BEFORE THE NATIONAL ADJUDICATORY COUNCIL

FINANCIAL INDUSTRY REGULATORY AUTHORITY

In the Matter of Department of Enforcement, Complainant, vs. Aon D. Miller Chattanooga, TN, Respondent.	DECISION Complaint No. 2012034393801 Dated: May 23, 2018

Respondent participated in private securities transactions without providing written notice to his firm. Held, findings affirmed, sanctions modified.

Appearances

For the Complainant: Margery Shanoff, Esq., David Monachino, Esq., Department of Enforcement, Financial Industry Regulatory Authority

For the Respondent: Donald J. Aho, Esq., David Barnes, Esq., Miller & Martin, PLLC

Decision

Aon D. Miller appeals an Extended Hearing Panel decision issued on December 18, 2015. The Extended Hearing Panel found that Miller participated in five private securities transactions without providing the required prior written notice to his firm, in violation of NASD Rule 3040 and FINRA Rule 2010. For his misconduct, the Extended Hearing Panel suspended Miller from association with any FINRA member in all capacities for two years and fined him $50,000.

Miller does not dispute that he did not give his employing member firm prior written notice as required under NASD Rule 3040. He also does not challenge that the investments were securities and thus subject to the rule. Rather, Miller argues that he did not participate in the transactions at issue and therefore was not required to provide notice under NASD Rule 3040. After our independent review of the record, we affirm the Extended Hearing Panel's findings of violation against Miller with respect to the private securities transactions, but we reduce the sanctions imposed.

I. Background

Miller entered the securities industry in 1998. He worked at several brokerage firms before he associated with Benjamin F. Edwards & Company, Inc. ("BFE" or "Firm"), a FINRA member firm, as a general securities representative in July 2011. BFE terminated Miller's employment in October 2012. His most recent association with a FINRA member firm ended in April 2013. Currently, Miller is a registered investment adviser at an investment advisory firm that he owns.

II. Procedural History

On October 12, 2012, and subsequently on January 11, 2013, BFE filed a Uniform Termination Notice for Securities Industry Registration ("Form U5") disclosing that Miller violated its procedures on outside business activities and private securities transactions. A FINRA investigation ensued.

On September 10, 2014, the Department of Enforcement ("Enforcement") filed an amended complaint alleging a single cause of action. It alleged that, from April to September 2012, Miller participated in five private securities transactions involving three separate issuers in which four customers collectively invested $1,550,000 without Miller providing prior written notice to the Firm, in violation of NASD Rule 3040 and FINRA Rule 2010.[1] During a four-day hearing, the Extended Hearing Panel heard testimony from eight witnesses, including Miller, and found that Miller engaged in the misconduct, as alleged. This timely appeal followed.

III. Facts

A. The CDP Transactions (Issuer No. 1)

CDP was a commercial real estate investment firm founded by SW, a childhood friend of Miller's, and two other principals, GR and JS1. Around September 2011, SW sought Miller's assistance in raising capital and obtaining investors for CDP. Miller provided SW sample offering documents of another investment fund to assist with CDP's business strategy. SW and Miller also met at BFE's office individually in September 2011, and together with Miller's supervisor, William Petty, in October 2011 and March 2012, to discuss CDP as a potential investment opportunity.

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[1] This decision discusses the conduct rules in effect when the conduct occurred. After the relevant period in this case, NASD Rule 3040 was superseded by FINRA Rule 3280. *See Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Adopt FINRA Rule 3280 (Private Securities Transactions of an Associated Person)*, Exchange Act Release No. 75757, 2015 SEC LEXIS 3471 (Aug. 25, 2015).

Shortly after the March 2012 meeting, Miller forwarded materials on CDP to the Firm's product review committee and requested the Firm's approval to serve as CDP's selling agent.[2] In a March 27, 2012 email to the product review committee, Peter Biebel, vice president of alternative products and strategies and a member of the product review committee, reviewed the CDP investment proposal and recommended that the committee reject selling CDP as a Firm product.[3] Biebel also suggested to the committee that if Miller and Petty wished to invest in CDP themselves, they should properly document the transaction as an outside investment in accordance with Firm procedures by contacting the Firm's compliance group. Biebel additionally recommended that Miller and Petty "be reminded of the restrictions on soliciting their clients and prospects on outside investments."

On or about that day, the product review committee unanimously voted that BFE would not serve as CDP's selling agent, and that Miller and Petty could not solicit or recommend sales but could seek the Firm's approval to invest in CDP personally so long as they followed the Firm's procedures.[4]

Biebel verbally communicated the product review committee's decision to Miller and Petty around March 27, 2012. Biebel testified that he informed Miller via a phone call that the product review committee determined CDP "would not be an approved product," but if Miller wanted to invest in CDP, then he would have to follow BFE's policies and procedures. Biebel also testified that he reminded Miller that he could not solicit any Firm customers to invest in CDP.

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[2] BFE had a product review committee that determines whether the Firm will offer and sell a security.

[3] According to Biebel, CDP was similar to, and potentially more inferior than, other private real estate investment trusts ("REITs") that the Firm had previously reviewed and rejected because of CDP's high costs relative to its size, dependency on outside commercial real estate developers, and inability to accurately reflect a limited partner's current capital commitment or market value of the partnership units.

[4] BFE's written policies and procedures required associated persons to obtain prior written approval from the compliance department before participating in a private securities transaction "regardless of whether or not the activity is done for compensation or whether the associated person receives compensation." The Firm also expressly prohibited its registered representatives from raising money or capital for any investments or investment programs, distributing unauthorized sales materials, or acting as an agent, or arranging a transaction, for any limited partnership or other security without BFE's written consent.

On April 18, 2012, Miller executed CDP's promissory note, subscription agreement and partnership agreement and invested $50,000 in CDP. Miller did not, however, provide BFE with the requisite notice or obtain written approval beforehand.[5]

In addition to his own CDP investment, Miller continued to assist CDP's principals in marketing CDP to potential investors. Miller opened an account on behalf of CDP at the Firm on or about May 1, 2012, for the deposit of invested funds. Shortly after SW and Miller met to discuss CDP, SW emailed Miller promotional materials on May 30, 2012, instructing Miller that they were "for those who want to quickly get a sense of our business." In that email, SW also promised to send Miller additional materials on CDP. The next day, SW told Miller in an email that JS1 was going to send SW and Miller to "his place in Cabo since [Miller was] helping us so much," to which Miller replied: "Sounds good to me."

As further evidenced in the transactions detailed below, Miller also reached out to BFE customers—all sophisticated wealthy individuals—on SW's behalf. Miller sent the customers CDP promotional materials and recommended that they invest a specified amount in CDP. Miller also provided SW with status updates of his communications with potential investors.

1. Customer JH (Transaction No. 1)

JH was a BFE customer and Miller's close family friend. JH also knew two of the CDP principals, SW and GR, for many years. JH first learned of CDP at a golf game through JS1, a CDP principal whom JH did not know very well. Shortly after the golf outing, SW emailed Miller on June 11, 2012, stating that JS1 thought JH would be interested in hearing more about CDP and asking Miller how SW should proceed. That same day, Miller replied stating: "I will call [JH]. Will update you after I hear from [JH]." On the next day, Miller reported to SW by email that he spoke with JH. Miller also stated that he was "mailing [JH] the package today," followed by "I told [JH] that he should give you a couple hundred K."

JH testified at the hearing that he discussed CDP with Miller. He considered Miller to be his investment adviser in whom he had confidence and stated that it was not unusual for him to discuss outside investments with Miller. JH wanted Miller's opinion about JS1's work history. JH also discussed with Miller how much money he should invest in CDP.

In an email dated July 12, 2012 to SW, Miller stated: "I am going to recommend that [JH] invest tonight," and Miller promised to keep SW updated. On the next day, Miller informed SW that he discussed CDP with JH, and stated: "[JH] has a note coming due in a couple of weeks which is an IRA with me. I suggested he take those proceeds and invest with you. He said he will more than likely do 1 to 2 units. Good news." JH invested $100,000 in CDP.

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[5] SW, on behalf of CDP, countersigned Miller's executed documents on May 11, 2012. Miller did not send the money for his CDP investment, however, until September 2012.

2. Customer KJ (Transaction No. 2)

KJ was also a BFE customer and Miller's long-time close friend. KJ first learned of CDP through SW—a good friend of his for 35 years. KJ initiated a discussion about CDP with Miller in an email dated May 30, 2012, by stating: "Have you had [SW]'s pitch on a private equity fund focused on real estate financing for small to mid size deals . . . I am considering putting $100-200K in . . . he has raised $3-4MM, looking for total of $10MM." KJ testified at the hearing that he emailed Miller about CDP "to see if it would fit in [his] portfolio."

On the same day, Miller replied by email that he reviewed the CDP deal "Very closely." Miller then informed KJ that he already signed the CDP offering documents and invested $50,000. Miller further remarked that CDP was a good investment, stating: "It is a solid income play with upside as you mentioned." He then endorsed one of the CDP promoters, GR, by stating that he was "tight as a tick" who "WILL NOT lose a penny," while offering his views on the other CDP principals.

KJ testified at the hearing that he valued Miller's opinion "like any stockbroker" and wanted his thoughts on CDP before he invested. KJ also testified that Miller's thoughts did factor into his decision to invest in CDP but maintained that the ultimate decision to purchase CDP as an investment was his own—and not Miller's. KJ invested $200,000 in CDP.

3. Customer WR (Transaction No. 3)

WR, another BFE customer, previously had worked with the CDP principals in other business ventures. WR first learned of CDP through SW, who contacted him about investing. WR thereafter emailed Miller on August 29, 2012, and asked his thoughts on CDP, including whether it would be a good investment for his mother-in-law, to which Miller replied: "Let's talk. When are you available?"

A couple of days before WR's August 29 email, SW emailed Miller, informing him that WR and WR's mother-in-law were potentially interested in investing in CDP and that WR was planning to call Miller to discuss the CDP investment. SW closed his email by asking for Miller's endorsement by stating: "Would appreciate a good word for us." Miller responded: "Of course. I will go over it with [WR] as well." WR testified that he did discuss the CDP investment with Miller and that, at some point during their discussion, Miller told him that he was investing in CDP. WR invested $50,000 in CDP.

B. The KBI Transaction (Issuer No. 2)

KG is the owner of KBI, a specialty chemical company that focused on the development and sale of drilling fluids for the excavation of foundations worldwide. Around May 2012, KG contacted Miller initially for his assistance in finding investors for KBI's sale of Class B membership units, and later for KBI's marketing of a short-term note.

On May 10, 2012, KG emailed Miller KBI's offering materials, including a confidential private placement memorandum, operating agreement and subscription agreement. Miller responded to KG's email on May 20, 2012, stating that he reviewed the offering materials and that: "I do have a number of clients who fit the profile and might be interested. . . . How would you like to proceed?" KG and Miller thereafter met and discussed the KBI offering.

On May 23, 2012, KG emailed another KBI disclosure document for Miller's use to solicit investors—a confidential information brochure that KG referred to as "a little simpler and suited for investors to review." That same day, Miller emailed the confidential information brochure to JS2, a sophisticated customer and shareholder of BFE and very close friend, and stated: "Take a look at this. It is [KG]'s deal. He approached me about it. Let's discuss briefly at your convenience."

JS2 testified that Miller contacted him about investing in KBI and that KG "was looking for money." JS2 described Miller's involvement in the KBI transaction as "[h]e was like a conduit." JS2 also testified that he may have asked Miller about KG's background, including whether "[KG] had been in trouble," to determine whether to proceed with the transaction. Had Miller stated that KG was in trouble, JS2 testified that he would not have invested in KBI.

On June 4, 2012, Miller updated KG that he would be meeting with JS2 to review and discuss the KBI offering and stated: "I thought we should give him first option. . . . I will update you if I [hear] anything from him before. I did email everything to him."

Shortly thereafter the terms of the KBI offering changed. On June 12, 2012, KG informed Miller by email that he was having difficulty raising capital and had an immediate need for a cash infusion to buy raw materials. He attached an offering term sheet addressed "To: INVESTORS" with the subject line "KB Loan Offering" in which KBI was offering to pay a five percent "fee" in exchange for a four-month promissory note of $200,000, guaranteed by a first lien on the company's inventory. That same day, Miller forwarded KG's email and attachment to JS2 and stated: "This doesn't look like a bad deal!" Miller admitted at the hearing that he discussed with JS2 the offering terms of the note, including the interest rate, and also discussed KG's character as a principal of KBI.

The next day, KG emailed Miller a completed promissory note in the amount of $200,000 for JS2's signature and wire instructions for the funds. Miller promptly forwarded KG's email and the attached promissory note to JS2 and stated: "Here is [KG]'s deal." JS2 invested $200,000 in KBI.

C. The CTL Transaction (Issuer No. 3)

Before joining BFE, Miller was a limited partner in an investment limited partnership, LMP, along with customer JS2.[6] Miller disclosed LMP as an outside investment when he joined the Firm and the Firm approved it. On JS2's behalf, Miller listened in on conference calls that provided updates on LMP's performance and Miller would often send his thoughts—along with any materials that LMP provided—to JS2. Miller testified that he considered this as "providing good customer service" to JS2. JS2 testified that there were a couple of people that he liked to "run stuff by . . . just to get their opinions" and to see if they would invest themselves.

On July 31, 2012, LMP's director of operations, KH, sent an email seeking interest from its limited partners in an "investment opportunity." LMP was in the process of refinancing the outstanding debt of CTL, "a specialty finance company specializing in asset-backed loans to individuals secured by an automobile title." Attached to KH's email seeking potential investors were CTL's financing summary, loan and security agreement, and a secured promissory note paying 16 percent per annum until the maturity date of April 1, 2015.

On August 5, 2012, Miller responded to KH's email stating that he was unable to invest in CTL, but that he would "follow up with [JS2] and check on his interest." Miller and JS2 thereafter discussed the CTL investment. JS2 testified that he asked what Miller thought about CTL as an investment and whether Miller was going to invest.

On August 6, 2012, Miller sent JS2 an email highlighting CTL's 16 percent interest rate and stating, "I spoke with them this morning about the details. This is not a bad deal." Miller also attached a couple of the pages from the CTL financing summary, and circled and starred the phrase "The Loan Agreement provides for 16% annual interest."

On August 8, 2012, JS2 asked Miller what additional information he found regarding the CTL investment. The next day, Miller responded: "I like this if you're looking for a 2-3 year (Max) income play. Your capital is very safe/low risk. I will explain the 16% this morning." Miller thereafter reached out to LMP on JS2's behalf and asked more questions about the CTL investment. On August 10, 2012, LMP's managing partner sent Miller an email summarizing key points of the CTL investment, and Miller forwarded that email to JS2 with a recap of the investment terms.[7]

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[6] Upon joining BFE, Miller disclosed and requested approval on the Firm's Outside Accounts form to hold membership interests in LMP and another private equity fund away from the Firm. BFE approved Miller's request.

[7] That same day, KH sent another email on behalf of LMP to its limited partners. She stated that LMP had received "significant interest" to move forward with the CTL financing among the limited partners. She also attached financing documents, including CTL's secured promissory note. Both Miller and JS2 received KH's email and the CTL financing documents.

Several days later, Miller asked JS2 whether they still needed to discuss the CTL investment, to which JS2 replied by email: "Yes, I want to do it all if it meets with your approval." Miller thereafter stated that he wished that he could invest personally, that the investment has a "solid/VERY low risk income play" and that "It makes sense for you and the [] Family in my opinion." On August 20, 2012, JS2 confirmed his desire to invest in CTL stating to Miller: "Tell them I'll take it all or a large portion. I don't want to bother with a small amount." The next day, Miller reported to JS2: "[LMP has] $1MM remaining. I told them to hold it for you."

JS2 testified that Miller facilitated communications with LMP on his behalf because Miller knew the "LMP guys" more than he did and the money used to purchase CTL was coming out of his BFE account. When Miller told JS2 that CTL had an investable amount of $1 million remaining, JS2 asked Miller for his thoughts and whether he had "collateral" to make the CTL investment, to which Miller responded on August 23: "My recommendation would be $1MM. You personally have $10MM in collateral." JS2 testified that the term "collateral" referred to the amount of funds JS2 had available to invest in CTL.

On August 24, 2012, Miller emailed KH confirming that JS2 would invest $1 million in CTL, stating "We are going to do a $1MM to start. I will start the paperwork on Monday." On August 29, 2012, KH sent to Miller the CTL forms for JS2 to complete, including a lender information sheet, the signature page of the loan and security agreement, and wire instructions. The next day, Miller forwarded KH's email to staff at the Firm asking that they send the CTL documents to JS2's assistant, DL. JS2 invested $1 million in CTL.

D. BFE's Investigation of Miller's Unauthorized Participation in Private Securities Transactions

In September 2012, Miller discovered that he owed a two percent upfront fee on his $50,000 CDP investment made in April 2012. On September 18, 2012, Miller attempted to deposit a $1,000 check in the CDP account at BFE. He gave his check to an assistant branch manager, Julie Wilson, who refused to make the deposit until Miller completed the appropriate form requesting the Firm's approval of his outside investment. That same day, Miller completed an "Outside Activity Approval Request Form" on which he indicated that he invested in CDP on September 15, 2012. Wilson sent Miller's request form, along with his executed subscription agreement dated several months prior in April 2012, to the Firm's compliance group. The inconsistent transaction dates prompted the Firm's internal investigation.

Jane Matoesian, BFE's vice president and managing counsel, investigated whether Miller had potentially engaged in an unauthorized private securities transaction. She interviewed Miller on three separate occasions. Primarily focused on CDP, Miller admitted to Matoesian that he discussed the CDP investment with a number of customers. Miller also explained that he did not think there was anything wrong with him telling people that he personally invested in CDP. Miller also admitted that he told potential investors that the principals of CDP were good guys and that he thought CDP was a good deal.

The Firm determined that Miller participated in private securities transactions without following its procedures. The Firm terminated Miller on October 2, 2012, for his violation of Firm procedures.

E. Customer Sworn Affidavits Disavow Miller's Participation in the Securities Transactions

After Miller's termination, Matoesian interviewed 13 individuals, including BFE customers who had invested in CDP. At the hearing, Matoesian explained that, from the Firm's standpoint, the Firm had incurred the risk that these investors believed BFE had sponsored or was otherwise involved with the CDP transactions. Matoesian drafted affidavits for some of the individuals she spoke with and obtained their signatures. The affidavits generally absolved the Firm of any responsibility in connection with the CDP investment. The affidavits acknowledged that their CDP investment had nothing to do with the Firm or any of its current or former representatives, including Miller. The affidavits also stated that the undersigned made an independent decision whether to invest in CDP and understood that BFE had no involvement with CDP.

Miller's counsel also obtained sworn affidavits from the four customers who invested in the transactions at issue. The affidavits generally provided the customer's background, level of investment experience, and their relation to Miller. They also stated that, based on their personal knowledge, Miller did not solicit the customer to invest and that the customer was aware that neither Miller nor BFE had anything to do with their respective transaction or their decision to invest.[8]

IV. Discussion

The Extended Hearing Panel found that Miller participated in the five private securities transactions charged, in violation of NASD Rule 3040 and FINRA Rule 2010. On appeal, Miller does not challenge whether the transactions at issue involved securities. He also admits that, for each private securities transaction, he failed to provide BFE prior written notice as required by the rule. Miller argues instead that, based on the standard of participation articulated in *James W. Browne*, Exchange Act Release No. 58916, 2008 SEC LEXIS 3113, at *30 (Nov. 7, 2008), his activities did not cause or effect a particular transaction and thus he committed no rule violation. After careful consideration of the evidentiary record, we affirm the Extended Hearing Panel's findings of violation with regard to the five private securities transactions.

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[8] Miller's counsel also obtained a written declaration from KH. It explained that LMP understood that any communication made by Miller regarding CTL was either in his capacity as an LMP limited partner or as JS2's friend, and not in his capacity as a BFE registered representative. The affidavit also stated that LMP did not at any time "ask, encourage, or expect" Miller "to solicit, or encourage [JS2] to make a loan to [CTL]."

A. The CDP Units, and KBI and CTL Promissory Notes, Were Securities

Miller has admitted, and we accordingly find, that CDP sold securities. The Supreme Court in *SEC v. W.J. Howey Co.* explained that a product is an investment contract and therefore a "security" under Section 3(a)(10) of the Securities Exchange Act of 1934 ("Exchange Act") if: (1) there is an investment of money, (2) in a common enterprise, (3) with the expectation of profits produced by the efforts of others. 328 U.S. 293, 301 (1946). Applying the *Howey* test, we find that CDP, through its sale of limited partnership units, pooled investor funds to invest in commercial real estate projects that a general partner managed. The CDP limited partners invested their money in a common business enterprise with a reasonable expectation of receiving a profit solely through the managerial efforts of others. *See SEC v. Murphy*, 626 F.2d 633, 640-41 (9th Cir. 1980) ("[A] limited partnership generally is a security . . . because, by definition, it involves investment in a common enterprise with profits to come solely from the efforts of others.") (citations omitted). We therefore find that the CDP units were investment contracts and thus securities.

We also determine that the KBI and CTL promissory notes were securities. The Exchange Act also defines a "security" to include "any note," except notes with maturities of less than nine months. *See* 15 U.S.C. § 78c(a)(10). The Supreme Court in *Reves v. Ernst & Young*, 494 U.S. 56 (1990), adopted the "family resemblance" test, along with four factors, to consider in determining whether a note is a security under Section 3(a)(10) of the Exchange Act.[9] Under the *Reves* test, a note is presumed to be a security and that presumption may be rebutted only by demonstrating that the note bears a strong resemblance (considering the four factors) to one of the enumerated categories of instrument that are deemed as non-securities.[10] If a note is not sufficiently similar to the enumerated categories of non-securities, the family resemblance test requires an examination—based on the same four factors—of whether another category should be added.

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[9] The *Reves* four factors determine whether the transaction nonetheless involves a security by evaluating: (1) the motivations of the buyer and seller (i.e., whether the seller is raising money for general use of a business enterprise and whether the buyer is interested in the profit the note is expected to generate); (2) the plan of distribution (i.e., whether the note is an instrument in which there is a common trading for speculation or investment); (3) the reasonable expectation of the investing public; and (4) the existence of another regulatory scheme that makes oversight by federal securities laws unnecessary. *See Reves*, 494 U.S. at 66-67.

[10] The enumerated non-securities categories are (1) notes delivered in consumer financing; (2) notes secured by a mortgage on a home; (3) short-term notes secured by a lien on a small business or some of its assets; (4) notes evidencing a character loan to a bank customer; (5) short-term notes secured by an assignment of accounts receivable; or (6) notes which simply formalize an open-account debt incurred in the ordinary course of business (particularly if, as in the case of the customer of a broker, it is collateralized). *See id.* at 65 (citing *Exchange Nat'l Bank of Chicago v. Touche Ross & Co.*, 544 F.2d 1126, 1138 (2d Cir. 1976)).

Applying the family resemblance test to the present case, we find that KBI and CTL notes were securities. The KBI promissory notes were short-term, collateralized and secured, and thus appeared similar to one of the enumerated categories (i.e., a short-term note secured by a lien on a small business or some of its assets). In evaluating the KBI and CTL transactions under the *Reves* four factors, however, we have little doubt that the notes were securities. KBI and CTL sold notes for investment purposes and not in commercial or consumer contexts. KBI issued short-term notes to raise capital for its general business operations; and LMP facilitated the issuance of the CTL notes to refinance CTL's outstanding debt and for working capital.

Customer JS2, who purchased the KBI and CTL notes, had no commercial relationship with KBI or CTL. Instead, JS2 entered into the KBI and CTL transactions seeking to earn a profit in the form of interest. The KBI and CTL notes were widely disseminated to interested parties with no apparent limitation on the amount of investors, and the disclosure materials used for solicitation had investing terms such as "investment opportunity," "offering," "attractive risk/return," or "investors." Moreover, the KBI and CTL notes provided its holders a guaranteed interest rate or fee that significantly exceeded any rate paid by local banks or savings and loan associations and thus the investing public reasonably would view them as "securities." *See Stoiber v. SEC*, 161 F.3d 745, 750 (D.C. Cir. 1998) (explaining that notes with a favorable interest rate indicate that profit was the lender's primary goal). Lastly, both the KBI and CTL notes were uninsured and not subject to the federal banking laws and thus would otherwise escape federal regulatory oversight if deemed non-securities. Based on these considerations, we conclude that the KBI and CTL promissory notes were securities. The notes did not bear a strong family resemblance to the notes listed as non-securities, and there is no basis for adding a new category considering the *Reves* factors.

B. Miller Participated in the CDP, KBI, and CTL Private Securities Transactions, in Violation of NASD Rule 3040 and FINRA Rule 2010

NASD Rule 3040 prohibits an associated person from participating in any manner in a private securities transaction without providing prior written notice to his or her employing member firm. *See* NASD Rule 3040(a) and (b). The written notice must describe in detail the proposed transaction, the associated person's role therein, and whether the associated person will receive selling compensation. A "private securities transaction" includes any securities transaction outside the regular course or scope of an associated person's scope of employment with a member. *See* NASD Rule 3040(e)(1). In accordance with the rule, associated persons must provide prior written notice of their participation in a private securities transaction irrespective of whether they will receive selling compensation.[11] There is no evidence that Miller received selling compensation in any of the transactions at issue.

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[11] *See* NASD Rule 3040(c) and (d); *see also* NASD Rule 3040(e)(2). "Selling compensation" includes "any compensation paid directly or indirectly from whatever source in connection with or as a result of the purchase or sale of a security, including though not limited to, commissions; finder's fees; securities or rights to acquire securities; rights of participation in profits, tax benefits or dissolution proceeds, as a general partner or otherwise; or expense reimbursements."

It is well established that the clause "participate in any manner" in NASD Rule 3040 is interpreted broadly to further the regulatory objectives of the rule. *See Siegel v. SEC*, 592 F.3d 147, 158 (D.C. Cir. 2010) ("[T]he purpose of NASD Conduct Rule 3040 is to protect investors from unsupervised sales and securities firms from exposure to loss and litigation."), *aff'g in relevant part*, Exchange Act Release No. 58737, 2008 SEC LEXIS 2459 (Oct. 6, 2008) (internal quotation marks omitted). Activities that constitute participation under NASD Rule 3040 are broader than solicitation. *See Joseph Abbondante*, 58 S.E.C. 1082, 1098-99, *aff'd*, 209 F. App'x 6 (2d Cir. 2006) ("Conduct Rule 3040 is broad in scope and is not limited merely to solicitation of an investment.").

The record establishes that Miller participated in the CDP, KBI, and CTL private securities transactions. For CDP, Miller invested in CDP himself and then assisted the issuer in marketing the investment and finding potential investors. The CDP investments made by the three BFE customers totaled $350,000. Even after BFE instructed Miller not to speak about CDP to any Firm customers, Miller continued to solicit them. Miller facilitated discussions between the CDP principals and customer JH. He mailed the CDP offering "package" to customer JH and recommended that he invest a specified dollar amount. Miller pitched customers KJ and WR by telling them that he had invested in CDP and discussing the merits of the investment. He provided a CDP principal with status updates on communications that he had with potential investors. A CDP principal even offered to send Miller on a trip for his assistance in soliciting CDP. Miller also "put in a good word" by endorsing CDP and its principals to customers JH, KJ, and WR, who ultimately purchased CDP as an investment. Miller's extensive sales activities for CDP undoubtedly violated NASD Rule 3040. *See Mark H. Love*, 57 S.E.C. 315, 320 (2004) (finding a NASD Rule 3040 violation where the associated person, among other things, vouched for the issuer's principal, discussed the validity of the investments, disclosed his own interest in investing, and served as an intermediary between the issuer and customer); *Allen S. Klosowski*, 48 S.E.C. 954, 955 (1988) (finding a NASD Rule 3040 violation where the associated person purchased the investment for his own account and recommended that firm customers purchase a similar investment "because [he] thought it had merit").

For KBI, Miller told KBI's principal that he knew of potential investors who would "fit the profile and might be interested" in investing. Miller reviewed KBI's offering materials and brought KBI as an investment opportunity to customer JS2. JS2 invested $200,000 in KBI. Miller provided JS2 with the offering materials and asked JS2 to discuss the investment. Miller also endorsed KBI as a good deal and gave JS2 a favorable character opinion of KBI's principal. In addition to fielding any questions JS2 had about the transaction, Miller also assisted KBI in processing the transaction, including sending KBI's promissory note and wire transfer instructions to JS2 for his execution. Miller's activities constituted participation in the KBI transaction as defined in NASD Rule 3040. *See Siegel*, 2008 SEC LEXIS 2459, at *12, 18-19 (finding a violation of NASD Rule 3040 where the associated person endorsed the benefits of the investment, assured investors that it looked like a really good deal, and facilitated their purchase of the investment); *Phillipe N. Keyes*, Exchange Act Release No. 54723, 2006 SEC LEXIS 2631, at *6 (Nov. 8, 2006) (finding a NASD Rule 3040 violation where the associated person, among other things, solicited customers with sales literature describing the investment).

Miller also participated in the CTL transaction. Serving as the intermediary between customer JS2 and CTL, Miller communicated with the LMP representatives, obtained further details about the CTL investment, and relayed that information back to JS2. Miller also reviewed CTL's investment documents and sent snippets of the CTL financing summary to JS2, drawing his attention to CTL's favorable interest rate and stating: "This is not a bad deal." When JS2 asked whether he had enough "collateral" in his account to invest in CTL, Miller responded in the affirmative and recommended that JS2 invest in CTL at a specified dollar amount (i.e., the remaining amount on offer). JS2 invested $1 million in CTL. Miller also facilitated the CTL transaction by notifying the LMP representative of JS2's decision to invest in CTL and obtaining the CTL investment "paperwork," including wire transfer instructions, for JS2's execution. Even accounting for the fact that Miller did not initially solicit JS2 with the financing summary, promissory note, and related documents, his actions qualify as participation under NASD Rule 3040. *See Love*, 57 S.E.C. at 320 (finding a NASD Rule 3040 violation where the associated person, among other things, vouched for the character of the issuer's principal and intervened with the issuer on the customer's behalf, even though the associated person received no fee or compensation); *Stephen J. Gluckman*, 54 S.E.C. 175, 183 (1999) (finding that the associated person violated NASD Rule 3040 by recommending the securities transaction and source of funds). Accordingly, we affirm the Extended Hearing Panel's findings that Miller violated NASD Rule 3040.

Miller's primary argument on appeal against his liability is that participation under NASD Rule 3040 is not without limitation and, as the SEC held in *Browne*, 2008 SEC LEXIS 3113, at *26-27, there was no "factual nexus" between his involvement and the transactions charged. We disagree and find *Browne* easily distinguishable.

In *Browne*, two registered representatives introduced customers to the issuer of a software marketing business, e2, in late 1997 and early 1998. The client introductions made by the representatives were for networking and business purposes (i.e., "purposes other than investing"). *Id.* at *5 & n.5. In the spring of 1998, e2 initiated a private offering of its common shares and some of the customers, along with the representatives, purchased e2's stock. The representatives told several people about their investments in e2's common stock, and some invested. The National Adjudicatory Council found that the representatives violated NASD Rule 3040 in connection with the customers' purchases of e2's Series B preferred shares—a subsequent offering that occurred almost two years later. In dismissing the NASD Rule 3040 allegation against the representatives, the SEC held that a preponderance of the evidence must show that (1) a respondent took specific actions to effect a particular transaction, and (2) there was a "reasonably close factual nexus" between the participatory conduct and a specific securities transaction. *Id.* at *30. Finding that there was no factual nexus between the client introductions to e2 and the customers' purchases of the Series B preferred shares two years later, the SEC dismissed the NASD's finding of NASD Rule 3040 liability against the representatives.

The *Browne* decision does not alter our finding that Miller violated NASD Rule 3040. As we described above, a preponderance of the evidence demonstrated the active steps Miller took to effect the CDP, KBI, and CTL transactions, which constituted participation under NASD Rule 3040. Miller's involvement went well beyond generally discussing the issuers' businesses for noninvestment purposes or providing a customer referral, and his activities occurred in close

proximity to the securities transactions.[12] For example, Miller facilitated the CTL private securities transaction by serving as an intermediary and giving a specific recommendation on JS2's $1 million investment. We therefore conclude that a "reasonably close factual nexus" did in fact exist between Miller's participatory conduct and the transactions.

Miller next argues that the Extended Hearing Panel refused to consider evidence—in particular the testimony and affidavits by the customers—that proved his nonparticipation in the transactions. The customers attested that they made an independent decision to invest in their transaction. Customers KJ, JH, and JS2 also testified, however, that Miller's opinions, which they valued and respected, factored in their decisions to invest in the transactions. *See Abbondante*, 58 S.E.C. at 1100 (finding participation under NASD Rule 3040 when respondent's representations about a potential investment influenced the customers' decision to invest); *see also John P. Goldsworthy*, 55 S.E.C. 818, 835 (May 15, 2002) (finding an associated person liable under NASD Rule 3040 even though the purchaser's decision to invest "assertedly resulted from the representations made by third parties").

The Extended Hearing Panel accepted and considered the customers' testimony and affidavits as evidence, but concluded that for a number of reasons the affidavits lacked probative value in determining whether Miller's involvement in the transactions constituted participation under NASD Rule 3040. One reason stated by the Extended Hearing Panel was that the customer affidavits expressed opinions and conclusions, rather than facts. As an example, customer JH's affidavit stated: "At no time during our relationship has [Miller] done anything, either as my friend or as a stockbroker, that I felt was morally, ethically, or legally wrong." Indeed, this statement by Miller's customer and friend represents what JH believed to be true. We agree with the Extended Hearing Panel, however, that JH's statement—no matter how true—has no bearing on whether Miller's involvement in his CDP investment implicated a notice requirement under NASD Rule 3040. *See FTC v. Publ'g Clearing House, Inc.*, 104 F.3d 1168, 1171 (9th Cir. 1997) ("A conclusory, self-serving affidavit, lacking detailed facts and any supporting evidence, is insufficient to create a genuine issue of material fact.").

Moreover, while the Extended Hearing Panel found the customers' testimony to be credible and honest, the Panel declined to rely solely on their representations to make an informed decision about Miller's obligation under NASD Rule 3040 because the customers could not remember important details about Miller's involvement. For example, customer KJ testified that he could not recall whether he had any previous or other communications with Miller about the CDP investment besides his May 30, 2012 email. Customer JH could not recall whether Miller sent him investment materials or recommended CDP, and customer JS2 could not remember how he first learned about KBI's initial offering. We find no error with the Extended Hearing Panel's decision to rely on other documentary evidence in the record to establish

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[12] Miller contends that FINRA's "know your customer" rule obligates him to obtain essential facts about the customer, including discussing outside investments, before making a suitable recommendation. Any required communication with a customer under FINRA Rule 2090, however, does not eliminate Miller's obligation under NASD Rule 3040 to provide written notice to his Firm before participating in any private securities transaction.

Miller's participation instead of concluding that a customer's inability to recall established that an event did not happen. *See Kirlin Sec. Inc.*, Exchange Act Release No. 61135, 2009 SEC LEXIS 4168, at *53 n.71 (Dec. 10, 2009) (entitling the credibility determination of an initial fact finder to considerable weight and deference because "it is based on hearing the witnesses' testimony and observing their demeanor"); *see also Scott Epstein*, Exchange Act Release No. 59328, 2009 SEC LEXIS 217, at *48 (Jan. 30, 2009), *aff'd*, 416 F. App'x 142 (3d Cir. 2010) (finding that customer testimony is not essential if the relevant evidence can be derived from other sources in the record).

Miller argues further that his customers were fully aware that neither he nor the Firm was sponsoring the transactions, and there were no customer complaints about his involvement. We give little weight to his "after-the-fact" claims. First, it is not a defense to this rule violation to claim that customers understood that the Firm did not sponsor the product they purchased when Miller did not have BFE's permission to solicit sales and the Firm did not supervise the transactions. *See Abbondante*, 58 S.E.C. at 1099 n.45 (finding that the customer's knowledge that the investment was not approved by the employing firm is no defense to a Rule 3040 violation). Second, the benefit of following the rule is to limit firms' litigation risk of unsupervised sales activity, both when customers have no complaints about the sales and when they do. Indeed, the absence of customer complaints or Firm and customer losses does not obviate Miller's violation.

Lastly, we reject Miller's claim that the language of NASD Rule 3040 itself is vague and so broad that it fails to provide representatives with fair notice of what constitutes sanctionable conduct. As the SEC has previously held, "[NASD] Rule [3040] gives fair guidance to firms, their associated persons, and NASD decision makers with respect to the types of activities that are subject to its restrictions." *Love*, 57 S.E.C. at 322; *see also NASD Notice to Members 01-79*, 2001 NASD LEXIS 85 (Dec. 2001) (reminding registered persons of their responsibilities regarding private securities transactions). In any event, Miller had actual notice of his NASD Rule 3040 regulatory obligation. BFE explicitly instructed Miller not to communicate with any customers regarding CDP. As BFE's registered representative, Miller also represented in writing that he understood BFE's procedures on private securities transactions, including his duty to report his participation on the Outside Activity Approval Request Form before engaging in any outside investment or transaction.

Miller failed to provide his firm prior written notice of his participation in the private securities transactions as required by NASD Rule 3040. Miller's violation of NASD Rule 3040 also constituted a violation of FINRA Rule 2010, which requires members in the conduct of their business to "observe high standards of commercial honor and just and equitable principles of trade."[13] *See Sirianni v. SEC*, 677 F.2d 1284, 1288 (9th Cir. 1982) (failing to comply with Rule 3040 constitutes conduct inconsistent with just and equitable principles of trade); *Harry Friedman*, Exchange Act Release No. 64486, 2011 SEC LEXIS 1699, at *23 (May 13, 2011)

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[13] FINRA Rule 2010 applies to Miller through FINRA Rule 0140(a), which provides that a person associated with a member shall have the same duties and obligations as a member.

("A violation of a Commission or NASD Rule or regulation also constitutes a violation of [FINRA] Rule [2010].").

V. Sanctions

For Miller's participation in the private securities transactions, the Extended Hearing Panel imposed unitary sanctions of a two-year suspension from associating with a FINRA member in all capacities and a $50,000 fine. Based on our independent review of the record, including weighing both aggravating and mitigating factors, we conclude that the two-year suspension and $50,000 fine that the Extended Hearing Panel imposed are too high.

As discussed more fully below, we modify the sanctions imposed by the Extended Hearing Panel and impose separate, consecutive suspensions for Miller's participation in the CDP and KBI transactions and the CTL transaction. Moreover, we affirm the Extended Hearing Panel's imposition of a fine, but reduce the fine to $25,000. The fine, which is designed to deter future misconduct by Miller and to protect the public interest and investors, is consistent with the FINRA Sanction Guidelines ("Guidelines").[14]

The Guidelines have specific recommendations for selling away violations in addition to the general principles that apply to all sanction determinations.[15] They ask us to consider a fine of $5,000 to $73,000 and a suspension or bar based on the following dollar amount of sales:

- Up to $100,000 in sales: 10 business days to 3 months
- $100,000 to $500,000: 3 to 6 months
- $500,000 to $1,000,000: 6 to 12 months
- Over $1,000,000: 12 months to a bar.[16]

The selling away guideline instructs that the first step in determining sanctions is to "assess the extent of the selling away, including the dollar amount of sales, the number of customers, and the length of time over which the selling occurred."[17] For the CDP and KBI transactions, Miller sold away from BFE in four private securities transactions that, over the course of several weeks, four customers invested a total of $550,000. Based on this level of sales, the Guidelines recommend a suspension ranging from six to 12 months. In the CTL transaction, Miller sold away one private securities transaction in which a single customer invested $1 million. Based on this sales amount, the Guidelines also recommend a suspension range of six to 12 months.

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14 *See FINRA Sanction Guidelines* 14 (2018), https://www.finra.org/sites/default/files/Sanctions_Guidelines.pdf [hereinafter *Guidelines*].

15 *See Guidelines*, at 14.

16 *Id.*

17 *Id.*

The Guidelines next instruct us to consider other factors in determining the most suitable sanction, including the enumerated principal considerations under the selling away guideline, the general principles applicable to all guidelines, and the presence of any mitigating or aggravating factors.[18] The enumerated principal considerations relevant to this case include, but are not limited to: the dollar volume of sales; the number of customers; the length of time over which the selling away activity occurred; whether the product sold away was found to involve a violation of federal or state securities laws or SRO rules; whether the respondent had a proprietary or beneficial interest in, or was otherwise affiliated with, the issuer; whether the respondent attempted to create the impression that his or her employer sanctioned the activity; whether the respondent sold away to customers of his employer; and whether the respondent sold away after being instructed by his firm not to sell the type of product involved.[19]

A. CDP and KBI Transactions

For the CDP and KBI transactions, Miller sold away from BFE in four private securities transactions that totaled $550,000. For these transactions, there were several aggravating factors. BFE explicitly prohibited Miller from soliciting or recommending CDP to any customers.[20] Yet, against the Firm's directives, Miller consciously continued to communicate with BFE customers about outside transactions without the Firm's knowledge.[21] Moreover, Miller communicated with the customers during business hours and using BFE's facilities and office equipment, including his work email address, and thereby he reasonably created the impression that the Firm had sanctioned his activities.[22] Miller's participation was not limited to a single communication, but instead included multiple selling away activities that he conducted over the course of several weeks.[23] Miller also ignored Firm policy and invested in CDP himself without obtaining the requisite written approval first, which demonstrates his reckless disregard of adhering to known Firm requirements.[24]

On the other hand, there were factors presented in the record that weighed against imposing heavier sanctions on Miller. We agree with the Extended Hearing Panel that the number of customers involved, four, was not exceptionally high. We also note that the customers who invested—particularly JS2, a shareholder of the Firm—were highly sophisticated

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18 *Id.*; *see also id.* at 2-8.

19 *See id.* at 14-15.

20 *See id.* at 15 (Principal Considerations in Determining Sanctions, No. 10).

21 *See id.* (Principal Considerations in Determining Sanctions, No. 8).

22 *See id.* at 14 (Principal Considerations in Determining Sanctions, No. 6).

23 *See id.* at 7 (Principal Considerations in Determining Sanctions, No. 8).

24 *See id.* at 15 (Principal Considerations in Determining Sanctions, No. 13).

wealthy businesspersons.[25] *See Siegel*, 2008 SEC LEXIS 2459, at *43-44 (considering the customers' levels of sophistication when determining sanctions). Although Miller participated in the transactions without the Firm's knowledge, we found no evidence that the products he sold away involved a violation of federal or state securities laws.[26] While it does not excuse his rule violation, we also consider the lack of evidence that Miller received compensation or pecuniary interest resulting from any of the transactions.[27]

We find the additional arguments that Miller presented for mitigation are unpersuasive. First, Miller argues that he never held himself or BFE out to be involved in the transactions. Although Miller might never have stated that he was acting as a BFE representative, he participated in the transactions at issue using the Firm's facilities and office equipment, including his work email, and therefore "[h]is customers could have reasonably assumed that his recommendations were authorized by [BFE]." *Klosowski*, 48 S.E.C. at 956. Second, Miller asserts that neither the Firm nor the investing public was ever at risk. As we indicated above, NASD Rule 3040's purpose is to shield investors from the "hazards of unmonitored sales" and to protect firms from the risks of loss and litigation *in advance of one's participation*. *Keith L. Mohn*, 54 S.E.C. 457, 467 (1999). Miller's participation in private securities transactions in violation of the rule only exacerbated these inherent risks. Third, Miller contends that the investors suffered no harm. Although we acknowledge this claim, a key aspect of the rule, which Miller undermined here, is that the respondent's prior notice gives his employing firm the ability to apply supervisory protections over such transactions. *See Blair C. Mielke*, Exchange Act Release No. 75981, 2015 SEC LEXIS 3927, at *63 (Sept. 24, 2015) (finding lack of customer harm not mitigating for NASD Rules 3040 and 3030 violations).[28]

Based on the CDP and KBI sales level, the Guidelines recommend a suspension ranging from six to 12 months. We find that Miller's extensive participation in the CDP and KBI private securities transactions, and the aggravating factors that predominate for the transactions, warrant a suspension above the low end of the suspension range. Accordingly, we suspend Miller for

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25 *See id.* at 8 (Principal Considerations in Determining Sanctions, No. 18).

26 *See id.* at 14 (Principal Considerations in Determining Sanctions, No. 4).

27 *See id.* at 8 (Principal Considerations in Determining Sanctions, No. 16).

28 Other principal considerations that Miller claims the Extended Hearing Panel decision failed to address are not dispositive here. For example, a lack of disciplinary history is not mitigating for purposes of sanctions "because an associated person should not be rewarded for acting in accordance with his duties as a securities professional." *Keyes*, 2006 SEC LEXIS 2631, at *23. Similarly, associated persons are required to abide by, and provide full cooperation in accordance with, FINRA rules. *See id.* (finding that Keyes' compliance with the unequivocal obligation to cooperate with NASD is not mitigating). Therefore, Miller's willingness to participate during Enforcement's investigation and his lack of concealment of any communications he had with the investors are not mitigating factors.

nine months in all capacities for his selling away activities in the CDP and KBI transactions. We find that Miller's nine-month suspension is appropriately remedial to address the severity of his participation in those transactions, and will serve to deter him and others from engaging in similar misconduct.

B. The CTL Transaction

In the CTL transaction, Miller sold away one private securities transaction in which a single customer invested $1 million. Based on this sales amount, the Guidelines also recommend a suspension range of six to 12 months. Miller's selling away in the CTL private securities transaction, however, involved a different balancing of factors. Based on the evidence in the record, Miller's level of participation in CTL was less substantial than in the CDP and KBI transactions. Miller did not, for example, introduce or offer to introduce CTL as an investment opportunity to any potential investors. Customer JS2—a shareholder of the Firm—was a sophisticated wealthy businessperson who learned of the CTL investment opportunity at the same time, and through the same investment channel, as Miller did. The CTL transaction involved one customer and Miller received no compensation in relation to the transaction.

Accordingly, we suspend Miller separately for three months in all capacities for his selling away in the CTL private securities transaction. The three-month suspension, which falls slightly below the recommended suspension range, is tailored to remediate the extent of Miller's misconduct in this particular private securities transaction, while also impressing the importance of complying with NASD Rule 3040 before participating in any private securities transaction. Miller is to serve the suspension orders consecutively.

VI. Conclusion

Miller participated in five private securities transactions without providing the requisite prior written notice to his employer firm, in violation of NASD Rule 3040 and FINRA Rule 2010. Miller is suspended for nine months from association with any FINRA member in all capacities for selling away from BFE in four private securities transactions; he is suspended in all capacities for three months for selling away in one private securities transaction; and he is fined $25,000. Miller is to serve the suspensions consecutively.

We also affirm the Extended Hearing Panel's order that Miller pay $9,474.35 in hearing costs.[29]

On Behalf of the National Adjudicatory Council,

Jennifer Piorko Mitchell,
Vice President and Deputy Corporate Secretary

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[29] Pursuant to FINRA Rule 8320, FINRA will revoke for non-payment the registration of any person associated with a member who fails to pay any fine, costs, or other monetary sanctions after seven days' notice in writing.