U.S. SECURITIES AND EXCHANGE COMMISSION

FINRA DEPARTMENT OF ENFORCEMENT,	:	
Complainant,	:	
v.	:	Admin. Proc. File No. 3-21516
RICKY ALAN MANTEI (CRD No. 1098981)	:	**ORAL ARGUMENT REQUESTED**
	:	
Respondent.		

APPEAL BRIEF OF RESPONDENT RICK MANTEI

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Respondent Rick Mantei respectfully submits this brief in support of his appeal from the FINRA National Adjudicatory Council ("NAC") Decision dated May 30, 2023. ("Decision") (R. 4358-89) For the reasons set forth below, the Decision should be reversed, the sanctions vacated, and the Complaint dismissed.

Preliminary Statement

The SEC recently warned: "FINRA cannot base liability on [a] suggestion [where] it is speculative and has no basis in the record." <u>In re David B. Tysk</u>, Exchange Act Release No. 91268 at 11 (March 5, 2021)(reversing findings of violations and imposition of sanctions). Neither the DOE nor the NAC connected the dots between DOE's charges, the policies ***as written,*** and Respondent's ***actual*** actions, relying instead on "interpretations" of those written policies – and not the plain words of the written policies – and speculation as to what certain employees of Respondent's firm J.P. Turner ("JPT") and its trading counterparties did or did not do to bridge critical factual gaps. Those are impermissible bases upon which to impose discipline.

Beyond the absolute failure of proof, the Decision should be reversed for five principal reasons. First, the Decision rests on two structured CD ("SCD") transactions; however, FINRA has no jurisdiction over those products because they are not securities and FINRA should not have been investigating much less evaluating Respondent's conduct as to them. Second, the entire case should be dismissed because DOE's years-long delays unfairly prejudiced Respondent. Third, DOE did not charge aiding and abetting as to Respondent, but its case was based on an aiding and abetting theory in that DOE's case assumed as matters of fact that JPT executed impermissible prearranged trades, but no principal liability was ever charged by JPT or any regulator or firm. Fourth, Respondent was unfairly prejudiced by the exclusion of his expert's testimony on the prearranged trading policy. Fifth, the sanctions dramatically increased by NAC

– a 30 day suspension taken to two three-month suspensions (and made consecutive rather than concurrent) without explanation and citation to any authority -- are much too harsh, considering that DOE proved no harm to JPT, customers, or the market and Respondent's liability is not based on violation of any substantive securities rule or regulation.

The Decision affirms the Hearing Panel's finding that "Mantei violated FINRA Rule 2010 and Municipal Securities Rulemaking Board Rule G-17 by **directing** prearranged trades with counterparties in contravention of his firm's prearranged trading prohibition to circumvent the firm's cross trade policy." (R.4360; emphasis added) As is detailed below, those two conclusions are fundamentally inaccurate because as to each transaction, Respondent did not as a matter of fact or law "direct" any "pre-arranged" trades that violated the very clear **written trading policies** of JPT as to cross trades.

The NAC's almost citation-free Decision rests upon tape recordings admitted into evidence that contain profane, cryptic, occasionally unprofessional, and immature and vague calls that Respondent knew were being recorded with Sam Palermo, the one JPT trader with whom he dealt. The calls are random, set no dates or times, discuss no counterparties or traders of those counterparties, form no agreements and express only Respondent's constant frustration with the opaque market and illiquid market in which accurate pricing for SCDs was very difficult to find. (R. 2228, 2298-2301, 2303) As he testified, "I wanted the paper. It was great paper. I wanted it back if I could get it. . . So because it's out there, if there is any way I can get it, I would like it. I've had my heart broken many times where I did that and called back five minutes later and they said, hey it's gone." (R. 2290-91) [1] Respondent had no "prearranged" or specific client in mind to

[1] The Complaint failed to acknowledge the complex, opaque and illiquid market for the products at issue and DOE thus expressed shock at the lively conversations Palermo had with his

sell the paper to if in fact it came back to JPT, as the NAC and Hearing Panel found (R. 3955 n. 83, 3958, 3959, 4369) Those fundamental facts make the transactions, without more, neither "prearranged trades" nor "cross trades."

The Decision also rests upon the deeply flawed testimony of JPT's Chief Compliance Officer, Ed Woll (who among countless memory failures could not recall when he graduated from college (R. 2332, 3972)). Remarkably, Mr. Woll constructed and approved one of the subject trades **in writing** (JX-5, R. 3589), facts the NAC simply ignored.

The Decision takes no issue with a 54 month delay to file a Complaint against Respondent; DOE waited until after JPT had filed its Form BWD (for reasons having nothing to do with Respondent). After that delay, DOE filed no charges for sales practices violations as it had threatened. (JX-25, R 3639-40) The 10 trades here purportedly representing the scheme were plucked out of the thousands of trades made at Respondent's very sizable branch each year (R. 1-18, 2772, 3493-96) and tens of thousands of trades reviewed by DOE in its investigation. (R. 3479-82, 2722, 1919-20)

Undisputed Facts Ignored by the Decision

The NAC summarily dismisses multiple material undisputed facts demonstrating that Respondent did not execute or approve any of the transactions at issue ***and*** facts that Respondent did not have the authority to execute or approve any of those trades. (JX-5, R. 3589-90, JX-9 through JX-17, R. 3599-24; R. 4375, 4376 n.18, 4382 n.26, 4383 n.28):

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counterparties. Respondent's expert, James Reilly, testified that SCDs are traded in "over-the-counter negotiated markets that are illiquid." (R. 2921) Patrick McWalter similarly testified that prices for SCDs are not shown on the TRACE system, and that there is no central public place to see "where CDs are actually trading, where they are actually clearing." (R. 821) Rather, a trader "[c]omes up with what he thinks the value of the CD is, based on market color and/or what his model says." (R. 2467)

a. Respondent was a retail broker sitting in a JPT branch in Lexington, South Carolina (R. 1926, Jx-2, R. 3579; R. 2439); the JPT bond trading desk was in Atlanta, Georgia (R. 1926-27);

b. Respondent had no ability to execute trades (R. 2440, 2826), had no access to or authority over the bond desk (R. 2365, 2802-03), and maintained no "inventory" at his branch (R. 2440-41);

c. Respondent did not speak to and did not know the name of the counterparty firms or traders (R. 1150, 1680, 2147, 2545);

d. Respondent did not know or set a price, date, time as to when a trade would be made for an alleged "cross trade" to be started or concluded (R. 2289-2290)**;**

e. the SCDs and bond at issue indisputably were sold out to the market by JPT for days and were thus at risk for respectively 13, seven, and two days (JX-5, R. 3589-90; JX-9 through JX-17, R. 3599-24; R. 6, 8, 9, 2009, 2390, 2441, 2443-44, 2951-52, 2955-56, 3965);

f. CCO Woll placed the sell order for the Wells Fargo SCD shares and approved the trade (JX-5, R. 3589);

g. through emails, JPT's General Counsel was aware of and involved in the Wells Fargo SCD transaction (JX-8, R. 3593-98; 2442-43);

h. Sam Palermo – the only JPT trader on the tapes – was the trader on only one trade of the 10 at issue – JPT's irrelevant buy of 10,000 shares of the Citibank SCD from the market (JX-17, R. 3623-24; CX-1, R. 3149); JPT trader Paul Raymundo executed six of the remaining trades (JX-5, R. 3589-90; JX-9 through JX-11, R. 3599-07; JX-15 through JX-16, R. 3619-24) DOE produced no evidence concerning who executed the other three trades; there is no evidence that Respondent ever spoke to or dealt with Raymundo or gave him "direction" of any type;

i. Because each of the subject trades went out to the market, JPT had no assurance that the counterparties would sell the products back to it or at any particular time or price and thus the trades could not by JPT's written definition be considered "cross trades" (CX-27, R. 3329, 3402; RX-40, R. 3497, 3500, R. 2441, 2511);

j. Respondent gained absolutely nothing financially from any of the activities with which he was charged (R. 4386)[2]; and

[2] Without citation to anything, the Decision finds that Respondent wanted to avoid the potential filing of a form U-4 disclosure by "settling" with a disgruntled customer regarding Wells Fargo

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k. Neither Respondent nor anyone else at JPT identified a customer or customers to sell the products to when and if those products were actually bought back by JPT from the market. (R. 2284-86, 2559)

Not only does the Decision ignore these facts, but then it simply dismisses their combined effect, casually concluding:

> "That Mantei **did not know** or **deal** with the counterparties, **did not** have access to the firm's trading system, and **did not** have formal authority over the firm's bond desk **does not negate** the fact that Mantei **devised the plan** to use prohibited prearranged trades to conceal customer-to-customer transactions that otherwise would have been subjected to J.P Turner's cross trade procedures.

(R. 4375; emphasis added)[3] This vague, non-specific summary dismissal is grossly disingenuous given that it may not be disputed that Respondent had **no** authority at all, and no **"formal"** authority, and there was no intra JPT **"customer-to-customer transaction."** FINRA Rule 2010 and MSRB Rule G-17 must be grounded in something and undisputed material facts that bring conduct within the legal standards of the industry cannot be dismissed as "irrelevant."

DOE's Case

Although JPT **never** took issue with the conduct of Respondent **or** any of its traders or supervisors~~,~~ five years ex post facto, DOE applied the JPT policies to two sets of Structured CD ("SCD") transactions and one set of municipal bond trades (R. 8-11):

SCD (R. 4386); but that client was not Respondent's. (JX-8, R. 3594; R. 3949 n.39) Woll, JPT's CCO, personally asked the firm's General Counsel and Respondent to deal with the issue before it developed into a Complaint. (JX-8, R. 3593-3594). Indeed, after the sale of the customer's SCD – as to which Woll signed the trade ticket (JX-5, R.3589-90) – Woll sent Palermo an email with a picture from the movie "Pulp Fiction", quoting the characters saying after a murder: "We happy?; Yeah, we happy." (JX-6, R. 3591) Respondent's role was working with members of his branch, his firm's CCO, GC and a trader to assure a client that his firm was trying to do the right thing, which his CCO apparently accomplished. (Id.) There is no evidence that JPT marked anyone's CRD over the event.

A. Wells Fargo Market-Linked Certificate of Deposit (the "Wells Fargo SCD") consisting of the following trades:

October 1, 2014: Sell 96,000 to the street
October 7, 2014: Buy 30,000 from the street
October 13, 2014: Buy 66,000 from the street

B. Fresno California Joint Powers Financing Authority Lease Revenue Taxable Capital Projects Series C Bond (the "Fresno Bond") consisting of the following trades:

December 22, 2014: Sell 30,000 to the street
December 26, 2014: Buy 10,000 from the street
December 26, 2014: Buy 10,000 from the street
December 29, 2014: Buy 10,000 from the street

C. Citibank Market-Linked CD traded in February 2015 (the "Citi SCD") consisting of the following trades:

February 25, 2015: Sell 40,000 to the street
February 26, 2015: Buy 40,000 from the street
February 27, 2015: Buy 10,000 from the street[3]

(R. 10, 12, 13)

<u>JPT's Bond Cross-Trade and Prearranged Trading Policies</u>

The JPT Bond Cross Trade policy states:

> A **cross-trade** occurs when an office sells a **bond** for **one** of its clients and purchases the bond for **another** of its clients. **These trades are executed internally by the firm and never reach the market**.

(JX-19, R. 3631; emphasis added). The Prearranged Trading Policy states:

> An offer to sell **coupled with** an offer to buy back at the same or a higher price, or the reverse, is a prearranged trade and is prohibited. Options or written agreements such as repurchase agreements are not included in this prohibition.

[3] Although the trade ticket for this 10th trade was submitted at the hearing (JX-17, R. 3623-3624), DOE did not charge anything as to this trade (R. 13), and it appears irrelevant to the charge of prearranged trading because it occurred after JPT had replaced the 40,000 shares of the Citi SCD.

(CX-27, R. 3402; emphasis added).

<u>The Flaws in DOE's Case and the NAC's Decision</u>

The NAC affirms the Hearing Panel's finding that "Mantei violated his firm's prearranged trading prohibition and circumvented the firm's cross trade policy by **directing** prearranged trading with counterparties to facilitate and disguise cross trades, in violation of FINRA Rule 2010 and MSRB Rule G-17" (R. 4371; emphasis added) The Decision alternatively states that Respondent "**devised a strategy** to use prearranged trades with a broker-dealer counterparty for the purpose of concealing what was in effect a sale from one firm customer to another firm customer." (R. 4373; emphasis added)

Analysis of the Decision and this case can stop with the following undisputed facts from the Record below: It is undisputed that (a) Respondent did not speak to or arrange with any counterparty a sale and buyback at any time (R. CX-2, R. 3151-3125; R. 2133, 2147, 1150, 3962); (b) all products that were the subject of the Complaint went to the market and were not "internal" trades (R.1929-30 (Hegeman); (R. 2441-43 (Woll)); (c) the SCDs were not "bonds" as a matter of law; and (d) no JPT customer is identified as being "prearranged" to purchase at any price in whole or in part any product bought back by JPT. (R. 2284-86, 2559) The NAC simply glosses over these core evidentiary facts and it is error to do that.

The Decision implicitly assumes that Respondent ran the JPT trading desk and had authority over it and that JPT had no compliance or supervision system. The Decision then applies **trading** policies to a retail broker and adopts the vague phrase that he "directed" the trades; but that ignores the industry terms of execution and approval and simply sets aside the realities and checks and controls of the securities industry. Next, contrary to all rules of legal construction, the Decision circumvents the plain and unambiguous language of the JPT policies at issue and either

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ignores obvious language or inserts its own speculation. The first analytical miss by the NAC is that two of the transactions at issue involved structured CDs which, because they are not bonds, are simply not covered by the "Bond Cross Trade Policy." The NAC deals with this difficulty by ignoring it. The second NAC failure is to ignore JPT's definition of a "cross trade" which requires that a trade is executed ***internally*** and does not go out to the market; again, the Decision ignores the very plain language of the rule. The tranches of securities at issue, the Wells Fargo SCD, the Fresno Bond and the Citi SCD, were out to the market for 13, 7, and 2 days respectively. (R. 10, 12, 13; CX-1, R. 3147-49)

The Prearranged Trading Policy required an "offer to sell coupled with an offer to repurchase at the same or a higher price" (CX-27, R. 3402), and there is no evidence that Respondent ever made such an offer to any counterparty. There is no evidence of that of course because, as the audiotapes demonstrated (CX-2, R. 3151-52), Respondent **never spoke to any counterparty.** In fact, DOE failed to offer any communication between **anyone** at JPT – including Palermo – and the counterparties as to two of the three transactions (the Fresno Bond and Citi SCD transactions.) (CX-2, R. 3151-52) The Decision ignores the plain language of the policies at issue, holding that the "totality of the evidence" refutes Respondent's "narrow" interpretation. (R. 4374) Presumably, the Decision here derisively equates "narrow" with "actual evidence that can be cited to," but that is improper.

The Decision, which does not cite the record for any elements of this "strategy," has the following false premise: "Palermo located counterparties for transactions and negotiated the terms of the transactions following Mantei's instructions" (R. 4361), but there was no proof of that. DOE presented just three taped conversations between Palermo and **one** counterparty (CX-2, R. 3151-52; CX-4, R. 3159-62; CX-11, R. 3195-99; CX-15, R. 3211) and no evidence that Palermo spoke to the counterparty on the one trade that he in fact executed. (CX-2, R. 3151-52) It may not be disputed that evidence as to that "locat[ing]" and "negotiat[ing]" is completely missing as to all nine of the relevant trades. Fairly put, the NAC makes no effort to get it right.

Traders other than Palermo – with whom Respondent did not speak – presumably executed nine of the trades at issue. (JX-9 through JX-16, R. 3599-22) With respect to the one trade in evidence that Palermo executed (CX-1, R. 3149), JPT's buy of 10,000 shares of Citi SCDs, it occurred **after** JPT's buy of 40,000 shares from the counterparty had been completed (in one purchase of 25,000 and another purchase of 10,000). Thus, Palermo's one trade had nothing to do with any alleged prearranged trading and the Complaint did not mention that trade. (R. 9) Significantly, DOE offered no evidence of any conversation – let alone any agreement – between Palermo and the counterparty to the one transaction that Palermo executed. (JX-17, R. 3623-24; CX-2, R. 3151-52)

Yet the Decision dismisses the critical undisputed facts: "Who ultimately executed the transactions is **irrelevant** to our finding of liability." (R. 4376 n.18; emphasis added) and similarly adds: "the fact that other firms were involved, and the trading occurred over multiple days, during which time the firms held the instruments, does not preclude Mantei's liability for directing Palermo to use prearranged trading." (R. 4383 n.28)

The Decision assumes that Mantei "devised" a "plan" (R. 4375), but does not provide details. A plan requires a detailed proposal for doing or achieving something and assigns tasks to a person or people with timelines and detailed tasks, identifies resources, and states specific goals. Mantei, who had no power or control over Palermo (or the other unnamed traders), had some wishful, furtive and speculative conversations with one person at his own firm with limited power, who then may or may not have had other conversations with other people (at other firms) on topics not in the record. The Decision makes no effort to connect the dots.

The Decision acknowledges the lengthy time periods before DOE brought its Complaint (R.4379) and also notes that more than two years elapsed between Respondent's On the Record examination and DOE's Wells notice to Respondent. (R. 4379-80) However, the Decision finds no significance in the inherent prejudice to Respondent caused by DOE's long delays. The Decision also dismisses Respondent's actual prejudice – the loss of access to witnesses, documents and audiotapes and the memory issues of the actual witnesses. Despite the fact that the FINRA investigator "could not recall who sat on the JPT bond desk and incorrectly testified that Palermo entered most of the relevant trades at issue when in fact he executed only one trade" (R. 4380), the Decision remarkably continues: "These facts **are not relevant** to our finding that Mantei, through his conversations with Palermo, directed prearranged trading with counterparties in order to circumvent his firm's cross trade procedures." (R. 4380; emphasis added) But these facts are critical. The Decision also holds that the failure of JPT's CCO to recall basic facts offered no evidence of prejudice. (R. 4380-81) Similarly, the NAC finds no prejudice in the fact that Respondent lost the ability to get audiotapes other than those cherry-picked by JPT and DOE – of other conversations between Respondent and Palermo and of conversations between the JPT traders who executed the orders at issue with the counterparties: "These audiotapes, even if they existed, **are not material**." (R. 4381; emphasis added) Particularly where the Decision's findings "are primarily based on recorded conversations and trading records," (R. 4380) the prejudice in Respondent's loss of access to other recorded conversations must be assumed.

Although the Decision recites the unambiguous cross trade and prearranged trading policies (JX-19, R. 3631; CX-27, R. 3329; R. 4361), it ignores their plain language. The NAC impermissibly turns to the extrinsic "totality of the evidence" (R 4374) allowing Woll to interpret the policy to include not just bonds, but the SCDs at issue here. (Id.) Next, despite the fact that all of the trades at issue reached the market and were not executed internally at JPT (CX-1, R. 3147-50; JX-5, R. 3589; JX-9 through JX-17, R. 3599-23) – thus not meeting the definition of a cross trade in the policy -- the Decision holds the transactions "were cross trades 'in substance.'"(R. 4374) The Decision adds: "the fact that other firms were involved, and the trading occurred over multiple days, during which time the firms held the instruments, does not preclude Mantei's liability for directing Palermo to use prearranged trading." (R. 4383 n.28) The NAC is not permitted to create ad hoc rules to make something a violation.

Moreover, the Decision also rests on patently erroneous statements of fact, e.g.,

> The firm's prearranged trading policy prohibited "an offer to sell coupled with an offer to buy back at the same or higher price, or the reverse." Mantei directed the **traders [sic]** on JPT's bond desk to do precisely that.

(R. 4375; emphasis added) But there was **no** evidence presented at the hearing that Mantei ever spoke to the "traders" who executed nine of ten orders at issue, let alone "directed" them (CX-2, R. 3151-52), and the use of the plural in the quotation cannot be dismissed as mere oversight. Further, that lack of proof cannot be ignored when coupled with the Decision's declaration that such basic facts do not matter: "Who ultimately executed the transactions is **irrelevant** to our finding of liability." (R. 4376 n.18; emphasis added)

In the same vein, the Decision's statement that "Mantei devised the plan to use prohibited prearranged trades to conceal **customer-to-customer** transactions that otherwise would have been subjected to JPT's cross trade procedures" (R. 4375; emphasis added) is inaccurate because these transactions were **not** "customer-to-customer." In fact, the Decision itself recognizes that "Mantei said that he did not have an ultimate customer in mind to buy the Wells Fargo R66 SCD until **well after** the customer sold it," (R. 4366 n.9; emphasis added). This provides further proof that these were not cross trades at all. Palermo's statement to Respondent "'We're not crossing it.'" (R. 4369) and Respondent's taking "cross" off the order ticket (R. 4369 n.12; JX-11, R. 3603) were correct.

In rejecting Respondent's point that the Hearing Panel's finding of liability proved only, at best, aiding and abetting, a charge not found in the Complaint, the Decision repeats the same false statement: "Rather, Mantei is directly liable for engaging in unethical and dishonest conduct for directing the J.P. Turner bond desk to use prearranged trades to circumvent J.P. Turner's cross trade policy." (R 4383) Adding more circular logic, the Decision states: "Mantei was given the opportunity to defend against the specific charges against him because the Hearing Panel found him liable for the charges brought against him in the Complaint." (Id.) But that misses the point entirely; Respondent did **not** instruct the JPT bond desk and there was no evidence to the contrary at the hearing. Respondent's "devising a plan" is not sufficient for direct liability. <u>United States v. Wilson</u>, No. CR 14-209-1, 2021 WL 4480845, at *7 (E.D. Pa. Sept. 30, 2021) ("Principal liability requires a defendant to commit the elements of an offense.")

Having already concluded that Respondent breached the Prearranged Trading Policy of JPT, the Decision makes the easy transition to its finding that Respondent's actions with respect to the Fresno Municipal Bond were "willful." (R. 4377) But, by the Decision's own reasoning, that finding requires a finding that Respondent "voluntarily engaged in the misconduct." (Id.) However, the evidence does not establish that **Respondent** engaged in misconduct.

ARGUMENT

The SEC has broad powers of *de novo* review over the Decision and can affirm, dismiss, modify, or reverse with respect to each finding, or remand the disciplinary proceeding with instructions. See Scottsdale Cap. Advisors Corp. v. Fin. Indus. Regul. Auth., Inc., No. CV 23-1506 (BAH), 2023 WL 3864557, at *3 (D.D.C. June 7, 2023) ("A NAC decision may then be appealed to the SEC… which conducts *de novo* review and may consider evidence not previously considered by FINRA"). The Decision below rests on numerous material errors of law and fact, any one of which should result in reversal of the Decision and its sanctions, and dismissal of the Complaint.

POINT I

STRUCTURED CDs ARE NOT SECURITIES AND FINRA HAS NO JURISDICTION OVER THEM

Two of the transactions at issue here involved SCDs, which are neither bonds nor securities. (CX-42, R. 3473; R. 2939-40, 3500) The Complaint did not allege that SCDs were either (R. 7), and DOE did not elicit testimony at the hearing to the contrary. As such, FINRA has no jurisdiction over those two transactions, yet DOE's investigation focused on these products and nuanced regulatory and sales practices conduct related to them. The NAC declines to address this issue in the Decision, instead ruling on a different point – whether the facts here violate FINRA 2010 – which misses the point, because if FINRA has no jurisdiction over SCD transactions, FINRA should not be present. [4]

FINRA has no jurisdiction over the two SCD transactions. FINRA's jurisdiction is limited to a member's business that involves securities or investment banking. FINRA's Restated Certificate of Incorporation specifies that its primary regulatory mission is:

> [t]o promote through cooperative efforts the **investment banking and securities business**, to standardize its principals and practices, to promote therein high standards of commercial honor, and to encourage and promote among members observance of **federal and state securities laws**. (emphasis added)

Similarly, FINRA Rule 12100(u) defines "person associated with a member" to mean, *inter alia*, "a natural person engaged in the **investment banking or securities business** who is indirectly controlling or controlled by a member. . .." (emphasis added)

Numerous federal appellate and district court decisions confirm that FINRA's jurisdiction is limited to a member's business that involves securities or investment banking. See Goldman Sachs & Co. v. City of Reno, 747 F.3d 733, 741 (9th Cir. 2014); UBS Fin. Servs., Inc. v. Carilion Clinic, 706 F.3d 319, 326 (4th Cir. 2013); Morgan Keegan & Co. v. Silverman, 706 F.3d 562, 566 (4th Cir. 2013).

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[4] The Decision cites several cases that support the breadth of FINRA Rule 2010 as covering misconduct that does not involve a security. (R. 4372) Thus, FINRA Rule 2010 covers: false statements about borrowing money from customers, DOE v. Davenport, 2003 NASD Discip. LEXIS 4 at *5 (NAC May 7, 2003); false statements about contributing to a charity in order to obtain matching funds, In re Goetz, Admin. Proc. File No. 3-9206, 1998 SEC LEXIS 499 at *11 (SEC March 25, 1998); evasion of federal currency reporting requirements, In re White, 2019 NASD Discip. LEXIS 30 at *41 (NAC July 26, 2019); false statements on customer's variable annuity applications, DOE v. Skiba, 2010 FINRA Discip. LEXIS 6 at *13 (NAC April 23, 2010); and improperly converting investors' funds to cover net capital deficiency, In re Grivas, 2016 SEC LEXIS 1173 at *11, *21 (SEC March 29, 2016). However, **none** of these cases raised or addressed the jurisdictional issue here, where FINRA has no jurisdiction over a banking product, namely a SCD.

SCDs cannot be morphed into securities and JPT's trading of them does not accomplish that. CDs and SCDs are bank instruments representing a deposit of a specified amount of money for a fixed period of time. The two kinds of instruments are not identical, in part because a traditional CD pays interest periodically based on a fixed or floating rate, whereas an SCD often pays interest periodically based on an underlying formula. Nevertheless, neither instrument constitutes a security when it is issued by an FDIC-insured domestic bank, except in limited situations not applicable herein. The United States Supreme Court held more than 40 years ago that CDs are not securities. In Marine Bank v. Weaver, 455 U.S. 551 (1982), the Supreme Court held that a $50,000 CD purchased by plaintiffs was not a security. In so holding, the Supreme Court underscored the fundamental differences between CDs and securities. First, the CD purchased by plaintiffs "was issued by a federally regulated bank which is subject to the comprehensive set of federal regulations governing the banking industry." Id. at 558. Second, "deposits are insured by the Federal Deposit Insurance Corporation" and "the purchaser of a certificate of deposit is virtually guaranteed payment in full, whereas the holder of an ordinary long term debt obligation assumes the risk of the borrower's insolvency." Id. Since the Supreme Court decided Marine Bank, numerous lower courts have held, consistent with that case, that CDs are not securities subject to regulation under the federal securities laws. This is primarily because "bank certificates of deposit are abundantly protected under the federal banking laws." Draney v. Westco Chem., Inc., 2023 WL 2186422, at *8 (C.D. Cal. Feb. 23, 2023) (citing Marine Midland).[5]

[5] Neither do the two SCD transactions at issue involve investment banking, which entails underwriting and the facilitation of mergers and acquisitions and corporate reorganizations. Investopedia, *Investment Banking: What It Is, What Investment Bankers Do* (Mar. 9, 2023), https://www.investopedia.com/terms/i/investment-banking.asp.

Federal banking laws provide a robust system of regulation. The U.S. Office of the Comptroller of the Currency (OCC) charters, regulates, and supervises all national banks and federal savings associations, and it regulates and supervises state-chartered banks that choose to become members of the Federal Reserve System. The FDIC directly supervises and examines state-chartered banks and regional banks that are not members of the Federal Reserve System. Zinman v. FDIC, 567 F. Supp. 243, 252 (E.D. Pa. 1983). Almost all banks are subject to the regulatory authority of more than one agency.[6]

The overall import of this substantial body of law is that FINRA rules cannot govern CDs or SCDs. Case law and commentary are in accord on this point. See Mraz v. JPMorgan Chase Bank, N.A., 2018 WL 2075427, at *5 n.4 (E.D.N.Y. May 3, 2018) ("FINRA rules govern securities transactions, not FDIC-insured bank accounts."); Mayer Brown LLP, *Structured Certificates of Deposit* 5 (2022), https://www.mayerbrown.com/en/perspectives-events/publications/2022/05/whats-the-deal-structured-certificates-of-deposit (noting that because SCDs generally are not securities, FINRA rules generally are inapplicable to their sales). In light of this overwhelming body of law, DOE was not authorized to investigate SCDs transactions or prosecute conduct related to them, but that is what it did.

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[6] Marine Bank has long been the law. See Dubach v. Weitzel, 135 F.3d 590, 592 (8th Cir. 1998) ("The district court correctly determined that the CD was not a security for the purposes of the federal securities laws. . .. To apply federal securities laws would 'double-coat the transaction."); accord Tafflin v. Levitt, 865 F.2d 595, 598-99 (4th Cir. 1989), aff'd, 493 U.S. 455 (1990); Wolf v. Banco Nacional de Mexico, S.A., 739 F.2d 1458, 1463-64 (9th Cir. 1984).

POINT II

IT WAS ERROR NOT TO DISMISS THE CASE IN LIGHT OF DOE'S UNJUSTIFIED DELAYS IN BRINGING THE CASE

The transactions at issue here occurred in late 2014 and early 2015; JPT took no issue with them, its supervisors approved them and its CCO was directly involved in all aspects of one of them. DOE opened its investigation here, according to Hegeman, in late 2014 or in 2015: "The time frame of our investigation was 2014 and 2015" (R. 1924) and filed its Complaint on August 1, 2019, more than 54 months later. Looking back from the August 2019 Complaint (R. 5-16), DOE delayed:

- **Four years and six months from the start of the investigation** (RX-1, R. 3479-81);
- **54 months from the last transaction** from the last act of alleged misconduct (the February 26, 2015 trade of the Citibank FN6 SCD) (CX-40; R. 8; JX-17, R. 3457-58, R. 3623-24);
- **More than three years** after it took Mantei's investigative testimony (JCX41, R. 3459)); and
- **Three years** after the end of the investigation on September 1, 2016) (R. 3969-70)

In addition, more than two years elapsed from the date of Respondent's OTR interview to the Wells Notice. (CX-41, R. 3459; JX-25, R. 3639-40, 4380) By the time the Complaint was filed JPT was out of business, most of the key players were long gone and unavailable to DOE and Respondent and key evidence and documents were lost. By the time the Hearing Panel held the Zoom hearing during the global pandemic in August 2020, memories and events from five and six years priors had well receded. DOE's Investigator, Hegeman, could not recall who sat on the JPT fixed income desk (R. 1925) or the name of the supervisors on the desk (R. 1926), and critically testified incorrectly that Palermo entered "most" of the trades at issue (R. 1934), when he actually entered just one. (R. 3589-90, 3599-22) Woll's recollection was particularly spotty relating to his conversations around the Wells Fargo transaction at the heart of the case (R. 2698, 3972). Woll could not even remember the year he graduated from college. (R. 2332, 3972) Similarly, Respondent could not recall critical details concerning the Wells Fargo SCD transaction including his interactions with Woll. (R. 1971, 1977, 2271)

DOE's Wells Notice threatened to charge violations of FINRA Rules 2010 and 4511, and willful violations of MSRB Rules G-8, G-14, and G-17 (JX-25, R. 3639-40), but eight months later, the Complaint charged **only** that Respondent violated JPT internal policies and FINRA Rule 2010 and MSRB G-17. (R. 14-15) This change of strategy by DOE further deprived Respondent of early notice of what actions he would have to defend.[7]

These delays alone justify dismissal of DOE's Complaint. In re Hayden, supra, 2000 SEC LEXIS 946, at *5. In Hayden, the Commission set aside the Hearing Panel's holding that Hayden had made unsuitable investment recommendations, misrepresentations, and omissions to investors in violation of the Securities Exchange Act and Exchange Rules, based exclusively on the Exchange's delay in bringing the disciplinary action against him. Id. at *6. The Commission based its holding on the Exchange Act provisions governing disciplinary actions: "a fundamental principle governing all SRO disciplinary proceedings is **fairness**." Id. at *4 (emphasis added). Without **any** consideration of prejudice or harm to Hayden (id. at *6), the SEC held that the Exchange's delays were "**inherently** unfair" to him. Id. at *4 (emphasis added). In fact, in Hayden,

[7] These delays resulted in the absence from trial of critical documents and witnesses. No complete tape recording was played at trial and the voice of one counterparty was heard but he never mentioned the name "Mantei." The witnesses who testified all had memory gaps on material facts due to the simple passage of time. (R. 3972, 3589-90; 3599-22; 1925-26, 1934 (Hegeman), 2332, 2698 (Woll))

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the SEC stated that it could not find, "as a factual matter, that Hayden's ability to mount an adequate defense was impaired by the Exchange's delay." Id. at *6. Despite that, the SEC went on to find inherent unfairness in those same delays. Id. See OHO Redacted Decision CAF000045, at 11, 17 (Dec. 14, 2001) (dismissing disciplinary proceeding "despite the seriousness of the charges and the alleged degree of investor harm," under Hayden, noting that the SEC in Hayden did not consider the underlying facts, nature of the charges or the relative equities, but ruled solely on the Exchange's delays in bringing the action). The same should apply to DOE's significant delays here.

In determining whether the proceedings were fair, the SEC in Hayden, reviewed four time periods:

> (1) the time between the first alleged occurrence of misconduct and the date the NYSE filed the Complaint (thirteen years and ten months); (2) the time between the last alleged occurrence of misconduct and the date the NYSE filed the Complaint (six years and seven months); (3) the time between the date that the NYSE received notice of the alleged misconduct and the date the NYSE filed the Complaint (five years); and (4) the time between the date the NYSE commenced its investigation and the date the NYSE filed its Complaint (three years and six months).

DOE v. Morgan Stanley DW lnc, No. CAF000045, 2002 NASD Discip. LEXIS 11, at *14-15 (NAC July 29, 2002, citing Hayden, 2000 SEC LEXIS 946, at *5-6). In Morgan Stanley, the NAC emphasized that "adjudicators should consider all four of the periods" referenced in Hayden. Morgan Stanley, 2002 NASD Discip. LEXIS 11, at *22 n.12.

Here, the period between the start of the investigation and the filing of the Complaint (four and a half years) is a longer period than in Hayden – by a year. In Morgan Stanley, the NAC recognized the inherent unfairness of excessive delay in bringing an action:

> after a certain period of time it is unfair to require respondents to attempt to piece together defenses to old claims. With the passage of time, memories fade, witnesses become unavailable, and documents are lost or destroyed. Indeed, **even without a showing of actual harm**, it can be inherently unfair to require respondents to face the prospect of potential claims for prolonged and indeterminate periods of time.

Id. at *17-18 (emphasis added). In Morgan Stanley, the NAC noted that requiring actions to be brought in a reasonable amount of time serves another important purpose: it encourages self-regulatory organizations "to investigate promptly wrongdoing and prevents adjudicators from being overburdened with stale claims." Id. at *18 n.10. Thus, delays of a certain length – such as those here, of multiple years – are presumed to be unfair, **without** a showing of prejudice.

In this case, the elapsed time periods of DOE's delays are significant and in one respect ***longer*** than those in Hayden. Standing alone, these delays necessitate dismissal. First, Respondent's last act of alleged misconduct was in February 2015 (R. 8) DOE did not file its Complaint until August 2019, four and one-half years later. (R. 16) Second, DOE became aware of the facts upon which the claims at issue are based no later than April 17, 2015, more than four years before it filed the Complaint. (CX-40, R. 3457-58; R. 3969-70) Third, DOE's Investigator, Michael Hegeman, testified that the "time frame of our investigation was 2014 to 2015" (R. 1670), almost five years before DOE filed its Complaint in August 2019, and significantly longer than the period in Hayden. In addition, DOE waited eight months after it served its Wells Notice on December 3, 2018 (JX-25, R. 3639-40) to file the Complaint. (R. 16)

Critically, in the intervening period between DOE's investigation and its Complaint, JPT, which indisputably was the repository for almost all the evidence in this case[8] filed a Form BDW on February 4, 2016 (R. 787, 795), to withdraw as a broker-dealer member, which was accepted shortly thereafter in April 2016. (R. 787, 801) As a result of DOE's delays, Respondent was severely prejudiced in his ability to interview witnesses and gather and review documents, emails, and audiotapes, particularly from JPT, which had disappeared. Respondent's evidentiary disadvantage here lies in stark contrast to DOE's unfettered access to witnesses and records. (R. 1670, 1705) With respect to Respondent's inability to access JPT audiotapes other than the ones cherry-picked by JPT and DOE, the Decision simply states: "These audiotapes, even if they existed, are not material." (R. 4381) But audiotapes of Palermo and other JPT traders with counterparties might have confirmed that Respondent did not commit prearranged trading or further confirmed Respondent's regular vague rambling diatribes about his "love" of certain fixed income paper, his problems with the lack of price transparency and product visibility, his frustration when his clients directed him to sell, and his desire to recommend the product to other clients.

Respondent lost access to various important witnesses who had left the business in the years between DOE's investigation and the filing of the Complaint, beyond the names of counterparties whose names he did not know. (R. 1738-39). Had he been available and still in the business, Palermo could have testified to the fact that he did not work for Respondent and was not required to take direction from Respondent; that he did not execute prearranged trades; and that he

[8] Apart from the counterparty firms on the trades at issue, with whom Respondent never dealt and whose identities Respondent did not learn until the hearing. (R. 2545) The names of the traders at those firms – who in theory would be liable for executing "prearranged" trades – have never been disclosed.

was properly supervised and was not disciplined for anything that he did or did not do regarding business from Respondent's branch. The NAC believes that a complete factual record would be "inconsequential." (R. 4382) Given that Respondent was charged with searching for firms and traders he never dealt with, the burden on him pre-trial was impossible.

Meanwhile, incredibly, FINRA Investigator Hegeman testified that FINRA did not even **ask anyone** at counterparty firms Janney Montgomery and RBC about the transactions at issue, and with respect to counterparty Maxim, FINRA spoke to trader Marciano, but did not ask him any substantive questions. (R. 1950-54) Neither did FINRA ask those firms for documents: Hegeman said: "Aside from those trade records from Maxim, no we didn't go to the other firms." (R. 1954) Despite the fact that FINRA would have had access to those firm's traders, salespeople, and supervisors (R. 1953-54), it never took advantage of those resources and instead delayed and delayed until documents were gone – indeed, until JPT was gone – and memories had sharply faded.

As a matter of law, DOE's delays in finally filing the Complaint were inherently prejudicial to Respondent, and the actual prejudice to Respondent is clear from this record and from the language of the Decision itself. Based on the In re Hayden and Morgan Stanley precedents, all claims should be dismissed on the basis of this fundamental unfairness.

POINT III

IT WAS ERROR TO FIND THAT RESPONDENT VIOLATED JPT'S WSPs

The JPT Cross-Trade Bond Policy defines cross trade:

> A cross-trade occurs when an office sells a ***bond*** for one of its clients and purchases the bond for another of its clients. **These trades are executed *internally* by the firm and never reach the *market*.**

(JX-19, R. 3631, 3633; emphases added) The fact that Respondent was not a trader and **did not**

act as trader regarding any transactions, makes no difference to the Decision's holding. (R. 4383 n.28) Like the Hearing Panel, the NAC elects to disregard the very simple and plain language of the policy. Instead, the Decision inserts "the totality of the evidence" to "interpret" and in essence re-write the actual language of the policy and hold that the transactions were cross trades "in substance" (R. 4374) and that the policy applied to SCDs, which undisputedly are not bonds. (R. 4374) That is not analysis or logic or reasonable rule interpretation. It is fundamentally unfair. Respondent's taped conversations about certain clients who wanted to sell and then his desire for JPT to continue to buy the same or similar products are the NAC's main focus. (R. 4380)

Lacking any analysis, the Decision reads out of the relevant policy the term "bond" and instead substitutes "fixed income product," based on Woll's extrinsic view of the policy's "meaning". (R. 4374) The Decision proceeds to ignore the definitional requirements that cross trades be "executed internally" and "never reach the market" by adopting DOE's contrary interpretation that the trades at issue were "cross trades 'in substance'" -- without any guidance or definition as to what a "trade in substance" might be. (R.4374) Trades are trades and made for notionally trillions of dollars a day to the penny and not made "in substance". To find Respondent liable, these gyrations are used to set aside the actual JPT Policies that governed the transactions.

It is hornbook law that clear unambiguous statutory language must be given its plain meaning, **without extrinsic evidence of interpretation or custom and usage**. <u>BedRoc Ltd., LLC v. United States</u>, 541 U.S. 176, 178 (2004) ("The inquiry begins with the statutory text, and ends there as the text is unambiguous."); <u>Safety Nat'l Cas. Corp. v. Certain Underwriters</u>, 587 F.3d 714, 750 (5th Cir. 2009) ("Where the statutory text is unambiguous, there is neither need *nor warrant* to look elsewhere. A court should depart from the official text of the statute and seek extrinsic aids to its meaning *only if* the language is not clear or if apparent clarity of language leads

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to absurdity of result when applied.") (emphasis in original), cert. denied, 560 U.S. 902 (2010); accord A. T. Massey Coal Co. v. Barnhart, 472 F.3d 148, 172 (4th Cir. 2006). This standard applies to contracts as well. E.g., United Ass'n of Journeymen & Apprentices of the Plumbing & Pipe Fitting Indus. of the United States & Canada v. Gemma Power Sys., LLC, 22-7109, 2023 WL 4113333, at *2 (D.C. Cir. June 22, 2023) ("If the parties' intent can be determined from the face of the agreement because its words are "clear and unambiguous," then a court's inquiry ends with the text.") (internal quotations omitted). No person from the NAC, the Hearing Panel, DOE or JPT (which used them for years) ever suggested that the JPT compliance policies were ambiguous in any way.

DOE's Investigator Hegeman admitted that all transactions "reached the market" (R. 2009) and were not executed internally at JPT. JPT President Dean Vernoia testified that "[a] distinguishing factor between a cross trade and a regular market trade is that the cross trade does not go to the market." (R. 2849) Woll and Reilly both testified that the three transactions were not "cross-trades." (R. 2443-44, 2390, 3965)[9] Perhaps in response to this evidence, the Decision goes one large step beyond avoiding the language of the cross trade policy to hold that whether the trades were cross trades **"does not matter"**; liability still attaches to Respondent, even if the Bond

[9] Woll admitted that he never **told** Respondent or his staff that the Bond Cross-Trade Policy applied to CDs. (R. 3967) Holding Respondent accountable to an interpretation of a firm policy that is **contrary** to the actual terms of the rule itself and which was **never communicated** to Respondent is fundamentally unfair. See Upton v. SEC, 75 F.3d 92, 98 (2d Cir. 1996) (vacating SEC order issuing sanctions for conduct that violated an SEC rule interpretation memo that was not issued until after the alleged violation of the rule, reasoning that the alleged violator "was not on reasonable notice that [it]'s conduct might violate the Rule"); Timpinaro v. SEC, 2 F.3d 453, 460 (D.C. Cir. 1993) ("[a] vague rule denies due process by imposing standards of conduct so indeterminate that it is impossible to ascertain just what will result in sanctions") (internal quotation marks omitted).

Cross-Trade Policy does **not** apply to the SCD transactions. The Decision restates its one-liner: "Mantei's liability is premised on his circumvention of his firm's written supervisory procedures by directing prohibited prearranged trading" and then adds: "**not** the applicability of the cross trade policy to the transactions." (R. 4374) This is quite a development; if the applicability of the Bond Cross Trade Policy does not matter, the Complaint has no basis, and the case should be dismissed.

Respondent cannot fairly be held to have devised a scheme of prearranged trading with Palermo, who did not execute any of the purchase orders that match the earlier sell orders. There is absolutely no evidence as to how the other trades were accomplished. Respondent did not deal with any JPT trader other than Palermo (CX-2, R. 3151-52)) and did not know of or communicate with the counterparties to the transactions directly or indirectly (Id.; R. 2133, 2147, 1150, 3962), and the record established that he did not know who they were. (R. 2147, 2545) Respondent had no access to JPT's trading systems and no authority over the fixed income desk or its business conduct. (R. 2365, 2802-03) Thus, Respondent could not execute the trades himself and could not "direct" a JPT trader to do anything regarding price, volume, or timing of trades. (R. 2018, 2440, 2826) Those missing items, of course, are key ingredients to an overarching plan.

To find against Respondent and sanction him, the Decision should delineate as to each transaction what Respondent did, when, where and how, but it does not. Instead, it says: "Palermo located counterparties for transactions and negotiated the terms of the transactions following Mantei's instructions." (R. 4361) As to that "locata[ting]" the Decision does not bother to go through the exercise of who, what, when, where, price, date, time, counterparty, or any other nuance because it would lay bare that Respondent had nothing to do with the transactions and was nowhere near them.

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Even Woll testified that, without more, he could not say that two transactions – the Fresno bond and the Citi SCD – were prearranged. (R. 2712) When JPT sold products to the market, Respondent did not have a customer in mind that he could sell it to if JPT bought the product back. (2284-86, 2559, 4366 n.9, 4369) All of the transactions went out to the market and thus moved the market risk to the counterparty for 13 days, seven days, and two days, respectively. (JX-5, R. 3589-90; JX-9 through JX-17, R. 3599-3624; R. 2446-47, 2951-52, 2955-56)

With respect to whether the counterparty was free to sell the product, Patrick McWalter (of Morgan Stanley at the relevant time) testified: "Yes, they did have the ability to sell at any time. Typically, the common practice with a circle is you would call the person that has circled it and say, 'I have another buyer looking to buy this. Either you need to purchase it now or we're going to sell it away from you.' That term is referred to as a fill or a kill." (R. 2497)

DOE did not attempt to prove any harm to any investor or to the market. (R. 3983 n.288, 4386) Respondent's expert, Reilly, confirmed that there was no such harm. (R. 2915) Reilly compared the trades at issue with trades of similar investments and found that for the SCDs, the prices to customers in this case were "reasonable prices given the various factors, including the low liquidity in these products." (RX-40, R. 3501) With respect to the Fresno Bond, he concluded that "the trades executed for JPT customers are well within the prices and current yields for other trades on this bond." (Id.) His overall conclusion was: "I do not find any evidence of customer or market harm in these trades." (Id.)

Yet the Decision dismisses with little or no discussion the following undisputed facts as **irrelevant** to the finding that Respondent devised a plan and directed the JPT bond desk to enter prearranged trades to circumvent the JPT Bond Cross Trade Policy:

- Respondent did not know or deal with the counterparties (R. 4375)

- Respondent did not place any of the trades (R. 4383 n.28)
- Respondent had no access to firm's trading system (R. 4375)
- Respondent had no authority over the bond desk or Palermo (R. 4375, 4382 n.26)
- Palermo executed only one of the trades (R. 4376 n.18, 4382 n.26, 4383 n.28)
- Respondent did not speak to the other traders on the desk (R. 4375-76)
- The order records showing who executed the trades (JX-5, R. 3589-90; JX-9 through JX-17, R. 3599-24; R.4383 n.28)
- DOE proved no harm to the market or to customers (R. 4383, 4386)
- Respondent had no intent to manipulate the mkt (R. 4383)
- The plain language of the Policies (R. 4374-75)
- The small number of transactions at issue (three) (R. 4386)
- At the time JPT sold the products to the market, Respondent had no customer identified to whom he would sell the products if JPT bought them back (R. 2284-86, 2559, 4366 n.9, 4374)

Only speculation can connect Respondent to the charged violations – speculation that Respondent talked to the traders on the bond desk and could – and did – order them to execute the subject transactions; speculation that Palermo spoke to the bond desk; speculation that Respondent spoke to the counterparties; speculation that somehow Respondent executed the subject transactions himself; and speculation that Respondent set the price and time of the trades at issue. DOE presented no evidence of any of these points.

Speculation caused the SEC to reverse the NAC's findings and sanctions in the Tysk case. In Tysk, a registered representative supplemented his customer contact notes **after** that customer complained that Tysk had recommended unsuitable investments. In re Tysk, Release No. 91268 at 2. Tysk was "'bothered'" that his notes in the firm's computer system that record client contacts, ACT! did not show the "true extent of his contacts" with that client. After the dates of contact with that customer had passed, Tysk went back to add approximately **70** contact notes, entering the dates of contacts, not the dates he added the entries. Tysk testified that because the relationship with the client was ending, he 'wanted to preserve . . . details of a complicated and personal relationship.'" Id. at 3. Further, in supplementing his entries into ACT!, Tysk overrode the ACT! default prompts that would have automatically populated the date of the entries. Id. at 8.

DOE charged Tysk with a violation of FINRA Rule 2010 for Tysk's "violation of his firm's policies," despite the fact the firm itself had not found a violation of its internal policies or its Code of Conduct. Tysk, Release No. 91268 at 8-9. After the Hearing Panel found Tysk liable, fined him $50,000, and suspended him for three months, the NAC increased Tysk's suspension to one year. Id. at 6. The SEC reversed the NAC's ruling the first time for lack of clarity "to discern why FINRA had found violations." Id. On remand, the NAC held that Tysk violated his firm's retention policies and violated FINRA's ethical rule by "'intentionally backdat[ing] his ACT! Notes' . . . which 'created the impression that he wrote contemporaneous notes." Id. The NAC imposed a $50,000 fine and a one-year suspension.

Although it was undisputed that Tysk had backdated his client contact notes, the SEC reversed, finding that the "record does not show that Tysk violated FINRA Rule 2010 and NASD Rule 2110 [FINRA Rule 2010's predecessor] by intentionally backdating his ACT! notes to create the false impression that he wrote contemporaneous notes of his conversations with his client." Tysk, Release No. 91268 at 13. The SEC found Tysk's explanation that he was trying to create a chronological record "plausible." Id. at 8. In its decision, the SEC held: "A violation of firm policy **does not necessarily** mean that a registered representative has also violated [FINRA Rule 2010 and NASD Rule 2110]." Id. at 10, Significantly, the SEC rejected the NAC's conclusion

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that Tysk "'threatened the integrity of the arbitration process' because without the forensic expert's review of Tysk's computer, "'Tysk may well have hidden the truth from the arbitration panel.,'" and held that "FINRA cannot base liability on this suggestion because it is speculative and has no basis in the record." Id. at 10-11.

The significance of the Tysk decision is that despite the behavior by the registered representative in intentionally backdating client contact records, the SEC questioned all of the NAC's assumptions that led to its findings and sanctions and required **proof** of every aspect of the case to support DOE's charges. This is summarized in its holding that FINRA liability cannot be based on speculation but must be based on evidence in the record. Tysk, Release No. 91268 at 11. That reasoning must be applied here to the undisputed facts that counter the speculation that Respondent "directed" the JPT traders to enter prearranged trades with counterparties in order to violate two JPT policies.

POINT IV

COUNT II FOR VIOLATION OF MSRB G-17 SHOULD BE DISMISSED

With respect to the alleged violation of MSRB Rule G-17 based on JPT's transactions in Fresno municipal bonds, DOE's failure of proof is striking. DOE offered tape recorded calls between Respondent and Palermo, but presented **no evidence** that Palermo or **any** JPT trader spoke to the counterparty involved. (CX-2, R. 3151-52) There is no evidence that anyone from JPT, much less Respondent, reached any sort of agreement with the counterparty – the critical element of a prearranged trade. Further, DOE presented **no evidence** that Palermo executed any of the Fresno bond transactions. (JX-11 through JX-14, R. 3607-14) There was no evidence that Respondent or Palermo spoke to the JPT bond desk about the Fresno bond. (CX-2, R. 3151-52) There was no evidence that either Mantei or Palermo spoke to Paul Raymundo, the

JPT trader who sold the Fresno bond shares to the street. (Id.) With respect to the sale from the customer to JPT, the evidence shows that the order ticket was "submitted from Mantei's branch office [JUE]," not by Mantei. (R. 4368; JX-11, R. 3603-07) Further, DOE established that Mantei had no particular customer in mind to buy Fresno bonds if JPT ever bought them back (R. 2285, 2559**)** and the order tickets indicate that JPT's purchase of bonds was not completed until seven days after JPT's sale. (JX-11 through JX-14, R. 3607-14) Thus, DOE simply failed to prove there was an offer to sell coupled with an offer to buy back **or** that a cross trade occurred that involved Mantei much less was orchestrated by him. Moreover, "DOE offered no evidence about Mantei's payout for the trades at issue, and there is no evidence that Mantei personally benefitted from any markup or markdown related to the transactions at issue." (R. 4386)

This fact pattern renders the Decision's finding of "willfulness," which depends on whether Respondent "voluntarily engaged in the misconduct" (R. 4377), impossible as a matter of the proofs that exist in the record. Surely the Decision does not cite to them.

POINT V

DOE DID NOT CHARGE AIDING AND ABETTING AND IT WAS ERROR TO GROUND LIABILITY ON THAT

DOE charged that Respondent directly violated Rule 2010 and MSRB G-17:

> 47. By his conduct in engaging in the Wells Fargo R66 SCD Trades and the Citibank FN6 SCD Trades and by submitting, or causing to be submitted, order tickets to JPT that failed to reflect Mantei's directions to SP, identify those transactions as cross-trades, or provide the information required by JPT's procedures for cross-trades, Mantei circumvented JPT's supervisory procedures and contravened JPT's prohibition against prearranged trading.
>
> 48. As a result of the foregoing conduct, Mantei violated FINRA Rule 2010.

(R. 14) Similarly, with respect to the Fresno Bond, the Complaint charged that by his actions, Respondent "circumvented JPT's supervisory procedures and contravened JPT's prohibition against prearranged trading" and as a result, "willfully violated MSRB Rule G-17." (R. 15) The Complaint did not charge Respondent with aiding and abetting Palermo, Raymundo, or anyone else in a violation of JPT rules, FINRA Rule 2010 or MSRB G-17.

Instead, the Decision rests entirely on its finding that Respondent "**directed"** prearranged trading to circumvent his firm's cross trade procedures. (R. 4362 (emphasis added); R. 4372, 4374, 4375, 4377, 4380, 4382, 4385) If the Decision is to be believed it means that Respondent "***directed***" ***Palermo*** who in turn was supposed to direct others (within his firm) and then other persons at other member firms to make or execute or place "prearranged trades" (a) in contravention of the prohibition of the JPT prearranged trading policy (and presumably the counterparty firms' as well) to (b) circumvent the firm's cross-trade policy. The Decision explains: "Mantei nevertheless **devised a strategy** to use prearranged trades with a broker-dealer counterparty for the purpose of concealing what was in effect a sale from one firm customer to another firm customer." (R. 4373; emphasis added) It is unclear what is meant by "a sale from one firm customer to another firm customer." However, as is demonstrated above, Respondent was **at least** two steps away from any counterparty because he did not speak to any counterparty and did not know who any of the counterparties was.

Moreover, "devising a plan" is not sufficient for principal liability. At most, this wrongdoing analysis approaches aiding and abetting the actions of a primary violator. <u>See</u> <u>SEC v. Tambone</u>, 597 F.3d 436, 438-46 (1st Cir. 2010) (executives of broker-dealer could not be held primarily liable for trading practices that contravened representations made in prospectuses that were distributed to investors, despite allegedly "enter[ing] into, approv[ing] and/or knowingly permit[ing] arrangements allowing" such practices to occur, because their alleged conduct constituted "at most, aiding and abetting"); Stoneridge Investment Partners, LLS v. Scientific-Atlanta, Inc. (In re Charter Communs., Inc.), 443 F.3d 987, 992 (8th Cir. 2006) ("[A]ny defendant . . . who does not directly engage in manipulative securities trading practices, is at most guilty of aiding and abetting.").

DOE neither charged nor proved any principal securities violation here. The Decision rests on its oft-repeated reasoning that Respondent "directed Palermo to execute [prearranged trades] with the counterparties," (R. 4374) But the proof offered at the hearing showed only that Palermo spoke to one counterparty. (CX-2, R. 3151-52; CX-11, R. 3195; CX-15, R. 3211) There was no evidence of Palermo directing or talking to other JPT traders or of any other JPT trader speaking to a counterparty, much less prearranging trades. (CX-3 through CX-25, R. 3153-47) Neither JPT, DOE, nor any securities regulator charged Palermo with any offense or violation related to the three transactions. (RX-16, R. 3493-95) Without a principal wrongful act, an aiding and abetting claim fails. ICD Cap., LLC v. CodeSmart Holdings, Inc., 842 F. App'x 705, 706 (2d Cir. 2021) (to properly plead an aiding and abetting claim there must be an underlying wrongful act); see also In re Agape Litig., 773 F. Supp. 2d 298 (E.D.N.Y. 2011); Hancock v. Homeq Servicing Corp., No. CIV.A. 05-0307PLF, 2007 WL 1238746, at *9 (D.D.C. Apr. 27, 2007) ("Like civil conspiracy, aiding and abetting requires an underlying tortious act."), aff'd, 526 F.3d 785 (D.C. Cir. 2008).

Respondent may not be punished for aiding and abetting violations when DOE did not charge him for those violations. Dep't of Enforcement v. Zenke, No. 2006004377701, 2009 FINRA Discip. LEXIS 37, at *11 (NAC Dec. 14, 2009) (dismissing Complaint, where it alleged only a violation of FINRA Rule 2010 predecessor, because "Hearing Panel improperly found [respondent] liable for misconduct that was beyond the scope of the allegations in the Complaint"); In re James J. Chica, Admin. Proc. No. 3-4368, 1974 SEC LEXIS 3640, at *23-24 (Dec. 26, 1974) (respondent was "not charged . . . with committing or aiding and abetting any offense;" SEC dismissed charges despite fact "shown to warrant sanctions had such conduct been properly alleged," because respondent not given adequate notice of charges prior to hearing); In re Frank J. Crimmins, Admin. Proc. No. 3-3261, 1973 SEC LEXIS 3508, at *3-4 (Aug. 31, 1973) (denying motion to amend to add aiding and abetting after evidentiary hearing had already been conducted).

The Decision essentially bypasses aiding and abetting with two statements, both illogical and conclusory. First, the Decision repeats: "Mantei is **directly** liable for engaging in unethical and dishonest conduct for directing the J.P. Turner bond desk to use prearranged trades to circumvent J.P. Turner's cross trade policy." (R. 4383; emphasis added) The Decision does not explain why the liability is direct, nor does it address Respondent's authority on this point. Further, as noted above, Respondent **did not direct** the JPT bond desk; he spoke to one trader, Palermo, who did not execute the nine relevant trades. Second, the Decision states, in wholly circular logic: "Mantei was given the opportunity to defend against the specific charges against him because the Hearing Panel found him liable for the charges brought against him in the Complaint." (R. 4383) Again, this says nothing about aiding and abetting – which is the absolute most DOE established, but did not charge, in this case.

POINT VI

IT WAS ERROR TO PRECLUDE RESPONDENT'S EXPERT FROM TESTIFYING ABOUT PREARRANGED TRADING

The NAC denied Respondent's Motion to Introduce Additional Evidence (R. 4039-59) to remedy the Hearing Officer's error in excluding **all** of Respondent's expert's testimony and report on prearranged trading (R. 4313-14), despite the fact that it was material to the issue and despite the fact that the Hearing Panel allowed DOE's fact witness, CCO Woll – who did not draft the policy (R. 1056)– to testify expansively on that topic as if he were an expert. This ruling should be reversed because it unfairly and prejudicially deprived Respondent of the right to offer expert testimony on a crucial part of the case.

As is set forth in his Declaration submitted with Respondent's Motion (R. 4039-59), Respondent's expert, James Reilly, would have testified that based on his years of experience in compliance and training, "there was no prohibited prearranged trading in this case because, in short, there was no intent to manipulate the market and no harm to the market or any investor." (R. 4051, 4052) Further, after listening to the taped calls in the case, Reilly concluded that Respondent "as a retail financial advisor not executing or negotiating either side of a trade, could not be adjudged to have executed a pre-arranged trade." (R. 4059)

This testimony was important because the Complaint failed to acknowledge the opaque and illiquid market for the products at issue and DOE thus expressed shock at the lively conversations Palermo had with his counterparties. Reilly testified that SCDs are traded in "over-the-counter negotiated markets that are illiquid," (R. 2921) he was precluded from further describing the operation of price discovery.

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The NAC erred by affirming the Hearing Panel's exclusion of Respondent's expert testimony concerning prearranged trading (R.4384, R. 4039-59, R. 4313-14), even though the Hearing Panel allowed DOE to introduce extrinsic evidence of the "meaning" of the Prearranged Trading Policy. (R. 2375-78) Woll did not draft the Prearranged Trading Policy. (R. 2701) The Decision finds that testimony from Mantei's expert – but not Woll – would "encompass the ultimate legal conclusion, which is the province of the Hearing Panel." (R.4384) Allowing DOE's fact witness to opine on the meaning of the Prearranged Trading Policy contrary to its plain language, but not allowing Respondent to offer his own expert on the point is unfair and error.

James Reilly would have testified that "there was no prohibited prearranged trading in this case because, in short, there was no intent to manipulate the market and no harm to the market or any investor." (R. 4051-52) Further, Reilly's report concluded that Respondent "as a retail financial advisor not executing or negotiating either side of a trade, could not be adjudged to have executed a pre-arranged trade" (R. 4059) and his testimony would have explained why.

POINT VII

THE DECISION SHOULD BE VACATED BECAUSE THE FINRA FORUM IS UNCONSTITUTIONAL

The FINRA proceeding below was unconstitutional because the FINRA hearing officers acted with executive authority without being properly appointed officers of the executive branch and Respondent was repeatedly deprived of due process rights. An instructive case is Alpine Securities Corp. v. FINRA, 2023 WL 4703307 (D.C. Cir. July 5, 2023). In that case the D.C. Circuit enjoined FINRA from expelling Alpine, a registered securities broker, pending resolution of Alpine's argument that the FINRA officers were not properly appointed officers. The D.C. Circuit found that Alpine was likely to prevail on the merits of its argument. In so doing, the

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D.C. Circuit relied on the Supreme Court precedent of Lucia v. SEC, 138 S. Ct. 2044 (2018). In Lucia, the Supreme Court held that SEC ALJs are officers of the United States, subject to the Appointments Clause of the Constitution. In Alpine, the D.C. Circuit concluded that FINRA hearing officers are "near carbon copies" of SEC ALJs and therefore also likely subject to the Appointments Clause. The D.C. Circuit concluded that this "may be a constitutional problem." 2023 WL 4703307, at *2, 4. See also SEC v. Cochran, No. 21-1239 (S. Ct. Apr. 14, 2023).

POINT VIII

IT WAS AN ABUSE OF DISCRECTION FOR THE NAC TO INCREASE THE SANCTIONS AND TO RUN THE SUSPENSIONS CONSECUTIVELY

It was an abuse of discretion for the NAC to increase the suspension sanction on Respondent from 30 days to two consecutive three-month suspensions by concluding that Rule 2010 and MSRB G-17 "involve different rules and raise separate" regulatory concerns. (R. 4388) The NAC fails to specify what those regulatory concerns are or how the sanctions are remedial and not punitive.[10] In substance, those rules are quite similar.

As grounds for making the suspensions consecutive rather than concurrent, the Decision essentially holds that Respondent's insistence on defending himself can serve as three aggravating factors. First, the Decision cites "Mantei's refusal to acknowledge his wrongdoing and efforts to shift blame." (R. 4385) Second, the Decision refers to Respondent's "lack of remorse," and finds that Respondent's "continued denial that his conduct was wrongful demonstrates either a misunderstanding or a lack of recognition of his duties as a professional and

[10] The D.C. Circuit has stated that the Commission may affirm FINRA sanctions only if they are "remedial" and not "punitive." In re Saad., Sec. Exch. Act Release No. 86751, 2019 SEC LEXIS 2216, *3 (Aug. 23, 2019)(citing Siegel v S.E.C., 592 F.3d 147, 158 (D.C. Cir. 2010)).

of his regulatory obligations." (R. 4387) Third, the Decision points to Respondent's defense that he never received guidance from JPT compliance or managers on the policies at issue, calling it "blame-shifting" and stating that it "find[s] it aggravating that Mantei continues to try to shift the blame for his own misconduct to others." (R. 4387) The Decision cites to no testimony and nothing in the record justifying such finding. Neither Respondent nor his attorneys tried to shift blame and Respondent pointed the finger at no person. Rather, Respondent and his attorneys, on his behalf, argued that it was improper to use interpretations of JPT policies rather than the plain language of the rules themselves (R. 2700-01), and that these "interpretations" had never been communicated to Respondent or anyone else prior to the hearing. Woll conceded the accuracy of Respondent's position when questioned (R. 2702, R. 3965, 2406, 2437, 2443).[11]

Even if the liability holdings are upheld, the sanctions are far too harsh. This is particularly true for the violations affirmed by the NAC – violations of the catchall FINRA Rule 2010 and MSRB Rule G-17 **without a charge or violation of any substantive securities law, rule or regulation**.[12] Critically, DOE did not charge or prove **any** harm to a customer or the market. (R. 2021-22, 3983, 4383)[13] It is appropriate to consider the "degree of harm to investors

[11] The Decision thus violates the basic doctrine that everyone has a fundamental right to be given notice of the rules they will be held to and disciplined for violating. Bazzi v. Gacki, 468 F. Supp. 3d 70, 81 (D.D.C. 2020)("the requirement that agencies give 'fair notice' of its rules before imposing criminal or civil punishment is thoroughly incorporated into administrative law.") (internal quotation omitted).

[12] The Decision acknowledges that the FINRA Sanction Guidelines ("Guidelines") do not "address Mantei's conduct at issue – i.e., directing prearranged trades with counterparties in contravention of the firm's prearranged trading prohibition to circumvent his firm's cross trade procedures." (R. 4385).

[13] The Decision mentions the absence of many aggravating factors including (1) "a long and successful record in the industry," (2) the fact that Respondent did not receive any guidance on cross-trade policy (3) Respondent's cooperation in the FINRA investigation, (4) the lack of

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and the marketplace resulting from the violation." See In re Rosedale Asset Mgmt., LLC, Sec. Exch. Act Release No. 1410, 2021 SEC LEXIS 2283, at *6 (Aug. 12, 2021) ("in determining sanctions…the Commission also considers…the degree of harm to investors and the marketplace resulting from the violation.”).

Punishing Respondent with increased sanctions for defending himself against DOE’s charges is fundamentally unjust and violates Respondent’s due process rights. Sanctions cannot be supported by blaming Respondent for defending himself. SEC v. First City Financial Corp., 890 F.2d 1215, 1229 (D.C. Cir. 1989) (defendants “are not to be punished because they vigorously contest the government’s accusations. We think ‘lack of remorse’ is relevant only where defendants have previously violated court orders, or otherwise indicate that they did not feel bound by the law”); SEC v. Gunn, No. 3:08-CV-1013-G, 2010 WL 3359465, at *5 (N.D. Tex. Aug. 25, 2010) (“the mere fact that a defendant… does not admit fault after losing at trial does not, standing alone, suggest that the defendant is likely to commit another violation of the securities laws.”).

The NAC finds it aggravating that Respondent “concealed” the transactions at issue from JPT, but the evidence existing for this is in clear trade tickets and tapes of calls Respondent knew were being recorded and proves the opposite. The Decision rejects the obviousness defense on the grounds that it “does not negate the **inherently deceptive** nature of his conduct, which was

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evidence of actual harm to the public, and (5) the short period over which the transactions occurred. (R. 4387) Rather than finding a lack of aggravating factors, the Decision finds many of these facts irrelevant in determining the sanctions. For example, the Decision explicitly disregards the small number of transactions and the short period over which they occurred and puts undue weight on to the purported significance of the transactions. (R. 4386) The Decision cites factor 17 of the Guidelines (“the number, size and character of the transactions at issue”) but rather than using the factor to mitigate the sentence, uses it as support for its decision to enhance it. (Id.)

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designed to mislead J.P. Turner and evade the firm's cross trade procedures." (R. 4385; emphasis added). Asserting that fully disclosed conduct requiring mandatory supervision is "inherently deceptive"—whatever that may mean—does nothing to prove that Respondent concealed such conduct. Furthermore, the absence of evidence establishing deceit should not count against Respondent.

The Decision finds a "pattern of wrongdoing" while stating that "Mantei's conduct involved only a small number of transactions, the transactions themselves were not insignificant." (R. 4386). But relative to the totality of Respondent's transactions—notionally hundreds of millions of dollars annually—the transactions at issue are dwarfed and cannot possibly be considered significant. Thus, there is no empirical evidence to conclude that the transactions themselves were "significant" and, in fact, they were just the opposite, so much so that DOE never addressed the sales credits generated by the trades. It cannot fairly be said that there was a "pattern" of wrongdoing here. <u>Dep't of Enforcement v. Iiada</u>, No. 2012033351801, 2016 FINRA Discip. LEXIS 32, at *17-18 (NAC May 18, 2016) respondent "did not engage in a pattern of misconduct over an extended period of time, nor did he engage in numerous violations").

The Decision finds another aggravating factor illogically, in that: "Mantei's conduct . . . put the buying and selling customers at risk." (R. 4386) This is despite the fact that DOE did not allege or prove **any** harm to a customer or the market. (R. 4383; RX-40, R. 3497, 3501). Without explication, the Decision conclusorily states: "The fact that the evidence does not establish **actual harm** suffered by clients is **not dispositive**." (R. 4386; emphasis added). Such a statement contradicts the fundamental purpose of securities laws, rules, regulations, and particularly disciplinary rules, which is to protect the investing public. See FINRA Guidelines

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statement of purpose: "'sanctions should be designed to **protect the investing public** by deterring misconduct and upholding high standards of business conduct.'" (R. 3981; emphasis added); McCarthy v. SEC, 406 F.3d 179, 188 (2d Cir. 2005) ("[T]he purpose of expulsion or suspension from trading is to protect investors, not to penalize brokers."); In re Howard F. Rubin, Sec. Exch. Rel. No. 35179, A.P. File No. 3-8293 at *2 (Dec. 30, 1994) (recognizing that "[w]hen we suspend or bar a person, it is to protect the public from future harm at his or her hands."). But here, the Decision affirms and increases the penalty for actions which undisputedly did not harm JPT, any customer, or the markets generally. (R. 3983, 4383) Although the absence of actual harm may not always be a mitigating factor, it should not be entirely disregarded.

But as to a principal reason that the Hearing Panel stated for imposing discipline, that "Mantei created the potential for monetary gain and increasing his payout by circumventing J.P. Turner's cross trade policy and its markup/markdown limitations," the Decision states "[w]e disagree." (R. 4386) The NAC properly finds that there was nothing in the record regarding payouts or compensation regarding the trades and nevertheless deems "the potential for monetary gain" an aggravating factor. (Id.) Given the NAC's one concession to the facts established at the hearing—that Respondent **did not** benefit financially from the markup or markdown related to any of the transactions (R. 4386)—thereby eliminating one of DOE's proposed aggravating factors, the NAC's Decision **increasing** the penalty six-fold is unsupportable.

It Was Error to Run the Suspensions Consecutively

The NAC's decision to dramatically increase the suspensions and then make the suspensions run consecutively, rather than continuing to allow them to run concurrently, was an abuse of discretion. Both suspensions stem from the same conduct and were issued pursuant to essentially the same two catch-all rules. Fundamentally, cumulative "sentencing" under two statutes is permitted only if legislative intent is clear. This is true even if such statutes proscribe the same conduct. Missouri v. Hunter, 459 U.S. 359, 368, 362 (1983) (multiple convictions based on the same conduct were only permitted because there was clear legislative intent to subject a defendant to cumulative punishment. The relevant statute stated that the "punishment imposed…shall be in addition to any punishment provided by law for the crime committed…")

Consecutive suspensions are permissible where the underlying conduct involves rule violations of fundamentally distinct harms. In Siegel v SEC, 592 F.3d 147, 158 (D.C. Cir. 2010), the court upheld the SEC's decision to allow consecutive suspensions "to protect the public from two fundamentally different types of harms." In Siegel, 592 F.3d at 158, the court differentiated the two consecutive suspensions at issue by finding that the underlying rules that were the basis of the suspensions had different purposes. The SEC has used the "fundamentally different" framework to determine whether suspensions should run concurrently or consecutively. See In re Mullins, Sec. Exch. Act Release No. 66373, 2012 WL 423413, at *56 (Feb. 10, 2012) ("we concur with [NAC's] determination that [respondent's] failure to disclose information on compliance forms is fundamentally different from her failure to obtain the appropriate approval from her Firm before accepting a loan from a client, and that consecutive suspensions appropriately remedy the two types of violation.") (internal citation omitted).

The rules that the Decision bases its consecutive suspensions on are not fundamentally different and do not demonstrate legislative intent supporting multiple punishments for the same conduct.

The NAC's rulings as to sanctions should be reversed.

CONCLUSION

For the reasons set forth above, Decision should be reversed in all respects, the sanctions vacated, and the Complaint dismissed. Respondent respectfully requests oral argument of this appeal.

Dated: New York, New York
October 27, 2023

Respectfully submitted,

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CERTIFICATION OF COMPLIANCE WITH WORD LIMIT

I hereby certify that the word count of this Appeal Brief complies with the word limits of Rule 17 C.F.R. § 201.450(c) for opening briefs of 14,000 words exclusive of pages containing the table of contents, table of authorities, and any addendum that consists solely of copies of applicable cases, pertinent legislative provisions or rules, and exhibits. According to the word-processing system (Microsoft Word) used to prepare this Appeal Brief, the total word count for all printed text exclusive of the material omitted under 17 C.F.R. § 201.450(c) is 13,358 words.

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CERTIFICATE OF SERVICE

I certify that on October 27, 2023, I served a copy of the foregoing via email on:

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