FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. SILVER LEAF PARTNERS, LLC (CRD No. 126694), Respondent.	Disciplinary Proceeding No. 2014042606902 Hearing Officer—DRS **EXTENDED HEARING PANEL DECISION** January 29, 2019

Respondent Silver Leaf Partners, LLC, is fined $100,000 for paying transaction-based compensation to non-FINRA members and for supervisory failures. Further, Respondent is prohibited from engaging in certain business lines, required to retain an independent consultant to review its supervisory procedures, and ordered to pay costs.

Appearances

For the Complainant: Danielle I. Schanz, Esq., and Jason W. Gaarder, Esq., Department of Enforcement, Financial Industry Regulatory Authority.

For the Respondent: Fyzul Khan, President and CEO, Silver Leaf Partners, LLC, Jeffrey A. Sexton, Esq., PIRATA PSC, and Salah Borghei-Razavi, Esq., Razavi Legal P.C.

DECISION

I. Introduction

By rule, FINRA prohibits its member firms from paying transaction-based compensation to non-members. FINRA's Department of Enforcement charged Silver Leaf Partners, LLC ("Silver Leaf" or the "Firm"), a FINRA member firm, with violating that prohibition. According to the Complaint, the Firm used an unregistered finder to facilitate stock loans and block trades by bringing together parties seeking to engage in these types of transactions. Further, the Complaint alleges, when a transaction resulted from the finder's introductions, the Firm received fees that it shared with a non-member entity the finder owned. The Complaint also avers that the Firm paid commissions to several non-member entities owned by Silver Leaf's brokers. Finally,

Silver Leaf was charged with failing to reasonably supervise its business, including having inadequate written supervisory procedures.[1]

Silver Leaf denied any wrongdoing and requested a hearing. A hearing was held before a FINRA Extended Hearing Panel. As discussed below, the Panel finds that Silver Leaf committed the alleged violations and imposes appropriately remedial sanctions.

II. Findings of Fact

A. Respondent Silver Leaf Partners, LLC and Its Supervisors

Silver Leaf, located in New York, New York,[2] has been a FINRA member since September 2003.[3] It began as an institutional trading firm providing correspondent clearing, financing, and trading services to institutional money managers.[4] It expanded its business in 2004 to include introductory and marketing services to hedge funds and other institutional money managers seeking introductions to institutional investors.[5] In 2009, Silver Leaf started offering those services to operating companies also seeking introductions to investor capital, debt or other financial arrangements with institutional investors, lenders, and various types of sophisticated counterparties.[6] From January 2012 to April 2015 (the "relevant period"), the Firm had 65 to 75 registered representatives.[7]

During the relevant period, Silver Leaf had two business lines pertinent to this proceeding: investment banking and hedge fund marketing.[8] The alleged improper payments occurred in both business lines. Investment banking consisted of "providing corporate services to clients who had financial needs" but did not include underwriting public offerings.[9] More specifically, the Firm helped parties that were looking for capital locate other parties that could provide it.[10] Hedge fund marketing consisted of serving hedge fund managers by seeking out entities that might want to invest in the hedge fund managers' investment products.[11] The Firm's

---

[1] FINRA has jurisdiction over this matter under Article IV of FINRA's By-Laws because (a) the Firm currently is a FINRA member; and (b) the Complaint ("Compl.") charges the Firm with securities-related misconduct committed while it was a FINRA member. Amended Statement of Answer ("Ans.") ¶ 6; Stipulations ("Stip.") ¶ 3.

[2] Stip. ¶ 2.

[3] Ans. ¶ 6; Stip. ¶ 1.

[4] Stip. ¶ 4.

[5] Stip. ¶ 5.

[6] Stip. ¶ 6.

[7] Ans. ¶ 7; Stip. ¶ 2.

[8] The Firm also offered trading services, but they are not relevant to this proceeding. Tr. 1058.

[9] Tr. 1053–55.

[10] Tr. 1055–56.

[11] Tr. 1059–60.

hedge fund marketers, also known as third-party marketers, were independent contractors of Silver Leaf and were hired by the institutional money managers to introduce institutional investors to the funds. If the investors then invested in the hedge fund based on the introductions, then a portion of the manager's compensation would be paid to Silver Leaf and to the marketer.[12] By May 31, 2013, the Firm viewed the hedge fund marketing business line as having been "critical" to the Firm's continuation "as a going concern."[13]

Fyzul Khan and Kevin Meehan were the Firm's co-owners during the relevant period.[14] Khan, the majority owner,[15] was a co-founder of the Firm and served as its chief executive officer, chief compliance officer, and managing member.[16] Khan oversaw the Firm's hedge fund marketing services and capital introductory and investment banking transactions, and was responsible for the Firm's general compliance supervision.[17] Meehan, the Firm's financial and operations principal,[18] was also the Firm's vice-chairman, president, chief financial officer, and minority owner.[19] Meehan oversaw the institutional brokerage services and was responsible for the Firm's finance and accounting functions. His day-to-day activities primarily involved dealing with accounting operations, net capital computations, payroll, cash reconciliations, and various office management issues.[20]

B. Silver Leaf's Transaction-Based Compensation Payments to an Unregistered Finder's Non-Member Entity

In 2012, Silver Leaf began a working relationship with SH, a U.S. citizen[21] and chief executive officer of NAPI, a Florida corporation.[22] SH helped develop existing business lines for Silver Leaf in which the Firm brought together persons and entities interested in participating as counterparties in stock loan and block trade transactions. The Firm's payments to SH for

---

[12] Tr. 87–89, 91–92.

[13] JX-7, at 1; Tr. 95. *See also* Tr. 1831 (Khan describing hedge fund marketing as developing into a "major line of business for the firm").

[14] Tr. 99–100, 1825.

[15] JX-7, at 1.

[16] Tr. 1241–42, 1810–11; JX-42, at 6. Khan, a licensed attorney, represented that at the time of the hearing, he was the Firm's principal officer and owner. Tr. 6, 1804, 2169.

[17] Stip. ¶ 7.

[18] Stip. ¶ 9.

[19] Tr. 82–84, 1826–28; JX-7, at 3; JX-21, at 1; JX-19, at 9. Meehan testified that he resigned from the Firm in December 2015 but remained at the Firm for another year as a consultant. Tr. 64. According to FINRA's Central Registration Depository ("CRD"), his registrations with the Firm terminated on February 28, 2017. JX-45, at 5. Meehan gave up his ownership interest on December 31, 2015. JX-21; Tr. 67.

[20] Tr. 324.

[21] Tr. 1271, 1943; CX-178.

[22] CX-39.

facilitating these types of transactions underlie one set of charges alleging improper payments to a non-member. The payments to SH were reflected and discussed in numerous emails sent and received by the Firm. As discussed later in the section pertaining to supervision, these communications constituted red flags of misconduct that Khan and Meehan ignored or failed to see and, in some instances, demonstrated their direct participation in the alleged wrongdoing.

* * *

SH became involved with Silver Leaf through Jay Chapler,[23] the Firm's head of investment banking.[24] Chapler generated stock loan and block trade business for Silver Leaf.[25] The loans he focused on involved somewhat illiquid foreign stocks with relatively small capitalization.[26] There was some overlap in the block trading and stock loan business because they were in the same sector, and the lenders sometimes found that they needed to sell the collateral when a loan defaulted.[27] The Firm did not act as a counterparty. Rather, it served as a facilitator, also called a referral agent, introducing parties who wanted to enter into these transactions.[28] As Chapler pursued capital introductory and investment banking transactions, he interacted with a variety of principals and agents seeking counterparties for themselves or for their clients.[29]

Silver Leaf's stock loan and block trade business took a new turn around the end of 2011 or early 2012, when Chapler met SH.[30] Chapler learned that SH had connections to successful businesspersons in Turkey and the Middle East.[31] He concluded SH "was a very good networker"[32] and "could be a good source" of deal flow[33] because he "had a network in Turkey

---

[23] Under a Letter of Acceptance, Waiver and Consent ("AWC") dated April 19, 2017, Chapler was fined $22,500 and suspended for four months in all capacities by FINRA. Without admitting or denying the findings, Chapler consented to findings that from 2012–2013, he paid or caused to be paid transaction-based compensation earned by his member firm (Silver Leaf) to an unregistered entity (NAPI). JX-44, at 13–14; JX-32; Tr. 389.

[24] Tr. 1083–86. According to Chapler, he was the managing director of investment banking—a title he said Khan had approved. Tr. 370, 381, 551. But at the hearing, Khan claimed that he, rather than Chapler, was really the head of investment banking and that Chapler's title was basically an "honorific." Tr. 1919–20. That said, Khan held out Chapler as the head of the Firm's "investment banking business" and head of the "investment banking division." CX-31; CX-32; CX-35, at 3.

[25] Ans. ¶ 57; Schedule of Initials to Complaint, at 1.

[26] Tr. 405–09.

[27] Tr. 410–12.

[28] Tr. 2377–79, 2382–83.

[29] Stip. ¶ 10.

[30] Tr. 475, 1090.

[31] Stip. ¶ 12; Tr. 1110, 1923.

[32] Tr. 475.

[33] Tr. 476.

to drum up business."[34] Six months after meeting SH, Chapler introduced him to Khan.[35] This eventually led to SH playing a key role in Silver Leaf's business. In Khan's words, the Firm needed SH "to sort of represent us as our agent locally" in Turkey and the Middle East.[36] Silver Leaf (through Khan) authorized SH "to review and recommend companies for funding and lending as well as recommend a company's suitability" and "to investigate and do any due diligence on companies that Silver Leaf may potentially look to finance or provide services to."[37] He acted as the "introducing agent" for the Firm,[38] finding parties in Turkey who wanted to obtain a loan against their stocks.[39] SH also generated "structuring ideas" on certain deals[40] and operated as a facilitator between the Firm and other brokers.[41] According to Chapler, SH reviewed all of the Firm's deals in Turkey.[42]

Chapler and SH sought to match SH's Turkish and Middle Eastern connections with securities lenders, including BHP, a Bahamian company with offices in Toronto, Canada,[43] and its competitor,[44] EFH,[45] a Delaware limited liability company with a place of business in Indianapolis, Indiana.[46] On April 24, 2012, Silver Leaf entered into an advisory agreement with BHP.[47] Under the agreement, Silver Leaf would introduce BHP to "prospective borrowers suitable for BHP's collateralized stock loan and block purchase business." In exchange, BHP agreed to pay Silver Leaf a reasonable commission percentage based on the net amount of stock loans or block trades executed as a result of Silver Leaf's efforts.[48]

---

[34] Tr. 450.

[35] Tr. 1090, 1922.

[36] Tr. 2043.

[37] CX-45.

[38] Tr. 391.

[39] Tr. 391.

[40] Tr. 940; CX-57, at 2.

[41] Tr. 1111–12.

[42] CX-43, at 1.

[43] Tr. 448.

[44] Tr. 462.

[45] Stip. ¶ 13.

[46] CX-182.

[47] JX-40. While Khan testified that SH "secured" the Firm's relationship with BHP, CX-57, at 2, Chapler maintained that he introduced BHP to Silver Leaf. Tr. 448, 1088–89.

[48] Stip. ¶ 14; JX-40, at 1. This "reasonable commission" is also referenced in the agreement as an "origination fee." JX-40, at 1.

The next day, April 25, 2012, SH and Chapler's company, DEMC Capital LLC ("DEMC Capital"),[49] entered into a consulting agreement under which DEMC Capital would split equally with SH any fees it received.[50] The agreement recited that the Firm had "agreements with stock lenders BHP and EFH, to receive the origination fee … on stock loans it arrange[d]"; that DEMC Capital had an agreement with the Firm to receive a payout on those fees for loans that it arranged; and that SH was "providing consulting and introductory services to DEMC Capital in connection with the arrangement of those stock loans …."[51] According to Chapler, the purpose of the agreement was to share his fees from stock loans with SH[52] because, as he put it, "nobody works for free."[53] Both a partially executed agreement (signed by SH) and a fully executed version passed through Silver Leaf's email system.[54]

On five occasions from September 2012 to August 2013, Chapler split fees with SH on stock loan and block trade transactions SH helped facilitate—two in 2012 and three in 2013. These transactions benefited the Firm.[55] During that period, neither SH nor NAPI became registered.[56] After the hearing, Enforcement withdrew the three 2013 payments to SH as a basis for liability.[57] The 2013 payments, however, are still relevant to the supervision charge as well as to sanctions.[58] Therefore, we address each of the five payments, below.

---

[49] Chapler was the sole owner of DEMC Capital. Tr. 380–81.

[50] CX-41.

[51] CX-41, at 2. The agreement reflected that the parties had addresses within the United States and provided that it was governed by New York law. CX-41, at 2–3.

[52] Tr. 463–64.

[53] Tr. 456.

[54] CX-40; CX-41. That said, Chapler testified he never told anyone at the Firm about his fee-splitting agreement with SH. Tr. 465, 469.

[55] Tr. 2424–25.

[56] Tr. 389, 392, 481, 1926–27. The Firm started the process of registering SH because, according to Chapler, they "wanted to figure out a way to pay him in a proper way." Tr. 480–81. This process included conversations between the Firm and SH and involved Khan. Tr. 1104; CX-159. But SH "just never followed up" on becoming registered, Chapler said. Tr. 481.

[57] *See* Department of Enforcement's Post Hearing Brief at 22–23.

[58] *See Dep't of Enforcement v. Ahmed*, No. 2012034211301, 2015 FINRA Discip. LEXIS 45, at *121 n.107 (NAC Sept. 25, 2015) ("Evidence of misconduct that is not alleged in the complaint, but is similar to the misconduct charged in the complaint, is admissible to determine sanctions.") (citing *Wanda P. Sears*, Exchange Act Release No. 58075, 2008 SEC LEXIS 1521, at *22 n.33 (July 1, 2008) (finding in an unauthorized trading case that evidence of unauthorized trading not alleged in the complaint was still admissible for assessing sanctions)), *aff'd*, Exchange Act Release No. 81759, 2017 SEC LEXIS 3078 (Sept. 28, 2017).

1. The September 7, 2012 Payment

IH, a Turkey-based company, was one of SH's Turkish contacts.[59] SH introduced IH to Chapler, who, in turn, introduced a transaction to EFH.[60] On August 28, 2012, IH and EFH entered into a stock purchase agreement.[61] Under the agreement, IH would sell shares of Usas Ucak Servisi AS ("UCAK") in several tranches to EFH.[62] The agreement provided for the payment of origination fees to Silver Leaf in connection with each tranche.[63]

On September 6, 2012, EFH paid Silver Leaf $13,233.00 in transaction-based compensation for a block trade transaction[64]—the first tranche under the agreement. The next day, September 7, Meehan emailed a payout calculation to Chapler reflecting that "S" was due 45 percent of this amount, i.e., $5,954.85.[65] That day, Chapler received a net payout of $11,413.46 ($13,233.00 minus an administrative fee of $1,819.54)[66] and then, through DEMC Capital, Chapler wired $5,954.85 to SH's firm, NAPI.[67]

2. The September 14, 2012 Payment

On September 13, 2012, Silver Leaf received $99,383.03 from EFH in transaction-based compensation relating to the second tranche of the IH/EFH block trade transaction.[68] On September 14, 2012, in connection with this transaction, the Firm wired $85,612.86 to Chapler's firm, DEMC Capital,[69] and Chapler wired $44,722.36 to SH's firm, NAPI.[70] This payment to NAPI again represented 45 percent of the amount Silver Leaf received.[71]

---

[59] Tr. 488.

[60] Tr. 489.

[61] CX-182.

[62] CX-182, at 2.

[63] CX-182, at 2.

[64] Ans. ¶ 21; CX-16; JX-3, at 1.

[65] JX-4. Chapler's testimony confirmed that "S" referred to SH. Tr. 513. Here, we use the letter "S" to represent the actual name appearing on the payout calculation.

[66] CX-63, at 1.

[67] CX-62, at 4.

[68] CX-65, at 1–2; JX-6, at 1; Stip. ¶ 16; Ans. ¶ 25.

[69] CX-62, at 1; CX-63, at 1.

[70] CX-62, at 4.

[71] As the FINRA examiner testified, Silver Leaf at that time had a 90 percent override, "[s]o 50 percent of that 90 percent would be 45 percent of the commission due to Silver Leaf." Tr. 1617–18.

3. The July 11, 2013 Payment

On or about June 4, 2013, LE signed a loan agreement with BHP under which LE agreed to transfer shares of Lateck Holding AS ("LTHOL") to BHP[72] in exchange for a cash loan to be funded in multiple tranches.[73] Silver Leaf's fee under the agreement was 1.95 percent of the gross loan amount.[74] SH brought the deal to Silver Leaf.[75]

On July 5, 2013, BHP paid Silver Leaf $21,162.18 in transaction-based compensation under the first tranche of the LTHOL stock loan.[76] This fee was 3.95 percent (the 1.95 percent origination fee plus a 2 percent back-end fee)[77] of the gross loan amount.[78] That day, Khan, Meehan, Chapler, and SH exchanged emails relating to the fee split with SH. According to Khan, he received an email from Meehan on July 5, 2013, indicating that Silver Leaf had received a fee payment from BHP for a transaction in which Chapler had played a role.[79] On July 5, Khan also saw an email of the same date indicating that a fee would be split on the transaction between Chapler and SH.[80] Also on July 5, SH sent Chapler an email detailing the fee split.[81] Khan saw SH's email and forwarded it to Meehan later that day.[82]

The email exchanges continued on July 8, 2013. Chapler sent Meehan an email attaching a spreadsheet, copying Khan. The spreadsheet reflected fee payment splits with rows titled "Gross [S] & Jay Fee," "Fee to [S]," and "Wire to [S] (Including Turkey Broker's Fee) 10,380.18."[83] Later that day, after receiving Chapler's email, Meehan responded that it seemed

---

[72] BHP was identified in the agreement as the "SLP Arranged Funding Source." CX-96, at 1.

[73] CX-96, at 1. It is unclear whether CX-96 is the final version of the agreement, as it was not signed by BHP. Tr. 597, 599–600. Nevertheless, according to Chapler, "[i]t makes sense there was an agreement signed either this exact one or one similar to that but probably something was signed because [the transaction] was executed." Tr. 603.

[74] CX-96, at 3.

[75] Tr. 577.

[76] Stip. ¶ 17; JX-8.

[77] Chapler also negotiated an additional 2 percent back-end fee for Silver Leaf. Tr. 684–85.

[78] Stip. ¶ 17.

[79] CX-177, at 18, 21.

[80] CX-177, at 19, 24.

[81] JX-11.

[82] JX-10.

[83] JX-13. Khan testified that he probably read that email but "categorically" denied that he would have read the attached spreadsheet. Tr. 2435–36. He acknowledged, however, that had he read it, the references to fee splits and a wire to SH would have concerned him, and he would have contacted Meehan about it. Tr. 2436–38.

"straightforward to [him]."[84] Also on July 8, Khan received copies of email exchanges between Meehan and Chapler about facilitating Silver Leaf's payments to SH.[85]

On July 10, 2013, after receiving the $21,162.18 payment, Silver Leaf deducted its override of $2,812.70 and paid Chapler the remaining $18,349.49,[86] which was deposited into DEMC Capital's account that day.[87] The next day, July 11, 2013, Chapler shared his commission with SH[88] by wiring $10,380.18 from DEMC Capital to SH's firm, NAPI.[89]

* * *

Khan denied knowing about Silver Leaf's payments to SH[90] and maintained that he tried to prevent them. According to Khan and Meehan, on July 8, 2013, Khan told Meehan that because SH was not a Silver Leaf broker, Silver Leaf could not pay him.[91] Meehan and Khan claimed that the next day, July 9, Khan met with Meehan and Chapler, and Chapler told them that he and SH assumed Silver Leaf would pay SH.[92] Meehan and Khan testified that, in response, they told Chapler at that meeting that Silver Leaf could not pay SH.[93]

It is questionable that Khan and Meehan clearly told Chapler at that meeting that Silver Leaf could not pay SH. Khan did not memorialize what occurred at that meeting.[94] Moreover, neither Khan nor Meehan mentioned this version during the investigation that led to these

---

[84] CX-67.

[85] CX-177, at 19, 25–26; JX-12. One email sent by Meehan to Chapler and copied to Khan made it clear that Silver Leaf planned to pay SH directly. "We need to set [SH] up with our payroll company," the email began. "Can you please forward these forms to [SH] to complete and scan/email back to me along with a copy of a 'voided' check for direct deposit[?]" JX-12, at 1.

[86] Stip. ¶ 21; CX-68, at 1.

[87] CX-69, at 2; Tr. 663.

[88] Tr. 694–95.

[89] CX-69, at 6; *see also* SH's invoice requesting payment in that amount. CX-66, at 2.

[90] Tr. 1970–72, 1982–83, 2445–46.

[91] CX-177, at 19; Tr. 1968–69.

[92] Tr. 1969–70. Based on his discussions with Khan, Chapler maintained that, from the beginning, Khan was at least generally aware that SH would be paid. Tr. 467, 1161–62, 1167. We found this testimony credible. At times during the hearing, Chapler's testimony was rambling and evasive, and this undercut his credibility somewhat. But we detected no hostility from Chapler toward Silver Leaf. Nor did we discern a motive for him to shade his testimony to Silver Leaf's detriment. By the time of the hearing, his disciplinary issues with FINRA had already been resolved by an AWC. Moreover, Silver Leaf paid legal fees totaling $170,000 that Chapler incurred in connection with the BTIG arbitration (discussed below) in which he was a respondent. He now owes reimbursement to the Firm for that payment. Thus, given that sizeable debt, we found it unlikely Chapler would be inclined to create ill will with Silver Leaf. Tr. 1291–92, 1294.

[93] CX-177, at 2–3, 19–20; *see also* Tr. 223–25.

[94] Tr. 2017.

proceedings or during the Wells process.[95] For his part, Chapler was vague about whether Meehan or Khan directly told him that Silver Leaf could not pay SH because he was unregistered. Chapler testified that he only remembered general discussions on this subject, and not at the July 9 meeting in particular.[96]

Events following the meeting cast additional doubt on Khan and Meehan's recollection. As discussed below, just days after the meeting, Chapler emailed Meehan about proposed fee splits on the second tranche. The email reflected both the earlier payment to SH in connection with the first tranche and a proposed fee split on the second one. Six weeks later, Chapler and Khan exchanged emails discussing an escrow fee-splitting arrangement with SH relating to a stock loan transaction; the communications indicate that Khan decided the terms of the split between Chapler and SH. From this we conclude that Khan and Meehan either did not instruct Chapler on July 9, 2013, that the Firm could not pay SH, or that, shortly afterward, they decided to abandon the prohibition. In any event, the payments to SH continued.

4. The July 22, 2013 Payment

On July 17, 2013, six days after splitting fees with SH on the first tranche, Chapler emailed Meehan a spreadsheet with the payouts for the second tranche.[97] This spreadsheet still had a row labelled "Gross [S] & Jay Fee" and noted the prior $10,380.18 payment to SH, this time referring to him as "Jay2."[98]

---

[95] Tr. 1672–73. Once informed by FINRA staff in a Wells notice that the staff intends to recommend formal discipline, a potential respondent is given the opportunity during the Wells process "to submit a writing, called a Wells submission, which discusses the facts and applicable law and explains why formal charges are not appropriate." Regulatory Notice 09-17 at 3 (Mar. 2009), https://www.finra.org/sites/default/files/NoticeDocument/p118171.pdf (explaining FINRA's Wells process). While Khan and Enforcement counsel did not recall specifics, they generally recalled that Silver Leaf responded to the Wells notice. Tr. 2418–19.

[96] Tr. 645–47, 1167–68, 1313, 1315.

[97] CX-70.

[98] Tr. 674. Chapler was initially hesitant to say that Meehan knew the identity of Jay2. Tr. 675–79. Throughout his testimony, Chapler expressed discomfort when asked what others knew and tried to avoid answering such questions. *See, e.g.*, Tr. 1106–07. After much evasiveness, however, Chapler eventually said he assumed Meehan knew the identity of Jay2 because "he could read, I could read, we are both financial people. He is college educated." Tr. 682. For his part, Meehan said he did not recall asking Chapler why he was splitting the fee between Jay1 and Jay2, did not recall what Jay1 or Jay2 referred to, and did not recall asking Chapler if Jay2 was SH. Tr. 243–44, 251, 253, 255–56. Further, when asked directly if he had "any idea" of the identity of Jay2, Meehan replied that he just assumed Jay1 was Jay 2. Tr. 253. We did not find Meehan's testimony credible. Given his involvement in the transaction and receipt of emails and spreadsheets reflecting the fee splits, Meehan must have known that Jay2 (as well as S) was SH or recklessly disregarded that fact.

The next day, July 18, 2013, BHP paid Silver Leaf $33,648.18 in transaction-based compensation in connection with the second tranche of the LTHOL stock loan.[99] This fee was 3.95 percent (the 1.95 percent origination fee plus a 2 percent back-end fee) of the gross loan amount.[100] The same day, Chapler emailed Meehan a spreadsheet showing a payment due SH of $16,434.84, now labelling the payment "Wire to Jay2 (Including Expenses)."[101] From the $33,648.18 payment Silver Leaf received, Silver Leaf's override was $4,453.31, and Silver Leaf paid the remaining $29,052.56 to Chapler on July 19, 2013.[102] On July 22, 2013, Chapler, in turn, through DEMC Capital, wired $16,434.84 to SH's firm, NAPI.[103]

* * *

Even though Silver Leaf received payment for both tranches, the transactions did not go smoothly. Payment under the first tranche was delayed. And beginning in late June 2013, LE started complaining, accusing BHP of selling the shares to fund the loan, and threatening legal action. SH and Chapler knew about the situation,[104] as did Khan.[105] The second tranche fared no better. BHP was again late delivering payment to LE, and LTHOL's stock price declined.[106] Khan knew that LE was upset, leading him to have "concerns" about BHP and LE.[107] Chapler, too, had concerns about how BHP did business, testifying that BHP was "sloppy."[108] Still, as discussed below, Silver Leaf continued entering into transactions with BHP or a related entity.

---

[99] Stip. ¶ 22; JX-14, at 1. The Complaint alleged that the amount of the payment was $33,505.88—lower by $142.30. Compl. ¶ 34. The difference, according to Enforcement, was based on a bank wire and payroll fee deduction. Department of Enforcement's Post Hearing Brief at 9, n.76; CX-68, at 1.

[100] Stip. ¶ 22.

[101] CX-71. The spreadsheet also contained a "Gross [S] & Jay Fee" reference, and references to "Fee to Jay1" and "Fee to Jay2" and "Wire to Jay1." CX-71, at 2. Chapler insisted at the hearing that he did not know what he "was trying to accomplish by saying Jay one and Jay two." Tr. 690. But the only credible explanation is that Chapler was making a feeble attempt to shield SH's identity as a fee-split recipient.

[102] Stip. ¶ 23; CX-68, at 1.

[103] CX-69, at 6.

[104] Tr. 628–29. Several communications relating to this situation were on the Silver Leaf email system. CX-97; CX-98; CX-99.

[105] Tr. 2055–56.

[106] Tr. 806.

[107] Tr. 2058, 2061. When asked if Khan was aware of the problems connected with both tranches, Chapler gave a long, rambling, evasive answer to the effect that he likely told Khan about the problems because he did not hide problems that affected the Firm. "[O]dds are I spoke to him and odds are I told him about the problems," Chapler said. Tr. 696–98.

[108] Tr. 637, 668.

5. The August 26, 2013 Payment

On August 7, 2013, a BHP affiliate or subsidiary,[109] CFO, and IH entered into a non-recourse loan agreement, which included a related stock security delivery and re-delivery agreement.[110] Under the loan agreement, IH agreed to provide shares of UCAK to CFO in exchange for a $51.8 million loan and Silver Leaf would be paid an origination fee[111] of 3 percent of the gross share loan amount.[112] Silver Leaf would also receive other compensation,[113] including a fee for serving as escrow agent.[114] The agreement stated that the UCAK shares would be deposited into an escrow account and the loan would be funded in two disbursements.[115] SH brought this deal to Silver Leaf,[116] helped craft the escrow agreement's terms and conditions,[117] and would be paid for his efforts. By email dated August 14, 2013, Khan memorialized a fee split that included SH.[118]

On August 20, 2013, Chapler sent SH an email detailing the anticipated fee split that Chapler had calculated.[119] The fee split included fees for the Firm, Chapler, and SH.[120] This time the spreadsheet detailing fee splits did not reference Chapler and SH by name.[121] Instead, it referenced fees to "Broker 1" and "Broker 2." Chapler was "Broker 1" and SH was "Broker 2."[122] According to Chapler's interpretation of the spreadsheet, the chart broke out the payments due Silver Leaf into two payments by BHP: one to the Firm and Chapler, and one that included a payment to SH.[123] Later that same day, after sending the spreadsheet to SH, Chapler sent it to Meehan.[124] On August 21, 2013, Chapler emailed BHP, informing it of the commission amount

---

[109] Tr. 260, 701, 787.

[110] CX-73.

[111] CX-73, at 2; Tr. 820.

[112] CX-73, at 2.

[113] The additional compensation consisted of a separate 2 percent back-end fee Silver Leaf negotiated with BHP. CX-76, at 2; Tr. 820. It also included an escrow fee of 0.25 percent of the net loan amount because the Firm would serve as escrow agent. CX-76, at 2; Stip. ¶ 24.

[114] CX-72.

[115] CX-73, at 1, § 1.b.

[116] Tr. 811.

[117] Tr. 811.

[118] CX-74; CX-75.

[119] CX-78; Tr. 821–22.

[120] CX-78, at 2.

[121] CX-78, at 2.

[122] Tr. 821–22.

[123] CX-78; *see also* Tr. 826–27.

[124] CX-77.

and providing it with the following wiring instructions: BHP was to wire a portion of the Firm's commission to the Firm's account,[125] and the remainder to NAPI (designated on the email as "Wire 2").[126] On August 23, Chapler sent another payout sheet to Meehan setting forth the fee splits that included payouts to Broker 1 and Broker 2.[127]

Ultimately, the Firm was due $262,783.[128] But it did not receive that amount. Instead, on August 26, 2013, BHP wired Silver Leaf $142,296 in transaction-based compensation in connection with the first tranche of the UCAK stock loan,[129] and paid the remaining $120,487 to SH.[130]

* * *

Like the earlier loan transactions with BHP, this one was also plagued with problems, as Khan knew.[131] Silver Leaf received emails from the borrower complaining about the late payment of the loan proceeds, accusing the lender of selling the shares provided as collateral, and expressing concerns about involvement by the Capital Markets Board of Turkey, the regulatory and supervisory authority in charge of the securities markets in Turkey.[132] After payment for the first tranche on August 29, 2013, BHP made no more loan payments.[133]

---

[125] The wire to the Firm's account included Chapler's share. Tr. 842.

[126] CX-80; Tr. 842. Chapler explained why he asked BHP to make the payment to SH. He claimed that based on the expectation that SH would become registered, he understood it was permissible to make one or two "introductory type payments" to him. But by this point, Chapler said, it had become clear to him that SH would not get registered and he became concerned that future payments would be problematic for him and the Firm. Tr. 843–45, 1278, 1284. So, according to Chapler, he told BHP that since SH was not registered, BHP would have to make the payment. Tr. 852.

[127] CX-81.

[128] CX-20; CX-82, at 3.

[129] Stip. ¶ 25; JX-15; CX-82, at 3.

[130] Tr. 1640; CX-20; CX-82, at 5. While Meehan did not admit knowing that Chapler had directed BHP to pay SH a portion of the compensation due to Silver Leaf, it is likely he knew. On August 27, 2013, Chapler emailed Meehan a spreadsheet reflecting the payouts in the transaction. CX-82. The spreadsheet showed the payment to SH (designated as "Broker 2"), which was part of the total compensation due Silver Leaf. Also, Meehan used Chapler's spreadsheet to calculate the amounts due Silver Leaf for its overrides and the amount due Chapler for his payout. Tr. 280–81. Tellingly, when Meehan calculated the Firm's overrides, he based them on the amount due the Firm (namely, $262,783.00), not the amount the Firm actually received from BHP ($142,296.13). Thus, Meehan must have realized that SH's payment came out of the amount due Silver Leaf. Tr. 286–87, 289–90, 1641–42.

[131] *See, e.g.*, CX-105; CX-48; Tr. 888–908, 929–31.

[132] CX-48; CX-104; CX-105; Tr. 887–90.

[133] Tr. 900–01. Because of the problems in this transaction, the Firm decided to seek an indemnification agreement with BFP/CFO protecting the Firm for past and future transactions, and Khan provided a draft indemnification agreement for Chapler to use. Tr. 933; CX-50; CX-51. BHP never signed the indemnification agreement. Tr. 938–39. Even so, Silver Leaf continued to do business with BHP, as discussed above.

C. Silver Leaf's Transaction-Based Compensation Payments to Its Brokers' Non-Member Entities

In addition to Silver Leaf's transaction-based compensation payments to NAPI, Silver Leaf also paid transaction-based compensation to several unregistered, non-member entities owned by the Firm's brokers. We now turn to those payments.

For over a decade—2005 through 2015—Silver Leaf paid transaction-based compensation to unregistered, non-member entities owned by the Firm's hedge fund marketers.[134] This practice did not go unnoticed by the Securities and Exchange Commission ("SEC"). In 2012, an SEC examination of the Firm uncovered this activity. Following the exam, on March 26, 2012, SEC staff sent a letter to Khan containing "Examination Findings." The findings identified certain "deficiencies and weaknesses,"[135] including one entitled "Payments to Non-Registered Entities—NASD Conduct Rule 2420."[136] That finding stated that from April through September 2011, Silver Leaf had shared hedge fund marketing fee compensation with ten unregistered, non-FINRA member entities affiliated with the Firm's hedge fund marketers ("LLCs"). The compensation totaled over $224,000.[137] The letter requested that Silver Leaf respond to each of the findings and explain how the Firm intended to address them.[138]

In its September 13, 2012 response, Silver Leaf disagreed that its payments to the LLCs raised "any regulatory issues of any consequence." But the Firm "recognize[d] that the 'no-action' letter process is the only appropriate method to seek relief from the technical requirements of NASD Conduct Rule 2420." And it assured the SEC staff that "[p]ending the no-action relief process, [it would] immediately begin to convert [its] payables to individual representatives rather than the entities owned by them."[139] The Firm then stopped making these problematic payments to its hedge fund marketers' LLCs.[140]

Five months later, however, following "grumblings" from the Firm's brokers,[141] Silver Leaf resumed payments to LLCs.[142] And over the next two years and two months (February

[134] Tr. 123, 1856–57.

[135] CX-86, at 1.

[136] CX-86, at 3.

[137] CX-86, at 4.

[138] CX-86, at 1.

[139] JX-5, at 1.

[140] Tr. 1399.

[141] CX-132, at 1; *see also* Tr. 882.

[142] Tr. 1399. Silver Leaf made the payments to the LLCs' bank accounts. Tr. 149–50.

2013 through April 2015), Silver Leaf paid over $2.6 million to seven LLCs,[143] including Chapler's firm, DEMC Capital, as shown in the chart below:[144]

Registered Representative	Non-Registered Affiliated Entity	Compensation Payment Period	Total Compensation Paid
Michael Leverone	Leverone Capital Partners LLC	Feb. 2013–Feb. 2015 (Two years)	$24,619.67
Michael Fields	MSF Enterprises, LLC	Mar. 2013–Dec. 2014 (One year and nine months)	$176, 501.81
Jason Okie	Silver Q Partners, LLC	May 2013–Apr. 2015 (One year and 11 months)	$1,719,732.61
James Lawler	Newfield Advisors LLC	Sept. 2013–Apr. 2015 (One year and seven months)	$314,232.57
Christian Larsen	Climbing Tiger Consulting LLC	Oct. 2013 (One month)	$14,875.00
Jay Chapler	DEMC Capital LLC	Nov. 2013–Apr. 2015 (One year and five months)	$85,294.99
Jorge Corro	Nortesur Partners LLC	June 2014–Apr. 2015 (Ten months)	$339,379.99
		Total: **Two years and two months**	**Total:** **$2,674,636.64**

None of these LLCs were registered with FINRA.[145] Two of them—Newfield Advisors LLC and DEMC Capital—were among those unregistered entities identified in the SEC's examination findings as having received hedge fund marketing compensation from Silver Leaf.[146] Despite telling the SEC staff that it would not resume paying the LLCs unless it obtained no-action relief from the SEC, Silver Leaf resumed the payments without doing so.[147]

[143] CX-22. The Complaint alleged, but the evidence did not show, that Silver Leaf made payments totaling $2,719,407.27 to eight LLCs. Compl. ¶ 48.

[144] CX-22.

[145] Tr. 162.

[146] CX-86, at 7–8.

[147] Ans. ¶ 46; Tr. 2346–47. Nor did the Firm consult with outside counsel, review SEC no-action letters or FINRA settlements, or speak to anyone at the SEC or with the Firm's regulatory coordinator about the propriety of resuming the payments. Tr. 163, 1894–96. Meehan also had no recollection of the Firm ever seeking a no-action letter from FINRA. Tr. 343.

Indeed, it expanded the payments to include additional LLCs beyond those identified in the SEC exam.

Meehan explained how the Firm came to resume payments. After receiving the SEC exam findings, the Firm began converting Forms W-9 (Request for Taxpayer Identification Number and Certification) ("W-9s")[148] from the names of the LLCs to the names of the individual brokers who owned them.[149] Meehan testified that this structure was the way the Firm's outside payroll processing firm "wanted it to be done."[150] The payroll processor also wanted letters showing that individuals solely owned the LLCs' bank accounts, Meehan recalled.[151] In short, according to Meehan, converting the W-9s meant that Silver Leaf was paying the individuals.[152] "[W]e thought we were satisfying the [SEC's] directive by changing all the W-9s," he explained.[153] That said, Meehan testified he did not recall why the Firm concluded that it was not "violating the spirit of what was being told to us [by the SEC staff]."[154]

At the hearing, Khan provided his recollection about the resumption of payments to the LLCs. Khan testified that he decided to re-commence payments based on a conversation with Meehan without fully appreciating that the Firm would be making direct deposits into the LLCs' bank accounts or considering whether the new payment practice satisfied the requirements of NASD Rule 2420.[155] Khan went on to say he understood from that conversation that if the brokers completed the W-9s, then Silver Leaf's books would reflect that it was paying the individual brokers, so he approved it.[156] "The fact of where as a technical matter it ends up, is not something I really thought about," Khan said, adding, "There was no deep thought put into it."[157] In sum, he claimed that this approach dealt appropriately with the concerns raised by the SEC because the Firm's records reflected that Silver Leaf was paying the individuals.[158] Thus, it was unnecessary to seek a no-action letter, he concluded.[159]

---

[148] RX-22.

[149] Tr. 137–38. For the most part, the third-party marketers were independent contractors, according to Meehan. Tr. 314. Those who were independent contractors completed the W-9s. Tr. 314.

[150] Tr. 148.

[151] Tr. 150–51.

[152] Tr. 148–49. One of the LLCs, Nortesur Partners, was not wholly owned by a Silver Leaf broker. That broker's wife held a 10 percent interest in that entity. CX-122; Tr. 2235–36.

[153] Tr. 139.

[154] Tr. 139. *See also* Tr. 141–43.

[155] Tr. 1883–87, 1891–93.

[156] Tr. 1883–85.

[157] Tr. 1885–86.

[158] Tr. 1886, 1891.

[159] Tr. 1892.

D. Silver Leaf's Supervision of Its Stock Lending and Block Trading Business

We begin our examination of Silver Leaf's supervision of its stock lending and block trading business with its written supervisory procedures ("WSPs").[160] Khan approved the WSPs;[161] was responsible for reviewing and updating them; and was responsible for developing and implementing the Firm's policies.[162] The WSPs specified Meehan and Khan's supervisory responsibilities.[163] Meehan was responsible for, among other things, supervising Khan.[164] Khan's responsibilities included supervising the registered representatives and associated persons; reviewing and approving transactions; and approving outgoing and incoming correspondence.[165] He was responsible for supervising Chapler and Meehan, among others.[166] As Khan described it, he was responsible for supervising "the entire business."[167]

That "entire business" included the stock loan and block trade activities that Chapler conducted—activities that Khan viewed as "risky."[168] Elaborating on his risk assessment, Khan said that from a supervision point of view, he was most concerned about ensuring that (1) the registered representatives contacted the "appropriate parties," limiting themselves to "the right set of people to contact"; (2) they provided "correct and appropriate information to those parties"; and (3) once they made the "match" and facilitated the transaction, that they looked "for an exit as quickly as possible."[169]

Before September 2012, Khan had never supervised stock loan introductions.[170] Notwithstanding his lack of experience, as well as the risks inherent in the stock loan and block trade business lines, Khan demonstrated a lax attitude toward supervision. "I focused on bringing the business in," Khan said. "[A]s long as we made payments, I didn't really pay attention. It was

---

[160] The FINRA examiner characterized the manual as "an off the shelf compliance manual," adding, "It relates more directly to a retail business as opposed to the institutional business that the firm does and described to me that they do." These procedures, according to the examiner, were "not tailored to the business that the firm described that they were doing …." Tr. 1647–48. Khan said that the WSPs began with an "off the shelf" set of procedures. Tr. 2142.

[161] JX-19, at 84. The WSPs were titled "Broker-Dealer Compliance Manual and Written Supervisory Procedures." JX-19, at 1. Two versions were admitted into evidence. One was dated November 1, 2012 (amended on December 10, 2014). JX-19, at 1. And the other was dated March 28, 2011 (amended on November 1, 2012). CX-152, at 1.

[162] JX-19, at 86; CX-152, at 87.

[163] JX-19, at 85–89; CX-152, at 86–90.

[164] JX-19, at 90; CX-152, at 90.

[165] JX-19, at 86; CX-152, at 87.

[166] JX-19, at 87; CX-152, at 88; Tr. 401.

[167] Tr. 1819.

[168] CX-26; Tr. 168–69, 1959; *see also* Tr. 344–45, 472–73.

[169] Tr. 2427–28.

[170] Tr. 2031.

just the way I chose to run the business. I focus on dealing with the people, [Meehan] focuse[d] on the money during this time period."[171]

Both the WSPs and Khan's supervision methods reflected this laxity. The WSPs contained only one sentence addressing compensation payments to persons or entities not registered with the Firm. Under a section titled "Prohibited Practices," the WSPs prohibited "Registered Reps (and Principals handling customer accounts)" from "[c]ompensating any person, firm, or entity other than a registered representative of [Silver Leaf] for any services rendered in connection with the sale of a security to a customer without express written advance approval of an authorized Principal."[172] The WSPs included no provisions governing (or prohibiting) payments to brokers' unregistered entities.[173] Nor did the WSPs address the Firm's business of facilitating stock loans or block trades,[174] or paying finder's fees.[175] In short, the procedures did not address how the Firm's supervisors should ensure that stock loan and block trading-related activities were conducted in compliance with FINRA rules or the federal securities laws.

While Khan testified that email review was part of his supervisory responsibilities,[176] the WSPs did not contain procedures for how he should conduct those reviews. Khan explained his approach to email review. According to Khan, he reviewed emails at least three times per week, sometimes daily.[177] He did not use software to assist him.[178] Instead, among other things, he used search terms, looked at the subject lines, and sometimes selected emails to review based on the status of different transactions.[179] Khan did not memorialize his email reviews.[180]

---

[171] Tr. 1847.

[172] JX-19, at 19, § 4.2, no. 16; CX-152, at 19, § 4.2, no. 16.

[173] Tr. 1664.

[174] Tr. 1648–49, 1664. The Firm also used various training materials and a compliance questionnaire. *See, e.g.*, RX-16; RX-17; RX-19; RX-20; RX-23. But for the most part, these materials were not specifically tailored to the stock lending and block trading activities at issue in this proceeding. For example, the December 2014 Silver Leaf Partners Firm Element Training (used since 2010) merely reiterates the prohibition contained in the WSPs against compensating anyone who is not a registered representative of the Firm for services rendered in connection with the sale of a security to a customer without approval from an authorized principal. RX-20, at 11; Tr. 1334–35. And, to the extent the Firm Element Training materials addressed "Investment Banking and Corporate Advisory" activities, the treatment was cursory. *See, e.g.*, RX-20, at 5.

[175] Tr. 1648–49.

[176] Tr. 1950.

[177] Tr. 1951.

[178] Tr. 1950.

[179] Tr. 1951–53.

[180] Tr. 1954.

Khan's email review was inadequate. For example, if he "saw Mr. Meehan's name in the to line or the from line," Khan said, "[he] skipped past it."[181] His review also failed to identify numerous emails between Chapler and Meehan containing red flags indicating that the Firm was splitting fees with an unregistered finder's unregistered, non-member entity, and that Chapler was trying to disguise the identity of fee-split recipients. These emails included attachments referencing fee splits with "S," "Jay1," "Jay2," "Broker 1," and "Broker 2."[182] These red flags required follow-up to determine the identity of the persons receiving payouts in connection with Firm transactions. Khan's email review also failed to uncover SH's email to Chapler attaching the signed fee-splitting agreement between SH and DEMC Capital.[183] Even minimal follow-up would have revealed that the Firm was paying transaction-based compensation to SH.

Moreover, when Khan did see emails indicating fee splitting, he failed to take appropriate action in response to determine whether it was permissible. As discussed above, Khan said he met with Meehan and Chapler on July 9, 2013, to tell them in no uncertain terms that the Firm could not, and would not, split fees with SH. But, Khan admitted, he did not follow-up to confirm that Chapler had abided by this purported instruction,[184] such as engaging in a heightened review of Chapler and Meehan's emails. Worse, Khan not only failed to follow up on indications of fee splitting, but also facilitated the conduct when he memorialized a fee split that included SH in connection with the escrow agreement for the CFO/IH stock loan.

Khan also adopted an unreasonably loose approach to supervising Chapler, given the nature of Chapler's activities and the risk the stock loan and block trade business posed to the Firm. According to Chapler, the working environment was "very open." Khan, he said, initially gave them considerable latitude in sourcing deals, leaving Chapler to work without day-to-day oversight. But when it was time for the Firm to enter into a transaction, he would bring it to Khan's attention. At that point, Khan would become involved and would perform his due diligence and make sure the deal was appropriate for the Firm.[185] That said, Chapler pointed to no other supervision that Khan performed in connection with Chapler's risky activities.

Finally, the substantial risks associated with the Firm's stock loan and block trade business lines called for robust supervision. This was especially true for transactions involving BHP, given the problems associated with those transactions, as discussed above. As a result, the Firm should have been wary of entering into any more deals with BHP, or, at a minimum, Silver Leaf should have enhanced its supervision of them. It failed to do so, however, and entered into another block trade involving BHP—a transaction that nearly led to the Firm's demise.

---

[181] Tr. 2020–21.

[182] *See, e.g.*, CX-70; Tr. 1992; CX-71; Tr. 1994–95; CX-79; Tr. 2019–20; CX-81; Tr. 2022–23; CX-77; Tr. 2020–22; CX-82; Tr. 2023–24; JX-4; Tr. 1960–61.

[183] Tr. 1954–55.

[184] Tr. 1967.

[185] Tr. 401–02, 1310–12.

In mid-October 2013, BHP asked Silver Leaf to find a buyer for its large block of GAMA shares.[186] Silver Leaf introduced BHP to a potential buyer, FA,[187] which, according to Khan, was a stock lending and block trading firm.[188] Mark Valentine, a BHP associate,[189] was the trader for this transaction.[190] Because of Valentine's role at BHP, Meehan viewed him as an important customer of Silver Leaf.[191] And Chapler interacted with him "pretty consistently" in connection with the GAMA trade.[192] Meehan claimed not to know, however, that Valentine had pleaded guilty to federal securities fraud violations in 2004 and that, based on that plea, the SEC had barred him from participating in penny stock offerings.[193] Chapler, too, said he was unaware that Valentine had been convicted of securities fraud[194] and conceded he should have investigated Valentine's background.[195] A basic search of publicly available information would have revealed Valentine's criminal and SEC disciplinary history.[196]

Likewise, Jacques Tizabi, an FA representative and Silver Leaf's main contact on the trade,[197] had regulatory problems; NASD (FINRA's predecessor) had barred him in 2005 for failing to respond to an NASD information request.[198] Chapler testified he was unaware that NASD had barred Tizabi. In fact, Chapler said, he knew nothing about Tizabi's background.[199]

Although the Firm spoke with BHP about potentially executing the transaction,[200] BHP executed the trade through another broker, BTIG LLC ("BTIG").[201] After BTIG bought $18 million worth of GAMA shares from BHP, FA refused to pay for the shares.[202] BTIG ended up

---

[186] Tr. 939–40. According to Chapler, GAMA was an Indonesian company listed on the Indonesia Stock Exchange. Tr. 953–54.

[187] Tr. 418–19, 941–42.

[188] Tr. 2369.

[189] Tr. 205.

[190] Tr. 957.

[191] CX-110; Tr. 205.

[192] Tr. 957.

[193] CX-108; CX-109; Meehan claimed that he was familiar with Valentine's background and had performed a background check on him but could not recall the details. Tr. 206–08.

[194] Tr. 959–60. The record does not reflect whether Khan was aware of Valentine's criminal and regulatory record.

[195] Tr. 1299–1302.

[196] CX-107; Tr. 1534–35.

[197] Tr. 948–49.

[198] CX-14A, at 10–11.

[199] Tr. 962. The record is silent as to whether Meehan and Khan knew about Tizabi's disciplinary history.

[200] Tr. 947.

[201] Tr. 947–48.

[202] Tr. 972.

holding the shares in its own account, and their value dropped.[203] Yet again, Silver Leaf found itself embroiled in a contentious dispute between BHP and a counterparty.[204] This time, however, Silver Leaf was directly drawn into the dispute.

In April 2014, BTIG filed a FINRA arbitration against several parties, including Silver Leaf, for damages from the failed transaction.[205] A FINRA Dispute Resolution arbitration award dated December 27, 2016, found Silver Leaf, among other respondents, jointly and severally liable for damages of $20,024,772. The award nearly put the Firm out of business before it settled the matter for less.[206] BTIG has not recovered all of its losses.[207] But even after this problematic transaction, Silver Leaf still sought to engage in further transactions with BHP and SH.[208]

III. Conclusions of Law

A. Silver Leaf Violated NASD Rule 2420 and FINRA Rule 2010 by Paying Transaction-Based Compensation to Non-Member Entities

The Complaint charged Silver Leaf with paying transaction-based compensation to non-member entities, in violation of NASD Rule 2420 and FINRA Rule 2010. NASD Rule 2420, which was in effect at all relevant times,[209] prohibited members from dealing "with any non-member broker or dealer except at the same prices, for the same commissions or fees, and on the same terms and conditions as are by such member accorded to the general public."[210] More specifically, the Rule prohibited a member firm from allowing or granting to non-member brokers or dealers "any selling concession, discount or other allowance allowed by such member to a member of a registered securities association and not allowed to a member of the general public."[211]

---

[203] Tr. 972–74.

[204] JX-20, at ¶¶ 96, 98; Tr. 973–77, 2372–73.

[205] Ans. ¶ 77.

[206] JX-23; Ans. ¶ 78.

[207] JX-27; Tr. 2321–23, 2358. This arbitration triggered the FINRA investigation that led to the filing of this disciplinary action. Tr. 1361–63.

[208] CX-54; CX-55; CX-57; CX-58; CX-59; CX-60; CX-172; Tr. 991–93, 2135.

[209] NASD Rule 2420 was superseded by FINRA Rule 2040, effective August 24, 2015. *See* Securities Exchange Act Release No. 34-73954, 2014 SEC LEXIS 5051 (Dec. 30, 2014); FINRA Regulatory Notice 15-07 (Mar. 2015), http://www.finra.org/industry/notices/15-07.

[210] NASD Rule 2420(a).

[211] NASD Rule 2420(b)(1). This prohibition, according to the SEC, is "directed to the member firm making improper payments and to the persons associated with that member who are responsible for making those payments." *Dep't of Enforcement v. Walker*, No. C10970141, 2000 NASD Discip. LEXIS 2, at *25 (NAC Apr. 20, 2000) (citing *Lawrence W. Legel*, 51 S.E.C. 589, 591 (1993)).

Rule 2420 defined "non-member or dealer" as a broker or dealer that uses the mail or "any means or instrumentality of interstate commerce to effect any transaction in, or to induce the purchase or sale of, any security, otherwise than on a national securities exchange, who is not a member of any securities association registered with the" SEC under Section 15A of the Securities Exchange Act of 1934.[212] Under FINRA's By-Laws, a broker is a person (other than a bank) "engaged in the business of effecting transactions in securities for the account of others."[213] According to FINRA's National Adjudicatory Council ("NAC"), NASD Rule 2420 complements the federal regulatory framework governing the registration of brokers and dealers "by prohibiting FINRA members from paying any commissions or fees derived from securities transactions to any non-member that may be acting as an unregistered broker-dealer."[214] The Rule also prohibits a member firm from making indirect payments to a non-member.[215]

In determining whether a non-member may be acting as an unregistered broker-dealer, the NAC has looked to SEC authority. "The Commission has identified a number of factors as relevant to the determination of whether a person is acting in a capacity requiring registration as a broker-dealer pursuant to Exchange Act Section 15(a)(1)," the NAC observed.[216] In particular, according to the NAC, the SEC "considers whether the person (1) actively solicited investors; (2) advised investors as to the merits of an investment; (3) acted with a certain regularity of participation in securities transactions; and (4) received commissions or transaction-based

---

[212] NASD Rule 2420(d). The Rule excepts from this definition "a broker or dealer who deals exclusively in commercial paper, bankers' acceptances or commercial bills." *Id.* This exception is not relevant here.

[213] FINRA By-Laws Article I(e).

[214] *Continuance in Membership Application of Firm A*, No. 20100226181, 2011 FINRA Discip. LEXIS 19, at *16–17 (NAC Apr. 15, 2011) (affirming FINRA's Department of Market Regulation's denial of a member firm's application to change ownership and control) (citing FINRA Regulatory Notice 09-69 (Dec. 2009), http://www.finra.org/industry/notices/09-69); Interpretive Letter to Jay Adams Knight, Esq., Musick, Peeler & Garrett LLP (Mar. 2001) ("NASD Rule 2420 generally prohibits payment of fees and commissions to nonmember broker/dealers. This rule has been interpreted by NASD Regulation to prohibit such payments to entities that operate (or based on the proposed activities, would operate) as unregistered broker/dealers.").

[215] *See* NASD Notice to Members 05-18 (Mar. 2005), http://www.finra.org/industry/notices/05-18 ("A member also may not evade Rule 2420 through indirect payments.").

[216] *Continuance in Membership Application of Firm A*, 2011 FINRA Discip. LEXIS 19, at *14 (citing *Joseph Kemprowski*, Exchange Act Release No. 35058, 1994 SEC LEXIS 3743, at *5 (Dec. 8, 1994). Under Exchange Act Section 15(a)(1), 15 U.S.C. § 78o(a)(1), which governs the registration of brokers and dealers, "[a]bsent an exception or exemption, a broker-dealer that 'effect[s] any transactions in, or … induce[s] or attempt[s] to induce the purchase or sale of any security' must register with the SEC.'" A "broker" is "any person engaged in the business of effecting transactions in securities for the account of others." 15 U.S.C. § 78c(a)(4)(A). A "dealer" is "any person engaged in the business of buying and selling securities for such person's own account through a broker or otherwise." 15 U.S.C. § 78c(a)(5)(A). The NAC noted that its "use of 'person,' similar to the Commission's use of the term, contemplates not only a 'natural person,' but also a 'company, government, or political subdivision, agency, or instrumentality of a government.'" 15 U.S.C. § 78c(a)(9). *Continuance in Membership Application of Firm A*, 2011 FINRA Discip. LEXIS 19, at *14 n.10.

remuneration."[217] The NAC noted that the SEC views this last factor as the "hallmark of broker-dealer activity"[218] and thus typically requires "any person receiving transaction-based compensation in connection with another person's purchase or sale of securities" to "register as a broker-dealer."[219] NAPI and the LLCs received transaction-based compensation from Silver Leaf, a FINRA member broker-dealer, and "acted with a certain regularity of participation in securities transactions." Accordingly, we conclude these entities may have been acting as broker-dealers.

Silver Leaf did not dispute that these entities were non-FINRA members, unregistered with the SEC as broker-dealers. The Firm argued, however, that they were exempt from SEC registration based on the United States Supreme Court decision in *Morrison v. National Australia Bank Ltd.*[220] There, the Supreme Court held that the Securities Exchange Act had no extraterritorial application and concluded that no civil suit under Section 10(b) could be sustained unless it were predicated on a transaction involving (1) a security listed on a domestic exchange, or (2) a domestic purchase or sale of another security.[221] Silver Leaf maintained that the transactions giving rise to the commission payments do not meet this test and therefore the improper payments charge should be dismissed.

We reject Silver Leaf's *Morrison*-based argument. *Morrison* dealt with Section 10(b), the federal antifraud section, not Section 15(a), the federal broker-dealer registration provision. Thus, "[i]t is unclear … how the holding in [*Morrison*] might be extended to the broker-dealer registration context, although some courts have found that *Morrison* narrows the scope of broker-dealer registration requirements to apply only to domestic transactions."[222] Also, neither the Supreme Court, federal appellate courts, the SEC, nor FINRA has addressed whether

---

[217] *Continuance in Membership Application of Firm A*, 2011 FINRA Discip. LEXIS 19, at *14 (citing *Kemprowski*, 1994 SEC LEXIS 3743, at *5).

[218] *Id*. at *15 (citing *Brumberg, Mackey & Wall, P.L.C*, 2010 SEC No-Act. LEXIS 406, at *2 (May 17, 2010)).

[219] *Id.* at *15–16 (citing *Brumberg*, 2010 SEC No-Act. LEXIS 406, at *2); *1st Global, Inc*., 2001 SEC No-Act. LEXIS 557, at *5–6 (May 7, 2001) ("Absent an exemption, an entity that receives commissions or other transaction-related compensation in connection with securities-based activities that fall within the definition of 'broker' or 'dealer' … generally is required to register as a broker-dealer.").

[220] 561 U.S. 247 (2010).

[221] *Morrison*, 561 U.S. at 267.

[222] Robert Colby, Lanny Schwartz, & Zachary Zweihorn, Broker Dealer Regulation, § 2:7.2 at 2-103–2-104, https://www.davispolk.com/files/whats_a_broker_dealer_2.pdf (citing *SEC v. Benger*, 934 F. Supp. 2d 1008 (N.D. Ill. 2013) (holding that *Morrison* precluded the SEC from bringing an action against a person for failure to register as a broker-dealer where the person conducted brokerage activity from within the United States, but the transactions were to occur outside the United States and involved non-U.S. securities) and *SEC v. Battoo*, 158 F. Supp. 3d 676 (N.D. Ill. 2016) (finding broker-dealer registration requirements applied because, under *Morrison*, at least some investors incurred irrevocable liability within the United States)).

Morrison exempts brokers from registration or how, if at all, it impacts NASD Rule 2420 or its successor rule.[223]

Moreover, Silver Leaf offered no evidence that the SEC considered the entities exempt from registration. This omission is critical. As FINRA explained in its SEC rule filing seeking adoption of the successor to NASD Rule 2420, "FINRA generally has interpreted the provisions of the NASD Non-Member Rules, through interpretive letters and other guidance, to prohibit the payment of commissions or fees derived from a securities transaction to any non-member that may be acting as an unregistered broker-dealer."[224] But, the rule filing continued, "FINRA has refrained from providing interpretive guidance on whether a person is acting as an unregistered broker-dealer, as the authority to interpret Section 15(a) of the Exchange Act rests with the SEC."[225] Thus, when issuing interpretive guidance under NASD Rule 2420, the staff has not considered "it appropriate to conclude that a particular arrangement would not violate Rule 2420 unless the non-member entity has obtained a no-action letter from the SEC staff indicating that the entity is not required to register as a broker/dealer."[226] Neither Silver Leaf, NAPI, nor the LLCs obtained no-action letters from the SEC advising that NAPI or the LLCs were not required to register as broker-dealers.

Finally, as to the allegedly violative payments to SH, they related to domestic securities transactions, even under *Morrison*. "[A] transaction involving securities is a 'domestic

---

[223] Complicating matters further, after the Supreme Court decided *Morrison*, Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act, which amended the federal antifraud provisions to enable the SEC to commence civil actions extraterritorially in certain cases. Pub. L. No. 111-203, § 929P(b), 124 Stat. 1376, 1864-65 (2010) (codified at 15 U.S.C. §§ 77v, 78aa, 80b-14); *SEC. v. Gruss*, 2012 U.S. Dist. LEXIS 114007, at *8 (S.D.N.Y. Aug. 13, 2012). Whether that amendment superseded *Morrison* is another issue that the courts have not yet conclusively resolved. *See, e.g., United States v. Vasquez*, 899 F.3d 363, 373 (5th Cir. 2018) (stating that Dodd-Frank "superseded" *Morrison*); *SEC v. Tourre*, 2013 U.S. Dist. LEXIS 78297, at *1 n.4 (S.D.N.Y. June 4, 2013) (holding that the Dodd-Frank Act "effectively reversed *Morrison* in the context of SEC enforcement actions"); *see generally SEC v. A Chi. Convention Ctr., LLC*, 961 F. Supp. 2d 905, 910 n.1 (N.D. Ill., E. Div. 2013) (collecting cases in which "[s]ome courts have, in dicta, assumed, without analysis, that Section 929P(b) superseded *Morrison*"). *But see SEC v. Battoo*, 158 F. Supp. 3d 676, 692 n.12 (N.D. Ill., E. Div. 2016) (noting that according to the SEC, "some courts have expressed doubt that Section 929(b) overruled *Morrison*"); *SEC v. Brown*, 2015 U.S. Dist. LEXIS 25787, at *17 (N.D. Ill. Mar. 4, 2015) ("[C]onstruing the Dodd-Frank Act to supersede *Morrison* may be problematic."); Robert Colby, et al, Broker Dealer Regulation, § 2:7.2 at 2-104 n.435 (observing that "[c]ommentators and courts have … questioned whether the Dodd-Frank amendments actually supersede *Morrison*").

[224] SR-FINRA-2014-037 at 7 (Sept. 10, 2014), http://www.finra.org/industry/rule-filings/sr-finra-2014-037.

[225] *Id*. at 7–8. Interpretive Letter to Jay Adams Knight, Esq., Musick, Peeler & Garrett LLP (Mar. 8, 2001), http://www.finra.org/industry/interpretive-letters/march-8-2001-1200am (Rule 2420 "has been interpreted by NASD Regulation to prohibit" payment of fees and commissions to non-member broker/dealers "that operate … as unregistered broker/dealers. The determination of whether an entity should be registered as a broker-dealer rests with the SEC.").

[226] Interpretive Letter to Jay Adams Knight, Esq. (Mar. 8, 2001). *See also* Interpretive Letter to Bob E. Lehman, Esq., Lehman & Eilen LLP (Aug. 7, 2001), http://www.finra.org/industry/interpretive-letters/august-7-2001-1200am-0.

transaction' under *Morrison* if irrevocable liability is incurred or title passes within the United States." [227] "'[I]rrevocable liability' attaches 'when the parties to the transaction are committed to one another,' or, 'in the classic contractual sense, there was a meeting of the minds of the parties.'"[228] "Thus, to determine whether the Exchange Act reaches a transaction not involving securities traded on a U.S. exchange, the relevant inquiry is 'the location of the securities *transaction*.'"[229] Additionally, "[t]hat location falls within the United States when a purchaser agrees 'to take and pay for a security' in the United States or when the seller agrees 'to deliver a security' in this country."[230] The two 2012 payments to SH upon which liability rests derive from the August 28, 2012 stock purchase agreement between IH and EFH. The agreement became binding upon the parties when it was "actually signed by Buyer."[231] Under the agreement, there were certain conditions to the Buyer's obligations. Among those conditions was that the Seller shall have delivered the securities to the Buyer, who was located in the United States.[232] Therefore, the transactions under that agreement were domestic.[233]

In its defense against the improper-payment allegations, Silver Leaf made several additional arguments unrelated to *Morrison*. We reject them as well. As for the payments to the LLCs, Silver Leaf claims, first, that it had a "good faith belief that its payroll practices were consistent with its discussions with the SEC, and securities rules and regulations."[234] Second, it asserts that it is blameless because FINRA and National Futures Association examiners never found any deficiencies in its payroll practices after the SEC's 2012 examination.[235] Third, it maintains that it informed the SEC staff that it disagreed with the SEC staff's exam finding and "[t]hat disagreement was not challenged by, or followed up on, by the SEC."[236] And fourth, Khan claimed, without corroboration, that FINRA and SEC representatives told him that it was permissible for the Firm to pay transaction-based compensation to unregistered entities owned by

---

[227] *Myun-Uk Choi v. Tower Research Capital LLC*, 890 F.3d 60, 66 (2d. Cir. 2018) (quoting *Absolute Activist Value Master Fund Ltd. v. Ficeto*, 677 F.3d 60, 67 (2d Cir. 2012)).

[228] *Id*. (quoting *Absolute Activist*, 677 F.3d at 68).

[229] *Schentag v. Nebgen*, 2018 U.S. Dist. LEXIS 104065, at *28 (S.D.N.Y. June 21, 2018) (quoting *City of Pontiac Policemen's and Firemen's Ret. Sys. v. UBS AG*, 752 F.3d 173, 180 (2d Cir. 2014)).

[230] *Id*. (quoting *Absolute Activist*, 677 F.3d at 68).

[231] CX-182, at 7.

[232] CX-182, at 4.

[233] *See Plumbers' Union Local No. 12 Pension Fund v. Swiss Reinsurance Co.*, 753 F. Supp. 2d 166, 177 (S.D.N.Y. 2010) (holding that a purchase of securities is "domestic" if the purchaser "incur[s] an irrevocable liability to take and pay for the stock" in the United States) (quoting *Blau v. Ogsbury*, 210 F.2d 426, 427 (2d Cir. 1954)); *Giunta v. Dingman*, 893 F.3d 73, 79 (2d. Cir. 2018) (citing *Absolute Activist*, 677 F.3d at 68–69) ("To determine whether irrevocable liability was incurred within the United States, courts look to the terms, timing, and place of the parties' contracting and liabilities thereunder.").

[234] Respondent's Brief ("Resp. Br.") at 21.

[235] Resp. Br. at 4.

[236] Resp. Br. at 5.

registered persons.[237] These arguments fail. They are an attempt by Silver Leaf to shift its compliance responsibilities to regulators, and both the SEC and the NAC have made it clear that a broker-dealer may not do so.[238]

Silver Leaf also defended its LLC payment practices as reasonable and beyond the intended reach of NASD Rule 2420.[239] To support this argument, the Firm pointed out that it required the brokers to own the LLCs and to complete W-9s establishing that they (the brokers) were the payees of record.[240] Further, according to the Firm, because its records reflected which brokers received the fee payments, it was not attempting to "end run the SEC."[241] Silver Leaf thus argues that, to the extent it violated NASD Rule 2420, any violations were "unintended, technical and trivial."[242]

Silver Leaf's arguments miss the mark. The SEC staff has made it clear that this type of payment arrangement is improper. In its publicly available Guide to Broker-Dealer Registration, the SEC's Division of Trading and Markets, citing no-action letters, stated that the law "does not permit unregistered entities to receive commission income on behalf of a registered representative. **For example, associated persons cannot set up a separate entity to receive commission checks**." Instead, the Guide continues, "[a]n unregistered entity that receives commission income in this situation must register as a broker-dealer."[243]

This guidance reflects the SEC staff's long-standing practice of declining "to give no-action assurances under Section 15(a) in situations involving Employee Owned Corporations."[244] In particular, the staff "consistently declined to grant no-action relief with respect to the practice of routing commissions or other transaction-related compensation directly from a broker-dealer to an unregistered entity established and controlled by the broker-dealer's registered

---

[237] Tr. 2408–13. Under further questioning, however, Khan conceded that after the Firm responded to the exam finding, neither FINRA nor the SEC told him these payments were permissible. Tr. 2454–56.

[238] *See, e.g.*, *Dep't of Enforcement v. Pellegrino*, No. C3B050012, 2008 FINRA Discip. LEXIS 10, at *50 n.34 (NAC Jan. 4, 2008) ("The SEC has 'repeatedly pointed out that a broker-dealer cannot shift its responsibility for compliance with applicable requirements' to regulators.") (quoting *Quest Capital Strategies, Inc*., 55 S.E.C. 362, 377–78 (2001)), *aff'd*, Exchange Act Release No. 59125, 2008 SEC LEXIS 2843 (Dec. 19, 2008).

[239] Resp. Br. at 4.

[240] Resp. Br. at 21–23.

[241] Resp. Br. at 6.

[242] Resp. Br. at 25.

[243] Guide to Broker-Dealer Registration, SEC Division of Trading & Markets at §II. D.1. (Apr. 2008) (modified Dec. 12, 2016) (emphasis in original), https://www.sec.gov/reportspubs/investor-publications/divisionsmarket regbdguidehtm .html.

[244] *ADP TotalSource, Inc*., 2007 SEC No-Act. LEXIS 669, at *2 n.2 (Dec. 4, 2007).

representatives."[245] The rationale for declining to grant these requests, according to the staff, is that

> the receipt of securities commissions or other transaction related compensation is a key factor in determining whether a person or an entity is acting as a broker-dealer. Absent an exemption, an entity that receives commissions or other transaction-related compensation in connection with securities-based activities that fall within the definition of "broker" or "dealer" contained in Sections 3(a)(4) and 3(a)(5), respectively, of the Exchange Act generally is required to register as a broker-dealer under Section 15 thereof. No exemption from broker-dealer registration exists for corporate entities formed by registered representatives of broker-dealers that receive securities commissions.[246]

That rationale applies here; therefore, we reject Silver Leaf's argument that its LLC payment practices were rule compliant.[247]

Turning next to the payments to SH, the Firm sought to avoid responsibility by casting itself as a victim of Chapler's purported treachery. Silver Leaf asserted that Chapler betrayed its trust[248] and described him as a "cunning"[249] "wolf in sheep's clothing"[250] "determined to 'switch sides'" from helping Silver Leaf to helping SH.[251] Silver Leaf also claimed it was "caught unawares by Mr. Chapler's deceit"[252] and that Chapler—not the Firm—dealt with SH and benefited from the relationship.[253] It also argued that Chapler "tricked" Khan and Meehan "into

---

[245] *BMH Inv. Group, LLC*, 1998 SEC No-Act. LEXIS 866, at *1 (Aug. 17, 1998) (and no-action letters cited therein). *See also Christopher J. Juall and Marc S. Wolff, Wolff Juall Invs., LLC*, 2005 SEC No-Act. LEXIS 617, at *3–4 (May 17, 2005).

[246] *BMH Inv.*, 1998 SEC No-Act. LEXIS 866, at *2.

[247] Silver Leaf also claimed that other firms engaged in the practice of paying registered persons' unregistered entities. Tr. 2414–15. Even if true—and Silver Leaf presented no evidence it was true—this is not a defense. *Dep't of Enforcement v. Bullock*, No. 2005003437102, 2011 FINRA Discip. LEXIS 14, at *58, n.27 (NAC May 6, 2011) ("[I]t is no defense that others in the industry may have been operating in a similarly illegal or improper manner.") (citing *Patricia H. Smith*, 52 S.E.C. 346, 348 n.8 (1995)).

[248] Resp. Br. at 7.

[249] Resp. Br. at 2.

[250] Resp. Br. at 7.

[251] Resp. Br. at 7.

[252] Resp. Br. at 30.

[253] Resp. Br. at 2, 6–10, 16, 19. Chapler denied hiding SH's involvement in the deals from Khan. "I think everyone at Silver Leaf knew [SH] was involved in these transactions," Chapler said. "He was the man on the ground working it. … I think everybody knew that I was not in Turkey." Tr. 530.

believing that his initial two unauthorized payments to [SH] were the result of an honest misunderstanding on his part."[254]

These blame-shifting protestations of innocence ring hollow and are unavailing.[255] As a threshold matter, based on his email communications with Chapler and his review of fee split schedules, Meehan must have known, from as early as the September 7, 2012 payment, that Silver Leaf was splitting fees with SH. Indeed, he helped facilitate the payments. At a minimum, he closed his eyes to Silver Leaf's fee splitting with SH as well as to Chapler's clumsy attempts to disguise SH's identity on the schedules. Khan, too, knew in advance about at least one fee split with SH because he memorialized an escrow-related fee split that included SH and resulted in the August 26, 2013 payment to him.[256]

But Silver Leaf's arguments suffer from a more fundamental flaw. The Firm's responsibility for the payments to SH—including the two 2012 payments upon which liability is based—is not limited by whether Meehan or Khan was aware them. "It is well established that a firm may be held accountable for the misconduct of its associated persons because it is through such persons that a firm acts."[257] More specifically, based on the doctrine of respondeat superior,[258] "wrongful acts of an employee undertaken within the scope of employment can be

---

[254] Resp. Br. at 8.

[255] *Cf., e.g.*, *Dep't of Enforcement v. Davidofsky*, No. 2008015934801, 2013 FINRA Discip. LEXIS 7, at *40 n.41 (NAC Apr. 26, 2013) (rejecting respondent's blame-shifting arguments). Indeed, these arguments show a lack of remorse and failure to accept responsibility that serve to aggravate sanctions, as discussed in the section on sanctions. *See Dep't of Enforcement v. Hedge Fund Capital Partners*, No. 2006004122402, 2012 FINRA Discip. LEXIS 42, at *42–43 (NAC May 1, 2012).

[256] Neither Khan nor Meehan dispute that Chapler told them at the July 9, 2013 meeting that he and SH were operating on the understanding that Silver Leaf would pay SH. There was no credible evidence that, after the meeting, Meehan and Khan reasonably came to believe that someone else was paying SH. Thus, leaving aside the evidence of their knowledge of Silver Leaf's fee splitting, this circumstance alone would have caused them to suspect that Silver Leaf, directly or indirectly, was continuing to split fees with SH.

[257] *vFinance Invs., Inc.*, Exchange Act Release No. 62448, 2010 SEC LEXIS 2216, at *36 & n.25 (July 2, 2010) (quoting *SIG Specialists, Inc.*, Exchange Act Release No. 51867, 2005 SEC LEXIS 1428 at *31 n.35 (June 17, 2005)).

[258] The NAC observed that the SEC has "long recognized the doctrine of respondeat superior in enforcement or disciplinary actions." *Dep't of Mkt. Regulation v. Yankee Fin. Group, Inc.*, No. CMS030182, 2006 NASD Discip. LEXIS 21, at *59 (NAC Aug. 4, 2006). Silver Leaf argued that Chapler was an independent contractor, not an employee, and that this undercuts its liability under that doctrine. Resp. Br. at 15–16. The NAC, however, has explicitly rejected this argument. *See Yankee Fin. Group, Inc.*, 2006 NASD Discip. LEXIS 21, at *64 (rejecting argument that respondents' representatives were "independent contractors" and that, therefore, it was not "responsible for their misconduct under respondeat superior principles," explaining: "The notion that a broker-dealer might escape responsibility for the actions of its registered representatives by virtue of such representatives' so-called status as 'independent contractors' is antithetical to the whole purpose of the broker-dealer registration and supervision requirements."); *see also vFinance Invs., Inc.*, 2010 SEC LEXIS 2216, at *30 (observing that the SEC has "long held the view that the designation of an independent contractor has no relevance for purposes of the securities laws") (internal quotations omitted).

imputed to the employer."[259] "An employee acts within the scope of employment when performing work assigned by the employer or engaging in a course of conduct subject to the employer's control."[260] By contrast, "[a]n employee's act is not within the scope of employment when it occurs within an independent course of conduct not intended by the employee to serve any purpose of the employer."[261]

Chapler—and in one instance, BHP, at Chapler's request—made or directed transaction-based compensation payments to SH's entity, NAPI. Khan conceded that these actions, which were performed under the Firm's control, were intended to, and did in fact, benefit Silver Leaf.[262] Thus, when making or directing the payments to NAPI, Chapler acted within the scope of his authority as head of investment banking and his actions are attributable to Silver Leaf. Therefore, acting through at least Chapler, Silver Leaf was responsible for the improper payments to SH's firm.

Finally, for its defense, Silver Leaf impugned FINRA's motives and competence in investigating and filing this disciplinary proceeding.[263] These arguments, however, are not a defense to liability. Decisions to initiate investigations and bring disciplinary proceedings "are exercises of FINRA's prosecutorial discretion. … Absent a showing of selective enforcement, the motives behind these decisions are irrelevant. To succeed on a claim of improper selective prosecution," Silver Leaf needed to establish that it "was singled out for discipline while others who were similarly situated were not, and that this action was motivated by arbitrary or unjust considerations such as race, religion, or the desire to prevent the exercise of a constitutionally-protected right."[264] Silver Leaf has not proven any of these elements.

* * *

[259] *SEC v. Sells*, No. C 11-4941 CW, 2012 U.S. Dist. LEXIS 112450, at *24 (N.D. Cal. Aug. 10, 2012) (concluding, for purposes of an SEC civil enforcement action for fraud, that an officer's "knowledge may be imputed to [his firm] by application of the doctrine of respondeat superior under which wrongful acts of an employee undertaken within the scope of employment can be imputed to the employer"); *see also Ahmed*, 2015 FINRA Discip. LEXIS 45, at *80 (affirming fraud finding against firm based on the intentional acts of the firm's owner and manager). While Meehan, an officer and owner of Silver Leaf, and Chapler, the head of investment banking, were, at a minimum, aware of the improper payments, we need not, and do not, address whether a showing of scienter is required to establish a violation of NASD Rule 2420.

[260] *Vanderwall v. Marriott*, Civil No. 2012-84, 2013 U.S. Dist. LEXIS 117764, at *35 (D.V.I. Aug. 20, 2013) (quoting Restatement (Third) of Agency § 2.04(2006)).

[261] *Id.* at *35–36.

[262] Tr. 2424–25.

[263] *See, e.g.*, Resp. Br. at 1–7, 13, 32.

[264] *Dep't of Enforcement v. Epstein*, No. C9B040098, 2007 FINRA Discip. LEXIS 18, at *78 (NAC Dec. 20, 2007) *aff'd*, Exchange Act Release No. 59328, 2009 SEC LEXIS 217 (Jan. 30, 2009), *aff'd*, 416 F. App'x 142 (3d Cir. 2010).

Because Silver Leaf made securities transaction-based compensation payments to non-member entities (NAPI and the LLCs) that may have been acting as unregistered broker-dealers, it violated NASD Rule 2420 and, by virtue of that violation, also violated FINRA Rule 2010.[265]

B. Silver Leaf Violated NASD Rule 3010 and FINRA Rules 3110 and 2010

"Assuring proper supervision is a critical component of broker-dealer operations," according to the SEC.[266] Indeed, "[p]roper supervision is the touchstone to ensuring that broker-dealer operations comply with the securities laws and [FINRA] rules."[267] To that end, FINRA Rule 3110 (a) requires member firms to "establish and maintain" a supervisory system "that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA Rules." Its predecessor, NASD Rule 3010(a), contained a similar requirement.[268]

"Whether supervision is 'reasonable' depends on the particular circumstances of each case."[269] When circumstances present red flags suggesting that misconduct may be occurring, then the duty of supervision includes an obligation to investigate and to "and to act upon the results of such investigation."[270] Moreover, "[s]upervisors must respond with the utmost vigilance when there is any indication of irregularity, and take decisive action when they are made aware of suspicious circumstances."[271] When a supervisor discovers red flags suggesting irregularities, the supervisor cannot "discharge his or her supervisory obligations simply by relying on the unverified representations of employees."[272]

FINRA Rule 3110(b)(1) requires member firms, as part of an appropriate supervisory system, to "establish, maintain and enforce written procedures to supervise the types of business

---

[265] *Geoffrey Ortiz*, Exchange Act Release No. 58416, 2008 SEC LEXIS 2401, at *23 (Aug. 22, 2008) (finding that a violation of any NASD rule constitutes a violation of the predecessor to FINRA Rule 2010).

[266] *Richard F. Kresge*, Exchange Act Release No. 55988, 2007 SEC LEXIS 1407, at *27 (June 29, 2007).

[267] *Dennis S. Kaminski*, Exchange Act Release No. 65347, 2011 SEC LEXIS 3225, at *35 (Sept. 16, 2011).

[268] FINRA Rule 3110 became effective on December 1, 2014, superseding NASD Rule 3010 without substantive change, although with some modifications not at issue here. FINRA Regulatory Notice 14-10 (Mar. 2014), http://www.finra.org/industry/notices/14-10. Thus, NASD Rule 3010 applies to Silver Leaf's conduct before December 1, 2014, and FINRA Rule 3110 applies to its conduct beginning on that date.

[269] *KCD Fin., Inc.*, Exchange Act Release No. 80340, 2017 SEC LEXIS 986, at *35 (Mar. 29, 2017).

[270] *Dep't of Enforcement v. Newport Coast Sec., Inc*., No. 2012030564701, 2018 FINRA Discip. LEXIS 14, at *167 (NAC May 23, 2018) (quoting *Michael T. Studer*, 57 S.E.C. 1011, 1023–24 (2004)), *appeal docketed*, No. 3-18555 (SEC June 22, 2018).

[271] *KCD Fin., Inc.*, 2017 SEC LEXIS 986, at *34–35.

[272] *Dep't of Enforcement v. VMR Capital Mkts.*, No. C02020055, 2004 NASD Discip. LEXIS 18, at *33 (NAC Dec. 2, 2004) (quoting *Michael H. Hume*, 52 S.E.C. 243, 248 (1995) (finding a failure to supervise where supervisor relied on the broker's unverified representations that excessive trading in a customer's account was consistent with customer's objectives)).

in which it engages and the activities of its associated persons." This Rule superseded NASD Rule 3010(b)(1), which was similarly worded. A firm's WSPs must be "reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules."[273] "Reasonably designed WSPs serve as a 'frontline' defense to protect investors from fraudulent trading practices and help to ensure that members are complying with rules designed to promote the transparency and integrity of the market."[274]

FINRA has provided guidance about provisions a firm's WSPs should contain. General reference materials are insufficient.[275] Instead, WSPs "must be tailored to the specific nature of the firm's business."[276] They also must require *specific* steps to resolve issues once detected.[277] But "[t]he presence of procedures alone is not enough. Without sufficient implementation, guidelines and strictures do not ensure compliance."[278]

Silver Leaf's supervision, including its WSPs, was inadequate and unreasonable. The WSPs were devoid of procedures addressing the supervision of its business of facilitating stock loans and block trades. They also lacked provisions aimed specifically at preventing Silver Leaf from paying transaction-based compensation to non-members. It was especially troublesome that the Firm failed to amend its WSPs to include these safeguards even after the SEC cited it for making improper payments and after the BHP transactions experienced problems.

In addition to having deficient WSPs, Silver Leaf failed to reasonably supervise its stock lending and block trade-related business lines, including failing to follow-up on red flags suggesting misconduct. As discussed above, Khan generally took a hands-off approach to supervision. Further, as part of his supervisory email review, Khan saw, or should have seen, emails indicating that Chapler was sharing, or intended to share, transaction based-compensation with an unregistered finder by making payments to the finder's non-member, unregistered entity. And Meehan, for his part, plainly saw such emails. While Khan (and not Meehan) was Chapler's supervisor, Meehan was also a supervisor at the Firm and a co-owner. The circumstances

---

[273] FINRA Rule 3110(b)(1).

[274] *Dep't of Enforcement v. North Woodward Fin. Corp*., No. 2011028502101, 2014 FINRA Discip. LEXIS 11, at *42 & n.95 (OHO May 16, 2014), *aff'd in relevant part*, 2016 FINRA Discip. LEXIS 35 (NAC July 19, 2016).

[275] *Dep't of Enforcement v. Respondent Firm*, No. C01040001, 2005 NASD Discip. LEXIS 47, at *24 (NAC Sept. 6, 2005).

[276] *Dep't of Enforcement v. Midas Sec., LLC*, No. 2005000075703, 2011 FINRA Discip. LEXIS 62, *20 (NAC Mar. 3, 2011), *aff'd*, Exchange Act Release No. 66200, 2012 SEC LEXIS 199 (Jan. 20, 2012). *Cf. Dep't of Enforcement v. Merrimac Corp. Sec., Inc.*, No. 2011027666902, 2017 FINRA Discip. LEXIS 16, at *36–41 (NAC May 26, 2017) (finding that the adoption of FINRA's small firm template with virtually no tailoring to a firm's business did not satisfy the firm's AML compliance obligations), *appeal docketed*, No. 3-18045 (SEC June 26, 2017).

[277] *See Merrimac*, 2017 FINRA Discip. LEXIS 16, at *35 (finding written supervisory procedures deficient in part because they provided "no specific guidance for what to do if red flags were identified").

[278] *KCD Fin., Inc.*, 2017 SEC LEXIS 986, at *34 (quoting *Rita H. Malm*, 52 S.E.C. 64, 69 n.17 (1994)) (internal quotation marks omitted).

demanded that both Khan and Meehan carefully investigate whether Silver Leaf was continuing to make improper payments and take appropriate action based on that investigation.

But they failed to do so. For example, Khan did not engage in a heightened review of Meehan's and Chapler's emails, which would have revealed evidence of continued fee splitting. Also, by no later than July 9, 2013, Khan knew that SH expected Silver Leaf to pay him for his services.[279] Even if Khan did tell Meehan and Chapler at that time that Silver Leaf could not pay SH—as Khan and Meehan claimed—he performed no follow up.[280] Moreover, six weeks after this purported conversation, Khan saw another red flag: Chapler sent Khan an email making it clear that SH expected to be paid, this time in connection with the Firm's escrow fee.

Khan's and Meehan's reactions to red flags of improper conduct was worse than inadequate. Not only did Khan fail to follow up and ensure that Silver Leaf did not pay SH, he also facilitated the wrongdoing by memorializing an escrow fee split with SH. And, to an even greater degree, as outlined above, Meehan facilitated improper payments to SH. This active participation in wrongdoing was an egregious breach of their supervisory responsibilities and an abdication of the proper exercise of supervisory authority.[281]

Additionally, it was unreasonable for the Firm to continue entering into transactions with BHP without heightened supervision or adequate due diligence in light of the complications resulting from the prior transactions with that entity. Doing so exposed Silver Leaf and market participants to serious risk. This risk was very real, as evidenced by the arbitration award that nearly put the Firm out of business.

Silver Leaf maintained, however, that its supervision was reasonable and that only one broker, Chapler, "act[ed] contrary to the requirements of that system."[282] Silver Leaf claims that it lacked access to Chapler's personal emails, text messages, and other indicia of his wrongdoing and thus cannot be blamed for not uncovering his wrongdoing at the time.[283] These arguments are contrary to the credible evidence and our findings. There were almost no applicable "requirements of the system" and the Firm not only had access to emails containing red flags of misconduct, but Meehan and Khan received and sent some of them.

---

[279] *See, e.g.*, CX-177, at 19.

[280] As noted above, there was no evidence that the counterparties to stock loan and block trading transactions (or anyone else) would be paying SH. The absence of such evidence should have been a red flag to Khan and Meehan that Silver Leaf might well be paying SH, contrary to Khan's purported instruction at the July 9, 2013 meeting.

[281] *John Montelbano*, Exchange Act Release No. 47227, 2003 SEC LEXIS 153, at *29 (Jan. 22, 2003) ("Where, as here, a supervisor, whose duty it is to prevent misconduct by subordinates, actually fosters and encourages that misconduct, it constitutes an egregious breach of that responsibility, an abdication of the proper exercise of supervisory authority.").

[282] Resp. Br. at 30.

[283] Resp. Br. at 30–31.

Finally, Silver Leaf denied that it was involved in the stock loan or block trading business, and "having no such business, acted reasonably with regard to the business that actually existed." [284] We disagree. As discussed above, neither the Firm's WSPs nor its actual supervision was reasonable "with regard to the business that actually existed": facilitating stock loans and block trades entered into by others.

* * *

Based on the above findings, we conclude that Silver Leaf violated NASD Rule 3010 and FINRA Rules 3110 and 2010.[285]

IV. Sanctions

A. Overview

In considering the appropriate sanctions to impose on Silver Leaf, we begin our sanctions analysis with FINRA's Sanction Guidelines ("Guidelines") as a benchmark.[286] The Guidelines contain (1) General Principles Applicable to All Sanction Determinations ("General Principles") "that should be considered in connection with the imposition of sanctions in all cases"; (2) a list of Principal Considerations in Determining Sanctions ("Principal Considerations") "which enumerates generic factors for consideration in all cases"; and (3) guidelines applicable to specific violations ("Specific Considerations"), which also typically "identify potential principal considerations that are specific to the described violation."[287]

The General Principles explain that "sanctions should be designed to protect the investing public by deterring misconduct and upholding high standards of business conduct." Adjudicators are therefore instructed to "design sanctions that are meaningful and significant enough to prevent and discourage future misconduct by a respondent and deter others from engaging in similar misconduct." Further, sanctions should "reflect the seriousness of the misconduct at issue,"[288] and should be "tailored to address the misconduct involved in each particular case."[289] "[T]o achieve deterrence and remediate misconduct," the Guidelines permit Adjudicators to "impose sanctions that … require a respondent firm to retain a qualified independent consultant to design and/or implement procedures for improved future compliance with regulatory

---

[284] Resp. Br. at 31.

[285] *Dep't of Enforcement v. Clements*, No. 2015044960501, 2018 FINRA Discip. LEXIS 11, at *46 (NAC May 17, 2018) ("A violation of NASD Rule 3010 or FINRA Rule 3110 is also a violation of FINRA Rule 2010.") (citing *Blair C. Mielke*, Exchange Act Release No. 75981, 2015 SEC LEXIS 3927, at *51 n.40 (Sept. 24, 2015)).

[286] *See, e.g.*, *Success Trade Sec., Inc.*, Exchange Act Release No. 81759, 2017 SEC LEXIS 3078, at *80 (Sept. 28, 2017) (finding that a sanctions analysis should begin with the Sanction Guidelines as a benchmark).

[287] FINRA Sanction Guidelines at 1 (2018) (Overview), http://www.finra.org/industry/sanction-guidelines.

[288] *Id.* at 2 (General Principle No. 1).

[289] *Id.* at 3 (General Principle No. 3).

requirements" or to "suspend or bar a respondent firm from engaging in a particular line of business."[290]

The sanctions we impose, here, are appropriate, proportionally measured to address Silver Leaf's misconduct, and designed to protect and further the interests of the investing public, the industry, and the regulatory system.

B. Sanctions for Paying Transaction-Based Compensation to Non-Member Entities

There are no Guidelines directly applicable to Silver Leaf's violative payments to non-members. We therefore looked to the Guidelines for the most analogous violation.[291] Because Silver Leaf's conduct perpetuated unregistered activities, it is appropriate to analogize Silver Leaf's conduct to a registration violation.[292] So we used those Guidelines to assist our formulation of sanctions. They recommend a fine of $2,500 to $73,000 and, in egregious cases, the Panel should consider suspending the firm in any or all activities or functions for up to 30 business days.[293] The Guideline for this violation contains two Specific Considerations: (1) whether the respondent has filed a registration application; and (2) the nature and extent of the unregistered person's responsibilities. We also considered the Principal Considerations applicable to all violations.

There are numerous aggravating factors present here. The Firm did not accept responsibility for its misconduct,[294] which occurred over an extended period,[295] and involved a pattern of misconduct.[296] The misconduct was also intentional.[297] Silver Leaf obtained monetary benefit from the misconduct,[298] as the Firm made payments to non-members in connection with transactions in which it received compensation. The compensation paid to the unregistered

---

[290] *Id.* at 3 (General Principle No. 3).

[291] Guidelines at 1 ("For violations that are not addressed specifically, Adjudicators are encouraged to look to the guidelines for analogous violations.").

[292] *Dep't of Enforcement v. Ryerson*, No. C9B040033, 2006 NASD Discip. LEXIS 17, at *43 n.48 (NAC Aug. 3, 2006) ("There is no specific sanction guideline for paying commissions to a non-NASD member. However, because such conduct perpetuates unregistered activities, we believe it appropriate to analogize [the respondent's] conduct to a registration violation.").

[293] Guidelines at 45.

[294] *Id*. at 7 (Principal Consideration No. 2). *See also Dep't of Enforcement v. Casas*, No. 2013036799501, 2017 FINRA Discip. LEXIS 1, at *45 (NAC Jan. 13, 2017).

[295] Guidelines at 7 (Principal Consideration No. 9).

[296] *Id*. at 7 (Principal Consideration No. 8).

[297] *Id*. at 7–8 (Principal Consideration Nos. 10 & 14).

[298] *Id*. at 8 (Principal Consideration No. 16).

entities was substantial.[299] A highly aggravating factor is that Silver Leaf resumed payments to the LLCs just months after SEC staff notified it that the conduct was improper, and after Silver Leaf, in response, assured the staff that it would not make these payments unless it received an SEC no-action letter.[300] Finally, there is no evidence that the unregistered entities, whose owners played an important role in the Firm's business, ever tried to become registered.[301]

Counterbalanced against these aggravating factors, the Panel found it somewhat mitigating that the payments to the LLCs benefited the persons who rightfully earned the compensation, namely, the Firm's brokers who owned the LLCs. We found no other mitigation.

Considering the aggravating and mitigating factors, we conclude that the Firm should be fined $50,000.

C. Sanctions for Supervisory Violations

The Guidelines for supervisory violations vary depending on the type of supervisory failure. The Guideline for systemic supervisory failures applies when the "failure is significant and is widespread or occurs over an extended period of time."[302] We find that this Guideline applies here because the Firm's supervisory failures constitute systemic failures; they were significant and occurred over an extended period. The Guideline recommends a fine of $10,000 to $292,000. Where aggravating factors predominate, Adjudicators should consider an even higher fine and "a suspension of the firm with respect to any or all relevant activities or functions for a period of 10 business days to two years, or consider expulsion of the firm." The Guideline also recommends that Adjudicators "consider imposing undertakings, ordering the firm to revise its supervisory systems and procedures, or ordering the firm to engage an independent consultant to recommend changes to the firm's supervisory systems and procedures."[303] It also identifies eight Specific Considerations applicable to a sanctions determination.

Deficient WSPs carry their own sanctions. The Guideline recommends a fine of $1,000 to $37,000. In egregious cases, Adjudicators should "consider suspending the firm with respect to any or all relevant activities or functions for up to 30 business days and thereafter until the

---

[299] As noted above, we considered for sanctions' purposes both the 2012 and 2013 transactions in which SH's entity, NAPI, received nearly $200,000 in transaction-based compensation. We also considered that the Firm paid transaction-based compensation to brokers' unregistered entities as far back as 2005 and that from February 2013 through April 2015, alone, that amount exceeded $2.6 million.

[300] Guidelines at 7–8 (Principal Consideration Nos. 10 & 14).

[301] *Id.* at 45.

[302] *Id.* at 105. "While systemic supervisory failures typically involve failures to implement or use supervisory procedures that exist, systemic supervisory failures also may involve supervisory systems that have both ineffectively designed procedures and procedures that are not implemented[,]" according to the Guideline. *Id.*

[303] *Id.* at 105–06.

supervisory procedures are amended to conform to rule requirements."[304] The Guideline specifies two Specific Considerations when determining sanctions for deficient WSPs: (1) "Whether deficiencies allowed violative conduct to occur or to escape detection," and (2) "[w]hether the deficiencies made it difficult to determine the individual or individuals responsible for specific areas of supervision or compliance."

We aggregate Silver Leaf's supervisory violations for the purposes of sanctions because the violations stem from a common cause: a generally lax approach to supervision.[305] In determining the appropriately remedial sanction to impose for these violations, we considered the numerous aggravating factors present here:

1. The deficiencies allowed violative conduct to occur or to escape detection;[306]

2. The Firm failed to respond reasonably to prior warnings from the SEC staff and other "red flag" warnings (which we finding highly aggravating);[307]

3. Silver Leaf failed to appropriately allocate its resources to prevent or detect the supervisory failure, taking into account the potential impact on customers or markets;[308]

4. The dollar value of the transactions not adequately supervised as a result of the deficiencies was substantial;[309]

5. The stock loan and block trade transactions were complex and, as Khan recognized, risky;[310]

---

[304] *Id.* at 107.

[305] *See Dep't of Enforcement v. Scottsdale Capital Advisors Corp.*, No. 2014041724601, 2018 FINRA Discip. LEXIS 16, at *249 & n.211 (NAC July 20, 2018) (aggregating supervisory violations and citing Sanction Guidelines at 4 (General Principle No. 4) (explaining that the aggregation or "batching" of violations may be appropriate for purposes of determining sanctions in disciplinary proceedings)), *appeal docketed*, No. 3-18612 (SEC July 23, 2018). *See also Dep't of Mkt. Regulation v. Naby*, No. 20120320803-01, 2017 FINRA Discip. LEXIS 27, at *28 (NAC July 24, 2017) (finding it appropriate to impose a unitary sanction because respondent's violations result from the same course of conduct).

[306] Guidelines at 105 (Specific Consideration No. 1), 107 (Specific Consideration No. 1).

[307] *Id.* at 105 (Specific Consideration No. 2), 8 (Principal Consideration No. 14). *See also Wedbush Sec. Inc.*, Exchange Act Release No. 78568, 2016 SEC LEXIS 2794, at *55 (Aug. 12, 2016) (finding "highly aggravating" that the firm failed to take action to improve compliance after explicit regulatory warnings of deficiencies), *petition for review denied*, 719 F. App'x 724 (9th Cir. 2018).

[308] Guidelines at 105 (Specific Consideration No. 3).

[309] *Id.* (Specific Consideration No. 5).

[310] *Id.* at 106 (Specific Consideration No. 6).

6. The Firm failed to accept responsibility for its supervisory failures;[311]

7. The misconduct occurred over an extended period of time;[312]

8. The supervisory failures were at least reckless;[313] and

9. By not exercising reasonable supervision, the Firm permitted numerous acts of wrongful conduct[314] to continue, to its financial benefit.[315]

Based on these aggravating factors and the absence of mitigation, we find that significant sanctions are required to remind Silver Leaf, and other similarly situated firms that facilitate stock loan and block trading activities, of their compliance obligations in this area. We impose monetary as well as non-monetary sanctions on the Firm. First, we impose a $50,000 fine.[316] Second, because of the gross inadequacies in Silver Leaf's supervisory procedures, we order the Firm to engage an independent consultant to review its supervisory procedures, as set out in detail in the Order below.[317] Finally, we bar the Firm from directly or indirectly facilitating stock loan and block trading transactions. We impose this last sanction given the severity and pervasiveness of the supervisory misconduct, and because the risk to the securities markets and other market participants is too great to permit Silver Leaf to continue engaging in that activity.[318] In light of this business-line bar, we decline to also censure Silver Leaf.[319]

---

[311] *Id*. at 7 (Principal Consideration No. 2); *see. e.g.*, *Dep't of Enforcement v. Reeves*, No. 2011030192201, 2014 FINRA Discip. LEXIS 41, at * 24 (NAC Oct. 8, 2014) (finding it "decidedly aggravating that [respondent] continues to refuse to take responsibility for his misconduct, [and] blames" others, including "FINRA for his current disciplinary troubles …"), *aff'd*, Exchange Act Release No. 76376, 2015 SEC LEXIS 4568 (Nov. 5, 2015).

[312] Guidelines at 7 (Principal Consideration No. 9).

[313] *Id.* at 8 (Principal Consideration No. 13).

[314] *Id.* at 8 (Principal Consideration No. 17).

[315] *Id.* at 8 (Principal Consideration No. 16).

[316] In light of the non-monetary sanctions we are imposing and the Firm's size (see footnote 333), we decline to impose a higher fine.

[317] In determining the procedures governing the retention of the independent consultant, the Panel found instructive the procedures set forth in *Scottsdale Capital*, 2018 FINRA Discip. LEXIS 16, at *244–49, and *Dep't of Enforcement v. Merrimac Corp. Sec., Inc.*, No. 2009017195204, 2015 FINRA Discip. LEXIS 4, at 24–28 (NAC Apr. 29, 2015).

[318] For the purposes of this business-line bar, the term "block trading" refers to transactions in equity securities involving 10,000 or more shares, or a market value of $200,000 or more, of a security, an underlying security or a related financial instrument overlying such number of shares, *Cf.* FINRA Rule 5270, Supplementary Material .03 (containing examples of block transactions); NYSE Rule 127.10 ("Definition of a Block").

[319] *Cf.* Guidelines at 9 (Technical Matters) (stating that Adjudicators should generally not impose a censure when imposing a bar, expulsion, or suspension).

D. Silver Leaf's Financial Inability-to-Pay Argument

Silver Leaf requested the Panel to consider its purportedly precarious financial condition, as well as Khan's, when imposing sanctions.[320] Under the Guidelines, "Adjudicators are required to consider a respondent's bona fide inability to pay when imposing a fine or ordering restitution."[321] "[R]espondents bear the burden of demonstrating an inability to pay and their burden is very high," according to the NAC.[322] In support of its argument, the Firm submitted, among other things, its most current Focus Report (as of June 30, 2018), which reflected net capital of about $370,000;[323] a Loan Agreement and Promissory Note between Khan and his brother-in-law;[324] evidence relating to Khan's draw down on a personal line of credit;[325] and a legal bill relating to the BTIG arbitration, which the Firm purportedly paid.[326] According to Khan, the Firm's excess net capital was about $120,000. Based on his "guesstimate," by the end of the year, the Firm's outstanding indebtedness to BTIG and Khan's indebtedness to his brother-in-law would exceed its excess net capital.[327] Khan also testified about the Firm's current financial hardships.[328]

Silver Leaf did not meet the high burden necessary to prove an inability to pay. "A firm's net capital does not govern monetary sanctions imposed on a member."[329] Moreover, a firm "must show that … it is unable to obtain the needed funds by, among other things, reducing expenses and salaries, raising capital, or borrowing money."[330] Stated a bit differently, a firm must prove that it "could not obtain financing, employ other sources of funds to discharge the monetary liability, or agree to an appropriate installment payment plan or other alternate

---

[320] *See, e.g.*, Tr. 2169–86.

[321] Guidelines at 6 (General Principle No. 9).

[322] *Dep't of Enforcement v. Meyers Assoc., L.P.*, No. 2010020954501, 2018 FINRA Discip. LEXIS 1, at *35, n.41 (NAC Jan. 4, 2018), *appeal docketed*, No. 3-18359 (SEC Feb. 20, 2018).

[323] RX-65, at 4.

[324] RX-51; Tr. 2290–91.

[325] Tr. 2292–93; RX-53.

[326] Tr. 2293–94; RX-54.

[327] Tr. 2313.

[328] *See, e.g.*, Tr. 2295–96.

[329] *Meyers Assoc.*, 2018 FINRA Discip. LEXIS 1, at *35, n. 41 (citing *ACAP Fin., Inc.*, Exchange Act Release No. 70046, 2013 SEC LEXIS 2156, at *76 & n.158 (July 26, 2013) (citing 2011 Guidelines at 5), *aff'd*, 783 F.3d 763 (10th Cir. 2015)); *see also* Guidelines at 6 (General Principle No. 9) ("Although Adjudicators must consider a respondent's *bona fide* inability to pay when the issue is raised by a respondent, monetary sanctions imposed on member firms need not be related to or limited by the firm's required minimum net capital.").

[330] *Dep't of Enforcement v. Wood*, No. 2011025444501, 2017 FINRA Discip. LEXIS 30, at *47 (NAC Mar. 15, 2017) (quoting *Dep't of Enforcement v. Merrimac Corp. Sec., Inc.*, No. 2007007151101, 2012 FINRA Discip. LEXIS 43, at *44 (Bd. of Governors May 2, 2012)).

payment option with FINRA."[331] Silver Leaf has not done so.[332] Accordingly, we reject its inability-to-pay argument.[333]

V. Order

Respondent Silver Leaf Partners LLC is:

1. Fined $50,000 for (a) paying transaction-based compensation to an unregistered finder's non-member, unregistered entity; and (b) paying transaction-based compensation to non-member, unregistered entities owned by its brokers, in violation of NASD Rule 2420 and FINRA Rule 2010.
2. Fined $50,000 for failing to adequately supervise its business and for failing to establish, maintain, and enforce adequate written supervisory procedures, in violation of NASD Rule 3010 and FINRA Rules 3110 and 2010.
3. Prohibited from directly, or indirectly, facilitating stock loan or block trading transactions, including using a finder to introduce prospective participants in such transactions.
4. Required to retain an independent consultant and comply with the following procedures:
    a. Within 60 days of this decision becoming FINRA's final disciplinary action, Silver Leaf shall retain an independent consultant acceptable to Enforcement. The independent consultant will conduct a comprehensive review of each of the Firm's policies, systems, and procedures (written and otherwise).

    b. Silver Leaf shall exclusively bear all costs, including compensation and expenses, associated with the retention of the independent consultant.

    c. Silver Leaf shall cooperate with the independent consultant in all respects, including providing staff support. The Firm shall place no restrictions on the independent consultant's communications with FINRA staff and, upon request, shall make available to FINRA staff any and all communications between the independent consultant and the Firm and documents reviewed by the independent consultant in connection with his or her engagement.

---

[331] *Meyers Assoc.*, 2018 FINRA Discip. LEXIS 1, at *35, n.41 (citing *ACAP Fin.*, 2013 SEC LEXIS 2156, at *77).

[332] Indeed, Khan made it clear that he will not seek a loan for the Firm. "Everybody has potential sources of funding," Khan stated, adding that he knows "lots of people but I have no intention of asking anybody for a loan." Tr. 2331–32.

[333] That said, as directed by the Guidelines, we have considered Silver Leaf's "size with a view toward ensuring that the sanctions imposed are remedial and designed to deter future misconduct." Guidelines at 2 (General Principle No. 1) (directing Adjudicators to consider a firm's size when tailoring sanctions).

Once retained, the Firm shall not terminate its relationship with the independent consultant without Enforcement's written approval.

d. Silver Leaf shall not have an attorney-client relationship with the independent consultant and shall not seek to invoke the attorney-client privilege or other doctrine or privilege to prevent the independent consultant from transmitting any information, reports, or documents to FINRA.

e. Silver Leaf shall require that the independent consultant enter into a written agreement that provides that, for the period of engagement and for a period of two years from completion of the engagement, the independent consultant shall not enter into any other employment, consultant, attorney-client, auditing, or other professional relationship with the Firm, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such. In addition, any firm with which the independent consultant is affiliated in performing his or her duties pursuant to this decision shall not, without prior written consent of FINRA staff, enter into any employment, consultant, attorney-client, auditing or other professional relationship with the Firm or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such for the period of the engagement and for a period of two years after the engagement.

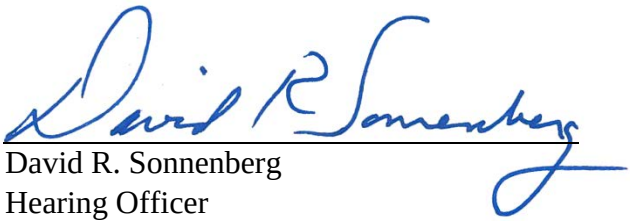
f. At the conclusion of the independent consultant's review, which shall be no more than 90 days after retention of the independent consultant, Silver Leaf shall require the independent consultant to submit to the Firm and FINRA staff a "Report." At a minimum, the Report shall provide (i) a description of the review performed and the conclusions reached; and (ii) recommended changes to the Firm's policies, systems, procedures, and training.

g. Within 60 days after delivery of the Report, Silver Leaf shall adopt and implement the recommendations of the independent consultant.

h. Within 30 days after the issuance of the independent consultant's Report, Silver Leaf shall provide to FINRA staff a written implementation report, certified by an officer of the Firm, attesting to, containing documentation of, and setting forth the details of the Firm's implementation of the independent consultant's recommendations.

5. Ordered to pay the costs of the hearing in the amount of $19,651.94, which includes a $750 administrative fee and a $18,901.94 fee for the cost of the hearing transcripts.

The fines and costs shall be payable on a date set by FINRA, but not sooner than 30 days after this decision becomes FINRA's final disciplinary action in this matter. The business-line bar shall be effective immediately if this Decision becomes FINRA's final disciplinary action in this matter.[334]



David R. Sonnenberg
Hearing Officer
For the Extended Hearing Panel

Copies to:

Fyzul Khan, Silver Leaf Partners, LLC (via overnight courier, email, and first-class mail)
Jeffrey A. Sexton, Esq. (via email and first-class mail)
Salah Borghei-Razavi, Esq. (via email)
Danielle I. Schanz, Esq. (via email and first-class mail)
Jason W. Gaarder, Esq. (via email)
Lara C. Thyagarajan, Esq. (via email)

[334] The Extended Hearing Panel considered and rejected without discussion all other arguments of the parties.