

THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION

ROUNDTABLE ON REGULATORY APPROACHES
TO COMBATING RETAIL INVESTOR FRAUD

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U.S. Securities and Exchange Commission

100 F Street, NE

Washington, D.C.

Page 2

1	PARTICIPANTS:
2	
3	Jay Clayton, Chairman
4	Kara Stein, Commissioner
5	Robert Jackson, Commissioner
6	Elad Roisman, Commissioner
7	Hester Peirce, Commissioner
8	Brett Redfearn
9	Lizzie Baird
10	Valerie Dahiya
11	Laura Gold
12	Tim White
13	Lourdes Gonzalez
14	Christian Sabella
15	Moshe Rothman
16	Mark Saltzburg
17	Racquel Russell
18	Owen Donley
19	
20	Panel One
21	Charu Chandrasekhar
22	Cameron Funkhouser
23	Christopher Gerold
24	Nicole Iannarone
25	Jean Setzfand

Page 4

1	PARTICIPANTS (Continued):
2	
3	Panel Three
4	David Becker
5	Cromwell Coulson
6	Robert Franz
7	Christopher Gerold
8	Mark Harmon
9	Andrea Manning
10	Christy Oeth
11	Michael Paley
12	Chris Stone
13	Gerri Walsh
14	
15	
16	
17	
18	
19	
20	
21	
22	
23	
24	
25	

Page 3

1	PARTICIPANTS (Continued):
2	
3	Panel Two
4	Troy Carlson
5	Faith Colish
6	James Fiebelkorn
7	Christopher Gerold
8	Sarah Green
9	Yvonne Huber
10	Michael Rufino
11	Ignacio Sandoval
12	Daniel Zinn
13	
14	
15	
16	
17	
18	
19	
20	
21	
22	
23	
24	
25	

Page 5

1	CONTENTS	
2		PAGE
3	Opening Remarks	6
4		
5	Panel One - Types of Fraudulent and Manipulative	
6	Schemes Currently Targeting Retail Investors	19
7		
8	Panel Two - Enhancing the ability of	
9	Broker-Dealers to Combat Retail Investor Fraud	78
10		
11	Panel Three - Additional Ways to Combat Retail	
12	Investor Fraud	198
13		
14	Closing Remarks	208
15		
16		
17		
18		
19		
20		
21		
22		
23		
24		
25		

Page 6

1 P R O C E E D I N G S

2 MR. REDFEARN: So good morning and welcome to

3 the Securities and Exchange Commission Staff's Roundtable

4 on Combating Retail Investor Fraud. I'm Brett Redfearn,

5 deputy -- excuse me --

6 (Laughter.)

7 MR. REDFEARN: -- Director of the Division of

8 Trading and Markets. It's still early -- I'll have a sip

9 of my coffee -- Director of the Division of Trading and

10 Markets.

11 I also want to introduce my Deputy Director in

12 the Division, Lizzie Baird. My other Deputy Director,

13 Christian Sabella, will be joining us later today.

14 I would also like to welcome Chairman Clayton

15 and Commissioner Roisman and Commissioner Jackson, who

16 are here. And we also expect the other Commissioners,

17 Peirce and Stein, to join us later.

18 So I will begin by asking Chairman Clayton to

19 make his opening remarks. Chairman Clayton.

20 CHAIRMAN CLAYTON: Good morning, everyone. And

21 thank you, Brett. And also, thanks to the Division of

22 Trading and Markets for organizing this roundtable on

23 what is a critical topic, combating retail investor

24 fraud.

25 Serving and protecting Main Street investors

Page 7

1 has been and will remain a top priority for me as SEC

2 Chairman. Our agency has historically worked very hard

3 to identify, punish and deter misconduct that affects

4 retail investors. But the relative propensity of retail

5 fraud, including in the penny stock and digital asset

6 markets, continues to trouble me and many of my

7 colleagues.

8 Today's roundtable is part of a broader effort

9 across the SEC to examine whether there are additional

10 steps we can take to protect Main Street investors. Last

11 September, for instance, the Division of Enforcement

12 formed the Retail Strategy Task Force, which draws on

13 expertise from across the agency to develop strategies

14 and techniques for addressing the types of activities

15 that harm retail investors. These include microcap pump

16 and dump frauds, Ponzi schemes and the sale of unsuitable

17 products, among other things.

18 I am going to deviate from my prepared remarks

19 and note that our Division of Enforcement just last week

20 halted a multimillion-dollar Ponzi scheme in the

21 Baltimore area. And I applaud them for their action. As

22 we all know, when those types of -- the longer those

23 types of schemes go on, the more money people lose. And

24 I am happy to see that our Enforcement Division

25 recognizes that and is acting on it.

Page 8

1 Additionally, in May, we launched the SEC

2 Action Lookup for Individuals, or SALI, a new online

3 search feature that enables retail investors to research

4 whether the person trying to sell them investments has a

5 judgment or order entered against them in an enforcement

6 action. SALI is intended to help investors avoid

7 financial fraud by giving them more information about who

8 they are dealing with. Our agency also participates in a

9 joint agency task force, spearheaded by the Department of

10 Justice on market integrity and consumer fraud.

11 In addition to detecting and punishing

12 fraudulent conduct that has already occurred, it is

13 paramount that we act proactively and consider preventive

14 measures. Put simply, we need to continue to examine

15 whether our regulatory framework is appropriately

16 tailored to help prevent fraudulent activity before it

17 occurs.

18 Today's roundtable will explore many of the

19 questions in this area that have been on my mind. For

20 example, are there specific rule changes the Commission

21 should consider that would better deter fraudulent

22 practices? Are the rules governing the distribution and

23 trading of penny stocks appropriately tailored in this

24 regard? Are there ways that we can help enhance the

25 ability of broker-dealers, investment advisers and other

Page 9

1 industry participants to identify and combat retail

2 fraud? Are there things that gatekeepers such as lawyers

3 and accountants can do to help in this regard? Are there

4 steps that the Commission, our fellow regulators and the

5 financial services industry can take to help investors

6 better protect themselves?

7 I am extremely passionate about this topic and

8 have been looking forward to this event. Let me pause,

9 again deviating from my prepared remarks and say how I

10 look at this.

11 As we look at the field that is presented to

12 retail investors and we look at the available field of

13 investments, the available field of investments is larger

14 than the field presented to retail investors. But is the

15 field that we're having them play on the right one? Are

16 there places where they are investing where there is

17 really no upside and there's a great deal of risk?

18 Perhaps we should restrict that field or make it more

19 protective? And are there places where they're not

20 allowed to participate where there is opportunity and we

21 can limit the risk of fraud?

22 It has been a long time since we have looked

23 across the field of available investments for retail

24 investors and said, what makes sense? And I look forward

25 to the contributions of this group with that perspective

1 in mind.

2 I want to thank the participants for being

3 willing to share their time and I look forward to the

4 day. Thank you.

5 MR. REDFEARN: Thank you, Chairman.

6 So for other opening statements, Commissioner

7 Peirce? Thank you and welcome.

8 COMMISSIONER PEIRCE: Thanks, Brett. And

9 thanks to all of you for being here today. I especially

10 thank the participants in today's roundtable. One thing

11 that has not changed over time is the capacity and

12 ingenuity of people who want to engage in retail fraud.

13 And so I think we are working very hard. That's

14 reflected in today's roundtable and also reflected in the

15 work of the Divisions of Enforcement, Trading and

16 Markets, Office of Investor Education and Advocacy and

17 the Office of Compliance, Inspections and Examinations,

18 among others here at the agency, working very hard to

19 combat retail fraud.

20 I am very enthusiastic about today's

21 roundtable. I think it looks at some issues that can

22 help us take a more systematic approach to dealing with

23 retail fraud, which I think is important. I'm

24 particularly interested in the work that we can do with

25 respect to transfer agents and finders, which could again

1 be helpful in taking a systematic approach but also could

2 be helpful in making sure that we don't squelch

3 legitimate activity in our efforts to combat fraud.

4 So I think the conversation today will be very

5 useful to me. Although I won't be able to be here for

6 much of it in person, I do look forward to watching it

7 afterwards. And thank you again for your time and the

8 effort of everyone who put this roundtable together.

9 Thanks.

10 MR. REDFEARN: Thank you, Commissioner Peirce.

11 Commissioner Jackson.

12 COMMISSIONER JACKSON: Thank you, Director

13 Redfearn. I just want to join my colleagues in

14 expressing our deep gratitude to the panelists and

15 participants today. And I'll be brief, because we are

16 really here to hear from you.

17 But the point I want to make is I've spent some

18 time recently thinking through, working through the long

19 and detailed history of the issues in this area. And I

20 want to say that in my view, we're starting in exactly

21 the right place, which is how it affects retail

22 investors. To me, it's really easy to get lost in the

23 complexities of market structure. It's really easy to

24 wonder about all the different institutional choices

25 we've made over the years, how we got here, why we got

1 here. And I think we are starting in exactly the right

2 place, which is, regardless of how we got here, what is

3 the best way forward for average investors we're sworn to

4 protect?

5 That's why I'm so excited, not only about

6 today's roundtable but about all the conversations we're

7 going to have in this area over the coming months. I am

8 very pleased to have the opportunity to work with the

9 Chairman, with Director Redfearn and others on these

10 important subjects. I know we all have the same goal,

11 which is creating markets where retail investors are

12 protected and safe and have the opportunity to

13 participate in our nation's economic growth.

14 Thanks so much to all of you for being here

15 today and I look forward to the conversation.

16 MR. REDFEARN: Thank you, Commissioner Jackson.

17 Commissioner Roisman.

18 COMMISSIONER ROISMAN: Well, good morning.

19 Thank you, everyone attending the roundtable today in

20 person and those watching online as well. Today's event

21 is one of particular importance to all of us at this

22 agency. The first part of the SEC's three-part mission

23 is to protect investors. And this particularly motivates

24 many of us in this building who know victims of retail

25 investor fraud who have worked on these types of SEC

1 matters.

2 While I have only served as commissioner for a

3 short period of time, I've been greatly troubled by the

4 number of cases involving harm to Main Street investors,

5 some of whom have lost their life savings. Like my

6 fellow commissioners and the incredible Staff here at the

7 SEC, I am committed to doing everything I can to

8 eradicate these types of behavior. While OIEAs, OCs and

9 Enforcement's roles in combatting retail investor fraud

10 are more apparent, the entire SEC, including the policy-

11 making divisions, actively work to address it. Today's

12 roundtable demonstrates this, and also it brings together

13 many important market participants, including regulated

14 entities such as investment advisers, broker-dealers,

15 market centers, regulatory organizations, as well as

16 state authorities, amongst others. We're all in this

17 together, working to make the market safer and bolster

18 investor confidence.

19 Today's panels provide an excellent launching

20 pad for many of the issues on which the SEC and others

21 are focused. Thank you to the Division of Trading and

22 Markets for hosting this roundtable, and to our Office of

23 Compliance Inspections and Examinations and Division of

24 Enforcement for all that you do to identify bad actors

25 and hold them accountable.

1 Finally, I commend my fellow commissioners and
 2 Chairman Clayton for their continued focus on Main Street
 3 investors in both enforcement matters and in our
 4 rulemaking agenda here at the Commission. I look forward
 5 to hearing from all of the panelists about your
 6 experiences as well as any suggestions as to how we can
 7 improve our current effort. Thank you.

8 MR. REDFEARN: Thank you, Commissioner Roisman.
 9 Commissioner Stein.

10 COMMISSIONER STEIN: Thank you, Brett. I just
 11 want to welcome you all again for being here and taking
 12 time out of very busy schedules to give us your best
 13 thoughts today.

14 Retail fraud and, I think, more importantly,
 15 how to prevent retail fraud is at the heart of the
 16 Commission's mission. And unfortunately, as Elad was
 17 saying, every week I see investors harmed by different
 18 types of cons and schemes and market manipulation. And
 19 sadly, I think a lot of the time, there's very little we
 20 can do to get money back to investors because the money
 21 is already gone. And that's why the focus on prevention
 22 is so important.

23 And I think we need to think about prevention
 24 broadly, because I guess fraud -- and they, when it comes
 25 in so many forms, so I think sometimes it's like whack-a-

1 mole, there's always a new scheme. It's about Ebola
 2 vaccines or marijuana dispensing machines or there's
 3 always some new investment scheme. And these lies or
 4 misrepresentations are not limited to individuals or
 5 small groups of people. You know, unfortunately it can
 6 happen at major institutions, at small institutions, on
 7 the Internet. And therefore, I think we all need to be
 8 looking at all corners of the market to pleas for fraud.

9 And I think the other thing that about being a
 10 Securities and Exchange commissioner that's hard
 11 sometimes is you see the real-world effects that fraud
 12 has on real people. It affects retirements, college
 13 plans, homebuying and other things that people were
 14 saving money for. And to prevent the damage caused by
 15 fraudsters, government and industry need to work hand in
 16 hand in partnership.

17 So please give us your best thoughts today.
 18 Are there any changes to existing rules, policies or laws
 19 that could help in this area? And what other advice do
 20 you have for us, you know, on this important part of our
 21 mission?

22 So again, thank you to everyone for being here
 23 and I look forward to the conversation.

24 MR. REDFEARN: Thank you, Commissioner Stein.
 25 Great. So before I start with a couple other

1 introductory comments, I just want to provide our
 2 standard disclaimer that the views I and the Staff that
 3 are here today provide are our own and do not necessarily
 4 reflect the views of the Commission, Chairman Clayton,
 5 other commissioners or my colleagues on the SEC Staff.

6 So as you all know, this is the second in a
 7 series of roundtables we will be holding that are focused
 8 on trading and market-specific rules and topics. In
 9 April, we held a roundtable focused on thinly traded,
 10 exchange-listed securities. And as we announced on
 11 Monday, we will be holding a two-day roundtable on market
 12 data and market access on October 25 and 26.

13 Today, as you know, our focus is on retail
 14 investor fraud and possible regulatory measures to help
 15 counteract fraudulent activity. The U.S. securities
 16 markets, like other global markets, historically have
 17 attracted fraudsters, particularly with respect to
 18 schemes involving the latest hot or in trend. Over the
 19 years, we've witnessed schemes involving penny stocks,
 20 mining stocks, tech stocks. And, more recently, digital
 21 asset securities. These schemes are perpetrated by both
 22 registered and unregistered persons who work hard to
 23 convince individuals to invest in enterprises that they
 24 claim will be sure to be moneymakers.

25 Targets of such fraudulent activities have

1 changed little over the years. Seniors and members of
 2 affinity groups continue to be preyed upon by the
 3 unscrupulous. And we don't have to look far to find
 4 these schemes.

5 As Chairman Clayton and others have mentioned,
 6 just last week, the Commission announced that it had
 7 charged several individuals and entities with engaging in
 8 a Ponzi-like scheme that netted more than \$345 million.
 9 The investors included retirees, doctors, accountants and
 10 current and former professional athletes. The Commission
 11 alleges the defendants faked documents to show phony
 12 transfers, bank statements and portfolio reports, and
 13 stole money to fund their own lavish lifestyles.

14 The Commission has been busy bringing cases
 15 against scammers as well as seeking trading suspensions
 16 in instances of suspected fraud. In fact, in fiscal year
 17 2017, the Commission suspended trading in the securities
 18 of 309 issues, a 55 percent increase over fiscal year
 19 2016, in order to combat potential market manipulation in
 20 microcap fraud threats to investors.

21 In fiscal year 2017, the Commission brought
 22 charges against 13 individuals allegedly involved in two
 23 Long Island-based cold calling scams that bilked more
 24 than 100 victims out of more than \$10 million through
 25 high-pressure sales tactics and lies about penny stocks.

1 And also 27 individuals and entities behind various
2 alleged stock promotion schemes that left investors with
3 the impression they were reading independent, unbiased
4 analyses on investing websites, while writers actually
5 were being secretly compensated for touting company
6 stock.

7 The Commission's Enforcement Staff cannot carry
8 this burden alone. Well-tailored regulatory measures
9 along with investor education efforts can also help to
10 protect investors from fraudulent and manipulative
11 schemes. To that end, we are holding this roundtable to
12 highlight problems associated with retail investor fraud
13 and possible regulatory approaches to these problems.

14 Today's roundtable will consist of three
15 panels. I will be moderating the first panel that will
16 focus on the types of fraudulent and manipulative schemes
17 that are currently targeting retail investors.
18 Specifically, we will discuss what types of schemes
19 retail investors should be wary of and the role that the
20 Internet chatrooms, online platforms and social media
21 play in these schemes.

22 The next two panels will focus on the ways that
23 we can enhance the ability of broker-dealers to combat
24 retail fraud that are discussed during the first panel,
25 and whether there are steps the Commission can take with

1 space. And so why don't we start with Charu
2 Chandrasekhar? We'll start with you. Did I get that
3 right?

4 MS. CHANDRASEKHAR: Great, perfect. Yes,
5 thanks, very much, Brett.

6 Hi, I'm Charu Chandrasekhar. I am the Chief of
7 the Retail Strategy Task Force in the Division of
8 Enforcement. Delighted to be here. As always, my
9 remarks reflect my own views and not those of the Staff
10 or the Commission.

11 So the task force is the newest national group
12 within the Enforcement Division. We launched earlier
13 this year and we have a presence in eight of the 12
14 regional offices and here in the home office.

15 Retail fraud is obviously a very broad category
16 and, accordingly, our mandate as a task force is
17 similarly expansive. Retail fraud includes classic
18 frauds such as Ponzi schemes, boiler room schemes,
19 misappropriation and churning by brokers, market
20 manipulation and pump and dumps and, more recently, fraud
21 involving cryptocurrencies and digital assets. And the
22 common thread across all of these cases is harm to an
23 ordinary, everyday investor.

24 So, in turn, our task force has two objectives,
25 enforcement and investor advocacy. So first, when it

1 respect to broker-dealer regulation. Panel Two will be
2 moderated by Lizzie and will discuss Rule 15c2-11,
3 Broker-Dealer Registration and Suspicious Activity
4 Reports.

5 The third and final panel will be moderated by
6 Christian Sabella, my other deputy, and will address
7 transfer agents, trading halts and investor education.

8 Our panelists today represent a wide array of
9 participants from industry, regulators and academia and
10 I'm looking forward to hearing what they -- what you have
11 to say about these important issues. So first, I want to
12 thank you all for being here and thanks again for
13 agreeing to do this. We are very enthusiastic about
14 hearing your views.

15 I would also like to thank the Staff that
16 worked very hard on this, especially Arisa Koenig who put
17 in a lot of work making this all come together.

18 So now, let's go ahead and turn to our first
19 panel to explore what ploys are duping retail investors
20 and the current trends that regulators and industry
21 participants are noticing.

22 So first, I would like to ask each of our
23 panelists to introduce themselves. And I think it would
24 be helpful for each panelist to just explain for a minute
25 or two your role in the market, key concerns in this

1 comes to enforcement, the task force deploys data and
2 technology to strategically identify widespread abuses
3 that target retail investors. And we apply this data-
4 driven approach to bring enforcement actions that target
5 these high priorities of retail investor harm. And doing
6 so, we partner with several other groups across the
7 Commission, including Staff from our national exam
8 program and Staff from our Division of Risk and Economic
9 Analysis.

10 Second, in terms of investor education and
11 advocacy, we collaborate with the Commission's Office of
12 Investor Education and Advocacy on investor outreach.
13 And that messaging is focused on increasing investor
14 awareness about common investment frauds and red flags
15 that the everyday investor should look out for when
16 protecting themselves against investment fraud.

17 So in terms of areas of emerging risk for
18 retail investors that concern me the most, I would say
19 the first would be the central role of the Internet in
20 propagating retail investor fraud. We see many of these
21 schemes unfolding in very pernicious ways across the
22 Internet. Second, financial professionals who are bad
23 actors in the space. And I would say third, retail
24 investors who are purchasing products that aren't
25 necessarily suitable for them in terms of the complexity

1 and appropriateness.
2 Thank you.
3 MR. REDFEARN: Thank you. Secondly, I'd like
4 to introduce Cam Funkhouser from the Office of Fraud
5 Detection and Market Intelligence at FINRA.

6 MR. FUNKHOUSER: Thank you. First of all,
7 thank you, Chairman, for hosting this event and inviting
8 FINRA. We, too, share your concerns that retail
9 investors are our primary mission. In fact, FINRA's
10 mission statement is very simple. It's investor
11 protection and market integrity. And we have about 3,000
12 people who every day work to carry out that mission in a
13 variety of ways.

14 I oversee the Office of Fraud Detection and
15 Market Intelligence. That's a group we started about 10
16 years ago, designed specifically to be a centralized
17 intake group of all tips, complaints and other techniques
18 we use to identify fraudulent or potentially fraudulent
19 schemes and identify the perpetrators and gatekeepers of
20 these schemes.

21 One of the things we do in my office is we're
22 really a fusion group where we're bringing in a lot of
23 data through our surveillance, our electronic
24 surveillance of the marketplace, and also through the
25 human intelligence that we gather through tips,

1 complaints, field reports from our examining force and
2 other parts of FINRA, through interaction with my
3 colleagues at state regulators and the SEC. Our general
4 sort of concerns, and it's a broad question of retail
5 fraud, in my office, we see a very steady diet of
6 microcap pump and dump schemes. These are very large-
7 scale operations that are borderless. So both the
8 perpetrators of these schemes are potentially inside the
9 U.S. and outside the U.S. The victims of these schemes
10 are both inside the U.S. and outside the U.S. So it not
11 only impacts retail investors in the U.S. but potentially
12 globally.

13 But all fraud is local, right? So to the
14 retail investor, how you become a victim of fraud could
15 be through the Internet or through individuals, very
16 personal type of events. The Chairman just mentioned a
17 Ponzi scheme that was uncovered and confronted in the
18 last two weeks and this was done by really four
19 individuals and they were able to perpetrate this fraud
20 on a national basis right outside of Baltimore.

21 So for the victims of that fraud, I'm sure as
22 this case unfolds, it will show that the victims were
23 personally I guess approached in some manner to invest in
24 what was purportedly something that was good for them,
25 right? So with interest rates low, you have people who

1 can't get the kind of return on cash in banks or through
2 safe investments and they are approached with higher
3 interest rate returns and they're purported to be safe
4 investments. I mean, that's a very big challenge for
5 regulators and law enforcement.

6 So we work very hard to identify through the
7 tips and complaints we see about these types of schemes
8 and put them together at FINRA and send them to law
9 enforcement and the SEC. We work very closely with the
10 SEC's Office of Market Intelligence to identify these
11 schemes, the trends we see, the people we see. Last
12 year, my office sent about 850 referrals to the SEC. We
13 also worked with the state regulators in sharing
14 intelligence. In fact, in just the last couple of weeks,
15 my co-panelist Chris and I had a discussion about a
16 situation he was looking at and we had intelligence on
17 that situation which we happily share with our colleagues
18 in other regulatory agencies.

19 MR. REDFEARN: Thank you, Cam. Next, Chris
20 Gerold, Chief of the New Jersey Bureau of Securities.

21 MR. GEROLD: Thank you. And thank you,
22 Chairman Clayton and the rest of the Commissioners, for
23 welcoming us here and allowing us to be on the panel. I
24 am the chief of the New Jersey Bureau of Securities. We
25 are the agency in the state of New Jersey charged with

1 investor protection. And it's within the New Jersey
2 Attorney General's Office. I am also the chair of
3 NASAA's Enforcement Committee -- and for anyone that
4 doesn't know, NASAA is the North American Security
5 Administrators Association, which is comprised of all the
6 states as well as other securities regulators from Canada
7 and Mexico and some of the U.S. territories, as well.

8 So as Cam alluded to, the securities markets
9 and capital markets are global. But securities primarily
10 are sold locally. And state securities regulators tend
11 to be the cops on the beat. We're the closest to the
12 fraud, I guess, when it does happen with retail
13 investors. So our approach is pretty broad in that we
14 regulate the securities markets in our states -- New
15 Jersey in my case -- we have dealings with the
16 unregistered community, those selling Ponzi schemes,
17 there are straight misappropriation cases. We also
18 register and have authority over registrants, the broker-
19 dealers, as well as investment advisers. And states are
20 responsible for state-registered IAs exclusively, those
21 that have less than \$100 million. So in New Jersey, we
22 have a rigorous exam program to go out and make sure that
23 they are being compliant.

24 Some of the things that we're seeing, and I'm
25 sure we'll be touching on it later, some of the greatest

1 risks again are the unregistered area, the Ponzi schemes.
 2 One of the big ones that the SEC brought action against
 3 recently is a \$1 billion Ponzi scheme out of Florida,
 4 which was in bankruptcy in Delaware -- I'm forgetting the
 5 name as I'm sitting right here --
 6 MR. FUNKHOUSER: Woodbridge. It remains front
 7 of mind. Woodbridge.
 8 MR. GEROLD: Woodbridge, thank you. Forgive
 9 me. Woodbridge, where 10,000 investors were impacted and
 10 a billion dollars potentially lost. You know, those
 11 things, those cases, unfortunately are all too common.
 12 And so those are certainly things that are a risk to
 13 retail investors as well as classic pump and dump, Ponzi
 14 schemes and, of course, as you've stated, whatever the
 15 hot issue is at that point in time, whether it's
 16 cryptocurrency, tech or unicorn companies, fraudsters
 17 will latch onto that and use that to sell and defraud
 18 individuals and investors. So those are the areas we're
 19 in. Thank you.
 20 MR. REDFEARN: Thank you, Chris. Next, I'd
 21 like to turn it over to Jean Setzfand, SVP of AARP
 22 programs, AARP.
 23 MS. SETZFAND: Thank you. Thank you to the
 24 Chair and commissioners for your remarks on your focus
 25 and concern for the retail investors.

1 Hello, everybody. I'm Jean Setzfand from AARP.
 2 For those of you who aren't familiar with AARP, we're a
 3 membership organization protecting the interest of those
 4 over the age of 50. We are a membership organization
 5 that's mission based, as well as nonpartisan. We have 38
 6 million members that we represent.
 7 What we do for our members is really focused on
 8 providing sort of trusted resources focused on helping
 9 them prevent fraud. We also provide them guidance on
 10 where to report scams. They like to share their
 11 experiences and stories. But also, for those who have
 12 actually been victimized or have been impacted in some
 13 way by victimization, they actually want to actually join
 14 forces and combat fraud. So we actually have several of
 15 our members who are very active volunteers who really are
 16 out there fighting fraud.
 17 So for AARP and for where we sit as an
 18 organization, we are all about fighting for the older
 19 consumers as well as empowering them through resources.
 20 The ways that we go about that beyond education is, one,
 21 we hear a lot from our members. We hear a lot just in
 22 terms of the overall calls that we receive. But we also
 23 have a dedicated help line where we are -- we have
 24 volunteer staff who actually take incoming calls around
 25 fraud. And later on, I'll share some insights in terms

1 of what we hear about frauds in general but more
 2 specifically focused on investment fraud.
 3 Through our education, we always want to ensure
 4 that what we're providing content wise is basically
 5 current and relevant to our consumers, but also the way
 6 that we approach them. So we do a fair amount of
 7 research, understanding the profile of victims compared
 8 to the general population. So there's where I can also
 9 share some insights in terms of our research profiling
 10 older investors as well as vulnerable segments, like the
 11 military.
 12 But the key concerns in terms of what we see
 13 from AARP is for older individuals -- this is not going
 14 to be s shock to anybody -- they are targeted as victims.
 15 What we see in terms of evidence and reports, if we look
 16 at the Federal Trade Commission, the Consumer Sentinel
 17 Report, we know that older victims represent more than
 18 half of those victims. But the losses are far greater.
 19 So 53 percent of the victims who actually
 20 report are over the age of -- or older -- over the age of
 21 50. But the losses represent over 60 percent, 61
 22 percent. So as you actually age as a victim, the size of
 23 impact or size of loss continues to grow. And that
 24 continues if you actually look at the various age
 25 segments. So for those over the age of 70, they

1 represent 16 percent of the victims and yet 23 percent of
 2 the losses. So the impact is not only greater
 3 financially but it also emotionally takes a much greater
 4 toll amongst older consumers. One, they have less time
 5 to recover and also several of them are suffering
 6 diminished capacity.
 7 Beyond that, in terms of just the pure impact,
 8 other emerging trends that we see, there's been several
 9 discussions around technology and the pervasiveness that
 10 fraud exhibits right now. And what we hear from our
 11 consumers is a sense of apathy, quite frankly. So a lot
 12 more people are feeling like it's inevitable, it's just
 13 going to happen to me, I might as well brace myself
 14 rather than protect myself.
 15 So that notion, that emotional notion, is
 16 something that we have to really guard against. And we
 17 can't sort of -- and so a lot of, I think, what we do
 18 educationally has to be smarter and penetrate through
 19 that apathy.
 20 Another concern we have around sort of the
 21 emotions of people is the treatment of victims. And what
 22 we like to say, if we take a look at a victim who has
 23 been held at gunpoint, versus those who have fallen prey
 24 as a result of a bad action they've taken or feel like
 25 it's a bad action, they're treated very differently. So

1 the shaming of the victims is also another trend that we
2 want to be careful of. Because again, reporting wise, in
3 terms of what we see, particularly around the older
4 victims, is far lower, far less than the general
5 population. So we have to be very careful in terms of
6 how we treat victims so they can come forward and report.

7 Thank you.

8 MR. REDFEARN: Thank you, Jean. And last but
9 not least, by webcast, we have Nicole Iannarone,
10 Associate Clinical Professor at Georgia State University
11 College of Law. Welcome.

12 MS. IANNARONE: Hello. Thank you for having me
13 with you today.

14 I work with a clinic at Georgia State
15 University College of Law. We represent investors who
16 have already been defrauded or been harmed financially in
17 some way. We work with investors who have claims before
18 FINRA arbitration. They've typically worked with a
19 retail broker. And the things that we see are the same
20 things that we've seen for some time. While there may be
21 some new trends in products from time to time, we
22 continually see high-fee products being suggested to
23 retail investors. We are still seeing some REITs. We
24 see variable annuities. We see things like mutual funds
25 with high levels of fees.

1 MR. REDFEARN: Thank you very much, Nicole, and
2 we appreciate your efforts to join us even remotely.

3 So obviously, there is a lot of different areas
4 of fraud, retail fraud, that we're seeing that are of
5 great concern to us. And I think what I'd like to
6 explore first are just some of the -- you know, some
7 things that we should be looking at as the more recent
8 trends and some of the newer forms of fraud that seem to
9 be popping up. Because it does seem these things kind of
10 get reinvented in new ways depending on the times and new
11 technologies and so on.

12 So, Charu, maybe we can start with you. What
13 are some of like the key trends? You mentioned earlier
14 Ponzi schemes, pump and dump, churning. But if you had
15 to sort of say like the biggest areas that you're focused
16 on right now, what are they and what is sort of unique
17 about them in the packaging they're in today?

18 MS. CHANDRASEKHAR: Sure. So to your point, I
19 do think that a lot of traditional retail frauds are now
20 taking new forms and transforming with technology. The
21 first one that immediately comes to mind is the ICO
22 cryptocurrency space. And in terms of enforcement, the
23 Commission has been very active here in bringing cases
24 against multiple individuals and entities that have, we
25 allege, perpetrated these sorts of cryptocurrency-related

1 We also do some work with our state securities
2 administrator. And in that realm, we see a great deal of
3 unregistered investments related to things that are
4 important locally in our area and in our news. So
5 Georgia is a great state for movies and new development
6 there, so we are seeing more unregistered securities
7 being offered to folks related to the movie deals that
8 we're having in Georgia.

9 For what our clients see, when they come to us
10 in the clinic and what they tell us is that they trusted
11 the individual they were working with. They didn't
12 understand the products that were being provided to them.
13 They don't know what they cost. And a lot of the harms
14 come from that trust and a reliance upon the professional
15 to do the right thing for the individual.

16 So we can always provide legal assistance and
17 help out a consumer investor who can't otherwise obtain
18 an attorney to help them recover their costs. But we
19 prefer that they don't ever need our services at all. So
20 we do engage in some investor education and outreach and
21 we're really grateful for opportunities like this to talk
22 about how to prevent fraud with retail investors so
23 perhaps someday our services are not needed.

24 Thank you very much for the opportunity to join
25 you and I'm very sorry I can't be there in person today.

1 frauds.

2 To give you some examples, we can tick through
3 cases like the Titanium Blockchain case, the BitFunder
4 case, the AriseBank case, all cases involving either
5 cryptocurrency platforms or digital assets, where really
6 in an older era these might have been more traditional
7 offering frauds. But now with the advent of digital
8 technology and ICOs, they have become Internet-based and
9 digital frauds. And again, the Internet is front and
10 central here to recruiting investors and to perpetrating
11 false statements about the business lines and the
12 potential for expansion. So I think that would be the
13 first area.

14 The second area is one Cam touched upon, which
15 is the global proliferation of market manipulation
16 schemes, pump and dumps. As Cam put it well, the
17 Internet really is borderless and we've seen global rings
18 of market manipulators and fraudsters really deploy the
19 Internet and technology really to recruit victims
20 worldwide and to propagate false statements about product
21 lines and businesses across the globe.

22 MR. REDFEARN: Thank you, Charu.

23 So, Cam, again, for you, you mentioned a number
24 of different things. But how would you answer that in
25 terms of the most pressing things that you're seeing now

1 in the sort of packaging of these sorts of frauds?
 2 MR. FUNKHOUSER: Yeah, it's a good question
 3 that we probably could expand on for hours. I think it
 4 comes down to two kind of big things, right? So you have
 5 the people who perpetrate fraud do it really in one of
 6 two ways. They're either going to use this mass
 7 marketing campaign, right, to either send out spam
 8 emails, you know, even get fliers in the mailbox, you
 9 know, advertising some investment. You might even get
 10 text messages, you might see these things in social
 11 media. And so that impacts a whole bunch of people who
 12 have computers and cell phones, so that segment of the
 13 market.
 14 And then in terms of the other broad place is
 15 sort of the very personal, one on one, I'm going to
 16 target a senior citizen group, a church group, some sort
 17 of affinity group. And somebody somehow hacks into that
 18 person or that church or some source, some school or some
 19 affinity group and becomes the trusted adviser for that
 20 person. And then they recruit other people. And that
 21 can happen pretty frequently. And it's not easy to
 22 identify that wolf in sheep's clothing until you try to
 23 get your money back.
 24 You know, this is an industry where it's highly
 25 regulated, the securities industry, right? The SEC and

1 FINRA regulate registrants. But, you know, a lot of what
 2 we see in terms of victimization is by people who are
 3 unregistered, who are out there victimizing individuals
 4 in a variety of these schemes.
 5 And so it's important for us to send that
 6 message out that, you know, you've got to educate -- and
 7 this is what's great about this discussion is, one of the
 8 things we try to do is educate investors. And we have
 9 some great resources to -- so people can educate
 10 themselves to help prevent being victimized. And also --
 11 what also we encourage is if you see something, say
 12 something. Because many times, you know, the regulators
 13 are coming in from behind when, you know, these schemes
 14 start to unfold. Like we really appreciate any tips you
 15 might have of people that are, you know, sort of nosy
 16 neighbors type tips.
 17 I know, again, back to this Ponzi scheme that
 18 the Chairman talked about. I mean, one of the
 19 perpetrators of that had 25 cars in his driveway.
 20 Probably a pretty good sign he's either doing something
 21 well or maybe something else. So those are the types of
 22 very subtle pieces of data that might help head off a
 23 retail fraud.
 24 MR. REDFEARN: Thank you, Cam. So, Chris, from
 25 the perspective a state regulator, are the trends you're

1 seeing consistent with this or is there something you
 2 would add in terms of new packaging, new trends?
 3 MR. GEROLD: Sure. Actually, the NASAA and the
 4 enforcement committee specifically, their annual survey
 5 of all the state regulators and the types of actions that
 6 they've brought over the course of 2017, the trend that
 7 emerged from that is that, for the first time in three
 8 years, there were more actions brought against non-
 9 registrants than registrants. And that's -- like I said,
 10 that's a change over the last -- it wasn't that way over
 11 the last two years.
 12 I think part of that has to do with the number
 13 of cases that have been brought related to
 14 cryptocurrencies or I call them crypto-frauds, because
 15 they're not really against currencies, they're just cases
 16 involving crypto, blockchain and essentially frauds
 17 around cryptocurrencies that we've seen emerge the end of
 18 '17 and continued into '18.
 19 State securities regulators filed or have open
 20 investigations on more than 200 cases. We actually did
 21 Operation Crypto Sweep, which was a multijurisdictional
 22 effort to stop some of these online crypto frauds. I
 23 think it was very successful. But I think the biggest
 24 success to come out of it was to raise awareness and as a
 25 deterrent. Especially -- and I'll give the example, at

1 Christmas 2017, I'm sitting around the table and my
 2 mother starts talking to me about cryptocurrencies and
 3 everyone is getting rich. And right there, saying,
 4 there's a problem here. And, sure enough, over the next
 5 couple months, we did a great number of actions and
 6 hopefully have raised awareness that this is ripe for
 7 fraud.
 8 The other thing that Cam alluded to was a
 9 classic pump and dump. One of the things we've seen, and
 10 it's sort of evolved over time, is -- it started -- I
 11 don't know if it started but I recall in years past, it
 12 was someone calling up and saying, invest in a penny
 13 stock, buy it from me. With the Internet, it evolved
 14 into paid promoters, which we still see as an ongoing
 15 issue, where companies are paid to promote specific
 16 stocks and you see the price go up. And then insiders
 17 sell out.
 18 And then more recently, in the last two months,
 19 we've had three complaints along those same lines of
 20 people actually getting phone calls, seniors primarily,
 21 getting telephone calls promoting a stock -- not offering
 22 to sell it to them or for them to buy it from them but
 23 rather telling them to go on their online account, check
 24 it out, it's publicly traded, and buy it. And they've
 25 done that in a coordinated effort with both a website and

1 a paid promotion along with that phone call. And those
2 people did go out and buy it and within two months, the
3 stock price went way up and came crashing right down. So
4 that was something new.

5 And New Jersey is putting out -- actually NASAA
6 is working on an investor alert about that, about not
7 only the promotion via the Internet, which we've all seen
8 before, but along with personal telephone calls from
9 local phone numbers with -- I don't want to say very
10 common-sounding names. We've traced those calls to
11 overseas and it seems like it's an international effort
12 in manipulating a stock or a penny stock. So those are
13 some of the trends we've been seeing.

14 MR. REDFEARN: Very interesting. And it is
15 particularly notable that this trend of sort of ICOs and
16 cryptocurrencies has been coupled with the observation
17 that more non-registrants than registrants are the
18 problem now, right? And this has been a big area of
19 focus for Chairman Clayton and the Commission as we try
20 to get our arms around this new sort of asset class, some
21 of which may be okay but much seem to be kind of
22 problematic.

23 MR. FUNKHOUSER: And also, Brett, on that note,
24 you have the direct cryptocurrency issue. We also
25 observe stocks that claim to be somehow tied into a

1 cryptocurrency. In effect, FINRA just brought its first
2 case involving a registered person who was involved in a
3 cryptocurrency issue. You can see the public
4 announcement on that. But it's not only the
5 cryptocurrency, but that evolved into some sort of
6 microcap pump and dump scheme, where they just latch onto
7 the cryptocurrency.

8 CHAIRMAN CLAYTON: I'm holding my tongue. I
9 want to comment on all of this. But I'm going to let
10 Jean and Nicole comment before I make a comment. Thank
11 you.

12 MR. REDFEARN: Okay. So, Jean, it's
13 interesting. We're hearing about, you know, sort of the
14 crypto and a lot of the issues that are coming out across
15 from the Internet. Are you seeing with seniors a very
16 similar trend? Or is there something different or unique
17 you're seeing for your constituency?

18 MS. SETZFAND: I don't think we have enough
19 volume to actually make any comments around the
20 particular types of investment trends or the use of
21 different product tactics. But one of the things that we
22 see is consistent with what Cameron touched on, what
23 Christopher touched on, which is the mode of fraud is
24 very much still the same, which is by phone.

25 I think technology has allowed the expansion of

1 the phone use with robocalls and better targeting, per
2 se. But that's still the main form of loss, based on
3 what we hear. So in terms of our sort of helpline, we
4 have seen -- our top 10 frauds, investment fraud is
5 eighth in our rank. It's roughly about 3 percent of the
6 calls we get, and we get roughly about 20,000 calls a
7 year just on our fraud line.

8 From a profile standpoint, I think this is
9 relatively well known as well. The typical victim tends
10 to be older. So our victims are 74 years in age, they
11 tend to be more male than female, so 59 percent are male.

12 The losses involved are relatively great. They're over
13 \$100,000 is what they report to us. And again, the most
14 common method of contact is inbound phone calls. They
15 are also reporting online and in-person contact as well.

16 But that's kind of just what we see. Over and over
17 again, phone is by far, I think, greatly used. Emails as
18 well. More so, the expansion and use of technology-based
19 ways of reaching people more through the phone base
20 still, unfortunately, still a bad mode.

21 The other thing I wanted to pick up on in terms
22 of the profiling as well, we are looking at sort of more
23 of the psychological behavior. So how certain victims
24 have a different view or perspective on investing. And I
25 think there is -- the newness factor of products I think

1 speak to this whole notion that, from the victim's
2 perspective, the psychological mindset that we see more
3 so in victims versus nonvictims is that they really value
4 wealth accumulation. So one, some of the most important
5 things to them in life is achieving or acquiring money
6 and wealth. And they are also kind of very open to sales
7 pitches. So they keep their eyes and ears open for
8 emerging new investments.

9 This is no surprise, no shock. But again,
10 these are sort of, again, typical profile psychologically
11 of victims. And I think whatever new factor, whatever,
12 whether it's credible or not, fraudsters know that they
13 can use that to kind of prey on victims.

14 MR. REDFEARN: If investment fraud is eighth,
15 what's -- what do you have as first?

16 MS. SETZFAND: Imposter frauds, like
17 grandparents, or IRS scams. That's definitely one,
18 that's 11 percent. That's actually tied with
19 sweepstakes, prizes, lottery. And then most recently, I
20 think we've seen more around tech scams, computer
21 viruses, malware, software, phishing also is fourth. So
22 technology wise, three and four are tech scams, phishing.
23 Fifth is identity theft. Six is fraudulent sales.

24 Seventh, home repair. And then eighth is investment
25 fraud. Followed by auto sales/repairs and real estate

1 timeshares as tenth.

2 MR. REDFEARN: That's really interesting. And

3 I'm sure on the educational side, it's good to let people

4 know that when you hear you just won the sweepstakes or

5 you just won a lottery or any of those things, that, you

6 know, obviously, beware of those.

7 MS. SETZFAND: Absolutely.

8 MR. REDFEARN: When you said grandparents, what

9 was that one?

10 MS. SETZFAND: So a lot of grandparents are

11 preyed upon by scammers where the fraudster will pretend

12 to be a grandchild, usually stuck in a foreign country,

13 saying that they've either lost their passport or they've

14 been kidnapped and they need ransom money. So they need

15 sort of a wire transfer. And unbelievably so, a lot of

16 grandparents do fall for that.

17 And with the advent of social media, you can

18 get a lot of information about your family through

19 Facebook and other means. And that's why I think it's

20 become more and more rampant.

21 MR. REDFEARN: Great, thank you.

22 So Nicole, out in Georgia, is it the same kind

23 of stuff? Or is it something a little bit different in

24 terms of what you're hearing from the folks who are

25 reaching out to your folks?

1 MS. IANNARONE: I think we have a little bit of

2 a difference in that it takes folks a couple of years to

3 get to us after they've realized that they lost something

4 as a result of a scam. But we are seeing along the same

5 lines as Jean the same methods of communication that have

6 previously been used. So telephone is definitely one

7 that we see, as well as getting to know the community and

8 the individuals within it before putting a new product or

9 investment out there.

10 One that we're beginning to see that I hope is

11 not a trend, and it comes up more quickly because the

12 losses come up more quickly, is in currency trading. We

13 are beginning to get calls from individuals who are

14 engaged in currency swaps and really should not be in

15 them. They are very unsuitable investments for the

16 individuals who are reaching out to us.

17 I've spoken with another clinic who also has

18 seen something like that. So we're going to hope that

19 that is not a continuing issue, simply because it is so

20 easy to quickly lose money within that trading. And it's

21 usually done by the investor themselves.

22 MR. REDFEARN: So that's somebody reaches out

23 by phone or by email and they say I have a currency

24 trading strategy that is great and you're likely to make

25 a bunch of money doing this? And they get them into it

1 and somehow or another, they are able to just defraud

2 them and take their money while they're trying to run

3 these strategies?

4 MS. IANNARONE: Yeah, the trades happen very,

5 very quickly in the process. Sometimes, I've heard from

6 another claim, that one of them involved, well, learn

7 before you start investing your money. We'll set up a

8 dummy account for you so you can trade in that account.

9 But perhaps the dummy account isn't as easy to discern

10 from the regular account with the investor's own money.

11 So they start practicing through what really seems to be

12 like play gambling and it can lead to a loss of a

13 significant amount of money very, very quickly.

14 When we get currency trading calls at our

15 clinic, we are looking at someone losing 90 percent of

16 what they had invested, usually in a few months, because

17 they start out thinking they're going to do okay, they

18 lose some money initially and they are trying to make it

19 up, there are significant losses later. And after a

20 while, pretty much all of the investment is gone.

21 MR. REDFEARN: Thank you. I want to take a

22 minute to look at a couple more -- the details on some of

23 the specifics to see if we can understand both how they

24 work and what people should look out for. And the Ponzi

25 scheme has come up a lot and people know of a lot of the

1 big, more famous Ponzi schemes, but Charu, can you just

2 help? Give us an example of another -- yet another Ponzi

3 scheme is out there. What does it look like? What is an

4 example? How do people see the footprint of a Ponzi

5 scheme coming their way?

6 MS. CHANDRASEKHAR: Sure. So the Ponzi

7 schemes, to Jean's point, are perpetrated both through a

8 lot of traditional means, for example, outreach via phone

9 or personal contact, but also some online Internet

10 recruiting. And this is a space, where we in partnership

11 with our Office of Investor Advocacy and Education, have

12 been very active in reaching out to warn people about the

13 red flags of Ponzi schemes. We see a lot of the same

14 problematic indicia, such as promises of high returns,

15 promises of guaranteed returns, a sense of urgency that

16 people need to get in and invest right away or the

17 opportunity will vanish. So a lot of the same high-

18 pressure sales tactics with reassurances of large, large

19 payouts at the end.

20 And we've also been, as both the Chairman and

21 you noted, the Commission has been very active in

22 bringing cases in this space, most recently the \$345

23 million case in Baltimore, the Woodbridge case, the Life

24 Pay case, the First Nationle case, a lot of the same

25 methods of recruitment are being used over and over again

1 and it's an area we are very much focused on in terms of
2 raising investor awareness.

3 MR. REDFEARN: Thank you. So Cam, you
4 mentioned affinity fraud, affinity groups. You said it
5 could be church, it could be school, it could be
6 military. How do those work? How does that targeting
7 happen?

8 MR. FUNKHOUSER: Yeah, again, these are some of
9 the, I guess, worst of the worst type offenders. They
10 somehow integrate themselves into a community, either
11 through a church or another type of, you know, retiree
12 group, it could be a cultural community. And, you know,
13 so in these types of schemes, it's very personal. You
14 go, you show up at the meeting, you find someone who is
15 vulnerable. You explain to them how you can help them.
16 Generally, people aren't really trying to hit the
17 lottery. They're trying to get some type of return for
18 the humble money they have and this person says, you
19 don't want to trust the people on Wall Street, those guys
20 are all thieves. Let me tell you about a very special
21 investment that I have. Right?

22 So, let me give you an example. We had one
23 case that came in through our whistleblower program. It
24 was -- actually, the tip came in by somebody that FINRA
25 had barred for a securities fraud violation. And he

1 said, I'm working at this place that even I can't work
2 here. Right?

3 And it turned out that this person was working
4 with an individual who was targeting older women who
5 lived alone who were on fixed incomes up in Staten
6 Island. And he would personally pitch them that I've got
7 a real estate investment that is going to return 6 to 8
8 percent to you. You're only getting 1 percent in your
9 CDs. What I'd like you to do is take out a second
10 mortgage on your house or a first mortgage on your house
11 if it's fully paid off, take the equity out of your home.
12 You can get a mortgage at 3 percent. Invest all that
13 money with me and we're going to turn around and you're
14 going to make 8 percent and you can pay your mortgage and
15 you will have a profit.

16 This would -- the youngest victim in this
17 scheme was like 80 years old. And, of course, this guy
18 had whole display of plans and photos, all rigged to make
19 it look like it was a legitimate investment.

20 Fortunately, we were able to assess the
21 situation. It was obviously at the highest threat level.

22 And we got that to the FBI in New York, who went in and
23 ultimately busted it and this perpetrator of this is
24 currently incarcerated.

25 But that is the type of off-the-grid type of

1 scheme that doesn't show up on our surveillance reports,
2 doesn't show up, you know, in any type of data analytics.
3 This is very personal. And as my colleagues have
4 pointed out, the victims of this scheme are really
5 retirees who trust this person. And, in fact, in many
6 ways, they don't realize they're being defrauded. And
7 they like the person. And so when you meet them, the
8 Ponzi schemers, they're very likable people. They put on
9 the charm offensive and you trust them. So you don't
10 realize you're being defrauded. In fact, you willingly
11 give your money and then you recruit -- the bad guy there
12 sort of counts on one of the victims to recruit more
13 victims.

14 So it's a very dangerous situation for retirees
15 and other retail investors. It's also incredibly hard to
16 detect for regulators.

17 CHAIRMAN CLAYTON: Hey, Brett, do you mind if I
18 jump in?

19 MR. REDFEARN: No, please. Please. I welcome
20 that.

21 CHAIRMAN CLAYTON: First, I want to thank, you
22 know, our friends in FINRA, the states, AARP, Nicole,
23 what you do. You know, this is a partnership. We have
24 limited resources. And, as you note, particularly in
25 some of these retail investment frauds, acting quickly is

1 very important. Ponzi schemes grow for all the reasons
2 you say, and we need to do that.

3 I just want to make some observations. They're
4 observations that come out of today's presentation and
5 actually when I was in Georgia, Nicole and I had a chance
6 to spend some time together, and how we look at
7 prevention or how I'm looking at prevention.

8 Where are there indicia of legitimacy that are
9 illegitimate? So where do people see indicia of a
10 legitimate investment when they shouldn't? So, you know,
11 I just want to give you some current examples.

12 Crypto asset trading on an unregulated Internet
13 platform looks like an S&P 500 stock trading. Nothing
14 could be farther from the truth. The opportunities for
15 manipulation, for fraud, are -- we all know. But it
16 looks the same.

17 Penny stocks, they have tickers. They look
18 like an S&P 500 stock. Financials may be, you know,
19 incredibly stale. Trading may be incredibly thin.

20 Let me give you an example. If I can call a
21 bunch of retail investors and their individual online
22 actions -- call a bunch of retail investors and say, hey,
23 this is a good stock, and their individual actions can
24 change the price of that stock, that's nothing like the
25 kind of stock that they're thinking it is, right? I

1 mean, if the trading of a few retail investors can move
 2 the price significantly, that's not a stock that should
 3 look like, you know, a large-cap stock.

4 Another thing. Unregistered investment
 5 professionals, they look like registered investment
 6 professionals. We all know, because we sit through the
 7 cases every week, 500 of them a year, if you're in
 8 unregistered land, the risk of fraud -- it's orders of
 9 magnitude higher. We have bad actors in the registered
 10 world. We seek to identify them and get them out.
 11 That's, you know, FINRA, what you spend a lot of time,
 12 you know, doing, what we spend a lot of time doing. But
 13 once you move into unregistered land, you know, enough
 14 said.

15 One of the hardest things is taking confidence
 16 in the confidence of others. That's a really tough nut
 17 to crack but it is an indicia of legitimacy. Smart-
 18 looking people, friends of mine are investing, I take
 19 confidence from that. I think about that one. I'm not
 20 as sure about how to crack the code on that.

21 So what comes out of all this from my
 22 perspective? How do we help investors? We know what to
 23 do in Enforcement, we're trying to get better. How do we
 24 help investors? Key questions. Are you registered? You
 25 know, if you're not registered with the SEC or the states

1 as an investment professional, you really need to take a
 2 pause. Like every potential investor should know that.

3 Is the investment registered? If it's not
 4 registered, it doesn't mean it's bad. But you need to
 5 take a pause, you really need to take a pause.

6 A question I love to ask, how much of my money
 7 is going to work for me? To Nicole's point, if there's a
 8 high fee, there's a high carrying cost, there's, you
 9 know, a back-end fee, no.

10 Last question, and then I'll pause, are there
 11 audited financial statements anywhere around this
 12 investment? I have not seen, you know, a better question
 13 in terms of separating the speculative from the less
 14 speculative.

15 So those are my thoughts. I wanted to share
 16 them with the group. And, you know, I really appreciate
 17 your spending the time. Prevention is key here and we
 18 are looking at all of our rules, trading rules,
 19 disclosure rules, registration rules. You know we are
 20 pursuing regulation, best interest, with an eye toward
 21 greatly reducing the opportunity for retail fraud. So
 22 thank you.

23 MR. REDFEARN: Thank you, Chairman.

24 I think that that set of questions and set of
 25 issues sort of provides an opening for us to just

1 transition just for a second to just sort of -- I want to
 2 throw something out generally to whomever wants to answer
 3 it. Which is that, so the Chairman just listed four
 4 questions that we think people should be on the lookout
 5 for that will help them to basically have a little bit of
 6 a screening to determine whether or not they actually
 7 want to take their money in that direction.

8 Let me just ask, is there anything -- maybe
 9 since we just finished, Chris, is there anything else you
 10 would add to that list? What other things do you think
 11 we should tell people to really kind of think about
 12 before they put their money somewhere?

13 MR. GEROLD: Well, I think the Chairman's
 14 questions kind of run into the second and third part of
 15 today's program in terms of both investor education as
 16 well as finders and really private offerings, which some
 17 of those questions makes -- scares you when it comes to
 18 private offerings and who those are being sold to.

19 In terms of what we would add to that, we in
 20 New Jersey have had a long-running initiative, Check
 21 Before You Invest, which encourages anyone before they
 22 sign up with an adviser or buy any securities from a
 23 broker to go on BrokerCheck, which FINRA has and is
 24 readily available, to go on there and check their
 25 background out and make sure they're registered.

1 You know, one of the things that we always
 2 teach in our investor education classes is don't invest
 3 in anything that you don't fully and completely
 4 understand. I take it one level even above that, is
 5 don't invest in things that you don't use. That's my
 6 philosophy. But, you know, others have a different one.

7 In terms of, I guess, what to add to that, I
 8 think some of the questions that he encourages investors
 9 to ask are fantastic. And I wish every investor would
 10 have done that.

11 Going back to what Cam touched upon was -- and
 12 what I have found is people only do business with other
 13 individuals that they know, like and trust. And
 14 naturally, almost every victim that we've ever spoken to
 15 is, oh, he's a great -- I'm going to say guy. It's
 16 traditionally men but we have some bad actors that are
 17 women. No, he's such a nice guy, we have complete
 18 confidence in him.

19 And then in other cases, for instance, when we
 20 investigated Woodbridge, for instance, we spoke to a
 21 number of individuals and they said, don't screw this up.
 22 We're getting 5 percent interest, the bank is paying us
 23 less than 1, don't screw this up on us. They drank the
 24 Kool-Aid, I mean, that's how we refer to it in our
 25 office. And once someone has bought into the product or

1 the individual, it is extremely hard, especially if
2 they're continuing to get paid the commission -- excuse
3 me, not the commission but their interest or their coupon
4 to back them away from that and say, well, there are
5 problems here. And oftentimes, they don't come to that
6 realization until after a case is filed. Or even,
7 sometimes after the case is filed, the bad actor will
8 blame the regulator and say, hey, they're the ones who
9 screwed this up; you'd still be getting paid otherwise.
10 But those are, you know, the problems we run into.

11 The Chairman did offer some fabulous questions
12 that all investors can and should be asking. And that's
13 going to touch upon our investor ed on how we get that
14 word out.

15 MR. REDFEARN: I will just ask one other thing,
16 Chris. Earlier, you mentioned paid promoters and we
17 haven't talked about that much. So I just want -- like,
18 the paid promoter type scheme, just tell me a little bit
19 more.

20 MR. GEROLD: Yeah, so what I was referring to
21 was not so much the individual paid promoter but paid
22 promotional ads, where they go out to these companies
23 that have email lists and then go by various names, Penny
24 Stock Locks or Guaranteed Penny Stock Returns or what
25 have you on the Internet. These are typically paid for

1 by the issuer of a penny stock and they will send out
2 newsletters touting the stock.

3 Now, technically, it's legal. I mean, the SEC
4 has guidance on it. As long as they're disclosing -- as
5 long as they're not saying anything false -- and we
6 generalize, so anyone, go check out the rules. But as
7 long as they're not saying anything false, as long as
8 they're disclosing they're being paid, the amount they're
9 being paid, they will send out email blasts to hundreds
10 of thousands of people. Actually, the more email
11 addresses they have, the more they'll get paid for their
12 promotion of it. And they'll say things such as, if you
13 bought at yesterday's opening of 1 penny and sold in the
14 afternoon and sold in the afternoon when it traded at,
15 you know, 2 cents, you would have made a 100 percent
16 gain, you know, exclamation point, underline. And
17 they'll go on with this, usually in conjunction with some
18 news release by the issuer about some contract they're
19 about to enter or some other news, depending on how
20 nefarious or how far they want to stretch the truth in
21 terms of how they frame the story.

22 That's what I meant by paid promoters. Really,
23 internet promoters, newsletters and the like. And then,
24 going one step further, which we've seen lately, are
25 actually the phone calls coming in promoting the stock

1 for individuals, typically seniors, to go out and buy
2 that security in their online account.

3 MR. REDFEARN: Thank you. Jean, just kind of
4 continue on this trend. One of the things you had
5 mentioned in your sort of top list was identity fraud.
6 And can you just describe a little bit more in detail
7 about how that works and how that works to defraud
8 investors?

9 MS. SETZFAND: So identity fraud is -- or
10 identity theft, quite frankly, fraud is all about
11 stealing somebody's identity through various means. A
12 lot of it can come in different forms.

13 So one that we really focused on a lot was the
14 issuance of the new Medicare cards that came out earlier
15 this year. There's a process that you go through or
16 actually don't have to go through. But fraudsters will
17 convince you that you do have to go through a process,
18 relinquish information about you, and then from that they
19 claim -- they take your account information, identity,
20 and then start to essentially either steal your money or
21 use it to issue a fraudulent IRS tax return form, so on
22 and so forth, a whole host of different things. But they
23 take your identity, it wreaks havoc in your life. So
24 that's essentially another form of fraud.

25 But I also wanted to comment on the other

1 questions that you should ask. One of the things that
2 strike me is we're asking the consumers as well as
3 potential victims to do quite a bit. And yet, fraudsters
4 don't have to do a lot to steal money. So they make that
5 process of taking money away really easy and yet we make
6 the preventative action relatively hard.

7 So I think it's really important for us to list
8 out preventative actions that people can take, ask the
9 right questions. But also let's think about how we can
10 make this easier in terms of protecting people. Are
11 there places that, as we get into this world where Amazon
12 is going to make our lives so easy, we don't have to go
13 anywhere anymore, how do we actually make prevention that
14 way, too?

15 So that's something that strikes me is the
16 field that quite frankly isn't fair to consumers. They
17 are -- it is a little bit of a David and Goliath. So how
18 do we even that a little bit further and make the process
19 around prevention far easier for them, rather than
20 putting the onus and responsibility purely on consumers?

21 MR. REDFEARN: Thank you. Nicole, we've talked
22 about a lot of different things but I wanted to just make
23 sure that we touch upon actual registered securities,
24 initial offerings or secondary offerings a little bit
25 more, moving into that space. And I'm wondering if you

1 can -- you know, including microcap stocks. So I'm
 2 wondering if you have any insights from your
 3 constituencies in that area for us.
 4 MS. IANNARONE: I'm not sure I have anything
 5 more than really anecdotal evidence on what we're seeing
 6 from our clients and the people who are coming to us.
 7 Really, we are seeing investments that, if I could
 8 classify them generally, that the investor does not
 9 understand, can't understand, and trusted somebody else,
 10 and that's why they're in them.
 11 So they might have asked some of the questions
 12 that the Chairman set forth. They developed a trust
 13 relationship with somebody. And they are in an
 14 investment that they cannot explain. They don't know
 15 what a REIT is. Sometimes, we hear some accents in
 16 Georgia. And we hear about the names of the products
 17 like "Areat," that they believe they have, and we're
 18 looking for a legal document like a writ. And we realize
 19 what they have is a real estate investment trust. It's
 20 not something that the client can explain, they wouldn't
 21 have the background necessarily to ask questions about to
 22 understand it and know whether it's something that's
 23 suitable for them.
 24 Added to the Chairman's list of questions, I
 25 might ask, what do you get from this? How much are you

1 being paid and by whom?
 2 It's surprising to me how many of the people
 3 who come to us actually believe that they haven't paid
 4 anything for the advice that they have been provided, or
 5 that the products that they're purchasing come with no
 6 fees at all.
 7 And I think finally, convincing victims and
 8 encouraging them to come forward early and asking
 9 questions is really very, very important. Don't just
 10 look at your account statement and say, is my money still
 11 there? Ask questions about, what's going on? How is
 12 this working? Why is this good for me? How would I
 13 explain this to my family members? Encourage them to
 14 find some way to talk to their friends and their family
 15 about it to make sure that it is the right investment for
 16 them.
 17 MR. REDFEARN: Thank you. I want to get for a
 18 second to the question of who are these people? Right?
 19 So, Cam, you mentioned it's somebody with charisma and
 20 very likable people, but there's a lot of, you know,
 21 different flavors that we may be running into here. Are
 22 we talking about just straight up con men, fraudsters?
 23 Are they typically securities professionals gone bad,
 24 other sorts of bad actors from overseas markets?
 25 Charu, can you give us some sense of -- and

1 answer the question of who are these people? Where would
 2 you point us to look?
 3 MS. CHANDRASEKHAR: Sure. As Cam and Jean and
 4 Nicole all noted, there are often cases in which the
 5 frauds are perpetrated by people who are known to and
 6 trusted by the victims. For example, there was a case
 7 the Commission charged earlier this year involving a very
 8 prominent pastor who allegedly lured seniors into an
 9 entirely fraudulent scheme involving -- involving false
 10 bonds and told them they were worth millions. There are
 11 other cases where you have members of certain religious
 12 communities or ethnic communities and really affinity
 13 frauds, people who are really members of the community,
 14 who are capitalizing and exploiting that trust and that
 15 compassion and care really to defraud people who are
 16 known to them.
 17 And, as Cam mentioned, I think in many cases,
 18 the fraudsters are well known and well-liked members of
 19 the community and they use that, that hook, to their
 20 advantage.
 21 I think in other cases, we see people who are
 22 portraying themselves as somehow skilled professions,
 23 where there is a seeming inequality in the amount of
 24 knowledge or competence -- to Chris's point -- and taking
 25 advantage of that seeming differential to lure in

1 victims. So I think it comes in a couple of different
 2 flavors. But I think in all of these cases, it's really
 3 exploiting a relationship of trust and confidence to
 4 reign in victims.
 5 MR. FUNKHOUSER: Let me follow up on that, too.
 6 I think, you know, one of the interesting things about
 7 the Internet, while we talk about how the bad guys can
 8 exploit information, you too can do your own research on
 9 people. And so many of these perpetrators, the
 10 individuals that you come into contact, will claim to
 11 have educational backgrounds that can be checked out,
 12 they'll have work histories that can be checked out. And
 13 a simple Google search, just a simple Google search could
 14 uncover a whole lot of information about the person that
 15 you're about to entrust your money with. And I think
 16 that's one of the simple things people can do.
 17 Don't believe what you're reading or seeing.
 18 Check it out. And, like I said, sometimes you will see
 19 even a simple search of the person's name plus fraud
 20 might return some sort of commentary on a blog or some
 21 other type of news story that might be of interest to
 22 you. That's a very simple thing to do for individuals.
 23 Also, you know, for FINRA, I mean, Chris
 24 mentioned our BrokerCheck. If it's a licensed person,
 25 you can get the whole history of the person if they're

1 registered. But mostly the trouble, most of these
2 schemes, the vast, vast majority are perpetrated by
3 people who are working in some unregistered capacity but
4 will claim to be registered in some ways, and you can
5 check that out, too.

6 MR. REDFEARN: Yeah, Chris, you did mention
7 BrokerCheck before. I mean, do you think many people are
8 in the habit of saying, oh, let me check BrokerCheck and
9 see what the situation is here? Or do you think that's
10 just something that's just not happening?

11 MR. GEROLD: The short answer is, no. I don't
12 think hardly anyone does. I don't want to say anyone.
13 I'm sure millions of people go on BrokerCheck, just not
14 nearly in terms of percentage the number that should be
15 going on there and checking out the person they're giving
16 their money to.

17 And I really thought Jean asked a very
18 interesting question on why is it so easy for the bad
19 guys and so hard for the investors? It's a little
20 different perspective than we normally -- or normally the
21 way I look at it. But I think it's a very interesting
22 question. I know FINRA has passed some rules recently
23 about disbursing money to -- excuse me, I'm forgetting
24 the rule number.

25 MR. GEROLD: Yes, thank you.

1 where it then requires the -- it's related to all
2 financial professionals but certainly broker-dealers as
3 well as IAs, in those situations to notify state
4 regulators and adult protective services of that
5 potential exploitation. And about two years ago, some
6 states started enacting it. I know Alabama and Texas,
7 for instance, both have that as part of our enforcement
8 survey. And that is actually starting to yield results.

9 I know Texas got 200 additional reports as a
10 result of -- approximately 200 -- of that act that they
11 passed. And that act actually has the support of both
12 industry as well as advocacy groups, because it does
13 provide a safe harbor for not disbursing money and for
14 reporting senior exploitation or vulnerable adult
15 exploitation. And it's starting to yield results, where
16 investigations are being opened and cases being
17 prosecuted.

18 So it is some effort to address the problem.
19 Hopefully, more jurisdictions will be passing it in the
20 near future. Hopefully, we'll hit a tipping point where
21 eventually all jurisdictions pass it. Because that
22 information is critical and it does give us one more tool
23 to identify bad actors that are in the space.

24 MR. REDFEARN: Indeed. And we will be in our
25 panels later spending a lot of time on how do we

1 MR. FUNKHOUSER: It's FINRA Rule 2165. And we
2 took some -- not to hijack what you were just saying, but
3 so I can tell you about the rule, you know, you talk
4 about what can you do to prevent it. Well, FINRA took
5 sort of an offensive action and empowered our registered
6 brokers across the country to, in certain circumstances,
7 and I'll give you the short story here, is when you see
8 potential financial exploitation by someone who is senior
9 or of diminished capacity or of some sort of vulnerable
10 type of customer, they can -- they can intervene and
11 prevent certain transactions from happening within their
12 account so they can be checked out.

13 And we have also asked all of our registered
14 persons in firms to get a trusted adviser or trusted
15 individual assigned to the account so that if, you know,
16 you mentioned your mother or grandmother and my mother-
17 in-law is always getting these calls. Before they give
18 up the information or do the transaction within the
19 brokerage account, the registered rep in the firm can
20 contact the trusted person on the account and get them
21 involved, so it's done, you know, sort of at a family
22 level or a trusted adviser.

23 MR. GEROLD: No, I appreciate that. And states
24 have actually gone one step further with that. I think
25 13 jurisdictions have enacted the NASAA Senior Safe Act,

1 hopefully make it a little harder for the bad guys to,
2 you know, make it not so easy for them and harder for the
3 investor. I think that's part of the intent there.

4 I guess, Jean, I just want to follow up with
5 the same question in terms of who are these people? Now,
6 obviously, they're coming in, in many cases, you talked
7 about through the phone or roboadialing. I don't know if
8 in that vein then it's that easy to know who are these
9 people?

10 MS. SETZFAND: Right. I think it's been stated
11 before but it's probably more bad actors than registered
12 reps who are perpetrating the really egregious acts. But
13 even to kind of build on Chris's point there, what we're
14 trying to do is in the course of any transaction, we're
15 just trying to make sure that investors have the right
16 tools to make the best decision. So we've actually
17 teamed up with NASAA to build an ask-your-investor --
18 interview-your-investor tool. So what are the sort of
19 standard questions you should ask, regardless? Because
20 again, going back to the profile of victims, we know that
21 victims are actually more investor savvy, are making more
22 transactions. So probability wise, they're kind of in
23 the course of both good and bad, because they're in the
24 vein of action, and therefore they fall prey.

25 So what we want to do is ensure that they're

1 taking -- taking the right steps to at least ask a set of
2 basic questions. A lot of the questions the Chair, Chair
3 Clayton, outlined. And that also brings them and
4 presents them the easy access to BrokerCheck, quite
5 frankly. So what we want to do is have them ask a set of
6 questions and then at the end of that whole process,
7 ensure that they're actually looking and making sure that
8 the person they're talking to is a registered rep with no
9 issues, so on and so forth.

10 So if that helps. Again, we're just trying to
11 get people in the sort of practice of doing these things
12 regularly.

13 MR. REDFEARN: It sounds like a good thing
14 there.

15 So Nicole, just again from your perspective, I
16 don't know what kind of insight you would have in terms
17 of who are the people behind the, you know, the schemes
18 that the folks you're dealing with are experiencing?

19 MS. IANNARONE: So we don't deal as much with
20 the things in the unregistered world and with the bad
21 actors in that sense. I can say, in regard to the
22 earlier question, do a lot of investors automatically do
23 a BrokerCheck? No, they don't. In our experience,
24 someone who has come to us has typically not done a great
25 deal of research on the professional who is registered

1 that they will be working with. And in some cases, in
2 looking at a BrokerCheck, they would have been alerted to
3 a great number of disclosure events that might have
4 caused them to ask some questions at the front end as to
5 whether this is someone they felt comfortable working
6 with. So the more that we can do to continue to get
7 investors to run a quick Google search, as Chris and Cam
8 said, or to run the BrokerCheck and see if there's
9 information out there that might prevent -- might give
10 them pause as to whether they want to work with the
11 individual or at least give rise to some questions about
12 what the individual has to say about those past events
13 could help prevent some situations that many of our
14 clients have dealt with.

15 MR. REDFEARN: Thanks. So probably just a
16 couple more questions before we wrap up.

17 I want to turn back for a second to this area
18 of cryptocurrencies and digital assets, because it is so
19 new and it is seemingly on the rise. And, you know,
20 notwithstanding the fact that certainly there will be
21 digital assets or cryptocurrencies that are out there
22 that are, you know, fine and legitimate in their own
23 right, presumably. But what is your take right now on
24 this space, on cryptocurrencies and digital assets? And
25 how do you think that people should sort of be thinking

1 about, you know, if some opportunity is presenting itself
2 in that space. Charu?

3 MS. CHANDRASEKHAR: So I think people should
4 interrogate cryptocurrency investments in the same way
5 they would look at a traditional bricks-and-mortar
6 investment. And many of the red flags we've seen in the
7 classic frauds such as Ponzi schemes still apply to
8 online investments. Promises of high returns, promises
9 of swift returns, guarantees that there won't be any
10 losses, pressure to invest, these are all the same old
11 techniques that are being imported into the
12 cryptocurrency and digital asset space.

13 Really, it's -- I would say encourage investors
14 to stay on alert for these claims that have migrated to
15 the online and the Internet context and the
16 cryptocurrency context. So it's really in some ways, I
17 think the expression, old wine in new casks really
18 applies to a lot of the Internet and crypto frauds. And
19 I would encourage, as all of our panelists have said,
20 people really should be doing the same sorts of diligence
21 about the promoters in these investments, about the
22 actual business plan of the investments. A lot of these
23 investments have so-called whitepapers. People should
24 really read those, think through the claims in those and
25 generally remain on alert in the space of these

1 investments.

2 MR. REDFEARN: Same question, Cam. And is it -
3 - do you think that in that space, where in terms of the
4 related fraud activities, we're at the bottom of the
5 curve, at the middle of the curve? Or do you think that
6 this is still a pretty rapidly growing trend?

7 MR. FUNKHOUSER: Well, I've been doing this a
8 long time and I never think there is a finish line to
9 fraud, right? So I would -- that would even be
10 speculating on the answer, forgetting the investment
11 itself.

12 So I think it's always a challenge when there's
13 something new out there that's sort of unknown, and so
14 investors want to get in on it, right? I missed the .com
15 era, I -- you know, there's always this, I'm going to
16 miss this next investment. So the currency itself, I
17 think, is
18 -- it's unknown because there's -- it's really
19 unregulated in many ways. So that's hard to predict.

20 But what I do know is that most people know
21 nothing about it. So how -- for the retail investor,
22 from where I sit, one of the most dangerous places is,
23 you know, somebody calling them or getting pitched.
24 Here's a fund that invests in digital currency. Here's a
25 stock that's involved with currencies. Because that's

1 what retail investors do understand. They have invested
2 in stocks, they have invested in funds.

3 So I think, from where I sit, of course, the
4 digital currency is an unknown. But how it's going to be
5 pitched to retail people is probably, at least in one
6 way, the stocks or the funds that are investing in it,
7 which is the safe place where people think it's
8 disclosed, it's regulated, and it may not be.

9 MR. REDFEARN: Yeah, I think that we've been
10 very cautious here about actual securities coming into
11 our markets that are based upon these products. We still
12 contemplate these things. But so far, we're not seeing a
13 lot of it and you have seen the messaging come out of the
14 Commission, the Division as well as IM, about crypto --
15 potential crypto-related funds and ETFs and so on.

16 Chris, any thoughts on the crypto digital asset
17 space that you'd like to share?

18 MR. GEROLD: Well, New Jersey has filed a
19 number of actions, cease and desists against crypto-
20 related frauds. Going back to actually what Jean was
21 mentioning and I think for her base, the AARP
22 individuals, the telephone is how they get solicited.

23 In the crypto space, it's the complete
24 opposite. It is Twitter, Facebook, Snapchat, any other
25 one you can think of. I am sure there are a bunch I

1 older population, is unfortunately a very popular scam.

2 So interestingly enough, I think if there is
3 some sense of prospecting, it's the new gold of the
4 future. Right? So that's, I think, where I would pay my
5 attention. Is how closely sold or pushed, promoted
6 cryptocurrencies is to gold coins amongst our population.

7 MR. REDFEARN: That's interesting. So they
8 know the interest in that community of gold and gold
9 coins.

10 MS. SETZFAND: Correct.

11 MR. REDFEARN: And they try to repackage it in
12 that kind of a wrapper to get that kind of --
13 interesting.

14 Nicole, again, cryptocurrencies, digital
15 assets, in terms of the incoming calls that you're
16 getting there, is this something that you see also as a
17 rising trend that keeps you concerned?

18 MS. IANNARONE: I think we will begin to see
19 more of it. We haven't begun to see it just yet. I do
20 see a great deal out on Twitter. And the folks that I
21 hear most about it from are, frankly, our students who
22 are incredibly interested in it, seeing more of it from
23 younger generations. And whenever a student comes and
24 asks me about it, what do I think about investing in some
25 cryptocurrency idea that they've seen, my response is, if

1 don't even know about. And once we started getting into
2 that space and trying to identify these crypto frauds and
3 we set up a dummy account on those, the information
4 starts pouring in from those mediums. And so we are
5 very, very, very, very cautious of the cryptocurrencies
6 and the crypto space. Not the technology, necessarily,
7 which is different than cryptocurrencies. But we are
8 extremely cautious when it comes to the crypto space and
9 cryptocurrencies specifically.

10 MR. REDFEARN: Thank you. So Jean, with
11 respect to seniors, right, we're talking about Facebook,
12 Twitter, Snapchat, I don't know about everybody else's
13 grandmother, I don't know if that would be the first one
14 I'd see, but maybe so.

15 Is the vulnerability to cryptocurrencies and
16 digital assets the same for seniors, you think, and a
17 trend there, as well?

18 MS. SETZFAND: I think I agree with what Cam
19 actually said, is if cryptocurrencies will have appeal to
20 an older audience, it probably is through more of a
21 better-known asset. And so one of the things that
22 strikes me is how cryptocurrencies are actually -- a lot
23 of the language or promotional elements around it have
24 similar elements to gold, quite frankly. There's the
25 mining of it. And gold coins, quite frankly, amongst the

1 you or I can't explain the investment opportunity, how it
2 is working and how I have an opportunity to make money, I
3 don't think it would be the right investment for me or
4 for somebody else to get into.

5 So, yes, I do think that we are going to begin
6 to see more of it. I think we're going to see it
7 probably from younger generations who tend to be more son
8 on Twitter and Instagram. And I think it's going to take
9 some time for them to come to us and tell us if they
10 suffered an injury as a result of a fraud related to it,
11 particularly because of the embarrassment factor that all
12 of our clients and all of our victims face and have to
13 overcome before they seek out help to address the harms
14 against them.

15 MR. REDFEARN: Thank you. So we have time for
16 one more question. And just very quickly, since we are
17 going to be moving on in the next panel to the policy
18 things that we can potentially do to deal with this, I
19 just wanted to ask if there was, you know, one or two
20 sort of quick thoughts you have about policy areas we
21 should be exploring, to use Jean's term, to make it maybe
22 not so easy for the bad guys to be able to defraud
23 investors? What are the policy areas that you think we
24 should be focused on? Charu.

25 MS. CHANDRASEKHAR: So I think Reg Best

1 Interest will be an important regulatory vehicle going
 2 forward to really help both members of the financial
 3 community but also customers really to understand what
 4 the obligations are in terms of educating customers,
 5 placing them in suitable investments and the like.
 6 MR. REDFEARN: Thank you. Cam.
 7 MR. FUNKHOUSER: Just off the top of my head,
 8 but I think the FINRA Rule 2165 is sort of forward
 9 thinking and maybe can be expanded so that there are some
 10 responsibilities on gatekeepers and, you know, others who
 11 are handling financial transactions for individuals to
 12 maybe do some first-alert type of prevention. But like I
 13 said, if you take a look at FINRA Rule 2165, I think
 14 that's a really good start in that regard.
 15 MR. REDFEARN: Great. Chris.
 16 MR. GEROLD: Sure. I think the largest policy
 17 and one that we're in the process of adopting in New
 18 Jersey will be a uniform fiduciary standard, which the
 19 governor announced last week that we're going to be
 20 pursuing over the next couple months.
 21 MR. REDFEARN: Okay. Jean.
 22 MS. SETZFAND: So building on Chris, definitely
 23 I think keeping the investor and insuring that the advice
 24 that they get is of best interest to them is definitely
 25 important. And then I think just kind of underscoring

1 the fact that, again, whatever we can do to make the
 2 preventative actions as easy as possible for investors, I
 3 think is to what degree we can use policy to make that
 4 happen would be fabulous.
 5 Last but not least, I think what are things
 6 that regulators can do to actually frighten the
 7 fraudsters, quite frankly? Are there more enforcement or
 8 greater punitive actions that make conning, scamming,
 9 stealing money scary or harder is another consideration?
 10 MR. REDFEARN: Thank you. Nicole.
 11 MS. IANNARONE: I think to Jean's great point,
 12 in addition to everyone else said about making prevention
 13 more Amazon like and easy, I think it would be very
 14 interesting for us to explore technology and whether we
 15 can use any of the new technologies to help meet
 16 investors where they are with their level of
 17 understanding about investments, to help educate them
 18 about who they are working with, what they are getting
 19 from a proposed investment, and how they will fare. So
 20 looking a little bit into the technology to see if we can
 21 use it to help the relationship between an adviser, a
 22 broker and an individual to ensure that everyone
 23 understands what's happening, why it's happening and what
 24 expectations they should have going forward.
 25 MR. REDFEARN: Great. Listen, I think that

1 that is a great place to wrap up. I think that, you
 2 know, we have a lot more discussion to come later today.
 3 We probably jumped into some of those areas a little bit
 4 here but we have the benefit of having you all here with
 5 us today. And so I think that this discussion in those
 6 areas was extremely useful. So I'd like to thank you all
 7 again for coming here, sharing all of these thoughts and
 8 we really appreciate it and we look forward to the
 9 additional discussions this afternoon.
 10 Also, thank you, Commissioner Roisman, for
 11 staying here with us as well.
 12 And we will now take a break and we will be
 13 back here at 11:30 for our second panel. So thank you
 14 all very much.
 15 (Recess.)
 16 MR. REDFEARN: Okay, for the second panel, I am
 17 pleased to be able to turn this one over to Lizzie Baird,
 18 my deputy director, who has been here about a month now,
 19 a little over a month. So happy to have you, Lizzie.
 20 Thank you. And take it away.
 21 MS. BAIRD: Thanks. Well, welcome back,
 22 everyone. As you probably heard, one of the themes that
 23 I think emerged from the morning panel was the benefits
 24 of being registered and that so many of the fraudsters
 25 out there today are themselves unregistered. The firms

1 they purport to work for are probably also unregistered.
 2 And in many cases, the securities are unregistered, as
 3 well.
 4 This is one of two panels where you will hear
 5 about the tools that those entities that are registered
 6 have to try and combat fraud. And you will also hear
 7 about how that also helps the Commission and FINRA with
 8 their oversight and surveillance to combat fraud, as
 9 well.
 10 So without further ado, I want to introduce you
 11 to some of my new colleagues in Trading and Markets that
 12 are going to help with this upcoming panel.
 13 First, Val Dahiya in the Division of Trading
 14 and Markets will be moderating our Rule 15c2-11 panel.
 15 Tim White, also from the Division of Trading and Markets,
 16 will be moderating the broker-dealer registration panel.
 17 And Lourdes Gonzalez, again from the Division of Trading
 18 and Markets, will be moderating the suspicious activity
 19 reports panel.
 20 So without further ado, let's turn to Val and
 21 ask her if she can kick off our Rule 15c2-11 discussion.
 22 MS. DAHIYA: Thank you for the introduction.
 23 First of all, I'll start out by giving a brief overview
 24 of Rule 15c2-11. Also, I wanted to introduce Laura Gold,
 25 who is a senior counsel in the Division and she does a

Page 78

1 substantial amount of work administering Rule 15c2-11.
 2 And so she will also be moderating this portion of the
 3 panel.
 4 So in 1971, the Commission adopted Rule 15c2-11
 5 as a means to protect the investing public from
 6 fraudulent and manipulative potential inherent in
 7 situations when a broker-dealer submits quotations
 8 concerning any infrequently traded security in the
 9 absence of certain information. At a very basic level,
 10 Rule 15c2-11 requires broker-dealers to publish
 11 quotations in OTC securities to understand the products
 12 that they are quoting.
 13 The rule requires broker-dealers to review
 14 certain specific information prior to initiating or
 15 resuming a quotation in an OTC security and form a
 16 reasonable basis for understanding that the information
 17 that's being quoted is reliable and accurate.
 18 There are many exceptions to the requirements
 19 of the rule, such as unsolicited customer orders, the
 20 piggyback exception and securities that are admitted to
 21 trade on a national securities exchange. As with many
 22 rules, understanding the exceptions is important to fully
 23 appreciate the rule's strengths and limitations.
 24 Over the last two decades, the Commission has
 25 proposed to amend the rule by modifying certain existing

Page 79

1 exceptions and adding new ones. In 1999, the Commission
 2 sought to limit the piggyback exception, require annual
 3 review of current information about the issuer, expand
 4 the information required for certain nonreporting
 5 issuers, and create new exceptions for certain
 6 securities, amongst other things. Although the
 7 Commission did not adopt the 1999 proposed amendments,
 8 the 1999 proposal contains an appendix that includes
 9 guidance regarding the Commission's expectations for
 10 broker-dealers when they conduct the review. I recommend
 11 that broker-dealers who are involved in conducting 15c2-
 12 11 reviews acquaint themselves with the 1999 release and,
 13 in particular, the red flags discussed within that
 14 release.
 15 Recent actions by the Commission as well as
 16 other matters that have come to the Staff's attention
 17 suggest that some broker-dealers are not fulfilling their
 18 review obligations as required by the rule.
 19 I'm looking forward to the discussion and
 20 hearing your views on the rule and receiving your input
 21 on ways that it can be improved. Thanks.
 22 And first, I am going to turn it over to Troy
 23 Carlson, who is senior vice president at FIG partners.
 24 MR. CARLSON: Thank you. Again, my name is
 25 Troy Carlson from FIG Partners. FIG Partners is an

Page 80

1 investment banking boutique focused in the community bank
 2 space. And today's discussion on the 2-11 applications
 3 was certainly intriguing and thought that it would be
 4 best if I participated with my opinions.
 5 15c2-11 is the official application. But for
 6 today, I think the abbreviated 2-11 is probably how it
 7 will be mostly referred to. So again, I appreciate the
 8 invitation and thank you.
 9 MS. DAHIYA: Next, we are going to turn it over
 10 to Yvonne Huber, who is the senior vice president of
 11 market regulation at FINRA.
 12 MS. HUBER: Hi, thank you. So I am a vice
 13 president in the market regulation department at FINRA
 14 and I oversee the OTC compliance team. But by way of
 15 background, I have been working at FINRA for 28 years and
 16 when I started, it was 1990 and it was right at the
 17 height of a lot of scrutiny on the over-the-counter
 18 securities and the over-the-counter space. And there was
 19 the penny stock task force, there were the amendments to
 20 15c2-11 that were being proposed and subsequently adopted
 21 and FINRA had or NASD at the time had just started the
 22 Form 211 filing process.
 23 In fact, I was hired to staff a team of people
 24 that FINRA had -- or NASD had created solely for the
 25 purpose of conducting surveillance in over-the-counter

Page 81

1 securities. So I spent the first five years of my tenure
 2 with the organization conducting surveillance and
 3 investigations into potentially fraudulent activity in
 4 over-the-counter stocks.
 5 I moved out of that area and for the next 19
 6 years focused on short sale regulations. But in January
 7 of 2014, I was brought back into the over-the-counter
 8 space to take over heading up the OTC compliance team.
 9 And in addition to my short sale regulatory
 10 responsibilities.
 11 The OTC compliance team is responsible for
 12 receiving Form 211 applications from broker-dealers who
 13 wish to quote securities in the over-the-counter markets.
 14 We have a Rule 6432 which requires that firms file these
 15 applications with us to demonstrate that they have met
 16 the information review and gathering requirements of Rule
 17 15c2-11. Our team is responsible for reviewing these
 18 Form 211s when they're received to ensure that they --
 19 that the broker-dealer has, in fact, met these
 20 requirements. And if, during our review, we find that
 21 there are any deficiencies in the information that
 22 they've gathered or any red flags or discrepancies in the
 23 information, then we will issue a letter back to the
 24 broker-dealer asking for them to address those
 25 discrepancies.

1 Once we believe that a broker-dealer has fully
2 complied with Rule 15c2-11 and any outstanding
3 deficiencies or discrepancies have been addressed, then
4 we will process the Form 211 and allow the broker-dealer
5 to begin quoting the security. It's important though to
6 know that this process that we undergo is in no way a
7 merit review of the issuer. We do not weigh in on the
8 qualifications of the issuer in any way. This isn't a
9 listing process at FINRA. It's really strictly a
10 compliance review to ensure that the requirements of the
11 rule have been met.

12 I very much appreciate, though, having an
13 opportunity to sit at the table today and to provide some
14 feedback on the rule. So thank you.

15 MS. DAHIYA: Thanks, Yvonne. Next, we'll go to
16 Dan Zinn, general counsel at OTC Markets.

17 MR. ZINN: Thank you, Val, and thanks to Brett
18 and Lizzie, everybody at the SEC, for having us and for
19 putting this panel together.

20 As Val said, I'm the general counsel at OTC
21 Markets. For a little bit of background on what we do,
22 we operate the primary interdealer quotation system.
23 It's an alternative trading system, known as OTC Link,
24 for the quoting and trading of OTC equity securities. So
25 for purposes of this discussion, when Yvonne's team has

1 of an iterative process that winds up with the business
2 that's conducted on our market.

3 I think we will get into a number of the other
4 issues and kind of explanations as we go through the
5 questions. But just in terms of how we all sit,
6 hopefully that gives some good background.

7 MS. DAHIYA: Thanks, Dan. Laura is going to
8 kick it off with our first question.

9 MS. GOLD: Thank you, Val. And thanks to
10 everyone who is participating today.

11 So to jump into our conversation, I would like
12 to pose the following question. Since the last time the
13 Commission proposed amendments to 15c2-11, there have
14 been many changes to the over-the-counter market,
15 particularly for equity securities, including the move
16 towards an electronic quoting market, greater
17 transparency and regulation of quotation mediums.

18 In your view, given the changes that have taken
19 place, are there any considerations that the Commission
20 should take into consideration if it were to engage in
21 rulemaking in this space? Troy, would you like to start
22 us off?

23 MR. CARLSON: Sure, thank you. Yes, well, I'll
24 certainly say that today's OTC market is not your
25 father's OTC market. There's been tremendous leaps made

1 done the work that they do and approved a 211 and told a
2 broker-dealer that they can quote that security, they
3 will quote it most likely on our market. There are some
4 other competitors as well.

5 And so we sort of take the ball after the
6 broker-dealer, after somebody in Troy's position, has put
7 a filing together, after FINRA has done the work to
8 ensure that that compliance responsibility has been met,
9 we then allow for the broker to begin quoting.

10 Upon receiving a Form 211, an approved 211 from
11 FINRA, we will do a couple of things. We will contact
12 the applicable broker-dealer to make sure that they
13 understand the form has been approved and that we will
14 open the market for them to be able to quote. We will
15 also then start tracking the time line and making sure
16 that they meet their responsibilities, that the time line
17 is met before other brokers can begin quoting on what's
18 called piggyback eligibility, which I'm sure we'll get
19 into to some degree.

20 As the market, our interaction is with about
21 100 or so FINRA member broker-dealer subscribers. And so
22 our interest is in seeing them have as much information
23 as possible, seeing them have -- be able to offer their
24 clients and particularly retail as much of a transparent
25 trading experience as they can. And so this is all kind

1 in terms of improving the transparency and communication,
2 including, Yvonne, being able to electronically apply for
3 the 211 application was a tremendous improvement and
4 increased efficiency, which has just been the last year
5 or two. There's been a tremendous advancement in terms
6 of all the groups and parties working together in the OTC
7 market.

8 And I guess I would say that if I was going to
9 suggest any sort of change or amendment to the rules, it
10 would be just to continue increased visibility and
11 reporting by the issuers.

12 MS. HUBER: I'll be happy to go next. I would
13 definitely agree that the environment is much different
14 today than it was when the amendments were first approved
15 back in 1991. And I think that the disclosure issues
16 that were inherent, you know, at the time, they're not as
17 big a concern. I mean, with the Internet, not that I
18 think there shouldn't continue to be disclosure, just
19 that they're not as prevalent an issue.

20 But I do think that the rule could be more
21 effective if there was a little bit more of an onus
22 placed on the broker-dealers to just ensure that they are
23 looking over the information more critically from a
24 potential fraud standpoint. As you mentioned, there were
25 these red flags that were issued in 1999 when certain

1 amendments were proposed that are still -- that are still
2 out there. But I feel that the way that the rule is
3 structured, that the narrow amount of information that
4 broker-dealers need to review in compliance with the
5 rule, these red flags would not necessarily make
6 themselves evident. They would not necessarily be
7 something that would be observed. They tend to be
8 something that gets observed after we make an inquiry
9 back to the firm to ask certain questions or for them to
10 get certain pieces of information.

11 So I think that either to somehow formally
12 codify some of these red flags or potentially pull some
13 of them -- certain key red flags into the rule could be
14 helpful. For example, one major area that I think should
15 be considered would be the tradability aspect,
16 concentration of ownership.

17 We've received Form 211s where the freely
18 trading shares, as far as we could tell, totaled 5,000.
19 There were two shareholders that held shares totaling
20 5,000, one held one for 1,500 shares and the other held,
21 you know, 3,500 shares. Those types of things, I think,
22 should be on the onus of the broker-dealer to be looking
23 at and assessing before coming forward and filing those
24 forms with us.

25 MR. ZINN: We have about 20 minutes left? I

1 can go?

2 (Laughter.)

3 MR. ZINN: I wanted to address even the first
4 part of the question and just the developments in the OTC
5 market, I think. Yvonne did a great job of talking about
6 what it was like, certainly, in 1990 and even up to 1999,
7 when we were talking about the SEC release. What we've
8 done over the past 21 years at this point is take what
9 was a paper-based, basically, a phonebook market, where
10 brokers would publish quotes and that physical
11 publication would be mailed out to interested broker-
12 dealers, and made that a real-time electronic market.

13 So now, coming kind of full circle towards
14 almost where the exchanges sit, broker-dealers can quote.

15 It's an attributable market so they can see who's on
16 either side of the market. They use our system to
17 communicate with one another for the purpose of
18 negotiating trades or ultimately executing trades. But
19 on -- you know, outside of just the broker-dealer
20 experience, what we have is roughly 10,000 OTC equity
21 securities that trade -- that are quoted on the platform.

22 And we've categorized them based on the amount of
23 information that they make available and the timeliness
24 of that information.

25 So at the very top, we have what we call the

1 OTCQX market, which for context is roughly 380 or so of
2 those companies. Those are companies that are meeting
3 certainly the 15c2-11 standards in terms of audited
4 financial information. They also have quarterly and
5 current reporting obligations. And they're also meeting
6 a set of quantitative requirements.

7 Beneath that, we have the OTCQB market which we
8 call our venture stage market. The disclosure
9 qualifications, which I think is really of import when
10 we're talking about Rule 15c2-11, are similar, the same
11 in terms of current information and having audited
12 financials and the like. But some of the quantitative
13 standards are more geared towards what you might think of
14 with a venture company.

15 And then at the bottom we have what we call the
16 pink market, which is the open market. It's certainly a
17 nod to the Pink Sheets, which was that predecessor
18 publication. And pink is the open market, and it exists
19 because broker-dealers have the responsibility to give
20 their clients the best possible trading experience, have
21 best execution and other responsibilities under the FINRA
22 rules. And the pink market allows that to happen in a
23 transparent manner.

24 I am going to bring this back to the question
25 about regulation, specifically. So certainly one of the

1 biggest differences between the way the market was set
2 up, I think, in 1999, if that's our reference point, and
3 the way it's set up now is the ability for the system on
4 which these securities are quoted to provide information.

5 So we are already building in all of these incentives
6 for companies to try to basically move up the
7 categorization system and be qualified as OTCQB or OTCQX.

8 Even within the pink category, we will discern whether a
9 company is current in their reporting, has limited
10 information or has no information. No information comes
11 with a stop sign next to it, as an investor warning. So
12 even the fact that there isn't disclosure is a form of
13 disclosure in itself and allows investors to access that
14 information.

15 So with respect to some of the changes to 211
16 and how that works, because we have that capacity, A, you
17 have the opportunity for the information that a broker
18 files, that a broker is looking through and sending to
19 FINRA, to be made publicly available. So that now
20 everyone can have access to that, and that includes
21 investors, certainly, and regulators, but also other
22 broker-dealers who may have customers who are interested
23 in quoting the security or who may have a proprietary
24 interest themselves. So that's a big change and I think
25 being able to have that information disclosed as soon as

1 possible from the 211 filing and then have other brokers
2 be able to work with that information in order to create
3 a better market is something that can be addressed to the
4 211 process.

5 Similarly, having a system like ours, you know,
6 our system is now an SEC-regulated alternative trading
7 system. We are a FINRA member broker-dealer, which is a
8 requirement of all alternative trading systems. So
9 having the system be more involved in the process itself,
10 even to the extent that we have all of the relevant
11 information and sometimes more, or sometimes have a
12 contractual relationship with the issuer with respect to
13 OTCQB and OTCQX, we may be able to file a Form 211 or
14 otherwise provide that kind of support and background for
15 other broker-dealers to file a Form 211.

16 I think having all of the capability that we
17 have now should cause kind of a second look at what we
18 can do from a technology standpoint and even from a
19 regulatory standpoint with respect to where we sit to
20 help improve the process.

21 MS. GOLD: Thanks, everyone. And so what
22 you've all brought up is the need to address the
23 disclosure that's being provided, whether it's, you know,
24 on the Form 211 and to retail investors. And so, you
25 know, it sounds like there will be -- there could

1 there who are interested and sort of jumping into the
2 market and, you know, investing in their companies.

3 So I think at the end of the day, putting forth
4 regulations to make sure that the markets are fair and
5 the investors are protected really is going to help all
6 the market participants.

7 MR. ZINN: Just jumping in on that, I think
8 there's a lot of truth to that, certainly. But it
9 obviously can go too far, just to some degree, right? If
10 you only allowed the S&P 500 to trade, certainly there
11 would be massive investor confidence in everything that
12 trades on the markets. But that's not, you know, an end
13 goal in itself. And so I agree with you, there's always
14 going to be that rub and trying to get to that
15 appropriate point where investor protection concerns are
16 being met and being met at various stages in the process,
17 as we kind of all represent from broker-dealers to the
18 regulators to the market.

19 And so one of the things that we've thought
20 about from kind of a specific proposal standpoint is how
21 do you allow the broker-dealer -- and, you know, I think
22 Val kind of led off with what the broker-dealers'
23 responsibilities are -- how do you allow the broker-
24 dealer to best fulfill their responsibilities? In some
25 circumstances, the broker is already going to have an

1 potentially be some increased costs to broker-dealers
2 based on these suggestions that you've provided.

3 So in your opinion, in the context of, you
4 know, if the Commission were to engage in rulemaking,
5 what would be the best ways to achieve an appropriate
6 balance between capital formation and retail investor
7 protection?

8 MS. HUBER: Well, I'd have to say that there's
9 always going to be a rub between adequately protecting
10 investors and enabling companies to go and enter into the
11 capital formation process. But I don't necessarily think
12 that they need to be mutually exclusive. I don't
13 necessarily think that you'd have investor protection at
14 the cost of capital formation. And in fact, I really
15 think investor protection will foster the capital
16 formation process. And the reason is because at the
17 heart of it, what you really are looking for is investor
18 confidence.

19 If you let frauds go through, if you let
20 companies who are frauds be traded and quoted, in time,
21 that's going to erode investor confidence. And all the
22 rulemaking that you want to put in place, however easy
23 you want to make it for companies to be able to get their
24 securities, you know, publicly traded, it's not going to
25 do them any good if there aren't going to be investors

1 existing relationship, they're going to have informed the
2 issuer with respect to an offering or provide other
3 investment banking services. In other circumstances, you
4 have a broker that their primary responsibility is to
5 facilitate trading and to do that in securities where,
6 you know, some work needs to be done to some degree in
7 order to kind of meet that standard that Yvonne was
8 talking about.

9 And so just like an underwriter is compensated
10 for taking that risk and going out and doing the work
11 necessary to get that offering qualified and to kind of
12 stand in that underwriter role, a firm that is taking a
13 company public, which is really what it is through the
14 211 process, should also have an opportunity to establish
15 a direct relationship with the issuer. That's the kind
16 of communication you want. You want there to be an open
17 line between the broker and the issuer. And to
18 potentially be compensated for it by the issuer so that
19 there is maybe some of that offsetting -- or that helps
20 offset some of the attendant cost and gives the market a
21 better experience when that information is ultimately
22 brought to FINRA and that security is ultimately traded
23 with us.

24 MR. CARLSON: I'd like to add, I agree with
25 Dan. But with regards to the additional costs

1 associated, I just don't see that being a significant
2 deterrent. As it ties to my thoughts on rulemaking or
3 changes to rulemaking, to think about the relationship
4 about the broker-dealer, underwriter and issuer, should
5 play a significant part of the amount of disclosure or
6 the amount of -- of protection that the retail investor
7 is going to be the beneficiary of.

8 You know, as an underwriter, we are, when
9 representing that issuer, absolutely doing what it is
10 that we do every day as part of our core business. The
11 expenses that are incurred in the application process,
12 the listing, all of that again is -- we have not seen a
13 significant increase. And it's again just the natural
14 course of us doing business.

15 And I think it needs to be taken into
16 consideration when you have that relationship between
17 issuer and underwriter and investment bank, who is in
18 this case filing the application and listing those
19 shares, the checks and balances are already existent,
20 they're already there. The investor has been given the
21 opportunity or is being protected for any fraud because
22 of the amount of liability that we've already basically
23 put on ourselves as the underwriter, the broker-dealer.

24 I guess to summarize, I'd say that in thinking
25 about the rulemaking, some emphasis should be put on the

1 But there are often times when there is still
2 somebody who is out there in a name only quote or with an
3 unpriced quote. And they are -- they feel precluded from
4 being able to inactivate the symbol in that situation.
5 Now, typically, they will go and they will approach the
6 firm and let them know, hey, you've got a quote out here
7 or an unpriced quote out here in a stock that hasn't
8 traded in a certain amount of time. And usually, they're
9 not aware and they take it down and it gets resolved.

10 But I think if we built into Rule 15c2-11 the
11 ability for us to or for the piggyback exemption to be
12 sunset in situations where there's been -- you know, the
13 stock has been inactive for a certain period of time, I
14 think that would be beneficial.

15 MR. ZINN: I will go quick, I promise.

16 You know, I think, largely in respect to the
17 types of securities that Yvonne is talking about, that's
18 where you kind of need to focus, which is the securities
19 that we have identified for the most part as no
20 information. The SEC has done a really good job,
21 particularly of late, with suspensions. We work kind of
22 directly with the SEC on, you know, unable to contact,
23 companies that don't seem to exist anymore for whatever
24 reason. And that certainly is a great tool for clearing
25 those out.

1 relationship between the broker-dealer and underwriter
2 and who is actually filing the application.

3 MS. DAHIYA: Thanks. So we are running a
4 little short on time but we wanted to get in one last
5 question, and one that everyone has strong views on, on
6 the piggyback exception.

7 So with the piggyback exception, it allows
8 broker-dealers to quote even for issuers who don't have
9 currently available information. And oftentimes, issues
10 that are dormant or no longer exist. So do you have
11 recommendations or thoughts on how the rule could be
12 amended to address this issue with the piggyback
13 exception?

14 MS. HUBER: Well, I think we definitely think
15 that there should be some consideration to putting a
16 sunset on the piggyback exemption, particularly when, in
17 your example, the company is dormant or doesn't seem to
18 exist anymore.

19 We currently have a process in our operations
20 department, where we get alerts or get notified if
21 there's a company that hasn't had any trading activity
22 for a certain period of time or there have been no
23 corporate actions for a certain period of time. And in
24 those situations, they'll inactivate the quote. Or,
25 sorry, they'll inactivate the symbol.

1 You know, there are investors, there are
2 sometimes very sophisticated investors, who still have an
3 interest in those securities. I think if it's -- if it's
4 not clear that a company could have that symbol pulled or
5 that piggyback eligibility could be sunset, you're going
6 to have a lot of unnatural impact on the trading of that
7 security. Who is going to want to be left holding the
8 hot potato, basically? Before you know some deadline is
9 coming up or some other action is going to be taken.

10 One of the things that we've been thinking
11 about is whether you can take those kinds of issuers and
12 put them in some kind of an experts-only market or
13 otherwise indicate that, you know, these are securities
14 that have certain characteristics and don't have
15 information, which is certainly something we're putting
16 out there already, where there may be a legitimate
17 trading interest by sophisticated investors but maybe
18 it's not right for everyone.

19 And so, similar to how broker-dealers deal on
20 the options market or how the SEC looks at the accredited
21 investor standard for certain investments, being able to
22 build something like that so that you don't run into that
23 kind of hot potato problem and you actually allow the
24 people who are able to trade those knowingly to continue
25 interacting with them.

1 CHAIRMAN CLAYTON: Brett, can I jump in here?
 2 MR. REDFEARN: Please.
 3 CHAIRMAN CLAYTON: You know, going back to what
 4 I said at the beginning, which is the playing field for
 5 retail investors, and I think your comment -- both of
 6 your comments bring this out, there's a lot of activity
 7 based on the piggyback exception that, speaking for
 8 myself, I don't think is an appropriate playing field for
 9 retail investors. I think your comments draw that out.
 10 And your comments also make it clear that, if we feel
 11 that way and the market feels that way, the market
 12 functions better if we make it clear.
 13 You can come back.
 14 MR. ZINN: No, believe me, I'm not trying to
 15 cut you off.
 16 No, I think, again, with respect to that subset
 17 of securities where there is no information, I think that
 18 makes, you know, some degree of sense, having that
 19 experts only or otherwise sort of segmenting that off.
 20 But the piggyback exemption generally, what you want
 21 really is to provide more opportunity for price
 22 discovery, to have more brokers that are available. So I
 23 wouldn't want to cut it off, you know, at the knees,
 24 right?
 25 CHAIRMAN CLAYTON: No, I understand. But where

1 it stands today, I think there's room for improvement.
 2 MR. ZINN: Yeah, I agree. And I think with
 3 respect to the types of issuers, certainly, we're
 4 aligned.
 5 MS. HUBER: And I think particularly, and this
 6 is probably not a question we are going to be able to get
 7 to today, given our limited time, but I think under
 8 certain circumstances, piggyback eligibility should be
 9 taken away, such as in the reverse merger scenario, where
 10 there has been a completely different -- a complete shift
 11 in the business line of a company, a complete change in
 12 ownership, a complete change in officers and directors.
 13 That's essentially a new company and it probably doesn't
 14 make sense in that space to allow piggybacking to
 15 continue.
 16 CHAIRMAN CLAYTON: Can I explain that for the
 17 retail investors, who may be watching via webcast? Which
 18 is you have a very low capitalization, thinly traded
 19 stock which happens to be in our registration regime.
 20 And a large company merges with that. The resulting
 21 company is the large company, but the large company has
 22 not been through the vetting process that we at the SEC
 23 and other regulators apply for it to become a public
 24 company. Some would call it a back door. But that is a
 25 process that troubles me.

1 MR. REDFEARN: I know that we are going to need
 2 to move on to the next panel. I just want to say we do
 3 have a place to post comments for all of the discussions
 4 that we're having here. I think this question in
 5 particular is one that we're keenly interested in, which
 6 is specifically to the extent that there is no financial
 7 information for an extended period of time, or any of the
 8 other factors, no corporate actions or whatever, the
 9 question is what do we do? Do you eliminate the
 10 piggyback exception? You'd suggested, you know,
 11 potentially a professional's market. But I think there's
 12 a view that more clarity would be helpful and perhaps
 13 some evolution of the regulatory regime here would be
 14 beneficial for the marketplace, especially when it
 15 pertains to retail. Because we have had experiences
 16 where retail investors do find their way into some of
 17 these names.
 18 CHAIRMAN CLAYTON: As usual in this space,
 19 Brett said it better than I did.
 20 MR. REDFEARN: I'm going to differ with you on
 21 that one.
 22 So I apologize, but I do think that we do need
 23 to move on to the next subpanel.
 24 MS. BAIRD: So thank you, Val and Laura. And
 25 thank you, Troy, Yvonne and Dan.

1 Next up, Tim can you help provide us with an
 2 overview of what the current requirements are for broker-
 3 dealer registration?
 4 MR. WHITE: Absolutely. Thank you, Lizzie.
 5 So this subpanel is focused on BD registration.
 6 But it's not only BD registration, it's also people who
 7 are unregistered as broker-dealers who are almost as
 8 important to the equation as BD registration.
 9 You've heard a lot in the previous panel about
 10 BD responsibility and that's where registration basically
 11 gets you, is the broker-dealer is responsible for certain
 12 things. Broker-dealers play an important role in both
 13 protecting investors and increasing capital formation.
 14 They have been described as gatekeepers and, for most of
 15 retail investors, they are the entry point into investing
 16 in the market. That's the person that they know in terms
 17 of recommendations for investments or, you know, where do
 18 they put their money, that sort of thing.
 19 So what is a broker? A broker is a person
 20 engaged in the business of effecting securities
 21 transactions for the account of others. Broker-dealers
 22 interact with retail investors, are typically registered
 23 with the SEC and are members of FINRA. Among other
 24 things, these broker-dealers are subject to legal
 25 requirements that govern their conduct in the marketplace

1 and provide important safeguards for investors. They are
2 subject to books and records requirements, financial
3 responsibility obligations, targeted antifraud
4 provisions, supervisory obligations, anti-money
5 laundering requirements which will, I think, be discussed
6 later, and examinations by regulators.

7 Many retail investors buy securities through
8 registered broker-dealers and are afforded these
9 protections of registration. Although fraud may still
10 happen in these instances, the system is set up to try to
11 minimize and address such circumstances.

12 But there are also persons that sell securities
13 that are not registered broker-dealers but maybe need to
14 be or maybe should be registered.

15 This takes us to our topic of discussion for
16 this subpanel, finders and private placement agents. To
17 discuss this topic, I am pleased to have the panelists
18 introduce themselves, starting with Faith.

19 MS. COLISH: Thank you. It's a privilege to be
20 here. And I am looking forward to a good dialogue with
21 you all. I am Faith Colish. I am a securities lawyer.
22 I am in private practice in New York at Carter Ledyard.
23 I started my career at the SEC in 1960 in the general
24 counsel's office in a much smaller building. And most of
25 my practice over the years has been focused on smaller

1 broker-dealers, investment advisers and other financial
2 service providers.

3 In 1999, I was asked to join a, at that point,
4 nascent ABA task force addressing the issue of finders.
5 And one of the things I will hope to give you some
6 insight into is what that task force has done and is
7 still hoping to do with respect to finders.

8 In addition to being on the task force I was,
9 how shall I say, invited to participate with the SEC
10 Staff in what became the M&A broker no-action letter,
11 which came out in 2014. And there is now a bill in
12 Congress, in the House, H.R. 6127, which we will get into
13 in a little more detail, which I did not write and I did
14 not lobby, but which I was consulted about. And it is
15 the furthest that has been accomplished in terms of a
16 proposal to alleviate or to address the balancing -- and
17 that's my view -- balancing of two important goals of the
18 SEC, which were mentioned by Ms. Huber.

19 There are essentially three goals of the SEC,
20 if you want to look at it from a 30,000-foot level. It's
21 investor protection, capital formation and orderly
22 trading markets. So I'm not talking about trading
23 markets because this is all going to be private placement
24 stuff. But I think it's important to focus on an
25 appropriate balancing of investor protection and capital

1 formation, which was one of the, I believe, the
2 motivations behind this bill. And also a concern for the
3 original founders of the task force.

4 So I will be glad to elaborate on that later.
5 MR. WHITE: Thank you. Maybe if we could just
6 go down the line. Chris, if you don't mind introducing
7 yourself again?

8 MR. GEROLD: Sure, Christopher Gerold. I am
9 the chief of the New Jersey Bureau of Securities. The
10 bureau is in charge of regulating the securities markets
11 in New Jersey and protecting investors. One of the
12 things I forgot to say before and I should have is the
13 views expressed here today are my own and do not reflect
14 those views of the attorney general or any other state
15 agency.

16 Well, I'm sure we'll get into our discussion
17 after.

18 MR. REDFEARN: We'll apply that retroactively
19 for the last panel then, Chris.

20 MR. GEROLD: Thank you.

21 MR. WHITE: Ignacio.

22 MR. SANDOVAL: Thanks, Tim. I'm Ignacio
23 Sandoval, a partner in the Washington office of Morgan
24 Lewis. I work in all things related to securities
25 intermediaries and, in particular, registered broker-

1 dealers. So I actually started my career at the
2 Commission, I would say about 11 years ago, in the
3 Division of Trading and Markets, working on broker status
4 issues. So I've been here for a while.

5 So even though my current work focuses on
6 registered broker-dealers, the status issues regarding
7 brokers, finders and private placement agents still
8 present themselves often, usually in the transactional
9 context, where a lot of the transactional attorneys in
10 our firm are, you know, trained to recognize compensation
11 arrangements that could raise broker status issues. So
12 that's generally when we're brought in and we evaluate
13 the situation. So these finder issues and evaluating
14 whether someone is effecting transactions or engaged in
15 the business, it's still a part of my bread and butter.

16 MR. WHITE: Thank you, Ignacio. You just
17 mentioned finders. I think that's important, because
18 there are a lot of retail investors hopefully watching
19 over webcast, to describe what is a finder, what is a
20 private placement agent so we all kind of know what we're
21 talking about, and also why has it been an issue in the
22 industry for a number of years?

23 MR. SANDOVAL: Sure, Tim. So, you know, when I
24 think of a finder, you know, and part of this might have
25 been the training I received while I was on Staff, you

1 know, at its core, when I think of a finder, I think of
2 someone who just gets paid for making introductions and
3 that's it. You just make the introductions and you walk
4 away. Now, that's the typical framework under which I
5 evaluate whether someone is a finder or a broker.

6 And so, you know, in speaking whether -- on
7 whether someone is a finder or not, really the epicenter
8 of most of this focuses on the so-called Paul Anka
9 letter. It was issued in 1991 by the SEC Staff and that
10 sort of provides the framework under which you've
11 evaluated the situations where that may arise broker
12 registration issues.

13 So the premise of the Paul Anka letter -- so
14 Paul Anka was a Canadian singer. So, incidentally, he
15 wrote the song -- he wrote the lyrics to "My Way" even
16 though Frank Sinatra sang it. It was something I was
17 actually taught on the Staff my first day here. So he
18 was looking to get paid a success-based fee for
19 furnishing the names of potential investors to personnel
20 of a Canadian hockey team that was looking to raise
21 funds.

22 So under the terms of the letter -- and when I
23 read no-action letters, especially those older ones, you
24 read what the Staff's response is, but you also have to
25 read what the incoming letter represents. Because in

1 As Tim mentioned earlier, you know, broker
2 status is you typically look at it as having two prongs.
3 You know, one is whether the person is effecting
4 transactions and the other is whether the person is
5 engaged in the business. And engaged in the business,
6 you know, the indicia there is whether somebody is
7 getting paid based on the size, value or occurrence of a
8 transaction. So when I think about what it means to
9 effect a transaction, I usually associate that with
10 affirmative efforts to make the deal go through, right?
11 You have a salesman stake, right?

12 So when you look at indicia that the Staff has
13 sort of provided over the years, suggesting that these
14 are indicia of effecting transactions, right, you
15 contrast that with the activities Paul Anka couldn't do,
16 right? So the activities typically associated with
17 effecting include soliciting investors, preparing
18 offering materials and sending them to investors,
19 collecting those materials back, sending them to the
20 issuer. Offering advice. Hey, this is a pretty good
21 investment. Or conducting, you know, other types of due
22 diligence.

23 So when you look at the Paul Anka letter, even
24 though he was getting paid what was arguably a success-
25 based fee based on which of the contacts he provided

1 some of those older letters, the Staff's response is a
2 little different than what was represented. You know,
3 just adding that as a bit of an additional note.

4 So under the premise of the Paul Anka letter,
5 he was effectively going to hand over his Rolodex to this
6 Canadian hockey team and let them see if anyone they
7 contacted through that Rolodex would be interested in
8 investing. So, you know, the important thing to think
9 about in terms of the Paul Anka letter was what he was
10 not allowed to do. Right? So under the terms of that
11 letter, he wasn't allowed to solicit potential investors,
12 negotiate transactions, participate in any advertisement,
13 endorsement or general solicitation, help prepare any
14 materials or provide those materials to investors, wasn't
15 permitted to do any due diligence or analysis of the
16 issuer, provide financing or any advice, or be involved
17 or have been involved in any other securities
18 transactions.

19 And so, you know, from my perspective and the
20 way I've always reviewed the Paul Anka letter, the reason
21 the Staff back then was comfortable in issuing the letter
22 was because he was arguably not effecting transactions,
23 even though he was getting paid transaction-based
24 compensation. So, yeah, I wanted to sort of unpack that
25 a little bit more.

1 actually invested, because he was limited in what he can
2 do to just an introduction, you know, I've always
3 analyzed that as being, well, you have one part of the
4 prong, you have the business prong, but you don't have
5 the effecting transactions prong. So it's really through
6 that framework where you -- both when I was on the Staff
7 and in private practice, when I evaluate whether somebody
8 rises to the level of a broker or not.

9 So, you know, contrast what Paul Anka was
10 permitted to do against, you know, cases where the SEC
11 has gone after folks for unregistered broker status. I
12 think in recent memory, the most significant one had to
13 do with unregistered broker activity involving a private
14 equity fund. So there, I think even though the purported
15 unregistered broker was characterized as a consultant,
16 they were getting paid transaction-based compensation and
17 the efforts that this person engaged in, you know, you
18 can just check the boxes, effecting transactions, right?
19 Sending private placement memorandum, collecting
20 subscription agreements, due diligence, you know, urging
21 people to invest. You know, things of that nature.

22 So, you know, that's typically how you -- at
23 least I analyze the issue. But given the dichotomy that
24 I've just sort of outlined, I would be remiss if I didn't
25 mention a 2011 case out of the Middle District of

1 Florida, where the SEC suffered a loss. It's SEC v.
2 Kramer case. You know, in that case, when the -- the
3 reason I mention that case is the Court, even though the
4 Staff made some pretty compelling arguments that the
5 Defendant in that case was actually effecting
6 transactions and acting as an unregistered broker-dealer,
7 the Court in that case eventually took the view that the
8 person was acting -- was merely facilitating a
9 transaction.

10 And so the reason I think Kramer is important
11 is because, unlike other broker cases out of the district
12 courts, the judge in Kramer actually went through the
13 process of evaluating each of the indicia that typically
14 get thrown out by the Staff as indicative of broker
15 status and really just tore them all apart.

16 So I normally would have been a little
17 dismissive of Kramer except for the fact that you have a
18 lot more courts citing to it now to find people that were
19 not acting as broker-dealers.

20 So that's a long-winded way of saying that this
21 area has become grayer over the years. And, you know,
22 probably could benefit from some clarity.

23 In the private placement context, I think,
24 there, you're going to see people engaging a little more
25 in solicitation efforts and passing documents back and

1 And the issuers, their clients, were small.
2 They had no track record. They had no assets. They
3 might be working out of a garage, whatever. They could
4 not get a registered broker-dealer to pay attention to
5 them. They could not get a registered broker-dealer to
6 answer their phone calls, and with good reason. Because
7 the amount of money that could be raised would not -- and
8 the fee that would be earned -- would not justify the
9 amount of work and the overhead of a registered broker-
10 dealer.

11 So what were they doing? They were going to
12 unregistered finders. And actually -- and so these what
13 I'll call '33 Act lawyers were concerned about was
14 there's a provision in the '34 Act that says any
15 transaction made in violation of the '34 Act, which would
16 include using an unregistered broker who should be
17 registered, is void. Which means that there are
18 rescission rights against the issuer and presumably also
19 against the intermediary. And this was a very scary
20 thing to them.

21 That coupled with the then lack of clarity or
22 lack of landscape, if you will, in terms of what the SEC
23 at least thought or what the courts thought about what
24 does or doesn't trigger the need to be registered as a
25 broker led to the formation of the task force. And since

1 forth.

2 MR. WHITE: And I think clarity, exactly, is
3 what sort of, Faith, you're trying to get to with some of
4 your efforts. I'm glad you mentioned Paul Anka, Ignacio,
5 because that's a very limited letter. So in reality,
6 nobody has a paper Rolodex anymore, clearly, so -- and
7 people who solicit generally want to have conversations
8 with the people they're soliciting and not just hand over
9 names. So practically, that doesn't seem to be workable
10 in today's environment.

11 But absent Paul Anka, Faith, if you could talk
12 a little bit of your efforts as trying to bring clarity
13 in this area of private placements and/or finders.

14 MS. COLISH: Thank you, I'd be glad to.

15 As I mentioned, I've been a participant in this
16 ABA task force that got started in 1999. And it actually
17 started -- was started by a group of lawyers who
18 represented issuers, as it happened in California and
19 Silicon Valley, and you may remember what kind of market
20 there was for innovation even then. And these lawyers
21 who were essentially -- and I'm going to use a shorthand
22 term, but I hope everybody will understand -- they were
23 essentially '33 Act lawyers. They were representing
24 issuers who were doing some sort of offering of
25 securities, typically a private placement.

1 these were all, as I say, '33 Act lawyers, they thought
2 it might be helpful to have someone who knew something
3 about broker-dealer registration. And that's how I came
4 in, because that has always been a large part of my
5 practice.

6 And the report, and I've had occasion to reread
7 it not so long ago, and of course things have happened in
8 the interim. But a lot of it is still absolutely
9 applicable and valid and it's readable. And if anybody
10 has, I don't know, an hour to spare, I would encourage
11 you to read it. It's available on the SEC website and a
12 lot of other places.

13 It essentially had two kinds of
14 recommendations. One was greater clarification from the
15 SEC of whatever the SEC would say does or doesn't
16 constitute engaging in the business of effecting
17 transactions. It's a two-part definition and there
18 really is no de minimis exception. If you're engaging in
19 the business but you only do it once and you only raise
20 \$100, technically you're supposed to be registered. I
21 mean, that may be a little hyperbolic but technically
22 that's correct. And on the other hand, what is effecting
23 a transaction? And of course, the Paul Anka case is an
24 example where the Staff felt that the activity of just
25 selling your Rolodex -- and, by the way, I do have a

1 paper Rolodex still on my desk -- it was not -- it didn't
2 involve you enough in the interaction or potential for
3 misleading people. So that was thing number one, was we
4 need more clarification.

5 And, B, we need a more customized, bespoke,
6 hospitable process for becoming a registered broker, what
7 we sometimes refer to as BD Lite. Not to throw out the
8 baby with the bathwater, not to completely disregard the
9 need for regulation, but to come up with a regulatory
10 scheme that was more well designed for people who do a
11 limited kind of business. The limited kind of business
12 would be with no custody of any customer assets, with
13 essentially relatively smaller transactions and a few
14 other indicia that we felt were overburdened by the
15 existing regulatory structure.

16 And, by the way, and this is not to denigrate
17 FINRA. I mean, FINRA is a wonderful organization and we
18 couldn't live without it. But most of the burdens of
19 being a registered broker-dealer come from FINRA
20 regulation. Once you are registered as a broker-dealer,
21 obviously, there are antifraud requirements but I would
22 say the single biggest burden that a registered broker-
23 dealer has that comes directly from the SEC and the
24 federal securities laws as opposed to FINRA is the Net
25 Capital Rule.

1 And I know when I've had discussions with
2 people on the SEC Staff about maybe dropping the Net
3 Capital Rule for certain kinds of brokers such as
4 finders, I've -- the reaction has been shock and horror.

5 I mean, it was like sacrilege to even suggest it. But,
6 frankly, most of these broker-dealers are eligible for
7 the lowest net capital bracket which effectively means --
8 and I'm going to oversimplify -- but essentially net
9 worth of \$5,000. But it means that under FINRA rules you
10 have to have a FINOP, which is a registered financial and
11 operations principal, you have to file FOCUS reports,
12 which are at least quarterly financial reports, and the
13 most burdensome in terms of cost is you have to have an
14 independent audit, which as of now, although maybe that
15 will change, has to be by a PCAOB qualified auditor and
16 that's going to cost you, I don't know, 20 grand, 25
17 grand, which is just too much money.

18 So you end up with finders who either are -- or
19 potential finders who are actually doing an illegal
20 business, and I see them all the time. I can't tell you
21 how many there are but they're out there. And they say,
22 I haven't been caught and I'm not going to commit any
23 fraud so I'll take my chances. And the issuers will also
24 take their chances. Or what is even perhaps more
25 troublesome is they don't, they don't participate and

1 they don't -- they're the missing link between the issuer
2 and the source of capital. And these are typically
3 smaller issuers who don't -- the owners of them don't
4 necessarily know a bunch of accredited investors or
5 people that they can go to directly. So you have those
6 tensions there.

7 And by the way, one of the suggestions I've
8 made when I've shocked and horrified people by suggesting
9 to drop the Net Capital Rule for certain categories of
10 finders is to replace it with a concept which is fairly
11 common among the states, and I would commend it to the
12 Commission or to whoever is going to be in charge of
13 this, which is a bonding requirement. And for probably a
14 relatively -- certainly less than \$20,000 a year, you can
15 purchase -- you will be able -- I guarantee you, there
16 will be insurers out there that will see a market and
17 will be willing to write insurance that will provide
18 investor protection that will be less expensive for the
19 general population of finders and which will eliminate a
20 whole lot of regulatory -- I don't want to say red tape,
21 but a lot of regulatory burdens that, frankly, I think
22 are a disincentive to finders to come out of the closet,
23 to come into the sunshine and to be known to regulators.
24 And so I think that is a win-win situation.

25 There have been a number of things that have

1 happened since the task force report was issued in 2005.

2 I mentioned this M&A broker letter which I am very
3 pleased to have participated in. There are a bunch of
4 both Commission actions and legislative actions to
5 facilitate capital formation for small businesses, but
6 essentially all on what I'm calling the '33 Act side. So
7 you have Regulation A+ and you have a number of other
8 initiatives that are designed to make it easier for small
9 businesses to raise money. But in most cases, you still
10 have the missing link between those issuers and the
11 retail investors.

12 Now, FINRA has a CAB, a capital appreciation
13 broker rule, which went into effect two or three years
14 ago. But in that -- and these are obviously registered
15 broker-dealers and FINRA members, but they can only
16 solicit investments from not just accredited investors
17 but institutional investors, which typically means 50
18 million and up. That's not retail in my book.

19 We also have the issue of what is an accredited
20 investor, which I know is a whole topic much too big for
21 this discussion today. But is an accredited investor the
22 retail investor that we're talking about today? And I
23 think it would be helpful to define those terms to see
24 what category of investors do we consider to be the most
25 vulnerable and which are presumed to be able to fend for

1 themselves? Which is how we got to the definition of
2 accredited.

3 MR. WHITE: And, Faith, can I just add to what
4 you just said there? And I know we're running short on
5 time. But I think you hit the nail on the head in terms
6 of bringing people into the light and trying to give
7 options to finders or broker-dealers that people can rely
8 on at a lower cost basis.

9 There have been many options thrown around
10 including, as you stated, legislation, your task force.
11 We've also been -- it was suggested to us about
12 disclosures in which the finder tells the person they're
13 finding that, hey, I'm getting paid to provide them a
14 document, just to show the conflict of interest.

15 But, Faith, you also mentioned the states. I
16 just want, because we're short on time, want to give
17 Chris an opportunity just to very quickly state --

18 MS. COLISH: Okay.

19 MR. WHITE: -- whether or not -- what he's
20 seeing on a state level in terms of unregistered broker-
21 dealers and any concerns for people who might be in your
22 state.

23 MR. GEROLD: Sure. Thank you, Tim.

24 We do have a concern in this area, New Jersey
25 specifically and other states as well. The idea, and you

1 unregistered securities by unregistered agents,
2 unregistered broker-dealers. And perhaps our view is
3 jaded somewhat because that's what we see. But I guess
4 the -- does this serve retail investors? Does having
5 this exemption serve retail investors? Or is it just
6 serving capital formation? And as a retail investor
7 forum in our function to protect investors, we have a lot
8 of concern around that. And primarily, you know, who's
9 selling what? And without that knowledge, we won't learn
10 until there's a problem -- we won't find out until
11 there's a problem.

12 MR. WHITE: Thank you. And I think we're
13 running out of time. But, in essence, from what I'm
14 hearing from the panel, the takeaway is, there are a lot
15 of people outside of the regulatory framework that are
16 unregistered but performing potentially broker-dealer
17 activities, and that's fraught for fraud, affinity fraud
18 or whatever the case may be. And there are many ways to
19 bring them into the light. To Faith's point, maybe full
20 registration is over-costly and overburdensome for these
21 type of people but there must be some sort of middle
22 ground.

23 So thank you very much for highlighting this
24 for us and we appreciate it.

25 Lizzie, back to you.

1 mentioned it, bringing them into the light.

2 Registration is one of the tools we have. We
3 need to know who is selling what in our state. And
4 without that information, we're at a disadvantage until
5 there is a problem. And so exempting or, I know the
6 proposed legislation actually has that awful P-word in
7 it, preemption.

8 MR. WHITE: Can you explain what that is for
9 the retail investor?

10 MR. GEROLD: Sorry?

11 MR. WHITE: Can you explain what preemption is
12 for the retail investor?

13 MR. GEROLD: Yeah, sure. Preemption,
14 essentially, and it exists -- well, in the securities
15 field, where the federal government essentially says this
16 is our area exclusively and states have no ability to
17 regulate that portion, whatever it happens to be. In
18 this case, securities. So it takes us as state
19 regulators out of the equation. In this case, it would
20 be as to the registration or any state-based requirements
21 for finders.

22 So our concern, well, first is preemption in
23 general, we have a concern. But, you know, what we see
24 as state regulators in this area, unfortunately, is we
25 see a lot of fraud in this area. We see a lot of sale of

1 MS. BAIRD: Thank you, Tim. And thank you,
2 Faith, Chris and Ignacio. And, Faith, especially thank
3 you for giving a shout out to the Net Capital Rule, which
4 is another way that Trading and Markets, our brethren who
5 are not here today, provide various filters to prevent
6 certain entities from entering the broker-dealer market.

7 Now, Lourdes is going to tell us about
8 suspicious activity reports.

9 MS. GONZALEZ: So thank you, Lizzie. So this
10 segment of the roundtable is focused on the U.S.
11 government's use of suspicious activity reports, or SARs
12 for short, in identifying and combating retail fraud. As
13 most of you know, the Bank Secrecy Act requires a broker-
14 dealer to detect and report suspicious transactions
15 occurring by at or through a broker-dealer above certain
16 specified thresholds. And those reports are enormously
17 helpful to the SEC, FINRA as well as law enforcement in
18 detecting retail customer fraud.

19 So before we begin, let me introduce our
20 panelists. And Sarah, let's start with you.

21 MS. GREEN: Thank you, Lourdes. And thanks so
22 much for having me. I am global head of the financial
23 crimes program at Vanguard. But before I came to
24 Vanguard, I started out, after a brief stint at a law
25 firm, here at the Commission, developing the program for

1 compliance with the Bank Secrecy Act for broker-dealers
2 and investment companies. Followed that by a stint in
3 Enforcement, running the SAR review program there, where
4 we reviewed suspicious activity reports. Then came over
5 to FINRA with Mike, here, and worked on both the
6 enforcement and the examination programs in the anti-
7 money laundering area and also running FINRA's program
8 that reviews suspicious activity reports. And now I'm
9 here at Vanguard on the other side of the table.

10 MS. GONZALEZ: And Jim.

11 MR. FIEBELKORN: You bet. Also very happy to
12 be here. Thank you, Lourdes. My name is Jim Fiebelkorn.
13 I am the anti-money laundering officer and identity
14 theft prevention officer for Ameriprise Financial, where
15 I also lead the anti-fraud and surveillance functions.
16 Ameriprise Financial is a large, publicly traded company
17 that includes wealth management, insurance, trust bank
18 and asset management services.

19 MS. GONZALEZ: And Mike.

20 MR. RUFINO: Sure, and thank you, Lourdes, and
21 thank you for the invitation, as well, on such an
22 important topic. Michael Rufino and I oversee our sales
23 practice program at FINRA. And a major part of what we
24 do in our program is conducting examinations of our
25 member firm broker-dealers, including those branch

1 that is, a broker-dealer must report a transaction to
2 FinCEN, which is the Financial Requirements Enforcement
3 Network, which is part of the U.S. Treasury, if it's
4 conducted or attempted by, at or through a broker-dealer.

5 It involves or aggregates funds or other assets of at
6 least \$5,000, and the broker-dealer knows, suspects or
7 has reason to suspect that the transaction or pattern of
8 those transactions involve funds derived from illegal
9 activity or are conducted to disguise the funds or assets
10 derived from that illegal activity, designed to evade the
11 Bank Secrecy Act and the requirements thereunder, clearly
12 serve no apparent business reason. Fourth is not the
13 sort of activity that the customer would normally deal
14 in, and there is really no reasonable explanation as to
15 why they're conducting such activity. And lastly, if it
16 involves using the broker-dealer to facilitate the
17 criminal activity. And that's a synopsis of both the
18 reporting and the AML program requirements.

19 MS. GONZALEZ: Great. And now I'm going to ask
20 Sarah and Jim to begin and tell me, so what are some of
21 the typologies that you're seeing at your firms.

22 MS. GREEN: Sure. Well, a lot of the
23 typologies certainly are things that we've already talked
24 about today. I think we filed the most SARs on, I would
25 say, account intrusion and account takeover. And that

1 offices and the registered individuals that work at those
2 locations.

3 MS. GONZALEZ: Great. So, Mike, set the stage
4 for us. Will you give us a brief overview of the anti-
5 money laundering, or AML for short, and SAR filing
6 requirements for brokers?

7 MR. RUFINO: Sure. With regard to broker-
8 dealers, as Lourdes said, broker-dealers are required to
9 have an anti-money laundering program. Under Section 352
10 of the Patriot Act, it requires broker-dealers to have
11 such a program. The program needs to be in writing and
12 have like five major components. First and foremost is
13 policies, procedures and internal controls reasonably
14 designed to achieve compliance with the Bank Secrecy Act
15 and the implementing rules. Second, having policies and
16 procedures that can be reasonably expected to detect and
17 cause the reporting of transactions and the implementing
18 of regulations thereunder. Third, the designation of an
19 AML compliance officer. Fourth is having ongoing AML
20 training. And last is an independent test of the firm's
21 AML program.

22 As part of that, as you can see in the
23 reporting requirement, Section 356 of the U.S.A. Patriot
24 Act requires a reporting requirement for broker-dealers.

25 With regard to that, just to give you a synopsis of what

1 includes both new account fraud, so people stealing
2 credentials or stealing people's identity and then
3 opening up new accounts, and also breaking into existing
4 accounts, sometimes using credentials, sometimes using
5 stolen answers to security questions and then developing
6 new credentials and getting into those accounts.

7 I will also add that one fraud that we spent so
8 much time on at FINRA and also the SEC is what I would
9 call this convertible note that is used with microcap
10 firms. So essentially what happens is an investor will
11 loan money to the issuer and the issuer will issue a
12 convertible note which essentially says, if we can't pay
13 you back, we will issue you shares in the -- in the
14 company. A lot of times, the note is not paid back.
15 Many times, because the company is not making any money.
16 So shares are issued. Then the shares are oftentimes
17 unloaded onto the market, into the hands of unsuspecting
18 investors. And that's -- that's a fraud that we see a
19 lot and is -- is terrible to see.

20 I do want to add that you included the
21 suspicious activity reports portion of this panel. This
22 is a big way in which law enforcement and regulators know
23 about all these retail frauds. The woman from the AARP
24 mentioned it briefly. People are embarrassed to report
25 these to law enforcement a lot of times. They're

1 embarrassed to tell relatives. A lot of times, the only
2 way we as regulators and law enforcement know about these
3 crimes is through these suspicious activity reports.

4 MR. FIEBELKORN: That's right. And I'll add,
5 echoing Sarah's comments, there is a current typology
6 that's especially pernicious so I thought I would take a
7 minute to mention it. It's the latest evolution and it
8 shows how the bad actors or cybercriminals continue to
9 evolve their typologies.

10 We as an industry have spent a lot of time
11 battling email account compromises, to use FinCEN's term,
12 where bad actors or cybercriminals would gain control of
13 retail investors' email accounts. And the fraud that we
14 saw in the past was the bad actors would use that email
15 account to send an email to their adviser or registered
16 representative to try and disburse funds from their
17 accounts.

18 As firms have increased awareness around that
19 typology and implemented controls around that typology,
20 we've seen the next iteration of that fraud, which I call
21 real estate email account compromise. And the red flags
22 here are those same bad actors are gaining control of
23 real estate agents' email accounts or title insurance
24 companies or attorneys involved in real estate
25 transactions, and shortly before a retail investor is

1 closing on a house or a property, that bad actor will
2 send an email saying that the account for closing for
3 those funds has changed. Instead of sending those funds
4 to bank A as you previously had been instructed, send
5 them to bank B.

6 That retail investor gives authorized
7 instructions to their financial firm to send those
8 closing funds to bank B, not realizing that bank B
9 account is actually controlled by the bad actor. And
10 this is a fraud that we've seen, that we know many other
11 firms have seen, and therefore we're spending a lot of
12 time trying to educate our employees, advisers and
13 clients about it.

14 MS. GONZALEZ: And then, Mike, do you have
15 anything to add?

16 MR. RUFINO: Just for the most part, as Sarah
17 said, a lot of what we do see is on the microcap
18 securities side. What we do at FINRA is, on an ad hoc
19 basis, depending on our examinations, if we do see
20 underlying problematic behavior, we will go to the SAR
21 database, we will see whether the SAR has been filed by
22 the firm or other firms. So it's important as something
23 that we see, because that's something that we're looking
24 for in terms of fraud against retail investors.

25 MR. ZINN: Lourdes, I'm so sorry to break in,

1 but to the extent that we're talking about -- sorry --
2 about these kinds of funds in the OTC market, I think
3 certainly with that kind of stock loan fraud you're
4 talking about, a lot of times that is involved with a
5 pump and dump scheme as well, where the lender is trying
6 to increase, you know, the number of shares. All they
7 want is a liquid market, basically. And one of the
8 things we have sort of talked to the SEC about, that I
9 don't know if it would be helpful in the way you think
10 about it, is looking at promoters and increasing the
11 disclosure required of promoters and making sure that
12 when that activity is being engaged in, when the pump
13 part of the pump and dump is happening, that might help
14 you backfill and sort of see who's -- you know, who's
15 responsible, who is working with those bad actors.

16 It's sort of tangential but your comment made
17 me think about that potential unfortunate solution.

18 MS. GONZALEZ: So I checked down with the folks
19 in Enforcement. There's a SAR review group, it's called
20 the Office of Market Intelligence within the Division of
21 Enforcement and I asked them what we are seeing here at
22 the SEC, and this is what they told me from the SEC's
23 perspective in SARs that are being filed. Ponzi schemes
24 or Ponzi-like schemes involving misappropriation of
25 funds, offering frauds involving retail investors who are

1 unsophisticated, unaccredited or solicited to participate
2 in the offering in connection with they're members of an
3 affinity group, such as seniors or specific ethnic or
4 religious communities. Also seeing pyramid schemes,
5 which are really multilevel marketing opportunities.
6 Initial coin offerings involving fraudulent conduct in
7 the solicitation of investor funds. Also seeing more SAR
8 filings from brokers with investment adviser platforms.
9 The suspicious activities in these SARs include cherry
10 picking, elder exploitation, investment fraud, excessive
11 fees, other activities such as breach of fiduciary duty,
12 failure to disclose material facts to clients about
13 private investments. So quite the range in the SARs that
14 the SEC is seeing.

15 Let me switch to the next topic which is
16 detecting retail fraud at your firms. So the SAR
17 requirement is very broad and requires reporting of a
18 wide range of suspicious activities. So, Jim and Sarah,
19 in your AML program, how do you detect potentially
20 suspicious activity involving fraud directed at
21 individual investors?

22 Now, you have two very different firms here.
23 Are the detection methods different than those that you
24 would use in, for example, market manipulation? And,
25 Jim, let's start with you.

1 MR. FIEBELKORN: That's right, absolutely. I
 2 often describe AML and antifraud as two halves to the
 3 same coin. From an AML perspective, we are trying to
 4 prevent our firm's platforms and the U.S. financial
 5 system from being exploited by bad actors. From an
 6 antifraud perspective, we're trying to protect clients
 7 from being defrauded. Nonetheless, the way that we
 8 identify and surveil for AML and antifraud are very
 9 similar. Therefore, we've combined much of our antifraud
 10 and AML operations to make sure that we're leveraging
 11 technology, the case management systems are very similar,
 12 the investigations that our teams conduct are very
 13 similar. So there's a lot of overlap between AML and
 14 antifraud. But there are a couple of key differences.

15 Typically, in AML, we're looking for patterns
 16 over time for large amounts of money moving through an
 17 account. From an antifraud perspective, we're much more
 18 interested in analyzing transactions on a one-by-one
 19 basis in almost real time, because the goal is to try and
 20 prevent unauthorized money from leaving the firm in the
 21 first place. So a lot of overlap but a few differences.

22 MS. GREEN: Right. I would add, so in your
 23 typical what you might think of money laundering schemes,
 24 we rely on a lot of automated surveillances to look at
 25 things like sudden change in activity. For instance,

1 maybe a senior investor who is buying a microcap stock
 2 for the first time. We would certainly look at things
 3 like international wires, when they haven't been sent
 4 before. Unrelated customers all sending money to the
 5 same place, that can be an indication of, for instance, a
 6 Ponzi scheme or an unregistered investment professional.
 7 That's for more, I would say, common money laundering
 8 scenarios.

9 On the fraud side, when we think of the account
 10 intrusion and so forth, our most important detection
 11 scenario is people. It's the people on the phones, it's
 12 the people looking at, say, when people come into their
 13 account online. They're picking up the phone, they are
 14 submitting internal referrals to us and telling us that
 15 something doesn't seem right.

16 And for this reason, it is critically important
 17 within a financial institution such as both of ours that
 18 we train everybody on the indicia of retail fraud and we
 19 have policies and procedures and quality assurance to
 20 make sure that when we are receiving indicia of fraud in
 21 all areas of the firm, that those people know to give us
 22 a call and let us know about it and that they are
 23 escalating the types of things that we need to hear
 24 about.

25 MS. GONZALEZ: Great. This leads me to my next

1 question which is a particular challenge, I think, in a
 2 lot of firms. Often, when we see that something goes
 3 wrong at a firm, it wasn't that the suspicious activity
 4 was missed entirely, it was that the information formed
 5 the basis of a SAR didn't get to the right group. And
 6 how do you address this problem at your firms?

7 MR. FIEBELKORN: That's right, Lourdes.

8 Several different ways, echoing what Sarah just said in
 9 terms of training and education. We provide AML and
 10 antifraud training to all of our employees, broadly. And
 11 then, as new fraud risks or trends emerge, we will do
 12 targeted trainings with the groups in the firm that would
 13 be most likely to experience them, typically in an
 14 operational area like new account openings or wire
 15 processing.

16 Ameriprise is fortunate to have a business
 17 model where our advisers typically meet with clients face
 18 to face. It's a financial planning relationship. They
 19 have a deep knowledge of our clients' financial needs.
 20 And therefore, they are very well positioned to be able
 21 to identify financial transactions that are out of
 22 pattern for the client and refer those. So we spend a
 23 lot of time making sure that all of our employees and
 24 advisers know how to refer, to make sure that information
 25 is getting into the hands of AML and antifraud.

1 A couple of other methods that I'll mention.
 2 Number one is systematizing high-risk transactions like
 3 Sarah mentioned. Human referrals, referrals where people
 4 are always valuable but for those transactions that we
 5 know are high risk, trying to implement technology so
 6 that they're reviewed beforehand, so you don't rely on a
 7 person having to push a button.

8 I think it's very important for our industry,
 9 financial firms, to be talking with each other and talk
 10 about new risks that they see emerging, because that
 11 helps protect our firms and helps protect our clients.
 12 And we're also seeing a trend in the industry where
 13 vendors, third party vendors, are providing fraud-related
 14 services, where they aggregate information that might be
 15 indicative of fraud, such as devices that have been used
 16 for fraud, bad IP addresses, bad phone numbers,
 17 collecting that from financial firms, anonymizing it and
 18 then sharing that information back down so it can become
 19 a source of intelligence that a single financial firm, in
 20 and of themselves, wouldn't have.

21 MS. GONZALEZ: Great. So, Mike, I want to turn
 22 to you and talk a little bit about how SARs are used from
 23 the FINRA perspective and how valuable they are. And
 24 before I do that, I want to preface it and explain how
 25 SARs are used from the SEC perspective and the sort of

1 review that we do.
 2 So the SEC aspires to review all SARs by
 3 broker-dealers as well as other financial institutions
 4 that report on potential securities violations. There's
 5 also a SAR filing hotline for more serious tips and we
 6 urge people to use it. It's 202-551-SARS. Talking to
 7 our Enforcement colleagues, they told me that in the past
 8 year, past fiscal year, the SEC reviewed approximately
 9 30,000 SARs which were a combination of securities, bank
 10 and money service businesses. And they do one of three
 11 things. They may do a triage process where they look at
 12 SARs individually, they may do an analytical process
 13 where they aggregate large groups of SARs looking for
 14 trends, and the third way is they do a daily proactive
 15 search where they look for certain securities-related
 16 categories of SARs.

17 So, Mike, I am going to turn it over to you
 18 because you're our partners in this effort. How does
 19 FINRA use SARs and review SARs?

20 MR. RUFINO: Sure. And first, as you said, we
 21 are partners in that. And of all the reviews I've been
 22 involved in over the years, the partnership that we have
 23 with the SEC in terms of making sure we're lockstep on
 24 conducting reviews, making sure that we're consistent,
 25 has really been kind of, in my mind, you know, the kind

1 of like the model for what we can do from a coordination
 2 perspective.

3 With that being said, we know that the industry
 4 spends a lot of time, effort and money on their anti-
 5 money laundering program. But when you look at the end
 6 goal of protecting retail investors, it's really money
 7 well spent. And I'll share with you some examples as
 8 well.

9 When you look at what we do, we conduct, as I
 10 said before, many examinations in a given year. And what
 11 we will do is we have a program rule, our Rule 3310,
 12 FINRA Rule 3310, is an AML program rule. As part of that
 13 review, we will look at underlying activity. We will try
 14 to identify what might be some high -- you know, high
 15 kind of not suspicious but questionable activity that we
 16 want to ask questions of the firm. We'll test a firm's
 17 systems. And what we'll sometimes do is we'll identify
 18 what we -- we'll look at money movements.

19 In this one example, we saw some money
 20 movements that were somewhat questionable. When you see
 21 a multitude, you know, wiring money, say, to the same
 22 account, the question is why. Many brokers will have
 23 outside business activities. So when you look at their
 24 U4 and the question is -- and sometimes it's outside
 25 activity that the firm is unaware of and they're never

1 told about it.
 2 In this one example, we had money movements
 3 that were somewhat questionable. We went to the SAR
 4 database and realized that a bank had also filed a SAR
 5 with regard to this individual. And when you read the
 6 narrative of the bank, it really gave us a lot more
 7 information that really helped us uncover a Ponzi-like
 8 scheme on an investment fraud.

9 So when we look at the importance of it,
 10 sometimes you may be filing it, looking at it as activity
 11 in your respective financial institution. But from a law
 12 enforcement, regulators, sometimes other activities --
 13 we're looking at it through the lens of one broker-
 14 dealer. But if we see that it's going on elsewhere -- a
 15 lot of conversations today are microcap. Well, microcap
 16 happens, there's a buy and a sell somewhere, activities,
 17 money movements going through. Because the name of the
 18 game is to move the money sometimes through the financial
 19 system. And if you can muddy the waters a little bit,
 20 then you want to move the money, you know, to, you know,
 21 the end -- the end state. So when we see these SARs
 22 being filed, it's invaluable to the regulators,
 23 invaluable to law enforcement.

24 And I know sometimes firms will kind of raise
 25 their hand and say, is it really being utilized by the

1 regulators? I will assure you that it's being used day
 2 in and day out.

3 MS. GONZALEZ: Thank you, Mike. So I often
 4 think of SARs as only as useful as the information that
 5 is on the SAR. Is there information from your
 6 perspective that is often omitted that you wish were
 7 there?

8 MR. RUFINO: What sometimes happens, Lourdes,
 9 is
 10 -- first and foremost, as you said, the narrative is
 11 paramount to the SAR. Those checkboxes are very
 12 important. They're also critical for doing analytics
 13 because you can analyze off a checkbox. It's harder to
 14 do off narratives without kind of machine learning or
 15 artificial intelligence. But the narrative is critical,
 16 critically important, when you look at overall a SAR.

17 Sometimes what happens is we'll see -- they'll
 18 list the transactions in the narrative but they won't say
 19 why the activity is suspicious or why they have concerns.
 20 So it's great to have all of that activity but without
 21 the underlying rationale -- because the institution is
 22 going to know best why they think it's suspicious and why
 23 they're filing the SAR. So the more that you can take
 24 the time and effort to identify the activity, the
 25 individuals involved and inviting a clear, concise and

1 really comprehensive narrative goes a long way.
 2 MS. GONZALEZ: That's great. So from the SEC's
 3 perspective, we urge you to consider the SAR drafting
 4 tips that FinCEN has issued before. And the narrative,
 5 make sure to include who, what, when, where and why.
 6 That's very helpful. Because the best leads tell a good
 7 story. And finally, if it's possible to state up front
 8 in the summary what the problem is. And please avoid
 9 using all caps. That's very helpful to reviewers.

10 And the last part, we only have a few minutes,
 11 and I'm going to turn it to Jim and Sarah, to --
 12 considering everything that you have filed, what sort of
 13 -- if you have any further observations on sort of trends
 14 that you're seeing and, finally, what sort of guidance
 15 would you suggest if any that regulators can give to the
 16 industry? Knowing full well that we are providing
 17 guidance not just for the biggest firms, but for a lot of
 18 firms that have a very small employee base.

19 MS. GREEN: Sure. Well, I think the one thing
 20 we've really seen in the AML and the SAR area is that
 21 what we are filing on is very different from what firms
 22 were filing on in 2003 when this rule was passed, right?

23 We are expecting -- there are checkboxes on the form for
 24 account intrusion, for elder exploitation. A lot of
 25 things, and identity theft.

1 As that scope broadens of what we are expecting
 2 financial institutions to file on, which I think is very
 3 important, and financial institutions play a key
 4 gatekeeper role in this area, I think that we should be
 5 mindful of laying out expectations for the areas on which
 6 we are expecting firms to file in the form of, say, an OC
 7 risk alert or other guidance, as opposed to say an
 8 enforcement action.

9 MR. FIEBELKORN: That's right. Echoing Sarah's
 10 comments, I think in the industry as a whole, many firms
 11 have started to reach a tipping point where they file
 12 more fraud-related SARs than AML-related SARs. And
 13 that's because of the increasing fraud attempts across
 14 the industry, as we've heard the previous speakers talk
 15 about.

16 Certainly, in our firm, we're very attuned to
 17 vulnerable client issues, as retail investors start to
 18 age and typically a lot of their assets are held within
 19 broker-dealers in the form of IRAs or 401(k) accounts.
 20 So making sure that we have good relationships with state
 21 regulators and adult protective services can be very
 22 useful towards that end.

23 And in terms of asking for what kind of
 24 guidance would be beneficial, Lourdes, OC alerts are very
 25 helpful. But also just encouraging information sharing

1 between financial firms. Because if there is a fraud
 2 targeting a retail investor, as Mike said, typically that
 3 money will move between financial institutions. And to
 4 the extent that financial institutions are able to
 5 communicate with each other pretty quickly, when we're
 6 able to do that, we have a much better chance of
 7 protecting clients and keeping client assets safe.

8 MS. GONZALEZ: Thank you, Jim. And I'm going
 9 to end by asking Mike to -- if you could give us just a
 10 little recap of the guidance that's out there? Because
 11 FINRA has actually issued a lot of very good guidance to
 12 firms over the years.

13 MR. RUFINO: There's a lot of guidance out
 14 there for the membership to really -- and the broker-
 15 dealer community to utilize. First and foremost is, you
 16 look at the websites of FINRA and the SEC, dedicated
 17 sections with regard to anti-money laundering. We
 18 recently updated our small firm template for the smaller
 19 firms that really gives an outline for a firm to follow
 20 in terms of putting together an AML program.

21 You also look at, as we said, the risk alerts
 22 put out by the SEC. We've issued many reg notices with
 23 regard to AML. We issued one even when the rules were
 24 first promulgated that really laid out a lot of red flags
 25 for the firms to consider. When you look at firms'

1 overall programs, a lot of them are incorporated within
 2 there.

3 The typologies. When you look at the typology
 4 put out by FinCEN, put out by FATF, those are great
 5 opportunities for firms to learn from and say, if it's
 6 happening somewhere else, these are the type of
 7 typologies. Is it happening within my respective
 8 organization?

9 So when you took this all together, and just
 10 the fact that you can pick up the phone and communicate
 11 with the regulators -- as we've always said, we're here
 12 to assist the broker-dealer community as best as we can.
 13 And working with the broker-dealers, with the
 14 associations, that's part of our responsibility as
 15 regulators to make sure that, you know, we're working
 16 with you to assist you.

17 MS. GONZALEZ: Thank you, Mike. For our part,
 18 we work with the broker-dealer community. I've worked
 19 for a long time with Jim and Sarah. I've also worked for
 20 a long time with Mike on these issues. And we continue -
 21 - we look forward to continuing that. We also represent
 22 the SEC internationally, so there are a lot of players
 23 here. But we learn from you, so we're very grateful for
 24 that.

25 And with that, I'm going to turn it over to

1 Lizzie.
 2 MS. BAIRD: Thank you, Lourdes. And thank you,
 3 Sarah, Mike and Jim. And I want to thank all the
 4 panelists for helping us to paint the picture of how
 5 protections are provided to retail investors through the
 6 requirement for disclosures and reviews before a security
 7 can be quoted, for registration requirements, for
 8 entities engaged in the securities business, and even how
 9 registered entities help us to surveil for investors who
 10 may be engaged in illegal activity.

11 This discussion will continue at 2:00 with our
 12 final panel. We are going to take a quick break now
 13 until then. Thank you.

14 (Whereupon, at 1:00 p.m., a luncheon recess was
 15 taken.)

16 A F T E R N O O N S E S S I O N

17 MR. SABELLA: Okay, I think we're going to kick
 18 off, if folks can find their seats, please.

19 Great, so I would like to welcome everyone back
 20 who has been with us since this morning. And for those
 21 of you who weren't, welcome.

22 My name, for those of you who aren't familiar
 23 with me, I'm Christian Sabella. I am the other deputy
 24 director for Trading and Markets. I know that Brett
 25 Redfearn and Lizzie Baird were here this morning. And so

1 I am the third piece of that puzzle.

2 We're looking very much forward to today's
 3 third and final panel, scheduled for about an hour and 30
 4 minutes, focusing on transfer agents, trading halts and
 5 investor education. And that's why we have such a long
 6 table of panelists who are here today and we will work
 7 our way down and thank everyone again for agreeing to
 8 participate.

9 Before we get into the meat of this, I just
 10 want to introduce the panelists -- or, sorry, the
 11 moderators who will be helping facilitate the discussion
 12 today. So immediately to my left, you have Moshe
 13 Rothman, who is an assistant director in the Division of
 14 Trading and Markets. He will be moderating the transfer
 15 agent subpanel with the assistance of Mark Saltzburg here
 16 as well.

17 For those of you who aren't familiar with Mark
 18 and Moshe, they are part of the team that spearheaded the
 19 Commission's 2015 concept release and advanced notice of
 20 proposed rulemaking on transfer agents. So this is part
 21 of the core team in Trading and Markets dealing with
 22 those policy issues.

23 Once we move beyond the transfer agent issues
 24 into trading halts, the moderation will turn to lady to
 25 my right, Racquel Russell, who is an associate general

1 counsel at FINRA and also former alum of the Commission
 2 Staff, so we're happy to see her again.

3 And then finally, we'll be closing out on the
 4 investor education piece with Owen Donley, who is just
 5 sitting to the right of Racquel, who is the chief counsel
 6 in the Office of Investor Education and Advocacy and will
 7 be moderating that final panel.

8 So let's jump in right away. So the first
 9 subpanel discussion will focus on transfer agents. And
 10 we know there's a whole range of issues to discuss with
 11 respect to policy matters and transfer agents, given the
 12 focus of today's roundtable on measures to prevent retail
 13 fraud. We're going to try to keep the discussion very
 14 much on the point of that theme. But in particular
 15 today, I think we're looking forward to discussion about
 16 the role transfer agents play in removing restrictive
 17 legends.

18 For those of you who follow this space, you
 19 would be aware that transfer agents will provide services
 20 to issuers of restricted and control securities and
 21 they're generally responsible for processing requests
 22 from selling shareholders to remove these restrictive
 23 legends in connection with the intended resale of the
 24 securities by the owners. Now, if the transfer agent
 25 improperly or inappropriately removes a legend, the

1 result could be the facilitation of an illegal public
 2 distribution of securities and that could harm investors,
 3 including retail investors. And this is a topic that was
 4 discussed in not a small amount of detail in the 2015
 5 advanced notice of proposed rulemaking and concept
 6 release. And so I don't have to say that mouthful again,
 7 we will just refer to it as the concept release.

8 But for today's discussion, as I said, we're
 9 going to focus on some of the issues related to transfer
 10 agent processes for removing restrictive legends and
 11 potential regulatory or other solutions that may be
 12 implicated with respect to how these issues interact with
 13 the problem of retail fraud.

14 And so with that, I will turn it over to Moshe
 15 to take us further into the discussion and start off the
 16 dialogue with the panelists.

17 MR. ROTHMAN: Thanks, Christian. Before I turn
 18 it over to the panelists, I would like to just set the
 19 stage for the discussion of this subpanel today. I don't
 20 think it will come as a surprise to anybody who is
 21 familiar with this space that curbing illegal
 22 distributions of securities in violation of Section 5 of
 23 the Securities Act is a priority here in Trading and
 24 Markets and more broadly within the Commission.

25 The Commission has brought a number of

1 enforcement actions in this area, often involving small
2 microcap companies. In some of these transactions, a key
3 step in the illegal distribution is the removal of
4 restrictive legends to make what would otherwise be
5 restricted or control securities freely tradable. In
6 these instances, transfer agents may be positioned to
7 serve as a gatekeeper in preventing the fraud, due to
8 their role in processing those requests for the removal
9 of the restrictive legend.

10 While we recognize that this is a complicated
11 area that, on its own, could probably merit its own full-
12 day roundtable, for our purposes today we would like to
13 focus on two areas in particular. First, we'd like to
14 hear from our panelists about their day-to-day practices
15 and experiences regarding legend removal. And second, in
16 light of those day-to-day practices and experiences, we'd
17 like to hear their views on some of the potential
18 policymaking solutions that were discussed in the concept
19 release that Christian alluded to. It's our hope that
20 through this discussion today we could gain further
21 insight into the many different perspectives on and
22 potential solutions to these complex issues.

23 So before we begin, I'd like to turn it over to
24 our panelists so they can introduce themselves. David,
25 if you don't mind, let's start with you.

1 MR. BECKER: Sure, I'm David Becker. I'm the
2 general counsel and chief risk and compliance officer for
3 Equiniti Trust Company, doing business as EQ by Equiniti.
4 We are the business that used to be known as Wells Fargo
5 Shareowner Services. We changed ownership back in
6 February.

7 MR. FRANZ: Robert Franz from Broadridge. I'm
8 the senior director of compliance for the transfer agent.

9 MR. HARMON: Mark Harmon. I'm a partner at
10 Hodgson Russ's New York City office for the last 25
11 years. And a substantial portion of my practice has been
12 representing transfer agents that don't have in-house
13 counsel and assisting them in review of issuances, legend
14 removals and compliance with state and federal law.

15 MS. MANNING: I'm Andrea Manning. I'm
16 corporate counsel at Computershare. I've been at
17 Computershare for over 20 years now in the TA industry.
18 I'm also the cochair of the Securities Transfer
19 Association Legal Committee.

20 MR. ROTHMAN: Thank you all and welcome.

21 So to start the discussion, we thought it might
22 make sense for each of our transfer agent panelists and,
23 Mark, maybe your experience with your clients, start with
24 maybe a discussion of what your firm or your clients do
25 when they receive requests to remove restrictive legends

1 on restricted securities.

2 What's the standard practice in sort of the
3 day-to-day, run-of-the-mill legend removal requests?
4 What do you do to process the transaction? What does it
5 look like from your perspective? And if you have
6 specific examples or anything like that, it might help
7 set the table for what the normal process might look like
8 and that will help us get into some of the trickier,
9 thornier issues that we see in this space.

10 MR. BECKER: Sure. So I've been at three
11 different transfer agents, actually four if you count one
12 that was in a merger. A couple of things we do -- and
13 remember that transfer agents by law, according to the
14 Securities and Exchange Act, are -- take their actions on
15 behalf of the issuer, not on behalf of the shareholder.
16 So that's the first thing we have to keep in mind.

17 But when we get in restrictive legends that
18 have to be removed, we get in the letters, what do we
19 actually do with those? So the first thing we do is we
20 review the letter to make sure it's consistent. Does it
21 actually say what it's supposed to say? Does it have the
22 required time parameters of ownership? Does it say
23 everything -- does it look professional? Let's start
24 with that.

25 What we also do is we check -- and we started

1 this ourselves several years ago at a prior transfer
2 agent and I've carried it forward to where we are today.

3 We check a list of attorneys who have been sanctioned by
4 the Commission, particularly for bad 144 letters. And
5 there's a number of those that we've uncovered. But, in
6 addition to that, and something that we uncovered -- that
7 we discovered just a little while ago, is that one of the
8 market participants, OTC Markets, actually maintains a
9 page that has bad attorneys and bad accountants and
10 others, and we do look at that as well to make sure we
11 didn't miss anybody. So we do look for all of that as we
12 go through it.

13 Once we do that, we then move forward with the
14 processing of that, depending on how we feel about that
15 letter. And if we have questions, we do look further
16 into the letter itself. We might look at the law firm or
17 the lawyer involved to make sure we're comfortable with
18 them.

19 I've never been a big fan of the lawyers who
20 advertise themselves as 144 lawyers. There's a couple
21 websites out there like that. I've never been a big fan
22 of those because I think they're just shops that are just
23 doing this quickly and possibly inappropriately, although
24 not always inappropriately. But we do like to check
25 those as well.

1 MR. FRANZ: At Broadridge, we also have a
 2 practice where we check the Department of Justice list of
 3 disbarred attorneys. We check the OTC Markets list that
 4 David mentioned. We do a quality control review of the
 5 opinion. Is it addressed appropriately to the transfer
 6 agent, as opposed to the issuer. We can make exceptions
 7 there, if need be. Does it address all the points that
 8 are required to qualify for the exemption, things like
 9 the holding period, the volume limitations, the reporting
 10 status of the issuer. The presentation will also include
 11 a broker's rep letter for affiliates, a seller's rep
 12 letter, and we'll quality control all those documents and
 13 make sure that everything relates to the same transaction
 14 because those things can get mixed up.

15 You know, I don't want to add anything, Mark.

16 MR. HARMON: So speaking for the smaller agents
 17 and clients, it would be a lot -- the world would be a
 18 lot easier if all they got were 144 opinions, because
 19 those are really straightforward and they receive the
 20 opinion, they make sure that the opinion matches to the
 21 information they have, they do as much as they can to
 22 obtain documentary evidence on shareholder
 23 representations, broker representations. But the real
 24 issues, I think, for them, the challenges for them come
 25 because of the Rule 144I exclusion for former shell

1 companies. So it's very difficult to make that
 2 determination when you're getting conflicting
 3 information. They do what they can to determine that.
 4 They then have to deal with 4(a)(1) opinions for shares
 5 having come to rest if they can't qualify for the 144
 6 safe harbor.

7 But beyond legend removal and something that
 8 wasn't mentioned in terms of this space are the issuance
 9 requests that come for free-trading stock other than
 10 through registered shares. And that frequently involves
 11 debt conversions, 3(a)(10) offerings, and a myriad of
 12 other scenarios that people can try to come up with. The
 13 problem for the smaller agents then is they try to get
 14 information but don't have any authority to compel
 15 providing information, so they're stuck between trying to
 16 amass the information and their duty and obligation to
 17 effect the transfer because, under state law, the failure
 18 to remove the legend is a violation of state law and
 19 exposes them to liability for conversion damages or delay
 20 damages on the value of the stock.

21 MS. MANNING: I don't have too much more to
 22 add. I mean, I think, you know, we all look for
 23 opinions, we look for rep letters. Because Computershare
 24 is one of the largest TAs in the country, and so we
 25 process thousands of restricted stock items a year, so we

1 have a very detailed guide for various scenarios for our
 2 staff that we train them on, so that they can, you know,
 3 maneuver their way through the various scenarios.

4 As indicated, Rule 144 are the kind of easy,
 5 vanilla transactions. But we have a lot of things that
 6 kind of go outside of that. Reg S, for example, has
 7 become more common. 144(a). So there's a variety of
 8 other exemptions and abilities to remove restrictive
 9 legends, so we have a very detailed guide that goes
 10 through various scenarios in terms of what to look for
 11 for those transactions.

12 MR. ROTHMAN: That's really helpful. I think
 13 one of the things that, at the Staff level, we're
 14 interested in and we've talked about internally is, it
 15 seems like a lot of the recommendations deal with the
 16 Rule 144, kind of the standard exception. So a lot of
 17 the potential solutions maybe might gear towards that
 18 more routine, easier transaction, if you will. So I
 19 heard everyone kind of allude to this easy -- easy
 20 situation. But Mark and Andrea, in particular, you guys
 21 mentioned sort of these outliers or these additional
 22 situations.

23 I think one area that would be helpful and we
 24 think might be worth discussing is what do you do in
 25 those? How does the process look different? What

1 changes? What additional steps might you take or
 2 different steps might you take if you're not dealing with
 3 a vanilla 144 request or something like that?

4 So, Mark, if you see anything in your area that
 5 you can speak to that? And I would invite any of the
 6 other panelists as well to jump in. I'm sure you all see
 7 those as well.

8 MR. HARMON: So debt conversions or the use of
 9 debt to create tacking of holding periods is a particular
 10 problem. I know one of the markers for my clients in
 11 reviewing those is getting evidence that the debt was
 12 actually incurred and that it's not just a debt, but that
 13 it was actually a security because the tacking is based
 14 upon the exchange of one security for another. So
 15 there's an effort on the part of the agents to obtain
 16 independent evidence that consideration was paid.

17 In the 3(a)(10) space, I know that you need to
 18 get a copy of the court order and look at the background
 19 between the court order and then you try to take a look
 20 at the parties to the litigation that led to the issuance
 21 of the court order. Because too frequently, these
 22 actions are brought in really small courts where the
 23 judges are not familiar with securities laws, don't
 24 understand the idea of a fairness hearing and are just
 25 happy to get the case off their docket and sign an order.

1 So it creates, again, a particular problem for agents
2 trying to do their job who would reject that request and
3 then expose themselves to the potential liability of the
4 loss of a customer because they're trying to get
5 information that they don't necessarily have a right to
6 get but that they think that they need in order to create
7 a good file.

8 In most instances, I think that they create or
9 try to create that file but they could use some
10 assistance in protecting them, A, in getting the
11 information they need, making sure that they have a right
12 to get the opinion of counsel, that the opinion matches,
13 and also removes them from the difficult position of
14 having to be exposed to liability if they're trying to do
15 their job and question the propriety of the opinion or
16 the issuance request.

17 MR. BECKER: Well, I think it goes beyond just
18 the potential risk of loss of a customer. There's also a
19 conflict between what we have to do in the eyes of the
20 SEC in terms of monitoring the transaction that's coming
21 in and what state law mandates. There's a conflict in
22 that area because state law mandates that unless we see
23 something overtly wrong, we're supposed to act on it and
24 process that transaction. And that's not what the
25 Commission and the industry expect from us. And that

1 leads to a major issue.

2 I know that came up in some of the comment
3 letters that were sent in in response to the concept
4 release.

5 MR. SALTZBURG: I'd like to ask one follow-up
6 question. Robert, you mentioned some of the issues that
7 are attendant to control securities that are held by an
8 affiliate, like volume limitations and the reporting
9 status of the issuer and the holding period. I just
10 wanted to focus a little bit more on where there's an
11 affiliate and a controlled securities situation. Does
12 that -- that's a more complex situation than when you
13 have a nonaffiliate and the holding period is met.

14 Are there additional steps in your standard
15 practice that you use to examine and address those
16 issues?

17 MR. FRANZ: So we do have a policy procedure
18 guide that outlines all the different scenarios for
19 removing restrictions as it relates to affiliate versus
20 nonaffiliate for 144 restrictions. The bigger
21 difference, really the most material difference between
22 the documentation requirements is the broker rep letter,
23 what you need for the affiliate versus the nonaffiliate.

24 And that's where the broker attests to the fact that
25 it's an ordinary brokerage transaction.

1 But I think that's the biggest difference. But
2 the importance, of course, is on having the staff -- I
3 think Andrea mentioned having a guide for the staff to
4 follow that, you know, when something is called into
5 question, most of it is addressed in the policy and
6 issues can be escalated to counsel or internal compliance
7 for review.

8 MR. BECKER: Yeah, I mean, along those lines,
9 remember that our employees are not generally -- they're
10 rarely registered individuals. They don't have extensive
11 training in the federal securities laws and rules. They
12 perform administrative tasks. So we have to give them
13 outlines of what to look for.

14 But, of course, when an anomaly arises, it's
15 going to raise questions. And that causes delays which
16 can lead to further issues as we go down the road.

17 MR. SABELLA: I just wanted to drill into one
18 topic that I think David unearthed initially, which is
19 the ability to get the information in the first place.
20 So focusing on -- forget about like if you get all the
21 information and you see some anomalies or something, but
22 even the right to get information in the first place.
23 How important is that, do you think, for each of the
24 panelists, to your ability to do the work you need to do
25 in this area? In other words, recognizing UCC Article 8

1 does put pressure right on you from a state law
2 perspective to move things quickly, you know, how helpful
3 would it be if basically you had a firmer ability to get
4 the information you needed sooner rather than later so
5 you could move along. As opposed to, well, even if you
6 get the information quickly, it's still going to be a
7 complex facts and circumstances process?

8 MR. FRANZ: I think the first thing it does is
9 it addresses kind of the headaches that arise between the
10 agent and its client in pushing for the information. Or,
11 you know, the shareholder and the issuer in being asked
12 for the information. So a lot of times, you'll get
13 pushback because they feel that the documentation they've
14 supplied is sufficient and there's no reason to push
15 further. And now, as I think all of us have mentioned,
16 there's the conflict between needing to do the
17 transaction timely and needing to ensure that it's done
18 properly. And I think that having a regulation that
19 specifically points to requirements in this case, it
20 makes it easier for the transfer agent to push.

21 MR. HARMON: I think it would be incredibly
22 helpful to have that. I cannot tell you the number of
23 calls I get from disgruntled shareholders saying that XYZ
24 transfer agent doesn't require that. And fortunately,
25 many times, I also represent XYZ and I know that that's

1 not true. But still, that's something that you hear all
2 the time. "Why are you asking for this? Nobody else
3 asks for this." And if there were some assistance in
4 saying, this is what you need and the transfer agent has
5 the right to ask for it, then they would have a much
6 easier time doing their job and, in my view, most of
7 these agents are trying to do their job.

8 MS. MANNING: Yeah, I agree. Because
9 sometimes, you know, we'll get a legal opinion and it has
10 absolutely no detail in it. You know, they'll just say
11 that we believe, you know, this transaction is exempt.
12 And then we have to go back and we have to ask for more
13 information and sometimes they push back and say, well,
14 we're the issuer, we're instructing you to do it. We've
15 given you the opinion that says it's okay.

16 But we need to understand the facts a little
17 bit better and there's pushback. And that creates delay
18 and sometimes shareholders will be calling and saying,
19 why hasn't this been processed yet? And the issuer is
20 not getting back to us quickly.

21 So I think having some parameters there for the
22 types of information we should be able to obtain would be
23 very helpful.

24 MR. BECKER: And I think along those lines,
25 look, we all know it's really difficult if not impossible

1 have disciplinary history.

2 You know, fortunately, we do get a lot of
3 opinions from, you know, a lot of the larger firms. So
4 those don't, you know, usually have the same scrutiny.
5 But certainly, if it's not coming directly from issuer's
6 counsel, internal or external, we do take a closer look
7 at those opinions.

8 MR. BECKER: Agreed. We try not to have to go
9 outside the four corners if we don't have to, because
10 that just opens us up to a greater amount of additional
11 work, delay. But if we have to do it, we will do it,
12 depending on the circumstances.

13 MR. ROTHMAN: Thank you for that. I think just
14 sort of pivoting off of something that David mentioned in
15 terms of the safe harbor and some of the other potential
16 policy solutions, one of the -- as I think you all know,
17 in the 2015 concept release, we discussed three potential
18 policy solutions in this area with respect to transfer
19 agents and their role in removing restrictive legends.

20 The first approach would involve a standard
21 that prohibits transfer agent negligence in facilitating
22 illegal distributions, such as by removing legends while
23 being aware of illegality and turning a blind eye, or
24 being ignorant of apparent illegality. This has sort of
25 been referred to as an antifraud approach, if you will.

1 to lay out you have to have A, B, C, D, E, F, G. But I
2 think if it was to be set up in such a way that it acted
3 more like a safe harbor, as was suggested in some of the
4 comment letters, particularly the STA letter to the
5 concept release, where as long as you have A, B, C, D, E,
6 F and G, you have some protection against liability.
7 That might be more helpful than a prescription that says
8 you absolutely have to have and get A, B, C, D, E, F, G.

9 MR. SALTZBURG: One quick follow up before we
10 get into those issues about potential policymaking
11 solutions, David and Andrea and others, you mentioned
12 your legal review process and some of your policies. I'm
13 just wondering if you could just spend very quickly a
14 moment addressing how much time and resources do you
15 spend on the legal review and then, you know, beyond the
16 legal review, of the opinions and other supporting
17 documents, do you do independent due diligence, you know,
18 outside the four corners of those documents?

19 MS. MANNING: Our process to kind of go outside
20 is really when we're getting shareholder counsel
21 opinions, rather than an opinion from the issuer's
22 counsel. In those situations, we do take a closer look,
23 is it a national law firm, is it a small solo
24 practitioner who is giving the opinion? We will look
25 into make sure they're licensed, make sure they don't

1 The second approach would be more flexible and
2 principles based, creating a standard that would require
3 transfer agents to adopt policies and procedures
4 addressing how they process restricted securities.

5 And the third approach is the one that you
6 alluded to, David, with -- that would create a safe
7 harbor for potential participant liability for illegal
8 distributions if a transfer agent took certain steps in
9 processing those restrictive legend removal requests.

10 And another approach that has been discussed
11 that we've seen in comments and talked to among industry
12 participants is that the Commission might mandate legal
13 opinions in all restrictive legend removal situations.

14 I'd like to ask each of the panelists, just in
15 your view, if you have a particular view about any of
16 these approaches, if you think any of them have
17 particular merit from a cost/benefit approach or a
18 practicality approach. And specifically, how -- in light
19 of that view, how do you understand that that particular
20 approach would work in practice for how you guys do
21 things?

22 MR. HARMON: So the first option, I would say,
23 sounds like it's already covered by application of
24 potential violations of Section 5, to which transfer
25 agents -- for which transfer agents might be liable and

1 for which they've been held liable in various situations,
2 and probably increasingly in the recent past. And I
3 think that agents are already very aware of the potential
4 for being charged with a Section 5 violation if they
5 don't act in good faith. So I don't know that layering
6 it on with a specific rule is going to make a lot of
7 difference.

8 Having specific policies and procedures is
9 difficult because of the myriad of options for legend
10 removal or issuance free trading would make it virtually
11 impossible to cover every area. And so you could have a
12 generalized policy and procedure talking about due
13 diligence but the specifics of it aren't going to work
14 because it's something new every time.

15 So I -- you know, I think that those two
16 probably are not good. I think it absolutely would be
17 helpful to mandate that an opinion is required, whether
18 it's a shareholder's opinion, which creates more
19 problems, or issuer's opinion, but the requirement to
20 have an opinion would at least give the transfer agents
21 leverage when they go to somebody and say, we need an
22 opinion that fully covers every aspect of this, so not
23 just an opinion, as Andrea said, that said we think that
24 this is okay, but an opinion that addresses tacking, that
25 addresses affiliate status, shell status, everything that

1 is on the checklist for what you need to do. So that, I
2 think -- that, together with authorizing transfer agents
3 or just recommending that transfer agents have the
4 ability to get independent support for that would go a
5 long way in assisting transfer agents in fulfilling the
6 gatekeeper function that the SEC imposes on them.

7 MR. BECKER: Well, I hate the term
8 "gatekeeper." I think it raises implications that are
9 just incorrect, but we can talk about that offline.

10 I agree with Mark. You can't have something
11 that says you have to have A, B, C, D, E, F. But if you
12 have something that says, if you have A, B, C, D, E, F,
13 you've got air cover, I think would be very helpful. So
14 really providing the safe harbor type of provision.

15 MR. FRANZ: We've talked about it, I think all
16 four of us. The requirement for an opinion would be
17 great. Because we get a lot of pushback on folks who
18 don't want to pay for the opinion. And you don't have a
19 transfer agent, I don't think, that will do it without an
20 opinion. So you'd kind of resolve that impasse.

21 And I think if you can develop a rule that
22 prescribes not specific policies or steps but a series of
23 actions that can be taken reasonably to provide for a
24 safe harbor for the transfer agent, I think that works.
25 Things like ensuring that there is a policy or procedure

1 available to staff that includes details of opinion
2 requirements, letter requirements, details around the
3 regulations for which the exemptions apply, I think that
4 helps. I think a minimum level of due diligence on the
5 firms presenting those opinions. It's hard to say or
6 hard to list specific red flags, because they change
7 every day. But a reasonable level of due diligence on
8 the issuing firm, I think, is also something that could
9 fit into that. And if those conditions are met by the
10 agent, a safe harbor is provided, if an action is brought
11 as a result of that transaction.

12 MS. MANNING: I guess I agree on the safe
13 harbor as kind of the best approach here. It provides
14 the protection, I think, for investors and the industry.
15 It also will set some, I think, commercial certainty
16 amongst agents, brokers, issuers. Everyone will know
17 kind of what the rules are so there will be less pushback
18 and the expectations will be set up front as to what
19 agents are going to be looking for to remove that legend.
20 So I think that's also the best approach.

21 MR. SALTZBURG: I would like to drill down a
22 little bit more on two of the concepts that were
23 mentioned here, the notion of mandating legal opinions
24 and the creation of a safe harbor. I'd like to ask
25 panelists to examine a potential downside of that issue,

1 particularly the question of if those requirements were
2 instituted, would it slow down or make more expensive the
3 processing of private securities transactions? And, you
4 know, another potential downside that's been noted is,
5 you know, there's this risk that if a safe harbor is
6 created, would fraudsters try to squeeze within it and,
7 you know, follow the letter of the law but not the
8 spirit? And would they be shielded by the safe harbor?

9 MR. BECKER: And interesting question, Mark.
10 If you think about -- I'll take the second part. If you
11 think about fraudsters, the safe harbor really would not
12 be protecting them, so much. It would not be protecting
13 the bad actor on the outside. The safe harbor would
14 really be there to help protect the agent who's acting in
15 accordance with the letter. We're making sure that we
16 have the right information there.

17 It would still be incumbent upon us to make
18 sure that we're not accepting letters from people who are
19 on bad lists or who we know to be bad actors, even if
20 they haven't yet been caught up with by the Commission or
21 a state agency. So I think that -- I think that's not
22 necessarily a major concern, from my perspective.

23 With respect to whether it would slow down the
24 process, I don't think so. Because what it would do is
25 it would prevent the delays that we face now where we

1 have to go back at someone and tell them you have to get
2 us the letter that you haven't yet given us. And now
3 they have to go out and get that letter. And the expense
4 of it is something they should have borne from the
5 beginning anyway. So I don't think that's a major
6 concern as we look at it.

7 MR. HARMON: So the removal of a legend is a
8 nonroutine item to begin with and doesn't fall within the
9 guidelines for the processing of routine items. So built
10 into the concept that you're removing a legend is that
11 it's going to take some time.

12 Putting the onus on the presenter and requiring
13 an opinion that fully deals with all of the requirements
14 for the exemption shifts the burden onto the shareholder
15 and the potential fraudster and the fraudster's lawyer to
16 do the work that you asked the transfer agent to do but
17 without the transfer agent having the authority to do it.
18

19 So the transfer agent retains whatever due
20 diligence it has in reviewing the presentment but now
21 you've created a real burden for the presenter and the
22 presenter's attorney to do that due diligence as well and
23 not just make a presentment that superficially looks okay
24 and then requires the transfer agent to dig down into it.
25

MS. MANNING: I definitely agree with the safe

1 harbor. I'm not sure that I agree necessarily with
2 mandating opinions in every scenario. Because I think --
3 I can't speak for the other agents here but there are
4 certainly, I think, less risky transactions, a
5 nonaffiliate that's held for a year, I can't speak to
6 others' practices but there are certain transactions,
7 gifting scenarios, that, you know, to require an opinion
8 in some of those scenarios, you know, I'm not sure I'd
9 want that mandated. You know, I think to Mark's point,
10 you know, you are now creating an expense for a scenario
11 that not every agent may decide they want to ask their
12 client for or the clients are going to push back on.

13 And we all know opinions are extremely
14 expensive, especially the law firms. A lot of them don't
15 even want to give opinions. We have certain major law
16 firms that have essentially refused to give a legal
17 opinion. They'll give us an instruction and an
18 authorization to release a legend, but they will refuse
19 to provide an actual legal opinion.

20 So I think mandating versus a safe harbor, I
21 think there is a distinction there. And I -- you know,
22 my view is I think the safe harbor is the better
23 approach. It gives agents a little bit of discretion for
24 those transactions where they feel it might not be
25 necessary to get a legal opinion.

1 MR. COULSON: Just, you know, from my side as a
2 market operator downstream, you know, we published a list
3 of attorneys who didn't do the work and, you know, part
4 of it was we got them to sign a letter saying they'd
5 indemnify us if they sued us. Which, you know, an
6 attorney then who threatens to sue you after indemnifying
7 you is probably -- that's another tell that they're not
8 the greatest attorney. So we put that out to the market
9 and turned on a bunch of things and actually John Palisi
10 was running the microcap efforts back then and really
11 turned on an underbelly that needed to be worked on where
12 the work wasn't being done by lawyers.

13 But, you know, from the market operator
14 standpoint, the problem we see is both sides. You know,
15 number one, it's a cost issue. You know, for JOBS Act,
16 crowdfunding Reg A, you know, these are distributed
17 offerings that need to have a cost-effective way to get
18 into the regulated broker-dealer community. And, you
19 know, a \$1,000 opinion on a \$200 investment is not going
20 to work.

21 The other part though is we're seeing blunt
22 force of brokers and clearing firms not accepting any
23 shares that have had their restrictions lifted. These
24 are fully SEC reporting issuers and, you know, right now
25 they've done it to OTC securities. But since we've seen

1 the recent Honig case which the SEC brought, these take
2 place in smaller exchange, NASDAQ and NYSE MKT
3 securities, so the risks are going to be there for
4 brokers and clearing firms as well.

5 And unless we figure out a way to create the
6 transfer agents be trusted recordkeepers that give the
7 information brokers need to be able to fulfill their
8 duties, you know, this is all just wasting time. Because
9 the brokers just aren't going to accept it.

10 And, you know, it's been a little frustrating
11 for us to watch, because we would think there should be
12 differentiation between many transfer agents have really
13 high-quality processes and some don't. So how do we get
14 to a level that transfer agents are providing the level
15 of information they need to brokers so they can do what
16 they need to do? And then when it gets in the brokerage
17 system, we've got other work to do. But that's another
18 panel.

19 MR. SABELLA: Thanks for that. I'd like to
20 thank all of you for your comments. I think, Cromwell,
21 you've highlighted how complex this area is and how much
22 thinking we have to do. So we really appreciate your
23 time in contributing to that conversation.

24 I think we have just a few minutes left. So I
25 would like to, if any of you have any closing comments or

1 final thoughts you'd like to share, I'd like to offer
 2 that opportunity and thank you for your time.
 3 David, we'll start with you.
 4 MR. BECKER: I want to thank the Staff for the
 5 opportunity to be heard on this issue. This is obviously
 6 a very significant issue for us as transfer agents. I
 7 think as you move forward, hopefully -- hopefully -- with
 8 the ideas that were raised in the concept release, this
 9 will lead to much more extensive discussion between all
 10 of us.
 11 I think including Mark to get the perspective
 12 of the smaller transfer agent was really a very good
 13 idea. Because you normally just hear from the big guys,
 14 and it's good to get that other perspective. So thank
 15 you.
 16 And, look, you all know that the STA and the
 17 individual members of the STA are all very interested in
 18 this topic and others and stand ready, willing and able
 19 to do what we can to help you get to where we all need to
 20 be as we go forward. So thank you.
 21 MR. FRANZ: I just want to echo David's
 22 sentiments. I mean, thank you for the opportunity for
 23 the dialogue and certainly look forward to future
 24 dialogue and all of those entities that David's
 25 mentioning all ready to talk about this openly, so look

1 forward to making good changes where it's appropriate.
 2 MR. HARMON: Right. So, of course, thank you.
 3 And I appreciate the opportunity to be here. And, of
 4 course, I'm available for follow up. I would use my few
 5 minutes or few seconds left to make one final plug to
 6 help transfer agents or protect transfer agents from
 7 lawsuits when they are trying to do the right thing by
 8 rejecting a transfer because they don't think it's
 9 compliant with federal securities laws and are between
 10 that duty to the SEC and the securities laws and the
 11 state law obligation to process the transfer. And so
 12 they subject themselves to large liability, even if they
 13 win the case, having to pay lawyers to protect them,
 14 which can be an onerous burden on the smaller agent.
 15 MS. MANNING: I also want to thank the
 16 Commission for inviting me to participate in this. It
 17 definitely is a very important topic for transfer agents.
 18 I have to say there's not a day that goes by that I
 19 don't get pulled into some restricted stock transfer
 20 issue at Computershare, whether it's pushback from
 21 clients, having to talk to clients to explain to them why
 22 we need an opinion, it's a problem that's not going away.
 23 So, you know, really appreciate the opportunity and hope
 24 that we'll have some rulemaking soon.
 25 MR. BECKER: And I see Eric out there. It

1 wouldn't be appropriate to have a meeting between the
 2 transfer agent community and the division without
 3 mentioning escheatment and loss shareholders, so I will
 4 just throw it out there. You guys know what I'm talking
 5 about. It's a topic that we raise at every meeting with
 6 you and I can say for the record it was raised today.
 7 MR. SABELLA: Well, as everyone knows, there
 8 will be a public transcript of this roundtable, so that
 9 will be duly noted in the record, David. So thank you
 10 for that.
 11 And the reference is to Eric Garvey, who heads
 12 up the OC transfer agent program, who is sitting over in
 13 the audience over there. Just raised his hand.
 14 So I will thank Moshe and Mark for leading the
 15 panel through, I agree, a very fruitful discussion. In
 16 many ways, I think, you know, and we'll do a wrap up
 17 later, but, you know, familiar echoes of comment letters.
 18 But always helpful to dig down deeper and refresh on
 19 that.
 20 I think without any further delay, I will now
 21 turn the mic over to Racquel Russell and ask her to
 22 launch us into the trading halt panel. Thank you,
 23 Racquel.
 24 MS. RUSSELL: Thank you, Christian. I am
 25 pleased to be here discussing this important topic, a

1 topic that is important for FINRA, investors and for our
 2 membership.
 3 As part of FINRA's oversight responsibilities,
 4 we do have Rule 6440, which provides authority to impose
 5 trading halts in OTC equity securities under limited
 6 circumstances. The rule generally provides that, when
 7 it's necessary to protect investors and the public
 8 interest, FINRA is permitted to halt trading in three
 9 general buckets of cases. The first one is a foreign
 10 regulatory halt. This is where the stock is trading OTC
 11 here in the U.S. but it's listed overseas and subject to
 12 the regulation of a foreign jurisdiction, who then halts
 13 a security and we follow that here. The second is a
 14 derivative halt. This is where the OTC equity security
 15 is a derivative or a component of a security that's
 16 listed and that listed security is halted. Then we, for
 17 reasons of price discovery, et cetera, we halt the
 18 related OTC equity security. And the final category is
 19 probably the one of most interest today, which is the
 20 extraordinary event halt. This is where FINRA determines
 21 that an extraordinary event has occurred or is ongoing
 22 that has had a material effect on the market for the
 23 security or has caused or has the potential to cause
 24 major disruption to the marketplace or a significant
 25 uncertainty in the settlement and clearance process. And

1 once FINRA provides notice of a halt, quoting and trading
2 by members is prohibited until FINRA provides notice that
3 the halt no longer is in effect.

4 Some of the factors that FINRA considers under
5 our rule to determine whether or not imposing a halt is
6 appropriate are the nature of the event, whether the
7 material facts surrounding the event are undisputed and
8 not in conflict, whether or not the event has caused
9 widespread confusion in the marketplace, whether there
10 has been a material negative effect on the market for the
11 security, whether the potential exists for a major
12 disruption to the marketplace and whether there is
13 significant uncertainty in the settlement and clearance
14 process.

15 And in addition to halts declared for any of
16 those first three prongs, we also halt whenever the SEC
17 issues a trading suspension. Due to the fact that FINRA
18 does not have a direct relationship with issuers, FINRA's
19 halt authority historically has been used in limited
20 circumstances.

21 To get into the discussion further today, I'm
22 happy to introduce our panelists. We have a great
23 representation, cross section of regulators and market
24 participants here.

25 We have Chris Stone, vice president of

1 creator of graduates to exchanges in the world. And, you
2 know, we'd like to do more. I mean, I wish Facebook and
3 Spotify traded on our market before. But a lot of these
4 regulations to stop fraudsters have made it harder for
5 there to be transparent trading in these securities
6 earlier.

7 Now, we've taken a different view, is, you
8 know, we want to make our markets data and disclosure
9 driven. Put more information on the screen. Make it
10 available to be used in a machine. And that's going to
11 make markets more efficient over the long term.

12 But with transparency, not everything is great.

13 You turn on the lights and you see things, often things
14 you don't want to see. You know, we live in a culture --
15 I went to see the movie Oceans 8 this summer with my wife
16 this summer who works in a museum. And, you know, most
17 people cheer. They think it's a great movie. But it's
18 about robbing a museum and defrauding an insurance
19 company. And we have that culture in the United States.
20 It's more widespread than we think.

21 So those people are going to be in markets all
22 the time. You may think it's fun watching George Clooney
23 or his sister. But they're trying to take advantage of
24 every part of the system of our lives. And, you know, in
25 our space, in the small company world, financing takes

1 Transparency Services at FINRA; Christy Oeth, chief
2 compliance officer at Virtu Financial; Cromwell Coulson,
3 president and CEO of OTC Markets; and Michael Paley,
4 assistant regional director, Division of Enforcement at
5 the SEC.

6 I would like to start off by asking each of you
7 to just provide us a bit of an overview of your
8 touchpoints in your role with trading halts and your
9 high-level observations on this topic as it concerns
10 retail investor fraud.

11 I'll start with you, Cromwell, if that's okay.

12 MR. COULSON: Great. So at OTC Markets, we
13 despise fraud. I mean, fraud makes markets not work. It
14 puts your thumb on the scale, fraud and manipulation.
15 Most of the time, you can have markets handle that. But
16 as the Chair said, in microcap securities on exchanges in
17 the OTC market, there's less liquidity, there's less
18 active trading. You know, there's also a lot less short
19 selling. While Tesla can see 25 percent of its market
20 cap sold short, the most sold short stocks OTC is 5
21 percent and the average illiquid OTC security is less
22 than 1 percent of its shares sold short, and that's from
23 Reg SHO. So there are -- there's more volatility here.

24 But our market serves an important role. We
25 have ADRs. We have community banks. We're the largest

1 place in the PIPE space. It's the private market. It's
2 unregulated. It's unregulated entities. It's opaque.
3 And it has very many bad effects on the public markets.

4 So when we went to see Jay Clayton, we came in
5 and we said, you know, one of the things we need to think
6 about is how do we act more like credit card issuers, to
7 freeze things the second we see something wrong? The
8 second we see George Clooney on the video cameras, let's
9 freeze it. And let's also have a way to restart when we
10 make a mistake. Let's have a rehabilitation process.
11 And Jay, you know, to his credit, we saw much more active
12 SEC suspensions of frauds that we'd pointed out or others
13 had and much faster. Mike's team -- Mike's team really
14 sped up and it was a really -- you know, Jay Clayton is a
15 law and order guy, and that was great.

16 But, you know, we need to see how the FINRA
17 halt authority that can act quicker, how it fits in.
18 And, you know, when are the times we should use it?

19 And I'm very glad that we have everyone on the
20 panel. Except -- you know, the only ones missing is the
21 exchanges. Because, as I said earlier, there have been
22 quite a few microcap cases, enforcement cases brought by
23 the SEC shining a light on the fact that the problems
24 that we're talking about today are not only on the OTC
25 market. If you look -- you know, if you looked at the

1 Honig case, one was OTC, it's now on NASDAQ. Another one
2 NYSE MKT, it's now OTC. And then another one is still
3 NASDAQ. You know, and then there's another one, Riot
4 Blockchain, which they didn't -- which one of the
5 executives was named, and it's still on NASDAQ.

6 So what I'd like to see from one side is we'd
7 learn when do they decide to use their halt authority and
8 when do they not? When do they let the market function,
9 knowing the market will eventually correct itself?
10 Because long term, if we turn on the transparency,
11 eventually the market gets it right, no matter how
12 illiquid or inefficient the market is.

13 Thank you for having me.
14 MS. RUSSELL: Thank you. Christy, would you
15 like to share your thoughts?

16 MS. OETH: Sure, I'll be brief here. Just to
17 give you some context, I ended up on this panel by virtue
18 of the fact that Virtu serves as one of the largest
19 market makers in the U.S. equities markets.

20 Globally, we made markets by providing
21 competitive bids and offers in 19,000 securities in 235
22 trading venues in 36 different countries. Here in the
23 United States, we're one of the biggest market players in
24 the OTC securities space and we regularly interact with
25 OTC Markets as well as FINRA on issues of market

1 What we focus on, among other things, is
2 coordinating and sharing intelligence in this, you know,
3 very massive area where there are huge webs of
4 participants. And, in particular, on gatekeepers such as
5 attorneys and auditors who facilitate these crimes and
6 serial violators and we are constantly trying to do our
7 job faster and more efficiently with better data analysis
8 and better communications with market participants.

9 In particular, I want to add that in addition
10 to the FINRA trading halts, the SEC has 12(k) authority
11 to get a trading suspension. And the trading suspensions
12 may be brought in situations where, you know, it is
13 "necessary in the public interest for the protection of
14 investors." And that's a very broad authority. The SEC,
15 however, generally applies a higher standard than that to
16 make sure that we are not sort of interfering more than
17 necessary in the market. But I would say that there are
18 -- you can look at the statistics that we have out there
19 on our trading suspension releases, about how often it is
20 that we do find it necessary to have a trading
21 suspension. And yet we -- it seems that we are not --
22 sometimes it feels as if we're not really making a dent.

23 And that's why I'm very glad that we're also
24 talking about FINRA trading halts because with the limit
25 on SEC resources and all of the other areas that we have

1 transparency, market stability and investor protection.
2 So we are thrilled to have this opportunity to share our
3 view as a market maker and a dealer in this space and to
4 provide some of our thoughts on what FINRA's role should
5 be when it's invoking its both trading halt rule and its
6 clearly erroneous rule.

7 Thank you.
8 MS. RUSSELL: Thank you, Christy. Michael.

9 MR. PALEY: Hi, I'm Michael Paley. I'm with
10 the Division of Enforcement of the SEC. And before I say
11 anything else, as a Staff member at the SEC, I need to
12 remind everyone that any opinions that I express are my
13 own, probably my own, but certainly do not represent the
14 opinion of anyone else at the Commission, much less the
15 commissioners themselves.

16 And with that, I just want to briefly introduce
17 why it is that I'm included in this panel. I am a
18 cochair of the Microcap Fraud Task Force, which is a
19 group within Enforcement that started in about 2013,
20 specifically in response to the need that many Staff felt
21 to do more to combat microcap fraud. And, you know,
22 largely what we were looking at at the time was OTC
23 Markets, which is the subject of this panel. But I agree
24 with Cromwell that many of the issues that we see are not
25 limited to OTC Markets.

1 to focus on, to the extent that we can find a way for
2 FINRA or others to act in this area, it would be very
3 helpful in cleaning up the market.

4 MS. RUSSELL: Thank you, Michael. And Chris,
5 your thoughts from the FINRA perspective?

6 MR. STONE: Sure. Thanks, Racquel.

7 I'm Chris Stone, vice president in FINRA's
8 Transparency Services Department. And I am responsible
9 for the business units that run our fixed income and
10 equity markets systems, this is the TRFs that we run in
11 partnership with our exchange partners, the ORF, the OTC
12 BB, the ADF and our OTC volume dissemination product.

13 Specifically with respect to the ORF, I am part
14 of the team that in real time, intraday, analyzes
15 potential OTC equity U3 extraordinary market, market
16 halts. And I think one thing that's worth noting is I
17 think FINRA's general theme throughout the usage of 6440
18 and extraordinary market condition halts is that we're
19 not an exchange in this space. So we lack contractual
20 privity with issuers in the OTC equity space and we don't
21 have listing agreements in the same way that the
22 exchanges do. So for the 18,000-plus OTC equity symbols,
23 and that compares with over 8,000 national market system
24 symbols, it can be challenging to find in real time the
25 valid information that we need to execute a U3

1 extraordinary market halt in this space.
 2 That said, we have a range of exchange-like
 3 tools that we use in the space. Yvonne spoke at length
 4 earlier about our 211 qualification process. We also
 5 have a Rule 6490, which has allowed us to declare certain
 6 corporate actions deficient and not process them if we
 7 believe they're related to fraud or would otherwise
 8 threaten the clearance at settlement system. And then,
 9 obviously, lastly is 6440, our halt provision.

10 So I think, you know, I know we're going to get
 11 into this a little bit later on the panel, some other
 12 ideas around things that people have talked about and
 13 things we've thought about in terms of changes to 6440 or
 14 ways we could use 6440. But I guess that's just one
 15 thing I would like to set the table with for FINRA is, I
 16 think, our difference from being an exchange is kind of
 17 critical in this space.

18 MS. RUSSELL: Thank you, Chris. And in a
 19 complex issue like deciding when to halt trading, you
 20 know, everyone has a role. So we'd like to kind of start
 21 the in-depth discussion with talking a bit about
 22 everyone's role in your space in the marketplace.

23 So Christy, if you don't mind, starting with
 24 just some thoughts on what you view your role as a dealer
 25 when you see activity in a security that may be

1 problematic?

2 MS. OETH: Sure. So we really see our role as
 3 threefold, right? First, it's identification, then it's
 4 escalation and then there are reporting responsibilities.
 5 And we heard quite a bit about the SAR reporting
 6 responsibilities in the previous panel, so I won't really
 7 spend much time on that.

8 But, you know, our business model is a bit
 9 unique in the sense that we're a large market maker,
 10 we're largely automated. But when it comes to OTC
 11 securities, we have a cash trading desk, we've got human
 12 traders who have been trading these same securities for
 13 numerous years. So these individuals who sit on the
 14 trading desk have a vast amount of experience in how
 15 these securities trade and what's atypical trading and
 16 what looks atypical in order flow from our broker-dealer
 17 clients.

18 So that's one thing that we really try to do,
 19 is when we see something that is problematic, there is
 20 investor confusion about the security, there is a
 21 misprocessed corporate action or there's asymmetric
 22 information disseminated about a corporate action, or we
 23 just otherwise see indicia of potential fraudulent
 24 activity, we're escalating that to FINRA. We try to have
 25 a direct line of communication and we try to do it in

1 real time and then follow up with, obviously, our SAR
 2 reporting responsibilities. So that's our general
 3 proposition.

4 Our experience has been -- and obviously, it's
 5 contextualized in what Chris has shared and what Racquel
 6 shared in her overview, is that this market doesn't
 7 operate the same way as an exchange does because there
 8 isn't the same privity between the issuers and the
 9 regulator that there is in the exchange context. And we
 10 fully appreciate, because we have very robust and
 11 comprehensive dialogue with FINRA, how challenging these
 12 situations become.

13 So I think that where the real hard work needs
 14 to be done between the industry and FINRA and with SEC as
 15 sort of, you know, an interested party in this whole
 16 conversation is if we want to view trading halts in OTC
 17 securities as a tool to prevent or minimize or mitigate
 18 this type of fraud, then we need to find a tool that's
 19 effective. Because right now, it's a very limited tool
 20 that has limited applicability in its current context.
 21 And we just need to, I think, find some rules of the road
 22 that are more comfortable for the broker-dealers who are
 23 escalating this and who are at the end of the day, their
 24 client base is getting impacted by it and our business is
 25 getting impacted by these securities that don't trade

1 efficiently and the price discovery process is not as
 2 efficient as it should be. So that would be our
 3 perspective.

4 MS. RUSSELL: Thank you. And Cromwell, in your
 5 position, how do you view your role in terms of, you
 6 know, if you see something you think is problematic?

7 MR. COULSON: So our mission is to create
 8 better informed and more efficient markets. So we lean
 9 into transparency and market efficiency. And, you know,
 10 I'm always a little cynical of someone who says they
 11 believe in free markets. And then when a free market is
 12 doing something whacky, they say, you need to stop that.
 13 Because usually the market fixes it. But I also
 14 understand in this space we need to freeze things. It
 15 gets broken. And there's things because of how Reg SHO
 16 works, clearing works, how limited liquidity in microcap
 17 and how people try and hide.

18 So we see our role, because we have contractual
 19 privity with a lot of issuers, and we also deal with
 20 issuers in getting better disclosure out of issuers we do
 21 not have contractual privity with.

22 You know, one of the things I think we did most
 23 innovatively was we started segmenting our market based
 24 on disclosure and data and then making that machine
 25 readable. And, you know, that part where we started out

1 was creating
2 -- it's a two-part process. Providing services for
3 companies that are doing the right thing and having them
4 see a benefit of doing that. And also exposing when
5 something icky is happening.

6 And we have been very successful, you know, and
7 we probably use more behavioral economics than we do
8 standard economics, but getting that to move along. And
9 our top market is recognized by, you know, 30-plus states
10 for blue sky disclosure, which is a pretty incredible
11 invention in 10 years if you understand the development
12 of state securities law speed.

13 So where we see in this role is, you know, we
14 think we can provide a very good side of feeding
15 information in as part of it, who's going to the SEC, to
16 going to FINRA. When FINRA has done a halt, ourselves
17 and the market makers have been very much in the
18 conversation.

19 I also see a value for companies where we have
20 contractual privity for them to be able to do news halts
21 when they see something not happening right in the
22 market. And because we -- you know, we brought out last
23 year a disclosure product around tracking promotion. And
24 we did two parts of it. We flagged promotion that was
25 occurring and we made it machine readable to the

1 And the final part is, after FINRA does a halt
2 or the SEC does one, it does a suspension, it would be
3 very good to quickly publish to investors what they
4 found. And, you know, FINRA has SRO immunity, we don't,
5 so we're a little more careful about what we can put out
6 there. But it would be really good for investors, saying
7 these are the reasons we did it and then let the market
8 have a rehabilitation process to bring something in, how
9 it gets cured, what are the things we need to do.
10 Because, you know, at the end of the day, the way you
11 stop the Oceans 8 guys and girls is you bankrupt them.
12 You stop them in the middle when they've got their
13 investment and they can't get the money.

14 And, you know, if we're suspending things, if
15 it's taking too much time or there's not enough capacity,
16 we want to be able to do it. You know, I think we can
17 probably hire some small-cap analysts because there
18 wasn't a hiring boom after the tick pilot. So, you know,
19 put some smart analysts' look on these things and, you
20 know, start to, you know, make our markets safer in real
21 time to build confidence. And that way, we don't have
22 the cost on the honest issuers who are compliant and
23 doing the right thing.

24 MS. RUSSELL: Thank you. Those are great
25 points and you both mentioned escalating these issues in

1 brokerage industry, and available on the screen to
2 investors.

3 But a second part is we require companies to
4 issue a press release and correct any misinformation,
5 disclose if they've been doing any financing and disclose
6 if any of the insiders or affiliates are selling. And
7 that part is I really think issuers have a requirement in
8 this real-time world, it's an old rule that the New York
9 Stock Exchange used to have, that companies have a duty
10 to immediately release material information, as well as
11 correct any misleading information that's affecting the
12 market. And so we should be able to freeze the market
13 and then get the companies to come back and say, this is
14 what is here, this is here, if there's something breaking
15 it.

16 I mean, we live in a world where, you know, the
17 Kardashians took a billion dollars' worth of Snap's
18 market cap out with one tweet. And, you know, we're
19 going to have these things happening. That one gets
20 fixed by the market. Bomb at the White House gets fixed.

21 Other things in these less liquid securities don't get
22 fixed as quickly as market forces. So I think we need to
23 think like credit card issuers and, you know, work
24 together as a team, each feeding them in and then putting
25 them to a regulator.

1 kind of interaction with the regulators. And I think it
2 would be a great segue to hear more from Chris and
3 Michael about, you know, your thoughts on what Christy
4 and Cromwell just said and what you think of in terms of
5 the relationship between the front-line kind of folks
6 that oftentimes may notice something kind of in real time
7 and what the communication escalation to the regulators
8 should be.

9 Chris, can we start with you?

10 MR. STONE: Sure. Yeah, I would like to echo
11 what both Christy and Cromwell said in terms of the
12 benefits of market participant, market maker and ATS
13 involvement in funneling the information we need to the
14 regulator. You know, I wouldn't say there's a lot of
15 magic to how we get information in connection with U3
16 extraordinary market halt declarations. It's Bloomberg,
17 it's blogs, it's talking to investors, issuers, issuers'
18 counsel and market participants.

19 So I know one of the questions that I saw on
20 the agenda was, you know, what are the additional sources
21 of information that might help FINRA? And I'm not sure
22 there's a magic bullet for that. It's still we just need
23 better information quicker that's more granular in
24 connection with issuers.

25 You know, sometimes we'll have cases, fairly

1 recently within the last two weeks, where a price will
2 move dramatically such that we'll get calls from Christy
3 or Cromwell, saying, you know, the price moved at a point
4 where clearly this needs to be halted. Then when we look
5 back at our kind of precedent around U3 usage, there's so
6 many illiquid stocks that can be so volatile in the space
7 that we tend to want to see that price spike tied to a
8 huge share volume move as well, to indicate that there's
9 clear investor confusion around what they're even
10 trading.

11 So the Twitter tweeter example was a good one,
12 GM Liquidation Trust was another good one, and those were
13 U3s.

14 But again, the way the rules are written,
15 they're rare. And we've done three U3s year to date.

16 MR. PALEY: Yeah, I would add to that. You
17 know, first, I would be remiss if I didn't note how much
18 of the trading suspension work that we're able to do and
19 the reason we can do it in a timely manner is often
20 because of information that FINRA provides to us. And,
21 you know, so FINRA has been really, you know, terrific
22 and we've been working with them in terms of the
23 information that we need and how we need it, how we need
24 to get it, so that it can be sort of incorporated as
25 quickly as possible into our own process.

1 But I would love to hear sort of more
2 specifics, you know, to the extent that there is time
3 from everybody about, you know, what exactly we can do to
4 define what is an extraordinary event and if there are
5 some particular parameters, you know, whether it is an
6 asset, certain asset to market value ratio, whether there
7 are certain types of disclosure deficiencies or other red
8 flags or particular trading patterns or, you know, a
9 particular level of volatility. I do think that we could
10 probably come up with some, you know, standards.

11 I also just want to remark on that I thought it
12 was fantastic that there was that panel on suspicious
13 activity reporting. As Christy mentioned, that is hugely
14 important to us in this area. It's also really important
15 to the extent that anyone that maybe is working on
16 something like that, because acting on a trading
17 suspension is only effective if it happens immediately.
18 The harm to investors can happen while you're writing a
19 report to the SEC. So if you can give us a heads up,
20 that is hugely valuable.

21 And finally, I just want to refer to something
22 that Cromwell said about providing reasons for the
23 trading suspensions. Of course, there are limits, there
24 are various reasons why we can't, you know, always
25 provide detailed reasons. But if you look at trading

1 suspension orders over time, we have actually been making
2 a concerted effort to provide additional detail in our
3 orders about the underlying reasons, maybe referring to
4 specific press releases, for example, that we believe to
5 have false statements or suspicious trading or more
6 specific guidance to investors.

7 MR. COULSON: And that's been very helpful. My
8 comment was more when FINRA does it to have the same --
9 you know, we go back and look when we're talking to an
10 issuer that's been suspended and very quickly know the
11 level of concern at the SEC.

12 MS. RUSSELL: Thank you for that, Michael. And
13 it's a great segue into exploring kind of how do you get
14 at solutions. Part of that is to explore the challenges
15 and look at the challenges kind of head on.

16 In this space, as folks have noted, it's
17 difficult to get definitive and reliable information.
18 You also have to consider the needs of, you know, all of
19 the investors. Which I'm sure Gerri will kind of talk
20 about. Sometimes you get calls on both sides when
21 there's a halt. And then balancing. Michael, you
22 mentioned interfering with the market, you know, kind of
23 restricting how much regulators do that and balancing
24 kind of when that's appropriate.

25 So, Chris, if you don't mind, you know, what's

1 your view kind of on the challenges? And then everyone,
2 you know, kind of provide your thoughts on that quickly.

3 MR. STONE: Yeah, I think you hit the nail on
4 the head with your question. There's a tension between
5 the market integrity, investor protection side versus
6 letting market forces take effect and making sure you're
7 not preventing buyers and sellers from buying and selling
8 securities when they need to, probably when they most
9 want to in those cases.

10 So we're always open for looking at our rules
11 and thinking about ways to improve them and enhance them.

12 I mean, I know there's been conversations around what
13 Cromwell just said. We ask issuers for information
14 directly. If they're not responsive, you know, maybe
15 there's room there for a halt. I mean, again, some of
16 these things would require rule changes. Drastic or
17 extreme corporate actions, maybe you could halt around
18 those. You know, again, those aren't in the rule
19 currently.

20 And then finally, Cromwell, I know we've talked
21 over the years about the reopen. It's been -- because
22 there's not a book to build on like on an exchange, the
23 way our rule reads now, it talks about allowing closed
24 quote periods. You know, are there ways we can improve
25 that reopening process to make it smoother intraday?

1 Those are the kind of things we'd be willing to continue
 2 to talk about for sure.

3 MS. RUSSELL: Thank you. And Cromwell,
 4 Christy, your thoughts on that or on the challenges and
 5 potential solutions overall?

6 MR. COULSON: So the challenges part I would
 7 say, you know, I think a good example where a FINRA halt
 8 would have been better was the crypto company about a
 9 year ago. Which was -- you know, it was one of the
 10 companies where a name changed. They were engaging in
 11 some crypto-type businesses. SEC-registered company.
 12 But the market just broke. And this happens when some
 13 market makers get short and then the Reg SHO buy-ins
 14 start to come in. And once that happens, the price stops
 15 reflecting any market forces. It's just a real -- the
 16 system breaks really badly.

17 Now, that company has still tried being
 18 reporting. It was a broken market rather than this is a
 19 fraud going on. And, you know, it was a bit more
 20 aggressive because I think the other parts to get in the
 21 conversation is, you know, the people have histories
 22 doing this much better as the exchanges. And, you know,
 23 why does LongFin Financial get halted by the exchanges
 24 and then other kind of crypto names don't? And with
 25 other questionable actors in it. And what's the call to

1 do? Because I don't think we want to go like suddenly,
 2 this area gets harsher.

3 And, you know, I'm a big believer in bringing
 4 in the companies. Because when we have panels like this,
 5 we focus on, you know, the characters George Clooney
 6 plays that exist in our markets. But we don't have, you
 7 know, the people trying to do the right thing.

8 And, you know, securities law is all about
 9 companies being completely truthful with high-quality
 10 information. There's other practices of law.
 11 Matrimonial law, I mean, I've heard cynically said,
 12 everybody is a liar. And juvenile law, which I think for
 13 smaller companies is more important to use, is where
 14 early intervention and understanding that maybe they
 15 didn't know the full rule, the laws. And a third is a
 16 rehabilitation process for the deserving. And how do we
 17 make the halt process be able to do that, to bring things
 18 in, so we make it not as -- you know, if a pump and dump,
 19 because sometimes companies are involved with pump and
 20 dumps. Otherwise, just companies ran into bad financing
 21 players. And the longer those goes on, the more stuck
 22 the company gets.

23 So that's my like, is -- if we want to move
 24 this forward and make this safer place for capital
 25 formation, because this is not -- these problems are not

1 unique to our markets. We see it in every market around
 2 the world that has successful small company markets.

3 MS. RUSSELL: Thank you. As everyone can tell,
 4 we could probably continue to explore these issues at
 5 length. And we thank you, Christian, for having us here.
 6 We at FINRA look forward to continuing this dialogue
 7 with our members and with the SEC.

8 MR. SABELLA: Thanks so much, Racquel, and
 9 thank you to the panelists.

10 So I'm mindful of the clock and I know folks
 11 have come from near and far to get here and have
 12 traveling schedules to adhere to, so I will pass the mic
 13 now to Owen to bring us home on, last but certainly by no
 14 means least, investor education issues.

15 Thanks, Owen.

16 MR. DONLEY: Thanks, Christian. And I do know
 17 our panelists have a hard 3:30 stop, so I'm going to talk
 18 for about 30 seconds about what we're doing here at the
 19 SEC in investor education and turn it over to our
 20 esteemed panelists.

21 Very briefly, very briefly, we have a robust
 22 investor education platform here at the SEC. We spend a
 23 great deal of time creating public-facing content for
 24 retail investors, much of which is in the retail space.
 25 In the last year or so, we've spent a lot of time on

1 background checks. I know this morning one of the
 2 panelists noted that a significant portion if not a
 3 majority of retail-facing fraud is committed by persons
 4 who are not licensed with a state, with FINRA or with the
 5 SEC and that has been a key focus of our -- including a
 6 public service campaign.

7 We similarly create dozens of investor alerts
 8 and bulletins a year, many of them focused on retail-
 9 facing fraud.

10 In terms of distribution, our primary platform
 11 is our website, our award-winning website, investor.gov.
 12 A little plug.

13 In addition, we are using new digital and
 14 social channels from RSS feeds to content marketing, spam
 15 email lists -- I would not spam email lists -- as well as
 16 social channels. We have a fairly prolific Twitter
 17 account.

18 I would be remiss not to mention we are
 19 engaging in some interesting digital strategies in the
 20 ICO space. Maybe we will get a chance to talk about
 21 those. And, of course, we participate in 100-plus in-
 22 person events, often in partnership with the states and
 23 FINRA, everything from military bases to schools to
 24 libraries to senior centers. So that is sort of the
 25 gamut of what the SEC is doing.

1 Gerri, Chris, can I ask you guys to introduce
 2 yourself, describe your investor education programs,
 3 especially how they are focused on retail fraud?
 4 MR. GEROLD: Sure, thank you. Christopher
 5 Gerold. I am the chief of the New Jersey Bureau of
 6 Securities.
 7 Certainly part of our mission is investor
 8 education and we are doing many of the same things that
 9 the SEC does but at the state level. We have a number of
 10 initiatives. We do put out investor alerts from time to
 11 time. We are going out into the community. In New
 12 Jersey, if you walk into any public library, there's one
 13 of our posters in it. But it's challenging.
 14 And so one of the examples I always give to our
 15 investor ed people is that broker-dealers and investment
 16 advisers are inviting the public in to a nice restaurant,
 17 giving them a free dinner and then soliciting money from
 18 them. And how are we supposed to compete with that? We
 19 can't give away nice dinners.
 20 You know, the good thing is that many of those
 21 programs, you know, they're getting decent information
 22 from good people. I'm not going to knock all of them.
 23 But too often, they're not.
 24 So, you know, the challenge for investor ed is
 25 how do we get people in the seats? How do we get them to

1 listen? And how do we do that? And the only way to
 2 really do it is creatively.
 3 I mean, we're doing what we can now. We are
 4 exploring other avenues to do that. And some of the ones
 5 we're looking at, and I just came from NASAA's annual
 6 event, fraud bingo. Keep it interesting. Videos, kind
 7 of like American Greed. We've gone out to one of the
 8 local colleges to have them build out the video for us
 9 and they're doing it for free.
 10 But at the end of the day, I think our focus
 11 has started to be, and we're shifting a little, is to
 12 getting to investors before they're investors, getting to
 13 them while they're younger. I recently went to a -- I
 14 was doing an investor ed presentation to teachers and the
 15 -- it was eye opening, unfortunately. Not to knock
 16 teachers by any means, but one of the participants there
 17 was telling me how her local bartender was giving out
 18 investment advice and selling securities. And my head
 19 almost exploded. And it was eye opening because the
 20 level of financial literacy, I think, in the country is
 21 pretty poor. And unfortunately, people aren't paying
 22 attention to investing until maybe they have some money
 23 to invest, at which point they're not sure where to go.
 24 So there are certainly a lot of challenges in
 25 this area that we're trying to focus on. And one of them

1 is to try to go back to the basics, focus on some, you
 2 know, younger individuals before, you know, maybe even
 3 before they become adults and have money to invest, put
 4 the focus there.
 5 MS. WALSH: Thanks for having me. It's great
 6 to be here. My name is Gerri Walsh. I am the president
 7 of the FINRA Investor Education Foundation and I am
 8 senior vice president at FINRA, head of the Investor
 9 Education Department. So everything Owen said,
 10 everything Chris just said, and we all work together.
 11 Which is really important. I think it's the only way
 12 that we're going to be able to combat fraud.
 13 The foundation has a variety of strategic
 14 priorities, including benchmarking financial wellness and
 15 financial health and financial knowledge in the United
 16 States. And, Chris, you're spot on. It is low. And
 17 people are financially fragile.
 18 The truth is, most Americans are not investing.
 19 Only about 30 percent of people have taxable brokerage
 20 accounts. About half of Americans are investing through
 21 the workplace, so the workplace is a really important
 22 platform that we should all be thinking about.
 23 But there is no doubt that if you start young,
 24 if you get people even before they're investing, then
 25 they're more likely to contribute to a workplace

1 retirement plan and to get into the markets that way,
 2 which is probably, you know, a less risky onramp to
 3 investing.
 4 There are other things that we do, as Chris was
 5 -- similar to what Chris was saying. We try to get out
 6 into the community. We're a small shop, so the
 7 foundation does it through intermediaries. We work in
 8 partnership with United Way Worldwide, with the American
 9 Library Association, Catholic Charities, AARP, AARP
 10 Foundation, Better Business Bureau, others. The list
 11 goes on. But we really work hard to train those who then
 12 train the community, like military service members, like
 13 Native Americans.
 14 When it comes to fraud, we do have a robust
 15 investor protection campaign. It has multifaceted
 16 components. There's a big research component that looks
 17 at why those who become targets of fraud and fall prey to
 18 that fraud do that. Why are they targeted? Why are they
 19 falling for the scams? How can we help them recover?
 20 Are there differences between people that report frauds,
 21 for example, to the Better Business Bureau, which is a
 22 huge repository of fraud information. They've got a
 23 terrific scam tracker tool. We're trying to tease that
 24 out to inform the field, not just for our own programming
 25 but so we can share it with others and everyone else can

1 benefit.

2 We are also looking at the psychology of scams.

3 What are the behavioral biases that people have

4 generally when it comes to investing? And then are there

5 differences between victims and nonvictims? And again,

6 we're seeing that there are.

7 We do outreach. We work with partners, as I

8 alluded to. But we really think about three things when

9 it comes to fraud. We focus on the types, we focus on

10 the targets and we focus on the tactics that the cons

11 use. And while we often hear the really good advice that

12 if something sounds too good to be true it probably is,

13 the reality is that for most investors that's very

14 difficult advice to implement. Because to paraphrase an

15 SEC colleague who -- I don't even know who said it first.

16 But if something doesn't sound too good to be true, then

17 you're probably dealing with an amateur. Fraudsters are

18 super smart, they're super slick. And they cause people

19 who fall prey to fraud to buy that dream. You're

20 invested before you even pull out your checkbook.

21 And so that's what we're combatting when we're

22 combatting fraud. It's a very emotional reality. And

23 that's hard to overcome and so that's part of what we're

24 trying to tease out.

25 MR. DONLEY: Thanks, Gerri. That's fantastic.

1 You mentioned types. And, you know, today

2 we're focused on trading and markets issues. We've

3 discussed the microcap space, some trading scams this

4 morning. What are the, say, top two or three types of

5 fraud that's focused on retail? You know, putting aside

6 -- you know, you look at the Commission's docket. You

7 know, half the docket is retail facing, not the FCP and

8 not the accounting but the core retail issues. What are

9 you seeing in the last 12 months?

10 MS. WALSH: Absolutely. And it's already been

11 alluded to by this panel and by previous panels. Pump

12 and dumps. Pump and dumps of thinly traded securities,

13 especially securities that used to be mining companies

14 and gambling companies in China and clean air and now,

15 all of a sudden, they're crypto. And I'm not entirely

16 sure that there's any one company that meets that five-

17 part test that I just laid out but that's pretty much the

18 path that a lot of these thinly traded securities follow.

19 You know, going out in the field, talking to

20 investors, you know, people want to get in on the next

21 big thing. And I happened to be out in Hawaii -- don't

22 feel sorry for me but it was my first time -- and there

23 were a number of investors there who were saying, you

24 know, these sugar plantations are now going fallow and

25 we're hearing that cannabis might be coming in. How can

1 we get into legitimate cannabis investing?

2 And so there is this array of opportunities

3 that people see and they glom on to these companies that

4 are being pumped inappropriately. So that's one of the

5 areas that I'm most concerned about.

6 MR. DONLEY: Chris, anything in particular to

7 New Jersey that you're saying at the NASAA level?

8 MR. GEROLD: Yeah. Well, certainly a few

9 items. Unregistered promissory notes, they continue to

10 be an issue. How they package those keeps changing but

11 it's usually some promissory note attached to it.

12 Specifically and most recently, real estate schemes. We

13 mentioned Woodbridge earlier. There are others, there

14 are more local ones in New Jersey that we've brought in

15 the last year. Real estate continues to be popular, I

16 guess.

17 Pre-IPO type of offerings where a unicorn is

18 identified, whether it's Uber or Facebook before it went

19 public. We've seen a number of frauds where individuals

20 say they have access to pre-IPO shares from either former

21 employees or employees at the time. So really forward

22 contracts and they're marketing them. Whether or not

23 they're enforceable contracts is a question but most

24 times they are a fraud. And it just so happens everyone

25 has heard of Uber and it's a private company, how do I

1 get in on that. We've certainly seen that.

2 And then you touched upon cannabis. New

3 Jersey, it does appear, is working on some cannabis

4 legislation. We're trying to get out ahead of it on the

5 securities side to warn people because we're sure that's

6 going to be the next area where we'll see some fraudsters

7 promoting companies that would be trying to get into that

8 area and certainly over-promising. So those are some

9 areas we're looking at.

10 MR. DONLEY: Yeah, I'll note, we just put out

11 an alert on marijuana fraud companies last week, so we're

12 on the same page.

13 So this week, many of you may know, is World

14 Investor Week. And I know, Gerri, this is a coordinated

15 effort between international regulators, state

16 regulators, FINRA, the CFTC and other federal regulators.

17 So it brings to mind how we can work better together.

18 This is a question. We seem to all identify a common

19 sort of suite of fraud. It does change every year. We

20 sort of know the messages.

21 How can we work better or what channels should

22 we be using to more narrowly target like these particular

23 frauds?

24 MS. WALSH: We could learn a lot from our

25 international colleagues. And I know Chris knows that

1 from his involvement with NASAA, with the Canadian
 2 regulators and the Mexican regulators. And you and I
 3 have had the opportunity to be part of IOSCO, the
 4 International Organization of Securities Commissions,
 5 Standing Committee on Retail Investor Education.
 6 And, you know, in Brazil, in Australia, in the
 7 U.K., in Canada right now, there's a big focus on how we
 8 can harness the power of behavioral insights and
 9 behavioral economics, which Cromwell just mentioned
 10 earlier, to better inform investor education and retail
 11 protection. Some of that comes in the form of message
 12 testing. Some of it comes in the form of data gathering,
 13 understanding who's at risk, you know, how big the
 14 problem is. That's one of the big bugaboos is that we
 15 really don't have a good handle on -- we don't quantify
 16 the harm caused by retail investment fraud and how many
 17 people are actually subjected to that. We're actually
 18 working with the Department of Justice to try to tease
 19 out some of those statistics in the National Crime
 20 Victimization Survey.
 21 But those kinds of lessons, where we can learn
 22 from one another and leverage one another's really
 23 terrific tools. At FINRA, there was a team of us that
 24 connected with the authorities in the Netherlands because
 25 they've been doing a lot in using behavioral insights,

1 not only for education but also for regulation. And what
 2 are the implications for FINRA, for the SEC, for state
 3 securities regulators here in the United States? So
 4 there's a great deal that we can do together.
 5 And one of the things that I love is that when
 6 we go out into the field, you know, virtually every time
 7 we're doing any of our law enforcement trainings, we
 8 connect with our state security regulator colleagues, the
 9 SEC comes along. When you go to military installations,
 10 you invite us to come along. That kind of collaboration
 11 is key, because resources are so limited. And we're
 12 always encouraging the financial services industry to get
 13 on the bandwagon as well, and many of them have actually
 14 been key innovators in terms of developing games, making
 15 things interesting for investors, along the line of
 16 investment fraud bingo.
 17 We really have to deliver so many messages so
 18 many different ways and we're competing with all the
 19 commercial messages as well as the out and out scams.
 20 MR. DONLEY: I know both of you have
 21 exceptionally hard deadlines so, Chris, and thank you so
 22 much, just because the conversation is a little short, I
 23 know that the NASAA website, the FINRA education website
 24 and investor.gov have far more on all these subjects,
 25 especially related to the content thing today.

1 Thank you so much. Apologies for the short
 2 panel.
 3 MR. SABELLA: Yeah, thanks very much, Owen.
 4 And thanks to everyone. And again, appreciate the shout
 5 out for World Investor Week, which I think hopefully will
 6 continue the important themes of this panel or this
 7 discussion at the end of the panel.
 8 So with that, I know we're at time. So I would
 9 just like to close out by thanking -- expressing very
 10 deep gratitude to all the panelists for, you know, taking
 11 time out of your busy schedules to come down here in
 12 Washington on the only sunny day in September to visit
 13 with us as we sit in this windowless room. So, thank
 14 you.
 15 I think it's interesting. I mean, certainly
 16 from the Staff, we're absorbing a lot. There will
 17 obviously be a comment file made available for this
 18 roundtable for folks to submit further information. But
 19 a lot to absorb across the board.
 20 Interesting, just from a personal perspective,
 21 and like Michael, I take the disclaimer as well, just a
 22 personal view. A lot of ecosystem challenges, it sounds
 23 like, across the different areas, where the institutions
 24 you represent are in the middle of a larger dynamic and
 25 trying to maximize communication, decisionmaking, who

1 holds the responsibility at which stage of the process,
 2 all for the benefit of the retail investor. It sounds
 3 like it's something that you're all thinking about and
 4 that you're also thinking about ways this organization
 5 can be more involved in that process, so we thank you for
 6 your thoughts on that.
 7 As I said, we will have a public comment file
 8 for this roundtable. It will be available on the
 9 website. And there will be instructions, as there always
 10 are, for public comment files the SEC puts out in terms
 11 of submitting that, so we look forward to further
 12 thoughts from you or others and folks who have been
 13 listening in, either through the webcast or otherwise.
 14 Thank you all very much for your interest. We
 15 will continue this going forward. And have a great
 16 afternoon. Thanks again.
 17 (Whereupon, at 3:31 p.m., the roundtable was
 18 concluded.)
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PROOFREADER'S CERTIFICATE

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In the Matter of: ROUNDTABLE - COMBATTING RETAIL
INVESTOR FRAUD
File Number: OS-0926
Date: Wednesday, September 26, 2018
Location: Washington, D.C.

This is to certify that I, Christine Boyce, (the undersigned) do hereby swear and affirm that the attached proceedings before the U.S. Securities and Exchange Commission were held according to the record, and that this is the original, complete, true and accurate transcript, which has been compared with the reporting or recording accomplished at the hearing.

(Proofreader's Name) (Date)

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I, JEMIMA EUELL, reporter, hereby certify that the foregoing transcript is a complete, true and accurate transcript of the matter indicated, held on 9/26/2018, at Washington, D.C., in the matter of:
ROUNDTABLE - COMBATING RETAIL INVESTOR FRAUD.

I further certify that this proceeding was recorded by me, and that the foregoing transcript has been prepared under my direction.

Date: 9/26/2018
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A				
a.m 1:14	204:20	acted 159:2	127:9 165:13	addressing 7:14
AARP 26:21,22	accomplished	acting 7:25	actors 13:24	103:4 159:14
27:1,2,17	103:15 210:15	48:25 110:6,8	21:23 50:9	161:4
28:13 48:22	account 37:23	110:19 165:14	53:16 59:24	adequately 91:9
70:21 125:23	44:8,8,9,10	191:16	64:23 65:11	ADF 181:12
201:9,9	56:2,19 59:10	action 7:21 8:2,6	66:21 126:8,12	adhere 196:12
ABA 103:4	63:12,15,19,20	26:2 29:24,25	126:14,22	administering
111:16	71:3 101:21	57:6 63:5	128:15 130:5	78:1
abbreviated	124:25,25	65:24 97:9	165:19 194:25	administrative
80:6	125:1 126:11	139:8 164:10	acts 65:12	156:12
abilities 152:8	126:15,21	183:21,22	actual 57:23	administrator
ability 5:8 8:25	127:2,9 130:17	actions 21:4	68:22 70:10	31:2
18:23 89:3	131:9,13	36:5,8 37:5	167:19	Administrators
96:11 119:16	132:14 135:22	49:22,23 57:8	ad 127:18	25:5
156:19,24	138:24 197:17	70:19 75:2,8	add 36:2 52:10	admitted 78:20
157:3 163:4	accountable	79:15 95:23	52:19 53:7	ado 77:10,20
able 11:5 23:19	13:25	100:8 117:4,4	93:24 118:3	adopt 79:7
44:1 47:20	accountants 9:3	146:1 148:14	125:7,20 126:4	161:3
73:22 76:17	17:9 149:9	153:22 163:23	127:15 130:22	adopted 78:4
83:14,23 85:2	accounting	182:6 193:17	150:15 151:22	80:20
89:25 90:2,13	203:8	active 27:15	180:9 190:16	adopting 74:17
91:23 96:4	accounts 125:3	32:23 45:12,21	Added 58:24	ADRs 175:25
97:21,24 99:6	125:4,6 126:13	175:18 177:11	adding 79:1	ads 54:22
116:15 117:25	126:17,23	actively 13:11	107:3	adult 64:4,14
132:20 140:4,6	139:19 200:20	activities 7:14	addition 8:11	139:21
158:22 169:7	accredited 97:20	16:25 69:4	75:12 81:9	adults 200:3
170:18 186:20	116:4 117:16	108:15,16	103:8 149:6	advanced
187:12 188:16	117:19,21	120:17 129:9	174:15 180:9	143:19 145:5
190:18 195:17	118:2	129:11,18	197:13	advancement
200:12	accumulation	135:23 136:12	additional 5:11	85:5
absence 78:9	41:4	136:16	7:9 64:9 76:9	advantage 60:20
absent 111:11	accurate 78:17	activity 8:16	93:25 107:3	60:25 176:23
absolutely 42:7	210:13 211:4	11:3 16:15	152:21 153:1	advent 33:7
94:9 101:4	achieve 91:5	19:3 77:18	155:14 160:10	42:17
113:8 130:1	123:14	81:3 95:21	189:20 192:2	advertise 149:20
158:10 159:8	achieving 41:5	98:6 109:13	Additionally 8:1	advertisement
162:16 203:10	acquaint 79:12	113:24 121:8	address 13:11	107:12
absorb 208:19	acquiring 41:5	121:11 122:4,8	19:6 64:18	advertising 34:9
absorbing	act 8:13 63:25	124:9,10,13,15	73:13 81:24	advice 15:19
208:16	64:10,11	124:17 125:21	87:3 90:22	59:4 74:23
abuses 21:2	111:23 112:13	126:3 128:12	95:12 102:11	107:16 108:20
academia 19:9	112:14,15	129:20 130:25	103:16 132:6	199:18 202:11
accents 58:15	113:1 117:6	132:3 135:13	150:7 155:15	202:14
accept 169:9	121:13 122:1	135:15,25	addressed 82:3	adviser 34:19
accepting	123:10,14,24	136:10 137:19	90:3 150:5	52:22 63:14,22
165:18 168:22	124:11 145:23	137:20,24	156:5	75:21 126:15
access 16:12	148:14 154:23	142:10 182:25	addresses 55:11	129:8
66:4 89:13,20	162:5 168:15	183:24 191:13	133:16 157:9	advisers 8:25
	177:6,17 181:2	actor 54:7 127:1	162:24,25	13:14 25:19

103:1 127:12 132:17,24 198:16 advocacy 10:16 20:25 21:11,12 45:11 64:12 144:6 affiliate 155:8 155:11,19,23 162:25 affiliates 150:11 187:6 affinity 17:2 34:17,19 46:4 46:4 60:12 120:17 129:3 affirm 210:10 affirmative 108:10 afforded 102:8 afternoon 55:14 55:14 76:9 209:16 age 27:4 28:20 28:20,22,24,25 40:10 139:18 agencies 24:18 agency 7:2,13 8:8,9 10:18 12:22 24:25 104:15 165:21 agenda 14:4 189:20 agent 105:20 143:15,23 144:24 145:10 147:8,22 149:2 150:6 157:10 157:20,24 158:4 160:21 161:8 163:19 163:24 164:10 165:14 166:16 166:17,19,24 167:11 170:12 171:14 172:2 172:12 agents 10:25 19:7 102:16	105:7 120:1 143:4,20 144:9 144:11,16,19 146:6 147:12 148:11,13 150:16 151:13 153:15 154:1 158:7 160:19 161:3,25,25 162:3,20 163:2 163:3,5 164:16 164:19 167:3 167:23 169:6 169:12,14 170:6 171:6,6 171:17 agents' 126:23 aggregate 133:14 134:13 aggregates 124:5 aggressive 194:20 ago 22:16 64:5 105:2 113:7 117:14 149:1,7 194:9 agree 71:18 85:13 92:13 93:24 99:2 158:8 163:10 164:12 166:25 167:1 172:15 179:23 Agreed 160:8 agreeing 19:13 143:7 agreements 109:20 181:21 ahead 19:18 205:4 air 163:13 203:14 Alabama 64:6 alert 38:6 68:14 68:25 139:7 205:11 alerted 67:2 alerts 95:20	139:24 140:21 197:7 198:10 aligned 99:4 allege 32:25 alleged 18:2 allegedly 17:22 60:8 alleges 17:11 alleviate 103:16 allow 82:4 83:9 92:21,23 97:23 99:14 allowed 9:20 39:25 92:10 107:10,11 182:5 allowing 24:23 193:23 allows 88:22 89:13 95:7 allude 152:19 alluded 25:8 37:8 146:19 161:6 202:8 203:11 alternative 82:23 90:6,8 alum 144:1 amass 151:16 amateur 202:17 Amazon 57:11 75:13 amend 78:25 amended 95:12 amendment 85:9 amendments 79:7 80:19 84:13 85:14 86:1 American 25:4 199:7 201:8 Americans 200:18,20 201:13 Ameriprise 122:14,16 132:16 AML 123:5,19	123:19,21 124:18 129:19 130:2,3,8,10 130:13,15 132:9,25 135:12 138:20 140:20,23 AML-related 139:12 amount 28:6 44:13 55:8 60:23 78:1 86:3 87:22 94:5,6,22 96:8 112:7,9 145:4 160:10 183:14 amounts 130:16 analyses 18:4 analysis 21:9 107:15 180:7 analysts 188:17 analysts' 188:19 analytical 134:12 analytics 48:2 137:12 analyze 109:23 137:13 analyzed 109:3 analyzes 181:14 analyzing 130:18 and/or 111:13 Andrea 4:9 147:15 152:20 156:3 159:11 162:23 anecdotal 58:5 Anka 106:8,13 106:14 107:4,9 107:20 108:15 108:23 109:9 111:4,11 113:23 announced 16:10 17:6 74:19 announcement 39:4	annual 36:4 79:2 199:5 annuities 30:24 anomalies 156:21 anomaly 156:14 anonymizing 133:17 another's 206:22 answer 33:24 52:2 60:1 62:11 69:10 112:6 answers 125:5 anti- 122:6 123:4 135:4 anti-fraud 122:15 anti-money 102:4 122:13 123:9 140:17 antifraud 102:3 114:21 130:2,6 130:8,9,14,17 132:10,25 160:25 anybody 28:14 113:9 145:20 149:11 anymore 57:13 95:18 96:23 111:6 anyway 166:5 apart 110:15 apathy 29:11,19 Apologies 208:1 apologize 100:22 apparent 13:10 124:12 160:24 appeal 71:19 appear 205:3 appendix 79:8 applaud 7:21 applicability 184:20 applicable 83:12 113:9
---	--	---	---	---

application 80:5 85:3 94:11,18 95:2 161:23	11:19 12:7 15:19 26:1 31:4 33:13,14	59:8 81:24 139:23 140:9 158:2 175:6	155:7	113:11 164:1 171:4 176:10 187:1 208:17 209:8
applications 80:2 81:12,15	38:18 46:1 58:3 67:17 81:5 86:14	asks 72:24 158:3 aspect 86:15 162:22	attending 12:19 attention 72:5 79:16 112:4 199:22	avenues 199:4 average 12:3 175:21
applies 68:18 180:15	110:21 111:13 118:24 119:16 119:24,25	aspires 134:2 assess 47:20 assessing 86:23	attests 155:24 attorney 25:2 31:18 104:14 166:22 168:6,8	avoid 8:6 138:8 award-winning 197:11
apply 21:3 68:7 85:2 99:23 104:18 164:3	122:7 132:14 138:20 139:4 146:1,11	asset 7:5 16:21 38:20 49:12 68:12 70:16 71:21 122:18 191:6,6	attorneys 105:9 126:24 149:3,9 150:3 168:3 180:5	aware 96:9 144:19 160:23 162:3
appreciate 32:2 35:14 51:16 63:23 76:8 78:23 80:7 82:12 120:24 169:22 171:3 171:23 184:10 208:4	152:23 153:4 154:22 156:25 160:18 162:11 169:21 180:3 181:2 191:14 195:2 199:25 205:6,8	assets 20:21 33:5 67:18,21 67:24 71:16 72:15 112:2 114:12 124:5,9 139:18 140:7	attracted 16:17 attributable 87:15 attuned 139:16 atypical 183:15 183:16	awareness 21:14 36:24 37:6 46:2 126:18 awful 119:6
appreciation 117:12	areas 21:17 26:18 32:3,15 73:20,23 76:3 76:6 131:21 139:5 146:13 180:25 204:5 205:9 208:23	assistant 143:13 175:4	audience 71:20 172:13	<hr/> B <hr/> B 114:5 127:5,8 127:8 159:1,5 159:8 163:11 163:12
approach 10:22 11:1 21:4 25:13 28:6 96:5 160:20,25 161:1,5,10,17 161:18,20 164:13,20 167:23	areat 58:17 arguably 107:22 108:24	assist 141:12,16 assistance 31:16 143:15 154:10 158:3	audit 115:14 audited 51:11 88:3,11 auditor 115:15 auditors 180:5 Australia 206:6	authorities 13:16 206:24 authority 25:18 151:14 166:17 173:4 174:19 177:17 178:7 180:10,14
approached 23:23 24:2	arguments 110:4	assistant 143:13 175:4	authorities 13:16 206:24	authorization 167:18
approaches 1:5 18:13 161:16	arguements 110:4	assisting 147:13 163:5	authority 25:18 151:14 166:17 173:4 174:19 177:17 178:7 180:10,14	authorized 127:6
appropriate 91:5 92:15 98:8 103:25 171:1 172:1 174:6 192:24	Arisa 19:16 AriseBank 33:4 arises 156:14 arms 38:20 arrangements 105:11	associate 30:10 108:9 143:25 associated 18:12 94:1 108:16 Association 25:5 147:19 201:9	authorities 13:16 206:24	authorizing 163:2
appropriately 8:15,23 150:5	array 19:8 204:2	associations 141:14	authorization 167:18	authorized 127:6
appropriateness 22:1	Article 156:25 artificial 137:15 aside 203:5	assurance 131:19 assure 137:1 asymmetric 183:21	authorizing 163:2	authorizing 163:2
approved 83:1 83:10,13 85:14	ask-your-inve... 65:17	assure 137:1 asymmetric 183:21	auto 41:25 automated 130:24 183:10	auto 41:25 automated 130:24 183:10
approximately 64:10 134:8	asked 58:11 62:17 63:13 103:3 128:21 157:11 166:16	athletes 17:10 ATS 189:12 attached 204:11 210:10	automatically 66:22 available 9:12 9:13,23 52:24 87:23 89:19 95:9 98:22	automatically 66:22 available 9:12 9:13,23 52:24 87:23 89:19 95:9 98:22
April 16:9	asking 6:18 54:12 57:2	attempted 124:4 attempts 139:13 attendant 93:20	available 9:12 9:13,23 52:24 87:23 89:19 95:9 98:22	back-end 51:9 backfill 128:14 background 52:25 58:21 80:15 82:21 84:6 90:14 153:18 197:1
arbitration 30:18				
area 7:21 8:19				

backgrounds 61:11	bartender 199:17	182:7 185:11 192:4	125:22 149:19 149:21 170:13	boom 188:18
bad 13:24 21:22 29:24,25 40:20 48:11 50:9 51:4 53:16 54:7 59:23,24 61:7 62:18 64:23 65:1,11 65:23 66:20 73:22 126:8,12 126:14,22 127:1,9 128:15 130:5 133:16 133:16 149:4,9 149:9 165:13 165:19,19 177:3 195:20	base 40:19 70:21 138:18 184:24 based 27:5 40:2 70:11 87:22 91:2 98:7 108:7,25,25 153:13 161:2 185:23	believer 195:3 benchmarking 200:14 Beneath 88:7 beneficial 96:14 100:14 139:24 beneficiary 94:7 benefit 76:4 110:22 186:4 202:1 209:2 benefits 76:23 189:12 bespoke 114:5 best 12:3 14:12 15:17 51:20 65:16 73:25 74:24 80:4 88:20,21 91:5 92:24 137:22 138:6 141:12 164:13,20	195:3 201:16 203:21 206:7 206:13,14 bigger 155:20 biggest 32:15 36:23 89:1 114:22 138:17 156:1 178:23 bilked 17:23 bill 103:11 104:2 billion 26:3,10 187:17 bingo 199:6 207:16 bit 42:23 43:1 52:5 54:18 56:6 57:3,17 57:18,24 75:20 76:3 82:21 85:21 107:3,25 111:12 133:22 136:19 155:10 158:17 164:22 167:23 175:7 182:11,21 183:5,8 194:19	borderless 23:7 33:17 borne 166:4 bottom 69:4 88:15 bought 53:25 55:13 boutique 80:1 boxes 109:18 Boyce 210:9 brace 29:13 bracket 115:7 branch 122:25 Brazil 206:6 breach 129:11 bread 105:15 break 76:12 127:25 142:12 breaking 125:3 187:14 breaks 194:16 brethren 121:4 Brett 2:8 6:4,21 10:8 14:10 20:5 38:23 48:17 82:17 98:1 100:19 142:24
badly 194:16 Baird 2:9 6:12 76:17,21 100:24 121:1 142:2,25 balance 91:6 balances 94:19 balancing 103:16,17,25 192:21,23 ball 83:5 Baltimore 7:21 23:20 45:23 bandwagon 207:13 bank 17:12 53:22 80:1 94:17 121:13 122:1,17 123:14 124:11 127:4,5,8,8 134:9 136:4,6 banking 80:1 93:3 bankrupt 188:11 bankruptcy 26:4 banks 24:1 175:25 barred 46:25	bases 197:23 basic 66:2 78:9 basically 28:4 52:5 87:9 89:6 94:22 97:8 101:10 128:7 157:3 basics 200:1 basis 23:20 78:16 118:8 127:19 130:19 132:5 bathwater 114:8 battling 126:11 BB 181:12 BD 101:5,6,8,10 114:7 beat 25:11 Becker 4:4 147:1,1 148:10 154:17 156:8 158:24 160:8 163:7 165:9 170:4 171:25 becoming 114:6 beginning 43:10 43:13 98:4 166:5 begun 72:19 behalf 148:15,15 behavior 13:8 40:23 127:20 behavioral 186:7 202:3 206:8,9,25 believe 58:17 59:3 61:17 82:1 98:14 104:1 158:11	bet 122:11 better 8:21 9:6 40:1 50:23 51:12 90:3 93:21 98:12 100:19 140:6 158:17 167:22 180:7,8 185:8 185:20 189:23 194:8,22 201:10,21 205:17,21 206:10 better-known 71:21 beware 42:6 beyond 27:20 29:7 143:23 151:7 154:17 159:15 biases 202:3 bids 178:21 big 24:4 26:2 34:4 38:18 45:1 85:17 89:24 117:20	195:3 201:16 203:21 206:7 206:13,14 bigger 155:20 biggest 32:15 36:23 89:1 114:22 138:17 156:1 178:23 bilked 17:23 bill 103:11 104:2 billion 26:3,10 187:17 bingo 199:6 207:16 bit 42:23 43:1 52:5 54:18 56:6 57:3,17 57:18,24 75:20 76:3 82:21 85:21 107:3,25 111:12 133:22 136:19 155:10 158:17 164:22 167:23 175:7 182:11,21 183:5,8 194:19 BitFunder 33:3 blame 54:8 blasts 55:9 blind 160:23 blockchain 33:3 36:16 178:4 blog 61:20 blogs 189:17 Bloomberg 189:16 blue 186:10 blunt 168:21 board 208:19 boiler 20:18 bolster 13:17 Bomb 187:20 bonding 116:13 bonds 60:10 book 117:18 193:22 books 102:2	bricks-and-m... 68:5 brief 11:15 77:23 121:24 123:4 178:16 briefly 125:24 179:16 196:21 196:21 bring 21:4 88:24 98:6 111:12 120:19 188:8 195:17 196:13 bringing 17:14 22:22 32:23 45:22 118:6 119:1 195:3 brings 13:12 66:3 205:17 broad 20:15 23:4 25:13

34:14 129:17 180:14 broadens 139:1 broader 7:8 broadly 14:24 132:10 145:24 Broadridge 147:7 150:1 broke 194:12 broken 185:15 194:18 broker 30:19 52:23 75:22 83:9 89:17,18 92:25 93:4,17 101:19,19 103:10 105:3 105:11 106:5 106:11 108:1 109:8,11,13,15 110:11,14 112:16,25 114:6 117:2,13 150:23 155:22 155:24 broker's 150:11 broker- 25:18 87:11 92:23 101:2 104:25 112:9 114:22 118:20 121:13 123:7 136:13 140:14 broker-dealer 19:1,3 77:16 78:7 81:19,24 82:1,4 83:2,6 83:12,21 86:22 87:19 90:7 92:21 94:4,23 95:1 101:11 110:6 112:4,5 113:3 114:19 114:20 120:16 121:6,15 124:1 124:4,6,16 141:12,18 168:18 183:16 broker-dealers	5:9 8:25 13:14 18:23 64:2 78:10,13 79:10 79:11,17 81:12 85:22 86:4 87:14 88:19 89:22 90:15 91:1 92:17 95:8 97:19 101:7,12,21,24 102:8,13 103:1 105:6 110:19 115:6 117:15 118:7 120:2 122:1,25 123:8 123:10,24 134:3 139:19 141:13 184:22 198:15 broker-dealers' 92:22 brokerage 63:19 155:25 169:16 187:1 200:19 BrokerCheck 52:23 61:24 62:7,8,13 66:4 66:23 67:2,8 brokers 20:19 63:6 83:17 87:10 90:1 98:22 105:7 115:3 123:6 129:8 135:22 164:16 168:22 169:4,7,9,15 brought 17:21 26:2 36:6,8,13 39:1 81:7 90:22 93:22 105:12 145:25 153:22 164:10 169:1 177:22 180:12 186:22 204:14 buckets 173:9 bugaboos 206:14 build 65:13,17	97:22 188:21 193:22 199:8 building 12:24 74:22 89:5 102:24 built 96:10 166:9 bullet 189:22 bulletins 197:8 bunch 34:11 43:25 49:21,22 70:25 116:4 117:3 168:9 burden 18:8 114:22 166:14 166:21 171:14 burdens 114:18 116:21 burdensome 115:13 bureau 24:20,24 104:9,10 198:5 201:10,21 business 33:11 53:12 68:22 84:1 94:10,14 99:11 101:20 105:15 108:5,5 109:4 113:16 113:19 114:11 114:11 115:20 124:12 132:16 135:23 142:8 147:3,4 181:9 183:8 184:24 201:10,21 businesses 33:21 117:5,9 134:10 194:11 busted 47:23 busy 14:12 17:14 208:11 butter 105:15 button 133:7 buy 37:13,22,24 38:2 52:22 56:1 102:7 136:16 202:19 buy-ins 194:13	buyers 193:7 buying 131:1 193:7 <hr/> C <hr/> C 5:1 6:1 159:1 159:5,8 163:11 163:12 CAB 117:12 California 111:18 call 36:14 38:1 49:20,22 87:25 88:8,15 99:24 112:13 125:9 126:20 131:22 194:25 called 83:18 128:19 156:4 calling 17:23 37:12 69:23 117:6 158:18 calls 27:22,24 37:20,21 38:8 38:10 40:6,6 40:14 43:13 44:14 55:25 63:17 72:15 112:6 157:23 190:2 192:20 Cam 22:4 24:19 25:8 33:14,16 33:23 35:24 37:8 46:3 53:11 59:19 60:3,17 67:7 69:2 71:18 74:6 cameras 177:8 Cameron 2:22 39:22 campaign 34:7 197:6 201:15 Canada 25:6 206:7 Canadian 106:14,20 107:6 206:1 cannabis 203:25	204:1 205:2,3 cap 175:20 187:18 capability 90:16 capacity 10:11 29:6 62:3 63:9 89:16 188:15 capital 25:9 91:6 91:11,14,15 101:13 103:21 103:25 114:25 115:3,7 116:2 116:9 117:5,12 120:6 121:3 195:24 capitalization 99:18 capitalizing 60:14 caps 138:9 card 177:6 187:23 cards 56:14 care 60:15 career 102:23 105:1 careful 30:2,5 188:5 Carlson 3:4 79:23,24,25 84:23 93:24 carried 149:2 carry 18:7 22:12 carrying 51:8 cars 35:19 Carter 102:22 case 23:22 25:15 33:3,4,4 39:2 45:23,23,24,24 46:23 54:6,7 60:6 94:18 109:25 110:2,2 110:3,5,7 113:23 119:18 119:19 120:18 130:11 153:25 157:19 169:1 171:13 178:1 cases 13:4 17:14
--	--	---	--	--

20:22 25:17	79:4,5 85:25	69:12 132:1	charm 48:9	207:21
26:11 32:23	86:9,10,13	198:24	Charu 2:21 20:1	Chris's 60:24
33:3,4 36:13	95:22,23 96:8	challenges	20:6 32:12	65:13
36:15,20 45:22	96:13 97:14,21	150:24 192:14	33:22 45:1	Christian 2:14
50:7 53:19	99:8 101:11	192:15 193:1	59:25 68:2	6:13 19:6
60:4,11,17,21	115:3 116:9	194:4,6 199:24	73:24	142:23 145:17
61:2 64:16	121:6,15	208:22	chatrooms	146:19 172:24
65:6 67:1 77:2	134:15 161:8	challenging	18:20	196:5,16
109:10 110:11	167:6,15 182:5	181:24 184:11	check 37:23	Christine 210:9
117:9 173:9	191:6,7	198:13	52:20,24 55:6	Christmas 37:1
177:22,22	certainly 26:12	chance 49:5	61:18 62:5,8	Christopher
189:25 193:9	64:2 67:20	140:6 197:20	109:18 148:25	2:23 3:7 4:7
cash 24:1 183:11	80:3 84:24	chances 115:23	149:3,24 150:2	39:23 104:8
casks 68:17	87:6 88:3,16	115:24	150:3	198:4
categories 116:9	88:25 89:21	Chandrasekhar	checkbook	Christy 4:10
134:16	92:8,10 96:24	2:21 20:2,4,6	202:20	175:1 178:14
categorization	97:15 99:3	32:18 45:6	checkbox	179:8 182:23
89:7	116:14 124:23	60:3 68:3	137:13	189:3,11 190:2
categorized	128:3 131:2	73:25	checkboxes	191:13 194:4
87:22	139:16 160:5	change 36:10	137:11 138:23	church 34:16,18
category 20:15	167:4 170:23	49:24 85:9	checked 61:11	46:5,11
89:8 117:24	179:13 196:13	89:24 99:11,12	61:12 63:12	churning 20:19
173:18	198:7 199:24	115:15 130:25	128:18	32:14
Catholic 201:9	204:8 205:1,8	164:6 205:19	checking 62:15	circle 87:13
caught 115:22	208:15	changed 10:11	checklist 163:1	circumstances
165:20	certainty 164:15	17:1 127:3	checks 94:19	63:6 92:25
cause 90:17	CERTIFICA...	147:5 194:10	197:1	93:3 99:8
123:17 173:23	210:1 211:1	changes 8:20	cheer 176:17	102:11 157:7
202:18	certify 210:9	15:18 84:14,18	cherry 129:9	160:12 173:6
caused 15:14	211:3,9	89:15 94:3	chief 20:6 24:20	174:20
67:4 173:23	cetera 173:17	153:1 171:1	24:24 104:9	citing 110:18
174:8 206:16	CFTC 205:16	182:13 193:16	144:5 147:2	citizen 34:16
causes 156:15	chair 25:2 26:24	changing 204:10	175:1 198:5	City 147:10
cautious 70:10	66:2,2 175:16	channels 197:14	China 203:14	claim 16:24
71:5,8	Chairman 2:3	197:16 205:21	choices 11:24	38:25 44:6
CDs 47:9	6:14,18,19,20	characteristics	Chris 4:12 24:15	56:19 61:10
cease 70:19	7:2 10:5 12:9	97:14	24:19 26:20	62:4
cell 34:12	14:2 16:4 17:5	characterized	35:24 52:9	claims 30:17
centers 13:15	22:7 23:16	109:15	54:16 61:23	68:14,24
197:24	24:22 35:18	characters	62:6 67:7	clarification
central 21:19	38:19 39:8	195:5	70:16 74:15,22	113:14 114:4
33:10	45:20 48:17,21	charge 104:10	104:6,19	clarity 100:12
centralized	51:23 52:3	116:12	118:17 121:2	110:22 111:2
22:16	54:11 58:12	charged 17:7	174:25 181:4,7	111:12 112:21
cents 55:15	98:1,3,25	24:25 60:7	182:18 184:5	class 38:20
CEO 175:3	99:16 100:18	162:4	189:2,9 192:25	classes 53:2
certain 40:23	Chairman's	charges 17:22	198:1 200:10	classic 20:17
60:11 63:6,11	52:13 58:24	charisma 59:19	200:16 201:4,5	26:13 37:9
78:9,14,25	challenge 24:4	Charities 201:9	204:6 205:25	68:7

classify 58:8	closer 159:22	202:21,22	208:17 209:7	commit 115:22
Clayton 2:3 6:14	160:6	210:3	209:10	committed 13:7
6:18,19,20	closest 25:11	combination	commentary	197:3
14:2 16:4 17:5	closet 116:22	134:9	61:20	committee 25:3
24:22 38:19	closing 5:14	combined 130:9	comments 16:1	36:4 147:19
39:8 48:17,21	127:1,2,8	come 19:17 30:6	39:19 98:6,9	206:5
66:3 98:1,3,25	144:3 169:25	31:9,14 36:24	98:10 100:3	common 20:22
99:16 100:18	clothing 34:22	43:12 44:25	126:5 139:10	21:14 26:11
177:4,14	co-panelist	49:4 54:5	161:11 169:20	40:14 116:11
clean 203:14	24:15	56:12 59:3,5,8	169:25	131:7 152:7
cleaning 181:3	cochair 147:18	61:10 66:24	commercial	205:18
clear 97:4 98:10	179:18	70:13 73:9	164:15 207:19	common-soun...
98:12 137:25	code 50:20	76:2 79:16	commission 1:1	38:10
190:9	codify 86:12	98:13 114:9,19	1:23 6:3 8:20	communicate
clearance	coffee 6:9	116:22,23	9:4 14:4 16:4	87:17 140:5
173:25 174:13	coin 129:6 130:3	131:12 145:20	17:6,10,14,17	141:10
182:8	coins 71:25 72:6	150:24 151:5,9	17:21 18:25	communication
clearing 96:24	72:9	151:12 187:13	20:10 21:7	43:5 85:1
168:22 169:4	cold 17:23	191:10 194:14	28:16 32:23	93:16 183:25
185:16	Colish 3:5	196:11 207:10	38:19 45:21	189:7 208:25
clearly 111:6	102:19,21	208:11	54:2,3 60:7	communicatio...
124:11 179:6	111:14 118:18	comes 14:24	70:14 77:7	180:8
190:4	collaborate	21:1 32:21	78:4,24 79:1,7	communities
client 58:20	21:11	34:4 43:11	79:15 84:13,19	60:12,12 129:4
132:22 139:17	collaboration	50:21 52:17	91:4 105:2	community
140:7 157:10	207:10	61:1 71:8	116:12 117:4	25:16 43:7
167:12 184:24	colleague 202:15	72:23 89:10	121:25 144:1	46:10,12 60:13
clients 31:9 58:6	colleagues 7:7	114:23 183:10	145:24,25	60:19 72:8
67:14 73:12	11:13 16:5	201:14 202:4,9	149:4 154:25	74:3 80:1
83:24 88:20	23:3 24:17	206:11,12	161:12 165:20	140:15 141:12
112:1 127:13	48:3 77:11	207:9	171:16 179:14	141:18 168:18
129:12 130:6	134:7 205:25	comfortable	210:12	172:2 175:25
132:17 133:11	207:8	67:5 107:21	Commission's	198:11 201:6
140:7 147:23	collecting	149:17 184:22	14:16 18:7	201:12
147:24 150:17	108:19 109:19	coming 12:7	21:11 79:9	companies
153:10 167:12	133:17	35:13 39:14	143:19 203:6	26:16 37:15
171:21,21	college 15:12	45:5 55:25	commissioner	54:22 88:2,2
183:17	30:11,15	58:6 65:6	2:4,5,6,7 6:15	89:6 91:10,20
clients' 132:19	colleges 199:8	70:10 76:7	6:15 10:6,8	91:23 92:2
clinic 30:14	com 69:14	86:23 87:13	11:10,11,12	96:23 122:2
31:10 43:17	combat 5:9,11	97:9 154:20	12:16,17,18	126:24 146:2
44:15	9:1 10:19 11:3	160:5 203:25	13:2 14:8,9,10	151:1 186:3,19
Clinical 30:10	17:19 18:23	commend 14:1	15:10,24 76:10	187:3,9,13
clock 196:10	27:14 77:6,8	116:11	commissioners	194:10 195:4,9
Clooney 176:22	179:21 200:12	comment 39:9	6:16 13:6 14:1	195:13,19,20
177:8 195:5	combating 1:6	39:10,10 56:25	16:5 24:22	203:13,14
close 208:9	6:4,23 121:12	98:5 128:16	26:24 179:15	204:3 205:7,11
closed 193:23	211:8	155:2 159:4	Commissions	company 18:5
closely 24:9 72:5	combatting 13:9	172:17 192:8	206:4	88:14 89:9

93:13 95:17,21 97:4 99:11,13 99:20,21,21,21 99:24 122:16 125:14,15 147:3 176:19 176:25 194:8 194:11,17 195:22 196:2 203:16 204:25 compared 28:7 210:14 compares 181:23 compassion 60:15 compel 151:14 compelling 110:4 compensated 18:5 93:9,18 compensation 105:10 107:24 109:16 compete 198:18 competence 60:24 competing 207:18 competitive 178:21 competitors 83:4 complaints 22:17 23:1 24:7 37:19 complete 53:17 70:23 99:10,11 99:12 210:13 211:4 completely 53:3 99:10 114:8 195:9 complex 146:22 155:12 157:7 169:21 182:19 complexities 11:23 complexity	21:25 compliance 10:17 13:23 80:14 81:8,11 82:10 83:8 86:4 122:1 123:14,19 147:2,8,14 156:6 175:2 compliant 25:23 171:9 188:22 complicated 146:10 complied 82:2 component 173:15 201:16 components 123:12 201:16 comprehensive 138:1 184:11 comprised 25:5 compromise 126:21 compromises 126:11 computer 41:20 computers 34:12 Computershare 147:16,17 151:23 171:20 con 59:22 concentration 86:16 concept 116:10 143:19 145:5,7 146:18 155:3 159:5 160:17 166:10 170:8 concepts 164:22 concern 21:18 26:25 29:20 32:5 85:17 104:2 118:24 119:22,23 120:8 165:22 166:6 192:11 concerned 72:17 112:13 204:5	concerning 78:8 concerns 19:25 22:8 23:4 28:12 92:15 118:21 137:19 175:9 concerted 192:2 concise 137:25 concluded 209:18 condition 181:18 conditions 164:9 conduct 8:12 79:10 101:25 129:6 130:12 135:9 conducted 84:2 124:4,9 conducting 79:11 80:25 81:2 108:21 122:24 124:15 134:24 confidence 13:18 50:15,16 50:19 53:18 61:3 91:18,21 92:11 188:21 conflict 118:14 154:19,21 157:16 174:8 conflicting 151:2 confronted 23:17 confusion 174:9 183:20 190:9 Congress 103:12 conjunction 55:17 connect 207:8 connected 206:24 connection 129:2 144:23 189:15,24 conning 75:8 cons 14:18	202:10 consider 8:13,21 117:24 138:3 140:25 192:18 consideration 75:9 84:20 94:16 95:15 153:16 considerations 84:19 considered 86:15 considering 138:12 considers 174:4 consist 18:14 consistent 36:1 39:22 134:24 148:20 constantly 180:6 constituencies 58:3 constituency 39:17 constitute 113:16 consultant 109:15 consulted 103:14 consumer 8:10 28:16 31:17 consumers 27:19 28:5 29:4,11 57:2 57:16,20 contact 40:14,15 45:9 61:10 63:20 83:11 96:22 contacted 107:7 contacts 108:25 contains 79:8 contemplate 70:12 content 28:4 196:23 197:14 207:25 context 68:15,16	88:1 91:3 105:9 110:23 178:17 184:9 184:20 contexted 184:5 continually 30:22 continue 8:14 17:2 56:4 67:6 85:10,18 97:24 99:15 126:8 141:20 142:11 194:1 196:4 204:9 208:6 209:15 continued 3:1 4:1 14:2 36:18 continues 7:6 28:23,24 204:15 continuing 43:19 54:2 141:21 196:6 contract 55:18 contracts 204:22 204:23 contractual 90:12 181:19 185:18,21 186:20 contrast 108:15 109:9 contribute 200:25 contributing 169:23 contributions 9:25 control 126:12 126:22 144:20 146:5 150:4,12 155:7 controlled 127:9 155:11 controls 123:13 126:19 conversation 11:4 12:15 15:23 84:11
--	---	---	---	---

169:23 184:16	counsel 77:25	165:6 166:21	67:18,21,24	163:11,12
186:18 194:21	82:16,20 144:1	creates 154:1	71:5,7,9,15,19	D.C 1:25 210:7
207:22	144:5 147:2,13	158:17 162:18	71:22 72:6,14	211:6
conversations	147:16 154:12	creating 12:11	cryptocurrency	Dahiya 2:10
12:6 111:7	156:6 159:20	161:2 167:10	26:16 32:22	77:13,22 80:9
136:15 193:12	159:22 160:6	186:1 196:23	33:5 38:24	82:15 84:7
conversion	189:18	creation 164:24	39:1,3,5,7 68:4	95:3
151:19	counsel's 102:24	creatively 199:2	68:12,16 72:25	daily 134:14
conversions	count 148:11	creator 176:1	cryptocurrenc...	damage 15:14
151:11 153:8	counteract	credentials	32:25	damages 151:19
convertible	16:15	125:2,4,6	cultural 46:12	151:20
125:9,12	countries 178:22	credible 41:12	culture 176:14	Dan 82:16 84:7
convince 16:23	country 42:12	credit 177:6,11	176:19	93:25 100:25
56:17	63:6 151:24	187:23	curbing 145:21	dangerous 48:14
convincing 59:7	199:20	Crime 206:19	cured 188:9	69:22
coordinated	counts 48:12	crimes 121:23	currencies 36:15	Daniel 3:12
37:25 205:14	couple 15:25	126:3 180:5	69:25	data 16:12 21:1
coordinating	24:14 37:5	criminal 124:17	currency 43:12	22:23 35:22
180:2	43:2 44:22	critical 6:23	43:14,23 44:14	48:2 176:8
coordination	61:1 67:16	64:22 137:12	69:16,24 70:4	180:7 185:24
135:1	74:20 83:11	137:15 182:17	current 14:7	206:12
cops 25:11	130:14 133:1	critically 85:23	17:10 19:20	data- 21:3
copy 153:18	148:12 149:20	131:16 137:16	28:5 49:11	database 127:21
core 94:10 106:1	coupled 38:16	Cromwell 4:5	79:3 88:5,11	136:4
143:21 203:8	112:21	169:20 175:2	89:9 101:2	date 190:15
corners 15:8	coupon 54:3	175:11 179:24	105:5 126:5	210:6,19
159:18 160:9	course 26:14	185:4 189:4,11	184:20	211:14
corporate 95:23	36:6 47:17	190:3 191:22	currently 5:6	David 4:4 57:17
100:8 147:16	65:14,23 70:3	193:13,20	18:17 47:24	146:24 147:1
182:6 183:21	94:14 113:7,23	194:3 206:9	95:9,19 193:19	150:4 156:18
183:22 193:17	156:2,14 171:2	cross 174:23	curve 69:5,5	159:11 160:14
correct 72:10	171:4 191:23	crowdfunding	custody 114:12	161:6 170:3
113:22 178:9	197:21	168:16	customer 63:10	172:9
187:4,11	court 110:3,7	crypto 36:16,21	78:19 114:12	David's 170:21
cost 31:13 51:8	153:18,19,21	36:22 39:14	121:18 124:13	170:24
91:14 93:20	courts 110:12,18	49:12 68:18	154:4,18	day 10:4 22:12
115:13,16	112:23 153:22	70:14,16,23	customers 74:3	92:3 94:10
118:8 168:15	cover 162:11	71:2,6,8 194:8	74:4 89:22	106:17 137:1,2
188:22	163:13	194:24 203:15	131:4	146:12 164:7
cost-effective	covered 161:23	crypto- 70:19	customized	171:18 184:23
168:17	covers 162:22	crypto-frauds	114:5	188:10 199:10
cost/benefit	crack 50:17,20	36:14	cut 98:15,23	208:12
161:17	crashing 38:3	crypto-related	cybercriminals	day-to-day
costs 31:18 91:1	create 79:5 90:2	70:15	126:8,12	146:14,16
93:25	153:9 154:6,8	crypto-type	cynical 185:10	148:3
Coulson 4:5	154:9 161:6	194:11	cynically 195:11	de 113:18
168:1 175:2,12	169:5 185:7	cryptocurrenc...		deadline 97:8
185:7 192:7	197:7	20:21 36:14,17	D	deadlines
194:6	created 80:24	37:2 38:16	D 6:1 159:1,5,8	207:21

deal 9:17 31:2 66:19,25 72:20 73:18 97:19 108:10 124:13 151:4 152:15 185:19 196:23 207:4	define 117:23 191:4 definitely 41:17 43:6 74:22,24 85:13 95:14 166:25 171:17 definition 113:17 118:1 definitive 192:17 defraud 26:17 44:1 56:7 60:15 73:22 defrauded 30:16 48:6,10 130:7 defrauding 176:18 degree 75:3 83:19 92:9 93:6 98:18 Delaware 26:4 delay 151:19 158:17 160:11 172:20 delays 156:15 165:25 Delighted 20:8 deliver 207:17 demonstrate 81:15 demonstrates 13:12 denigrate 114:16 dent 180:22 department 8:9 80:13 95:20 150:2 181:8 200:9 206:18 depending 32:10 55:19 127:19 149:14 160:12 deploy 33:18 deploys 21:1 deputy 6:5,11,12 19:6 76:18 142:23 derivative	173:14,15 derived 124:8 124:10 describe 56:6 105:19 130:2 198:2 described 101:14 deserving 195:16 designation 123:18 designed 22:16 114:10 117:8 123:14 124:10 desists 70:19 desk 114:1 183:11,14 despise 175:13 detail 56:6 103:13 145:4 158:10 192:2 detailed 11:19 152:1,9 191:25 details 44:22 164:1,2 detect 48:16 121:14 123:16 129:19 detecting 8:11 121:18 129:16 detection 22:5 22:14 129:23 131:10 deter 7:3 8:21 determination 151:2 determine 52:6 151:3 174:5 determines 173:20 deterrent 36:25 94:2 develop 7:13 163:21 developed 58:12 developing 121:25 125:5 207:14	development 31:5 186:11 developments 87:4 deviate 7:18 deviating 9:9 devices 133:15 dialogue 102:20 145:16 170:23 170:24 184:11 196:6 dichotomy 109:23 diet 23:5 differ 100:20 difference 43:2 155:21,21 156:1 162:7 182:16 differences 89:1 130:14,21 201:20 202:5 different 11:24 14:17 32:3 33:24 39:16,21 40:24 42:23 53:6 56:12,22 57:22 59:21 61:1 62:20 71:7 85:13 99:10 107:2 129:22,23 132:8 138:21 146:21 148:11 152:25 153:2 155:18 176:7 178:22 207:18 208:23 differential 60:25 differentiation 169:12 differently 29:25 difficult 151:1 154:13 158:25 162:9 192:17 202:14 dig 166:24	172:18 digital 7:5 16:20 20:21 33:5,7,9 67:18,21,24 68:12 69:24 70:4,16 71:16 72:14 197:13 197:19 diligence 68:20 107:15 108:22 109:20 159:17 162:13 164:4,7 166:20,22 diminished 29:6 63:9 dinner 198:17 dinners 198:19 direct 38:24 93:15 174:18 183:25 directed 129:20 direction 52:7 211:11 directly 96:22 114:23 116:5 160:5 193:14 director 6:7,9,11 6:12 11:12 12:9 76:18 142:24 143:13 147:8 175:4 directors 99:12 disadvantage 119:4 disbarred 150:3 disburse 126:16 disbursing 62:23 64:13 discern 44:9 89:8 disciplinary 160:1 disclaimer 16:2 208:21 disclose 129:12 187:5,5 disclosed 70:8 89:25 disclosing 55:4,8
---	---	---	---	--

disclosure 51:19 67:3 85:15,18 88:8 89:12,13 90:23 94:5 128:11 176:8 185:20,24 186:10,23 191:7	dismissive 110:17 dispensing 15:2 display 47:18 disregard 114:8 disruption 173:24 174:12 disseminated 183:22 dissemination 181:12 distinction 167:21 distributed 168:16 distribution 8:22 145:2 146:3 197:10 distributions 145:22 160:22 161:8 district 109:25 110:11 division 6:7,9,12 6:21 7:11,19 7:24 13:21,23 20:7,12 21:8 70:14 77:13,15 77:17,25 105:3 128:20 143:13 172:2 175:4 179:10 divisions 10:15 13:11 docket 153:25 203:6,7 doctors 17:9 document 58:18 118:14 documentary 150:22 documentation 155:22 157:13 documents 17:11 110:25 150:12 159:17 159:18 doing 13:7 21:5 35:20 43:25	50:12,12 66:11 68:20 69:7 93:10 94:9,14 111:24 112:11 115:19 137:12 147:3 149:23 158:6 185:12 186:3,4 187:5 188:23 194:22 196:18 197:25 198:8 199:3,9 199:14 206:25 207:7 dollars 26:10 dollars' 187:17 Donley 2:18 144:4 196:16 202:25 204:6 205:10 207:20 door 99:24 dormant 95:10 95:17 doubt 200:23 downside 164:25 165:4 downstream 168:2 dozens 197:7 drafting 138:3 dramatically 190:2 drank 53:23 Drastic 193:16 draw 98:9 draws 7:12 dream 202:19 drill 156:17 164:21 driven 21:4 176:9 driveway 35:19 drop 116:9 dropping 115:2 due 107:15 108:21 109:20 146:7 159:17 162:12 164:4,7 166:19,22 174:17	duly 172:9 dummy 44:8,9 71:3 dump 7:16 23:6 26:13 32:14 37:9 39:6 128:5,13 195:18 dumps 20:20 33:16 195:20 203:12,12 duping 19:19 duties 169:8 duty 129:11 151:16 171:10 187:9 dynamic 208:24	echoing 126:5 132:8 139:9 economic 12:13 21:8 economics 186:7 186:8 206:9 ecosystem 208:22 ed 54:13 198:15 198:24 199:14 educate 35:6,8,9 75:17 127:12 educating 74:4 education 10:16 18:9 19:7 21:10,12 27:20 28:3 31:20 45:11 52:15 53:2 132:9 143:5 144:4,6 196:14,19,22 198:2,8 200:7 200:9 206:5,10 207:1,23 educational 42:3 61:11 educationally 29:18 effect 39:1 108:9 117:13 151:17 173:22 174:3 174:10 193:6 effecting 101:20 105:14 107:22 108:3,14,17 109:5,18 110:5 113:16,22 effective 85:21 184:19 191:17 effectively 107:5 115:7 effects 15:11 177:3 efficiency 85:4 185:9 efficient 176:11 185:2,8 efficiently 180:7 185:1
E				
E 5:1 6:1,1 142:16,16 159:1,5,8 163:11,12 earlier 20:12 32:13 54:16 56:14 60:7 66:22 108:1 176:6 177:21 182:4 204:13 206:10 early 6:8 59:8 195:14 earned 112:8 ears 41:7 easier 57:10,19 117:8 150:18 152:18 157:20 158:6 easy 11:22,23 34:21 43:20 44:9 57:5,12 62:18 65:2,8 66:4 73:22 75:2,13 91:22 152:4,19,19 Ebola 15:1 echo 170:21 189:10 echoes 172:17				

effort 7:8 11:8 14:7 36:22 37:25 38:11 64:18 134:18 135:4 137:24 153:15 192:2 205:15	73:11 emerge 36:17 132:11 emerged 36:7 76:23 emerging 21:17 29:8 41:8 133:10 emotional 29:15 202:22 emotionally 29:3 emotions 29:21 emphasis 94:25 employee 138:18 employees 127:12 132:10 132:23 156:9 204:21,21 empowered 63:5 empowering 27:19 enables 8:3 enabling 91:10 enacted 63:25 enacting 64:6 encourage 35:11 59:13 68:13,19 113:10 encourages 52:21 53:8 encouraging 59:8 139:25 207:12 ended 178:17 endorsement 107:13 enforceable 204:23 enforcement 7:11,19,24 8:5 10:15 13:24 14:3 18:7 20:8 20:12,25 21:1 21:4 24:5,9 25:3 32:22 36:4 50:23 64:7 75:7	121:17 122:3,6 124:2 125:22 125:25 126:2 128:19,21 134:7 136:12 136:23 139:8 146:1 175:4 177:22 179:10 179:19 207:7 Enforcement's 13:9 engage 10:12 31:20 84:20 91:4 engaged 43:14 101:20 105:14 108:5,5 109:17 128:12 142:8 142:10 engaging 17:7 110:24 113:16 113:18 194:10 197:19 enhance 8:24 18:23 193:11 Enhancing 5:8 enormously 121:16 ensure 28:3 65:25 66:7 75:22 81:18 82:10 83:8 85:22 157:17 ensuring 163:25 enter 55:19 91:10 entered 8:5 entering 121:6 enterprises 16:23 enthusiastic 10:20 19:13 entire 13:10 entirely 60:9 132:4 203:15 entities 13:14 17:7 18:1 32:24 77:5 121:6 142:8,9	170:24 177:2 entrust 61:15 entry 101:15 environment 85:13 111:10 epicenter 106:7 EQ 147:3 equation 101:8 119:19 Equiniti 147:3,3 equities 178:19 equity 47:11 82:24 84:15 87:20 109:14 173:5,14,18 181:10,15,20 181:22 era 33:6 69:15 eradicate 13:8 Eric 171:25 172:11 erode 91:21 erroneous 179:6 escalated 156:6 escalating 131:23 183:24 184:23 188:25 escalation 183:4 189:7 escheatment 172:3 especially 10:9 19:16 36:25 54:1 100:14 106:23 121:2 126:6 167:14 198:3 203:13 207:25 essence 120:13 essentially 36:16 56:20,24 99:13 103:19 111:21 111:23 113:13 114:13 115:8 117:6 119:14 119:15 125:10 125:12 167:16 establish 93:14 estate 41:25	47:7 58:19 126:21,23,24 204:12,15 esteemed 196:20 et 173:17 ETFs 70:15 ethnic 60:12 129:3 EUELL 211:3 211:15 evade 124:10 evaluate 105:12 106:5 109:7 evaluated 106:11 evaluating 105:13 110:13 event 9:8 12:20 22:7 173:20,21 174:6,7,8 191:4 199:6 events 23:16 67:3,12 197:22 eventually 64:21 110:7 178:9,11 everybody 27:1 71:12 82:18 111:22 131:18 191:3 195:12 everyday 20:23 21:15 everyone's 182:22 evidence 28:15 58:5 150:22 153:11,16 evident 86:6 evolution 100:13 126:7 evolve 126:9 evolved 37:10 37:13 39:5 exactly 11:20 12:1 111:2 191:3 exam 21:7 25:22 examination 122:6 examinations
---	--	--	---	--

10:17 13:23	exclusion 150:25	87:20 88:20	extensive 156:10	factor 40:25
102:6 122:24	exclusive 91:12	93:21 132:13	170:9	41:11 73:11
127:19 135:10	exclusively	147:23 183:14	extent 90:10	factors 100:8
examine 7:9	25:20 119:16	184:4	100:6 128:1	174:4
8:14 155:15	excuse 6:5 54:2	experiences 14:6	140:4 181:1	facts 129:12
164:25	62:23	27:11 100:15	191:2,15	157:7 158:16
examining 23:1	execute 181:25	146:15,16	external 160:6	174:7
example 8:20	executing 87:18	experiencing	extraordinary	failure 129:12
36:25 45:2,4,8	execution 88:21	66:18	173:20,21	151:17
46:22 49:20	executives 178:5	expertise 7:13	181:15,18	fair 28:6 57:16
60:6 86:14	exempt 158:11	experts 98:19	182:1 189:16	92:4
95:17 113:24	exempting 119:5	experts-only	191:4	fairly 116:10
129:24 135:19	exemption 95:16	97:12	extreme 193:17	189:25 197:16
136:2 152:6	96:11 98:20	explain 19:24	extremely 9:7	fairness 153:24
190:11 192:4	120:5 150:8	46:15 58:14,20	54:1 71:8 76:6	faith 3:5 102:18
194:7 201:21	166:14	59:13 73:1	167:13	102:21 111:3
examples 33:2	exemptions	99:16 119:8,11	eye 51:20 160:23	111:11 118:3
49:11 135:7	152:8 164:3	133:24 171:21	199:15,19	118:15 121:2,2
148:6 198:14	exhibits 29:10	explanation	eyes 41:7 154:19	162:5
excellent 13:19	exist 95:10,18	124:14		Faith's 120:19
exception 78:20	96:23 195:6	explanations	F	faked 17:11
79:2 95:6,7,13	existent 94:19	84:4	F 1:24 142:16	fall 42:16 65:24
98:7 100:10	existing 15:18	exploded 199:19	159:1,6,8	166:8 201:17
113:18 152:16	78:25 93:1	exploit 61:8	163:11,12	202:19
exceptionally	114:15 125:3	exploitation	fabulous 54:11	fallen 29:23
207:21	exists 88:18	63:8 64:5,14	75:4	falling 201:19
exceptions 78:18	119:14 174:11	64:15 129:10	face 73:12	fallow 203:24
78:22 79:1,5	expand 34:3	138:24	132:17,18	false 33:11,20
150:6	79:3	exploited 130:5	165:25	55:5,7 60:9
excessive 129:10	expanded 74:9	exploiting 60:14	Facebook 42:19	192:5
exchange 1:1,23	expansion 33:12	61:3	70:24 71:11	familiar 27:2
6:3 15:10	39:25 40:18	explore 8:18	176:2 204:18	142:22 143:17
78:21 148:14	expansive 20:17	19:19 32:6	facilitate 93:5	145:21 153:23
153:14 169:2	expect 6:16	75:14 192:14	117:5 124:16	172:17
181:11,19	154:25	196:4	143:11 180:5	family 42:18
182:16 184:7,9	expectations	exploring 73:21	facilitating	59:13,14 63:21
187:9 193:22	75:24 79:9	192:13 199:4	110:8 160:21	famous 45:1
210:11	139:5 164:18	expose 154:3	facilitation	fan 149:19,21
exchange-like	expected 123:16	exposed 154:14	145:1	fantastic 53:9
182:2	expecting	exposes 151:19	facing 197:9	191:12 202:25
exchange-listed	138:23 139:1,6	express 179:12	203:7	far 17:3 28:18
16:10	expense 166:3	expressed	fact 17:16 22:9	30:4,4 40:17
exchanges 87:14	167:10	104:13	24:14 48:5,10	55:20 57:19
175:16 176:1	expenses 94:11	expressing	67:20 75:1	70:12 86:18
177:21 181:22	expensive	11:14 208:9	80:23 81:19	92:9 196:11
194:22,23	116:18 165:2	expression	89:12 91:14	207:24
excited 12:5	167:14	68:17	110:17 141:10	fare 75:19
exclamation	experience	extended 100:7	155:24 174:17	Fargo 147:4
55:16	66:23 83:25		177:23 178:18	farther 49:14

180:7	figure 169:5	30:16 200:17	117:15 121:17	139:6,10 140:1
FATF 141:4	file 81:14 90:13	financials 49:18	122:5,23 125:8	140:12,19,25
father's 84:25	90:15 115:11	88:12	127:18 133:23	141:5 160:3
FBI 47:22	139:2,6,11	financing	134:19 135:12	164:5 167:14
FCP 203:7	154:7,9 208:17	107:16 176:25	140:11,16	167:16 168:22
feature 8:3	209:7 210:5	187:5 195:20	144:1 173:1,8	169:4
February 147:6	filed 36:19 54:6	FinCEN 124:2	173:20 174:1,2	firms' 140:25
federal 28:16	54:7 70:18	138:4 141:4	174:4,17 175:1	first 12:22 18:15
114:24 119:15	124:24 127:21	FinCEN's	177:16 178:25	18:24 19:11,18
147:14 156:11	128:23 136:4	126:11	180:10,24	19:22 20:25
171:9 205:16	136:22 138:12	find 17:3 46:14	181:2,5 182:15	21:19 22:6
fee 51:8,9	files 89:18	59:14 81:20	183:24 184:11	32:6,21 33:13
106:18 108:25	209:10	100:16 110:18	184:14 186:16	36:7 39:1
112:8	filing 80:22 83:7	120:10 142:18	186:16 188:1,4	41:15 45:24
feedback 82:14	86:23 90:1	180:20 181:1	189:21 190:20	47:10 48:21
feeding 186:14	94:18 95:2	181:24 184:18	190:21 192:8	71:13 77:13,23
187:24	123:5 134:5	184:21	194:7 196:6	79:22 81:1
feeds 197:14	136:10 137:23	finder 105:13,19	197:4,23 200:7	84:8 85:14
feel 29:24 86:2	138:21,22	105:24 106:1,5	200:8 205:16	87:3 106:17
96:3 98:10	filings 129:8	106:7 118:12	206:23 207:2	119:22 123:12
149:14 157:13	filters 121:5	finders 10:25	207:23	130:21 131:2
167:24 203:22	final 19:5	52:16 102:16	FINRA's 22:9	134:20 137:10
feeling 29:12	142:12 143:3	103:4,7 105:7	122:7 173:3	140:15,24
feels 98:11	144:7 170:1	105:17 111:13	174:18 179:4	144:8 146:13
180:22	171:5 173:18	112:12 115:4	181:7,17	148:16,19
fees 30:25 59:6	188:1	115:18,19	firm 63:19 86:9	156:19,22
129:11	finally 14:1 59:7	116:10,19,22	93:12 96:6	157:8 160:20
fellow 9:4 13:6	138:7,14 144:3	118:7 119:21	105:10 121:25	161:22 173:9
14:1	191:21 193:20	finding 118:13	122:25 127:7	174:16 183:3
felt 67:5 113:24	financial 8:7 9:5	fine 67:22	127:22 130:20	190:17 202:15
114:14 179:20	21:22 51:11	finish 69:8	131:21 132:3	203:22
female 40:11	63:8 64:2 74:2	finished 52:9	132:12 133:19	first-alert 74:12
fend 117:25	74:11 88:4	FINOP 115:10	135:16,25	fiscal 17:16,18
fiduciary 74:18	100:6 102:2	FINRA 22:5,8	139:16 140:18	17:21 134:8
129:11	103:1 115:10	23:2 24:8	140:19 147:24	fit 164:9
Fiebelkorn 3:6	115:12 121:22	30:18 35:1	149:16 159:23	fits 177:17
122:11,12	122:14,16	39:1 46:24	164:8	five 81:1 123:12
126:4 130:1	124:2 127:7	48:22 50:11	firm's 123:20	five- 203:16
132:7 139:9	130:4 131:17	52:23 61:23	130:4 135:16	fixed 47:5 181:9
field 9:11,12,13	132:18,19,21	62:22 63:1,4	firmer 157:3	187:20,20,22
9:14,15,18,23	133:9,17,19	74:8,13 77:7	firms 63:14	fixes 185:13
23:1 57:16	134:3 136:11	80:11,13,15,21	76:25 81:14	flagged 186:24
98:4,8 119:15	136:18 139:2,3	80:24 82:9	124:21 125:10	flags 21:14
201:24 203:19	140:1,3,4	83:7,11,21	126:18 127:11	45:13 68:6
207:6	175:2 194:23	88:21 89:19	127:22 129:16	79:13 81:22
Fifth 41:23	199:20 200:14	90:7 93:22	129:22 132:2,6	85:25 86:5,12
FIG 79:23,25,25	200:15,15	101:23 114:17	133:9,11,17	86:13 126:21
fighting 27:16	207:12	114:17,19,24	136:24 138:17	140:24 164:6
27:18	financially 29:3	115:9 117:12	138:18,21	191:8

flavors 59:21 61:2	following 84:12	58:12 66:9	147:7 150:1	201:17,18,22
flexible 161:1	footprint 45:4	92:3 111:1	155:17 157:8	202:9,19,22
fliers 34:8	force 7:12 8:9 20:7,11,16,24	131:10	163:15 170:21	203:5 204:24
Florida 26:3 110:1	21:1 23:1	fortunate	fraud 1:6 5:9,12	205:11,19
flow 183:16	80:19 103:4,6	132:16	6:4,24 7:5 8:7	206:16 207:16
focus 14:2,21 16:13 18:16,22	103:8 104:3	fortunately	8:10 9:2,21	210:4 211:8
26:24 38:19	111:16 112:25	47:20 157:24	10:12,19,23	fraud-related
96:18 103:24	117:1 118:10	160:2	11:3 12:25	133:13 139:12
115:11 144:9	168:22 179:18	forum 120:7	13:9 14:14,15	frauds 7:16
144:12 145:9	forces 27:14	forward 9:8,24	14:24 15:8,11	20:18 21:14
146:13 155:10	187:22 193:6	10:3 11:6 12:3	16:14 17:16,20	28:1 32:19
180:1 181:1	194:15	12:15 14:4	18:12,24 20:15	33:1,7,9 34:1
195:5 197:5	foregoing 211:4 211:10	15:23 19:10	20:17,20 21:16	36:16,22 40:4
199:10,25	foreign 42:12	30:6 59:8 74:2	21:20 22:4,14	41:16 48:25
200:1,4 202:9	173:9,12	74:8 75:24	23:5,13,14,19	60:5,13 68:7
202:9,10 206:7	foremost 123:12	76:8 79:19	23:21 25:12	68:18 70:20
focused 13:21	137:10 140:15	86:23 102:20	27:9,14,16,25	71:2 91:19,20
16:7,9 21:13	forget 156:20	141:21 143:2	28:2 29:10	125:23 128:25
27:7,8 28:2	forgetting 26:4	144:15 149:2	31:22 32:4,4,8	177:12 201:20
32:15 46:1	62:23 69:10	149:13 170:7	34:5 35:23	204:19 205:23
56:13 73:24	Forgive 26:8	170:20,23	37:7 39:23	fraudster 42:11
80:1 81:6	forgot 104:12	171:1 195:24	40:4,7 41:14	166:15
101:5 102:25	form 40:2 56:21	196:6 204:21	41:25 46:4,25	fraudster's
121:10 197:8	56:24 78:15	209:11,15	49:15 50:8	166:15
198:3 203:2,5	80:22 81:12,18	foster 91:15	51:21 56:5,9	fraudsters 15:15
focuses 105:5	82:4 83:10,13	found 53:12	56:10,24 61:19	16:17 26:16
106:8	86:17 89:12	188:4	69:4,9 73:10	33:18 41:12
focusing 143:4	90:13,15,24	foundation	77:6,8 85:24	56:16 57:3
156:20	138:23 139:6	200:7,13 201:7	94:21 102:9	59:22 60:18
folks 31:7 42:24	139:19 206:11	201:10	115:23 119:25	75:7 76:24
42:25 43:2	206:12	founders 104:3	120:17,17	165:6,11 176:4
66:18 72:20	formally 86:11	four 23:18 41:22	121:12,18	202:17 205:6
109:11 128:18	formation 91:6	52:3 148:11	125:1,7,18	fraudulent 5:5
142:18 163:17	91:11,14,16	159:18 160:9	126:13,20	8:12,16,21
189:5 192:16	101:13 103:21	163:16	127:10,24	16:15,25 18:10
196:10 208:18	104:1 112:25	fourth 41:21	128:3 129:10	18:16 22:18,18
209:12	117:5 120:6	123:19 124:12	129:16,20	41:23 56:21
follow 61:5 65:4	195:25	fragile 200:17	131:9,18,20	60:9 78:6 81:3
140:19 144:18	formed 7:12	frame 55:21	132:11 133:15	129:6 183:23
156:4 159:9	132:4	framework 8:15	133:16 136:8	fraught 120:17
165:7 171:4	former 17:10	106:4,10 109:6	139:13 140:1	free 162:10
173:13 184:1	144:1 150:25	120:15	144:13 145:13	185:11,11
203:18	204:20	Frank 106:16	146:7 175:10	198:17 199:9
follow-up 155:5	forms 14:25	frankly 29:11	175:13,13,14	free-trading
Followed 41:25	32:8,20 56:12	56:10 57:16	179:18,21	151:9
122:2	86:24	66:5 71:24,25	182:7 184:18	freely 86:17
	forth 56:22	72:21 75:7	194:19 197:3,9	146:5
		115:6 116:21	198:3 199:6	freeze 177:7,9
		Franz 4:6 147:7	200:12 201:14	185:14 187:12

frequently 34:21 151:10 153:21	77:10,20 138:13 145:15	generally 46:16 52:2 58:8	45:2 46:22 48:11 49:11,20	149:12 152:6 156:16 158:12
friends 48:22 50:18 59:14	146:20 149:15 156:16 157:15	68:25 98:20 105:12 111:7	59:25 63:7,17 64:22 67:9,11	159:19 160:8 162:21 163:4
frighten 75:6	172:20 174:21 208:18 209:11	144:21 156:9 173:6 180:15	88:19 103:5 118:6,16 123:4	166:1,3 170:20 192:9 195:1
front 26:6 33:9 67:4 138:7	211:9 furthest 103:15	202:4 generations	123:25 131:21 138:15 140:9	199:23 200:1 207:6,9
164:18	fusion 22:22	72:23 73:7	156:12 162:20	goal 12:10 92:13
front-line 189:5	future 64:20 72:4 170:23	George 176:22 177:8 195:5	167:15,16,17 169:6 178:17	130:19 135:6
fruitful 172:15		Georgia 30:10 30:14 31:5,8	191:19 198:14 198:19	goals 103:17,19
frustrating 169:10	G	42:22 49:5 58:16	given 84:18 94:20 99:7	goes 132:2 138:1
fulfill 92:24 169:7	G 6:1 159:1,6,8	Gerold 2:23 3:7 4:7 24:20,21	109:23 135:10 144:11 158:15	152:9 154:17 171:18 195:21
fulfilling 79:17 163:5	gain 55:16 126:12 146:20	26:8 36:3 52:13 54:20	166:2 gives 84:6 93:20	201:11 going 7:18 12:7
full 87:13 120:19 138:16	gaining 126:22	62:11,25 63:23 70:18 74:16	127:6 140:19 167:23	28:13 29:13 34:6,15 39:9
195:15	gambling 44:12 203:14	104:8,8,20 118:23 119:10	giving 8:7 62:15 77:23 121:3	43:18 44:17 47:7,13,14
full- 146:11	game 136:18	119:13 198:4,5 204:8	159:24 198:17 199:17	51:7 53:11,15 54:13 55:24
fully 47:11 53:3 78:22 82:1	games 207:14	Gerri 4:13 192:19 198:1	glad 104:4 111:4 111:14 177:19	57:12 59:11 62:15 65:20
162:22 166:13 168:24 184:10	gamut 197:25	200:6 202:25 205:14	180:23 global 16:16	69:15 70:4,20 73:5,6,8,17
fun 176:22	garage 112:3	getting 37:3,20 37:21 43:7	25:9 33:15,17 121:22	74:1,19 75:24 77:12 79:22
function 120:7 163:6 178:8	Garvey 172:11	47:8 53:22 54:9 63:17	globally 23:12 178:20	80:9 84:7 85:8 88:24 91:9,21
functions 98:12 122:15	gatekeeper 139:4 146:7	69:23 71:1 72:16 75:18	globe 33:21 glom 204:3	91:24,25 92:5 92:14,25 93:1
fund 17:13 69:24 109:14	gatekeepers 9:2 74:10 101:14	107:23 108:7 108:24 109:16	GM 190:12 go 7:23 19:18	93:10 94:7 97:5,7,9 98:3
fun 17:13 69:24 109:14	180:4	118:13 125:6 132:25 151:2	25:22 27:20 37:16,23 38:2	99:6 100:1,20 103:23 107:5
fun 17:13 69:24 109:14	gatekeeps 22:19	153:11 154:10 158:20 159:20	46:14 52:23,24 54:22,23 55:6	110:24 111:21 112:11 115:8
fun 17:13 69:24 109:14	gather 22:25	184:24,25 185:20 186:8	55:17 56:1,15 56:16,17 57:12	115:16,22 116:12 121:7
fun 17:13 69:24 109:14	gathered 81:22	198:21 199:12 199:12	62:13 82:15 84:4 85:12	124:19 134:17 136:14,17
fun 17:13 69:24 109:14	gathering 81:16 206:12	gifting 167:7 girls 188:11	87:1 91:10,19 92:9 96:5,15	137:22 138:11 140:8 141:25
fun 17:13 69:24 109:14	gear 152:17	give 14:12 15:17 33:2 36:25	104:6 108:10 116:5 127:20	142:12,17 144:13 145:9
fun 17:13 69:24 109:14	geared 88:13			156:15 157:6 162:6,13
fun 17:13 69:24 109:14	general 23:3 28:1,8 30:4			164:19 166:11
fun 17:13 69:24 109:14	82:16,20 102:23 104:14			
fun 17:13 69:24 109:14	107:13 116:19 119:23 143:25			
fun 17:13 69:24 109:14	147:2 173:9 181:17 184:2			
fun 17:13 69:24 109:14	General's 25:2			
fun 17:13 69:24 109:14	generalize 55:6			
fun 17:13 69:24 109:14	generalized 162:12			

167:12 168:19 169:3,9 171:22 176:10,21 182:10 186:15 186:16 187:19 194:19 196:17 198:11,22 200:12 203:19 203:24 205:6 209:15 gold 2:11 71:24 71:25 72:3,6,8 72:8 77:24 84:9 90:21 Goliath 57:17 Gonzalez 2:13 77:17 121:9 122:10,19 123:3 124:19 127:14 128:18 131:25 133:21 137:3 138:2 140:8 141:17 good 6:2,20 12:18 23:24 34:2 35:20 42:3 49:23 59:12 65:23 66:13 74:14 84:6 91:25 96:20 102:20 108:20 112:6 138:6 139:20 140:11 154:7 162:5,16 170:12,14 171:1 186:14 188:3,6 190:11 190:12 194:7 198:20,22 202:11,12,16 206:15 Google 61:13,13 67:7 govern 101:25 governing 8:22 government 15:15 119:15 government's	121:11 governor 74:19 graduates 176:1 grand 115:16,17 grandchild 42:12 grandmother 63:16 71:13 grandparents 41:17 42:8,10 42:16 granular 189:23 grateful 31:21 141:23 gratitude 11:14 208:10 grayer 110:21 great 9:17 15:25 20:4 31:2,5 32:5 35:7,9 37:5 40:12 42:21 43:24 53:15 66:24 67:3 72:20 74:15 75:11,25 76:1 87:5 96:24 123:3 124:19 131:25 133:21 137:20 138:2 141:4 142:19 163:17 174:22 175:12 176:12,17 177:15 188:24 189:2 192:13 196:23 200:5 207:4 209:15 greater 28:18 29:2,3 75:8 84:16 113:14 160:10 greatest 25:25 168:8 greatly 13:3 40:17 51:21 Greed 199:7 Green 3:8 121:21 124:22 130:22 138:19	ground 120:22 group 9:25 20:11 22:15,17 22:22 34:16,16 34:17,19 46:12 51:16 111:17 128:19 129:3 132:5 179:19 groups 15:5 17:2 21:6 46:4 64:12 85:6 132:12 134:13 grow 28:23 49:1 growing 69:6 growth 12:13 guarantee 116:15 guaranteed 45:15 54:24 guarantees 68:9 guard 29:16 guess 14:24 23:23 25:12 46:9 53:7 65:4 85:8 94:24 120:3 164:12 182:14 204:16 guidance 27:9 55:4 79:9 138:14,17 139:7,24 140:10,11,13 192:6 guide 152:1,9 155:18 156:3 guidelines 166:9 gunpoint 29:23 guy 47:17 48:11 53:15,17 177:15 guys 46:19 61:7 62:19 65:1 73:22 152:20 161:20 170:13 172:4 188:11 198:1	habit 62:8 hacks 34:17 half 28:18 200:20 203:7 halt 172:22 173:8,10,14,17 173:20 174:1,3 174:5,16,19 177:17 178:7 179:5 182:1,9 182:19 186:16 188:1 189:16 192:21 193:15 193:17 194:7 195:17 halted 7:20 173:16 190:4 194:23 halts 19:7 143:4 143:24 173:5 173:12 174:15 175:8 180:10 180:24 181:16 181:18 184:16 186:20 halves 130:2 hand 15:15,16 107:5 111:8 113:22 136:25 172:13 handle 175:15 206:15 handling 74:11 hands 125:17 132:25 happen 15:6 25:12 29:13 34:21 44:4 46:7 75:4 88:22 102:10 191:18 happened 111:18 113:7 117:1 203:21 happening 62:10 63:11 75:23,23 128:13 141:6,7 186:5,21	187:19 happens 99:19 119:17 125:10 136:16 137:8 137:17 191:17 194:12,14 204:24 happily 24:17 happy 7:24 76:19 85:12 122:11 144:2 153:25 174:22 harbor 64:13 151:6 159:3 160:15 161:7 163:14,24 164:10,13,24 165:5,8,11,13 167:1,20,22 hard 7:2 10:13 10:18 15:10 16:22 19:16 24:6 48:15 54:1 57:6 62:19 69:19 164:5,6 184:13 196:17 201:11 202:23 207:21 harder 65:1,2 75:9 137:13 176:4 hardest 50:15 harm 7:15 13:4 20:22 21:5 145:2 191:18 206:16 harmed 14:17 30:16 Harmon 4:8 147:9,9 150:16 153:8 157:21 161:22 166:7 171:2 harms 31:13 73:13 harness 206:8 harsher 195:2 hate 163:7 havoc 56:23
<hr/> H <hr/>				
H.R 103:12				

Hawaii 203:21	92:5 101:1	highlighting 120:23	97:8,23	132:21 135:14
head 35:22 74:7 118:5 121:22 192:15 193:4 199:18 200:8	107:13 128:13 142:9 148:6,8 165:14 170:19 171:6 189:21 201:19	highly 34:24	hotline 134:5	135:17 137:24 205:18
headaches 157:9	helped 136:7	hijack 63:2	hour 113:10 143:3	identifying 121:12
heading 81:8	helpful 11:1,2 19:24 86:14 100:12 113:2 117:23 121:17 128:9 138:6,9 139:25 152:12 152:23 157:2 157:22 158:23 159:7 162:17 163:13 172:18 181:3 192:7	hire 188:17	hours 34:3	identity 41:23 56:5,9,10,11 56:19,23 122:13 125:2 138:25
heads 172:11 191:19	helping 27:8 142:4 143:11	hired 80:23	house 47:10,10 103:12 127:1 187:20	Ignacio 3:11 104:21,22 105:16 111:4 121:2
health 200:15	helpline 40:3	hiring 188:18	Huber 3:9 80:10 80:12 85:12 91:8 95:14 99:5 103:18	ignorant 160:24
hear 11:16 27:21,21 28:1 29:10 40:3 42:4 58:15,16 72:21 77:4,6 131:23 146:14 146:17 158:1 170:13 189:2 191:1 202:11	helps 66:10 77:7 93:19 133:11 133:11 164:4	historically 7:2 16:16 174:19	huge 180:3 190:8 201:22	illegal 115:19 124:8,10 142:10 145:1 145:21 146:3 160:22 161:7
heard 44:5 76:22 101:9 139:14 152:19 170:5 183:5 195:11 204:25	help 8:6,16,24 9:3,5 10:22 15:19 16:14 18:9 27:23 31:17,18 35:10 35:22 45:2 46:15 50:22,24 52:5 67:13 73:13 74:2 75:15,17,21 77:12 90:20	hit 46:16 64:20 118:5 193:3	hugely 191:13 191:20	illegality 160:23 160:24 illegitimate 49:9
hearing 14:5 19:10,14 39:13 42:24 79:20 120:14 153:24 203:25 210:15	Hester 2:7	hoc 127:18	human 22:25 133:3 183:11	illiquid 175:21 178:12 190:6
heart 14:15 91:17	hey 48:17 49:22 54:8 96:6 108:20 118:13	hockey 106:20 107:6	humble 46:18	IM 70:14
height 80:17	Hi 20:6 80:12 179:9	Hodgson 147:10	hundreds 55:9	immediately 32:21 143:12 187:10 191:17
held 16:9 29:23 86:19,20,20 139:18 155:7 162:1 167:5 210:12 211:5	hide 185:17	hold 13:25 holding 16:7,11 18:11 39:8 97:7 150:9 153:9 155:9,13	hyperbolic 113:21	immunity 188:4
hello 27:1 30:12	high 21:5 30:25 45:14 51:8,8 68:8 133:5 135:14,14	holds 209:1	I	impacted 26:9 27:12 184:24 184:25
help 8:6,16,24 9:3,5 10:22 15:19 16:14 18:9 27:23 31:17,18 35:10 35:22 45:2 46:15 50:22,24 52:5 67:13 73:13 74:2 75:15,17,21 77:12 90:20	high-level 175:9	home 20:14 41:24 47:11 196:13	Iannarone 2:24 30:9,12 43:1 44:4 58:4 66:19 72:18 75:11	impacts 23:11 34:11
	high-pressure 17:25	homebuying 15:13	IAs 25:20 64:3	impasse 163:20
	high-quality 169:13 195:9	home 20:14 41:24 47:11 196:13	icky 186:5	implement 133:5 202:14
	high-risk 133:2	hook 60:19	ICO 32:21 197:20	implemented 126:19
	higher 24:2 50:9 180:15	hope 43:10,18 103:5 111:22 146:19 171:23	ICOs 33:8 38:15	implementing 123:15,17
	highest 47:21	hopefully 37:6 64:19,20 65:1 84:6 105:18 170:7,7 208:5	idea 72:25 118:25 153:24 170:13	implicated 145:12
	highlight 18:12	horrified 116:8	ideas 170:8 182:12	implications 163:8 207:2
	highlighted 169:21	horror 115:4	identification 183:3	import 88:9
		hospitable 114:6	identified 96:19 204:18	
		host 56:22	identify 7:3 9:1 13:24 21:2 22:18,19 24:6 24:10 34:22 50:10 64:23 71:2 130:8	
		hosting 13:22 22:7		
		hot 16:18 26:15		

importance 12:21 136:9 156:2	95:25 96:4	157:21	105:22 126:10	185:8
important 10:23 12:10 13:13 14:22 15:20 19:11 31:4 35:5 41:4 49:1 57:7 59:9 74:1 74:25 78:22 82:5 101:8,12 102:1 103:17 103:24 105:17 107:8 110:10 122:22 127:22 131:10,16 133:8 137:12 137:16 139:3 156:23 171:17 172:25 173:1 175:24 191:14 191:14 195:13 200:11,21 208:6	inactive 96:13 inappropriately 144:25 149:23 149:24 204:4 inbound 40:14 incarcerated 47:24 incentives 89:5 incidentally 106:14 include 7:15 108:17 112:16 129:9 138:5 150:10 included 17:9 125:20 179:17 includes 20:17 79:8 89:20 122:17 125:1 164:1 including 7:5 13:10,13 21:7 58:1 84:15 85:2 118:10 122:25 145:3 170:11 197:5 200:14	incumbent 165:17 incurred 94:11 153:12 indemnify 168:5 indemnifying 168:6 independent 18:3 115:14 123:20 153:16 159:17 163:4 indicate 97:13 190:8 indicated 152:4 211:5 indication 131:5 indicative 110:14 133:15 indicia 45:14 49:8,9 50:17 108:6,12,14 110:13 114:14 131:18,20 183:23 individual 31:11 31:15 47:4 49:21,23 54:1 54:21 63:15 67:11,12 75:22 129:21 136:5 170:17	inform 201:24 206:10 information 8:7 42:18 56:18,19 61:8,14 63:18 64:22 67:9 71:3 78:9,14 78:16 79:3,4 81:16,21,23 83:22 85:23 86:3,10 87:23 87:24 88:4,11 89:4,10,10,10 89:14,17,25 90:2,11 93:21 95:9 96:20 97:15 98:17 100:7 119:4 132:4,24 133:14,18 136:7 137:4,5 139:25 150:21 151:3,14,15,16 154:5,11 156:19,21,22 157:4,6,10,12 158:13,22 165:16 169:7 169:15 176:9 181:25 183:22 186:15 187:10 187:11 189:13 189:15,21,23 190:20,23 192:17 193:13 195:10 198:21 201:22 208:18	infrequently 78:8 ingenuity 10:12 inherent 78:6 85:16 initial 57:24 129:6 initially 44:18 156:18 initiating 78:14 initiative 52:20 initiatives 117:8 198:10 injury 73:10 innovation 111:20 innovatively 185:23 innovators 207:14 input 79:20 inquiry 86:8 inside 23:8,10 insiders 37:16 187:6 insight 66:16 103:6 146:21 insights 27:25 28:9 58:2 206:8,25 Inspections 10:17 13:23 Instagram 73:8 installations 207:9 instance 7:11 53:19,20 64:7 130:25 131:5 instances 17:16 102:10 146:6 154:8 instituted 165:2 institution 131:17 136:11 137:21 institutional 11:24 117:17 institutions 15:6
impose 173:4 imposes 163:6 imposing 174:5 impossible 158:25 162:11 Imposter 41:16 impression 18:3 improperly 144:25 improve 14:7 90:20 193:11 193:24 improved 79:21 improvement 85:3 99:1 improving 85:1 in- 197:21 in-depth 182:21 in-house 147:12 in-law 63:17 in-person 40:15 inactivate 95:24	income 181:9 incomes 47:5 incoming 27:24 72:15 106:25 incorporated 141:1 190:24 incorrect 163:9 increase 17:18 94:13 128:6 increased 85:4 85:10 91:1 126:18 increasing 21:13 101:13 128:10 139:13 increasingly 162:2 incredible 13:6 186:10 incredibly 48:15 49:19,19 72:22	individually 134:12 individuals 8:2 15:4 16:23 17:7,22 18:1 23:15,19 26:18 28:13 32:24 35:3 43:8,13 43:16 53:13,21 56:1 61:10,22 70:22 74:11 123:1 137:25 156:10 183:13 200:2 204:19 industry 9:1,5 15:15 19:9,20 34:24,25 64:12	informed 93:1	

15:6 134:3 139:2,3 140:3 140:4 208:23 instructed 127:4 instructing 158:14 instruction 167:17 instructions 127:7 209:9 insurance 116:17 122:17 126:23 176:18 insurers 116:16 insuring 74:23 intake 22:17 integrate 46:10 integrity 8:10 22:11 193:5 intelligence 22:5 22:15,25 24:10 24:14,16 128:20 133:19 137:15 180:2 intended 8:6 144:23 intent 65:3 interact 101:22 145:12 178:24 interacting 97:25 interaction 23:2 83:20 114:2 189:1 interdealer 82:22 interest 23:25 24:3 27:3 51:20 53:22 54:3 61:21 72:8 74:1,24 83:22 89:24 97:3,17 118:14 173:8,19 180:13 209:14 interested 10:24 72:22 87:11 89:22 92:1 100:5 107:7	130:18 152:14 170:17 184:15 interesting 38:14 39:13 42:2 61:6 62:18,21 72:7 72:13 75:14 165:9 197:19 199:6 207:15 208:15,20 interestingly 72:2 interfering 180:16 192:22 interim 113:8 intermediaries 104:25 201:7 intermediary 112:19 internal 123:13 131:14 156:6 160:6 internally 152:14 international 38:11 131:3 205:15,25 206:4 internationally 141:22 internet 15:7 18:20 21:19,22 23:15 33:9,17 33:19 37:13 38:7 39:15 45:9 49:12 54:25 55:23 61:7 68:15,18 85:17 Internet-based 33:8 interrogate 68:4 intervene 63:10 intervention 195:14 interview-you... 65:18 intraday 181:14 193:25	intriguing 80:3 introduce 6:11 19:23 22:4 77:10,24 102:18 121:19 143:10 146:24 174:22 179:16 198:1 introducing 104:6 introduction 77:22 109:2 introductions 106:2,3 introductory 16:1 intrusion 124:25 131:10 138:24 invaluable 136:22,23 invention 186:11 invest 16:23 23:23 37:12 45:16 47:12 52:21 53:2,5 68:10 109:21 199:23 200:3 invested 44:16 70:1,2 109:1 202:20 investigated 53:20 investigations 36:20 64:16 81:3 130:12 investing 9:16 18:4 40:24 44:7 50:18 70:6 72:24 78:5 92:2 101:15 107:8 199:22 200:18 200:20,24 201:3 202:4 204:1 investment 8:25 13:14 15:3 21:14,16 25:19	28:2 34:9 39:20 40:4 41:14,24 43:9 44:20 46:21 47:7,19 48:25 49:10 50:4,5 51:1,3,12 58:14,19 59:15 68:6 69:10,16 73:1,3 75:19 80:1 93:3 94:17 103:1 108:21 122:2 129:8,10 131:6 136:8 168:19 188:13 198:15 199:18 206:16 207:16 investments 8:4 9:13,13,23 24:2,4 31:3 41:8 43:15 58:7 68:4,8,21 68:22,23 69:1 74:5 75:17 97:21 101:17 117:16 129:13 investor 1:6 5:9 5:12 6:4,23 10:16 12:25 13:9,18 16:14 18:9,12 19:7 20:23,25 21:5 21:10,12,12,13 21:15,20 22:10 23:14 25:1 31:17,20 38:6 43:21 45:11 46:2 51:2 52:15 53:2,9 54:13 58:8 65:3,21 69:21 74:23 89:11 91:6,13,15,17 91:21 92:11,15 94:6,20 97:21 103:21,25 116:18 117:20 117:21,22	119:9,12 120:6 125:10 126:25 127:6 129:7 131:1 140:2 143:5 144:4,6 175:10 179:1 183:20 190:9 193:5 196:14 196:19,22 197:7 198:2,7 198:10,15,24 199:14 200:7,8 201:15 205:14 206:5,10 208:5 209:2 210:4 211:8 investor's 44:10 investor.gov 197:11 207:24 investors 5:6 6:25 7:4,10,15 8:3,6 9:5,12,14 9:24 11:22 12:3,11,23 13:4 14:3,17 14:20 17:9,20 18:2,10,17,19 19:19 21:3,18 21:24 22:9 23:11 25:13 26:9,13,18,25 28:10 30:15,17 30:23 31:22 33:10 35:8 48:15 49:21,22 50:1,22,24 53:8 54:12 56:8 62:19 65:15 66:22 67:7 68:13 69:14 70:1 73:23 75:2,16 89:13,21 90:24 91:10,25 92:5 97:1,2,17 98:5 98:9 99:17 100:16 101:13 101:15,22 102:1,7 104:11
--	---	---	--	--

105:18 106:19 107:11,14 108:17,18 116:4 117:11 117:16,17,24 120:4,5,7 125:18 127:24 128:25 129:21 135:6 139:17 142:5,9 145:2 145:3 164:14 173:1,7 180:14 187:2 188:3,6 189:17 191:18 192:6,19 196:24 199:12 199:12 202:13 203:20,23 207:15 investors' 126:13 invests 69:24 invitation 80:8 122:21 invite 153:5 207:10 invited 103:9 inviting 22:7 137:25 171:16 198:16 invoking 179:5 involve 114:2 124:8 160:20 involved 17:22 39:2 40:12 44:6 63:21 69:25 79:11 90:9 107:16,17 126:24 128:4 134:22 137:25 149:17 195:19 209:5 involvement 189:13 206:1 involves 124:5 124:16 151:10 involving 13:4 16:18,19 20:21 33:4 36:16	39:2 60:7,9,9 109:13 128:24 128:25 129:6 129:20 146:1 IOSCO 206:3 IP 133:16 IRAs 139:19 IRS 41:17 56:21 Island 47:6 Island-based 17:23 issuance 56:14 151:8 153:20 154:16 162:10 issuances 147:13 issue 26:15 37:15 38:24 39:3 43:19 56:21 81:23 85:19 95:12 103:4 105:21 109:23 117:19 125:11,13 155:1 164:25 168:15 170:5,6 171:20 182:19 187:4 204:10 issued 85:25 106:9 117:1 125:16 138:4 140:11,22,23 issuer 55:1,18 79:3 82:7,8 90:12 93:2,15 93:17,18 94:4 94:9,17 107:16 108:20 112:18 116:1 125:11 125:11 148:15 150:6,10 155:9 157:11 158:14 158:19 192:10 issuer's 159:21 160:5 162:19 issuers 79:5 85:11 95:8 97:11 99:3 111:18,24 112:1 115:23	116:3 117:10 144:20 164:16 168:24 174:18 177:6 181:20 184:8 185:19 185:20,20 187:7,23 188:22 189:17 189:24 193:13 issuers' 189:17 issues 10:21 11:19 13:20 17:18 19:11 39:14 51:25 66:9 84:4 85:15 95:9 105:4,6,11,13 106:12 139:17 141:20 143:22 143:23 144:10 145:9,12 146:22 148:9 150:24 155:6 155:16 156:6 156:16 159:10 174:17 178:25 179:24 188:25 196:4,14 203:2 203:8 issuing 107:21 164:8 item 166:8 items 151:25 166:9 204:9 iteration 126:20 iterative 84:1 <hr/> J Jackson 2:5 6:15 11:11,12 12:16 jaded 120:3 James 3:6 January 81:6 Jay 2:3 177:4,11 177:14 Jean 2:25 26:21 27:1 30:8 39:10,12 43:5	56:3 60:3 62:17 65:4 70:20 71:10 74:21 Jean's 45:7 73:21 75:11 JEMIMA 211:3 211:15 Jersey 24:20,24 24:25 25:1,15 25:21 38:5 52:20 70:18 74:18 104:9,11 118:24 198:5 198:12 204:7 204:14 205:3 Jim 122:10,12 124:20 129:18 129:25 138:11 140:8 141:19 142:3 job 87:5 96:20 154:2,15 158:6 158:7 180:7 JOBS 168:15 John 168:9 join 6:17 11:13 27:13 31:24 32:2 103:3 joining 6:13 joint 8:9 judge 110:12 judges 153:23 judgment 8:5 jump 48:18 84:11 98:1 144:8 153:6 jumped 76:3 jumping 92:1,7 jurisdiction 173:12 jurisdictions 63:25 64:19,21 Justice 8:10 150:2 206:18 justify 112:8 juvenile 195:12 <hr/> K	Kara 2:4 Kardashians 187:17 keenly 100:5 keep 41:7 144:13 148:16 199:6 keeping 74:23 140:7 keeps 72:17 204:10 key 19:25 28:12 32:13 50:24 51:17 86:13 130:14 139:3 146:2 197:5 207:11,14 kick 77:21 84:8 142:17 kidnapped 42:14 kind 24:1 32:9 34:4 38:21 40:16 41:6,13 42:22 49:25 52:11,14 56:3 65:13,22 66:16 72:12,12 74:25 83:25 84:4 87:13 90:14,17 92:17,20,22 93:7,11,15 96:18,21 97:12 97:23 105:20 111:19 114:11 114:11 128:3 134:25,25 135:15 136:24 137:14 139:23 152:4,6,16,19 157:9 159:19 163:20 164:13 164:17 182:16 182:20 189:1,5 189:6 190:5 192:13,15,19 192:22,24 193:1,2 194:1 194:24 199:6
--	---	---	--	---

207:10	106:1,6 107:2	187:16,18,23	land 50:8,13	159:23 165:7
kinds 97:11	107:8,19 108:1	188:4,10,14,16	landscape	167:14,15
113:13 115:3	108:3,6,21	188:18,20,20	112:22	171:11 177:15
128:2 206:21	109:2,9,10,17	189:3,14,19,20	language 71:23	186:12 195:8
knees 98:23	109:20,21,22	189:25 190:3	large 45:18,18	195:10,11,12
knew 113:2	110:2,21	190:17,21,21	99:20,21,21	207:7
knock 198:22	113:10 115:1	191:2,3,5,8,10	113:4 122:16	laws 15:18
199:15	115:16 116:4	191:24 192:9	130:16 134:13	114:24 153:23
know 7:22 12:10	117:20 118:4	192:10,18,22	171:12 183:9	156:11 171:9
12:24 15:5,20	119:3,5,23	192:25 193:2	large- 23:6	171:10 195:15
16:6,13 25:4	120:8 121:13	193:12,14,18	large-cap 50:3	lawsuits 171:7
26:10 28:17	125:22 126:2	193:20,24	largely 96:16	lawyer 102:21
31:13 32:6	127:10 128:6,9	194:7,9,19,21	179:22 183:10	149:17 166:15
34:8,9,24 35:1	128:14 131:21	194:22 195:3,5	larger 9:13	lawyers 9:2
35:6,12,13,15	131:22 132:24	195:7,8,15,18	160:3 208:24	111:17,20,23
35:17 37:11	133:5 134:25	196:10,16	largest 74:16	112:13 113:1
39:13 41:12	135:3,14,21	197:1 198:20	151:24 175:25	149:19,20
42:4,6 43:7	136:20,20,24	198:21,24	178:18	168:12 171:13
44:25 46:11,12	137:22 141:15	200:2,2 201:2	lastly 124:15	lay 159:1
48:2,22,23	142:24 144:10	202:15 203:1,5	182:9	layering 162:5
49:10,15,18	150:15 151:22	203:6,7,19,20	latch 26:17 39:6	laying 139:5
50:3,6,11,12	152:2 153:10	203:24 205:13	late 96:21	lead 44:12
50:13,22,25	153:17 155:2	205:14,20,25	lately 55:24	122:15 156:16
51:2,9,12,16	156:4 157:2,11	206:6,13 207:6	latest 16:18	170:9
51:19 53:1,6	157:25 158:9	207:20,23	126:7	leading 172:14
53:13 54:10	158:10,11,25	208:8,10	Laughter 6:6	leads 131:25
55:15,16 58:1	159:15,17	knowing 138:16	87:2	138:6 155:1
58:14,22 59:20	160:2,3,4,16	178:9	launch 172:22	lean 185:8
61:6,23 62:22	162:5,15	knowingly	launched 8:1	leaps 84:25
63:3,15,21	164:16 165:4,5	97:24	20:12	learn 44:6 120:9
64:6,9 65:2,7,8	165:7,19 167:7	knowledge	launching 13:19	141:5,23 178:7
65:20 66:16,17	167:8,9,10,13	60:24 120:9	laundering	205:24 206:21
67:19,22 68:1	167:21 168:1,2	132:19 200:15	102:5 122:7,13	learning 137:14
69:15,20,20,23	168:3,5,13,14	known 40:9 60:5	123:5,9 130:23	leaving 130:20
71:1,12,13	168:15,16,19	60:16,18 82:23	131:7 135:5	led 92:22 112:25
72:8 73:19	168:24 169:8	116:23 147:4	140:17	153:20
74:10 76:2	169:10 170:16	knows 124:6	Laura 2:11	Ledyard 102:22
82:6 85:16	171:23 172:4	172:7 205:25	77:24 84:7	left 18:2 86:25
86:21 87:19	172:16,17	Koenig 19:16	100:24	97:7 143:12
90:5,23,25	175:18 176:2,8	Kool-Aid 53:24	lavish 17:13	169:24 171:5
91:4,24 92:2	176:14,16,24	Kramer 110:2	law 24:5,8 30:11	legal 31:16 55:3
92:12,21 93:6	177:5,11,14,16	110:10,12,17	30:15 121:17	58:18 101:24
94:8 96:6,12	177:18,20,25		121:24 125:22	147:19 158:9
96:16,22 97:1	178:3 179:21	L	125:25 126:2	159:12,15,16
97:8,13 98:3	180:2,12	lack 112:21,22	136:11,23	161:12 164:23
98:18,23 100:1	182:10,10,20	181:19	147:14 148:13	167:16,19,25
100:10 101:16	183:8 184:15	lady 143:24	149:16 151:17	legend 144:25
101:17 105:10	185:6,9,22,25	laid 140:24	151:18 154:21	146:9,15
105:20,23,24	186:6,9,13,22	203:17	154:22 157:1	147:13 148:3

151:7,18 161:9	78:9 103:20	185:16 207:11	136:19 140:10	21:15 28:15,24
161:13 162:9	109:8 118:20	limits 191:23	149:7 155:10	29:22 44:22,24
164:19 166:7	152:13 164:4,7	line 27:23 40:7	158:16 164:22	45:3 47:19
166:10 167:18	169:14,14	69:8 83:15,16	167:23 169:10	49:6,17 50:3,5
legends 144:17	191:9 192:11	93:17 99:11	182:11 185:10	59:10 60:2
144:23 145:10	198:9 199:20	104:6 183:25	188:5 197:12	62:21 68:5
146:4 147:25	204:7	207:15	199:11 207:22	74:13 76:8
148:17 152:9	levels 30:25	lines 33:11,21	live 114:18	90:17 103:20
160:19,22	leverage 162:21	37:19 43:5	176:14 187:16	108:2,12,23
legislation	206:22	156:8 158:24	lived 47:5	130:24 131:2
118:10 119:6	leveraging	link 82:23 116:1	lives 57:12	134:11,15
205:4	130:10	117:10	176:24	135:5,9,13,18
legislative 117:4	Lewis 104:24	liquid 128:7	Lizzie 2:9 6:12	135:23 136:9
legitimacy 49:8	liability 94:22	187:21	19:2 76:17,19	137:16 140:16
50:17	151:19 154:3	Liquidation	82:18 101:4	140:21,25
legitimate 11:3	154:14 159:6	190:12	120:25 121:9	141:3,21 148:5
47:19 49:10	161:7 171:12	liquidity 175:17	142:1,25	148:7,23
67:22 97:16	liable 161:25	185:16	loan 125:11	149:10,11,15
204:1	162:1	list 52:10 56:5	128:3	149:16 151:22
lender 128:5	liar 195:12	57:7 58:24	lobby 103:14	151:23 152:10
lends 136:13	libraries 197:24	137:18 149:3	local 23:13 38:9	152:25 153:18
length 182:3	library 198:12	150:2,3 164:6	199:8,17	153:19 156:13
196:5	201:9	168:2 201:10	204:14	158:25 159:22
lessons 206:21	licensed 61:24	listed 52:3	locally 25:10	159:24 160:6
let's 19:18 57:9	159:25 197:4	173:11,16,16	31:4	166:6 170:16
77:20 121:20	lies 15:3 17:25	listen 75:25	Location 210:7	170:23,25
129:25 144:8	life 13:5 41:5	199:1	locations 123:2	177:25 180:18
146:25 148:23	45:23 56:23	listening 209:13	Locks 54:24	188:19 190:4
177:8,9,10	lifestyles 17:13	listing 82:9	lockstep 134:23	191:25 192:9
letter 81:23	lifted 168:23	94:12,18	long 9:22 11:18	192:15 196:6
103:10 106:9	light 118:6	181:21	17:23 55:4,5,7	203:6 209:11
106:13,22,25	119:1 120:19	lists 54:23	55:7 69:8	looked 9:22
107:4,9,11,20	146:16 161:18	165:19 197:15	113:7 138:1	177:25
107:21 108:23	177:23	197:15	141:19,20	looking 9:8 15:8
111:5 117:2	lights 176:13	Lite 114:7	143:5 159:5	19:10 24:16
148:20 149:15	likable 48:8	literacy 199:20	163:5 176:11	32:7 40:22
149:16 150:11	59:20	litigation 153:20	178:10	44:15 49:7
150:12 155:22	limit 9:21 79:2	little 14:19 17:1	long-running	50:18 51:18
159:4 164:2	180:24	42:23 43:1	52:20	58:18 66:7
165:7,15 166:2	limitations	52:5 54:18	long-winded	67:2 75:20
166:3 168:4	78:23 150:9	56:6 57:17,18	110:20	79:19 85:23
letters 106:23	155:8	57:24 62:19	longer 7:22	86:22 89:18
107:1 148:18	limited 15:4	65:1 75:20	95:10 174:3	91:17 102:20
149:4 151:23	48:24 89:9	76:3,19 82:21	195:21	106:18,20
155:3 159:4	99:7 109:1	85:21 95:4	LongFin 194:23	127:23 128:10
165:18 172:17	111:5 114:11	103:13 107:2	look 9:10,11,12	130:15 131:12
letting 193:6	114:11 173:5	107:25 110:16	9:24 10:3 11:6	134:13 136:10
level 47:21 53:4	174:19 179:25	110:24 111:12	12:15 14:4	136:13 143:2
63:22 75:16	184:19,20	113:21 133:22	15:23 17:3	144:15 164:19

179:22 193:10	136:6,15	86:14 122:23	manner 23:23	180:17 181:3
199:5 202:2	138:17,24	123:12 155:1	88:23 190:19	181:15,15,18
205:9	139:18 140:11	165:22 166:5	Manning 4:9	181:23 182:1
lookout 52:4	140:13,24	167:15 173:24	147:15,15	183:9 184:6
looks 10:21	141:1,22	174:11	151:21 158:8	185:9,11,13,23
49:13,16 97:20	150:17,18	majority 62:2	159:19 164:12	186:9,17,22
166:23 183:16	152:5,15,16	197:3	166:25 171:15	187:12,12,18
201:16	157:12 160:2,3	maker 179:3	marijuana 15:2	187:20,22
Lookup 8:2	162:6 163:17	183:9 189:12	205:11	188:7 189:12
lose 7:23 43:20	167:14 175:18	makers 178:19	Mark 2:16 4:8	189:12,16,18
44:18	176:3 185:19	186:17 194:13	143:15,17	191:6 192:22
losing 44:15	189:14 196:25	making 11:2	147:9,23	193:5,6 194:12
loss 28:23 40:2	199:24 203:18	13:11 19:17	150:15 152:20	194:13,15,18
44:12 110:1	205:24 206:25	65:21 66:7	153:4 163:10	196:1
154:4,18 172:3	208:16,19,22	75:12 83:15	165:9 170:11	market-specific
losses 28:18,21	lottery 41:19	106:2 125:15	172:14	16:8
29:2 40:12	42:5 46:17	128:11 132:23	Mark's 167:9	marketing 34:7
43:12 44:19	Lourdes 2:13	134:23,24	markers 153:10	129:5 197:14
68:10	77:17 121:7,21	139:20 154:11	market 8:10	204:22
lost 11:22 13:5	122:12,20	165:15 171:1	11:23 13:13,15	marketplace
26:10 42:13	123:8 127:25	180:22 185:24	13:17 14:18	22:24 100:14
43:3	132:7 137:8	192:1 193:6	15:8 16:11,12	101:25 173:24
lot 14:19 19:17	139:24 142:2	207:14	17:19 19:25	174:9,12
22:22 27:21,21	love 51:6 191:1	male 40:11,11	20:19 22:5,11	182:22
29:11,17 31:13	207:5	malware 41:21	22:15 24:10	markets 6:8,10
32:3,19 35:1	low 23:25 99:18	management	33:15,18 34:13	6:22 7:6 10:16
39:14 42:10,15	200:16	122:17,18	80:11,13 83:3	12:11 13:22
42:18 44:25,25	lower 30:4 118:8	130:11	83:14,20 84:2	16:16,16 25:8
45:8,13,17,24	lowest 115:7	mandate 20:16	84:14,16,24,25	25:9,14 59:24
50:11,12 56:12	luncheon 142:14	161:12 162:17	85:7 87:5,9,12	70:11 77:11,14
56:13 57:4,22	lure 60:25	mandated 167:9	87:15,16 88:1	77:15,18 81:13
59:20 61:14	lured 60:8	mandates	88:7,8,16,16	82:16,21 92:4
64:25 66:2,22	lyrics 106:15	154:21,22	88:18,22 89:1	92:12 103:22
68:18,22 70:13		mandating	90:3 92:2,6,18	103:23 104:10
71:22 76:2	M	164:23 167:2	93:20 97:12,20	105:3 121:4
80:17 92:8	M&A 103:10	167:20	98:11,11	142:24 143:14
97:6 98:6	117:2	maneuver 152:3	100:11 101:16	143:21 145:24
101:9 105:9,18	machine 137:14	manipulating	111:19 116:16	149:8 150:3
110:18 113:8	176:10 185:24	38:12	121:6 125:17	175:3,12,13,15
113:12 116:20	186:25	manipulation	128:2,7,20	176:8,11,21
116:21 119:25	machines 15:2	14:18 17:19	129:24 149:8	177:3 178:19
119:25 120:7	magic 189:15,22	20:20 33:15	168:2,8,13	178:20,25
120:14 124:22	magnitude 50:9	49:15 129:24	173:22 174:10	179:23,25
125:14,19,25	mailbox 34:8	175:14	174:23 175:17	181:10 185:8
126:1,10	mailed 87:11	manipulative	175:19,24	185:11 188:20
127:11,17	main 6:25 7:10	5:5 18:10,16	176:3 177:1,25	195:6 196:1,2
128:4 130:13	13:4 14:2 40:2	78:6	178:8,9,11,12	201:1 203:2
130:21,24	maintains 149:8	manipulators	178:19,23,25	mass 34:6
132:2,23 135:4	major 15:6	33:18	179:1,3 180:8	massive 92:11

180:3	132:17	merger 99:9	142:3	14:16 15:21
matches 150:20	meeting 46:14	148:12	Mike's 177:13	22:9,10,12
154:12	88:2,5 172:1,5	merges 99:20	177:13	27:5 185:7
material 129:12	meets 203:16	merit 82:7	military 28:11	198:7
155:21 173:22	member 83:21	146:11 161:17	46:6 197:23	mistake 177:10
174:7,10	90:7 122:25	message 35:6	201:12 207:9	mitigate 184:17
187:10	179:11	206:11	million 17:8,24	mixed 150:14
materials	members 17:1	messages 34:10	25:21 27:6	MKT 169:2
107:14,14	27:6,7,15,21	205:20 207:17	45:23 117:18	178:2
108:18,19	59:13 60:11,13	207:19	millions 60:10	mode 39:23
Matrimonial	60:18 74:2	messaging 21:13	62:13	40:20
195:11	101:23 117:15	70:13	mind 8:19 10:1	model 132:17
matter 178:11	129:2 170:17	met 81:15,19	26:7 32:21	135:1 183:8
210:3 211:5,7	174:2 196:7	82:11 83:8,17	48:17 104:6	moderated 19:2
matters 13:1	201:12	92:16,16	134:25 146:25	19:5
14:3 79:16	membership	155:13 164:9	148:16 182:23	moderating
144:11	27:3,4 140:14	method 40:14	192:25 205:17	18:15 77:14,16
maximize	173:2	methods 43:5	mindful 139:5	77:18 78:2
208:25	memorandum	45:25 129:23	196:10	143:14 144:7
mean 24:4 35:18	109:19	133:1	mindset 41:2	moderation
50:1 51:4	memory 109:12	Mexican 206:2	mine 50:18	143:24
53:24 55:3	men 53:16 59:22	Mexico 25:7	minimis 113:18	moderators
61:23 62:7	mention 62:6	mic 172:21	minimize 102:11	143:11
85:17 113:21	109:25 110:3	196:12	184:17	modifying 78:25
114:17 115:5	126:7 133:1	Michael 3:10	minimum 164:4	mole 15:1
151:22 156:8	197:18	4:11 122:22	mining 16:20	moment 159:14
170:22 175:13	mentioned 17:5	175:3 179:8,9	71:25 203:13	Monday 16:11
176:2 187:16	23:16 32:13	181:4 189:3	minute 19:24	money 7:23
193:12,15	33:23 46:4	192:12,21	44:22 126:7	14:20,20 15:14
195:11 199:3	54:16 56:5	208:21	minutes 86:25	17:13 34:23
208:15	59:19 60:17	microcap 7:15	138:10 143:4	41:5 42:14
means 42:19	61:24 63:16	17:20 23:6	169:24 171:5	43:20,25 44:2
45:8 56:11	85:24 103:18	39:6 58:1	misappropriat...	44:7,10,13,18
78:5 108:8	105:17 108:1	125:9 127:17	20:19 25:17	46:18 47:13
112:17 115:7,9	111:4,15 117:2	131:1 136:15	128:24	48:11 51:6
117:17 196:14	118:15 119:1	136:15 146:2	misconduct 7:3	52:7,12 56:20
199:16	125:24 133:3	168:10 175:16	misinformation	57:4,5 59:10
meant 55:22	150:4 151:8	177:22 179:18	187:4	61:15 62:16,23
measures 8:14	152:21 155:6	179:21 185:16	misleading	64:13 73:2
16:14 18:8	156:3 157:15	203:3	114:3 187:11	75:9 101:18
144:12	159:11 160:14	middle 69:5	misprocessed	112:7 115:17
meat 143:9	164:23 188:25	109:25 120:21	183:21	117:9 122:7
media 18:20	191:13 192:22	188:12 208:24	misrepresenta...	123:5 125:11
34:11 42:17	203:1 204:13	migrated 68:14	15:4	125:15 130:16
Medicare 56:14	206:9	Mike 122:5,19	missed 69:14	130:20,23
mediums 71:4	mentioning	123:3 127:14	132:4	131:4,7 134:10
84:17	70:21 170:25	133:21 134:17	missing 116:1	135:4,5,6,18
meet 48:7 75:15	172:3	137:3 140:2,9	117:10 177:20	135:19,21
83:16 93:7	merely 110:8	141:17,20	mission 12:22	136:2,17,18,20

140:3 188:13 198:17 199:22 200:3 moneymakers 16:24 monitoring 154:20 month 76:18,19 months 12:7 37:5,18 38:2 44:16 74:20 203:9 Morgan 104:23 morning 6:2,20 12:18 76:23 142:20,25 197:1 203:4 mortgage 47:10 47:10,12,14 Moshe 2:15 143:12,18 145:14 172:14 mother 37:2 63:16 mother- 63:16 motivates 12:23 motivations 104:2 mouthful 145:6 move 50:1,13 84:15 89:6 100:2,23 136:18,20 140:3 143:23 149:13 157:2,5 170:7 186:8 190:2,8 195:23 moved 81:5 190:3 movements 135:18,20 136:2,17 movie 31:7 176:15,17 movies 31:5 moving 57:25 73:17 130:16 muddy 136:19 multifaceted	201:15 multijurisdictional 36:21 multilevel 129:5 multimillion-dollar 7:20 multiple 32:24 multitude 135:21 museum 176:16 176:18 mutual 30:24 mutually 91:12 myriad 151:11 162:9 <hr/> N <hr/> N 5:1,1 6:1 142:16,16,16 nail 118:5 193:3 name 26:5 61:19 79:24 96:2 122:12 136:17 142:22 194:10 200:6 210:19 named 178:5 names 38:10 54:23 58:16 100:17 106:19 111:9 194:24 narrative 136:6 137:10,15,18 138:1,4 narratives 137:14 narrow 86:3 narrowly 205:22 NASAA 25:4 36:3 38:5 63:25 65:17 204:7 206:1 207:23 NASAA's 25:3 199:5 nascent 103:4 NASD 80:21,24 NASDAQ 169:2 178:1,3,5 nation's 12:13	national 20:11 21:7 23:20 78:21 159:23 181:23 206:19 Nationle 45:24 Native 201:13 natural 94:13 naturally 53:14 nature 109:21 174:6 NE 1:24 near 64:20 196:11 nearly 62:14 necessarily 16:3 21:25 58:21 71:6 86:5,6 91:11,13 116:4 154:5 165:22 167:1 necessary 93:11 167:25 173:7 180:13,17,20 need 8:14 14:23 15:7,15 31:19 42:14,14 45:16 49:2 51:1,4,5 86:4 90:22 91:12 96:18 100:1,22 102:13 112:24 114:4,5,9 119:3 131:23 150:7 153:17 154:6,11 155:23 156:24 158:4,16 162:21 163:1 168:17 169:7 169:15,16 170:19 171:22 177:5,16 179:11,20 181:25 184:18 184:21 185:12 185:14 187:22 188:9 189:13 189:22 190:23 190:23,23	193:8 needed 31:23 157:4 168:11 needing 157:16 157:17 needs 93:6 94:15 123:11 132:19 184:13 190:4 192:18 nefarious 55:20 negative 174:10 negligence 160:21 negotiate 107:12 negotiating 87:18 neighbors 35:16 net 114:24 115:2 115:7,8 116:9 121:3 Netherlands 206:24 netted 17:8 Network 124:3 never 69:8 135:25 149:19 149:21 new 8:2 15:1,3 24:20,24,25 25:1,14,21 30:21 31:5 32:10,10,20 36:2,2 38:4,5 38:20 41:8,11 43:8 47:22 52:20 56:14 67:19 68:17 69:13 70:18 72:3 74:17 75:15 77:11 79:1,5 99:13 102:22 104:9 104:11 118:24 125:1,3,6 132:11,14 133:10 147:10 162:14 187:8 197:13 198:5 198:11 204:7	204:14 205:2 newer 32:8 newest 20:11 newness 40:25 news 31:4 55:18 55:19 61:21 186:20 newsletters 55:2 55:23 nice 53:17 198:16,19 Nicole 2:24 30:9 32:1 39:10 42:22 48:22 49:5 57:21 60:4 66:15 72:14 75:10 Nicole's 51:7 no-action 103:10 106:23 nod 88:17 non- 36:8 non-registrants 38:17 nonaffiliate 155:13,20,23 167:5 nonpartisan 27:5 nonreporting 79:4 nonroutine 166:8 nonvictims 41:3 202:5 normal 148:7 normally 62:20 62:20 110:16 124:13 170:13 North 25:4 nosy 35:15 notable 38:15 note 7:19 38:23 48:24 107:3 125:9,12,14 190:17 204:11 205:10 noted 45:21 60:4 165:4 172:9
--	---	--	--	--

192:16 197:2 notes 204:9 notice 143:19 145:5 174:1,2 189:6 notices 140:22 noticing 19:21 notified 95:20 notify 64:3 noting 181:16 notion 29:15,15 41:1 164:23 notwithstandi... 67:20 number 13:4 33:23 36:12 37:5 53:21 62:14,24 67:3 70:19 84:3 105:22 114:3 116:25 117:7 128:6 133:2 145:25 149:5 157:22 168:15 198:9 203:23 204:19 210:5 numbers 38:9 133:16 numerous 183:13 nut 50:16 NYSE 169:2 178:2	observed 86:7,8 obtain 31:17 150:22 153:15 158:22 obviously 20:15 32:3 42:6 47:21 65:6 92:9 114:21 117:14 170:5 182:9 184:1,4 208:17 OC 139:6,24 172:12 occasion 113:6 occurred 8:12 173:21 occurrence 108:7 occurring 121:15 186:25 occurs 8:17 Oceans 176:15 188:11 OCs 13:8 October 16:12 Oeth 4:10 175:1 178:16 183:2 off-the-grid 47:25 offenders 46:9 offensive 48:9 63:5 offer 54:11 83:23 170:1 offered 31:7 offering 33:7 37:21 93:2,11 108:18,20 111:24 128:25 129:2 offerings 52:16 52:18 57:24,24 129:6 151:11 168:17 204:17 offers 178:21 office 10:16,17 13:22 20:14 21:11 22:4,14 22:21 23:5	24:10,12 25:2 45:11 53:25 102:24 104:23 128:20 144:6 147:10 officer 122:13 122:14 123:19 147:2 175:2 officers 99:12 offices 20:14 123:1 official 80:5 211:15 offline 163:9 offset 93:20 offsetting 93:19 oftentimes 54:5 95:9 125:16 189:6 oh 53:15 62:8 OIEAs 13:8 okay 38:21 39:12 44:17 74:21 76:16 118:18 142:17 158:15 162:24 166:23 175:11 old 47:17 68:10 68:17 187:8 older 27:18 28:10,13,17,20 29:4 30:3 33:6 40:10 47:4 71:20 72:1 106:23 107:1 omitted 137:6 once 50:13 53:25 71:1 82:1 113:19 114:20 143:23 149:13 174:1 194:14 one-by-one 130:18 onerous 171:14 ones 26:2 54:8 79:1 106:23 177:20 199:4 204:14	ongoing 37:14 123:19 173:21 online 8:2 12:20 18:20 36:22 37:23 40:15 45:9 49:21 56:2 68:8,15 131:13 onramp 201:2 onus 57:20 85:21 86:22 166:12 opaque 177:2 open 36:19 41:6 41:7 83:14 88:16,18 93:16 193:10 opened 64:16 opening 5:3 6:19 10:6 51:25 55:13 125:3 199:15,19 openings 132:14 openly 170:25 opens 160:10 operate 82:22 184:7 Operation 36:21 operational 132:14 operations 23:7 95:19 115:11 130:10 operator 168:2 168:13 opinion 91:3 150:5,20,20 154:12,12,15 158:9,15 159:21,24 162:17,18,19 162:20,22,23 162:24 163:16 163:18,20 164:1 166:13 167:7,17,19,25 168:19 171:22 179:14 opinions 80:4	150:18 151:4 151:23 159:16 159:21 160:3,7 161:13 164:5 164:23 167:2 167:13,15 179:12 opportunities 31:21 49:14 129:5 141:5 204:2 opportunity 9:20 12:8,12 31:24 45:17 51:21 68:1 73:1,2 82:13 89:17 93:14 94:21 98:21 118:17 170:2,5 170:22 171:3 171:23 179:2 206:3 opposed 114:24 139:7 150:6 157:5 opposite 70:24 option 161:22 options 97:20 118:7,9 162:9 order 8:5 17:19 90:2 93:7 153:18,19,21 153:25 154:6 177:15 183:16 orderly 103:21 orders 50:8 78:19 192:1,3 ordinary 20:23 155:25 ORF 181:11,13 organization 27:3,4,18 81:2 114:17 141:8 206:4 209:4 organizations 13:15 organizing 6:22 original 104:3 210:13
O	O 5:1 6:1 142:16 142:16,16 objectives 20:24 obligation 151:16 171:11 obligations 74:4 79:18 88:5 102:3,4 observation 38:16 observations 49:3,4 138:13 175:9 observe 38:25			

OS-0926 210:5	overburdened	108:7,24	paramount 8:13	132:1 144:14
OTC 78:11,15	114:14	109:16 118:13	137:11	146:13 152:20
80:14 81:8,11	overburdenso...	125:14 153:16	paraphrase	153:9 154:1
82:16,20,23,24	120:20	paint 142:4	202:14	161:15,17,19
84:24,25 85:6	overcome 73:13	Paley 4:11 175:3	part 7:8 12:22	180:4,9 191:5
87:4,20 128:2	202:23	179:9,9 190:16	15:20 36:12	191:8,9 204:6
149:8 150:3	overhead 112:9	Palisi 168:9	52:14 64:7	205:22
168:25 173:5	overlap 130:13	panel 2:20 3:3	65:3 87:4 94:5	particularly
173:10,14,18	130:21	4:3 5:5,8,11	94:10 96:19	10:24 12:23
175:3,12,17,20	overseas 38:11	18:15,24 19:1	105:15,24	16:17 30:3
175:21 177:24	59:24 173:11	19:5,19 24:23	109:3 113:4	38:15 48:24
178:1,2,24,25	oversee 22:14	73:17 76:13,16	122:23 123:22	73:11 83:24
179:22,25	80:14 122:22	76:23 77:12,14	124:3 127:16	84:15 95:16
181:11,12,15	oversight 77:8	77:16,19 78:3	128:13 135:12	96:21 99:5
181:20,22	173:3	82:19 100:2	138:10 141:14	149:4 159:4
183:10 184:16	oversimplify	101:9 104:19	141:17 143:18	165:1
OTCQB 88:7	115:8	120:14 125:21	143:20 153:15	parties 85:6
89:7 90:13	overtly 154:23	142:12 143:3	165:10 168:3	153:20
OTCQX 88:1	overview 77:23	144:7 169:18	168:21 173:3	partner 21:6
89:7 90:13	101:2 123:4	172:15,22	176:24 181:13	104:23 147:9
others' 167:6	175:7 184:6	177:20 178:17	185:25 186:15	partners 79:23
outliers 152:21	Owen 2:18	179:17,23	187:3,7 188:1	79:25,25
outline 140:19	144:4 196:13	182:11 183:6	192:14 194:6	134:18,21
outlined 66:3	196:15 200:9	191:12 203:11	198:7 202:23	181:11 202:7
109:24	208:3	208:2,6,7	203:17 206:3	partnership
outlines 155:18	owners 116:3	panelist 19:24	participant	15:16 45:10
156:13	144:24	panelists 11:14	111:15 161:7	48:23 134:22
outreach 21:12	ownership	14:5 19:8,23	189:12	181:11 197:22
31:20 45:8	86:16 99:12	68:19 102:17	participants 2:1	201:8
202:7	147:5 148:22	121:20 142:4	3:1 4:1 9:1	parts 23:2
outside 23:9,10		143:6,10	10:2,10 11:15	186:24 194:20
23:20 87:19	P	145:16,18	13:13 19:9,21	party 133:13
120:15 135:23	P 6:1	146:14,24	92:6 149:8	184:15
135:24 152:6	P-word 119:6	147:22 153:6	161:12 174:24	pass 64:21
159:18,19	p.m 142:14	156:24 161:14	180:4,8 189:18	196:12
160:9 165:13	209:17	164:25 174:22	199:16	passed 62:22
outstanding	package 204:10	196:9,17,20	participate 9:20	64:11 138:22
82:2	packaging 32:17	197:2 208:10	12:13 103:9	passing 64:19
over-costly	34:1 36:2	panels 13:19	107:12 115:25	110:25
120:20	pad 13:20	18:15,22 64:25	129:1 143:8	passionate 9:7
over-promising	page 5:2 149:9	77:4 195:4	171:16 197:21	passport 42:13
205:8	205:12	203:11	participated	pastor 60:8
over-the-coun...	paid 37:14,15	paper 111:6	80:4 117:3	path 203:18
80:17,18,25	38:1 47:11	114:1	participates 8:8	Patriot 123:10
81:4,7,13	54:2,9,16,18	paper-based	participating	123:23
84:14	54:21,21,25	87:9	84:10	pattern 124:7
overall 27:22	55:8,9,11,22	parameters	particular 12:21	132:22
137:16 141:1	59:1,3 106:2	148:22 158:21	39:20 79:13	patterns 130:15
194:5	106:18 107:23	191:5	100:5 104:25	191:8

Paul 106:8,13,14 107:4,9,20 108:15,23 109:9 111:4,11 113:23	114:10 115:2 116:5,8 118:6 118:7,21 120:15,21 125:1,24 131:11,11,12 131:12,21 133:3 134:6 151:12 165:18 176:17,21 182:12 185:17 194:21 195:7 198:15,22,25 199:21 200:17 200:19,24 201:20 202:3 202:18 203:20 204:3 205:5 206:17	45:7 60:5 62:2 perpetrating 33:10 65:12 perpetrator 47:23 perpetrators 22:19 23:8 35:19 61:9 person 8:4 11:6 12:20 31:25 34:18,20 39:2 46:18 47:3 48:5,7 61:14 61:24,25 62:15 63:20 66:8 101:16,19 108:3,4 109:17 110:8 118:12 133:7 197:22 person's 61:19 personal 23:16 34:15 38:8 45:9 46:13 48:3 208:20,22 personally 23:23 47:6 personnel 106:19 persons 16:22 63:14 102:12 197:3 perspective 9:25 35:25 40:24 41:2 50:22 62:20 66:15 107:19 128:23 130:3,6,17 133:23,25 135:2 137:6 138:3 148:5 157:2 165:22 170:11,14 181:5 185:3 208:20 perspectives 146:21 pertains 100:15 pervasiveness 29:9	philosophy 53:6 phishing 41:21 41:22 phone 37:20 38:1,9 39:24 40:1,14,17,19 43:23 45:8 55:25 65:7 112:6 131:13 133:16 141:10 phonebook 87:9 phones 34:12 131:11 phony 17:11 photos 47:18 physical 87:10 pick 40:21 141:10 picking 129:10 131:13 picture 142:4 piece 143:1 144:4 pieces 35:22 86:10 piggyback 78:20 79:2 83:18 95:6,7,12,16 96:11 97:5 98:7,20 99:8 100:10 piggybacking 99:14 pilot 188:18 pink 88:16,17 88:18,22 89:8 PIPE 177:1 pitch 47:6 pitched 69:23 70:5 pitches 41:7 pivoting 160:14 place 11:21 12:2 34:14 47:1 70:7 76:1 84:19 91:22 100:3 130:21 131:5 156:19 156:22 169:2	177:1 195:24 placed 85:22 placement 102:16 103:23 105:7,20 109:19 110:23 111:25 placements 111:13 places 9:16,19 57:11 69:22 113:12 placing 74:5 plan 68:22 201:1 planning 132:18 plans 15:13 47:18 plantations 203:24 platform 49:13 87:21 196:22 197:10 200:22 platforms 18:20 33:5 129:8 130:4 play 9:15 18:21 44:12 94:5 101:12 139:3 144:16 players 141:22 178:23 195:21 playing 98:4,8 plays 195:6 pleas 15:8 please 15:17 48:19,19 98:2 138:8 142:18 pleased 12:8 76:17 102:17 117:3 172:25 ploys 19:19 plug 171:5 197:12 plus 61:19 point 11:17 26:15 32:18 45:7 51:7 55:16 60:2,24 64:20 65:13
--	---	---	---	---

75:11 87:8 89:2 92:15 101:15 103:3 120:19 139:11 144:14 167:9 190:3 199:23 pointed 48:4 177:12 points 150:7 157:19 188:25 policies 15:18 123:13,15 131:19 159:12 161:3 162:8 163:22 policy 73:17,20 73:23 74:16 75:3 143:22 144:11 155:17 156:5 160:16 160:18 162:12 163:25 policy- 13:10 policymaking 146:18 159:10 Ponzi 7:16,20 20:18 23:17 25:16 26:1,3 26:13 32:14 35:17 44:24 45:1,2,4,6,13 48:8 49:1 68:7 128:23 131:6 Ponzi-like 17:8 128:24 136:7 poor 199:21 popping 32:9 popular 72:1 204:15 population 28:8 30:5 72:1,6 116:19 portfolio 17:12 portion 78:2 119:17 125:21 147:11 197:2 portraying 60:22 pose 84:12	position 83:6 154:13 185:5 positioned 132:20 146:6 possible 16:14 18:13 75:2 83:23 88:20 90:1 138:7 190:25 possibly 149:23 post 100:3 posters 198:13 potato 97:8,23 potential 17:19 33:12 51:2 57:3 63:8 64:5 70:15 78:6 85:24 106:19 107:11 114:2 115:19 128:17 134:4 145:11 146:17,22 152:17 154:3 154:18 159:10 160:15,17 161:7,24 162:3 164:25 165:4 166:15 173:23 174:11 181:15 183:23 194:5 potentially 22:18 23:8,11 26:10 73:18 81:3 86:12 91:1 93:18 100:11 120:16 129:19 pouring 71:4 power 206:8 practicality 161:18 practically 111:9 practice 66:11 102:22,25 109:7 113:5 122:23 147:11 148:2 150:2 155:15 161:20	practices 8:22 146:14,16 167:6 195:10 practicing 44:11 practitioner 159:24 Pre-IPO 204:17 204:20 precedent 190:5 precluded 96:3 predecessor 88:17 predict 69:19 preemption 119:7,11,13,22 preface 133:24 prefer 31:19 premise 106:13 107:4 prepare 107:13 prepared 7:18 9:9 211:10 preparing 108:17 prescribes 163:22 prescription 159:7 presence 20:13 present 105:8 presentation 49:4 150:10 199:14 presented 9:11 9:14 presenter 166:12,21 presenter's 166:22 presenting 68:1 164:5 presentment 166:20,23 presents 66:4 president 79:23 80:10,13 174:25 175:3 181:7 200:6,8 press 187:4	192:4 pressing 33:25 pressure 45:18 68:10 157:1 presumably 67:23 112:18 presumed 117:25 pretend 42:11 pretty 25:13 34:21 35:20 44:20 69:6 108:20 110:4 140:5 186:10 199:21 203:17 prevalent 85:19 prevent 8:16 14:15 15:14 27:9 31:22 35:10 63:4,11 67:9,13 121:5 130:4,20 144:12 165:25 184:17 preventative 57:6,8 75:2 preventing 146:7 193:7 prevention 14:21,23 49:7 49:7 51:17 57:13,19 74:12 75:12 122:14 preventive 8:13 previous 101:9 139:14 183:6 203:11 previously 43:6 127:4 prey 29:23 41:13 65:24 201:17 202:19 preyed 17:2 42:11 price 37:16 38:3 49:24 50:2 98:21 173:17 185:1 190:1,3 190:7 194:14	primarily 25:9 37:20 120:8 primary 22:9 82:22 93:4 197:10 principal 115:11 principles 161:2 prior 78:14 149:1 priorities 21:5 200:14 priority 7:1 145:23 private 52:16,18 102:16,22 103:23 105:7 105:20 109:7 109:13,19 110:23 111:13 111:25 129:13 165:3 177:1 204:25 privilege 102:19 privity 181:20 184:8 185:19 185:21 186:20 prizes 41:19 proactive 134:14 proactively 8:13 probability 65:22 probably 34:3 35:20 65:11 67:15 70:5 71:20 73:7 76:3,22 77:1 80:6 99:6,13 110:22 116:13 146:11 162:2 162:16 168:7 173:19 179:13 186:7 188:17 191:10 193:8 196:4 201:2 202:12,17 problem 37:4 38:18 64:18 97:23 119:5
--	--	--	--	---

120:10,11 132:6 138:8 145:13 151:13 153:10 154:1 168:14 171:22 206:14 problematic 38:22 45:14 127:20 183:1 183:19 185:6 problems 18:12 18:13 54:5,10 162:19 177:23 195:25 procedure 155:17 162:12 163:25 procedures 123:13,16 131:19 161:3 162:8 proceeding 211:9 proceedings 210:11 process 44:5 56:15,17 57:5 57:18 66:6 74:17 80:22 82:4,6,9 84:1 90:4,9,20 91:11,16 92:16 93:14 94:11 95:19 99:22,25 110:13 114:6 134:11,12 148:4,7 151:25 152:25 154:24 157:7 159:12 159:19 161:4 165:24 171:11 173:25 174:14 177:10 182:4,6 185:1 186:2 188:8 190:25 193:25 195:16 195:17 209:1,5 processed 158:19	processes 145:10 169:13 processing 132:15 144:21 146:8 149:14 161:9 165:3 166:9 product 33:20 39:21 43:8 53:25 181:12 186:23 products 7:17 21:24 30:21,22 31:12 40:25 58:16 59:5 70:11 78:11 professional 17:10 31:14 51:1 66:25 131:6 148:23 professional's 100:11 professionals 21:22 50:5,6 59:23 64:2 professions 60:22 Professor 30:10 profile 28:7 40:8 41:10 65:20 profiling 28:9 40:22 profit 47:15 program 21:8 25:22 46:23 52:15 121:23 121:25 122:3,7 122:23,24 123:9,11,11,21 124:18 129:19 135:5,11,12 140:20 172:12 programming 201:24 programs 26:22 122:6 141:1 198:2,21 prohibited 174:2	prohibits 160:21 proliferation 33:15 prolific 197:16 prominent 60:8 promise 96:15 promises 45:14 45:15 68:8,8 promissory 204:9,11 promote 37:15 promoted 72:5 promoter 54:18 54:21 promoters 37:14 54:16 55:22,23 68:21 128:10 128:11 promoting 37:21 55:25 205:7 promotion 18:2 38:1,7 55:12 186:23,24 promotional 54:22 71:23 promulgated 140:24 prong 109:4,4,5 prongs 108:2 174:16 Proofreader's 210:1,19 propagate 33:20 propagating 21:20 propensity 7:4 properly 157:18 property 127:1 proposal 79:8 92:20 103:16 proposed 75:19 78:25 79:7 80:20 84:13 86:1 119:6 143:20 145:5 proposition 184:3 proprietary	89:23 propriety 154:15 prosecuted 64:17 prospecting 72:3 protect 7:10 9:6 12:4,23 18:10 29:14 78:5 120:7 130:6 133:11,11 165:14 171:6 171:13 173:7 protected 12:12 92:5 94:21 protecting 6:25 21:16 27:3 57:10 91:9 101:13 104:11 135:6 140:7 154:10 165:12 165:12 protection 22:11 25:1 91:7,13 91:15 92:15 94:6 103:21,25 116:18 159:6 164:14 179:1 180:13 193:5 201:15 206:11 protections 102:9 142:5 protective 9:19 64:4 139:21 provide 13:19 16:1,3 27:9 31:16 64:13 82:13 89:4 90:14 93:2 98:21 101:1 102:1 107:14 107:16 116:17 118:13 121:5 132:9 144:19 163:23 167:19 175:7 179:4 186:14 191:25 192:2 193:2	provided 31:12 59:4 90:23 91:2 108:13,25 142:5 164:10 providers 103:2 provides 51:25 106:10 164:13 173:4,6 174:1 174:2 190:20 providing 27:8 28:4 133:13 138:16 151:15 163:14 169:14 178:20 186:2 191:22 provision 112:14 163:14 182:9 provisions 102:4 psychological 40:23 41:2 psychologically 41:10 psychology 202:2 public 39:3 78:5 93:13 99:23 145:1 172:8 173:7 177:3 180:13 197:6 198:12,16 204:19 209:7 209:10 public-facing 196:23 publication 87:11 88:18 publicly 37:24 89:19 91:24 122:16 publish 78:10 87:10 188:3 published 168:2 pull 86:12 202:20 pulled 97:4 171:19 pump 7:15 20:20 23:6
--	---	---	---	--

26:13 32:14	43:8 57:20	67:11,16 84:5	113:19 117:9	15:11
33:16 37:9	82:19 92:3	86:9 125:5	136:24 156:15	reality 111:5
39:6 128:5,12	95:15 97:15	135:16 149:15	172:5	202:13,22
128:13 195:18	140:20 166:12	156:15 189:19	raised 37:6	realization 54:6
195:19 203:11	187:24 203:5	quick 67:7 73:20	112:7 170:8	realize 48:6,10
203:12	puzzle 143:1	96:15 142:12	172:6,13	58:18
pumped 204:4	pyramid 129:4	159:9	raises 163:8	realized 43:3
punish 7:3		quicker 177:17	raising 46:2	136:4
punishing 8:11	Q	189:23	rampant 42:20	realizing 127:8
punitive 75:8	qualification	quickly 43:11,12	ran 195:20	really 9:17
purchase 116:15	182:4	43:20 44:5,13	range 129:13,18	11:16,22,23
purchasing	qualifications	48:25 73:16	144:10 182:2	22:22 23:18
21:24 59:5	82:8 88:9	118:17 140:5	rank 40:5	27:7,15 29:16
pure 29:7	qualified 89:7	149:23 157:2,6	ransom 42:14	31:21 33:5,17
purely 57:20	93:11 115:15	158:20 159:13	rapidly 69:6	33:18,19 34:5
purport 77:1	qualify 150:8	187:22 188:3	rare 190:15	35:14 36:15
purported 24:3	151:5	190:25 192:10	rarely 156:10	41:3 42:2
109:14	quality 131:19	193:2	rate 24:3	43:14 44:11
purportedly	150:4,12	quite 29:11	rates 23:25	46:16 48:4
23:24	quantify 206:15	56:10 57:3,16	ratio 191:6	50:16 51:1,5
purpose 80:25	quantitative	66:4 71:24,25	rationale 137:21	51:16 52:11,16
87:17	88:6,12	75:7 129:13	reach 139:11	55:22 56:13
purposes 82:25	quarterly 88:4	177:22 183:5	reaches 43:22	57:5,7 58:5,7
146:12	115:12	quotation 78:15	reaching 40:19	59:9 60:12,13
pursuing 51:20	question 23:4	82:22 84:17	42:25 43:16	60:15 61:2
74:20	34:2 51:6,10	quotations 78:7	45:12	62:17 65:12
push 133:7	51:12 59:18	78:11	reaction 115:4	68:13,16,17,20
157:14,20	60:1 62:18,22	quote 81:13 83:2	read 68:24	68:24 69:18
158:13 167:12	65:5 66:22	83:3,14 87:14	106:23,24,25	74:2,3,14 76:8
pushback	69:2 73:16	95:8,24 96:2,3	113:11 136:5	82:9 88:9
157:13 158:17	84:8,12 87:4	96:6,7 193:24	readable 113:9	91:14,17 92:5
163:17 164:17	88:24 95:5	quoted 78:17	185:25 186:25	93:13 96:20
171:20	99:6 100:4,9	87:21 89:4	readily 52:24	98:21 106:7
pushed 72:5	132:1 135:22	91:20 142:7	reading 18:3	109:5 110:15
pushing 157:10	135:24 154:15	quotes 87:10	61:17	113:18 124:14
put 8:14 11:8	155:6 156:5	quoting 78:12	reads 193:23	129:5 134:25
19:16 24:8	165:1,9 193:4	82:5,24 83:9	ready 170:18,25	135:6 136:6,7
33:16 48:8	204:23 205:18	83:17 84:16	real 15:12 41:25	136:25 138:1
52:12 83:6	questionable	89:23 174:1	47:7 58:19	138:20 140:14
91:22 94:23,25	135:15,20		126:21,23,24	140:19,24
97:12 101:18	136:3 194:25	R	130:19 150:23	150:19 152:12
140:22 141:4,4	questions 8:19	R 6:1 142:16	166:21 181:14	153:22 155:21
157:1 168:8	50:24 51:24	Racquel 2:17	181:24 184:1	158:25 159:20
176:9 188:5,19	52:4,14,17	143:25 144:5	184:13 188:20	163:14 165:11
198:10 200:3	53:8 54:11	172:21,23	189:6 194:15	165:14 168:10
205:10	57:1,9 58:11	181:6 184:5	204:12,15	169:12,22
puts 175:14	58:21,24 59:9	196:8	real-time 87:12	170:12 171:23
209:10	59:11 65:19	raise 36:24	187:8	177:13,14
putting 38:5	66:2,2,6 67:4	105:11 106:20	real-world	180:22 183:2,6

183:18 187:7	113:14 152:15	104:18 142:25	102:8,13,14	99:23 102:6
188:6 190:21	recommending	reducing 51:21	104:25 105:6	116:23 119:19
191:14 194:16	163:3	refer 53:24	112:4,5,9,17	119:24 125:22
199:2 200:11	record 112:2	114:7 132:22	112:24 113:20	126:2 136:12
200:21 201:11	172:6,9 210:12	132:24 145:7	114:6,19,20,22	136:22 137:1
202:8,11	recorded 211:9	191:21	115:10 117:14	138:15 139:21
204:21 206:15	recording	reference 89:2	123:1 126:15	141:11,15
206:22 207:17	210:15	172:11	142:9 151:10	174:23 189:1,7
realm 31:2	recordkeepers	referrals 24:12	156:10	192:23 205:15
reason 91:16	169:6	131:14 133:3,3	registrants	205:16,16
96:24 107:20	records 102:2	referred 80:7	25:18 35:1	206:2,2 207:3
110:3,10 112:6	recover 29:5	160:25	36:9,9 38:17	regulatory 1:5
124:7,12	31:18 201:19	referring 54:20	registration	8:15 13:15
131:16 157:14	recruit 33:19	192:3	19:3 51:19	16:14 18:8,13
190:19	34:20 48:11,12	reflect 16:4 20:9	77:16 99:19	24:18 74:1
reasonable	recruiting 33:10	104:13	101:3,5,6,8,10	81:9 90:19
78:16 124:14	45:10	reflected 10:14	102:9 106:12	100:13 114:9
164:7	recruitment	10:14	113:3 119:2,20	114:15 116:20
reasonably	45:25	reflecting	120:20 142:7	116:21 120:15
123:13,16	red 21:14 45:13	194:15	regular 44:10	145:11 173:10
163:23	68:6 79:13	refresh 172:18	regularly 66:12	rehabilitation
reasons 49:1	81:22 85:25	refuse 167:18	178:24	177:10 188:8
173:17 188:7	86:5,12,13	refused 167:16	regulate 25:14	195:16
191:22,24,25	116:20 126:21	reg 73:25 140:22	35:1 119:17	reign 61:4
192:3	140:24 164:6	152:6 168:16	regulated 13:13	reinvented
reassurances	191:7	175:23 185:15	34:25 70:8	32:10
45:18	Redfearn 2:8	194:13	168:18	REIT 58:15
recall 37:11	6:2,4,7 10:5	regard 8:24 9:3	regulating	REITs 30:23
recap 140:10	11:10,13 12:9	66:21 74:14	104:10	reject 154:2
receive 27:22	12:16 14:8	123:7,25 136:5	regulation 19:1	rejecting 171:8
147:25 150:19	15:24 22:3	140:17,23	51:20 80:11,13	related 31:3,7
received 81:18	24:19 26:20	regarding 79:9	84:17 88:25	36:13 64:1
86:17 105:25	30:8 32:1	105:6 146:15	114:9,20 117:7	69:4 70:20
receiving 79:20	33:22 35:24	regardless 12:2	157:18 173:12	73:10 104:24
81:12 83:10	38:14 39:12	65:19	207:1	145:9 173:18
131:20	41:14 42:2,8	regards 93:25	regulations 81:6	182:7 207:25
recess 76:15	42:21 43:22	regime 99:19	92:4 123:18	relates 150:13
142:14	44:21 46:3	100:13	164:3 176:4	155:19
recognize	48:19 51:23	regional 20:14	regulator 35:25	relationship
105:10 146:10	54:15 56:3	175:4	54:8 184:9	58:13 61:3
recognized	57:21 59:17	register 25:18	187:25 189:14	75:21 90:12
186:9	62:6 64:24	registered 16:22	207:8	93:1,15 94:3
recognizes 7:25	66:13 67:15	39:2 50:5,9,24	regulators 9:4	94:16 95:1
recognizing	69:2 70:9	50:25 51:3,4	19:9,20 23:3	132:18 174:18
156:25	71:10 72:7,11	52:25 57:23	24:5,13 25:6	189:5
recommend	73:15 74:6,15	62:1,4 63:5,13	25:10 35:12	relationships
79:10	74:21 75:10,25	63:19 65:11	36:5,19 48:16	139:20
recommendati...	76:16 98:2	66:8,25 76:24	64:4 75:6	relative 7:4
95:11 101:17	100:1,20	77:5 101:22	89:21 92:18	relatively 40:9

40:12 57:6 114:13 116:14 relatives 126:1 release 55:18 79:12,14 87:7 143:19 145:6,7 146:19 155:4 159:5 160:17 167:18 170:8 187:4,10 releases 180:19 192:4 relevant 28:5 90:10 reliable 78:17 192:17 reliance 31:14 religious 60:11 129:4 relinquish 56:18 rely 118:7 130:24 133:6 remain 7:1 68:25 remains 26:6 remark 191:11 remarks 5:3,14 6:19 7:18 9:9 20:9 26:24 remember 111:19 148:13 156:9 remind 179:12 remiss 109:24 190:17 197:18 remotely 32:2 removal 146:3,8 146:15 148:3 151:7 161:9,13 162:10 166:7 removals 147:14 remove 144:22 147:25 151:18 152:8 164:19 removed 148:18 removes 144:25 154:13 removing 144:16 145:10	155:19 160:19 160:22 166:10 reopen 193:21 reopening 193:25 rep 63:19 66:8 150:11,11 151:23 155:22 repackage 72:11 repair 41:24 replace 116:10 report 27:10 28:17,20 30:6 40:13 113:6 117:1 121:14 124:1 125:24 134:4 191:19 201:20 reporter 211:3 211:15 REPORTER'S 211:1 reporting 30:2 40:15 64:14 85:11 88:5 89:9 123:17,23 123:24 124:18 129:17 150:9 155:8 168:24 183:4,5 184:2 191:13 194:18 210:14 reports 17:12 19:4 23:1 28:15 48:1 64:9 77:19 115:11,12 121:8,11,16 122:4,8 125:21 126:3 repository 201:22 represent 19:8 27:6 28:17,21 29:1 30:15 92:17 141:21 157:25 179:13 208:24 representation	174:23 representations 150:23,23 representative 126:16 represented 107:2 111:18 representing 94:9 111:23 147:12 represents 106:25 reps 65:12 request 153:3 154:2,16 requests 144:21 146:8 147:25 148:3 151:9 161:9 require 79:2 157:24 161:2 167:7 187:3 193:16 required 79:4 79:18 123:8 128:11 148:22 150:8 162:17 requirement 90:8 116:13 123:23,24 129:17 142:6 162:19 163:16 187:7 requirements 78:18 81:16,20 82:10 88:6 101:2,25 102:2 102:5 114:21 119:20 123:6 124:2,11,18 142:7 155:22 157:19 164:2,2 165:1 166:13 requires 64:1 78:10,13 81:14 121:13 123:10 123:24 129:17 166:24 requiring	166:12 reread 113:6 resale 144:23 rescission 112:18 research 8:3 28:7,9 61:8 66:25 201:16 resolve 163:20 resolved 96:9 resources 27:8 27:19 35:9 48:24 159:14 180:25 207:11 respect 10:25 16:17 19:1 71:11 89:15 90:12,19 93:2 96:16 98:16 99:3 103:7 144:11 145:12 160:18 165:23 181:13 respective 136:11 141:7 response 72:25 106:24 107:1 155:3 179:20 responsibilities 74:10 81:10 83:16 88:21 92:23,24 173:3 183:4,6 184:2 responsibility 57:20 83:8 88:19 93:4 101:10 102:3 141:14 209:1 responsible 25:20 81:11,17 101:11 128:15 144:21 181:8 responsive 193:14 rest 24:22 151:5 restart 177:9 restaurant 198:16 restrict 9:18	restricted 144:20 146:5 148:1 151:25 161:4 171:19 restricting 192:23 restrictions 155:19,20 168:23 restrictive 144:16,22 145:10 146:4,9 147:25 148:17 152:8 160:19 161:9,13 result 29:24 43:4 64:10 73:10 145:1 164:11 resulting 99:20 results 64:8,15 resuming 78:15 retail 1:6 5:6,9 5:11 6:4,23 7:4 7:4,12,15 8:3 9:1,12,14,23 10:12,19,23 11:21 12:11,24 13:9 14:14,15 16:13 18:12,17 18:19,24 19:19 20:7,15,17 21:3,5,18,20 21:23 22:8 23:4,11,14 25:12 26:13,25 30:19,23 31:22 32:4,19 35:23 48:15,25 49:21 49:22 50:1 51:21 69:21 70:1,5 83:24 90:24 91:6 94:6 98:5,9 99:17 100:15 100:16 101:15 101:22 102:7 105:18 117:11 117:18,22
---	---	--	---	---

119:9,12 120:4 120:5,6 121:12 121:18 125:23 126:13,25 127:6,24 128:25 129:16 131:18 135:6 139:17 140:2 142:5 144:12 145:3,13 175:10 196:24 196:24 198:3 203:5,7,8 206:5,10,16 209:2 210:3 211:8 retail- 197:8 retail-facing 197:3 retains 166:19 retiree 46:11 retirees 17:9 48:5,14 retirement 201:1 retirements 15:12 retroactively 104:18 return 24:1 46:17 47:7 56:21 61:20 returns 24:3 45:14,15 54:24 68:8,9 reverse 99:9 review 78:13 79:3,10,18 81:16,20 82:7 82:10 86:4 122:3 128:19 134:1,2,19 135:13 147:13 148:20 150:4 156:7 159:12 159:15,16 reviewed 107:20 122:4 133:6 134:8	reviewers 138:9 reviewing 81:17 153:11 166:20 reviews 79:12 122:8 134:21 134:24 142:6 rich 37:3 rigged 47:18 right 9:15 11:21 12:1 20:3 23:13,20,25 26:5 29:10 31:15 32:16 34:4,7,25 37:3 38:3,18 45:16 46:21 47:2 49:25 57:9 59:15,18 65:10 65:15 66:1 67:23,23 69:9 69:14 71:11 72:4 73:3 80:16 92:9 97:18 98:24 107:10 108:10 108:11,14,16 109:18 126:4 130:1,22 131:15 132:5,7 138:22 139:9 143:25 144:5,8 154:5,11 156:22 157:1 158:5 165:16 168:24 171:2,7 178:11 183:3 184:19 186:3 186:21 188:23 195:7 206:7 rights 112:18 rigorous 25:22 rings 33:17 Riot 178:3 ripe 37:6 rise 67:11,19 rises 109:8 rising 72:17 risk 9:17,21 21:8 21:17 26:12	50:8 93:10 133:5 139:7 140:21 147:2 154:18 165:5 206:13 risks 26:1 132:11 133:10 169:3 risky 167:4 201:2 road 156:16 184:21 robbing 176:18 Robert 2:5 4:6 147:7 155:6 robocalls 40:1 robodialing 65:7 robust 184:10 196:21 201:14 Roisman 2:6 6:15 12:17,18 14:8 76:10 role 18:19 19:25 21:19 93:12 101:12 139:4 144:16 146:8 160:19 175:8 175:24 179:4 182:20,22,24 183:2 185:5,18 186:13 roles 13:9 Rolodex 107:5,7 111:6 113:25 114:1 room 20:18 99:1 193:15 208:13 Rothman 2:15 143:13 145:17 147:20 152:12 160:13 roughly 40:5,6 87:20 88:1 roundtable 1:5 6:3,22 7:8 8:18 10:10,14,21 11:8 12:6,19 13:12,22 16:9	16:11 18:11,14 121:10 144:12 146:12 172:8 208:18 209:8 209:17 210:3 211:8 roundtables 16:7 routine 152:18 166:9 RSS 197:14 rub 91:9 92:14 Rufino 3:10 122:20,22 123:7 127:16 134:20 137:8 140:13 rule 8:20 19:2 62:24 63:1,3 74:8,13 77:14 77:21,24 78:1 78:4,10,13,19 78:25 79:18,20 81:14,16 82:2 82:11,14 85:20 86:2,5,13 88:10 95:11 96:10 114:25 115:3 116:9 117:13 121:3 135:11,11,12 135:12 138:22 150:25 152:4 152:16 162:6 163:21 173:4,6 174:5 179:5,6 182:5 187:8 193:16,18,23 195:15 rule's 78:23 rulemaking 14:4 84:21 91:4,22 94:2,3,25 143:20 145:5 171:24 rules 8:22 15:18 16:8 51:18,18 51:19,19 55:6 62:22 78:22	85:9 88:22 115:9 123:15 140:23 156:11 164:17 184:21 190:14 193:10 run 44:2 52:14 54:10 67:7,8 97:22 181:9,10 run-of-the-mill 148:3 running 59:21 95:3 118:4 120:13 122:3,7 168:10 Russ's 147:10 Russell 2:17 143:25 172:21 172:24 178:14 179:8 181:4 182:18 185:4 188:24 192:12 194:3 196:3
S				
s 5:1 6:1 28:14 142:16,16,16 152:6 S&P 49:13,18 92:10 Sabella 2:14 6:13 19:6 142:17,23 156:17 169:19 172:7 196:8 208:3 sacrilege 115:5 sadly 14:19 safe 12:12 24:2,3 63:25 64:13 70:7 140:7 151:6 159:3 160:15 161:6 163:14,24 164:10,12,24 165:5,8,11,13 166:25 167:20 167:22 safeguards 102:1				

safer 13:17 188:20 195:24	189:19	schemers 48:8	114:23 115:2	6:3 15:10
sale 7:16 81:6,9 119:25	saying 14:17 37:3,12 42:13	schemes 5:6 7:16,23 14:18	121:17 125:8	16:10,15,21
sales 17:25 41:6 41:23 45:18	55:5,7 62:8	16:18,19,21	128:8,22	17:17 24:20,24
122:22	63:2 110:20	17:4 18:2,11	129:14 133:25	25:6,8,9,10,14
sales/repairs	127:2 157:23	18:16,18,21	134:2,8,23	31:1,6 34:25
41:25	158:4,18 168:4	20:18,18 21:21	140:16,22	36:19 46:25
salesman 108:11	188:6 190:3	22:19,20 23:6	141:22 154:20	52:22 57:23
SALI 8:2,6	201:5 203:23	23:8,9 24:7,11	163:6 168:24	59:23 70:10
Saltzburg 2:16	204:7	25:16 26:1,14	169:1 171:10	77:2 78:11,20
143:15 155:5	says 46:18	32:14 33:16	174:16 175:5	78:21 79:6
159:9 164:21	112:14 119:15	35:4,13 45:1,7	177:12,23	80:18 81:1,13
sanctioned	125:12 158:15	45:13 46:13	179:10,11	82:24 84:15
149:3	159:7 163:11	49:1 62:2	180:10,14,25	87:21 89:4
Sandoval 3:11	163:12 185:10	66:17 68:7	184:14 186:15	91:24 93:5
104:22,23	scale 23:7	128:23,24	188:2 191:19	96:17,18 97:3
105:23	175:14	129:4 130:23	192:11 196:7	97:13 98:17
sang 106:16	scam 43:4 72:1	204:12	196:19,22	101:20 102:7
SAR 122:3	201:23	school 34:18	197:5,25 198:9	102:12,21
123:5 127:20	scammers 17:15	46:5	202:15 207:2,9	104:9,10,24
127:21 128:19	42:11	schools 197:23	209:10	107:17 111:25
129:7,16 132:5	scamming 75:8	scope 139:1	SEC's 12:22	114:24 119:14
134:5 136:3,4	scams 17:23	screen 176:9	24:10 128:22	119:18 120:1
137:5,11,16,23	27:10 41:17,20	187:1	138:2	127:18 134:4,9
138:3,20 183:5	41:22 201:19	screening 52:6	SEC-registered	142:8 144:20
184:1	202:2 203:3	screw 53:21,23	194:11	144:24 145:2
Sarah 3:8	207:19	screwed 54:9	SEC-regulated	145:22,23
121:20 124:20	scares 52:17	scrutiny 80:17	90:6	146:5 147:18
127:16 129:18	scary 75:9	160:4	second 16:6	148:1,14
132:8 133:3	112:19	se 40:2	21:10,22 33:14	153:23 155:7
138:11 141:19	scenario 99:9	search 8:3 61:13	47:9 52:1,14	155:11 156:11
142:3	131:11 167:2	61:13,19 67:7	59:18 67:17	161:4 165:3
Sarah's 126:5	167:10	134:15	76:13,16 90:17	168:25 169:3
139:9	scenarios 131:8	seats 142:18	123:15 146:15	171:9,10 173:5
SARs 121:11	151:12 152:1,3	198:25	161:1 165:10	175:16 176:5
124:24 128:23	152:10 155:18	SEC 7:1,9 8:1	173:13 177:7,8	178:21,24
129:9,13	167:7,8	12:25 13:7,10	187:3	183:11,12,15
133:22,25	scheduled 143:3	13:20 16:5	secondary 57:24	184:17,25
134:2,9,12,13	schedules 14:12	23:3 24:9,12	Secondly 22:3	186:12 187:21
134:16,19,19	196:12 208:11	26:2 34:25	seconds 171:5	193:8 195:8
136:21 137:4	scheme 7:20	50:25 55:3	196:18	198:6 199:18
139:12,12	15:1,3 17:8	82:18 87:7	Secrecy 121:13	203:12,13,18
saving 15:14	23:17 26:3	96:20,22 97:20	122:1 123:14	205:5 206:4
savings 13:5	35:17 39:6	99:22 101:23	124:11	207:3 210:11
savvy 65:21	44:25 45:3,5	102:23 103:9	secretly 18:5	securities-rela...
saw 126:14	47:17 48:1,4	103:18,19	section 123:9,23	134:15
135:19 177:11	54:18 60:9	106:9 109:10	145:22 161:24	security 25:4
	114:10 128:5	110:1,1 112:22	162:4 174:23	56:2 78:8,15
	131:6 136:8	113:11,15,15	sections 140:17	82:5 83:2
			securities 1:1,23	89:23 93:22

97:7 125:5	204:3 205:6	127:7	serving 6:25	139:25 180:2
142:6 153:13	seeing 25:24	sending 89:18	120:6	sheep's 34:22
153:14 173:13	30:23 31:6	108:18,19	set 44:7 51:24,24	Sheets 88:17
173:14,15,16	32:4 33:25	109:19 127:3	58:12 66:1,5	shell 150:25
173:18,23	36:1 38:13	131:4	71:3 88:6 89:1	162:25
174:11 175:21	39:15,17 43:4	senior 34:16	89:3 102:10	shielded 165:8
182:25 183:20	58:5,7 61:17	63:8,25 64:14	123:3 145:18	shift 99:10
207:8	70:12 72:22	77:25 79:23	148:7 159:2	shifting 199:11
see 7:24 14:17	83:22,23	80:10 131:1	164:15,18	shifts 166:14
15:11 21:20	118:20 124:21	147:8 197:24	182:15	shining 177:23
23:5 24:7,11	128:21 129:4,7	200:8	settlement	SHO 175:23
24:11 28:12,15	129:14 133:12	seniors 17:1	173:25 174:13	185:15 194:13
29:8 30:3,19	138:14 168:21	37:20 39:15	182:8	shock 28:14
30:22,24,24	202:6 203:9	56:1 60:8	Setzfand 2:25	41:9 115:4
31:2,9 34:10	seek 50:10 73:13	71:11,16 129:3	26:21,23 27:1	shocked 116:8
35:2,11 37:14	seeking 17:15	sense 9:24 29:11	39:18 41:16	shop 201:6
37:16 39:3,22	seemingly 67:19	45:15 59:25	42:7,10 56:9	shops 149:22
40:16 41:2	seen 30:20 33:17	66:21 72:3	65:10 71:18	short 13:3 62:11
43:7,10 44:23	36:17 37:9	98:18 99:14	72:10 74:22	63:7 81:6,9
45:4,13 49:9	38:7 40:4	147:22 183:9	Seventh 41:24	95:4 118:4,16
60:21 61:18	41:20 43:18	sent 24:12 131:3	shaming 30:1	121:12 123:5
62:9 63:7 67:8	51:12 55:24	155:3	share 10:3 22:8	175:18,20,20
71:14 72:16,18	68:6 70:13	sentiments	24:17 27:10,25	175:22 194:13
72:19,20 73:6	72:25 94:12	170:22	28:9 51:15	207:22 208:1
73:6 75:20	126:20 127:10	Sentinel 28:16	70:17 135:7	shorthand
87:15 94:1	127:11 138:20	separating	170:1 178:15	111:21
107:6 110:24	161:11 168:25	51:13	179:2 190:8	shortly 126:25
115:20 116:16	204:19 205:1	September 1:12	201:25	shout 121:3
117:23 119:23	segment 34:12	7:11 208:12	shared 184:5,6	208:4
119:25,25	121:10	210:6	shareholder	show 17:11
120:3 123:22	segmenting	serial 180:6	148:15 150:22	23:22 46:14
125:18,19	98:19 185:23	series 16:7	157:11 159:20	48:1,2 118:14
127:17,19,21	segments 28:10	163:22	166:14	shows 126:8
127:23 128:14	28:25	serious 134:5	shareholder's	side 42:3 87:16
132:2 133:10	segue 189:2	serve 120:4,5	162:18	117:6 122:9
135:20 136:14	192:13	124:12 146:7	shareholders	127:18 131:9
136:21 137:17	sell 8:4 26:17	served 13:2	86:19 144:22	168:1 178:6
144:2 148:9	37:17,22	serves 175:24	157:23 158:18	186:14 193:5
153:4,6 154:22	102:12 136:16	178:18	172:3	205:5
156:21 168:14	seller's 150:11	service 103:2	Shareowner	sides 168:14
171:25 175:19	sellers 193:7	134:10 197:6	147:5	192:20
176:13,14,15	selling 25:16	201:12	shares 86:18,19	sign 35:20 52:22
177:4,7,8,16	113:25 119:3	services 9:5	86:20,21 94:19	89:11 153:25
178:6 179:24	120:9 144:22	31:19,23 64:4	125:13,16,16	168:4
182:25 183:2	175:19 187:6	93:3 122:18	128:6 151:4,10	significant
183:19,23	193:7 199:18	133:14 139:21	168:23 175:22	44:13,19 94:1
185:6,18 186:4	send 24:8 34:7	144:19 147:5	204:20	94:5,13 109:12
186:13,19,21	35:5 55:1,9	175:1 181:8	sharing 24:13	170:6 173:24
190:7 196:1	126:15 127:2,4	186:2 207:12	76:7 133:18	174:13 197:2

significantly 50:2	138:18 140:18 145:4 146:1	43:22 46:24 58:9,13 59:19	197:24 205:19 205:20	specifically 18:18 22:16
Silicon 111:19	153:22 159:23	69:23 73:4	sorts 32:25 34:1	28:2 36:4 71:9
similar 39:16	176:25 196:2	83:6 96:2	59:24 68:20	88:25 100:6
71:24 88:10	201:6	108:6 109:7	sought 79:2	118:25 157:19
97:19 130:9,11	small-cap 188:17	162:21	sound 202:16	161:18 179:20
130:13 201:5	smaller 102:24	somebody's 56:11	sounds 66:13	181:13 204:12
similarly 20:17	102:25 114:13	someday 31:23	90:25 161:23	specifics 44:23
90:5 197:7	116:3 140:18	somewhat 120:3	202:12 208:22	162:13 191:2
simple 22:10	150:16 151:13	135:20 136:3	209:2	specified 121:16
61:13,13,16,19	169:2 170:12	son 73:7	source 34:18	speculating 69:10
61:22	171:14 195:13	song 106:15	116:2 133:19	speculative 51:13,14
simply 8:14	smart 188:19	soon 89:25	sources 189:20	sped 177:14
43:19	202:18	171:24	space 20:1 21:23	speed 186:12
Sinatra 106:16	Smart- 50:17	sooner 157:4	32:22 45:10,22	spend 49:6
singer 106:14	smarter 29:18	sophisticated 97:2,17	57:25 64:23	50:11,12
single 114:22	smoother 193:25	sorry 31:25	67:24 68:2,12	132:22 159:13
133:19	Snap's 187:17	95:25 119:10	68:25 69:3	159:15 183:7
sip 6:8	Snapchat 70:24	127:25 128:1	70:17,23 71:2	196:22
sister 176:23	71:12	143:10 203:22	71:6,8 80:2,18	spending 51:17
sit 27:17 50:6	so-called 68:23	sort 23:4 27:8	81:8 84:21	64:25 127:11
69:22 70:3	106:8	29:17,20 32:15	99:14 100:18	spends 135:4
82:13 84:5	social 18:20	32:16 34:1,15	144:18 145:21	spent 11:17 81:1
87:14 90:19	34:10 42:17	34:16 35:15	148:9 151:8	125:7 126:10
183:13 208:13	197:14,16	37:10 38:15,20	153:17 176:25	135:7 196:25
sitting 26:5 37:1	software 41:21	39:5,13 40:3	177:1 178:24	spike 190:7
144:5 172:12	sold 25:10 52:18	40:22 41:10	179:3 181:19	spirit 165:8
situation 24:16	55:13,14 72:5	42:15 48:12	181:20 182:1,3	spoke 53:20
24:17 47:21	175:20,20,22	51:25 52:1	182:17,22	182:3
48:14 62:9	solely 80:24	56:5 61:20	185:14 190:6	spoken 43:17
96:4 105:13	solicit 107:11	63:5,9,21	192:16 196:24	53:14
116:24 152:20	111:7 117:16	65:18 66:11	197:20 203:3	spot 200:16
155:11,12	solicitation 107:13 110:25	67:25 69:13	spam 34:7	Spotify 176:3
situations 64:3	129:7	73:20 74:8	197:14,15	squeeze 165:6
67:13 78:7	solicited 70:22	83:5 85:9 92:1	spare 113:10	quelch 11:2
95:24 96:12	129:1	98:19 101:18	speak 41:1	SRO 188:4
106:11 152:22	soliciting 108:17	106:10 107:24	153:5 167:3,5	STA 159:4
159:22 161:13	111:8 198:17	108:13 109:24	speakers 139:14	170:16,17
162:1 180:12	solo 159:23	111:3,24	speaking 98:7	stability 179:1
184:12	solution 128:17	120:21 124:13	106:6 150:16	staff 13:6 16:2,5
Six 41:23	solutions 145:11	128:8,14,16	spearheaded 8:9	18:7 19:15
size 28:22,23	146:18,22	133:25 138:12	143:18	20:9 21:7,8
108:7	152:17 159:11	138:13,14	special 46:20	27:24 80:23
skilled 60:22	160:16,18	148:2 152:21	specific 8:20	103:10 105:25
sky 186:10	192:14 194:5	160:14,24	37:15 78:14	106:9,17
slick 202:18	somebody 34:17	180:16 184:15	92:20 129:3	107:21 108:12
slow 165:2,23		190:24 191:1	148:6 162:6,8	109:6 110:4,14
small 15:5,6			163:22 164:6	
112:1 117:5,8			192:4,6	

113:24 115:2 144:2 152:2,13 156:2,3 164:1 170:4 179:11 179:20 208:16 Staff's 6:3 79:16 106:24 107:1 stage 88:8 123:3 145:19 209:1 stages 92:16 stake 108:11 stale 49:19 stand 93:12 170:18 standard 16:2 65:19 74:18 93:7 97:21 148:2 152:16 155:14 160:20 161:2 180:15 186:8 standards 88:3 88:13 191:10 Standing 206:5 standpoint 40:8 85:24 90:18,19 92:20 168:14 stands 99:1 start 15:25 20:1 20:2 32:12 35:14 44:7,11 44:17 56:20 74:14 77:23 83:15 84:21 121:20 129:25 139:17 145:15 146:25 147:21 147:23 148:23 170:3 175:6,11 182:20 188:20 189:9 194:14 200:23 started 22:15 37:10,11 64:6 71:1 80:16,21 102:23 105:1 111:16,17,17 121:24 139:11 148:25 179:19	185:23,25 199:11 starting 11:20 12:1 64:8,15 102:18 182:23 starts 37:2 71:4 state 13:16 23:3 24:13,25 25:10 30:10,14 31:1 31:5 35:25 36:5,19 64:3 104:14 118:17 118:20,22 119:3,18,24 136:21 138:7 139:20 147:14 151:17,18 154:21,22 157:1 165:21 171:11 186:12 197:4 198:9 205:15 207:2,8 state-based 119:20 state-registered 25:20 stated 26:14 65:10 118:10 statement 22:10 59:10 statements 10:6 17:12 33:11,20 51:11 192:5 Staten 47:5 states 1:1 25:6 25:14,19 48:22 50:25 63:23 64:6 116:11 118:15,25 119:16 176:19 178:23 186:9 197:22 200:16 207:3 statistics 180:18 206:19 status 105:3,6 105:11 108:2 109:11 110:15 150:10 155:9	162:25,25 stay 68:14 staying 76:11 steady 23:5 steal 56:20 57:4 stealing 56:11 75:9 125:1,2 Stein 2:4 6:17 14:9,10 15:24 step 55:24 63:24 146:3 steps 7:10 9:4 18:25 66:1 153:1,2 155:14 161:8 163:22 stint 121:24 122:2 stock 7:5 18:2,6 37:13,21 38:3 38:12,12 49:13 49:18,23,24,25 50:2,3 54:24 54:24 55:1,2 55:25 69:25 80:19 96:7,13 99:19 128:3 131:1 151:9,20 151:25 171:19 173:10 187:9 stocks 8:23 16:19,20,20 17:25 37:16 38:25 49:17 58:1 70:2,6 81:4 175:20 190:6 stole 17:13 stolen 125:5 Stone 4:12 174:25 181:6,7 189:10 193:3 stop 36:22 89:11 176:4 185:12 188:11,12 196:17 stops 194:14 stories 27:11 story 55:21 61:21 63:7	138:7 straight 25:17 59:22 straightforward 150:19 strategic 200:13 strategically 21:2 strategies 7:13 44:3 197:19 strategy 7:12 20:7 43:24 Street 1:24 6:25 7:10 13:4 14:2 46:19 strengths 78:23 stretch 55:20 strictly 82:9 strike 57:2 strikes 57:15 71:22 strong 95:5 structure 11:23 114:15 structured 86:3 stuck 42:12 151:15 195:21 student 72:23 students 72:21 stuff 42:23 103:24 subject 101:24 102:2 171:12 173:11 179:23 subjected 206:17 subjects 12:10 207:24 submit 208:18 submits 78:7 submitting 131:14 209:11 subpanel 100:23 101:5 102:16 143:15 144:9 145:19 subscribers 83:21 subscription	109:20 subsequently 80:20 subset 98:16 substantial 78:1 147:11 subtle 35:22 success 36:24 success- 108:24 success-based 106:18 successful 36:23 186:6 196:2 sudden 130:25 203:15 suddenly 195:1 sue 168:6 sued 168:5 suffered 73:10 110:1 suffering 29:5 sufficient 157:14 sugar 203:24 suggest 79:17 85:9 115:5 138:15 suggested 30:22 100:10 118:11 159:3 suggesting 108:13 116:8 suggestions 14:6 91:2 116:7 suitable 21:25 58:23 74:5 suite 205:19 summarize 94:24 summary 138:8 summer 176:15 176:16 sunny 208:12 sunset 95:16 96:12 97:5 sunshine 116:23 super 202:18,18 superficially 166:23
--	---	--	--	---

supervisory 102:4	174:7	124:17	takeaway 120:14	140:2
supplied 157:14	surveil 130:8	system 82:22,23	taken 29:24	targets 16:25
support 64:11	142:9	87:16 89:3,7	84:18 94:15	201:17 202:10
90:14 163:4	surveillance	90:5,6,7,9	97:9 99:9	TAs 151:24
supporting	22:23,24 48:1	102:10 130:5	142:15 163:23	task 7:12 8:9
159:16	77:8 80:25	136:19 169:17	176:7	20:7,11,16,24
supposed	81:2 122:15	176:24 181:23	takeover 124:25	21:1 80:19
113:20 148:21	surveillances	182:8 194:16	takes 29:3 43:2	103:4,6,8
154:23 198:18	130:24	systematic 10:22	102:15 119:18	104:3 111:16
sure 11:2 16:24	survey 36:4 64:8	11:1	176:25	112:25 117:1
23:21 25:22,25	206:20	systematizing	talk 31:21 59:14	118:10 179:18
32:18 36:3	suspect 124:7	133:2	61:7 63:3	tasks 156:12
37:4 42:3 45:6	suspected 17:16	systems 90:8	111:11 133:9	taught 106:17
50:20 52:25	suspects 124:6	130:11 135:17	133:22 139:14	tax 56:21
57:23 58:4	suspended	181:10	163:9 170:25	taxable 200:19
59:15 60:3	17:17 192:10	T	171:21 192:19	teach 53:2
62:13 65:15	suspending	T 5:1,1 142:16	194:2 196:17	teachers 199:14
66:7 70:25	188:14	TA 147:17	197:20	199:16
74:16 83:12,15	suspension	table 37:1 82:13	talked 35:18	team 80:14,23
83:18 84:23	174:17 180:11	122:9 143:6	54:17 57:21	81:8,11,17
92:4 104:8,16	180:19,21	148:7 182:15	65:6 124:23	82:25 106:20
105:23 118:23	188:2 190:18	tacking 153:9,13	128:8 152:14	107:6 143:18
119:13 122:20	191:17 192:1	162:24	161:11 163:15	143:21 177:13
123:7 124:22	suspensions	tactics 17:25	182:12 193:20	177:13 181:14
128:11 130:10	17:15 96:21	39:21 45:18	talking 37:2	187:24 206:23
131:20 132:23	177:12 180:11	202:10	59:22 66:8	teamed 65:17
132:24 134:20	191:23	tailored 8:16,23	71:11 87:5,7	teams 130:12
134:23,24	suspicious 19:3	take 7:10 9:5	88:10 93:8	tease 201:23
138:5,19	77:18 121:8,11	10:22 18:25	96:17 103:22	202:24 206:18
139:20 141:15	121:14 122:4,8	27:24 29:22	105:21 117:22	tech 16:20 26:16
147:1 148:10	125:21 126:3	44:2,21 47:9	128:1,4 133:9	41:20,22
148:20 149:10	129:9,18,20	47:11 50:18	134:6 162:12	technically 55:3
149:17 150:13	132:3 135:15	51:1,5,5 52:7	172:4 177:24	113:20,21
150:20 153:6	137:19,22	53:4 56:19,23	180:24 182:21	techniques 7:14
154:11 159:25	191:12 192:5	57:8 67:23	189:17 192:9	22:17 68:11
159:25 165:15	SVP 26:21	73:8 74:13	203:19	technologies
165:18 167:1,8	swaps 43:14	76:12,20 81:8	talks 193:23	32:11 75:15
178:16 180:16	swear 210:10	83:5 84:20	tangential	technology 21:2
181:6 183:2	Sweep 36:21	87:8 96:9	128:16	29:9 32:20
189:10,21	sweepstakes	97:11 115:23	tape 116:20	33:8,19 39:25
192:19 193:6	41:19 42:4	115:24 126:6	target 21:3,4	41:22 71:6
194:2 198:4	swift 68:9	137:23 142:12	34:16 205:22	75:14,20 90:18
199:23 203:16	switch 129:15	145:15 148:14	targeted 28:14	130:11 133:5
205:5	sworn 12:3	153:1,2,19	102:3 132:12	technology-ba...
surprise 41:9	symbol 95:25	159:22 160:6	201:18	40:18
145:20	96:4 97:4	165:10 166:11	targeting 5:6	telephone 37:21
surprising 59:2	symbols 181:22	169:1 176:23	18:17 40:1	38:8 43:6
surrounding	181:24	193:6 208:21	46:6 47:4	70:22
	synopsis 123:25			tell 31:10 46:20

52:11 54:18	190:22 197:10	170:14,20,22	188:23 195:7	33:12 34:3
63:3 73:9	207:14 209:10	171:2,15 172:9	198:20 203:21	36:12,23,23
86:18 115:20	terrible 125:19	172:14,22,24	207:25	39:18,25 40:8
121:7 124:20	terrific 190:21	178:13,14	things 7:17 9:2	40:17,25,25
126:1 138:6	201:23 206:23	179:7,8 181:4	15:13 22:21	41:11,20 42:19
157:22 166:1	territories 25:7	182:18 185:4	25:24 26:11,12	43:1 50:19
168:7 196:3	Tesla 175:19	188:24 192:12	30:19,20,24	51:24 52:4,10
telling 37:23	test 123:20	194:3 196:3,5	31:3 32:7,9	52:11,13 53:8
131:14 199:17	135:16 203:17	196:9 198:4	33:24,25 34:4	57:7,9 59:7
tells 118:12	testing 206:12	207:21 208:1	34:10 35:8	60:17,21 61:1
template 140:18	Texas 64:6,9	208:13 209:5	37:9 39:21	61:2,6,15 62:7
tend 25:10 40:11	text 34:10	209:14	41:5 42:5	62:9,12,21
73:7 86:7	thank 6:21 10:2	thanking 208:9	50:15 52:10	63:24 65:3,10
190:7	10:4,5,7,10	thanks 6:21 10:8	53:1,5 55:12	67:25 68:3,17
tends 40:9	11:7,10,12	10:9 11:9	56:4,22 57:1	68:24 69:3,5,8
tension 193:4	12:16,19 13:21	12:14 19:12	57:22 61:6,16	69:12,17 70:3
tensions 116:6	14:7,8,10	20:5 67:15	66:11,20 70:12	70:7,9,21,25
tenth 42:1	15:22,24 19:12	76:21 79:21	71:21 73:18	71:16,18 72:2
tenure 81:1	19:15 22:2,3,6	82:15,17 84:7	75:5 79:6	72:4,18,24
term 73:21	22:7 24:19,21	84:9 90:21	83:11 86:21	73:3,5,6,8,23
111:22 126:11	24:21 26:8,19	95:3 104:22	92:19 97:10	73:25 74:8,13
163:7 176:11	26:20,23,23	121:21 145:17	101:12,24	74:16,23,25
178:10	30:7,8,12	169:19 181:6	103:5 104:12	75:3,5,11,13
terms 21:10,17	31:24 32:1	196:8,15,16	104:24 109:21	75:25 76:1,5
21:25 27:22,25	33:22 35:24	200:5 202:25	113:7 116:25	76:23 80:6
28:9,12,15	39:10 42:21	208:3,4 209:16	124:23 128:8	84:3 85:15,18
29:7 30:3,5	44:21 46:3	theft 41:23	130:25 131:2	85:20 86:11,14
32:22 33:25	48:21 51:22,23	56:10 122:14	131:23 134:11	86:21 87:5
34:14 35:2	56:3 57:21	138:25	138:25 148:12	88:9,13 89:2
36:2 40:3,21	59:17 62:25	theme 144:14	150:8,14 152:5	89:24 90:16
42:24 46:1	71:10 73:15	181:17	152:13 157:2	91:11,13,15
51:13 52:15,19	74:6 75:10	themes 76:22	161:21 163:25	92:3,7,21 94:3
53:7 55:21	76:6,10,13,20	208:6	168:9 176:13	94:15 95:14,14
57:10 62:14	77:22 79:24	thereunder	176:13 177:5,7	96:10,14,16
65:5 66:16	80:8,12 82:14	123:18 124:11	180:1 182:12	97:3 98:5,8,9
69:3 72:15	82:17 84:9,23	they'd 168:4	182:13 185:14	98:16,17 99:1
74:4 84:5 85:1	100:24,25	thieves 46:20	185:15,22	99:2,5,7 100:4
85:5 88:3,11	101:4 102:19	thin 49:19	187:19,21	100:11,22
101:16 103:15	104:5,20	thing 10:10 15:9	188:9,14,19	102:5 103:24
106:22 107:9	105:16 111:14	31:15 37:8	193:16 194:1	105:17,24
107:10 112:22	118:23 120:12	40:21 50:4	195:17 198:8	106:1,1 107:8
115:13 117:23	120:23 121:1,1	54:15 61:22	201:4 202:8	108:8 109:12
118:5,20	121:2,9,21	66:13 101:18	207:5,15	109:14 110:10
127:24 132:9	122:12,20,21	107:8 112:20	think 10:13,21	110:23 111:2
134:23 139:23	137:3 140:8	114:3 138:19	10:23 11:4	116:21,24
140:20 151:8	141:17 142:2,2	148:16,19	12:1 14:14,19	117:23 118:5
152:10 154:20	142:3,13 143:7	157:8 171:7	14:23,23,25	120:12 124:24
160:15 182:13	147:20 160:13	181:16 182:15	15:7,9 19:23	128:2,9,17
185:5 189:4,11	169:20 170:2,4	183:18 186:3	29:17 32:5,19	130:23 131:9

132:1 133:8	52:14 123:18	ties 94:2	timeshares 42:1	74:7 87:25
137:4,22	133:13 134:14	Tim 2:12 77:15	tip 46:24	186:9 203:4
138:19 139:2,4	143:1,3 161:5	101:1 104:22	tipping 64:20	topic 6:23 9:7
139:10 142:17	195:15	105:23 108:1	139:11	102:15,17
144:15 145:20	thornier 148:9	118:23 121:1	tips 22:17,25	117:20 122:22
149:22 150:24	thought 62:17	time 9:22 10:3	24:7 35:14,16	129:15 145:3
151:22 152:12	80:3 92:19	10:11 11:7,18	134:5 138:4	156:18 170:18
152:23,24	112:23,23	13:3 14:12,19	Titanium 33:3	171:17 172:5
154:6,8,17	113:1 126:6	26:15 29:4	title 126:23	172:25 173:1
156:1,3,18,23	147:21 182:13	30:20,21,21	today 6:13 10:9	175:9
157:8,15,18,21	191:11	36:7 37:10	11:4,15 12:15	topics 16:8
158:21,24	thoughts 14:13	49:6 50:11,12	12:19 14:13	tore 110:15
159:2 160:13	15:17 51:15	51:17 64:25	15:17 16:3,13	totaled 86:18
160:16 161:16	70:16 73:20	69:8 73:9,15	19:8 30:13	totaling 86:19
162:3,15,16,23	76:7 94:2	80:21 83:15,16	31:25 32:17	touch 54:13
163:2,8,13,15	95:11 170:1	84:12 85:16	76:2,5,25 80:6	57:23
163:19,21,24	178:15 179:4	91:20 95:4,22	82:13 84:10	touched 33:14
164:3,4,8,14	181:5 182:24	95:23 96:8,13	85:14 99:1,7	39:22,23 53:11
164:15,20	189:3 193:2	99:7 100:7	104:13 117:21	205:2
165:10,11,21	194:4 209:6,12	115:20 118:5	117:22 121:5	touching 25:25
165:21,24	thousands 55:10	118:16 120:13	124:24 136:15	touchpoints
166:5 167:2,4	151:25	125:8 126:10	143:6,12	175:8
167:9,20,21,22	thread 20:22	127:12 130:16	144:15 145:19	tough 50:16
169:11,20,24	threat 47:21	130:19 131:2	146:12,20	touting 18:5
170:7,11 171:8	threaten 182:8	132:23 135:4	149:2 172:6	55:2
172:16,20	threatens 168:6	137:24 141:19	173:19 174:21	traced 38:10
176:17,20,22	threats 17:20	141:20 148:22	177:24 203:1	track 112:2
177:5 181:16	three 4:3 5:11	158:2,6 159:14	207:25	tracker 201:23
181:17 182:10	18:14 36:7	162:14 166:11	today's 7:8 8:18	tracking 83:15
182:16 184:13	37:19 41:22	169:8,23 170:2	10:10,14,20	186:23
184:21 185:6	103:19 117:13	175:15 176:22	12:6,20 13:11	tradability
185:22 186:14	134:10 148:10	179:22 181:14	13:19 18:14	86:15
187:7,22,23	160:17 173:8	181:24 183:7	49:4 52:15	tradable 146:5
188:16 189:1,4	174:16 190:15	184:1 188:15	80:2 84:24	trade 28:16 44:8
191:9 193:3	202:8 203:4	188:21 189:6	111:10 143:2	78:21 87:21
194:7,20 195:1	three-part 12:22	191:2 192:1	144:12 145:8	92:10 97:24
195:12 199:10	threefold 183:3	196:23,25	told 60:10 83:1	183:15 184:25
199:20 200:11	thresholds	198:10,11	128:22 134:7	traded 16:9
202:8 208:5,15	121:16	203:22 204:21	136:1	37:24 55:14
thinking 11:18	thrilled 179:2	207:6 208:8,11	toll 29:4	78:8 91:20,24
44:17 49:25	throw 52:2	timeliness 87:23	tongue 39:8	93:22 96:8
67:25 74:9	114:7 172:4	timely 157:17	tool 64:22 65:18	99:18 122:16
94:24 97:10	thrown 110:14	190:19	96:24 184:17	176:3 203:12
169:22 193:11	118:9	times 32:10	184:18,19	203:18
200:22 209:3,4	thumb 175:14	35:12 96:1	201:23	traders 183:12
thinly 16:9	tick 33:2 188:18	125:14,15,25	tools 65:16 77:5	trades 44:4
99:18 203:12	tickers 49:17	126:1 128:4	119:2 182:3	87:18,18 92:12
203:18	tied 38:25 41:18	157:12,25	206:23	trading 6:8,9,22
third 19:5 21:23	190:7	177:18 204:24	top 7:1 40:4 56:5	8:23 10:15

13:21 16:8 17:15,17 19:7 43:12,20,24 44:14 49:12,13 49:19 50:1 51:18 77:11,13 77:15,17 82:23 82:24 83:25 86:18 88:20 90:6,8 93:5 95:21 97:6,17 103:22,22 105:3 121:4 142:24 143:4 143:14,21,24 145:23 162:10 172:22 173:5,8 173:10 174:1 174:17 175:8 175:18 176:5 178:22 179:5 180:10,11,11 180:19,20,24 182:19 183:11 183:12,14,15 184:16 190:10 190:18 191:8 191:16,23,25 192:5 203:2,3 traditional 32:19 33:6 45:8 68:5 traditionally 53:16 train 131:18 152:2 201:11 201:12 trained 105:10 training 105:25 123:20 132:9 132:10 156:11 trainings 132:12 207:7 transaction 63:18 65:14 108:8,9 110:9 112:15 113:23 124:1,7 148:4 150:13 152:18	154:20,24 155:25 157:17 158:11 164:11 transaction-b... 107:23 109:16 transactional 105:8,9 transactions 63:11 65:22 74:11 101:21 105:14 107:12 107:18,22 108:4,14 109:5 109:18 110:6 113:17 114:13 121:14 123:17 124:8 126:25 130:18 132:21 133:2,4 137:18 146:2 152:5,11 165:3 167:4,6 167:24 transcript 172:8 210:14 211:4,5 211:10 transfer 10:25 19:7 42:15 143:4,14,20,23 144:9,11,16,19 144:24 145:9 146:6 147:8,12 147:18,22 148:11,13 149:1 150:5 151:17 157:20 157:24 158:4 160:18,21 161:3,8,24,25 162:20 163:2,3 163:5,19,24 166:16,17,19 166:24 169:6 169:12,14 170:6,12 171:6 171:6,8,11,17 171:19 172:2 172:12 transfers 17:12 transforming	32:20 transition 52:1 transparency 84:17 85:1 175:1 176:12 178:10 179:1 181:8 185:9 transparent 83:24 88:23 176:5 traveling 196:12 Treasury 124:3 treat 30:6 treated 29:25 treatment 29:21 tremendous 84:25 85:3,5 trend 16:18 30:1 36:6 38:15 39:16 43:11 56:4 69:6 71:17 72:17 133:12 trends 19:20 24:11 29:8 30:21 32:8,13 35:25 36:2 38:13 39:20 132:11 134:14 138:13 TRFs 181:10 triage 134:11 trickier 148:8 tried 194:17 trigger 112:24 trouble 7:6 62:1 troubled 13:3 troubles 99:25 troublesome 115:25 Troy 3:4 79:22 79:25 84:21 100:25 Troy's 83:6 true 158:1 202:12,16 210:13 211:4 trust 31:14 46:19 48:5,9	53:13 58:12,19 60:14 61:3 122:17 147:3 190:12 trusted 27:8 31:10 34:19 58:9 60:6 63:14,14,20,22 169:6 truth 49:14 55:20 92:8 200:18 truthful 195:9 try 34:22 35:8 38:19 72:11 77:6 89:6 102:10 126:16 130:19 135:13 144:13 151:12 151:13 153:19 154:9 160:8 165:6 183:18 183:24,25 185:17 200:1 201:5 206:18 trying 8:4 44:2 44:18 46:16,17 50:23 65:14,15 66:10 71:2 92:14 98:14 111:3,12 118:6 127:12 128:5 130:3,6 133:5 151:15 154:2,4 154:14 158:7 171:7 176:23 180:6 195:7 199:25 201:23 202:24 205:4,7 208:25 turn 19:18 20:24 26:21 47:13 67:17 76:17 77:20 79:22 80:9 133:21 134:17 138:11 141:25 143:24 145:14,17 146:23 172:21	176:13 178:10 196:19 turned 47:3 168:9,11 turning 160:23 tweet 187:18 tweeter 190:11 Twitter 70:24 71:12 72:20 73:8 190:11 197:16 two 3:3 5:8 17:22 18:22 19:1,25 20:24 23:18 34:4,6 36:11 37:18 38:2 64:5 73:19 77:4 78:24 85:5 86:19 103:17 108:2 113:13 117:13 129:22 130:2 146:13 162:15 164:22 186:24 190:1 203:4 two-day 16:11 two-part 113:17 186:2 type 23:16 35:16 46:9,11,17 47:25,25 48:2 54:18 61:21 63:10 74:12 120:21 141:6 163:14 184:18 204:17 types 5:5 7:14 7:22,23 12:25 13:8 14:18 18:16,18 24:7 35:21 36:5 39:20 46:13 86:21 96:17 99:3 108:21 131:23 158:22 191:7 202:9 203:1,4 typical 40:9
--	--	--	---	---

41:10 106:4 130:23 typically 30:18 54:25 56:1 59:23 66:24 96:5 101:22 108:2,16 109:22 110:13 111:25 116:2 117:17 130:15 132:13,17 139:18 140:2 typologies 124:21,23 126:9 141:3,7 typology 126:5 126:19,19 141:3	uncovered 23:17 149:5,6 underbelly 168:11 undergo 82:6 underline 55:16 underlying 127:20 135:13 137:21 192:3 underscoring 74:25 undersigned 210:10 understand 31:12 44:23 53:4 58:9,9,22 70:1 74:3 78:11 83:13 98:25 111:22 153:24 158:16 161:19 185:14 186:11 understanding 28:7 75:17 78:16,22 195:14 206:13 understands 75:23 underwriter 93:9,12 94:4,8 94:17,23 95:1 undisputed 174:7 unearthed 156:18 unfold 35:14 unfolding 21:21 unfolds 23:22 unfortunate 128:17 unfortunately 14:16 15:5 26:11 40:20 72:1 119:24 199:15,21 unicorn 26:16 204:17 uniform 74:18 unique 32:16	39:16 183:9 196:1 United 1:1 176:19 178:23 200:15 201:8 207:3 units 181:9 University 30:10 30:15 unknown 69:13 69:18 70:4 unloaded 125:17 unnatural 97:6 unpack 107:24 unpriced 96:3,7 unregistered 16:22 25:16 26:1 31:3,6 35:3 50:4,8,13 62:3 66:20 76:25 77:1,2 101:7 109:11 109:13,15 110:6 112:12 112:16 118:20 120:1,1,2,16 131:6 204:9 unregulated 49:12 69:19 177:2,2 Unrelated 131:4 unscrupulous 17:3 unsolicited 78:19 unsophisticated 129:1 unsuitable 7:16 43:15 unsuspecting 125:17 upcoming 77:12 updated 140:18 upside 9:17 urge 134:6 138:3 urgency 45:15 urging 109:20	usage 181:17 190:5 use 22:18 26:17 34:6 39:20 40:1,18 41:13 53:5 56:21 60:19 73:21 75:3,15,21 87:16 111:21 121:11 126:11 126:14 129:24 134:6,19 153:8 154:9 155:15 171:4 177:18 178:7 182:3,14 186:7 195:13 202:11 useful 11:5 76:6 137:4 139:22 usual 100:18 usually 42:12 43:21 44:16 55:17 96:8 105:8 108:9 160:4 185:13 204:11 utilize 140:15 utilized 136:25	vanish 45:17 variable 30:24 variety 22:13 35:4 152:7 200:13 various 18:1 28:24 54:23 56:11 92:16 121:5 152:1,3 152:10 162:1 191:24 vast 62:2,2 183:14 vehicle 74:1 vein 65:8,24 vendors 133:13 133:13 venture 88:8,14 venues 178:22 versus 29:23 41:3 155:19,23 167:20 193:5 vetting 99:22 vice 79:23 80:10 80:12 174:25 181:7 200:8 victim 23:14 28:22 29:22 40:9 47:16 53:14 victim's 41:1 victimization 27:13 35:2 206:20 victimized 27:12 35:10 victimizing 35:3 victims 12:24 17:24 23:9,21 23:22 28:7,14 28:17,18,19 29:1,21 30:1,4 30:6 33:19 40:10,23 41:3 41:11,13 48:4 48:12,13 57:3 59:7 60:6 61:1 61:4 65:20,21 73:12 202:5
<hr/> U <hr/> U.K 206:7 U.S 1:23 16:15 23:9,9,10,10 23:11 25:7 121:10 124:3 130:4 173:11 178:19 210:11 U.S.A 123:23 U3 181:15,25 189:15 190:5 U3s 190:13,15 U4 135:24 Uber 204:18,25 UCC 156:25 ultimately 47:23 87:18 93:21,22 unable 96:22 unaccredited 129:1 unauthorized 130:20 unaware 135:25 unbelievably 42:15 unbiased 18:3 uncertainty 173:25 174:13 uncover 61:14 136:7			<hr/> V <hr/> v 110:1 vaccines 15:2 Val 77:13,20 82:17,20 84:9 92:22 100:24 Valerie 2:10 valid 113:9 181:25 Valley 111:19 valuable 133:4 133:23 191:20 value 41:3 108:7 151:20 186:19 191:6 Vanguard 121:23,24 122:9 vanilla 152:5 153:3	

video 177:8 199:8	walk 106:3 198:12	wary 18:19	193:24 207:18	183:10,24
Videos 199:6	Wall 46:19	Washington	209:4	187:18 188:5
view 11:20	Walsh 4:13	1:25 104:23	we'll 20:2 25:25	188:14 190:18
40:24 84:18	200:5,6 203:10	208:12 210:7	44:7 64:20	192:9 193:10
100:12 103:17	205:24	211:6	82:15 83:18	196:18 199:3,5
110:7 120:2	want 6:11 10:2	wasn't 36:10	104:16,18	199:11,25
158:6 161:15	10:12 11:13,17	107:11,14	135:16,17,17	200:12 201:6
161:15,19	11:20 14:11	132:3 151:8	135:18 137:17	201:23 202:6
167:22 176:7	16:1 19:11	168:12 188:18	144:3 150:12	202:21,21,23
179:3 182:24	27:13 28:3	wasting 169:8	158:9 170:3	203:2,25 205:4
184:16 185:5	30:2 38:9 39:9	watch 169:11	171:24 172:16	205:5,9,11
193:1 208:22	44:21 46:19	watching 11:6	189:25 190:2	206:17 207:7
views 16:2,4	48:21 49:3,11	12:20 99:17	205:6	207:11,18
19:14 20:9	52:1,7 54:17	105:18 176:22	we're 9:15 11:20	208:8,16
79:20 95:5	55:20 59:17	waters 136:19	12:3,6 13:16	we've 11:25
104:13,14	62:12 65:4,25	way 12:3 27:13	22:21,22 25:11	16:19 30:20
146:17	66:5 67:10,17	28:5 30:17	25:24 26:18	33:17 36:17
violation 46:25	69:14 77:10	36:10 38:3	27:2 28:4 31:8	37:9,19 38:7
112:15 145:22	91:22,23 93:16	45:5 57:14	31:21 32:4	38:10,13 41:20
151:18 162:4	93:16 97:7	59:14 62:21	39:13 43:10,18	45:20 53:14
violations 134:4	98:20,23 100:2	68:4 70:6	47:13 50:23	55:24 57:21
161:24	103:20 111:7	80:14 82:6,8	53:22 57:2	65:16 68:6
violators 180:6	116:20 118:16	86:2 89:1,3	58:5,17 65:13	70:9 86:17
Virtu 175:2	118:16 125:20	98:11,11	65:14 66:10	87:7,22 92:19
178:18	128:7 133:21	100:16 106:15	69:4 70:12	94:22 97:10
virtually 162:10	133:24 135:16	107:20 110:20	71:11 73:6	118:11 124:23
207:6	136:20 142:3	113:25 114:16	74:17,19 88:10	126:20 127:10
virtue 178:17	143:10 150:15	116:7 121:4	97:15 99:3	130:9 138:20
viruses 41:21	163:18 167:9	125:22 126:2	100:4,5 105:12	139:14 140:22
visibility 85:10	167:11,15	128:9 130:7	105:20 117:22	141:11 149:5
visit 208:12	170:4,21	134:14 138:1	118:4,16 119:4	152:14 158:14
void 112:17	171:15 176:8	143:7 152:3	120:12 127:11	161:11 163:15
volatile 190:6	176:14 179:16	159:2 163:5	127:23 128:1	168:25 169:17
volatility 175:23	180:9 184:16	168:17 169:5	130:6,10,15,17	176:7 182:13
191:9	188:16 190:7	177:9 181:1,21	133:12 134:23	183:11 190:15
volume 39:19	191:11,21	184:7 188:10	134:24 136:13	190:22 193:20
150:9 155:8	193:9 195:1,23	188:21 190:14	139:16 140:5	196:25 199:7
181:12 190:8	203:20	193:23 199:1	141:11,15,23	203:2 204:14
volunteer 27:24	wanted 40:21	200:11 201:1,8	142:17 143:2	204:19 205:1
volunteers 27:15	51:15 56:25	ways 5:11 8:24	144:2,13,15	wealth 41:4,6
vulnerability	57:22 73:19	18:22 21:21	145:8 149:17	122:17
71:15	77:24 87:3	22:13 27:20	152:13 154:23	webcast 30:9
vulnerable	95:4 107:24	32:10 34:6	158:14,14	99:17 105:19
28:10 46:15	155:10 156:17	40:19 48:6	159:20 165:15	209:13
63:9 64:14	wants 52:2	62:4 68:16	165:18 168:21	webs 180:3
117:25 139:17	warn 45:12	69:19 79:21	175:25 177:24	website 37:25
W	205:5	91:5 120:18	178:23 180:22	113:11 197:11
	warning 89:11	132:8 172:16	180:23 181:18	197:11 207:23
		182:14 193:11	182:10 183:9	207:23 209:9

websites 18:4 140:16 149:21	116:17 170:18 194:1	141:18 143:6 156:24 160:11	wrap 67:16 76:1 172:16	149:1 183:13 186:11 193:21
Wednesday 1:12 210:6	willingly 48:10	161:20 162:13 166:16 168:3	wrapper 72:12	yesterday's 55:13
week 7:19 14:17 17:6 50:7 74:19 205:11 205:13,14 208:5	win 171:13	168:12,20 169:17 175:13 184:13 187:23 190:18 200:10 201:7,11 202:7 205:17,21	wreaks 56:23	yield 64:8,15
weeks 23:18 24:14 190:1	win-win 116:24	workable 111:9	writ 58:18	York 47:22 102:22 147:10 187:8
weigh 82:7	windowless 208:13	worked 7:2 12:25 19:16 24:13 30:18 122:5 141:18 141:19 168:11	write 103:13 116:17	young 200:23
welcome 6:2,14 10:7 14:11 30:11 48:19 76:21 142:19 142:21 147:20	winds 84:1	working 10:13 10:18 11:18 13:17 31:11 38:6 47:1,3 59:12 62:3 67:1,5 73:2 75:18 80:15 85:6 105:3 112:3 128:15 141:13,15 190:22 191:15 205:3 206:18	writers 18:4	younger 72:23 73:7 199:13 200:2
welcoming 24:23	wine 68:17	workplace 200:21,21,25	writing 123:11 191:18	youngest 47:16
well-liked 60:18	wire 42:15 132:14	works 56:7,7 89:16 163:24 176:16 185:16 185:16	written 190:14	Yvonne 3:9 80:10 82:15 85:2 87:5 93:7 96:17 100:25 182:3
Well-tailored 18:8	wires 131:3	world 50:10 57:11 66:20 150:17 176:1 176:25 187:8 187:16 196:2 205:13 208:5	wrong 132:3 154:23 177:7	Yvonne's 82:25
wellness 200:14	wiring 135:21	worldwide 33:20 201:8	wrote 106:15,15	Z
Wells 147:4	wise 28:4 30:2 41:22 65:22	worst 46:9,9	X	Zinn 3:12 82:16 82:17 86:25 87:3 92:7 96:15 98:14 99:2 127:25
went 38:3 47:22 110:12 117:13 136:3 176:15 177:4 199:13 204:18	wish 53:9 81:13 137:6 176:2	worth 60:10 115:9 152:24 181:16 187:17	XYZ 157:23,25	0
welcoming 24:23	witnessed 16:19	wouldn't 58:20 98:23 133:20 172:1 189:14	Y	1
well-liked 60:18	wolf 34:22		yeah 34:2 44:4 46:8 54:20 62:6 70:9 99:2 107:24 119:13 156:8 158:8 189:10 190:16 193:3 204:8 205:10 208:3	1 26:3 47:8 53:23 55:13 175:22
Well-tailored 18:8	woman 125:23		year 17:16,18,21 20:13 24:12 40:7 50:7 56:15 60:7 85:4 116:14 134:8,8 135:10 151:25 167:5 186:23 190:15 194:9 196:25 197:8 204:15 205:19	1,000 168:19 1,500 86:20 1:00 142:14 10 17:24 22:15 40:4 186:11 10,000 26:9 87:20
wellness 200:14	women 47:4 53:17		years 11:25 16:19 17:1 22:16 36:8,11 37:11 40:10 43:2 47:17 64:5 80:15 81:1,6 87:8 102:25 105:2 105:22 108:13 110:21 117:13 134:22 140:12 147:11,17	100 1:24 17:24 25:21 55:15 83:21 113:20 100-plus 197:21 100,000 40:13 11 41:18 79:12 105:2 11:30 76:13 12 20:13 203:9 12(k) 180:10
Wells 147:4	won 42:4,5			
went 38:3 47:22 110:12 117:13 136:3 176:15 177:4 199:13 204:18	wonder 11:24			
weren't 142:21	wonderful 114:17			
whack-a- 14:25	wondering 57:25 58:2 159:13			
whacky 185:12	Woodbridge 26:6,7,8,9 45:23 53:20 204:13			
whistleblower 46:23	word 54:14			
White 2:12 77:15 101:4 104:5,21 105:16 111:2 118:3,19 119:8 119:11 120:12 187:20	words 156:25			
whitepapers 68:23	work 10:15,24 12:8 13:11 15:15 16:22 19:17 22:12 24:6,9 30:14 30:17 31:1 44:24 46:6 47:1 51:7 61:12 67:10 77:1 78:1 83:1 83:7 90:2 93:6 93:10 96:21 104:24 105:5 112:9 123:1			
wide 19:8 129:18				
widespread 21:2 174:9 176:20				
wife 176:15				
willing 10:3				

13 17:22 63:25	145:4 160:17	352 123:9	9:30 1:14
144 149:4,20	2016 17:19	356 123:23	90 44:15
150:18 151:5	2017 17:17,21	36 178:22	
152:4,16 153:3	36:6 37:1	38 27:5	
155:20	2018 1:12 210:6	380 88:1	
144(a) 152:7	202-551-SARS		
144I 150:25	134:6	<hr/> 4 <hr/>	
15c2- 79:11	208 5:14	4(a)(1) 151:4	
15c2-11 19:2	21 87:8	401(k) 139:19	
77:14,21,24	211 80:22 81:12		
78:1,4,10 80:5	82:4 83:1,10	<hr/> 5 <hr/>	
80:20 81:17	83:10 85:3	5 53:22 145:22	
82:2 84:13	89:15 90:1,4	161:24 162:4	
88:3,10 96:10	90:13,15,24	175:20	
16 29:1	93:14 182:4	5,000 86:18,20	
17 36:18	211s 81:18 86:17	115:9 124:6	
18 36:18	2165 63:1 74:8	50 27:4 28:21	
18,000-plus	74:13	117:17	
181:22	23 29:1	500 49:13,18	
19 5:6 81:5	235 178:21	50:7 92:10	
19,000 178:21	25 16:12 35:19	53 28:19	
1960 102:23	115:16 147:10	55 17:18	
1971 78:4	175:19	59 40:11	
198 5:12	26 1:12 16:12		
1990 80:16 87:6	210:6	<hr/> 6 <hr/>	
1991 85:15	27 18:1	6 5:3 47:7	
106:9	28 80:15	60 28:21	
1999 79:1,7,8,12		61 28:21	
85:25 87:6	<hr/> 3 <hr/>	6127 103:12	
89:2 103:3	3 40:5 47:12	6432 81:14	
111:16	3(a)(10) 151:11	6440 173:4	
<hr/> 2 <hr/>	153:17	181:17 182:9	
2 55:15	3,000 22:11	182:13,14	
2-11 80:2,6	3,500 86:21	6490 182:5	
2:00 142:11	3:30 196:17		
20 86:25 115:16	3:31 209:17	<hr/> 7 <hr/>	
147:17	30 143:3 196:18	70 28:25	
20,000 40:6	200:19	74 40:10	
116:14	30-plus 186:9	78 5:9	
200 36:20 64:9	30,000 134:9		
64:10 168:19	30,000-foot	<hr/> 8 <hr/>	
2003 138:22	103:20	8 47:7,14 156:25	
2005 117:1	309 17:18	176:15 188:11	
2011 109:25	33 111:23	8,000 181:23	
2013 179:19	112:13 113:1	80 47:17	
2014 81:7	117:6	850 24:12	
103:11	3310 135:11,12		
2015 143:19	34 112:14,15	<hr/> 9 <hr/>	
	345 17:8 45:22	9/26/2018 211:6	
		211:14	

