
2021 PIABA MID-YEAR MEETING

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2021 PIABA Mid-Year Meeting

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2021 PIABA Mid-Year Meeting Speaker Biographies

Pierre F. de Ravel d'Esclapon **New York, New York**

Mr. de Ravel is an international arbitrator and mediator with over 45 years of experience in cross-border business transactions (M&A, Joint ventures, licensing, distribution, off-take agreements, direct investment) in a wide range of industries: : finance and investments (banking, insurance, structured financing, derivatives, project finance), energy (power generation, electricity transmission and distribution, power marketing) electronics, chemicals, computer leasing, ship financing, medical devices, pharmaceuticals, metals (steel , carbon and specialty, non-ferrous alloys), fashion (licensing and IP litigation) and wholesale distribution. He has been appointed as counsel and arbitrator in AAA, ICC, FINRA and ad hoc arbitrations. As arbitrator he served in several cross-border disputes relating to computer software, manufacturer/distributor disputes, construction, pharmaceuticals (licensing and valuation of technology) and sports. He has published numerous articles in English and in French on a broad range of legal topics. He is an Adjunct Professor of Law at the University of Montreal Law School and of Corporate Governance at HEC-MBA in France.

Sandra Grannum, Esq. **Faegre Drinker Biddle & Reath LLP** **Florham Park, New Jersey**

Sandra Dawn Grannum is a Partner in the Business Litigation Group at Faegre Drinker Biddle & Reath LLP where she serves on the Firm's governing board and is co-chair of the Firm's nationwide Securities and Financial Services Litigation Team. Sandy is a fellow of the American College of Trial Lawyers and concentrates her practice on securities, broker-dealer arbitration, litigation, mediation and regulatory defense. Sandy has written and lectured widely on securities and ethics issues. She assists in preparing clients for SEC Regulation Best Interest and Interpretation RIA. She chairs the full-day PLI Securities Arbitration Seminar conducted annually in New York City and regularly speaks at the SIFMA C&L Annual Conference, ABA Conferences and on other CLE programs addressing securities and employment law. Sandy was one of 13 individuals on the FINRA Dispute Resolution Task Force. FINRA impaneled this group to collaborate and suggest strategies to enhance the transparency, impartiality, and efficiency of FINRA's securities dispute resolution forum for all participants. On December 16, 2015, the task force issued its recommendations detailed in the Final Report and Recommendations of the FINRA Dispute Resolution Task Force. Sandy earned her law degree from Harvard Law School and her bachelor's degree from New York University. She began her career as a litigation associate at the New York law firm of Cravath, Swaine & Moore before moving to Tenzer Greenblatt to practice securities litigation. Sandy moved in-house to be an Associate General Counsel handling securities litigation at PaineWebber (now UBS Financial Services) in 1997. In November 2001, she became Senior Vice President and Senior Associate General Counsel in UBS's Employment Law Unit. In 2003, she formed her own firm, Davidson & Grannum, with a former PaineWebber/UBS colleague. She joined Drinker in January 2016 and that firm merged to become Faegre Drinker in February 2020.

Brian Henderson **Securities Litigation and Consulting Group, Inc.** **McLean, Virginia**

Dr. Henderson is Associate Professor of Finance at The George Washington University where he teaches investment analysis and portfolio management, performance evaluation, derivatives, and fixed income. He is a Chartered Financial Analyst. He has presented his research at academic conferences, universities, and market regulators. He publishes extensively in elite peer-reviewed journals and professional books.

Dr. Henderson is as expert in damages computation, derivatives, portfolio management, investment performance evaluation, structured products, fixed income, and investment companies. He has testified in FINA arbitrations as well as both state and federal courts.

His investment management experience includes retirement plan design, investment performance evaluation, portfolio design, and quantitative investment research. He has also been on the investment committee at a tactical ETF portfolio manager and worked in the Asset-Backed Securities Practice at PricewaterhouseCoopers LLP.

Aaron Israels, Esq.
Israels & Neuman, PLC
Denver, Colorado

Aaron Israels' primary practice involves representing investors in proceedings to recover their investment losses from stockbrokers, investment advisors, financial planners, and broker-dealers. He represents investors in FINRA (Financial Industry Regulatory Authority) Arbitration proceedings in every state, for claims arising from violations of securities laws, "sold away" investments, PONZI schemes, trading and concentration issues, unsuitable investments, fraud in the sale of securities and due diligence failures related to financial products.

In addition to securities litigation, Aaron represents individuals and businesses in a variety of transactional matters, which include business formations, purchase and sale transactions, restricted stock sales, private securities offerings and licensing matters. Most of Aaron's business clients operate in highly regulated industries, such as alcohol, firearms, and private finance.

Aaron is licensed to practice law in Colorado, Arizona, Michigan, and Illinois, and is admitted to practice before the United States Tax Court and various federal districts around the country. He is also admitted to the Federal Trial Bar in the Northern Federal District of Illinois, a bar limited to attorneys with significant federal trial experience.

Aaron graduated from Eastern Michigan University in 2004 with a bachelor's degree in philosophy and a minor in business. During his undergraduate studies, at the age of 20, he started his first law job as an intern at a personal injury law firm in Ypsilanti, Michigan. He has continued to work in the legal field ever since. Aaron graduated law from the University of Detroit Mercy Law School in 2007, where he received several academic accolades. In 2016 and 2019, he was named a "Rising Star" in the area of securities litigation by Super Lawyers magazine.

Aaron is an active member of PIABA (the Public Investors Arbitration Bar Association), an organization for lawyers committed to protecting the rights of investors and investor education, where he is currently the co-chair of the PIABA Arbitration Committee. He was recently admitted to the prestigious Thompson G. Marsh American Inn of Court in Denver, Colorado.

Joshua B. Kons, Esq.
Kons Law Firm
Hartford, Connecticut

Attorney Joshua B. Kons has a breadth of experience in FINRA arbitration and securities litigation matters. His significant accomplishments include representing a group of Ponzi scheme victims with damages in excess of \$10 million in FINRA arbitration against a national broker-dealer, multiple confidential FINRA arbitration settlements exceeding \$1 million, as well as being named special FINRA arbitration counsel to a bankruptcy trustee in the Central District of California. In 2014-2016, 2018-2019, Joshua B. Kons was recognized as a "Rising Star" for securities litigation by Super Lawyers, which recognizes no more than 2.5% of attorneys. Prior to attending law school, Mr. Kons worked for as a mutual fund trader, where he learned the securities business from the ground up. After receiving his law degree, Mr. Kons worked as an in-house attorney for a Fortune 500 company, where he was responsible for corporate and commercial transactional matters. Prior to forming his own practice in 2012, Mr. Kons worked with a boutique corporate and securities law firm, where the focus of his practice was representing investors and financial advisors in securities arbitration matters. Mr. Kons received a B.B.A. from the University of Wisconsin-Madison and his J.D. from the Pepperdine University School of Law. Mr. Kons concentrated his legal education in the areas of corporate and securities law, and served as a senior fellow at the Geoffrey Palmer Center for Entrepreneurship and the Law. Mr. Kons is a member of the State Bar of Connecticut, the State Bar of Illinois, the State Bar of California and the State Bar of Wisconsin, and is admitted to practice in the United States District Courts for the Central District of California, Eastern District of California, Northern District of California, Southern District of California, Eastern District of Wisconsin, Western District of Wisconsin, Northern District of Illinois, Southern District of Illinois, District of Connecticut, and District of North Dakota. He is a member of the Public Investors Arbitration Bar Association (PIABA).

Christine Lazaro, Esq.
St. John's University School of Law
Queens, New York

Christine Lazaro is a Professor of Clinical Legal Education and the Director of the Securities Arbitration Clinic at St. John's University School of Law. Professor Lazaro is also Of Counsel to the Law Offices of Brent A. Burns, LLC, where she consults on securities arbitration and regulatory matters. Professor Lazaro has been a member of PIABA since 2008. She served as its President from October 2018 through October 2019, and currently serves on its Board of Directors. She is currently co-chair of the Association's Fiduciary Standards Committee. Professor Lazaro also serves on the FINRA Investor Issues Advisory Committee, and is a member of the Editorial Advisory Board of the Securities Arbitration Commentator, and occasionally contributes to its Arbitration Alerts. Professor Lazaro speaks and writes regularly on the topics of securities arbitration and the duties of brokers and brokerage firms.

Jennifer Lupo, Esq.
Lupo Law, Arbitration and Mediation PLLC
New York, New York

Jennifer Lupo is the Managing Member of Lupo Law, Arbitration and Mediation PLLC with offices in Manhattan and Garden City. Jennifer's *legal career* began at the age of fifteen as an intern in her father's criminal and civil rights law firm in Brooklyn. It was there that she learned the importance of thorough preparation, grace under fire and integrity. Since then, Ms. Lupo has had a diverse legal career in government, law firms, corporate legal departments, as a law professor and as a dispute resolution neutral.

Lupo Law acts as outside general counsel to several companies and assists its' clients in formulating strong, cohesive business strategies. Its attorneys provide advice in the areas of: corporate formation; financing; tax; core contracts, intellectual property □ brand protection; operations; human resources; employee, vendor and investor relations; transactions (M □ A); and dispute resolution. Representative industries include: FinTech, Information Technology, E □ V - Commerce, EnergyTech, Public Relations, Hospitality, and Borrowed Personnel.

As a dispute resolution neutral, Jennifer is a mediator and arbitrator. She has more than 20 years' dispute resolution experience in all capacities. Her core areas of expertise as a neutral are in: Complex Commercial Business (IT □ P, Trade Secrets, Investment, Shareholder Derivative Actions, and Insurance); Employment, Family and Divorce, Municipal (NYC □ NYS); and Civil Rights (e.g. FLSA, Title VII; NYC □ NYS HR; □ 1983, NYPD, NYFD, NYC and NYS DOE, NYS and NYC DOH; ADA, ADEA; Age; Pregnancy; Title XII). Ms. Lupo sits on several state and federal court mediation panels and the Financial Industry Regulatory Authority (FINRA) arbitration panel. At present, she is onboarding with the American Arbitration Association as both an arbitrator and mediator.

During the 2017-18 academic year, Ms. Lupo is the Judith S. Kaye fellow of the *Historical Society of the New York Courts* and is teaching a course entitled "An Introduction to Civil Rights and Civil Liberties Law and History" to eight graders at the George Jackson Academy, a private, independent all-boys school in Manhattan educating academically exceptional boys of color.

Jennifer holds an A.B. from Bard College; an M.A. from SUNY Stony Brook, and a J.D. from Touro Law Center, with honors.

Thomas D. Mauriello, Esq.
Mauriello Law Firm, APC
San Diego, California

Tom Mauriello is the principal of the Mauriello Law Firm, APC in San Diego, which he founded after beginning his legal career at a large national plaintiffs' securities class action firm. The firm focuses on investment disputes representing investors in FINRA arbitrations and courts and also has represented registered representatives, broker dealers, institutional investors, and issuers in various contractual, operational, employment, and other matters. Tom is a member of the California, New Jersey and Pennsylvania bars. He received his BA from Brown University in 1983 and his JD from the University of San Diego School of Law in 1988. Prior to law school, he worked as a

paralegal at a New York City law firm registering securities offerings with the SEC and state securities agencies. After law school, Tom served as a judicial clerk to Judge Robert E. Cowen of the U.S. Court of Appeals for the Third Circuit. He is in his second term on the Board of Directors of the Public Investors Advocate Bar Association ("PIABA") as well as its current Secretary.

Michael Murman
Murman & Associates
Lakewood, Ohio

Michael E. Murman is the principal in Murman and Associates, Lakewood, Ohio. He is currently a Bar Examiner and formerly served as a member of the Board of Commissioners on Grievances and Discipline and the Commission on the Certification of Specialists of the Ohio Supreme Court. He has represented the relator as bar counsel and defended respondents in professional discipline cases. He is past Chair of the Legal Ethics and Professional Conduct Committee of the Ohio State Bar Association and recipient of the Ohio State Bar Association's Eugene R. Weir award for ethics and professionalism. He is a former municipal law director and prosecutor and past President of the Ohio Municipal Attorneys Association and Cuyahoga County Law Directors Association.

A substantial portion of Mr. Murman's practice is devoted to advising lawyers and judges in matters of legal ethics, judicial conduct, professional responsibility, and compliance with Ohio ethics statutes. He frequently provides opinions and testifies as an expert witness on probate, municipal law, and professional responsibility issues.

Mark Pugsley, Esq.
Ray, Quinney & Nebeker
Salt Lake City, Utah

Mark Pugsley is a trial attorney whose practice is focused on financial services litigation, FINRA arbitrations, and whistleblower cases filed with the SEC, CFTC and IRS. He frequently handles civil enforcement actions and regulatory investigations brought by the U.S. Securities and Exchange Commission (SEC), the Utah Division of Securities, the Commodity Futures Trading Commission (CFTC) and the Financial Industry Regulatory Authority (FINRA) involving individuals, brokers, brokerage firms and investment advisors.

Alan Rosca, Esq.
Goldman Scarlato & Penny, PC
Beachwood, Ohio

Alan focuses his legal practice on complex financial and commercial matters, particularly in the areas of securities litigation, investment fraud, banking industry litigation, antitrust index manipulation, and international disputes. He often represents institutional and individual investors in disputes with financial and banking industry members arising out of investment fraud or misconduct, or banking industry violations. He prosecutes claims on behalf of investors through class actions and FINRA arbitrations.

He is an adjunct professor of Securities Regulation at Cleveland-Marshall College of Law, Cleveland State University.

Alan received his Juris Doctor degree summa cum laude from Cleveland-Marshall College of Law in May 2008. While in law school he served as a Managing Editor of the Cleveland State Law Review, received the Dean's (full) scholarship for the entire Juris Doctor program, and won the "Best Oralist" award in the Jessup Moot Court competition, Pacific Region. Prior to law school, Alan was an investment analyst for a major financial data corporation and prepared investment research for fund managers.

He is licensed to practice law in the Ohio state and federal courts, and other federal courts nationwide.

Alan also holds a Master of Business Administration degree from Baldwin-Wallace College, Ohio.

Jeffery E. Schaff
Ardor Fiduciary Services, Ltd.
Northfield, Illinois

Jeffery Schaff is a principal shareholder of and consultant for the Ardor group of companies, independent, fee-only financial consulting practices specializing in the needs of fiduciaries. The private boutique collectively offers fiduciary, investment and financial consulting services to attorneys and fiduciaries, in tandem with private clients, trusts and companies.

Jeffery's investment management background began in 1987 while he was a college student. Initially a financial planner, his career path included becoming a stockbroker, managing a brokerage branch with over fifty stockbrokers and then forming an independent business with his own brokerage branch and registered investment advisory. In 2000, Jeffery dropped his brokerage licenses and founded a fee-only registered investment advisory firm.

Prior to developing the advisory practice, Jeffery augmented his investment management skills and experiences by earning the Certified Investment Management Consultant accreditation. To bolster an expertise in investment fiduciary responsibilities, Jeffery earned the Certified Fiduciary Auditor credential as a graduate of the inaugural program of the Center for Fiduciary Studies. This credential was later expanded and replaced by the Accredited Investment Fiduciary Analyst™, which Jeffery also earned in its inaugural program.

When Ardor expanded to offer fiduciary support and litigation support services, Jeffery's professional role expanded to include assisting attorneys with litigation proceedings and helping fiduciaries with their responsibilities and litigation mitigation. As an expert in securities regulations, investment advisor duties, portfolio management and investment fiduciary duties, Jeffery works with plaintiff/claimant clients as well as defendant/respondent clients in mediation, arbitration and court proceedings.

Andrea Seidt
Ohio Securities Commissioner
Columbus, Ohio

Andrea Seidt is a national leader in state securities regulation through her role with the North American Securities Administrators Association. Seidt has served as Commissioner of Securities since 2008. Prior to her appointment, she worked on investor and consumer protection litigation as Deputy Chief Counsel for the Ohio Attorney General's Office. She has also worked in private practice. Seidt received her undergraduate and law degrees from The Ohio State University.

Sam A. Silverstein, Esq.
Kaufmann Gildin & Robbins, LLP
New York, New York

Sam A. Silverstein concentrates his practice in the areas of securities arbitration, commercial litigation and general corporate law. He represents investors, brokers and brokerage firms in commercial disputes before the Financial Industry Regulatory Authority (FINRA). Mr. Silverstein also represents the firm's franchise and commercial clients in all phases of litigation, from pre-action investigation through trial and appeal.

Mr. Silverstein is a 2011 graduate from the Benjamin N. Cardozo School of Law, where he was a member of the Cardozo Securities Arbitration Clinic and the Cardozo Business Law Society. Prior to law school, Mr. Silverstein was a Vice President in the Private Wealth Management divisions of two broker-dealers where he helped to raise and manage nearly \$20 million in new capital for an advisory team that held over \$100 million under management.

Debra Speyer, Esq.
Debra Speyer Law Firm
Bala Cynwyd, Pennsylvania

Debra G. Speyer is principal of the Law Offices of Debra G. Speyer and handles arbitrations throughout the United States. When she is not at her law office, she can be found on her solar powered farm raising heritage Scottish long horned Highland cattle, Galloway cattle, Llamas, and Dorper and Kahadian sheep.

Before going into private practice in 1990, Debra was an attorney with the Enforcement Division of the National Association of Securities Dealers (now known as FINRA) prosecuting brokerage firms and stockbrokers for investment fraud and regulatory violations. Prior to that, she was an attorney and vice president with Thomson McKinnon Securities, Inc., an international brokerage firm which later merged with Prudential Securities. While at Thomson McKinnon, she passed every stockbroker and brokerage firm examination that the securities industry offered, including all options and commodities examinations.

Debra holds a law degree, a master's degree in finance with a thesis on program trading and stock markets, and a bachelor's degree in accounting. Prior to entering law school, she was an accountant. She has been listed in Philadelphia Magazine's Best Lawyers, SuperLawyers, Suburban Magazine and Mainline Magazine for her work handling securities fraud and elder law matters. She is also listed in Who's Who in American Law and Who's Who in America. She was honored by the National Organization of Women Business Owners with their "Women Making History" award. Debra is a member of the Million Dollar Advocates Forum for her securities arbitration work. The Million Dollar Advocates Forum is limited to attorneys who have won million - and multi-million-dollar verdicts and settlements.

Debra is a frequently invited guest speaker for business, professional and non-profit organizations, and is a legal commentator for radio talk shows and television. She has appeared on Wall Street Journal Radio, NBC TV, CNN Financial News TV, CNBC TV's "Wake Up Call" and "Power Lunch Financial News," The Suzanne Show, Anderson Cooper 360, CN8 TV, Fox News, and WB17, as well as Comcast TV's "Legal View" with the Securities and Exchange Commission Director speaking on topics related to securities fraud. Debra has written extensively about investment fraud and elder fraud, and those articles have appeared in various newspapers and magazines. She is frequently quoted in periodicals such as Newsweek, Kiplinger's Magazine, USA Today, Crain's New York Business, American Banker, The Street.com, Securities Week, Investment News, Registered Representative Magazine, the Philadelphia Inquirer, and Long Island's Newsday.

Debra is a lecturer for the Pennsylvania Bar Institute, Philadelphia Bar Association, AAJ, NBI, Public Investors Arbitration Bar Association and other continuing legal education programs on the subject of investment fraud, elder fraud, and elder law. She has been a co-lecturer with the Pennsylvania Securities Commissioner on the subject of investment fraud. She is co-chair of the Pennsylvania Bar Institute's annual course "Legal Issues in an Age of Aging," and was chair of an elder fraud conference in conjunction with the Philadelphia Corporation for Aging, the purpose of which was to educate senior citizens on how not to become victims of fraud. She was on the Lawyer Advisory Board of the Pennsylvania Securities Commission until that Board dismantled. She has also been an adjunct professor at Drexel Law School.

Debra has been chair of the Elder Law Committee, and is a member of the Securities Regulations Committee of the Philadelphia Bar Association. She was co-chair of the American Trial Lawyers Association's (now known as AAJ) Investment Fraud Committee of the Business Tort's Section, and serves on various committees and subcommittees of the American Bar Association, International Bar Association, Pennsylvania Bar Association, Public Investors American Bar Association, AAJ, Connecticut Bar Association, Florida Bar Association, New York State Bar Association and DC Bar Association. She is also an arbitrator for FINRA.

Pro bono work is an integral part of her law practice. She is on the Farmer Advisory Council of Waterkeepers Chesapeake which addresses environmentally responsible farming practices. She is on numerous other non-profit boards including AMIT Children in which she received an award from the organization for her fundraising efforts on behalf of abused and disadvantaged children.

Dennis Stubblefield
Stubblefield Expert Services
Washougal, Washington

Former SEC Enforcement attorney Dennis A. Stubblefield brings over 43 years' experience in representing clients in securities enforcement, and securities and employment litigation matters. Key to this representation is the strategic use of internal investigations. He also serves as an expert witness on matters involving Ponzi Schemes

and other major frauds, and broker-dealer compliance and supervision. He is a mediator of customer-advisor and securities industry disputes. Mr. Stubblefield has significant experience in matters involving microcap penny stock fraud, private placements, insider trading and parallel proceedings.

At the Securities and Exchange Commission, he investigated and litigated various cases, including the successful three-week trial against the perpetrators of a "pump-and-dump" manipulation scheme. As head of Enforcement at the then Miami Branch Office, he obtained both emergency and permanent injunctive relief to stop an oil and gas "boiler room" fraud; other assignments at the Commission included matters involving counterfeit securities, insider trading, accounting fraud, investment adviser fraud, broker-dealer failure-to-supervise, corporate governance, FCPA-related compliance, municipal securities and parallel proceedings.

Following the SEC, Mr. Stubblefield served in both private law firms and within major corporations, including broker-dealers and a major franchise system. At Stroock & Stroock & Lavan LLP, he was a senior member of a litigation team which obtained a rare summary judgment on behalf of two officers and directors in a securities "fraud-on-the-market" class action. As a partner at Shustak Reynolds & Partners, P.C., Mr. Stubblefield was in charge of the litigation and settlement of an SEC civil injunctive insider trading case (and follow-on administrative proceeding) against a former wirehouse registered representative (engagement through criminal defense counsel in a parallel criminal case brought by the United States Attorney's Office for the Southern District of California). His most recent corporate position was General Counsel of three AIG SunAmerica broker-dealers (also serving in the capacity of Chief Compliance Officer of two of those firms).

He is an adjunct professor of law at Lewis & Clark Law School, in Portland, Oregon, where he teaches Securities Regulation, and Business Law: Lawyering and Ethics. He regularly presents and writes on topics concerning securities regulation, broker-dealer compliance and supervision, and investment-related arbitration and mediation.

Mr. Stubblefield obtained his undergraduate degree in 1972 from University of California at Berkeley (A.B. Social Science Field Major), and was awarded his law degree (J.D.) in 1976 from University of Southern California Law Center, where he served as a Note and Article Editor of its Law Review. He is a member of the California State Bar and admitted to practice before the United States Court of Appeals, Ninth Circuit, and all California federal district courts. Mr. Stubblefield's office is in Irvine, California, and he can be reached at 760-533-0233, or dennis@dastubblefield.com.

2021 PIABA BOARD OF DIRECTOR BIOGRAPHIES

Philip M. Aidikoff, Esq., Director Emeritus
Aidikoff, Uhl & Bakhtiari
Beverly Hills, California

Philip M. Aidikoff is a partner in the law firm of Aidikoff, Uhl & Bakhtiari and exclusively represents clients in securities arbitration and litigation. Mr. Aidikoff graduated from the University of California at Berkeley in 1969 where he was on the Dean's List and obtained his Juris Doctor degree from Southwestern University School of Law in 1975 where he was a member of Law Review. He is a past President and Director Emeritus of the Public Investors Arbitration Bar Association (PIABA). He served a five-year term (with three years as chair) on the National Arbitration and Mediation Committee of FINRA (formerly the NASD) which provides recommendations on rules, regulations and procedures governing arbitrations, mediations and dispute resolution. He served as one of three public members of the Securities Industry Conference on Arbitration (SICA), which was created with the support of the Securities and Exchange Commission to help protect the interests of public investors in securities arbitration. He also served as one of two investor advocates on the Securities Investor Protection Corporation (SIPC) Modernization Task Force. He served as a member of the FINRA Arbitration Task Force (2014- 2015) which provided recommendations aimed at improving the transparency, impartiality and efficiency of securities arbitration. Mr. Aidikoff was recognized as a 2005, 2006, 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014, 2015, 2016, 2017, 2018 and 2019 Southern California Super Lawyer and was profiled in the February 2012 issue of Southern California Super Lawyers Magazine. He was also named by the National Law Journal as one of the 50 Litigation Trailblazers & Pioneers (2014). His legal rating as an attorney is the highest available "AV".

Mr. Aidikoff has spoken before numerous professional and lay groups on the topic of stockbroker abuse and the handling of arbitration and litigation involving brokers and firms. He has authored or co-authored a number of articles including: Broker Abuse: Recovering for your Client, Los Angeles Trial Lawyers Advocate (1993); Take it or Leave it: Case Evaluation and Retention, Practicing Law Institute Securities Arbitration Handbook (1995); Recognizing and Evaluating Stockbroker Liability, Consumer Attorneys Association of Los Angeles Convention (1995); The Brave New World of Banks Selling Securities: Offline and Online, Practicing Law Institute Securities Arbitration Handbook (1996); Stockbrokerage Firm Liability: A Pre-Litigation Analysis, Consumer Attorneys Association of Los Angeles Advocate (1996), reprinted in the Arizona Trial Lawyer Association Advocate (January 1997); Recognizing and Guarding Against Fiduciary Abuse, National Guardianship Association Annual Convention (1996); Control Person Liability in the Securities Industry: A Legal Overview and Practical Applications, Practicing Law Institute Securities Arbitration Handbook (1997); Liability of Control Persons at Second Tier Firms, Public Investors Arbitration Bar Association (1997); Clearing Firm Liability: A Forward Looking Analysis, Practicing Law Institute Securities Arbitration Handbook (1998); Why Shouldn't Clearing Firms be Liable, Public Investors Arbitration Bar Association (1998); Motion Practice in Securities Arbitration: A Claimant's Point of View, Public Investors Arbitration Bar Association (1999); Selective Recession and the Offset Defense in Securities Cases: A Survey of the Law, Public Investors Arbitration Bar Association (2000); After the Correction: Are Your Losses Recoverable?, American Pathology Foundation (2001); 2001: An Update On Best Execution and Suitability Standards For Online Trading, Public Investors Arbitration Bar Association (2001); Arbitration: Can It Be Waived?, Practicing Law Institute Securities Arbitration Handbook (2002); Comments on The Claimant's Bar On Proposed Changes In The Expungement Process, The Association of the Bar of the City of New York (2002); Due Diligence or Don't: Pre-Filing Considerations and Claim Drafting, Public Investors Arbitration Bar Association (2003); Confidentiality and Compliance Manuals: The Fight for Unfettered Access, Public Investors Arbitration Bar Association (2004), republished in the Practicing Law Institute (2005); From Wall Street to Main Street: A Guide to Litigation Over Hedge Funds Sold by Brokerage Firms to Retail Investors, Public Investors Arbitration Bar Association (2005); I Didn't Say That / Oh Yes, You Did: The Use of Court Reporters in Securities Arbitration, Public Investors Arbitration Bar Association (2005); Third Party Money Managers: Brokerage Firms' Duty to Monitor and Resulting Liability, Practicing Law Institute (2005); A Practical Guide To The New NASD Code of Arbitration Procedure For Customer Disputes, Practicing Law Institute Securities Arbitration Handbook (2006); republished Public Investors Arbitration Bar Association (2006); Trying Asset/Mortgage Backed Securities Cases: A Practical Guide, Public Investors Arbitration Bar Association (2007); Wall Street Does It Again: The Auction Rate Securities Fraud, Public Investors Arbitration Bar Association (2008); The Prospectus Defense: Defeating It As A Matter of Fact and Law, PIABA Bar Journal, Vol. 16, No. 4 (2009); Discovery of Regulatory Documents: Debunking the Myth of the "SEC" Privilege in Securities Arbitration, Public Investors Arbitration Bar Association (2010); Arbitrators Misclassified: Looking Back to Move Forward, PIABA Bar Journal Vol. 18, No. 1 (2011); Discoverability Of Wells Submissions: What They Are And How To Get Them, PIABA Bar Journal Vol. 19, No. 2 (2012); FINRA Six-Year Eligibility Rule 12206: The Purchase Date is Often Not the Triggering "Occurrence or Event Giving Rise to a Claim", PIABA Bar Journal Vol. 20, No. 1 (2013); Market Adjusted Damages in the FINRA Forum, PIABA Bar Journal Volume 21, No. 2 (2014), reprinted in the Consumer Attorneys Associations for Southern California Advocate (April 2016); and most recently published The Use of Third Party Subpoenas to Determine a Brokerage Firm's Pre-Hiring Due Diligence and Post-Hiring Supervision, Public Investors Arbitration Bar Association (2015).

Mr. Aidikoff has served on the faculty of the Practicing Law Institute (1996, 1997, 2002), NASD Fall Securities Conference (2002, 2004, 2005, 2006), NASAA Enforcement Conference (2002, 2004), NASAA Attorney Investigator Training Conference (2006), University of Cincinnati School of Law Symposium-Twenty Years after Shearson v. McMahon (2007), SCMA Conference (2005), NERA Securities Litigation Seminar (2004), New York City Bar Securities Arbitration program (2002), Los Angeles County Bar Association Securities

Arbitration program (2006, 2011, 2013 and 2015), the NASD faculty for training of discovery arbitrators, and on the JAMS faculty for training of securities arbitrators. He was a member of the NASD Neutral Roster Task Force (2005-2006), the FINRA Arbitrator Training Task Force (2009- 2010), FINRA Discovery Guide Task Force (2010–2013) and National Roundtable on Consumer and Employment Dispute Resolution, Pepperdine University 2012. He has appeared on CNBC, CNN, PBS Nightly Business Report, National Public Radio, CBS Radio, and the Business Channel addressing investor rights topics, and has been quoted on securities matters in the Wall Street Journal, the Dow Jones News Service, Newsweek, Reuters, Fortune Magazine, Business Week, Money Magazine, Bloomberg News Service, Forbes, Medical Economics, Registered Representative, The New York Times, USA Today, The Los Angeles Times, The Washington Post and other national and local press. For five years he wrote a weekly column in the Palm Springs Desert Sun on issues of interest to investors. (www.securitiesarbitration.com)

Robert S. Banks, Esq., Director Emeritus
Banks Law Office, P.C.
Portland, Oregon

Bob Banks has been practicing law for 36 years. He represents individuals and businesses in disputes with financial advisors, legal malpractice cases, and in business tort and minority shareholder rights cases. Mr. Banks has been an adjunct professor at Lewis and Clark Law School in Portland, Oregon. He practices at Banks Law Office PC in Portland, Oregon.

Honors

- 2017 Investor Champion Award, given by the North American Securities Administrators Association (NASAA)
- Distinguished Service Award, Public Investor Arbitration Bar Association (PIABA), 2016
- Distinguished Service Award, Federal Bar Association, Oregon Chapter
- Director Emeritus, PIABA
- PIABA President's Award, "For Leadership Efforts In Protecting Investors Throughout the Country"
- Oregon Super Lawyers, 2006 – 2019, every year that it has existed in Oregon
- Chambers Best Lawyers In America
- Best Lawyers in America – Securities Law
- Martindale Hubbell Law Directory, Highest Rating
- Multi-Million Dollar Advocates Forum

Bar Leadership Positions

- Past President and 10-year board member, PIABA
- Past Chair, Oregon State Bar Securities Regulation Section
- Past Chair, Oregon State Bar Alternative Dispute Resolution Section
- Past President, Federal Bar Association, Oregon Chapter
- Past Chair, FINRA Arbitrator Training Committee Task Force, 2008-2009

Current Bar Committees

- Investor Representative Member, FINRA National Arbitration and Mediation Committee (NAMC)
- Chair, Rules and Procedures Subcommittee for FINRA's NAMC
- Member, National Federal Judicial Selection Committee, American Constitution Society

Selected Publications

- "Securities Arbitration" Chapter in Oregon State Bar Manual on Arbitration and Mediation, to be published in 2019
- PIABA Bar Journal Vol. 21, No. 3 2014, Muzzling the Claimant: Due Process Denied in FINRA Expungement Hearing
- Northwest Securities Institute CLE, Investment Portfolio and Brokerage Statement Danger Signals, July 2013
osbar.inreachce.com
- Practicing Law Institute, 1 Securities Arbitration 2006 at 225, The NASD's Explained Awards Rule Filing
- Practicing Law Institute, 1 Securities Arbitration 2003 at 253, Clearing Firms and the 2002 Uniform Securities Act: What You Didn't Know Could Have Hurt You
- Practicing Law Institute, Securities Arbitration 2001 at 565, Clearing Firms, The Uniform Securities Act, and Koruga v. Fiserv Correspondent Services, Inc.
- Practicing Law Institute, Securities Arbitration 2000 at 995, Investor Protection-Not! SIPC and The Securities Investor Protection Act of 1970
- Practicing Law Institute, Securities Arbitration 2008 A Comment On the Financial Industry Regulatory Authority's Proposed Rules On Motions To Dismiss.

Selected Speaking Engagements

- "Challenges in Administering a Large Receivership" National Association of Federal Equity Receivers (NAFER) Seattle, Washington, (January, 2019)
- "Recent Developments at FINRA" Northwest Securities Institute, Seattle (May 2018)
- "View From the Claimant's Perspective" CNA Insurance Broker-Dealer Conference, Tampa (March 2018)

- “Becoming a FINRA Arbitrator,” with FINRA Executive Vice President and Director of Dispute Resolution, Richard Berry (April 2017)
- “Ethics Issues for Securities Lawyers” Oregon State Bar 35th Annual Northwest Securities Institute (April 2015)
- “What Every Securities Lawyer Should Know About Arbitration, Forum Selection, and Choice of Law Provisions” Oregon State Bar Securities Regulation Section Meeting (January 2014)
- “Remedies and Recompense: An Examination of Securities Arbitration and Class Actions” North American Securities Administrators Association (NASAA), Washington D.C., (October 7, 2013)
- “Detecting Anomalies in Investment Statements” Oregon State Bar seminar (July 16, 2013)
- “Recent Developments at FINRA,” 3rd Annual Northwest Securities Institute seminar (May 2013)
- “Securities Arbitration Cases” Oregon Trial Lawyers Association Business Litigation Section Meeting (February 2011)

Selected Court Decisions

- *Brown v. Price*, WL 3207235 2017 (D. Or. 2017) Representing Aequitas Investors
- *Amerivest v. Maloof*, Oregon Court of Appeals, No. A144457 (Pending) Representing North American Securities Administrators Association as Amicus Curiae
- *Boyer v. Salomon Smith Barney, Inc.* 344 Ore. 583 (2008) Representing Public Investors Arbitration Bar Association as Amicus Curiae)
- *Houston v. Seward* □ *Kissel, LLP*, 2008 U.S. Dist. LEXIS 23914 (March 27, 2008)
- *Marshall, et al. v. McCown DeLeeuw*, 391 F. Supp. 2d 880 (D. Idaho 2005)
- *Estate of Aguirre v. Koruga (I)* 2002 U.S. App. LEXIS 14632 (9th Cir. 2002)
- *Koruga v. Fiserv Correspondent Services, Inc.*, 183 F. Supp.2d 1245 (D.Or. 2001), 2002 U.S. App. LEXIS 6439 (9th Cir. 2002)

Prior Clients

Bob has served a broad array of individuals, organizations and groups, including physicians, teachers, gas pipeline workers, attorneys, judges, investment advisors, accountants, NBA basketball players, a former US Congressman, FINRA (opposing broker expungement), North American Securities Administrators Association and Public Investors Arbitration Bar Association (as amici curiae), retirees, and many others who have been victims of negligent investment advice and fraudulent conduct.

Educational Background

Reed College, B.A. 1977
University of Wisconsin Law School, J.D. 1982

Bar Memberships

Oregon, Washington.

Other

Finra Arbitrator Since 1989
Arbitration Services of Portland Arbitrator

Personal

Bob was born in New Jersey and grew up in upstate New York. He moved to Portland to attend Reed College and has considered himself to be an Oregonian for 40 years. He has completed 10 marathons, (2:46 PR), backpacked throughout the NW, and is an avid fly fisherman. He is married to Valerie Banks (25 years) and they have two adult sons.

Hugh D. Berkson, Esq. McCarthy, Lebit, Crystal & Liffman Co., LPA Cleveland, Ohio

Hugh D. Berkson is a Principal attorney with McCarthy Lebit Crystal □ Liffman Co., L.P.A., in Cleveland, Ohio, and focuses his practice in securities arbitration and litigation. After gaining extensive trial experience in both business and personal injury litigation, he began representing injured investors. Hugh tries and arbitrates investment cases and performs much of the required technical analysis.

Hugh obtained a business degree in Finance from the University of Texas at Austin and is a graduate of Case Western Reserve University School of Law, where he was a member of the Order of the Barristers and received both the American Jurisprudence Award (National Mock Trial) and the Jonathan M. Ault Mock Trial Prize. He later served as an Adjunct Professor at Case Western Reserve University School of Law, where he taught trial practice. Hugh is “AV Preeminent” rated by Martindale Hubbell, has been ranked as an Ohio “Super Lawyer” every year since 2013, and maintains a 10.0 “Superb” rating on Avvo.

Hugh has served on PIABA’s Board of Directors since 2011, and his term as President of PIABA ends with this annual meeting.

Scot D. Bernstein, Esq., Director Emeritus
Law Offices of Scot D. Bernstein
Folsom, California

Mr. Bernstein has practiced law in California since 1980. For more than a dozen years, he has concentrated his practice on representing plaintiffs in class actions. He has been named class counsel in more than 25 cases, including both employment (wage-and-hour) and privacy class actions. He has been co-counsel in successful appeals that resulted in published decisions as well. He also has served as counsel in cases involving securities and franchise law violations, unfair competition, unlawful business practices and false advertising. And he has handled numerous arbitration matters, including one that resulted in an unusual judgment that is viewable on his website.

Mr. Bernstein studied engineering and economics at UCLA, where he received his bachelor's degree Magna Cum Laude in 1977 and was an officer of the UCLA chapter of Tau Beta Pi, the engineering honors society. He was a member of Omicron Delta Epsilon (economics honors society) and Phi Beta Kappa as well. He received his Juris Doctor degree at Boalt Hall School of Law, University of California at Berkeley, in 1980.

Mr. Bernstein is a member of the board of directors of the California Employment Lawyers Association ("CELA"), an association of more than 1,200 attorneys dedicated to representing employees in employment disputes. He currently co-chairs CELA's Legislative Committee and serves on its Wage and Hour Committee as well.

Mr. Bernstein served for eleven years as a director of the Public Investors Arbitration Bar Association ("PIABA"), a national association of attorneys dedicated to representing investors in disputes with the securities industry. He has published numerous articles in the PIABA Bar Journal and its predecessor, The PIABA Quarterly. Since 2008, he has worked hard to help PIABA defeat multiple attempts to pass legislation that would have created a broad new exemption for securities sold through general solicitation and general advertising in California. More recently, he has negotiated with the sponsors of those prior bills to arrive at a bill, supported by PIABA, which would be beneficial to investor protection. Mr. Bernstein has given continuing legal education lectures to PIABA, the North American Securities Administrators Association, CELA and other professional groups on investors' rights and remedies and on employees' rights under the wage and hour laws. He is a member of the National Employment Lawyers Association ("NELA") as well.

Reported Cases. Mr. Bernstein has served as co-counsel in successful federal and state appeals:
Kirby v. Immoos Fire Protection, Inc. (2012) 53 Cal.4th 1244 (co-counsel for successful appellants);

Stop Youth Addiction v. Lucky Stores, 17 Cal.4th 553, 950 P.2d 1086, 71 Cal.Rptr.2d 731 (1998) (attorney for amicus curiae in support of successful appellant);

Lippitt v. Raymond James Financial Services, et al., 340 F.3d 1033 (9th Cir. 09/22/2003)

(co-counsel for successful appellant);

Lazarin et al. v. Total Western, Inc. (2010) 188 Cal.App.4th 1560, 116 Cal.Rptr.3d 596, review denied, Jan. 19, 2011, S188164 (co-counsel for successful appellant).

Mr. Bernstein has been recognized as a Northern California Super Lawyer □ every year from 2010 through 2019.

Steven B. Caruso, Esq., Director Emeritus
Maddox Hargett & Caruso, P.C.
New York, New York

Steven B. Caruso, the Resident Partner in the New York City office of Maddox Hargett □ Caruso, P.C. (www.investorprotection.com), concentrates his practice on the representation of individual, high net worth and institutional investors in securities arbitration and litigation proceedings.

Mr. Caruso is the Chairman and a public member of the National Arbitration and Mediation Committee ("NAMC") of the Financial Industry Regulatory Authority ("FINRA"); former Chairman of the Discovery Task Force Committee of FINRA; former member of the Nasdaq OMX BX Arbitration Committee; former member of the Securities Investor Protection Corporation (SIPC) Modernization Task Force; Director Emeritus and former President of the Public Investors Arbitration Bar Association ("PIABA"); testified before the U.S. House of Representatives, Committee on Financial Services, Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises, in March 2012 and September 2010; and has served as a judge for the Yale University Mock Trial Invitational Tournament and for Invest-Write, the national investment strategy writing competition sponsored by the Securities Industry □ Financial Markets Association (SIFMA) Foundation.

Among the publications that Mr. Caruso has authored are ***An Introduction to FINRA's National Arbitration and Mediation Committee***, The Neutral Corner, FINRA Dispute Resolution, Vol. No. 1 (2018); ***Post-Settlement Expungements: An Investor Protection Problem that Continues to Wait for a FINRA Solution***, Practising Law Institute, Securities Arbitration (September 2017); ***Non-Attorney Representatives – Do They Present a Clear & Present Danger to the Integrity of FINRA Arbitration***, Association of the Bar of the City of New York, New York, N.Y. (May 2017); ***Arbitrator Disclosures: Requests for Additional Information***, The Neutral Corner, FINRA Dispute Resolution, Vol. No. 4 (December 2016); ***Ethical Implications of the Phantom Designation of Expert Witnesses in FINRA Securities Arbitration Proceedings***, Practising Law Institute, Securities Arbitration (September 2016); ***Definition of a FINRA Customer: To Be or Not To Be – That Is the Ultimate Question***, Practising Law Institute, Securities Arbitration (July 2015); ***Discovery in FINRA Arbitration***, The Neutral Corner, FINRA Dispute Resolution, Vol. No. 2 (2015); ***FINRA Six-Year Eligibility Rule 12206: The Purchase Date is Often Not the Triggering Occurrence or Event Giving Rise to the Claim***, PIABA Bar Journal, Volume 20, No. 1 (September 2013); ***All Public Arbitrator Panels: A More Level Playing Field***, Practising Law Institute, Securities Arbitration (August 2013); ***Arbitrator Challenges Under the FINRA Code of Arbitration Procedure for Customer Disputes***, Practising Law Institute, Securities Arbitration (August 2010); ***The Mandatory Industry Arbitrator: An Endangered Species on the Precipice of Extinction***, Practising Law Institute, Securities Arbitration (August 2009); ***Sunshine May be the Best Disinfectant for What Ails Securities Arbitration: A Discussion of the 2008 SICA Empirical Study of Fairness***, Practising Law Institute, Securities Arbitration (August 2008); ***Effective Closing Statements From the Perspective of Counsel for the Customer-Claimant***, New York State Bar Association, Securities Arbitration 2007 (November 2007); ***Essential Principles for Honorable Arbitrators***, Practising Law Institute, Securities Arbitration (August 2007); ***Motions to Dismiss: A Predatory Tactic That Must be Extinguished***, Association of the Bar of the City of New York, New York, N.Y. (June 2007); ***Ethical Standards for Securities Arbitrators: A Statistical Perspective of Potential Partiality (Bias)***, Practising Law Institute, Securities Arbitration (August 2006); ***Arbitrator Training in the Securities Dispute Arena***, The Review of Securities & Commodities Regulation (January 2005); ***Discovery Objections Which are Irrelevant, Unduly Burdensome and are Reasonably Calculated to Lead to the Concealment of Admissible Evidence***, New York State Bar Association, Securities Arbitration 2004 (October 2004); ***Model Arbitrator Instructions: Luxury or Emerging Necessity***, Practising Law Institute, Securities Arbitration (August 2004); ***Ethical Considerations in Settlement Agreements***, Association of the Bar of the City of New York, New York, N.Y. (June 2004); ***Examination of the Adverse Broker: Unimpeachable Questions with an Internet Twist***, Practising Law Institute, Securities Arbitration (August 2001); ***On-Line Trading: The New Frontier***, Practising Law Institute, Securities Arbitration (July 1999); and ***NASD Arbitration Discovery Procedures : Knowing Your Customer From the Securities Professional Perspective***, American Bar Association, Section of Litigation, Committee on Securities Litigation (August 1995).

Jason Doss, Esq., Director Emeritus
The Doss Firm, LLC
Marietta, Georgia

Jason Doss has represented investors in NASD and FINRA arbitrations for approximately sixteen (16) years. The Doss Firm, LLC, established by Jason Doss in January 2009, is a successful law firm primarily devoted to representing aggrieved consumers across the United States against financial services companies for mismanaging investments and engaging in financial fraud. The attorneys of the firm have represented almost 1000 clients and have a combined 45 years of experience representing individual retail investors, institutional investors, and businesses in financial fraud litigation, securities arbitrations, and collective and class actions. Jason Doss has represented dozens of investor clients in disputes with broker-dealers involving the unsuitable recommendations of life insurance products including but not limited to fixed-indexed and variable annuities. Since its inception, The Doss Firm has recovered tens of millions of dollars for investors and consumers.

In 2018, Jason Doss was selected by a federal court to serve as one of twelve attorneys to lead the Equifax Data Breach case on behalf of all consumers and small businesses across the country. The case is currently pending in the United States District Court, Northern District of Georgia.

Jason Doss was primarily responsible for originating a nationwide consumer class action consisting of approximately 420,000 policyholders in equity-indexed annuities against Allianz Life Insurance Company, *Linda L. Mooney et. al. v. Allianz Life Insurance Company of North America*, 06-cv-545, United States District Court of Minnesota. His former law firm Page Perry, LLC was co-lead counsel with two other firms.

Jason Doss has co-authored two books, Doss, J. and Frankowski, R., *A Practitioner's Guide To Securities Arbitration* (2013), American Bar Association (225 pages) and Armstrong, F. and Doss, J., *The Retirement Challenge: Will You Sink or Swim?* (Jan. 2009), FT Press, Prentice Hall Publishing (266 pages). *A Practitioner's Guide To Securities Arbitration* is used by law schools and practitioners across the country as a resource to help navigate the FINRA arbitration process. *The Retirement Challenge: Will You Sink or Swim?* is in bookstores across the country and is designed to help consumers avoid the pitfalls of investing and avoid becoming a victim of financial fraud.

Jason Doss is a past-President of the Public Investor Arbitration Bar Association (PIABA), a bar association of attorneys that represent investors in FINRA arbitrations. He also founded The PIABA Foundation, a Foundation devoted to preventing investment abuse, and currently serves as its President. In addition, Jason Doss helped create the Investor Advocacy Clinic at Georgia State University College of Law, a law clinic that represents investors *pro bono* in FINRA arbitration with investment losses too small for them to hire a private attorney.

Over the last ten years, Jason Doss has been quoted many times by major publications and news organizations about topics involving financial fraud including USA Today, The Wall Street Journal, The New York Times, Reuters, The Associated Press, Bloomberg, AARP Magazine, The Street, and The Atlanta Journal Constitution.

Michael S. Edmiston, Esq.
2021 PIABA Executive Vice President/President Elect
Jonathan W. Evans & Associates
Studio City, California

Michael S. Edmiston is an Associate with Jonathan W. Evans □ Associates in Studio City, California. He has practiced with the firm since 2006. Prior to entering private practice, Michael served as a Senior Staff Attorney with NASD Dispute Resolution (now FINRA) in Los Angeles, California (1997-2001), and as a Business Manager with JAMS in Dallas, Texas and Orange, California (2001-2005).

His practice focuses on representing investors before FINRA, private commercial arbitration forums, and in state and federal court. His work continues to result in successful recoveries for clients by way direct negotiation, mediation, and contested arbitrations. Since 2006, Michael volunteers his time to the Legal Aid Society of Orange County working with senior citizens in a variety of civil and administrative matters.

In 2015, Michael became a Director of PIABA and currently chairs the Bylaws Committee. He is enjoying his first term serving and working with his fellow Directors, Members, and PIABA administrative staff. Michael has and continues to serve in various capacities with the PIABA Bar Journal from 2011 to 2016, including Editor (2011-2012), Managing Editor (2013), Editor in Chief (2014-2015), and Advisor (2016 to present). He also authored and co-authored articles and materials for the Bar Journal.

Michael is a 1994 graduate of Whittier College, with degrees in Business Administration and Economics. In 1997, he obtained his J.D. from Pepperdine University School of Law, and was admitted to the California Bar later that same year. He received his Master's Degree in Dispute Resolution from Pepperdine in 2001.

Samuel B. Edwards, Esq.
Shepherd, Smith & Edwards, LLP
Houston, Texas

Samuel B. Edwards is a partner in the law firm of Shepherd, Smith, Edwards □ Kantas, LLP located in Houston, Texas. Mr. Edwards and the other members of his firm have a nationwide practice devoted to representing investors against brokers, brokerage firms, banks, investment advisors, hedge funds and other financial professionals and companies who defraud and mistreat investors, both large and small. Over the years, Mr. Edwards and his firm have represented thousands of investors, including individuals, families, trusts, smaller banks, credit unions, pension plans, public institutions and state entities in litigation and arbitration across the United States and abroad against Wall Street. In addition to his full time practice, Mr. Edwards is on the Board of Directors of PIABA and the former Editor-in-Chief of the PIABA Bar Journal and a consistent contributing author and lecturer on securities issues. His articles have been printed in the PLI Handbook for Securities Arbitration and other well-known publications. Mr. Edwards is a member of the Texas, Michigan and California Bars as well as licensed to practice before numerous federal courts across the country. Mr. Edwards can be reached at (800) 259-9010 or mail to: sedwards@sselaw.com.

Adam Gana, Esq.
Gana LLP
New York City, New York

Adam Gana is the managing partner of Gana LLP. His practice focuses on all aspects of securities arbitration, complex commercial and business litigation. Adam's experience includes litigation in both State and Federal Courts as well as in various alternative dispute resolution venues. He has tried more than twenty-five cases to verdict before the state and federal trial and appellate courts, AAA, JAMS, NFA and FINRA.

Mr. Gana was named in the New York Super Lawyers Rising Stars □ for five straight years and most recently to Super Lawyers, ranked AV® Preeminent™ by Martindale - Hubbell™ (the highest honor offered), and ranked by the National Trial Lawyers as one of the Top 100 attorneys in the state of New York.

Robert J. Girard, II, Esq.
Girard Bengali, APC
Los Angeles, California

Robert J. Girard II, a founding partner of Girard Bengali, APC, has more than 19 years of experience in the areas of securities litigation, securities arbitration and employment disputes. He represents clients in Los Angeles, California, and throughout the state.

Before law school, Mr. Girard first completed his undergraduate education at the University of Maryland, College Park, in 1996. He then went on to attend the Seton Hall University School of Law, from where he graduated cum laude with his Juris Doctor in 2001. He was admitted to practice law in California in 2001. Following law school, Mr. Girard worked at two different major law firms in Los Angeles, specializing in securities arbitration and litigation. His skill and determination have allowed him to build a reputation as a dedicated and fierce representative of his clients' interests.

Mr. Girard advocates for institutional and individual investors in their legal disputes. He has recovered millions of dollars on behalf of his clients from a majority of the biggest Wall Street brokerages. In July 2017, Mr. Girard secured an award of \$1.8 million for an elderly couple who were victims of elder financial abuse, with over \$1 million of the award representing punitive damages. He also represents securities professionals in their employment disputes with broker-dealer firms. In one such case, Mr. Girard secured a \$3.7 million arbitration award against a FINRA member in California on behalf of individual brokers. In another case, Mr. Girard secured a highly favorable settlement for an individual broker who had been wrongfully discharged and obtained an award for expungement of his Form U-5 after proving the language was incorrect and defamatory in nature.

Dedicated to his profession, Mr. Girard is actively involved in multiple legal organizations. His memberships include the Public Investors Arbitration Bar Association (PIABA), Los Angeles County Bar Association, the Italian American Lawyers Association of Los Angeles, the Beverly Hills Bar Association and the National Association of Independent Brokers-Dealers, Inc.

Marnie C. Lambert, Esq.
Lambert Law Firm, LLC
Columbus, Ohio

Marnie C. Lambert is a 1992 graduate of the Pepperdine University School of Law in Malibu, California. She has represented investors across the country in securities disputes with their brokerage firms in FINRA arbitrations (and in court) since 2005, handling hundreds of such cases. She has spent the remainder of her legal career primarily representing consumers in complex civil litigation, commercial litigation and class actions.

Ms. Lambert is the founding member of Lambert Law Firm, LLC, a firm committed to protecting consumers from bad actors of all types and sizes. Ms. Lambert is licensed to practice law in all state courts and federal district courts in Ohio and California.

Christine Lazaro, Esq.
St. John's University School of Law
Queens, New York

Christine Lazaro is an Associate Professor of Clinical Legal Education and the Director of the Securities Arbitration Clinic at St. John's University School of Law. The students in the Clinic represent investors in arbitration claims against brokerage firms and brokers on a pro bono basis. Professor Lazaro also teaches Broker-Dealer Regulation and Business Basics at St. John's, and is a faculty advisor for the Moot Court Honor Society and the Corporate and Securities Law Society. She joined St. John's in 2007 as a Supervising Attorney for the Clinic. Professor Lazaro is also currently Of Counsel to the Law Offices of Brent A. Burns, LLC, where she consults on securities arbitration and regulatory matters.

Professor Lazaro has been a member of the Public Investors Arbitration Bar Association (PIABA) since 2008. She currently serves on the Board of Directors, co-Chairs the Fiduciary Standard Committee, and is a member of the Legislation Committee, the SRO (Self Regulatory Organization) Committee and the Securities Law Seminar Committee. She also serves on the New York State Bar Association's Securities Litigation and Arbitration Committee.

Professor Lazaro holds a B.A. from New York University and a J.D. from Fordham Law School. After graduating from law school and prior to joining St. John's, she was an associate at Davidson & Grannum, LLP, representing broker-dealers and individual brokers in disputes with clients in both arbitration and mediation, and handling employment law cases and debt collection cases. She also advised broker-dealers regarding investment contracts they had with various municipalities and government entities.

She speaks and writes regularly on the topics of securities arbitration and the duties of brokers and brokerage firms.

Seth Lipner, Esq., *Director Emeritus*
Bernard M. Baruch College
New York, New York

Seth E. Lipner is a Professor of Law at the Zicklin School of Business of Bernard M. Baruch College in New York City, and a member of the firm Deutsch □ Lipner in Garden City, New York. Mr. Lipner is the author of numerous scholarly articles and law books on fields as diverse as international trade law, securities arbitration and law and technology. As a member of Deutsch □ Lipner, Mr. Lipner focuses his practice on representing investors, employees and other individuals with grievances against providers of financial services.

Mr. Lipner served as President of the Public Investors Arbitration Bar Association (PIABA) in 2000-01 as well as in 1994-95 and served as Secretary to the organization and on its Board of Directors since the organization's inception in 1990 until 2006, and now holds the title "Director Emeritus." He has appeared on CNN, NPR, BBC and the Wall Street Journal Report, and is often quoted in publications such as Forbes, Business Week, Newsweek, the Wall Street Journal, the New York Times, Newsday, the New York Law Journal and the National Law Journal. Mr. Lipner speaks often to bar groups, and in continuing legal education programs, including the New York State Bar Association, Association of the Bar of the City of New York, Practising Law Institute and PIABA. Mr. Lipner served on the National Arbitration and Mediation Committee of the NASO from 1998 to 2002, and was at one time a member of the Board of Editors at Securities Arbitration Commentator.

Mr. Lipner publishes extensively on various aspects of arbitration, particularly those involving NASO and NYSE member firms. The text of many articles is accessible at DeutschLipner.com. Mr. Lipner's treatise, Securities Arbitration Desk Reference (written together with Emeritus Professor Joe Long (deceased) and Professor William Jacobson) is available from Thomson West. His essay, "The Case Against Restitution," was published on the Op-Ed page of The New York Times on May 2, 2003.

Mark E. Maddox, Esq., *Director Emeritus*
Maddox Hargett & Caruso, P.C.
Fishers, Indiana

Mark E. Maddox is a founding partner of Maddox Hargett & Caruso, P.C., one of the nation's largest legal practices concentrating on the representation of securities investors. He has concentrated his career representing investors in disputes with stockbrokers and their firms.

From 1989 - 1991, Mr. Maddox served as the Securities Commissioner for the State of Indiana. During his tenure, he also served on the Indiana Governor's Initiative on Economic Development Policy Panel. Mr. Maddox also led the International Enforcement Committee of the North American Securities Administrators Association as its Chairperson. He served on the Board of Directors of the Public Investor Arbitration Bar Association from 1994 - 2002 and from 2014-2017, and was its President from 1998 - 2000. Mr. Maddox was also a public representative on the NASD Regulation's National Arbitration and Mediation Committee from 1996 - 1998 and 2003 - 2005, and was appointed its Chair for the 2004 - 2005 term. He was admitted to practice before the U.S. Supreme Court in February 1995.

In 1991, Mr. Maddox opened his current private practice that concentrates in the representation of investors in securities arbitration, litigation and regulation. He is a member of the Indianapolis Bar Association and the Indiana State Bar Association where he is a Past Chair of the Securities Sub-Committee. He is an adjunct professor at Butler University where he teaches Business Law to undergraduates.

Mr. Maddox is a graduate of Wabash College (magna cum laude), and earned his J.D. from Vanderbilt University in 1986. He has been a speaker and lecturer for various Continuing Legal Education and securities-related seminars and has been published extensively, most notably the book *Investor Rights for the 21st Century* (2001).

Thomas D. Mauriello, Esq.
2021 PIABA Secretary
Mauriello Law Firm, APC
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Tom Mauriello founded the Mauriello Law Firm, APC in 1996 after working at a large national plaintiffs' securities class action firm and several small firms. Tom focuses on investment and consumer disputes, with customer FINRA arbitrations constituting a large part of his practice. He also handles business litigation, consumer class actions, and appeals.

Tom is a member of the California, New Jersey and Pennsylvania bars. He received his BA from Brown University in 1983 and JD from the University of San Diego School of Law in 1988. Prior to law school, he worked as a paralegal in New York City for a law firm registering securities offerings with the SEC and state securities agencies. Following law school, Tom served as a judicial clerk to Judge Robert E. Cowen of the U.S. Court of Appeals for the Third Circuit.

Tom serves on the Administration of Justice Committee and the Mandatory Fee Arbitration Committee (as an attorney-client fee arbitrator) with the Orange County Bar Association. He also serves on the PIABA Legislation Committee and participated in PIABA's "Hill Day" in March 2016. From 2012 through 2015, Tom served as Co-Chair of the Legal Committee of the Angeles Chapter of the Sierra Club.

When he is not working, Tom enjoys spending time with his 17-year old daughter, surfing, wine tasting, fitness boot camp, traveling, and playing keyboards in several rock bands.

Dave P. Meyer, Esq.
2021 PIABA President
Meyer Wilson Co., LPA
Columbus, Ohio

David P. Meyer is the founding principal of the five attorney law firm Meyer Wilson. He has represented approximately 1,000 individual investors from all across the country in securities arbitration and litigation against all major brokerage firms. His firm has recovered more than \$350 million for its clients. David has the honor of winning the largest jury verdict in Ohio history; a class action verdict against Prudential Securities on behalf of 200 retirees.

He is listed in the Best Lawyers in America (2011-2017) in multiple categories and has been AV-rated for many years. He is a member of the PIABA Board of Directors.

David holds a business administration degree from Ohio University and a law degree and masters degree in tax law from Ohio's Capital University Law School. He is admitted to practice law in the states of Ohio and Michigan.

David P. Neuman, Esq.
Israels & Neuman PLC
Bellevue, Washington

David Neuman has been representing the interests of investors and consumers for over a decade. Before co-founding Israels & Neuman in the Summer of 2014, Mr. Neuman worked for over seven years at a law firm in Chicago which focused its practice on representing aggrieved and defrauded investors, mostly in FINRA arbitration. Through his years of experience, Mr. Neuman has represented over one thousand investors in hundreds of FINRA and court cases, on behalf of clients from over 40 states as well as investors from the international community. He has represented these clients from the inception of the case to their finish, including several that have gone to an arbitration hearing.

In addition to representing investors in FINRA Arbitration, Mr. Neuman has represented investors in numerous courts throughout the U.S., including victims of a Ponzi scheme in Utah, dozens of investors in Colorado state and federal court who lost money in a bond fund, successfully opposing an action to enjoin an arbitration in Idaho, intervening and opposing class action settlements in Iowa and Texas, opposing motions to vacate arbitration awards in Alabama and California, and representing investors of a failed hedge fund in Illinois. Mr. Neuman has also represented persons deceived by their insurance brokers and parties in shareholder disputes.

Prior to his work representing defrauded investors, Mr. Neuman worked for another law firm in the Chicagoland area which focused on consumer and commercial class action litigation. During law school, he also worked for a law firm that handled a number of NASD arbitrations and personal injury matters.

Mr. Neuman is currently on the Board of Directors of the Public Investors Arbitration Bar Association ("PIABA") and is the chair of the Legislation Committee of PIABA. He is also an arbitrator with FINRA Dispute Resolution.

Mr. Neuman was admitted to practice law in the State of Illinois in November 2005, the State of Florida in April 2010, and the State of Washington in 2014. He has also been admitted to the United States District Courts for the Western District of Washington, the Northern District of Illinois, the Central District of the Illinois, the District of Colorado, and the U.S. Court of Appeals, Seventh Circuit.

Mr. Neuman graduated with Honors from the University of Illinois in December 2001 with a B.S. in Finance. He attended the Northern Illinois University College of Law and graduated Magna Cum Laude in May 2005. While at the NIU College of Law, Mr. Neuman was on Law Review and was an Associate Justice for the Moot Court Society. In addition, during his time at the NIU College of Law, he also was a research assistant for Professor David Gaebler and researched various areas of contract, commercial, and consumer law.

Timothy J. O'Connor, Esq.
The Law Offices of Timothy J. O'Connor
Albany, New York

Timothy J. O'Connor maintains a private practice of law in Albany, New York and is licensed in New York and Florida. He has been representing investors in securities brokerage customer claims since 1985. Mr. O'Connor has been a solo practitioner since 2005, after having been affiliated with Ainsworth Sullivan for 21 years.

A graduate of Middlebury College (A.B. Economics, 1980) and the University of Denver College of Law (J.D. 1984), Mr. O'Connor was nominated in the Fall of 2003 as the Inaugural Visiting Clinical Instructor for the Investor Rights Project Securities Arbitration Clinic of Albany Law School of Union University in Albany, New York, funded through the efforts of New York State Attorney General, Eliot Spitzer, from the proceeds of a settlement obtained against several national securities brokerage firms involving allegations of analyst fraud and wrongdoing. Mr. O'Connor served in this adjunct position through 2005.

In addition to his private practice, he is currently an Adjunct Lecturer at State University of New York at Albany, teaching courses in Law in Financial Market Regulation and Technology in Financial Market Regulation.

He has also widely written on a number of topics relating to the topic of investors rights. Most recently, "Trends in Supervisory and Clearing Firm Liability"(New York State Bar Association Continuing Legal Education Department – "Securities Arbitration and Mediation 2017: The Courage to Simplify" – April 6, 2017).

Darlene Pasieczny, Esq.
2021 PIABA Treasurer
Samuels Yoelin Kantor, LLP
Portland, Oregon

Darlene Pasieczny (pronounced "Pah-shetch-nee") is a securities and fiduciary litigator and FINRA arbitrator, and leads the Investor Defenders practice group at Samuels Yoelin Kantor LLP, based in Portland, Oregon. Darlene works all stages of securities litigation and FINRA arbitration, fiduciary litigation in trust and estate disputes, elder financial abuse, and complex civil litigation. She represents investors nationwide to recover investment losses caused by financial advisor misconduct or defective securities products. Previously, Darlene worked at Banks Law Office PC, where she developed her concentration on securities litigation and FINRA arbitration.

Darlene brings a particular sensitivity to working with the all-too frequent targets of securities fraud and financial abuse: retirees and women investors. She helps her clients not only recover financial losses, but also rebuild trust in a professional advisor.

She serves on the Board of Directors of the Public Investors Arbitration Bar Association (PIABA) and is sought after as a speaker on securities law, FINRA arbitration, and estate matters. Other professional affiliations include the Oregon State Bar, Washington State Bar, U.S. District Court for the State of Oregon, Multnomah Bar Association, and the Gus J. Solomon American Inn of Court. Darlene earned a B.A. from Reed College, *Phi Beta Kappa*, an M.A. from Columbia University, and J.D. from Lewis and Clark Law School, *magna cum laude*. www.InvestorDefenders.com

Joseph C. Peiffer, Esq.
Peiffer Rosca Abdullah & Carr
New Orleans, Louisiana

Mr. Peiffer is a partner at Peiffer Rosca Abdullah & Carr. His practices consists of representing individuals and institutions in FINRA arbitration, prosecuting ERISA class actions, representing victims of labor trafficking and those that have suffered catastrophic injury.

Mr. Peiffer has represented hundreds of individual retirees against their brokers in FINRA arbitration. The highlights of this practice include representing 32 Exxon retirees in a 90-day FINRA arbitration against Securities America that resulted in a \$22 million verdict -- one of the largest ever awarded by a FINRA arbitration panel. He has also represented hundreds of Xerox and Kodak retirees against their broker resulting from the broker's fraudulent advice to retire and subsequent unsuitable investments. He currently represents clients against British Petroleum arising from the oil spill that occurred in the Gulf of Mexico. He was recently part of the legal team that filed a temporary restraining order to stop BP from paying dividends to its shareholders before it could show that it could pay to clean up the Gulf. Also, he currently represents the Louisiana Firefighters Retirement Fund in their case against Northern Trust concerning securities lending. Additionally, he represents the Baylor College of Medicine and about 25 other hospitals and municipalities in cases against their investment banks arising out of their issuance of auction rate securities. He also is on the plaintiffs' steering committee in a nationwide antitrust class action involving the illegal tying of cable set-top boxes to the provision of premium cable services and in the leadership of an ERISA class action arising out of securities lending.

Mr. Peiffer was one of three Louisiana lawyers ranked by Chambers USA for securities litigation. He has been quoted by *USA Today*, *Wall Street Journal*, the Associated Press, *New York Times*, *New York Daily News*, *The Los Angeles Times*, *Business Week*,

Investment News, and many other publications. Mr. Peiffer has also appeared on CNN. He was named as one of the fifty Leaders in Law by *New Orleans City Business Magazine*.

He has also taught and lectured extensively. He is co-authored a book on Litigating Business Torts for West, a Thomson Reuters Business. He co-created and taught a class entitled *Storytelling and Advocacy* at Loyola Law School. Also, at Loyola Law School, he has taught a course entitled "The Basics of Arbitration" and he also serves as an adjunct professor teaching Trial Advocacy. He has guest lectured at Tulane Law School in its Securities Regulations class and Syracuse Law School on securities arbitration. He has spoken at many national conventions on a variety of topics including prosecuting large, multi-client claims, broker's deficient advice to retire and FINRA arbitration.

Mr. Peiffer graduated from Tulane School of Law, *cum laude*, in 1999. While at Tulane, he served on the Tulane Law Review and was involved with the Tulane Legal Assistance Program. Prior to attending Tulane, he graduated from Bowling Green State University in 1996 with a major in communications. While at Bowling Green, he worked as the General Manager of the campus radio station and City Editor of the daily newspaper.

Mr. Peiffer has also successfully represented criminal defendants on a pro bono basis. He is a member of the Louisiana State and American Bar Associations. He also is a member of the American Association for Justice where he served as past Chairman for the Business Torts section. He is also a member of the Public Investors Arbitration Bar Association where he serves on the Board of Directors and was recently elected Executive Vice President.

Brian N. Smiley, Esq., Director Emeritus
Smiley Bishop & Porter LLP
Atlanta, Georgia

Brian Smiley is a partner in the firm of Smiley Bishop & Porter LLP. He was born in Augusta, Georgia, and grew up in Atlanta. He attended Emory College, where he was initiated into Phi Beta Kappa and from which he graduated with highest honors in 1975. Following graduation, he attended Emory University School of Law, where he served on the Board of Editors of the Emory Law Journal and was initiated into the Order of the Coif.

Upon graduation (with distinction) in 1978, Mr. Smiley received an appointment as a Trial Attorney in the United States Department of Justice. While at the Justice Department, Mr. Smiley acted as counsel for the Government in numerous cases that were deemed by the Attorney General to be of unusual importance to the United States, including *Nixon v. United States*, various constitutional cases and litigation involving the NATO treaty.

In 1981, Mr. Smiley returned to Atlanta from Washington, and entered into the private practice of law. As a litigator, Mr. Smiley has handled constitutional and civil rights suits, products liability claims, personal injury litigation, commercial controversies, shareholders' derivative suits, fidelity bond and RICO suits, and securities litigation and arbitration. For over 20 years, Mr. Smiley has concentrated in the securities field, primarily representing investors in FINRA arbitrations.

Mr. Smiley is the author of numerous articles including: "Stockbroker-Customer Disputes-Making a Case for Arbitration," (*Georgia State Bar Journal*, May 1987); "Spotting Common Forms of Stockbroker Misconduct" (*The Verdict*, Jan. - Feb. 1991); and, "The Law and Ethics of Witness Preparation" (*Practicing Law Institute*, 1998). He has spoken at numerous seminars sponsored by the Public Investors Arbitration Bar Association and has been quoted on securities matters in the national press.

Mr. Smiley is a frequent lecturer on the topics of stockbroker misconduct, the handling of litigation and arbitration involving stockbrokers, and legal ethics. He has testified as an expert at special hearings about the "penny stock" industry conducted by the Secretary of State of Georgia. Mr. Smiley testified before the United States Senate Committee on Banking, Housing and Urban Affairs, Securities Subcommittee, on the topics of "penny stock" fraud and securities industry arbitration.

In 2002, Mr. Smiley was appointed to the National Arbitration and Mediation Committee (NAMC). The 13 members of the NAMC advise the Board of Directors of FINRA, which is the world's largest forum for handling arbitration and mediation of disputes between clients and brokerage firms. The NAMC is actively involved in the drafting of arbitration rules and the recruitment, training and evaluation of arbitrators.

He has been elected to serve on the Board of Directors of PIABA for three terms and was honored to act as PIABA's President in 2008-2009.

Jeffrey R. Sonn, Esq.
Sonn Law Group, PA
Aventura, Florida

Jeffrey Sonn focuses his practice principally on securities litigation and arbitration matters, as well as business litigation, and class actions. Mr. Sonn is the managing partner of Sonn & Erez, and has handled over 1,000 of securities cases in his career. Mr. Sonn is “AV” rated by Martindale Hubbell, the highest rating for ethics and legal ability available by this independent ratings organization.

Mr. Sonn regularly lectures on the topic of securities litigation and securities fraud. Presently, Mr. Sonn is a lecturer at the Miami Dade County Police College on the subject of financial advisor fraud. Mr. Sonn has also served as a guest lecturer on securities fraud at the University of Miami Securities Law Clinic.

Mr. Sonn serves as a Director of the Public Investor Arbitration Bar Association (PIABA). Mr. Sonn is the author of many securities related articles, including *Top Ten Things to Do During a Final Hearing* (PIABA), *Top Ten Mistakes to Avoid in a Final Hearing* (PIABA), *Elder Abuse and the Securities Industry* (PIABA), *Ponzi Schemes, Picking up the Pieces from a Fallen House of Cards* (“Securities Arbitration in the Meltdown Era” Practising Law Institute, 2009), *The ABC’s of Mortgage Backed Securities* (PIABA), *The Broker Went Bankrupt—Now What?*(PIABA), *Survey of Arbitrator Misconduct, Group Arbitration Techniques* (PIABA), *How CPAs Can Detect Stockbroker Fraud*, and *Top Ten Mistakes To Avoid In an Arbitration Hearing*, as well as other securities-related publications.

During his career, Mr. Sonn has litigated numerous cases to successful resolution, recovering hundreds of millions of dollars for victims of investment fraud. He won a \$50 million final judgment in *Katz v. MRT Holdings*, one of the few cases under Private Securities Litigation Reform Act passed in 1995 to yield a final judgment on the merits. Mr. Sonn also served on the Plaintiffs’ Steering Committee that successfully negotiated a \$70 million dollar settlement for hundreds of investors who were the victims of the Medical Capital and Provident Shale Royalties Ponzi Schemes.

Mr. Sonn has acted as trial counsel to verdict in a number of successful cases, including *First Union vs. the FDIC and Hollywood Associates* (a \$16 million dollar verdict), *Madhany v. Citigroup* (\$11.1 million verdict), *Regas v. Painewebber* (a \$2.2 million dollar verdict), and *Tartell v. Krieger Financial* (\$1.7 million dollar verdict).

Mr. Sonn has also represented United States Bankruptcy Trustees and Court appointed receivers as counsel in securities fraud and Ponzi scheme cases. Mr. Sonn has also served as an expert witness in securities fraud cases on issues involving attorneys fees.

Prior to founding the Firm in 1995, Mr. Sonn was associated with the Miami-based securities-litigation firm Gilbride Heller & Brown; and the bankruptcy law firm of Mishan, Sloto, Hoffman and Greenberg.

Mr. Sonn has served as a legal correspondent and commentator on securities fraud and Ponzi schemes for CNBC, CBS, BBC Radio, ABC and MSNBC. Mr. Sonn served as a CNBC legal contributor on the Bernard Madoff Ponzi Scheme for the CNBC shows “On the Money” and the documentary “Scam of the Century, Bernie Madoff and the \$50 Billion Dollar Heist.”

Mr. Sonn also appeared in the television show “American Greed” on CNBC, about representing victims of the \$1 Billion Dollar Ponzi Scheme by convicted Fort Lauderdale attorney Scott Rothstein. Sonn & Erez represented victims in the Rothstein case and pushed the Rothstein law firm into bankruptcy when the fraud was discovered.

Mr. Sonn graduated from the University of Florida in 1984 and from University of Miami Law School in 1988. Mr. Sonn was an Associate Editor of the University of Miami InterAmerican Law Review.

Mr. Sonn is admitted to practice law in the State of Florida, the United States District Courts for the Southern and Middle Districts of Florida, and the 11th Circuit Court of Appeals.

Andrew J. Stoltmann, Esq.
Stoltmann Law Offices
Chicago, Illinois

Andrew Stoltmann, attorney and investor advocate, exclusively concentrates his practice in representing investors who are the victims of investment fraud. He has represented over one thousand individuals in lawsuits and securities arbitration actions against brokerage firms like LPL, Merrill Lynch, Morgan Stanley Dean Witter, Wachovia, Linsco, Prudential, Baird, Edward Jones, AG Edwards and Smith Barney and has tried approximately 80 cases. Previous to opening the Stoltmann Law Offices P.C. he was a partner in a law firm concentrating its practice in the representation of investors in lawsuits, arbitration claims and class actions against brokerage firms.

Mr. Stoltmann is currently an adjunct securities law professor at Northwestern University School of Law in Chicago. Mr. Stoltmann was the Editor-In-Chief of the PIABA (Public Investor Arbitration Bar Association) Bar Journal, a law journal for the national association of securities attorneys who represent investors in claims against brokerage firms and stockbrokers, from 2001 through 2005. Mr. Stoltmann is also the co-author of the book "Investor Rights for the Year 2000 and Beyond."

After graduating from the University of Wisconsin (Madison) with a Bachelor of Business Administration degree, Mr. Stoltmann worked as a licensed stockbroker for Olde Discount and Merrill Lynch. While in law school at DePaul University, Mr. Stoltmann clerked at the Chicago NASD Dispute Resolution office, where 95% of securities arbitration cases are decided.

Mr. Stoltmann has appeared as a guest providing legal opinions, commentary and analysis on CNN, CNBC, BBC, CBC, CBS, CNN-FN, Bloomberg TV and National Public Radio. Mr. Stoltmann has been quoted in various publications worldwide including the Wall Street Journal, Christian Science Monitor, Business Week, Forbes, Fortune, USA Today, Chicago Tribune, Los Angeles Times, Kiplinger's, Jerusalem Post, London Post, London Free Press, The Guardian (UK), Daily Telegraph of London, Montreal Gazette, Maclean's, Calgary Herald, Toronto Globe & Mail, Toronto Star, Mainichi Daily News (Tokyo), China Daily (Beijing), Mail & Guardian (Johannesburg), National Post, and The Scotsman (Edinburgh).

Mr. Stoltmann is a member of PIABA (Public Investor Arbitration Bar Association), ATLA (Association of Trial Lawyers of America), the Chicago Bar Association, Illinois State Bar Association and is admitted to the United States District Court for the Northern District of Illinois and the Eastern District of Wisconsin.

ETHICAL ISSUES RELATED TO ATTORNEY ARTICLES ON BAD BROKERS, PRODUCTS, OR ISSUERS: HANDLING TAKEDOWN REQUESTS, CEASE-AND-DESIST LETTERS

Alan Rosca, Michael Murman, Joshua Kons

Given the necessity of online advertising for lawyers as well as the unique nature of the Claimant FINRA practice, targeted blog posts or other online advertisements regarding individual financial advisors, brokerage firms, investment products, or issuers are a necessity. However, as one can imagine, targeted blog posts or internet advertisements can give rise to cease-and-desist letters from the targets of such advertisements. Fortunately for those doing the marketing, the laws of defamation and false light hold those claiming defamation to strict proof and absolute defenses if such posts are done correctly.

Application of the Model Rules of Professional Conduct

These limitations are found in Rule 7.1 Model Rules of Professional Conduct. Ordinarily we look to this rule as a limitation on what lawyers can say about the services they are offering, but the rule is not that limiting. False or misleading statements about another are another form of “false or misleading advertising.” In egregious cases the advertising lawyer might also run afoul of Rule 8.4(c) prohibiting lawyers from engaging in conduct involving dishonesty, fraud, deceit, or misrepresentation.

Among the practical questions to consider are:

- What happens if there is an inadvertent error in a blog published by a lawyer, and how to address that when lawyer becomes aware? Is there an obligation to update?

The answer is, absolutely, yes. Follow the example of the newspapers and promptly publish a “correction.” Experience indicates that disciplinary authorities are not eager to devote resources to “advertising” issues, and especially when the lawyer promptly acknowledges and corrects “mistakes.”

- If the broker’s counsel contacts the lawyer, how to handle the situation where the counsel makes threats of professional complaints?

Refer the lawyer to Model Rule 1.2 (e), “Unless otherwise required by law, a lawyer shall not present, participate in presenting, or threaten to [resent criminal charges or professional misconduct allegations solely to obtain an advantage in a civil matter.” (Note that if the lawyer tries to wiggle out from Rule 1.2, by claiming some noble purpose not connected to advantage in the civil matter, he or she will find themselves on the horns of the dilemma by acknowledging they are willing to violate Rule 8.3 (a), which requires them to inform a disciplinary authority if what they are accusing the publishing lawyer of is a violation of the Rules.)

The Elements of a Defamation Claim Favor the Advertising Attorney

Many targets of attorney advertisements will almost always claim such advertisements are defamatory, without appreciating how difficult proving such claims actually are.¹ Generally, other legal claims that could be asserted by a plaintiff financial advisor such as false light, trade libel, and other forms of defamation are subject to the same analysis and constitutional defenses as that of defamation. Therefore, insulating advertisements from defamation claims may prevent other potential claims as well.

Most of the claims made by those financial advisors issuing cease-and-desist letters would involve defamation of a private figure regarding a matter of public concern.² For purposes of this discussion, we will look at a California law on this matter (although the law may vary slightly in other jurisdictions). The standard legal elements as set forth in the California pattern jury instructions of a claim of defamation of a private figure regarding a matter of public concern are as follows³:

Plaintiff claims that Defendant harmed [him|her|nonbinary pronoun] by making [one or more of] the following statement(s): [list all claimed per se defamatory statement(s)].

To establish this claim, Plaintiff must prove both liability and damages as follows:

A. Liability

1. That Defendant made [one or more of] the statement(s) to [a person|persons] other than Plaintiff;
2. That [this person|these people] reasonably understood that the statement(s) [was|were] about Plaintiff;
3. That [this person|these people] reasonably understood the statement(s) to mean that [insert ground(s) for defamation per se, (e.g., "Plaintiff had committed a crime");]
4. That the statement(s) [was|were] false; and
5. That Defendant failed to use reasonable care to determine the truth or falsity of the statement(s).

¹Be wary of those investment products or issuers that have registered trademarks, as use of those marks may give rise to additional causes of action beyond common law defamation and false light such as unfair competition and Latham Act claims.

²The primary difference between a matter of public concern versus a private concern is the applicable burden of proof on the plaintiff.

³"In a defamation action against a newspaper by a private person suing over statements of public concern, however, the First Amendment places the burden of proving falsity on the plaintiff. As a matter of constitutional law, therefore, media statements on matters of public interest, including statements of opinion which reasonably imply a knowledge of facts, 'must be provable as false before there can be liability under state defamation law.' " Eisenberg v. Alameda Newspapers, (1999) 74 Cal.App.4th 1359, 1382 [88 Cal.Rptr.2d 802], internal citations omitted.)

B. Actual Damages

If Plaintiff has proved all of the above, then [he/she/nonbinary pronoun] is entitled to recover [his/her/nonbinary pronoun] actual damages if [he/she/nonbinary pronoun] proves that Defendant's wrongful conduct was a substantial factor in causing any of the following:

- a. Harm to Plaintiff's property, business, trade, profession, or occupation;
- b. Expenses Plaintiff had to pay as a result of the defamatory statements;
- c. Harm to Plaintiff's reputation; or
- d. Shame, mortification, or hurt feelings.

C. Assumed Damages

If Plaintiff has not proved any actual damages for harm to reputation or shame, mortification, or hurt feelings but proves by clear and convincing evidence that Defendant knew the statement(s) [was/were] false or that [he/she/nonbinary pronoun] had serious doubts about the truth of the statement(s), then the law assumes that Plaintiff's reputation has been harmed and that [he/she/nonbinary pronoun] has suffered shame, mortification, or hurt feelings. Without presenting evidence of damage, Plaintiff is entitled to receive compensation for this assumed harm in whatever sum you believe is reasonable. You must award at least a nominal sum, such as \$1.00.

Before even touching on defenses, you can see how difficult a claim of defamation would be for a financial advisor, issuer, or brokerage firm to prove. As for liability, they would not only have to prove falsity (which would be difficult if not impossible if such advertisements are tracking public sources of information), but would also have to show that the lawyer failed to use reasonable care to determine the truth or falsity of such statements. However, it is damages where their case would really fall part.

As for actual damages, it would be difficult if not impossible to prove that an advertisement was the actual and proximate cause of any sort of actual harm to their business or profession, as any such statements likely stem from an underlying FINRA disclosure which is the actual cause. As such, actual damages are extremely hard to prove.

As for any assumed damages, the Supreme Court has generally held that a Plaintiff must first prove actual damages before being awarded any presumed damages.⁴

⁴Our accommodation of the competing values at stake in defamation suits by private individuals allows the States to impose liability on the publisher or broadcaster of defamatory falsehood on a less demanding showing than that required by *New York Times*. This conclusion is not based on a belief that the considerations which prompted the adoption of the *New York Times* privilege for defamation of public officials and its extension to public figures are wholly inapplicable to the context of private individuals. Rather, we endorse this approach in recognition of the strong and legitimate state interest in compensating private individuals for injury to reputation. But this countervailing state interest extends no further than compensation for actual injury. For the reasons stated below, we hold that the States may not permit recovery of presumed or punitive damages, at least when liability is not based on a showing of knowledge of falsity or reckless disregard for the truth." *Gertz v. Robert Welch, Inc.*, (1974) 418 U.S. 323, 348–349 [94 S.Ct. 2997, 41 L.Ed.2d 789].

Furthermore, presumed damages requires proof of actual malice or recklessness.⁵ This actual malice requires clear and convincing evidence.⁶ Even if actual damages could be established, defendants would have a strong argument that any sort of “shame or harm” would not be caused by the republication of underlying factual, privileged information disclosed by FINRA – and not by the advertisement. Assuming attorneys track publicly available sources for the underlying information, it would not be possible to prove actual malice or recklessness.

Advertising Attorneys Have Multiple Affirmative Defenses to Raise Against Defamation Claims

Even if a financial advisor plaintiff could run the gauntlet on proving the elements of defamation, defendant attorneys have a powerful absolute defense that they can rely on – truth. Truth is an absolute defense to defamation claims. Pattern jury instructions reflect this defense as follows:

Defendant is not responsible for Plaintiff’s harm, if any, if Defendant proves that [his/her/nonbinary pronoun/its] statement(s) about Plaintiff [was/were] true. Defendant does not have to prove that the statement(s) [was/were] true in every detail, so long as the statement(s) [was/were] substantially true.

Attorneys can take comfort in the defense of truth in their advertising practices. Once again, assuming the underlying source information is non-confidential, public and accurate, there is no liability for defamation so long as the communication is “substantially true”. In other words, advertising attorney are insulated for minor inaccuracies so long as the substance of the communication is true.⁷ In other words, a statement is not considered false unless it would have a different effect on the reader than a true statement.⁸

In addition to the absolute defense of truth, advertising attorneys have a host of other powerful defenses at their disposal including statutes of limitation (which are very short in defamation cases), consent (by virtue of their form U4 reporting requirements), fair and true reporting privilege, and other privileges.

⁵Private-figure plaintiffs must prove actual malice to recover punitive or presumed damages for defamation if the matter is one of public concern. They are only required to prove negligence to recover damages for actual injury to reputation. Khawar v. Globe Internat., (1998) 19 Cal.4th 254, 273–274 [79 Cal.Rptr.2d 178, 965 P.2d 696].

⁶“To prove actual malice . . . a plaintiff must ‘demonstrate with clear and convincing evidence that the defendant realized that his statement was false or that he subjectively entertained serious doubts as to the truth of his statement.’ ” Khawar, supra, 19 Cal.4th at p. 275, internal citation omitted.

⁷“California law permits the defense of substantial truth and would absolve a defendant even if she cannot ‘justify every word of the alleged defamatory matter; it is sufficient if the substance of the charge be proved true, irrespective of slight inaccuracy in the details.’ ‘Minor inaccuracies do not amount to falsity so long as ‘the substance, the gist, the sting, of the libelous charge be justified.’ ” (GetFugu, Inc. v. Patton Boggs LLP (2013) 220 Cal.App.4th 141, 154 [162 Cal.Rptr.3d 831], internal citation omitted.)

⁸“Put another way, the statement is not considered false unless it ‘would have a different effect on the mind of the reader from that which the pleaded truth would have produced.’ ” (Jackson v. Mayweather (2017) 10 Cal.App.5th 1240, 1262–1263 [217 Cal.Rptr.3d 234].)

Anti-SLAPP Statutes also Offer Advertising Attorneys a Powerful Tool to Dismiss Claims against Protected Free Speech

In addition to defenses, some jurisdictions with “anti-SLAPP” statutes such as California and Connecticut allow defendants to file a motion to strike any sort of lawsuit regarding “any act . . . in furtherance of the person’s right of petition or free speech under the United States Constitution or the California Constitution in connection with a public issue.”⁹

Under the statute, the rights of free speech or petition in connection with a public issue include four categories of activities: statements made before a legislative, executive or judicial proceeding; statements made in connection with an issue under consideration by a governmental body; statements made in a place open to the public or a public forum in connection with an issue of public interest; and any other conduct in furtherance of the exercise of free speech or petition rights in connection with “a public issue or an issue of public interest.”¹⁰ Anti-SLAPP motions can dispose of defamation lawsuits early, and entitled the defendant to recovery of their attorneys fees if such motions are granted.

Practical Takeaways for Advertising Attorneys

Attorney advertising is a necessity in today’s law practice, and is a necessity for virtually every PIABA member. Accurate attorney advertisements are nothing to fear, nor or cease-and-desist letters received by financial advisors, brokerage firms, or issuers. Although the path of least resistance in many cases is to accommodate those sending letters by simply removing such if such advertisements have not yielded a response, the law is on the side of the advertising attorney who has truthful (or even substantially truthful) advertisements which comply with the applicable rules of professional conduct.

⁹Cal. Civ. Proc. Code § 425.16 (2019).

¹⁰Cal. Civ. Proc. Code § 425.16(e) (2019).

LITIGATING IN DIFFERENT FORUMS: JAMS, AAA, FINRA AND COURT

Debra Speyer

This panel addresses the differences between the most popular arbitration forums. Those forums are FINRA, AAA, JAMS and CPR. There are some substantial and some subtle difference between them which will be discussed by our seasoned panel. While most cases you will see with FINRA based brokerage firms will be with FINRA arbitration, the Investment Advisory firms and non FINRA members will use some of the other arbitration services.

American Arbitration Association

AAA is a non-profit that was founded more than ninety years ago. It has thousands of arbitrators on its National Roster. Most of their arbitrators are retired judges and lawyers and currently practicing lawyers. The lawyers are primarily trial lawyers with specific specialties.

AAA has multiple sets of rules. Investment firm disputes will be either under the Consumer rules or the Commercial rules. Employment cases are under the Employment rules. Under the Consumers rules, the amount of fees the consumer has to pay are capped to \$200 if the consumer brought the action and the consumer pays zero if the business brought the action. The business pays the bulk of the costs associated with the arbitration including the arbitrator fees. Under the Commercial rules, the amount of fees the consumer pays are not capped and are paid up front. If the arbitration clause does not set forth if the action will be under the Commercial or the Consumer rules, the parties can go to court for a ruling which the AAA will honor. Alternatively if the parties do not go to court, the AAA will evaluate and initially make a ruling based on its Consumer Due Process Protocol Statement of Principles and their rules. This Protocol was developed in association with the American Bar Association. The clause does not state if this falls under consumer or commercial. Even if the arbitration clause states the Commercial rules apply, and the consumer bringing the actions states they cannot afford to pay, AAA can override the arbitration clause and put the parties into the Consumer rules section.

AAA Consumer Rules

AAA has developed the Consumer Arbitration Rules for its arbitrations. The AAA's role is administrative only. It manages the administrative aspect of the arbitration such as appointment of arbitrators, preliminary decisions as to where hearings might take place, and handling the fees associated with the arbitration. AAA charges an administrative fee for their services. In the event of the consumer's extreme hardship, the AAA may defer or reduce the consumer's administrative fees. Arbitrators are compensated at a rate established by the AAA. Arrangements for the compensation of arbitrators are made through the AAA and not directly between the parties and arbitrators. The AAA may require the parties to deposit in advance of the hearing the sums of monies necessary to cover the cost of the arbitrator's fees. Once the arbitration is concluded, the AAA will render an account and return any unused money.

The AAA maintains a National Roster of arbitrators. If the arbitration clause does not set forth how arbitrators are selected, the parties have the ability to appoint their own arbitrators that are not on the National Roster. If they do not appoint arbitrators nor agree to a process, the AAA will administratively appoint an arbitrator from its National Roster. Under AAA rules if the parties have

not agreed to or if the arbitration agreement has not set forth the number of arbitrators, then the dispute shall be heard by one arbitrator. For cases under \$25,000 with no counterclaims, the dispute can be heard on the documents only. However, either party can ask for a hearing. If a claim is low enough to be considered a small claims court matter, the AAA does not have to accept jurisdiction and can direct the parties to small claims court.

Pre Hearing Preparation. If the parties request or if the AAA Administrator or the arbitrator decides to hold one, they will schedule a preliminary management hearing with the parties or their representatives as soon as practical. This hearing is conducted by telephone. The arbitrators will promptly issue a written order with their decision.

Location of the Hearing. At the request of either party, the AAA may hold a telephone conference with the parties or their representatives to discuss the location of the hearing. Even if the arbitration clause sets forth a hearing location near the business being sued, the AAA can decide a different location based on the Consumer Due Process Protocol.

Discovery. If the parties do not voluntarily share discovery or identify witnesses, a party can ask the arbitrator to decide. The arbitrator may direct specific documents and other information to be shared between the consumer and business as well as the parties identify witnesses.

Written Motions. The arbitrator may consider a party's request to file a written motion (except for Dispositive Motions (i.e. Motion to Dismiss) but only after the parties and the arbitrator conduct a conference call to attempt to resolve the issues that give rise to the proposed motion. Only after this conference call will the arbitrator consider a party's request to file a written motion.

Written Record of Hearing. If a party wants a written record of the hearing, that party must make arrangements with a stenographer and notify the opposing party, the AAA and the arbitrator.

The arbitration may proceed even if a party or representative is absent so long as proper notice was given and the party failed to appear or ask for a postponement. There are no default awards. The arbitrator shall require the party who participates in the hearing to submit the evidence needed by the arbitrator to make an award.

Awards are rendered within thirty calendar days from the close of the hearing.

AAA Commercial Rules.

There are limited differences between the Consumer Rules and the Commercial Rules.

Appointment of National Roster arbitrators. If the parties have not appointed an arbitrator and have not provided any other method of appointment, AAA shall appoint arbitrators by sending an identical list of ten names from the National Roster. Each party has fourteen calendar days to strike names objected to and rank the remaining names. The parties can choose the chairperson. If none is chosen within fourteen calendar days, the AAA will choose one.

A Claim or counterclaim of at least \$500,000 exclusive of interest, attorneys' fees, arbitration fees and costs are put through using the Large and Complex Commercial Disputes rules.

JAMS

JAM is a for profit organization started in 1979 by a judge in California. Panel members are charged a fee to be on the arbitration list to be chosen from. Some of the highlights of the differences is:

JAMS arbitrators charge by the hour.

JAMS Comprehensive Arbitration Rules and Procedures are used to govern disputes that exceeds □250,000 not including interest or attorneys' fees.

Arbitrator Selection. If the parties do not agree on an arbitrator, JAMS may facilitate agreement among the Parties regarding selection of the Arbitrator. If the Parties do not agree on an Arbitrator, JAMS shall send the Parties a list of at least five Arbitrator candidates in the case of a sole arbitrator, and ten arbitrators in the case of a three arbitrator panel. Within seven days of service each Party may strike two names in the case of a single Arbitrator and three names in the case of a three Arbitration panel. If there are too many strikes to form a panel, then JAMS shall designate the sole Arbitrator or as many members of the tree arbitration panel as is necessary to complete the panel.

Preliminary Conference. At the request of any Party or at the direction of the Arbitrator, a Preliminary Conference shall be conducted with the Parties or their counsel.

JAMS has an expedited procedure with more limited discovery.

JAMS allows for depositions.

CPR

CPR was formed in 1977. It is an independent nonprofit organization. Its niche is the international ADR market. Although it has administered arbitrations, it distinguishes itself as having non administered arbitrations for those clients who prefer non-administered arbitrations and look to CPR assistance for specific functions such as arbitrator selection. The non-administered arbitrations are managed by parties counsel and the arbitrators. CPR has two sets of arbitration rules – international and domestic for the administered arbitrations and two sets of rules – international and domestic for the non-administered arbitrations.

The administered arbitrations are useful as well as CPR has multilingual staff and international and provides assistance with arbitrator selection, resolution of challenges to arbitrators, timeliness of awards, mediation queries and other key aspects of the arbitral process.

FINRA

PIABA membership is quite familiar with the FINRA arbitration system. The highlights are that it is an administered arbitration system. Public Chair list consists of ten potential arbitrators with four strikes per party. The public arbitrator panel list provides for fifteen potential arbitrators with six strikes per party. The non-public list consists of ten potential arbitrators with ten strikes per party. There is a base administrative fee based on the value of the claim. The arbitrators are paid by the session.

TIPS FOR ZOOM HEARINGS AND ADVOCACY: AN ARBITRATOR AND MEDIATOR'S PERSPECTIVE

Pierre F de Ravel d'Esclapon, FINRA Mediator and Public Arbitrator

A veritable plethora of how-to guides to virtual hearings is available on the internet. The points below are far from exhaustive as I do not discuss the pros and cons of various platforms, the critical issues of cyber security beyond that which is provided by FINRA, how to organize the pre-hearing conference, time allocations, agreed by the parties or ordered by the panel, recording (FINRA handles it), oath by witnesses,

A. Understand and Master the Technology

1. Physical set-up

- a. use a desktop or laptop or a tablet
- b. fast internet connection
- c. use a good quality webcam
- d. use a table microphone preferably
- e. pay attention to proper lighting
- f. use dual monitors
- g. limit the chat function to messages to everyone.

2. Appearance and behaviour

- a. learn how to position the camera to project the impression you are looking at the arbitrators in the eyes-avoid the shifty eyes syndrome which occurs when your eyes move down or sideways to look at a document -having a second monitor helps
- b. maintain decorum in dress and appearance
- c. sitting is better than standing. Note: the further you are from the camera the more of you and your body language the panel will see.

3. Avoid distractions

- a. mute the microphone when not speaking
- b. turn off cell phones and office phones
- c. Use of virtual background: helps reduce distractions but can lead to jerky movements

4. Preparation

- a. do a dry run with your client and witnesses, make sure they have technology adequate for the task: having a client join by phone from a car does not do much to help your case.
- b. have a backup plan in case of technological glitches
- c. have a list of cell phone numbers

B. Handling documents

1. distribute a list of exhibits before the hearing, try to have stipulated exhibits joint exhibits, mark clearly stipulated facts
2. have your exhibits ready to be marked
3. ask the panel during the PHC if they want paper copies in addition to e-copies: paper copies are much easier for arbitrators especially if the documents are voluminous.
4. know how to use the shared screen function. Even if you have supplied paper copies to the panel know how to show on a shared screen a particular document or excerpt from a document.
5. It helps to know how to bookmark documents and or to create hyperlinks to retrieve documents easily and help the panel retrieve them during the hearing.

C. Handling Witnesses

1. make sure the witness is in a room alone. The use of a 360 degree camera is recommended. No coaching via e-mail!
2. develop a technique for courteous interjection of objections
3. Witnesses should not use virtual backgrounds: in a natural background the panel will find it easier to see that no one else is in the room coaching the witness and it makes it easier to "read" the witness.
4. provide breakout rooms for counsel and parties to confer.
5. make sure the parties are not talking over each other.
6. consider the use of a proctor in the room where the witness testifies to ensure no coaching by any means.

D. Managing Time

1. Be very well organized: virtual hearings exacerbate rambling, lack of organization, fumbling by counsel.
2. have clear objectives of what you want to get out of each witness
3. In a virtual world there is a premium for simplification and concision-no grandstanding in front of clients
4. speak much more slowly than you would in person and tell the same to your witnesses.

5. Don't be afraid to ask for breaks: virtual hearings are more tiring than in-person ones.

Conclusion

-In virtual hearings the chair has an even greater role in maintaining the smoothness of the proceedings, muting participants when proper etiquette is not observed or when more than one person speaks.

-Reading witnesses and assessing credibility: in some ways better than in person. The speaker view allows the panel to have close-ups of the faces and body language, better read of micro-expressions

-easier to see the counsel's and client's reaction to testimony

-as easy as in person to assess pauses, shifting eyes, hand covering mouth etc.

-much more efficient in many ways: no travel time, easier to schedule and far less costly.

-to be effective counsel must be mindful of the difficulties for the panel and strive to make the panel's task easier by being very well organized and prepared.

-virtual panel deliberations are a big plus and improve the process-very efficient.

Virtual works!

Further resources:

-AAA-ICDR Virtual Hearing Guide <https://go.adr.org/covid-19-virtual-hearings.html>

-American College of Trial Lawyers: <https://www.actl.com/home/news-publications/position-statements-white-papers> Mastering Zoom Advocacy; Conducting Remote Hearings

-JAMS has a series of short and useful articles of virtual hearings
<https://www.jamsadr.com/online/publications-details>

-ABA: <https://www.americanbar.org/groups/litigation/committees/childrens-rights/articles/2020/privacy-and-confidentiality-tips-for-virtual-hearings/>

-NYSBA: <https://nysba.org/products/conducting-a-virtual-evidentiary-hearing-in-arbitration-2020/> ; <https://nysba.org/events/handling-the-virtual-hearing-nysba-trial-academy-virtual-conference-webinar/>; <https://nysba.org/nysbas-definitive-guide-to-virtual-lawyering/>

-NYCLA :

<https://www.nycla.org/iParts/Common/ContentBlock/PostDefault.aspx?iUniformKey=eae03c3a-eb7e-444d-8ff1-7b3e0b6a38a2&ReplyOptions=4f157f78-bd79-48f8-8164-b198c1137218&TagKeys=&DefaultHtmlSessionKey=e8d8edfe-2790-48db-8463-043b011e77ed&WebsiteKey=80d9b981-d8fc-4862-bcde-1e1972943637>

AAA-ICDR PANELIST RESOURCE GUIDE FOR VIRTUAL ARBITRATION HEARINGS

This Resource Guide provides information which AAA arbitrators may find helpful when the parties to a particular matter have chosen to conduct their arbitration hearing via a videoconferencing platform. The information contained in this Guide can be applied or modified in ways to fit the specific needs of any particular case. Based on the circumstances of a specific case, arbitrators or parties may make decisions about their virtual hearing or take actions different from those provided in this Guide.

Clicking each of the topics below will take you to resources for that topic.

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USING AAA-HOSTED
VIRTUAL HEARINGS



USING PERSONAL VIDEO
CONFERENCING ACCOUNTS



USING PARTY VIDEO
CONFERENCING ACCOUNTS



VIRTUAL ARBITRATION
HEARINGS DISCLAIMER



RISKS OF
VIRTUAL ARBITRATION HEARINGS



COMPARISONS OF VIDEO
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ZOOM Tutorials



USING AAA-HOSTED VIRTUAL HEARINGS

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Upon request by an arbitrator, or upon the agreement of the parties, the AAA-ICDR will provide access to a third party platform to host an arbitration proceeding. Under those circumstances, the AAA-ICDR will utilize the Zoom platform. The AAA-ICDR has trained staff to utilize the Zoom video conferencing platform and has purchased Zoom Pro licenses. AAA Panelists not familiar with Zoom may want to consider getting a free Zoom account to familiarize themselves with the platform's features and navigation. Panelist may also contact their AAA case manager for additional information or assistance. Links to various tutorials of the Zoom platform can be found here: [Zoom Tutorials](#)

The following documents provide access to helpful information and guidance about AAA virtual arbitration hearings conducted using the Zoom platform. These "Virtual Hearings" documents can be found on the AAA-ICDR [COVID-19 Update](#)* page under the "Our Perspectives" section.

- Virtual Hearing Guide for Arbitrators and Parties Utilizing Zoom
- Order and Procedures for Virtual Hearing via Videoconference

****Press and hold the CTRL key then click the link to open the COVID-19 Page in a new browser tab.***



USING PERSONAL VIDEO CONFERENCING ACCOUNTS

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Upon request by an arbitrator or with the agreement of the parties, the arbitrator may provide access to a third party videoconferencing platform (e.g., Zoom, GoToMeeting, Microsoft Teams, etc.) to host an arbitration proceeding being administered by the AAA (see [AAA Guidelines for Virtual ADR Proceedings](#)). Particular attention should be paid to the contents of the [Considerations for Recording Virtual Hearings](#). If using the Zoom platform, please refer to the suggested default settings here: [AAA-ICDR Suggested Zoom Default Settings for Virtual Hearings](#). Links to various tutorials for the Zoom platform can be found here: [Zoom Tutorials](#). Any concerns regarding the use of a third party videoconferencing platform should be raised by copying correspondence to all parties to any particular matter.

The following documents provide access to general information and guidance about virtual arbitration hearings conducted using videoconferencing platforms. These “Virtual Hearings” documents can be found on the AAA-ICDR [COVID-19 Update](#)* page under the “Our Perspectives” section.

- Virtual Hearing Guide for Arbitrators and Parties
- Order and Procedures for a Virtual Hearing via Videoconference

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USING PARTY VIDEO CONFERENCING ACCOUNTS

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AAA Panelists conducting virtual arbitration and mediation proceedings administered by the AAA using a video conferencing account (e.g., Zoom, GoToMeeting, Microsoft Teams, etc.) provided by either a party or a party's representative, should make an inquiry to determine whether the parties have (i) made their own investigation as to the suitability and adequacy of the video conferencing platform for its proposed use for the virtual ADR proceeding, (ii) assessed any risks of using the platform regarding its security, privacy or confidentiality, and (iii) have mutually agreed to using the platform for the arbitration or mediation. Panelists may contact their AAA case manager for assistance with such an inquiry. Any concerns regarding the use of a third party video conferencing platform should be raised by copying correspondence to all parties to any particular matter. Should the parties and the arbitrator(s) wish to use the videoconferencing platforms recording feature, if any, particular attention should be paid to [Considerations for Recording a Hearing](#).

The following documents provide access to general information and guidance about virtual arbitration hearings conducted using videoconferencing platforms. These "Virtual Hearings" documents can be found on the AAA-ICDR [COVID-19 Update](#)* page under the "Our Perspectives" section.

- Virtual Hearing Guide for Arbitrators and Parties
- Order and Procedures for a Virtual Hearing via Videoconference

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AAA Guidelines for Virtual ADR Proceedings

AAA Panelists conducting virtual arbitration and mediation proceedings using personal video conferencing accounts (e.g., Zoom, GoToMeeting, Microsoft Teams, etc.) should follow the guidelines below established by the AAA for such proceedings conducted under its auspices. If following these guidelines is not possible, please contact your AAA case manager to discuss alternative video conferencing options.

1. The arbitrator(s)/mediator should possess a sufficient level of competence with whatever platform they propose using so as to facilitate the proceedings without delay or disruption.
2. The video conferencing platform must have security features sufficient to safeguard the confidentiality of the process and all such security features are enabled.
3. The platform's technology must provide for fair, equal and reasonable right of access to all participants.
4. The platform must guarantee equal opportunity for parties to reasonably present evidence and testimony, including direct and cross-examination of witnesses.
5. The platform must be able to accommodate participants having lesser technical capabilities and know-how.
6. The platform must provide the means to verify the identity of all participants.
7. The platform must provide the means for all participants [or the witness] to always be in view of the camera.
8. The platform must provide a means for sequestering witnesses.
9. The platform must provide the means to disclose and clearly identify relevant documents.
10. The platform's recording feature(s), if any, must be able to be enabled/disabled.
11. The arbitrator(s)/mediator must have a contingency plan in place, e.g., a back-up conference line, should the primary platform fail or otherwise become impractical.

Considerations for Recording Virtual Hearings

Should the case participants opt to use a videoconferencing platform's recording features, they should be fully aware of the platform's Terms of Service and the conditions under which the session will be recorded should be formalized and shared with case participants in advance of the hearing.

The recommended process for recorded sessions that are not conducted with AAA Zoom accounts is to use cloud storage (files sizes of recordings are quite large) and have the platform's account owner send a link to the recording to case participants as directed by the arbitrator(s) or as identified in the procedural order. The link should be password protected and the password should be sent separately from the communication containing the link. In cases where there is direct exchange, and where the arbitrator is the account holder, the arbitrator can send the recording link (or links if there is more than one day) to the parties directly, followed by an email with the password for the link. For cases without direct exchange where the arbitrator is the account holder, both the link and the password should go through the AAA case manage to be sent to the parties.

The recipients should have seven (7) calendar days to download a local copy of the recording via the link, after which the cloud recording should be deleted. The recipients are responsible for maintaining security around and controlling access to their locally stored copies of the recordings.

Should the case participants opt to not use cloud storage and save the recording locally, the host on whose computer the file is stored must (i) ensure that the space on their computer is sufficient to save the recordings, (ii) ensure to arrange to transmit the file to the specified case participants in a secure manner (such as via Citrix ShareFile or other file sharing tools) and, (iii) also take steps to maintain the security around and control access to their locally stored copy of the recording and to secure its deletion after the case concludes.



Appendix A

AAA-ICDR Suggested Zoom Default Settings for Virtual Hearings

Schedule Meeting Settings

Configuration Section	Default Setting	Comments
Host Video	On	Allows for default to video so participants can see who is in attendance
Participants Video	On	Allows for default to video so participants can see who is in attendance
Audio Type	Telephone and Computer Audio	Allows participant to choose which has better sound quality for them
Join Before Host	Off	Keeps one party and arbitrator from being in the room together
Use Personal Meeting ID (PMI) when scheduling a meeting	Off	We must use the "generate automatically" option to randomly create a new meeting code per hearing in order to keep someone who has a link from a prior meeting from joining
Use Personal Meeting ID (PMI) when starting an instant meeting	Off	PMI not to be used
Only authenticated users can join meetings	Off	This means that the meeting participants will have to sign in to their Zoom account to join the meeting. Would require every arbitrator/party/participant/witness to create a zoom account.
Require a password when scheduling new meetings	On	
Require a password for instant meetings	On	
Require a password for Personal Meeting ID (PMI)	Off	PMI not to be used
Embed password in meeting link for one-click join	Off	
Mute participants upon entry	Off	More appropriate to be managed by host and as needed
Upcoming meeting reminder	Off	Not needed as Outlook invitations should be used

In Meeting (Basic) Settings

Configuration Section	Default Setting	Comments
Require Encryption for 3rd Party Endpoints (H323/SIP)	On	This means zoom meetings where a participant is using a different room-based solution like WebEx or Lifesize would require an encrypted connection Set to "on" in case we ever have meetings with third party endpoints, but this will not impact anything with standard Zoom meetings using the Zoom client on desktops/laptops/mobile devices
Chat	On and check box to prevent participants from saving chat	Concern over who has access to Zoom data
Private chat	Off	Concern over who has access to Zoom data, <i>ex parte</i> communication with panel
Auto saving chats	Off	Concern over who has access to Zoom data
Play sound when participants join or leave	Off	Can be distracting; may be set to play only for the host
File Transfer	Off	Concern over who has access to Zoom data
Feedback to Zoom	Off	
Display end-of-meeting experience feedback survey	Off	
Co-host	On	
Polling	Off	
Allow host to put attendee on hold	On	Good for temporarily allowing the host to remove an attendee such as a witness

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Configuration Section	Default Setting	Comments
Always show meeting control toolbar	On	
Show Zoom windows during screen share	Off	Only need to share documents/presentation
Screen Sharing	On	
Who can share?	All Participants	
Who can start sharing when someone else is sharing?	Host Only	
Disable desktop/screen share for users	Off	Needed for presenting
Annotation	On	Allows participants to mark up a document
Whiteboard	On and Uncheck Auto save whiteboard content when sharing is stopped	Concern over who has access to Zoom data
Remote control	On	Allows others to control shared content
Nonverbal feedback – off	Off	
Allow removed participants to rejoin – off	Off	Keeps removed people from getting back in

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In Meeting (Advanced) Settings

Configuration Section	Default Setting	Comments
Breakout room	On and Check Allow host to assign participants to breakout rooms when scheduling	Only can pre-assign those with full license but n harm to allow this setting
Remote Support	Off	We do not want to get into others computers
Closed captioning	Off	
Save captions	Off	
Far end camera control	Off	
Group HD video	Off	To reduce bandwidth use
Virtual background	On	Use professional background image
Identify guest participants in the meeting/webinar	Off	Not needed as most are guests vs. someone on AAA corporate account
Auto-answer group in chat	Off	
Only show default email when sending email invites	Off	
Use HTML format email for Outlook plugin	On	
Allow users to select stereo audio in their client settings	Off	
Allow users to select original sound in their client settings	Off	

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Configuration Section	Default Setting	Comments
Attention tracking	Off	Feature disabled/removed by Zoom
Waiting room	On	Can be disabled if needed (Case by case basis)
Show a "Join from your browser" link	On	Do not want to force participants to download the app
Allow live streaming meetings	Off	

Email Notification Settings

Configuration Section	Default Setting	Comments
When a cloud recording is available	On	
When attendees join meeting before host	On	
When a meeting is cancelled	On	
When an alternative host is set or removed from a meeting	On	
When someone scheduled a meeting for a host	On	
When the cloud recording is going to be permanently deleted from trash	On	

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Other Settings

Configuration Section	Default Setting	Comments
Blur snapshot on iOS task switcher	Off	This setting can be used to hide potentially sensitive information on the Zoom iOS mobile app preview screen when multiple apps are open using the iOS tasks switcher Off as we don't see the need to enforce this
Direct call a room system	Off	This option enables a zoom client to directly call a room-based system instead of needing the room based system to be joined to a meeting first Off as it is not applicable to us
Invitation Email – Choose Language	English	
Schedule privilege – Assign scheduling privilege to	No one	May be used to assign privileges to other case staff

Recording Tab

Configuration Section	Default Setting	Comments
All settings	Off	See section on "Considerations for Recording a Zoom Meeting" if turning on

Telephone Tab

Configuration Section	Default Setting	Comments
All settings	On	

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Recommended Zoom Settings for Cloud Recordings

When setting up the meeting for recording, you will need to verify these configurations.

Configuration Section	Default Setting	Comments
Local Recording	Off	If changed to yes, do not select "Hosts can give participants the permission to record locally" You must document the file distribution/retention strategy
Cloud Recording	On	See detailed settings image below
Automatic Recording	Off	
IP Address Access Control	Off	
Only authenticated users can view cloud recordings	Off	
Require password to access shared cloud recordings	On	
Auto delete cloud recordings after days	21	Set to 21 as a precaution against inadvertently premature deletion; participants should be directed to download a local copy within 7 days
The host can delete cloud recordings	On	
Recording Disclaimer	On	Set to "Ask host to confirm before recording starts"
Multiple audio notifications of recorded meeting	Off	

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Detailed Cloud Recording Settings

These are the recommended settings when using cloud recording

Cloud recording

Allow hosts to record and save the meeting / webinar in the cloud

- Record active speaker with shared screen
- Record gallery view with shared screen ⓘ
- Record active speaker, gallery view and shared screen separately
- Record an audio only file
- Save chat messages from the meeting / webinar

Advanced cloud recording settings

- Add a timestamp to the recording ⓘ
- Display participants' names in the recording
- Record thumbnails when sharing ⓘ
- Optimize the recording for 3rd party video editor ⓘ
- Save panelist chat to the recording ⓘ

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RISKS OF VIDEO CONFERENCING*

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The advent of the COVID-19 outbreak has reinforced the demand for effective and seamless video conferencing capabilities to ensure that matters proceed to resolution through arbitration and mediation proceedings without prolonged disruptions. There are, however, potential issues with using video conferencing for such proceedings. Parties and their representatives need to be aware of these issues and take whatever steps they believe are necessary to mitigate risks the issues pose or, alternatively, forgo video conferencing in favor of in-person proceedings. The following three issues in particular are important to note.

Due Process – Fairness and Impartiality

Arbitrators and mediators must ensure that:

1. The video conferencing platform's technology provides for fair, equal and reasonable right of access to all involved.
2. The platform guarantees equal opportunity for parties to present evidence and testimony, including direct and cross-examination of witnesses.
3. The video conference will be terminated if proceeding will result in unfairness to a particular party.
4. The agreed-upon mutual technical requirements for video conferencing reduces the risk of unfairness against parties with witnesses who only have access to lesser technical capabilities and know-how.

5. All persons in each video conferencing location are relevant to the proceedings and identified before the proceedings begin so that no witnesses is being coached by off-screen individuals.
6. The proceedings are transparent by requiring that any relevant documents be clearly identified and disclosed.

Confidentiality & Security

Like most online services, video conferencing platforms may be breached and intruded upon in the absence of appropriate measures to ensure confidentiality and security. Cybersecurity breaches in the context of arbitration and mediation would be detrimental if non-participants gain access to confidential information. While no video conferencing service can guarantee 100% security, most have sophisticated platforms that provide significant security. Unfortunately, hackers are equally as sophisticated.

Arbitrators (and mediators as may be applicable), must strive to protect the confidentiality of the proceedings by

1. Ensuring that access to the video conference connection is adequately protected, e.g., by using the platform's security features and turning on its security settings.
2. Advising the parties that they and their representatives have a duty to use their best efforts to ensure the security of the video conference participants.
3. Requiring that only the witness and relevant individuals may participate in the video conference, and that these individuals must be identified.
4. Prohibiting recordings of the video conference made outside presence of the arbitrator(s), and limiting circulation of authorized recordings so that they are not accessed by non-parties.

Technology Challenges

There is always a risk to the smooth execution of a virtual arbitration or mediation proceeding when technology is involved. Chief among the disrupters are power outages and disconnections. Another significant challenge can be participants who aren't proficient, or at least minimally versed, in the applicable technology. Arbitrator, mediators, the parties and their representatives should (i) have contingencies in place they can easily turn to should the primary platform fail or otherwise become

impractical to use and, (ii) set up dry-runs or practice sessions to ensure all participants are comfortable with the technology.

* Adapted from “Safeguarding the Future of Arbitration: Seoul Protocol Tackles the Risks of Videoconferencing.”
<http://arbitrationblog.kluwerarbitration.com/2020/04/06/safeguarding-the-future-of-arbitration-seoul-protocol-tackles-the-risks-of-videoconferencing/>

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VIDEO CONFERENCING DISCLAIMER

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Upon request by an arbitrator or mediator, or upon the agreement of the parties, the AAA-ICDR will provide access to a third party platform to host an arbitration or mediation proceeding. Under those circumstances, the AAA-ICDR will utilize the Zoom platform. The AAA-ICDR has trained staff to utilize the Zoom video conferencing platform and has purchased Zoom Pro licenses. However, the use of video conferencing platforms for arbitration and mediation proceedings is subject to the platform's terms and policies, for example: <https://zoom.us/privacy-and-legal>. While the AAA-ICDR can provide access to Zoom, the parties and the arbitrator may utilize whichever third party platform they choose. The AAA-ICDR does not endorse any one platform over another nor does the AAA-ICDR guarantee the suitability or availability of any platform.



COMPARISONS OF VIDEO CONFERENCING PLATFORMS

[Main Menu](#)

The resources on this page are provided for informational purposes only. The AAA-ICDR does not endorse any one platform over another nor does the AAA-ICDR guarantee the suitability or availability of any platform.

The links below provide high-level reviews of popular business video conferencing platforms such as Zoom, GoToMeeting, Webex Meetings, Microsoft Teams, etc.

 ***Press and hold the CTRL key while clicking a logo to open the websites in a new browser window.***





ZOOM TUTORIALS

[Main Menu](#)

[Using AAA-Hosted Virtual Hearings](#)

[Using Personal Video Conference Accounts](#)

The links below navigate to YouTube video tutorials available on Zoom’s official website and are provided for your convenience. Zoom maintains the tutorials and is solely responsible for their content.

Ctrl

Press and hold the CTRL key while clicking a link to open the tutorial in a new browser window.

Account & Admin – User Management 0:45	Reporting & Dashboard 5:40
Assigning Scheduling Privileges in Outlook 5:02	Scheduling a Meeting 1:07
Audio & Video Controls 1:42	Scheduling a Meeting with Google Calendar 1:47
Breakout Rooms 3:18	Scheduling a Meeting with Outlook 0:52
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NON-TRADED REITS: KEY CHARACTERISTICS AND MARKET TRENDS

Brian Henderson PhD, CFA

1. Overview of Non-Traded REITs

Real Estate Investment Trusts (REITs) are companies that generate income through ownership and operation of real estate properties. REITs are tax advantaged compared to other companies, enhancing the profitability of real estate investment. To qualify as a REIT, a company must meet several requirements, including distributing to investors at least 90% of their taxable income, investing at least 75% of assets in real estate, deriving at least 75% of revenue from real estate activities, and several other requirements aimed at governance and breadth of ownership. Among publicly registered REITs, most are listed for trading on a stock exchange. Despite the availability of listed REITs, non-traded REITs have emerged as a major product sold to retail investors.

Non-traded REITs, unlike listed REITs, are direct participation programs (DPPs) marketed primarily to retail investors by broker-dealers. Traditionally, independent broker-dealers have been the primary distributors, but in recent years, wirehouses have also participated as the product space has continued to evolve. Although they share many characteristics with their listed counterparts, non-traded REITs have drawn considerable scrutiny from regulators due to their high fees, limited liquidity, and corporate structures laden with material conflicts of interest.

High fees

Non-traded REITs come with high fees. At the initial purchase, investors pay high fees including sales and distribution charges that can range from 5% to 20% of offering proceeds. The majority of those fees are sales charges to compensate brokers and advisors. Henderson Mallett and McCann (2016) analyzed a large sample of non-traded REITs and found that upfront fees averaged 13.2% and sales commissions average 6.7%. Other upfront fees include property acquisition fees, reserve fees, and “other” fees. These upfront fees reduce the amount of investor capital that goes toward the purchase and management of income producing assets and often compensates a network of entities affiliated with the sponsor.

In addition to the upfront fees, non-traded REITs pay fees to advisors and property managers on an ongoing basis. Although most listed REITs use internal advisors and managers, non-traded REITs tend to use external advisors and managers. Usually these external parties are affiliates of the sponsors, creating a conflict of interest.

Limited to no liquidity

Unlike their listed and traded counterparts, non-traded REITs offer investors almost no ability to redeem or sell their shares for years after their purchase. This lack of liquidity means that investors are usually unable to sell their investment if they need capital and are forced to continue paying the fees associated with the investment until a “liquidity event” takes place. Such events are usually mergers or listings that take place 5 or more years after purchase.

There is a dark side to non-traded REITs’ illiquidity that is often under-appreciated: the illiquidity obstructs shareholders’ ability to affect corporate governance. Liquidity is the key to affecting governance in two ways. First, when investors are pessimistic they “vote with their feet,” selling an underperforming investment and replacing it with another. Through secondary market liquidity,

market forces set prices, and declining prices put pressure on management to improve performance. The second avenue is through blockholders. Corporate governance is limited when there are many shareholders that each hold small proportional ownership. Most small investors do not vote and do not have an incentive to monitor management given the large costs of oversight. However, when an activist investor is able to amass a block of shares, then effective corporate governance becomes possible. The dearth of secondary market activity, and that the limited share redemptions take place through the sponsor, mean that investors are unable to vote with their feet and the formation of large control blocks is not feasible. Thus, the illiquidity works to shut down corporate governance.

Ongoing conflicts of interest

Non-traded REITs often conduct transactions and enter into business arrangements with parties affiliated with the sponsor, leading to significant conflicts of interest that can impact investment performance. An example of these conflicts of interest comes from non-traded REITs' use of advisors and portfolio managers owned by the same parties that own the REIT sponsor. Advisors and portfolio managers are critical to the performance of the REIT. Advisors' responsibilities include acquisition of investments while the property manager oversees the operation and maintenance of those portfolio properties. REITs compensate advisors and portfolio managers through fees assessed to shareholders. Not only should these parties be selected based on their expertise and performance, but their fee compensation arrangement should be determined at arms' length. Sponsors selection of their affiliates for these roles and determining the compensation is a clear conflict of interest.

2. Non-traded REITs underperform listed REITs

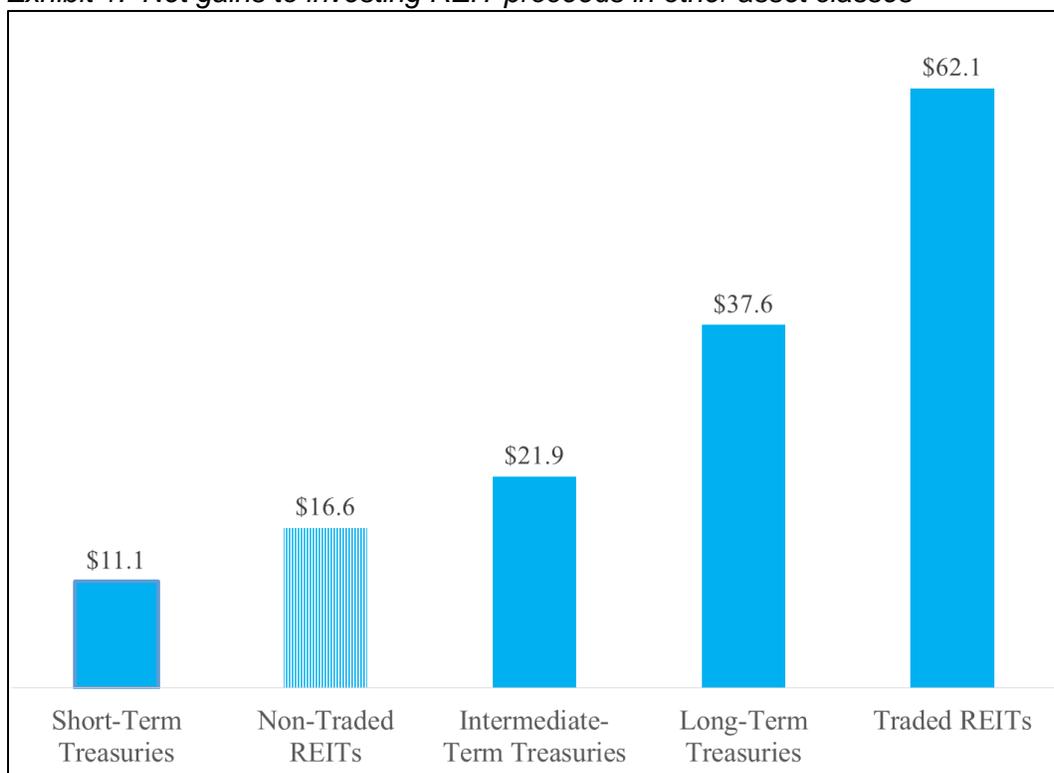
If non-traded REITs suffer from high fees and conflicts of interest, investors' returns should be inferior to those of otherwise identical investments. Investors have other choices for diversified income-producing real estate investments. Publicly-registered, exchange-traded REITs are an alternative to non-traded REITs. Investors can purchase these REITs directly or through mutual funds or ETFs focusing on REITs.

Henderson, Mallett, and McCann (2016) conducted a large-scale analysis of 89 non-traded REITs. Using SEC filings, they tracked the total amounts raised by those 89 companies, all their distributions, and the value when they listed, merged, or otherwise provided investors with a final amount. Using the Vanguard REIT Index fund as the alternative, they found that, overwhelmingly, investors would have been better off investing in listed REITs. Non-traded REIT investors lost \$44 billion of wealth compared to the wealth they would have had if they had instead invested in listed REITs through the REIT index fund. The results are robust to the choice of REIT index fund.

Of the estimated \$44 billion wealth loss that non-traded REITs experienced by not investing their capital in publicly traded REITs, approximately \$26 billion (60%) of that shortfall is attributed to the upfront fees and expenses. This staggering amount illustrates that when publicly traded REITs are available in low-fee, diversified mutual funds, investors suffer large losses from non-traded REITs' large upfront expenses. The remaining 40% of the wealth shortfall is attributable to the ongoing conflicts of interest in the non-traded REIT structure.

A basic principle of financial economics is that over reasonably long horizons, investment returns are proportional to investment risk. However, if there is a flaw in the design of an investment product, it consistently will provide returns that are less than those of other investments having similar risks. To investigate where non-traded REIT returns fall in the risk spectrum, we consider the net gains (net out of pocket amount) of investing in all non-traded REITs compared to those amounts had the same capital amounts been invested in other assets. The other assets we consider are short-term US Treasury bonds, intermediate-term US Treasury bonds, long-term US Treasury bonds, and publicly listed and traded REITs. Despite having nearly identical economic risk as the traded REITs, non-traded REITs' investment performance rank between short- and intermediate-term US Treasuries. Despite having much more risk than those US Treasuries, non-traded REIT investment performance resembles low-risk US Treasury bonds. Non-traded REIT investors would have been better off (lower risk and greater return) with well managed investment solutions.

Exhibit 1: Net gains to investing REIT proceeds in other asset classes



The pandemic of 2020 has been a challenging time for the real estate industry. During the first quarter of 2020, listed REITs' valuations plummeted along with almost every other publicly traded company. Since non-traded REITs do not trade on exchanges, their valuations are more difficult to observe. To gauge their performance over the past year requires relying on reported NAVs or on the very few available secondary market transactions.

Sponsors and advocates of non-traded REITs have promoted the fallacy that the absence of trading (secondary market liquidity) reduces the volatility of the investment. This is a complete fallacy because the risk and volatility of a company come from the company's assets as well as its financing structure. The REIT assets are the portfolio of real estate properties and related assets such as mortgage-backed securities. Those assets are not more or less risky, nor are their values more or less volatile, whether they are held by a listed or non-traded REIT. Next, the financing structure can add risk depending on the degree to which leverage is used. It is typical

for both listed and non-traded REITs to utilize leverage to finance their real estate portfolio. By suppressing secondary market activity, there is no reduction in the risk or volatility of an investment. Instead, the illiquidity masks the true risk and performance of the non-traded REIT. Ironically, every financial economist knows that illiquid investments are *riskier* than otherwise identical liquid investments. This means that the illiquidity imposed on non-traded REITs makes them riskier than their listed counterparts.

That non-traded REITs are still risky and subject to the same risks as listed REITs is evident in their performance during the pandemic of 2020. From November 2019 to November 2020, Exhibit 2 presents the price changes of the most traded non-traded REITs. The median price change was -32%. Most of these programs suspended dividends and buybacks during this time-period. By comparison, the return to the Vanguard REIT Index fund during this same period was -9.8%.

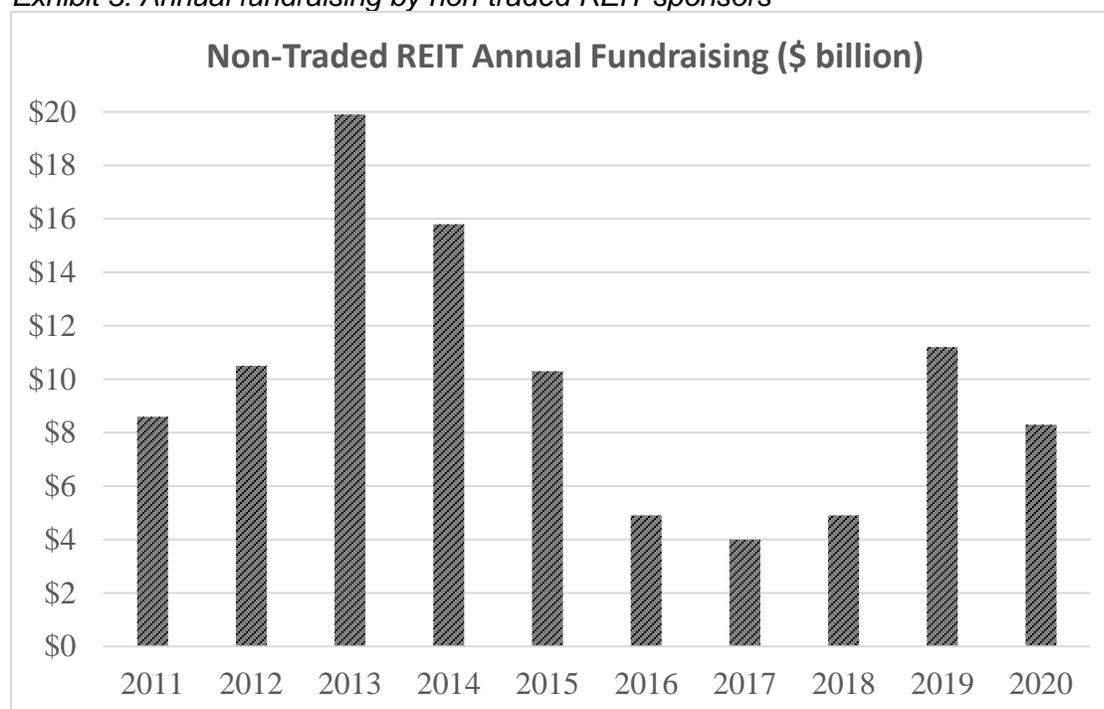
Exhibit 2: One-year change, non-traded REIT secondary market prices

Non-traded REIT	Secondary Market Price Change Nov 2019 to Nov 2020
Benefit Street Partners Realty Trust	-32%
CIM Real Estate Finance	-31%
CNL Healthcare Properties	-18%
Griffin Capital Essential Asset REIT	-16%
Healthcare Trust Inc	-50%
Highlands REIT	-13%
Hospitality Investors Trust	-84%
Inland Real Estate Income	-44%
InvenTrust Properties	-9%
KBS REIT III	-7%
Lightstone Value Plus II	-63%
Lightstone Value Plus III	-48%
New York City REIT	-37%
NorthStar Healthcare Income	-43%
Phillips Edison & Co	-30%
Sila Realty Trust	-9%
SmartStop Self Storage REIT	-7%
Steadfast Apartment REIT	-14%
Summit Healthcare REIT	-30%
Watermark Lodging Trust	-70%
Maximum	-7%
Minimum	-84%
Median	-31%

3. Recent trends and innovations

Across all sponsors, non-traded REIT fundraising has recovered from recent lows in the 2016 to 2018 time period during which annual amounts fell to \$4 to \$5 billion. During 2019, non-traded REITs raised more than \$11 billion. Despite steep declines early in 2020, fundraising rallied back during the second half of 2020 to bring the total amount raised to over \$8 billion for the year. Although fundraising has been on the up-swing, it has not returned to the levels seen in 2013 and 2014 (\$20 and \$16 billion, respectively). Exhibit 3 presents the annual non-traded REIT fundraising totals by all sponsors over the last decade.

Exhibit 3: Annual fundraising by non-traded REIT sponsors



Who are the sponsors raising money in the current environment? Exhibit 4 presents the sponsors that have raised at least \$75 during the challenging environment of 2020. Blackstone group accounted for the vast majority of proceeds with more than \$5 billion. Denver-based Black Creek Group was the only other sponsor to raise more than \$1 billion during 2020. Black Creek Group's capital raise was elevated as investors in Industrial Property Trust reinvesting their liquidating distributions in Black Creek Industrial REIT IV. Although other sponsors that have been prolific fundraisers in the past remain in the marketplace, such as Inland, Griffin Capital, and Philips Edison, they raised very small amounts during 2020.

Exhibit 4: 2020 Fundraising by Top Sponsors

Sponsor	2020 Fundraising (\$ billion)
Blackstone Group	5,071
Black Creek Group	1,103

Starwood Capital Group	975
Jones Lang LaSalle	332
Hines Interests	259
FS Investments	192
Nuveen LLC	87
Oaktree Capital Management	76

The non-traded REIT product space has seen a trend toward fewer offerings and fewer sponsors. The top 6 sponsors raised approximately 95% of funds in this space during 2020. There are 13 other active sponsors, totaling 19 sponsors. This is down from 24 sponsors as recently as 2018. Over the coming years, look for the number of sponsors to decline to roughly ten.

Around 2016, fundraising by non-traded REITs came under pressure due to regulatory pressures (Department of Labor Fiduciary Rule and FINRA 15-02) as well as high profile losses including United Development Funding and Nicholas Schorcsh's American Realty Capital offerings. To that point, the non-traded REIT market was dominated by high upfront fee products sold through independent broker-dealers. Many sponsors disclosed they have no track record for managing real estate and engaged with advisors and property managers also lacking relevant experience.

As fundraising has increased during the last two years, the product space has evolved in light of the regulatory pressures and high profile investor losses. Referring to Exhibit 3 reveals the market has seen the entrance of higher profile sponsors: Blackstone Group, Starwood Capital, and Oaktree Capital Management. Blackstone is a high-profile private equity firm specializing in alternative asset classes. So what is Blackstone doing in the non-traded REIT space?

An important innovation in the current product offerings is the introduction of new share classes that take smaller upfront fees. As an example, the Blackstone Real Estate Income Trust Inc offers T-shares that have a 3% upfront selling commission which is far less than those charged by the more traditional offerings. In addition to the 3% selling commission, the T-shares charge a 0.5% dealer manager fee and annual 0.85% servicing fee for up to seven years. Another class of shares, S-shares, have greater upfront fees and lower annual fees.

A recent trend is that major wirehouses, instead of the independent broker-dealers are distributing non-traded REITs. This has coincided with the entrance of higher profile sponsors and share classes having lower upfront commissions. Although distribution fees have come down, they are still motivational for selling brokers as 3% commission is much greater than commissions on other products such as mutual funds and publicly traded REITs. Brokerage commissions have been under pressure in recent years due to pressure from discount brokers and online platforms.

Do the new trends make non-traded REITs an appropriate product for investor portfolios? Not so fast. First, the structures still contain ongoing conflicts of interest. Despite having lower commissions and being distributed by wirehouses, the new products still have conflicts of interest that can impact returns. They come with hedge-fund like performance incentives for the managers that could encourage risk-taking. Blackstone's BREIT charges an annual incentive fee of 12.5% of the total returns subject to a 5% minimum returns and high water mark. Commercial real estate markets are very competitive – in fact that is a boilerplate disclosure in REIT prospectuses. The fee structure alone (upfront fees and annual incentive fees) make it very unlikely that Blackstone's REIT consistently outperforms a well-managed REIT Index Fund due to its higher cost structure.

The trend of the non-traded REIT product space toward institutional quality management teams, distribution through wirehouses, and lowering of upfront fees are certainly positive. But are they enough to make this an attractive asset class. For the same reason that hedge funds are challenged to produce returns that justify their fees, non-traded REITs that charge hedge-fund like incentive fees will face similar challenges. Time will bear out the evidence, but look for even exemplary management teams to struggle to consistently produce superior returns to well-managed publicly traded REITs that operate in the same commercial property markets.



> FOR INVESTORS > INVESTOR ALERTS

Investor Alert

Public Non-Traded REITs—Perform a Careful Review Before Investing

During extended period of low interest rates, investors often seek products offering more attractive yields. One such product is the publicly registered non-exchange traded real estate investment trust (REIT) or "non-traded REIT" for short. While non-traded REITs and exchange-traded REITs share many features in common, they differ in several key respects. Most significantly, as the name implies, shares of non-traded REITs do not trade on a national securities exchange. For this reason, non-traded REITs are generally illiquid, often for periods of eight years or more. Early redemption of shares is often very limited, and fees associated with the sale of these products can be high and erode total return. Furthermore, the periodic distributions that help make these products so appealing can, in some cases, be heavily subsidized by borrowed funds and include a return of investor principal. This is in contrast to the dividends investors receive from large corporations that trade on national exchanges, which are typically derived solely from earnings.

FINRA is issuing this alert to inform investors of the features and risks of publicly registered non-exchange traded REITs and the [attached tip sheet](#) to help you avoid pitfalls and misconceptions these investments. If you are considering a publicly registered non-exchange traded REIT, be prepared to ask questions about the benefits, risks, features and fees.

What Is a REIT?

A real estate investment trust, or REIT, is a corporation, trust or association that owns (and might also manage) income-producing real estate. REITs pool the capital of numerous investors to purchase a portfolio of properties—from office buildings and shopping centers to hotels and apartments, even timber-producing land—which the typical investor might not otherwise be able to purchase individually.

REITs can offer tax advantages. For instance, qualified REITs that meet [Internal Revenue Service requirements](#) can deduct distributions paid to shareholders from corporate taxable income, avoiding double taxation. The REIT must also distribute at least 90 percent of its taxable income to shareholders annually. These distributions are taxable to the extent of any ordinary income and capital gains included in the distribution.

There are two types of public REITs: those that trade on a national securities exchange and those that do not. REITs in this latter category are generally referred to as publicly registered non-exchange traded, or simply non-traded REITs, which are the focus of this alert.

Features of Non-Traded REITs

Like exchange-traded REITs, non-traded REITs invest in real estate. They are also subject to the same IRS requirements that an exchange-traded REIT must meet, including distributing at least 90 percent of taxable income to shareholders. Like exchange-traded REITs, non-traded REITs are registered with the Securities and Exchange Commission and are required to make regular SEC disclosures, including filing a prospectus and quarterly (10-Q) and annual reports (10-K), all of which are publicly available through the SEC's EDGAR database. While these two types of REITs share these similarities, there are also numerous differences between them, as illustrated in the chart below.

	Non-Traded REITs	Exchange-Traded REITs
Listing Status	Shares do not list on a national securities exchange.	Shares trade on a national securities exchange.
Secondary Market	Very limited. While a portion of total shares outstanding may be redeemable each year, subject to limitations, redemption offers may be priced below the purchase price or current price.	Exchange traded. Generally easy for investors to buy and sell.
Front-End Fees	Front-end fees that can be as much as 15% of the per share price. Those fees include selling compensation and expenses, which cannot exceed 10%, and additional offering and organizational costs.	Front-end underwriting fees in the form of a discount may be 7% or more of the offering proceeds. Investors who buy shares in the open market pay a brokerage commission.
Anticipated Source of Return	Investors typically seek income from distributions over a period of years. Upon liquidation, return of capital may be more or less than the original investment depending on the value of assets.	Investors typically seek capital appreciation based on prices at which REITs' shares trade on an exchange. REITs also may pay distributions to shareholders.

Valuation Methods and Disclosures

Broker-dealers involved in the sale of non-traded REITs are required to provide investors with a per share estimated value for the REIT using one of two methodologies described in [FINRA Notice 15-02](#):

- **Net Investment Methodology.** When this method is used, the firm must disclose to you whether part of your distribution from the REIT includes a return of capital, which reduces the estimated per share value shown on your account statement. The net investment methodology can be used until 150 days following the second anniversary of breaking escrow in the public offering, at which time a firm must use the appraised value methodology.
- **Appraised Value Methodology.** The valuation method can be used at any time and consists of the appraised valuation disclosed in the issuer's most recent periodic or current report filed with the SEC. FINRA's rule requires that the per share estimated value disclosed in the REIT's most recent periodic or current report be based on a valuation of the assets and liabilities of the REIT, and that the valuation be: performed at least annually; conducted by, or with the material assistance or confirmation of, a third-party valuation expert or service; and derived from a methodology that conforms to standard industry practice.

Firms that sell non-traded REITs are required to disclose some key aspects of the investment, including: that the securities are not listed on a securities exchange; that the securities are generally illiquid; and that, even if a customer is able to sell the securities, the price received may be less than the per share estimated value provided in the account statement.

Private REITs

There is another type of REIT—a **private** REIT, or **private-placement** REIT—that also does not trade on an exchange. Private REITs carry significant risk to investors. Not only are they unlisted, making them hard to value and trade, but they also generally are **exempt** from Securities Act registration. As such, private REITs are not subject to the same disclosure requirements as public non-traded REITs. The lack of disclosure documents makes it extremely difficult for investors to make an informed decision about the investment. Private REITs generally can be sold only to **accredited investors**, for instance those with a net worth in excess of \$1 million. As with any private investment, it is a good idea to have the investment reviewed by an investment professional who understands the product and can offer impartial advice.

Complexities and Risks

When it comes to investing in non-traded REITs, selling points such as the opportunity for capital appreciation, diversification and the allure of a robust distribution can be enticing. But investors should balance these selling points against the numerous complexities and risks these investments carry.

- **Distributions are not guaranteed and may exceed operating cash flow. Deciding whether to pay distributions and the amount of any distribution is within discretion of a REIT's Board of Directors in the exercise of its fiduciary duties.** Distributions can be suspended for a period of time or halted altogether. Many factors may influence the composition of these payments. For example, in newer programs, distributions may be funded in part or entirely by cash from investor capital or borrowings—leveraged money that does not come from income generated by the real estate itself, such as rents or hotel occupancy fees. The REIT's articles of incorporation often allow it to increase debt, dip into cash reserves and apply proceeds of the sale of new shares to sustain or even increase distributions. Some REITs even allow borrowing in excess of 100 percent of net assets. Leveraging, including the use of borrowed funds to pay distributions, can place the REIT at greater risk of default and devaluation, which can result in investment losses when it comes time to redeem or liquidate shares, as well as a reduction in, or suspension of, distributions.
 - **Tip:** Understand the REIT's borrowing policies, outlined in the prospectus, and use the SEC's [EDGAR database](#) of company filings to research how heavily leveraged the REIT may be, as well as how it is financing distributions. If *Net Cash from Operations* (what the company earns through its real estate alone) is less than the distribution (usually found in the *Financing Activities* section), then other sources, including borrowed funds, may be supporting the distribution. Before investing, be sure to ask the person offering the investment how much the REIT may have borrowed and whether the distributions include, or are likely to include, a return of principal. Ask how these factors might impact your investment. Keep these same factors in mind when deciding whether or not to reinvest distributions. **Caution: If a REIT issuer is behind or incomplete in its SEC filings this can be a red flag.**
- **Distributions and REIT status carry tax consequences.** Distributions for all REITs that are from current or accumulated earnings and profits are taxed as ordinary income, as opposed to the tax rate on qualified dividends, which generally carries a tax rate of 15 percent. But that rate can be 20 percent for people in the highest tax bracket or 0 percent for those in the lowest two tax brackets. If a portion of your distribution constitutes a return of capital, that portion is not taxed until your investment is sold or liquidated, at which time you will be taxed at capital gains rates.
 - **Tip:** Take steps to obtain an understanding of the tax consequences associated with this investment. Consider speaking with a tax advisor prior to investing and on an ongoing basis.
- **Lack of a public trading market creates illiquidity and valuation complexities.** As their name implies, non-traded REITs have no public trading market. However, most non-traded REITs are structured as a "finite life investment," meaning that at the end of a given timeframe, the REIT is required either to list on a national securities exchange or liquidate. Even if a liquidity event takes place, there is no

guarantee that the value of your investment will have gone up—and it may go down or lose all its value. Indeed, valuation of non-traded REITs is complex. Many factors affect the pricing, including the portfolio of real estate assets owned, strength of the trust's balance sheet (assets versus liabilities), overhead expenses, cost of capital and more. The boards and managers of non-traded REITs might even rely on third-party sources to estimate a per-share value.

- **Tip:** Ask your financial professional to explain the risk of illiquidity. Review the *Risks* section of the prospectus to find out more about the investment's expected holding period and potential liquidity events. Also ask if the offering has concluded—and, if not, when it is expected to conclude. Check your brokerage statements or with your financial professional to see if there has been a fluctuation in the per-share price. Whether the value fluctuated or not, ask the brokerage firm how—and how recently—the share price was valued.
 - **Advisory:** If the value of the REIT's portfolio has changed materially during the offering period, then new investors may be paying a per-share price above or below the per-share net value of the underlying real estate.
- **Early redemption is often restrictive and may be expensive.** Most public non-traded REIT offerings place limits on the amount of shares that can be redeemed prior to liquidation. Redemption provisions can be as restrictive as 5—or even 3—percent of the weighted average number of shares outstanding during the previous year. In addition, shares may have to be held for some period, typically one year, before they can be redeemed. Redemption programs may be terminated or adjusted, so investors should not count on them, even as an emergency exit strategy. While a redemption program may allow you to sell your shares prior to a liquidity event, the redemption price is generally lower than the purchase price, sometimes by as much as 10 percent.
 - **Tip:** When investing in non-traded REITs investors must consider their short-term needs for capital before investing in a long-term, illiquid security and should carefully review the section explaining the terms and limitations of the REIT's share redemption plan.
 - **Advisory:** Investors may be solicited to sell a stake in their non-traded REIT investment outside of the sponsor's redemption program through a process known as a “mini-tender offer.” Mini-tender offers are offers for less than 5 percent of a company's stock, and they typically carry far fewer protections to investors than traditional tender offers. For instance, there is no requirement to identify who the buyer is, provide disclosures to the SEC or provide competing bids. Investors can wind up receiving a price well below the sponsor's estimated per-share value or, if available, the early-redemption program price. For more information, see the SEC's information on [Mini-Tender Offers](#).
 - **Fees can add up.** Non-traded REITs can be expensive. Front-end fees generally come in two parts:
 1. Selling compensation and expenses, which cannot exceed 10 percent of the investment amount; and
 2. Additional offering and organizational costs, sometimes referred to as “issuer costs,” which are also paid from the offering proceeds. According to state regulatory guidelines, the total for both types of fees cannot exceed 15 percent. FINRA guidelines also limit the total for both types of fees to 15 percent in offerings that are sold by an affiliated broker-dealer. All investments carry fees, and they add up, reducing the amount of capital available for investment. For example, a 15 percent front-end fee on a \$10,000 investment means that \$8,500 is going to work for you at the time of investment. By comparison, the underwriting compensation associated with exchange-traded REITs is normally seven percent of the offering proceeds.
 - **Tip:** Non-traded REITs are rarely, if ever, suitable for short-term investors and even long-term investors must be willing to bear the risks of illiquidity. You should consider the front-end cost relative to the sales costs you would incur to buy and sell other securities during the same holding period as the life of the REIT. You may also want to consider how much share price appreciation and distributions you will need to receive to overcome these front-end charges.
 - **Properties may not be specified.** Most non-traded REITs start out as blind pools, which have not yet specified the properties to be purchased. Others may specify a portion of the properties the REIT plans to acquire, or they may be in various stages of acquisition. In general, the more properties that have been specified for purchase or that have actually been acquired the less risk an investor incurs because the investor has the opportunity to assess the nature and quality of the assets of the REIT before investing.
 - **Tip:** Ask what percentage of a non-traded REIT's properties have been specified for acquisition or actually acquired.
 - **Diversification can be limited.** While REITs as an investment class may help diversify your portfolio, putting all of your intended real estate investment in one REIT—including investments in different issuances or phases of the same REIT—can expose you to the risk of underdiversification.
 - **Tip: Review the offering document** relating to the REIT's investment policies to evaluate the intended diversification of the REIT's portfolio. Read ongoing disclosure documents to track how well the REIT is executing its business plan. As with any investment, avoid putting all your eggs in one basket.
 - **Remember Real Estate Risk.** There are risks associated with both the real estate market as a whole and any specific subset of the real estate market on which a particular REIT concentrates.
 - **Tip:** Understand risks associated with the types of properties the REIT holds (for instance, hotels have a different set of risks than shopping malls), the geographical area it concentrates in and the strategies the REIT uses, including leveraging to acquire assets. Have an in-depth discussion with your financial professional about risks and carefully read the prospectus.

Before You Invest

Be wary of pitches or sales literature offering simplistic reasons to buy a REIT investment. Sales pitches might play up high yields and stability while glossing over the product's lack of liquidity, fees and other risks. Ask whoever is recommending that you purchase a REIT how much they (and their company) are receiving in selling commissions or other fees. Also ask them to explain why they think the REIT is the right investment for you and how will it help you achieve your specific investment objectives and goals¹.

Always ask to review the initial prospectus and any prospectus supplements, as these documents will contain a more extensive and balanced discussion of the risks involved than any sales material you receive or pitches you hear. You can obtain a prospectus by going to the SEC's EDGAR database of company filings and typing in the name of the REIT, then search for entries titled "*Prospectus*." Remember that the fact that a company has registered its securities or has filed reports with the SEC does not mean that it will be a good investment—or that it will be right for you.

Ask about fees associated with the product. Also ask how the distribution is being funded and whether a portion of that distribution is comprised of a return of investor capital. Make sure you understand that you will be locking up your investment, with only limited avenues for redemption. If the REIT offers a share redemption program, make sure you understand how the repurchase price for your shares will be determined and, most importantly, the limitations of the plan. Review with your financial professional the risks associated with real estate investment and evaluate other products that could meet your investment objectives (investment income, for instance). Understand the various liquidity events specific to the REIT you are considering.

Remember to only invest if you are confident the product can help you meet your investment objectives and you are comfortable with the associated risks.

If you are suspicious about an investment or investment offer, or if you think the claims might be exaggerated or misleading, please [contact us](#).

Additional Resources

- [SEC Investor Bulletin: Publically Traded REITs](#)
- FINRA [Rule 2340](#)
- FINRA [Rule 2310](#)
- FINRA Regulatory Notice 09-09, [Unlisted REITs and DPPs](#)
- FINRA Investor Alert, ["Free Lunch" Investment Seminars—Avoiding the Heartburn of a Hard Sell](#)
- SEC [EDGAR database](#)
- SEC [Mini-Tender Offers](#)

To receive the latest Investor Alerts and other important investor information sign up for [Investor News](#).

1 FINRA initiated a [disciplinary complaint](#) against a brokerage firm, charging that the firm solicited investors to purchase shares in a non-traded REIT without conducting a reasonable investigation to determine whether it was suitable for investors. The complaint also alleged that the firm provided misleading information on its website regarding the REIT's distributions. The case was settled, and the firm agreed to pay a fine and restitution to investors.

Last Updated: November 30, 2016

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Communications With the Public

FINRA Provides Guidance on Communications With the Public Concerning Unlisted Real Estate Investment Programs

Executive Summary

FINRA is issuing this *Notice* to provide guidance to firms on communications with the public concerning unlisted real estate investment programs, including unlisted real estate investment trusts (REITs) and unlisted direct participation programs (DPPs) that invest in real estate.

Questions concerning this *Notice* should be directed to:

- ▶ Thomas A. Pappas, Vice President & Director, Advertising Regulation, at (240) 386-4553; or
- ▶ Amy C. Sochard, Director, Advertising Regulation, at (240) 386-4508.

Background and Discussion

Many firms are currently offering customers real estate investment programs in the form of either unlisted REITs or unlisted DPPs. REITs are pass-through entities that offer investors an equity interest in a pool of real estate assets, including land, buildings, shopping centers, hotels and office properties, and, in some cases, mortgages secured by real estate. As defined in FINRA Rule 2310, DPPs are investment programs that provide for flow-through tax consequences regardless of the structure of the legal entity or vehicle for distribution. DPPs include, among other investment vehicles, real estate programs that are not structured as REITs.¹ For purposes of this *Notice*, unlisted real estate investment programs (real estate programs) means REITs or DPPs that invest in real estate assets or mortgages and that are not listed on a national securities exchange.²

May 2013

Notice Type

- ▶ Consolidated Rulebook
- ▶ Guidance

Suggested Routing

- ▶ Advertising
- ▶ Compliance
- ▶ Legal
- ▶ Registered Representatives
- ▶ Senior Management

Key Topics

- ▶ Communications With the Public
- ▶ Direct Participation Programs
- ▶ Real Estate Investment Trusts

Referenced Rules & Notices

- ▶ FINRA Rule 2210
- ▶ FINRA Rule 2310

FINRA Rule 2210 requires that a broker-dealer's communications be fair, balanced and not misleading. Recent reviews by FINRA of communications with the public regarding real estate programs have revealed deficiencies. For example, some communications have contained inaccurate or misleading statements regarding the potential benefits of investing in real estate programs. Other communications have emphasized the distributions paid by a real estate program and failed to adequately explain that some of the distribution constitutes return of principal. In addition, some communications have not provided sufficient discussions of the risks associated with investing in the products in order to balance the presentation of benefits.

This *Notice* provides guidance to firms on communications with the public concerning real estate programs.³

Disclosure

In describing real estate programs, firms must ensure that their communications accurately and fairly explain how the products operate. Descriptions of real estate programs in communications need to be consistent with the representations in the program's current prospectus. For example, communications that include discussion of a program's objectives that are inconsistent with the objectives included in the program's prospectus or that do not explain that there is no assurance that the objectives will be met would not meet Rule 2210's requirements.

Since an investor's participation in a real estate program is an investment in the program and not a direct investment in real estate or any other assets owned by the program, communications that imply that they are direct investments also would be inconsistent with Rule 2210's requirements. Similarly, if a real estate program has not yet qualified under the U.S. tax code as a REIT, but is being marketed as a REIT, firms should ensure that the marketing communication discloses this fact and the possibility that the real estate program may not qualify as a REIT in the future.

In applying Rule 2210's standards, FINRA requires firm communications that discuss the benefits of an investment also to include a discussion of its risks.⁴ Accordingly, firm communications concerning real estate programs must balance any presentation of the potential benefits of such investments with disclosure concerning potential risks. This balance will be achieved if risk disclosure is presented in a clear and prominent manner, commensurate with the discussion of benefits, and is not relegated to a footnote.⁵ Providing risk disclosure in a separate document, such as the prospectus, does not substitute for the required disclosure, even if a communication is accompanied or preceded by a prospectus.

Distribution Rates

Firm communications concerning real estate programs often include distribution rates. Some real estate programs fund a portion of their distributions through return of principal or loan proceeds. For example, a portion of a newer program's distributions might include a return of principal until its real estate assets are generating significant cash flows from operations.

Rule 2210(d)(1)(B) prohibits firm communications from making any false, exaggerated, unwarranted, promissory or misleading claim. Accordingly, the rule prohibits firms from misrepresenting the amount or composition of a real estate program's distributions. Nor may firms state or imply that a distribution rate is a "yield" or "current yield" or that investment in the program is comparable to a fixed income investment such as a bond or note.

Presentations of distribution rates will be deemed to comply with Rule 2210's requirements that communications be fair and balanced, provided that the presentations clearly and prominently disclose:

- ▶ that distribution payments are not guaranteed and may be modified at the program's discretion;
- ▶ if the distribution rate consists of return of principal (including offering proceeds) or borrowings, a breakdown of the components of the distribution rate showing what portion of the quoted percentage represents cash flows from the program's investments or operations, what portion represents return of principal and what portion represents borrowings;
- ▶ the time period during which the distributions have been funded from return of principal (including offering proceeds), borrowings or any sources other than cash flows from investment or operations;
- ▶ if the distributions include a return of principal, that by returning principal to investors, the program will have less money to invest, which may lower its overall return; and
- ▶ if the distributions include borrowed funds, that because borrowed funds were used to pay distributions, the distribution rate may not be sustainable.

In order to be fair and balanced, firm communications concerning a real estate program may not include an annualized distribution rate until the program has paid distributions that are, on an annualized basis, at a minimum equal to that rate for at least two consecutive full quarterly periods.

Stability/Volatility Claims

Rule 2210(d)(1)(A) requires firm communications to provide a sound basis for evaluating the facts in regard to any particular security or type of security, industry or service. In addition, Rule 2210(d)(1)(D) requires communications to be consistent with the risks of fluctuating prices and the uncertainty of dividends, rates of return and yield inherent to investments.

Accordingly, a firm may not assert or imply in communications that the value of a real estate program is stable or that its volatility is limited without providing a sound basis to evaluate this claim. The fact that a program offers its securities at par value, or at another relatively stable price, does not evidence stability in the value of the underlying assets. A communication also may not state that the price at which the program is offered is stable or that its volatility is limited without disclosing that price stability does not indicate stability in the value of the underlying assets, which will fluctuate and may be worth less than the real estate program initially paid, and that the investor may not be able to sell the investment.

Redemption Features and Liquidity Events

Rule 2210(d)(1)(A) prohibits firms from omitting any material fact or qualification if the omission, in light of the context of the material presented, would cause the communications to be misleading. A communication could be misleading under this provision if it discusses a redemption feature without clearly and prominently explaining the restrictions and limitations of this feature, such as the fact that the real estate program's management may terminate or modify the ability to redeem. The fact that the real estate program has not satisfied all investor redemption requests in the past could be considered a fact that should be disclosed under this provision.

Any discussion about potential liquidity events or the timing of such events must be factual and balanced. A communication may not be balanced if it fails to disclose that the date of any liquidity event is not guaranteed or, if applicable, that it may be changed at the program management's discretion.⁶

Performance of Prior Related Real Estate Programs

If a communication includes prior performance or other historical information about related or affiliated entities, this information may not be "cherry-picked" from other programs; information about all related or affiliated programs should be included with equal prominence. Moreover, firms should ensure that this information is presented to easily differentiate it from information about the current program. Of course, the information must be consistent with information in the program's prospectus.

Use of Indices and Comparisons

Communications concerning real estate programs often use a real estate index's performance to demonstrate the sector's risk or return characteristics. As discussed above, Rule 2210(d)(1)(B) prohibits firms from making false or misleading statements or claims. In addition, Rule 2210(d)(2) requires that any comparison in retail communications between investments or services disclose all material differences between them, including (as applicable), investment objectives, costs and expenses, liquidity, safety, guarantees or insurance, fluctuation of principal or return, and tax features.

The use of any given index performance may be misleading if its underlying components do not correspond with those of the program's portfolio. For example, it would be misleading to cite the performance of an index of traded REITs to indicate how an unlisted REIT may perform.

In order to make a fair comparison if a communication includes an appropriate index, the communication must indicate the performance is not that of a particular real estate program, and describe the index's components and any relevant differences with the program's portfolio investments.

Pictures of Specific Properties

Communications for a new program often include photographs or other images of properties owned by investments managed by the program's sponsor that are similar to properties the program expects to purchase. In order to be clear that investors will not acquire an interest in the pictured property, prominent text must accompany each depiction explaining that the property is owned by an investment managed by the sponsor and not the program. Once the real estate program has acquired a portfolio, the communication may include depictions of properties that are limited to investments owned by the program.

A communication concerning a real estate program that holds real estate mortgages may include photographs or other images of properties in which the program has a security interest as long as the communication discloses that the program does not own the property and that the property is collateral for a loan owned by the program.

Capitalization Rates

A communication may include a capitalization rate for an individual property within a real estate program if the rate is based on current information contained in the prospectus, and the communication explains how the rate was calculated, that the rate applies to the individual property, and that it does not reflect a return or distribution from the REIT or DPP itself. As a general matter, however, it is misleading for a communication to include a rate that reflects a blending of multiple individual properties' capitalization rates. Individual properties within a program's portfolio typically will have different acquisition dates and their respective capitalization rates, which are generally based on the acquisition price of the property, may not reflect their current values. In addition, the individual properties' capitalization rates may reflect different calculation methodologies.

Endnotes

1. See FINRA Rule 2310(a)(4) for a complete definition of "direct participation program."
2. Real estate programs may be registered under the Securities Act of 1933 or may be offered pursuant to an exemption from such registration. The guidance in this *Notice* applies to communications regarding registered and non-registered real estate programs.
3. On December 19, 2011, the SEC's Division of Corporation Finance issued *CF Disclosure Guidance: Topic No. 3*, which discusses the SEC staff's views on a number of issues regarding materials submitted to the SEC staff pursuant to *Securities Act Industry Guide 5* (SEC Guidance). Guide 5 applies to real estate limited partnerships and unlisted REITs. The guidance in this *Notice* is intended to be consistent with the SEC Guidance.
4. See FINRA Rule 2210(d)(1)(D).
5. Information may be placed in a legend or footnote only in the event that such placement would not inhibit an investor's understanding of the communication. FINRA Rule 2210(d)(1)(C).
6. Under FINRA Rule 2310(b)(3)(D), before executing a purchase transaction in a public offering of DPP or unlisted REIT securities, a firm or associated person must inform the prospective participant of all pertinent facts relating to the liquidity and marketability of the DPP or REIT securities during the term of the investment. Included in the pertinent facts must be information regarding whether the sponsor has offered prior DPPs or unlisted REITs for which offering materials disclosed a date or time period at which the DPP or REIT might be liquidated, and whether liquidation occurred around that date or during the time period. This requirement does not apply to securities offerings of certain DPPs that are either listed or reasonably expected to be listed on a national securities exchange.

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Unlisted REITs and DPPs

Customer Account Statements and Due Diligence Requirements for Unlisted Real Estate Investment Trusts (REITs) and Direct Participation Programs (DPPs)

Executive Summary

FINRA is issuing this *Notice* to address certain requirements that apply to the per-share customer account statement values and dividend distributions of REITs and DPPs (collectively, “real estate investment programs”) that are sold through broker-dealers, invest in real estate and do not trade on a national securities exchange.¹

Questions regarding this *Notice* may be directed to:

- Joseph E. Price, Vice President, Corporate Financing, at (240) 386-4642;
- Gary L. Goldsholle, Vice President and Associate General Counsel, Office of General Counsel, at (202) 728-8104; or
- Lisa Jones Toms, Counsel, Corporate Financing, at (240) 386-4661.

Background and Discussion

Responsibility of Firms Concerning “Par Value”

NASD Rule 2340 (Customer Account Statements) requires a general securities member firm to include in a customer’s account statement an estimated value for a real estate investment trust (REIT) or direct participation program (DPP) security if the annual report of the security that is held in the customer’s account includes a per-share estimated value (and provided certain conditions set forth in the rule are met).² The rule permits a firm to use an estimated value disclosed in the program’s annual report, and in practice, that is the value typically used. During the offering period, the estimated value included in the annual report usually is the value at which securities are being offered to the public, commonly known as “par value.”

February 2009

Notice Type

- Guidance

Suggested Routing

- Compliance
- Legal
- Senior Management

Key Topic(s)

- Customer Account Statements
- Due Diligence
- Unlisted Real Estate Investment Trusts (REITs)
- Direct Participation Programs (DPPs)

Referenced Rules & Notices

- NASD Rule 2340
- NASD Rule 2810

NASD Rule 2340(c)(2) prohibits a firm from using a per-share estimated value that has been developed from data that is as of a date more than 18 months prior to the customer account statement's date. The 18-month requirement was designed to ensure that investors are provided with reasonably current valuations of these illiquid securities. In addition, by providing firms with an 18-month window in which to rely on the data, the rule ensures that either they or the sponsors have adequate time to appraise the program's assets and operations and calculate an estimated value.

During the offering period, it may be reasonable to determine that the estimated value is the value at which the shares are being offered to the public. However, 18 months after the conclusion of the offering, that value would be aged data and should not be the basis for the valuation provided on a customer's account statement. Thus, in accordance with NASD Rule 2340(c)(2), firms must not use par value in a customer account statement more than 18 months following the conclusion of an offering, unless an appraisal of the program's assets and operations yields the same value.

Responsibility of Firms Concerning Expected Dividend Distributions³

NASD Rule 2810 (Direct Participation Programs) regulates public offerings of real estate investment programs. Rule 2810(b)(3) requires that firms, prior to participating in a public offering of a real estate investment program, have reasonable grounds to believe that all material facts are adequately and accurately disclosed and provide a basis for evaluating the program.⁴ To determine the adequacy of the disclosed facts, a firm shall obtain information on material facts relating to, among other things, the financial stability and experience of the sponsor and the program's risk factors. Analysis of these factors should include an inquiry into the amount or composition of a real estate investment program's dividend distributions.⁵ As part of its inquiry, a firm should determine the amount of the distributions that represents a return of investors' capital and whether that amount is changing.⁶ In addition, firms should consider whether there are impairments to the real estate investment program's assets or other material events that would affect the distributions and whether disclosure regarding dividend distributions needs to be updated to reflect these events.

For example, firms should obtain information regarding whether there have been unscheduled cancellations of existing leases that impair or materially affect a real estate investment program's operating cash flows. If operating cash flows decline substantially, the program may decide to lower the dividend distributions or try to maintain historic dividend payments by borrowing funds or returning investors' capital. Paying dividend distributions that are unsustainable over the long term due to cash flow difficulties presents a significant risk to investors' future returns and to the long-term viability of the program.

Endnotes

- 1 Generally, REITs are pass-through entities governed in part by Section 856 of the U.S. Internal Revenue Code that offer investors an equity interest in a pool of real estate assets, including land, buildings, shopping centers, hotels and office properties. Some DPPs also invest in real estate. Similar to REIT investments, these DPPs typically offer investors an equity interest in an entity such as a limited partnership that provides flow-through tax consequences and distributes income generated from underlying real estate assets.
- 2 See *Notice to Members 01-08* (January 2001) and “DPP and REIT Valuations on Customer Account Statements,” *Regulatory & Compliance Alert* (Summer 2001). See also generally *Regulatory Notice 08-77* (December 2008) (providing guidance on estimated annual income and estimated yield on customer account statements for certain products, including REITs and DPPs).
- 3 As used in this *Notice*, “dividend distributions” or “distributions” refer to the periodic distributions by the real estate investment program to shareholders or limited partners in the form of cash or securities. These distributions generally consist of dividend income, and may include capital gains and some return of capital. Distributions to shareholders are declared by the REIT’s board of directors and usually paid on a monthly or quarterly basis.
- 4 “Participating” in a best-efforts offering includes participation in each offer or sale made pursuant to a registration statement. Accordingly, the Rule 2810(b)(3) requirements apply prior to participating in every sale in which prospectus delivery is required. See also, *In re Worldcom, Inc.* 346 F. Supp. 2d 628, 670 (S.D.N.Y. 2004) (noting that in adopting rules relating to shelf offerings the SEC stressed the use of “anticipatory and continuous due diligence programs” to augment underwriters’ fulfillment of their due diligence obligations); and Securities Act Rule 430B (providing that the effective date for a shelf registration statement for liability purposes for takedowns is the date a prospectus supplement is filed in connection with each takedown).
- 5 FINRA recently reminded firms of their sales practice obligations and related requirements regarding sales of securities in a high-yield environment. See *Regulatory Notice 08-81* (December 2008). The *Notice* generally addresses firms’ sale practice obligations with regard to the sale of securities in a high-yield environment and provides comparable guidance to firms concerning other fixed income and other securities products.
- 6 Many factors may influence the degree to which a distribution comprises a return of capital. For example, in a newer program a high proportion of the distributions to shareholders may consist of a return of capital until the proceeds raised from the real estate investment program’s initial public offering are generating cash flows from operations.

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DPP and Unlisted REIT Securities

SEC Approves Amendments to FINRA Rule 2310 and NASD Rule 2340 to Address Values of Direct Participation Program and Unlisted Real Estate Investment Trust Securities

Effective Date: April 11, 2016

Executive Summary

The SEC approved amendments to NASD Rule 2340 (Customer Account Statements) to modify the requirements relating to the inclusion of per share estimated values for direct participation program (DPP) and unlisted real estate investment trust (REIT) securities on account statements, and to FINRA Rule 2310 (Direct Participation Programs) to make corresponding changes to the requirements applicable to members' participation in public offerings of DPP or REIT securities.¹ The amendments become effective on April 11, 2016.

The amended rule text is available at www.finra.org/notices/15-02.

Questions concerning this *Notice* should be directed to:

- ▶ Joseph E. Price, Senior Vice President & Counsel, Advertising Regulation and Corporate Financing, at (240) 386-4642 or Joseph.Price@finra.org;
- ▶ Paul M. Mathews, Vice President & Director, Corporate Financing, at (240) 386-4639 or Paul.Mathews@finra.org; or
- ▶ James S. Wrona, Vice President & Associate General Counsel, Office of General Counsel, at (202) 728-8270 or Jim.Wrona@finra.org.

Background & Discussion

NASD Rule 2340 currently requires a general securities member to include on account statements an estimated value of a DPP or REIT security from the annual report, an independent valuation service or any other source, unless the member can demonstrate the estimated value is inaccurate. FINRA Rule 2310 provides that a member may not participate in a DPP or REIT offering unless the general partner or sponsor will disclose a per share estimated value in each annual report.

January 2015

Notice Type

- ▶ Rule Amendment

Suggested Routing

- ▶ Compliance
- ▶ Legal
- ▶ Senior Management

Key Topics

- ▶ Customer Account Statements
- ▶ Direct Participation Programs
- ▶ Unlisted Real Estate Investment Trusts

Referenced Rules & Notices

- ▶ FINRA Rule 2310
- ▶ NASD Rule 2340

The general industry practice is to use the offering price (or “par value”) of DPP and REIT securities as the per share estimated value during the offering period, which can continue as long as seven and one-half years. The offering price, typically \$10 per share, often remains constant on customer account statements during this period even though various costs and fees have reduced investors’ principal and underlying assets may have decreased in value.

The SEC recently approved FINRA’s proposed amendments to Rule 2340 and Rule 2310 that require general securities members to provide more accurate per share estimated values on customer account statements, shorten the time period before a valuation is determined based on an appraisal and provide various important disclosures. The effective date of the amendments is April 11, 2016.

I. NASD Rule 2340 (Customer Account Statements)

NASD Rule 2340 generally requires that general securities members provide periodic account statements to customers, on at least a quarterly basis, containing a description of any securities positions, money balances or account activity since the last statement. Paragraph (c) addresses the inclusion of per share estimated values for DPP and REIT securities held in customer accounts or included on customer account statements. The rule also provides for several disclosures regarding the illiquidity and resale value of DPP and REIT securities.

The SEC has approved amendments to Rule 2340(c) to require, among other things, general securities members to include in customer account statements a per share estimated value for a DPP or REIT security developed in a manner reasonably designed to ensure that the per share estimated value is reliable. In addition, the amended rule provides two methodologies for calculating the per share estimated value for a DPP or REIT security that is deemed to have been developed in a manner reasonably designed to ensure that it is reliable: (1) the net investment methodology and (2) the appraised value methodology. The amended rule also imposes various enhanced disclosure obligations, as discussed below.

A. Net Investment Methodology

The amendments to Rule 2340(c)(1)(A) require “net investment” to be based on the “amount available for investment” percentage in the “Estimated Use of Proceeds” section of the offering prospectus. Where “amount available for investment” is not provided, the amended rule requires “net investment” to be based on another equivalent disclosure that reflects the estimated percentage deduction from the aggregate dollar amount of securities registered for sale to the public of sales commissions, dealer manager fees and estimated issuer offering and organization expenses. In addition, the amended rule clarifies

that when an issuer provides a range of amounts available for investment, a member may use the maximum offering percentage unless the member has reason to believe that such percentage is unreliable. If the member has reason to believe that it is unreliable, the member must use the minimum offering percentage. The rule permits the net investment value to be used until 150 days following the second anniversary of breaking escrow in the public offering.

B. Appraised Value Methodology

The appraised value methodology, which can be used at any time, consists of the appraised valuation disclosed in the issuer's most recent periodic or current report filed with the SEC. As amended, Rule 2340(c)(1)(B) requires that the per share estimated value disclosed in an issuer's most recent periodic or current report be based on valuations of the assets and liabilities of the DPP or REIT, and that those valuations be:

- ▶ performed at least annually;
- ▶ conducted by, or with the material assistance or confirmation of, a third-party valuation expert or service; and
- ▶ derived from a methodology that conforms to standard industry practice.

Where a DPP is subject to the Investment Company Act of 1940 (1940 Act) (e.g., business development companies), instead of a valuation that meets the appraisal requirements listed immediately above, the rule requires that the appraised value must be consistent with the valuation requirements of the 1940 Act and the rules thereunder.

C. Disclosures

New Rule 2340(c)(2)(A) requires members that use the "net investment" methodology to provide, if applicable, enhanced disclosure relating to the return of investors' capital (often referred to as "over distributions") in order to address potential misunderstanding by customers when their capital is returned to them through a distribution that otherwise could appear to represent earnings on their investment. Rule 2340(c)(2)(A) requires an account statement that provides a "net investment" per share estimated value for a DPP or REIT security to disclose, if applicable, prominently and in proximity to disclosure of distributions and the per share estimated value the following statements: "IMPORTANT – Part of your distribution includes a return of capital. Any distribution that represents a return of capital reduces the estimated per share value shown on your account statement."

The disclosure under new Rule 2340(c)(2)(A) applies only to an account statement that provides a "net investment" per share estimated value where part of the distribution includes a return of capital. Thus, for example, this requirement does not apply to an account statement that provides an "appraised value" for the per share estimated value, which already would reflect returns of capital.

However, the disclosures under new Rule 2340(c)(2)(B) are required for all account statements that provide a per share estimated value for a DPP or REIT security. Pursuant to this new provision, a member must disclose that the DPP or REIT securities are not listed on a securities exchange, are generally illiquid and that, even if a customer is able to sell the securities, the price received may be less than the per share estimated value provided in the account statement.

II. FINRA Rule 2310 (Direct Participation Programs)

FINRA Rule 2310(b)(5) generally provides that a member may not participate in a public offering of DPP or REIT securities unless specified disclosures about the value of such securities will be made by the general partner or sponsor of the DPP or REIT in each annual report distributed to investors pursuant to Section 13(a) of the Exchange Act. FINRA amended the requirements to correspond to the amendments to NASD Rule 2340(c). As amended, Rule 2310(b)(5) prohibits a member from participating in a public offering of the securities of a REIT or DPP unless the issuer of the DPP or REIT has agreed to disclose:

- ▶ a per share estimated value of the DPP or REIT security, developed in a manner reasonably designed to ensure it is reliable, in the DPP or REIT periodic reports filed pursuant to Section 13(a) or 15(d) of the Exchange Act;
- ▶ an explanation of the method by which the value was developed; and
- ▶ the date of the valuation.

In addition, amended Rule 2310(b)(5) prohibits a member from participating in a public offering of the securities of a REIT or DPP unless the issuer of the DPP or REIT has agreed to disclose, in a periodic or current report filed pursuant to Section 13(a) or 15(d) of the Exchange Act within 150 days following the second anniversary of breaking escrow and in each annual report thereafter, a per share estimated value:

- ▶ based on the valuations of the assets and liabilities of the DPP or REIT performed at least annually by, or with the material assistance or confirmation of, a third-party valuation expert or service;
- ▶ derived from a methodology that conforms to standard industry practice; and
- ▶ accompanied by a written opinion or report by the issuer, delivered at least annually, that explains the scope of the review, the valuation methodology used and the basis for the reported value.

The amendments to Rule 2310(b)(5) do not apply to DPPs that are subject to the 1940 Act as such DPPs are already required to determine and publish net asset value on a regular basis.

Endnotes

1. See Securities Exchange Act Release No. 73339 (October 10, 2014), 79 FR 62489 (October 17, 2014) (Order Approving SR-FINRA-2014-006, as Modified by Amendment No. 1).

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**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK**

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

-- against --

**AR CAPITAL, LLC, NICHOLAS S. SCHORSCH
and BRIAN S. BLOCK,**

Defendants.

19 Civ. ____ ()

ECF Case

COMPLAINT

Plaintiff Securities and Exchange Commission (“Commission”), for its Complaint against Defendants AR Capital, LLC (“AR Capital”), Nicholas S. Schorsch (“Schorsch”), and Brian S. Block (“Block”) (together, “Defendants”), alleges:

PRELIMINARY STATEMENT

1. Between late 2012 and early January 2014 (the “Relevant Period”), Defendants improperly obtained millions of dollars to which they were not entitled from a publicly-traded

real estate investment trust (“REIT”) managed by Defendants, then known as American Realty Capital Properties, Inc. (“ARCP”).¹

2. AR Capital sponsored and externally managed REITs, including ARCP and two publicly-held, non-traded REITs (“NTRs”), American Realty Capital Trust III, Inc. (“T3”) and American Realty Capital Trust IV, Inc. (“T4”), that were merged into ARCP. At all relevant times, Schorsch was AR Capital’s chief executive officer (“CEO”) and principal owner, and Block was AR Capital’s chief financial officer (“CFO”) and a minority owner. Schorsch also served as the CEO and chairman of ARCP, T3, and T4, while Block also served as the CFO of each REIT. As a result, Defendants had management control over all three REITs during the Relevant Period.

3. In connection with separate mergers, first between ARCP and T3, and later between ARCP and T4, AR Capital, acting through Block and Schorsch—without the informed consent of the relevant REIT’s board, in contravention of the governing documents and disclosures to shareholders, and in violation of their fiduciary duties—improperly inflated an incentive fee calculation which operated as a fraud or deceit on ARCP and its shareholders. Through their actions, Defendants collected more than 2.9 million operating partnership units (“OP units”) of ARCP to which they were not entitled.

4. Defendants also directed the creation of and/or approved misleading asset purchase and sale agreements in which AR Capital received \$5.8 million from ARCP in connection with each merger, purportedly for ARCP’s purchase from AR Capital of furniture, fixtures, and equipment (“FF&E”) necessary for the T3- or T4-related post-merger operations of

¹ In 2015, ARCP changed its name to VEREIT, Inc.

ARCP and the reimbursement to AR Capital of certain “unreimbursed expenses.” Through those agreements, Defendants wrongfully obtained at least \$7.27 million in unsupported charges.

5. In connection with these activities, Defendants made material misstatements and omissions about the incentive fees and FF&E agreements relating to both mergers.

VIOLATIONS

6. By engaging in the conduct described in this Complaint, AR Capital and Block violated Sections 17(a)(1), (a)(2), and (a)(3) of the Securities Act of 1933 (“Securities Act”) [15 U.S.C. § 77q(a)(1), (a)(2), and (a)(3)] and Section 10(b) of the Securities Exchange Act of 1934 (“Exchange Act”) [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5], as well as Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78m(b)(2)] and Rule 13b2-1 thereunder [17 C.F.R. § 240.13b2-1]. Schorsch, by engaging in the conduct described in this Complaint, violated Sections 17(a)(2) and (a)(3) of the Securities Act [15 U.S.C. § 77q(a)(2) and (a)(3)] and Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1].

NATURE OF THE PROCEEDING AND RELIEF SOUGHT

7. The Commission brings this action pursuant to the authority conferred on it by Sections 20(b) and 20(d) of the Securities Act [15 U.S.C. §§ 77t(b) and 77t(d)] and Sections 21(d)(1), (d)(3), and (d)(5) of the Exchange Act [15 U.S.C. §§ 78u(d)(1), (d)(3), and (d)(5)] seeking a final judgment: (a) permanently restraining and enjoining AR Capital, Schorsch, and Block from engaging in the acts, practices and courses of business alleged herein; (b) requiring AR Capital, Schorsch, and Block to disgorge ill-gotten gains and to pay prejudgment interest thereon; and (c) imposing civil money penalties on AR Capital, Schorsch, and Block pursuant to Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)].

JURISDICTION AND VENUE

8. This Court has subject-matter jurisdiction over this action pursuant to Sections 20(b) and 22(a) of the Securities Act [15 U.S.C. §§ 77t(b) and 77v(a)] and Sections 21(d) and 27 of the Exchange Act [15 U.S.C. §§ 78u(d) and 78aa]. Defendants, directly or indirectly, have made use of the means or instruments of transportation or communication in interstate commerce, or of the mails, or of a facility of a national securities exchange in connection with the transactions, acts, practices and courses of business alleged in this Complaint.

9. Venue is proper in the Southern District of New York pursuant to 22(a) of the Securities Act [15 U.S.C. § 77v(a)] and Section 27 of the Exchange Act [15 U.S.C. § 78aa]. Certain of the transactions, acts, practices and courses of business constituting the violations alleged herein occurred in the Southern District of New York, including, among other things, certain of Defendants' communications and other actions concerning the incentive fees and FF&E transactions that occurred at AR Capital's principal office in New York, New York.

THE DEFENDANTS

10. **AR Capital** is a Delaware limited liability corporation with its principal place of business in New York, New York. Through various wholly-owned subsidiaries, AR Capital sponsored and externally managed T3 and T4 until their respective mergers with ARCP, as well as sponsored and externally managed ARCP, a publicly-traded REIT, until January 8, 2014, when ARCP became self-managed.²

11. **Schorsch**, age 57, resides in Newport, Rhode Island, and Meadowbrook, Pennsylvania. Schorsch directly or indirectly owns and controls a majority interest in AR Capital

² AR Capital and its wholly-owned subsidiaries are collectively referred to as "AR Capital" throughout this Complaint.

and, during the Relevant Period, served as CEO and Chairman of T3 and T4 until their mergers with ARCP, and as CEO and Chairman of ARCP. When ARCP became self-managed in January 2014, Schorsch became directly employed by ARCP and continued to serve as CEO and Chairman. Schorsch resigned from all roles with ARCP on December 14, 2014.

12. **Block**, age 46, resides in Hatfield, Pennsylvania. During the Relevant Period, Block served as CFO of T3 and T4 from their inceptions until their mergers with ARCP, and as CFO of ARCP. When ARCP became self-managed in January 2014, Block became directly employed by ARCP and continued to serve as CFO. Block resigned from all roles with ARCP on October 28, 2014. Block was a CPA licensed in Pennsylvania. His license is currently inactive.

OTHER RELEVANT ENTITIES

13. **ARCP** was incorporated in Maryland in 2010 as American Realty Capital Properties, Inc. and, during the Relevant Period, its principal place of business was in New York, New York. ARCP conducted an initial public offering of its common stock and began trading on NASDAQ's Global Select Market in September 2011 as a REIT sponsored and externally managed by AR Capital, and had no employees of its own. AR Capital continued as ARCP's external manager until January 8, 2014, when ARCP became self-managed. In 2015, ARCP changed its name to VEREIT, Inc. and its common stock trades on the NYSE. Notwithstanding its name change, the entity is referred to as ARCP in this Complaint.

14. **T3** was incorporated in Maryland and was an NTR sponsored and externally managed by AR Capital from its inception until the close of its merger with ARCP on February 28, 2013. T3 commenced a public offering of its stock in March 2011 pursuant to an effective Form S-11 registration statement at a fixed price of \$10 per share (less concessions) and closed

the offering in September 2012 after raising over \$1.5 billion. T3 entered into a merger agreement with ARCP on December 14, 2012, which closed on February 28, 2013.

15. T4 was incorporated in Maryland and was an NTR sponsored and externally managed by AR Capital from its inception until the close of its merger with ARCP in January 3, 2014. T4 commenced its public offering in June 2012 pursuant to an effective Form S-11 registration statement at a fixed price of \$25 per share (less concessions) and closed the offering in April 2013 after raising more than \$1.75 billion. T4 entered into a merger agreement with ARCP on July 1, 2013, and which closed (following certain amendments) on January 3, 2014.

FACTS

A. Defendants Obtained Improperly Inflated Promote Fees

16. AR Capital's business primarily involved creating and sponsoring NTRs and publicly-traded REITs, externally managing such REITs, and, for its NTRs, pursuing liquidity events such as mergers, sales, or public listings. AR Capital was contractually entitled to receive certain fees from the REITs for each of these activities or events.

17. ARCP, T3, and T4 were REITs whose common stock was offered to the public and registered with the Commission. Each REIT was structured as a corporation that conducted most of its business through an affiliated operating partnership ("OP") entity for which the REIT served as general partner—ARC Properties Operating Partnership, L.P. (the "ARCP OP"), American Realty Capital Operating Partnership III, L.P. (the "T3 OP"), and American Realty Capital Operating Partnership IV, L.P. (the "T4 OP"), respectively. Limited partnership agreements ("LPAs") governed the T3 OP and T4 OP. Schorsch signed the LPAs as CEO of each REIT.

18. The relevant REIT owned units of its affiliated OP entity (“OP units”) on a 1:1 basis with the number of shares of common stock outstanding of the REIT, which generally constituted in excess of 95% ownership of the OP entity. The remaining OP units not owned by the REIT were primarily issued to AR Capital and its members and employees as compensation. Subject to certain limitations, including but not limited to minimum holding periods, OP units owned by AR Capital and its members and employees could be converted on a 1:1 basis into shares of common stock of the REIT.

19. Because T3 and T4 were not publicly traded, generally, the only means through which the NTR could generate liquidity opportunities for its shareholders (other than dividends delivered to investors) would be through a liquidity event, such as a merger, sale, or public listing.

20. Among other things, the T3 OP and T4 OP LPAs provided that, if T3 or T4 achieved a certain level of return for its common stock shareholders through a liquidity event—such as a merger—AR Capital would be entitled to a “subordinated distribution,” colloquially referred to as a “promote fee.” The terms “subordinated distribution” and “promote fee” are used interchangeably in this Complaint.

21. Specifically, the LPAs provided that if the liquidity event provided shareholders with a return in excess of a 6% hurdle rate, AR Capital would be entitled to receive 15% of the amount that was above the hurdle rate. The LPAs further specified that the amount of the return to shareholders was to be determined by T3 and T4 “in good faith” using the “fair market value” of all issued and outstanding shares of the NTR common stock (*i.e.*, the total merger consideration received by the NTR’s shareholders) as of the date of the liquidity event (*i.e.*, merger closing date).

22. In a side letter that was executed in connection with each merger, AR Capital agreed to take the promote fee in OP units of the T3 or T4 OP, which would then be converted into OP units of the ARCP OP in the merger. The LPAs, as confirmed by these side letters, specified the conversion formula to calculate the number of T3 or T4 OP units to be issued for the promote fee. The formula involved simple division using the same fair market value that determined the return to NTR shareholders. The formula did not provide any enhanced value for agreeing to receive NTR OP units instead of cash. As set forth in the side letters and merger agreements, the T3 or T4 OP units would immediately convert to ARCP OP units at the specified merger exchange ratio in accordance with the merger agreements.

23. AR Capital, Schorsch, and Block each owed a fiduciary duty to T3, T4, and their shareholders. In calculating the promote fees, Defendants (as external managers of T3 and T4) acted on behalf T3 and T4, the entities with the obligation under the LPAs to perform the calculation. Defendants were obligated to act in the best interests of the REITs and their shareholders by either resolving financial conflicts in the shareholders' favor or by obtaining the informed consent of the NTR board.

24. AR Capital, acting through Block and Schorsch, inflated several aspects of the promote fee calculation and conversion formula in the T3 and T4 mergers that enriched the Defendants at the expense of the REITs and their shareholders. The Defendants' actions were contrary to shareholder disclosures, the LPAs, and the relevant merger side letters, and were not disclosed to the boards or the boards' advisors.

1. **Defendants Inflated the T3 Promote Fee**

25. T3 and ARCP entered into a merger agreement and related agreements on December 14, 2012. The merger agreement provided that T3 shareholders could elect to receive,

for every share of T3 common stock they held, either (i) 0.95 shares of ARCP common stock or (ii) \$12.00 in cash (capped at 30% of the aggregate merger consideration).

26. Similar to the conversion of the T3 common stock, the merger agreement further provided that T3 OP units, such as those held or to be received by AR Capital for the promote fee, would be automatically converted into 0.95 ARCP OP units.

27. As the external manager for both T3 and ARCP, AR Capital members, including Schorsch (who also served as Chairman and CEO of ARCP, T3 and T4) and Block (who also served as CFO of ARCP, T3 and T4), were heavily involved in discussions relating to the merger, including by participating in board meetings and providing the outside investment bankers retained by each REIT board with financial models and other information. Schorsch and Block also received memoranda from outside counsel for the REIT boards in connection with the merger that, among other things, set out the governing provisions from the LPA for the promote fee calculation and reminded that, as set forth in guidelines established by the North American Securities Administrators Association, a majority of the independent directors must approve all matters relating to the promote fee.

28. As authorized by both the T3 and ARCP boards, the related agreements entered into included a side letter with AR Capital (the "T3 side letter") in which T3 (and the T3 OP), ARCP (and the ARCP OP), and AR Capital agreed upon the governing provisions of the T3 OP LPA for the promote fee and that AR Capital would take the promote fee in T3 OP units. The T3 OP units would then be converted into 0.95 ARCP OP units as set forth in the merger agreement. The specified provision in the LPA with the formula for converting the cash value of the promote fee into T3 OP units involved simple division using the same fair market value that determined the return to T3 shareholders. This formula did not provide any enhanced value for AR Capital

agreeing to receive T3 OP units instead of cash. Schorsch signed the T3 side letter on behalf of AR Capital and ARCP.

29. The merger was announced on December 17, 2012, including in an ARCP Form 8-K filed with the Commission that Schorsch signed. Among other things, the Form 8-K included a description of the merger agreement terms and the T3 side letter, and included both agreements as exhibits.

30. The merger was contingent on approval by a majority of each of ARCP's and T3's shareholders. To solicit ARCP and T3 shareholders, ARCP and T3 issued a joint proxy statement/prospectus (the "T3 Proxy"), filed with the Commission on January 22, 2013, which set the shareholder voting meeting date for February 26, 2013. Among other things, the T3 Proxy incorporated the T3 side letter and made certain disclosures about the promote fee. In order to register the shares of ARCP common stock to be issued to T3 shareholders in connection with the merger, ARCP also filed a registration statement with the Commission on January 18, 2013, signed by Schorsch, Block, and other directors of the company, which repeated the information and disclosures appearing in the T3 Proxy (the "T3 Merger Registration Statement").

31. Because of their roles and affiliations with T3 and ARCP, AR Capital, Schorsch, and Block were required to disclose their interests in the merger in the T3 Proxy. The T3 Proxy disclosures designated to describe such interests made representations about how the promote fee (referred to as the subordinated distribution) would be calculated:

[AR Capital] ... will be entitled to subordinated distributions of net sales proceeds from the [T3] OP in an amount estimated to be equal to approximately \$59.0 million, assuming an implied price of [T3] common stock of \$12.26 per share in the merger (which assumes that 70% of the merger consideration is ARCP common stock based on a per share price of \$12.90, the closing price of ARCP common stock the last trading day before public announcement of the merger, and 30% of the merger consideration

is cash). Such subordinated distributions of net sales proceeds is to be finalized based on the closing price of ARCP common stock on the day immediately prior to the closing of the merger, payable in [T3] OP Units that will automatically convert into ARCP OP Units and will be payable upon the consummation of the partnership merger in accordance with the merger agreement.

32. The T3 Merger Registration Statement included an identical disclosure.

33. These disclosures set forth an understanding that the promote fee calculation would involve the actual cash/stock elections by T3 shareholders, consistent with the LPA's requirement to calculate the fair market value of all issued and outstanding shares of T3 common stock at the time of the merger closing. The disclosures also set forth that the promote fee would be "finalized based on the closing price of ARCP common stock on the day immediately prior to the closing of the merger"—*i.e.*, the determinative date for setting the implied price of T3 common stock for shares that elected to receive ARCP stock in the merger. According to the T3 Proxy and T3 Merger Registration Statement, AR Capital therefore would be entitled to a promote fee of approximately \$59.0 million if, among other things, (a) 30% of T3 shares elected cash; and (b) ARCP's closing price on the day immediately prior to the closing of the merger was \$12.90 per share.

34. Following the February 26, 2013 shareholder meetings, the companies announced that a majority of stockholders of both companies had approved the merger, that the preliminary T3 shareholder voting results showed approximately 15.5% of the outstanding T3 shares elected cash, and that the transaction was expected to close on February 28, 2013. The merger closed, as expected, on February 28, 2013, with final tabulations for T3 shareholder elections of 16.5% of shares electing cash (resulting in 83.5% receiving ARCP shares at the 0.95 exchange ratio).

35. In contravention of the T3 OP LPA, T3 side letter, and disclosures to shareholders, and without the informed consent of either the T3 or ARCP boards, the Defendants

inflated the calculation of the T3 promote fee in three ways: (i) using a trailing five-day average price of ARCP stock instead of the ARCP closing price on the day prior to the merger closing, (ii) disregarding the actual cash/stock elections by T3's shareholders, and (iii) using an unsupported multiplier in the conversion to OP units portion of the calculation.

a. Improper Change to a Trailing 5-Day Average Price Per Share

36. As specified in the T3 Proxy and T3 Merger Registration Statement, the promote fee payable to AR Capital "is to be finalized based on the *closing price* of ARCP common stock *on the day immediately prior to the closing of the merger*" (emphasis added), and the estimate provided used a single-day ARCP closing price per share. ARCP's closing price was \$13.90 on February 27, 2013, the day immediately prior to the closing of the merger.

37. Block prepared numerous model calculations of the promote fee leading up to and including the merger closing date of February 28, 2013, and provided certain versions to Schorsch. In each of these models, Block used a single-day closing price, consistent with the disclosure.

38. For example, on February 21, 2013, shortly before the merger vote date, Block sent Schorsch an email, attaching a projected promote fee calculation spreadsheet that used the single day ARCP closing price on February 20, 2013, and stating: "The attachment reflects all updated numbers—just ensuring we have no hiccups when this calculation is run final next week. We were pretty close so I'm feeling good about the computation. I'm feeling even better about the current schedule with a closing price of \$14.19..... (\$96.5MM)." Schorsch replied to the email, acknowledging its receipt and indicating that he read and understood it: "Agreed it looks [sic][.]"

39. Schorsch and Block tracked ARCP's closing share price in the days leading up to the merger. Although ARCP's share price reached a high in closing at \$14.54 on February 26, 2013, it closed down on heavier than average trading volume at \$13.90 on February 27, 2013, the day immediately prior to the merger closing.

40. On February 28, 2013 at 8:50 p.m., Schorsch sent Block an email with the subject line "Call re promote."

41. By mid-day on March 1, 2013, AR Capital, acting through Block, decided to inflate the promote fee by using an unweighted average of the closing prices on each of the five days prior to the merger closing ("5-day average") of \$14.264—instead of the ARCP closing price on the day immediately prior to the merger closing of \$13.90. Also on March 1, Block provided a spreadsheet with the final calculation to Schorsch.

42. In taking this unauthorized unilateral action that inflated (at the expense of ARCP's shareholders) the promote fee they would receive, AR Capital did not inform or obtain the consent of the T3 or ARCP boards.

b. Improper Change from Use of the Actual Merger Consideration

43. The final tabulation of the shareholder elections was that 16.5% of T3 common stock shares elected to receive \$12 in cash for each T3 share, and the remaining 83.5% of shares received 0.95 shares of ARCP common stock in exchange for each T3 share. Accordingly, Defendants should have calculated the T3 total merger proceeds using the actual consideration paid for the T3 common stock shares—including cash.

44. As set forth in the formulas disclosed in the T3 Proxy and T3 Merger Registration Statement, and using the actual inputs of the 16.5% cash elections and the ARCP closing share price on the day immediately prior to the merger closing of \$13.90, the implied T3 share price

should have been \$13.01 per share (*i.e.*, the product of the cash amount (\$12.00) multiplied by the percentage of cash elections (16.5%) plus the product of ARCP's share price the day prior to the merger closing (\$13.90) multiplied by the exchange ratio (0.95) multiplied by the stock-election percentage (83.5%)).

45. Defendants disregarded these formulas and disclosures. Instead, Schorsch instructed AR Capital and Block to ignore the actual cash elections and instead calculate the merger proceeds as if 100% of T3 shares had been exchanged for ARCP stock. This ran afoul of both the shareholder disclosures as well as the T3 OP LPA, which required that the promote fee be calculated using the fair market value of *all* issued and outstanding shares of T3 common stock—which included those shares exchanged for \$12.00 in cash. In effect, AR Capital's decision was to calculate the purported fair market value by assuming that the approximately 16.5% of T3 shares that received cash instead received shares of ARCP that AR Capital valued at more than \$394.4 million (including Defendants' use of the 5-day average price for ARCP stock)—despite the fact that those shareholders received only \$350.7 million in cash.

46. Following the merger closing, and as Schorsch and he discussed, Block performed the calculation as if 100% of the T3 shares were exchanged for ARCP shares, resulting in an inflated implied T3 price per share of \$13.55 (inclusive of the inflation caused by AR Capital's unauthorized decision to use a 5-day average price) versus the actual of \$13.01, and a promote fee cash value of \$98,359,915 versus the actual value of \$83,872,012.

47. Once again, Defendants did not inform or seek approval from the T3 or ARCP boards of their decision to change the calculation of the merger proceeds to assume 100% of the T3 shareholders had elected ARCP stock, a change that benefited Defendants at the expense of shareholders of the post-merger ARCP.

48. Moreover, on February 28, 2013, the same date as the merger closing, Block and Schorsch each signed ARCP's Form 10-K filed with the Commission for the fiscal year ended December 31, 2012, that reiterated that the merger was expected to close on that date and reiterated the T3 Proxy and T3 Merger Registration Statement disclosure concerning the promote fee, inclusive of the estimate being calculated with the assumption of 70% stock and 30% cash elections. This disclosure was materially misleading in light of the decision of Block and Schorsch to perform the promote calculation without consideration of the actual stock and cash elections.

c. Improper Conversion of the Promote Fee into ARCP OP Units

49. The T3 OP LPA, as confirmed by the T3 side letter, specified the formula for converting the promote fee value into T3 OP units. The conversion formula was simply to divide the cash value of the promote fee by the same fair value of one T3 share used to determine the total merger proceeds. In other words, whatever implied T3 price per share was used to calculate the total merger proceeds (which Defendants here—albeit wrongfully—had calculated as \$13.55 per T3 share) in the calculation of the cash value of the promote fee, that same implied T3 price per share should have been used to divide the cash value of promote fee to determine the T3 OP units to issue. Schorsch and Block each received legal memoranda that outside counsel provided to the boards of ARCP and T3 in connection with the merger negotiations, which summarized the promote fee and the conversion to OP units consistent with this method.

50. As the investment banking firms engaged by the respective boards were modeling the merger and preparing to provide a fairness opinion in early December 2012, AR Capital employees, including Block—as the management for both companies—were specifically asked by the investment bankers engaged by the T3 board in an email: “When calculating the number

of OP units to be issued for the promote, ... should we simply divide the total equity value of the promote by the implied offer price per share?" Block, copying Schorsch, responded by highlighting the phrase "simply divide the total equity value of the promote by the implied offer price per share" and confirmed that the highlighted phrase was appropriate.

51. After the closing of the T3 merger, AR Capital, acting through Block, instead took a third manipulative measure by changing the conversion formula to inflate the number of OP units AR Capital received, and further increase the value of the promote fee owing to AR Capital. Using the division conversion formula set forth in the T3 OP LPA (and T3 side letter) and the multiplication by the merger exchange ratio of 0.95 set forth in the T3 merger agreement (and T3 side letter) would have resulted in 6,895,675 ARCP OP units (*i.e.*, dividing the improperly derived \$98,359,915 by the purported \$13.55 implied T3 price per share for the conversion to T3 OP units, and then multiplying by the merger exchange ratio of 0.95)—versus the 6,126,199 ARCP OP units to which AR Capital was actually entitled for the promote fee (*i.e.*, dividing the properly calculated promote fee cash value of \$83,872,012 by \$13.01, the properly calculated implied T3 price per share used to calculate the promote fee cash value, and then multiplying by the merger exchange ratio of 0.95).

52. However, Block—without any basis—took additional manipulative measures that increased the number ARCP OP units that AR Capital received. Block instead first multiplied his inflated promote fee cash value of \$98,359,915 by 1.02618705. Then, rather than using the inflated 5-day average price that he had used to calculate the promote fee cash value, he reverted to the lower closing price per share on the day prior to the merger as the divisor, yielding 7,261,559 ARCP OP units.

53. These actions not only contravened the T3 OP LPA, T3 side letter, disclosures to boards and investors, and communications with the investment bankers, but also reflect Block's manipulative intent in the simultaneous use of different "fair market values" for the identical T3 shares measured as of the same date. Block's actions on behalf of AR Capital also served to further inflate the number of OP units for AR Capital's benefit at the expense of ARCP and its shareholders. Once again, no one from AR Capital informed the T3 or ARCP boards or shareholders of their actions to calculate the promote fee or conversion in this manner.

54. Block circulated to Schorsch a spreadsheet of the final promote fee calculation incorporating the manipulative calculations described above.

d. Impact of the Defendant's Improper T3 Promote Fee Calculation

55. Collectively, the three forms of manipulation resulted in AR Capital's receipt of 1,135,360 more ARCP OP units than AR Capital was entitled to receive (*i.e.*, 7,261,559 ARCP OP units received vs. 6,126,199 ARCP OP units to which AR Capital was entitled).

56. On March 1, 2013, Block circulated to Schorsch a spreadsheet with the final calculation of promote fee that showed each steps of the calculation, including the three manipulations alleged above. The final calculation spreadsheet was never provided to the boards of T3 or ARCP.

57. Instead, after Block finalized the spreadsheet on March 1, 2013, Defendants participated in creating or approving a "Contribution and Exchange Agreement" for AR Capital to enter into with the T3 OP and the ARCP OP (the "T3 Contribution and Exchange Agreement"). Block signed the agreement on behalf of AR Capital and Schorsch signed the agreement on behalf of the ARCP OP, in his capacity as the CEO of ARCP, the general partner

of the ARCP OP. The agreement was included as an exhibit to a Form 8-K signed by Schorsch that described the agreement and was filed with the Commission on March 6, 2013.

58. The agreement represented that, under the T3 OP LPA, AR Capital “will be entitled to receive” a promote fee of \$98,359,915, and that the conversion to OP units was calculated in accordance with the T3 OP LPA and T3 side letter. AR Capital further represented that nothing in the agreement violated or conflicted with any governing document or agreement by which it was bound—which included the T3 OP LPA and the T3 side letter.

59. These representations were materially false and misleading. AR Capital was not entitled to receive a promote fee with a cash value of more than \$83,872,012; nor was the conversion of the promote fee cash value to OP units calculated in accordance with the T3 OP LPA and T3 side letter, which resulted in further inflation of the value of the promote fee.

60. Similar misrepresentations were made in subsequent ARCP quarterly and annual reports filed with the Commission on Forms 10-Q and 10-K beginning with the first quarter of 2013 (filed May 6, 2013) through the second quarter of 2014 (filed July 29, 2014), each of which Block and Schorsch signed in their capacities as ARCP’s CFO and CEO, respectively. For example, the ARCP Form 10-Q for the first quarter of 2013 stated that upon the consummation of the T3 merger, AR Capital was “entitled to” a promote fee “which resulted in the issuance of [T3] OP units in the [T3] OP, when after applying the Exchange Ratio, resulted in the issuance of an additional 7.3 million [ARCP] OP Units.” In fact, AR Capital was only entitled to receive 6,126,199 ARCP OP Units for the promote fee.

61. Block, who personally performed the calculation of the promote fee and conversion to ARCP OP units in a spreadsheet that he maintained on behalf of AR Capital, knew or recklessly disregarded that each of the three manipulations alleged above contravened the

disclosures to shareholders, the T3 OP LPA, the side letter, legal memoranda prepared by outside counsel to the T3 and ARCP boards concerning the promote fee, presentations to the T3 and ARCP boards, and information provided to T3's and ARCP's investment bankers. Block also knew or recklessly disregarded that his actions improperly inflated the number of ARCP OP units that AR Capital would receive for the promote fee, from which he would also personally benefit. As the CFO of AR Capital, Block's actions and scienter are attributable to AR Capital.

62. Schorsch was at least negligent when he approved the promote fee and authorized the issuance of the ARCP OP units after receiving Block's spreadsheet with the final calculation of promote fee that showed each step of the calculation, including the three manipulations alleged above. Schorsch had participated in all of the merger-related board meetings for both the T3 and ARCP boards, received the legal memoranda that explained how the promote fee calculation was to be performed, and signed the T3 OP LPA, the T3 side letter, the T3 Merger Registration Statement, the T3 Contribution and Exchange Agreement, and the subsequent Form 10-Qs and Form 10-K. Schorsch knew or should have known that the calculation he approved did not conform to what was authorized by the T3 OP LPA and side letter, the presentation to the boards, and the disclosures to the investors.

2. Defendants Inflated the T4 Promote Fee

63. Four months after ARCP closed the merger with T3, ARCP and T4 entered into a merger agreement and related agreements on July 1, 2013 (the "T4 merger").

64. At the time, both ARCP and T4 were externally managed by AR Capital. As the external manager for both T4 and ARCP, AR Capital members, including Schorsch (who also served as Chairman and CEO of each REIT) and Block (who also served as CFO of each REIT), were heavily involved in discussions relating to the merger, including by participating in board

meetings and providing the outside investment bankers retained by each REIT board with financial models and other information. Schorsch and Block also received memoranda from outside counsel for the REIT boards in connection with the merger that, among other things, set out the governing provisions for the promote fee calculation and reminded that a majority of the independent directors must approve all matters relating to the promote fee.

65. The promote fee provisions in the T4 OP LPA were identical to those in the T3 OP LPA. Schorsch had signed the operative amended and restated T3 OP LPA and T4 OP LPA on November 13, 2013, and November 12, 2013, respectively—approximately one month prior to the T3 merger announcement. Among other things, the T4 OP LPA provision governing the conversion of the promote fee to T4 OP units was identical to that in the T3 OP LPA. The T4 OP LPA conversion formula was simply to divide the cash value of the promote fee by the same fair value of one T4 share used to determine the total merger proceeds. In other words, whatever implied T4 price per share was used to calculate the total merger proceeds in the calculation of the cash value of the promote fee, that same implied T4 price per share was required to be used to divide the cash value of the promote fee to determine the T4 OP units to issue.

66. Similarly, as authorized by both the T4 and ARCP boards, the merger-related agreements entered into on July 1, 2013, included a side letter with AR Capital (the “T4 side letter”) in which T4 (and the T4 OP), ARCP (and the ARCP OP), and AR Capital agreed upon the governing provisions of the T4 OP LPA for the promote fee (including the simple division conversion formula set forth above) and that AR Capital would take the promote fee in T4 OP units, which would then be converted into ARCP OP units at the merger exchange ratio specified in the merger agreement. Schorsch signed the T4 side letter.

67. The T4 merger was announced on July 2, 2013, including in an ARCP Form 8-K filed with the Commission that Schorsch signed. Among other things, the Form 8-K included a description of the merger agreement terms and the T4 side letter, and included both agreements as exhibits. The Form 8-K also estimated that the promote fee would be approximately \$65.2 million, assuming an implied price of T4 common stock of \$30.47 per share in the merger, and would be payable in the form of T4 OP units that would automatically convert into ARCP OP units upon the consummation of the T4 merger.

68. The T4 merger was contingent on approval by a majority of T4's shareholders and an effective ARCP registration statement to issue ARCP shares to T4 shareholders (the "T4 Merger Registration Statement"). To solicit T4 shareholder votes, T4 and ARCP issued a proxy statement/prospectus (the "T4 Proxy") on December 4, 2013.

69. Because of their roles and affiliations with T4 and ARCP, AR Capital, Schorsch, and Block were required to disclose their interests in the merger in the T4 Proxy. The T4 Proxy disclosures describing such interests made representations about how the promote fee (referred to as the subordinated distribution) would be calculated:

The amount of such subordinated distribution is estimated to equal approximately \$62.7 million, assuming a value of \$30.43 for the nominal consideration to [T4] stockholders in the merger (based on the closing price of ARCP common stock of \$12.70 per share on October 4, 2013). The amount of such subordinated distributions of net sales proceeds is to be finalized based on the closing price of ARCP common stock on the day immediately prior to the closing of the merger, and will be payable in [T4] OP Units that will automatically convert into ARCP OP Units upon consummation of the mergers in accordance with the [T4] side letter.

70. All of the relevant representations in the T4 Proxy were repeated in the T4 Merger Registration Statement signed by Schorsch and Block and filed with the Commission.

71. As set forth in the T4 side letter in reference to the T4 OP LPA, as well as the disclosures to shareholders in the T4 Proxy and T4 Merger Registration Statement, the cash value of the promote fee was to be determined by the implied value per share of T4 common stock derived from the closing price of ARCP common stock on the day immediately prior to the closing of the merger; the conversion into T4 OP units would be calculated by dividing the cash value of the promote fee by that same implied value per share of T4 common stock; and the T4 OP units would be automatically converted into ARCP OP units at the merger exchange ratio set forth in the T4 merger agreement.

72. Nevertheless, Defendants improperly disregarded the operative agreements and shareholder disclosures, instead using a \$22.50 per share insider initial T4 offering price (the “insider T4 initial price”) solely for purpose of dividing the cash value of the promote fee to yield the number of T4 OP units, rather than using the fair value of one share of T4 common stock on the date of the merger closing (which they had represented was \$30.43 assuming an ARCP closing price of \$12.70 per share). The improper use of \$22.50 per share as the denominator significantly inflated the number of OP units Defendants received—by approximately one-third. Moreover, once again, Defendants’ unauthorized actions were not disclosed to the boards and shareholders.

73. Schorsch approved AR Capital’s use of the \$22.50 insider T4 initial price for the conversion despite having signed the T4 side letter that specified the conversion must use the fair value of one share of T4 common stock on the date of the merger closing. Block carried out AR Capital’s use of the \$22.50 rate as the denominator for the conversion, despite knowledge of all of the agreements and his prior experience with the T3 merger, which included representing to

investment bankers on the T3 merger that the appropriate method was “simply divide the total equity value of the promote by the implied offer price per share.”

74. On January 3, 2014, the date of the closing of the T4 merger, in addition to the improper use of \$22.50 as the conversion denominator, Block also took one additional manipulative step to further inflate the promote fee. As of noon on January 3, 2014, Block updated his spreadsheet for the calculation of the promote fee using ARCP’s closing price of \$12.87 from January 2, 2014, the day immediately prior to the merger closing—the key date set forth in the T4 Proxy and T4 Merger Registration Statement—to calculate an implied T4 price per share of \$30.52. But ARCP’s share price closed higher at \$12.91 on January 3, 2014—the highest price it had achieved in approximately a month. Instead of calculating the promote fee using the closing price the day prior to the merger closing, as disclosures to investors dictated, Block recalculated it using the higher closing price on January 3, 2014, yielding an implied T4 price per share of \$30.54 and thereby inflating the cash value of the promote fee by over \$1 million.

75. Block then implemented the use of the \$22.50 per share value as the purported fair market value of one share of T4 common stock for the conversion to OP units, wholly disregarding the implied T4 price per share of \$30.54 he had just calculated. By doing so, Block substantially inflated the T4 OP units issued in exchange for the cash value of the promote fee, which would then be converted into ARCP OP units at the applicable merger exchange ratio. Block’s calculation yielded 6,734,148 ARCP OP units—1,787,085 more ARCP OP units than what AR Capital was entitled to under the T4 OP LPA and T4 side letter.

76. On or about January 7, 2014, Block shared his promote fee calculation spreadsheet with Schorsch for discussion that showed his use of the incorrect ARCP closing

price date and the conversion that used a \$22.50 denominator. Schorsch approved this T4 promote fee calculation. No one from AR Capital provided this final calculation spreadsheet to either the T4 or ARCP board or shareholders of either company.

77. Instead, similar to the T3 merger, after their T4 promote fee spreadsheet was finalized, Defendants participated in creating or approving a “Contribution and Exchange Agreement” for AR Capital to enter into with the T4 OP and the ARCP OP (the “T4 Contribution and Exchange Agreement”). Block signed the agreement on behalf of AR Capital. Schorsch signed the agreement on behalf of the T4 OP and the ARCP OP, in his capacity as the CEO of T4 and ARCP. The agreement was included as an exhibit to a Form 8-K, also signed by Schorsch, that described the agreement and was filed with the Commission at approximately 5:30 p.m. on January 3, 2014.

78. This agreement represented that under the T4 OP LPA, AR Capital “will be entitled to receive” a promote fee of \$63,235,388, and that the conversion to 6,734,148 ARCP OP units was calculated in accordance with the T4 OP LPA and the T4 side letter. AR Capital further represented that nothing in the agreement violated or conflicted with any governing document or agreement by which it was bound—which included the T4 OP LPA and the T4 side letter. These representations were materially false and misleading. AR Capital was not entitled to receive more than 4,947,063 ARCP OP units for the promote fee.

79. Similar misrepresentations regarding the promote fee were made in subsequent ARCP quarterly and annual reports filed with the Commission on Forms 10-K and 10-Q beginning with the Form 10-K for the fiscal year 2014 (filed February 27, 2014) through the second quarter of 2014 (filed July 29, 2014), each of which Block and Schorsch signed in their capacities as CFO and CEO, respectively, of ARCP. The statements regarding the promote fee

omitted material information that the T4 OP LPA, the T4 merger agreement, and the T4 side letter prohibited using a \$22.50 insider T4 initial price in converting the promote fee to OP units and that AR Capital's calculation was in contravention of those agreements, what was authorized by the two boards, and what was disclosed to shareholders.

80. Block, who personally performed the calculation of the T4 promote fee and conversion to ARCP OP units in a spreadsheet that he maintained on behalf of AR Capital, knew or recklessly disregarded that the manipulated calculations contravened the disclosures to shareholders, the T4 OP LPA, the T4 side letter, presentations to the T4 and ARCP boards, and information provided to the respective investment bankers retained by the T4 and ARCP boards. Block also knew or recklessly disregarded that his actions improperly inflated the number of ARCP OP units that AR Capital would receive for the promote fee, from which he would also personally benefit. As the CFO of AR Capital, Block's actions and scienter are attributable to AR Capital.

81. Schorsch was at least negligent when he approved the use of the \$22.50 denominator for the conversion and approved the T4 promote fee calculation performed by Block despite the fact that Schorsch signed the T4 side letter that specified the relevant T4 OP LPA provision that set forth the conversion formula. Schorsch was also present at all of the relevant ARCP and T4 board meetings and was aware or should have been aware that neither board had authorized the use of a different formula. Schorsch also knew or should have known that the impact from the use of a \$22.50 denominator for the conversion would result in a far greater number of OP units being issued versus the cash value of the promote fee, and significantly altered the promote fee calculation from what was authorized by the agreements

and from what was disclosed to the investors in the T4 Proxy and the T4 Merger Registration Statement.

B. Defendants Improperly Obtained Payments Purportedly for FF&E

82. In connection with both the T3 and T4 mergers, Defendants directed the creation of and/or approved misleading asset purchase and sale agreements with ARCP pursuant to which ARCP would purportedly purchase from AR Capital furniture, fixtures, and equipment necessary for the T3- and T4-related post-merger operations of ARCP and reimburse AR Capital for certain “unreimbursed expenses” (the “FF&E Agreements”). Each FF&E agreement required ARCP to pay \$5.8 million to AR Capital. Schorsch, on behalf of AR Capital, presented the first agreement, related to the T3 merger, to the ARCP board on December 14, 2012 (“T3 FF&E Agreement”), and the second, related to the T4 merger, to the ARCP board on July 1, 2013 (“T4 FF&E Agreement”).

83. Schorsch approved the \$5.8 million price for each FF&E Agreement and knew or should have known that the \$5.8 million price for each did not reflect the actual items being transferred, the cost of such items, and the actual unreimbursed expenses purportedly being reimbursed by ARCP—if any.

84. By creating and entering into these two FF&E Agreements, Defendants arranged to receive additional cash payments totaling \$11.6 million, and wrongfully obtained at least \$7.27 million dollars in unsupported compensation.

85. The T3 FF&E Agreement was an exhibit to the December 17, 2012 Form 8-K that announced the T3 merger, and the Form 8-K described that under the T3 FF&E Agreement, “concurrently with the closing of the Merger and in connection with the internalization by [ARCP] of certain property level management and accounting activities, [AR Capital] will sell to [ARCP] certain furniture, fixtures, equipment and other assets used by [AR Capital] in

connection with managing the property level business and operations and accounting functions of [T3 and the T3 OP] at the cost of such assets, for an aggregate price of \$5.8 million, which includes the reimbursement of certain costs and expenses incurred by [AR Capital].” The referenced “internalization” related to approximately 8 non-executive employees who would be performing certain property level management and accounting functions for ARCP.

86. The T3 FF&E Agreement included an exhibit of the purported “Purchased Assets and Reimbursed Expenses.” That exhibit listed items such as capitalized furniture, fixtures, and equipment (desks, chairs, computers, software, postage and binding machines), capitalized and other soft costs (such as marketing or software customization), and transaction costs both from the T3 offering and the T3 merger (such as legal, accounting, investor relations, marketing, employee handbooks, and help desk support manuals). No one from AR Capital took any meaningful steps to confirm the accuracy of the Exhibit.

87. Schorsch signed the Form 8-K as well as the T3 FF&E Agreement on behalf of ARCP as its CEO.

88. Similarly, the T4 FF&E Agreement was an exhibit to the July 2, 2013 Form 8-K announcing the T4 merger, and the Form 8-K described that under the T4 FF&E Agreement, “concurrently with the closing of the Merger, [AR Capital] will sell to [ARCP] certain furniture, fixtures, equipment and other assets used by [AR Capital] in connection with managing the property level business and operations and accounting functions of [T4 and the T4 OP], at the cost of such assets, for an aggregate price of \$5.8 million, which includes the reimbursement of certain costs and expenses incurred by [AR Capital].” The T4 FF&E Agreement included a purported “Purchased Assets and Reimbursed Expenses” exhibit that was identical to the exhibit

in the T3 FF&E Agreement. No one from AR Capital took any meaningful steps to confirm the accuracy of the Exhibit.

89. Schorsch signed the Form 8-K as well as the T4 FF&E Agreement on behalf of ARCP as its CEO.

90. The purported “Purchased Assets and Reimbursed Expenses” exhibit appended to the FF&E Agreements listing the purportedly transferred assets and expenses did not accurately reflect the items that AR Capital’s accounting department (at Block’s direction) recorded as being transferred.

91. In the T4 merger, the final schedule allocating the transaction amounts between cost and expense categories in the FF&E Agreement was not completed by AR Capital’s accounting department (at Block’s direction) until approximately six months after AR Capital and Schorsch presented the agreement to ARCP’s board for approval.

92. Moreover, the purportedly unreimbursed expenses were far in excess of actually incurred reimbursable expenses by T3 or T4 or duplicated services that were previously reimbursed. For example, although ARCP purportedly paid AR Capital for items such as “Employee Handbook development and continuous update” and a “Process and Procedures Manual development” in the T3 FF&E Agreement, those same items were again “sold” to ARCP in the T4 FF&E Agreement.

93. Schorsch knew or should have known that he was omitting material information when presenting the T3 and T4 FF&E Agreements to the ARCP board by not informing them that (i) the transaction amounts were determined without regard to the actual cost of the assets purchased or expenses purportedly being reimbursed, and (ii) that no one at AR Capital had taken steps to confirm the accuracy of the exhibits appended to the FF&E agreements. Schorsch

therefore knew or should have known that the T3 and T4 FF&E Agreements would result in false recordings on the books and records of ARCP with respect to the purported assets being transferred and expenses being reimbursed.

94. Because ARCP was externally managed by AR Capital at all relevant times, AR Capital was responsible for making and keeping ARCP's financial books and records. Block, as AR Capital's CFO, knew that AR Capital had proposed the \$5.8 million consideration amounts for the FF&E Agreements without regard to the actual FF&E and actual reimbursable costs or expenses incurred by AR Capital, but nevertheless proceeded to direct AR Capital employees responsible for recording entries on ARCP's books and records to falsely record the transactions in order to conceal that fact. As the CFO of AR Capital, Block's actions and scienter are attributable to AR Capital.

95. For example, a few days after the T3 FF&E Agreement was presented to ARCP's board and received approval, Block and accounting personnel reporting to him exchanged emails to try to identify assets on AR Capital's books that could be recorded as having been transferred to ARCP. Block selected the specific assets to falsely record as transferred—including certain assets that were not actually transferred to ARCP or used by the approximately 8 internalized employees. Other purportedly transferred FF&E assets were items such as improvements to the basement of AR Capital's New York office building that AR Capital continued to own.

96. With respect to the T4 FF&E Agreement, although the agreement was presented and signed on July 1, 2013, Block and the AR Capital accounting staff did not attempt to identify assets to be transferred or expenses to be reimbursed until after the closing of the T4 merger in January 2014. As with T3, Block selected the assets to falsely record as transferred—most of

which did not tie out to the specific items listed in the “Purchased Assets and Reimbursed Expenses” exhibit to the agreement.

FIRST CLAIM FOR RELIEF
Violations of Section 17(a) of the Securities Act
(AR Capital and Block)

97. The Commission realleges and incorporates by reference Paragraphs 1 through 96, above.

98. By engaging in the conduct described above, Defendants AR Capital and Block, with scienter, directly or indirectly, by use of the means or instruments of transportation or communication in interstate commerce, or of the mails, in connection with the offer or sale of securities: (a) employed devices, schemes and artifices to defraud; (b) obtained money or property by means of untrue statements of material fact, or omitted to state material facts necessary in order to make statements made, in light of the circumstances under which they were made, not misleading; and (c) engaged in transactions, acts, practices and courses of business which would operate as a fraud or deceit upon the purchaser.

99. By reason of the acts, omissions, practices, and courses of business set forth in this Complaint, Defendants AR Capital and Block have violated, and, unless restrained and enjoined, will continue to violate, Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)].

SECOND CLAIM FOR RELIEF
Violations of Section 10(b) of the Exchange Act and Rule 10b-5
(AR Capital and Block)

100. The Commission realleges and incorporates by reference Paragraphs 1 through 96, above.

101. By engaging in the conduct described above, Defendants AR Capital and Block, with scienter, directly or indirectly, by the use of any means or instrumentality of interstate

commerce or of the mails, and in connection with the purchase or sale of securities, have:

(a) employed devices, schemes or artifices to defraud; (b) made untrue statements of material fact or one or more omissions of material fact necessary to make the statements made, in light of the circumstances under which they were made, not misleading; and (c) engaged in acts, practices or courses of business which operated or would operate as a fraud or deceit upon any person.

102. By reason of the acts, omissions, practices, and courses of business set forth in this Complaint, Defendants AR Capital and Block have violated, and, unless restrained and enjoined, will continue to violate, Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

THIRD CLAIM FOR RELIEF
Violations of Sections 17(a)(2) and (a)(3) of the Securities Act
(Schorsch)

103. The Commission realleges and incorporates by reference Paragraphs 1 through 96, above.

104. By engaging in the conduct described above, Defendant Schorsch, acting at least negligently, directly or indirectly, by use of the means or instruments of transportation or communication in interstate commerce, or of the mails, in connection with the offer or sale of securities: (i) obtained money or property by means of untrue statements of material fact, or omitted to state material facts necessary in order to make statements made, in light of the circumstances under which they were made, not misleading; and (ii) engaged in transactions, acts, practices and courses of business which would operate as a fraud or deceit upon the purchaser.

105. By reason of the acts, omissions, practices, and courses of business set forth in this Complaint, Defendant Schorsch has violated, and, unless restrained and enjoined, will continue to violate, Sections 17(a)(2) and (a)(3) of the Securities Act [15 U.S.C. § 77q(a)(2) and (a)(3)].

FOURTH CLAIM FOR RELIEF
Violations of Section 13(b)(5) of the Exchange Act
(AR Capital and Block)

106. The Commission realleges and incorporates by reference Paragraphs 1 through 96, above.

107. By engaging in the conduct described above, Defendants AR Capital and Block, knowingly falsified books, records and accounts of ARCP that were subject to Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)].

108. As a result, Defendants AR Capital and Block have violated, and, unless restrained and enjoined, will continue to violate, Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78m(b)(2)(5)].

FIFTH CLAIM FOR RELIEF
Violations of Exchange Act Rule 13b2-1
(All Defendants)

109. The Commission realleges and incorporates by reference Paragraphs 1 through 96, above.

110. By engaging in the conduct described above, Defendants AR Capital, Block, and Schorsch, directly or indirectly, falsified or caused to be falsified, books, records and accounts of ARCP that were subject to Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)].

111. As a result, Defendants AR Capital, Block, and Schorsch have violated, and, unless restrained and enjoined, will continue to violate, Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1].

PRAYER FOR RELIEF

WHEREFORE, the Commission respectfully requests that the Court enter a Final Judgment:

I.

Permanently enjoining AR Capital and Block, and each of their agents, servants, employees, attorneys and other persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise from violating Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)].

II.

Permanently enjoining AR Capital and Block, and each of their agents, servants, employees, attorneys and other persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise from violating Section 10(b) of the Exchange Act, [15 U.S.C. §§ 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

III.

Permanently enjoining AR Capital and Block, and each of their agents, servants, employees, attorneys and other persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise from violating Section 13(b)(5) of the Exchange Act, [15 U.S.C. § 78m(b)(5)] and Rule 13b2-1 thereunder [17 C.F.R. § 240.13b2-1].

IV.

Permanently enjoining Schorsch, and each of his agents, servants, employees, attorneys and other persons in active concert or participation with him who receive actual notice of the injunction

by personal service or otherwise from violating Sections 17(a)(2) and (a)(3) of the Securities Act [15 U.S.C. § 77q(a)(2) and (a)(3)].

V.

Permanently enjoining Schorsch, and each of his agents, servants, employees, attorneys and other persons in active concert or participation with him who receive actual notice of the injunction by personal service or otherwise from violating Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1].

VI.

Ordering AR Capital, Schorsch, and Block to disgorge ill-gotten gains received from the conduct alleged in this Complaint and to pay prejudgment interest thereon.

VII.

Ordering AR Capital, Schorsch, and Block to pay civil money penalties pursuant to Section 20(d)(2) of the Securities Act [15 U.S.C. § 77t(d)(2)] and Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)].

VIII.

Granting such other and further relief as this Court deems just and appropriate.

Dated: July 16, 2019
New York, New York

By:

 _____

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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

-- against --

BRIAN S. BLOCK and
LISA PAVELKA MCALISTER,

Defendants.

16 Civ. 7003 ()

ECF Case

COMPLAINT
AND JURY DEMAND

Plaintiff Securities and Exchange Commission (“Commission”), for its Complaint against Defendants Brian S. Block (“Block”) and Lisa Pavelka McAlister (“McAlister”) (together, “Defendants”), alleges:

PRELIMINARY STATEMENT

1. This case concerns a fraudulent scheme in 2014 to manipulate and falsely report a key financial metric at the largest publicly traded net lease real estate investment trust (“REIT”), then known as American Realty Capital Properties Inc. (“ARCP” or the “Company”). Both

Block and McAlister, ARCP's then Chief Financial Officer and Chief Accounting Officer, respectively, played critical roles in orchestrating the scheme.

2. For financial reporting purposes, publicly traded issuers in the United States must follow accounting standards established by the Financial Accounting Standards Board and rules adopted by the Commission, which are commonly known as generally accepted accounting principles, or GAAP. The GAAP metrics used by investors to assess an issuer's performance typically include net income and earnings per share ("EPS"). Like most REITs, however, ARCP had a practice of publicly reporting a non-GAAP financial metric, Adjusted Funds From Operations ("AFFO"), which its management and the market viewed as a key metric of the Company's performance. Many analysts and investors view AFFO as the most useful indicator of the REIT's ongoing performance and ability to pay dividends. AFFO is an "adjusted" version of a standardized metric of REIT operating performance, Funds From Operations ("FFO"), defined by the National Association of Real Estate Investment Trusts ("NAREIT").

3. Before ARCP filed its Form 10-Q for the first quarter of 2014 ("1Q14") on May 8, 2014, senior ARCP accounting personnel raised concerns to ARCP's senior executives, including Block and McAlister, about the method by which ARCP had been calculating AFFO and AFFO per share, and the possibility that ARCP might overstate its AFFO by a material amount for that quarter if the method was incorrect. Notwithstanding those concerns, Block indicated his approval to file as-is. McAlister, despite understanding that the AFFO method was incorrect, did not object. On May 8, 2014, ARCP filed the Form 10-Q and related documents with the AFFO and AFFO per share numbers included as originally calculated.

4. Subsequently, ARCP accounting personnel confirmed internally that ARCP's method for calculating AFFO and AFFO per share (including for 1Q14) had been incorrect, and

that, as a result, ARCP had overstated its 1Q14 AFFO by \$12 million (out of \$147 million), or \$0.03 a share on a per share basis (out of \$0.26). In their respective roles as Chief Financial Officer and Chief Accounting Officer, Block and McAlister were briefed regularly on the AFFO calculation issue. McAlister directly supervised the accounting personnel who conducted this analysis. However, Block and McAlister failed to first grapple with the matter until the evening before ARCP filed its second quarter 2014 (“2Q14”) Form 10-Q and related disclosures.

5. That evening, in a meeting with McAlister and another member of the accounting staff (the “Accountant”), Block devised a scheme to conceal ARCP’s 1Q14 AFFO calculation error and also meet the company’s 2Q14 targeted AFFO per share numbers.

6. The scheme involved adding false amounts or a “plug” to several figures without any basis (the “plugged numbers”) in an internal spreadsheet that the Company used to calculate AFFO and AFFO per share for 2Q14 and for the six-month period from January through June 2014—the first half period (“FH14”). With McAlister and the Accountant in his office, Block fabricated these plugged numbers and typed them into the spreadsheet.

7. By using these plugged numbers, ARCP concealed from investors that it had overstated its AFFO per share for 1Q14 by \$0.03 per share out of \$0.26 per share, overstated its AFFO per share for 2Q14 by \$0.01 per share, and overstated its AFFO per share for FH14 by \$0.03 out of \$0.49.¹ Without these overstatements, ARCP would not have met analyst consensus projections for these periods.

8. On the morning of July 29, 2014, ARCP filed a Form 10-Q, signed by both Block and McAlister, which included the overstated 2Q14 and FH14 total AFFO. The same day,

¹ As is typical when public companies report their earnings, ARCP’s practice was to round up or down to the nearest penny. All per-share amounts referenced in this Complaint are presented on a rounded basis.

ARCP filed a more detailed financial schedule on Form 8-K, and its management conducted an “earnings call” in which it discussed the quarterly and year-to-date results with investors and analysts. These disclosures included the same misleading AFFO information, as well as the misleading per-share AFFO amounts.

9. By virtue of the conduct alleged herein, Defendants Block and McAlister have violated and/or aided and abetted the other Defendant’s and/or ARCP’s violations of, and unless restrained and enjoined, will continue violating, Section 10(b) of the Securities Exchange Act of 1934 (“Exchange Act”), 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5; and Section 13(a) of the Exchange Act, 15 U.S.C. § 78m(a), and Rules 12b-20, 13a-11, and 13a-13 thereunder, 17 C.F.R. §§ 240.12b-20, 240.13a-11 and 240.13a-13. In addition, Defendant Block violated, and unless restrained and enjoined, will continue violating, Rule 13a-14, 17 C.F.R. § 240.13a-14, promulgated under Section 13(a) of the Exchange Act.

NATURE OF THE PROCEEDING AND RELIEF SOUGHT

10. The Commission brings this action pursuant to the authority conferred on it by Sections 21(d)(1), (2), (3), and (5) of the Exchange Act, 15 U.S.C. §§ 78u(d)(1), 78u(d)(2), 78u(d)(3), and 78u(d)(5), seeking a final judgment: (a) permanently restraining and enjoining Block and McAlister from engaging in the acts, practices and courses of business alleged herein; (b) permanently restraining and enjoining Block and McAlister from acting as an officer or director of any issuer that has a class of securities registered under Section 12 of the Exchange Act, 15 U.S.C. § 781, or that is required to file reports pursuant to Section 15(d) of the Exchange Act, 15 U.S.C. § 78o(d); (c) requiring Block and McAlister to disgorge ill-gotten gains and to pay prejudgment interest thereon; and (d) imposing civil money penalties on Block and McAlister pursuant to Section 21(d)(3) of the Exchange Act, 15 U.S.C. § 78u(d)(3).

JURISDICTION AND VENUE

11. This Court has subject matter jurisdiction over this action pursuant to Sections 21(d) and 27 of the Exchange Act, 15 U.S.C. §§ 78u(d) and 78aa.

12. Venue is proper in the Southern District of New York pursuant to Section 27 of the Exchange Act, 15 U.S.C. § 78aa. Defendants, directly or indirectly, have made use of the means or instruments of transportation or communication in interstate commerce, or of the mails, or of a facility of a national securities exchange in connection with the transactions, acts, practices and courses of business alleged in this Complaint. Certain of these transactions, acts, practices and courses of business occurred in the Southern District of New York, including, among other things, Block's preparation of the fraudulent AFFO schedule, and calls between McAlister and ARCP's auditors during which McAlister fraudulently concealed the falsification of the AFFO and AFFO per share figures.

THE DEFENDANTS

13. **Block**, age 44, resides in Hatfield, Pennsylvania. Block served as CFO of ARCP from ARCP's inception in 2010 until his resignation on October 28, 2014. Block is a CPA licensed in Pennsylvania.

14. **McAlister**, age 52, resides in Arlington, Massachusetts. On November 4, 2013, McAlister was appointed Chief Accounting Officer of ARCP. She became an executive officer and Principal Accounting Officer of ARCP on May 29, 2014 and served in these roles until her resignation on October 28, 2014. McAlister is a CPA licensed in New York.

THE RELEVANT ENTITY

15. **American Realty Capital Properties, Inc.** (now known as VEREIT, Inc., but referred to in this Complaint as "**ARCP**" or the "Company"), was at all relevant times a publicly

traded REIT traded on NASDAQ's Global Select Market (ticker: ARCP). ARCP is a Maryland corporation and its headquarters were in New York, New York during the relevant time period. At the time of the scheme alleged in this Complaint, ARCP reported total assets of approximately \$21 billion.

FACTS

AFFO and AFFO Per Share

16. FFO and AFFO are two non-GAAP measures, commonly used by investors to evaluate the performance of REITs, that make certain adjustments to the REIT's GAAP-based net income or loss in order to provide an alternative presentation of its performance.

17. FFO is a standardized measure of REIT operating performance defined by NAREIT as: GAAP net income or loss "excluding gains or losses from sales of property, and adding back real estate depreciation."

18. Although AFFO has no standardized definition, it is typically understood by REIT managers, their investors and market analysts as FFO with further adjustments to exclude certain non-cash income and expense items (*e.g.*, unrealized gains and losses) and certain "special" or "non-routine" expenses (such as merger and acquisition-related expenses) that are expensed-as-incurred under GAAP.

19. REIT investors and analysts typically consider AFFO a measure of "normalized" residual cash flow after eliminating non-cash and non-recurring expenses, and an indicator of a REIT's ability to pay dividends.

20. As reflected in both internal and external communications, at all relevant times, AFFO was the single most important performance metric to ARCP management. ARCP publicly provided earnings guidance in the form of projected full-year AFFO per share and

internally prepared models for forecasting performance and evaluating potential transactions in terms of impact to AFFO per share.

21. ARCP included only FFO and AFFO per-share calculations – not earnings per share – in its earnings releases, financial supplements, and presentations furnished with Forms 8-K that ARCP filed contemporaneously with its Form 10-Q and Form 10-K filings.

22. Annual AFFO per share was one of the performance criteria established in early 2014 to determine ARCP's senior executives' annual bonuses. Block's base salary was \$500,000 per year, plus equity and cash incentive compensation based upon achievement of certain goals labeled "threshold," "target," and "maximum." According to a compensation plan established for senior executives in 2014, among the financial metrics that would be used to determine Block's incentive compensation were AFFO per share goals of \$1.06 per share ("threshold"), \$1.13 per share ("target"), and \$1.16 per share ("maximum").

23. ARCP provided the market a series of projections for 2014 AFFO per share beginning in early 2013, in connection with announcements about quarterly earnings and announced transactions. On October 23, 2013, ARCP updated its fiscal year 2014 per share AFFO projection to a range of \$1.13 to \$1.19. That projection remained unchanged from October 2013 through July 2014, and it was reaffirmed on numerous occasions during that period, including in a February 27, 2014 investor presentation furnished as an exhibit to a Form 8-K.

24. Market analysts also watched ARCP's AFFO results closely, and many included in their reports their predictions of ARCP's quarterly and annual AFFO per share results.

25. Because FFO and AFFO are non-GAAP measures, ARCP was required by Commission regulations to provide a reconciliation of those metrics to the "most directly

comparable GAAP financial measure.” *See* 17 C.F.R. §§ 228, 229, 244 and 249. The most directly comparable GAAP measure to FFO and AFFO is net income. And FFO per share or AFFO per share is most directly comparable to GAAP’s EPS metric.

The Operating Partnership and Non-Controlling Interests

26. ARCP, like many REITs, conducts substantially all of its business activities through an operating partnership (the “OP”). At all relevant times, ARCP was the sole general partner of the OP and owned in excess of 95% of its equity interests (the “OP units”). The remainder OP units (*i.e.*, those not owned by ARCP) were held by certain affiliated and unaffiliated investors and could be redeemed for a corresponding number of ARCP shares (or cash, at ARCP’s election) after a one-year holding period.

27. Under GAAP, these remainder OP units are deemed non-controlling interests (“NCI”). GAAP requires the consolidated income statement of ARCP to present net income or loss on a consolidated basis, as well as to identify separately the net income or loss attributable to the Company and to the NCI. As such, ARCP reported both forms of its net loss: one that included the total operations of ARCP and the OP, without eliminating the portion of the consolidated net loss that was attributable to the NCI interests (identified simply as “net loss”), and one that eliminated from the net loss the portion of the consolidated net loss that was attributable to the NCI interests (identified as “net loss attributable to the Company”).

28. Similarly, FFO and AFFO may be presented on a basis that includes NCI and reconciles to consolidated net income or loss, or on a basis that excludes NCI and reconciles to net income or loss attributable to the Company. If it reconciles to consolidated net loss, the adjustments made to calculate FFO and AFFO should be of the gross reported amounts of the adjustment items added back. To properly calculate FFO and AFFO per share under this method, the share count divisor would include the shares into which the NCI holders OP units

can be converted (“the NCI shares”). This Complaint refers to this method, which essentially gives credit for 100% of the results and shares of the OP, as the “gross method.” If the Company reconciles to “net loss attributable to the Company,” the adjustments made to calculate FFO and AFFO should be adjusted by only the Company’s portion of the applicable adjustment items added back, excluding that portion of the adjustment items that is attributable to NCI. To properly calculate FFO and AFFO per share under this method, the share count divisor would exclude the NCI shares. This Complaint refers to this method as the “net method.” Both methods are internally consistent and both should produce virtually the same FFO or AFFO per share if properly calculated.

29. Prior to 2Q14, ARCP represented that it was presenting FFO and AFFO on a “net” basis. However, as described in this Complaint, for its 1Q14 Form 10-Q, ARCP instead used an improper hybrid method to calculate AFFO and AFFO per share that overstated its results.

ARCP’s Improper Hybrid Method of Calculating AFFO in First Quarter 2014

30. On May 8, 2014, ARCP reported a net loss attributable to the Company of approximately \$332 million, total FFO of negative \$184 million, and total AFFO of approximately \$147 million (positive) for 1Q14 in its Form 10-Q, and reported AFFO per share of \$0.26 in a variety of related supplemental earnings materials furnished as exhibits to Forms 8-K filed on the same date.

31. In announcing the results, ARCP affirmed that it was maintaining its earnings guidance for 2014 of an AFFO per share range of \$1.13 to \$1.19 and stated that the reported AFFO per share of \$0.26 for the quarter was “in line with management estimates.”

32. In its Form 10-Q for 1Q14 and related supplemental earnings materials, ARCP purported to report FFO in accordance with NAREIT’s definition and to report both FFO and

AFFO on a “net” basis, as it had in prior reports since at least its Form 10-K for the year ended December 31, 2012 (“FY12”). Specifically, ARCP’s reports reconciled FFO and AFFO to “net loss attributable to the Company” and its Form 10-Q and 10-K further represented that the “[a]mounts are presented net of any non-controlling interest effect where applicable.”

33. As explained above, under the “net method,” the FFO and AFFO calculations begin with net income or loss attributable to the Company (*i.e.*, **excluding** amounts attributable to NCI holders), adjust or “add back” only the Company’s portion of the applicable line items, and the result is divided by a share number that **excludes** the NCI shares. In contrast, under the “gross method,” the FFO and AFFO calculations start with net income or loss attributable to both the Company and the NCI holders on a consolidated basis, and then adjust or “add back” the gross amounts of the applicable line items, and the result is divided by a share number that **includes** the NCI shares.

34. However, despite representing that it was reporting FFO and AFFO on a “net” basis, ARCP in 1Q14 and prior periods followed neither the “net method” nor “gross method.” Instead, ARCP improperly used elements of both methods in its annual and quarterly reports from at least the first quarter of 2013 through 1Q14: ARCP began the calculation with the net loss attributable to the Company (*i.e.*, a loss that was smaller than the consolidated net loss), made adjustments (most of which were positive) using the gross amounts of the applicable items (*i.e.*, both the Company’s portion **and** the NCI holders’ portion of these items, rather than only the Company’s portion, resulting in an increase in the total dollar amount of those adjustments and, in turn, an increase in positive AFFO), and divided by a share count that excluded the NCI shares (*i.e.*, a lower share count, resulting in greater AFFO per share). This Complaint refers to this method, which ARCP used in 1Q14 and prior periods, as the “improper hybrid method.”

35. ARCP's AFFO using the "net method" correctly would have been approximately \$135.8 million in total and \$0.23 per share for 1Q14. ARCP's improper hybrid method calculation thus overstated 1Q14 AFFO by approximately \$12 million in total and \$0.03 per share.

Block and McAlister Ignored Concerns Raised About the Improper Hybrid Method

36. Shortly before the 1Q14 Form 10-Q was filed, senior ARCP accounting personnel, including the Accountant, raised concerns about ARCP's method of calculating AFFO to Block, McAlister, and other senior executives. Despite those concerns, Block instructed that they file the Form 10-Q as-is. McAlister understood that ARCP's method of calculating AFFO was incorrect, but she took no action to prevent the filing. As a result, ARCP's Form 10-Q and related earnings materials were filed with the improper hybrid method calculation. Neither Block nor McAlister took steps to inform the Board of Directors, the Audit Committee, or the external auditors of the error or the concerns raised to them by ARCP's senior accounting personnel.

37. Having previously raised the issue in early May 2014 before the 1Q14 Form 10-Q was filed, the Accountant again analyzed ARCP's 1Q14 AFFO calculation, compared it to the proper "net method" calculation, and repeatedly advised Block, McAlister and others that he believed ARCP had made a mistake in its 1Q14 AFFO calculation, and thus, had reported incorrect results.

38. For example, by no later than May 23, 2014, the Accountant had informed McAlister that he believed the 1Q14 AFFO results, using either a calculation under the "net method" or the "gross method," should have been \$0.23 per share, rather than the \$0.26 per share ARCP reported.

39. McAlister participated in numerous meetings and conference calls with the Accountant and other ARCP employees concerning the AFFO calculation issue in May 2014 through July 2014. Block also participated in several of these meetings and calls during which the issue was discussed. McAlister also received, and in at least one case sent to Block, spreadsheets prepared by the Accountant that illustrated the \$0.03 difference between the as-reported and properly calculated 1Q14 AFFO per share.

Block and McAlister Knowingly Permitted ARCP's Audit Committee to Approve a Version of the 2Q14 Form 10-Q That Incorporated the Incorrect 1Q14 AFFO

40. For both quarterly filing and revenue-projection purposes, ARCP employees worked on various AFFO schedules throughout July in anticipation of reporting results for 2Q14 before market-open on July 29, 2014. Block and McAlister requested and received many of these schedules.

41. Block and McAlister were aware that, although the 1Q14 AFFO calculation would not explicitly appear in the 2Q14 Form 10-Q, ARCP would need to report not only the 3-month 2Q14 AFFO results, but also its AFFO results for the first half of the year (FH14) in the Form 10-Q. In order accurately to report the FH14 AFFO results, ARCP would have to add the first and second quarter amounts for each line in the calculation. Block and McAlister understood that if ARCP used the original, as-reported 1Q14 amounts, its FH14 results would be overstated.

42. Although both Block and McAlister were aware that a 2Q14 Form 10-Q that incorporated the reported AFFO amounts in ARCP's 1Q14 filing would overstate ARCP's FH14 AFFO results, neither instructed the ARCP accounting staff to correct the improperly-calculated 1Q14 AFFO amounts when preparing the 2Q14 Form 10-Q and related disclosures.

43. Block and McAlister also were aware that ARCP would report AFFO for both 1Q14 and 2Q14 in a document titled "Quarterly Supplemental Information," to be furnished on Form 8-K the same day ARCP filed the Form 10-Q.

44. Throughout June and July, McAlister and other ARCP senior managers tracked analysts' estimates of ARCP's second quarter AFFO per share.

45. Throughout most of July, McAlister worked with ARCP's accounting staff to identify a number of accounting reclassifications and adjustments they could use to help ARCP report AFFO results that were consistent with analysts' consensus AFFO estimates for 2Q14.

46. ARCP was scheduled to file its 2Q14 Form 10-Q, and make its related disclosures, before market-open on the morning of July 29, 2014.

47. Block and McAlister authorized the Accountant to circulate a draft of the Form 10-Q to ARCP's Audit Committee on July 24, 2014. The FH14 AFFO calculation in that document incorporated results for the first quarter that were calculated using the improper hybrid method, and the 2Q14 AFFO amounts were calculated using the correct "net method," creating an improperly inflated FH14 AFFO. Block and McAlister both received copies of the email circulating the draft, and they participated in the July 25, 2014 meeting with the Audit Committee to discuss the filing and other matters.

48. Although Block and McAlister understood that the AFFO schedule contained incorrectly calculated AFFO amounts from 1Q14 in reporting the FH14 AFFO results, neither Block nor McAlister informed the Audit Committee of the error or of any plans to change the AFFO schedule in the 2Q14 Form 10-Q before it was filed.

49. Having received no instruction from Block or McAlister to correct the previously reported 1Q14 AFFO amounts, on July 27, 2014, the Accountant sent Block, copying McAlister,

an AFFO schedule in which he noted in the cover email that “we are using Q1 as reported” to calculate ARCP’s FH14 (year-to-date) amounts. The Accountant suggested scheduling a call to discuss the schedule later that day. The schedule, like the draft Form 10-Q circulated to the Audit Committee, included the reported improper hybrid method amounts, and the 2Q14 AFFO amounts calculated using the correct “net method,” creating an improperly inflated FH14 AFFO result. Block and McAlister understood that unless they instructed the Accountant otherwise, the Accountant would use this schedule in the 2Q14 Form 10-Q.

50. Neither Block nor McAlister instructed the Accountant that ARCP should not use the improperly calculated 1Q14 AFFO amounts that had been previously reported.

Block and McAlister Represented to ARCP’s Auditors That They Had No Knowledge of Any Fraud Affecting the Company

51. On the evening of July 28, 2014, the engagement partner responsible for the audit of ARCP’s financial statements informed McAlister that he planned to sign off on ARCP’s 2Q14 Form 10-Q filing upon receipt of a representation letter from its management. He provided a draft letter for their review and signature.

52. McAlister informed Block of this development.

53. Block and McAlister both signed the representation letter.

54. In the letter, Block and McAlister represented, among other things, that they had “no knowledge of fraud or suspected fraud affecting the Company. . . .”

Block Added the Plugged Numbers to the AFFO Schedule

55. Late in the evening of July 28, 2014, McAlister and the Accountant met with Block in his office about ARCP’s AFFO calculation.

56. With McAlister and the Accountant sitting in his office, Block began preparing a spreadsheet in which he calculated AFFO and AFFO per share for 1Q14, 2Q14 and FH14 using

the gross method. Using this method properly, however, would have revealed the 1Q14 AFFO per share overstatement of \$0.03 per share. In addition, a correct calculation of 2Q14 AFFO would have shown that ARCP only achieved \$0.23 per share (versus analysts' consensus expectations of \$0.24) and \$0.46 for FH14 (out of an annual projected AFFO of \$1.13 to \$1.19).

57. Block then made several changes to inflate the figures while knowing that the changes were improper and unsupported. Block added a total of approximately \$13.1 million in unsupported plugged amounts to a certain line item in both the 1Q14 and 2Q14 AFFO calculations, which enabled ARCP to mask the overstatement of ARCP's reported 1Q14 AFFO as well as to meet analysts' consensus estimates for 2Q14 AFFO per share of \$0.24. Block also improperly deducted millions of shares from the weighted shares outstanding for FH14, thereby improperly inflating the FH14 AFFO per share from \$0.46 to \$0.49.

58. After Block entered these figures, Block instructed the Accountant to use the numbers and calculations from the spreadsheet he had just prepared in ARCP's 2Q14 Form 10-Q. McAlister told the Accountant that she would speak with the auditors.

59. At 10:59 p.m., Block sent his spreadsheet of manipulated AFFO calculations to McAlister and the Accountant by email.

60. Block and McAlister knew or were reckless in not knowing that the numbers Block inserted were unsupportable and resulted in an inaccurate AFFO calculation, and that including them in ARCP's 2Q14 Form 10-Q, earnings supplement and other disclosures would render those disclosures materially misleading.

McAlister and Block Misled ARCP's Auditors

61. At 11:20 p.m., McAlister spoke for less than two minutes with the audit manager at ARCP's audit firm. On that call, McAlister indicated that additional changes would be made to the Form 10-Q later that evening, but she did not tell her about Block's insertion of the

plugged numbers into the total AFFO calculation, or raise any concerns about his doing so. The manager later indicated to McAlister by email that the auditors would review the revised filing.

62. At 12:02 a.m. on July 29, 2014, the Accountant sent a slightly revised version of the calculations to Block and McAlister for their signoff. The Accountant's revised version did not remove any of Block's plugged numbers.

63. At 1:19 a.m., an updated draft of the Form 10-Q, containing Block's fabricated AFFO numbers, was emailed to ARCP's auditors, copying McAlister, an in-house attorney, and other ARCP employees. The email included a blacklined version of the Form 10-Q, which reflected that the only changes were to the AFFO table.

64. The manager at ARCP's audit firm did not respond to the email attaching the updated filing, nor did she alert the auditor's engagement partner to the changes.

65. Upon receiving the blackline, the in-house attorney forwarded it to ARCP's General Counsel, who called McAlister seeking an explanation of the changes. When he did not promptly receive a telephone call back, the General Counsel emailed McAlister at approximately 3:30 a.m. to ask whether the auditors had signed off on the AFFO calculation.

66. At approximately the same time, McAlister contacted the engagement partner and manager of the audit firm seeking approval to file the Form 10-Q. In neither of these contacts did McAlister mention the AFFO calculation method or the use of plugged numbers. Nor did she give either of the auditors any indication that special attention to the changes was warranted. The engagement partner, who had previously signed off on the filing and had not been alerted to the existence of the changes, texted back his approval.

67. At no point did either Block or McAlister seek to withdraw or modify their prior representation to the auditors that they were aware of no fraud affecting ARCP.

68. At approximately 4:00 a.m., the General Counsel spoke with McAlister by telephone. McAlister told him that the AFFO calculation had changed because ARCP had switched from the net method to the gross method. She did not mention making additional adjustments to any line items; nor did she express confusion or doubt about the accounting. When the General Counsel attempted to probe further, McAlister told him that she had discussed the revisions with the auditors and had obtained their signoff on the change in methodology.

ARCP's Materially Misleading 2Q14 Form 10-Q and Related Disclosures

69. On July 29, 2014, at approximately 6:00 a.m., ARCP filed its 2Q14 Form 10-Q, reporting total AFFO on a purportedly gross method basis for 2Q14 of \$205.3 million and FH14 or YTD AFFO of \$353 million.

70. The amounts previously reviewed and authorized by the Audit Committee, presented on a purportedly net method basis, were \$198.6 million for 1Q14, and \$346.4 million for FH14 AFFO. Neither Block nor McAlister notified the Audit Committee of the changes nor sought its approval before the filing occurred.

71. Block signed the Form 10-Q as ARCP's Principal Financial Officer.

72. McAlister signed the Form 10-Q as ARCP's Principal Accounting Officer.

73. Block also signed a certification, pursuant to Exchange Act Rule 13a-14(a), falsely attesting that, based on his knowledge, the report fairly presented in all material respects the financial condition, results of operations and cash flows of ARCP, and that the report did not "contain any untrue statement of a material fact."

74. In addition, Block signed a certification, pursuant to 18 U.S.C. 1350, and furnished pursuant to Exchange Act Rule 13a-14(b), falsely certifying that "all information contained in [ARCP's Form 10-Q] fairly presents, in all material respects, the financial condition and results of operations of the Company."

75. Later that morning, ARCP filed a related Form 8-K furnishing a press release and supplemental financial presentation, reporting AFFO per share figures of \$0.24 for 2Q14 and \$0.49 for FH14. ARCP's press release highlighted its total reported AFFO and AFFO per share figures and affirmed the prior 2014 guidance range.

76. ARCP also filed a second Form 8-K attaching an investor presentation. This presentation included a slide titled "AFFO Guidance Reconciliation," in which the Company predicted that, based on FH14 AFFO of \$353 million, ARCP expected to earn \$1.14 AFFO per share for the full fiscal year. This amount was within ARCP's previously-stated guidance range of \$1.13 to \$1.19.

77. On July 29, 2014, at 11:00 a.m., ARCP's management conducted a conference call with analysts to discuss the second quarter results. On the call, Block falsely reported 2Q14 AFFO per share of \$0.24 and reiterated ARCP's guidance of \$1.13 to \$1.19 for the year.

78. As a result of Block's and McAlister's fraudulent actions, ARCP publicly overstated its total AFFO by approximately \$1.6 million for 2Q14 and \$13.6 million for FH14. These amounts were material to investors.

79. As a result of Block's and McAlister's fraudulent actions, ARCP publicly overstated its AFFO per share by \$0.01 for 2Q14 and \$0.03 for FH14. These amounts were material to investors.

80. As a result of Block's and McAlister's fraudulent actions, ARCP failed to disclose the fact that it had overstated AFFO—its most important financial metric—when it reported its financial results for the previous quarter, 1Q14, and affirmatively misrepresented its FH14 AFFO per share results. This fact was material to investors.

81. Block and McAlister knew, or were reckless in not knowing, that ARCP improperly overstated its AFFO and AFFO per share for 1Q14, 2Q14 and FH14, which resulted in ARCP filing a materially false and misleading 2Q14 quarterly report with the Commission and making materially misleading statements in its quarterly financial supplement, press release, investor presentation and earnings call.

FIRST CLAIM FOR RELIEF
Violations of Section 10(b) of the Exchange Act and Rule 10b-5
(Both Defendants)

82. The Commission realleges and incorporates by reference Paragraphs 1 through 81, above.

83. By engaging in the conduct described above, Defendants Block and McAlister, with scienter, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, and in connection with the purchase or sale of securities, have:
(a) employed devices, schemes or artifices to defraud; (b) made one or more untrue statements of material fact or one or more omissions of material fact necessary to make the statements made, in light of the circumstances under which they were made, not misleading; and (c) engaged in one or more acts, practices or courses of business which operated or would operate as a fraud or deceit upon any person.

84. By reason of the acts, omissions, practices, and courses of business set forth in this Complaint, Defendants Block and McAlister have violated, and unless restrained and enjoined, will continue to violate, Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5.

SECOND CLAIM FOR RELIEF

**Aiding and Abetting Violations of Section 10(b) of the Exchange Act and Rule 10b-5
(Both Defendants)**

85. The Commission realleges and incorporates by reference Paragraphs 1 through 81, above.

86. By engaging in the conduct described above, Defendants Block and McAlister provided knowing and substantial assistance to the other Defendant and/or ARCP, which, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, and in connection with the purchase or sale of securities, with scienter, has: (a) employed devices, schemes or artifices to defraud; (b) made one or more untrue statements of material fact or one or more omissions of material fact necessary to make the statements made, in light of the circumstances under which they were made, not misleading; and (c) engaged in one or more acts, practices or courses of business which operated or would operate as a fraud or deceit upon any person.

87. By virtue of the foregoing, Defendants Block and McAlister aided and abetted and, unless enjoined, will continue to aid and abet, the other Defendant's and/or ARCP's violations of Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5.

THIRD CLAIM FOR RELIEF

**Aiding and Abetting Violations of Section 13(a) and
Rules 12b-20, 13a-11, and 13a-13
(Both Defendants)**

88. The Commission realleges and incorporates by reference Paragraphs 1 through 81, above.

89. Based on the conduct alleged above, ARCP violated Section 13(a) of the Exchange Act, 15 U.S.C. § 78m(a), and Rules 12b-20, 13a-11 and 13a-13 promulgated

thereunder, 17 C.F.R. §§ 240.12b-20, 240.13a-11, 240.13a-13, which require issuers of registered securities to file quarterly and current reports with the Commission that, among other things, do not contain untrue statements of material fact or omit to state material information necessary in order to make the required statements, in the light of the circumstances under which they are made, not misleading.

90. By engaging in the conduct alleged above, Defendants Block and McAlister provided knowing and substantial assistance to ARCP's filing of materially false and misleading filings with the Commission.

91. By virtue of the foregoing, Defendants Block and McAlister aided and abetted and, unless enjoined, will continue to aid and abet, ARCP's violations of Section 13(a) of the Exchange Act, 15 U.S.C. § 78m(a), and Rules 12b-20, 13a-11 and 13a-13 thereunder, 17 C.F.R. §§ 240.12b-20, 240.13a-11 and 240.13a-13.

FOURTH CLAIM FOR RELIEF
Violation of Rule 13a-14
(Block)

92. The Commission realleges and incorporates by reference Paragraphs 1 through 81, above.

93. Exchange Act Rule 13a-14, 17 C.F.R. § 240.13a-14, requires each principal executive officer and each principal financial officer of an issuer to include certain certifications on, among other things, quarterly reports filed on Form 10-Q. The certifications include, but are not limited to, that the report does not contain any untrue statements of material fact, or omit material facts necessary to make statements made therein not misleading, and that the report fairly presents in all material respects the financial condition, results of operations and cash flows of the registrant.

94. Block was ARCP's "principal financial officer" as that term is used in Rule 13a-14.

95. Block certified that ARCP's Form 10-Q for the reporting period ending June 30, 2014, did not contain any untrue statements of material fact, or omit material facts necessary to make statements therein not misleading, when, as he knew, the filing materially overstated ARCP's AFFO.

96. Block certified that ARCP's Form 10-Q for the reporting period ending June 30, 2014, fairly presented in all material respects the financial condition, results of operations and cash flows of ARCP, when, as he knew, the filing materially overstated ARCP's AFFO.

97. By virtue of the foregoing, Defendant Block violated Rule 13a-14, 17 C.F.R. § 240.13a-14, promulgated under Section 13(a) of the Exchange Act, 15 U.S.C. § 78m(a).

PRAYER FOR RELIEF

WHEREFORE, the Commission respectfully requests that the Court enter a Final Judgment:

I.

Permanently enjoining Block and McAlister, and each of their agents, servants, employees, attorneys and other persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise from violating Section 10(b) of the Exchange Act, 15 U.S.C. §§ 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5.

II.

Permanently enjoining Block and McAlister, and each of their agents, servants, employees, attorneys and other persons in active concert or participation with them who receive actual notice of the injunction by personal service or otherwise from violating Section 13(a) of the Exchange Act, 15 U.S.C. § 78m(a), and Rules 12b-20, 13a-1 and 13a-13 thereunder, 17 C.F.R. §§ 240.12b-20,

240.13a-1 and 240.13a-13 and, in the case of Block, Rule 13a-14 thereunder, 17 C.F.R.

§§ 240.13a-14.

III.

Ordering Block and McAlister to disgorge any ill-gotten gains received from the conduct alleged in this Complaint and to pay prejudgment interest thereon.

IV.

Ordering Block and McAlister to pay civil money penalties pursuant to Section 21(d)(3) of the Exchange Act, 15 U.S.C. § 78u(d)(3).

V.

Permanently barring Block and McAlister, pursuant to Section 21(d)(2) of the Exchange Act, 15 U.S.C. § 78u(d)(2), from acting as an officer or director of any issuer that has a class of securities registered under Section 12 of the Exchange Act, 15 U.S.C. § 781 or that is required to file reports pursuant to Section 15(d) of the Exchange Act, 15 U.S.C. § 78o(d).

VI.

Granting such other and further relief as this Court deems just and appropriate.

JURY DEMAND

Pursuant to Rule 38 of the Federal Rules of Civil Procedure, the Commission demands trial by jury in this action as to all issues so triable.

Dated: September 8, 2016
New York, New York

By: Sanjay Wadhwa
Sanjay Wadhwa
Wendy B. Tepperman
Nancy A. Brown
Karen E. Willenken
Victor Suthammanont
Attorneys for the Plaintiff
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USDC SDNY
DOCUMENT
ELECTRONICALLY FILED
DOC #:
DATE FILED: 2/08/2018

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

-- against --

**BRIAN S. BLOCK and
LISA PAVELKA MCALISTER,**

Defendants.

16 Civ. 7003 (LGS)

ECF Case

**FINAL JUDGMENT
AS TO DEFENDANT BRIAN S. BLOCK**

The Securities and Exchange Commission (“Commission”) having filed a Complaint and Defendant Brian S. Block having entered a general appearance; consented to the Court’s jurisdiction over Defendant and the subject matter of this action; consented to entry of this Final Judgment; waived findings of fact and conclusions of law; and waived any right to appeal from this Final Judgment:

I.

IT IS HEREBY ORDERED, ADJUDGED, AND DECREED that Defendant is permanently restrained and enjoined from violating, directly or indirectly, Section 10(b) of the Securities Exchange Act of 1934 (the “Exchange Act”) [15 U.S.C. § 78j(b)] and Rule 10b-5 promulgated thereunder [17 C.F.R. § 240.10b-5], by using any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange, in connection with the purchase or sale of any security:

- (a) to employ any device, scheme, or artifice to defraud;

- (b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or
- (c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, as provided in Federal Rule of Civil Procedure 65(d)(2), the foregoing paragraph also binds the following who receive actual notice of this Final Judgment by personal service or otherwise: (a) Defendant's officers, agents, servants, employees, and attorneys; and (b) other persons in active concert or participation with Defendant or with anyone described in (a).

II.

IT IS HEREBY FURTHER ORDERED, ADJUDGED, AND DECREED that Defendant is permanently restrained and enjoined from aiding and abetting any violation of Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)], and Rules 12b-20, 13a-11, or 13a-13 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, and 240.13a-13], by knowingly or recklessly providing substantial assistance to an issuer that files with the Commission any report required to be filed with the Commission by or on behalf of an issuer pursuant to Section 13(a) of the Exchange Act and the rules and regulations promulgated thereunder, which contains any untrue statement of material fact; omits to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; omits to disclose any information required to be disclosed; or fails to comply in any material respect with the requirements of Section 13(a) of the Exchange Act and the rules and regulations promulgated thereunder.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, as provided in Federal Rule of Civil Procedure 65(d)(2), the foregoing paragraph also binds the following who receive actual notice of this Final Judgment by personal service or otherwise: (a) Defendant's officers, agents, servants, employees, and attorneys; and (b) other persons in active concert or participation with Defendant or with anyone described in (a).

III.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that Defendant is permanently restrained and enjoined from violating, directly or indirectly, Rule 13a-14 [17 C.F.R. § 13a-14], promulgated under Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)], by making certifications, as a principal executive officer or principal financial officer of an issuer, of reports filed by an issuer on Forms 10-Q, Forms 10-K, Forms 20-F or Forms 40-F under Exchange Act Section 13(a) [15 U.S.C. § 78m(a)], that contain untrue statements of material fact or omit to state material information necessary in order to make the required statements, in light of the circumstances under which they are made, not misleading.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, as provided in Federal Rule of Civil Procedure 65(d)(2), the foregoing paragraph also binds the following who receive actual notice of this Final Judgment by personal service or otherwise: (a) Defendant's officers, agents, servants, employees, and attorneys; and (b) other persons in active concert or participation with Defendant or with anyone described in (a).

IV.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, pursuant to Section 21(d)(2) of the Exchange Act [15 U.S.C. § 78u(d)(2)], Defendant is prohibited from acting as an officer or director of any issuer that has a class of securities registered pursuant to Section 12 of

the Exchange Act [15 U.S.C. § 78l] or that is required to file reports pursuant to Section 15(d) of the Exchange Act [15 U.S.C. § 78o(d)].

V.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that Defendant shall pay a civil penalty in the amount of \$ 160,000 to the Securities and Exchange Commission pursuant to Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)]. Defendant shall make this payment within 14 days after entry of this Final Judgment.

Defendant may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request. Payment may also be made directly from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>. Defendant may also pay by certified check, bank cashier's check, or United States postal money order payable to the Securities and Exchange Commission, which shall be delivered or mailed to

Enterprise Services Center
Accounts Receivable Branch
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

and shall be accompanied by a letter identifying the case title, civil action number, and name of this Court; Brian S. Block as a defendant in this action; and specifying that payment is made pursuant to this Final Judgment.

Defendant shall simultaneously transmit photocopies of evidence of payment and case identifying information to the Commission's counsel in this action. By making this payment, Defendant relinquishes all legal and equitable right, title, and interest in such funds and no part of the funds shall be returned to Defendant. The Commission shall send the funds paid pursuant

to this Final Judgment to the United States Treasury. Defendant shall pay post-judgment interest on any delinquent amounts pursuant to 28 USC § 1961.

VI.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that the Consent is incorporated herein with the same force and effect as if fully set forth herein, and that Defendant shall comply with all of the undertakings and agreements set forth therein.

VII.

IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that, for purposes of exceptions to discharge set forth in Section 523 of the Bankruptcy Code, 11 U.S.C. § 523, the allegations in the complaint are true and admitted by Defendant, and further, any debt for disgorgement, prejudgment interest, civil penalty or other amounts due by Defendant under this Final Judgment or any other judgment, order, consent order, decree or settlement agreement entered in connection with this proceeding, is a debt for the violation by Defendant of the federal securities laws or any regulation or order issued under such laws, as set forth in Section 523(a)(19) of the Bankruptcy Code, 11 U.S.C. § 523(a)(19).

VIII.

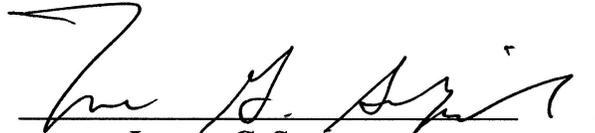
IT IS FURTHER ORDERED, ADJUDGED, AND DECREED that this Court shall retain jurisdiction of this matter for the purposes of enforcing the terms of this Final Judgment.

IX.

There being no just reason for delay, pursuant to Rule 54(b) of the Federal Rules of Civil Procedure, the Clerk is ordered to enter this Final Judgment forthwith and without further notice.

The Clerk of Court is directed to close this case.

Dated: February 8, 2018
New York, New York



LORNA G. SCHOFIELD
UNITED STATES DISTRICT JUDGE

**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK**

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

-- against --

**BRIAN S. BLOCK and
LISA PAVELKA MCALISTER,**

Defendants.

16 Civ. 7003 (LGS)

ECF Case

CONSENT OF DEFENDANT BRIAN S. BLOCK

1. Defendant Brian S. Block (“Defendant”) acknowledges having been served with the complaint in this action, enters a general appearance, and admits the Court’s jurisdiction over Defendant and over the subject matter of this action.

2. Defendant has been convicted after trial of criminal conduct relating to certain matters alleged in the complaint in this action. Specifically, in *United States v. Block*, No. 16 Cr. 595 (S.D.N.Y.) (“*United States v. Block*”), Defendant was convicted of violations of Section 10(b) of the Securities Exchange Act of 1934 (the “Exchange Act”) [15 U.S.C. § 78j(b)] and Rule 10b-5 promulgated thereunder [17 C.F.R. § 240.10b-5], and Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Rules 12b-20, 13a-11, 13a-13 and 13a-14 promulgated thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-11, 240.13a-13, and 240.13a-14], as well as violations of 18 U.S.C. § 371 (conspiracy) and 18 U.S.C. § 1350(c)(1) and (c)(2) (false certification). In connection with that conviction, the jury found the violations reflected in the jury verdict form that is attached as Exhibit A to this Consent. This Consent shall remain in full force and effect regardless of the existence or outcome of any further proceedings in *United States v. Block*.

3. Defendant hereby consents to the entry of the Final Judgment in the form attached hereto (the “Final Judgment”) and incorporated by reference herein, which, among other things:

- a) permanently restrains and enjoins Defendant from (i) violating Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5]; (ii) aiding and abetting Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Rules 12b-20, 13a-11 and 13a-13 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-11 and 240.13a-13]; and (iii) violating Exchange Act Rule 13a-14 [17 C.F.R. § 240.13a-14], promulgated under Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)];
- b) orders Defendant to pay a civil penalty in the amount of \$160,000 under Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)]; and
- c) prohibits Defendant from acting as an officer or director of any issuer that has a class of securities registered pursuant to Section 12 of the Exchange Act [15 U.S.C. § 78l] or that is required to file reports pursuant to Section 15(d) of the Exchange Act [15 U.S.C. § 78o(d)].

4. Defendant agrees that he shall not seek or accept, directly or indirectly, reimbursement or indemnification from any source, including but not limited to payment made pursuant to any insurance policy, with regard to any civil penalty amounts that Defendant pays pursuant to the Final Judgment, regardless of whether such penalty amounts or any part thereof are added to a distribution fund or otherwise used for the benefit of investors. Defendant further agrees that he shall not claim, assert, or apply for a tax deduction or tax credit with regard to any federal, state, or local tax for any penalty amounts that Defendant pays pursuant to the Final

Judgment, regardless of whether such penalty amounts or any part thereof are added to a distribution fund or otherwise used for the benefit of investors.

5. Defendant waives the entry of findings of fact and conclusions of law pursuant to Rule 52 of the Federal Rules of Civil Procedure.

6. Defendant waives the right, if any, to a jury trial and to appeal from the entry of the Final Judgment.

7. Defendant enters into this Consent voluntarily and represents that no threats, offers, promises, or inducements of any kind have been made by the Commission or any member, officer, employee, agent, or representative of the Commission to induce Defendant to enter into this Consent.

8. Defendant agrees that this Consent shall be incorporated into the Final Judgment with the same force and effect as if fully set forth therein.

9. Defendant will not oppose the enforcement of the Final Judgment on the ground, if any exists, that it fails to comply with Rule 65(d) of the Federal Rules of Civil Procedure, and hereby waives any objection based thereon.

10. Defendant waives service of the Final Judgment and agrees that entry of the Final Judgment by the Court and filing with the Clerk of the Court will constitute notice to Defendant of its terms and conditions. Defendant further agrees to provide counsel for the Commission, within thirty days after the Final Judgment is filed with the Clerk of the Court, with an affidavit or declaration stating that Defendant has received and read a copy of the Final Judgment.

11. Consistent with 17 C.F.R. § 202.5(f), this Consent resolves only the claims asserted against Defendant in this civil proceeding. Defendant acknowledges that no promise or representation has been made by the Commission or any member, officer, employee, agent, or

representative of the Commission with regard to any criminal liability that may have arisen or may arise from the facts underlying this action or immunity from any such criminal liability. Defendant waives any claim of Double Jeopardy based upon the settlement of this proceeding, including the imposition of any remedy or civil penalty herein. Defendant further acknowledges that the Court's entry of a permanent injunction may have collateral consequences under federal or state law and the rules and regulations of self-regulatory organizations, licensing boards, and other regulatory organizations. Such collateral consequences include, but are not limited to, a statutory disqualification with respect to membership or participation in, or association with a member of, a self-regulatory organization. This statutory disqualification has consequences that are separate from any sanction imposed in an administrative proceeding. In addition, in any disciplinary proceeding before the Commission based on the entry of the injunction in this action, Defendant understands that he shall not be permitted to contest the factual allegations of the complaint in this action.

12. Defendant understands and agrees to comply with the terms of 17 C.F.R. § 202.5(e), which provides in part that it is the Commission's policy "not to permit a defendant or respondent to consent to a judgment or order that imposes a sanction while denying the allegations in the complaint or order for proceedings." As part of Defendant's agreement to comply with the terms of Section 202.5(e), Defendant acknowledges the criminal conviction for related conduct described in paragraph 2 above, and: (i) will not take any action or make or permit to be made any public statement denying, directly or indirectly, any allegation in the complaint or creating the impression that the complaint is without factual basis; (ii) will not make or permit to be made any public statement to the effect that Defendant does not admit the allegations of the complaint, or that this Consent contains no admission of the allegations;

(iii) upon the filing of this Consent, Defendant hereby withdraws any papers filed in this action to the extent that they deny any allegation in the complaint; and (iv) stipulates for purposes of exceptions to discharge set forth in Section 523 of the Bankruptcy Code, 11 U.S.C. § 523, that the allegations in the complaint are true, and further, that any debt for disgorgement, prejudgment interest, civil penalty or other amounts due by Defendant under this Final Judgment or any other judgment, order, consent order, decree or settlement agreement entered in connection with this proceeding, is a debt for the violation by Defendant of the federal securities laws or any regulation or order issued under such laws, as set forth in Section 523(a)(19) of the Bankruptcy Code, 11 U.S.C. § 523(a)(19). If Defendant breaches this agreement, the Commission may petition the Court to vacate the Final Judgment and restore this action to its active docket. Nothing in this paragraph affects Defendant's: (i) testimonial obligations; or (ii) right to take legal or factual positions in litigation or other legal proceedings in which the Commission is not a party.

13. Defendant hereby waives any rights under the Equal Access to Justice Act, the Small Business Regulatory Enforcement Fairness Act of 1996, or any other provision of law to seek from the United States, or any agency, or any official of the United States acting in his or her official capacity, directly or indirectly, reimbursement of attorney's fees or other fees, expenses, or costs expended by Defendant to defend against this action. For these purposes, Defendant agrees that Defendant is not the prevailing party in this action since the parties have reached a good faith settlement.

14. Defendant agrees that the Commission may present the Final Judgment to the Court for signature and entry without further notice.

15. Defendant agrees that this Court shall retain jurisdiction over this matter for the purpose of enforcing the terms of the Final Judgment.

Dated: 12/4/2017

Brian S. Block
Brian S. Block

On December 4, 2017, Brian S. Block, a person known to me, personally appeared before me and acknowledged executing the foregoing Consent.

[Signature]
Notary Public
Commission expires 02/19/2018

Approved as to form:
[Signature]

Michael C. Miller
Reid H. Weingarten
Michelle Levin
Michael G. Scavelli
Steptoe & Johnson LLP
1114 Avenue of the Americas
New York, NY 10036

Attorneys for Defendant

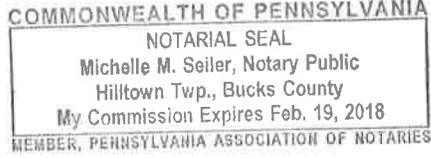


EXHIBIT A

U.S. DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK
ELECTRONICALLY FILED
DOC#:
DATE FILED: 7/18/17

Court
exhibit # 4

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

UNITED STATES OF AMERICA,

-v-

BRIAN BLOCK,

Defendant.

16-CR-595 (JPO)

VERDICT FORM

Count One (Conspiracy)

Guilty Not Guilty

Count Two (Securities Fraud)

Guilty Not Guilty

Count Three (False Statements in Filings with the SEC – Second Quarter 10Q)

Guilty Not Guilty

Count Four (False Statements in Filings with the SEC – Second Quarter 8K)

Guilty Not Guilty

Count Five (False Certification of Disclosure Filed with the SEC)

Guilty Not Guilty

Count Six (False Section 1350 Certification Filed with the SEC)

Guilty Not Guilty

If and only if you find the defendant guilty of Count Six, did the defendant act willfully?

Yes No

06/30/17
Date

GREG ROBSTAD 
Foreperson

AN OVERVIEW OF THE REGULATION BEST INTEREST RULE PACKAGE

Christine Lazaro

On June 5, 2019, the SEC adopted the Regulation Best Interest Rule Package. The package consists of (I) Regulation Best Interest: The Broker-Dealer Standard of Conduct;¹ (II) Form CRS Relationship Summary and Amendments to Form ADV;² (III) the SEC Interpretation Regarding Standard of Conduct for Investment Advisers;³ and (IV) the SEC Interpretation Regarding the “Solely Incidental” Prong of the Broker-Dealer Exclusion from the Definition of Investment Adviser.⁴ Each of these four releases is summarized below. Additionally, FINRA has issued its own rules changes in response to the adoption of Regulation Best Interest. FINRA’s changes are also discussed below.

I. Regulation Best Interest

a. General Obligation

Regulation Best Interest requires that brokerage firms and their brokers must act in the best interests of their retail customers when making recommendations of securities or investment strategies.⁵ Put simply, the brokerage firm and the broker may not place their own interests ahead of the customers’ interests.⁶

For purposes of this standard, the term “recommendation” has the same meaning that it currently has under FINRA rules.⁷ It is a fact-based determination. The SEC recognizes that factors to consider are “whether the communication ‘reasonably could be viewed as a ‘call to action’ and ‘reasonably would influence an investor to trade a particular security or group of securities.’”⁸

The SEC provides some guidance as to what would not be considered a recommendation, including communications such as general financial and investment information; descriptive

¹ Regulation Best Interest: The Broker-Dealer Standard of Conduct, 84 Fed. Reg. 33,318 (July 12, 2019) (to be codified at 17 C.F.R. pt. 240).

² Form CRS Relationship Summary; Amendments to Form ADV, 84 Fed. Reg. 33,492 (July 12, 2019) (to be codified at 17 C.F.R. pts. 200, 240, 249, 275, and 279).

³ Commission Interpretation Regarding Standard of Conduct for Investment Advisers, 84 Fe. Reg. 33,669 (July 12, 2019).

⁴ Commission Interpretation Regarding the Solely Incidental Prong of the Broker-Dealer Exclusion From the Definition of Investment Adviser, 84 Fed. Reg. 33,681 (July 12, 2019).

⁵ 17 C.F.R. §240.15l-1(a)(1) (2019).

⁶ *Id.*

⁷ 84 Fed. Reg. 33,318, 33,337.

⁸ *Id.* at 33,335.

information about an employer-sponsored retirement plan; certain asset allocation models; and interactive investment materials.⁹

Recommendations include, for example, advice about the type of securities account to open, as well as advice to roll over or transfer assets from one account to another.¹⁰ Additionally, a broker may be deemed to have made an implicit hold recommendation, triggering the obligations of the Rule, if the broker has agreed to perform periodic account monitoring.¹¹

Brokerage firms and brokers owe this obligation to “retail customers.” The SEC defines retail customer to focus on natural persons and their legal representatives, seeking advice for personal, family, or household purposes.¹²

b. Component Obligations

Regulation Best Interest is comprised of four components: (i) the Disclosure Obligation; (ii) the Care Obligation; (iii) the Conflict of Interest Obligation; and (iv) the Compliance Obligation.¹³

i. Disclosure Obligation

The Disclosure Obligation requires that a broker or brokerage firm make full and fair disclosure in writing of “material facts relating to the scope and terms of the relationship” with the customer; and “material facts relating to such conflicts of interest that are associated with the recommendation.”¹⁴ “Materiality” has the same meaning that the Supreme Court articulated in *Basic v. Levinson*.¹⁵

Material facts related to the scope of the relationship explicitly include the following types of information: (i) the capacity in which the broker is acting (as a broker-dealer or investment adviser); (ii) fees and costs associated with the transactions and the accounts more generally; and (iii) the type and scope of services the brokerage firm will offer, including any limitations on those services.¹⁶

Regardless of whether the firm and individual are dually-registered, both still have to disclose the capacity in which they are acting. If the firm or individual is not dually-registered but uses the term “advisor” or “adviser”, they will likely be in violation of this obligation because their disclosure about capacity will not be accurate.¹⁷

⁹ *Id.* at 33,337 – 33,338.

¹⁰ *Id.* at 33,338.

¹¹ *Id.* at 33,340.

¹² *Id.* at 33,343.

¹³ 17 C.F.R. §240.15l-1(a)(2) (2019).

¹⁴ 84 Fed. Reg. at 33,347.

¹⁵ *Id.* See also *Basic, Inc. v. Levinson*, 485 U.S. 224 (1988).

¹⁶ 84 Fed. Reg. at 33,349.

With respect to fees and costs, the SEC expects that brokerage firms will build on the disclosure of fees and costs that are set forth in Form CRS (to be discussed in further detail below).¹⁸ The obligation does not require that the brokerage firm provide “individualized” costs and fees, but rather may provide standardized or hypothetical amounts or percentage ranges.¹⁹ Brokerage firms may also satisfy this part of their disclosure obligations by providing mandated disclosure documents, such as prospectuses, and trade confirmations.²⁰

With respect to the type of services the brokerage firm offers, the firm must disclose whether it monitors transactions and strategies.²¹ As part of this disclosure, the brokerage firm must be specific as to the frequency and duration of the services offered.²² The brokerage firm may rely on information disclosed in the Form CRS (as will be discussed below), but it will likely need to expand on that information to meet this disclosure obligation.²³ However, the brokerage firm may rely on other documents, including account agreements, to make these disclosures.²⁴ As part of this disclosure, brokerage firms must also disclose whether they require any account balance minimums.²⁵

The brokerage firm must also disclose any limitations on its offerings.²⁶ Limitations include for example, if the brokerage firm only offers proprietary products.²⁷ Additionally, if the brokerage firm is dually registered but the broker is not, the broker must disclose that he cannot offer advisory services.²⁸

The conflicts of interest disclosure obligation should summarize how the brokerage firm and the brokers are compensated for their recommendations as well as the conflicts that the compensation arrangements create.²⁹ These conflicts need not be disclosed on a recommendation by recommendation basis.³⁰

¹⁷ *Id.* at 33,352.

¹⁸ *Id.* at 33,354.

¹⁹ *Id.* at 33,355.

²⁰ *Id.*

²¹ *Id.* at 33,356.

²² *Id.*

²³ *Id.* at 33,357.

²⁴ *Id.*

²⁵ *Id.* at 33,358.

²⁶ *Id.* at 33,357.

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.* at 33,363.

While the disclosure obligation requires that the disclosures be made in writing, the SEC recognizes that it may be necessary to supplement, clarify, or update written disclosures with oral disclosures.³¹ If the brokerage firm does supplement the written disclosures, however, the brokerage firm must keep a record of the fact that an oral disclosure was provided.³²

ii. Care Obligation

The Care Obligation, in many ways, mirrors the FINRA Suitability Rule. It requires that the broker, when making a recommendation, exercise “reasonable diligence, care, and skill to:”

- (A) Understand the potential risks, rewards, and costs associated with the recommendation, and have a reasonable basis to believe that the recommendation could be in the best interest of at least some retail customers;
- (B) Have a reasonable basis to believe that the recommendation is in the best interest of a particular retail customer based on that retail customer’s investment profile and the potential risks, rewards, and costs associated with the recommendation and does not place the financial or other interest of the broker, dealer, or such natural person ahead of the interest of the retail customer; and
- (C) Have a reasonable basis to believe that a series of recommended transactions, even if in the retail customer’s best interest when viewed in isolation, is not excessive and is in the retail customer’s best interest when taken together in light of the retail customer’s investment profile and does not place the financial or other interest of the broker, dealer, or such natural person making the series of recommendations ahead of the interest of the retail customer.³³

The first prong is similar to the “reasonable basis” obligation under the FINRA Suitability Rule.³⁴ As a threshold issue, the broker must understand the security or investment strategy recommended before being capable of determining whether the recommendation is in the best interest of a particular customer.³⁵ The SEC sets forth factors that the broker or brokerage firm should consider when investigating the security or investment strategy: “the security’s or investment strategy’s investment objectives, characteristics (including any special or unusual features), liquidity, volatility, and likely performance in a variety of market and economic conditions; the expected return of the security or investment strategy; as well as any financial incentives to recommend the security or investment strategy.”³⁶

³⁰ *Id.*

³¹ *Id.* at 33,368.

³² *Id.*

³³ 17 C.F.R. §240.15l-1(a)(2)(ii) (2019).

³⁴ See FINRA Rule 2111.05(a).

³⁵ 84 Fed. Reg. at 33,375 – 33,376.

³⁶ *Id.* at 33,376.

The SEC has included “costs” as a factor in evaluating securities or strategies because it recognizes that cost will always be a relevant factor.³⁷ “Costs” includes both costs associated with purchasing a security, as well as future costs associated with exchanging or selling a security.³⁸ However, the SEC cautions that cost is not a dispositive factor. The Rule does not require that a broker recommend the lowest cost option.³⁹

The second prong incorporates the “customer specific” prong of the FINRA Suitability Rule,⁴⁰ but enhances it by replacing “suitable” with a best interest standard.⁴¹ In sum, the broker must determine that a recommendation is in the customer’s best interest based on that customer’s investment profile. The customer’s investment profile includes “age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, risk tolerance,” and any other information that may be disclosed.⁴² This is the same information that firms must currently consider as part of the investor’s profile under the FINRA Suitability Rule.⁴³ If a customer does not provide the information, the SEC cautions that a firm may not have sufficient information to make a best interest determination.⁴⁴

In evaluating whether a recommendation is in the customer’s best interest, the broker should consider reasonably available alternatives offered by the broker’s firm.⁴⁵ The broker need not recommend the “best” of all possible alternatives.⁴⁶ The Rule also does not require that the broker be familiar with every product available by the brokerage firm.⁴⁷ The scope of the reasonably available alternatives that are considered with respect to any particular recommendation will depend on several factors, including, the broker’s customer base; the products available to the broker to recommend; and specific limitations on the available products, including that products may only be available in certain geographical locations or to particular types of accounts.⁴⁸

For dually registered brokers, the options with respect to account type must be considered as reasonably available alternatives.⁴⁹ If the broker may only offer brokerage accounts, the broker

³⁷ *Id.* at 33,373.

³⁸ *Id.*

³⁹ *Id.*

⁴⁰ See FINRA Rule 2111.05(b).

⁴¹ 84 Fed. Reg. at 33,377.

⁴² 17 C.F.R. §240.15l-1(b)(3) (2019).

⁴³ See FINRA Rule 2111(a).

⁴⁴ 84 Fed. Reg. at 33,379.

⁴⁵ *Id.* at 33,381.

⁴⁶ *Id.*

⁴⁷ *Id.*

⁴⁸ *Id.* at 33,382.

must consider the customer's objectives before recommending a brokerage account.⁵⁰ For example, if the customer is requesting that the broker have unlimited discretion, a brokerage account would not be appropriate.⁵¹

When recommending a rollover, the broker must consider a number of factors, including, "fees and expenses; level of service available; available investment options; ability to take penalty-free withdrawals; application of required minimum distributions; protection from creditors and legal judgments; holdings of employer stock; and any special features of the existing account."⁵² A broker may not just consider whether the rollover may offer additional options beyond the customer's current plan.

The final component is similar to the "quantitative suitability" requirement,⁵³ except that the "control" element has been eliminated.⁵⁴ This component is intended to prevent trading that is so excessive that a positive return is virtually impossible.⁵⁵

iii. Conflict of Interest Obligation

The Conflict of Interest Obligation requires a firm to adopt policies and procedures designed to identify and, at a minimum, disclose all conflicts associated with a recommendation.⁵⁶ The obligation further requires that a brokerage firm mitigate or eliminate certain types of conflicts.⁵⁷

With respect to the content of the policies and procedures, the SEC contemplates that brokerage firms will have the flexibility to design policies and procedures that are risk-based rather than requiring a detailed review of each recommendation.⁵⁸ The SEC suggests certain components that a brokerage firm should consider when adopting policies and procedures including:

[P]olicies and procedures outlining how the firm identifies conflicts, identifying such conflicts and specifying how the broker-dealer intends to address each conflict; robust compliance and monitoring systems; processes to escalate identified instances of noncompliance for remediation; procedures that designate responsibility to business line personnel for supervision of functions and persons, including determination of compensation; processes for escalating conflicts of

⁴⁹ *Id.* at 33,383.

⁵⁰ *Id.*

⁵¹ *Id.*

⁵² *Id.*

⁵³ See FINRA Rule 2111.05(c).

⁵⁴ 84 Fed. Reg. at 33,384.

⁵⁵ *Id.*

⁵⁶ *Id.* at 33,385.

⁵⁷ *Id.*

⁵⁸ *Id.* at 33,386.

interest; processes for periodic review and testing of the adequacy and effectiveness of policies and procedures; and training on policies and procedures.⁵⁹

Under this obligation, the brokerage firm has a duty to, at a minimum, disclose all conflicts of interest.⁶⁰ Disclosure must be full and fair; if it is not possible to fully and fairly disclose a conflict, it must be mitigated such that full and fair disclosure is possible.⁶¹

Brokerage firms also have a duty to identify and mitigate conflicts of interest that create an incentive for the broker to place the interests of the broker or the firm ahead of the interests of the customer.⁶² The SEC has primarily chosen to limit the duty to mitigate to broker-level conflicts, allowing the brokerage firms to generally deal with firm-level conflicts through disclosure.⁶³ The requirement to identify and mitigate broker-level conflicts applies only to incentives provided to the broker, either by the firm or third parties that are within the control of or associated with the firm.⁶⁴ Accordingly, the requirement does not create an obligation with respect to private securities transactions.⁶⁵ The SEC does provide examples of conflicts that must be mitigated: (i) compensation from the brokerage firm or third parties, including fees and other charges associated with the service or recommendation provided; (ii) employment incentives, including those tied to asset accumulation, special awards, variable compensation, and compensation tied to performance reviews; and (iii) commissions, sales charges, or other fees whether paid by the customer, the brokerage firm, or a third party.⁶⁶

Mitigation measures should be based on the nature and significance of the incentive, as well as other factors related to the brokerage firm's business model, such as the size of the firm, the types of customers, and the complexity of the security product or strategy.⁶⁷

The SEC provides a list of best practices for brokerage firms developing policies and procedures for mitigation methods:

- Avoiding compensation thresholds that disproportionately increase compensation through incremental increases in sales;
- Minimizing compensation incentives for employees to favor one type of account over another; or to favor one type of product over another, proprietary or preferred provider

⁵⁹ *Id.* at note 688.

⁶⁰ *Id.* at 33,388.

⁶¹ *Id.*

⁶² *Id.* at 33,390.

⁶³ *Id.*

⁶⁴ *Id.* at 33,391.

⁶⁵ *Id.* at note 744.

⁶⁶ *Id.* at 33,391.

⁶⁷ *Id.*

products, or comparable products sold on a principal basis, for example, by establishing differential compensation based on neutral factors;

- Eliminating compensation incentives within comparable product lines by, for example, capping the credit that an associated person may receive across mutual funds or other comparable products across providers;
- Implementing supervisory procedures to monitor recommendations that: are near compensation thresholds; are near thresholds for firm recognition; involve higher compensating products, proprietary products or transactions in a principal capacity; or, involve the roll over or transfer of assets from one type of account to another (such as recommendations to roll over or transfer assets in an ERISA account to an IRA) or from one product class to another;
- Adjusting compensation for brokers who fail to adequately manage conflicts of interest; and
- Limiting the types of retail customer to whom a product, transaction or strategy may be recommended.⁶⁸

If a brokerage firm materially limits its securities offerings or investment strategies, the brokerage firm must prevent such limitations from causing the firm to put its interests ahead of the customers'.⁶⁹ The SEC considers that recommending only proprietary products, products with revenue sharing arrangements, or a specific asset class would be material limitations.⁷⁰ The SEC recommends that brokerage firms offering limited menus consider establishing a "product review process" that includes evaluating the use of preferred lists; restrictions on the customers to whom a product may be sold; requiring brokers selling certain products to have minimum knowledge requirements; as well as period product reviews to further evaluate conflicts.⁷¹

Certain practices are completely prohibited pursuant to this obligation. For example, brokerage firms must eliminate "sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific securities or specific types of securities within a limited time."⁷² Non-cash compensation includes merchandise, gifts and prizes, travel expenses, meals and lodging.⁷³ This obligation is not intended to eliminate all incentives, only those that create high-pressure situations to sell specific securities within a limited period of time.⁷⁴ It likely will not capture contests or other incentives tied to total products sold or asset accumulation and growth.⁷⁵

⁶⁸ *Id.* at 33,392.

⁶⁹ *Id.* at 33,393.

⁷⁰ *Id.*

⁷¹ *Id.* at 33,394.

⁷² 17 C.F.R. §240.15l-1(a)(2)(iii)(D) (2019).

⁷³ 84 Fed. Reg. at 33,396.

⁷⁴ *Id.*

Brokerage firms may also continue to hold annual conferences, so long as attendance is not premised on the sale of specific securities within a limited period of time.⁷⁶

iv. Compliance Obligation

The Compliance Obligation is an overarching requirement to adopt policies and procedures that are reasonably designed to achieve compliance with the Rule as a whole.⁷⁷ The Rule does not specify which policies and procedures must be adopted. The SEC expects brokerage firms to design policies and procedures that “prevent violations from occurring, detect violations that have occurred, and to correct promptly any violations that have occurred.”⁷⁸ Brokerage firms are expected to tailor their policies and procedures to account for the “scope, size, and risks associated with the operations of the firm and the type of business in which the firm engages.”⁷⁹

II. Form CRS Relationship Summary

In addition to adopting a new standard of conduct for brokers and brokerage firms, the SEC also adopted a new disclosure obligation for both brokerage firms and investment advisers.⁸⁰ The SEC will require that brokerage firms and investment advisers create and deliver a relationship summary to prospective and existing customers. The relationship summary and the firms’ delivery obligations are described in this section.

a. Presentation and Format

The SEC allows firms to use a mix of prescribed wording along with firm-authored wording in drafting the relationship summary.⁸¹ For example, firms will be able to describe their services, investment offerings, fees, and conflicts of interest.⁸² Firms will be required, however, to use prescribed headings, conversation starters, and statement describing their standard of conduct when providing investment advice.⁸³

The SEC requires that headings be in the form of prescribed questions, in a set order.⁸⁴ The relationship summary may not exceed four pages for a dual registrant that includes both its

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ *Id.* at 33,397.

⁷⁸ *Id.*

⁷⁹ *Id.*

⁸⁰ 84 Fed. Reg. 33,492.

⁸¹ *Id.* at 33,502.

⁸² *Id.*

⁸³ *Id.*

⁸⁴ *Id.* at 33,504.

brokerage and advisory services in a single summary.⁸⁵ Otherwise, the relationship summary may not exceed two pages for brokerage firms and investment advisers that are describing one of their services.⁸⁶

The SEC is encouraging the use of graphics to facilitate comprehension, including charts, graphs, tables, text colors, and graphical cues such as dual-column charts.⁸⁷ Additionally, firms may include QR codes and hyperlinks to facilitate layered disclosure.⁸⁸ However, a firm may not satisfy its disclosure obligations of the relationship summary through the use of “incorporation by reference.”⁸⁹

b. Content

i. Introduction

Firms are required to open the relationship summary with a standardized introduction that includes (i) the name of the firm and whether it is a brokerage firm or investment adviser; (ii) a statement that brokerage and advisory services and fees differ; and (iii) a statement that research tools are available at Investor.gov [CRS].⁹⁰

ii. Relationships and Services

Following the introduction, firms must summarize the relationships and services that they offer under the heading, “What investment services and advice can you provide me?”⁹¹ Additionally, firms must include any material limitations on the services that they offer to investors.⁹² In the description of services, firms must address (i) monitoring; (ii) investment authority; (iii) limited investment offerings; and (iv) account minimums and other requirements.⁹³

With respect to monitoring, firms must explain whether they monitor an investor’s accounts, including the frequency of the monitoring and any limitations on the monitoring.⁹⁴ If an investment adviser accepts discretionary authority, the firm must describe how the authority will be exercised.⁹⁵ For example, if the firm requires investor input before exercising discretion in certain

⁸⁵ *Id.* at 33,505.

⁸⁶ *Id.*

⁸⁷ *Id.* at 33,507.

⁸⁸ *Id.*

⁸⁹ *Id.* at 33,508.

⁹⁰ *Id.* at 33,513.

⁹¹ *Id.* at 33,515.

⁹² *Id.* at 33,516.

⁹³ *Id.* at 33,517.

⁹⁴ *Id.* at 33,518.

circumstances, the firm must explain that.⁹⁶ Both investment advisers and brokerage firms that offer non-discretionary services must explain that the investor is the ultimate decision-maker.⁹⁷ If a firm has a limited menu of offerings, such as only proprietary products or a specific asset class, the firm must explain those limitations.⁹⁸ Firms must also disclose whether there are any required minimums to open an account or place a trade, or if there is a tiered fee schedule.⁹⁹

In the relationship and services section of the form, firms must also provide additional information that further explains the firms' services.¹⁰⁰ This section should provide the information about services that would be available in an investment adviser's Form ADV, Part 2A brochure, or that a brokerage firm otherwise has to provide under Reg. BI.¹⁰¹ This section of the disclosure may be layered, providing hyperlinks or other ways of directing the investor to the source of the information.¹⁰²

The relationship and services section will also contain three conversation starters.¹⁰³ The first conversation starter will be tailored to the nature of the firm's business. For firms that are not dual registrants, the firm will include, "Given my financial situation, should I choose a brokerage service? Why or why not?" or "Given my financial situation, should I choose an investment advisory service? Why or why not?"¹⁰⁴ Dual registrants will include, "Given my financial situation, should I choose an investment advisory service? Should I choose a brokerage service? Should I choose both types of services? Why or why not?"¹⁰⁵

Additionally, firms will also include the following two questions: (i) "How will you choose investments to recommend to me?;" and (ii) "What is your relevant experience, including your licenses, education and other qualifications? What do these qualifications mean?"¹⁰⁶

⁹⁵ *Id.* at 33,519.

⁹⁶ *Id.*

⁹⁷ *Id.*

⁹⁸ *Id.* at 33,520.

⁹⁹ *Id.* at 33,521.

¹⁰⁰ *Id.*

¹⁰¹ *Id.*

¹⁰² *Id.*

¹⁰³ *Id.*

¹⁰⁴ *Id.*

¹⁰⁵ *Id.*

¹⁰⁶ *Id.*

iii. Summary of Fees, Costs, Conflicts, and Standards of Conduct

Firms will begin the discussion of fees, costs, conflicts, and standards of conduct with the heading, “What fees will I pay?”¹⁰⁷ In this section, the firm must summarize the principal costs and fees that investors will incur, including how frequently they are assessed and what conflicts of interest the fees may create.¹⁰⁸ Additionally, firms must describe other fees and costs associated with their services or investments, whether paid directly or indirectly.¹⁰⁹ The SEC provides some examples of the other fees and costs that may need to be disclosed, including: custodial fees; account maintenance fees; fees related to mutual funds and variable annuities; distribution fees; platform fees; and shareholder servicing fees.¹¹⁰

Finally, firms are required to include the following statement: “You will pay fees and costs whether you make or lose money on your investments. Fees and costs will reduce any amount of money you make on your investment over time. Please make sure you understand what fees and costs you are paying.”¹¹¹

Firms must also include a conversation starter about fees: “Help me understand how these fees and costs might affect my investments. If I give you \$10,000 to invest, how much will go to fees and costs, and how much will be invested for me?”¹¹²

Following the fees and costs discussion, firms must discuss the standard of conduct that applies, using prescribed language.¹¹³ Additionally, this section must include a summary of certain firm-level conflicts.¹¹⁴

The disclosure that a firm has to make will vary based on whether it is [a broker making a recommendation], [an investment adviser], or [a dual registrant]:

[When we provide you with a recommendation,] [When we act as your investment adviser,] [When we provide you with a recommendation as your broker-dealer or act as your investment adviser,] we have to act in your best interest and not put our interest ahead of yours. At the same time, the way we make money creates some conflicts with your interests. You should understand and ask us about these conflicts because they can affect the [recommendations] [investment advice] [recommendations and investment advice] we provide you. Here are some examples to help you understand what this means.¹¹⁵

¹⁰⁷ *Id.* at 33,524.

¹⁰⁸ *Id.*

¹⁰⁹ *Id.*

¹¹⁰ *Id.*

¹¹¹ *Id.* at 33,527.

¹¹² *Id.* at 33,528.

¹¹³ *Id.* at 33,530.

¹¹⁴ *Id.* at 33,529.

Following the prescribed wording, a firm must summarize the following ways that the firm makes money that involve conflicts: (i) from proprietary products; (ii) from third-party payments; (iii) by revenue sharing; and (iv) by principal trading.¹¹⁶ If the firm does not have any of these conflicts, it must describe one material conflict of interest that will affect retail investors.¹¹⁷

In this section, firms must include the following conversation starter: “How might your conflicts of interest affect me, and how will you address them?”¹¹⁸ Finally, firms must include the heading, “How do your financial professionals make money?” and include a description of how their financial professionals are compensated, including both cash and non-cash compensation, as well as the conflicts that the payments create.¹¹⁹

iv. Disciplinary History

The relationship summary will also include a section about whether the firm or its financial professionals have any disciplinary history, as well as where an investor may find additional information.¹²⁰ This section will begin with the following question: “Do you or your financial professionals have legal or disciplinary history?” Firms will have to answer yes if they have any of a number of disclosable events as set forth in the instructions.¹²¹ For example, firms will have to answer yes if a broker has any items disclosed pursuant to question 14 A through M on the Form U4.¹²²

This section must also include the following conversation starter: “As a financial professional, do you have any disciplinary history? For what type of conduct?”¹²³

v. Additional Information

The final section of the relationship summary will state where the investor can find additional information.¹²⁴ This section will also include the following conversation starters: “Who is my primary contact person? Is he or she a representative of an investment adviser or a broker-dealer? Who can I talk to if I have concerns about how this person is treating me?”¹²⁵ Finally,

¹¹⁵ *Id.* at 33,532 – 33,533, notes 507 – 509.

¹¹⁶ *Id.* at 33,533.

¹¹⁷ *Id.*

¹¹⁸ *Id.* at 33,535.

¹¹⁹ *Id.* at 33,536.

¹²⁰ *Id.*

¹²¹ *Id.* at 33,537 – 33,538.

¹²² *Id.* at 33,538.

¹²³ *Id.* at 33,539.

¹²⁴ *Id.*

¹²⁵ *Id.* at 33,540.

this section must include a phone number where investors can request up-to-date information as well as a copy of the relationship summary.¹²⁶

c. Filing, Delivery, and Updating Requirements

Firms must file the relationship summary with the SEC; and the SEC will make the forms publicly available through the website, Investor.gov.¹²⁷ Additionally, firms must make the forms available on their own websites.¹²⁸

Firms may deliver the relationship summary electronically, so long as the firm complies with the SEC's rules regarding electronic delivery.¹²⁹ Essentially, the firm must make the investor aware that the form is available electronically; the access to the information must be comparable to that which would have been provided in paper form; and the firm must maintain evidence of delivery.¹³⁰

Brokerage firms must deliver the relationship summary before or at the earliest of: (i) a recommendation as to account type, a securities transaction, or an investment strategy; (ii) placing an order; or (iii) opening a brokerage account.¹³¹ Investment advisers must deliver the relationship summary before or at the time of entering into an investment advisory contract with an investor.¹³²

After the initial delivery of the form, firms must re-deliver the relationship summary whenever: (i) an account is opened that is different than the investor's existing account(s); (ii) there is a recommendation to roll over assets; or (iii) there is a recommendation for a new service or product that would not be held in an existing account.¹³³ This last item contemplates recommendations for investments such as direct-sold mutual funds or insurance products.¹³⁴

Finally, firms must update the relationship summary within 30 days whenever the relationship summary becomes materially inaccurate.¹³⁵ At that time, the revised relationship summary must be filed with the SEC and posted to the firm's website.¹³⁶ Firms will have 60 days to deliver the revised relationship summary to existing clients.¹³⁷ When delivering the revised relationship

¹²⁶ *Id.*

¹²⁷ *Id.* at 33,545.

¹²⁸ *Id.*

¹²⁹ *Id.* at 33,546.

¹³⁰ *Id.* at 33,547.

¹³¹ *Id.* at 33,550.

¹³² *Id.* at 33,551.

¹³³ *Id.* at 33,552.

¹³⁴ *Id.*

¹³⁵ *Id.* at 33,554.

¹³⁶ *Id.*

¹³⁷ *Id.*

summary, firms must highlight any changes by either marking the revised text or including a summary of the changes.¹³⁸

III. Investment Adviser Interpretation

As part of the Regulation Best Interest Rule package, the SEC issued an interpretation of the investment adviser standard of conduct.¹³⁹ The SEC recognized that the investment adviser's fiduciary duty follows the contours of the relationship with the client.¹⁴⁰ Further, an investment adviser can shape that relationship by agreement, so long as there is full and fair disclosure, and informed consent by the client.¹⁴¹ The specific duties that an investment adviser owes to a client will depend on the services that the adviser has agreed to perform for the client.¹⁴² However, an investment adviser cannot have a client waive the fiduciary duty.¹⁴³

a. Duty of Care

An investment adviser's fiduciary duty includes a duty of care. This duty includes: (i) the duty to provide advice that is in the best interest of the client; (ii) the duty to seek best execution of a client's transactions where the adviser has the duty to select the broker-dealer that will execute the client's trades; and (iii) the duty to provide advice and monitoring over the course of the relationship.¹⁴⁴

The duty to provide advice that is in the best interest of the client is a duty to provide advice that is suitable for the client.¹⁴⁵ To be able to satisfy this duty, the investment adviser must make a reasonable inquiry into the client's financial situation, financial sophistication, investment experience, and financial goals, among other things.¹⁴⁶ Further, the investment adviser must determine that the client can and is willing to tolerate the risks of any recommended investment, and that the potential benefits of the investment recommendation justify the risks.¹⁴⁷

Next, the investment adviser must conduct a reasonable investigation into the investment being recommended.¹⁴⁸ As part of the investigation, the investment adviser must consider a number of

¹³⁸ *Id.*

¹³⁹ 84 Fed. Reg. 33,669.

¹⁴⁰ *Id.* at 33,671.

¹⁴¹ *Id.*

¹⁴² *Id.*

¹⁴³ *Id.* at 33,672.

¹⁴⁴ *Id.* at 33,672.

¹⁴⁵ *Id.*

¹⁴⁶ *Id.* at 33,673.

¹⁴⁷ *Id.*

¹⁴⁸ *Id.* at 33,674.

factors relating to the investment, including the cost associated with the investment advice; as well as the investment product's or strategy's investment objectives, characteristics, liquidity, risks and potential benefits, volatility, likely performance in a variety of market and economic conditions, time horizon, and cost of exit.¹⁴⁹ This duty applies to advice about investment strategy, engaging a sub-adviser, and account type.¹⁵⁰ Accordingly, advice to open a particular type of account (brokerage or investment advisory) as well as advice about rolling over assets would trigger this duty.¹⁵¹

In seeking best execution, an investment adviser must try to execute trades such that the costs or proceeds from each transaction are the most favorable for the client.¹⁵²

The duty to monitor means the investment adviser must monitor a client's account at a frequency that is in the best interest of the client.¹⁵³ However, if the investment adviser has been engaged for a limited duration, the investment adviser is unlikely to have a duty to monitor.¹⁵⁴

b. Duty of Loyalty

In simple terms, an investment adviser has a duty of loyalty, which prohibits the investment adviser from subordinating its clients' interests to its own.¹⁵⁵ As part of this duty, the investment adviser must make full and fair disclosure of any material facts relating to the advisory relationship.¹⁵⁶

Additionally, the investment adviser must eliminate or at least expose through full and fair disclosure all conflict of interest that might incline an adviser to render advice that is not disinterested.¹⁵⁷ For disclosure to be full and fair, the disclosure must be specific enough so that the client can understand the material fact or the conflict of interest and be able to make an informed decision as to whether to provide consent.¹⁵⁸

As part of its disclosure, an investment adviser may not state that the adviser "may" have a conflict if the conflict actually exists; however, "may" could be appropriate if the conflict does not currently exist but might reasonably present itself in the future.¹⁵⁹ In other words, disclosure will not be full and fair if the adviser states that a conflict "may" exist if the conflict already does exist.

¹⁴⁹ *Id.*

¹⁵⁰ *Id.*

¹⁵¹ *Id.*

¹⁵² *Id.*

¹⁵³ *Id.* at 33,675.

¹⁵⁴ *Id.*

¹⁵⁵ *Id.*

¹⁵⁶ *Id.*

¹⁵⁷ *Id.* at 33,676.

¹⁵⁸ *Id.*

¹⁵⁹ *Id.*

Investment advisers do not have to determine whether the client actually understood the disclosure that was made.¹⁶⁰ The investment adviser merely has to put the client into the position to be able to understand the disclosure.¹⁶¹ However, if the investment adviser actually knows, or reasonably should know, that the client does not understand the disclosure, the adviser cannot accept the client's consent.¹⁶²

If the conflict is of a nature and to an extent that it would be difficult to be able to fully explain the conflict in a way that it could be understood by a client, the investment adviser must eliminate or mitigate the conflict.¹⁶³

IV. Solely Incidental Prong of the Broker-Dealer Exclusion from the Definition of Investment Adviser

In the last item of the Regulation Best Interest Rule package, the SEC provided an interpretation of the "solely incidental" prong of the broker-dealer exclusion from the definition of "investment adviser."¹⁶⁴ In this interpretation, the SEC clarified that if a broker exercises unlimited discretion, such conduct would not be "solely incidental" to the business of the broker-dealer, and accordingly, the brokerage firm would meet the definition of "investment adviser."¹⁶⁵ However, discretion that is limited in scope would not necessarily turn a brokerage firm into an investment adviser.¹⁶⁶

With respect to monitoring a customer's account, if the monitoring is at specific intervals for the purpose of determining whether to provide a buy, sell, or hold recommendation, such conduct would be considered "solely incidental" to the broker-dealer's primary business of effecting securities transactions.¹⁶⁷ It would not turn the brokerage relationship into an advisory relationship.

V. FINRA Changes and Guidance

On June 19, 2020, FINRA issued Regulatory Notice 20-18, "Reg BI-Related Changes to FINRA Rules."¹⁶⁸ FINRA has explained that FINRA Rule 2111 (the "Suitability Rule") will not apply to

¹⁶⁰ *Id.* at 33,677.

¹⁶¹ *Id.*

¹⁶² *Id.*

¹⁶³ *Id.*

¹⁶⁴ 84 Fed. Reg. 33,681.

¹⁶⁵ *Id.* at 33,686.

¹⁶⁶ *Id.*

¹⁶⁷ *Id.* at 33,687.

¹⁶⁸ FINRA Regulatory Notice 20-18, "Reg BI-Related Changes to FINRA Rules" (June 19, 2020) ("Reg. Notice 20-18"), available at <https://www.finra.org/sites/default/files/2020-06/Regulatory-Notice-20-18.pdf>.

recommendations subject to Regulation Best Interest.¹⁶⁹ FINRA also explained that there remained certain recommendations to which Regulation Best Interest would not apply.¹⁷⁰ For example, Regulation Best Interest only applies to recommendations to retail customers seeking advice for personal, family, or household purposes. Accordingly, the Suitability Rule would continue to apply to recommendations to entities and institutions, such as pension funds.¹⁷¹ The Suitability Rule will also apply to recommendations made to natural persons who will not be using the investment recommendation for personal, family, or household purposes, such as small business owners or charitable trusts.¹⁷² In those instances when the Suitability Rule would apply, FINRA has modified the quantitative suitability component to remove the control element, thereby making it consistent with Regulation Best Interest.¹⁷³

Finally, certain FINRA rules restrict, but permit, the payment and receipt of non-cash compensation in connection with the sale and distribution of certain types of securities, including direct participation programs, variable insurance contracts, and investment company securities.¹⁷⁴ As discussed above, Regulation Best Interest requires firms to eliminate non-cash compensation that is based on the sales of specific securities or specific types of securities within a limited time. Accordingly, to the extent the referenced FINRA rules permit non-cash compensation, FINRA makes it clear that such compensation must be consistent with the requirements of Regulation Best Interest.¹⁷⁵ The changes set forth in the Regulatory Notice were effective on June 30, 2020, the same date Regulation Best Interest became effective.

¹⁶⁹ *Id.* at 2. See also FINRA Rule 2111.08.

¹⁷⁰ Reg. Notice 20-18 at 2.

¹⁷¹ *Id.* at note 3.

¹⁷² *Id.*

¹⁷³ *Id.* at 2. See also FINRA Rule 2111.05(c).

¹⁷⁴ See FINRA Rules 2310, 2320, 2341, and 5110.

¹⁷⁵ Reg. Notice 20-18 at 2. See also FINRA Rules 2310(c)(2), 2320(g)(4), 2341(l)(5), 5110(h)(2).