BEFORE THE NATIONAL ADJUDICATORY COUNCIL

FINANCIAL INDUSTRY REGULATORY AUTHORITY

In the Matter of Department of Enforcement, Complainant, vs. Adam James Makkai Castle Rock, CO, Respondent.	DECISION Complaint No. 2018058924502 Dated: January 6, 2023

Registered representative paid securities transaction-based compensation to an unregistered person. Held, findings affirmed, and sanctions modified.

Appearances

For the Complainant: John R. Baraniak, Esq., Jennifer L. Crawford, Esq., Michael Manning, Esq., Department of Enforcement, Financial Industry Regulatory Authority

For the Respondent: Dochtor Kennedy, Esq., Joseph P. Miller, Esq.

Decision

Adam James Makkai appeals a Hearing Panel decision. The Hearing Panel found that Makkai paid securities transaction-based compensation to an unregistered person, in violation of FINRA Rules 2040 and 2010. For this misconduct, the Hearing Panel fined Makkai $2,000 and suspended him 10 business days from associating with any FINRA member in any capacity.

After an independent review of the record, we affirm the Hearing Panel's findings of violations but modify the sanctions it imposed.

I. Background

Makkai entered the securities industry in 1999. He was registered in 2009 as a general securities representative and an investment company and variable contracts products representative of LPL Financial, LLC ("LPL").

LPL commenced a routine examination of one of its branch offices in late March 2018. During that examination, LPL received a call from a whistleblower who alleged that Makkai shared commissions with a representative, Scott Mason, whom LPL had earlier dismissed. After investigating the whistleblower's allegations, LPL concluded that Makkai indeed had paid Mason commissions when Mason was not registered in the securities brokerage industry, in violation of LPL policies that expressly referenced FINRA Rule 2040 and prohibited LPL representatives from sharing commissions and other revenue derived from securities transactions with any unregistered person without LPL's prior written approval.

LPL dismissed Makkai from the firm on June 4, 2018.[1] He has not associated subsequently with another FINRA member.[2]

II. Procedural History

Following an investigation of the circumstances that led LPL to dismiss Makkai, the Department of Enforcement filed a single-cause complaint on June 12, 2020. The complaint alleged Makkai violated FINRA Rules 2040 and 2010 when he paid Mason more than $27,000 from the commissions LPL paid to Makkai for securities transactions in accounts of LPL customers who were assigned previously to Mason. Makkai paid Mason the commissions from December 2017 to March 2018, a four-month period during which Mason was not registered with a broker-dealer.

Makkai filed an answer to the complaint on July 10, 2020. Makkai admitted in his answer that he paid Mason the securities transaction-based compensation on which the complaint is based, but he denied that the payments violated FINRA rules. Makkai claimed the payments

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[1] The Uniform Termination Notice for Securities Industry Registration ("Form U5") LPL filed on June 20, 2018, stated that the firm dismissed Makkai for "[s]haring commissions and fees with an unregistered person."

[2] In 2016, Makkai was registered as an investment adviser representative of Western Wealth Management, LLC ("Western Wealth"), an investment adviser firm and LPL office of supervisory jurisdiction. Western Wealth also dismissed Makkai on June 4, 2018, providing the same reason for his termination as LPL. Makkai was a registered investment adviser representative of Northwest Asset Management from June to October 2018. He has been a registered investment adviser representative of Advisory Services Network since November 2018.

were made pursuant to an oral agreement by which Makkai agreed to purchase Mason's "book of business."

On June 3, 2021, following a three-day hearing, the Hearing Panel issued its decision. The Hearing Panel found that Makkai violated FINRA Rules 2040 and 2010 by paying Mason, an unregistered person, securities transaction-based compensation. For this misconduct, the Hearing Panel fined Makkai $2,000 and suspended him from associating with any FINRA member in any capacity for 10 business days.

Makkai timely appealed the Hearing Panel's decision.

III. Facts

A. Scott Mason's Background

Mason was registered in 2013 as a general securities representative and an investment company and variable contracts products representative of LPL, and until the firm dismissed him on October 5, 2017.[3] Mason was not registered again with a FINRA member until August 30, 2018.[4]

B. Makkai Orally Agrees to Buy Mason's Book of Business

Makkai met Mason in 2016. Makkai began managing accounts for Mason in early 2017, a service for which Mason paid Makkai $1,500 each month.

Around the time LPL dismissed Mason, he told Makkai that he planned to retire, and he offered to sell Makkai his book of business, which consisted of between 100 and 150 LPL brokerage customers and Western Wealth investment adviser clients. Makkai orally agreed to

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[3] The Form U5 LPL filed on October 27, 2017, stated that the firm dismissed Mason for "[b]orrowing money from a client and being a joint owner on a client bank account, in violation of firm policy."

[4] Mason, like Makkai, was registered in 2016 as an investment adviser representative of Western Wealth. Western Wealth also dismissed Mason on October 5, 2017. Mason was registered as a general securities representative and an investment company and variable contracts products representative of Voya Financial Advisors, Inc., from August 2018 to November 2018. On July 3, 2019, Mason consented to the entry of FINRA findings that he borrowed money from an elderly LPL customer without notice to or permission from the firm. FINRA fined Mason $5,000 and suspended him for four months in all capacities for this misconduct. FINRA subsequently barred Mason from associating in any capacity with any FINRA member on June 29, 2020, for failing to respond to a FINRA request for information and testimony.

buy Mason's business production.[5] Makkai and Mason, however, continued to negotiate the terms of a formal purchase and sale agreement after LPL dismissed Mason. Makkai and Mason never memorialized their understanding in writing because, in Makkai's words, he and Mason "were still working on the details" and "there wasn't a contract in place."

C. LPL Assigns Mason's LPL Brokerage Accounts to Makkai

On October 6, 2017, the day after LPL dismissed Mason, the firm assigned Mason's brokerage accounts to Makkai.[6] LPL created a new representative code, "8KVK," that was established exclusively to allow Makkai to receive the commissions paid for these accounts.[7] From the day the accounts were assigned to Makkai, and until his dismissal in June 2018, LPL paid Makkai all the commissions earned from securities transactions effected for Mason's former LPL brokerage customers.

D. LPL Policies Prohibit Sharing Securities Transaction-Based Compensation with Unregistered Persons

LPL maintained written compliance policies for registered representatives of LPL, as well as persons registered dually through LPL and an investment adviser firm. These policies, which specifically referenced FINRA Rule 2040, prohibited registered representatives of LPL from directly or indirectly sharing commissions and other revenue derived from securities transactions with any unregistered person without the prior written approval of LPL's Governance, Risk and Compliance department.[8] These policies were in effect during the entire period of Makkai's alleged misconduct. Makkai knew in November 2017 that LPL's policies prohibited him from sharing securities transaction-based compensation with an unregistered person without first obtaining the firm's written permission. Indeed, Makkai completed a 2017 hybrid-advisor compliance questionnaire in which he attested that LPL prohibited him from

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[5] Makkai testified that this oral agreement meant that he "intended" to buy Mason's book of business.

[6] Makkai's supervisor testified that it was LPL's regular practice to reassign the accounts of a registered representative who was dismissed by the firm to another registered representative who was willing to service those accounts.

[7] Only accounts of Mason's former LPL brokerage customers were assigned to Makkai using the representative code 8KVK. The accounts of Mason's investment adviser clients were assigned separately to Makkai by Western Wealth. Investment adviser fees earned from those accounts were paid by Western Wealth to Makkai under a separate representative code.

[8] The written compliance policies for LPL's registered representatives, and dually registered representatives, aligned with LPL's written supervisory procedures, which also prohibited registered representatives of LPL from sharing securities transaction-based compensation with unregistered persons without the firm's prior written approval.

paying or otherwise directing securities transaction-based compensation to another person without prior LPL approval.

E. Makkai Agrees to Pay Mason Commissions Earned from the Accounts of Mason's Former LPL Brokerage Customers

In November 2017, Mason asked Makkai to pay him the commissions that LPL was paying Makkai for the accounts of Mason's former LPL brokerage customers. When Mason made this request, Makkai knew that LPL had dismissed Mason, the reasons for Mason's dismissal, and that Mason was not registered with another FINRA member. Makkai nevertheless acceded to Mason's request.[9] Makkai neither asked for nor received LPL's prior oral or written approval to pay Mason commissions that Makkai earned from Mason's former LPL brokerage accounts.

F. Makkai Pays Mason Commissions from Securities Transactions

During a four-month period, beginning in December 2017, and ending in March 2018, Makkai paid Mason $27,037.52 in commissions that LPL paid Makkai for securities transactions effected for Mason's former LPL brokerage customers.[10] These commissions comprised both continuing commissions that LPL paid on the accounts and commissions that LPL paid Makkai for securities transactions that he effected for the accounts after LPL reassigned them to him. Makkai paid Mason the commissions in seven transactions that adhered to the following pattern.

First, LPL paid the securities transaction-based commissions for representative code 8KVK, the representative code by which LPL assigned Makkai the accounts of Mason's former LPL brokerage customers, to a personal bank account that Makkai established for the dedicated purpose of receiving the revenues he earned from Mason's book of business. Next, Makkai transferred these commissions in their entirety to a separate business account that Makkai used to

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[9] Makkai testified that keeping the revenues from Mason's "years of hard work" made him "uncomfortable," and he felt it gave him an "unfair advantage" in his negotiations with Mason for purchase of his book of business. Thus, as a "gesture of goodwill," Makkai agreed to pay Mason all of the commissions and fees earned from Mason's former LPL brokerage customers and Western Wealth investment adviser clients, less $1,000 that Makkai and Mason agreed Makkai would keep for himself each month as a service fee, while they continued to negotiate the purchase and sale of Mason's book of business. The commissions included transaction-based commissions LPL was paying to Makkai.

[10] In total, Makkai paid Mason $101,503.50 during the relevant four-month span. This sum comprised both commissions that Makkai derived from securities transactions made for the accounts of Mason's former LPL brokerage customers and fees that Makkai earned from the accounts of Mason's former Western Wealth investment adviser clients. Makkai kept $4,000—$1,000 for each month from December 2017 to March 2018—that he earned from Mason's former investment adviser clients.

pay his business expenses. Then, Makkai paid Mason the commissions that he received from LPL for representative code 8KVK, either by check or electronically, from the business account. Finally, to be "transparent," Makkai emailed Mason copies of the brokerage commission statements that Makkai received from LPL for representative code 8KVK, along with snap shots of statements from Makkai's personal bank account.[11] These documents were meant to show Mason the sums of commissions that LPL paid Makkai and that Makkai transferred these sums in their entirety to the business account from which he eventually paid the commissions to Mason.

G. Makkai Pays Mason Commissions After Receiving Disapproving Guidance About These Types of Payments

Makkai's supervisor and LPL's Strategic Business Solutions group were both aware that Makkai and Mason were engaged in negotiations for Mason's book of business.[12] Makkai, however, never disclosed to anyone at LPL that he was paying Mason commissions that Makkai received for securities transactions effected for the accounts of Mason's former LPL brokerage customers.

Without advising his supervisor that he was already doing so, Makkai asked his supervisor in late 2017 or early 2018 whether he was permitted to pay Mason the commissions that Makkai earned from these accounts. The supervisor told Makkai, unequivocally, that he was not allowed to share securities transaction-based commissions with an unregistered person.[13] According to Makkai's supervisor, and as Makkai confirmed in his testimony, the supervisor told Makkai that he could make payments to Mason only pursuant to a final, written contract to purchase Mason's book of business that was approved by LPL.[14]

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[11] Makkai sent these emails using his LPL email address, but he addressed them only to Mason.

[12] Makkai and Mason asked LPL's Strategic Business Solutions group to assist them with valuing Mason's book of business.

[13] Makkai claims he told his supervisor that he had begun making payments towards the purchase of Mason's book of business, but he testified that he never disclosed to his supervisor the "specifics" or "mechanics" of those payments, including the fact that they comprised commissions earned from securities transactions effected for LPL brokerage customers. Makkai testified, "I guess if it was important to him, he would have asked me how they worked and I just figured it was okay [to pay Mason commissions]." Makkai's supervisor testified that he was not aware that Makkai had made any payments to Mason, and he learned that Makkai paid Mason commissions from securities transactions only after LPL conducted the investigation that resulted in Makkai's dismissal.

[14] The supervisor testified that he had no authority to allow an LPL registered representative to share securities transaction-based compensation with an unregistered person. He also testified that he did not have the power to approve any agreement by which a retiring registered

[Footnote continued on next page]

In addition, LPL also told Makkai that he could not share commission with an unregistered person when it reviewed Makkai's purchase agreement for another registered representative's book of business. When Makkai completed his 2017 hybrid-advisor compliance questionnaire, Makkai disclosed to LPL that he had entered into a written agreement to purchase the book of business of this other LPL registered representative, who planned to retire. As a result of this disclosure, LPL directed Makkai to forward a copy of the written agreement to LPL's Strategic Business Solutions group, which he did on January 16, 2018. According to the terms of that agreement, which Makkai and the other registered representative executed in October 2016, Makkai agreed to pay the representative a percentage of the revenues, including commissions, derived from the representative's book of business for a period of seven years.

On January 31, 2018, however, after reviewing the agreement that Makkai submitted, the Strategic Business Solutions group notified Makkai that he could not share commissions earned from LPL brokerage accounts with the representative after the representative's "license termination."[15] The Strategic Business Solutions group therefore informed Makkai that the agreement with the other representative, who was at that time still an LPL registered representative, would have to be amended before the representative's securities industry licenses were terminated and he retired.[16]

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representative sold his or her book of business to another registered representative. Such approvals would have to be obtained from LPL in writing.

[15] This is consistent with LPL's written compliance policies for its registered representatives. These policies expressly prohibited the ongoing payment of commissions and fees to retired registered representatives of the firm. The policies further required that all compensation arrangements with retired registered representatives be documented and provide for either a flat, one-time payment or ongoing payments based on a valuation of the retired registered representative's book of business prior to the termination of his or her association with LPL. Under no circumstances could the valuation of a retiring registered representative's book of business be derived from any future commissions or fees generated following the termination of the retiring registered representative's association with LPL.

[16] The Strategic Business Solutions group advised Makkai of the permissible methods for paying the retiring registered representative for his book of business. These included either the payment of a flat purchase price or payments made pursuant to a payment plan based on a third-party valuation of the retiring representative's book of business, with the potential for downward adjustment to account for any diminishment in assets under management. A sample purchase and sale agreement that the Strategic Business Solutions group sent Makkai made clear that continuing commissions paid on the retiring registered representative's accounts could be taken into account for valuation purposes, but under no circumstances could the value be determined based on any future commissions earned by the registered representative who acquired the retiring registered representative's book of business.

Notwithstanding the guidance that Makkai received from his supervisor and LPL's Strategic Business Solutions group, which explicitly warned Makkai against sharing commissions derived from securities transactions with an unregistered person, four of the seven payments that Makkai made to Mason for commissions generated by the accounts of Mason's former LPL brokerage customers occurred after January 31, 2018.

H. Mason Continues to Communicate and Meet with His Former LPL Brokerage Customers

On October 10, 2017, a few days after LPL discharged Mason, Makkai asked LPL and Western Wealth to employ Mason as a "relationship manager" so that Mason could continue to have access to the accounts of Mason's former LPL brokerage customers and Western Wealth investment adviser clients. LPL immediately informed Makkai that this was not permitted because LPL had terminated Mason's association with the firm, and Mason thus could not "affiliate, in any way, with LPL Financial." Makkai testified that he understood this to mean that Mason could not engage in any activities that required a "securities license, which involved having access to client accounts and making securities recommendations and those kind of things."

Mason nevertheless continued to communicate and meet with his former LPL brokerage customers and Western Wealth investment adviser clients. For example, Mason sent an email to a former customer on November 9, 2017. In this email Mason wrote, "I am pleased to announce that I have merged my practice with another advisor, Adam Makkai."[17] Mason further explained that Makkai "is an experienced advisor" who "is in the same firm, Western Wealth Advisors [sic] and has the same broker dealer, LPL Financial, that I've been affiliated with for the past four years." Mason informed the customer, "I have moved my client accounts to Adam's LPL Financial representative code, in anticipation of my eventual retirement. However, under the terms of the merger I will continue to be your point of contact for the next 5 years or so." Mason asserted that the only change "is my email address," and concluded, "I look forward to our continued relationship and helping you achieve your financial goals. I will be introducing you to Adam over time. Thank you for allowing me to [be your] Financial guy!" Mason forwarded this email to Makkai on November 10, 2017. Makkai never contacted the customer to correct any apparent inaccuracies in Mason's email or to inform the customer that Mason was no longer a registered representative of LPL or associated with Western Wealth. Makkai testified, "These were [Mason's] relationships. He communicated with his clients."

[17] Mason sent a similar email to a former customer on October 24, 2017, claiming that he had "merged" his practice with Makkai's. Mason declared in this email, "I'll be sending an email to all my clients about the change. Please know, I'm still here. We are just changing the org structure."

Mason also met with his former LPL brokerage customers and Western Wealth investment adviser clients at the LPL offices where Makkai and Mason both worked—after LPL dismissed him.[18] Makkai described this phase of Mason's involvement with what were now Makkai's customers and clients as a "transition period" during which Mason facilitated the transfer of his former accounts to Makkai and discussed with customers and clients "financial planning matters that [did] not include securities or investment management." Mason and his assistant scheduled these meetings, and Mason decided whether to invite Makkai based on the financial needs of the customers and clients with whom Mason met. Makkai claimed that Mason understood he could not recommend securities transactions, or otherwise engage in activities that required Mason be a registered representative of a broker-dealer, without Makkai also being in attendance. Makkai nevertheless also testified that he was too busy to attend all the meetings that Mason scheduled.[19] Indeed, Makkai could recall meeting only one of Mason's former customers or clients, and he did not remember any specific meetings that he may have attended.

I. Makkai Decides Against Purchasing Mason's Book of Business

Makkai and Mason could not agree on terms, including the price, for the purchase of Mason's book of business. Makkai concluded that the purchase price Mason proposed was too high, and Mason sought guarantees to which Makkai would not agree. Additionally, Makkai concluded that servicing the accounts of Mason's former LPL brokerage customers and Western Wealth investment adviser clients consumed too much of his time. Makkai accordingly decided to back out of his oral agreement to acquire Mason's book of business in March 2018, and Makkai and Mason ceased their negotiations. Because they did not agree on the terms of a final purchase and sale agreement, at no time did they reduce any agreement to writing.[20]

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[18] Mason was an insurance agent, and his former customers and clients had insurance contracts that they had purchased through him. Mason therefore was permitted to maintain an office at the LPL offices at which both he and Makkai worked. Makkai's supervisor, who had also been Mason's supervisor, testified that he told Makkai and Mason that Mason could only meet with Makkai's customers and clients to discuss insurance products—any discussions concerning a transaction involving securities required Makkai's presence.

[19] Mason or his assistant prepared agendas and took notes for the meetings, which Mason shared with Makkai. Enforcement claims that these agendas and notes show that at least two of Mason's former customers engaged in securities transactions in their LPL brokerage accounts within a few weeks of meeting Mason in January 2018. We find the evidence insufficient to infer that any LPL brokerage customer engaged in a securities transaction as a result of a recommendation that Mason made after LPL dismissed him. On at least one occasion, however, Mason emailed Makkai informing him about the specifics of a securities transaction involving a sale of stock, which Mason informed Makkai he would need to have reversed through LPL.

[20] When Makkai backed out of his oral agreement to purchase Mason's book of business, Mason began offering his book of business to others. LPL, however, informed Mason that it would not support the sale of his book of business to a registered representative of LPL.

Makkai did not ask Mason to return any portion of the $101,503.50 in securities brokerage commissions and investment adviser fees that Makkai paid Mason from December 2017 to March 2018. Makkai and Mason never agreed—or even discussed—that these payments would be treated as part of the purchase price for Mason's book of business. Consistent with his view that these payments represented a "gesture of goodwill," Makkai intended to make them only until he and Mason executed a formal purchase and sale agreement for Mason's business production.

IV. Discussion

The Hearing Panel found that Makkai paid securities transaction-based compensation to an unregistered person, in violation of FINRA Rules 2040 and 2010. We affirm the Hearing Panel's findings. In so doing, we reject each of the challenges to these findings that Makkai poses in this appeal.

A. FINRA Retained Jurisdiction to Discipline Makkai

As a threshold matter, Makkai argues that because Enforcement filed the complaint more than two years after LPL discharged him, FINRA lacked jurisdiction to bring this disciplinary action. Makkai mistakes the limits of FINRA's jurisdiction.[21] We find that the complaint in this matter was filed timely.

Article V, Section 4(a)(i) of the FINRA By-Laws stipulates that FINRA retains jurisdiction to file a complaint against a person whose association with a member has been ended for "two years after the effective date of termination of registration." The termination upon which FINRA's continuing jurisdiction is grounded thus "is not termination of employment or association, but termination of *registration*." *Donald M. Bickerstaff*, 52 S.E.C. 232, 234 (1995) (emphasis in original). A person who becomes registered through a FINRA member remains registered until FINRA ends the registration after it receives a Form U5.[22] *See David Kristian Evansen*, Exchange Act Release No. 75531, 2015 SEC LEXIS 3080, at *13 (July 27, 2015).

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[21] On August 25, 2020, Makkai filed a notice of appeal requesting that the NAC review the Hearing Officer's July 31, 2020 order denying Makkai's request for summary disposition based on his argument that FINRA lacked jurisdiction over him. A Review Subcommittee of the NAC reviewed Makkai's notice of appeal but dismissed it as interlocutory in nature and impermissible under FINRA rules.

[22] The Form U5 expressly reminds the person who is the subject of the filing that he or she "continue[s] to be subject to the jurisdiction of regulators for at least two years after your registration is terminated" and that FINRA "determines the effective date of registration." *See* Form U5, https://www.finra.org/sites/default/files/form-u5.pdf.

LPL filed a Form U5 on June 20, 2018, which reported to FINRA that LPL discharged Makkai on June 4, 2018, for "[s]haring commissions and fees with an unregistered person."[23] Accordingly, FINRA terminated all registrations that Makkai held with FINRA on June 20, 2018. FINRA therefore possessed jurisdiction to file a complaint for a period of two years following this date, i.e., until June 20, 2020. Because Enforcement filed the complaint initiating a disciplinary action against Makkai on June 12, 2020, within the permitted two-year period, FINRA retained jurisdiction to bring a disciplinary action against Makkai for the misconduct at issue in this case.[24]

B. Makkai Paid an Unregistered Person Securities Transaction-Based Compensation in Violation of FINRA Rules

We find, as did the Hearing Panel, that Makkai paid Mason securities transaction-based compensation when Mason was not registered in the securities industry, in violation of FINRA Rules 2040 and 2010.

FINRA Rule 2040 controls the payment of securities transaction-based compensation to unregistered persons. It states:

> No member or associated person shall, directly or indirectly, pay any compensation, fees, concessions, discounts, commissions or other allowances to

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[23] Makkai states in his opening appeal brief that LPL discharged him on June 8, 2018. The evidence nevertheless establishes June 4, 2018, as the date of his dismissal from the firm. Makkai's error has no bearing on the issue of whether FINRA retained jurisdiction to discipline him.

[24] Makkai argues in the alternative that the date for establishing the two-year period of FINRA's retained jurisdiction is June 12, 2018, the date Makkai claims FINRA "[became] aware of the allegations" of his misconduct. On this date, Northwest Asset Management filed a Uniform Application for Securities Industry Registration or Transfer ("Form U4") registering Makkai as an investment adviser representative of that firm. The Form U4 answered "Yes" in response to question 14J(1): "Have you ever voluntarily resigned, been discharged, or permitted to resign after allegations were made that accused you of . . . violating *investment-related* statutes, regulations, rules, or industry standards of conduct?" The Disclosure Reporting Page for this answer also disclosed that LPL ended Makkai's association with it on June 4, 2018, for "[s]haring commissions and advisory fees with an unregistered person." The Form U4, however, did not effect a termination of Makkai's registrations as a representative of LPL. It therefore does not answer the question of when the period of FINRA's retained jurisdiction began or ended in this case. *See Evansen*, 2015 SEC LEXIS 3080, at *13. Nonetheless, in the event Makkai was correct, which he is not, and the Form U4 filed on June 12, 2018, operated to commence the two-year period of retained jurisdiction in this case, Enforcement timely filed the complaint within two years of this date.

> . . . any person that is not registered as a broker-dealer under Section 15(a) of the Exchange Act but, by reason of receipt of any such payments and the activities related thereto, is required to be so registered under applicable federal securities laws and SEA rules and regulations.

FINRA Rule 2040(a)(1).

FINRA Rule 2040 is aligned expressly with Section 15(a) of the Securities Exchange Act of 1934 ("Exchange Act") and related Securities and Exchange Commission ("Commission") guidance addressing whether registration is required of persons who receive transaction-based compensation derived from broker-dealer activities.[25] *See Approval Order*, 80 Fed. Reg. at 554-55, 561; *FINRA Regulatory Notice 15-17*, 2015 FINRA LEXIS 5, at *3 (Mar. 2015). Section 15(a)(1) of the Exchange Act generally requires that any person engaged in the business of effecting transactions in securities register with the Commission as a broker-dealer.[26]

The Commission has provided guidance in this area through a series of no-action letters. *See, e.g.*, *Brumberg, Mackey & Wall, P.L.C.*, SEC No-Action Letter, 2010 SEC No-Act. LEXIS 406 (May 17, 2010); *Wolff Juall Invs., LLC*, SEC No-Action Letter, 2005 SEC No-Act. LEXIS 617 (May 17, 2005); *Herbruck, Alder & Co.*, SEC No-Action Letter, 2002 SEC No-Act. LEXIS 499 (May 3, 2002); *1st Glob., Inc.*, SEC No-Action Letter, 2001 SEC No-Act. LEXIS 557 (May 7, 2001); *Birchtree Fin. Servs, Inc.*, SEC No-Action Letter, 1998 SEC No-Act. LEXIS 874 (Sept.

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[25] FINRA Rule 2040 is aligned also with prior FINRA interpretations under NASD Rule 2420. *See Order Approving Proposed Rule Change Relating to Payments to Unregistered Persons* ("*Approval Order*"), Exchange Act Release No. 73954, 80 Fed. Reg. 553, 555 (Jan. 6, 2015) (SR-FINRA-2014-37); *FINRA Regulatory Notice 09-69*, 2009 FINRA LEXIS 199, at *9 (Dec. 2009). NASD Rule 2420 generally prohibited FINRA members from paying fees or commissions to non-member broker-dealers. *See* NASD Rule 2420 (*superseded by* FINRA Rule 2040 (Aug. 24, 2015)). FINRA interpreted this and other NASD non-member rules to prohibit the payment of securities transaction-based compensation to any person that may be acting as an unregistered broker-dealer. *See Approval Order*, 80 Fed. Reg. at 554, 555 & n.12; *FINRA Regulatory Notice 09-69*, 2009 FINRA LEXIS 199, at *6.

[26] Section 15(a)(1) of the Exchange Act states:

> It shall be unlawful for any broker or dealer which is either a person other than a natural person or a natural person not associated with a broker or dealer which is a person other than a natural person . . . to make use of the mails or any means or instrumentality of interstate commerce to effect any transactions in, or to induce or attempt to induce the purchase or sale of, any security . . . unless such broker or dealer is registered in accordance with subsection (b) of this section.

15 U.S.C. § 78o(a)(1). "The term 'broker' means any person engaged in the business of effecting transactions in securities for the account of others." 15 U.S.C. § 78c(a)(4)(A).

22, 1998). Focusing specifically on situations that are similar to this case, well-recognized Commission guidance states that the receipt of securities transaction-based compensation indicates that a person is engaged in the securities business and generally should be registered as a broker-dealer under the Exchange Act. *See Approval Order*, 80 Fed. Reg. at 555.

The Commission has in its adjudicated decisions referred to the following factors when determining whether a person is engaging in acts that require registration as a broker-dealer: (1) holding oneself out as a broker-dealer; (2) recruiting or soliciting potential investors; (3) advising investors as to the merits of an investment; (4) acting with regularity in securities transactions; and (5) receiving transaction-based compensation. *See, e.g.*, *James S. Tagliaferri*, Exchange Act Release No. 80047, 2017 SEC LEXIS 481, at *13-14 (Feb. 15, 2017); *Anthony Fields*, Exchange Act Release No. 74344, 2015 SEC LEXIS 662, at *44 (Feb. 20, 2015). Both the Commission and FINRA have emphasized that the receipt of securities transaction-based compensation is a distinguishing characteristic of activity requiring registration as a broker-dealer.[27] *See Tagliaferri*, 2017 SEC LEXIS 481, at *14; *Dep't of Enf't v. Silver Leaf Partners, LLC*, Complaint No. 2014042606902, 2020 FINRA Discip. LEXIS 36, at *46 (FINRA NAC June 29, 2020).

In this case, the evidence establishes that Makkai indirectly paid Mason more than $27,000 in securities transaction-based compensation, which comprised commissions LPL paid to Makkai for securities transactions effected for the accounts of Mason's former LPL brokerage customers.[28] Makkai paid these sums to Mason during a four-month period—spanning late 2017

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[27] This is consistent with statements by the courts, which apply a non-exclusive list of factors to determine whether a person is a broker-dealer within the meaning of Section 15(a)(1) of the Exchange Act. *See, e.g.*, *SEC v. Collyard*, 861 F.3d 760, 766 (8th Cir. 2017); *see also SEC v. Moss*, No. 4:20-CV-972-SDJ, 2022 U.S. Dist. LEXIS 43600, at *14-15 (E.D. Tex. Mar. 11, 2022) (collecting cases). These factors include: (1) regular participation in securities transactions; (2) employment with the issuer of the securities; (3) payment by commission as opposed to salary; (4) history of selling the securities of others; (5) involvement in advice to investors; and (6) active recruitment of investors. *Collyard*, 861 F.3d at 766. Of these factors, the receipt of commissions or other transaction-based compensation from the purchase or sale of securities has been described as a "hallmark" of being a broker-dealer. *See, e.g.*, *SEC v. Mieka Energy Corp.*, 259 F. Supp. 3d 556, 561 (E.D. Tex. 2017); *see also Landegger v. Cohen*, No. 11-cv-01760-WJM-CBS, 2013 U.S. Dist. LEXIS 140634, at *16 (D. Colo. Sept. 30, 2013) (collecting cases).

[28] In his appeal brief, Makkai appears to argue that there is no evidence that the commissions he paid Mason were derived from securities transactions. Assuming this is Makkai's position, his argument lacks merit. A preponderance of the evidence supports finding that Makkai paid Mason securities transaction-based compensation. *See Seaton v. SEC*, 670 F.2d 309, 311 (D.C. Cir. 1982) (upholding application of the preponderance of evidence standard in FINRA disciplinary proceedings). Among other things, Makkai admitted when he answered the complaint that he paid Mason more than $27,000 in commissions derived from securities transactions. This admission is binding on Makkai. *See Gibbs v. CIGNA Corp.*, 440 F.3d 571,

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and early 2018—when Mason was not registered as a broker-dealer. By reason of his receipt of the commissions Makkai paid him, and the securities activities related thereto, Mason was required to be so registered under Section 15(a) of the Exchange Act. We therefore find that Makkai violated FINRA Rules 2040 and 2010 by paying securities transaction-based compensation to an unregistered person.[29] *Cf. Silver Leaf*, 2020 FINRA Discip. Lexis 36, at *48 (finding FINRA member violated NASD Rule 2420 because it deposited securities transaction-based compensation into accounts owned by non-member entities, "and that is not allowed").

C. Makkai's Other Appeal Arguments Lack Merit

Despite the clarity of the evidence and of the foregoing findings, Makkai contends that he nevertheless is not liable under FINRA rules for paying Mason securities transaction-based compensation. He also claims that the Hearing Officer erred by excluding certain evidence from the record. We conclude that each of these appeal arguments lacks merit.

1. Makkai Did Not Pay Mason Commissions Pursuant to a Bona Fide Contract

Makkai asserts that FINRA Rule 2040(b), which permits FINRA members to pay continuing commissions to retiring registered representatives of the member if conditions are met, shields him from disciplinary action here. We find that FINRA Rule 2040(b) provides Makkai no safe harbor under the facts of this case.

First, FINRA Rule 2040(b), by its express terms, permits only a FINRA *member* to pay continuing commissions to a retiring registered representative of the *member* pursuant to a bona fide contract between the *member* and the retiring registered representative.[30] The rule thus

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578 (2d Cir. 2006) ("Facts admitted in an answer, as in any pleading, are judicial admissions that bind the defendant throughout the litigation."). Moreover, Makkai's admission is consistent with his testimony, which established that Makkai agreed to pay Mason all the commissions Makkai earned from securities transactions made for the accounts of Mason's former LPL brokerage customers. Finally, the documentary evidence, in the form of brokerage commission statements and statements from Makkai's bank accounts, shows that Makkai paid the commissions to Mason.

[29] FINRA Rule 2010 states "[a] member, in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade." Conduct that violates the federal securities laws or a FINRA rule also violates FINRA Rule 2010. *See Dep't of Enf't v. Luo*, Complaint No. 2011026346206, 2017 FINRA Discip. LEXIS 4, at *20-21 (FINRA NAC Jan. 13, 2017).

[30] FINRA Rule 2040(b) states:

[Footnote continued on next page]

cannot serve to justify the payments of securities transaction-based compensation that Makkai, who was not a FINRA member but rather a registered representative of a member, made to Mason.[31] *See id*; *see also FINRA Regulatory Notice 15-17*, 2015 FINRA LEXIS 5, at *6 ("Under Rule 2040(b), a *member firm* can pay continuing commissions to its retiring registered representatives . . . ." (emphasis added)).

Second, the term "retiring registered representative" is defined under FINRA Rule 2040(b) to mean a person who retires from a FINRA member and leaves the securities industry. *See* FINRA Rule 2040(b)(2). This term does not apply to describe Mason. Mason did not retire from LPL. Instead, he was discharged by the firm for violating firm policies, and his registrations through the firm were accordingly terminated. Mason also did not leave the securities industry. Rather, Mason continued to meet and communicate with his former LPL brokerage customers and Western Wealth investment adviser clients. In this respect, Mason explained that he had merged his business practice with Makkai's "in anticipation of [his] *eventual* retirement," but that he would continue to participate in the securities industry as the "point of contact" for their accounts under Makkai's LPL representative code. Indeed, after being unemployed for a period of several months, Mason returned to the securities industry as a registered representative of another FINRA member.

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> A member may pay continuing commissions to a retiring registered representative of the member, after he or she ceases to be associated with such member, that are derived from accounts held for continuing customers of the retiring registered representative regardless of whether customer funds or securities are added to the accounts during the period of retirement, provided that:
>
> > (A) a bona fide contract between the member and the retiring registered representative providing for the payments was entered into in good faith while the person was a registered representative of the member and such contract, among other things, prohibits the retiring registered representative from soliciting new business, opening new accounts, or servicing the accounts generating the continuing commission payments; and
> >
> > (B) the arrangement complies with applicable federal securities laws, SEA rules and regulations.

FINRA Rule 2040(b)(1).

[31] Were we to conclude, which we do not, that FINRA Rule 2040(b) provides Makkai some protection here, the rule permits the payment of continuing commissions only. The rule does not justify Makkai's decision to pay Mason commissions that Makkai earned for securities transactions that Makkai effected for Mason's former LPL brokerage customers.

Finally, the commissions that Makkai shared with Mason were not, as required under FINRA Rule 2040(b), paid pursuant to a bona fide contract that was entered into while Mason was a registered representative of LPL. *See* FINRA Rule 2040(b)(1)(A). Although Makkai orally agreed to purchase Mason's business production around the time LPL dismissed Mason, Makkai and Mason continued to negotiate the terms of a formal purchase and sale agreement after Mason's dismissal. In this respect, Makkai viewed his oral agreement with Mason as an expression of his intention to buy Mason's book of business, but as he testified, "there wasn't a contract in place," and, indeed, Makkai subsequently changed his mind and walked away from the intended purchase without consequences.

Moreover, even were we to find, which we do not, that Makkai's oral agreement to purchase Mason's book of business constituted a bona fide contract for purposes of FINRA Rule 2040(b), the commission payments that Makkai made to Mason were not, as Makkai now claims, made pursuant to this agreement.[32] Makkai agreed to pay Mason the commissions generated by the accounts of Mason's former LPL brokerage customers sometime after he orally agreed to purchase Mason's book of business. Makkai voluntarily made these payments as a "gesture of goodwill," not pursuant to a binding agreement, and he intended them to stop once he and Mason executed a formal purchase and sale agreement for Mason's business production. Makkai and Mason thus never agreed that the commissions Makkai paid Mason would be treated as part of the purchase price that Makkai would pay Mason for acquiring his book of business. Consistent with this intention, when the sale was not consummated, Makkai never asked Mason to return any of the commissions Makkai had paid him.

[32] The Hearing Panel found that no bona fide contract existed for purposes of FINRA Rule 2040(b) because Makkai and Mason never reduced their oral agreement to writing. We affirm the Hearing Panel's finding, but also find—as noted above—other reasons why Mason did not satisfy the requirements of FINRA Rule 2040(b). FINRA Rule 2040(b) codified existing FINRA guidance on the payment by members of continuing commissions to retiring registered representatives. *See Approval Order*, 80 Fed. Reg. at 555. That guidance was premised on the existence of a "duly executed" or "written contract" between the member and the retiring registered representative. *See id.* n.13 (citing FINRA Interpretive Letters). The necessity that a bona fide contract be written is further supported by the express terms of FINRA Rule 2040(b). *See Victor Elias Photography, LLC v. ICE Portal, Inc.*, No. 21-11892, 2022 U.S. App. LEXIS 22472, at *10 (11th Cir. Aug. 12, 2022) ("A statute should be construed to give effect to all its provisions, so that no part of it will be inoperative or superfluous, void or insignificant."). Among other things, FINRA Rule 2040(b) recognizes that, "[i]n the case of the death of the retiring registered representative, the retiring registered representative's beneficiary designated in the *written* contract . . . may be the beneficiary of the respective member's agreement with the deceased representative." S*ee* FINRA Rule 2040(b)(2) (emphasis added).

2. Makkai Misjudges the Proof Needed to Find He Violated FINRA Rule 2040

Makkai claims that the Hearing Panel's findings that he violated FINRA Rule 2040 lack support in the record. Specifically, Makkai asserts that there is no evidence that Mason recommended or effected any of the securities transactions that resulted in Makkai paying Mason commissions earned from the accounts of Mason's former LPL brokerage customers. Makkai claims that, in the absence of such evidence, he cannot be held liable for violating FINRA Rule 2040 because there is no proof Mason engaged in activities that required his registration as a broker-dealer under the Exchange Act. We disagree with Makkai's assessment of the evidence required to establish a violation of FINRA Rule 2040.

As we explained above (*supra* Part IV.B), FINRA Rule 2040 is aligned expressly with Exchange Act Section 15(a) and related Commission guidance that addresses whether registration as a broker-dealer is required for persons who receive transaction-based compensation. *See Approval Order*, 80 Fed. Reg. at 554-55, 561. "Registration as a broker-dealer provides a framework of rules to regulate the conduct of persons who receive securities transaction-based compensation, the receipt of which can create potential incentives for abusive sales practices." *Id.* at 554. This "helps to ensure that persons who have a 'salesman's stake' in a securities transaction operate in a manner that is consistent with customer protection standards governing broker-dealers and their associated persons." *Herbruck, Alder & Co.*, 2002 SEC No-Act. LEXIS 499, at *4; *accord 1st Glob., Inc.*, 2001 SEC No-Act. LEXIS 557, at *5.

FINRA Rule 2040 accordingly focuses on the *receipt of* commissions or other compensation and the *activities related to* the commissions or other compensation for purposes of conferring broker-dealer status on an unregistered person under the rule.[33] *See* FINRA Rule 2040(a). And in this respect, the Commission's guidance is abundantly clear. The receipt of commissions and other compensation derived from the purchase or sale of securities indicates that a person is engaged in the business of effecting securities transactions and generally should be registered as a broker-dealer under the Exchange Act. *See Approval Order*, 80 Fed. Reg. at 554, 555. Or, stated more precisely, "any person receiving transaction-based compensation in connection with another person's purchase or sale of securities typically must register as a broker-dealer or be an associated person of a registered broker-dealer."[34] *Brumberg, Mackey & Wall, P.L.C.*, 2010 SEC No-Act. LEXIS 406, at *2.

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[33] The rule recognizes inherently that Commission guidance "provides that certain activities may be deemed (alone or in combination) to confer 'broker' status, and the receipt of transaction-based compensation coupled with these activities may trigger the requirement to register as a broker-dealer under the Exchange Act." *Approval Order*, 80 Fed Reg. at 558.

[34] In his opening appeal brief, Makkai argues that the Hearing Panel embraced a "broad interpretation" of the Exchange Act's registration requirements for broker-dealers, which would "preclude any and all licensed brokers from making payments to any unregistered person, if such payments could be traced back to commissions received by the broker from his or her member firm." We disagree with Makkai's assessment that the Hearing Panel's decision rests on an

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As the evidence confirms, Makkai paid Mason more than $27,000 in commissions that Makkai earned for securities transactions effected for the accounts of Mason's former LPL brokerage customers. By virtue of his receipt of this securities transaction-based compensation, Mason was himself required to be registered as a broker-dealer under the Exchange Act. Because he was not so registered, Makkai violated FINRA Rule 2040.[35] *Cf. Silver Leaf*, 2020 FINRA Discip. Lexis 36, at *48.

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overly broad interpretation of broker-dealer registration requirements. The Hearing Panel's liability findings are consistent with Commission guidance that is founded on the unambiguous proposition that a broker-dealer or registered representative generally may not pay securities transaction-based compensation to another person or entity unless the recipient of that compensation is also registered as a broker-dealer under the Exchange Act. *See Wolff Juall Invs.*, 2005 SEC No-Act. LEXIS 617, at *4 (stating that, absent an exemption, an entity that receives securities commissions or other transaction-based compensation in connection with securities-based activities that fall within the definition of "broker" or "dealer" generally itself is required to be registered as a broker dealer); *Herbruck, Alder & Co.*, 2002 SEC No-Act. LEXIS 499, at *4 (same); *1st Glob. Inc.*, 2001 SEC No. Act. LEXIS 557, at *5 (same); *Birchtree Fin. Servs, Inc.*, SEC No-Action Letter, 1998 SEC No-Act. LEXIS 874, at *2 (same).

[35] In any event, we disagree with Makkai's claim that there exists no evidence, other than Mason's receipt of commissions, from which to conclude that Mason engaged in activities requiring that he be registered as a broker dealer under the Exchange Act. As an initial matter, we note that Makkai ignores the fact that he paid Mason continuing commissions that were not permitted absent a bona fide contract under FINRA Rule 2040(b), which, as we find above, did not exist in this case. Moreover, Makkai provided Mason a "salesman's stake" in his securities business, thus creating heightened incentives for Mason to engage in abusive sales efforts. Those risks were patently evident in this case. Among other things, Mason told his former customers that he would, in effect, continue to act as their broker when he informed them that he had merely "merged" his securities business with Makkai's but would "continue to be [their] point of contact for the next 5 years or so," or as he put it, their "Financial guy." *See Fields*, 2015 SEC LEXIS 662, at *44 (finding respondents held themselves out as brokers and "that is sufficient to trigger Section 15(a)(1)'s registration requirement"). Mason also continued to meet with his former customers and clients at LPL's offices. As Makkai explained, Mason decided whether to invite Makkai based on Mason's assessment of their financial needs. Mason thus essentially prescreened customers to determine their potential interest in buying or selling securities. *See Brumberg, Mackey & Wall, P.L.C.*, 2010 SEC No-Act. 406, at *4 (denying no action relief to an unregistered broker-dealer after observing that their introduction of only those persons with a potential interest in investing in an issuer's securities implied that they would be "pre-screening" or "pre-selling" investors). Finally, Mason directed Makkai to reverse at least one securities transaction effected for Mason's former LPL brokerage customers. This position of influence over Makkai's securities activities served to trigger the requirement that Mason be registered as a broker-dealer. *See Herbruck, Alder & Co.*, 2002 SEC No-Act. LEXIS 598, at *4-5 ("[Registration] not only encompasses the individual who directly takes a customer's order for a securities transaction, but also any other person who acts as a broker with respect to that order,

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3. The Hearing Officer Did Not Abuse His Discretion by Excluding an Affidavit from the Record

In his appeal briefs, Makkai argues that the Hearing Officer erred by excluding from the record an affidavit signed by Mason, which Makkai claims is evidence of their "bona fide contract." We review the Hearing Officer's exclusion of the affidavit for abuse of discretion.[36] *See Dep't of Enf't v. Weinstock*, Complaint No. 2010022601501, 2016 FINRA Discip. LEXIS 34, at *37 (FINRA NAC July 21, 2016). We conclude that the Hearing Officer did not abuse his discretion here.

"[I]t is well-established that hearsay evidence is admissible in administrative proceedings and can provide the basis for findings of violation, regardless of whether the declarants testify." *Scott Epstein*, Exchange Act Release No. 59328, 2009 SEC LEXIS 217, at *46-47 (Jan. 30, 2009), *aff'd*, 416 F. App'x 142 (3d Cir. 2010). In determining whether to rely upon hearsay evidence, it is necessary to evaluate its probative value, reliability, and fairness of use. *Charles D. Tom*, 50 S.E.C. 1142, 1145 (1992). Factors to consider in this respect include the possible bias of the declarant, the type of hearsay at issue, whether the statements are signed and sworn, whether the statements are contradicted by direct testimony, whether the declarant was available to testify, and whether the hearsay is corroborated. *Id.*

In justifying the exclusion of Mason's affidavit, the Hearing Officer appropriately considered its probative value, reliability, and fairness of use in the context of this hearing. The Hearing Officer concluded that it would be unfair to allow Makkai to offer the affidavit into evidence because Makkai did not show that Mason was unavailable to testify. Makkai rationalized the use of the affidavit because Mason's attorney represented that Mason did not wish to testify in any future FINRA proceedings. As the Hearing Officer found, however, Makkai did not establish that Mason was not available to testify, but rather, he simply did not want to testify in a FINRA proceeding. Given that Mason was earlier barred from associating with any FINRA member for refusing to provide documents and testimony to FINRA, we agree with the Hearing Officer's conclusion that it would be unfair to allow Makkai to use Mason's affidavit as evidence without Enforcement having the opportunity to cross-examine Mason about its contents. *Cf. Pouhova v. Holde*r, 726 F.3d 1006, 1015-16 (7th Cir. 2013) (finding it

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such as the employer of the registered representative or any other person in a position to direct or influence the registered representative's securities activities."); *1st Glob. Inc.*, 2001 SEC No-Act. LEXIS 557, at *5-6 (same).

[36] Makkai also argues that the Hearing Officer erred by excluding an affidavit prepared by an attorney who Makkai engaged after LPL discovered he had paid securities transaction-based compensation to Mason. Because Makkai raises this argument for the first time in his reply brief, we decline to entertain it in this decision. *See Robbi J. Jones*, Exchange Act Release No. 91045, 2021 SEC LEXIS 241, at *7 n.17 (Feb. 2, 2021) (explaining that arguments raised for the first time in a reply brief are waived).

fundamentally unfair for a proponent of evidence to make no effort to call an available witness and rely instead on that witness's hearsay affidavit, thus denying the opposing party a reasonable opportunity to cross-examine the witness).

V. Sanctions

The Hearing Panel fined Makkai $2,000 and suspended him from associating with any FINRA member in any capacity for 10 business days. After an independent review of the record, and careful consideration of the FINRA Sanction Guidelines ("Guidelines"), we modify the Hearing Panel's sanctions.[37]

There are no specific Guidelines that address violations of FINRA Rule 2040. We therefore refer to the Guidelines for registration violations, which we conclude, like the Hearing Panel, are most analogous for the purpose of assessing sanctions for the misconduct that confronts us.[38] *See Silver Leaf*, 2020 FINRA Discip. LEXIS 36, at *69 (finding the Guidelines for registration violations under FINRA Rules 2010 and 1122 most analogous for purposes of assessing sanctions under the predecessor rule to FINRA Rule 2040). The Guidelines for registration violations instruct adjudicators to consider imposing a fine of $2,500 to $77,000.[39] For individual respondents, these Guidelines further instruct adjudicators to consider suspending the individual in any or all capacities for up to six months, or in egregious cases, a lengthier suspension of up to two years or a bar.[40]

Applying the Guidelines to this case, we disagree with the Hearing Panel's decision to consider several factors mitigating for the purpose of justifying the sanctions it imposed. First, we disagree with the Hearing Panel's conclusion that Makkai's conduct was simple negligence. Reckless conduct includes "a highly unreasonable omission, involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known . . . or is so obvious that the actor must have been aware of it." *Sundstrand Corp. v. Sun Chem. Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977). In other words, reckless conduct is conduct that "departs so far from the standards of ordinary care that it is very difficult to believe the [actor] was not aware of what

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[37] *FINRA Sanction Guidelines* (Oct. 2021), https://www.finra.org/sites/default/files/2022-09/2021_Sanctions_Guidelines.pdf [hereinafter *Guidelines*]. Under FINRA Rule 9348, the NAC may affirm, modify, increase, or reduce any sanctions, or impose any other fitting sanction.

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

[39] *Guidelines*, at 45.

[40] *Id.*

he was doing." *First Commodity Corp. v. CFTC*, 676 F.2d 1, 6-7 (1st Cir. 1982). We conclude that Makkai acted, at a minimum, recklessly under the facts presented.[41]

The Hearing Panel based its finding of Makkai's negligence on Makkai's "credible" belief that he was simply using the commissions LPL paid him to buy Mason's book of business. Makkai's good faith belief in his actions, however, must be considered with all the other evidence of knowledge or recklessness because the reasonableness, and therefore the credibility, of that claim of good faith must be evaluated considering the circumstances of each case and in light of the conduct expected of a reasonable person. *Alvin W. Gebhart, Jr.*, Exchange Act Release No. 58951, 2008 SEC LEXIS 3142, at *34 (Nov. 14, 2008). We therefore test Makkai's belief that he was acting in good faith by reference to objective criteria. *See id.* at *35.

The record shows that Makkai knew prior to making any payments to Mason that LPL's policies, which referenced FINRA Rule 2040, prohibited the sharing of commissions or other securities transaction-based compensation with any unregistered person absent prior written approval from LPL. Makkai nevertheless did not disclose to anyone at LPL that he was paying Mason commissions that LPL paid Makkai for securities transactions effected for the accounts of Mason's former LPL brokerage customers. Moreover, when Makkai asked his supervisor in late 2017 or early 2018 whether he could pay Mason commissions Makkai earned from these accounts, the supervisor informed Makkai that he was not permitted to share securities transaction-based compensation with an unregistered person, and that he could make payments to Mason under a final, written contract for the purchase of Mason's book of business that was approved by LPL only.[42] Makkai nevertheless ignored his supervisor's unequivocal response, and continued to pay Mason commissions that Makkai was receiving from LPL. Lastly, Makkai knew that his payments to Mason were improper based on warnings that Makkai received after submitting a written agreement under which he had agreed to purchase another registered representative's book of business. LPL's Strategic Business Solutions group specifically notified Makkai that he could not share commissions earned from LPL brokerage accounts with the registered representative after the representative's "license termination." Makkai admitted that he was concerned, based on this information, that his payments to Mason were not "correct," and he recognized he would "probably need to adjust" his agreement with Mason accordingly. Makkai, however, never sought to make any adjustments to his conduct, and he did not seek or receive any additional guidance or approval from LPL. Instead, Makkai continued to make commissions payments to Mason after receiving cautionary guidance concerning their impropriety.[43] Given the record that confronts us, we conclude that Makkai must have known

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[41] *Cf. Joseph Abbondante*, 58 S.E.C. 1082, 1104 (2006) (affirming the NAC's authority to review a Hearing Panel's findings concerning scienter), *aff'd*, 209 F. App'x 6 (2d Cir. 2006).

[42] *See Guidelines*, at 8 (Principal Considerations in Determining Sanctions, No. 14).

[43] Makkai admitted that he never told his supervisor that he was paying Mason commissions earned from LPL brokerage accounts. Makkai assumed rather that, "if it was important to him," the supervisor would have asked him questions concerning the specifics of the payments he was making. Because the supervisor never asked those questions, Makkai "just

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that his conduct represented an extreme departure from the standards of ordinary care that presented an obvious risk that his payments to Mason were improper, and that he thus, at a minimum, acted recklessly.

Second, unlike the Hearing Panel, we do not find it mitigating that LPL dismissed Makkai for the same misconduct in which we find he engaged here.[44] To receive mitigation for a member's prior termination of the respondent based on the same misconduct, the respondent has the burden to show that the member's termination of the respondent has materially reduced the likelihood of future misconduct by the respondent.[45] In this respect, we have found prior termination by a member mitigating when a respondent has expressed true remorse and made credible assurances against future misconduct. *See Dep't of Enf't v. Doherty*, Complaint No. 2015047005801, 2020 FINRA Discip. LEXIS 29, at *17 (FINRA NAC June 15, 2020) (citing *Dep't of Enf't v. Doni*, Complaint No. 2011027007901, 2017 FINRA Discip. LEXIS 46 (FINRA NAC Dec. 21, 2017)).

We find the record here falls short of evidence showing that Makkai has expressed true remorse for his actions and provided credible assurances that he will not engage in similar misconduct in the future.[46] *See Doherty*, 2020 FINRA Discip. LEXIS 29, at *17-18 ("Doherty

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figured it was okay [to pay Mason commissions]." Makkai's belief that his supervisor's silence permitted him to continue paying Mason commissions is disingenuous and inconsistent with the proactive efforts to ensure compliance that are contemplated under FINRA Rule 2040. Supplementary Material .01 to FINRA Rule 2040 provides guidance to member firms that are uncertain as to whether an unregistered person may be required to be registered under Section 15(a) of the Exchange Act by reason of receiving payments from the member firm and the activities related thereto. Members may derive support for their determination, which must be reasonable, by relying on previously released releases, no action letters, or interpretations from Commission staff that apply to the facts or circumstances; seeking a no-action letter from Commission staff; or obtaining a legal opinion from independent, reputable counsel with knowledge in the area. Mason did none of these things.

[44] *See id.* at 5 (General Principles Applicable to All Sanction Determinations, No. 7 ("Where appropriate, Adjudicators should consider . . . previous corrective action imposed by a firm on an individual respondent based on the same conduct.")).

[45] *Id.*

[46] The Hearing Panel found credible Makkai's belief that "he did not feel he was fairly entitled to keep the commissions so long as he and [Mason] were still negotiating the terms of the contract." Although we defer to the Hearing Panel's credibility determinations, *John Edward Mullins*, Exchange Act Release No. 66373, 2012 SEC LEXIS 464, at *35 (Feb. 10, 2012), we find that Makkai's claim that he believed it was unfair for him to keep the commissions he was earning from the accounts of Mason's former LPL brokerage customers does not establish either his remorse or his assurance that he will not engage in future wrongdoing.

has not demonstrated, and the record does not show, that BGC's termination of him has materially reduced the likelihood that he will engage in future misconduct."). Our independent review of the record shows that Makkai has taken no responsibility for his misconduct.[47] He instead has repeatedly blamed LPL and his supervisor for not informing him that he could not pay Mason securities transaction-based compensation while Makkai and Mason negotiated a formal purchase and sale agreement for Mason's book of business. In his view, his dismissal by LPL was unwarranted and LPL should be held responsible for not preventing his acts of misconduct. We reject these blame-shifting arguments. *See Abbondante*, 58 S.E.C. at 1114. We conclude that Makkai's attempts to blame others for his misconduct calls into question whether he appreciates the seriousness of his misconduct and his responsibility to comply with high standards of commercial honor. *See Edward S. Brokaw*, Exchange Act Release No. 70883, 2013 SEC LEXIS 3583, at *44-45 (Nov. 15, 2013).

We therefore conclude that a fine and period of suspension greater than those imposed by the Hearing Panel are appropriate in this case. While the record does not show that any customers were harmed because of Makkai's FINRA rule violations, we do not believe that the sanctions the Hearing Panel imposed capture the seriousness of Makkai's misconduct.[48] The Exchange Act's registration requirements work to regulate the conduct of persons who receive securities transaction-based compensation and to protect against the types of abusive sales practices that can occur in an unregulated environment. They help to ensure that individuals, like Mason, who possess a "salesman's stake" in securities transactions operate according to the standards of conduct that govern the activities of broker-dealers and their associated persons for the purpose of protecting customers. By violating FINRA Rule 2040, Makkai deprived customers of these important protections and exposed them to the potential for abusive sales practices. The potential for abuse was apparent and of particular concern here because Makkai shared commissions with a person he knew LPL had dismissed for customer-related misconduct. In light of this, we depart from the Hearing Panel's decision and find it aggravating in this case that Makkai paid Mason a significant amount of securities transaction-based compensation on several occasions over an extended period of several months.[49]

In sum, we fine Makkai $5,000 and suspend him from associating with any FINRA member in any capacity for a period of 30 calendar days.

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[47] *See Guidelines*, at 7 (Principal Considerations in Determining Sanctions, No. 2).

[48] Absence of customer harm is not a mitigating factor for sanctions. *See Coastline Fin., Inc.*, 54 S.E.C. 388, 396 (1999).

[49] *See Guidelines*, at 7-8 (Principal Considerations in Determining Sanctions, Nos. 8, 9, 17).

VI. Conclusion

We find that Makkai violated FINRA Rules 2040 and 2010 by paying securities transaction-based compensation to an unregistered person. For this misconduct, we fine Makkai $5,000 and suspend him for a period of 30 calendar days from associating with any FINRA member in any capacity. Finally, we affirm the Hearing Panel's order that Makkai pay hearing costs of $5,565.38, and we impose appeal costs of $1,555.02.[50]

On behalf of the National Adjudicatory Council,

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Jennifer Piorko Mitchell,
Vice President and Deputy Corporate Secretary

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[50] Pursuant to FINRA Rule 8320, any member that fails to pay any fine, costs, or other monetary sanction imposed in this decision, after seven days' notice, will summarily be suspended or expelled from membership for non-payment. Similarly, the registration of any person associated with a member who fails to pay any fine, costs, or other monetary sanction, after seven days' notice in writing, will summarily be revoked for non-payment.