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UNITED STATES OF AMERICA

BEFORE THE

SECURITIES AND EXCHANGE COMMISSION

Admin. Proc. File No. 3-18143 - (FINRA SD-2130)

IN THE MATTER OF THE APPLICATION
OF ROBERT J. ESCOBIO FOR REVIEW
OF ACTION TAKEN BY FINRA.
_____/

APPLICANT, ROBERT J. ESCOBIO'S REPLY BRIEF TO FINRA'S BRIEF IN OPPOSITION TO HIS APPLICATION FOR REVIEW

December 8, 2017

Attorneys for Applicant,
ROBERT J. ESCOBIO,

Joseph W. Beasley, Esq.
BEASLEY, DEMOS & BROWN, LLC
201 Alhambra Circle, Suite 601
Coral Gables, FL 33134
Tel.: 305-669-3131, Fax: 786-615-8945
jbeasley@beasleydemos.com
jmanley@beasleydemos.com

TABLE OF CONTENTS

PAGE

TABLE OF CONTENTS i

TABLE OF AUTHORITIES ..... ii-iii

INTRODUCTION 2

ARGUMENT 4

I. The Facts Refute FINRA's Contention That Susan Escobio Is Not Capable of Supervising a Statutorily Disqualified Person 4

II. The Proposed Supervisory Plan is More Than Adequate 9

III. FINRA's Opposition Reveals Its Denial of Mr. Escobio's Employment Relies Solely On the CFTC Judgment, Not the "Totality of the Circumstances" 11

IV. FINRA's Denial of Mr. Escobio's Application for Continued Employment in the Securities Industry is Punitive Regardless of Whether it Arises from a Statutory Disqualification or Disciplinary Proceeding 12

CONCLUSION 15

CERTIFICATE OF COMPLIANCE WITH RULE 450 (d) 16

CERTIFICATE OF SERVICE 16

TABLE OF AUTHORITIES/CITATIONS

Page

Cases

Bank of America Corp v. City of Miami, FL,
137 S. Ct. 1296 (May 1, 2017) 12, 14

CFTC v. Southern Trust Metals, Lorely Overseas Corp and Robert Escobio,
Appeal No. 16-16544 3

Dura Pharm. Inc. v. Broudo,
544 U.S. 336 (2005) 12

Kokesh v. S.E.C.,
137 S.Ct. 1635 (2017) 13, 14

Luther E. Oliver,
51 S.E.C. 914 (1993) 8

Matthews v.Eldridge,
424 U.S. 319 (1976) 4

Patricia Ann Bellows,
67 SEC Docket 2910, 2912 (Sept. 8, 1998) 7

Planned Parenthood v. Casey,
505 U.S. 833 (1992) 4

Prime Capital Servs., Inc.,
SEC Administrative Proceeding File No. 3-13532,
Initial Decision Release No. 398 (June 25, 2010) 7

Richard Hoffman,
SEC Administrative Proceeding File No. 3-9786,
Initial Decision Release No. 158 (Jan. 27, 2000) 7

Saad v. S.E.C.,
718 F.3d 904 (D.C. Cir. 2017) 13

The Securities and Exchange Act of 1934 ("Exchange Act")

Securities Exchange Act
Section 3(a)(39)(F) 13

The Securities Exchange Act of 1934 ..... 14, 15

Rules and Regulations

FINRA Rule 3012 6

FINRA Rule 3110(b)(6)(c) and (7), Supp. Note 10 6

FINRA Rule 3130, Supp. Note .08 8

S.E.C. Rule 452, 17 C.F.R. 201.452 6

INTRODUCTION

Robert J. Escobio, ("Mr. Escobio"), replies to FINRA's Opposition Brief to Mr. Escobio's Application for Review of FINRA's decision barring his continuing association with Southern Trust Securities, Inc., ("STS"), based on statutory disqualification as follows:

FINRA, in its opposition, focuses on essentially two reasons to support its position. First, it asserts that STS's supervision and supervisory plan for Mr. Escobio is inadequate; and second, the "recency" and "seriousness" of the CFTC Judgment. FINRA's arguments in support of its positions underscore Mr. Escobio's position that FINRA's arguments reflect that its decision is not based on any specific criteria, rules or law and lacks any real factual basis. In short, FINRA's arguments reflect it did not consider the "totality of the circumstances" and applied no specific standards, other than its erroneous conclusion that a female spouse cannot supervise her male spouse in the securities industry, regardless of her own decades of extensive experience in every aspect of the securities industry, including exemplary compliance and undisputed supervisory responsibilities, and the lack of any regulatory issues during the entire time.

FINRA's opposition causes and/or contributes to the alleged supervision issue by taking the position that STS's proposed supervisory plan is not good, but points to nothing of substance to support its claim. In other words, FINRA's position is that STS's supervisory plan is not good, despite FINRA's lack of any stated requirements, rules or guidance as to what is needed for a suitable supervisory plan or what FINRA would find proper. FINRA's unreasonable position is that it does not provide help or guidance, and FINRA can simply reject any supervisory plan that does not meet its unarticulated and hidden criteria for a proper plan of supervision. FINRA's position lacks any procedural and

substantive due process protections. It constitutes a deprivation of livelihood based on arbitrary rules that provide no realistic process.

FINRA's position that it looked at the "totality of circumstances" and explained its basis for the conclusions are contradicted by its assertion that Mr. Escobio's continued association and continued employment in the securities industry creates an unreasonable risk of harm to the securities market or investors. FINRA, in making this assertion, ignores (1) Mr. Escobio's lack of any securities related complaints and lack of any disciplinary action for over thirty (30) years, (2) the fact that the events giving rise to the CFTC matter arose more than four (4) years ago and in a span of time, going back as far as 2009, and (3) Mr. Escobio's full cooperation with NFA, including liquidation of all customers' metal holdings and audits reflecting no missing customer funds, and the agreement by all customers who testified that their losses were due to market declines and the NFA's forced liquidation of the their holdings. These are all part of the totality of the circumstances that support Mr. Escobio's application. Yet, FINRA instead admittedly ignores these circumstances and arbitrarily argues all these circumstances are irrelevant for making a determination regarding Mr. Escobio's risk to the market, investors and the public.

FINRA's position that it will refuse to look beyond the CFTC's existing judgment, and will ignore anything collaterally attacking that judgment, even though the judgment is not final, due to a pending appeal, additionally undermines its assertion that it looks at the "totality of circumstances." This is particularly reprehensible where the undisputed testimony reflected not one customer knew, spoke to or ever dealt with Mr. Escobio regarding the matters involved; Mr. Escobio made no profit at all from the transactions; and Mr. Escobio was provided letters from the principals of the entities involving the metals

transactions confirming that the customer's metals were held by those entities and available for delivery upon the customer's requests, which were never made. R. 986-989, 1000-1004, 1259-1262, 2123.

In effect, FINRA's position is that despite the fact a procedure exists whereby a statutorily disqualified person is provided a process to avoid being barred from working in the securities industry due to a judgment, it will look only to the judgment, not the *actual circumstances* that might shed light or explain the issue as to whether there is a threat or unreasonable risk of harm to the market, investors or the public, and in spite of the fact that an appeal is pending, rendering the judgment non-final. Even if the judgment were final, the result would be whatever the judgment required, a monetary penalty. The double punishment, a draconian constitutional deprivation of livelihood without due process, is improper. As the appellate briefs in the case on appeal show, the CFTC all but admitted that it could not show a direct link between the alleged violations the district court found and the customer loses. R. 1082-1091. The CFTC's "evidence" amounted to cherry-picked phrases from account-opening agreements, expressly refuted by communications from Hantec and Berkley's principals, stating that any gold or silver purchased for an account and paid, can be "delivered for you when requested" and that the accounts held "only trade in silver bullion." R. 987, 1178-1183. CFTC v. Southern Trust Metals, Lorely Overseas Corp and Robert Escobio, Appeal No. 16-16544, Briefs of Appellants. R 1081-1023, 1137-1148, 1178-1183. Importantly, the SEC cannot accept determinations from another proceeding which not only are not final, but which involved different legal determinations. Mr. Escobio cannot be subjected to two penalties for the same alleged conduct especially when FINRA has provided no independent determination other than its

accepting CFTC's conclusions. The record of the CFTC proceeding is not before this court and cannot be used to deprive Mr. Escobio of his livelihood. FINRA's conclusions amount to violations of substantive due process because they shock the conscience, essentially ordering the death penalty in securities for someone with a clean lifelong record who was not even identified by the clients in the proceeding on which FINRA relies as the person they dealt with, and where the clients admitted the losses were caused by the decline in the silver markets. See, e.g., Planned Parenthood v. Casey, 505 U.S. 833 (1992) (rights enumerated in the bill of rights and certain penumbral rights are protected). Certainly, the right to a livelihood is one of those rights. Moreover, FINRA conducted its "process" without any procedures, without any rules, arbitrarily making determinations to deprive Mr. Escobio of his livelihood without procedural due process. See, e.g., Matthews v.Eldridge, 424 U.S. 319 (1976) (procedural due process imposes constraints on government which deprive individuals of property within the meaning of the due process clause of the Fifth and Fourteenth Amendment).

The process is further undermined by FINRA's position that a clean record of compliance by the person is meaningless and irrelevant to such determination and its unreasonable refusal to provide any meaningful guidelines or criteria for the supervision. In short, the position articulated by FINRA is its decision here renders the process a meaningless exercise in futility for Mr. Escobio and persons in his position.

ARGUMENT

I. The Facts Refute FINRA's Contention That Susan Escobio Is Not Capable of Supervising a Statutorily Disqualified Person.

FINRA argues that its denial of Mr. Escobio's application is based on matters that

"exist in fact." Primarily, it argues Mrs. Susan Escobio is incapable of supervising a statutory disqualified person, in this case, her husband. FINRA asserts that it made the required evaluation of Mrs. Escobio's proposed supervision of Mr. Escobio, considering her qualifications, experience, independence and objectivity and the adequacy of the proposed heightened supervisory plan. FINRA's basis for its assertion is that Mrs. Escobio lacks substantial supervising experience and because she is married to Robert Escobio, she has a conflict and cannot be independent or objective in supervising him.

Facts are the enemy of FINRA's claim. First, as set forth in Mr. Escobio's Initial Brief, at pages 20-23, Susan Escobio's thirty-eight (38) year background in the securities industry clearly reflects she has the extensive experience in all facets of the securities industry, including direct supervision of sales activity and employees. FINRA admits Mrs. Escobio has held a general securities principal license for over seventeen (17) years; FINRA's attempt to minimize Mrs. Escobio's experience in supervision for seven (7) years while she was at Credit Lyonnaise, mistakenly asserts that she could not supervise because she had no principal license. Credit Lyonnaise was a bank engaged in asset management, regulated by the state and no securities principal license was required to be a supervisor there. FINRA does not dispute Mrs. Escobio's thirty-eight (38) year history of work in the securities industry, nor that she has in fact supervised a statutorily disqualified person and has been the Chief Compliance Officer for over 17 years at STS, during which time there has been absolutely no complaints or regulatory actions filed against it. Mrs. Escobio has been on its Board of Directors, had ownership of controlling shares and has been and still is President of STS. There is simply nothing within the record that FINRA can point to that establishes she is incapable of supervising STS's employees or a

statutorily disqualified person. FINRA argues that the record failed to contain testimony of her supervision of a statutorily disqualified person, Sandro Flores. This is something FINRA's own records clearly show. The fact exists and if FINRA is interested in properly evaluating as opposed to simply reinforcing is arbitrary denial, it should be considered. S.E.C. Rule 452, 17 C.F.R. 201.452 (allowing additional evidence if material). If FINRA can attempt to dredge up stale 30-year old claims against Mr. Escobio for its decision from its records, it clearly could have found the much more recent information reflecting supervision of the statutorily disqualified Sandro Flores.

If thirty-eight (38) unblemished years of experience in all facets of the securities industry (decades of experience as a Chief Compliance Officer, being a Director, controlling or major shareholder and Officer of a securities broker dealer) does not qualify a person to supervise employees of the broker dealer, then nothing does. Such experience clearly provides the person with the knowledge and proficiency to easily know how and what to watch out for in supervising any sales person or employee of a broker dealer. Mrs. Escobio's testimony regarding detecting, preventing and firing registered representatives establishes this and her actual ability and authority to affect the conduct of STS's employees. R. 2188-2196

The testimony further establishes that STS is a very small one location broker dealer, with a handful of employees who work in very close proximity, such that anything being done is easily seen and overheard, which makes supervision far easier. R. 1178-1183, FINRA Rules 3012 (limited size and resource exception) and 3110(b)(6)(c) and (7), Supp. Note 10 (recognizing difference in size of firms impacts supervision). FINRA's attempt to use a case involving firms the size of Raymond James with multiple locations

and others with remote one-person offices to support its argument reflects the extent to which FINRA inaccurately attempts to justify the lack of factual basis for its decision.

Further, FINRA's argument is belied by the fact that the cases it relies upon to distinguish compliance experience from direct supervisory experience involve circumstances in which FINRA is actually holding a compliance officer responsible for a failure to supervise the firm's employees, as direct supervisors, recognizing that whether someone is a direct supervisor depends on the circumstances of the case. *See e.g.,* Prime Capital Servs., Inc., SEC Administrative Proceeding File No. 3-13532, Initial Decision Release No. 398 (June 25, 2010); Richard Hoffman, SEC Administrative Proceeding File No. 3-9786, Initial Decision Release No. 158 (Jan. 27, 2000). In these cases, the ALJ quoted from Patricia Ann Bellows, 67 SEC Docket 2910, 2912 (Sept. 8, 1998), stating:

> Determining if a particular person is a "supervisor" depends on whether, under the facts and circumstances of a particular case, that person has a requisite degree of responsibility, ability, or authority to affect the conduct of the employee whose behavior is at issue.

Indeed, FINRA's citations are out of context, and deceptively truncated to force its point. The full quotes recognize the distinction between "persons who are clearly direct, line supervisors, ***for example, a branch manager***," Richard Hoffman, *supra,* or **a category that includes a president of a broker dealer firm**, Prime Capital Services, Inc., from "employees of brokerage firms who ... have legal or compliance responsibilities" without the ability to control employees. To be considered a supervisor of an employee, "a compliance officer must be shown to have the responsibility, ability and authority to affect the conduct of an employee...." Richard Hoffman, *supra,* and Prime Capital Services, Inc.,

supra. Thus, FINRA's own cases recognize that a compliance officer can be a direct supervisor; the positions are not mutually exclusive. See FINRA Rule 3130, Supp. Note .08. As such, Mrs. Escobio's actions while the Compliance Officer for 17 years also constituted direct supervisory experience because she had the ability and authority to affect employee conduct by overseeing all sales and trading activity, evaluating same for suitability, and hiring and firing employees based on their sales activity. The evidence of these seventeen (17) years of direct supervisory experience was amply supported and undisputed in the record. See R. 2188-2196. The argument that she has "at best" three years of experience is not founded upon any reasonable interpretation of this direct evidence.

FINRA's position that Mrs. Escobio cannot "supervise her long-time spouse" reeks of sexist discriminatory bias. The fact is Mrs. Escobio has been in the industry for thirty-eighty (38) years, in charge of compliance for more than a decade at STS, an Officer, Director and President of STS, has major financial interests in its success and holds necessary securities licenses, all of which would be jeopardized if she did not properly supervise and ensure compliance with all applicable laws and rules. Furthermore, the facts establish she not only has, but continues to supervise Mr. Escobio regardless of their marital relationship. There are no FINRA or securities laws or rule prohibiting a wife from supervising her husband or vice versa in the securities industry.

FINRA points to nothing establishing Mrs. Escobio has <u>not</u> been able to supervise Mr. Escobio or to any authority that this arrangement presents an actual impermissible conflict. FINRA's reliance on the <u>Luther E. Oliver</u>, 51 S.E.C. 914 (1993), (p.17 of Opposition Brief), case in an attempt to find some case to support its assertion is amazing.

In that case, the decision had nothing to do with the persons being spouses; it was based on the fact that the proposed supervising spouse ***had no financial training***. That is the polar opposite of the case with Mrs. Escobio. The fact that this is the only authority FINRA can cite to support this position speaks volumes as the prime evidence that there was no support for this conclusion and it is wholly arbitrary.

FINRA's further attempt to hide its bias by stating there was nothing addressing the "potential conflict" created by the marriage, ignores that nothing can eliminate such "potential conflict" because the marriage in fact exists. This is no different than a "potential conflict" that can exist between parents and children, step-parents and children, or siblings. Such "potential conflict" does not mean a person cannot objectively supervise another who is related to the supervisor. This is a position FINRA has not previously advanced. FINRA's assertion that Mrs. Escobio cannot objectively supervise her spouse is simply an attempt to indirectly dress up a discriminatory bias as fact.

FINRA claims back-up supervision is insufficient when Mrs. Escobio is out of the office for a period of time because this is not stated in the supervisory plan, conveniently ignoring Mr. Trombatore's testimony that he would come to Miami to supervise Mr. Escobio. R. 2241-2242. The fact is that both he and Mrs. Escobio testified that this would be done. Mr. Trombatore has worked in the securities industry for decades. His decades of experience in securities provides him with the skill, experience and knowledge to know where and how to ensure a person involved in securities sales can be properly monitored and supervised. Experience in the particular areas of the business is the best way to gain the required expertise. FINRA points to nothing showing Mr. Trombatore is incapable of

providing the necessary supervision as a back-up for Mrs. Escobio, when she is out of the office.

II. The Proposed Supervisory Plan is More Than Adequate.

FINRA asserts that STS's proposed supervisory plan is not acceptable. FINRA states the plan is: "lacking in design to prevent future fraudulent activities by Escobio;" "provisions appear applicable to all of the firms registered representatives;" "fails to provide for documentation with firm's compliance plan;" and, "fails to designate Trombatore as Escobio's alternate supervisor." A cursory review of the proposed plan clearly refutes FINRA's position. See STS' Revised Heightened Supervisory Plan, R. 1251-1258.

STS in its Initial Brief set out at pages 23-25 specific provisions of the plan which clearly state they are specifically directed at Mr. Escobio, and require action by Mr. Escobio, not just persons in general. R. 1251-1258. Even if FINRA were correct, which it is not, there is no reason STS or any firm could not apply heightened supervisory requirements to all registered representatives; this is especially true and easy for a firm with only two or three registered representatives, such as STS. Additionally, the proposed plan required written documents to be executed attesting to the various compliance requirements and signing off by Mr. Escobio's supervisor on various records of STS reflecting STS had reviewed Mr. Escobio's transactions, communications and compliance with the plan's requirements. R. 1251-1258. The proposed supervisory plan details the process and reflects how virtually nothing done will escape it. Id.

FINRA attempts to minimize the fact that the plan implemented, and even the prior plan, clearly were effective because no disciplinary complaints or regulatory violations have occurred over the years. FINRA claims too little time has passed, stating it is only a

year since the CFTC judgment. This ignores the 4+ years that have passed since the matters underlying the judgment concluded without a violation, despite Mr. Escobio having been engaged in the securities business at STS. Facts refute FINRA's conclusory assertions that STS's plan fails to address its unspecified concerns as to what is "lacking" in the plan. FINRA's stated position is that it can simply state the plan lacks sufficient safeguards to prevent fraudulent activities, but it has no obligation and will provide no guidance as to what might satisfy it if included in such plan. This underscores the arbitrariness and capriciousness of FINRA's decision.

III. FINRA's Opposition Reveals Its Denial of Mr. Escobio's Employment Relies Solely On the CFTC Judgment, Not the "Totality of the Circumstances."

FINRA acknowledges that its decision determining whether to allow Mr. Escobio to continue employment in the securities industry requires that it examine and consider the "totality of the circumstances," not just the disqualifying event - the stated goal being to determine whether Mr. Escobio's continued employment poses an unreasonable risk to the securities markets or investors. FINRA's opposition clearly reflects it relies solely upon the CFTC judgment, not the totality of the circumstances to deny Mr. Escobio's application. FINRA states its denial is based on the "recency" and "seriousness" of the CFTC judgment. FINRA relies on the CFTC judgment for its assertion that Mr. Escobio's continued employment presents an unreasonable risk of harm to the market and investors and "that too little time has passed since the judgment to demonstrate otherwise." This reasoning exposes FINRA did not rely on the "totality of the circumstances," as required, especially when FINRA states its position is not to consider the issues and facts underlying the judgment or consider the facts and issues raised and set out in the pending appeal.

A cursory examination of the appellate briefs and issues undermines the basis for claiming Mr. Escobio was engaged in a wide spread fraudulent commodities scheme that harmed more than 100 customers and caused over $2.5 million claimed losses. R. 960-1028, 1129-1165, 1259-1262, Initial Brief at pages 11-19. Recent Supreme Court decisions, applying long-standing loss causation requirements clearly point to a reversal of the $2.5 million amount because the award is contrary to the law in that it is based on transaction causation, not loss causation as is required and ignores the lack of supporting evidence as well as statute of limitations issues. Bank of America v. City of Miami, 137 S. Ct. 1296 (May 1, 2017); Dura Pharm. Inc. v. Broudo, 544 U.S. 336 (2005).

FINRA's position is that it will not look beyond the non-final judgment, despite the pending appeal, nor consider Mr. Escobio's history of compliance, before, during and after the judgment. It ignores that the customers all testified that none ever dealt with Mr. Escobio, did not know who he was, never communicated with him and had no idea of any involvement by him. They all testified that their losses were due to declines in the metals market and the NFA forced liquidation of their metals without regard to their desire to keep the metals positions. FINRA's position on this emphasizes that it is not relying on anything of substance but the CFTC judgment, as opposed to considering the "totality of the circumstances". Such position renders the process for continuation a meaningless process if there is a judgment, regardless of finality.

IV. FINRA's Denial of Mr. Escobio's Application for Continued Employment in the Securities Industry is Punitive Regardless of Whether it Arises from a Statutory Disqualification or Disciplinary Proceeding.

FINRA cites several S.E.C. decisions to support its assertion that FINRA does not subject a person to statutory disqualification as a penalty or remedial sanction. FINRA

says it is done by operation of the Exchange Act, Section 3(a)(39)(F). This ignores that FINRA has created a process for allowing relief and continued employment in the securities industry regardless of statutory disqualification. It is FINRA's decision that determines the application of the remedy, not the disqualification statute. The end result is that such determination by FINRA is identical in impact and result whether the decision is a result of a disciplinary proceeding barring employment or the process after statutory disqualification. It is a distinction without a difference.

The U.S. Supreme Court's recent decision in Kokesh v. S.E.C., 137 S.Ct. 1635 (2017) and District of Columbia Court of Appeals decision in Saad v. S.E.C., 873 F. 3d 297 (D.C. Cir. 2017) clearly establish that a bar to employment in the securities industry is punitive, not remedial. Most importantly, the decisions FINRA relies upon to avoid the meaningless distinction without a difference pre-date the above recent controlling decisions. This is particularly important because the Court in Saad held that the legal precedents established before Kokesh are no longer good law. Saad *supra*. These recent decisions emphasize that the relief sought under the securities laws are to focus on the nature of the result, not the label of the relief.

For years FINRA and the S.E.C., under prior legal precedent claimed expulsion or suspension was "remedial" not "punitive" and "disgorgement" was not a "penalty". However, the Supreme Court, in Kokesh, *supra* overturned that line of cases. They are no longer good law. *See* Saad, *supra*. These decisions are clear that a bar to employment is a punishment, not remedial. This is because the bar to employment does not compensate the purported victims of the alleged wrongdoing. Id. Here the denial of Mr. Escobio's continued employment in the securities industry is the equivalent of expulsion or

suspension, which is, therefore not remedial but a penalty. *See* Saad, *supra* at 304-305. Applying the recent law here establishes the actions taken in denying Mr. Escobio continued employment is the functional equivalent of a penalty, in effect the "death penalty," and is improper and prohibited because it is impermissibly punitive as imposed under the circumstances. Additionally, Kokesh, *supra* clearly establishes that not only is the court's monetary award in the CFTC judgment contrary to applicable law because it is impermissibly based on transaction causation, as opposed to loss causation, *See*, Bank of America v. City of Miami, *supra* (reinforcing that the proximate cause requirement in Dodd Frank leaves no question that loss causation is required for determination of damages in CFTC case) but in large part is barred by applicable statutes of limitations as a penalty and based on improperly applying Dodd Frank retroactively. Applying the correct and recently established law and legal standard eliminates FINRA's reliance on the $2.5 million purported damage figure to support its conclusions of "seriousness" of the violation, among other reasons. Without that, FINRA has no argument. FINRA's analysis is further flawed in that it attempts to apply Dodd-Frank retroactively, in violation of legal and constitutional theories, including due process.

FINRA's assertion that such matters are not to be considered in its decision emphasizes it did not consider the "totality of the circumstances". Instead FINRA relied on the CFTC judgment in its decision imposing an excessive and oppressive punitive sanction by denying Mr. Escobio's application for continued employment in the securities industry. This is underscored by FINRA's failure to establish any fact reflecting Mr. Escobio presents an unreasonable risk of harm to the securities markets or investors despite years having passed since the events giving rise to the CFTC judgment, now pending decision before

the Eleventh Circuit Court of Appeals. FINRA's refusal to consider the "totality of the circumstances" and barring Mr. Escobio's continued employment imposes an excessive and oppressive punishment that is unfair and inconsistent with the goals of the Securities Exchange Act of 1934 under the circumstances, especially when the CFTC judgment is very likely to be reversed due to clear errors of law.

FINRA's opposition brief shows no basis for its action against Mr. Escobio. FINRA should be required to comply with the law, regardless of how its status is characterized as non-governmental, quasi-governmental or governmental. The civil rights laws apply to it when it conspires with governmental agencies under color of the law to deprive citizens of their constitutionally protected rights.

CONCLUSION

For all of the above reasons and those set forth in Mr. Escobio's Initial Brief, the S.E.C. should reverse FINRA's denial, and order that Mr. Escobio be allowed to associate with STS, or at a minimum, order such association be allowed pending the final determination of his appeal of the CFTC Judgment since it is the sole basis for FINRA's decision.

Attorneys for Applicant,
ROBERT J. ESCOBIO,
BEASLEY, DEMOS & BROWN, LLC
201 Alhambra Circle, Suite 601
Coral Gables, FL 33134
Tel.: 305-669-3131, Fax: 786-615-8945

By: _____
JOSEPH W. BEASLEY
Florida Bar No. 172074
jbeasley@beasleydemos.com
jmanley@beasleydemos.com

CERTIFICATE OF COMPLIANCE WITH RULE 450 (d)

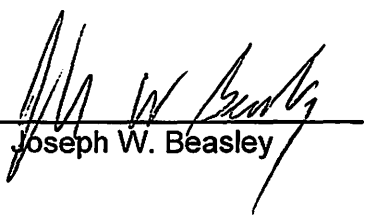
Counsel for Applicant hereby submits its Certificate of Compliance stating that the Applicant's Brief complies with the 14,000 word and page limit of Rule 450 (c) in that the word processing system used to prepare the brief determined it was 4,576 words, exclusive of pages containing the table of contents, table of authorities and any addendums.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been served upon the following parties this 8th day of December, 2017 as follows:

VIA FAX & FEDERAL EXPRESS
Office of The Secretary
United States Securities & Exchange Commission
100 F Street, N.E.
Mail Stop 1090-Room 10915
Washington, D.C. 20549
Tel.: 202-551-5400
Fax: 202-772-9324
(Original + 3 copies)

VIA E-MAIL, FAX & FEDERAL EXPRESS:
Andrew J. Love, Esq.
Associate General Counsel
FINRA
Office of General Counsel
1735 K Street, N.W.
Washington, DC 20006
Tel.: 202-728-8281, Fax: 202-728-8264
Andrew.love@finra.org
nac.casefilings@finra.org

By: 
Joseph W. Beasley