

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS**

Department of Enforcement,

Complainant,

v.

Dean S. Mustaphalli
(CRD No. 2792038),

Respondent.

Disciplinary Proceeding
No. 2013036880302

Hearing Officer: KBW

**ORDER ACCEPTING OFFER OF
SETTLEMENT**

Date: December 15, 2014

INTRODUCTION

Disciplinary Proceeding No. 2013036880302 was filed on July 9, 2014, by the Department of Enforcement of the Financial Industry Regulatory Authority (FINRA) (Complainant). Respondent Dean S. Mustaphalli submitted an Offer of Settlement (Offer) to Complainant dated December 4, 2014. Pursuant to FINRA Rule 9270(e), the Complainant and the National Adjudicatory Council (NAC), a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs (ODA) have accepted the uncontested Offer. Accordingly, this Order now is issued pursuant to FINRA Rule 9270(e)(3). The findings, conclusions and sanctions set forth in this Order are those stated in the Offer as accepted by the Complainant and approved by the NAC.

Under the terms of the Offer, Respondent has consented, without admitting or denying the allegations of the Complaint (as amended by the Offer of Settlement), and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to

which FINRA is a party, to the entry of findings and violations consistent with the allegations of the Complaint (as amended by the Offer of Settlement), and to the imposition of the sanctions set forth below, and fully understands that this Order will become part of Respondent's permanent disciplinary record and may be considered in any future actions brought by FINRA.

BACKGROUND

Mustaphalli entered the securities industry on September 9, 1996, as a General Securities Representative of a member of FINRA. Mustaphalli, during all periods mentioned herein, was associated with Sterne Agee Financial Services, Inc. ("Sterne Agee" or the "Firm") and was registered with FINRA under Article V of the By-Laws as a General Securities Representative.

On August 19, 2011, Mustaphalli's employment with the Firm was terminated. On January 10, 2013, Sterne Agee filed an amendment to Mustaphalli's Form U5 to include an Initial Complaint Disclosure extending the two-year jurisdiction period. Although Mustaphalli is not currently registered with a FINRA member firm, he is subject to the jurisdiction of FINRA, pursuant to Article V, Section 4 of FINRA's By-Laws, because (1) the Complaint was filed within two years after the Firm filed an amendment to Mustaphalli's Form U5 to include an Initial Complaint Disclosure, namely, January 10, 2013; and (2) the Complaint charges him with misconduct committed while he was registered or associated with a FINRA member and with failing to respond to FINRA requests for information during the two-year period after the filing of an amendment to his Form U5 to include an Initial Complaint Disclosure.

Mustaphalli has no prior disciplinary history.

FINDINGS AND CONCLUSIONS

It has been determined that the Offer be accepted and that findings be made as follows:

SUMMARY

1. Respondent Dean S. Mustaphalli ("Mustaphalli" or "Respondent"), over a six-month period in 2011, formed and acted as managing director for a hedge fund through which he sold investments totaling approximately \$6 million and received compensation for managing the hedge fund, all without providing prior written notice to or receiving written acknowledgment from his employer member firm regarding his role as managing director, his planned participation, or his expected compensation, in violation of NASD Rule 3040 and FINRA Rules 3270 and 2010.
2. In addition, as part of FINRA's subsequent investigation into Mustaphalli's conduct, Mustaphalli failed to timely provide a list of the hedge fund clients or unredacted account statements for the business account he controlled, in violation of FINRA Rules 8210 and 2010.

RESPONDENT AND JURISDICTION

3. Mustaphalli entered the securities industry on September 9, 1996, as a General Securities Representative of a member of FINRA. During the relevant time period, Mustaphalli was associated with Sterne Agee Financial Services, Inc. ("Sterne Agee" or the "Firm") and was registered with FINRA under Article V of the By-Laws as a General Securities Representative. On September 16, 2011, Sterne Agee filed a Form U5 terminating Mustaphalli's registration and association as of August 19, 2011.

4. On January 10, 2013, within two years of Mustaphalli's termination by Sterne Agee, Sterne Agee filed an amendment to Mustaphalli's Form U5 to include an Initial Complaint Disclosure.
5. Although Mustaphalli is no longer registered or associated with a FINRA member, he remains subject to FINRA's jurisdiction for purposes of this proceeding, pursuant to Article V, Section 4 of FINRA's By-Laws, because (1) the Complaint was filed within two years after the Firm filed an amendment to Mustaphalli's Form U5 to include an Initial Complaint Disclosure, namely, January 10, 2013, and (2) the Complaint charges him with misconduct committed while he was registered or associated with a FINRA member and with failing to respond to FINRA requests for information during the two-year period after the filing of an amendment to his Form U5 to include an Initial Complaint Disclosure.

FACTS

Background Information

6. Mustaphalli was registered with Sterne Agee from December 8, 2009 through August 19, 2011.
7. On December 11, 2009, Mustaphalli formed the Mustaphalli Advisory Group, LLC in Suffolk County, New York, and it was approved in New York as a Registered Investment Advisory firm (the "RIA"), effective February 1, 2010. Mustaphalli is the owner of 75% or more of the RIA and is the managing member of the RIA. Mustaphalli disclosed the RIA to Sterne Agee and received prior approval to operate the RIA.

8. Although Mustaphalli sought and received prior approval for the RIA, Mustaphalli never provided notice to Sterne Agee of his plan to form, operate, and sell limited partnership interests in a hedge fund that he formed in 2011.

Outside Business Activity

9. On January 31, 2011, Mustaphalli filed a Form D with the Securities Exchange Commission for the Mustaphalli Capital Partners Fund, L.P. (the "Hedge Fund"), which he identified in the filing as a hedge fund. He further identified his RIA as the investment manager of the Hedge Fund and the limited liability company he owned, Mustaphalli Group, LLC as the General Partner of the Hedge Fund. In the Form D, he also disclosed that Mustaphalli Group, LLC would receive a performance fee and that the RIA would receive a management fee from the Hedge Fund.
10. The Hedge Fund was a business activity outside the course and scope of Mustaphalli's employment with Sterne Agee.
11. Just prior to the filing of the Form D, on January 13, 2011, Mustaphalli opened an institutional account for the Hedge Fund at the broker-dealer TradeStation Securities, Inc. ("TSSI"). The Hedge Fund engaged in buying and selling of securities through TSSI in April and May 2011. The closing balance in the TSSI account as of May 31, 2011 was \$6,201,415.87.
12. On February 15, 2011, the Hedge Fund issued a Private Placement Memorandum (the "PPM") identifying the general partner of the Hedge Fund to be Mustaphalli Group, LLC and the Investment Manager of the Hedge Fund to be the RIA. In addition, the PPM identified the Managing Director and Portfolio Manager of the Hedge Fund to

13. be Mustaphalli. Mustaphalli as Portfolio Manager made all investment decisions for the Hedge Fund. Consequently, Mustaphalli was a director and employee of the Hedge Fund.
14. The PPM also provided details regarding compensation to Mustaphalli and the entities he controlled. The Hedge Fund would pay the RIA a management fee equal to 1/12th of 2% (a 2% annual rate) of the opening balance of the Hedge Fund at the beginning of each month. In addition, Mustaphalli Group, LLC would receive a performance allocation if the returns on the Hedge Fund exceeded 6% annually. The performance allocation ranged from 1.4% to 3.6%, depending on the performance. Because Mustaphalli was a controlling person of the RIA and the General Partner, Mustaphalli had an expectation of compensation from the Hedge Fund. Furthermore, based upon the account statements for the Hedge Fund, for the months April 2011 through August 1, 2011, Mustaphalli did receive approximately \$41,800 in management fees.
15. Prior to forming and operating the Hedge Fund, Mustaphalli failed to provide Sterne Agee with written or oral notice of his role as a director and employee of the Hedge Fund, or the compensation he expected to receive from the Hedge Fund.

Private Securities Transactions

16. Between February 15, 2011 and August 19, 2011, Mustaphalli not only managed the Hedge Fund but also sold limited partnership interests in the Hedge Fund to at least 25 investors in the total amount of approximately \$6 million.
17. The limited partnership interests sold by Mustaphalli in the Hedge Fund were securities. Investors in the Hedge Fund signed subscription agreements to purchase

limited partnership interests in the Hedge Fund. The investment objective of the Hedge Fund was to seek long-term, above-market returns by investing principally in publicly traded, marketable equity and debt securities of U.S. and non-U.S. companies. The PPM stated that the Hedge Fund's trading strategy "may also employ the trading of the intra-day oscillations of the stock, bond, equities, ETFs, index equities, equity and index. The strategies utilized will include both long and short trades in all the markets traded in both the cash and cash derivative contracts."

18. Under the Limited Partnership Agreement for the Hedge Fund, investors had no right to participate in the management of the Hedge Fund and could not remove the General Partner. The liability of each limited partner was limited to the amount of the investment. Mustaphalli as the Portfolio Manager and Managing Director of the Hedge Fund made all investment decisions for the Hedge Fund.
19. Mustaphalli's sale of limited partnership interests in the Hedge Fund constituted participation in a private securities transaction.
20. Prior to participating in the private securities transactions, Mustaphalli failed to provide Sterne Agee with written or oral notice describing the transactions, his proposed role in the transactions or his expectation of compensation therefrom.
21. In 2013 and 2014, as part of its investigation of Mustaphalli's formation and operation of the Hedge Fund, FINRA issued multiple requests pursuant to FINRA Rule 8210 to Mustaphalli to provide FINRA information, including but not limited to, a list of investors in the Hedge Fund as well as unredacted financial statements showing the details of money movement into and out of the Hedge Fund. These requests were served on Mustaphalli's counsel.

22. While Mustaphalli has provided some information in response to these 8210 requests, Mustaphalli failed to timely provide FINRA with (a) a list of the investors in the Hedge Fund, or (b) unredacted financial statements from which FINRA can determine the source of funds into and out of the accounts.

FIRST CAUSE OF ACTION
(*FINRA Rules 3270 and 2010*)
(*Outside Business Activity*)

23. FINRA Rule 3270 provides that:

No registered person may be an employee, independent contractor, sole proprietor, officer, director or partner of another person, or be compensated, or have the reasonable expectation of compensation, from any other person as a result of any business activity outside the scope of the relationship with his or her member firm, unless he or she has provided prior written notice to the member, in such form specified by the member.

24. FINRA Rule 2010 requires associated persons in the conduct of their business to

“observe high standards of commercial honor and just and equitable principles of trade.”

25. Between January 31, 2011 and August 19, 2011, Mustaphalli, acting outside the course and scope of his employment with Sterne Agee, was the managing director and portfolio manager of the Hedge Fund and had a reasonable expectation of compensation from the Hedge Fund in the form of management and performance fees. Mustaphalli, however, failed to provide prior written or oral notice to Sterne Agee of his proposed role in, or the compensation that he might receive from, the Hedge Fund.

26. As a result of the foregoing, Mustaphalli violated FINRA Rules 3270 and 2010.

SECOND CAUSE OF ACTION
(NASD Conduct Rule 3040 and FINRA Rule 2010)
(Private Securities Transactions)

27. NASD Conduct Rule 3040(b) provides that:

Prior to participating in any private securities transaction, an associated person shall provide written notice to the member with which he is associated describing in detail the proposed transaction and the person's proposed role therein and stating whether he has received or may receive selling compensation in connection with the transaction; provided however that, in the case of a series of related transactions in which no selling compensation has been or will be received, an associated person may provide a single written notice.

28. From on or about January 31, 2011 through August 19, 2011, Mustaphalli, acting outside the course and scope of his employment with his employing member firm Sterne Agee, participated in private securities transactions by selling at least 25 security interests in the Hedge Fund in the total amount of approximately \$6 million, without providing prior written or oral notice to Sterne Agee describing the proposed transaction, his role in selling the securities or his expectation of compensation therefrom.

29. As a result of the foregoing conduct, Mustaphalli violated NASD Rule 3040 and FINRA Rule 2010.

THIRD CAUSE OF ACTION
(FINRA Rules 8210 and 2010)
(Failure to Timely Respond)

30. FINRA Rule 8210 provides that for the purposes of an investigation FINRA staff shall have the right to require a person subject to FINRA's jurisdiction to provide

information or testimony “with respect to any matter involved in the investigation, complaint, examination, or proceeding,” as well as obtain copies of “the books, records, and accounts” of such person with respect to “any matter” involved in the investigation, complaint, examination or proceeding. Pursuant to FINRA Rule 8210(c), no person “shall fail to provide information or testimony or to permit an inspection and copying of books, records, or accounts pursuant to this Rule.”

31. Furthermore, if FINRA staff knows that the person is represented by counsel regarding the investigation, the notice of the Rule 8210 request may be served upon counsel and any notice served upon counsel shall be deemed to be received by the person.
32. On or about May 15, 2013, FINRA staff received notice that for purposes of the investigation giving rise to this proceeding, Mustaphalli was represented by counsel.
33. By letter dated August 7, 2013, and pursuant to FINRA Rule 8210, FINRA staff requested that Mustaphalli provide information and documents in connection with the staff’s investigation. The August 7 letter requested, among other things, a list of clients of the Hedge Fund. The August 7 letter was sent by first class and certified mail to the business address of Mustaphalli’s counsel, and a carbon copy was sent to Mustaphalli by first class mail to his last known residential address. The letter sent by certified mail was signed for and delivered to the business address of Mustaphalli’s counsel on August 12, 2013. The letters sent by first class mail were not returned to FINRA.
34. By letter dated August 28, 2013, Mustaphalli provided some of the requested information, but refused to provide the list of the Hedge Fund clients to the staff,

claiming that he was not registered at the time he established the Hedge Fund and that FINRA lacked jurisdiction.

35. By letter dated October 4, 2013, and pursuant to FINRA Rule 8210, FINRA staff requested that Mustaphalli appear for on-the-record testimony on October 29, 2013, and provide tax returns, audited financial statements, and personal and business account statements for accounts controlled by Mustaphalli for the period January 1, 2011 to August 31, 2011. The letter was sent by first class and certified mail to the business address of Mustaphalli's counsel. The letter sent by certified mail was signed for and delivered to the business address of Mustaphalli's counsel on October 6, 2013. The letter sent by first class mail was not returned to FINRA.
36. By email dated October 28, 2013, Mustaphalli provided tax returns and audited financial statements, but failed to provide personal and business account statements for accounts he controlled.
37. On October 29, 2013, Mustaphalli appeared for on-the-record testimony, pursuant to FINRA Rule 8210. During testimony, the staff asked Mustaphalli to provide the list of Hedge Fund clients and the account statements previously requested but not provided. Mustaphalli, through counsel, took the position that the account statements were outside FINRA's jurisdiction, and otherwise refused to provide the names of the Hedge Fund investors.
38. By letter dated October 29, 2013, pursuant to FINRA Rule 8210, the staff again requested personal and business account statements for accounts controlled by Mustaphalli for the period January 1, 2011 to August 31, 2011 and expanded the request to include statements through December 31, 2012. The October 29 letter was

sent by first class and certified mail to the business address of Mustaphalli's counsel. The letter sent by certified mail was signed for and delivered to the business address of Mustaphalli's counsel on October 31, 2013. The letter sent by first class mail was not returned to FINRA.

39. By emails dated December 13, 2013 and December 16, 2013, Mustaphalli provided account statements for two bank accounts. Mustaphalli, however, redacted critical information from the statements for the business account, such as the names of the recipients of wire transfers from the bank account for the Hedge Fund, making the response incomplete.

40. By letter dated December 19, 2013, pursuant to FINRA Rule 8210, FINRA staff requested that Mustaphalli provide the unredacted account statements previously requested and produced in redacted form, and to provide a list of all clients of the Hedge Fund as previously requested. The December 19 letter was sent by first class and certified mail to the business address of Mustaphalli's counsel. The letter sent by certified mail was signed for and delivered to the business address of Mustaphalli's counsel on December 26, 2013. The letter sent by first class mail was not returned to FINRA.

41. Mustaphalli provided no response to this request.

42. By letter dated January 7, 2014, pursuant to FINRA Rule 8210, FINRA staff sent Mustaphalli a third request for the previously requested account statements without redactions and for the previously requested list of all clients of the Hedge Fund. The January 7 letter was sent by first class and certified mail to the business address of Mustaphalli's counsel. The letter sent by certified mail was signed for and delivered

to the business address of Mustaphalli's counsel on January 14, 2014. The letter sent by first class mail was not returned to FINRA.

43. By letter dated January 17, 2014, Mustaphalli's counsel informed the staff that Mustaphalli continued to decline to provide a list of clients of the Hedge Fund and would not provide unredacted account statements to the staff.
44. The December 19, 2013 and January 7, 2014 letters discussed above notified Mustaphalli that the failure to deliver the requested information to FINRA could subject Mustaphalli to the institution of a "formal disciplinary proceeding leading to sanctions, including a bar from the securities industry."
45. The documents and information that Mustaphalli refused to provide to the staff, namely the identity of the Hedge Fund clients and the bank account statements documenting the flow of funds to and from the Hedge Fund, are material to the staff's investigation and impeded the staff by not permitting the staff to fully investigate and confirm the extent of Mustaphalli's violations, including but not limited to, making a determination of whether the Hedge Fund customers were also Sterne Agee customers and tracing the source of funds into and out of the Hedge Fund account to determine if other violations and/or sanctions are appropriate. Subsequent to Enforcement's filing of the Complaint in this matter, Mustaphalli produced all of the documents requested by FINRA staff.
46. As a result of the foregoing conduct, Mustaphalli violated FINRA Rules 8210 and 2010.

Based on the foregoing, Respondent Mustaphalli violated FINRA Rules 2010, 3270 and 8210 and NASD Rule 3040.

Based on these considerations, the sanctions hereby imposed by the acceptance of the Offer are in the public interest, are sufficiently remedial to deter Respondent from any future misconduct, and represent a proper discharge by FINRA, of its regulatory responsibility under the Securities Exchange Act of 1934.

SANCTIONS

It is ordered that Respondent Dean S. Mustaphalli receive the following sanctions:

- a suspension in all capacities for a period of two years;
- payment of a fine in the amount of \$20,000;
- payment of \$41,800, in disgorgement of management fees, plus interest at the rate set forth in Section 6621(a)(2) of the Internal Revenue code, 26 U.S.C. 6621(a)(2) from September 15, 2011 until the date paid.

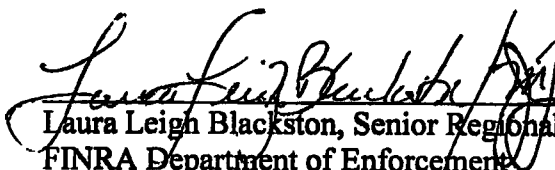
The fine shall be due and payable either immediately upon reassociation with a member firm following the two-year suspension noted above, or prior to any application or request for relief from any statutory disqualification resulting from this or any other event or proceeding, whichever is earlier.

The sanctions imposed herein shall be effective on a date set by FINRA staff

SO ORDERED.

FINRA

Signed on behalf of the
Director of ODA, by delegated authority


Laura Leigh Blackston, Senior Regional Counsel
FINRA Department of Enforcement
1100 Poydras Street, Suite 850
New Orleans, LA 70163-1108
Phone: 504-412-2408 Fax: 504-522-4077
E-mail: laura.blackston@finra.org