

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2017054925801**

TO: Department of Enforcement
Financial Industry Regulatory Authority (FINRA)

RE: Chardan Capital Markets, LLC, Respondent
Member Firm
CRD No. 120128

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Respondent Chardan Capital Markets, LLC (the "Firm," "Respondent" or "Chardan") submits this Letter of Acceptance, Waiver and Consent ("AWC") for the purpose of proposing a settlement of the alleged rule violations described below. This AWC is submitted on the condition that, if accepted, FINRA will not bring any future actions against Respondent alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

- A. Respondent hereby accepts and consents, without admitting or denying the findings, 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, prior to a hearing and without an adjudication of any issue of law or fact, to the entry of the following findings by FINRA:

BACKGROUND

Chardan has been a member of FINRA since July 2, 2002, and its registration remains in effect. The Firm employs approximately 43 registered representatives and offers a range of broker dealer services, including investment banking, sales and trading, and research. The Firm's investment banking group underwrites public offerings as well as private investments in public entities ("PIPEs") for small to mid-cap issuers, mostly in the healthcare and technology sectors. The research group produces and publishes research reports on similar companies, some of which had a direct investment banking relationship with the Firm. Its principal place of business is New York, New York.

RELEVANT DISCIPLINARY HISTORY

Respondent does not have any relevant disciplinary history with the Securities and Exchange Commission, any state securities regulators, FINRA, or any other self-regulatory organization.

OVERVIEW

NASD Rule 2711 primarily addresses conflicts of interest that arise when research analysts work for firms that have investment banking or other business relationships with subject companies, or when analysts or firms own securities of subject companies or make a market in those securities. The rule implemented structural reforms designed to increase analysts' independence and further manage conflicts of interest, and required increased disclosure of conflicts in research reports and public appearances.¹ FINRA Rule 2241, which replaced Rule 2711 in 2015, generally retains the core provisions of Rule 2711 and, among other things, broadens the obligations on members to identify and manage research-related conflicts of interest.² From March 5, 2013 through August 31, 2016 (the "Review Period"), Chardan violated certain research report disclosure requirements of FINRA Rule 2241 and NASD Rule 2711 (collectively, the "Research Rules"), and failed to establish and maintain a supervisory system and written supervisory procedures reasonably designed to achieve compliance with those rules.

Specifically, Chardan improperly published at least 103 research reports that contained 123 disclosure deficiencies, including failing to accurately disclose investment banking relationships, in violation of FINRA Rules 2241(c) and 2010, and NASD Rule 2711(h).

The Firm's disclosure failures were the result of Chardan's failure to establish and maintain a supervisory system and written supervisory procedures reasonably designed to achieve compliance with the disclosure requirements of the Research Rules. By this conduct, the Firm violated FINRA Rules 3110(a), 3110(b)(1) and 2010, and NASD Rules 2711(i), 3010(a) and 3010(b)(1).

Also, during the Review Period, Chardan failed to enforce written supervisory procedures reasonably designed to achieve compliance with provisions of the Research Rules that require firms to manage conflicts of interest between research analysts and those engaged in investment banking services. These failures involved the supervision of the Special Equities Group ("SEG"), which was a subgroup of the Firm's investment banking department during the Review Period.³ Chardan's supervisory failure created the risk that research analysts could be inappropriately influenced by the Firm's interest in attracting and maintaining investment banking business. By this conduct, the Firm violated FINRA Rules 2241(b)(1), 2241(b)(2)(G), 2241(b)(2)(M)(i), 3110(b)(1) and 2010, and NASD Rules 2711(i) and 3010(b)(1).

¹ See Order Approving Rule Changes, Release No. 34-45908, 67 FR 34968, (May 10, 2002).

² FINRA Notice to Members ("NTM") 15-30. FINRA Rule 2241 became effective in part as of September 25, 2015, and in whole on December 24, 2015, and governs research analysts and research reports.

³ The SEG group personnel left the Firm in or around May 2019, after the Review Period.

FACTS AND VIOLATIVE CONDUCT

1. Research Report Disclosure Deficiencies

During the Review Period, Chardan published at least 103 research reports covering 15 subject companies in which the Firm omitted, or erroneously included, disclosures required by the Research Rules.⁴ The published reports contained 123 specific disclosure deficiencies. Specifically,

- **FINRA Rule 2241(c)(4)(C)(i) and NASD Rule 2711(h)(2)(A)(ii)(a)** require members to disclose in research reports if they “managed or co-managed a public offering of securities for the subject company in the past 12 months[.]” During the Review Period, Chardan failed to disclose that it was the co-manager of a securities offering in 16 reports to which this disclosure applied.
- **FINRA Rule 2241(c)(4)(C)(ii) and NASD Rule 2711(h)(2)(A)(ii)(b)** require that members disclose in research reports if they “received compensation for investment banking services from the subject company in the past 12 months[.]” During the Review Period, Chardan failed to disclose that it received compensation for investment banking services in 10 reports to which this disclosure applied. Further, Chardan inaccurately disclosed in 35 research reports that it received compensation for investment banking services from the subject company when this disclosure did not apply.
- **FINRA Rule 2241(c)(4)(G) and NASD Rule 2711(h)(8)** require that a member “disclose in research reports if it was making a market in the subject company’s securities at the time that the research report was published.” During the Review Period, Chardan failed to disclose in 62 reports that it was a market maker in securities issued by the subject company at the time of publishing.

By virtue of the foregoing, Chardan violated FINRA Rule 2241(c) for conduct on and after December 24, 2015, NASD Rule 2711(h) for conduct prior to December 24, 2015, and FINRA Rule 2010.

2. Failure to Establish a Reasonable Supervisory System and Written Procedures For Review and Approval of Research Report Disclosures

FINRA Rule 3110(a), which became effective December 1, 2014, and its predecessor NASD Rule 3010(a) require that member firms “establish and maintain a system to supervise the activities of each associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules.” FINRA Rule 3110(b)(1), which became effective December 1, 2014, and its predecessor NASD Rule 3010(b)(1) require that member firms “establish, maintain, and

⁴ NASD Rule 2711(h) was effective through December 23, 2015. FINRA Rule 2241(c) superseded NASD Rule 2711(h), and became effective on December 24, 2015.

enforce written procedures to supervise the types of business in which it engages and the activities of its associated persons that are reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable FINRA rules.”

NASD Rule 2711(i) required member firms to “adopt and implement written supervisory procedures reasonably designed to ensure that the firm and its employees comply with the provisions of this rule.”⁵

FINRA Rule 2241(c)(4) and NASD Rule 2711(h) require specified disclosures in research reports concerning, *inter alia*, (i) ownership of the subject company’s securities by the research analyst or the member; (ii) the member’s receipt of, or intention to seek, investment banking compensation from the subject company; (iii) the member’s management or co-management of a public offering of securities for the subject company; and (iv) the member making a market in the securities of the subject company. Chardan’s supervisory systems and written procedures were not reasonably designed to achieve compliance with these disclosure requirements because the Firm failed to reasonably track and communicate the information necessary to make required disclosures to the research supervisors who were responsible for reviewing and approving each research report before publication. Further, this resulted in the disclosure deficiencies set forth in the section above.

By virtue of the foregoing, Chardan violated FINRA Rules 3110(a) and (b)(1) (for conduct on and after December 1, 2014), NASD Rules 3010(a) and (b)(1) (for conduct before December 1, 2014) and 2711(i) (for conduct on and before September 24, 2015), and FINRA Rule 2010.

3. Failure to Supervise and Manage Conflicts of Interest Between Research and Investment Banking

As set forth above, FINRA Rule 3110 and NASD Rules 2711(i) and 3010 govern member firms’ supervisory obligations under the Research Rules. Further, FINRA Rule 2241(b)(1) requires that members “establish, maintain and enforce written policies and procedures reasonably designed to identify and effectively manage conflicts of interest related to ... the preparation, content and distribution of research reports [and] the interaction between research analysts and those outside of the research department[.]” Additionally, FINRA Rule 2241(b)(2) requires member firms to have written policies and procedures that are reasonably designed to promote objective and reliable research.

During the Review Period, Chardan’s supervisory systems and written supervisory procedures provided that “[d]irect email communications between investment banking personnel and research personnel has been blocked” and that “[a]ll communications between the two departments require compliance to act as an intermediary.” These policies and procedures were established to achieve compliance with (i) NASD Rule

⁵ The supervision provision in NASD Rule 2711(i) was not carried over to FINRA Rule 2241 and was removed effective September 25, 2015. Supervision relating to research analysts and research reports is now governed exclusively by FINRA Rule 3110. *See* Regulatory Notice 15-30.

2711(c)(6)(A), which prohibits investment banking personnel from directly or indirectly directing a research analyst to engage in sales or marketing efforts related to an investment banking services transaction; (ii) FINRA Rule 2241(b)(2)(M)(i), which requires firms to establish and enforce written policies and procedures reasonably designed to prohibit investment banking personnel from engaging in such conduct; and (iii) FINRA Rule 2241(b)(2)(G), which requires information barriers or other institutional safeguards reasonably designed to ensure that research analysts are insulated from the review, pressure or oversight by persons engaged in investment banking services activities.⁶

During the Review Period, the Firm's investment banking department consisted of 16 employees, seven of whom were members of SEG. However, the Firm failed to enforce its policies and procedures to block direct email communications between the SEG investment banking personnel and research personnel or ensure that compliance acted as an intermediary for communications between the SEG investment banking personnel and research personnel.

During the Review Period there were a number of direct email communications between SEG personnel and research personnel without compliance as an intermediary or any other institutional safeguards or supervisory review. Further, some direct email communications between SEG personnel and research personnel included improper suggestions by SEG investment bankers that research personnel should help solicit investment banking clients.⁷ For example:

- In an email dated February 24, 2015, sent by a SEG employee to other SEG employees and two research analysts, the SEG employee proposed establishing weekly meetings between research and investment banking, and stated that the investment banking department would use research staff "as the first introduction to new companies to bait them in" and get investment banking's "foot in the door[.]"
- An email dated November 19, 2015, sent by the head of SEG to a research analyst, asked whether the head of SEG should have the head of research "show []some love" to a prospective investment banking customer.

By failing to enforce (i) policies and procedures reasonably designed to achieve compliance with the Research Rules cited above; and (ii) information barriers or other institutional safeguards reasonably designed to ensure that research analysts are insulated from the review or potential pressure by persons engaged in investment banking services activities, Chardan violated FINRA Rule 3110(b)(1) (for conduct on and after December 1, 2014), Rules 2241(b)(1), 2241(b)(2)(G) and 2241(b)(2)(M)(i) (for conduct on and after December 24, 2015) and 2010, and NASD Rules 3010(b)(1) (for conduct before December 1, 2014) and 2711(i) (for conduct on and before September 24, 2015).

⁶ FINRA Rules 2241(b)(2)(G) and 2241(b)(2)(M)(i) became effective on December 24, 2015.

⁷ The review of this matter found no evidence that the activities suggested ultimately occurred.

B. Respondent also consents to the imposition of the following sanctions:

- A censure; and
- A total fine of \$100,000.

In addition, Respondent shall comply with the following undertakings within the time periods specified (unless otherwise extended by FINRA staff following a written request by Respondent):

Respondent shall undertake to review its supervisory system and procedures concerning research reports and the supervision of research analysts for compliance with FINRA rules and the federal securities laws and regulations. Within 90 calendar days of the issuance of this AWC, Respondent's Chief Compliance Officer will certify to FINRA in writing that the firm has completed its review and that it currently has in place systems and procedures reasonably designed to achieve compliance with those rules, laws and regulations. The certification, along with the current procedures, must be submitted to Department of Enforcement staff at FINRA's New York District Office. Although FINRA staff may review the revised procedures, said review shall in no way constitute an approval of the revised procedures. The failure of FINRA staff to alert Respondent to any deficiencies in the revised procedures shall not preclude FINRA from instituting a subsequent disciplinary action as a result of deficiencies in the revised procedures.

Chardan agrees to pay the monetary sanction upon notice that this AWC has been accepted and that such payment is due and payable. Chardan has submitted an Election of Payment form showing the method by which it proposes to pay the fine imposed.

Chardan specifically and voluntarily waives any right to claim an inability to pay, now or at any time hereafter, the monetary sanctions imposed in this matter.

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

II.

WAIVER OF PROCEDURAL RIGHTS

Chardan specifically and voluntarily waives the following rights granted under FINRA's Code of Procedure:

- A. To have a Complaint issued specifying the allegations against it;
- B. To be notified of the Complaint and have the opportunity to answer the allegations in writing;

- C. To defend against the allegations in a disciplinary hearing before a hearing panel, to have a written record of the hearing made and to have a written decision issued; and
- D. To appeal any such decision to the National Adjudicatory Council (NAC) and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, Chardan specifically and voluntarily waives any right to claim bias or prejudgment of the Chief Legal Officer, the NAC, or any member of the NAC, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including acceptance or rejection of this AWC.

Chardan further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of FINRA Rule 9143 or the separation of functions prohibitions of FINRA Rule 9144, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including its acceptance or rejection.

III.

OTHER MATTERS

Chardan understands that:

- A. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by the NAC, a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs (ODA), pursuant to FINRA Rule 9216;
- B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against Chardan; and
- C. If accepted:
 - 1. this AWC will become part of Chardan's permanent disciplinary record and may be considered in any future action brought by FINRA or any other regulator against Chardan;
 - 2. this AWC will be made available through FINRA's public disclosure program in accordance with FINRA Rule 8313;
 - 3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with FINRA Rule 8313; and
 - 4. Chardan may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or

indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. Chardan may not take any position in any proceeding brought by or on behalf of FINRA, or to which FINRA is a party, that is inconsistent with any part of this AWC. Nothing in this provision affects Chardan's: (i) testimonial obligations; or (ii) right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.

- D. Chardan may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Chardan understands that it may not deny the charges or make any statement that is inconsistent with the AWC in this Statement. This Statement does not constitute factual or legal findings by FINRA, nor does it reflect the views of FINRA or its staff.

The undersigned, on behalf of Chardan, certifies that a person duly authorized to act on its behalf has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that it has agreed to the AWC's provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce it to submit it.

Respondent Chardan Capital Markets, LLC

May 26, 2020
Date

By: Steven Urbach

Print Name: Steven Urbach

Title: CEO

Reviewed by:

Robert I. Rabinowitz

Robert I. Rabinowitz, Esq.
Counsel for Respondent
Becker & Poliakoff, LLP
45 Broadway, 17th Floor
New York, New York 10006

Accepted by FINRA:

7-6-2020
Date

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

Kerry Land /slb

Kerry J. Land
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