New York Law Journal

NEW YORK LAW JOURNAL SPECIAL REPORT

An ALM Publication

Litigation

WWW.NYLJ.COM

VOLUME 260—NO. 93

TUESDAY, NOVEMBER 13, 2018

The **Criminal Practitioner's Guide** To Representing Financial Professionals

SHUTTERSTOCK

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New York's status as the global finance capital means that members of the metro-area criminal bar sometimes find themselves defending stockbrokers, investment bankers, traders, research analysts, compliance officers, and other financial professionals. While these cases often generate robust retainers, they also present unique challenges resulting from the regulatory reporting regime that governs the securities industry. A basic understanding of this regime is critical to effectively representing financial professionals so as to avoid collateral economic and reputational harm to clients.

Broker-dealer regulation includes oversight by government actors like Securities & Exchange Commission (SEC) and state Blue Sky authorities as well as by self-regulatory organizations (SROs) like the Financial Industry Regulatory Authority and the enforcement arms of individual exchanges, the most notable of which is the New York Stock Exchange (NYSE). Banks and insurance companies are not included within this regulatory scheme.

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In order to buy and sell stocks for the account of others, financial firms are required to register as broker-dealers with the SEC and with the states in which they wish to transact business. They are also required to apply for membership in FINRA. Similarly, individuals that want to work at, or in industry parlance, become "associated" with brokerage firms, have to become registered and take qualifying licensing examinations (like the Series 7) through a process overseen by FINRA. Once an application is submitted, the applicant becomes an "associated person" subject to FINRA's jurisdiction and disciplinary reach.

FINRA is not a governmental agency. Created in 2007 as a result of a merger between the regulatory arms of the National Association of Securities Dealers and the NYSE, FINRA is responsible for policing its member firms and associated persons through enforcement of its own rules, SEC regulations and federal securities laws. It has the power to discipline member firms and associated persons through the imposition of suspensions, bars, fines, disgorgement, restitution and remediative undertakings. In 2016, the NYSE rejoined the regulatory beat when it took back some of the regulatory responsibilities it had ceded to FINRA in the 2007 merger.

Financial professionals consent to regulatory oversight by FINRA (and the NYSE if their employer is an Exchange member) as a condition of registration and the privilege of making a living in the brokerage industry. Registration is accomplished through the completion and submission to FINRA of the "Uniform Application for Securities Registration and Transfer," known as the "Form U4" or simply "U4." Financial professionals are required to submit a Form U4 when they first join the securities industry and each time they join a new brokerage firm. In addition to requiring basic personal background information, employment history and licensing status, the U4 contains a series of disclosure questions that ask whether the applicant has ever been the subject of a lien, bankruptcy, judgment, civil suit, customer complaint, administrative action, and, relevant to our purposes, criminal prosecution. After completing a Form U4, industry members are under a continuing obligation to amend their U4 in the event that answers to any of these disclosure questions change.

A basic understanding of this regime is critical to effectively representing financial professionals so as to **avoid collateral economic and reputational harm to clients.**

Once an applicant completes the U4, his or her employer uploads it to FINRA's Central Registration Depository (CRD) database, which functions as an informational clearing house for industry members and regulators. In that connection, the Form U4 is both résumé and rap sheet. Brokerage firms use it to assess the background of prospective hires. Regulators monitor U4 amendments to determine if a change of information requires the initiation of an investigation. FINRA also makes available a public version of an individual's Form U4 through its "BrokerCheck" portal, accessible at https://brokercheck.finra.org. FINRA touts BrokerCheck as a tool for investors to vet the qualifications and background of financial professionals with whom they may want to invest.

As set forth above, the U4 disclosure questions encompass criminal prosecutions. More specifically, associated persons are required to disclose charges, convictions and nolo contendere pleas for all felonies and for misdemeanors involving honesty or investing, occurring in domestic, foreign and military courts. Associated persons are also required to disclose charges against and convictions of organizations over which they exercised control. Question 14A, the disclosure question related to felonies, illustrates how the U4 criminal disclosure questions are worded:

(1) Have you ever:

(a) been convicted of or pled guilty or nolo contendere ("no contest") in a domestic, foreign, or military court to any felony?

(b) been charged with any felony?

(2) Based upon activities that occurred while you exercised control over it, has an organization ever:

(a) been convicted of or pled guilty or nolo contendere ("no contest") in a domestic or foreign court to any felony?

(b) been charged with any *felony*?

Question 14B(1), uses the same language to require the disclosure of misdemeanors involving "investments or an investment-related business or any fraud, false statements, or omissions, wrongful taking of property, bribery, perjury, forgery, counterfeiting, extortion, or a conspiracy to commit any of these offenses."

Once the answer to any of these questions becomes "yes," an associated person is required to disclose the criminal justice event to his or her brokerage firm. The firm then gathers information and documents pertaining to the charge or conviction and files a Form U4 amendment with FINRA that reflects the "yes" answer and contains a disclosure page that sets forth the date of the event, a description of the charge, and the present status of the case. FINRA then incorporates the amendment into both the CRD and BrokerCheck versions of the associated person's U4 profile.

Given these reporting obligations, the most important collateral consequence of which defense counsel should be

aware is the potential for a client to be "statutorily disqualified" from the securities industry as a result of criminal justice disclosure. A statutory disqualification results when an associated person is convicted of a felony or any of the misdemeanors enumerated above. Once an associated person becomes subject to a statutory disqualification, he or she is prohibited from working in the securities industry for 10 years. While it is possible to apply to FINRA for a waiver of the 10-year sit-down, these waivers are potentially costly to pursue and difficult to obtain. As it is with clients facing immigration and probation issues, it is critical that defense attorneys preparing to recommend a reportable plea fully discuss the plea's ramifications with his or her client.

As ruinous as a statutory disqualification can be for a client, it is not the only consequence that defense attorneys need to keep in mind. Once a criminal justice event appears on a client's BrokerCheck profile, it is accessible to clients, prospects, potential employers, co-workers, friends, family, neighbors, rival brokers looking to poach clients, and members of the press. Suffice it to say, the economic and reputational harm resulting from a criminal justice-related entry is potentially disastrous even if it does not result in a statutory disqualification.

Given these stakes, criminal practitioners must be vigilant regarding this potential. This is easier said than done, especially in post-arrest engagements where the client's obligation to disclose the charge has already been triggered. In those situations, counsel's efforts are best focused on obtaining a disposition that not only avoids a statutory disqualification but also effectively "walks back" the information in the initial disclosure resulting from the arrest. This way, if called upon by a prospective client or employer to explain the brush with the law, an associated person can chalk up the charge to a law enforcement overreach, a misunderstanding, or some other face-saving, euphemistic rationale. In this context, with an eye toward the content of the eventual disclosure resulting from the conviction, defense attorneys should prevail upon prosecutors to agree to charges and/or charging language that cast the client in the best possible light. Of course, misdemeanors are better than felonies and misdemeanors not implicating the client's investment activities or honesty are preferable to those that do. And it goes without saying that non-criminal dispositions are the best result in this context.

While securing a non-criminal disposition is a tough ask, defense attorneys might find themselves surprisingly well-positioned to appeal to a prosecutor's self-interest to bring about this very result. For instance, prosecutions of financial professionals often involve investors who have suffered financial loss such that restitution may be a priority for the assistant district attorney. In these cases, defense counsel can argue for a deferred prosecution agreement under the rationale that if the prosecutor insists on a disposition that results in a damaging BrokerCheck disclosure, then the client will lose his or her ability to maintain or find gainful employment and thus, will not be able to make the victim whole.

This pitch is potentially more useful in cases where counsel is engaged prior to the client being charged. In these cases, counsel can argue that once a prosecutor files a reportable charge, he or she is forever undercutting the defendant's ability to pay restitution to the complaining witness. If that approach does not work, counsel can still use the same rationale to convince the prosecutor to agree to charges and/or a plea that doesn't require a U4 amendment. Failing this disposition, the argument can still be employed in service to favorable or at least mitigating charging language.

The foregoing discussion is limited to situations where the client is not exposed to significant jail time or other serious penalties. Of course, in cases with serious charges, preserving the client's liberty takes precedence over insulating him or her from damning regulatory disclosures.

Defense counsel should also be cognizant of the consequences for an associated person who fails to disclose a reportable criminal justice event. All brokerage firms have policies and procedures that require both the prompt reporting of criminal justice events as well as the annual completion of compliance questionnaires that ask whether any reportable events have occurred in the last year. Associated persons who fail to make prompt disclosures or who lie on their compliance questionnaires are subject to termination. Similarly, in order to give teeth to its disclosure regime, FINRA will move aggressively against any associated person who willfully fails to make a required disclosure, regardless of the outcome of the criminal case. In these situations, FINRA typically seeks a multi-month suspension that nearly always results in job termination. In egregious cases, involving, for example, the failure to disclose serious crimes, or prolonged non-disclosure or elaborate attempts to shield a reportable arrest or conviction from an employer, FINRA typically seeks a permanent bar. Finally, cases involving a willful failure to disclose a reportable criminal justice event result in a statutory disqualification. The FINRA enforcement docket is often populated by cases of this ilk. For these reasons, criminal counsel should never advise a client to shirk his or her disclosure obligations.