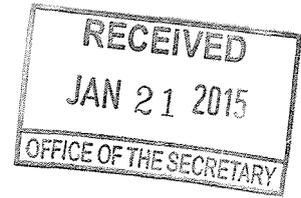


UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION



ADMINISTRATIVE PROCEEDING
File No. 3-15873

In the Matter of

THOMAS R. DELANEY II and
CHARLES W. YANCEY

Respondents.

RESPONDENT THOMAS R. DELANEY II'S RESPONSIVE POST-HEARING BRIEF

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INTRODUCTION

The Division of Enforcement's (the "Division") case against Respondent Thomas R. Delaney ("Delaney") grows ever more muddled. The Division pled this case, and received approval from the Commission to proceed, on a theory that Delaney was an active, knowing and willful participant in a scheme to violate Rule 204T/204 for profit. The evidence to support this case simply does not exist, however. There is no credible evidence of motive to Delaney or that Delaney knew about Stock Loan's alleged intentional and systematic policy or practice to violate Rule 204T/204 before approximately March of 2011. And, where Delaney did not know of the violations, there is no support for a finding that Delaney substantially assisted the violations.

The Division has therefore attempted to shift focus to a new theory—that Delaney aided and abetted the Rule 204 violations through recklessness, including by failing to provide sufficient guidance to Stock Loan to comply with the Rule. The Division also belatedly attempts to dust-off its causing claim. The Division's efforts to shift theories this late in the game cannot be countenanced. The Division's effort to transform alleged intentional misconduct into reckless disregard is, in fact, a telling admission that it did not prove the case it pled.

There is also no evidence establishing that Delaney acted either recklessly or negligently. The purported "red flags" do not show that Delaney consciously disregarded known risks. For example, a purported lack of guidance to Stock Loan about how to comply with Rule 204T/204 is legally immaterial where the Division has stipulated that Stock Loan knew Rule 204T/204 "required them to close out all long sale transactions by market open at or before market open on T+6."¹ In addition, the Division ignores significant evidence indicating that Rule 204 issues were tested and, those that were known to Compliance, were being diligently remediated. The claims against Delaney must be dismissed and the remedies sought denied.

¹ See Stipulated Finding of Fact 70.

ARGUMENT

I. THE DIVISION CANNOT CHANGE ITS CASE IN POST-HEARING BRIEFING IN RESPONSE TO A FAILURE TO PROVE THE CASE IT PLED.

In the Order Instituting Administrative Cease and Desist Proceedings (“OIP”), the Division alleges only intentional misconduct by Delaney—that Delaney was an active, knowing and willful participant in a scheme to violate Rule 204T/204 for profit. For example:

- “Delaney consciously chose profits over compliance.” (OIP, ¶39.)
- “Motivated by financial considerations, Delaney affirmatively assisted the violations resulted from the Stock Loan procedures.” (OIP, ¶7.)
- “Delaney agreed with Stock Loan officers that Stock Loan would continue implementing the non-compliant procedures and he agreed to reject certain procedures that would have brought Pension into Rule 204T/204 compliance because he did not want Pension to incur the associated costs.” (OIP, ¶7, *see also* ¶38 (same).)
- “Delaney further aided and abetted and caused Pension’s violations by intentionally concealing the violations from regulators.” (OIP, ¶8, *see also* ¶39)
- Delaney, intentionally, and repeatedly, concealed both the Buy Ins Rule 204(a) deficiencies and intentional Stock Loan Rule 204(a) violations from regulators.” (OIP, ¶42.)
- Delaney “authoriz[ed] WSPs he knew concealed the actual, non-compliant procedures.” (OIP, ¶8.) The “WSPs were intentionally designed to conceal the relevant procedures”; “the WSPs for Stock Loan’s compliance with Rule 204 relating to long sales of loaned securities went beyond silence about the actual practices and procedures in an affirmative effort to mislead . . .” (OIP, ¶41.)

There is no reading of the OIP or the Division’s pre-hearing motions or Brief that would even suggest the Division was asserting that Delaney acted recklessly or negligently. Telling, the OIP does not reference negligence or red flags with regard to Delaney. However, in its Post-Hearing Brief, the Division attempts to change to a new theory, using a disproportionate amount of space (15 of its 20 page argument against Delaney) to championing an unpled recklessness theory. Acts once alleged to be evidence of “intentional” misconduct in the OIP and before the

hearing have been now been repurposed as “red flags.”² The Division does not mention the purported financial motivation at all. In trying to change its case during post-hearing briefing, the Division admits there is no evidence to support the pleaded allegations against Delaney.

A failure of proof does not allow the Division to expand its case to pursue a new theory during post-hearing briefing to try to salvage a win.³ Rather, it is well-established that Delaney is entitled to notice of the theory upon which he is being charged before the final hearing. This right is guaranteed by the Administrative Procedures Act, which specifically requires the Division to provide timely notice of the matters of fact and law asserted.⁴ Under the APA, “it is well settled that an agency may not change theories in midstream without giving respondents reasonable notice of the change.”⁵ Furthermore, the constitutional right to due process requires “a fair trial in a fair tribunal,” in both courts and administrative agencies.⁶ This includes “giving the parties sufficient notice to enable them to identify the issues on which a decision may turn.”⁷

Several administrative decisions have also rebuffed efforts by the Division to expand its case beyond the four-corners of the OIP both prior to and after the hearing.⁸ In *Lohmann*, for

² For example, whereas the OIP alleged that Delaney had an “agreement” with Stock Loan to violate Rule 204T/204, the Division now asserts that Delaney recklessly or negligently failed to see “red flags that PFSI’s Stock Loan Department was having significant, ongoing problems with Rule 204 compliance,” (Division’s Post-Hearing Brief, p. 17), and did not provide Stock Loan with “guidance” on how to comply with the Rule. (*Id.*, p. 12.)

³ To the contrary, in such circumstances, the Division is obligated to dismiss. See *Freeport-McMoRan Oil & Gas Co. v. F.E.R.C.*, 962 F.2d 45, 47 (D.C. Cir. 1992) (observing, the Division “‘is the representative not of any ordinary party to a controversy . . . but of a sovereignty whose obligation . . . is not that it shall win a case, but that justice shall be done,’” and thus “should refrain from instituting or continuing litigation that is obviously unfair.” (emphasis added) (second ellipses in original) (quoting *Berger v. United States*, 295 U.S. 78, 88 (1935)).

⁴ See 5 U.S.C.A. § 554(b)(3).

⁵ *Rodale Press, Inc. v. F.T.C.*, 407 F.2d 1252, 1256 (D.C. Cir. 1968).

⁶ *Withrow v. Larkin*, 421 U.S. 35, 46 (1975) (quoting *In re Murchison*, 349 U.S. 133, 136, (1955)).

⁷ *Lankford v. Idaho*, 500 U.S. 110, 126 n. 22 (1991); accord *In re Oliver*, 333 U.S. 257, 273 (1948) (due process requires a person be given “reasonable notice of a charge against him, and an opportunity to be heard in his defense . . . to examine the witnesses against him, to offer testimony, and to be represented by counsel”); *Cleveland Bd. of Ed. v. Loudermill*, 470 U.S. 532, 546, (1985) (“The tenured public employee is entitled to oral or written notice of the charges against him, an explanation of the employer’s evidence, and an opportunity to present his side of the story”).

⁸ See, e.g., *In the Matter of Gregory M. Dearlove, CPA*, Init. Dec. Rel. No. 315 at 4546 n. 40, 4951, 2006 SEC LEXIS 1684 (July 27, 2006); *In the Matter of Robert Bruce Lohmann*, Init. Dec. Rel. No. 214 at 13, 17 n.5, 2002

example, the court declined to consider an argument that the respondent lacked candor in determining scienter and an appropriate sanction, where the Division did not include a lack-of-candor allegation in the OIP.⁹ As the court observed, “it would have been a very simple matter” to include such an allegation in the OIP.¹⁰ Notably, the OIP must also be approved by the Commission before it is filed.¹¹ Of course, the Commission cannot approve an unpled theory.

Here, similar to *Lohmann*, if the Division wanted to proceed on a recklessness theory, it would have been a very simple matter for the Division to include that theory in its OIP and identify purported red flags that Delaney ignored. This omission is all the more glaring when the allegations against Delaney are compared to the allegations against Yancey, where the Division specifically identified several items as “red flags” that Yancey purportedly ignored.¹² Allowing the Division to proceed on an unpled theory at this late juncture would substantially prejudice Delaney, who focused his efforts at the hearing on defeating the Division’s allegations that he was a willful and knowing participant in a scheme, for profit, to violate Rule 204T/204.

II. THE DIVISION’S AIDING AND ABETTING CLAIM FAILS.

A. The Division’s Post-Hearing Brief Confirms There is No Evidence of a Motive to Delaney to Meet the Scienter Element of Aiding and Abetting.

“To establish that one Respondent willfully aided and abetted the violation of another, the Division must show that the aider and abettor acted with scienter.”¹³ As detailed in Delaney’s

SEC LEXIS 2380 at *33, 46 n.5 (Sept. 19, 2002), *aff’d*, Exchange Act Rel. No. 48092, 2003 SEC LEXIS 1521 (June 26, 2003); *In the Matter of Richmark Capital Corp.*, Init. Dec. Rel. No. 201 at 25, 2002 SEC LEXIS 601 at *6769 (March 18, 2002), *aff’d*, Exchange Act Rel. No. 48758, 2003 SEC LEXIS 2680 (Nov. 7, 2003).

⁹ See *In the Matter of Robert Bruce Lohmann*, Init. Dec. Rel. No. 214 at 13, 17 n.5.

¹⁰ *Id.*

¹¹ See SEC, Division of Enforcement, *Enforcement Manual*, p. 25 (stating, “[t]he filing or institution of any enforcement action must be authorized by the Commission,” and “Commission authorization is sought by submitting an action memorandum that sets forth a Division recommendation and provides a comprehensive explanation of the recommendation’s factual and legal foundation.” (emphasis added)).

¹² See generally OIP, ¶¶74, 75, 81, 82 and 83.

¹³ See Stipulated Conclusion of Law 5.

opening Brief, to meet the scienter element, the Division must put forth “some reason to conclude that the defendant has thrown in his lot with the primary violators.”¹⁴ The question is: Was it “in the interest of the defendants”—“did they gain”?”¹⁵ Numerous courts have similarly refused to find scienter in the absence of motive.¹⁶ The need for the Division to provide a “reason” or motive is further inherent in the substantial assistance standard it stipulated to:

To satisfy the substantial assistance element of aiding and abetting, the SEC must show that the defendant “in some sort associated himself with the venture, that he participated in it as something that he wished to bring about, and that he sought by his action to make it succeed.”¹⁷

Notwithstanding these requirements, and despite its allegations in the OIP that Delaney was “motivated by financial considerations,” the Division made no effort in its Post-Hearing Brief to identify any incentive to Delaney to aid and abet Penson’s violations of Rule 204T/204. Why, for example, would Delaney—a CCO with a spotless record—help Stock Loan violate Rule 204T/204 by deliberately deceiving regulators? The Division does not even suggest a *theory*. This is not surprising because there is no *evidence* that Delaney had anything to gain, financial or otherwise, from such conduct. Conversely, the Division has amply shown that Delaney had “everything to lose” by participating in such conduct, just through the sanctions it seeks against him in this case.¹⁸ As observed by the D.C. Circuit in refusing to find scienter in a similar absence of any motive to the defendants, “[i]f we were to conclude that the [defendants]

¹⁴ *Barker v. Henderson, Franklin Starnes and Holt*, 797 F.2d 490, 492 (7th Cir. 1986).

¹⁵ *Id.*

¹⁶ *See, e.g., S.E.C. v. Steadman*, 967 F.2d 636, 642 (D.C. Cir. 1992) (reversing the finding of scienter based on recklessness where there was no evidence of “any motive” for the defendants to not register their shares under state Blue Sky laws and observing that “[a]ny accusation of bad faith would seem unfounded, because [defendants] had little, if anything to gain from discontinuing Blue Sky registration.”); *Warren v. Reserve Fund, Inc.*, 728 F.2d 741, 746 (5th Cir. 1984) (declining to find scienter, in part, because there was no evidence of “any motive which would lead the [defendant] Fund to misrepresent the earnings,” where “[t]he Fund neither retained nor gained any benefit at the expense of its shareholders.”).

¹⁷ *See* Stipulated Conclusion of Law 7 (emphasis added).

¹⁸ *See Barker*, 797 F.2d at 497 (determining there was “no sound basis,” as a matter of law, to conclude that the defendant aided and abetted a primary violation where the defendants “had nothing to gain and everything to lose”).

meant to defraud investors, we would have to believe that they did so for the sheer joy of it rather than for profit.”¹⁹ It was not tenable to that Court, and it should not be permitted by this Court.

Moreover, the Division also does not reference the purported “gain” to Penson of \$59,000 in its Post-Hearing Brief, even though this was the only “specifically quantified benefit” to Penson “from not timely closing out at market open on T+6.”²⁰ This omission is ultimately unsurprising for at least two reasons. First, as set forth in Delaney’s opening Brief, an incentive to Penson is not sufficient. The Division must show the existence of a motive personal to Delaney.²¹ Second, this \$59,000 “quantified benefit” is not a viable motive even to Penson, as it represents only 0.08% of Stock Loan’s total revenue of \$77 million during the relevant period.²²

Although the Division includes a couple of proposed findings of fact arguing there would have been “substantial costs to PFSI if it had bought shares at market-open T+6,” and that such purchases “could expose the firm to significant losses,” the Division produced no evidence to quantify or otherwise establish that such “costs” or “losses” actually existed.²³ The insinuation that Penson also benefitted through the avoidance of other costs or losses is based on pure speculation. Any shares purchased by Penson could have gone up in value and sold at a profit, as acknowledged by Lindsey Wetzig on cross-examination.²⁴ Rule 204T/204 also allowed Penson to borrow shares to close-out positions, avoiding any purchasing risks altogether.²⁵ The simple fact is that because the Division did not provide any evidence quantifying the purported

¹⁹ See *Steadman*, 967 F.2d at 642.

²⁰ See Stipulated Finding of Fact 53; see also Ex. 239 (Professor Harris’ Expert Report), ¶¶25 (indicating that Professor Harris calculated “the benefit that Penson obtained by failing to meet the Long Sale Close-Out Requirements when it had lent out the securities.”)

²¹ See Delaney’s Post-Hearing Brief, p. 10 and n. 41 (citing cases).

²² See Stipulated Finding of Fact 79-80.

²³ See Division’s Proposed Finding of Fact 43, 45.

²⁴ See Tr. 427:25-428:7.

²⁵ See Rule 204(a)(1); see also Tr. 426:22-427:3 (testimony by Wetzig confirming that Stock Loan “could have borrowed” to close out a position.)

costs or losses, it cannot be determined with any degree of reliability whether there were any. Indeed, if the publicly available trade data supported the existence of any such additional benefits to Penson, surely the Division would have had its expert witness calculate these benefits.

B. The Division Failed to Prove Delaney’s Knowledge of the Rule 204T/204 Violations at Issue during the Relevant Period.

1. The Division’s “Should Have Known” Theory Should be Rejected.

The Division agrees that one of the most important issues in this case is when Delaney learned of Stock Loan’s violations of Rule 204T/204 with respect to long sales of loaned securities.²⁶ This is a necessary concession because the Division alleged that Delaney had actual knowledge and it is well-established that a claim for aiding and abetting requires the Division to prove “awareness or knowledge by the aider and abettor that his or her role was part of an overall activity that was improper.”²⁷ Notably, under this standard, the Division must prove not just knowledge of the violative practice itself, but that Delaney was aware he was playing a role in it.

However, instead of focusing on its obligation to prove that Delaney knew Stock Loan was systematically violating Rule 204T/204 with respect to long sales of loaned securities before March of 2011 and his part in it, the Division now primarily focuses on trying to establish that Delaney *should have known* of the violations. For example, the Division argues at length that Delaney received “guidance” in the form of email newsletters indicating that Rule 204T/204 could create tension with the securities lending industry and thus he should have been aware that *Penson’s* Stock Loan department was having compliance issues with Rule 204T/204 with respect to long sales of loaned securities. All of the Division’s arguments that Delaney should have known he was assisting the violations suffer from two fundamental flaws, as well as more individualized failings (discussed below), that defeat the Division’s aiding and abetting claim.

²⁶ See Division’s Post-Hearing Brief, p. 7.

²⁷ *Howard v. SEC*, 376 F.3d 1136, 1142 (D.C. Cir. 2004).

First, as indicated in Section I, the Division’s assertions that Delaney should have known” or was “reckless in not knowing” he was assisting violations of Rule 204T/204 is not the case the Division pled, and the Division cannot now alter its theory. The Division’s OIP unequivocally alleges Delaney “knew at all relevant times that Stock Loan was not complying with the T+6 market open close-out requirement” for long sales of loaned securities.²⁸ In addition, all of the alleged acts of substantial assistance are premised upon a finding that Delaney knew of the purported practice—i.e., that he “agreed” with Stock Loan to implement non-compliant procedures; that he “intentionally conceal[ed]” violations from regulators and Yancey; and that he “intentionally designed” WSPs to “conceal” non-compliant procedures in an “affirmative effort to mislead.” None of these are possible without actual knowledge.

Second, the Division cannot rely on an argument that Delaney “should have known” he was assisting violations of Rule 204T/204 to satisfy the knowledge element. As stated by the D.C. Circuit, “aiding and abetting liability cannot rest on the proposition that the person ‘should have known’ he was assisting violations of the securities laws.”²⁹ “Awareness of wrongdoing means knowledge of wrongdoing.”³⁰ Extreme recklessness comes into play in the assistance element—whether Delaney assisted the violative practice through extreme recklessness.³¹

Here, this distinction is important because there is no evidence that Delaney had any actual role in the primary violation at issue; he was not involved in settling trades or closing-out failure-to-deliver positions on any transactions, including long sales of loaned securities. Delaney’s alleged assistance is limited to purportedly intentional acts of a different sort, i.e.,

²⁸ See OIP, ¶28; see also *id.*, ¶34, ¶35, ¶55.

²⁹ See *Howard*, 376 F.3d at 1143 (citations omitted) (observing that “the evidence showed that [defendant] was not aware, generally or otherwise, of any wrongdoing, and chastising the SEC for trying to meet this element by arguing the defendant’s “fault was in *not* being aware.” (emphasis in original)).

³⁰ *Id.* at 1142.

³¹ See *id.* at 1143.

deliberately concealing the alleged systematic practice and policy to violate Rule 204T/204 from Yancey and regulators in order to further the purported scheme. In order to substantially assist the violations by deliberately concealing them from regulators, as alleged by the Division, Delaney would have to know about it.³²

2. The Division Failed to Prove that Delaney Knew of the “Systematic” Practice or Policy to Violate Rule 204.

The Division’s argument that Delaney actually knew of the primary violation is based on the following four sources: (1) Delaney’s purported admission that he knew of the primary violations, based on the Wells Submission (Ex. 157); (2) the testimony of Michael Johnson; (3) the testimony of Rudy DeLaSierra; and (4) and the testimony of Brian Gover.

a. *The overwhelming majority of evidence, and the only credible evidence, establishes that Delaney did not know of the primary violation at issue prior to March of 2011.*

In his opening Post-Hearing Brief (p. 15-27, 33), and proposed Findings of Fact, Delaney comprehensively addressed each of the four pieces of evidence the Division relies upon and demonstrated that they are not credible evidence that Delaney had any knowledge of the primary violation at issue before March of 2011. In the interest of efficiency, Delaney will not repeat this exercise here, but rather incorporates it by reference and offers the following summary:

- Johnson did not testify that Delaney knew of the violations. When the Division asked Johnson, “[w]as Delaney aware that those practices we just saw in Exhibit 89 were how Stock Loan was operated?” Johnson answered: “I don’t know.” Johnson further indicated that, at most, he “communicated” to Delaney that there was a conflict between “the rule and the *industry* practice,” not the practice at Penson. Finally, Johnson testified that in response to this communication, “I believe [Delaney] arranged a meeting with Rudy De La Sierra’s staff and Morgan Lewis.”³³ The Division responds to this testimony, primarily, by ignoring it.

³² See Stipulated Conclusion of Law 7. This is further inherent in, and required by, the substantial assistance standard stipulated to by the Division at the hearing, which requires that Delaney “participated in [the venture] as something he wished to bring about, and that he sought by his action to make it succeed.” Unintentional, and even reckless conduct, does not meet this standard.

³³ See Delaney’s Post-Hearing Brief, pp.16-19.

- DeLaSierra's testimony that Delaney knew is not credible: DeLaSierra's testimony has changed dramatically over time to become more favorable to the Division, in line with his receipt of a cooperation agreement and a promise of leniency. When DeLaSierra first provided investigative testimony in 2012, he said Compliance was not aware of the violative practice regarding Rule 204 until the beginning of 2011. DeLaSierra subsequently testified that Delaney knew of the practice in 2008. However, DeLaSierra's reasoning for why he believes Delaney knew of the practice in 2008 is dubious. He claimed that the fact that "we still ha[d] counterparties" should have alerted Delaney that Stock Loan was violating the law, even though DeLaSierra confirmed that the counterparties "don't stop [Stock Loan] from buying in at the open." DeLaSierra is also contradicted by numerous other witnesses.³⁴
- Gover's testimony is not reliable. Gover testified that he recalled a meeting with himself, Delaney, Holly Hasty, Johnson and potentially DeLaSierra and Brian Hall, to discuss a Rule 204 issue arising from Stock Loan's position that they "don't get bought in," and the need for Stock Loan to recall earlier. The Division claims this meeting happened between March and June of 2010. However, Gover's testimony of the timing and content of the meeting is contradicted by every other alleged participant of the purported meeting, and other events. Indeed, Gover himself testified that "he could not reliably say" when this purported meeting occurred.³⁵
- The Wells Submission: The Division's reliance on Delaney's Wells Submission to try to establish that Delaney admitted to knowledge of the primary violation fails, as this Court has already determined in its Order entered January 15, 2015.³⁶

In addition to showing the Division's evidence was unreliable, Delaney also addressed numerous other sources in his Post-Hearing Brief (pp. 27-33) that contradicted the Division's position that Delaney knew of the violative practice before March 2011. Again, in the interest of efficiency, Delaney incorporates this discussion by reference, with the following summary:

- Delaney's testimony: Delaney has consistently denied knowledge that Stock Loan had a practice or policy of violating Rule 204T/204 before approximately March of 2011.³⁷ Although Delaney recalled some discussions with Johnson and potentially DeLaSierra around the time 204T was adopted regarding "counter-party pushback" as a result of Rule 204T, this did not alert him to non-compliance.³⁸ Delaney reasonably interpreted counterparty pushback to be an indication that Stock Loan was following

³⁴ See Delaney's Post-Hearing Brief, pp. 19-24.

³⁵ See Delaney's Post-Hearing Brief, pp. 24-27.

³⁶ See Order, January 15, 2015.

³⁷ See Delaney Finding of Fact 36.

³⁸ See Delaney Finding of Fact 26.

the Rule.³⁹ In addition, Delaney's conduct in arranging an escalation meeting for Stock Loan and outside counsel in mid-February 2011⁴⁰ is compelling evidence that no one from Stock Loan approached him for help with Rule 204 compliance earlier, and that Delaney did not deliberately or recklessly disregard violations that he knew about.

- No corroborative documents: The Division has produced no emails or other documents showing Delaney knew of the alleged violative practice. The first emails to Delaney discussing the issues here, are the February 2011 privileged emails.⁴¹
- Brian Hall: Hall told the Division that he did not ask legal or compliance for help complying with Rule 204 until "early 2011," when he met with Hasty and outside counsel" to seek guidance on Rule 204.⁴²
- Lindsey Wetzig: Wetzig testified "he did not have any discussions with Tom Delaney prior to" the February 2011 call with outside counsel.⁴³
- Eric Alaniz: Alaniz, one of the few non-interested parties, strongly suggests Delaney did not know.⁴⁴ Delaney directed Alaniz to conduct Rule 3012 testing of Penson's Rule 204 compliance, but did not tell Alaniz which departments to test or provide the methodology for the test.⁴⁵ If Delaney knew of the violations and was "in on it," as the Division alleged, giving Alaniz free reign on the 3012 testing makes no sense. In addition, that Alaniz did not discover Stock Loan's violations, despite conducting extensive 3012 testing,⁴⁶ strongly suggests that Stock Loan was concealing it from compliance, and that Delaney neither knew, nor was reckless in not knowing.

b. *The Division's attack on Delaney's credibility is unsupported and unwarranted.*

Delaney's honesty, high moral character, and competence as compliance officer, was universally attested to by every witness who was asked.⁴⁷ In the face of this uniform support, the Division attempts to attack Delaney's credibility by arguing Delaney has given multiple versions

³⁹ Tr. 1195:5-12.

⁴⁰ Tr. 1309:2-22.

⁴¹ See Delaney Post-Hearing Brief, pp. 29-30.

⁴² See Delaney Post-Hearing Brief, p. 31; see also Ex. 446, ¶3.

⁴³ See Delaney Finding of Fact 83.

⁴⁴ See Delaney Post-Hearing Brief, p. 33.

⁴⁵ See Tr. 743:17-25; 744:4-8; 864:12-865:10; 865:16-21.

⁴⁶ See Delaney Finding of Fact 39, 40.

⁴⁷ See Delaney Finding of Fact 1-4, 8.

of when he discovered the Rule 204 violations at issue and when he escalated them to Yancey.⁴⁸

Contrary to the Division's assertions, Delaney's testimony is not materially inconsistent, and any slight inconsistency can be explained by the simple passage of time.⁴⁹ Delaney has always consistently testified that he did not learn of any systematic practice or policy to violate Rule 204T/204 before approximately March of 2011.⁵⁰ Delaney has been under oath five times in this proceeding, including twice at the hearing. And yet, not only does the Division not rely on testimony actually heard by the Court, it cannot identify actual inconsistencies in his testimony.

For example, with respect to when he discovered the systematic violations, the Division claims Delaney (a) testified in his first investigative testimony that he "never" knew about Stock Loan's Rule 204 violations, (b) admitted in the Wells Submission that he knew Rule 204 close-out issues might begin with Stock Loan; and (c) testified in his third investigative testimony that he learned of Stock Loan's policy when he saw the March 2011 letter to FINRA. His actual testimony on this issue is not materially inconsistent. The colloquy during his first investigative testimony was: "During the time you were the CCO of Penson Worldwide or PFSI, were you aware that the stock loan department had a policy of closing out Rule 204 close-outs after market?"⁵¹ In response to this compound and poorly worded question, Delaney responded, "I

⁴⁸ The Division also argues that Delaney testified inconsistently on whether he was concerned about the disclosure to FINRA in March of 2011. In addition, the Division claims Delaney was "evasive" at the hearing because he would not admit that he had seen the exact adoption release from the Federal Register (Ex. 67), and indicated he was no longer the CCO of the brokerage for First Command. These arguments are nothing more than a desperate attempt by the Division to try to impugn Delaney's credibility. These issues are so immaterial to any issue in this case that it should be given short shrift and disregarded as an improper attempt to impeach a party on a collateral issue. *See e.g., U.S. v. Williamson*, 202 F.3d 974, 979 (7th Cir. 2000) (observing that attempts to "impeach by contradiction on a 'collateral or irrelevant matter,' to be "impermissible."). Indeed, they are faux impeachment; the Division has not established they are false. (Delaney's Response to Division's Proposed Finding of Fact 65, 322.)

⁴⁹ *See* Delaney's Response to Division's Finding of Fact 63(a).

⁵⁰ The number of Rule 204T/204 violations with respect to long sales of loaned securities is extremely small in comparison to the number of long sales of loaned security positions cleared by Penson during the relevant period (0.68%). *See* Stipulated Finding of Fact 52. In light of this, the issue of whether the approximately 1,500 violations the Division identified, out of 230,000 positions, constitutes a "systematic practice" is not conceded, but remains open for decision by the trier of fact.

⁵¹ *See* Division's Proposed Finding of Fact 63(a).

was not aware of that.”⁵² Delaney was, at one time, the CCO of both Penson Worldwide and PFSI. His tenure at Penson Worldwide ended before Rule 204T was adopted, so he could not possibly have been aware of a policy to close-out after market at that time.⁵³ It is also very vague what “after market” means in the question—market open or market close? The Division did not attempt to clean this question up at the hearing.

Nevertheless, even if Delaney understood the question to ask whether he discovered the violative policy in this case when he was the CCO of PFSI, Delaney’s response is not materially inconsistent with his response in his third testimony that he discovered the violative policy in March of 2011. It is undisputed Delaney “gave notice to Penson that he was resigning as chief compliance officer and leaving Penson . . . in mid-March 2011.”⁵⁴ The difference of a span of days—at best—is not materially inconsistent, particularly concerning events occurring years before. In his first testimony, furthermore, Delaney expressly notified the Division that he did not prepare and did not have a “good recollection of these events at that point.”⁵⁵

With respect to Delaney’s testimony regarding his escalation to Yancey, there is *no* inconsistency at all. As the Division acknowledges, Delaney has always testified that he did not escalate the violations at issue to Yancey.⁵⁶

In fact, the Division’s argument that Delaney has been inconsistent is entirely based on the Wells Submission. This position was erroneous, as confirmed by this Court’s ruling that it would not “rely upon” the Wells Submission “in deciding the pending claims and defenses.”⁵⁷

⁵² *See id.*

⁵³ *See* Delaney’s Response to Division’s Proposed Finding of Fact 63(a).

⁵⁴ *See* Stipulated Finding of Fact 56.

⁵⁵ *See* Delaney’s Response to Division’s Proposed Finding of Fact 63(a).

⁵⁶ *See* Division’s Post-Hearing Brief, p. 8.

⁵⁷ *See* Order, January 15, 2015.

3. **Delaney did not recklessly disregard violations of Rule 204T/204.**

Acknowledging there is no evidence that Delaney knew of the Rule 204 violations at issue, the Division alternatively argues that Delaney received “red flags” of non-compliance, and recklessly disregarded them.⁵⁸ This theory fails, even if the Division is allowed to pursue it.

To establish aiding and abetting based on recklessness, the Division must show “extreme recklessness.”⁵⁹ “‘Extreme recklessness’ or as many courts of appeals put it, ‘severe recklessness’ may be found if the alleged aider and abettor encountered ‘red flags,’ or ‘suspicious events creating reasons for doubt’ that should have alerted him to the improper conduct of the primary violator, or if there was ‘a danger ... so obvious that the actor must have been aware of’ the danger.”⁶⁰ The evidence of “red flags” or other “suspicious events” must be present in “abundance.”⁶¹ This is because the standard is not negligence or even gross negligence, but rather is “‘a state of mind closer to conscious intent.’”⁶²

The Division has not met this standard. The purported “red flags” identified by the Division are not “red flags” taken either individually or collectively, they are red herrings:

1. **Alleged Red Flag:** Delaney received email newsletters indicating Rule 204T/204 applied to long sales and could create difficulty for the stock lending industry.

Delaney’s Response: Delaney does not dispute that he received the email newsletters described by the Division. However, it is difficult to understand how the receipt of bulletins that Rule 204 could create difficulty for the stock lending industry should have alerted Delaney that Penson’s Stock Loan Department had instituted a policy or practice to violate the Rule. By analogy, a reasonable person who receives an email with a link to a news article indicating that infidelity is on the rise, would not be expected to be suspicious that his spouse is having an affair.

⁵⁸ As indicated, this argument is not the theory pled by the Division. By responding to it here, Delaney does not waive, but reaffirms, his objection to the Division’s efforts to change its case to try to circumvent a lack of proof.

⁵⁹ *Howard*, 376 F.3d at 1143.

⁶⁰ *Id.* (internal citations and footnotes omitted).

⁶¹ *Id.* at 1149 (quotations and citation omitted).

⁶² *Id.* at 1143 n. 10 (citation omitted).

2. Alleged Red Flag: Delaney purportedly did not provide guidance to Stock Loan on complying with Rule 204T/204.

Delaney's Response: This is neither accurate nor material. It is immaterial because it is undisputed that the members of Stock Loan knew at all relevant times that Rule 204T/204 required them to close out long sale transactions by market open T+6.⁶³ As Wetzig confirmed during his testimony regarding when he learned about the requirements of the Rule: "The rule came out in 2008. At that point, we had the rule We looked at the rule and read the rule."⁶⁴ Stock Loan members were the business line experts and were required to know the regulations and to develop procedures to comply with the laws.⁶⁵ Where Stock Loan knew that long sales needed to be closed out by the morning of T+6 under Rule 204T/204, and that recalls generally took three days before the shares were returned, they did not need Delaney to advise them to recall a day earlier, on T+2, to ensure compliance with Rule 204T/204. There is also expert testimony that the Rule 204 procedures in the Penson's WSPs were adequate and typical of the industry.⁶⁶ The WSPs detailed the requirements of the Rule and expressly directed Stock Loan to not only buy-in recalls if necessary to satisfy CNS obligations, but to "forward the Buy-In to the customer Buy-In department," when "Stock Loan does not have a counterparty to pass the Buy-In to."⁶⁷

The Division has also alleged that Stock Loan *intentionally* violated Rule 204T/204. As Wetzig testified, he knew they "were violating the rule, as [he] understood the rule."⁶⁸ Further "guidance" would not preclude intentional rule violations. Furthermore, Stock Loan continued to violate Rule 204 even after Delaney arranged a Rule 204 escalation meeting for Stock Loan with outside counsel in February of 2011, and ultimately left Penson.⁶⁹

Finally, as indicated in Delaney's opening Post-Hearing Brief (p. 39), there is no credible evidence that Stock Loan sought guidance. Several members of Stock Loan admitted as much (See Delaney Post-Hearing Brief, pp. 19-20, 22). Even assuming *arguendo* the Court believed that DeLaSierra and Johnson asked for guidance right after Rule 204T came out to deal with "counterparty pushback," this is not notice of a persistent practice to violate Rule 204T/204 through 2011. As Delaney testified, if counterparties are pushing back, this indicates that Stock Loan is enforcing the Rule.⁷⁰ And, there is no testimony or other evidence that

⁶³ See Stipulated Finding of Fact 70.

⁶⁴ Tr. 384:8-19.

⁶⁵ See Tr. 391:10-13, 396:15-18.

⁶⁶ See Delaney Finding of Fact 67.

⁶⁷ See, e.g., Ex. 66, pp. 387-88, 396-97.

⁶⁸ Tr. 411:8-10.

⁶⁹ See Stipulated Finding of Fact 67-68.

⁷⁰ Tr. 1195:5-12.

Delaney authorized Stock Loan to disregard the Rule.⁷¹

3. Alleged Red Flag: Delaney was copied on an email chain between Kimberly Miller and Brian Gover on May 17, 2010 regarding a FINRA observation that Penson failed to close out eight long sales in accordance with Rule 204. (Ex. 168.)

Delaney's Response: This email should be disregarded as irrelevant because there is no indication that the eight long sales referenced involved long sales of loaned securities, as opposed to fails from customer-caused long sales. Although Delaney did not recall at the hearing if he followed up on this email,⁷² he was not asked to take any action. If, however, the eight long sale close-out issues resulted from a customer initiated transaction, it is undisputed that "Delaney oversaw extensive remediation efforts" after "learning of the Rule 204 deficiencies."⁷³

4. Alleged Red Flag: Ex. 91 (the July 26, 2010 email).

Delaney's Response: Delaney comprehensively addressed the email chain in Ex. 91 in his opening Post-Hearing Brief (p. 47.) In the interest of efficiency and economy, he will not repeat that argument here but incorporates it by reference.

5. Alleged Red Flag: Delaney was copied on an email chain between Brian Gover and Mitchell Mintz, along with ten other persons, on October 13, 2010, indicating that "for Ridge Customers, although we can borrow to cover a failing long sale, we will not do so unless the correspondent contacts Stock Loan to arrange the borrow and agree the rate." (Ex. 26.)

Delaney's Response: This email is plainly irrelevant. In fact, it is so irrelevant that the Division did not ask Gover or any other witness about it at the hearing. This is not surprising as the email chain deals with the language of Penson's Buy-In notice to customers and involves only customer-caused failures of long sales, which are not at issue.⁷⁴ That the Division relies on it now is disingenuous and is a telling admission of its desperate search for evidence to try to support its case.

6. Alleged Red Flag: Delaney sent an email on October 21, 2010 attaching a FINRA exit meeting report stating, from a "review of ten CNS FTD's between February 1, 2010 and March 31, 2010," the "firm failed to recall securities from stock loan or borrow securities to close out all 10 of these fails." (Ex. 40)

Delaney's Response: This email is limited in scope and is not evidence of a consistent practice since 2008 to violate Rule 204T/204 with respect to long sales of loaned securities. Ten CNS fails over a one-month period is tiny compared to

⁷¹ See Delaney Finding of Fact 68.

⁷² See Tr. 597:23-598:11 (cited in connection with the Division's Proposed Finding of Fact 123).

⁷³ See Stipulated Finding of Fact 17.

⁷⁴ See Ex. 26.

the tens of millions of transactions cleared by Penson during that period. The Division has also not produced any evidence or testimony of the action that was to be taken in response to this exit meeting report. In fact, the Division ignores that Yancey is also copied on this email, but the Division has stipulated that he did not know of the Rule 204 violations.⁷⁵

In addition to mischaracterizing these six anecdotal occurrences as red flags of a persistent practice to violate Rule 204T/204 with respect to long sales of loaned securities, the Division also erroneously assumes that they should be read in a vacuum, instead of weighed against all of the other evidence detailed above and in Delaney's Post-Hearing Brief, indicating that Delaney did not recklessly disregard the violative practice. For example, despite meeting with members of both Penson's Stock Loan and Buy-Ins departments in connection with the extensive Rule 3012 testing of Penson's Rule 204 compliance, Alaniz did not learn that Stock Loan, rather than the Buy-Ins, closed-out fails from long sales of loaned securities or that Stock Loan was violating its close-out obligations on long sales of loaned securities.⁷⁶ Yet, the Division contends Delaney was supposed to deduce that the violations were occurring from six sporadic occurrences over a three-year period. Moreover, not only do the 3012 testing results not reference any close-out issues with respect to long sales of loaned securities,⁷⁷ they include representations from Buy-Ins and Stock Loan affirmatively indicating the adoption of measures to ensure compliance with Rule 204 for long sales:

The Stock Loan Department borrows for Rule 204 securities daily prior to market open and will monitor those borrows to ensure proper settlement of CNS fails.

* * *

The T+4 report has been reviewed and reworked to capture all required accounts per Rule 204... We are manually reviewing fails on the T+4 and T+6 reports to comply with the "close-out"

⁷⁵ See Stipulated Finding of Fact 43.

⁷⁶ See Delaney Finding of Fact 38-40.

⁷⁷ See Stipulated Finding of Fact 22, 40.

requirements. Since our discussions we have had a high success rate at meeting the “close-out” requirement. We will continue to work with the Securities Lending Department to minimize any and all violations. The T+6 report will be reviewed and reworked as necessary for compliance with Rule 204 to ensure that all account(s) that may have been missed in the past are included in the report going forward. Executions are now being done at or before the market open.... The buy in department is working to get all executions to the trading desk in sufficient time to execute, comply with the “close-out” requirements.⁷⁸

The Rule 3012 audit report alone serves as a powerful counterpoint to the six isolated “red flags” identified by the Division. When this is combined with the other evidence—including Penson’s compliance rate with Rule 204T/204 of over 99% and the fact that no one escalated any Rule 204T/204 compliance issues involving long sales of loaned securities to Delaney⁷⁹—there is simply no credible evidence that Delaney recklessly disregard an “abundance” of red flags that Penson’s Stock Loan department had instituted a policy or practice to violate Rule 204T/204, as would be necessary to find he acted with “extreme recklessness.”

4. Delaney did not have a “role” in furthering the violations.

As indicated, the Division must show that Delaney was aware not just of the primary violations, but also that “his role was part of an overall activity that was improper.”⁸⁰ To try to meet this requirement, the Division contends Delaney recklessly disregarded his “role” in furthering the violations, by failing to provide guidance on how to comply with Rule 204T/204 and by allowing Stock Loan’s compliance to go untested. Not only is it difficult to understand how Delaney could have the requisite awareness of such a role, this is far afield from the “role” alleged in the OIP and pre-hearing filings, where the Division described Delaney as an active and

⁷⁸ See Ex. 70, PFSI1136757, PFSI1136761 (emphasis added); see also Ex. 345 (containing an email from Hall to Alaniz and copying DeLaSierra and Summer Poldrack, dated March 11, 2010, indicating “I have updated the remediation document with a manual process that should keep us in compliance with Rule 204 until the development work is complete.”).

⁷⁹ See Delaney Finding of Fact 75.

⁸⁰ *Howard v. SEC*, 376 F.3d 1136, 1142 (D.C. Cir. 2004).

knowing co-conspirator with Stock Loan in a scheme to violate Rule 204T/204 for profit.⁸¹ It is also inconsistent with Delaney's purported acts of substantial assistance—deliberately concealing the violations from Yancey and regulators. In short, the Division knows it failed to prove the case it pled, and is now struggling to define what Delaney's "role" was, so it is switching to the throw-spaghetti-at-the-wall strategy. This is not permissible.

In addition to being procedurally improper, the newly envisioned "role" for Delaney is incompatible with the alleged scheme itself. A purported failure to provide guidance to Stock Loan on how to comply with Rule 204T/204 cannot further an *intentional* scheme by Stock Loan to violate the Rule. It is also undisputed that Stock Loan knew at all relevant times that Rule 204T/204 required them to close out all long sale transactions by or before market open on T+6, and that Stock Loan continued to violate Rule 204 even after Delaney arranged an escalation call to outside counsel, after the March 2011 disclosure to FINRA, and after Delaney stepped down as CCO. A purported lack of guidance thus played *no* role.

Furthermore, if the Division had intended to pursue this theory at the hearing, it needed to offer evidence establishing what a reasonable CCO's duties are in providing guidance or in ensuring compliance. Instead, the Division's "expert," David Paulukaitis, opined only on Delaney's duties assuming Delaney "became aware that Penson's Stock Loan Department was engaged in activity that violated Rule 204."⁸² That said, as detailed in pages 34-39 of his Post-Hearing Brief, Delaney satisfied any obligation he had to provide guidance.⁸³

⁸¹ See, e.g., Division's Opposition to Delaney's Motion for Postponement, p. 7 ("While the individual failures to timely close out failures to deliver on long sales of loaned securities in this matter were violations of Rule 204(a), the Division has *charged the overarching violation of the intentional practice of consistently violating Rule 204(a)*." (emphasis added)); see also OIP, ¶¶3-5, 22-24.

⁸² See Paulukaitis Expert Report, Exhibit 238, p. 16; see also Tr. 508:2-5.

⁸³ The Division argues that Delaney sent an email in August of 2009 regarding Rule 204 that did not expressly state that long sales needed to be closed out by market open T+6. This is another red herring because Stock Loan knew the rule requirements. See Delaney Finding of Fact 41. Moreover, Delaney took the language from the August 2009 email directly from guidance he received from Penson's outside counsel. See Delaney Finding of Fact 70.

The Division's argument that Delaney allowed Stock Loan to go untested is also unsupported and irrelevant. As indicated, Delaney directed Alaniz to test *Penson's* compliance with Rule 204.⁸⁴ Alaniz developed the testing process.⁸⁵ If Stock Loan's close-out procedures for long sales of loaned securities went untested, this is because neither Stock Loan nor Buy-Ins notified Alaniz that such procedures separately existed. There is no evidence that Delaney knew or allowed Stock Loan to go untested through conscious choice, recklessness or negligence.

C. Delaney Did Not Substantially Assist the Violations.

The Division argues that Delaney provided substantial assistance by misleading regulators and Yancey by intentionally concealing from them the alleged practice and policy to violate Rule 204T/204 at issue. Delaney comprehensively addressed these acts of purported assistance in his Post-Hearing Brief (pp.34-42) and, in the interest of efficiency, incorporates the argument by reference, rather than repeating it here.⁸⁶

In summary, the Division's concealment argument fails primarily because Delaney could not "conceal" something of which he was unaware because the very nature of the term concealment suggests hiding a known fact.⁸⁷ The *Kornman* decision relied upon by the Division regarding "misleading regulators" makes this point as it is limited to "deliberate deception."⁸⁸ There is also no evidence of any motive or intent for Delaney to mislead Yancey or regulators, or that any of the regulatory responses were misleading.

⁸⁴ Tr. 714:21 – 715:9; 743:17-25.

⁸⁵ Tr. 705:6-19; *See also* Delaney Finding of Fact 38.

⁸⁶ Delaney would like to correct a typographical error on page 40 of his Post-Hearing Brief, however. The sentence: "Rather it relies on data from November 2010 before remediation efforts were underway . . ." should instead read "November 2008."

⁸⁷ *See* footnote 32, *supra*.

⁸⁸ *See Gary M. Kornman*, Rel No. 34-59403, p. 10 (Feb. 13, 2009). In addition, Delaney notes that Kornman was charged and convicted of "material false statement to a federal official . . . for the purpose of misleading our investigation." *Id.* This is a very different alleged claim and primary violation that is involved here, particularly where the Division now purports to rely on a recklessness theory.

III. THE DIVISION'S CAUSING CLAIM FAILS.

The Division argues it should prevail on its causing claim because the “evidence shows that Delaney was at the very least negligent in contributing to PFSI’s Rule 204 violations.”⁸⁹ That is the sum total of the Division’s argument in this regard; it identifies no evidence and provides no analysis purporting to describe *how* Delaney acted negligently to cause Penson’s violations that is independent from its aiding and abetting analysis. This omission, combined with both the Division’s failure to mention the term “negligence” in the OIP with respect to Delaney, *and* the Division’s decision not to address its causing claim in its Pre-Hearing Brief, deprives Delaney of the requisite notice of the basis for the Division’s claims. This is impermissible for the reasons stated above in Section I. This claim should be dismissed.

In addition, where scienter is an element of the underlying primary violation, the Division cannot rely on negligence to establish causing.⁹⁰ Although Rule 204T/204 is a technical rule, the Division’s case is not based on a technical rule violation, but rather a purported “intentional practice” to “consistently” or “systematically” violate Rule 204T/204 on long sales of loaned securities.⁹¹ Similarly, all of Delaney’s alleged conduct in support of the purported primary violations is couched as intentional misconduct.⁹² Thus, the Division’s causing claim fails.

Furthermore, it is unclear what duties the Division claims Delaney breached. The evidence shows Delaney acted reasonably in fulfilling his duties as CCO of Penson, including with respect to his response, and the response of those under his direction, to the enactment of Rule 204T/204, and the alleged Rule 204T/204 violations at issue.⁹³ Delaney is not negligent, let

⁸⁹ See Division’s Post-Hearing Brief, p. 27.

⁹⁰ See *In re H.J. Meyers & Co., Inc.*, 2002 WL 1828078 at *29 (citing cases).

⁹¹ See footnote 81, *supra*.

⁹² See, e.g., OIP, ¶¶7, 8, 29, 31, 38, 39, 42, 47, 53, 60, 66, 68.

⁹³ For example, Delaney ordered extensive Rule 3012 testing of Penson’s Rule 204T/204 compliance, and it is undisputed that members of the Stock Loan department knew the requirements of the Rule. Further, there is expert

alone reckless, just because he fails to prevent a rule violation.

Finally, the Division has alleged that members of Stock Loan intentionally violated Rule 204T/204, which precludes a finding that Delaney caused any violation. Under established principles of negligence, “intentional misconduct” by a third party is a superseding cause that breaks a causal chain and relieves a party from possible negligence.⁹⁴ Where members of Penson’s Stock Loan knew of and decided to intentionally violate Rule 204T/204, no further advice that Delaney could provide, or procedures he could have put into place, would have changed the outcome. Indeed, the violations continued after Delaney left.⁹⁵

IV. THE REMEDIES SOUGHT BY THE DIVISION ARE NOT SUPPORTED.

As stated, the Division’s claims against Delaney fail. Thus, no remedies are allowed. However, even if the Court does find Delaney liable, the remedies sought are not warranted.

A. The Division Has Not Established that a Reasonable Application of the Relevant Factors Warrants a Cease and Desist Order.

The Division bases its argument that a cease and desist order is appropriate on its allegations that Delaney’s violations were egregious because he acted with a high degree of scienter, deliberately deceived regulators and was untruthful and evasive during this proceeding. As stated above, the Division has failed to prove any of these allegations. Indeed, the Division has not identified any motive or other reason as to *why* Delaney would help Stock Loan violate Rule 204T/204 or mislead regulators. This argument is so flawed that it should be disregarded outright. The Division’s attempted shift in theory to “recklessness” certainly does not support its

testimony indicating that Penson, under Delaney’s direction, had reasonable processes in place to comply with Rule 204T/204—a fact conformed by Penson’s actual compliance rate in excess of 99%. *See* Delaney Finding of Fact 75.

⁹⁴ *See, e.g., Rupert v. Daggett*, 695 F.3d 417, 426 (6th Cir. 2012) (observing “intentional misconduct by the victim or third party will generally be considered a superseding cause”); *U.S. v. Speakman*, 594 F.3d 1165 (10th Cir. 2010) (observing, “a third party’s intentional tort will generally be held as a superseding cause of harm, thereby relieving another party of liability for negligence, and sufficient to “break the causal chain”); Restatement (Second) of Torts § 448 (“The act of a third person in committing an intentional tort or crime is a superseding cause of harm to another resulting therefrom....”).

⁹⁵ *See* Stipulated Finding of Fact 67.

argument that Delaney “acted with a high degree of scienter.” The Division’s reliance on *Kornman* is misplaced for the reasons stated above.

The Division has also not established that Delaney is a risk of future violations. He has no past violations,⁹⁶ and the mere fact that he is still working in a compliance-related position is not sufficient to establish he is a risk of future violations.⁹⁷ Finally, the Division is correct on one point – Delaney has not admitted wrongful conduct. Of course, it is his right to defend himself and to deny the Division’s unproven allegations of misconduct.⁹⁸ Where Delaney’s assertion of his right to defend himself is the sole basis for the cease and desist order, the Division has failed in its proof.

B. There is No Basis to Impose the Extreme Sanction of a Bar.

To support its case for the extreme sanction of a bar against an individual with an otherwise spotless record, the Division relies on the same primary arguments it relied upon to support its request for cease and desist order. As indicated above, however, the Division has failed to establish that Delaney engaged in egregious behavior, or deliberately mislead anyone. A finding of liability based on recklessness is not sufficient to demonstrate egregiousness or bring this case within the authorities cited by the Division based on “deliberately” deceiving

⁹⁶ As set forth in Delaney’s response to the Division’s Proposed Conclusions of Law 32-33, the Division’s assertion that “a past violation suffices to establish a risk of future violations” is incorrect. The Division fails to tell the Court that the Commission backed off this position in a subsequent order in the *KPMG Peat Marwick* case. *See KPMG Peat Marwick LLP* Rel. No. 44050 (Mar. 8, 2001)—“This does not mean, however, that even in the ordinary case issuance of a cease-and-desist order is ‘automatic’ on a finding of past violation. Instead, as we made clear in our opinion, ‘[a]long with the risk of future violations, we will continue to consider our traditional factors in determining whether a cease-and-desist order is an appropriate sanction....’”

⁹⁷ *WHX Corp. v. SEC*, 362 F. 3d 854, 859 (DC Cir. 2004) (“Under [the SEC’s] view, apparently the “risk of future violation” is satisfied if (1) a party has committed a violation of a rule, and (2) that party has not exited the market or in some other way disabled itself from recommission of the offense. Given that the first condition is satisfied in every case where the Commission seeks a cease-and-desist order on the basis of past conduct, and the second condition is satisfied in almost every such case, this can hardly be a significant factor in determining whether a cease-and-desist order is warranted. The Commission itself has disclaimed any notion that a cease-and-desist is “automatic” on the basis of such an almost inevitably inferred risk of future violation.”)

⁹⁸ *KPMG, LLP v. S.E.C.*, 289 F.3d 109, 127 (D.C. Cir. 2002) (*dissent*) (observing “[t]he reconsideration order criticizes KPMG for its ‘consistent failure to recognize the seriousness’ of its violations. True, KPMG mounted a vigorous defense to the SEC’s case, but those charged with misconduct have a right to defend themselves.”).

regulators. Furthermore, the Division's argument that Delaney lied about stepping down as CCO is erroneous. Delaney testified only that he is no longer the CCO of in his current broker-dealer. This is completely true, and is supported by Delaney's publicly available Form U-4. Hugh Simpson does not contradict this where he testified that Delaney remained in a compliance role only in a separate "holding company."⁹⁹

In short, Delaney did not know about Stock Loan's Rule 204T/204 violations and he did not benefit from them. The investing public and the marketplace were not harmed. Delaney's defense of himself should not be considered a negative. He has a right to assert his position, especially since that position is the correct one. There is no reason to believe that Delaney will deviate from his strongly-held position that regulatory rules must be followed in all cases. Finally, there is no indication that the Division intends to bar DeLaSierra, Hall, Gover or Wetzig, all of whom knew of the Rule 204 violations.¹⁰⁰ No bar should be imposed.

C. A Civil Penalty Is Not Warranted Under These Circumstances.

The Division argues that the imposition of a civil penalty against Delaney under 15 U.S.C. §78u-2(a)(1)(B) is in the public interest. To assess what is in the public interest, the Commission may consider a number of factors, including whether the violation involved fraud or deceit or deliberate or reckless disregard of a regulatory requirement, the harm to other persons, the unjust enrichment of the violator, the previous regulatory and criminal history of the violator and the need for deterrence. Applying these factors here shows it would not be in the public interest to impose a civil penalty. No fraud was involved and there was no evidence of (a) deliberate or reckless violation of the rule; (b) harm to the investing public; (c) that Delaney was unjustly enriched; or (d) that Delaney has prior violations or criminal history. Delaney's

⁹⁹ See Delaney's Response to the Division's Proposed Finding of Fact 322.

¹⁰⁰ Wetzig admitted at the final hearing to violating Rule 204 as he understood the rule, but was not barred. See Tr. 404:7-16; 411:3-10.

commitment to seeing that regulatory rules are followed obviates the need for deterrence.

The Division further asks that the highest level of civil penalty - a third-tier penalty - be imposed. This is an onerous penalty. For an individual, it is now \$160,000. Under 15 U.S.C. §78u-2(b)(3), a third-tier penalty is justified when the act or omission involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement and the act or the substantial losses to other persons or resulted in substantial pecuniary gain to the person who committed the act or omission. The Division argues in its Post-Hearing Brief that Delaney's conduct involved a deliberate or reckless disregard of a regulatory requirement, but the Division does not even attempt to address the second prong of the test – the harm or risk of substantial loss. The reason the Division ignores this part of the test is that they have proven no such loss or risk of loss.¹⁰¹ Thus, the imposition of any a civil penalty is unwarranted. The Division's request for a third-tier penalty is unsupported by even its own allegations.

D. There is No Basis to Order Disgorgement.

There is no disagreement between the parties about the standards for disgorgement. The disagreement comes from the Division's speculation about what disgorgement should be in this case. The Division claims that Delaney got \$40,000 in bonuses during the relevant time period. The Division then speculates that one-third of Delaney's bonus, amounting to approximately \$13,000, comes from violations of Rule 204T/204. There is no proof to support the Division's speculations, or any other evidence to show how Delaney's bonuses were tied to the purported violations. Moreover, the Division did not seek disgorgement against Johnson or Wetzig.

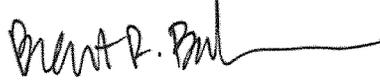
CONCLUSION

For the foregoing reasons, and those set forth in Delaney's opening Post-Hearing Brief, the claims and remedies sought against Delaney should be denied.

¹⁰¹ See Division's Post-Hearing Brief, pp. 47-48.

DATED this 20th day of January, 2015.

CLYDE SNOW & SESSIONS

A handwritten signature in black ink, appearing to read "Brent R. Baker", with a long horizontal flourish extending to the right.

BRENT R. BAKER

ATTORNEYS FOR RESPONDENT THOMAS R. DELANEY II

