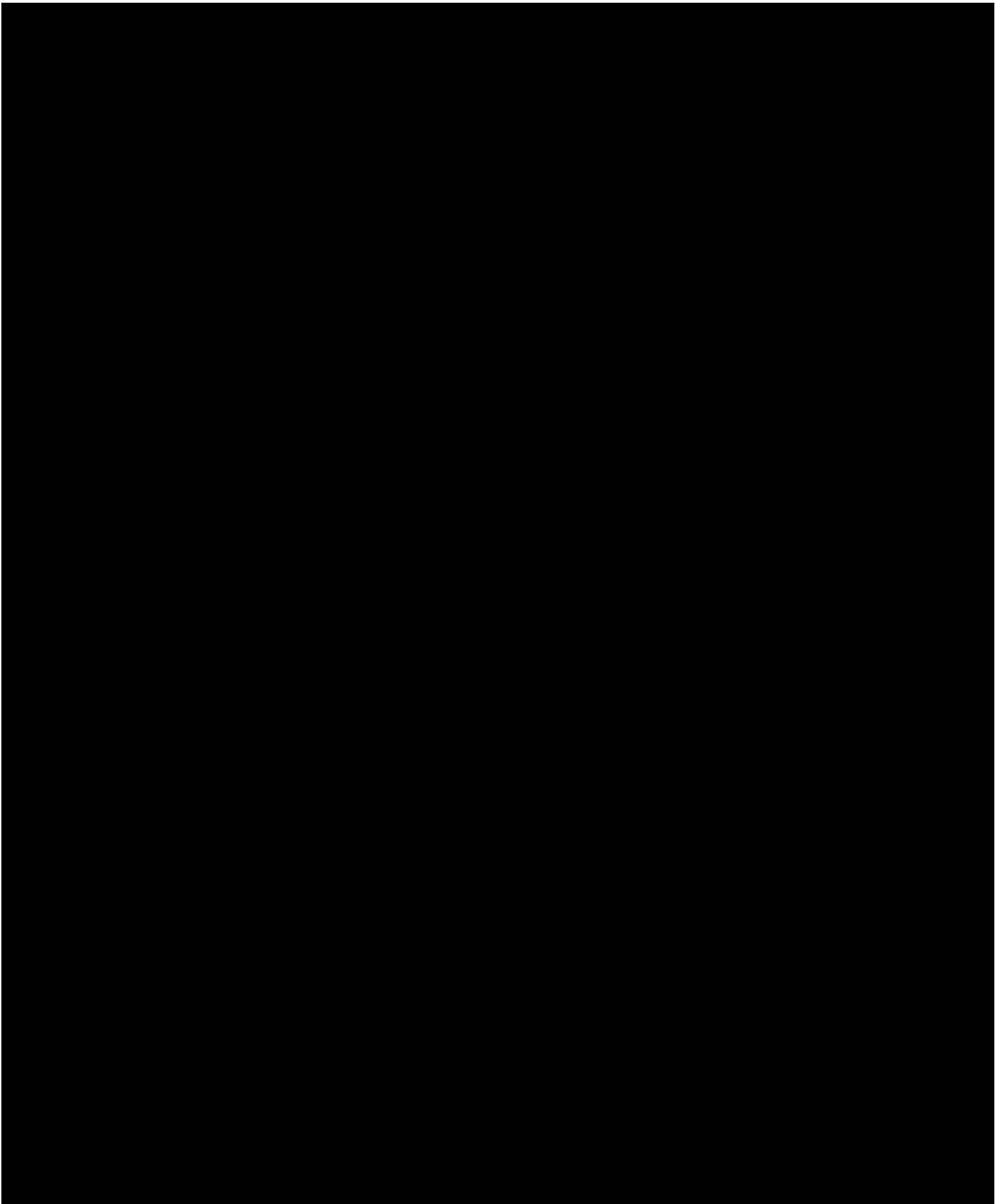


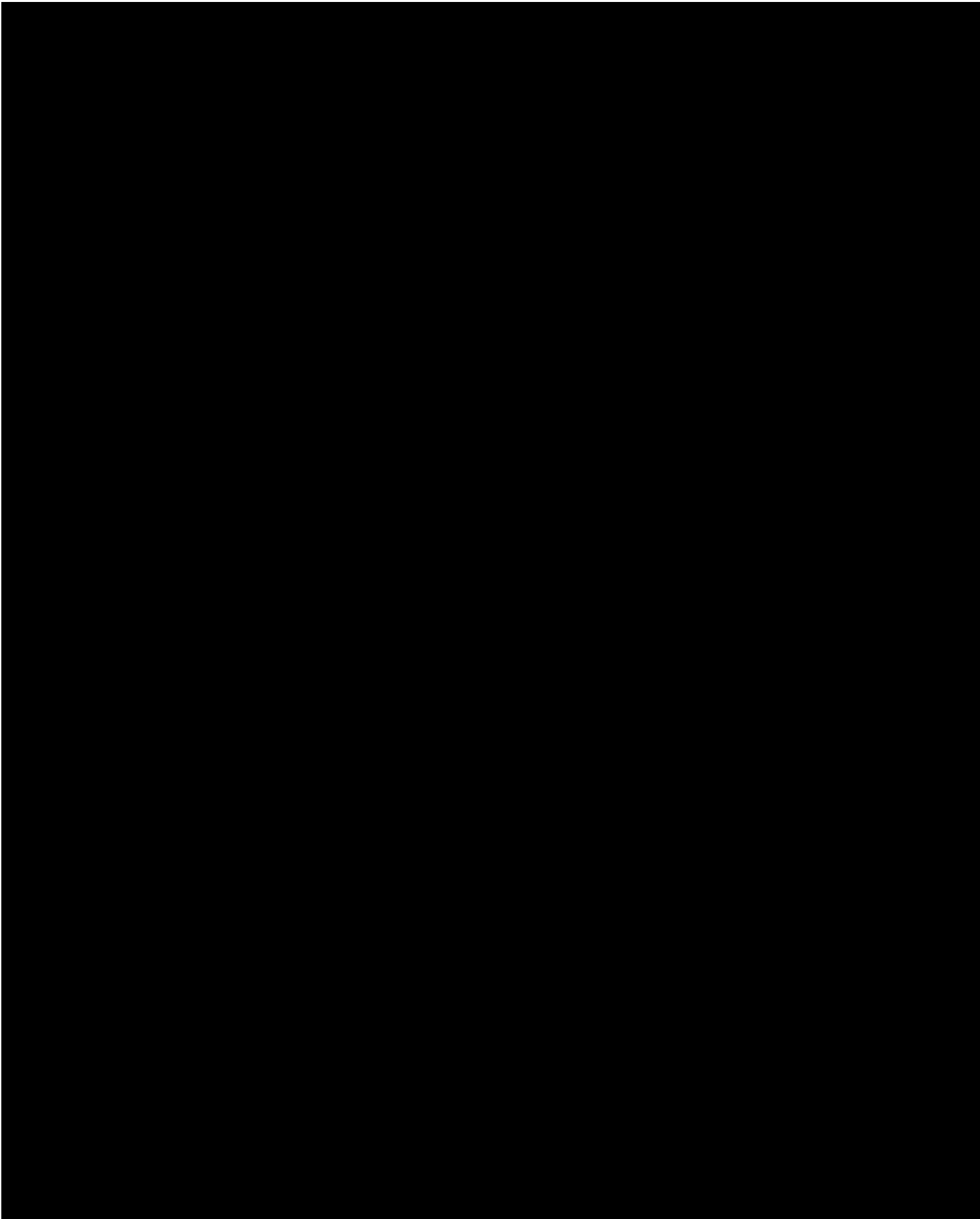


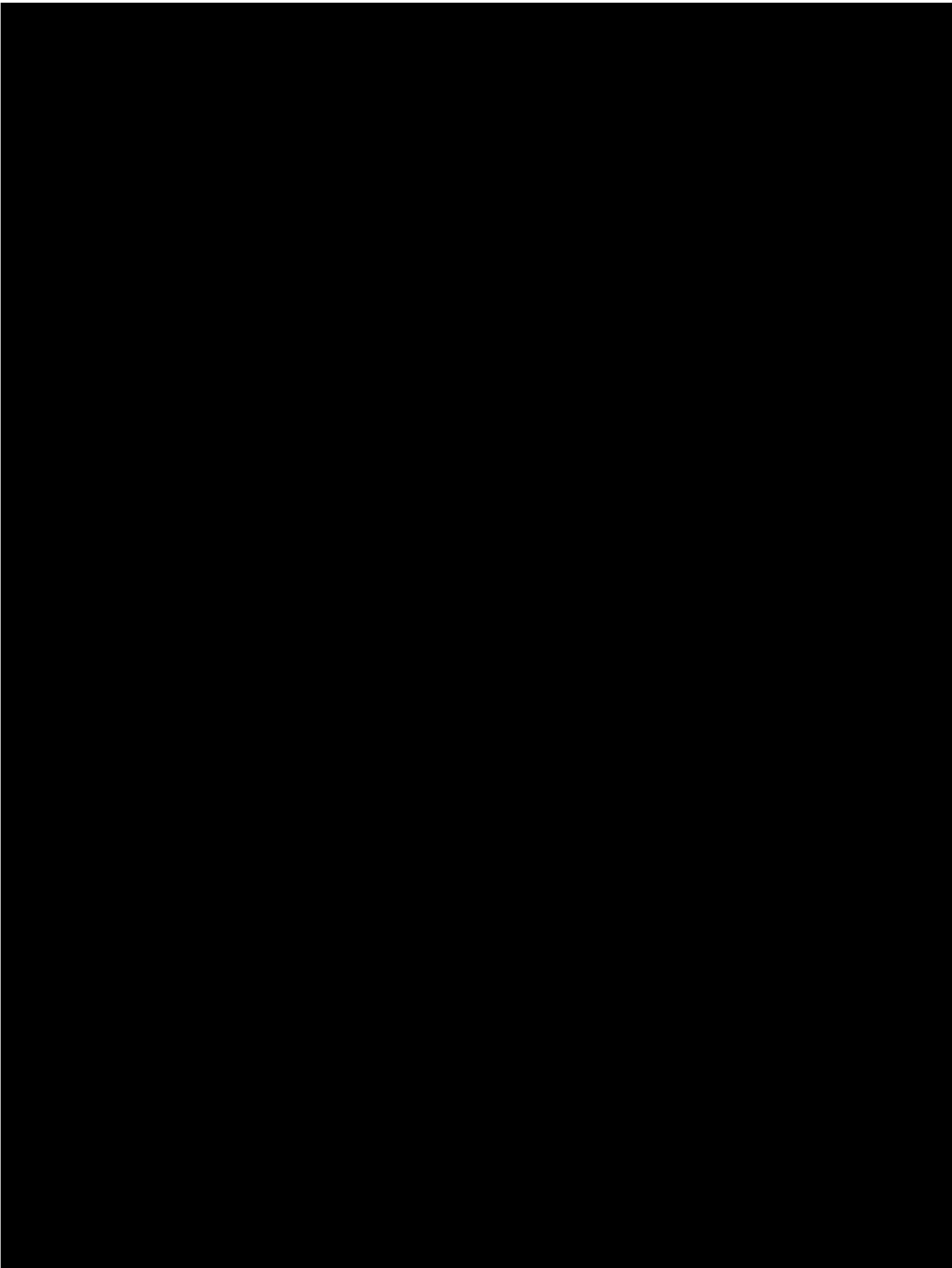
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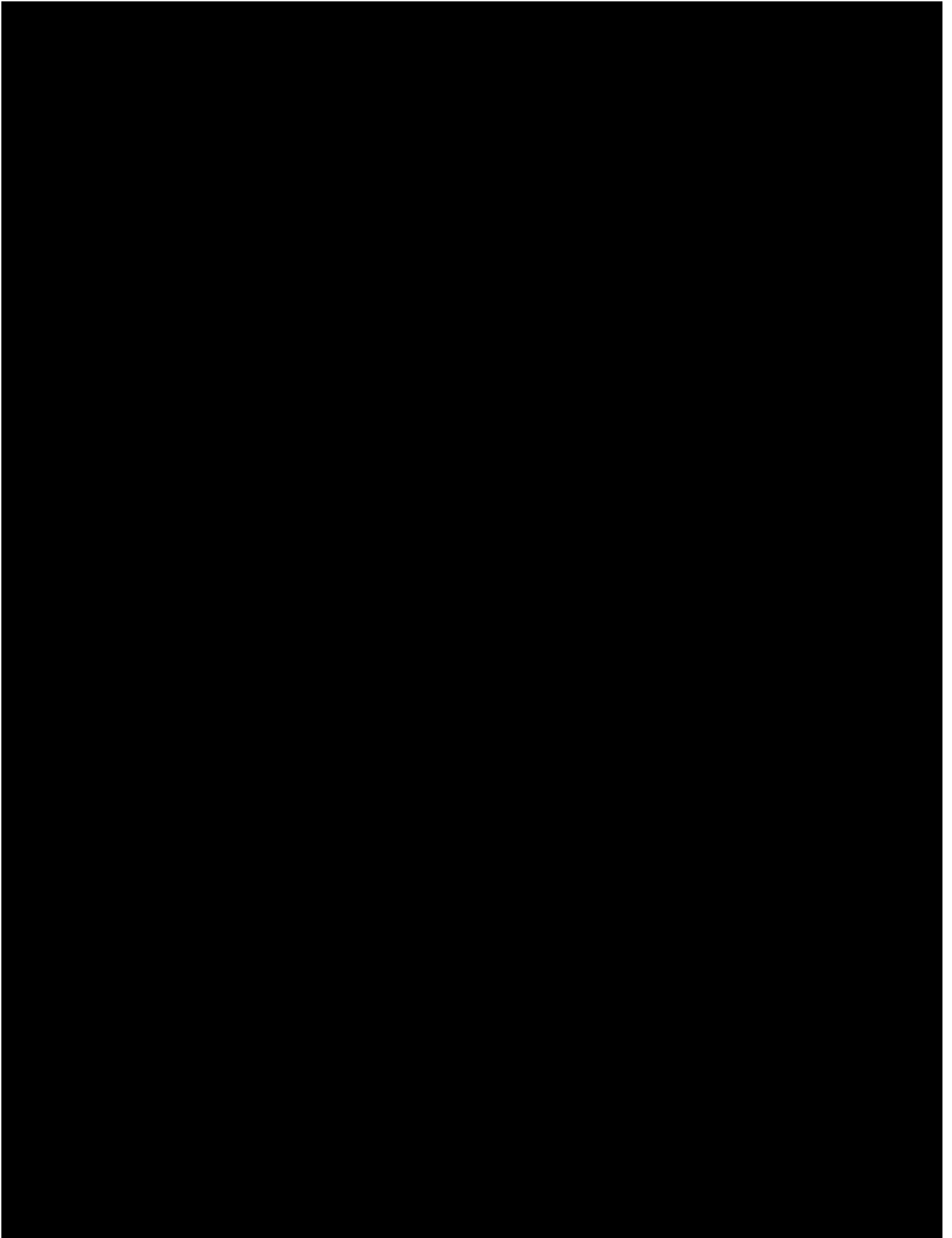
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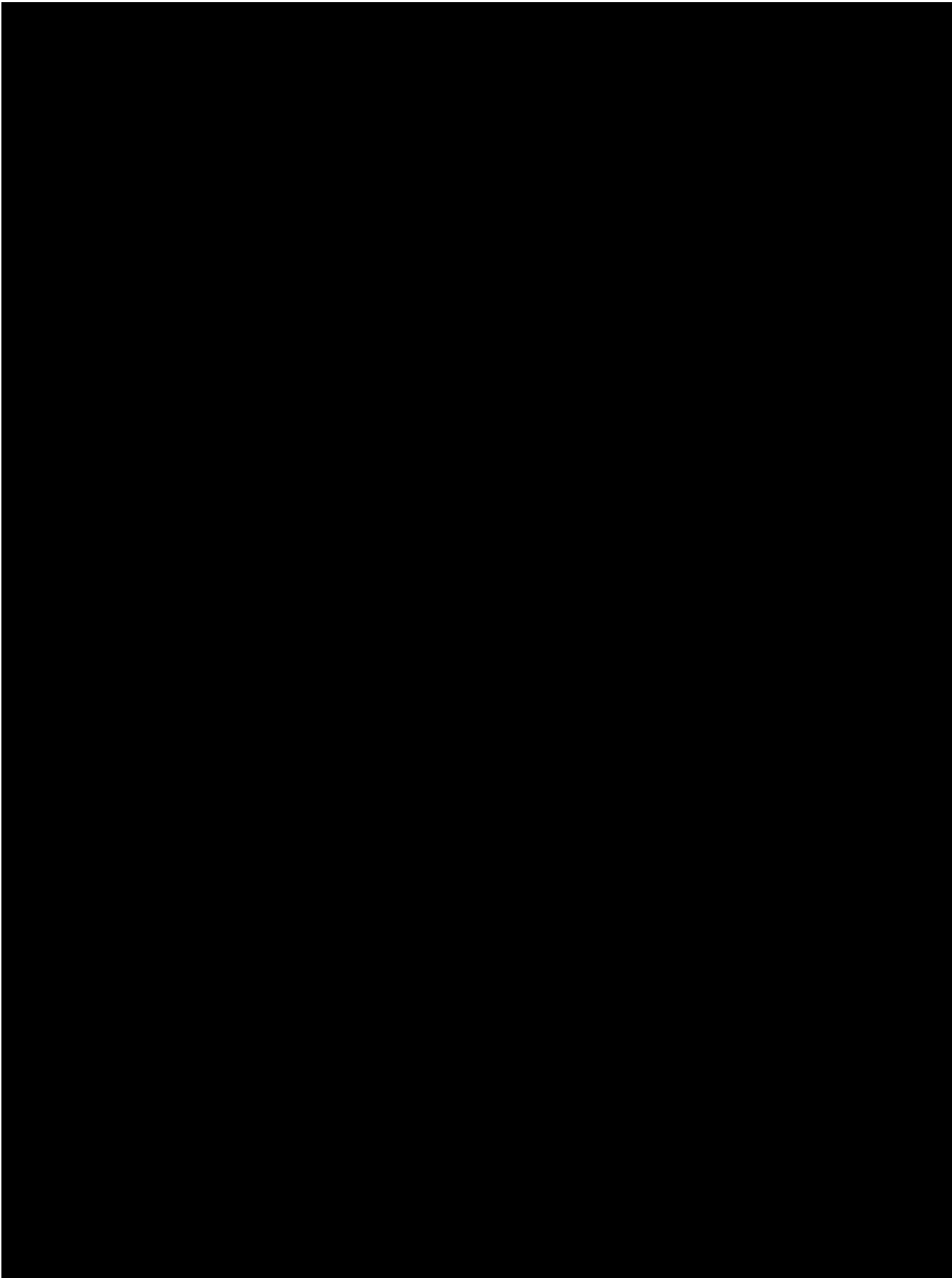
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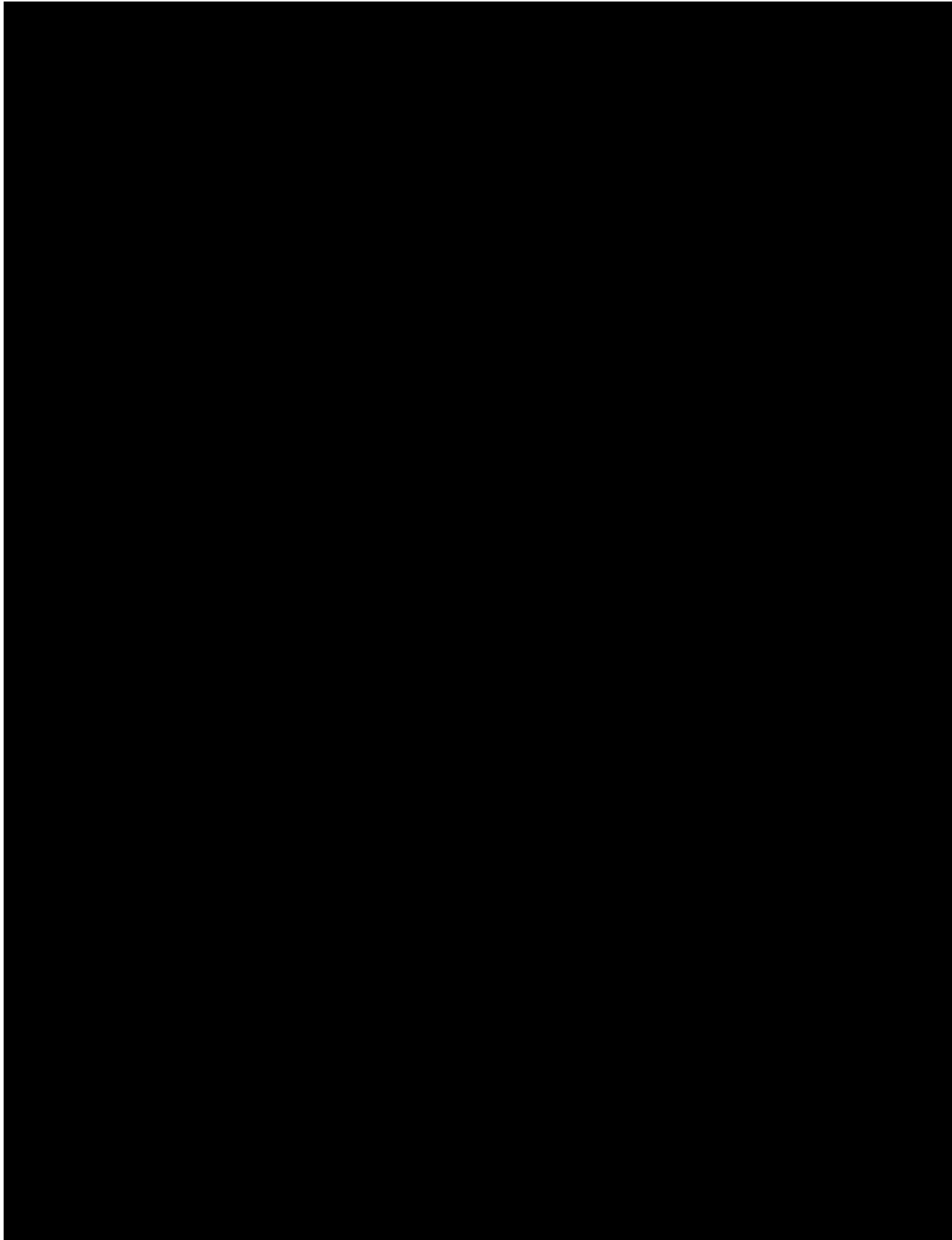


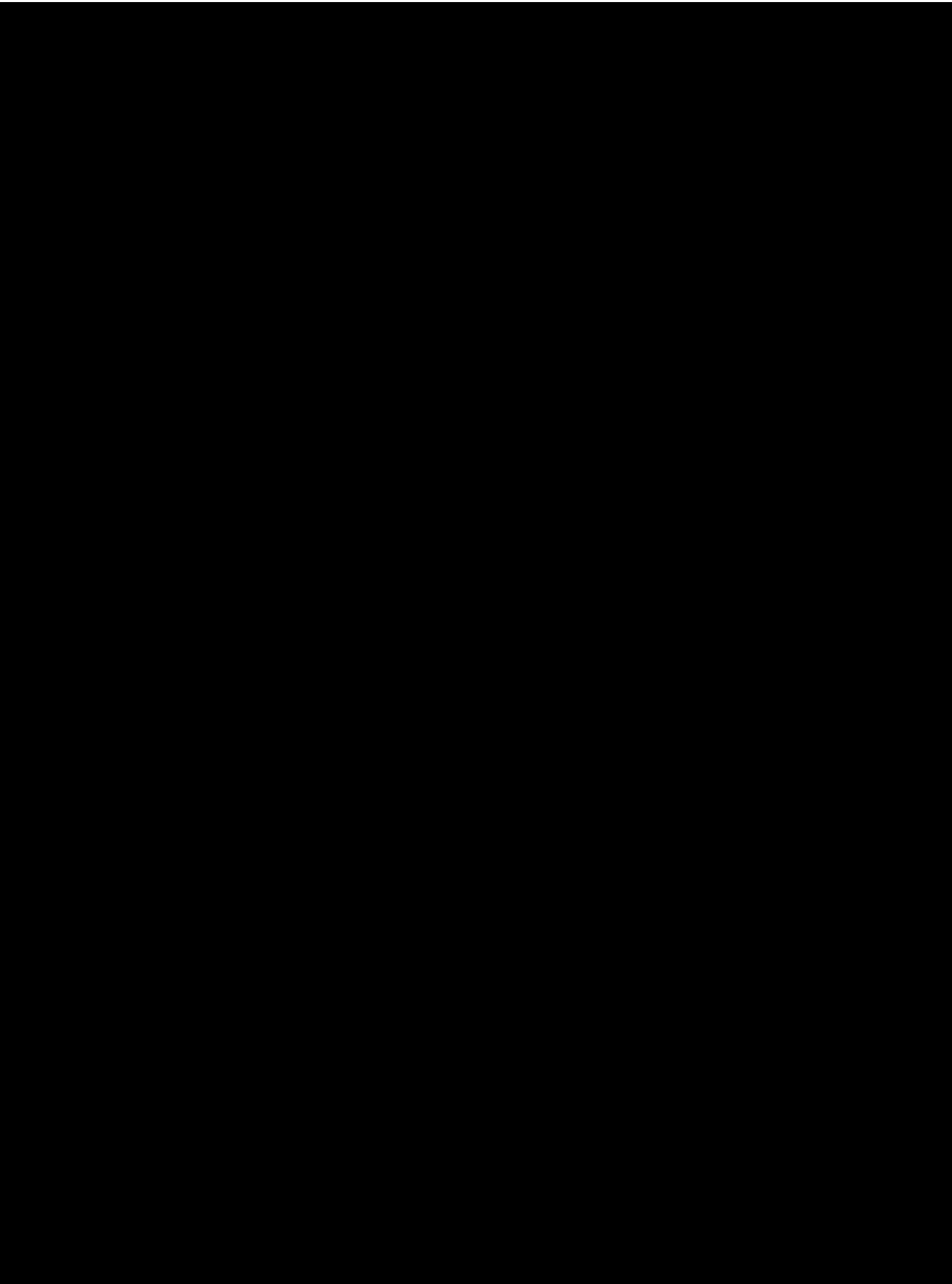


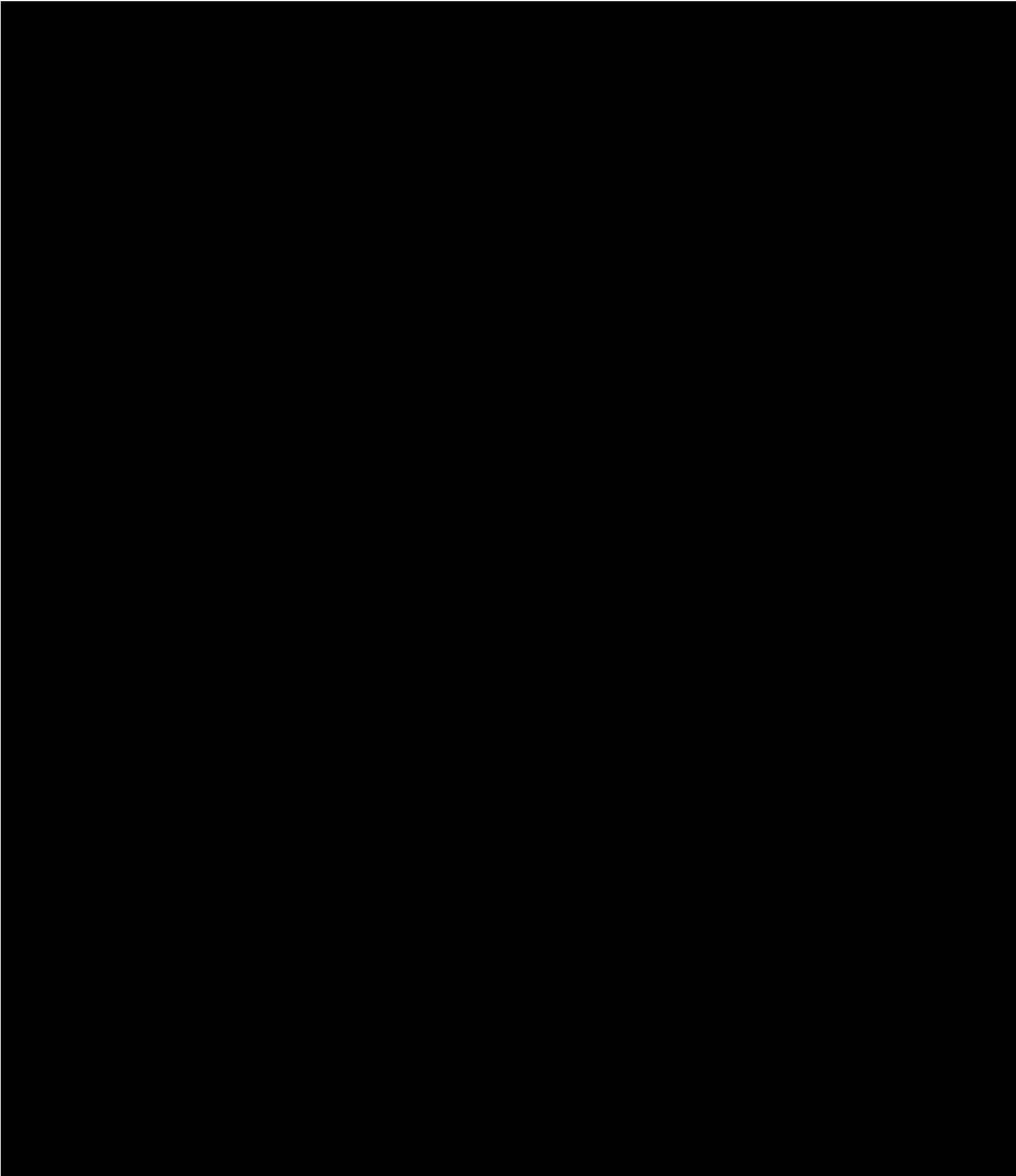


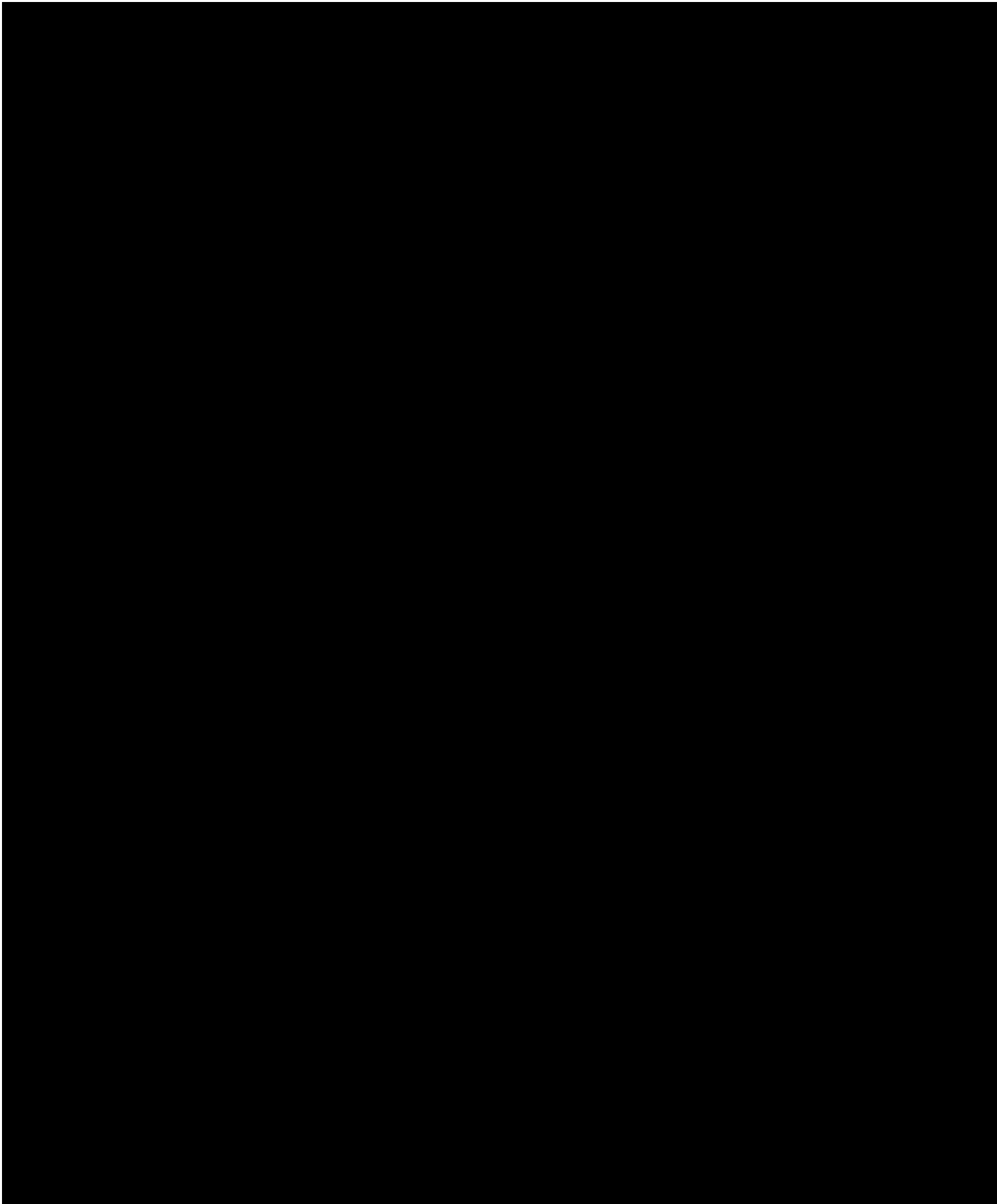


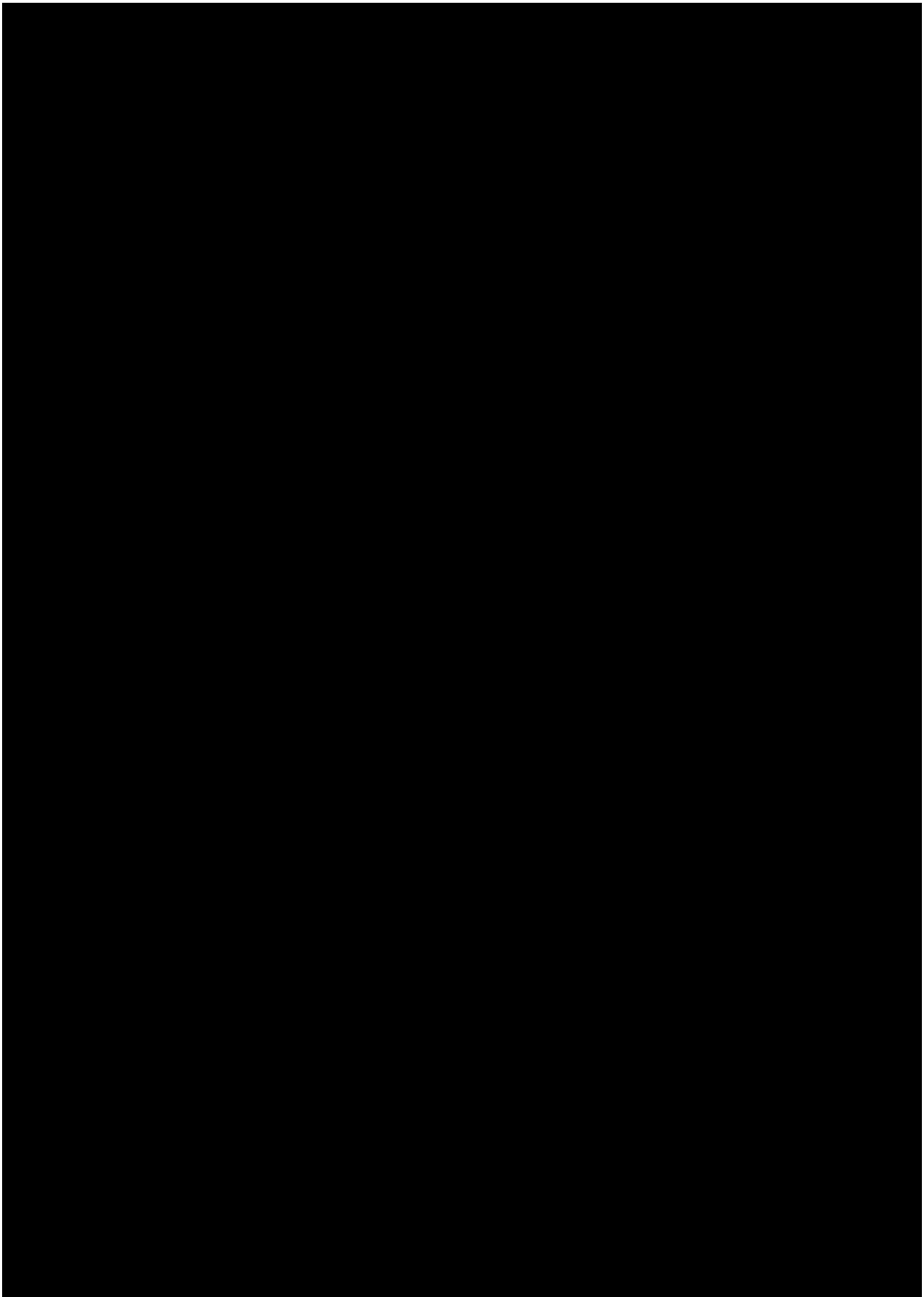


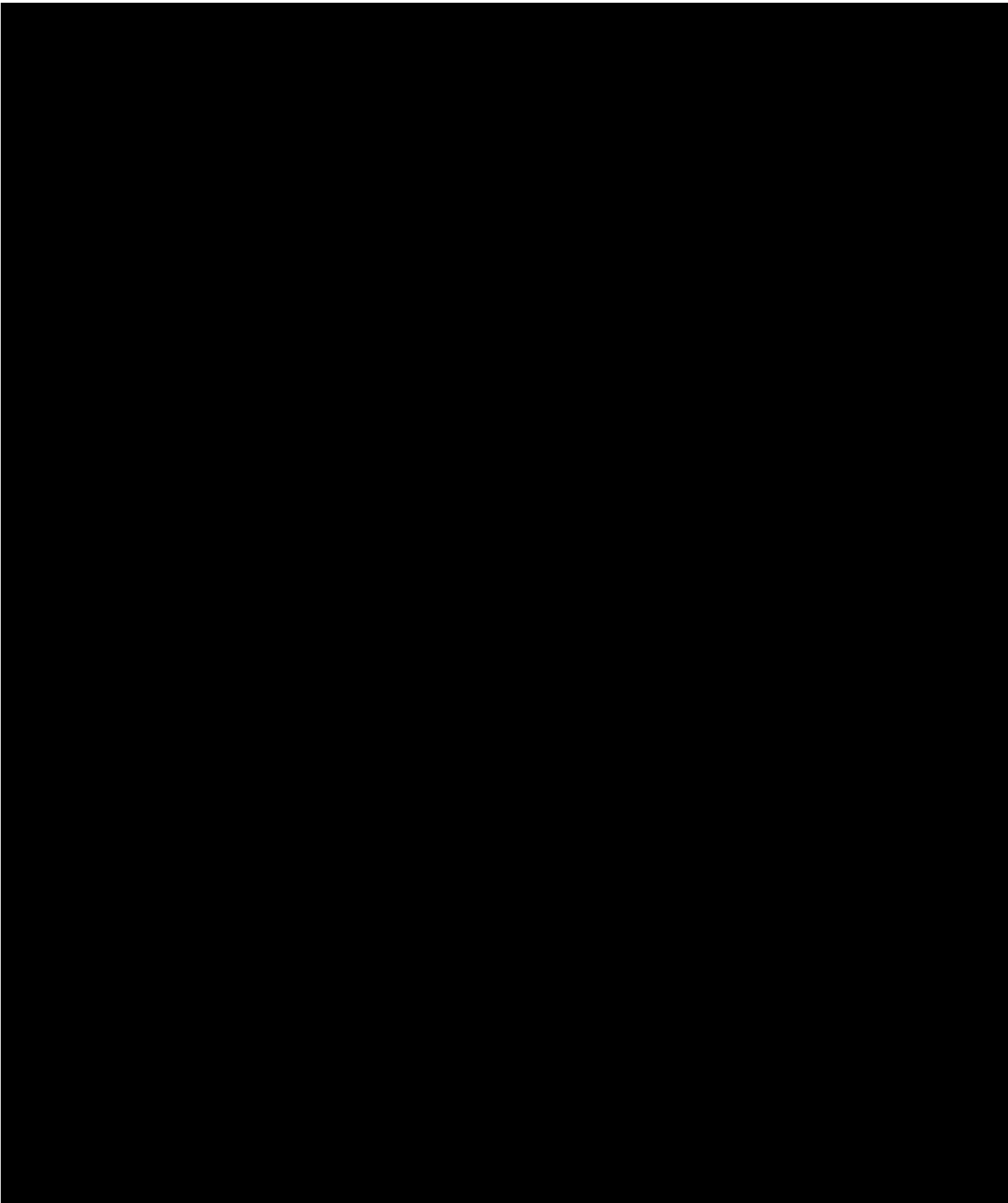


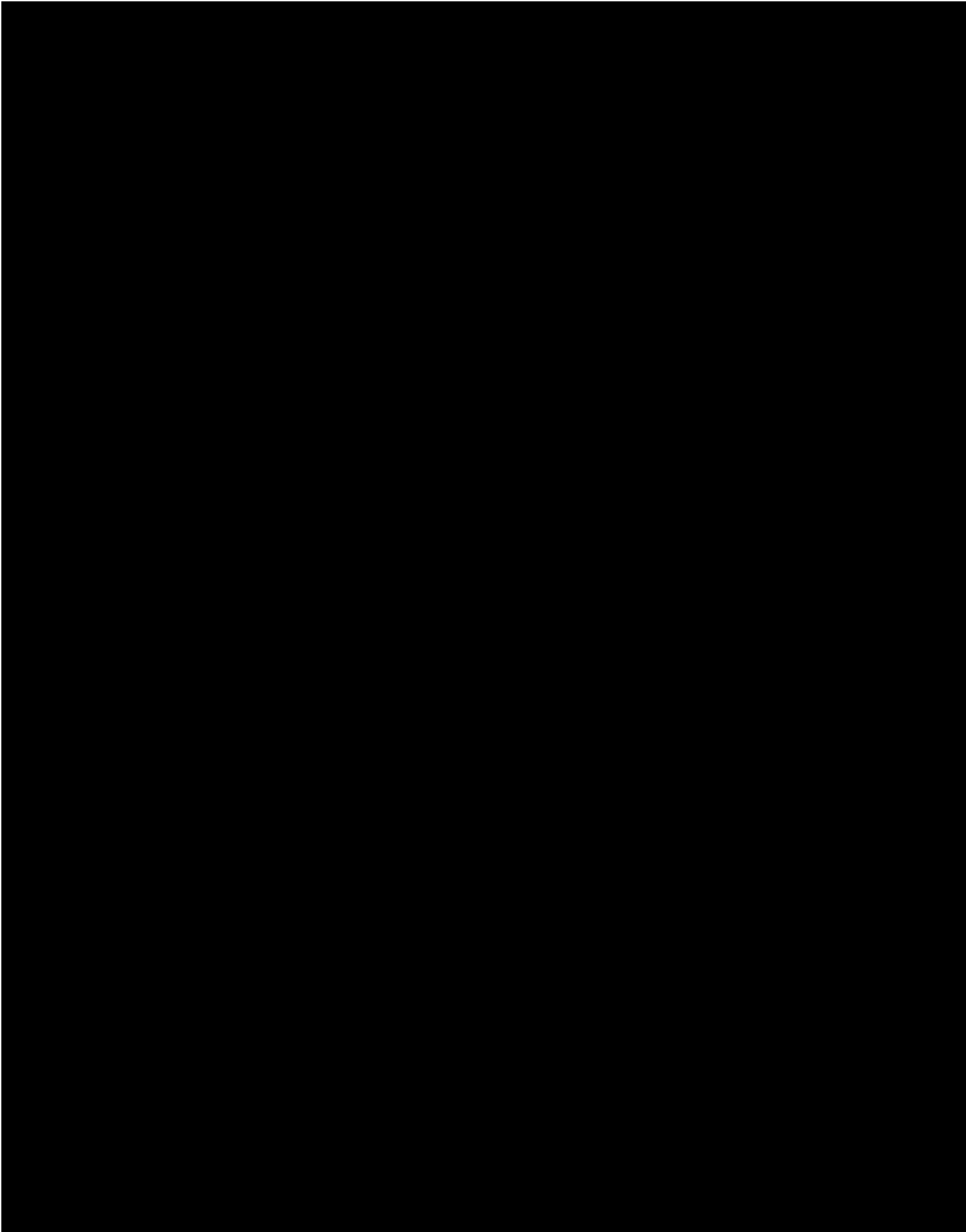


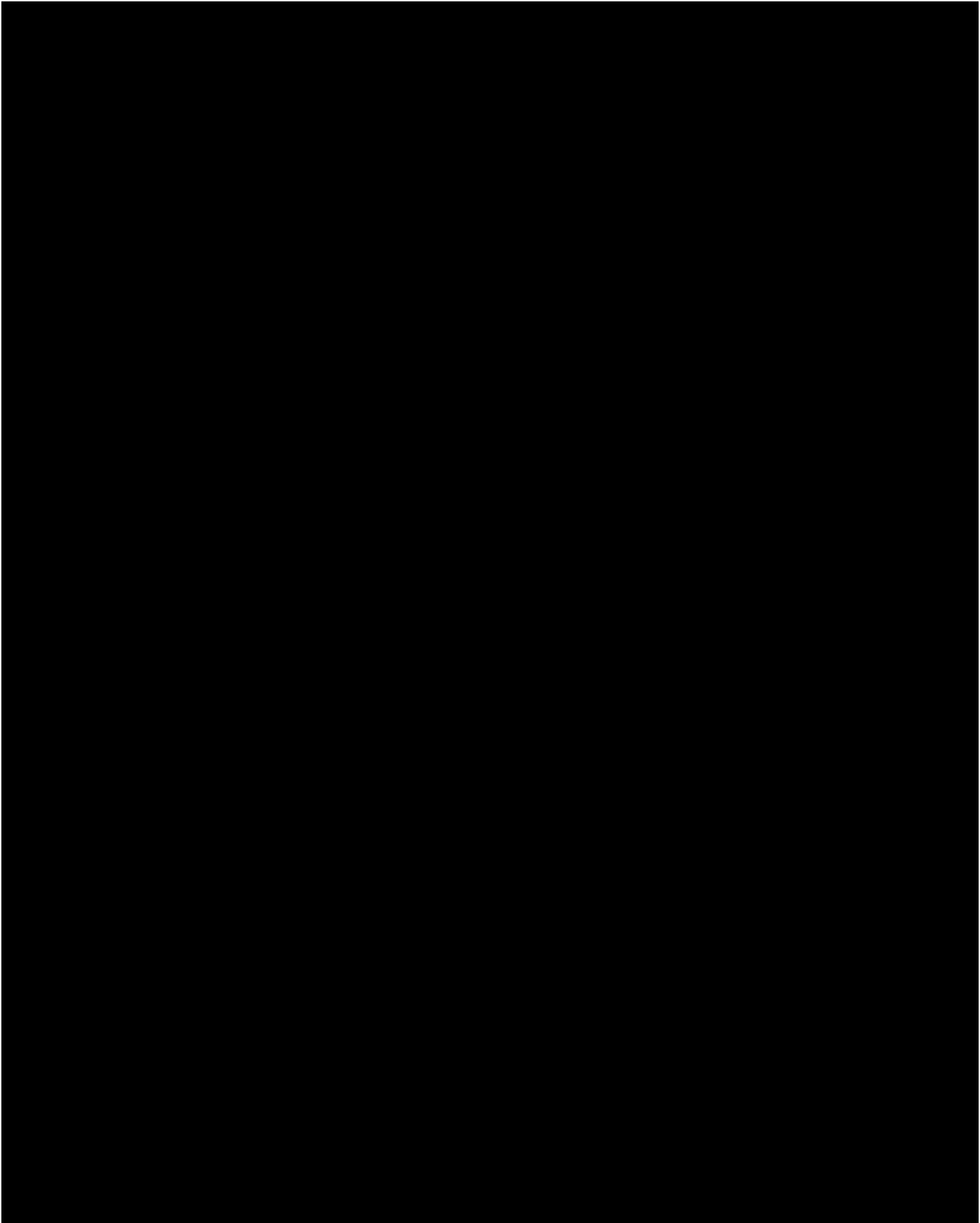


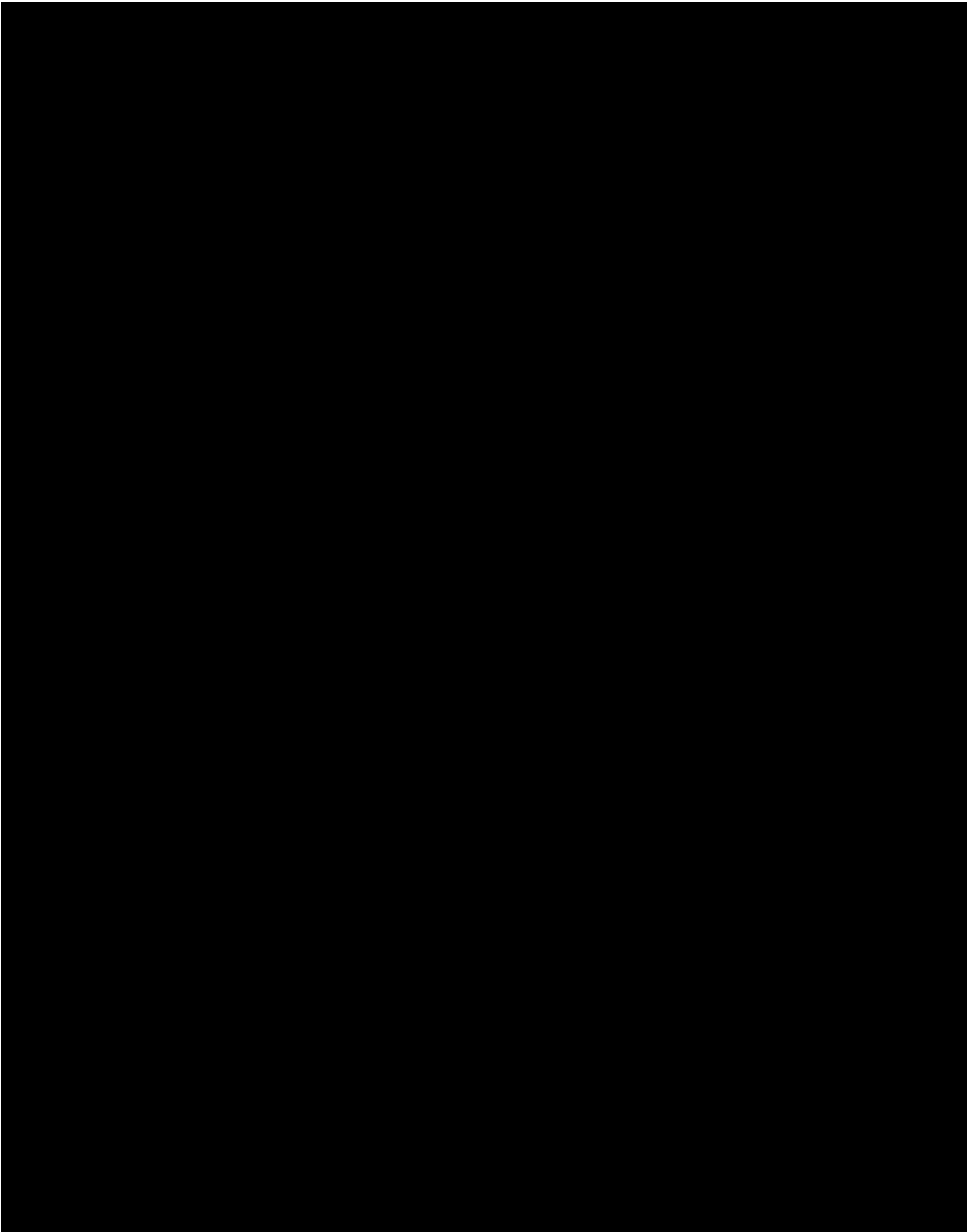






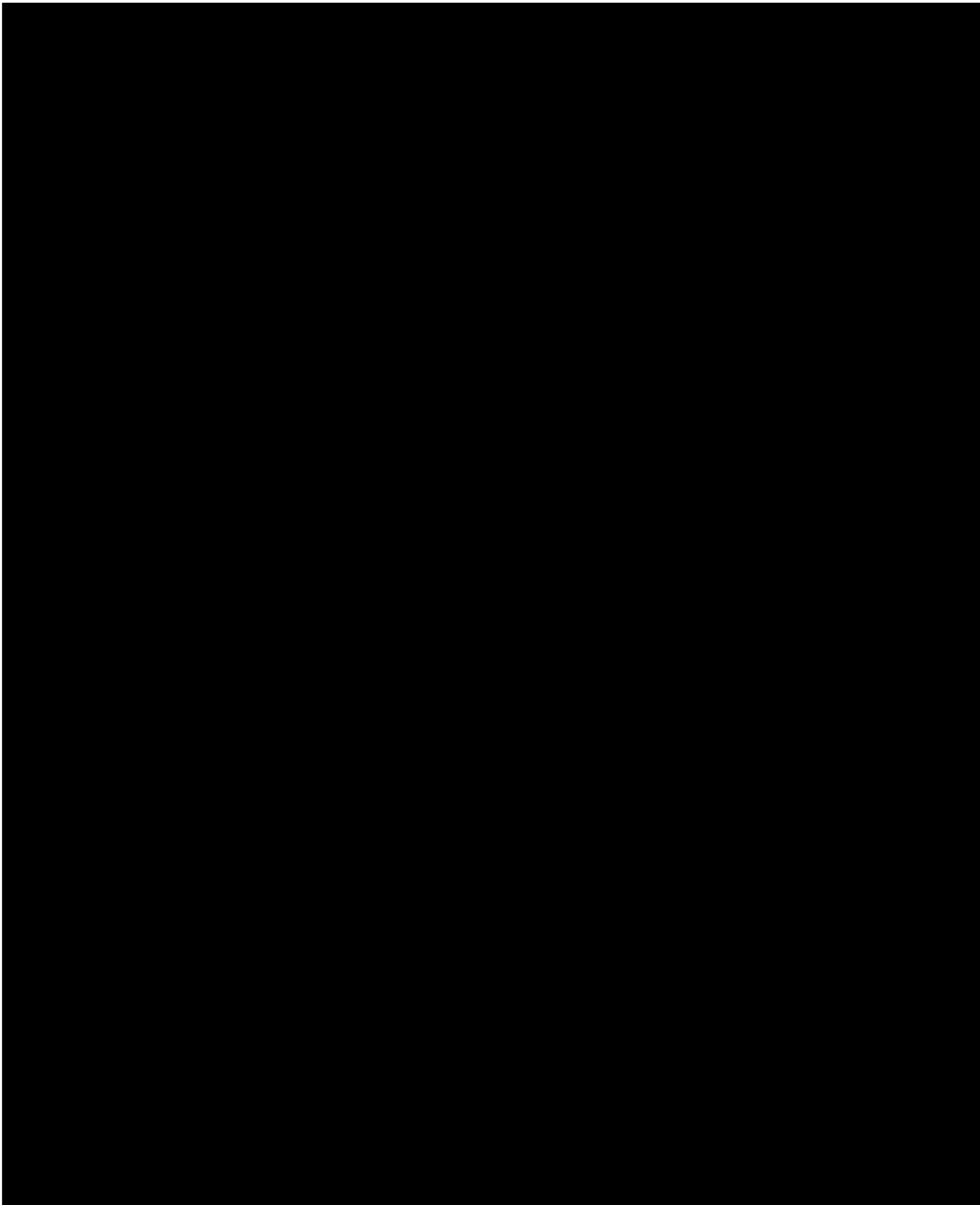


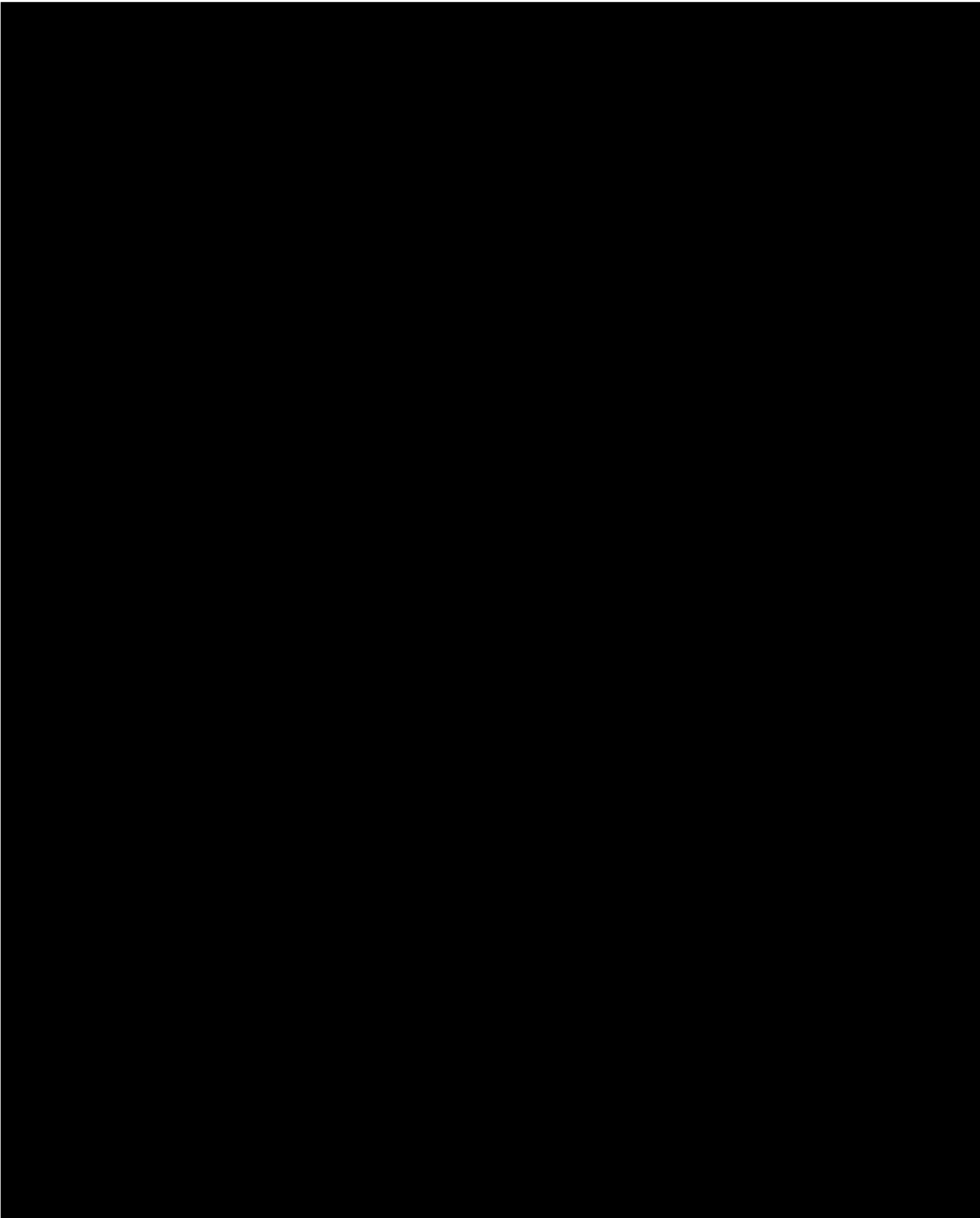


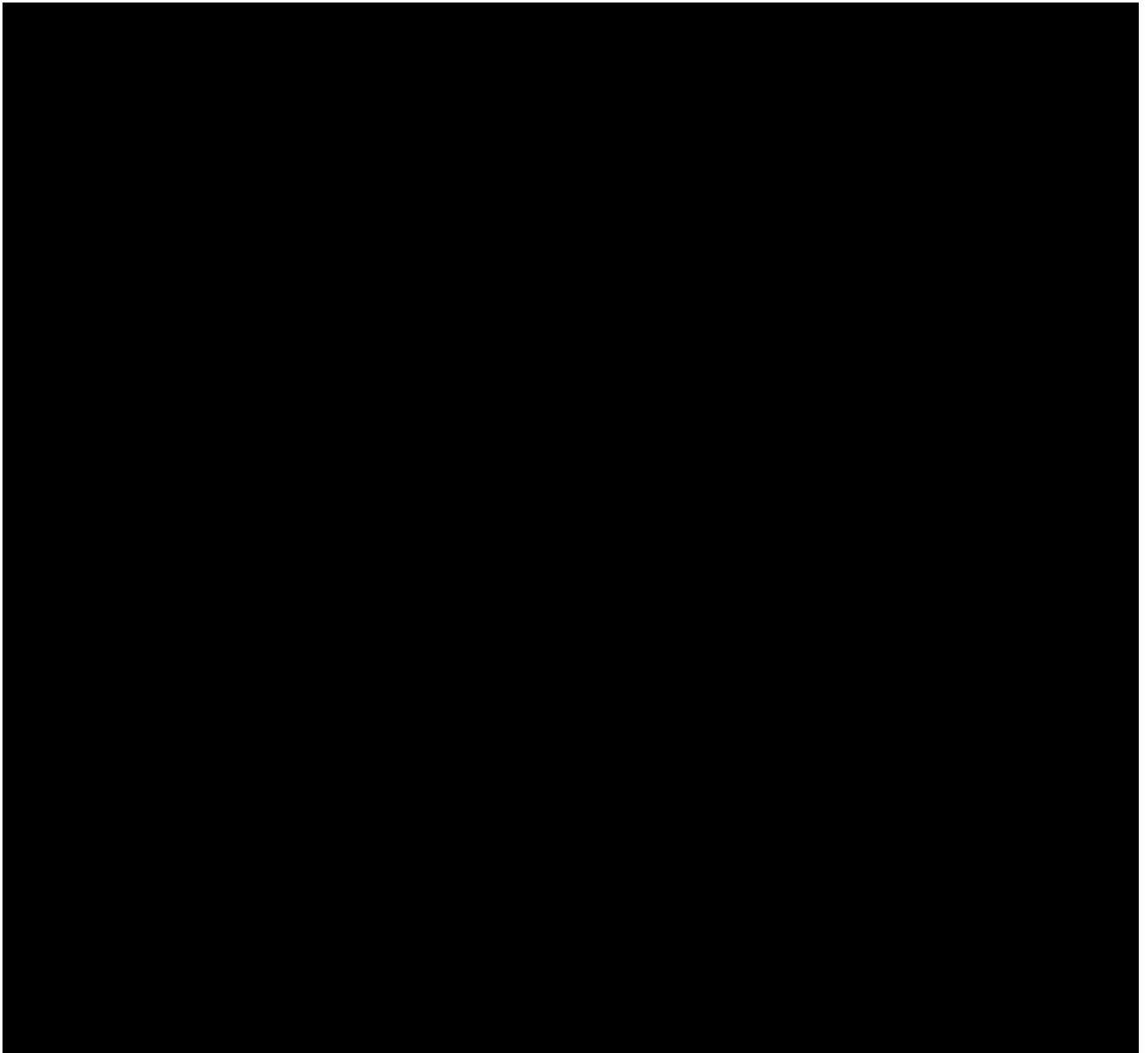


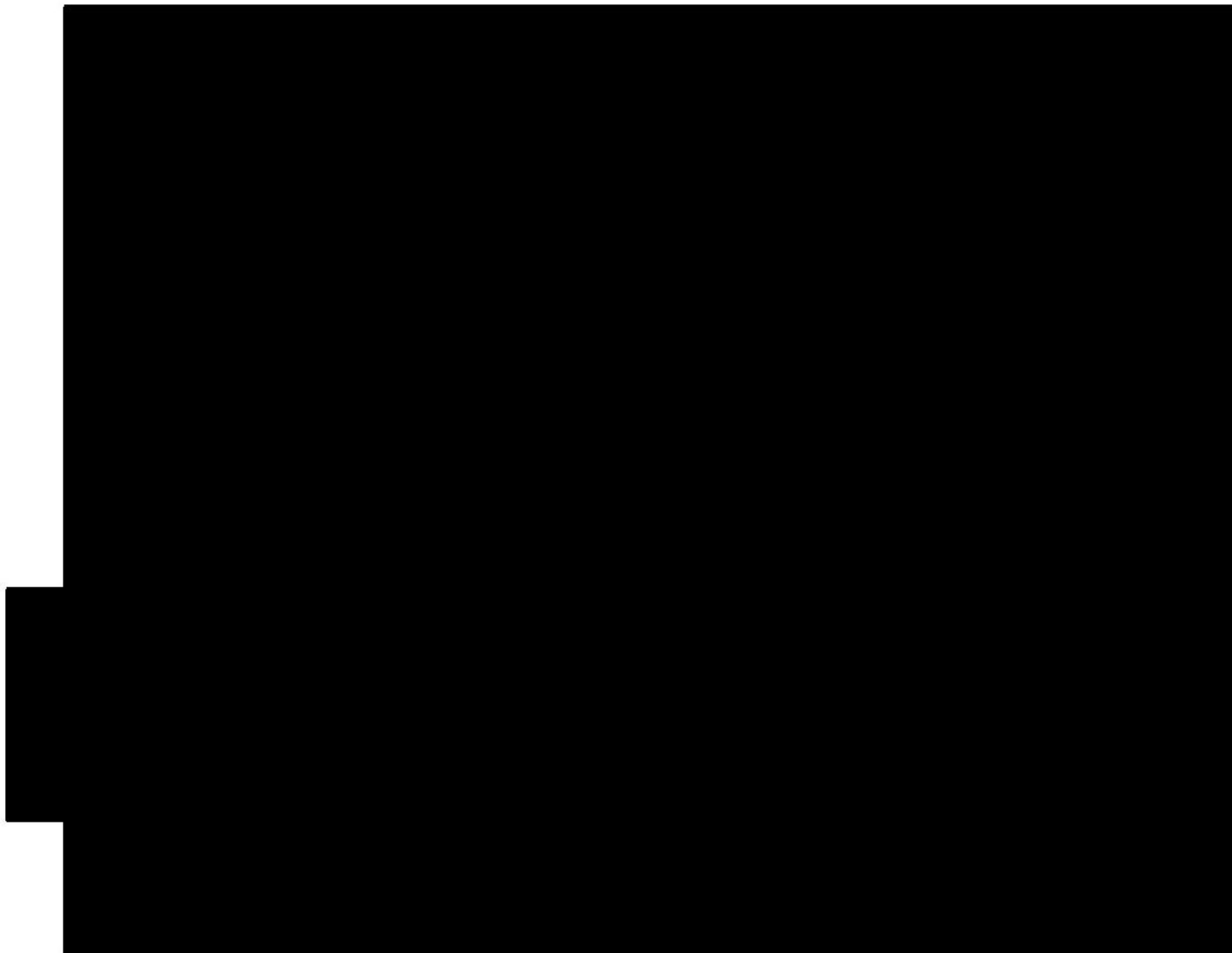
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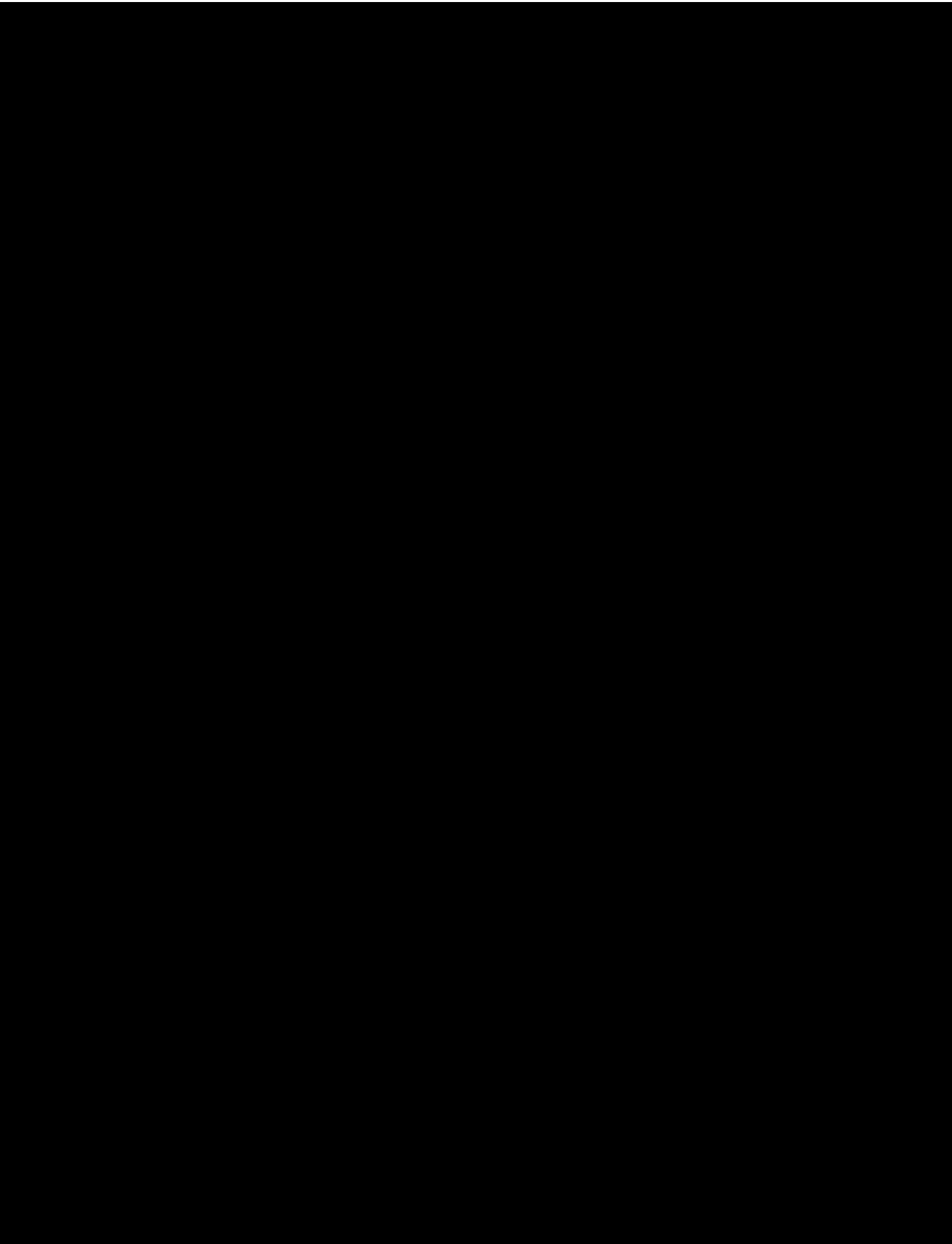


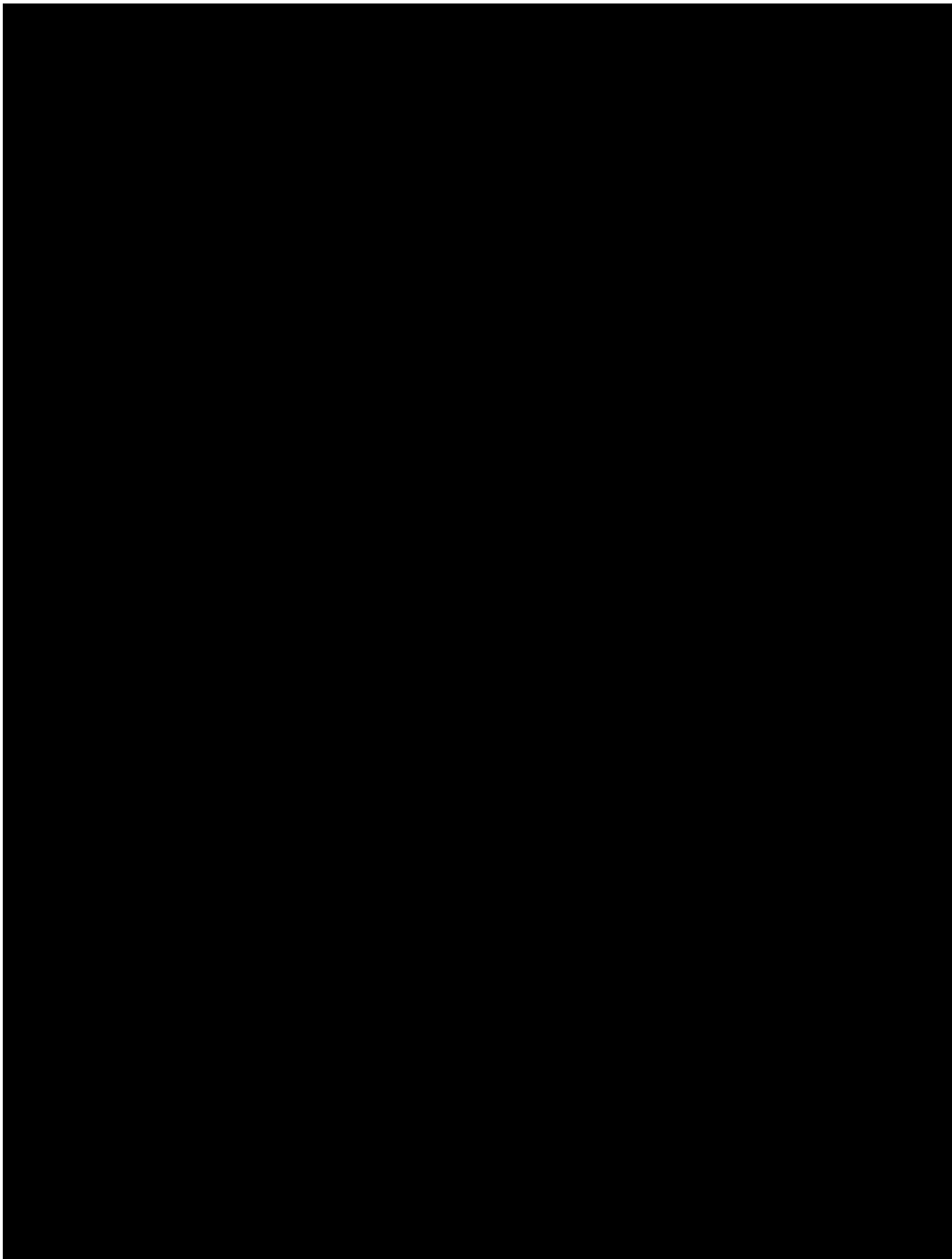


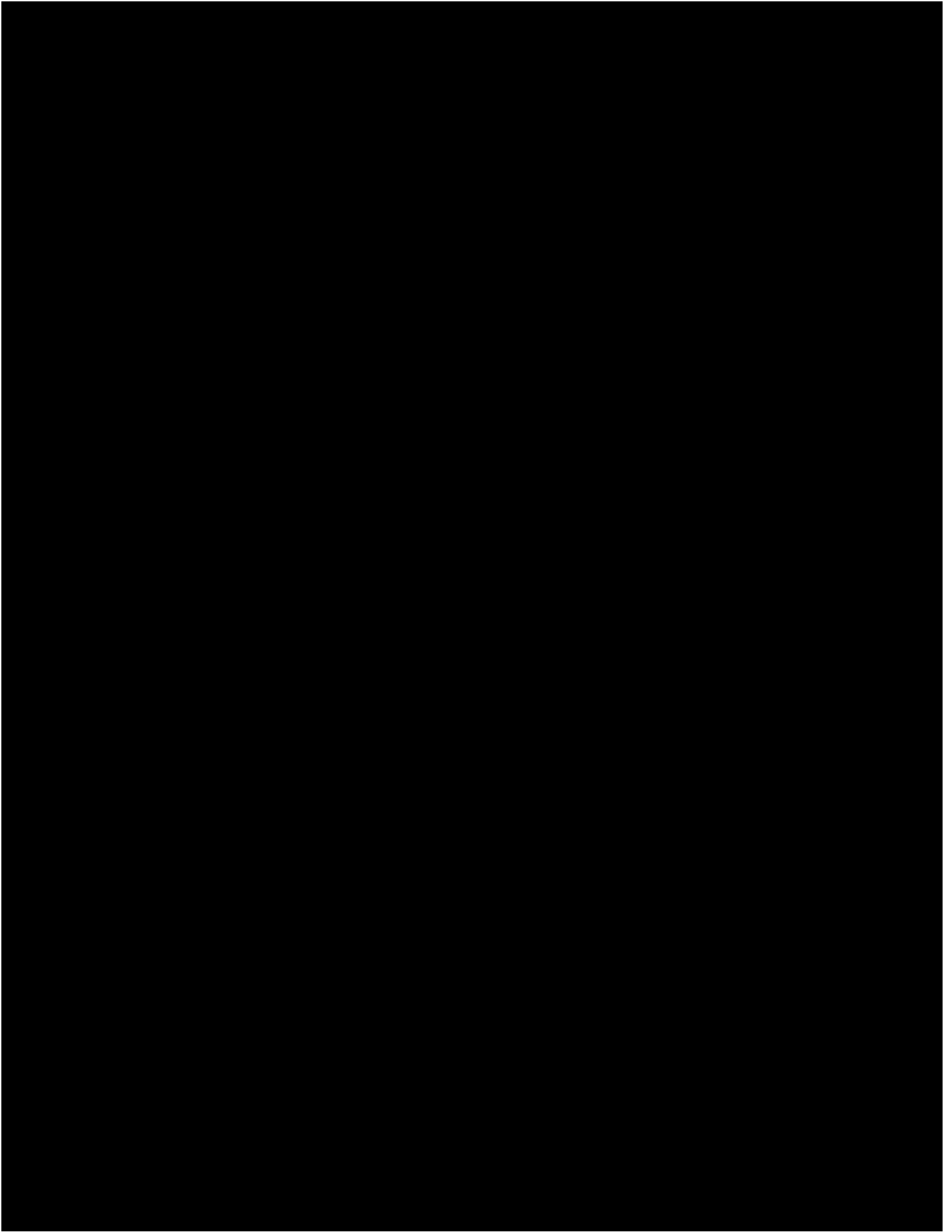


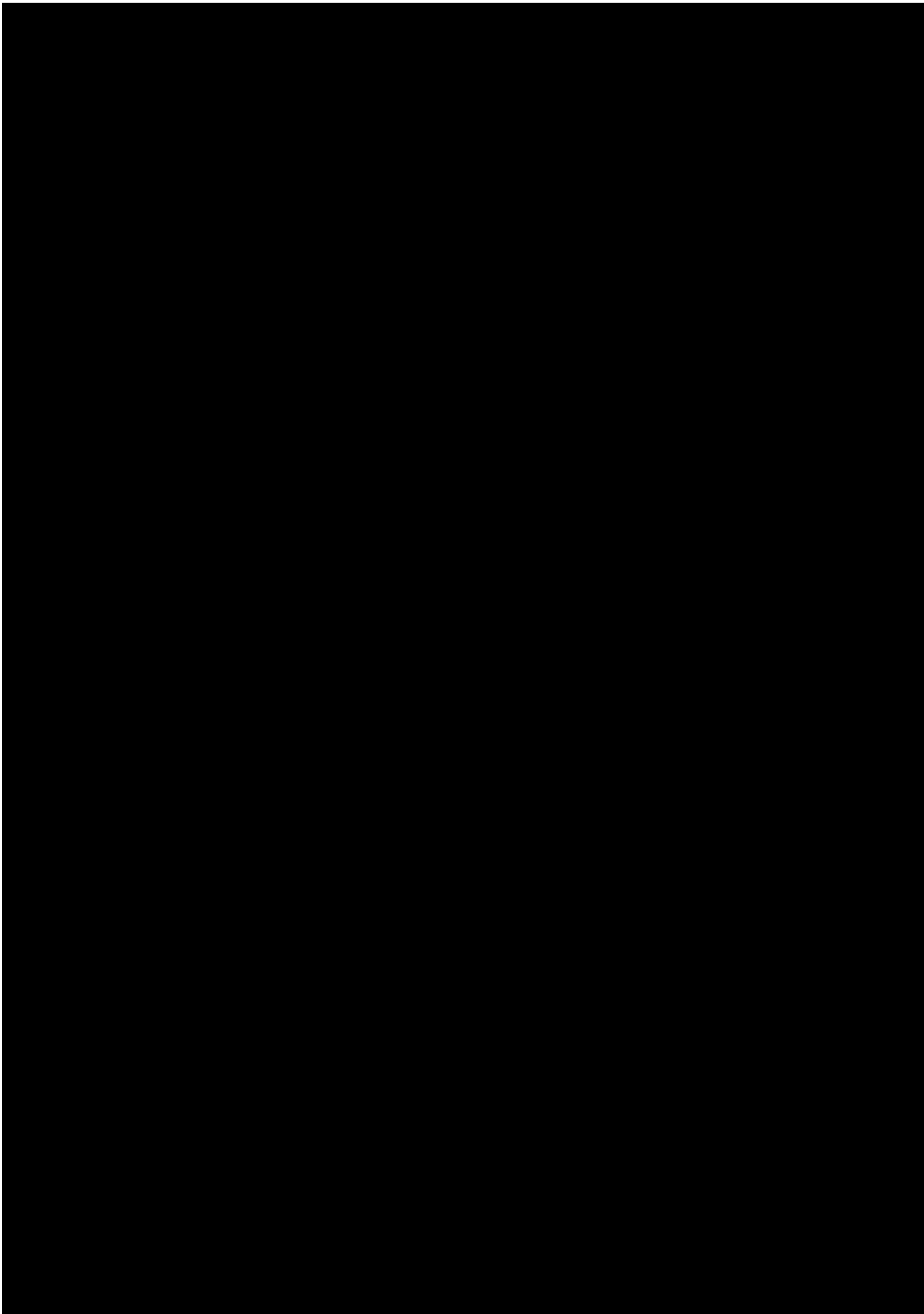


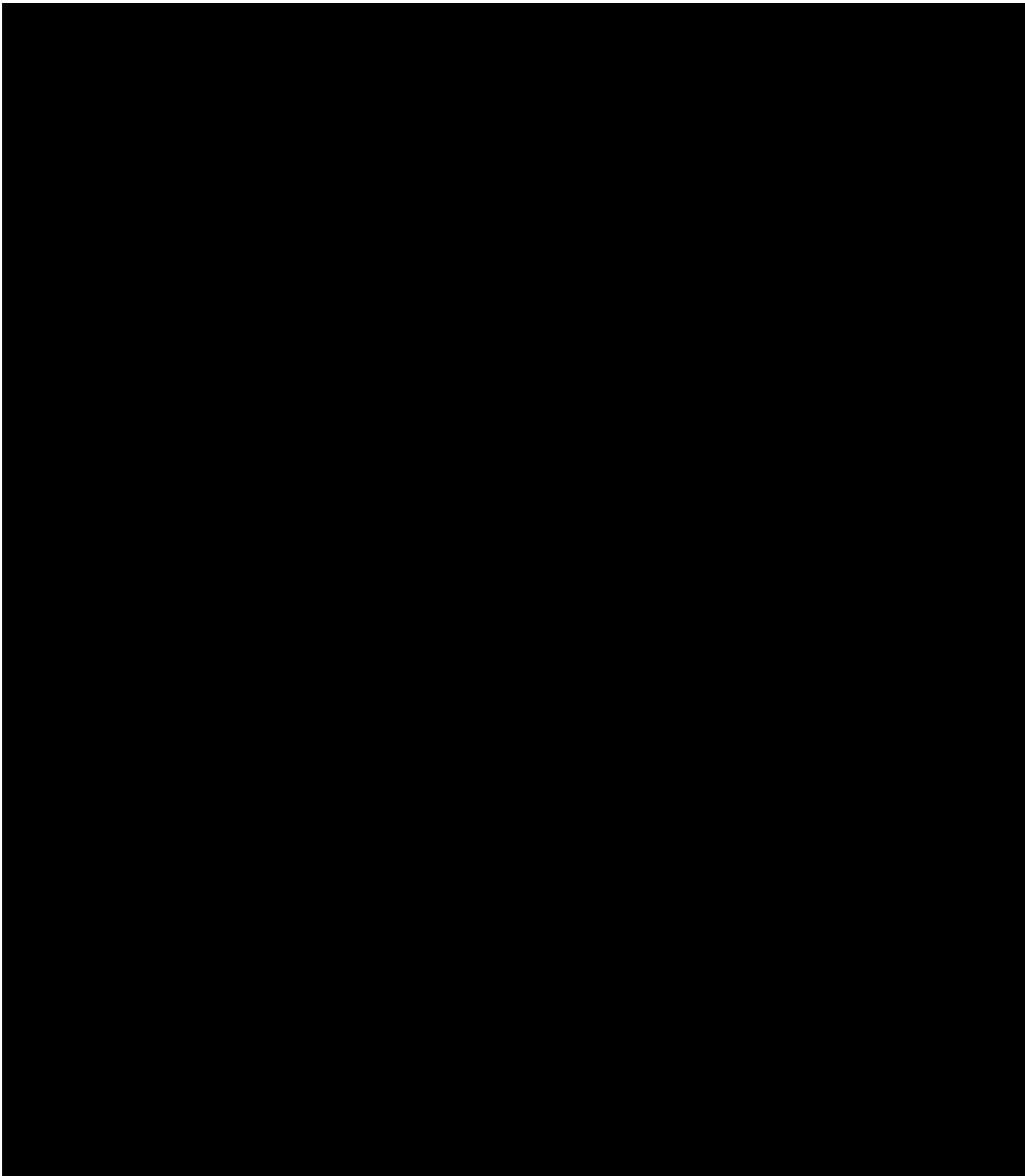
DTCC Attachment 8

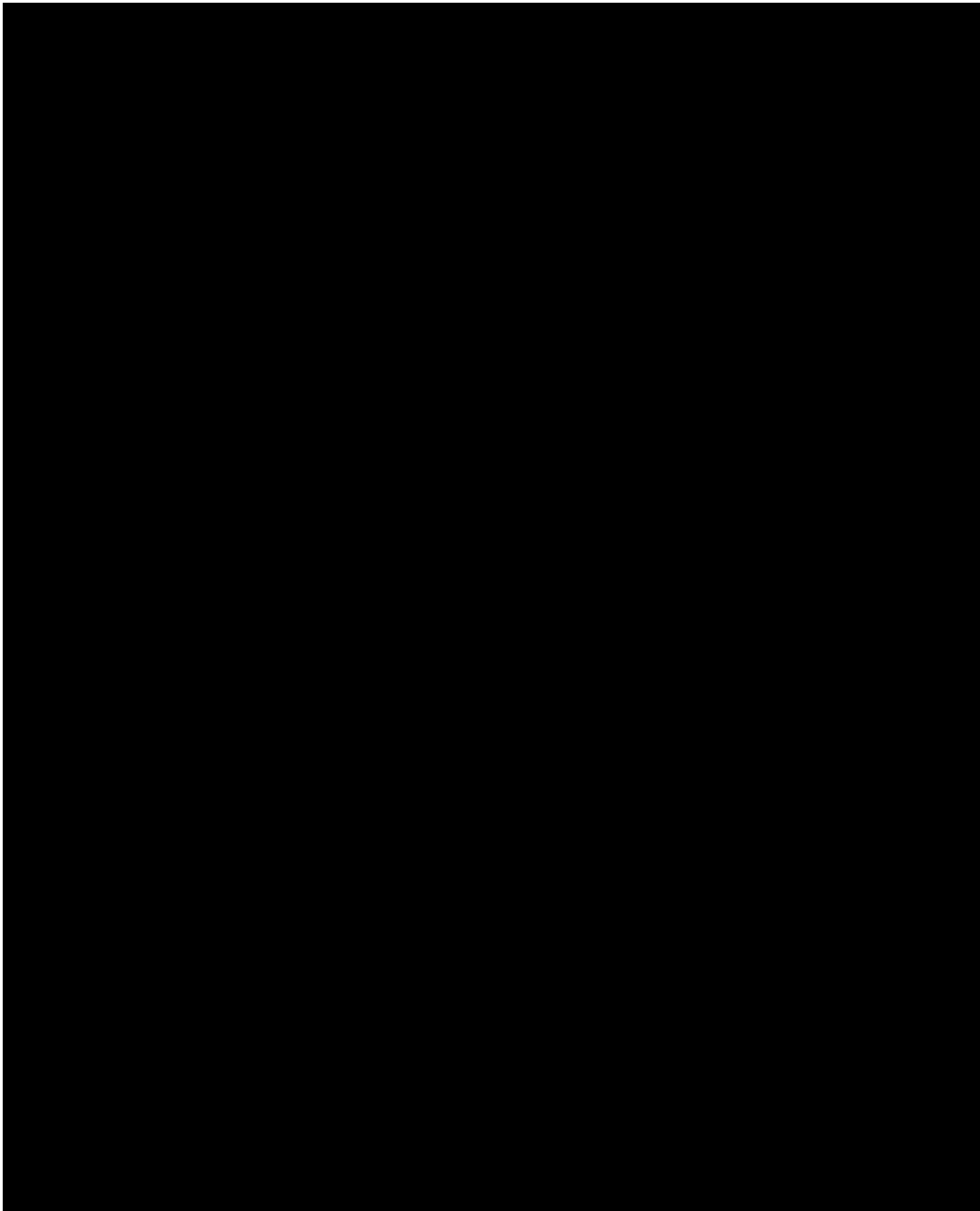


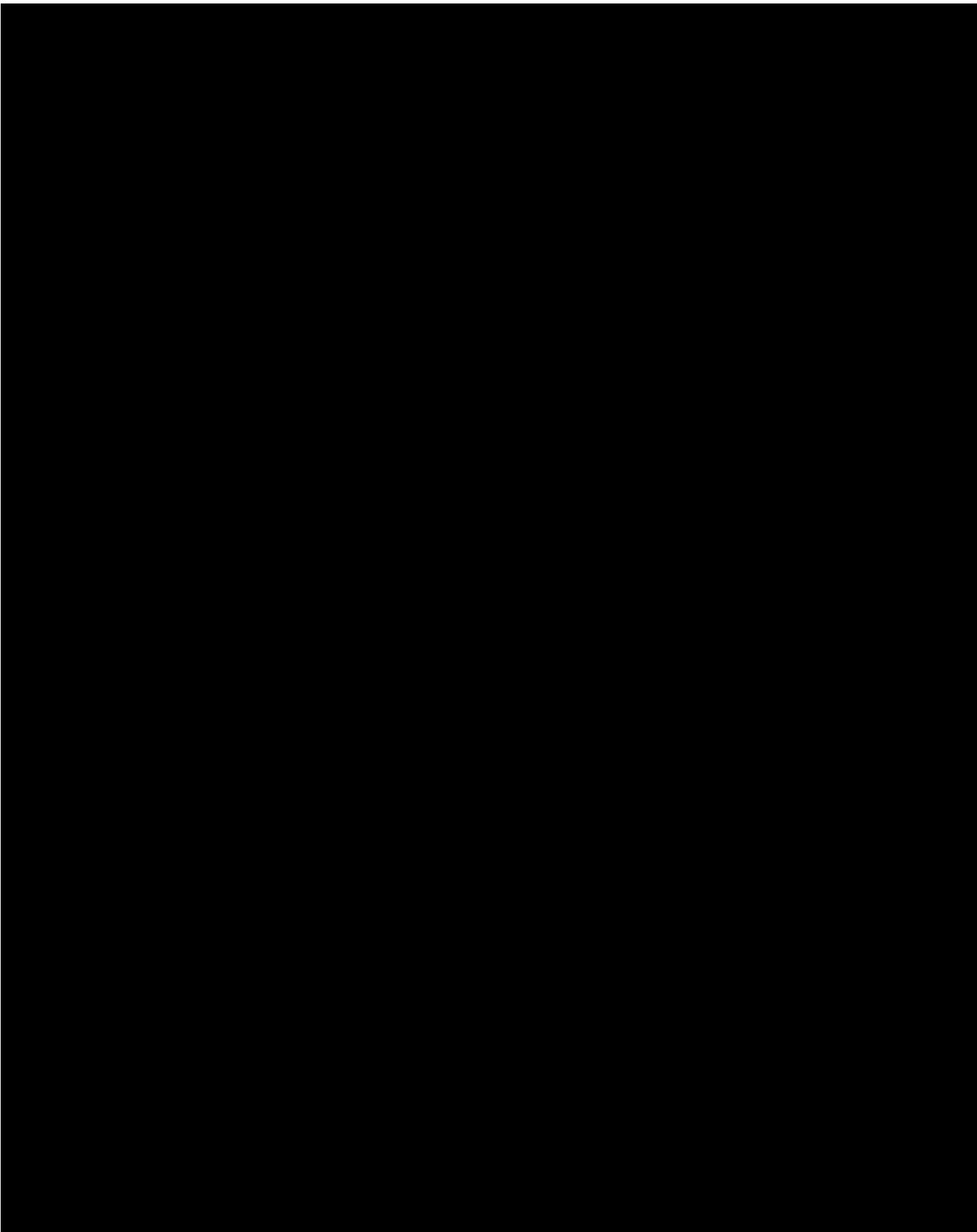


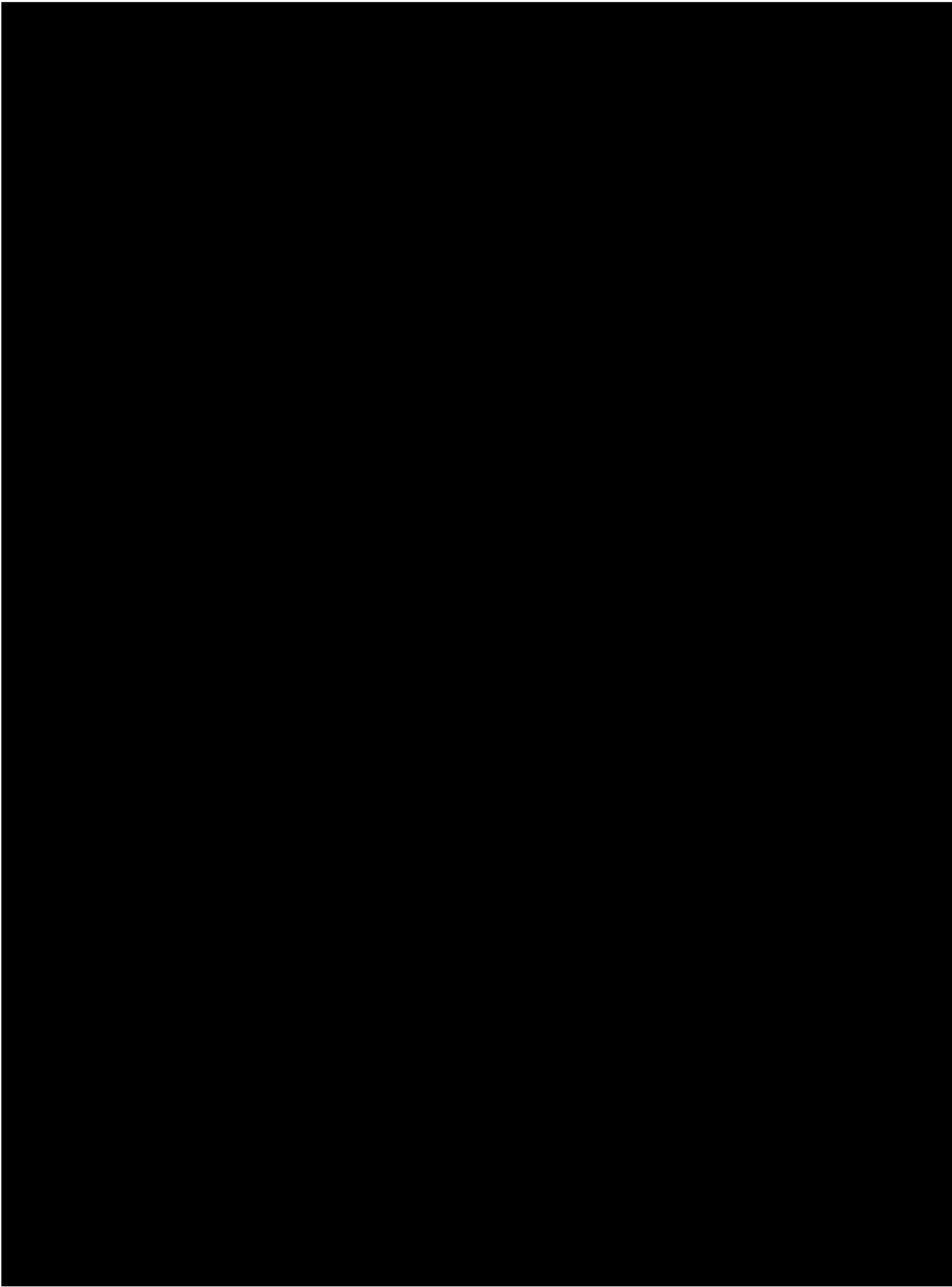


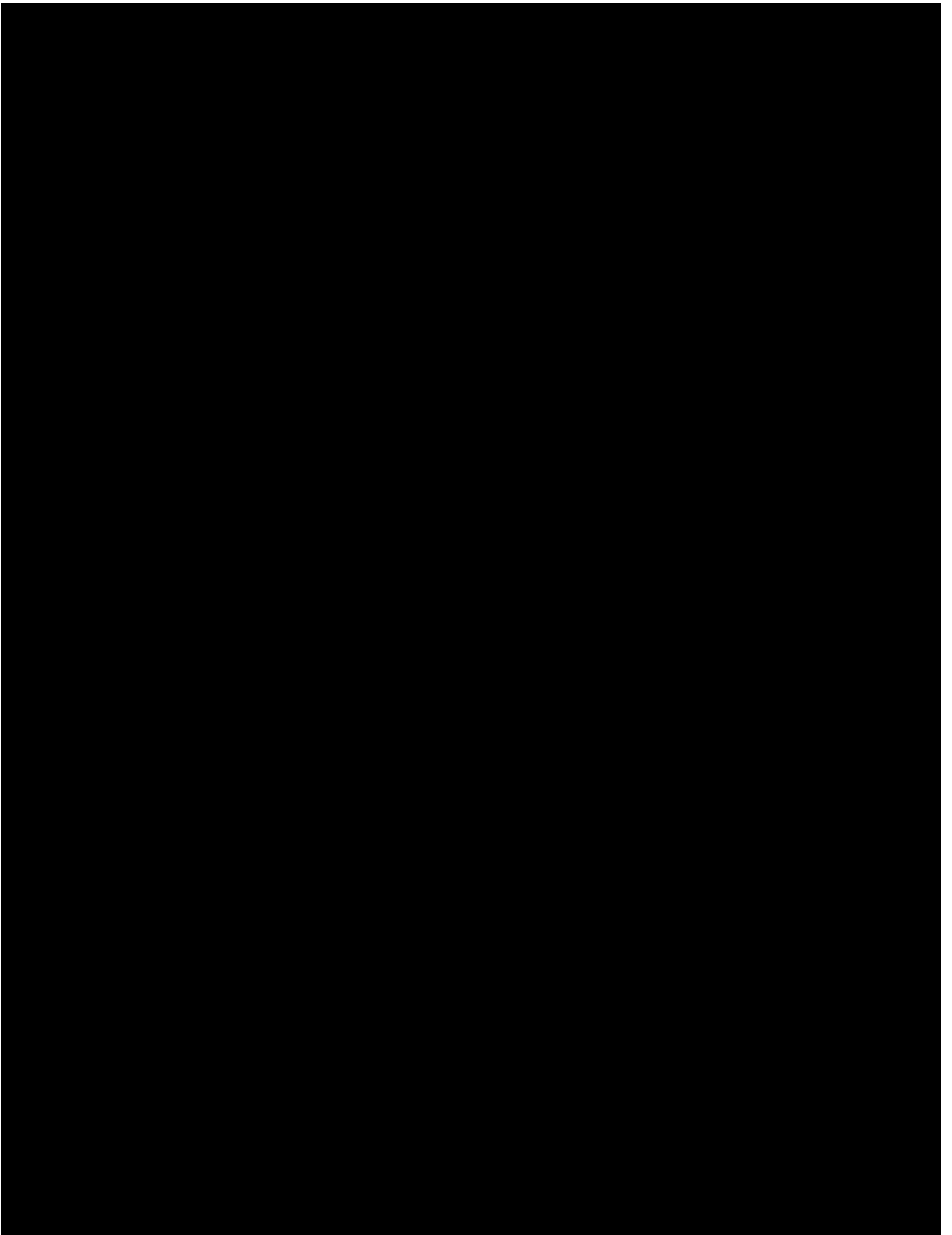






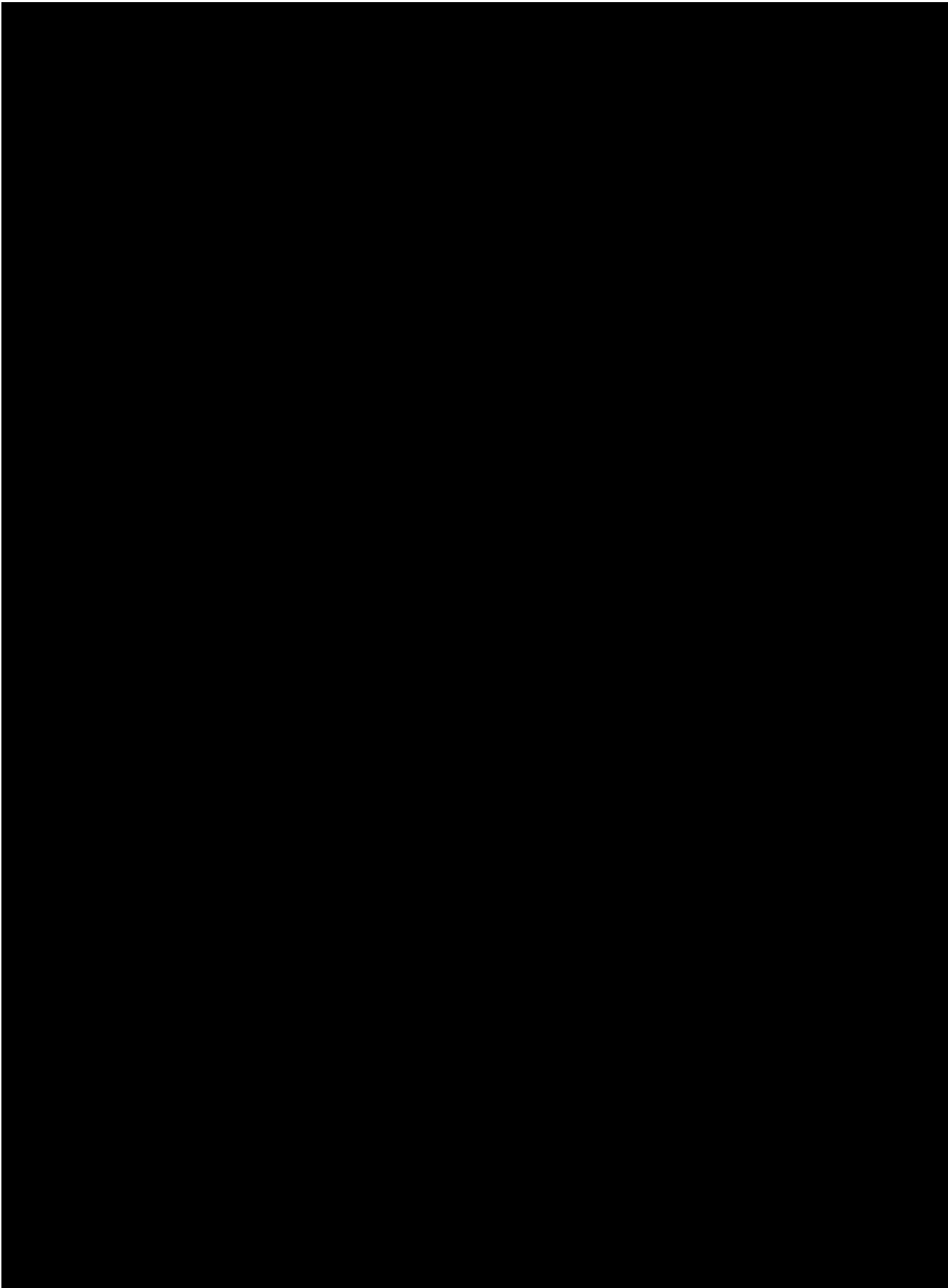


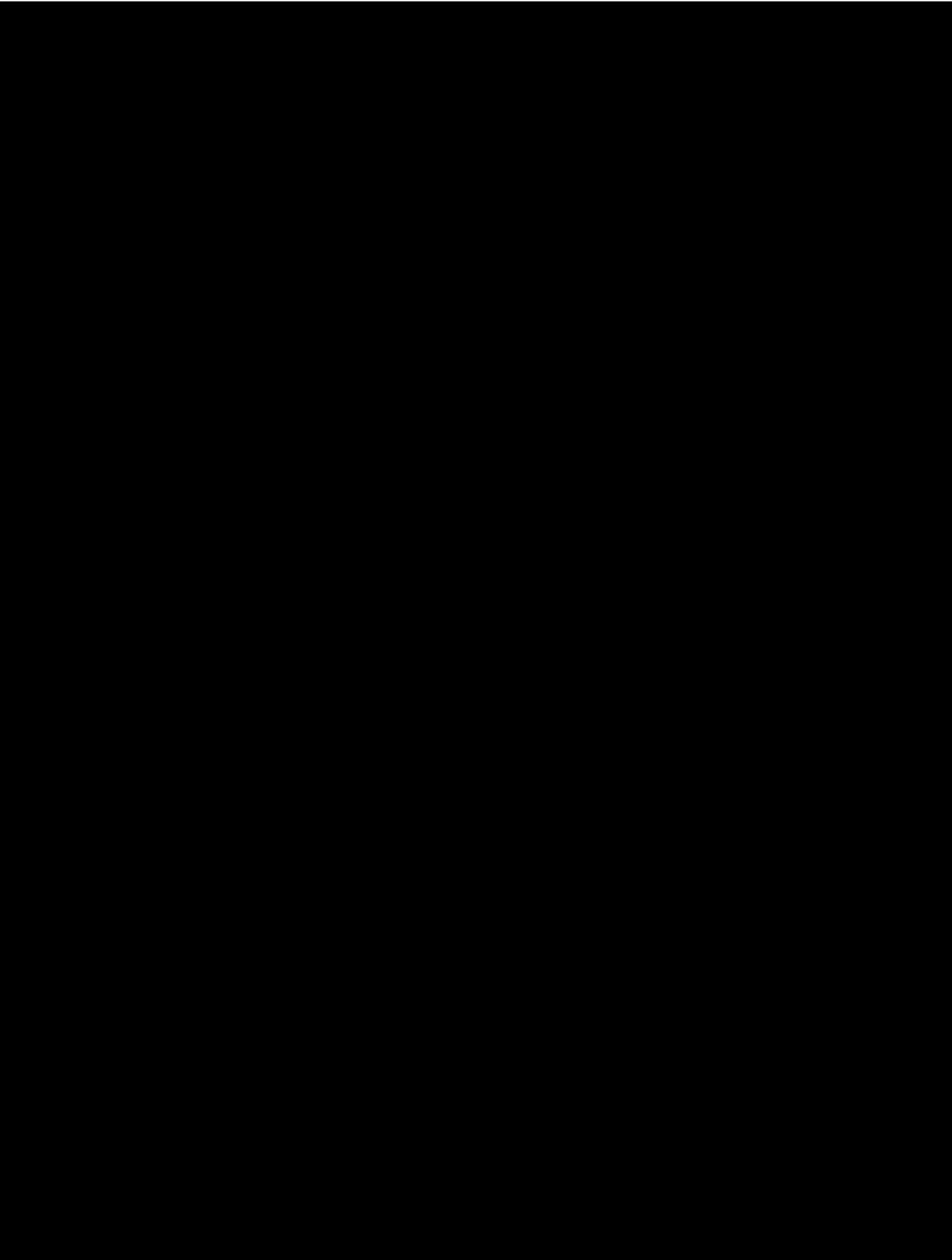


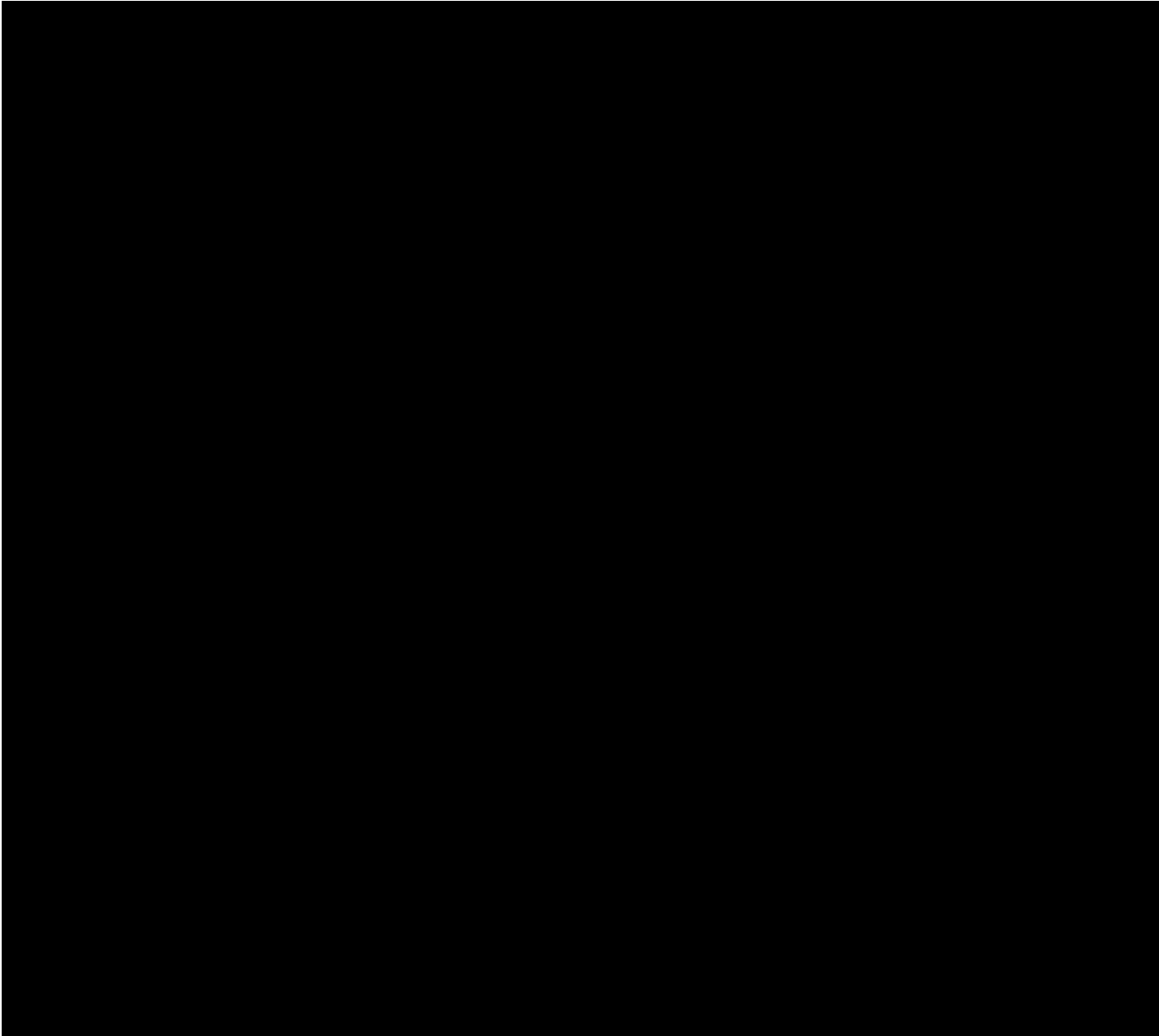


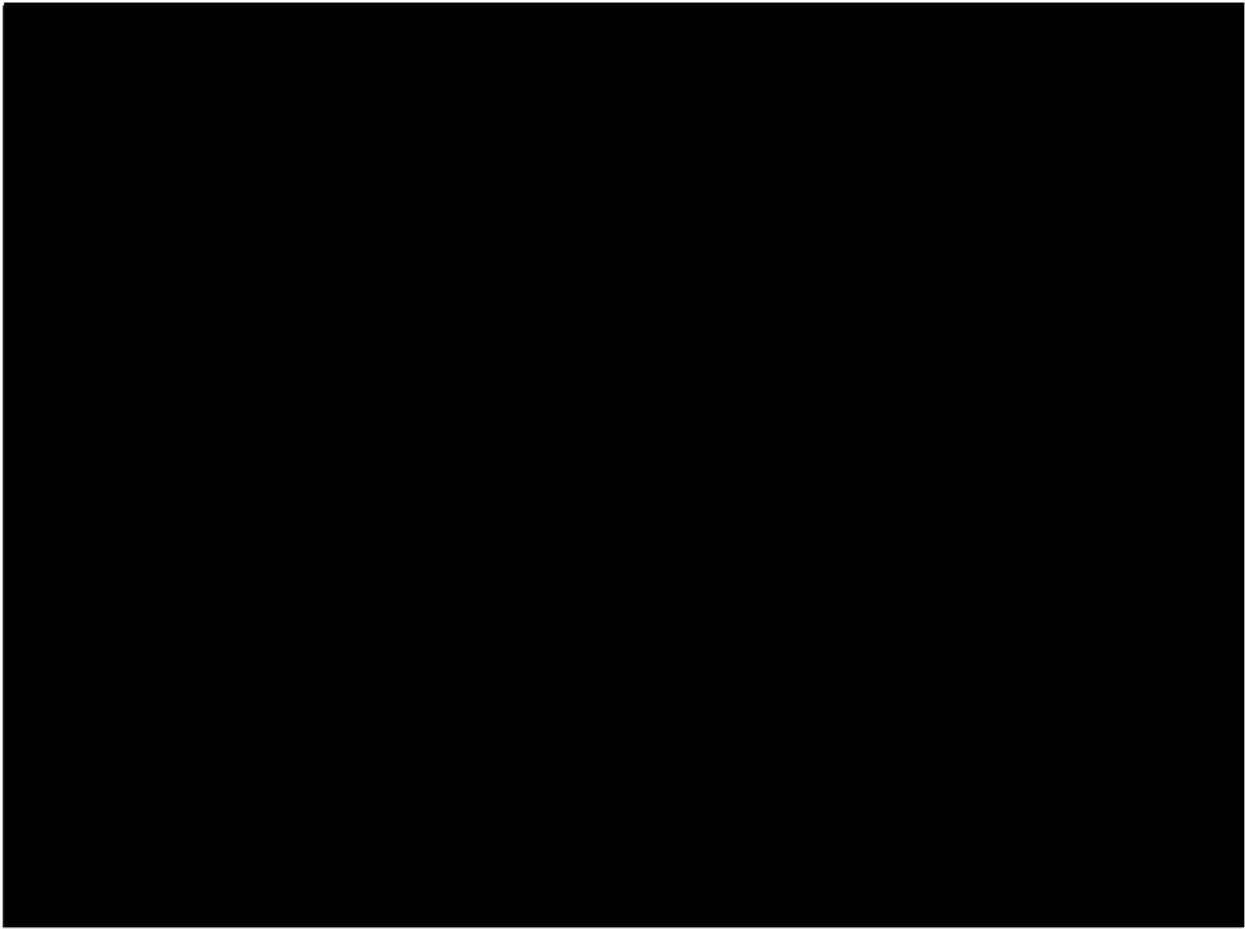
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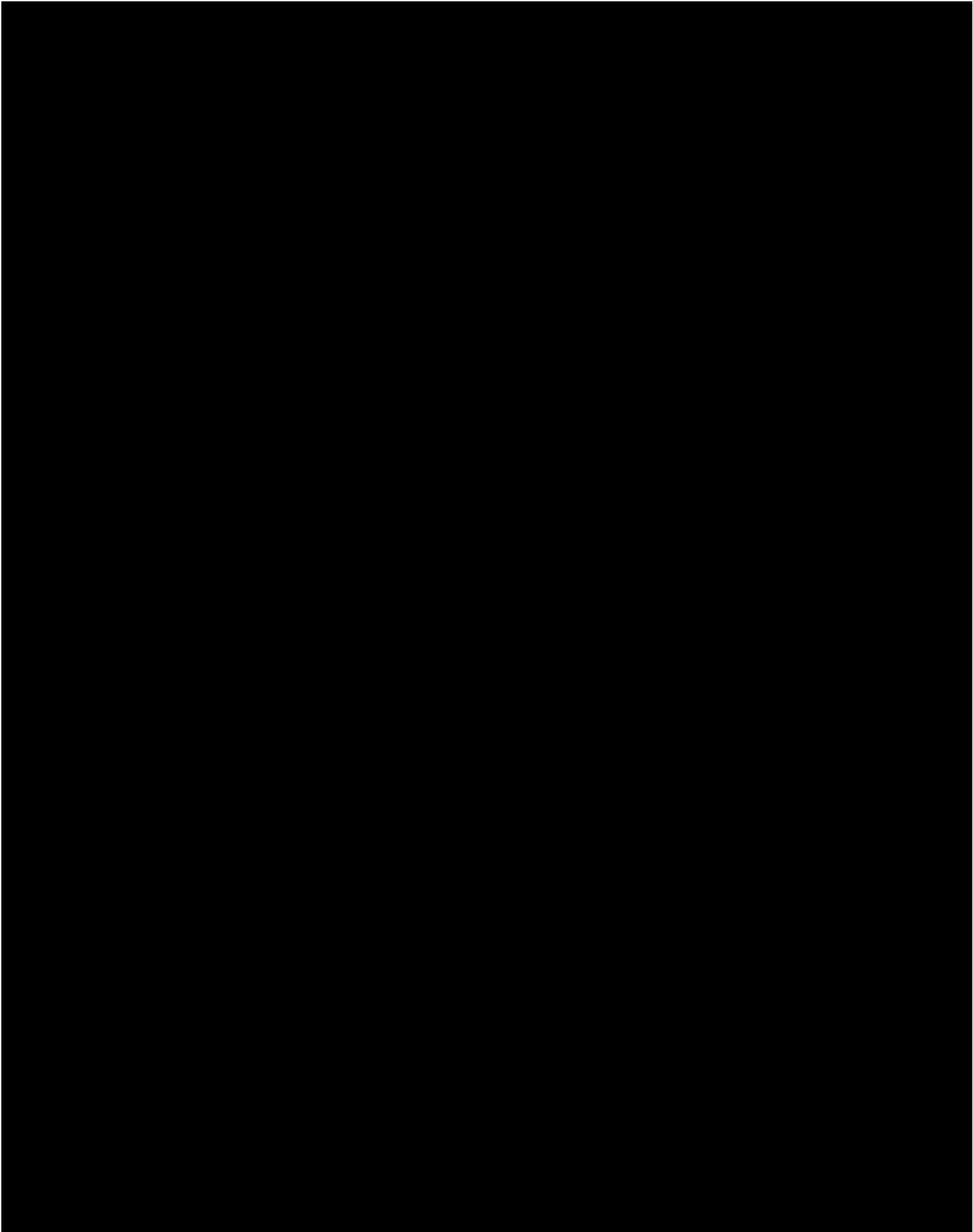






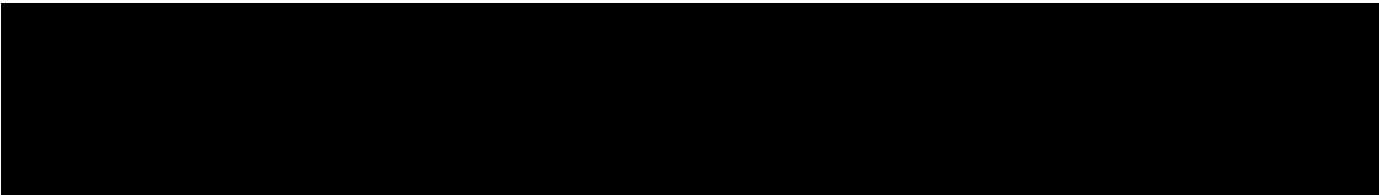
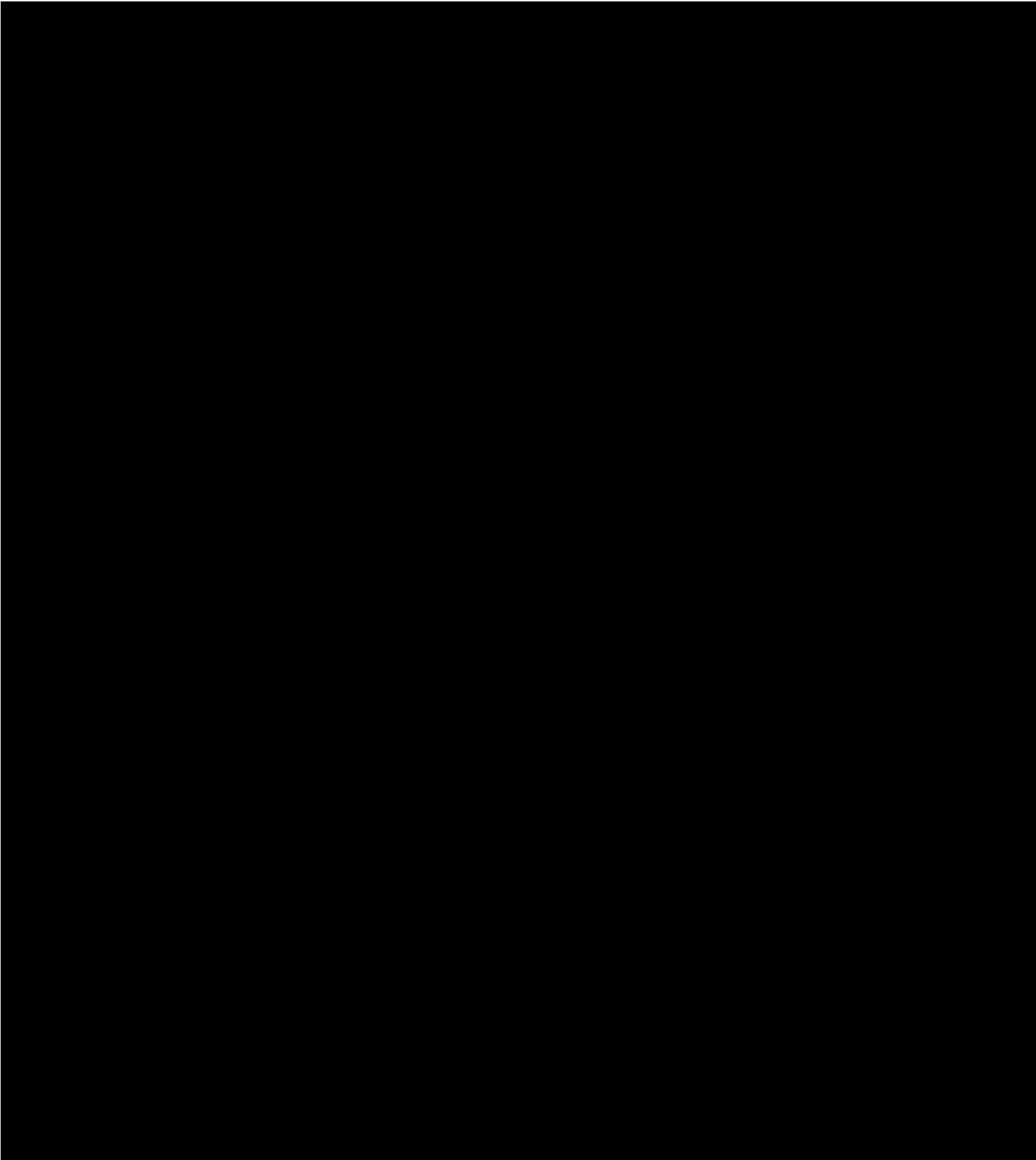


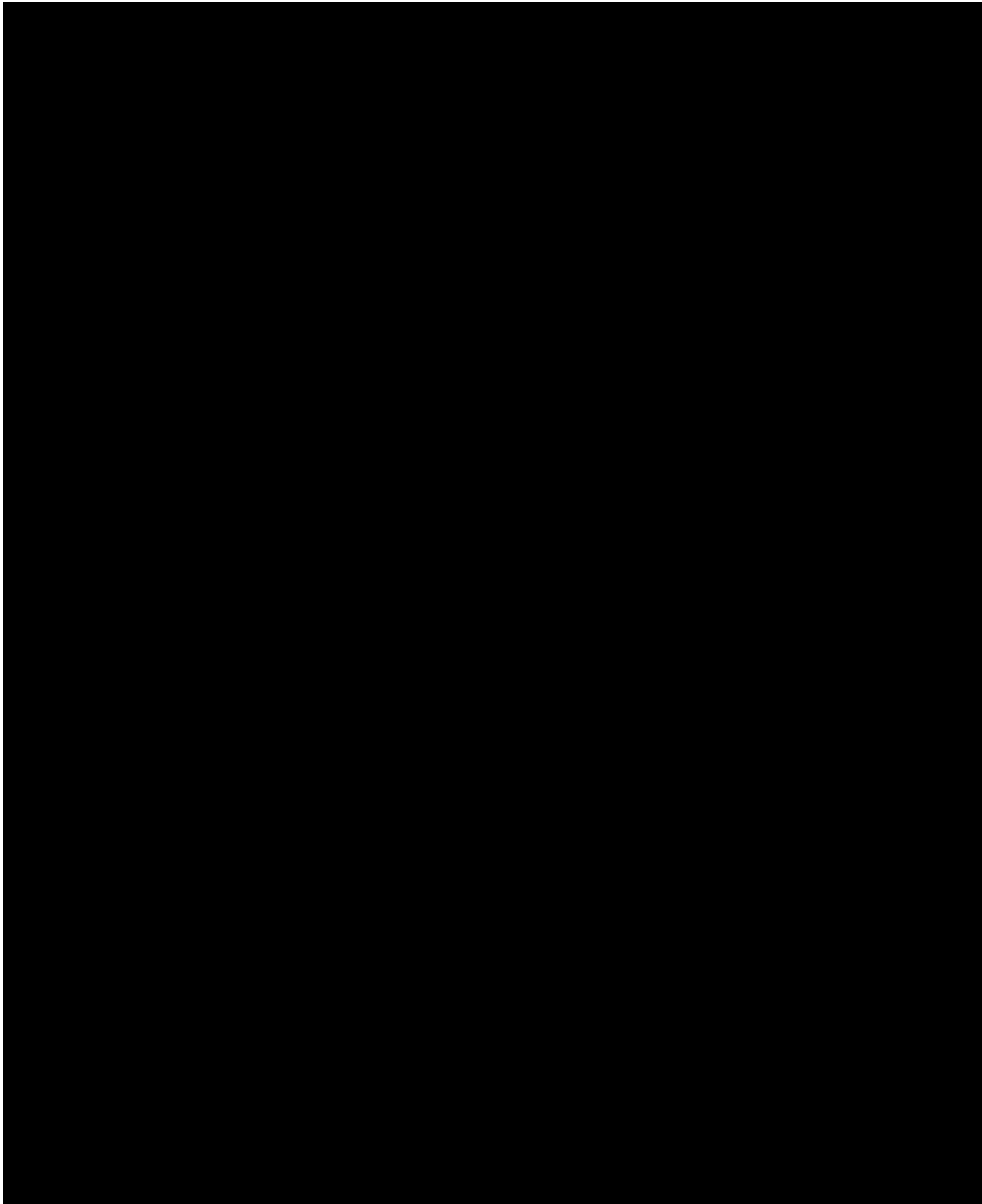
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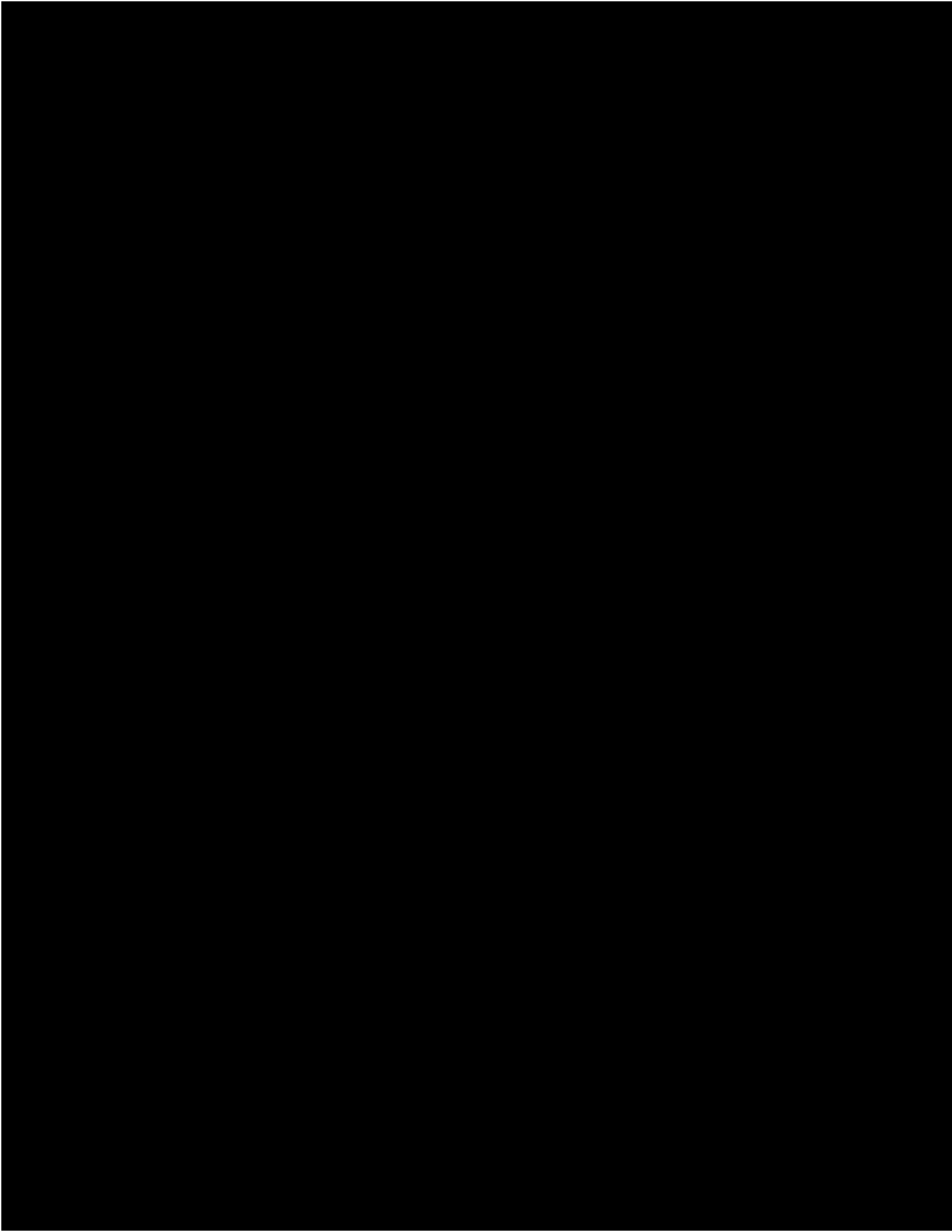


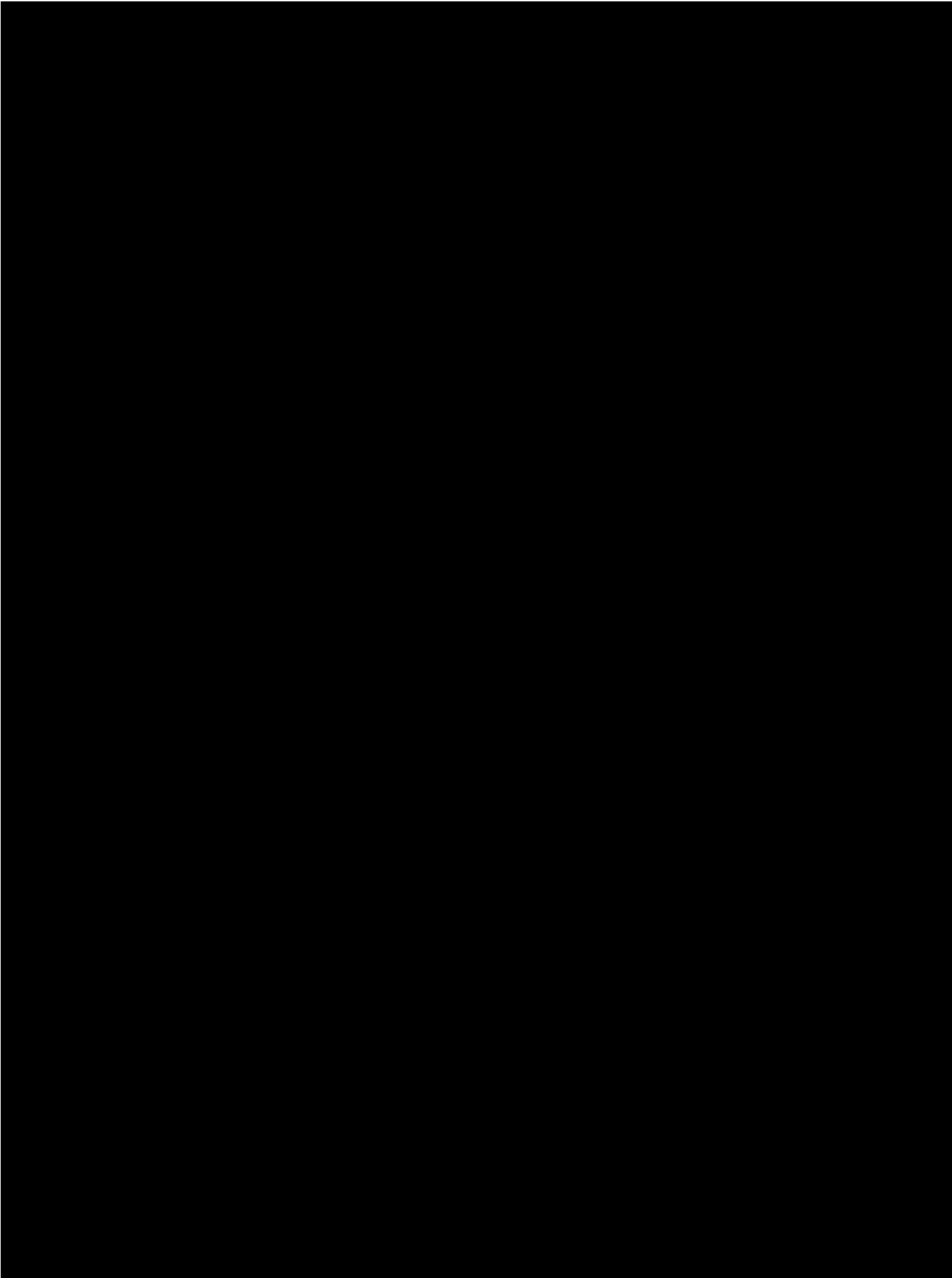
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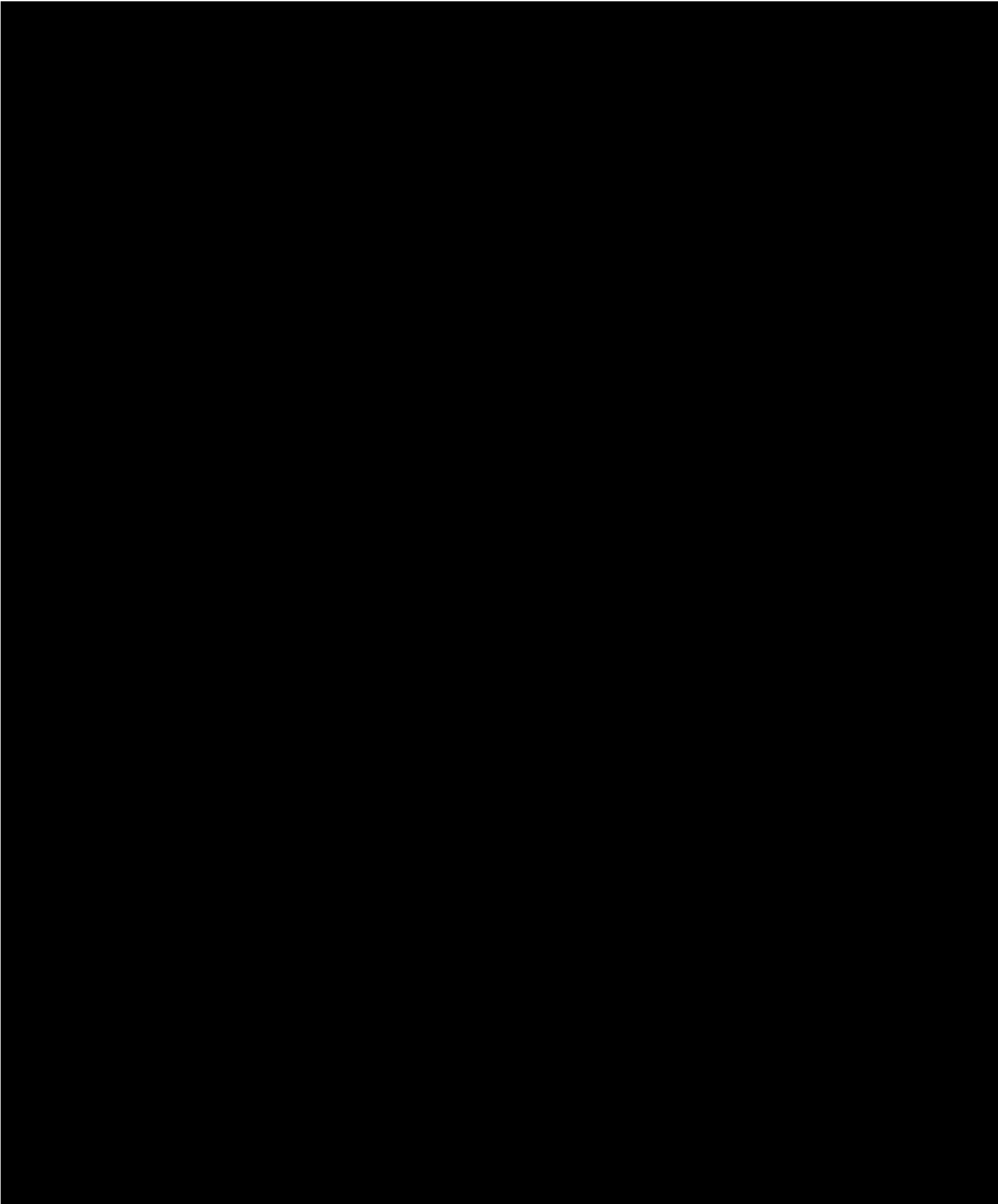
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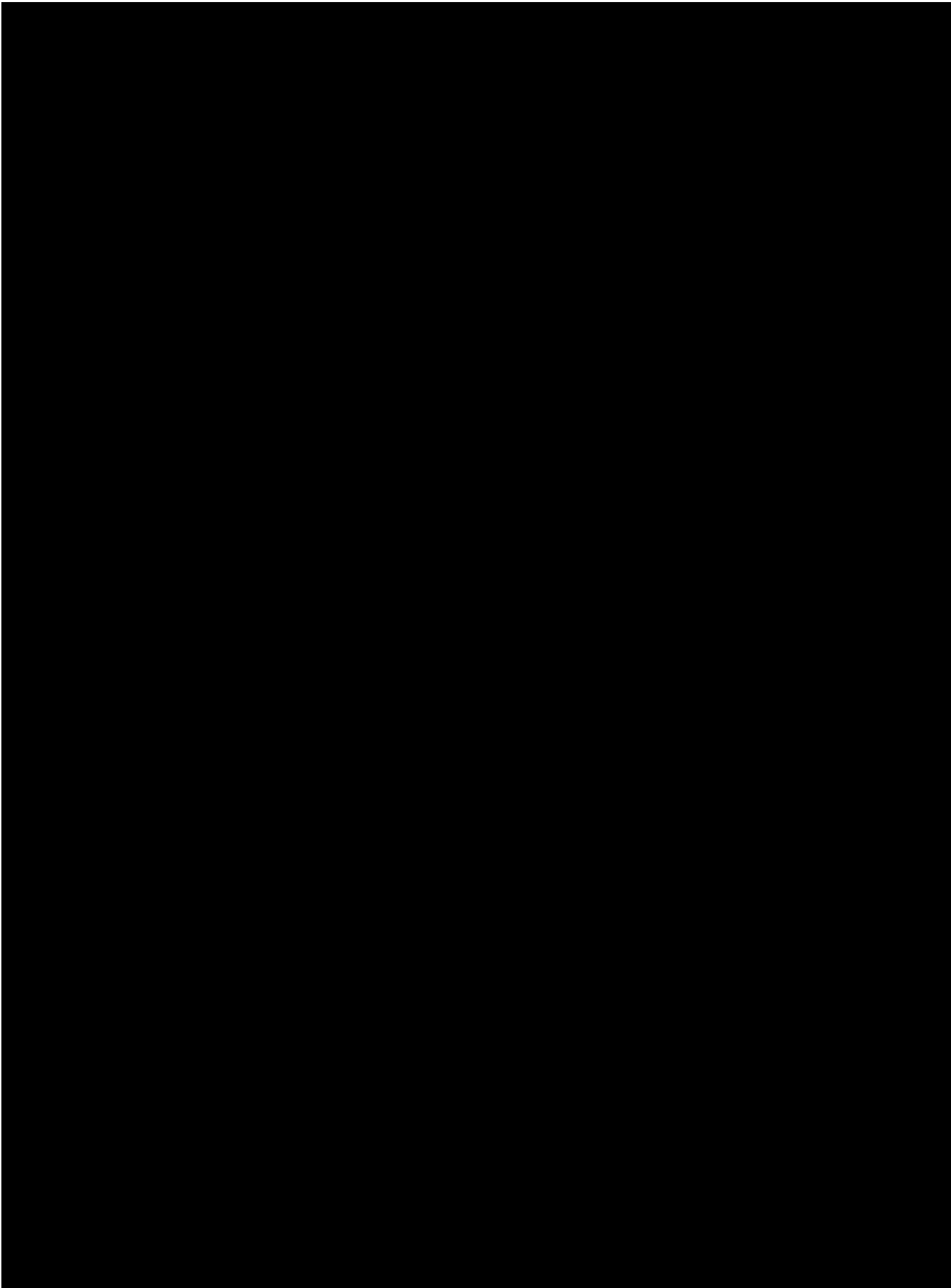


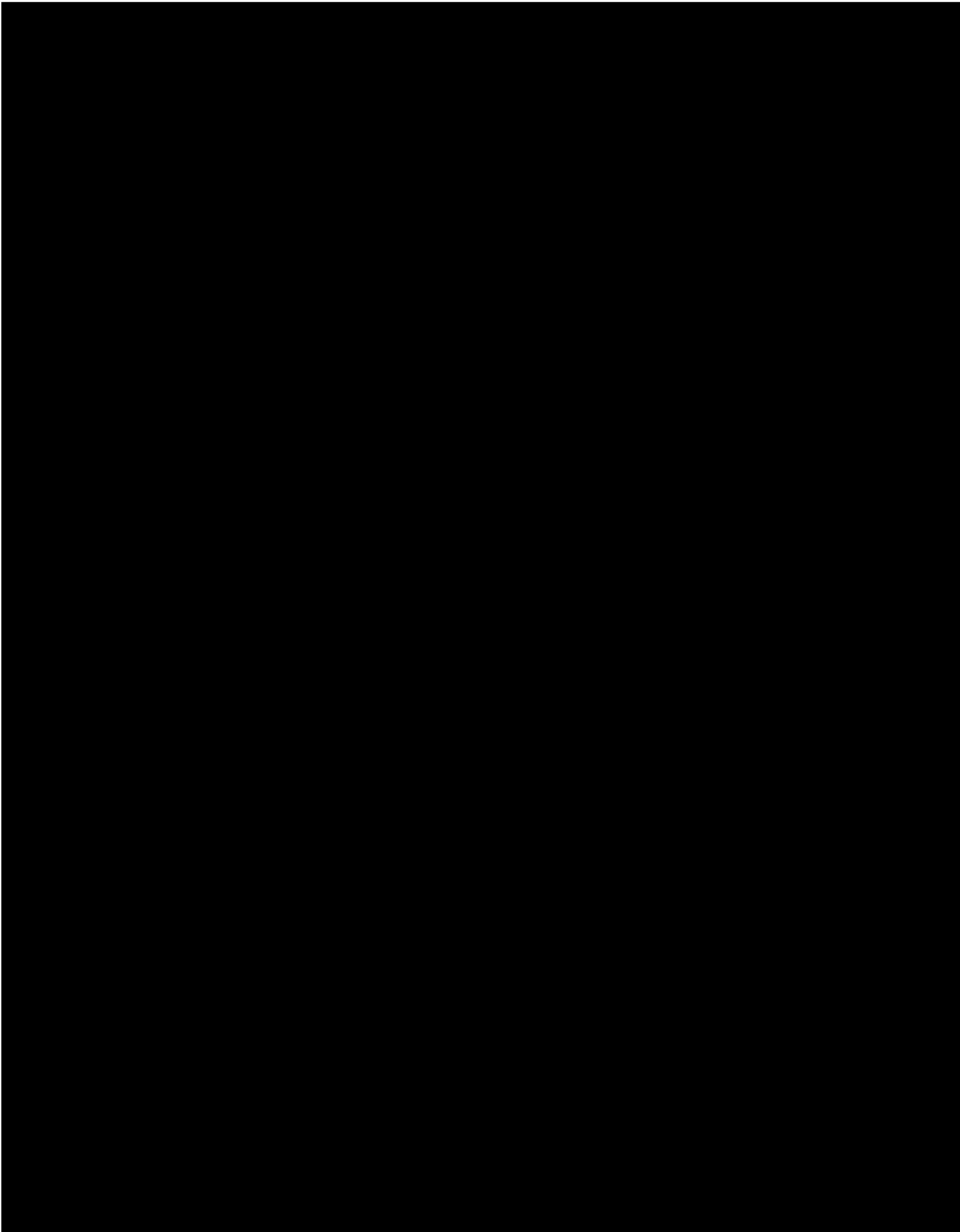


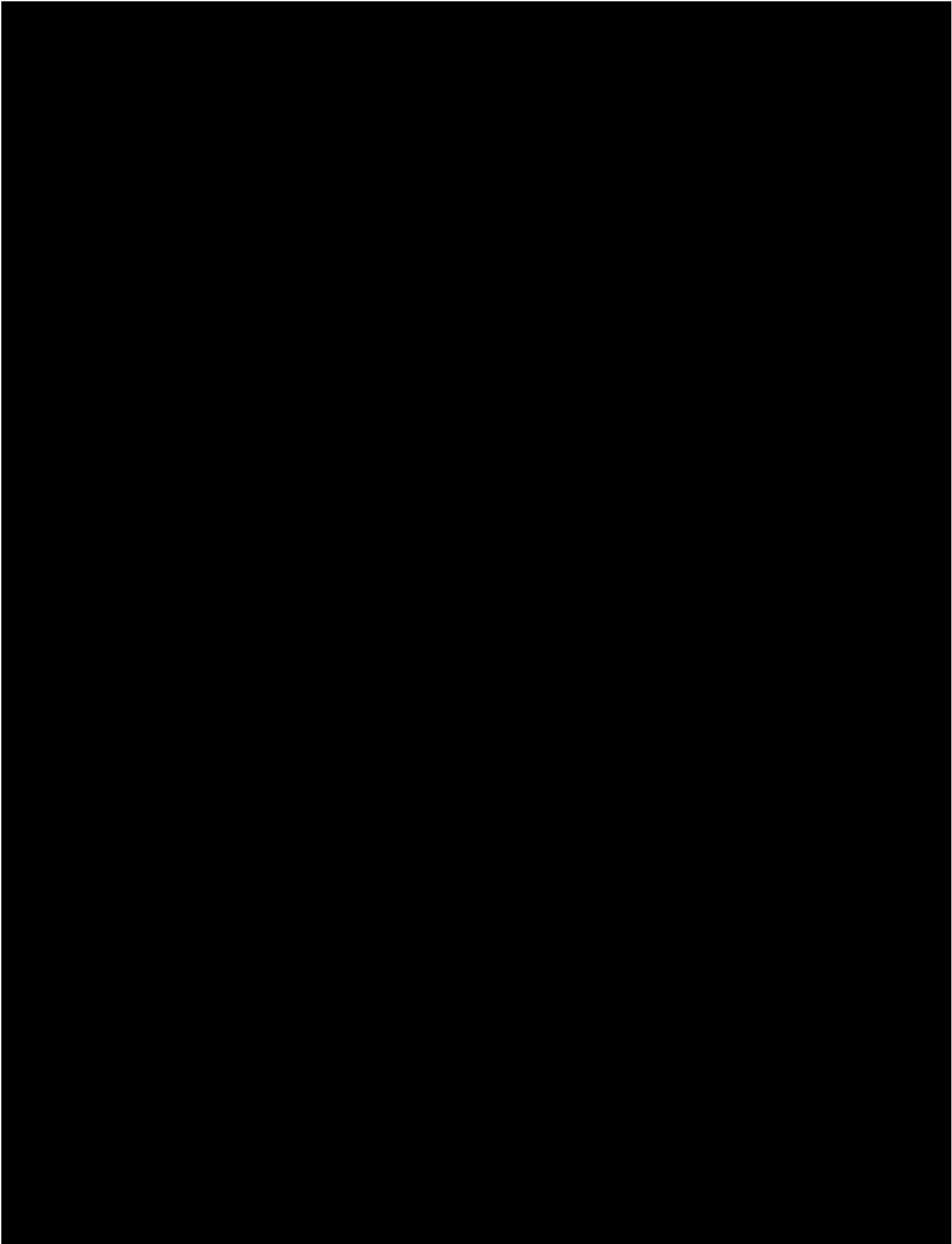


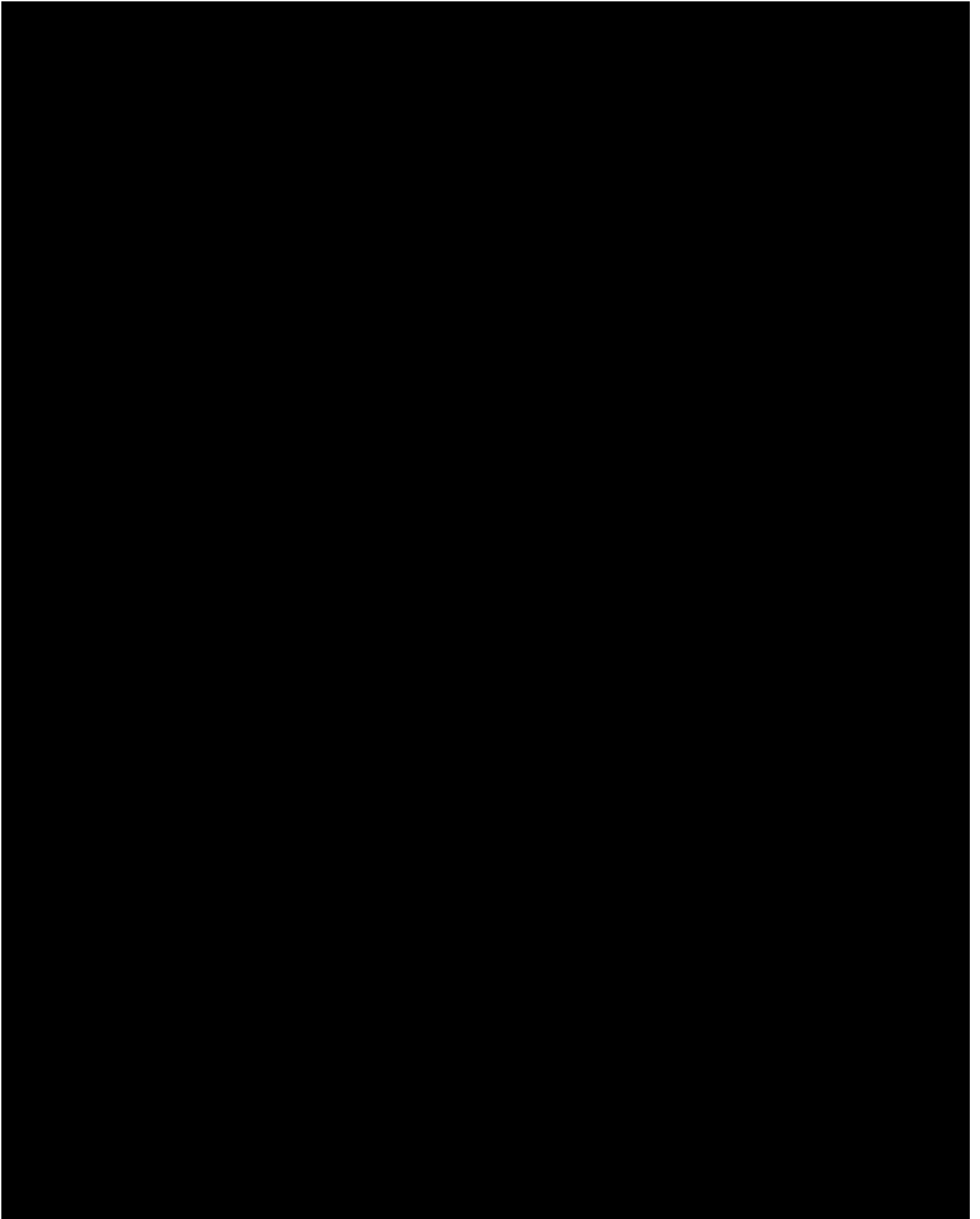


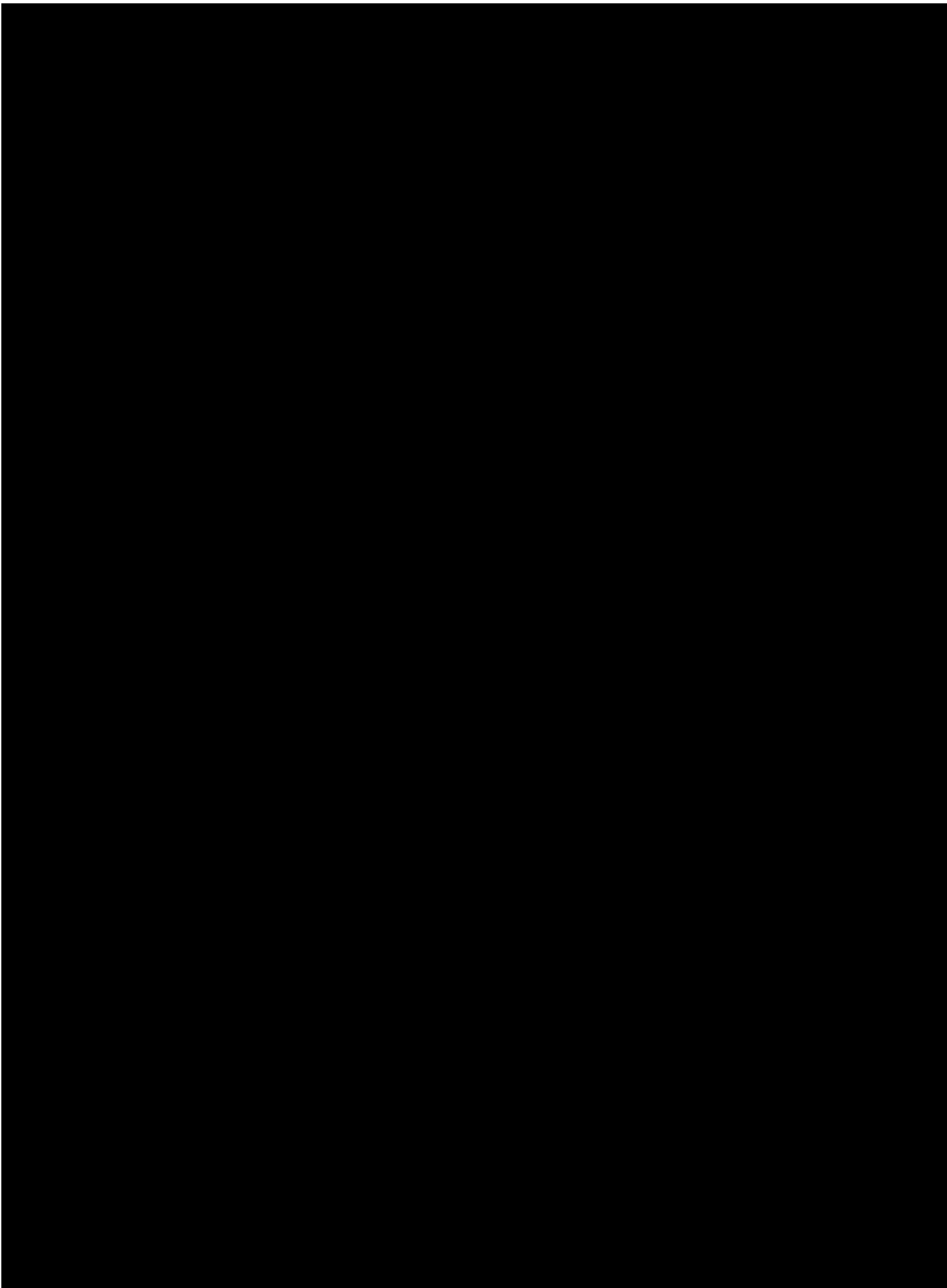


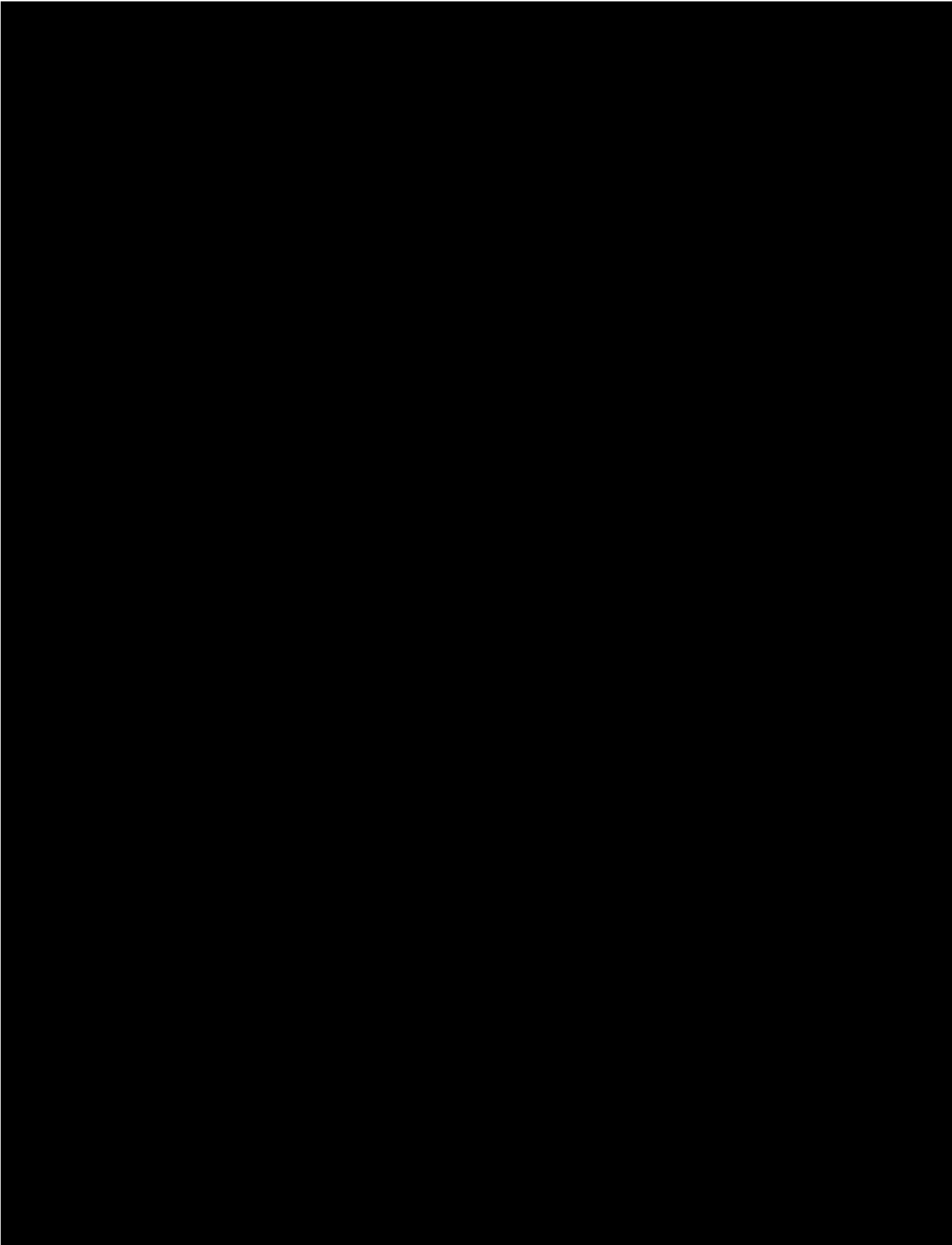


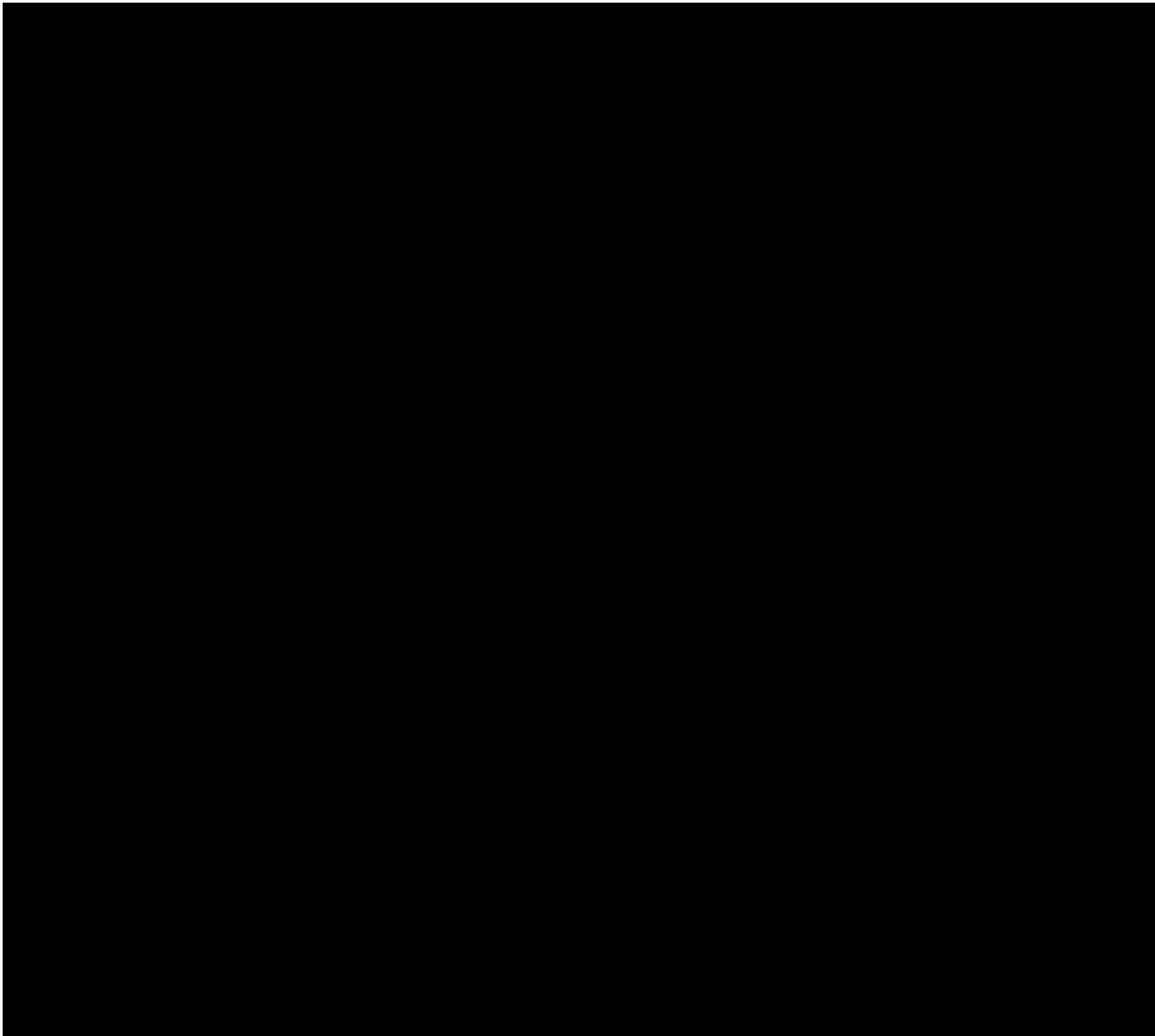


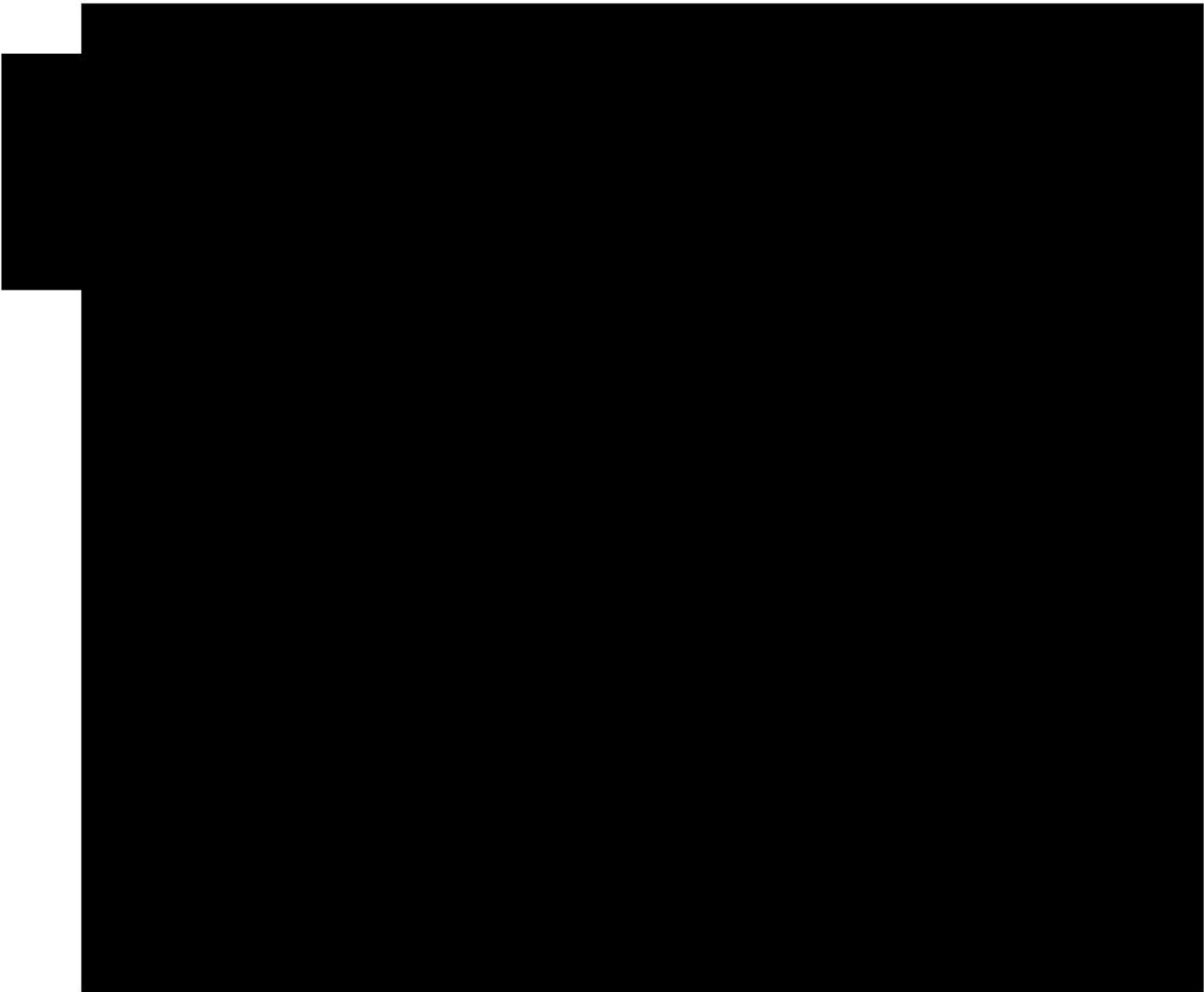


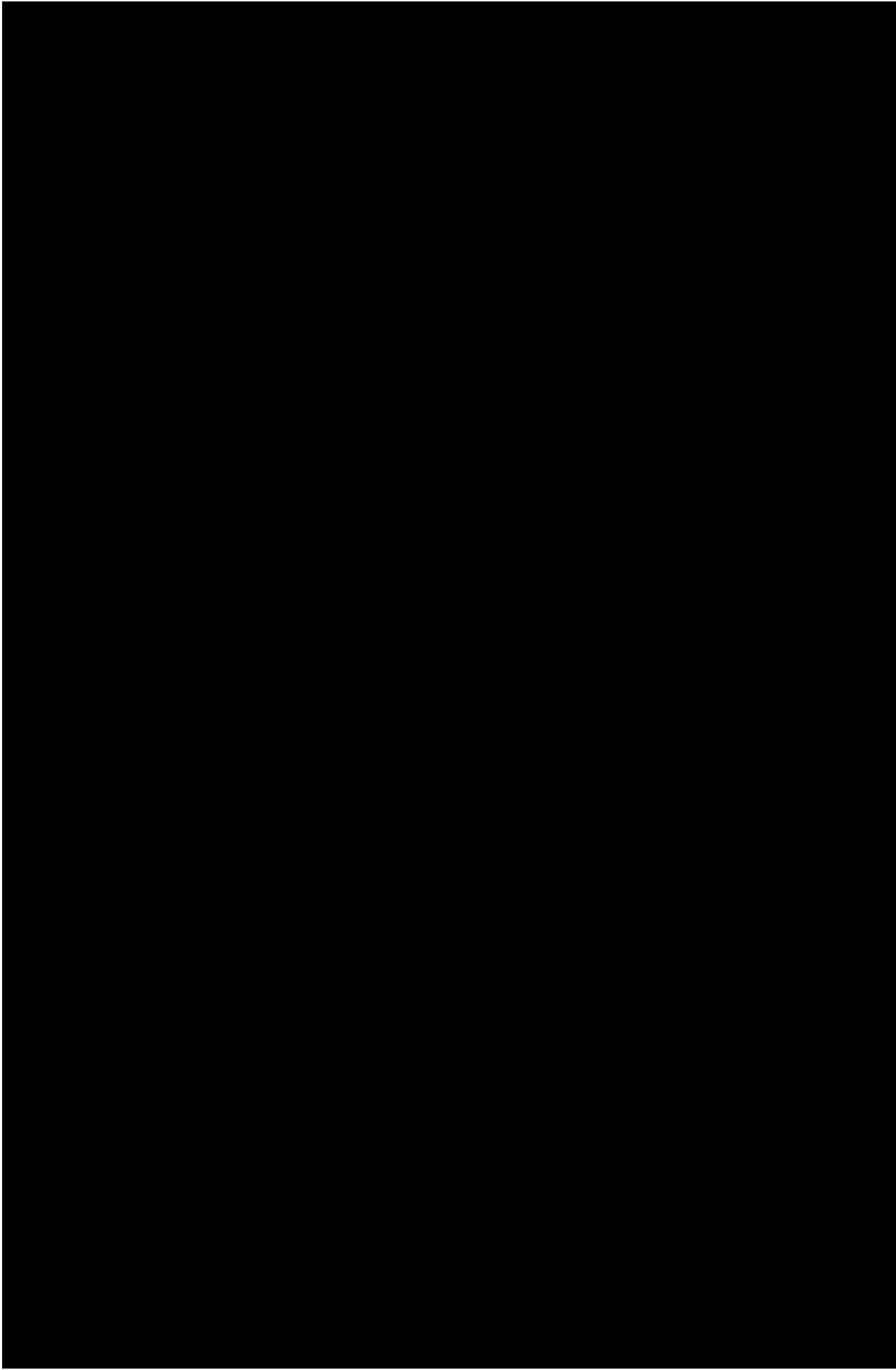


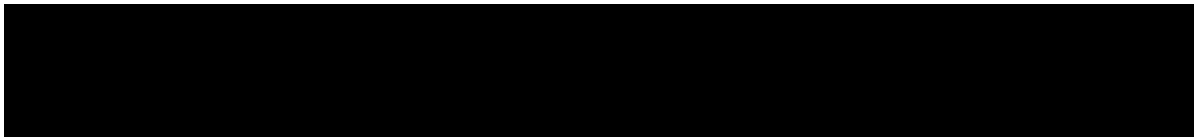
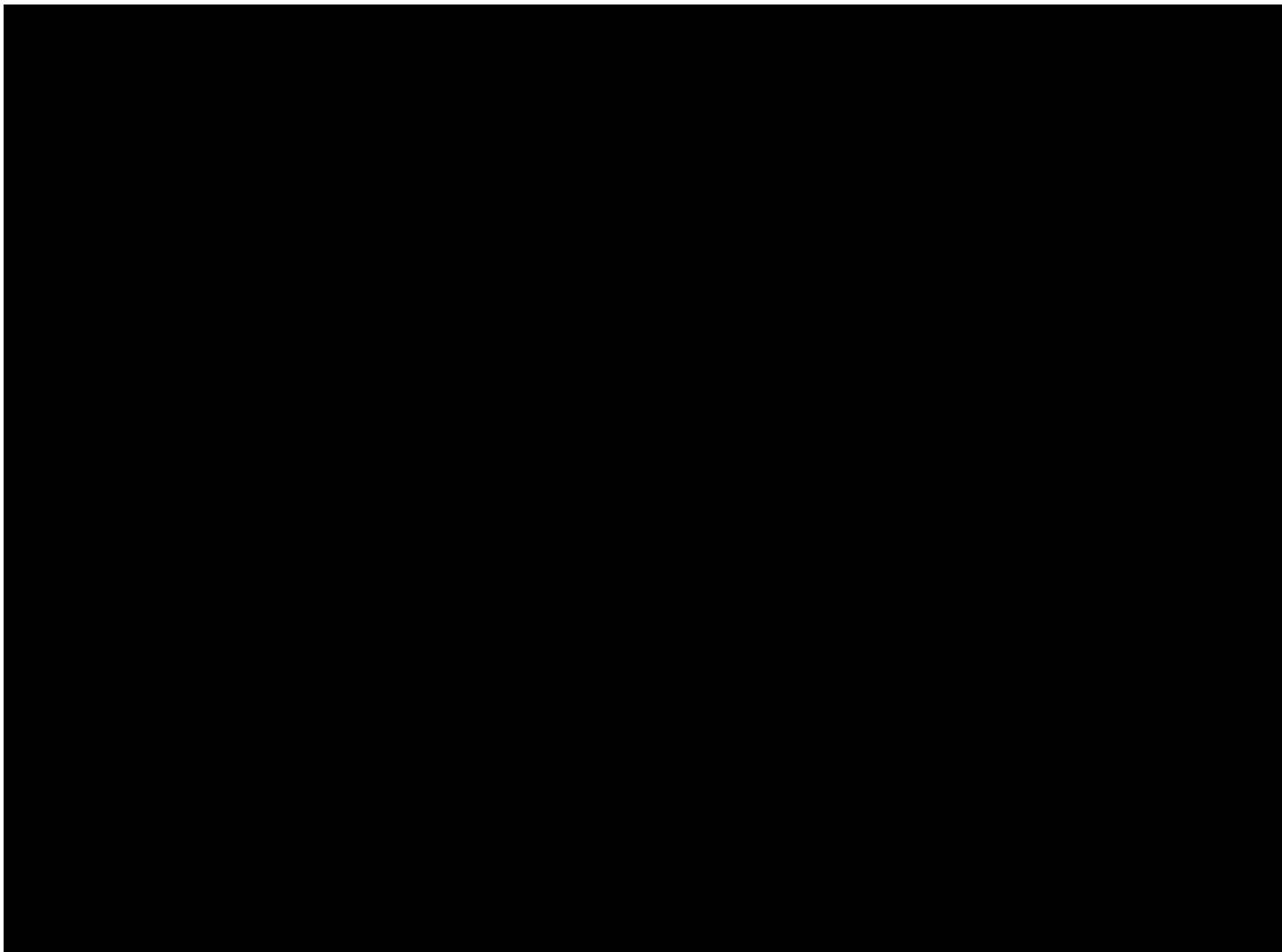


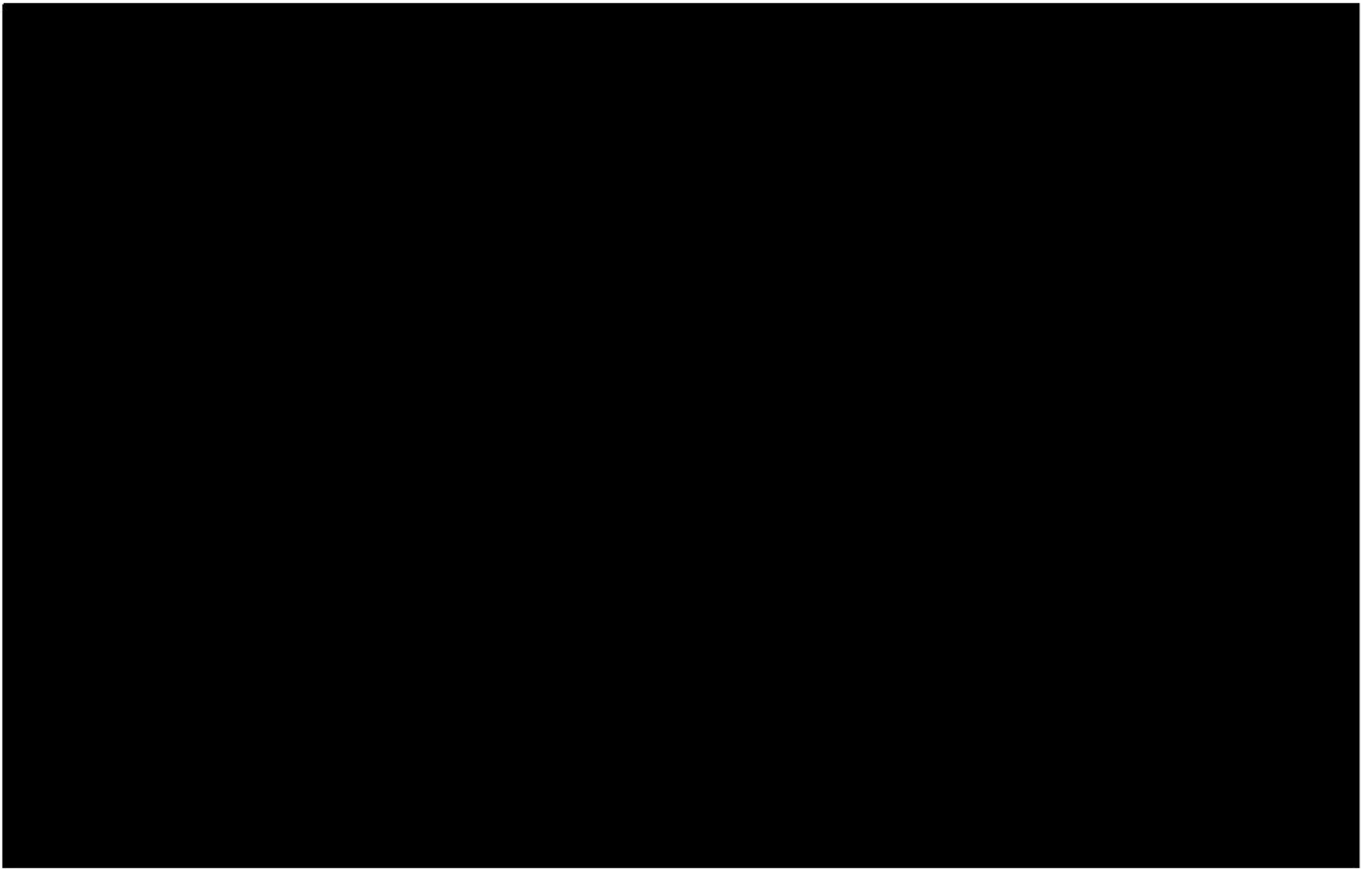




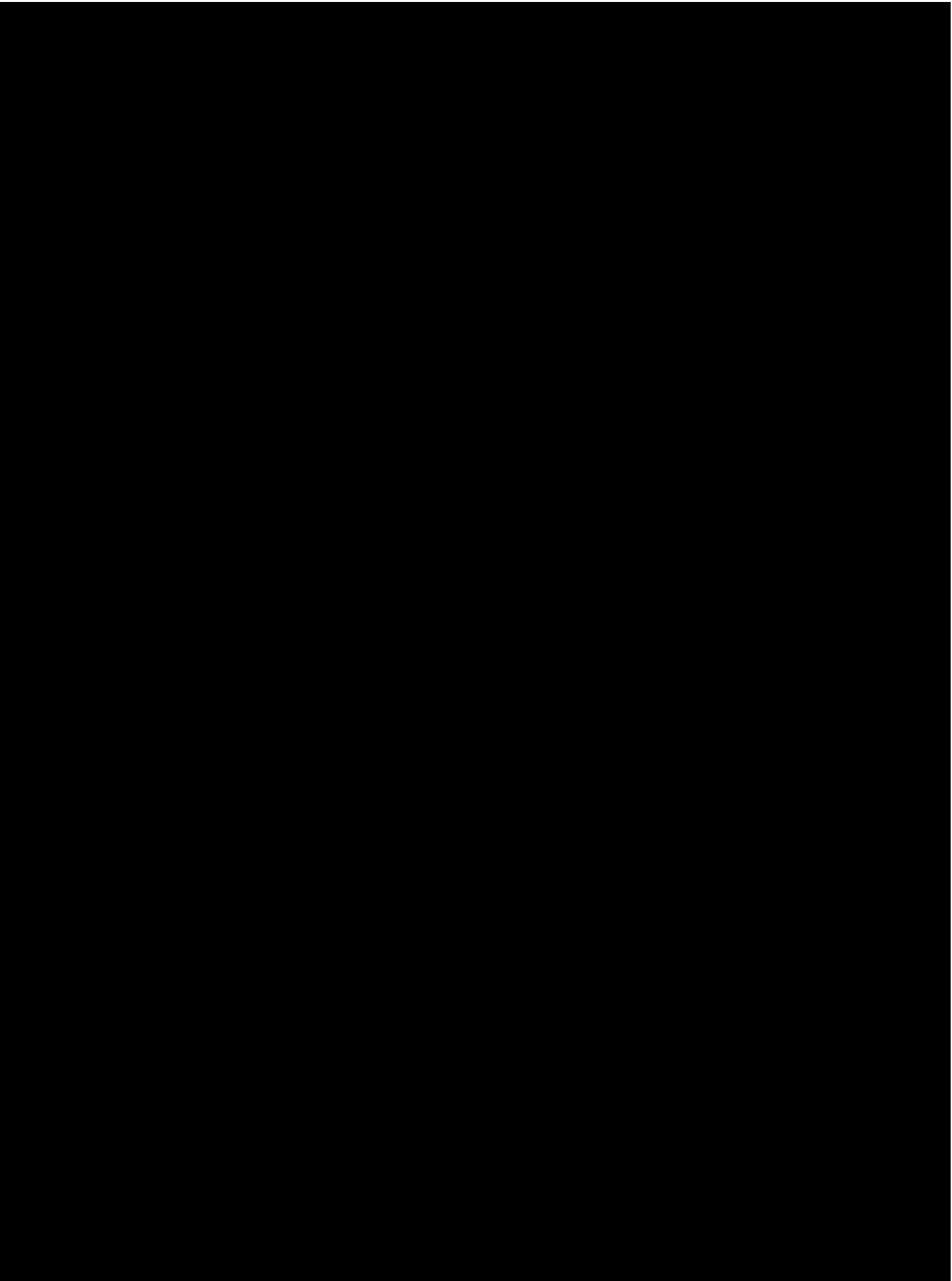


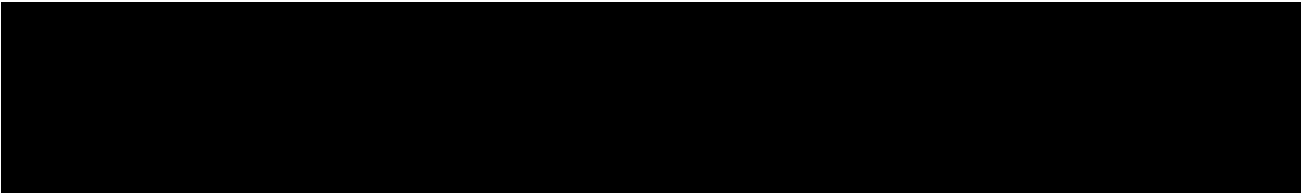
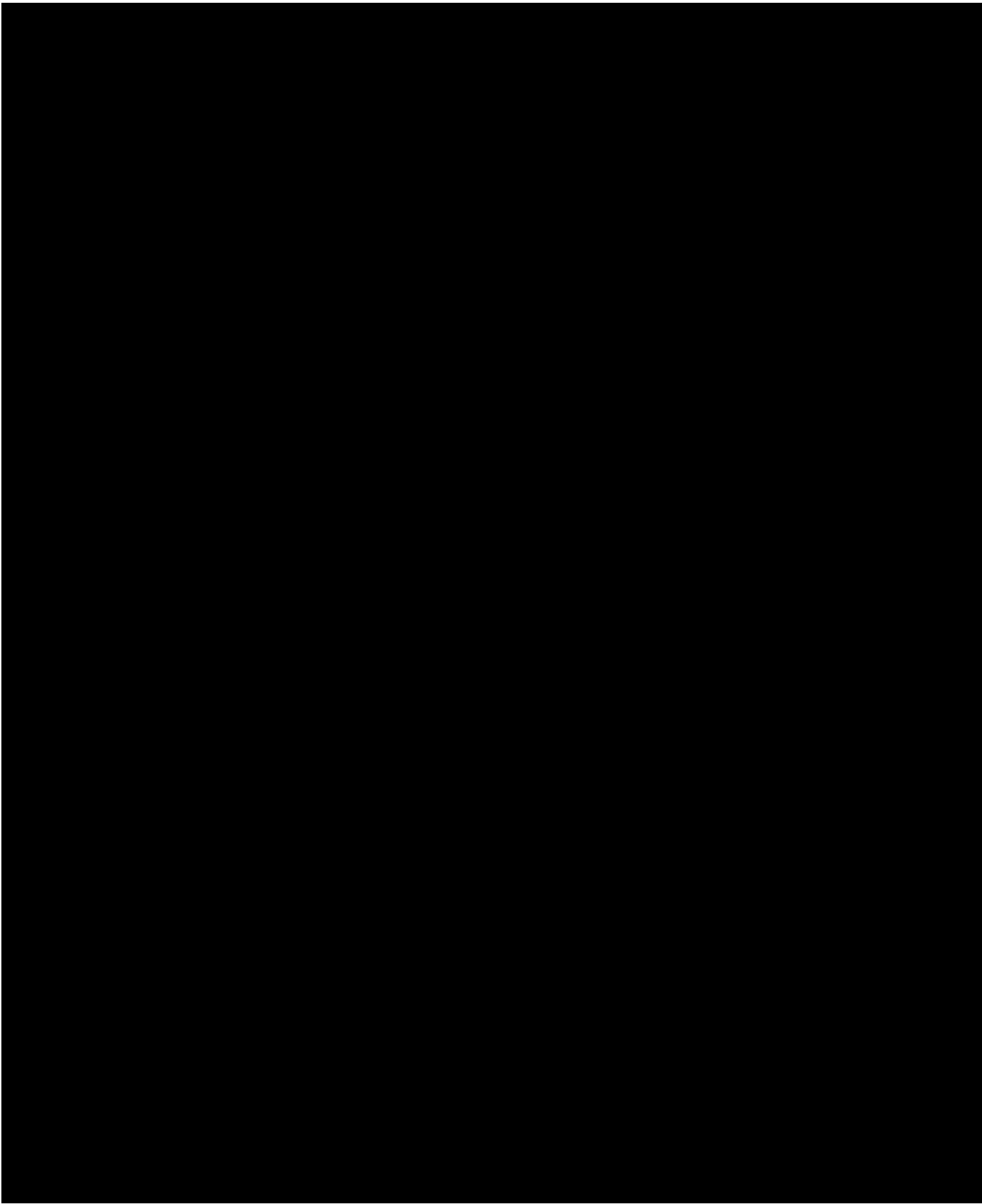


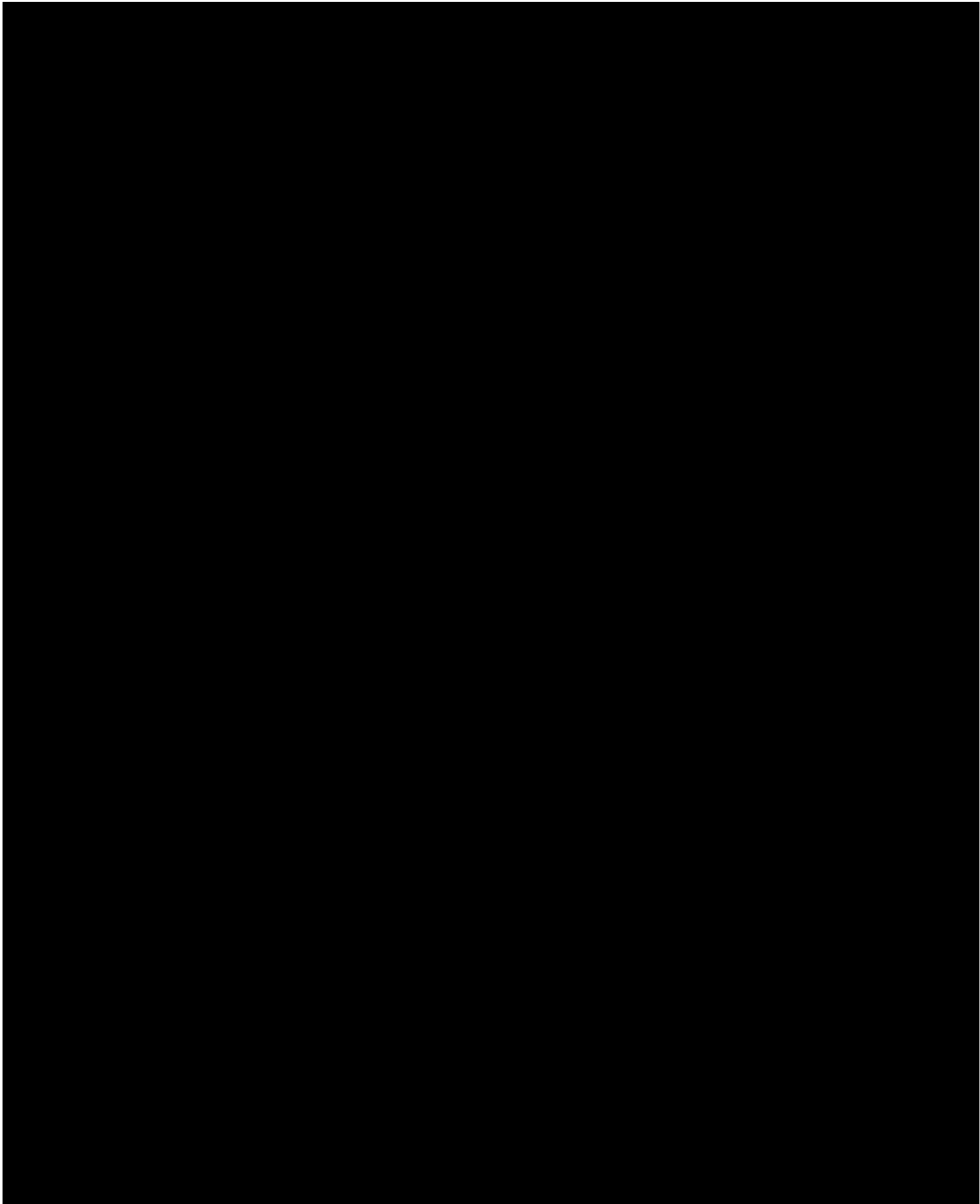


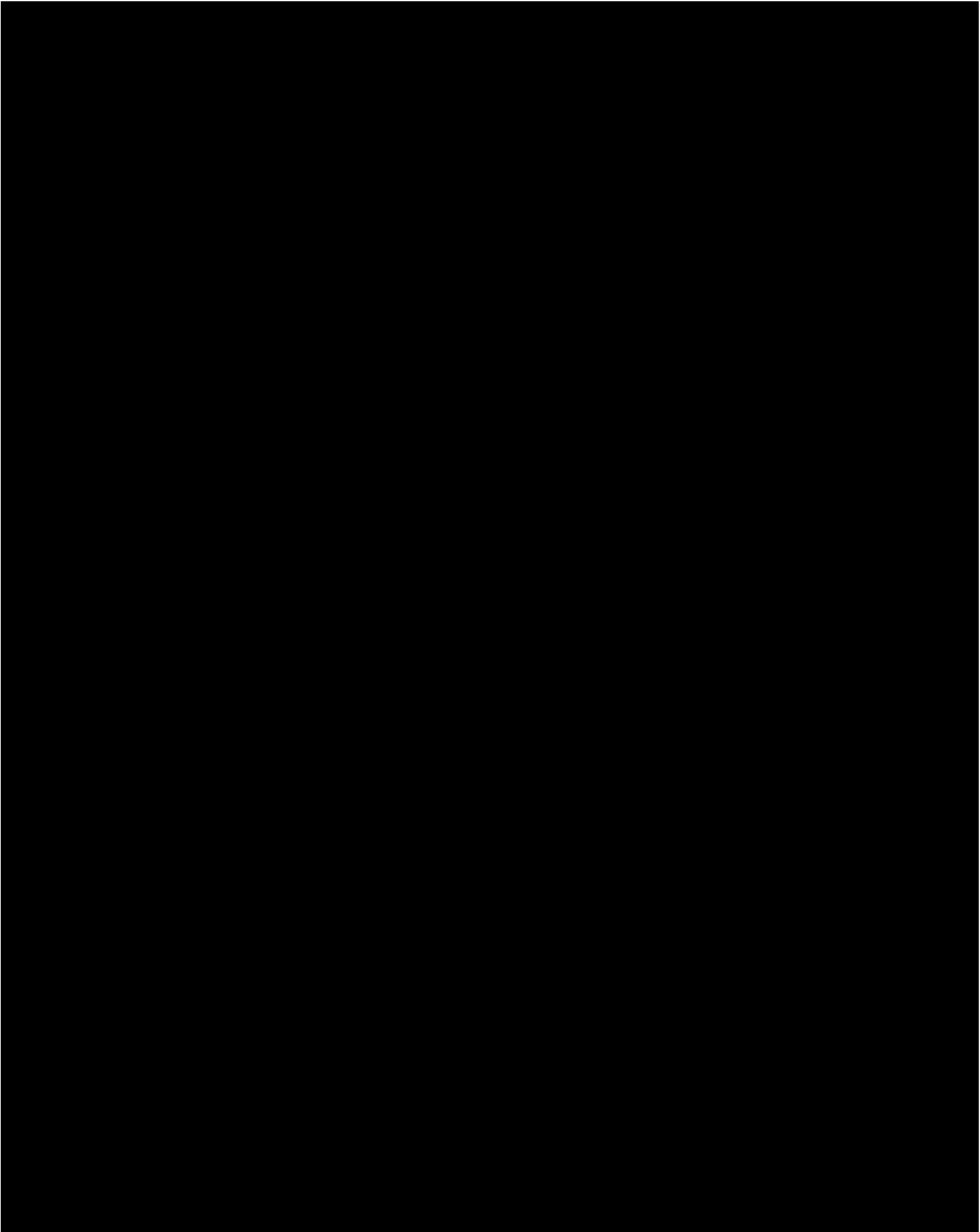


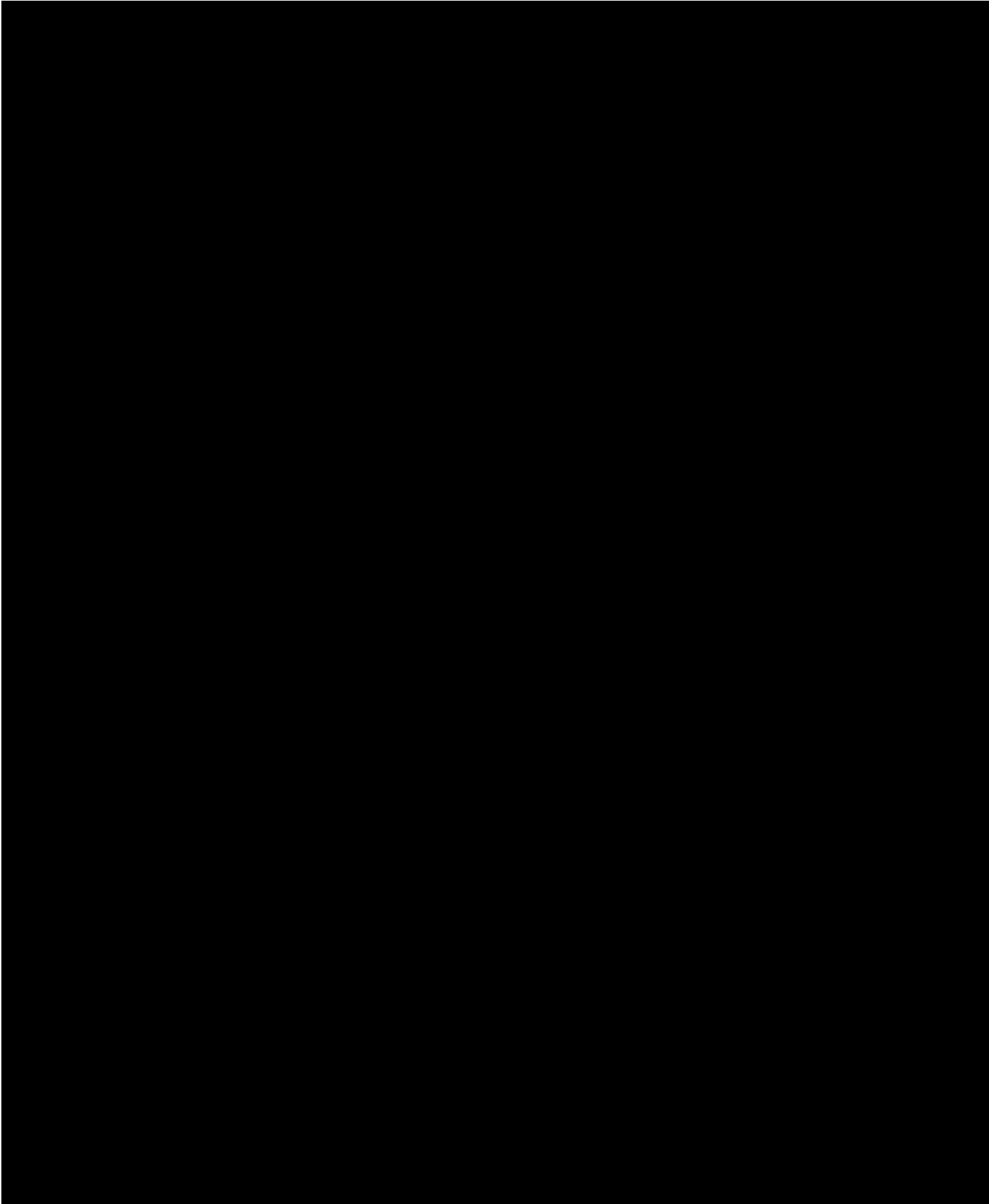
DTCC Attachment 10











DTCC Attachment 11

From: [Dale, Margaret A.](#)
To: [Kotwick, Mark D.](#)
Cc: [Dale, Margaret A.](#); [Catalano, Benjamin J.](#)
Subject: Lek
Date: Monday, April 4, 2022 4:32:45 PM

Dear Mark,

We received Lek's application for review and motion to stay on Sunday, April 3, 2022. Those papers make no mention of the dates I provided to you on Wednesday, March 30, 2022 regarding the timing of implementation of the cease to act at NSCC and DTC.

As I explained, with respect to NSCC, we intend to stop accepting trades for Lek on May 4, 2022, and the cease to act will become effective a week later on May 11, 2022. With respect to DTC, we intend the cease to act to be effective on June 9, 2022.

Margaret

Margaret A. Dale

Partner

Vice Chair, Litigation Department

[Proskauer](#)

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www.mindingyourbusinesslitigation.com

greenspaces

Please consider the environment before printing this email.

DTCC Attachment 12

In the Matter of the Application of

LEK SECURITIES CORPORATION

AFFIRMATION OF CHARLES F. LEK

I, Charles F. Lek, pursuant to 28 U.S.C. §1746, hereby declare under penalty of perjury under the laws of the United States of America that the following is true and correct to the best of my knowledge, information and belief:

1. I am the Chief Executive Officer of Lek Securities Corporation (“LSC” or the “Firm”) and have personal knowledge of the facts set forth herein, except as to matters that I believe to be true based on (a) information provided by FTI Consulting (“FTI”), (b) information about the positions of National Securities Clearing Corporation (“NSCC”), Depository Trust Company (“DTC”) and The Depository Trust & Clearing Corporation (“DTCC”) that I reviewed, or were reported to me by counsel, or learned during my participation in this proceeding, and (c) my review of business records of LSC and discussions with employees at LSC.

2. This Affirmation is submitted in support of LSC’s request for review by DTCC of (a) NSCC’s determination to cease to act for LSC and summary limitation of clearing activity, dated October 26, 2021 (the “October 26 NSCC Notice”) (*see* Ex. 53¹); (b) DTC’s determination to cease to act for LSC, dated October 26, 2021 (the “October 26 DTC Notice,”

¹ Exhibits referred to herein can be found in the LSC Compendium of Exhibits submitted contemporaneously with this Affirmation.

together with the October 26 NSCC Notice, the “October 26 DTCC Notices”) (*see* Ex. 52); (c) NSCC’s notice of modified activity cap and the imposition of censure and fines for violations of prior activity cap, dated November 5, 2021 (the “November 5 NSCC Notice”) (*see* Ex. 55); and (d) NSCC’s notice of violation of activity cap, imposition of censure and fine, and request for information, dated November 7, 2021 (the “November 7 NSCC Notice”). *See* Ex. 56.

3. I graduated with honors from Washington University in St. Louis with a Bachelor of Arts degree in economics. I began my career working on the floor of the New York Stock Exchange and have thirteen years of experience in the brokerage business. I have held my Series 24 license for eleven years and took over as Chief Executive Officer of LSC when my father, and founder of LSC, stepped away from LSC as part of a settlement with the SEC in October 2019.² I am very involved in the day-to-day management as well as an active leader and supervisor in all aspects of LSC’s business.

Procedural History

4. On October 26, 2021, LSC received the October 26 NSCC Notice advising that NSCC had (i) determined to cease to act for LSC and (ii) summarily limited LSC’s clearing activity by imposing a cap of \$300 million of aggregate unsettled clearing activity as

² On March 10, 2017, the United States Securities and Exchange Commission (the “SEC”) filed a Complaint in the U.S. District Court for the Southern District of New York alleging that LSC, and its then-principal, Samuel Lek, aided and abetted violations of the federal securities laws (the “SEC Complaint”). *SEC v. Lek Securities Corp., et al.*, 17-CV-1789 (DLC) (S.D.N.Y.). On October 1, 2019, the District Court entered a Consent Order (the “October 2019 Consent Order”) adopting a settlement agreement between the SEC and LSC pursuant to which LSC, *inter alia*, agreed to a limited injunction on certain activities, paid monetary penalties and retained an independent compliance monitor for a period of three years. *Id.* at ECF 466. Samuel Lek also agreed to divest his ownership interest in LSC and accepted a permanent bar from the securities industry as part of the resolution of the SEC Complaint. *Id.* at ECF 467.

measured by the gross market value of its unsettled portfolio each business day coinciding with the approval of LSC's start-of-day margin call (the "Initial Activity Cap"). Ex. 53 (October 26 NSCC Notice). The October 26 NSCC Notice stated that LSC had the right to request a hearing to object to NSCC's cease to act determination and imposition of the Initial Activity Cap. *See id.*

5. On that same day, DTC provided the October 26 DTC Notice to LSC advising that DTC had determined to cease to act for LSC, subject to its right to a hearing. Ex. 52 (October 26 DTC Notice).

6. By letter, dated October 29, 2021, LSC wrote to DTCC timely objecting to NSCC's determination to cease to act for LSC and imposition of the Initial Activity Cap in the October 26 NSCC Notice, and requesting a hearing on those determinations. *See* Ex. 54 (October 29, 2021 Seward & Kissel LLP ("S&K") letter to DTCC (the "October 29 Letter"). In that letter, LSC also timely objected to DTC's determination to cease to act for LSC in the October 26 DTC Notice and requested a hearing on that determination. *See id.*

7. On November 5, 2021, NSCC provided the November 5 NSCC Notice to LSC, informing LSC that NSCC had determined to modify the Initial Activity Cap on LSC's unsettled clearing activity from \$300 million to \$400 million (the "Modified Activity Cap") and impose an aggregate fine of \$100,000 on LSC and censure LSC via publication to the NSCC membership for LSC's alleged violation of the Initial Activity Cap. *See* Ex. 55. The November 5 NSCC Notice also advised LSC that NSCC would be increasing its minimum Required Fund Deposit from \$20 million to \$27 million, effective November 8, 2021, and that "if the calculated amount of its start-of-day Required Fund Deposit, exclusive of any Excess Net Capital Premium Charges, exceeds \$27 million on any date after Monday, November 8, Lek's minimum

Required Clearing Fund will automatically be re-set to such greater amount as the new minimum.” *See id.* The notice stated that LSC could request a hearing on the Modified Activity Cap and the related fines and sanctions, and that NSCC would deem LSC’s request for a hearing in the October 29 Letter with respect to the Initial Activity Cap to be a request for a hearing with respect to the Modified Activity Cap. *See id.*

8. On November 7, 2021, NSCC provided the November 7 NSCC Notice to LSC notifying LSC that it had determined to impose a fine of \$20,000 on LSC and censure LSC via publication to the NSCC membership for allegedly violating the Initial Activity Cap and Modified Activity Cap on November 8. Ex. 56 (November 7 NSCC Notice). The notice advised LSC of its right to request a hearing on the imposition of the fine and censure. *See id.* The notice also requested information with respect to the specific risk management controls and supervisory procedures LSC had implemented to comply with the Modified Activity Cap. *See id.*

9. On November 8, 2021, LSC timely responded to NSCC’s request for information in the November 7 NSCC Notice with respect to certain risk management controls and supervision procedures. *See* Ex. 57 (November 8, 2021 LSC letter to DTCC).

10. Also on November 8, 2021, LSC timely objected to NSCC’s determinations in the November 5 NSCC Notice and November 7 NSCC Notice and requested a hearing on NSCC’s determinations to: (i) impose the Activity Cap (both the Initial Activity Cap and the Modified Activity Cap); (ii) impose fines and sanctions for LSC’s violation of the Initial Activity Cap; and (iii) increase LSC’s minimum Required Fund Deposit from \$20 million to \$27 million. *See id.*

11. Pursuant to NSCC and DTC rules, on November 9, 2021, LSC timely provided a written statement, setting forth in particularity its bases for objecting to determinations of NSCC and DTC in the (a) October 26 NSCC Notice; (b) October 26 DTC Notice; (c) November 5 NSCC Notice; and (d) November 7 NSCC Notice. *See* Ex. 58 (November 9, 2021 S&K letter to DTCC).³

12. The Hearing Panel ultimately scheduled a hearing on this matter for January 20, 2022 and this Affirmation serves as my direct testimony for that hearing.

LSC's Business

13. LSC is an agency-only, independent order-executing and self-clearing broker that is engaged in the business of executing and clearing orders in equity securities, options and fixed income instruments, as agent directly or indirectly for over one million clients worldwide with roughly \$2.5 billion in client assets. Founded in 1990, LSC is a wholly owned subsidiary of Lek Securities Holdings Limited ("Lek Holdings"). Lek Securities UK Limited ("Lek UK"), also a wholly owned subsidiary of Lek Holdings, is a London-based broker offering the same services to customers in the United Kingdom and Europe that LSC offers in the United States.

³ On November 30, 2021, the Hearing Panel asked for clarity on whether LSC was seeking to have the increased minimum Required Fund Deposit reviewed by DTCC. LSC confirmed that it was, and the Hearing Panel requested submissions from the parties with respect to whether the increased required Minimum Fund Deposit was subject to review. *See* Ex. 59 (December 1, 2021 Eric Heichel email to Mark Kotwick and others). Following submissions by LSC (*see* Ex. 61 (December 6, 2021 S&K letter to Eric Heichel and Eric Levine)) and NSCC (*see* Ex. 60 (December 6, 2021 DTCC's Memorandum Concerning Subject Matter of Hearing)), on December 8, 2021 the Hearing Panel ruled that the NSCC Rules do not provide LSC with a right to a hearing with respect to the increase of its required Minimum Fund Deposit. *See* Ex. 62 (December 8, 2021 Ruling).

14. LSC and Lek UK (the “Firms”) currently employ approximately 40 people with offices in New York, Chicago and London.

15. Since it was founded some thirty years ago, LSC has been engaged in the business of executing, clearing and the safekeeping securities across a wide range of asset classes. It does not engage in market-making or proprietary trading, does not recommend investments to its customers and does not have any customers that are securities issuers, nor does LSC clear for broker-dealers that engage in underwriting or market-making. In that regard, it is one of the last remaining pure agency-based brokers that does not engage in proprietary trading.

16. As an agency broker, in fiscal year 2020, LSC derived approximately 65% of its revenue from clearing, execution and custody commissions and fees, and the balance of its revenue from interest income, including from securities lending transactions, margin financing and interest earned from cash deposits at banks.

17. LSC is registered with the SEC with regulatory oversight by the Financial Industry Regulatory Authority (“FINRA”), as its Self-Regulatory Organization.

18. The Firms are members of the following listed exchanges: (a) New York Stock Exchange; (b) London Stock Exchange; (c) Chicago Stock Exchange; (d) Philadelphia Exchange; (e) ARCA Exchange; (f) NASDAQ Stock Market; (g) International Securities Exchange; (h) Chicago Board Options Exchange; (i) BATS Exchange; (j) BOX Exchange; and (k) IEX.

19. The Firms conduct trading through various clearing organizations: (a) DTC; (b) NSCC; (c) The Option Clearing Corporation (“OCC”); (d) Canadian Depository Services, Inc.; and (e) Euroclear UK & Ireland (Crest).

20. Although the October 26 DTCC Notices reference that LSC can elect to voluntarily conduct an orderly wind down of its business, LSC has no intention of doing so. For some thirty years, LSC has provided a valuable service to its customers, providing them with direct access to U.S. securities markets. It has no intention of ceasing its operations based on what it believes is the arbitrary and unjustified determination of NSCC and DTC to cease to act for the Firm. Moreover, nothing has changed at LSC to warrant this determination. The Firm is not only profitable, but it is operating with the highest level of net capital in its 30 years of operations. LSC has never missed a margin call and has never failed to make a payment since joining DTC and NSCC in 1999. LSC maintains robust systems and controls, is solvent, and has failed on none of its financial obligations. LSC is responsible for the safekeeping of billions of dollars in client assets. NSCC and DTC ceasing to act for LSC would mark the first time a clearing firm was forced out of business, despite the firm being solvent and operating at multiple times its regulatory net capital.

LSC's Compliance Staff

21. LSC takes its compliance obligations very seriously and has five employees who have compliance responsibilities. While I am very involved in daily compliance-related matters, Jeffrey Tabak, an industry veteran and former co-CEO of Miller Tabak & Co., LLC was named Chief Compliance Officer of LSC in October 2019 and remains in that position today.

22. Mr. Tabak has more than forty years of industry experience. In addition to day-to-day compliance functions, Mr. Tabak has held his Series 24 and Series 4 licenses for more than 35 years and is ultimately responsible for the ongoing supervision and control of the Firm from a compliance perspective, reporting directly to me.

LSC's Capital

23. LSC had regulatory net capital of \$14,529,108 at year end 2020 (Ex. 7 (December 31, 2020 LSC X-17A-5 filing) at 18), some four times the SEC's minimum net capital requirement of \$3,678,770 (*see id.*). As per LSC's September 30, 2021 FOCUS Report, LSC had regulatory net capital of \$15,217,160 (Ex. 33 (LSC Focus Report September 2021)), eight times higher than the SEC's required minimum net capital of \$1,901,680 (*see id.*).

24. As noted in the October 26 DTCC Notices, LSC's excess net capital (as of September 24, 2021) was \$11.1 million (Ex. 52 (October 26 DTC Notice) at 2; Ex. 53 (October 26 NSCC Notice) at 3), far above the excess capital requirement at NSCC for correspondent brokers of \$1 million.

LSC's Access to Credit

25. As a starting point, it is noteworthy that there is nothing in any rules or regulations of either DTC or NSCC that requires its members to maintain any specific level of liquidity, maintain any lines of credit with a bank or have external credit facilities. Moreover, LSC has never been asked to agree, nor has it agreed with DTC, NSCC, or any other clearing corporation, regulator or SRO, to maintain any particular line or source of credit. When considering LSC's liquidity needs, it is critical to keep in mind that LSC is an agency-based broker that does not engage in proprietary trading, and thus it does not have the liquidity needs or incur the market risk of a broker-dealer that has a proprietary book. And LSC does not rely on its own capital and liquidity sources to pay for security transactions of its customers.

26. LSC's customers pay for their own securities, and LSC ensures that its customers have sufficient equity on deposit to support their transactions. LSC uses its own capital and liquidity sources only when it agrees to provide financing to its customers, and when

it agrees to do so, the loans are fully secured according to strict margin rules set by the Federal Reserve, FINRA and LSC's internal, even more conservative, "house margin" requirements.

27. LSC's capital and liquidity sources serve solely as a backstop to the market and the Firm's counterparties that its clients will honor their commitments. When evaluating the Firm's capital and liquidity sources, it would therefore be a mistake to ignore the same \$2.5 billion in equity that its customers have on deposit with LSC and conclude that LSC's market activity is solely supported by the Firm's own capital and liquidity sources, as if the Firm were trading for its own account, which, again, it does not.

28. To provide an additional backstop to the market and LSC's counterparties, LSC obtains liquidity from its capital and from borrowings. Credit obtained by borrowing funds falls into two categories: secured and unsecured. LSC has no proprietary inventory, so secured credit facilities are collateralized by customer securities.

29. A permissible method of financing customer debit balances is by lending securities in the stock loan market. Customer securities can be hypothecated with a value of up to 140% of each customer's debit balance. Moreover, if a security is needed to cover a short sale, the Firm might be able to borrow money at a negative interest rate, *i.e.*, it gets paid for borrowing money, and even if a security is not needed to cover a short sale, the Firm can still borrow money at favorable rates. LSC has approximately \$1 billion in stock loan facilities available from approximately a dozen different counterparties.

30. In addition to its stock lending facilities, in June 2021, LSC increased its secured loan facility with Lakeside Bank ("Lakeside") to \$20 million (the "Lakeside Secured LOC"), as well as an additional unsecured loan facility with Lakeside in the amount of \$10 million (the "Lakeside Unsecured LOC," together with the Lakeside Secured LOC, the

“Lakeside LOC”). Prior to that, LSC had in place with Lakeside a \$12.5 million line of credit, of which \$7.5 million could be used as unsecured.

31. As of September 30, 2021, LSC only had \$21.8 million in customer debit balances, so the Firm’s secured lines of credit were much larger than required. *See* Ex 33 (LSC Focus Report September 2021). In fact, LSC’s capital and credit facilities could support significantly more customer debits, but the Firm’s conservative credit standards limit the customers to which it is willing to lend money.

32. When possible, brokers avoid using proceeds from borrowings collateralized by customer securities because such borrowings will become a credit item in the reserve formula. This means that money borrowed this way must be deposited in the Special Reserve Account. If a firm does this, it would be borrowing money, at a cost, only to deposit the money in the Reserve Account and earn little or nothing.⁴

33. Secured bank lines of credit are, therefore, not an optimal means for a source of liquidity, other than to fund customer debit balances. Accordingly, a bank credit facility, which is collateralized by customer securities, is not useful to finance NSCC margin calls.

34. There is always enough collateral to secure loans to fund customer debit balances. This is because when a customer does not pay for his “buys,” LSC can utilize the

⁴ Credit items add to the money that must be deposited in the Special Reserve Account. Debit items reduce the deposit requirement. When brokers use customer securities as collateral for a loan, the proceeds constitute a credit item. However, the debit balance is itself a debit item, so borrowings to fund debit balances have little effect on the lockup requirements. Unlike debit balances and margin deposited with OCC, NSCC’s clearing fund requirement is not a debit in the formula. This means that brokers must obtain funds from sources where customer securities are not used as collateral, even if the trading is done for the account customer.

customer's securities to secure a loan, up to 140% of the debit balance. Banks will typically lend up to 80% (or more when needed) of the collateral, so the Firm only needs (Loan Amount) / .80 = 125% of the debit balance to finance the loan. This leaves 140% - 125% = 15% of the debit balance as excess collateral. If the Firm uses a stock loan, in which the borrower may provide collateral equal to 102% of the value of the securities loaned, it can monetize 102% * 140% = 142.8% of the debit balance, which would provide 42.8% of the financing need in excess collateral.

35. LSC has no proprietary positions, so unexpected liquidity drains would come from unexpected large customer withdrawals and spikes in the margin requirements at NSCC and at OCC. Customer credit balances are generally kept in cash in a Special Reserve Account, so sufficient cash is always available to meet customer withdrawals. Margin required by OCC is a debit item in the reserve formula, so for OCC the Firm can use the customers' money to pay for the customers' margin requirement.

36. NSCC, however, is different than OCC. Here a broker-dealer must have a sufficient amount of its own money and credit facilities not secured by customer securities to meet NSCC's margin requirements, even when the trading is done for the account of customers. In order to fund its NSCC margin requirements, as of September 30, 2021, LSC has access to the following sources of funding:

Main sources			
LSC capital and subordinated debt		\$ 15MM	
Accrued liabilities		\$ 4MM	September FOCUS Line 1600
Accumulated profits		\$ 14MM	September FOCUS Line 1670
Bank loans not collateralized by customer securities		\$ 10MM	(Lakeside Bank)
Borrowing under our unsecured note program		<u>\$100MM</u>	
	Total	\$143MM	
Additional sources (See footnote)			
Excess collateral on bank loans (15% of 30MM available)		\$ 3MM	
Two percent excess cash on stock lent out (2% of \$500MM)		\$ 5MM	September FOCUS Line 1520
	Total	\$ 8MM	
	Grand Total	\$151MM	

Note: LSC needs to be careful with this, because as of the following week, the loan will create a credit item in the Reserve Formula

37. LSC has developed operational controls, that are designed to ensure that client trading is limited so that NSCC margin calls do not exhaust available liquidity. By default, any order over \$500,000 is rejected by the Firm. In addition, selling OTC stocks can create large margin calls due to their high volatility. Therefore, by default any trade that would result in an aggregate position in OTC securities over \$500 is also rejected by the Firm. LSC uses its Q6 risk control system to ensure that trades that the Firm wants to reject are identified and blocked. Q6 has a track record of over a decade and has proven to be reliable. The Q6 risk control system and LSC's risk control system and liquidity management are described in "Lek Securities Risk Control System" (*see* Ex. 64) and "Q6 Trading Limits Explained." *See* Ex. 65.

38. An important Q6 feature is that it serves as a credit monitor to block trades that if executed would violate a margin rule or LSC's more sophisticated "House Margin" requirements. This way LSC's customers' credit risk is carefully controlled. In addition, a trade will also be blocked if the security that a customer wants to buy cannot be easily monetized unless the customer has sufficient cash in the account to fully pay for the security. Securities that can be difficult to monetize include stocks priced under \$5, corporate bonds and foreign securities.

39. LSC takes liquidity management seriously and it is a continuous process at the Firm. LSC subscribes to NSCC's webservice that calculates the mark-to-market (MTM) and the Value-at-Risk (VaR) of LSC's unsettled position at NSCC and monitors liquidity risk closely and in real time. LSC's technology provider has developed a webpage on the Firm's intranet that reflects the most recent state of NSCC's mark-to-market and VaR calculations. The data is obtained from NSCC's webservice. By viewing this webpage, LSC is aware of

NSCC's most recent calculation. Also, the securities that contribute to the calculations are also listed in order of significance.

The screenshot displays the Iscweb Risk Mgmt Dashboard for slice-id: 1. The Business Date is 20211223, and the Last Refresh is 12/26/2021 13:03:34.

SOD Requirement Overview

Requirement Total	MTM	\$324,007.49
Deposit Total	Volatility	\$5,610,480.53
Excess/(Deficit)	WI MTM	\$8.60
Total	CNS Fails	\$839,934.40
	Non-CNS Fails	\$2,744.00
	Fund/Serv	-
	MRD	\$2,149,600.94
	Min. Requirement	\$27,000,000.00

SOD Component Overview

Coverage	-
SPC	-
Illiquid	-
MMD	-
FIS	-
Special	-
CF Premium	-
ML Adjustment	-

VaR

SOD	\$5,610,480.53
Current (as of 1715):	\$4,941,368.31
Exposure	
SOD	\$324,007.49
Current (as of 1715):	\$1,318,882.44

Mark To Market

slice-id: 1715 Business Date: 20211223 MTM Total Requirement: \$1,318,882.44

Top Losers

Symbol	Amount	Quantity	Requirement	CUSIP
SBES	(\$526,619.61)	-52,661,961	(\$388,532.32)	83645W106
TMGI	(\$300,000.00)	-30,000,000	(\$297,000.00)	57161M205
AFOM	(\$183,000.00)	-18,300,000	(\$175,380.00)	01663M107
ARCT	\$985,719.20	24,680	(\$168,266.76)	03969T109
NEM	\$0.00	0	(\$168,212.02)	651639106
BOTY	(\$155,120.00)	-15,512,000	(\$144,812.80)	535742100
UVXY	\$1,694,773.80	119,772	(\$135,042.90)	74347Y839
MU	(\$2,164,011.98)	-22,919	(\$89,981.30)	595112103
ATLIN	\$622,724.63	60,734	(\$79,019.96)	04687A100

Top Gainers

Symbol	Amount	Quantity	Requirement	CUSIP
ALLK	\$42,834.55	4,099	\$562,144.90	01671P100
SAVA	\$486.09	11	\$321,675.88	14817C107
HUDI	\$0.00	0	\$287,957.73	G4645E105
ACAD	\$2,997,380.70	123,349	\$286,125.07	004225108
TQQQ	\$2,024,316.84	12,233	\$223,883.40	74347X831
TSLA	\$715,957.00	671	\$170,719.45	88160R101
SOPA	(\$80,919.99)	-5,067	\$93,405.28	83370P102
SEAC	\$23,817.45	13,015	\$65,769.31	811699107
ZBH	\$1,271,931.84	10,016	\$56,002.05	08056P102

VAR

slice-id: 1715 Business Date: 20211223 VAR Total Requirement: \$4,941,368.31 Total Requirement (VAR-MTM): \$3,622,485.87

Contributors

Symbol	Amount	Quantity	Requirement	CUSIP	Type
BTF	(\$861,427.94)	-43,201	\$861,427.94	91917A108	3
SBES	(\$526,619.61)	-52,661,961	\$552,950.59	83645W106	3
TMGI	(\$300,000.00)	-30,000,000	\$315,000.00	57161M205	3
AFOM	(\$183,000.00)	-18,300,000	\$192,150.00	01663M107	3
BOTY	(\$155,120.00)	-15,512,000	\$162,876.00	535742100	3
LSPRU	(\$1,005,000.00)	-100,500	\$160,800.00	51724W206	4
BITO	\$89,032.02	2,753	\$89,032.02	74347G440	3
TCEHY	\$548,155.65	9,095	\$87,704.90	88032Q109	3

Offsets

Symbol	Amount	Quantity	Requirement	CUSIP	Type
V	\$1,923,368.98	8,879	(\$30,049.40)	92826C839	0
NVDA	(\$1,131,951.60)	-3,819	(\$26,306.23)	67066G104	2
MU	(\$2,164,011.98)	-22,919	(\$22,069.48)	595112103	2
UPST	(\$302,205.60)	-2,040	(\$21,227.61)	91680M107	2
ZBH	\$1,271,931.84	10,016	(\$18,007.57)	98956P102	0
EW	\$669,978.27	5,211	(\$17,987.00)	28176E108	0
LW	\$654,920.50	10,606	(\$16,069.80)	513272104	0
ACN	\$692,483.27	1,717	(\$15,066.02)	G1151C101	0

40. When a customer proposes a trade which exceeds the Q6 limits discussed above, the proposed trade is entered into an NSCC simulation tool, and the impact of the trade is analyzed. If the impact is small, the trade is allowed and an adjustment is made in the Credit Limit Manager application to allow the trade to go through. If the impact of the proposed trade is large, however, the trade is blocked.

41. In order to be able to trade, LSC's customers have been willing to provide the necessary cash to meet anticipated NSCC margin calls. Normally, when a customer

leaves money at a broker-dealer, the broker is required to put the money in the Reserve Account. Customers must therefore find an alternative way to transfer funds to a firm if the money is intended by the customer to be used to finance an NSCC margin call. To accomplish this, LSC has implemented an unsecured note program with its parent, Lek Holdings (the “Lek Holdings Note Program”).

42. In February 2021, NSCC published a rule change (the “NSCC Rule Change”). The rule change effectively moved the illiquid charge into the volatility bucket. Since volatility is one of “core components” in calculating the Excess Capital Premium charge (“ECP”), LSC knew it would need more unsecured lines of credit to continue its current operations.

43. In response to the anticipated NSCC Rule Change, LSC implemented the Lek Holdings Note Program. The program works as follows: A customer lends money to Lek Holdings, the parent of LSC. Because Lek Holdings is not a broker-dealer, there is no requirement to place the money in a Reserve Account. Lek Holdings then is able to lend the money to LSC so that LSC can meet the NSCC margin call, although there is no requirement for Lek Holdings to use the money that way. In return, Lek Holdings signs a note to evidence the loan. The note has specific wording making important disclosures required by the SEC (*see, e.g.,* Ex. 67 (Adar Alef, LLC April 19, 2021 Note with Lek Holdings)):

- The loan is unsecured. *Id.* at § 6.
- The loan is not protected by SIPC. *Id.* at § 10.
- The note has not been registered with the SEC. *Id.* at § 9.
- The lender is a Qualified Institutional Buyer. *Id.* at § 9.
- The loan is payable on demand, upon three business days’ notice. *Id.* at § 2.
- There are no restrictions on how Lek Holdings can use the money. *Id.* at § 10.

44. The disclosures ensure that investors understand that making the loan is riskier than depositing funds with a broker-dealer. Moreover, there are no restrictions on the

use of the funds. The program is designed to ensure maximum flexibility so that LSC will have enough money to meet any NSCC margin call.

45. Specifically, anyone can lend money to Lek Holdings as long as Lek Holdings wants the money. Typically, the lender/investor will also be a customer of LSC, but it is not a requirement. For instance, a hedge fund that wants to earn interest on a short-term investment could be a lender to Lek Holdings.

46. The Lek Holdings Note Program is designed so that if a customer wants to engage in a trade that will create a margin call at NSCC, the customer will lend Lek Holdings the money to fund the margin call. When the Firm gets the money back from NSCC, it repays Lek Holdings, and the client gets its money back from Lek Holdings. All of the participants are wealthy, sophisticated investors and understand the benefits and detriments of participating in the program.

47. The Firm had assumed that NSCC would be satisfied with the Lek Holdings Note Program, because it was specifically designed to ensure that LSC would have enough money to meet its NSCC margin calls. Moreover, the Firm is conservative when estimating the NSCC margin call, so it typically borrows more money than it anticipates needing. Also, because there are no restrictions on the use of the money borrowed, the Firm has significant flexibility. This arrangement is much better than borrowing secured funds from a bank, most significantly because the proceeds from the Lek Holdings Note Program are not a credit item in the reserve formula.

48. The use of a holding company to raise money for a regulated financial institution is common, so the concept should be familiar to persons with experience in the industry, and programs like this have existed for years. The SEC staff had issued interpretations

addressing this type of borrowing. *See* SEC Division of Trading & Markets, SEA Rule 15c3-1(c)(2)/08 Interpretation, “Capital Contributions from Parent, Using Borrowed Funds” at 207, available at: <https://www.finra.org/sites/default/files/sea-rule-15c3-1-interpretations.pdf>.

Texas Capital LOC

49. Until or about late March 2021, LSC had a \$25 million secured line of credit with Texas Capital Bank (“Texas Capital” and the “Texas Capital LOC”).

50. In May 2020, an anticipated merger between Texas Capital and Independent Bank collapsed and Texas Capital subsequently significantly downsized. Consequently, on or about October 19, 2020, Bart McCain, Senior Vice President of Texas Capital and LSC’s relationship manager called me and Shaniqua Jones, LSC’s then-Chief Financial Officer. Mr. McCain explained that as part of the downsizing, Texas Capital was exiting its broker-dealer financing business, and that he would be leaving the bank. As a result, the bank intended to terminate the Texas Capital LOC, which it subsequently did in March 2021.

51. LSC did not view the loss of the Texas Capital LOC as material, and its loss did not compromise LSC’s operations or create any significant or additional liquidity risk for LSC. In fact, because the availability to LSC of other sources of liquidity, LSC had rarely utilized the Texas Capital LOC; the last loan under the Texas Capital LOC facility was paid off in June 2020.

52. Because the Texas Capital LOC was a secured line of credit, LSC could not use it to fund its NSCC’s clearing fund requirements, which requires an unsecured line, and Texas Capital LOC’s primary purpose was to be available to finance customer debit balances for which it, again, was seldom utilized.

BMOH LOC

53. In addition to the Texas Capital LOC terminating in March 2021, LSC's line of credit with Bank of Montreal Harris Bank ("BMOH" and "BMOH LOC") was wound down and ultimately terminated on or about October 6, 2021. While the termination of the BMOH LOC was potentially more significant than the termination of the Texas Capital LOC, in response to the pending termination of the BMOH, LSC was able to replace the BMOH LOC with sources of liquidity from the Lakeside LOC and the existing Lek Holdings Note Program that exceed the BMOH LOC. As a result, the Firm did not consider the termination of the BMOH LOC to be material to its liquidity or operations. Dealing with BMOH was convenient for LSC's staff because BMOH supported a wide range of SWIFT messages and SWIFT is LSC's preferred way to communicate with financial institutions.

54. Notably, the origin of DTC and NSCC's concerns with respect to LSC can be traced back to their misunderstanding of the circumstances surrounding the wind down of LSC's relationship with BMOH and their misplaced concerns about the effect of that wind down on LSC's liquidity.

55. Prior to the winding down of the relationship, BMOH was LSC's clearing bank for both DTC and NSCC. In addition, LSC was required under OCC's rules to maintain a settlement account at an OCC-approved settlement bank, and BMOH was LSC's OCC settlement bank. Except for a brief period during the 2008 financial crisis, when BMOH was experiencing its own problems, for some twenty-five years, BMOH was LSC's clearing bank for DTC and NSCC, as well as its OCC settlement bank, without incident or issue.

56. Prior to October 2021, in addition to BMOH and its parent, Bank of Montreal, there were only six other OCC-approved settlement banks: Bank of America, Citibank, BNY Mellon, JPMorgan Chase, U.S. Bank and Brown Brothers Harriman. For

different reasons, those other six OCC-approved settlement banks were not viable options to settle trades for LSC.⁵ Accordingly, LSC's relationship with BMOH was, in part, one of both convenience and necessity for LSC because of LSC's need for an OCC-approved settlement bank.

57. In addition to acting as LSC's OCC-approved settlement bank and its clearing bank for DTC and NSCC, LSC had a line of credit with BMOH. The BMOH LOC initially included a \$60 million secured lending facility (the "BMOH Secured LOC") with a \$15 million carve-out that could be used without the need to pledge customer securities (the "BMOH Unsecured LOC").

58. In or about 2016, BMOH assigned a new relationship manager to the LSC account and, on its own initiative, increased the BMOH Secured LOC to \$75 million. LSC did not ask for the additional credit -- and did not need it -- however LSC was aware that BMOH did not believe that the LSC relationship was particularly profitable, and it hoped that the additional fees generated by the increased line of credit would help the overall relationship since LSC at the time did not have a viable alternative OCC-approved settlement bank.

59. LSC used the BMOH Secured LOC primarily to finance customer margin loans. It would have been more economical for LSC to finance these loans in the stock loan market, but the BMOH Secured LOC was used to make the BMOH relationship more profitable to the bank. For the period February 1, 2021 through July 20, 2021 (i.e., the last day the line

⁵ Settlement services are not particularly remunerative, and the other OCC-approved settlement banks either do not provide settlement services to independent self-clearing brokers, like LSC, or, if they do, do so only as an accommodation to brokers that otherwise have substantial relationships with the bank.

was drawn), the daily average balance of the BMOH Secured LOC was only approximately \$22.6 million.

60. On the other hand, the BMOH Unsecured LOC, which was further reduced to \$8 million, *infra* at ¶ 63, was used by LSC for its NSCC funding requirements. The average draw on that unsecured line was \$7,338,983 during the period February 1 – July 20, 2021.

61. Following the filing of the SEC Complaint in March 2017, BMOH indicated to the Firm that it had various concerns about its relationship with LSC, although, it was not apparent that BMOH was actually intending to terminate its long-standing relationship with LSC. My belief was based both on discussions with BMOH, in which I was advised that the bank did not consider LSC to be a credit risk, and on BMOH's failure to take steps to cut its ties with LSC while discussing doing so in the abstract.

62. For example, BMOH advised LSC on or about October 2019 that it was contemplating reducing the \$15 million NSCC sublimit in the BMOH Unsecured LOC. However, it was not until more than a year later, in November 2020, that it reduced the NSCC sublimit from \$15 million to \$12 million, while otherwise taking no further steps to wind down its relationship with LSC.

63. On or about January 2021, BMOH further reduced the NSCC sublimit in the BMOH Unsecured LOC from \$12 million to \$8 million. I still did not consider it likely that BMOH would terminate its relationship with LSC, and in particular, its settlement services, which was what I considered the most important part of the relationship. My understanding was based, in part, on my discussions with Eric Bellendir, Vice President of the Financial Institution Group at BMOH, who assured me in early November 2020 that while BMOH was looking to

reduce its presence as a clearing and settlement bank for the clearing corporations, hence its reduction of the BMOH Unsecured LOC, BMOH did not consider LSC as a credit risk and that the Firm should not be concerned about losing BMOH as its clearing and settlement bank.

64. Consistent with my understanding that BMOH did not intend to cut its ties with LSC, on February 2, 2021, LSC and BMOH entered into an NSCC Renewal Letter Agreement (the “NSCC Letter Agreement”) that would allow BMOH to renew up to \$75 million of secured loans to LSC on a revolving, uncommitted basis, of which \$8 million would be available to cover margin requirements at NSCC. *See* Ex. 16 (February 2, 2021 Email from Eric Bellendir to LSC); Ex.17 (NSCC Letter Agreement). In the Letter Agreement, BMOH also stated that the “facility is subject to your continued acceptable financial condition,” *see* Ex. 17 (NSCC Letter Agreement), which again, did not seem problematic given Mr. Bellendir’s assurance that BMOH did not consider the Firm to be a credit risk.

65. In April 2021, I retained S&K to advise me of my rights with respect to the possible termination of LSC’s settlement bank relationship with BMOH and the lack of settlement banks approved by OCC. To be clear, my concerns at the time related solely to BMOH acting as LSC’s settlement bank, and not to the BMOH LOC, and I did not ask S&K advice on any aspect of the BMOH LOC. Similarly, I was not concerned about BMOH’s role as LSC’s settlement bank at DTCC as Lakeside is an approved settlement bank at DTCC and Lakeside had agreed to provide settlement services there to LSC.

66. On May 14, 2021, LSC wrote to Linda Haven, Managing Director of Financial Institutions at BMOH, inquiring about BMOH’s intentions concerning the LSC relationship and its rationale for possibly terminating its settlement bank relationships with LSC. Ex. 23 (May 14, 2021 S&K letter to Linda Haven) (the “May 14 Letter”). That letter

refers only to the settlement bank relationship and does not mention the BMOH LOC. *See id.* BMOH did not respond to that letter.

67. On May 28, 2021, S&K spoke with Joe Kamnik, Chief Regulatory Counsel of OCC, concerning BMOH and OCC's obligation to promote competition by maintaining an adequate number of approved settlement banks. During that call, Mr. Kamnik stated that BMOH had an obligation to inform OCC of its intention to terminate its relationship with LSC and that BMOH had not provided such notice. He volunteered to assist LSC in determining BMOH's intentions. That gave me further assurance that the BMOH relationship was not in serious jeopardy.

68. S&K spoke to Mr. Kamnik again on June 12, 2021. During that call, Mr. Kamnik stated that BMOH had informed OCC that it did intend to terminate the settlement banking relationship with LSC, but it intended to work with LSC to transition the settlement bank responsibilities to another OCC-approved bank.

69. On June 15, 2021, LSC wrote to Ms. Haven seeking a response to its May 14 Letter and noting S&K's conversations with Mr. Kamnik. Ex. 26 (June 15, 2021 S&K letter to Linda Haven) (the "June 15 Letter"). Again, that letter solely referenced BMOH's settlement banking services. *See id.*

70. On June 16, 2021, Ms. Haven responded to the June 15 Letter via e-mail stating that BMOH had not agreed with OCC to indefinitely delay the termination of its settlement bank relationship with LSC, but Ms. Haven indicated BMOH was willing to work with LSC on an orderly transition. Ex. 66 (June 16, 2021 Linda Haven Email to LSC).

71. In response, on June 23, 2021, S&K sent a letter to David Casper, CEO of BMOH, asserting that as one of only eight approved settlement banks at OCC, BMOH could

not, as a matter of law, arbitrarily terminate its relationship with LSC. Ex. 28 (June 23, 2021 S&K letter to David Casper). Again, this letter does not mention the BMOH LOC. *See id.*

72. Until the Firm got clarity about BMOH's actual intentions and timetable, and LSC had the opportunity to consider an appropriate transition plan, I did not believe there was a reason to alert other parties and cause any undue and premature alarm. To be clear, however, LSC's concern with BMOH was the potential termination of its services as LSC's OCC-approved settlement bank, and not the BMOH LOC.

73. It was not until July 8, 2021 that I came to believe that BMOH would actually terminate its relationship with LSC and was informed of the timing of the wind down of the relationship. On that date, counsel for BMOH wrote to S&K in response to its June 23, 2021 letter to Mr. Casper to advise that BMOH intended to orderly wind down its relationship with LSC, including discontinuing OCC settlement services, by early October 2021. *See* Ex. 36 (July 8, 2021 McGuire Woods letter to S&K) (the "July 8 BMOH Letter"). Prior to that correspondence, and for the reasons described above, I did not believe that LSC's relationship with BMOH was in true jeopardy.

74. In the July 8 BMOH Letter, BMOH also advised that it was reducing the BMOH LOC from \$75 million to \$50 million effective immediately and, in addition, would reduce the BMOH Unsecured LOC to \$4 million on August 9, 2021 and reduce the unsecured LOC further to \$0 on September 6, 2021. *See id.* at 3. As stated above, LSC had not inquired about the BMOH LOC in its previous letters because it was not a significant concern.

75. LSC was able to address the need for an OCC-approved settlement bank when OCC approved Lakeside as OCC's ninth settlement bank, after which LSC immediately established a settlement bank relationship with Lakeside. As mentioned above, *supra* at ¶ 53,

and in more detail below, *infra* at ¶¶ 79, 80, 108-110, 113, 115, LSC replaced the liquidity of the BMOH LOC with an increased \$30 million line of credit from Lakeside on June 28, 2021 and further supplemented its liquidity with the Lek Holdings Note Program that was implemented in February 2021.

76. On July 20, 2021, there was a call between LSC and DTCC regarding the wind down of the BMOH relationship, on which Ms. Jones, LSC's former CFO, provided an explanation about the BMOH and Lakeside lines of credit and the distinction of usage between the secured and unsecured lines. Ms. Jones explained why the loss of the BMOH LOC would not have a material impact on LSC: the BMOH Secured LOC could not be used to meet its margin calls at NSCC and satisfy NSCC's deposit requirements. On that call, Larry Pellecchio of DTCC acknowledged and appeared to understand that the Lek Holdings Note Program would be the primary source of liquidity to meet NSCC funding needs.

77. On July 21, 2021, DTCC advised LSC ("July 21 DTCC Letter") that it was aware that BMOH planned to reduce the BMOH LOC and that, eventually, BMOH planned to cease providing its services to LSC generally. *See* Ex. 37. In addition, the DTCC requested that LSC provide responses to a set of questions and information requests.

78. Importantly, the July 21 DTCC Letter evidences DTCC's misreading of the July 8 BMOH Letter and misinterpretation of the actions being taken with respect to the winding down of BMOH's relationship with LSC. Among other evidence of DTCC's confusion was the statement that:

We note that, unless Lakeside Bank increases the amount available to Lek under its line of credit, or Lek obtains another facility from Investor Bank or another bank, as far as we are aware, Lek would have only \$7.5MM of external bank borrowing availability after the termination of the BMO Harris Bank line of credit in September 2021.

Id. at 1.

79. As I explained in a July 26, 2021 letter to Michael Liebrock, DTCC Managing Director, in response to the July 21 DTCC Letter (“July 26 Letter”), while BMOH was reducing the BMOH Secured LOC from \$75 million to \$50 million as of August 4, 2021, DTCC incorrectly understood that the total line of credit (rather than simply the BMOH unsecured LOC/NSCC sublimit) was being further reduced to \$4 million before October 6, 2021:

BMOH will not reduce our line of credit to \$4MM as of August 4, 2021. The line will stand at \$50MM until October 6, 2021. Moreover, Lakeside Bank has already increased its line of credit from \$12.5MM to \$30MM. Therefore, as of August 6, the firm will have \$80MM in credit available to it, making the statement that we will have only \$7.5MM available to us materially inaccurate.

Ex. 39 (July 26 Letter) at 2.

80. I explained also in the July 26 Letter that the reduction of the BMOH LOC did not have a significant impact on LSC’s liquidity and that LSC had alternative sources of liquidity, specifically, an increased line of credit from Lakeside and the existing Lek Holdings Note Program, and that these sources were more diverse and reliable than the BMOH LOC and would more than offset the \$25 million reduction in BMOH’s Secured LOC and further reduction in the BMOH Unsecured LOC. I also stated that Lakeside was in the process of taking over BMOH’s role as LSC’s OCC settlement bank. *Id.* In addition, I provided information and documentation that was responsive to the questions posed in the July 21 DTCC Letter.

81. Notwithstanding LSC’s clarifications in the July 26 Letter, on July 28, 2021, DTCC informed LSC (“July 28 Letter”) that it intended to impose protective measures (*see* Ex. 40), and on August 2, 2021, the DTCC informed LSC (“August 2 Email”) that it was, (1) increasing LSC’s minimum Required Fund Deposit at the NSCC to \$20 million and (2)

reducing LSC's Net Debit Cap at the DTC to \$50 million. *See* Ex. 42. In doing so, the Staff ignored information that LSC provided about the DTCC's inaccurate interpretation of the July 8 BMOH Letter. Additionally, despite LSC's responses in the July 26 Letter to the questions that DTCC posed in the July 21 Letter, the Staff inaccurately claimed in the July 28 Letter and August 2 Email that LSC had been unresponsive to their questions. Upon my review of what was requested and what LSC produced, I am only aware of a single omission: The Staff's August 3 letter requested audited financials of our sister company Lek UK. Limited. *See* Ex. 14 (DTCC August 3, 2021 Letter) at 2. This was initially overlooked, but the financials were produced in response the Staff's letter dated September 13.⁶ *See* Ex. 51 (September 23, 2021 LSC Letter); Ex. 2 (Lek UK Financial Statements).

Optima and the SEC Monitorship

82. Prior to my becoming CEO of LSC and assuming control over the business, the SEC filed the SEC Complaint in New York federal court in March 2017. The SEC Complaint alleged that LSC aided and abetted Avalon FA Ltd. ("Avalon"), a foreign trading firm, in engaging in schemes to manipulate the securities market by providing Avalon, a customer of LSC, with access to the U.S. securities market.

83. LSC resolved the allegations in the SEC Complaint by agreeing to the October 2019 Consent Order. Pursuant to the October 2019 Consent Order, LSC, *inter alia*, agreed to retain an independent compliance monitor (the "Independent Monitor") for a period of at least three years. The terms of the retention of the Independent Monitor and scope of the

⁶ DTCC ultimately denied LSC's request to review the protective measures imposed in the August 2 email, finding that the measures were not subject to review. *See* Ex. 45 (August 6, 2021 DTCC Letter to LSC).

monitorship are set out in Independent Compliance Monitor Provisions. Ex. 3 (October 2019 Consent Order) at App. B.

84. The Independent Monitor was charged with performing a comprehensive and ongoing review of the various activities of LSC, including (a) whether LSC is complying with the Foreign Intraday Trading Injunction and (b) the reasonableness and sufficiency of LSC's controls and procedures to prevent manipulative trading and other market manipulation.

85. Joshua Mika from Optima Partners LLC ("Optima") was retained by LSC to serve as the Independent Monitor in November 2019. *See* Ex. 4 (November 26, 2019 Optima Engagement Letter).

86. As of October 26, 2021, Optima had filed five reports since its retention as Independent Monitor:

- Lek Securities Corporation 120-Day Monitorship Report, dated April 28, 2020 ("April 2020 Optima Report") (*see* Ex. 10)
- Lek Securities Corporation 120-Day Monitorship Report, dated August 26, 2020 ("August 2020 Optima Report") (*see* Ex. 12)
- Lek Securities Corporation 120-Day Monitorship Report, dated December 26, 2020 ("December 2020 Optima Report") (*see* Ex. 13)
- Lek Securities Corporation 120-Day Monitorship Report, dated April 26, 2020 ("April 2020 Optima Report") (*see* Ex. 21)
- Lek Securities Corporations 120-Day Monitorship Report, dated August 25, 2021 ("August 2021 Optima Report") (*see* Ex. 46)

87. As required under the October 2019 Consent Order, on May 27, 2020, LSC timely filed its Implementation Plan of 120-Day Monitorship Report with the SEC, certifying that it had adopted and implemented the recommendations of the Independent Monitor made in the April 2020 Optima Report ("LSC Monitorship Implementation Report"). *See* Ex. 11. LSC was not required under the October 2019 Consent Order to file an

implementation report or other formal response to any Optima reports after the initial April 2020 report.

88. Optima's monitoring of LSC pursuant to the terms of the October 2019 Consent Order remains ongoing.

BRG and the FINRA Independent Consultant

89. Separate and apart from the SEC Complaint, and again before I became CEO of LSC, FINRA commenced a disciplinary proceeding against LSC and Samuel Lek alleging that LSC had failed to develop and implement a reasonable anti-money laundering ("AML") program and system for the deposit and trading of microcap securities (the "FINRA Complaint"). *Dep't of Enforcement v. Lek Securities Corporation and Samuel Frederick Lek*, Disc. Pro. No. 2015045312501.

90. Shortly after LSC agreed to the October 2019 Consent Order resolving the SEC Complaint, it settled the FINRA Complaint and agreed to an Order Accepting Offer of Settlement, dated December 20, 2019 (the "December 2019 FINRA Order").

91. Under the December 2019 FINRA Order, LSC, among other things, agreed to retain an independent consultant (the "Independent Consultant") to "conduct a comprehensive review of the Firm's supervisory system and its [AML] and Section 5 obligations in connection with trading in [microcap securities] including but not limited to: (i) customer onboarding; (ii) acceptance of [microcap securities] for deposit in certificated or in other form or otherwise; (iii) customer trading of [microcap securities]; (iv) the Firm's systems and controls for monitoring for, detecting and investigating suspicious activity through the Firm; and (v) training of LSC staff regarding the foregoing subjects." Ex. 5 (December 2019 FINRA Order) at 34-35.

92. In addition to the retention of the Independent Consultant, LSC agreed to temporarily not sell or accept for deposit any microcap securities until the Firm certified to FINRA that it had implemented the recommendations of the Independent Consultant in the Initial Report (the “Temporary Microcap Business Suspension”). Ex. 5 (December 2019 FINRA Order) at 34. Under the terms of the December 2019 FINRA Order, the Temporary Microcap Business Suspension was to remain in place only until LSC certified that it had implemented the recommendations of the Independent Consultant in the Initial Report. *Id.*

93. Promptly after the December 2019 FINRA Report, LSC retained Bradley Mirkin from Berkeley Research Group, LLC (“BRG”) to serve as the Independent Consultant. *See* Ex. 6, LSC’s December 31, 2019 engagement letter with BRG.

94. The December 2019 FINRA Order directed the Independent Consultant to conduct its review and issue an initial report (the “Initial Report”) within 160 days from December 20, 2019 and, as necessary, make recommendations concerning how LSC should modify its processes, controls, policies, systems, procedures and training to manage its regulatory and other risks with respect to the adequacy of its supervisory system and its compliance with AML rules and other requirements in the Order. *See* Ex. 5 (December 2019 FINRA Order) at 36.

95. On February 4, 2020, BRG issued its Initial Report and made recommendations with respect to LSC’s processes, controls, policies, systems, procedures and training to manage its regulatory and other risks with respect to the adequacy of its supervisory system and its compliance with AML rules. *See* Ex. 8, BRG Initial Report, dated February 4, 2020 (“BRG Initial Report”).

96. Absent objection to the recommendations of the Independent Consultant in the Initial Report, LSC was to adopt and implement BRG's recommendations and provide a written report certifying the Firm's implementation of its recommendations in the BRG Initial Report (the "BRG Implementation Report"). *See* Ex. 5 (December 2019 FINRA Order) at 37-38.

97. Following the issuance of the BRG Initial Report, LSC implemented the recommendations in the Initial Report or otherwise confirmed that LSC was in compliance with the recommendations. Pursuant to the terms of the December 2019 FINRA Order, LSC self-certified that it had complied with its obligations in a February 10, 2020 letter to FINRA, and the Temporary Microcap Business Suspension was lifted. *See* Ex. 32 (February 10, 2020 LSC Certification); Ex. 5 (December 2019 FINRA Order) at 39-40.

98. LSC, as required under the December 2019 FINRA Order, filed a report with FINRA describing its implementation of the recommendations in the BRG Initial Report, dated March 3, 2020 (the "LSC Implementation Report"). *See* Ex. 9 (LSC Implementation Report).

99. Under the terms of the December 2019 FINRA Order, the Independent Consultant was to conduct a follow up review and issue a final report (the "Final Report") addressing LSC's implementation of the recommendations described in the BRG Implementation Report by not later than December 20, 2020. *See* Ex. 5 (December 2019 FINRA Order) at 34. After FINRA twice extended the deadline to file the Final Report to accommodate Mr. Mirkin, BRG ultimately filed its final report on April 19, 2021 (the "BRG Final Report"). *See* Ex. 20.

**LSC's Responses to Particular Grounds for NSCC
and DTC Determinations in October 26 DTCC Notices**

100. For the convenience of the Hearing Panel, I have set out below the alleged grounds identified by NSCC and DTC supporting their determinations in the October 26 DTCC Notices and LSC's responses thereto.⁷

Ground 1

[LSC] has [excess net capital] of \$11.1MM (as of September 24, 2021), which, although sufficient to meet the minimum capital requirement at NSCC, NSCC believes is inadequate to support the level of risk activity conducted by [LSC]. See Ex. 53 (October 26 NSCC Notice) at 3; Ex. 52 (October 26 DTC Notice) at 2.

101. As an initial matter, NSCC concedes that LSC has sufficient excess net capital to meet the minimum capital requirement of NSCC. According to its December 31, 2020 X-17A-5 filing with the SEC (*see* Ex. 7, at 18), LSC had \$14,529,108 of regulatory net capital, or 395% of its regulatory minimum requirement of \$3,678,770.

102. Moreover, the \$11.1MM excess net capital level as of September 24, 2021 exceeds LSC's excess net capital of \$10,850,338 as of December 31, 2020, and LSC's excess net capital never dropped below \$10,501,575 and was as high as \$13,315,480 over the nine-month period through September 30, 2021. This demonstrates the financial stability of LSC.

103. While NSCC alleges that LSC has inadequate excess net capital, despite my asking, NSCC has never identified to LSC the amount of capital it would find adequate to support the "level of risk activity conducted by LSC." Moreover, it has never identified what "risk activity" LSC is engaged in that justifies requiring some extraordinary level of excess net capital or how those activities correlate to any particular amount of capital. In fact, Tim

⁷ These same grounds also purport to underlie the actions taken by NSCC in the November 5 NSCC Notice and the November 7 NSCC Notice.

Cuddihy, Managing Director, Financial Risk Management, DTCC, has confirmed that there is no “magical number” in terms of the amount of LSC’s capital that DTCC would be satisfied with and DTCC has no particular metrics that it uses to determine the adequacy of a firm’s capital.

104. The premise that LSC is engaged in exceptionally risky activity justifying an additional amount of capital, moreover, is simply erroneous. As described above, *supra* at ¶¶ 15, 25, LSC is an agency broker and its activities, if anything, are inherently less “risky” than the activities of the types of brokers that engage in proprietary trading and that have failed in the past. For these reasons, it appears that DTCC’s determination that LSC has inadequate liquidity is arbitrary and not supported by any reasoned calculations or considerations.

Ground 2

[LSC] has minimal cash on its balance sheet - nonsegregated cash typically represents only a low percentage of assets, which increases its dependence on external credit for liquidity. See Ex. 53 (October 26 NSCC Notice) at 3; Ex. 52 (October 26 DTC Notice) at 2.

105. LSC’s cash and cash equivalents on its balance sheet as of September 30, 2021 in the amount of \$24,292,207 exceeded 5% of its total assets, which is consistent with the cash positions of other broker-dealers. As stated above, LSC’s regulatory capital far exceeds requirements, LSC is profitable and LSC’s dependence on external credit is also in line with regulatory standards and industry practices. *See Carr Aff.* at ¶ 60 (cash holdings of various broker-dealers).

106. Again, DTCC has declined to quantify to me what level of cash and cash equivalents it would find acceptable for the activities engaged in by LSC, or how DTCC purports to calculate that level. Moreover, Ground 2 falsely states that LSC’s balance sheet increases its dependence on “external credit.” As discussed above, *supra* at ¶¶ 29, 31-36, 41-48, and below, *infra* at ¶¶ 110, 114-115, 119, 125, 131-132, through the Lek Holdings Note

Program and its security lending arrangements, in 2021, LSC has diversified its liquidity sources and has reduced its reliance on bank borrowings.

Ground 3

[LSC's] liquidity position has been compromised by [BMOH's] termination of [LSC's] \$75 million line of credit ("BMOH LOC") as of October 6, 2021, and the termination of [LSC's] \$25 million line of credit ("Texas Capital LOC") with Texas Capital Bank ("Texas Capital") on March 31, 2021. See Ex. 53 (October 26 NSCC Notice) at 3; Ex. 52 (October 26 DTC Notice) at 2.

107. As described above, *supra* at ¶ 50, 53, the BMOH LOC totaling \$75 million and the \$25 million Texas Capital LOC have been terminated this year. However, contrary to the Staff's conclusory statement, LSC's liquidity has not been "compromised" as a result of the termination of those credit lines.

108. The BMOH LOC and Texas Capital LOC were terminated after the \$100 million Lek Holdings Note Program was implemented and were succeeded by the \$30 million Lakeside LOC. To understand better the adequacy of LSC's liquidity, it is important to understand LSC's primary financing needs and the use and importance of unsecured versus secured financing in meeting those needs. Aside from NSCC funding requirements, which require unsecured financing, LSC's other major financing need comes from customer margin accounts, which can be funded through secured financing.

109. Unsecured lines of credit, including the Lakeside Unsecured LOC and Lek Holdings Note Program, are available for, and are typically used to meet, LSC's NSCC funding requirements. On the other hand, customer debits are financed through the Lakeside Secured LOC and LSC's securities lending arrangements that exceed \$1 billion in total capacity from multiple counterparties.

110. In that regard, and by way of comparison, a summary of LSC's unsecured credit lines available to finance its NSCC funding obligations, as of the beginning of 2020 compared to October 26, 2021, is set out below:

	<u>January 1, 2020</u>	<u>October 26, 2021</u>
BMOH Unsecured LOC	\$15MM	0
Lakeside Unsecured LOC	\$7.5MM	\$10MM
Lek Holdings Note Program	<u>0</u>	<u>\$100MM</u>
Total	\$22.5MM	\$110MM

111. LSC has explained to the Staff the difference between LSC's secured and unsecured lines and how the two are used to address LSC's funding needs on more than one occasion, including during a lengthy telephone conversation with senior personnel on July 20, 2021. See *supra* at ¶ 76.

112. With respect to LSC's overall liquidity, to be clear, as described above, *supra* at ¶¶ 51-52, LSC seldom utilized the Texas Capital LOC, thus I did not consider that its termination was either material or compromised LSC's liquidity. Moreover, the Texas Capital LOC was a secured line of credit and not used to fund NSCC deposit requirements, thus its termination did not impact LSC's ability to satisfy its NSCC funding obligations.

113. Moreover, LSC rarely utilized all of the BMOH LOC. During the period February 1 through July 20, 2021, LSC's average daily outstanding balance drawn under secured and unsecured BMOH LOC was approximately \$22.6 million and \$7.3 million, respectively, in line with what is available under the current Lakeside Secured LOC of \$20 million and Lakeside Unsecured LOC of \$10 million. See Carr Aff. At ¶ 61 n.48. Accordingly,

the current Lakeside LOC alone provide liquidity in line with the average use of the former BMOH LOC.

114. To the extent LSC's secured financing needs exceed the \$20 million Lakeside Secured LOC, those needs can be satisfied by LSC's securities lending arrangements, which have a capacity of up to \$1 billion and, with the Lakeside Secured LOC, are "virtually guaranteed to be available to finance debit balances." *See Carr Aff.* at ¶ 70. And, moreover, securities lending is economically more attractive than using bank credit lines to finance customer debit balances.

115. LSC's unsecured financing needs beyond the \$10 million Lakeside Unsecured LOC are more than satisfied by the Lek Holdings Note Program, which supplies up to \$100 million of liquidity. Notably, the Lek Holdings Note Program is structured to have the desirable effect of aligning liquidity needs with the supply of liquidity. Unlike a typical unsecured line of credit that may not be available when a firm actually needs it, liquidity under the Lek Holdings Note Program originates from capital providers who employ LSC as their broker and drive a significant portion of LSC's daily liquidity requirements at NSCC. This aligns LSC's liquidity needs with LSC's liquidity sources and, therefore, unlike a traditional unsecured line of credit, is not subject to falling short of required liquidity in times of distress.

116. Notably, Optima, the Independent Monitor, concurs with the view that LSC has adequate liquidity and notes how the NSCC inappropriately fails to distinguish between the liquidity needs of pure agency brokers from brokers who engage in proprietary trading:

The SEC has recently expressed concern that broker dealers are not sufficiently aware of Liquidity Risk. Lek Securities was recently examined by the Commission Staff for exactly this purpose. As monitor, Optima deemed it prudent to conduct an independent review. In our review, we looked at how liquidity demands could be placed on the Firm and in which manner the Firm would meet these demands if necessary.

Of course, LSC's primary source of liquidity come from its customers. This is an important distinction that is often overlooked by counterparties. LSC uses its customers' money to pay for its customers' obligations. The Firm does not have proprietary positions, so LSC's capital serves as an additional buffer against losses, over and beyond customer equity. This is a very different situation from a firm like Lehman Brothers where the firm's capital was required to absorb losses. LSC has about 13.5 million in capital. But LSC's customer trading is funded primarily by the more than \$1 billion the firm holds in customer equity. This is the proverbial 800-pound gorilla in the room. The National Securities Clearing Corporation, for example, chooses to ignore this important fact and treats agency positions, which are backed up [by a] massive amount of customer equity, the same way as proprietary positions, which must be paid for from firm equity.

See Ex. 13 (December 2020 Optima Report) at 31.

117. Optima goes on in that report to describe how LSC adequately and appropriately mitigates liquidity risks associated with certain adverse events. *Id.* at 3-33.

Ground 4

[LSC] has a credit facility with [Lakeside], consisting of a \$20 million line of credit and a \$10 million line of credit (collectively, the "Lakeside LOC"). In violation of the NSCC [and DTCC] Rules, [LSC] has not fully responded to NSCC's [and DTC's] inquiries in respect of the Lakeside LOC, and has not been forthcoming about what collateral it would use to support each part of the line of credit and whether that same collateral is also being pledged to support any other liquidity sources. Accordingly, NSCC [and DTC] believes that there is a high probability that [LSC] does not have enough collateral to utilize the full Lakeside LOC. See Ex. 53 (October 26 NSCC Notice) at 3-4; Ex. 52 (October 26 DTC Notice) at 3.

118. LSC has provided the Lakeside loan documentation to DTCC. LSC has sufficient assets to collateralize the \$20 million Lakeside Secured LOC, which is used primarily for the purpose of financing customer debit balances. SEC rules permit rehypothecation of customer "margin securities" with a value of up to 140% of the customer's debit balance.

Therefore, collateral is virtually guaranteed in a sufficient amount to finance debit balances because haircuts are rarely, if ever, as high as 28.5% (1 minus 100/140). The typical haircut for bank secured lending is 20%, and, in securities lending, could be negative (generally, securities lending can be collateralized at 102% of the securities' market value as noted above, *supra* at ¶ 34).

119. Customer debit balances for LSC as of September 30, 2021 stood at \$21,378,559, and according to the formula above, LSC would be able to borrow approximately \$30 million (140% x \$21,378,559). The loan amount available through bank secured lending would be approximately \$17 million (80% x \$21,378,559), and the loan amount available through securities lending would be approximately \$21.80 million (102% x \$21,378,559). In addition, small debit balances do not require external financing, since they can be financed with excess free credit balances. Therefore, these debit balance amounts should free up sufficient collateral for the \$20 million Lakeside Secured LOC.

120. I strongly disagree with the allegation that LSC “has not fully responded” and “has not been forthcoming” about the Lakeside LOC and the collateral supporting the Lakeside Secured LOC. To the contrary, the Firm was responsive and provided DTCC with substantial information and materials with respect to the Lakeside LOC.

121. In its July 26 Letter, LSC provided information about its sources of liquidity, including the Lakeside LOC. Ex. 39 (July 26 Letter). In response, DTCC requested additional information, including with respect to the Lakeside LOC and “detail how the Lakeside facility can be used and what amount of the facility is available to Lek for meeting requirements at NSCC and DTC.” Ex. 40 (July 28 Letter) at 2. Two days later, on July 30, 2021, LSC timely responded to DTCC’s request for additional information, providing

documents regarding both the Lakeside Secured and Unsecured LOCs and stating in relevant part, “I believe that the documents speak for themselves with respect to the loan terms and conditions. Of the \$30MM, \$10MM can be used to meet our margin requirement at NSCC. The entire facility can be used to pay DTC.” Ex. 41 (July 30, 2021 LSC Letter) at 2; Ex. 29 (June 28, 2021 Lakeside 20MM Secured LOC Loan); Ex. 30 (June 28, 2021 Lakeside 10MM Unsecured LOC Loan).

122. LSC subsequently provided additional information and material about the Lakeside LOC and related collateral. For example, it provided the Lakeside Pledge Agreement in its September 23, 2021 letter. Ex. 51 (September 23, 2021 LSC Letter); Ex. 48 (Lakeside Agreement to Pledge). In its August 5, 2021 letter to DTCC, LSC explained how the \$20 million Lakeside Secured LOC is secured by the rehypothecation of customer securities, while the \$10 million Lakeside Unsecured LOC is backed by LSC’s receivable at NSCC. *See* Ex. 44 (August 5, 2021 LSC Letter). When DTCC asked where this explanation was referenced in the provided documents (Ex. 47 (September 13, 2021 DTCC Letter) at 2), LSC replied that this information would not be expressly stated in the loan documents. Ex. 51 (September 23, 2021 LSC Letter) at 2. Additionally, LSC provided a list of securities from its NSCC CNS-Projection Report (Ex. 50) and further explained that the securities in the report have yet to settle “and they are a large component of [LSC’s] NSCC requirement [and therefore] Lakeside understands that the loan is secured by the receivable from NSCC.” Ex. 51 (September 23, 2021 LSC Letter) at 2.

123. LSC also provided daily liquidity reports that showed the breakout of collateral for each source of liquidity, as requested by DTCC. *See, e.g.*, Ex. 49 (September 23, 2021 Daily Liquidity Report).

Ground 5

[LSC] has informed NSCC [and DTC] that it has a \$100 million promissory note from its parent, Lek Securities Holdings Limited (“Lek Holdings”). However, [LSC] has repeatedly failed to provide NSCC [and DTC] with requested information, including, but not limited to, audited financials of Lek Holdings and details about its financial relationship with [LSC]. Accordingly, NSCC [and DTC] does not have enough information to assess the reliability and sufficiency of the \$100 million promissory note, and therefore NSCC [and DTC] cannot responsibly consider the promissory note as a reliable source of liquidity for [LSC]. See Ex. 53 (October 26 NSCC Notice) at 4; Ex. 52 (October 26 DTC Notice) at 3.

124. LSC strenuously disagrees with the allegation that it has “repeatedly failed to provide” NSCC with requested information concerning the Lek Holdings Note Program. LSC has provided substantial materials to DTCC about the Note Program, and moreover, has repeatedly offered to include DTCC in meetings with FINRA and the SEC, to discuss the program. Troublingly, while the other entities have indicated they would welcome the opportunity to meet and discuss the note program with LSC, DTCC has repeatedly pushed off meeting, saying they needed more time to review the matter before any discussions.

125. The \$100 million Lek Holdings Note Program was established at an amount that exceeds foreseeable liquidity needs. Furthermore, the Lek Holdings Note Program aligns LSC’s liquidity needs with LSC’s liquidity sources. LSC believes that it is reasonable and in fact desirable to make appropriate arrangements such that clients fund the margin calls that they create.

126. It is not economically necessary or desirable for a clearing firm to use its own capital to fund its customers’ trading. Firms earn only a small commission, while customers trade as principal and stand to earn significant amounts. Investors that provide notes to Holdings that underpin the Lek Holdings Note Program are large, sophisticated investors that understand and accept the risk of providing unsecured financing to a non-broker-dealer (Lek Holdings) without SIPC protection.

127. As DTCC knows, FINRA also raised questions about the Lek Holdings Note Program, and on July 26, 2021, in response to DTCC's July 21 Letter, LSC provided to DTCC all of the materials previously provided to FINRA on July 8, 2021 (the "July 8, 2021 FINRA Production") with respect to the Lek Holdings Note Program. Ex. 39 (LSC July 26 Letter). Among other documents, the July 8, 2021 FINRA Production included the Promissory Note Agreements (Exs. 18-19, 22); correspondence with FINRA explaining the Note Program (Ex. 35); Lek Holdings Ledger Balances (Ex. 25), and a Lek Holdings Reconciliation spreadsheet that showed the source of funding for the Note Program (Ex. 15).

128. In its July 30, 2021 letter, LSC pro-actively alerted DTCC that it recently became aware of letter from FINRA that required follow-up information from LSC on the July 8, 2021 FINRA Production (the "July 21, 2021 FINRA Letter") (Ex. 38) and provided a copy of that letter to ensure that DTCC was aware of any developments regarding the Lek Holdings Note Program. Ex. 41 (July 30, 2021 LSC Letter) at 2-3. The Firm subsequently provided additional materials to DTCC concerning the Note Program on August 5, 2021, including Lek Holdings Balance and Income Statements for 2018-June 2021 (Ex. 2) and LSC's Response to the July 21 2021 FINRA Letter (Ex. 43 (August 4, 2021 LSC Letter to FINRA)). *See* Ex. 44 (August 5 LSC Letter). On September 23, 2021, LSC sent another production of documents provided to FINRA, as well as Lek UK's financial statements for 2018-2020 (Ex. 1). *See* Ex. 51 (September 23, 2021 LSC Letter).

129. DTCC misleadingly alleges that LSC failed to provide "audited financials of Lek Holdings." In fact, Lek Holdings does not have audited financials, as LSC explained to DTCC in a September 23, 2021 letter:

Lek Securities Holdings is a privately held, nonregulated entity which is not required under any rules, regulations, or covenants to produce or prepare audited consolidated and/or consolidating financial statements. As such Lek Securities Holdings does not have consolidated and/or consolidating financial statements. In place of audited consolidated and/or consolidating financial statements DTCC was previously provided with the Balance Sheets and Profit and Loss Statements for Lek Securities Holdings Limited. Additionally, DTCC receives annually the audited financial statements of Lek Securities Corporation, and as per the request below, Lek Securities is providing the audited financial statements of Lek Securities UK.

Ex. 51 (September 23, 2021 LSC letter) at 3.

130. Notably, I understand that the information provided has answered FINRA's questions about the Lek Holdings Note Program and alleviated any concerns it had. Brian Kowalski, FINRA's Senior Director of Risk Monitoring, moreover, has acknowledged that FINRA now believes that the Lek Holdings Note Program adequately addresses any liquidity risks associated with NSCC funding requirements.

Ground 6

LSC has told NSCC [and DTC] that it has access to certain uncommitted stock loan/borrowing arrangements, however, NSCC [and DTC] has not been able to ascertain whether these provide significant incremental liquidity to LSC. See Ex. 53 (October 26 NSCC Notice) at 4; Ex. 52 (October 26 DTC Notice) at 3.

131. As mentioned above, *supra* at ¶¶ 109, 114-115, LSC finances significant customer debit balances through securities lending. LSC's securities lending arrangements (i) exceed \$1 billion in total capacity from multiple counterparties, and (ii) provide sufficient collateral for securities lending under SEC rules. Customer debit balances are supported by more than sufficient collateral in customer margin accounts because SEC rules permit securities with a value of up to 140% of customer debit balances to be rehypothecated in securities lending. This makes available sufficient collateral for customer debit financing. Small debit balances are financed with available free credit balances and therefore do not require external

financing. LSC's securities lending operations have established over a billion dollars in stock loan facilities from multiple counterparties.

132. Securities lending counterparties have access to large pools of liquidity and will take almost any collateral to place in overnight investment funds and earn a spread. Moreover, LSC earns additional revenue when it lends hard to borrow securities. Notably, securities lending also has fewer restrictions on specific collateral, and therefore, is a preferable source of borrowing as opposed to bank lines of credit, including the Lakeside Secured LOC.

133. LSC has provided an explanation of the above to DTCC in its July 30, 2021 and August 5, 2021 letters. *See* Ex. 41 (July 30, 2021 LSC Letter); Ex. 44 (August 5, 2021 LSC Letter).

134. The statement that NSCC and DTC have not been able to ascertain whether stock loan provides significant incremental liquidity to LSC is remarkable, because all stock loans are made through DTC. When a stock is lent out, the lender delivers the stock to the borrower by means of a DTC delivery order versus payment with a "Reason Code 10." When a loan is returned from the borrower to the lender, a delivery order is issued to DTC with a "Reason Code 20." Moreover, DTC accurately tracks outstanding loans, and when there is a dividend, DTC debits the borrower and credits the lender. DTC has one of the most sophisticated systems in the world to keep track of stock loans, and the statement that the Staff cannot to ascertain whether stock loans provides significant incremental liquidity to LSC is the result of a failure to communicate with the proper professionals within DTCC.

Ground 7

Pursuant to [the December 2019 FINRA Order], [LSC] was suspended from selling or accepting for deposit any microcap security until it certified to FINRA that it had implemented the recommendations of an [Independent Consultant], who was required to conduct a comprehensive review of [LSC/s] supervisory system and its compliance with anti-money laundering and Section 5 of the Securities Act of 1933 obligations in connection

with microcap stock trading. See Ex. 53 (October 26 NSCC Notice) at 4; Ex. 52 (October 26 DTC Notice) at 3.

135. As described above, *supra* at ¶ 92, under the terms of the December 2019 FINRA Order, LSC was temporarily suspended from selling or accepting for deposit microcap securities until it certified to FINRA that it had implemented the recommendations of BRG, the Independent Consultant retained under the Order. As described in more detail below, however, LSC complied with its obligations under the December 2019 FINRA Order and has not been subject to the suspension since early February 2020. *See infra* at ¶ 168.

Ground 8

Although [LSC] submitted an implementation report and certified that it had remediated all ninety-eight of the [Independent] Consultant's findings, [the Final Report] indicated that [LSC] had not remediated the identified deficiencies and that the actions taken by [LSC] were not sufficiently compliant with the FINRA Order. The [Independent] Consultant also recommended that [LSC] voluntarily reimpose and maintain indefinitely the suspension of its microcap business that was set forth in the FINRA Order. [LSC's] failure to remediate widespread internal control deficiencies, as reported in the Consultant Final Report, undermines DTC's [and NSCC's] confidence in [LSC] ability to comply with their financial and clearance and settlement obligations and to satisfy all the qualifications of DTC [and NSCC] membership. See Ex. 53 (October 26 NSCC Notice) at 4; Ex. 52 (October 26 DTC Notice) at 3.

136. As an initial matter, the fact that the Independent Consultant made recommendations does not mean that he identified any deficiencies. He simply made recommendations which, in his opinion, could strengthen LSC's procedures and internal controls. LSC strenuously objects to DTCC's claim that LSC "fail[ed] to remediate widespread internal control deficiencies" identified in the BRG Final Report. DTCC has not engaged in any independent analysis of LSC's internal controls. DTCC's reliance on the BRG Final Report and its purported findings and recommendations, many of which are contrary to the findings of the Independent Monitor, and to which LSC has objected and is currently under review by FINRA, is misplaced and inappropriate.

137. LSC disputes the findings in the BRG Final Report and believes that it contains many material inaccuracies. Moreover, the rushed and incomplete manner in which the BRG Final Report was prepared was deeply flawed and undermines its findings. The report was prepared without the appropriate input of LSC, without the review of relevant materials, and without any onsite visits or meetings with relevant LSC employees.

138. It is important to note that the majority of the observations in the BRG Final Report relate to due diligence regarding client onboarding, post-trade exception reporting and suggested improvements in the Firm's compliance documentation. Notably, there is nothing in the BRG Final Report that goes to LSC's ability to comply with its financial and clearance and settlement obligations or otherwise with respect to its ability to satisfy the qualifications of its DTC and NSCC memberships.

139. Moreover, DTCC is well aware, but fails to acknowledge that LSC filed significant objections to the BRG Final Report with FINRA (Ex. 24 (May 19, 2021 Tannenbaum Helpert Syracuse & Hirschtitt letter to FINRA)), and FINRA is in the process of reviewing those objections and the findings of the BRG Final Report. In that regard, FINRA served 8210 requests MLSC, and I was examined on-the-record for two days in mid-December.

140. In addition, DTCC also fails to mention that the BRG Final Report is, in many important respects, contrary to the multiple reports filed by Optima, the Independent Monitor retained by LSC under the October 2019 SEC Order. And, notably, the Optima reports are more relevant than the Final BRG Report with respect to DTCC's concerns about the liquidity and capital of LSC and its financial and clearance and settlement obligations.

141. As an initial matter, DTCC has not made inquiries with respect to LSC's internal controls or, on information and belief, conducted any independent review or analysis of

those controls. Instead, it uncritically relies on the BRG Report, a report which DTCC knows is the subject of objections and is currently under review by FINRA. *See* Ex. 27 (June 2021 LSC letter to Barry Groveman, DTCC).

142. While it is beyond the scope of this proceeding to delve into the many problems with the BRG Final Report, since DTCC purports to rely on that report as grounds for ceasing to act for LSC, it is important for the Hearing Panel to understand at a high level the depth and scope of LSC's objections to the BRG Final Report.

143. Over the course of five weeks following its retention by LSC, BRG prepared and submitted on February 4, 2020 its Initial Report, making 98 recommendations with respect to how LSC should modify its processes, controls, policies, systems, procedures and training to manage its regulatory and other risks concerning the adequacy of its supervisory system and its compliance with AML rules and other requirements in the December 2019 FINRA Order. *See* Ex. 8 (BRG Initial Report). To be clear, while the BRG Initial Report made 98 recommendations, the significant majority of them were minor or ministerial in nature (*e.g.*, revising Written Supervisory Procedures (“WSPs”) to conform with actual practices), and BRG did not overtly criticize any of LSC's processes or identify any significant issues.

144. In preparing the BRG Initial Report, Mr. Mirkin spent a number of days on site at LSC's offices and met with me as well as, I understand, Mr. Tabak (LSC's CCO), Mr. Shapiro (LSC's then Senior Compliance Officer), Ramute Zukas (LSC's New Accounts & Deposit Review Specialist), and Ms. Jones (LSC's then-Chief Financial Officer). BRG also reviewed extensive books and records of LSC provided in response to BRG's requests. *See* Ex. 8 (BRG Initial Report) at 49-50.

145. LSC fully cooperated with Mr. Mirkin in connection with the preparation of the BRG Initial Report, and there is nothing in the BRG Initial Report that suggests otherwise.

146. LSC was, and continues to be, committed to addressing the historical concerns raised about its microcap securities business and has devoted extensive resources to aggressively, and I believe, successfully, address those concerns. In that regard, following the issuance of the BRG Initial Report, LSC implemented the recommendations in the Initial Report or otherwise confirmed that LSC was in compliance with the recommendations and certified as much. *See* Ex. 9 (LSC Implementation Report); Ex. 32 (February 10, 2020 LSC Certification).

147. After the submission of LSC's Implementation Report, BRG was to conduct a follow-up review and issue a Final Report addressing LSC's implementation of the recommendations described in the LSC Implementation Report by no later than December 20, 2020. *See* Ex. 5 (December 2019 FINRA Order) at 34.

148. The preparation of the BRG Initial Report had been a relatively quick (the Initial Report was prepared in just five weeks), efficient and collaborative process, and LSC hoped that would be the case with respect to the BRG Final Report. Unfortunately, that was not the case.

149. For substantial periods of time, Mr. Mirkin either did not respond, or would take weeks to respond, to LSC's efforts to provide him with information and materials concerning the implementation of the recommendations in the BRG Initial Report. The first sign of trouble in that regard was when LSC uploaded materials related to the BRG Implementation Report to Mr. Mirkin in June 2020. He responded some two months later, in mid-August, advising that he was having problems accessing the materials, and was struggling

to resolve those technical problems. I came to learn during this process that Mr. Mirkin was working remotely during the time he was preparing the Final Report and refused to visit BRG's offices to review documents and information.

150. Furthermore, unlike the BRG Initial Report which states that Mr. Mirkin met with a number of LSC personnel (*see* Ex. 8 (BRG Initial Report) at 49), in connection with the BRG Final Report, Mr. Mirkin declined to visit LSC's offices to review materials or to interview LSC personnel, even by conference call or videoconference.

151. Mr. Mirkin admitted to me and others at LSC that he did not have adequate remote technology to receive and review the voluminous materials LSC provided to him and that would have been necessary for him to adequately evaluate the BRG Implementation Report and prepare the BRG Final Report. Moreover, despite our urging, BRG failed to take steps to address the significant impediments posed by Mr. Mirkin's offsite working, and it was not until March 17, 2021, less than a month before the BRG Final Report was submitted, that BRG was able to facilitate a secure information transfer and Mr. Mirkin was able to receive substantial reams of relevant materials from LSC. Troublingly, two weeks before that secured transfer had been resolved and Mr. Mirkin was able to access the materials, on or about March 2, 2021, Mr. Mirkin told FINRA that the Final Report was largely completed, subject to some "blanks that need to be filled in," suggesting that he largely prepared the report without the benefit of the materials provided by LSC.

152. The BRG Final Report references that on April 8, 2021 – eleven days before the extended deadline for the submission of the Final Report – Mr. Mirkin issued to LSC twenty-five requests for information, and that he had additional questions for LSC. *See* Ex. 20 (BRG Final Report) at 5-7. Nonetheless, he admits that despite my offering, he refused to speak

to me and did not ask all the questions he wanted to ask to reach his conclusions because he believed it would be “futile.” *See id.* at 7.

153. Because of the delays caused by his remote working and technology problems, as well as his falling ill in February 2021, Mr. Mirkin had been given two extensions of the initial December 20, 2020 deadline to file the BRG Final Report, and FINRA had advised that after extending the filing deadline to April 19, 2021, it would not extend the deadline further. Accordingly, while Mr. Mirkin says he did not follow up on his requests for information to LSC because he did not think we would be responsive (*id.* at 7), the truth appears to be that he ran out of time, short cut the process and rushed to finalize the BRG Final Report.

154. Many of the deficiencies in the BRG Final Report are apparent on its face. For example, the BRG Final Report acknowledges that BRG did not perform a detailed review of all aspects of LSC’s microcap securities compliance program (*see id.* at 3); yet Mr. Mirkin goes out of his way to criticize that program. *See id.* at 13-17. Mr. Mirkin shrugs off accountability for performing a thorough review of LSC’s microcap securities compliance program, curiously saying that the analysis would take too long. *Id.* at 3. In addition, the BRG Final Report incorrectly speculated that LSC did not implement his recommendations, while expending no effort to ascertain what LSC had in fact done.

155. The BRG Final Report lacks any specificity as to what was provided to Mr. Mirkin and the basis for his conclusions and does not detail the steps he performed to reach his conclusions. That is perhaps because doing so would have made obvious that he did little document review, no interviews, no on-site inspections and no testing of the systems he criticized.

156. The BRG Final Report contains speculative language (e.g., “Lek *appears* to have done nothing to address its inability to perform necessary due diligence as to its microcap securities business” (*id.* at 14); “Charles Lek *appears* to be the sole designated microcap securities exception report reviewer” (*id.* at 18); “Lek *appears* to have disregarded FINRA’s concerns...” (*id.* at 22); “Mr. Lek *seems* to run the sales side of the microcap securities business...” (*id.* at 13)) regarding its findings, which further demonstrates the lack of a thorough investigation by Mr. Mirkin. *See also* Ex. 34 (LSC July 1, 2021 Letter to FINRA). While highlighting certain recommendations made in the BRG Initial Report that Mr. Mirkin believes had not been met, the BRG Final Report does not map the LSC Implementation Report with the status of the recommendations.

157. Another example of the insufficiency of the BRG Final Report is its recommendation to replace Mr. Tabak as CCO. The BRG Initial Report had raised concerns about the extent of Mr. Tabak’s involvement in supervising LSC’s microcap securities business and recommended that LSC consider hiring a new CCO, although Mr. Mirkin acknowledged that Mr. Tabak was a highly accomplished securities professional with over 40 years of experience in the securities industry. Ex. 8 (BRG Initial Report) at 45.

158. Mr. Mirkin asserts in the BRG Final Report that Mr. Tabak “did not appear to perform any compliance functions,” because Mr. Tabak’s “time in the office was spent at his desk performing other tasks.” Ex. 20 (BRG Final Report) at 4. Mr. Mirkin states further that he is concerned about the state of LSC’s compliance program and LSC’s compliance program as a whole. *Id.* at 3.

159. However, Mr. Mirkin did not even talk with Mr. Tabak in the fifteen months following his preparation of the BRG Initial Report, much less visit LSC’s offices and

have the opportunity to observe Mr. Tabak. Any conclusions about what work Mr. Tabak appeared to be doing and the state of LSC's compliance program, therefore, could not have been based on conversations or observations in the fifteen months between the BRG Initial Report and BRG Final Report, and Mr. Mirkin could not have reached an informed and reasoned view as to whether Mr. Tabak was performing his compliance functions.

160. Mr. Mirkin's "observations" and recommendations with respect to Mr. Tabak and LSC's compliance program, moreover, are in contrast to the views of Optima, both with respect of Mr. Tabak and the rest of LSC's compliance department. While Optima encouraged Mr. Tabak to take on a more active role, it found that he demonstrated a willingness to do so by attending the various meetings between LSC and Optima and ensuring that Optima's recommendations were implemented. Optima otherwise found LSC's compliance department covered key staffing issues (Ex. 13 (December 2020 Optima Report) at 23, 25), and while there was room for improvement, it found a "culture of compliance" at LSC, Ex. 10 (April 2020 Optima Report) at 15, 17, and that LSC "takes the Monitorship, and its various requirements, very seriously." Ex. 13, at 23.

161. The April 2021 Optima Report also commented on Mr. Tabak's performance as Chief Compliance Officer, stating, *inter alia*, that:

The Firm [*i.e.*, LSC] and the Monitor will continue to assess the effectiveness of the Compliance Program and the supervision and Compliance responsibilities of Mr. Tabak as the Chief Compliance Officer and Supervisory Principal of the Firm. At this point, *there is no immediate cause for concern as it relates to Mr. Tabak's ability to oversee the compliance program and Mr. Tabak*, and his team have proven to be responsive and again, we have appreciated his involvement and oversight. See Ex. 21(April 2021 Optima Report) at 27-28. (emphasis added).

* * *

Ongoing regular meetings with the Firm, including Mr. Tabak, are required by the Monitor and the entire compliance team at LSC have had near perfect

attendance during the Review Period for the Fourth 120-day report. *Id.* at 28.

* * *

As discussed previously, Mr. Tabak, Mr. Shapiro and Ms. Quintana understand and implement each of the recommendations of the Monitor when asked. Finally, *Mr. Tabak continues to understand his requirements as the Chief Compliance Officer and Supervisor of the Firm with regard to both his role at LSC and his role with regard to the Monitorship. Id.* (emphasis added).

* * *

Mr. Tabak was aware of and involved in, each of the ongoing meetings and knowledgeable of each of the Monitor's requests. The Monitor cannot overstate the importance of this fact in the ongoing success of the compliance program for LSC. *Id.* at 29.

162. In its August 2021 Report, Optima found LSC's compliance department was running smoothly. The report stated that Mr. Tabak was present and involved in the bi-monthly meetings with LSC and Optima and led the calls from the LSC side. Mr. Tabak's increased involvement was one of Optima's ongoing recommendations, and Optima was of the view that he had stepped up in that regard. Ex. 46 (August 2021 Optima Report) at 30.

163. Although BRG had been retained to perform a comprehensive review of LSC's supervisory system and its anti-money laundering (AML) and Section 5 obligations in connection with stock trading in low priced securities, Optima performed a similar review. Ex. 5 (FINRA Order) at 34-35. Optima assessed the sufficiency and reasonableness of LSC's controls and procedures for preventing manipulative trading and other market manipulation. Ex. 3 (October 2019 Consent Order, Appendix B) at 5. Similar to BRG, most of Optima's recommendations involved updating LSC's WSP and increasing supervisory review and documentation.

164. While BRG wrote in the Final Report that LSC inadequately implemented its recommendations, including failing to appropriately update its WSP and exception report procedures, Optima came to the opposite conclusion, finding that LSC appropriately updated its WSP for a supervisory review of all exception reports and updated its customer onboarding procedures. Ex. 12 (August 2020 Optima Report) at 37-43, 51.

165. I strenuously deny the allegation in the BRG Final Report that LSC did not cooperate with BRG's review. LSC continuously attempted to contact Mr. Mirkin in an attempt to solve his accessibility problems due to his working remotely and, on many occasions, Mr. Mirkin simply failed to respond at all. In fact, at one point, I became so frustrated with Mr. Mirkin's non-responsiveness that I reached out to BRG's in-house counsel, Kate Koppenhoefer, in an effort to get Mr. Mirkin to respond to our inquiries. *See* Ex. 24 (May 19, 2021 Tannenbaum Helpert Syracuse & Hirschtritt letter to FINRA). I also reached out to FINRA to express my frustration about my inability to contact Mr. Mirkin. *See id.*

166. Tellingly, contrary to Mr. Mirkin's claims that LSC was uncooperative and failed to provide him with information requested, Optima describes LSC's responsiveness and willingness to provide information. For example, the August 2020 Optima Report notes that LSC was prompt with responses and regularly communicated with Optima. *See* Ex. 12 (August 2020 Optima Report) at 38, 40. The August 2021 Optima Report specifically states that Optima continued to have regular interactions with LSC management and compliance staff, that Optima's meetings with LSC were "impactful" and "productive," and that LSC continued to provide necessary documents requested by Optima. Ex. 46 (August 2021 Optima Report) at 34-35.

167. Also, contrary to the suggestion in the BRG Final Report that LSC resisted implementing the recommendations in the BRG Initial Report, Optima found that LSC was cooperative and continuously worked to implement its recommendations. *See, e.g.*, Ex. 10 (April 2020 Optima Report) at 37, 59 (implementing recommendations regarding documenting supervisory sign-offs for exception reports, indicating that it takes its review for red flags seriously); Ex. 12 (August 2020 Optima Report) at 23-24, 37, 40 (LSC appropriately updating its customer onboarding procedures), 51 (compliance team working to ensure that every exception report is systematically reviewed and documented); Ex. 13 (December 2020 Optima Report) at 25-27; Ex. 21 (April 2021 Optima Report) at 35-37; Ex. 46 (August 2021 Optima Report) at 33-37. In fact, there is no indication in any of the Optima reports that LSC resisted implementing its recommendations, again, in contrast to the BRG Final Report.

168. The DTCC Notices reference the “recommendation” in the BRG Final Report that LSC voluntarily reimpose and maintain indefinitely the Temporary Microcap Business Suspension imposed in the December 2019 FINRA Order, and lifted on February 2020, when LSC submitted its certification that it had implemented the recommendations in the BRG Initial Report. Ex. 32 (February 10, 2020 LSC Certification).

169. That “recommendation” by Mr. Mirkin is patently improper, as is DTCC’s reliance on it. First, LSC has complied with its obligations under the December 2019 FINRA Order and the allegation to the contrary in the BRG Initial Report is flatly wrong. Second, that “recommendation” arbitrarily seeks to reimpose a draconian sanction against LSC that is far beyond the scope of BRG’s authority as Independent Consultant under the December 2019 FINRA Order. Moreover, the recommendation is contrary to the terms of the December

2019 FINRA Order, which expressly permitted LSC to resume its microcap securities business under conditions that LSC fully satisfied.

170. Following the issuance of the BRG Final Report, LSC filed objections to it with FINRA, describing many of the issues described above. *See* Ex. 24 (May 19, 2021 Tannenbaum Helpen Syracuse & Hirschtritt letter to FINRA). On or about June 10, 2021, I also provided a copy of the BRG Final Report to Barry Groveman, Senior Credit Risk Associate at DTCC, advising DTCC of LSC's view that the BRG Final Report was inaccurate and unsupportable and that FINRA is conducting an independent review of the report. Ex. 27 (June 2021 LSC letter to Barry Groveman, DTCC).

Ground 9

[LSC] had been on notice from BMOH that it intended to terminate its relationship with [LSC] since at least October 2019. [LSC] never informed DTC about the discussions, BMOH's interim reduction of the BMOH LOC, or BMOH's decision to fully terminate the BMOH LOC. DTC eventually learned about the pending BMOH LOC termination from FINRA and OCC on or around July 16, 2021. See Ex. 52 (October 26 DTC Notice) at 4.

[LSC] had been on notice from BMOH that it intended to terminate its relationship with [LSC] since at least October 2019. In violation of [LSC's] obligations under NSCC Rule 2B, Lek never informed NSCC about the discussions, BMOH's interim reduction of the BMOH LOC, or BMOH's decision to fully terminate the BMOH LOC. NSCC eventually learned about the pending BMOH LOC termination from FINRA and OCC on or around July 16, 2021. See Ex. 53 (October 26 NSCC Notice) at 5.

171. As described above, *supra* at ¶¶ 61-73, I did not believe that BMOH actually intended to terminate its longstanding relationship with LSC in October 2019 or thereafter, until the July 8, 2021 BMOH Letter. Among other things, Eric Bellendir, the Vice President of the Financial Institutions Group at BMOH well into late 2020, assured me that BMOH did not consider LSC a credit risk and that it did not intend to terminate its relationship, and in February 2021, LSC and BMOH entered into the NCSS Letter Agreement, which contemplated extending the BMOH LOC.

172. Even when I received the July 8, 2021 BMOH Letter, I believed that the wind down of the BMOH relationship was not material given LSC's historical use of the BMOH LOC, which was done largely as an accommodation to BMOH and to help make the LSC relationship more remunerative to BMOH, and the availability to LSC of alternative sources of liquidity.

173. LSC did not believe that the matter was material in view of its minimal use of the line, especially considering that the BMOH line was mostly secured and effectively could not be applied to LSC's Required Fund Deposit. LSC's view of the BMOH LOC's immateriality was substantiated as LSC continued to operate smoothly after the BMOH LOC was terminated. Regardless, this assessment of non-materiality was probably LSC's error, and LSC accepted responsibility for it and paid a \$5000 fine to NSCC.

Ground 10

Similarly, [LSC] failed to notify DTC of the March 31, 2021 termination of the Texas Capital LOC, both before and after it occurred. [LSC] did not disclose the Texas Capital LOC until a due diligence discussion with DTC in mid-to-late May 2021. See Ex. 52 (October 26 DTC Notice) at 4.

Similarly, in violation of its obligations under NSCC Rule 2B, [LSC] failed to notify NSCC of the March 31, 2021 termination of the Texas Capital LOC, both before and after it occurred. [LSC] did not disclose the Texas Capital LOC until a due diligence discussion with NSCC in mid-to-late-May 2021. See Ex. 53 (October 26 NSCC Notice) at 5.

174. As described above, *supra* at ¶¶ 51-52, 112, LSC did not consider the termination of the Texas Capital LOC significant or material, or as creating any additional liquidity risk for LSC. The Texas Capital LOC was a secured line of credit, not available for funding LSC's NSCC funding requirements, and, in any event, was rarely utilized by LSC (the last loan under the facility was paid off in June 2020). Similar to the BMOH LOC, the termination of the Texas Capital LOC proved to have no impact on LSC's liquidity and operations. In addition, the termination of the LOC was due to Texas Capital's downsizing and

not due to any issues or concerns Texas Capital had with LSC. Again, in hindsight, LSC perhaps however should have, in any event, notified DTCC of the termination of the Texas Capital LOC.

Ground 11

Not only did [LSC] fail to affirmatively inform DTC [and NSCC] of the terminations of these lines of credit, [LSC] provided inadequate and/or misleading responses to DTC [and NSCC] over the course of several due diligence questions sent by DTC [and NSCC] between February and May 2021 relating to [LSC's] liquidity and financial condition, thereby avoiding disclosure of the situation with the lines of credit. See Ex. 53 (October 26 NSCC Notice) at 5; Ex. 52 (October 26 DTC Notice) at 4.

175. This is a broad and general allegation. Suffice to say I believe that LSC has made reasonably efforts to attempt to answer all the questions it has received from DTC and NSCC, including over the period February to May 2021 and denies that it ever knowingly attempted to mislead or provide false information to them.

Ground 12

[LSC] failed to send DTC [and NSCC] a copy of the Consultant Final Report when it was issued on April 19, 2021, and only provided it to DTC[and NSCC] in June 2021 after numerous follow-up requests by DTC [and NSCC]. See Ex. 53 (October 26 NSCC Notice) at 5; Ex. 52 (October 26 DTC Notice) at 4.

176. LSC did not believe that it had an affirmative obligation to provide the BRG Final Report to DTCC and was unaware that either DTC or NSCC sought to receive a copy of the Report when it was issued. Notably, as discussed above, *supra* at ¶ 138, the BRG Final Report did not address LSC's ability to comply with its financial and clearance and settlement obligations or to satisfy its qualifications to be a member of DTC or NSCC. Therefore, LSC did not believe that the BRG Final Report included material information that it would be required to provide to DTCC. This is particularly true given the fact that NSCC and DTC took no action at the time when the Firm agreed to the December 2019 FINRA Order,

which, among other things, implemented the Temporary Microcap Business Suspension and mandated the BRG Initial Report.

177. LSC appears to have first received a request from DTCC for the BRG Final Report on June 2, 2021 and provided a copy of the report to it on June 10, 2021. *See* Ex. 27 (June 2021 LSC letter to Barry Groveman, DTCC).

Ground 13

As required by DTC [and NSCC], on July 30, 2021, [LSC] began submitting daily liquidity reports. However, the reports did not include all of the required information, including, without limitation, total funding available, and failed to respond to questions about a liquidity stress test and presentation of a contingency. In addition, the information that [LSC] did provide in the reports was internally inconsistent, for example, by alternating between referring to the promissory note as both secured and unsecured, and did not identify the different sources of collateral that the different liquidity sources depend on. The reports, on an ongoing basis, have been deficient and fail to provide DTC [and NSCC] with an accurate picture of [LSC's] liquidity. See Ex. 53 (October 26 NSCC Notice) at 5; Ex. 52 (October 26 DTC Notice) at 5.

178. At DTCC's request, LSC began submitting daily liquidity reports on a form designed by DTCC starting from July 30, 2021. *See* Ex. 40 (July 28 Letter) at 2, 4; Ex. 41 (July 30, 2021 LSC Letter) at 3-4. The LSC daily liquidity reports were materially accurate and contained all required information. Any incomplete or inaccurate information provided in the reports was unintentional and was remedied by LSC when brought to its attention.

179. Initially, there was a typo in the report stating in the "Secured/Unsecured" column that the Lek Holdings Note was "Secured," when, in fact, it is unsecured. In the column identifying the collateral, LSC wrote "N/A," because the note was unsecured and did not require collateral. *See* Ex. 51 (September 23, 2021 LSC Letter). The unsecured nature of the Lek Holdings Note Program was extensively discussed with the Staff in a July 20 phone call, and it was explained in detail that the unsecured nature of the Note Program was its essential advantage as the proceeds of the loans would not constitute a credit

item in the reserve formula. It has been abundantly clear that the promissory note in question was unsecured. LSC also provided copies of the documentation for the Leks Holdings Note Program. Exs. 18-19, 22. Paragraph 6 of each note reads as follows: “6. Unsecured Note: This Note is unsecured.” *Id.*

180. On August 2, 2021, LSC’s CFO Kristopher Minogue had a number of phone conversations with DTCC’s Barry Groveman. Mr. Groveman articulated that DTCC wanted the liquidity forms filled out slightly differently. On August 3, 2021, LSC received a letter from DTCC, requesting that the daily reports be amended, as indicated by Mr. Groveman. Ex. 14 (DTCC August 3, 2021 Letter). On August 4, 2021, LSC began sending amended daily reports pursuant to DTCC’s request. On September 13, 2021, LSC received a letter from DTCC asking the Firm to add a line to DTCC’s form to reflect the total funding available. Ex. 47 (September 13, 2021 DTCC Letter). The Firm complied, and since then, DTCC has not asked for other changes to the form. *See* Ex. 51 (September 23, 2021 LSC Letter); Ex. 49 (September 23, 2021 Daily Liquidity Report).

Ground 14

From mid-July 2021 through September 2021, NSCC [and DTC] sent a series of information requests to [LSC] regarding, among other things, (i) [LSC’s] plan for replacement funding, (ii) Lek Holdings and the \$100 million promissory note, and (iii) [LSC’s] existing and potential future sources of liquidity. In its response, [LSC] had:

Ground 14(a)

Provided information that showed \$50 million of the BMOH LOC as a source of “future” liquidity. [LSC] later acknowledged that the BMH LOC was terminating in full on October 6, 2021. See Ex. 53 (October 26 NSCC Notice) at 6; Ex. 52 (October 26 DTC Notice) at 5.

181. It is unclear to what information DTCC is referring and how DTCC suggests it was misled by LSC. The BMOH LOC was in place and an available source of liquidity for LSC until it was terminated on October 6, 2021. Accordingly, to the extent that

DTCC inquired about LSC's liquidity from "mid-July 2021 through September 2021," it was accurate to identify the BMOH LOC as an existing, or available or future source of liquidity. Moreover, for the avoidance of doubt on July 30, 2021, in response to one of the Staff's questions, the Firm responded as follows:

BMOH will not reduce our line of credit to \$4MM as of August 4, 2021. The line will stand at \$50MM. Although BMOH's letter is silent about what will happen to the line after October 6, 2021, it is reasonable to assume that the line will cease to exist as BMOH has set that as the date it will terminate the overall relationship.

See Ex. 41 (July 30, 2021 LSC Letter) at 1.

182. Moreover, DTCC was well aware in mid-July 2021 that the BMOH LOC was in the process of being wound down (see *supra* at ¶ 76), thus the suggestion that LSC was misleading them, or that they were misled, about the status of the BMOH LOC is dubious.

Ground 14(b)

Provided information that showed a new "future" source of liquidity in \$96 million in unsecured notes. LSC later acknowledged that it was referring to the \$100 million promissory note from Lek Holdings, and was not referring to a new source of liquidity. See Ex. 53 (October 26 NSCC Notice) at 5; Ex. 52 (October 26 DTC Notice) at 5.

183. LSC has never mentioned more than one promissory note program involving Lek Holdings. There should be no confusion in this regard. It is unclear in what context alleges it was being misled, and again, LSC strenuously disputes that it ever knowingly or intentionally misled or provided false information to DTC or NSCC. The fact that there are a number of different promissory notes, executed to represent different draw-downs under the Lek Holdings Note Program should not lead to the conclusion that the total amount of the program should be computed by summing the principal amount of each draw-down and ignoring repayments.

Ground 14(c)

Indicated to DTC [and NSCC] that Investors Bank intended to provide [LSC] with a \$20 million line of credit. In response to follow-up from DTC [and NSCC], [LSC] acknowledged that Investors Bank had only expressed an “interest” in providing [LSC] with a line of credit. To date, to DTC’s [and NSCC’s] knowledge, there is no \$20 million line of credit from Investors Bank. See Ex. 53 (October 26 NSCC Notice) at 6; Ex. 52 (October 26 DTC Notice) at 5.

184. In its July 26, 2021 letter to DTCC, LSC stated that “we are informed by Investor’s Bank that they intend to provide us with a \$20MM line of credit.” Ex. 39 (July 26 Letter) at 2. At the time I wrote that letter, that was LSC’s understanding. On July 23, 2021, Joseph DeVito, Senior Vice President of Investors Bank, informed Kristopher Minogue of LSC, that Investors Bank had “submitted the underwriting to credit on [July 21, 2021].” Mr. DeVito further stated that once Investors Bank gets credit on board, it will need another approval as the line of credit will be a new facility structure for Investors Bank and that he will provide another update as the process moves along. Ex. 31 (July 23, 2021 Investors Bank Email).

185. While Investors Bank has not yet provided LSC with a line of credit, in no way was the July 26 Letter misleading and the fact that the Investors Bank line has not yet come to fruition does not make my letter inaccurate. Investors Bank is in merger negotiations with Citizen’s Bank which has slowed down Investors Bank’s appetite for new business. Moreover, as already explained, LSC has significantly more secured credit facilities than it needs, and accordingly, LSC had not pushed Investors Bank on this issue.

Ground 14(d)

Indicated to DTC [and NSCC] that Lakeside was working with a number of banks to create a large syndicated loan facility for [LSC’s] benefit. In response to follow-up by DTC [and NSCC], [LSC] acknowledged that “none of this is certain to transpire.” To date, to DTC’s knowledge, there is no large syndicated loan facility for [LSC’s] benefit. See Ex. 53 (October 26 NSCC Notice) at 6; Ex. 52 (October 26 DTC Notice) at 5.

186. The discussed syndicated facility has not yet been established, but that does not make the statement false or misleading when I included it in the July 26 Letter.

Lakeside has indicated to me that it has arranged syndicated facilities for other customers and that they would be happy to do this for LSC. However, LSC is not pushing Lakeside, because as explained above, LSC has adequate secured lines of credit.

Ground 14(e)

Failed to fully respond to DTC [and NSCC] requests relating to the Lakeside LOC, particularly in connection with collateral that would support [LSC's] borrowings. See Ex. 53 (October 26 NSCC Notice) at 6; Ex. 52 (October 26 DTC Notice) at 5.

187. DTCC first asked for the Lakeside loan documents in its letter dated July 28, 2021: "Lek has not yet provided DTCC with documentation (including all terms and conditions of the facility(ies)) from Lakeside Bank of the increase in the facility to \$30MM." Ex. 40 (July 28 Letter) at 2. However, this was the first time LSC became aware that DTCC wanted this documentation, and it was promptly provided on July 30, 2021. Ex. 41 (July 30, 2021 LSC Letter) at 2. When the Staff had questions about the collateral that would support LSC's borrowings, LSC provided explanations and relevant documentation in its August 5, 2021 (Ex. 44) and September 23, 2021 (Ex. 51) responses referenced above, *supra* at ¶ 122.

Ground 14(f)

Failed to substantively respond to DTC's [and NSCC's] most recent letter to [LSC] on September 13, 2021, which followed up on DTC's [and NSCC's] previous unanswered and partially answered requests, including requests with respect to information about the promissory note, Lek Holdings, as well as a potential Investors Bank line of credit and syndicated loan that was referenced by [LSC] in several of its responses. The letter also identified and requested remediation of the deficiencies in [LSC's] daily liquidity reports. See Ex. 53 (October 26 NSCC Notice) at 6; Ex. 52 (October 26 DTC Notice) at 5.

188. LSC responded to DTCC's September 13, 2021 letter on September 23, 2021, by providing information to through a portal provided to LSC staff by DTCC and

provided an item-by-item response for each of the outstanding requests. *See* Ex. 51 (September 23, 2021 LSC Letter). There were no subsequent follow-up requests from DTCC.

Dated this 27th day of December 2021

/s/ Charles F. Lek

Charles F. Lek

SK 07392 0001 9083855

DTCC Attachment 13

AFFIDAVIT OF EMRE CARR, PH.D.

December 27, 2021

Contents

I. EXPERT QUALIFICATIONS	3
II. ASSIGNMENT	6
III. SUMMARY OF OPINIONS	7
IV. BACKGROUND: RISKS TO BROKERS	11
A. Margin Risk	12
B. Operational Risks	13
C. Metrics to Manage and Measure Broker Risk.....	13
i) Brokers Face Capital Requirements.....	14
ii) Brokers Have Liquidity Requirements	14
iii) Brokers Must Make Deposits with Clearing Organizations	16
V. LSC'S SETTLEMENT WITH THE SEC	17
VI. LSC HAS MET ALL CAPITAL AND LIQUIDITY REQUIREMENTS.....	18
A. LSC Has Adequate Capital	20
B. LSC Has Met All NSCC Deposit Requirements.....	21
VII. Analysis of Other DTCC's Concerns Regarding Capital and Liquidity	30
A. LSC Has Adequate Cash on its Balance Sheet	30
B. LSC Has Adequate Access to Liquidity	31
C. LSC Has Sufficient Collateral to Utilize the Lakeside LOC	33
D. LSC Has Access to Significant Levels of Liquidity Through Its Promissory Notes Program.....	35
E. Securities Lending Lines Provide Significant Incremental Liquidity to LSC 40	
VIII. Conclusion.....	42

I. EXPERT QUALIFICATIONS

1. I am a Senior Managing Director in the Forensic and Litigation Services Practice at FTI Consulting, Inc. (“FTI”). FTI is a multi-discipline consulting firm that provides a variety of financial advisory services to corporate clients in the U.S. and abroad. The Forensic and Litigation Services Practice within FTI, of which I am a part, specializes in providing financial, accounting, economic, and investigative consulting services to clients.

2. I have consulted in engagements that involve public and private companies, investment companies, banks, securities and commodities brokers and dealers, insurance companies, and financial regulators in the U.S. and elsewhere. The subjects of these engagements included financial regulations, market manipulation, structured finance, securities and commodities trading, clearing and execution, capital and liquidity requirements, investment advisory, corporate internal controls, corporate governance, and valuation.

3. Previously, I was a Senior Financial Economist at the Division of Risk, Strategy, and Financial Innovation (“RiskFin”) of the SEC, later renamed the Division of Economic and Risk Analysis. RiskFin was created as the agency’s “think tank” to provide sophisticated, interdisciplinary analysis and economic advice across the entire spectrum of SEC activities, including policymaking, rulemaking, enforcement, and examinations. As a Senior Financial Economist, I conducted economic analyses for the design of SEC rules to govern, security-based swaps clearing, execution, and reporting, conflicts of interest in security-based swap

entities, asset-backed securities issuance and reporting, beneficial ownership reporting, central counterparties, securities offerings, possible adoption of the international financial reporting standards in the U.S., restrictions on proprietary trading by commercial banks, resolution plans, and required disclosures of off-balance sheet exposures and liquidity, and executive compensation. I have statistically analyzed over-the-counter derivatives activities of security-based swap dealers, and banks' securitization of financial assets to inform the SEC's rulemaking process. I have reviewed rule proposals by self-regulatory organizations (SROs) including certain subsidiaries of the DTCC.

4. I have participated in enforcement investigations and compliance inspections related to equities, fixed income securities, swaps, other derivatives, and structured financial products. The subjects of these investigations included global banks headquartered in the U.S., Canada, and Europe, insurance companies, broker-dealers, and investment firms.

5. I have consulted in several engagements that involved risk and liquidity management, alleged fraud, customer cash handling, trading supervision at securities and commodities broker-dealers, structured finance activities, alleged accounting fraud, alleged market manipulation, corporate internal controls, and valuations of investment entities. Some of these engagements involved assessing the performance of regulators.

6. I have taught graduate-level courses on financial statement analysis for valuation and credit decisions, corporate finance, and accounting at the University

of Maryland, Columbia University, University of Southern California, University of Toronto, and Northwestern University.

7. I earned my Ph.D. degree in Accounting Information and Management at the Kellogg School of Management at Northwestern University. My Ph.D. dissertation examined the use of structured finance transactions for regulatory capital and earnings management in banking. In addition, I completed all coursework for the Ph.D. degree in finance (but did not complete a dissertation).

8. I earned my MBA degree with a concentration in finance from the University of Southern California. I am a Certified Financial Analyst (CFA) charterholder, granted by the CFA Institute. The CFA Institute is the premier global association for investment management professionals and represents the industry gold standard for effective and ethical investment management practices.¹

9. My curriculum vitae, including a list of all publications authored in the past ten years and the cases at which I have testified as an expert during the previous four years, are attached as **Exhibit 1**.

10. My business address is FTI Consulting, Inc., 1166 6th Avenue, Manhattan, New York 10036. FTI is being compensated for my services in this action at an hourly rate of \$875. Neither I nor FTI has any financial interest in the outcome of this matter. In addition, I was assisted by FTI staff who worked under my direction and who performed research and other tasks.

¹ <https://www.cfainstitute.org/en/programs>.

II. ASSIGNMENT

11. I understand that the Depository Trust Corporation (“DTC”) and National Securities Clearing Corporation (“NSCC”) (together “the DTCC” or “the Corporation”) have provided notices to cease to act for Lek Securities Corporation (“Lek”, “LSC” or “the Firm”), because LSC “is in such financial or operating difficulty, that the Corporation determined, in its discretion, that such action is necessary for the protection of the Corporation, the participants, creditors or investors.”²

12. I have been retained by counsel for LSC to review the financial condition and liquidity of LSC and provide my opinion on the DTC’s and NSCC’s determination that LSC’s capital and liquidity position is weak or inadequate. I understand that DTCC has also made determinations related to LSC’s internal controls and communications with DTCC. I have not been asked to respond to those determinations. Further, I understand that any expert testimony, including this Affidavit, may not challenge the legitimacy or reasonableness of NSCC’s or DTC’s Rules or Procedures and should be based only on information available at the time of the initial determinations made by NSCC and DTC.³

13. This Affidavit is based on the information I have reviewed as of the date of this Affidavit, all of which was available on or before October 26, 2021. I

² DTC Notice to Lek and NSCC Notice to Lek dated October 26, 2021.

³ Hearing Panel Decision dated December 14, 2021.

respectfully reserve the right to supplement my analysis if new information comes to light.

III. SUMMARY OF OPINIONS

14. As I explain further below, LSC is one of the last remaining agency brokers⁴ whose risks come almost entirely from customers' trades that are first and foremost supported by the equity and securities in those customers' accounts. Since the U.S. has strict margin rules and LSC has risk guidelines to match and exceed those rules, LSC has residual risk from those accounts only in the event that customers' equity is depleted. Moreover, the DTCC is protected by Required Fund Deposits, calculated first on the basis of sophisticated statistical models, then on various additional components—such as the Illiquid Securities⁵ component under which it is assumed that every sub-penny share has a price of one penny and the ECP component which rises rapidly as LSC's Illiquid Securities component increases.⁶ Since LSC's capital and liquidity positions have met and exceeded those total Required Fund Deposits, they have proved to be clearly sufficient for LSC's underlying activities. As a result, in my opinion, LSC does not present a heightened risk to the DTCC, or to participants, creditors or investors.

⁴ That is also a clearing broker.

⁵ The term illiquid securities is used within the meaning of NSCC's Rules and Procedures, Procedure XV. Clearing Fund Formula and Other Matters.

⁶ ECP is the product of the Calculated Net Amount and Excess Capital Ratio. These terms are defined later in the text. The relationship between LSC's Required Fund Deposit, Illiquid Securities Component and ECP are also analyzed in detail.

15. In its letters of October 26, 2021, DTCC made several determinations in connection with LSC's capital and liquidity. Below I describe these determinations and my replies.

- "Lek has ENC [Excess Net Capital] of \$11.1MM (as of September 24, 2021), which, although sufficient to meet the minimum capital requirement at NSCC, NSCC believes is inadequate to support the level of risk activity conducted by Lek."

Reply: I have analyzed the risks to which LSC is exposed due to its activity as an agency broker. As explained in more detail below, LSC has significantly more capital than is required under SEC rules and DTCC procedures; it has never failed to meet NSCC's Clearing Fund Deposits Requirements and never failed to settle its DTC obligations and after meeting these requirements, LSC has always had remaining sources of additional liquidity.

- "Lek has minimal cash on its balance sheet - non-segregated cash typically represents only a low percentage of assets, which increases its dependance on external credit for liquidity."

Reply: Lek has a level of cash as a percentage of assets that is consistent with that of other NSCC member brokers and consistent with the level needed by a well-capitalized broker.

- "Lek's liquidity position has been compromised by Bank of Montreal Harris N.A.'s ("BMOH") termination of Lek's \$75 million line of credit ("BMOH LOC") as of October 6, 2021, and the termination of Lek's \$25 million line of credit ("Texas Capital LOC") with Texas Capital Bank ("Texas Capital") on March 31, 2021."

Reply: The BMOH provided both secured and unsecured lines of credit ("LOC") and the Texas Capital LOC was a secured LOC. The unsecured LOC was used primarily to fund the NSCC Required Fund Deposit. LSC has a new unsecured Lakeside line

of credit (\$10 million) and in February 2021 established a new program, the Promissory Notes Program (up to \$100 million), that provides it with a level of funds that closely tracks its unsecured liquidity needs. Thus, LSC had larger unsecured financing sources as of October 26, 2021 than it did in 2020 while the BMOH unsecured line was available.

The secured portion of the BMOH and Texas Capital LOC could be used only to provide customer margin loans and other debit items in the SEC Rule 15c3-3 reserve formula. LSC has sufficient secured borrowing facilities both from the new Lakeside secured LOC and from its securities lending facilities.

- “Lek has a credit facility with Lakeside Bank (“Lakeside”), consisting of a \$20 million line of credit and a \$10 million line of credit (collectively, the “Lakeside LOC”). In violation of the NSCC Rules, Lek has not fully responded to NSCC’s inquiries in respect of the Lakeside LOC and has not been forthcoming about what collateral it would use to support each part of the line of credit and whether that same collateral is also being pledged to support any other liquidity sources. Accordingly, NSCC believes that there is a high probability that Lek does not have enough collateral to utilize the full Lakeside LOC.”

Reply: I was not asked to analyze LSC’s communications with DTCC, but I did review LSC’s collateral for the Lakeside LOC as well as its other LOCs and found it to be more than adequate to meet LSC’s financing needs for margin loans under the SEC’s customer protection framework. Since LSC’ \$20 million Lakeside Secured LOC is secured by the hypothecation of customer securities, while the \$10 million Lakeside Unsecured LOC is backed by LSC’s receivable at NSCC, the same collateral is not being pledged.⁷

⁷ Affidavit of Charlie Lek.

- “Lek has informed NSCC that it has a \$100 million promissory note from its parent, Lek Securities Holdings Limited (“Lek Holdings”). However, Lek has repeatedly failed to provide NSCC with requested information, including, but not limited to, audited financials of Lek Holdings and details about its financial relationship with Lek. Accordingly, NSCC does not have enough information to assess the reliability and sufficiency of the \$100 million promissory note, and therefore NSCC cannot responsibly consider the promissory note as a reliable source of liquidity for Lek.”

Reply: The Promissory Note Program is the mechanism by which Lek primarily finances the spikes in the NSCC Required Fund Deposit. As I explain below, spikes in the Required Fund Deposit result primarily from increases in the trading of illiquid securities. Lek does not permit such trading activity (in illiquid securities) unless Lek has the liquidity to meet its expected NSCC Required Fund Deposit and the customers engaging in those trades provide the necessary liquidity through the Promissory Notes Program prior to placing their trades. Below I explain how this program works and show that it enables LSC to manage appropriately the risks from trading securities that result in large NSCC Required Fund Deposits.

- “Lek has told NSCC that it has access to certain uncommitted stock loan/borrowing arrangements, however, NSCC has not been able to ascertain whether these provide significant incremental liquidity to Lek.”

Reply: LSC utilizes its stock lending facilities to finance customer debit balances and I have found that the amount of collateral that LSC has meets its secured borrowing needs used to finance customer margin loans under the SEC’s customer protection framework.

Below I explain my opinions in more detail.

IV. BACKGROUND: RISKS TO BROKERS

16. The Securities Exchange Act of 1934 (“the Exchange Act”) defines a “broker” as “any person engaged in the business of effecting transactions in securities for the account of others,” and a “dealer” as “any person engaged in the business of buying and selling securities for such person’s own account through a broker or otherwise.” Many brokerage firms function as both brokers and dealers (as “broker-dealers”). LSC does not: It acts only as a broker and does not buy and sell securities for its own account other than those incidental to its operations.

17. When a broker trades for its own account (also known as ‘proprietary trading’), it becomes significantly riskier.⁸ Because it does not trade for its own account, LSC is substantially less risky than many brokerage firms. Moreover, LSC is subject to the customary safeguards that protect customer assets of brokerage firms. As FINRA notes, in virtually all cases, when a brokerage firm ceases to operate, customer assets are safe.⁹

18. An agency broker is, however, exposed to some risks—primarily margin risk and operational risk. I discuss these risks and the metrics and methods for the management of these risks next.

⁸ In the banking context, this extra risk was prohibited under the so-called Volcker Rule of the Dodd-Frank Act. See Floyd Norris, “Bank Rules that Serve Two Masters,” New York Times, 10/13/11 https://www.nytimes.com/2011/10/14/business/new-dodd-frank-rules-muddled-by-congress-that-wants-it-both-ways.html?_r=1&src=recg (last accessed 12.17.21)

⁹ FINRA website, “If a Brokerage Firm Closes its Doors,” <https://www.finra.org/investors/alerts/if-brokerage-firm-closes-its-doors> (last accessed 12.20.21)

A. Margin Risk

19. One of the risks an agency broker faces is the risk that customers' margin accounts are not properly managed. An agency broker is exposed to a margin customer's losses if the customer's equity is not sufficient to cover losses in the account, which can happen if markets move against the customer's position quickly and dissipate the account equity.¹⁰

20. In practice, this margin risk is mitigated by several factors:

- The customer's equity must be completely depleted before the broker will suffer any loss and even if this happens the broker would still have a legal claim against the customer.
- The United States has strict margin rules limiting the risk that customers may incur as a function of their equity.
- The size of each customer's indebtedness to the broker is generally small relative to the broker's capital and the broker has control over the amount of leverage offered to each customer.
- The correlation between the risks of customers' portfolios tends to be small. If a customer incurs losses, it generally doesn't make it more likely that other customers will also incur losses.¹¹ Client holdings as a whole are generally "long" the market and it is possible that the market may fall sharply. But the market is still far less volatile than almost any individual component or security class due to diversification. In 1987, for example, the market dropped about 30% and this was a "once in a generation" event. However, there is often a 30% drop in a random individual security almost every day.
- The risk of correlated movements is mitigated further if a firm has many (smaller) customers (as opposed to only a few large customers). LSC has several large customers. However, the firm's large

¹⁰ LSC's models for managing account equity and customer shortfalls are discussed later in the Affidavit.

¹¹ A recent notable counterexample is when Robinhood restricted customer purchases of GameStop and AMC. <https://www.sec.gov/files/staff-report-equity-options-market-struction-conditions-early-2021.pdf>.

customers are omnibus accounts that have many underlying accounts which provide the same diversification benefit.

- Many firms, including LSC, have house requirements prohibiting customers from having concentrated positions.¹²

B. Operational Risks

21. Trading and back-office systems are highly automated, but there is the possibility of errors or “bugs” in a firm’s systems, causing un-wanted trades to be sent to the market.¹³ Bugs can also cause a firm’s clearing and settlement systems to fail. Cyber security issues are a new form of operational risk as hackers try to invade a firm’s systems. Intrusions could cause significant losses, both financially, through theft, and reputationally, leading to customer withdrawals. Brokers including LSC routinely retain IT specialists to test, review and monitor their systems to manage these operational risks.

C. Metrics to Manage and Measure Broker Risk

22. There are several methods and metrics that regulators and other entities like the SEC, FINRA, NSCC and OCC use to measure the risk of a broker’s capital and liquidity. Capital is a measure of the cushion a firm has—assets in excess of liabilities. Liquidity is defined as the ability to access sufficient cash for a firm to meet its obligations as they come due.¹⁴ These concepts overlap significantly. For

¹² LSC employs a house margin system that limits customers from having concentrated positions in a few securities. Please see the LSC Monitorship Report, SEC Case 1:17-cv-01789-DLC, dated April 26, 2021, p.43-44.

¹³ See for example, Jenny Strasburg and Jacob Bunge, “Loss Swamps Trading Firm,” Wall Street Journal 8/2/12 <https://www.wsj.com/articles/SB10000872396390443866404577564772083961412>. (Last accessed 12.17.21)

¹⁴ <https://www.sec.gov/corpfin/cf-manual/topic-9-at-9210.2>: “Liquidity is the ability of the registrant to generate adequate amounts of cash to meet its needs for cash.”

example, the SEC explains that having capital is important in order that brokers “have sufficient liquid resources on hand at all times to satisfy claims promptly.”¹⁵ Nevertheless, the concepts can be distinguished as I explain below.

i) Brokers Face Capital Requirements

23. Brokerage firms are highly leveraged financial institutions. Under the SEC’s financial responsibility rules,¹⁶ brokers are not permitted to have aggregate indebtedness in excess of 1500% of their net capital, or alternatively, net capital less than the greater of \$250,000 or 2 percent of aggregate debit items computed in accordance with the Formula for Determination of Reserve Requirements for Brokers and Dealers.¹⁷

ii) Brokers Have Liquidity Requirements

24. One of the purposes of the SEC's financial responsibility rules is to assure that broker-dealers have sufficient liquidity.¹⁸ However, there are other elements that go into an assessment of liquidity besides capital. Accordingly, FINRA expects broker-dealers to regularly assess their funding and liquidity risk management practices and in recent years has published guidance on liquidity, and in 2018 and 2019, discussed exam findings and observations on the effectiveness of liquidity risk management programs.¹⁹ However, FINRA’s guidance does not state bright-line

¹⁵ Key SEC Financial Responsibility Rules.

https://www.sec.gov/about/offices/oia/oia_market/key_rules.pdf (last accessed 12.17.21)

¹⁶ Rule 15c3–1, 17 CFR § 240.15c3-1.

¹⁷ Rule 15c3–3, 17 CFR § 240.15c3–3a.

¹⁸ Guidance on Liquidity Risk Management Practices, FINRA Regulatory Notice 15-33.

¹⁹ Guidance on Liquidity Risk Management Practices, FINRA Regulatory Notice 15-33.

requirements and do not specify liquidity levels and practices that are sufficient or insufficient.

25. For example, in Regulatory Notice 15-33, FINRA asked member firms to stress the following five factors concurrently for a 30-day period.

- Funding inventory positions
- Financing for mismatched financing transactions
- Operational drains
- Funding customer withdrawals
- Losses from forced deleveraging and reserves against trading losses

26. Only some of these factors are applicable to an agency broker like LSC.

Agency brokers such as LSC do not have inventory positions and are not exposed to trading losses. Financing for mismatched financing transactions is not a stress factor because LSC's secured lending and borrowing operations are financed overnight, and their maturities are therefore perfectly aligned. Accordingly, of the FINRA stress test factors above, only operational drains and customer withdrawals squarely fit the liquidity challenges at an agency broker such as LSC.

27. Customer withdrawals do not pose a meaningful risk to LSC because customer money is segregated in the reserve account and is available for immediate withdrawal. The reserve account is part of the SEC's broker-dealer customer protection rule.²⁰ Broker-dealers are required (i) to maintain physical possession or

²⁰ 17 CFR § 240.15c3-3 - Customer protection - reserves and custody of securities.

control of all fully-paid customer securities and excess margin securities and (ii) to deposit customer cash in banks under accounts specified as “Special Reserve Bank Account for the Exclusive Benefit of Customers”.

28. The amount to be reserved in that account is provided under a so-called reserve formula.²¹ The reserve formula in essence defines the amount of customer cash that must be segregated. For example, it includes the cash a broker receives by hypothecating customer securities and is reduced by customer margin loans. The OCC Required Fund Deposit is a reduction to the account but NSCC Required Deposit is not.

iii) Brokers Must Make Deposits with Clearing Organizations

29. NSCC and Options Clearing Corporation (“OCC”), serve as the central counterparties for equities and options trades in the United States markets. Participants of these clearing agencies are required to maintain a clearing fund deposit (what I have been calling the Required Fund Deposit at the NSCC).

30. NSCC assumes the settlement risk of securities trades. The current standard settlement cycle is two days. If a counterparty to a security trade is unable to perform at the end of those two days, NSCC will step in for that counterparty and complete (and settle) the trade. NSCC may be exposed to losses because it guarantees that all trades among its members will clear and securities prices

²¹ 17 CFR § 240.15c3-3a - Exhibit A - Formula for determination of customer and PAB account reserve requirements of brokers and dealers under § 240.15c3-3.

fluctuate between trade submission and settlement.²² In return, NSCC manages its risk by requiring its members to provide cash collateral that mitigates its exposure (“NSCC Requirement”). The Required Fund Deposit at NSCC serves as the NSCC members’ margin.²³

V. LSC’S SETTLEMENT WITH THE SEC

31. In October 2019, the U.S. District Court for the Southern District of New York (the "District Court") issued a "Consent Order" adopting a settlement between the SEC and LSC to resolve allegations of assisting foreign investors to manipulate stock prices. LSC agreed to pay a penalty, disgorge profits, and agreed to retain an independent compliance monitor for three years.²⁴ As set forth in the Consent Order, LSC agreed to retain an independent compliance monitor to perform a comprehensive and ongoing review of, among other things, “The reasonableness and sufficiency of LSC's controls and procedures to prevent manipulative trading and other market manipulation.” As noted above, this Affidavit does not address these internal controls.

32. In December 2019, FINRA’s Office of Hearing Officers issued an order adopting a settlement between FINRA and LSC. In that Order, LSC agreed to retain an independent consultant to conduct a comprehensive review of the Firm’s

²² Written Testimony of Michael C. Bodson, Chief Executive Officer of The Depository Trust & Clearing Corporation, May 6, 2021.

²³ NSCC Rules and Procedures.

²⁴ <https://www.sec.gov/news/press-release/2019-205>.

supervisory system and its anti-money laundering and Section 5 obligations in connection with stock trading in low priced securities.

33. I understand that several reports have been issued in connection with LSC's internal controls: one by the Monitor (under the SEC settlement) and one by a Consultant (under the FINRA settlement). The Monitor's April 26, 2021 Monitorship Report to the SEC addresses some issues related to LSC's pre-trade controls and liquidity management practices. I understand that there is a FINRA investigation in process concerning the Consultant's Final Report.²⁵

VI. LSC HAS MET ALL CAPITAL AND LIQUIDITY REQUIREMENTS

34. LSC is a wholly owned subsidiary of Lek Securities Holdings Limited ("Holdings") and is a registered broker dealer with the Securities and Exchange Commission ("SEC"), the Financial Industry Regulatory Authority ("FINRA") and is a member of the New York Stock Exchange and other principal exchanges. LSC is an independent order-execution and clearing firm that provides direct access to equities, options, fixed income, and foreign exchange markets. LSC primarily serves institutions and professional traders.

35. Regulatory authorities and self-regulatory organizations like FINRA, the NSCC and the OCC have metrics and requirements that measure and constrain a broker's capital and liquidity. The various methods overlap conceptually, but broadly, the SEC has capital requirements, the clearing organizations have clearing

²⁵ Letter to Perry Hubbard, Esq., FINRA, dated May 19, 2021.

fund deposit requirements, and the SEC has rules requiring the segregation of customer assets. All the concepts bear on liquidity.

36. I have analyzed LSC's capital and liquidity position, its reserve account computations, and liquidity sources, and concluded that LSC does not present a heightened risk to the NSCC or its constituents.

37. LSC's income is derived from its activities as an agency broker (and not from proprietary trading). In its most recent fiscal year, LSC derived 64.4% of its revenue from clearing, execution and custody commissions and fees, and 34.6% of revenue from interest income.²⁶ Interest income includes revenue from securities lending transactions, margin financing, and interest earned from segregated cash deposited at banks. LSC has no other material revenue streams. LSC had no investment losses because it does not engage in proprietary or principal trading. At year-end 2020, LSC's own securities holdings stood at \$2.2 million, which is less than 0.5% of LSC's total assets of \$477 million. Most of this amount represented its required holdings of DTCC stock.²⁷

38. LSC's liabilities consist primarily of short-term financing arrangements to facilitate margin trading by customers—and are secured by the securities purchased by those customers, supported by the customer account equity as well as by lines of credit and payables to clearing organizations and other broker dealers.

²⁶ Lek Securities Corporation annual audited report on Form X-17A-5 filed with the SEC, Statement of Operations for the year ended December 31, 2020.

²⁷ LSC's December 31, 2020 FOCUS report.

39. LSC's primary financial risk results from any residual exposure from its customer margin loans and customer short sales that are cash collateralized in the customers' accounts. If customers incur sudden losses that exceed the equity in the customer account and the customer otherwise does not cover the shortfall in the account, LSC would have to cover that shortfall. This is the primary way LSC could incur losses. But as noted above, there are several factors that mitigate this risk: regulations and internal policies that limit margin lending, each customer makes up a small percentage of the overall business and their activity is generally uncorrelated with that of other customers.

A. LSC Has Adequate Capital

40. LSC had regulatory net capital of \$14,529,108 at year end 2020 – \$10,580,338 in excess of the SEC's minimum net capital requirement of \$3,678,770 (4 times higher). On September 30, 2021 LSC's regulatory net capital was \$15,217,160 – \$13,315,480 higher than the SEC's required minimum net capital of \$1,901,680 (8 times higher).²⁸ LSC's risk-based regulatory capital has increased since the beginning of the year both in absolute terms and as a multiple of the required minimum. Minimum required capital for LSC to be an NSCC Member is \$1 million.²⁹

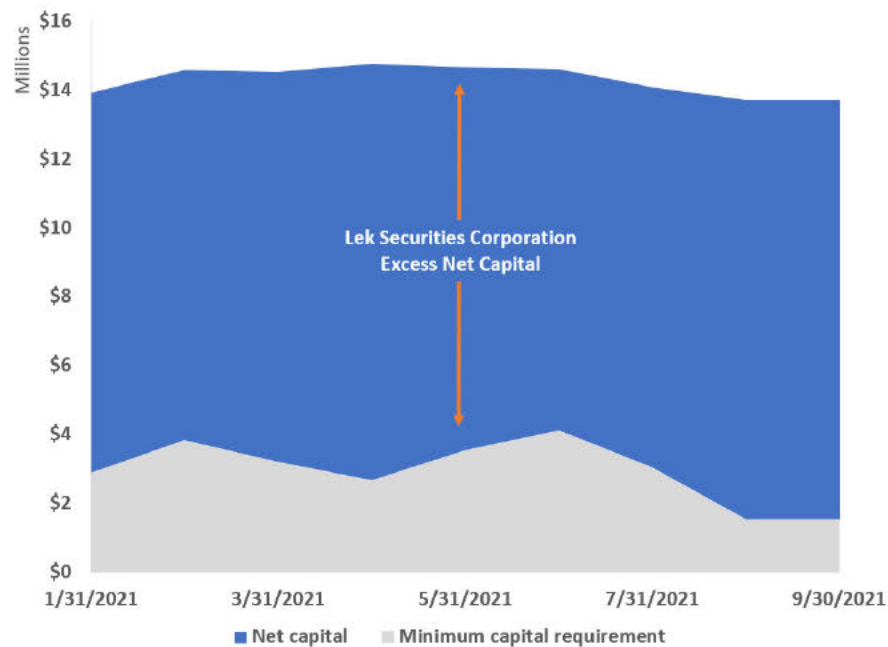
41. **Figure 1** shows LSC's regulatory net capital and excess regulatory net capital throughout 2021. As can be seen, LSC's capital remained stable over the

²⁸ LSC Focus Report September 30, 2021.

²⁹ NSCC Rules and Procedures.

period despite facing sharply higher NSCC requirements from illiquid stock settlement activity.

Figure 1 – LSC’s Total and Excess Net Capital in 2021



B. LSC Has Met All NSCC Deposit Requirements

42. The NSCC requires members to deposit funds to offset the risks to which it faces when it assumes the risk of its members failing to settle securities. For each member firm NSCC’s required deposit is derived from the risk characteristics of the NSCC Participant’s portfolio of unsettled securities from the time period spanning the trade date to two days later (conventional t+2 settlement). NSCC manages its requirements based on historical and current market statistics and its experience with the member.

43. NSCC’s Required Fund Deposit consists of various component charges driven by the member’s portfolio and trading activity, as well as some standard

charges.³⁰ The core component of the Requirement includes charges for Continuous Net Settlement (“CNS”) Fails, FundServ, Mark to Market (MTM), Minimum Requirement, Non-CNS Charge, and Value-at-Risk (VaR), now including the former Illiquidity charge.^{31,32} Other charges include Excess Capital Premium (“ECP”) when they are applicable.

44. The ECP was adopted by the NSCC in 2006.³³ Prior to its adoption, commenters pointed out the potential anti-competitive effect of the proposed rule on smaller broker-dealers. NSCC responded that the new ECP would be applied systematically to all members and NSCC’s discretion in determining the ECP would only be used to reduce or eliminate the premium, not to raise it, and that the situations where such discretion would be used were likely to be very fact and circumstances driven.³⁴ LSC has met all its NSCC clearing fund deposit

³⁰ See NSSC Rules and Procedures, September 20, 2021; DTCC Risk Portal User’s Guide, April 02, 2018.

³¹ The **Continuous Net Settlement CNS Fails** charge results from positions that did not settle on the Settlement Date. The CNS fails charge is a percentage of the market value of the fail. The percentage is based on Member credit ratings. A long fail position represents the quantity owed to the Member by CNS (the Member's fail-to-receive). A short fail position represents the quantity owed to CNS by the Member (the Member's fail-to-deliver). The **FundServ Charge** is based on the Member’s mutual fund activity. The value is derived from a Member’s settlement debits related to their FundServ activities over the last 20 business days. Margin Requirement Differential is a charge that represents a few factors, and driven off the Member’s VaR and MTM. It looks back at 100 days of history. The **Mark to Market (MTM)** charge is the difference between the contract price and the current market price applied to the end of the day Member portfolio. MTM profits and losses are aggregated at a Member’s account and charged as part of the Member's Clearing Fund. The **Minimum Requirement** is a base charge that is floor margin requirement. The **Non-CNS Charge** is comprised of settlement activities separate from CNS activities. The Volatility (VaR) charge is also known as **Value-at-Risk (VaR)** and provides an estimate of the potential maximum loss for a given portfolio, based on a given confidence level over a defined time horizon. See DTCC Risk Portal User’s Guide, April 02, 2018.

³² SEC Staff Releases Report on Equity and Options Market Structure Conditions in Early 2021

³³ SEC Release No. 34-54457, September 15, 2006.

³⁴ Id.

requirements, that include large amount for ECP through, among other sources, its Promissory Notes Program that matches LSC's liquidity sources to LSC's liquidity needs as discussed in Section VII.D.

Table 1 below summarizes data from LSC's Required Fund Deposit for 2021.

Table 1 – Components of LSC's Daily NSCC Requirements between 1/4/2021 – 10/13/2021³⁵

YTD 2021	VaR	MTM	VaR + MTM	ECP	Other	Requirement Total
Count	153	153	153	153	153	153
Average	13,559,303	4,226,861	17,786,164	13,180,380	4,930,019	35,896,563
Median	13,444,788	3,652,667	17,055,335	9,156,250	5,241,802	31,453,387
95th Percentile	18,887,488	9,602,543	26,182,843	36,966,281	5,676,782	68,825,906
99th Percentile	21,914,803	11,315,316	29,507,685	47,842,095	4,597,422	81,947,202
Max	24,673,122	13,700,873	31,021,603	50,234,364	3,513,885	84,769,851
Total - 2021	2,074,573,362	646,709,716	2,721,283,078	2,016,598,195	754,292,847	5,492,174,119
% of Requirement	38%	12%	50%	37%	14%	100%

*Source: LSC's daily NSCC requirements compiled by LSC. Values have only been calculated on days for which there is data for all the components. The calculation period runs from January 4, 2021 to October 13, 2021, which is prior to the DTCC notices dated October 26, 2021.

45. LSC's largest charges are VaR and ECP.³⁶ During 2021, VaR was 38%, ECP was 37%, and MTM was 12% of LSC's total Requirement. A large portion of the remaining 14% was the adjustment due to the Minimum Requirement because NSCC recently increased LSC's Minimum Required Deposit to \$20 million on or about August 20, 2021.³⁷

³⁵ In **Table 1**, I have included data only for those dates when there was data for each component of the Fund Deposit Requirement. In Appendix B, I present some variations on this Table, including days on which there was no ECP.

³⁶ "Generally, the largest component of Members' Required Fund Deposits is the volatility component. The volatility component is designed to calculate the amount of money that could be lost on a portfolio over a given period of time assumed necessary to liquidate the portfolio, within a 99% confidence level." Notice of Filing of Advance Notice to Enhance National Securities Clearing Corporation's Haircut-Based Volatility Charge Applicable to Illiquid Securities and UITs and Make Certain Other Changes to Procedure XV, April 9, 2020.

³⁷ I understand that this was later increased to \$27 million.

46. ECP is the amount by which a Member's Required Deposit exceeds its excess regulatory capital multiplied by the Member's ratio of Required Deposit to excess regulatory capital.³⁸ In essence, the ECP increases sharply as the amount of securities settled increases relative to the Member's regulatory capital.

47. A large portion of LSC's ECP arises from the Illiquid Securities component, which in turn is directly derived from the trading activity of a number of sophisticated LSC customers that invest in low-priced securities. The Illiquid component treats every sale as if it were a short sale and sub-penny securities as if they were a penny.³⁹

48. NSCC made certain rule changes effective February 1, 2021 and increased its impact of the Illiquid securities component: it eliminated the separate illiquid charge and included it as a component of VaR.⁴⁰ Previously, the illiquid charge was not included as a core charge in determining the ECP. But because the excess premium includes the VaR component, the inclusion of the illiquid charge under the VaR resulted in a large increase in the ECP and LSC's total NSCC requirement. The result is that ECP grows sharply as illiquid security activity grows beyond a certain point. See **Figure 2** below.

³⁸ The excess premium component, "is the amount by which a Member's Required Deposit exceeds its excess regulatory capital multiplied by the Member's ratio of Required Deposit to excess regulatory capital, expressed as a percent." Securities Exchange Act Release No. 79598 (December 19, 2016)

³⁹ NSCC Rules and Procedures.

⁴⁰ SR-NSCC-2020-003; DTCC Notice January 13, 2021.

Figure 2. LSC's Illiquidity Component and Required Fund Deposit

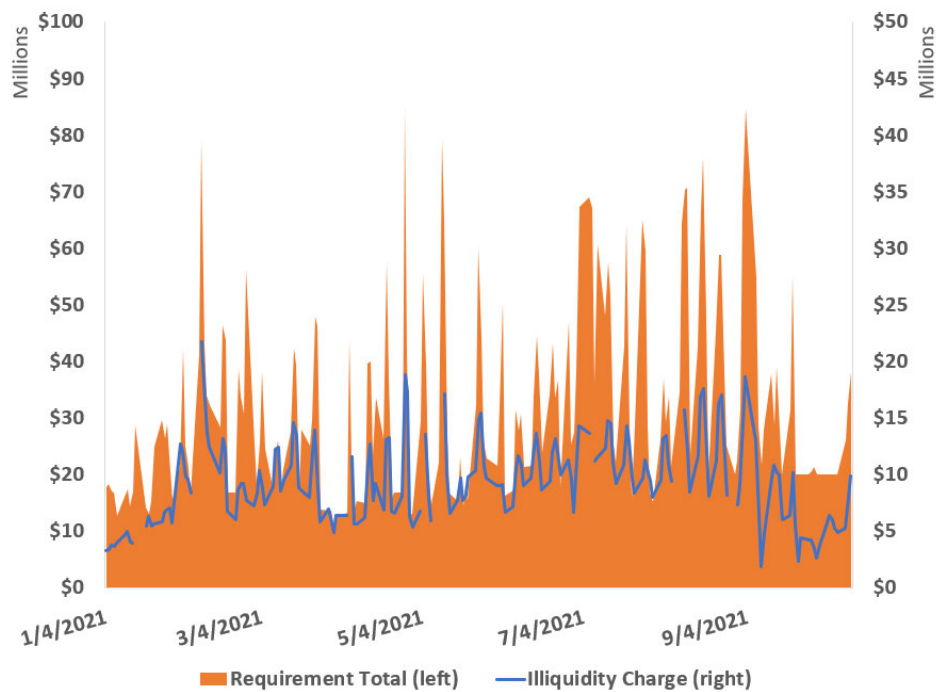


Figure 2 displays the high degree of correlation between the Illiquid component and the Required Fund Deposit. The spikes in LSC's Required Fund Deposit are caused by smaller spikes in LSC's settlement activity of illiquid shares. **Table 2** below summarizes components of the data by percentile and further lays out the impact of LSC's illiquid securities component on the total Required Fund Deposit.

Table 2 – Illiquidity Charge, ECP and Fund Deposit Requirement

Percentile	Illiquidity Charge	ECP	Requirement Total
0	\$3,330,728	\$2,799,885	\$18,413,271
5th	\$4,898,867	\$1,667,858	\$18,620,508
10th	\$6,039,400	\$3,326,015	\$19,986,582
15th	\$6,718,580	\$3,521,091	\$23,169,330
20th	\$7,330,672	\$3,171,739	\$22,836,882
25th	\$8,051,785	\$8,248,952	\$28,300,537
30th	\$8,516,874	\$2,579,389	\$20,909,377
35th	\$8,935,001	\$8,926,956	\$29,904,655
40th	\$9,226,259	\$8,137,721	\$30,308,135
45th	\$9,569,779	\$5,069,333	\$24,585,484
50th	\$9,821,716	\$8,519,544	\$29,047,316
55th	\$10,185,894	\$10,105,540	\$32,650,280
60th	\$10,827,525	\$8,316,180	\$30,550,551
65th	\$11,250,208	\$14,740,626	\$38,470,908
70th	\$11,937,788	\$15,527,184	\$39,329,842
75th	\$12,424,793	\$17,231,050	\$40,945,762
80th	\$13,149,013	\$16,444,621	\$40,643,070
85th	\$13,650,924	\$14,816,565	\$38,475,578
90th	\$14,475,158	\$27,009,449	\$54,599,651
95th	\$16,937,843	\$29,620,086	\$58,542,827
100th	\$21,707,988	\$36,005,632	\$66,538,435

Table 2 sorts the Illiquid Securities component into percentile rankings and shows the ECP and the associated Illiquid Securities component in each percentile cohort. As the Illiquid component increases, and reaches higher levels, the Required Deposit increases sharply.

49. It is primarily the increase in ECP that is driving the increase in the Required Fund Deposit. This is evident in **Figure 3** below, which shows that the remaining elements of the Required Fund Deposit—that is, the Required Fund Deposit less the ECP and less the Illiquid Securities component of VaR (denoted as remainder in **Figure 3**), is relatively stable over time. In other words, it is not the estimated underlying risk exposure per se that drives the spikes in the Required Fund Deposit. It is the NSCC’s non-linear ECP charge that drives the spikes in LSC Required Fund Deposit.

Figure 3 – Required Fund Deposit With and Without the ECP and Illiquidity Charge



50. The ECP, by design, fluctuates daily as a broker’s level of trading risk fluctuates. When LSC’s trading in illiquid securities fluctuates, for example, so does its NSCC Required Fund Deposit. In this way, the Required Fund Deposit is tied to the underlying trading activity of the broker and meets the goal of the NSCC when it filed for approval with the SEC to change the treatment of illiquid securities when calculating the Required Fund Deposit. The NSCC stated that the changes were:

“designed to assist NSCC in maintaining a risk-based margin system that considers, and produces margin levels commensurate with, the risks and particular attributes of portfolios that exhibit illiquid risk attributes.”⁴¹

51. The way the ECP is calculated reflects this daily adjustment. The ECP is charged to a Member when the Member’s Required Deposit exceeds its net capital

⁴¹ NSCC 2020-003 Illiquid Securities 3/16/2020.

as described in Procedure XV of NSCC Rules and Procedures. The ECP was designed to address temporary increases in a Member's Required Deposit based upon a single day's worth of activity. This is consistent with economic principles: the Required Deposit fluctuates on a daily basis as the daily underlying risk (as determined by the NSCC) changes.

52. The NSCC has itself recognized the importance of tying the Required Deposit to the underlying risk. For example, the NSCC excluded the MRD and Coverage Component from the ECP calculation because if these components were “included in the calculation of the Excess Capital Premium, especially during periods following an increase in activity, the increased MRD and Coverage Component could lead to more frequent ECP charges over an extended period of time.” [SR-NSCC-2016-005 New Clearing Fund Components, December 19, 2016] The ECP, in short, was designed to change daily and to provide additional Required Deposits to the NSCC as changes in the underlying daily activity increased—and decrease when that risk activity decreased.⁴²

53. I understand that the NSCC has adopted a separate, minimum Required Deposit specifically targeted at LSC: it requires LSC to maintain a minimum of \$20 million regardless of LSC's activity.⁴³ Such a minimum is inconsistent with the

⁴² Order Granting Approval of Proposed Rule Change to Accelerate its Trade Guaranty, Add New Clearing Fund Components, Enhance its Intraday Risk Management, Provide for Loss Allocation of “Off-the-Market Transactions,” and Make Other Changes. SR-NSCC-2016-005.

⁴³ I understand that the \$20 million has been increased to \$27 million after the date of the DTCC's notice to cease to act on behalf of Lek.

economic principle of tying the Deposit to the underlying risk and appears to be inconsistent with the principles DTCC has itself set forth in the past.

54. A minimum Required Deposit also imposes additional costs on a broker above what is required by the risk of the underlying trading activity. The operating model of an agency broker like LSC involves earning commissions and interest from the flow of trading activity. Imposing a minimum deposit requirement at all times – even when the business flow is low – amounts to a requirement that the broker raise capital when it is not needed. Such a policy needlessly imposes costs on the broker and impairs competition. From an economic perspective, tying the Deposit to the actual risk aligns risks and Required Deposits.

55. A minimum Required Deposit can also create unintended consequences and produce perverse incentives. If LSC needs to raise permanent funds from investors to meet the minimum Required Deposit, but those investors will only supply those funds if they are engaged in a commensurate level of trading in illiquid securities, the broker could have an incentive to encourage incremental illiquid trading and incremental risk, commensurate with the incremental funds needed to meet the minimum Required Deposit. This would be undesirable from a risk management point of view.

56. LSC monitors its customers' trading activity and uses the NSCC webservice on an intra-day basis to learn the impact of potential trading activity on the Firm's NSCC Deposit Requirement. In using the NSCC webservice, LSC can substantially

determine its Required Deposit prior to a trade.⁴⁴ If LSC believes a customers' trade may have a material impact on its NSCC requirement, it may restrict that trade until the Firm has analyzed the trade's impact on the firm's NSCC requirement.⁴⁵

57. On many days the Required Deposit has been substantial—exceeding \$70.0 million on six days, reaching a maximum of \$84.8 million, as shown in **Table 1**. Through the ECP, in other words, the NSCC has been subjecting LSC to a significant additional liquidity test over an extended period of time—which LSC has met.

58. I describe in more detail, in Section VII.D the Holdings Program, which LSC uses to generate liquidity from the same customers generating the Illiquid component in the first place.

VII. ANALYSIS OF OTHER DTCC'S CONCERNS REGARDING CAPITAL AND LIQUIDITY

A. LSC Has Adequate Cash on its Balance Sheet

59. Cash and liquidity sources such as lines of credit are complementary in financial management and should be considered together. LSC has sufficient amounts of both cash and lines of credit to match its liquidity needs.

⁴⁴ Except for the MTM component, which represents on average, only about 11% of the total, as shown in **Table 1**.

⁴⁵ LSC Monitorship Report, SEC Case 1:17-cv-01789-DLC, December 26, 2020, at p.42-43; Lek Securities Corporation Terms and Conditions of Computer Trading and Rox Use.

60. With respect to cash, LSC has in excess of 5% of total assets on its September 30, 2021 balance sheet. A casual sampling⁴⁶ of most recent annual SEC X-17a-5 filings by other broker-dealers suggests that LSC's cash position is in line with and in fact higher than many other, including non-agency-based, clearing brokers. A comparison based on various balance sheet ratios are provided below:

Table 3 – Cash Holdings reported on the Balance Sheets of Various Broker-Dealers

Broker-Dealer	Cash	Assets	Cash/ Assets	Seg. Cash	Cash/ SegCash
Lek Securities	24,292	448,022	5.4%	45,599	53.3%
Hilltop Securities	39,858	3,173,176	1.3%	290,357	13.7%
Wedbush Securities	74,649	8,183,145	0.9%	2,567,717	2.9%
Axos Clearing LLC	21,332	1,433,981	1.5%	322,153	6.6%
National Financial LLC	1,340,000	89,437,000	1.5%	n/a	n/a

Source: Dollars in thousands. Most recent Form X-17A-5 annual public filings of respective broker-dealers available on SEC-EDGAR. LSC's monthly X-17A-5 filing on September 30, 2021.⁴⁷

B. LSC Has Adequate Access to Liquidity

61. At the beginning of 2021, LSC had LOCs from BOMH and Texas Capital. But in early 2021, Texas Capital informed LSC that it would terminate an existing line of credit. I understand that Texas Capital made that decision in connection with its exiting that particular line of business and that, regardless, LSC had not in recent years regularly utilized that line of credit.⁴⁸ And on July 8, 2021, BMOH informed LSC that it intended to wind down its relationship with LSC, including its

⁴⁶ It is not possible to find precise comparables for LSC since there are no other agency broker NSCC members that are comparable to LSC.

⁴⁷ <https://www.sec.gov/edgar/search/?r=el#/dateRange=10y&category=custom&forms=X-17A-5>.

⁴⁸ LSC's December 31, 2020 and December 31, 2019 FOCUS Reports.

existing line of credit by October 2021. I understand that LSC had not been generally fully utilizing that line of credit as well.⁴⁹ BMOH also informed LSC that it would cease to act as LSC's settlement bank at the NSCC in October 2021.

62. LSC has successfully arranged for new sources of funding and also arranged for a new settlement bank. LSC now has the \$10 million unsecured Lakeside LOC and the \$100 million Holdings Promissory Notes Program in place of the \$12 million BMOH unsecured LOC at the end of 2020. LSC's secured financing needs are satisfied by a combination of the Lakeside secured LOC and securities lending operations that have a capacity up to a billion dollars to cover customer debit financing under SEC rules.⁵⁰ Moreover, as explained below, stock loan facilities are economically more attractive in financing customer debit balances and preferable to the bank secured lines of credit.

63. The unsecured financing needs of LSC are met with the unsecured \$10 million Lakeside LOC and the \$100 million Holdings Promissory Notes Program which at a total of \$110,000,000 far exceed the prior BMOH unsecured LOC.

64. The primary liquidity challenge for LSC comes from NSCC Fund Deposit Requirements that make it necessary to utilize unsecured lines. As explained below, after the introduction of the Holdings Promissory Notes Program, LSC's current unsecured funding capacity is essentially tailored to the amounts that are needed to fund the Required Fund Deposit.

⁴⁹ LSC's average use of the BMOH secured LOC was \$22,682,898 and the unsecured line was \$7,338,983 between February 1, 2021 and July 20, 2021.

⁵⁰ Responses to DTCC Inquiries, p. 3.

65. Therefore, in my opinion, the termination of the BMOH and Texas Capital LOC have not compromised LSC's liquidity—the BMOH and Texas Capital LOCs have been replaced by the Lakeside facilities and the Holdings Promissory Notes Program.

C. LSC Has Sufficient Collateral to Utilize the Lakeside LOC

66. DTCC also states that there is a high probability that LSC does not have sufficient collateral left to utilize the full Lakeside LOC. In my opinion, there are several reasons to believe LSC does have sufficient collateral.

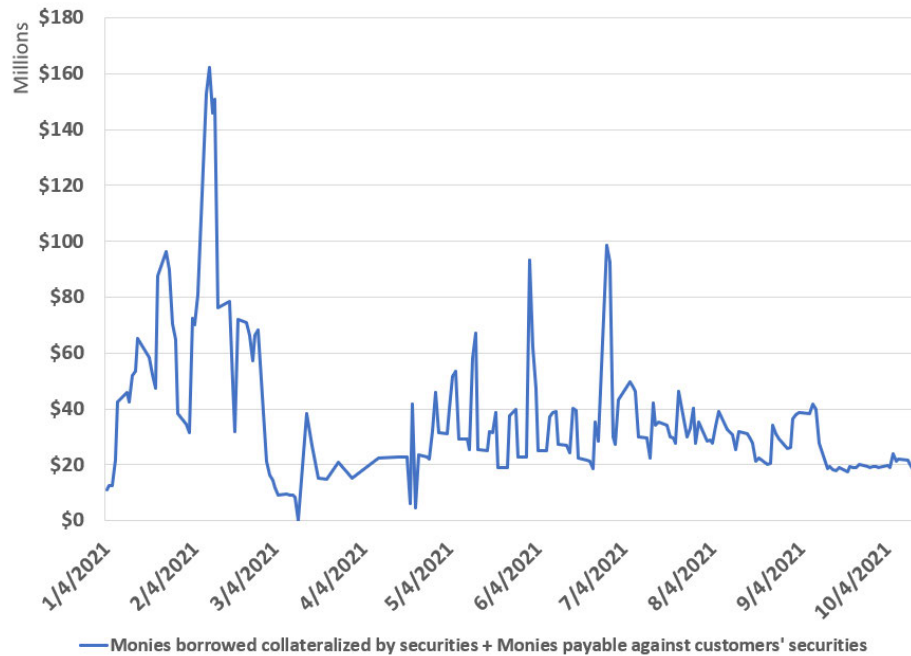
67. First, SEC Rule 15c3-3 was designed to ensure that there will always be a sufficient amount of collateral to finance customer debit balances. If the broker decides to use customer debit balances to obtain bank financing, Rule 15c3-3 allows the hypothecation of customer securities for up to 140% of the customers debit balances, and banks generally lend 80% of the securities' market value. This means that a broker can receive a bank loan equal to 112% of the value of the debit balances (140% times 80%). If the broker decides to use the customer debit balances in the securities lending market, it can generally raise even more funds. This is because in securities lending securities borrowers may lend higher than the securities' market value, typically 102%-105%.⁵¹ Even assuming that the securities lender receives only 100% of the securities' market value (instead of 80% at a bank), the broker will receive 140.0% of the value of debit balances. Securities lending, in general, provides more liquidity than bank lines.

⁵¹ Reporting of Securities Loans, SEC Proposed Rule, November 18, 2021.

68. Second, funds raised by hypothecating customer securities must, in any event, be segregated as customer cash and cannot generally be used by LSC to meet other liquidity needs because of the SEC's customer protection rules. LSC's only use for the secured LOC or securities lending is to finance customer debit balances. If LSC raised secured funds for some other purpose, then that money would also have to be largely segregated as well and could not be used to address LSC's general liquidity needs.

69. LSC has sufficient collateral to fully take advantage of the secured Lakeside LOC. Customer debit balances as of September 30, 2021, for example, were \$21,353,652. Under Rule 15c3-3, LSC may hypothecate up to approximately \$30 million ($=140\% \times \21.35 million). If borrowed from Lakeside, even with the overcollateralization required LSC would have sufficient funds ($=30 \text{ million} \times 80\% = \$24 \text{ million} > \$20 \text{ million LOC}$). And as described above, LSC could raise even more funds through stock lending. In 2021, LSC has consistently had sufficient collateral to support a \$20 million LOC, as can be seen from **Figure 4** in which the moneys borrowed by collateralized securities regularly exceeded \$20 million.

Figure 4. LSC Customer Securities Secured Borrowing and Securities Loaned*



70. The discussion above applies to large customer debit balances (defined as balances not in excess of 25% of the broker-dealer's tentative net capital). Small debit balances can be financed with excess free credit balances, and therefore do not require external financing.⁵² Under all circumstances, then, collateral is virtually guaranteed to be available to finance debit balances.

D. LSC Has Access to Significant Levels of Liquidity Through Its Promissory Notes Program

71. As noted above, LSC uses the Promissory Notes Program to fund the Required Fund Deposit. I understand that the DTCC has expressed concerns over the Promissory Notes Program. However, parent financing arrangements are

⁵² 17 CFR § 240.15c3-3a - Exhibit A - Formula for determination of customer and PAB account reserve requirements of brokers and dealers under § 240.15c3-3.

common among brokers and dealers and, in my opinion, the Program has effectively provided substantial financing for LSC in the past several months since the Program's adoption following the February 2021 changes in the NSCC Required Fund Deposit calculation with respect to illiquid securities.⁵³ The Program significantly augments LSC's unsecured bank LOC, both of which it uses to meet the NSCC Required Fund Deposit.⁵⁴

72. Under the Promissory Notes Program, Lek Securities Holdings Limited ("Holdings") obtains loans from investors and financial institutions who seek to earn a return by lending to Holdings on an unsecured basis ("Holdings Lenders"). Most Holdings Lenders are also customers of LSC. In order to ensure these investors are aware of the risk, and to ensure they understand the clear lines of separation between Holdings and LSC, each investor through its loan agreements acknowledges, agrees, and understands that:⁵⁵

- These loans are not customer funds,
- These loans do not constitute a deposit with a registered broker dealer,
- These loans are not protected by the Securities Investor Protection Corporation "SIPC", and
- These loans, while demand notes, are payable on the third business day after the date of recall notice.

⁵³ SR-NSCC-2020-003 and NSCC Notice, 1/13/2021.

⁵⁴ Response to FINRA's Flow of Funds Scenarios.

⁵⁵ Promissory Notes between Lek Holdings LLC and certain Noteholders.

73. The Holdings Promissory Note program was established in response to the NSCC's decision to begin including the illiquidity component within the VaR charge (thereby substantially increasing the ECP, as explained above).⁵⁶ However, the Holdings Promissory Note operates independently from the NSCC requirement. Under the Holdings Promissory Note LSC may use the proceeds freely in its business, including, but not limited to, satisfying NSCC requirements.⁵⁷

74. Moreover, LSC has no obligation to accept all or any part of an order from any customer, including those Holdings Lenders that may be also be customers of LSC. If customers who lend to Holdings are engaged in trading activity through LSC, there is no direct connection between their lending and trading. If these customers lend to Holdings, Holdings may in turn lend some or all of those funds to LSC, and LSC may use the funds as it sees fit to meet its liquidity needs. There is no requirement under the Holdings Promissory Note that LSC use the proceeds from the Holdings Promissory Note in connection with the underlying Holdings lenders' trading.

75. If the Holdings lenders seek to redeem their notes, they provide demand notices to Holdings. Holdings may or may not provide a demand notice in the same amount to LSC after the receipt of the notice from the Holdings Lenders. When a notice of demand is given by a Holdings lender to Holdings, Holdings has the contractual obligation to pay on the third business day after notice (T+3). Similarly,

⁵⁶ NSCC 2020-003 Illiquid Securities 3/16/2020.

⁵⁷ Promissory Note dated 4/27/21 between LSC and Lek Holdings LLC, p. 3.

when a notice of demand is given by Holdings to LSC, LSC has the contractual obligation to pay on the third business day after notice (T+3). For example, if Holdings gives written notice to LSC before 5:00 PM on a Monday, Holdings will receive repayment by wire transfer on Thursday by 5:00 PM. This notice period ensures that the standard “T+2” settlement cycle for all trades executed prior to the demand notice are completed and LSC’s margin is released before LSC has to fulfill the repayment to Holdings. This enhances LSC’s management and control of its liquidity.

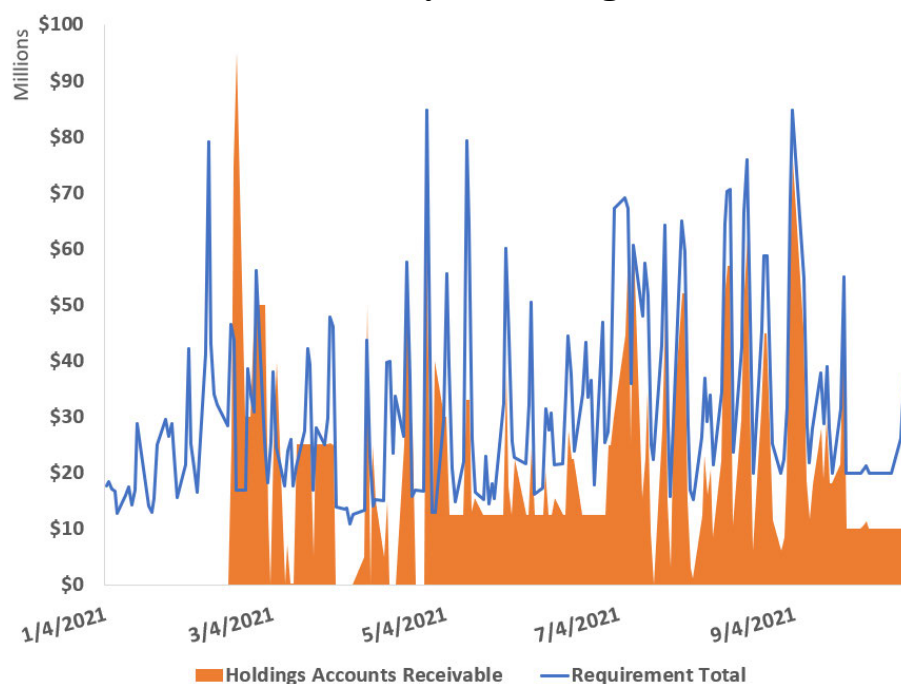
76. It seems reasonable for clients to fund margin calls that they themselves create. At the OCC and commodity exchanges, brokers use customer funds to finance customer margin requirements. Moreover, a broker may use money belonging to one customer to finance a margin call created by another customer since OCC requirements for a broker are computed on an aggregate customer basis.

77. Under LSC’s Holdings Promissory Note Program, and under LSC’s policy of pre-trade controls, each customer roughly funds the increase in the Fund Deposit Requirement that its trading would cause. It is not economically necessary for a broker to use its own capital to finance its customers’ trading. Brokers earn only a small commission, but customers trade as principals and are the right economic actors to fund their trading. Investors understand this, and, as a result, Holdings has not had difficulty raising funds from investors. The investors that provide funds to Holdings are large, sophisticated investors that understand and accept the risk of providing unsecured financing to a non-broker dealer without SIPC protection.

78. The Holdings Program has helped LSC meet the ECP requirements that arise from time to time. As **Table 1** shows, LSC's combined maximum VaR and MTM requirement in 2021 has been \$31,021,603. Because this is more than twice LSC's regulatory capital, NSCC has required additional deposits of approximately \$50 million as ECP. In turn, the promissory notes program has provided ample incremental liquidity for LSC on those days that settlement activity requires it. This is an effective and economically efficient solution that obtains the liquidity from the investors who drove the large settlement activity on those dates on an unsecured basis through LSC's parent. In fact, it is economically similar to how the NSCC pushes down its settlement risk to its member firms.

79. **Figure 5** below charts the Required Fund Deposit and the funds provided by the Holdings Program; it shows that the Holdings Program is being used to fill any gaps in LSC's funding of the Required Fund Deposit.

Figure 5 -- LSC's Required Fund Deposit and Borrowing under the Holding Promissory Note Program



E. Securities Lending Lines Provide Significant Incremental Liquidity to LSC

80. DTCC has questioned whether securities lending lines provide significant incremental liquidity to LSC. They do. LSC has arranged in excess of \$1 billion in stock loan facilities.⁵⁸ Securities lending counterparties have access to large pools of liquidity and will take almost any collateral to place assets in overnight investment funds and earn a spread. This is attractive for securities lending counterparties as there is generally no capital requirement or haircut on a matched book. Therefore, stock lending is available to finance debit balances even without identifying short

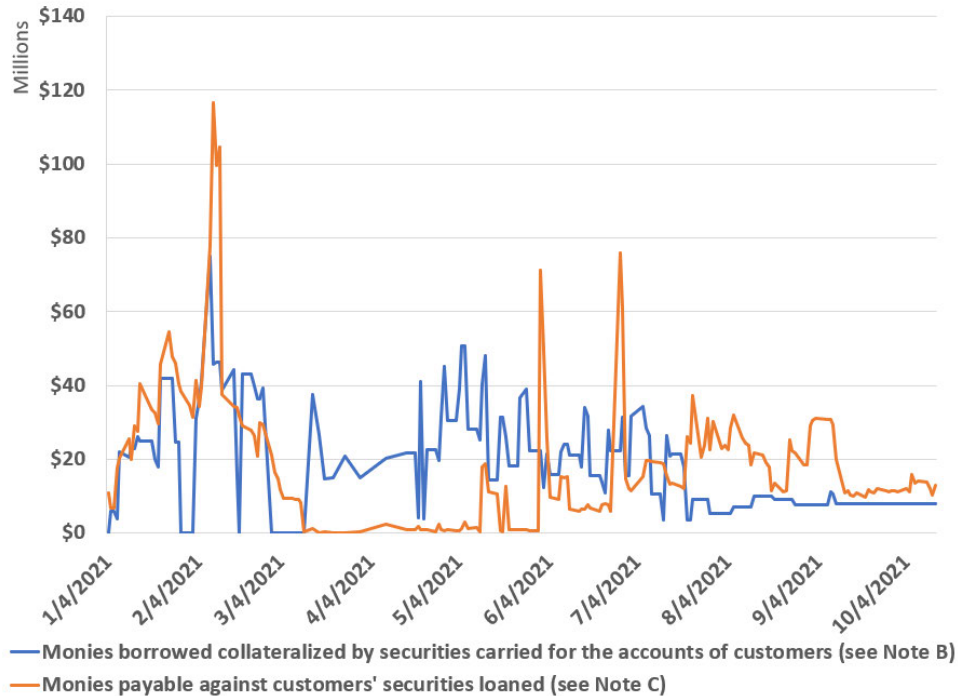
⁵⁸ Responses to DTCC Inquiries, p. 3.

sellers who would like to facilitate their short sales. Thus, stock loans are a reliable source of financing for the available collateral in margin accounts.

81. Stock loans generally carry more attractive terms than secured bank borrowing. As explained above, haircuts are lower than the typical secured bank facility. If the loaned securities are in especially high demand, the lending firm can raise funds at an effectively negative interest rate. Moreover, unlike banks, which prefer a diversified portfolio of high-quality securities for secured lines, borrowers in the stock lending market generally prefer larger blocks of the same shares as collateral. There are other, more restrictive conditions that apply to bank loans, making them less attractive than stock lending.

82. LSC's customer securities loaned activity and data is available from its weekly reserve calculations. **Figure 6** below shows the use of customer securities during January 4, 2021 and October 14, 2021 by LSC to collateralize bank lines of credit and for securities lending.

Figure 6 -- LSC's Use of Customer Securities for Collateralized Borrowing and Secured Lending 1/4/2021-10/14/2021



* Source: LSC's daily customer reserve bank account computation under 17 CFR § 240.15c3-3a - Exhibit A - Formula for determination of customer and PAB account reserve requirements of brokers and dealers under § 240.15c3-3: Line 2 - Monies borrowed collateralized by securities carried for the accounts of customers and Line 3 - Monies payable against customers' securities loaned.

VIII. Conclusion

83. LSC has met all applicable capital requirements, liquidity requirements and deposit requirements. LSC has instituted a promissory note program and a bank LOC whose total size exceeds its previous lines of credit. DTCC's determination that LSC's capital and liquidity are weak runs contrary to these facts.

84. As I have explained in this Affidavit, the fluctuations in LSC's settlement activity results from the uneven trade flows by certain large traders who from time

to time introduce a large amount of illiquid stock settlement activity and not from fluctuations in stock market conditions. These large traders not only fund their own trading activity within their LSC accounts under stringent margin regulations and LSC's house requirements, but also as unsecured investors in LSC's parent company which has instituted a Promissory Notes Program. Together with LSC's unsecured Lakeside Bank LOC, LSC's available unsecured funding capacity exceeds the largest spike in the Required Fund Deposit in 2021 of \$84 million by \$25 million.

85. The Holdings Promissory Notes Program matches LSC's liquidity source to LSC's fluctuating liquidity needs that result from certain customers' trading activity. The amount funded through this Program fluctuates from day to day. There is no fundamental economic reason that would require permanent capital to support fluctuating large settlement activity and such a requirement may have unintentional, adverse consequences.

86. As highlighted in the SEC Monitorship report, LSC has the necessary pre-trade controls to prevent any trading activity that would push its NSCC Required Fund Deposit above its liquidity sources. By meeting NSCC's stringent requirements in the last several months, LSC has demonstrated that its capital and liquidity position is strong, and it manages its trading activity and liquidity well.

87. In my opinion, LSC does not represent a heightened risk to DTCC, or to participants, creditors, or investors. A determination that LSC's capital and liquidity is not commensurate with its risk activity runs contrary to representations

that the NSCC maintains a risk-based margin system that considers and requires clearing fund deposits commensurate with the risk a broker's settlement activity introduces. The fact that LSC has met all such requirements contradicts the DTCC's determination that LSC's capital and liquidity is weak.



Emre Carr, Ph.D.

December 27, 2021

ADDITIONAL EXHIBITS

Table 1-A (Alternative to Table 1, with all Data As-is)

YTD 2021	VaR	MTM	VaR + MTM	ECP	Requirement Total
Count	197	182	182	161	197
Average	12,742,645	3,791,368	16,600,187	12,760,523	31,977,068
Median	12,431,255	3,217,435	15,747,402	8,745,536	27,378,094
95th Percentile	18,306,952	9,351,886	25,994,939	36,442,133	67,222,504
99th Percentile	21,252,135	11,100,883	29,141,546	47,679,193	79,608,114
Max	24,673,122	13,700,873	31,021,603	50,234,364	84,769,851
Total - 2021	2,510,301,102	690,028,984	3,021,234,040	2,054,444,142	6,299,482,422
% of Requirement	40%	11%	48%	33%	100%

*Source: LSC's daily NSCC requirements compiled by LSC. ECP has been charged on 161 days out of 197. Thus the average ECP computed above is over the 161 days with remaining 36 days having a zero ECP. MTM has been charged on 182 days out of 197. Thus the average MTM computed above is over the 182 days with remaining 15 days having a zero MTM. The calculation period extends to October 15, 2021 prior to the DTCC notices dated October 26, 2021.

Table 1-B (Alternative to Table 1 with Zeroes for all Components with No Values)

YTD 2021	VaR	MTM	VaR + MTM	ECP	Requirement Total
Count	197	197	197	197	197
Average	12,742,645	3,502,685	16,245,330	10,428,650	31,977,068
Median	12,431,255	3,066,830	15,403,054	6,167,319	27,378,094
95th Percentile	18,306,952	9,052,226	25,853,328	36,181,188	67,222,504
99th Percentile	21,252,135	10,989,969	28,952,164	46,946,136	79,608,114
Max	24,673,122	13,700,873	31,021,603	50,234,364	84,769,851
Total - 2021	2,510,301,102	690,028,984	3,200,330,086	2,054,444,142	6,299,482,422
% of Requirement	40%	11%	51%	33%	100%

*Source: LSC's daily NSCC requirements compiled by LSC. ECP has been charged on 161 days out of 197. Thus the average ECP computed above is over the 161 days with remaining 36 days having a zero ECP. MTM has been charged on 182 days out of 197. Thus the average MTM computed above is over the 182 days with remaining 15 days having a zero MTM. The calculation period extends to October 15, 2021 prior to the DTCC notices dated October 26, 2021.

DTCC Attachment 14

Via e-mail

July 21, 2021

Charles Lek
Chief Executive Officer
Lek Securities Corporation
4 World Trade Center, 44th Floor
New York, NY 10007
charles.lek@leksecurities.com

Re: Lek Securities Corporation: Membership in DTC and NSCC (Member #0512)

Dear Mr. Lek,

DTCC recently became aware of several material developments in regards to the liquidity profile of Lek Securities Corporation ("Lek"), which raises concerns about the firm's financial responsibility, operational capability and its continued ability to meet its obligations to NSCC and DTC. Among other developments, we became aware of the following:

- BMO Harris Bank reportedly reduced Lek's \$75MM line of credit to \$50MM, and informed Lek that it will further reduce the line to \$4MM as of August 4, 2021 and would terminate the line of credit as of September 6, 2021. Lek is reportedly in discussion with Lakeside Bank to increase its \$7.5MM line of credit and with Investors Bank for new line of credit to compensate for the reduction of the BMO Harris Bank credit facility, although definitive agreements have not yet been reached.

We note that, unless Lakeside Bank increases the amount available to Lek under its line of credit, or Lek obtains another facility from Investor Bank or another bank, as far as we are aware, Lek would have only \$7.5MM of external bank borrowing availability after the termination of the BMO Harris Bank line of credit in September 2021.

- BMO Harris Bank reportedly informed Lek it will no longer operate as Lek's Settling Bank as of October 6, 2021. Lek is reportedly pursuing the engagement of Lakeside Bank as its Settling Bank, although an agreement to establish this relationship has not yet been reached.
- FINRA is reportedly assessing the circumstances surrounding Lek's parent company's promissory note, under which Lek is a borrower, and, specifically, the impact of Lek's borrowings under this promissory note on Lek's customer reserve requirement.

We note that the result of this assessment could further greatly reduce Lek's liquidity.

Ongoing Membership Requirements: Reporting Requirements

Please confirm the accuracy of the above items, or provide written clarifications where necessary, including all relevant details regarding each of the three matters outlined above, in writing no later than **July 30, 2021**. Such information is required to be provided to NSCC and DTC pursuant to Lek's ongoing membership requirements set forth in the NSCC and DTC Rules, including, but not limited to NSCC Rule 2B and DTC Rule 2 and Lek's continued failure to provide this information could result in disciplinary action against the firm.

To that end, we note that Lek has already failed to provide NSCC and DTC with timely notification of the above described changes to Lek's financial condition, as required by its ongoing membership requirements set forth in NSCC Rule 2B and DTC Rule 2. Therefore, pursuant to Addendum P of the NSCC Rules and the DTC Fine

Schedule, Lek will be fined for this failure to provide timely notification. Notification of this fine will be delivered to Lek in a separate correspondence.

We also reiterate the importance of keeping DTCC apprised of all developments that could impact Lek's ability to remain a member in good standing at NSCC and DTC. Lek's ongoing membership requirements include timely notifications of any changes in the firm's liquidity resources, Settling Bank relationship, and any other material changes in condition or developments. For example, without limitation, Lek is required to inform us of any significant changes in its borrowing capacity under its stock loan/ borrowing arrangements.

This ongoing reporting requirement also requires, without limitation, Lek to notify us if there are any developments on FINRA's investigation into the recommendations in the final AML/Microcap settlement independent consultant's report, the counterclaims by Lek in regards to the consultant's report, or any changes to controls or business made by Lek as a result of this matter.

Request for Information

To allow NSCC and DTC to assess Lek's current financial condition, and pursuant to NSCC Rule 2B and DTC Rule 2, please also send us the following information by **Friday, July 30** at the latest.

- All recent correspondence with BMO Harris Bank relevant to both its line of credit and its Settling Bank relationship with Lek.
- A written plan on how Lek will address the reduction and ultimate termination of the BMO Harris line of credit and termination of its Settling Bank relationship with BMO Harris.
- Should the outcome of FINRA's inquiries into the structure of Lek's Promissory Note from its parent company lead to a full or partial negative impact on Lek's reserve requirements, how Lek intends to offset this impact to its liquidity.
- Information regarding Lek's parent company's financial standing and its funding/borrowing that supports the promissory notes it has extended to Lek, including all written materials and information provided to FINRA regarding these matters.

We remind you that Lek's ongoing membership requirements include the timely submission of any such information that NSCC and DTC may deem necessary or advisable, and your failure to comply with these requests will be deemed a violation of those requirements.

Ongoing Adequate Assurances Risk Controls

As noted above, the material developments described above raises concerns about the firm's financial responsibility, operational capability, and its continued ability to meet its obligations to NSCC and DTC. Therefore, pursuant to NSCC Rule 15 and DTC Rule 9(A), NSCC and DTC are also imposing the following risk controls to mitigate the risks such developments may present. Such controls will be effective until such time as we determine that Lek's risk profile has improved such that the above-mentioned liquidity concerns and any other material concerns have been alleviated.

- **Effective July 28**, Lek shall be subject to an increased Clearing Fund deposit, such that Lek's Required Fund Deposit to the NSCC Clearing Fund shall at all times be no lower than of \$31MM.
- **Effective July 28**, 2021 DTC will reduce Lek's Net Debit Cap to \$50 million from its current level of \$75 million.
- **Effective Friday, July 28**, in order to help us closely monitor Lek's available liquidity resources, Lek shall provide to NSCC and DTC a daily report detailing Lek's liquidity resources, including a description of all available liquidity resources, how much of each resources is utilized each day, and how much excess

liquidity is still available under each resources each day. Please see attached to this letter the required format of this daily report.

Please send the requested information to mleibrock@dtcc.com, dmcelligott@dtcc.com, thulse@dtcc.com, srosales@dtcc.com, and lpellecchio@dtcc.com. If Lek fails to provide the requested information in the required format by the prescribed due dates, NSCC and DTC will immediately consider additional actions available to them under their respective rules, which may include a restriction on Lek's access to NSCC's and DTC's services and facilities, and a termination of its membership with these clearing agencies.

We look forward to maintaining an open dialogue with Lek in connection with the matters described herein and in connection with our ongoing monitoring and assessment of the firm's risk profile and activities with NSCC and DTC.

This letter is without waiver of any of NSCC's, DTC's, and DTCC's legal and equitable rights, all of which are hereby expressly reserved, including, without limitation, NSCC's, DTC's, and DTCC's right to seek additional adequate assurances or take such other steps as it deems appropriate under its Rules and Procedures.

Sincerely,

Michael Leibrock
Managing Director
Depository Trust & Clearing Corporation

cc: Dan McElligott
Tim Cuddihy
Tim Hulse
Isaac Montal

Please provide the following Liquidity information on a daily basis, starting on July 23.

Using the table below, please provide an inventory of your firm's available liquidity sources and provide any supporting documentation (e.g. loan agreements, etc.). Please indicate the intended use of each liquidity source, which of these sources are available for meeting clearing fund requirements at DTCC, and any limitations or restrictions on the use of each liquidity source. Please provide documentation for each liquidity source as well.

Please describe what liquidity sources your firm typically uses to meet clearing fund requirement each day (i.e. what is your primary source, what is your secondary source, and what sources are available only as a back-up if additional liquidity is needed).

Please confirm whether your firm has had any significant change in its available liquidity resources since the last report provided to DTCC and confirm if the firm expects to have a need to raise any new sources of liquidity in the near term. If the firm has had or expects any significant change in liquidity, please describe the specific actions your firm has taken or plans to take and provide supporting documentation (e.g. executed or draft loan agreement).

Please describe the firm's liquidity stress testing (including the stress scenarios considered) and contingency plan in the event of an unexpected spike in the need for liquidity.

Source of Liquidity (i.e. name of counterparty, etc.)	Type of Liquidity Source (e.g. cash, line of credit, other)	Committed or Uncommitted	Secured or Unsecured	Intended Use	Available for Meeting DTCC Clearing Fund Requirements (yes/no)	Restrictions on Usage (describe)	Amount of Liquidity Source	Amount Currently Used			Balance Remaining	Collateral Available (if applicable)	Balance Available to Access
								Total	Used for Clearing Fund at NSCC and/or FICC	Used for Other Needs			
Example: TBD Bank	Line of credit	Uncommitted	Secured	Margin requirements	yes	N/A	\$30,000,000	\$8,000,000	\$3,000,000	\$5,000,000	\$22,000,000	\$12,000,000	\$12,000,000

Member Signature _____

Print Name _____

Print Title _____

Date: _____

DTCC Attachment 15

Via e-mail

July 28, 2021

Charles Lek
Chief Executive Officer
Lek Securities Corporation
4 World Trade Center, 44th Floor
New York, NY 10007
charles.lek@leksecurities.com

Re: Lek Securities Corporation: Membership in DTC and NSCC (Member #0512)

Dear Mr. Lek,

NSCC and DTC (collectively, DTCC) have reviewed the response from Lek Securities Corporation (“Lek”) dated July 26, 2021 (“Lek Response”) in connection with DTCC’s July 21, 2021 letter (“DTCC Letter”). As an initial matter, the Lek Response did not adequately address the questions in the DTCC Letter, nor did Lek provide DTCC with all the requested information and documentation. For example, the letter from Bank of Montreal Harris (“BMOH”) dated July 8, 2021 (“BMOH Letter”) is inconsistent with certain representations Lek made, both on the phone and in the Lek Response, that \$50MM of BMOH line of credit (“BMOH LOC”) will not be reduced and that it will continue past October 6, 2021. Specifically, the BMOH Letter states, in part:

I am now formally notifying you that BMOH will discontinue the settlement services it provides pursuant to the Agreement ninety days from the date of this letter, on October 6, 2021. In the interim, BMOH is reducing LSC’s uncommitted broker line of credit down from \$75,000,000 to \$50,000,000, effective immediately. Additionally, BMOH will reduce LSC’s NSCC sublimit to \$4,000,000 on August 9, 2021, and will reduce the sublimit to \$0 on September 6, 2021. BMOH will not extend any of these deadlines. To be clear, and for the avoidance of doubt, it remains BMOH’s position that LSC must transition all of its business (including, but not limited to, its settlement business with BMOH) away from BMOH and Bank of Montreal.

If Lek believes that the \$50MM of the BMOH LOC will not be reduced after August 9, 2021 or September 6, 2021 and/or that the \$50MM BMOH LOC will continue in full after October 6, 2021, Lek needs to provide DTCC with a letter of confirmation from BMOH as to Lek’s position that also clarifies: (i) what portion of BMOH LOC will remain after August 9, 2021, after September 6, 2021, and after October 6, 2021, (ii) what dollar amount would be available to Lek for meeting its requirements at DTC and NSCC after August 6, 2021, after September 6, 2021, and after October 6, 2021, and (iii) what relationship BMOH will have with Lek after October 6, 2021.

We further note that Lek did not seem to make a good faith effort to produce all recent correspondence with BMOH, as requested by DTCC, because it only provided the BMOH Letter. Although Lek claimed that it first learned of BMOH’s decisions with respect to its relationship with Lek on July 8, 2021, the BMOH Letter clearly indicates that conversations between Lek and BMOH have been ongoing on these topics since 2019, with several recent correspondences in May and June of this year. DTCC is therefore reiterating its request in the DTCC Letter, as well as specifically requesting all correspondence with BMOH since January 1, 2019 relating to the BMOH plans to change its relationship with Lek, including, but not limited to, correspondence related to the BMOH LOC and BMOH’s role as Settling Bank. Such correspondence should include, without limitation, the letters dated May 14, 2021, June 15, 2021, and June 23, 2021 that were referenced in BMOH Letter.

In addition, Lek needs to provide DTCC with a written plan and an updated summary of Lek’s expected liquidity resources after August 9, 2021, after September 6, 2021 and after October 6, 2021, as previously requested.

The table of liquidity resources on page 2 of the Lek Response (“Table”) is vague, confusing, and, as of now, unsubstantiated by Lek. First, the Table shows the BMOH LOC being reduced from \$75MM to \$50MM, but it does not reflect that BMOH will further reduce the \$50MM BMOH LOC to zero after October 6, 2021. If the BMOH LOC will end on October 6, 2021, then it should not be cited as a future source of liquidity in the Table. Second, the Table reflects an increase of Lek’s line of credit with Lakeside Bank to \$30MM. Lek has not yet provided DTCC with documentation (including all terms and conditions of the facility(ies)) from Lakeside Bank of the increase in the facility to \$30MM. Such documentation needs to also detail how the Lakeside facility can be used and what amount of the facility is available to Lek for meeting requirements at NSCC and DTC. Third, the Table reflects a future \$96MM in liquidity from Unsecured Notes but does not identify the specific source of those funds. If this line item is not referencing Lek’s promissory note with its parent company (“Lek Promissory Note”), which previously was disclosed as a \$100MM note, please provide DTCC with the documentation for these Unsecured Notes (including all terms and conditions of the Notes), including, but not limited to, how the funds can be used and what amount of the funds would be available to Lek for meeting requirements at NSCC and DTC.

If the “Unsecured Notes” line item in the Table is referring to the Lek Promissory Note, this should not be reflected as new source of funding that will supplement Lek’s liquidity in the future. It is DTCC’s understanding that the Lek Promissory Note has been in place since earlier this year – and DTCC believes that it would be misleading to note it as a new source of liquidity to offset the loss of liquidity support from BMOH. Further, with respect to the Lek Promissory Note, the DTCC Letter had additionally requested that Lek provide DTCC with its parent company’s financial standing and its funding/borrowing that supports the promissory notes it has extended to Lek, including all written materials and information provided to FINRA regarding these matters. In the Lek Response, Lek indicated that that it was attaching FINRA’s 8210 request, Lek’s answers to the request, and relevant documents. While there were documents provided with the Lek Response, DTCC was unable to view the documents since they were password-protected. Please provide copies of unprotected documents or the password to the protected documents. In addition, please ensure that Lek also provides any other responsive documents, including, but not limited to (i) the annual financial statements of Lek’s ultimate parent, Lek Securities Holdings Limited, the provider of the Promissory Note, for the three most recent fiscal years as well as its most recent year-to-date interim financial statement, and (ii) any material and information communicated to FINRA after the date of the Lek Response. This is critical because, although Lek represents that it has “more diverse” funding, it appears that the primary liquidity support for Lek is its parent company via the Lek Promissory Note, which demonstrates a lack of significant external liquidity support. Finally, Lek’s belief that there should be no concerns about the Lek Promissory Note notwithstanding, DTCC reiterates its request for Lek’s plan to offset a possible full or partial negative impact on its reserve requirement as a result of FINRA’s inquiries.

In addition to the above requests and the requests in the DTCC Letter, DTCC has additional follow-up requests relating to the Lek Response. First, Lek has indicated in the Lek Response that it has increased its borrowing capacity under its stock loan/borrowing arrangements. Please provide DTCC with specific details and documentation on how much this borrowing capacity has increased, the current borrowing capacity, who Lek’s counterparties are, and how Lek utilizes the liquidity under these arrangements. Second, the Lek Response indicated that Investor’s Bank intends to provide Lek with a \$20MM line of credit. Please provide DTCC with all the documentation (including all terms and conditions of the facility) from Investor’s Bank. The documentation should also detail how the Investor’s Bank facility can be used by Lek and what amount of the facility is available to Lek for meeting requirements at NSCC and DTC. Third, please provide an updated organization chart for senior management at Lek along with their job descriptions.

Finally, to reiterate DTCC’s request in the DTCC Letter, **effective July 30, 2021** (adjusted from July 28, 2021), Lek must provide to NSCC and DTC the requested daily report of Lek’s liquidity resources, including a description of all liquidity resources, how much of each resource is utilized each day, and how much excess liquidity is still available under each resource each day. Please see the DTCC Letter or pages [4-5] of this letter for the format and information to be provided each day.

Also **effective with Monday’s morning, August 2, 2021, collection of NSCC Clearing Fund** (adjusted from July 28, 2021) and as described in the DTCC Letter:

- Lek may be subject to an increased Clearing Fund deposit, such that Lek’s Required Fund Deposit to the NSCC Clearing Fund shall be, at all times, no lower than \$31MM.

- Lek's Net Debit Cap may be reduced to \$50MM.

Lek must send all requested information (and set forth in the DTCC Letter and this letter) to mleibrock@dtcc.com, dmcelligott@dtcc.com, thulse@dtcc.com, srosales@dtcc.com, lpellecchio@dtcc.com, and Credit-MarketRisk@dtcc.com no later than 12:00pm ET on **July 30, 2021**. If Lek fails to do so, NSCC and DTC will immediately consider additional actions, which may include, but is not limited to, a restriction on activity or a recommendation that NSCC and DTC cease to act for Lek.

DTCC reminds Lek that it is obligated to notify DTCC of developments that could impact Lek's ability to remain a member in good standing at NSCC and DTC, including, but not limited to, any changes in the firm's liquidity resources, settling bank, and any other significant developments. While Lek admitted in the Lek Response that such notification is "important," the Lek Response, in particular the BMOH Letter, reflects that Lek was aware of the pending material change in its credit and liquidity profile as a result of BMOH's termination for some time, and had failed to notify DTCC of these facts timely, as required by the DTC and NSCC Rules.

This letter is without waiver of any of NSCC's, DTC's, and DTCC's legal and equitable rights, all of which are hereby expressly reserved, including, without limitation, NSCC's, DTC's, and DTCC's right to seek additional adequate assurances or take such other steps as it deems appropriate under its Rules and Procedures.

Sincerely,

Michael Leibrock
Managing Director
Depository Trust & Clearing Corporation

cc: Dan McElligott
Tim Cuddihy
Tim Hulse
Isaac Montal

Please provide the following Liquidity information on a daily basis, starting on July 30.

Using the table below, please provide an inventory of your firm's available liquidity sources and provide any supporting documentation (e.g. loan agreements, etc.). Please indicate the intended use of each liquidity source, which of these sources are available for meeting clearing fund requirements at DTCC, and any limitations or restrictions on the use of each liquidity source. Please provide documentation for each liquidity source as well.

Please describe what liquidity sources your firm typically uses to meet clearing fund requirement each day (i.e. what is your primary source, what is your secondary source, and what sources are available only as a back-up if additional liquidity is needed).

Please confirm whether your firm has had any significant change in its available liquidity resources since the last report provided to DTCC and confirm if the firm expects to have a need to raise any new sources of liquidity in the near term. If the firm has had or expects any significant change in liquidity, please describe the specific actions your firm has taken or plans to take and provide supporting documentation (e.g. executed or draft loan agreement).

Please describe the firm's liquidity stress testing (including the stress scenarios considered) and contingency plan in the event of an unexpected spike in the need for liquidity.

Source of Liquidity (i.e. name of counterparty, etc.)	Type of Liquidity Source (e.g. cash, line of credit, other)	Committed or Uncommitted	Secured or Unsecured	Intended Use	Available for Meeting DTCC Clearing Fund Requirements (yes/no)	Restrictions on Usage (describe)	Amount of Liquidity Source	Amount Currently Used			Balance Remaining	Collateral Available (if applicable)	Balance Available to Access
								Total	Used for Clearing Fund at NSCC and/or FICC	Used for Other Needs			
Example: TBD Bank	Line of credit	Uncommitted	Secured	Margin requirements	yes	N/A	\$30,000,000	\$8,000,000	\$3,000,000	\$5,000,000	\$22,000,000	\$12,000,000	\$12,000,000

Member Signature _____

Print Name _____

Print Title _____

Date: _____

DTCC Attachment 16

Via e-mail

August 3, 2021

Charles Lek
Chief Executive Officer
Lek Securities Corporation
4 World Trade Center, 44th Floor
New York, NY 10007
charles.lek@leksecurities.com

Re: Lek Securities Corporation: Membership in DTC and NSCC (Member #0512)

Dear Mr. Lek,

NSCC and DTC (collectively, DTCC) have reviewed the responses from Lek Securities Corporation (“Lek”) dated July 26, 2021 (“Lek Response #1”) and July 30, 2021 (“Lek Response #2”) (and together the “Lek responses”) in connection with DTCC’s July 21, 2021 letter (“DTCC Letter #1”) and July 28, 2021 letter (“DTCC Letter #2”). Again, Lek fails to fully address the DTCC requests and questions and fails to adequately demonstrate that it has sufficient and reliable liquidity both in the immediate future and longer-term, particularly after the credit facility from BMOH terminates in October.

Please provide the following missing and follow-up information and documentation by Thursday, August 5, 2021:

1. A complete and accurate daily liquidity report. The daily liquidity study provided by Joseph Antico on July 30, 2021, signed by CFO Kristopher Minogue, was incomplete and inadequate, including the following:

- Lakeside Bank is listed as one liquidity source of \$30MM that indicates “yes” for whether this is available for meeting clearing fund requirements at NSCC. However, it is our understanding that two separate facilities comprise the \$30MM total and that only \$10MM of this facility is available for meeting clearing fund requirements at NSCC. For accuracy, please split this liquidity source into two lines to clarify this liquidity source and its availability for meeting clearing fund requirements at NSCC.

- The “Collateral Available (if applicable)” and “Balance Available to Access” columns of the daily liquidity study were left blank. These cannot be left blank because, given that all of these liquidity sources are Secured, the availability of each facility is dependent on the availability of collateral to support each source. These two columns must be completed to show how much liquidity Lek actually has available based on the amount of available collateral. Please also provide a total to the liquidity study to show the total liquidity available to Lek, without any double-counting of the available collateral. Please indicate on the liquidity study if any of these sources are dependent on the same set of collateral and, if so, they should not be added together to determine the total liquidity available to Lek.

- The liquidity study template that we provided also includes several narrative questions that were not addressed in the daily liquidity study provided by Lek on July 30, 2021. Lek is

required to answer each of these questions. The questions, as shown on page 5 of this letter, and as provided in DTCC Letter #1 and DTCC Letter #2, are:

- Please describe what liquidity sources your firm typically uses to meet clearing fund requirement each day (i.e. what is your primary source, what is your secondary source, and what sources are available only as a back-up if additional liquidity is needed).

- Please confirm whether your firm has had any significant change in its available liquidity resources since the last report provided to DTCC and confirm if the firm expects to have a need to raise any new sources of liquidity in the near term. If the firm has had or expects any significant change in liquidity, please describe the specific actions your firm has taken or plans to take and provide supporting documentation (e.g. executed or draft loan agreement).

- Please describe the firm's liquidity stress testing (including the stress scenarios considered) and contingency plan in the event of an unexpected spike in the need for liquidity.

2. Complete documentation on the financial standing of Lek's ultimate parent, Lek Securities Holdings Limited ("Lek Holdings"), the provider of the promissory notes and Lek's affiliate, Lek UK ("Lek UK"), a significant contributor to the promissory notes, and the specifics of Lek Holdings's funding/borrowing that supports the promissory notes to Lek, including all written materials and information provided to FINRA regarding these matters. In particular, but without limitation, Lek needs to provide DTCC with (i) the annual financial statements of Lek's ultimate parent, Lek Securities Holdings Limited, the provider of the Promissory Note, for the three most recent fiscal years as well as its most recent year-to-date interim financial statement, and (ii) any material and information communicated to FINRA, including, but not limited to, the document named "Lek Securities Holding Limited Ledger Balances.pdf" that Lek provided to FINRA and a copy of the response Lek will send to FINRA on August 4, 2021 in response to FINRA's second 8210 request.

3. Lek's plan to offset a possible full or partial negative impact on its reserve requirement as a result of FINRA's inquiries.

4. Lek Response #2 states that the Investors Bank and the Syndicated Loan Facility are not "certain to transpire." Please provide documents and correspondence that support Investors Bank interest/intent to provide Lek a \$20MM credit facility as well as estimated timing for when such line would be established. Please also provide documents and correspondence reflecting the status, discussion and projected timing of syndicate funding from Lakeside Bank.

5. If Lek does not have documents or correspondence relating to an Investors Bank credit facility or the Syndicated Facility, as requested above, please state so clearly in your response. In addition, given that (i) there isn't any certainty about the Investors Bank or syndicate bank facilities, (ii) Lek has not provided the requested information about the financial standings of either Lek Holdings or Lek UK (and so cannot be assessed by DTCC) and (iii) there is a possibility of a full or partial negative impact on Lek reserve requirements resulting from FINRA's inquiries, please explain: (1) how Lek would offset a possible full or partial negative impact on its reserve requirement as a result of FINRA's inquiries; and (2) Lek's belief that the increase of the line of credit from Lakeside Bank to \$30MM would be sufficient to meet Lek's liquidity needs at all times after the termination of the BMOH line, when the usage data shows that, although the average outstanding amount was just over \$27MM, Lek, utilized as much as \$75MM in February 2021 and over \$30MM as recently as July 2021.

6. An explanation of why the \$1MM guaranty from Samuel F. Lek for the \$10MM credit facility provided by Lakeside Bank is not a violation of the consent judgement and the offer of settlement between Lek Securities, FINRA, and the SEC in 2019 that included associational and penny stock bars for Samuel Lek for a minimum of ten years.

7. An explanation of how Lek utilizes the liquidity under the stock loan/stock borrow arrangements and whether this liquidity can support Lek's ability to meeting its clearing fund requirement at NSCC.

Lek must send DTCC all the requested information to mleibrock@dtcc.com, dmcelligott@dtcc.com, thulse@dtcc.com, srosales@dtcc.com, lpellecchio@dtcc.com, and Credit-MarketRisk@dtcc.com no later than **August 5, 2021**.

This letter is without waiver of any of NSCC's, DTC's, and DTCC's legal and equitable rights, all of which are hereby expressly reserved, including, without limitation, NSCC's, DTC's, and DTCC's right to seek additional adequate assurances or take such other steps as it deems appropriate under its Rules and Procedures.

Sincerely,

Michael Leibrock
Managing Director
Depository Trust & Clearing Corporation

cc: Dan McElligott
Tim Cuddihy
Tim Hulse
Isaac Montal

Please provide the following Liquidity information on a daily basis, starting on July 30.

Using the table below, please provide an inventory of your firm's available liquidity sources and provide any supporting documentation (e.g. loan agreements, etc.). Please indicate the intended use of each liquidity source, which of these sources are available for meeting clearing fund requirements at DTCC, and any limitations or restrictions on the use of each liquidity source. Please provide documentation for each liquidity source as well.

Please describe what liquidity sources your firm typically uses to meet clearing fund requirement each day (i.e. what is your primary source, what is your secondary source, and what sources are available only as a back-up if additional liquidity is needed).

Please confirm whether your firm has had any significant change in its available liquidity resources since the last report provided to DTCC and confirm if the firm expects to have a need to raise any new sources of liquidity in the near term. If the firm has had or expects any significant change in liquidity, please describe the specific actions your firm has taken or plans to take and provide supporting documentation (e.g. executed or draft loan agreement).

Please describe the firm's liquidity stress testing (including the stress scenarios considered) and contingency plan in the event of an unexpected spike in the need for liquidity.

Source of Liquidity (i.e. name of counterparty, etc.)	Type of Liquidity Source (e.g. cash, line of credit, other)	Committed or Uncommitted	Secured or Unsecured	Intended Use	Available for Meeting DTCC Clearing Fund Requirements (yes/no)	Restrictions on Usage (describe)	Amount of Liquidity Source	Amount Currently Used			Balance Remaining	Collateral Available (if applicable)	Balance Available to Access
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Example: TBD Bank	Line of credit	Uncommitted	Secured	Margin requirements	yes	N/A	\$30,000,000	\$8,000,000	\$3,000,000	\$5,000,000	\$22,000,000	\$12,000,000	\$12,000,000

Member Signature _____

Print Name _____

Print Title _____

Date: _____

DTCC Attachment 17

Via e-mail

September 13, 2021

Charles Lek
Chief Executive Officer
Lek Securities Corporation
4 World Trade Center, 44th Floor
New York, NY 10007
charles.lek@leksecurities.com

Re: Lek Securities Corporation: Membership in DTC and NSCC (Member #0512)

Dear Mr. Lek,

NSCC and DTC (collectively, DTCC) have reviewed the responses from Lek Securities Corporation (“Lek”) dated July 26, 2021 (“Lek Response #1”), July 30, 2021 (“Lek Response #2”) and August 5, 2021 (“Lek Response #3”) (collectively, the “Lek responses”) in connection with DTCC’s July 21, 2021 letter (“DTCC Letter #1”), July 28, 2021 letter (“DTCC Letter #2”) and August 3, 2021 (“DTCC Letter #3”) (collectively, the “DTCC letters”). The Lek responses have not fully addressed the questions and the requests for information in the DTCC letters. By providing incomplete and/or unclear responses, Lek has yet to demonstrate that it has sufficient and reliable sources of liquidity, in both the immediate future and longer-term, particularly as the credit facility from BMOH terminates as per its July 8, 2021 letter. In addition, Lek continues to fail to comply with its obligations under the NSCC and DTC Rules and Procedures, including, but not limited to NSCC Rule 15 and DTC Rule 9(A), by not furnishing DTCC with complete information and documentation relating to Lek’s financial responsibility and operational capability.

Please provide the following information by September 17, 2021:

1. Related to DTCC’s request for a complete and accurate daily liquidity report:
 - Explain why in some of the daily liquidity reports the firm labeled the \$100MM note from Lek Securities Holding Limited (or the “parent”) as “Secured” and some label it as “Unsecured”, and why when labeled “Secured” it indicated “N/A” for how much collateral is available to support the note.
 - In the daily liquidity report:
 - Please add a line to reflect “Total funding available”.
 - Include and answer in every daily liquidity report delivered to DTCC the 3 questions included in the daily liquidity template provided in DTCC’s Letter #3, in particular, but not limited to, the presentation of a liquidity stress test and contingency plan.
2. Related to DTCC’s request for complete documentation on the financial standing of Lek’s ultimate parent, Lek Securities Holdings Limited (“Lek Holdings”), , Lek UK (“Lek UK”), and the specifics of Lek Holdings’ funding/borrowing that supports the promissory notes to Lek, including all written materials and information provided to FINRA regarding the foregoing:
 - Explain the origin and use of the promissory note Lek UK received from the parent (per the parent’s June 2021 financial statements).

- Provide all communications with FINRA related to the “Lek Securities Holding Limited Ledger Balances.pdf” and provide an explanation of the information presented in this file.
 - Provide a copy of the Agreement to Pledge cited in the Lakeside Bank documentation you provided. Please explain what Lek meant in the August 5, Lek Response #3 with respect to the \$20MM line being secured by hypothecating customer securities, whereas the \$10MM being secured by Lek’s receivable from NSCC. Please also identify where this is referenced in the documentation.
 - We additionally note that Lek failed to fully comply with the below requests:
 - The request for a copy of the response Lek sent to FINRA in August in response to their second 8210 request as outlined in FINRA’s letter from July 21 as well as any other subsequent written communications on this matter.
 - The request for the audited consolidated and consolidating financial statements of Lek Securities Holding Limited for the last two fiscal years.
 - The request for the financial statements for Lek Securities UK Limited for the last three fiscal years and most recent available period.
3. Related to the DTCC request for a plan to offset the potential negative impact on reserve requirement from FINRA’s inquiries if FINRA were to take the position that the indirect customer borrowings under the promissory note borrowings were to be reflected as a credit item in Lek’s reserve calculation:
- Despite DTCC’s multiple requests, the only plan mentioned by Lek (in Lek Response #3) was to subordinate the promissory note borrowings. However, subordination of the borrowing would not necessarily change the way the indirect customer borrowings should be reflected in the reserve calculation, and this plan would not necessarily be sufficient to prevent a negative impact on Lek’s reserve requirement. Please provide Lek’s plan for alternative sources of liquidity in such a circumstance.
4. Related to the DTCC request for documentation supporting the potential credit line from Investor Bank:
- Lek’s response to this request in Response #3 included an e-mail from July 23 with no documents attached or reference to an amount under negotiation and that Lek would follow up with the bank about the status of the line. Please provide the current status of the bank’s evaluation, any additional correspondence with Investors Bank since July 23, and all additional documentation that demonstrates that Investors Bank continues to consider a \$20 million loan to Lek. Please also affirmatively state whether, or not, Investors Bank is still actively considering providing the line of credit to Lek.

If the information requested in this letter is not received by September 17, 2021 and/or Lek continues to fail to demonstrate that it has sufficient and reliable liquidity both the immediate future and longer-term, NSCC and DTC may institute further additional risk controls such as an increase in the minimum clearing fund deposit at NSCC or a further reduction in the net debit cap at DTC. NSCC and DTC may also consider additional actions, which may include, but is not limited to, a restriction on activity or a recommendation that NSCC and DTC cease to act for Lek.

DTCC reminds Lek of its obligations under the applicable Rules and Procedures to provide DTCC with complete and up-to-date information and documentation relating its financial responsibility – both in terms of the requests in the DTCC letters and other communications, as well as in terms of new and ongoing developments relating to its financial ability. Lek's continued failure to comply with such obligations may result in additional actions by NSCC and DTC as provided under their respective Rules and Procedures.

This letter is without waiver of any of NSCC's, DTC's, and DTCC's legal and equitable rights, all of which are hereby expressly reserved, including, without limitation, NSCC's, DTC's, and DTCC's right to seek additional adequate assurances or take such other steps as it deems appropriate under the applicable Rules and Procedures.

Sincerely,

Michael Leibrock
Managing Director
Depository Trust & Clearing Corporation

cc: Dan McElligott
Tim Cuddihy
Tim Hulse
Isaac Montal

Please provide the following Liquidity information on a daily basis.

Using the table below, please provide an inventory of your firm's available liquidity sources and provide any supporting documentation (e.g. loan agreements, etc.). Please indicate the intended use of each liquidity source, which of these sources are available for meeting clearing fund requirements at DTCC, and any limitations or restrictions on the use of each liquidity source. Please provide documentation for each liquidity source as well.

Please describe what liquidity sources your firm typically uses to meet clearing fund requirement each day (i.e. what is your primary source, what is your secondary source, and what sources are available only as a back-up if additional liquidity is needed).

Please confirm whether your firm has had any significant change in its available liquidity resources since the last report provided to DTCC and confirm if the firm expects to have a need to raise any new sources of liquidity in the near term. If the firm has had or expects any significant change in liquidity, please describe the specific actions your firm has taken or plans to take and provide supporting documentation (e.g. executed or draft loan agreement).

Please describe the firm's liquidity stress testing (including the stress scenarios considered) and contingency plan in the event of an unexpected spike in the need for liquidity.

Source of Liquidity (i.e. name of counterparty, etc.)	Type of Liquidity Source (e.g. cash, line of credit, other)	Committed or Uncommitted	Secured or Unsecured	Intended Use	Available for Meeting DTCC Clearing Fund Requirements (yes/no)	Restrictions on Usage (describe)	Amount of Liquidity Source	Amount Currently Used			Balance Remaining	Collateral Available (if applicable)	Balance Available to Access
								Total	Used for Clearing Fund at NSCC and/ or FICC	Used for Other Needs			
<i>Example: TBD Bank</i>	<i>Line of credit</i>	<i>Uncommitted</i>	<i>Secured</i>	<i>Margin requirements</i>	<i>yes</i>	<i>N/A</i>	<i>\$30,000,000</i>	<i>\$8,000,000</i>	<i>\$3,000,000</i>	<i>\$5,000,000</i>	<i>\$22,000,000</i>	<i>\$12,000,000</i>	<i>\$12,000,000</i>

Member Signature _____
 Print Name _____
 Print Title _____
 Date: _____

DTCC Attachment 18

