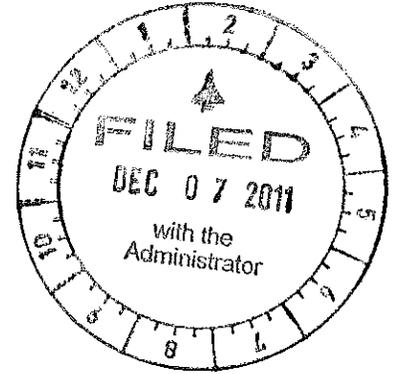


STATE OF OKLAHOMA
DEPARTMENT OF SECURITIES
THE FIRST NATIONAL CENTER
120 NORTH ROBINSON, SUITE 860
OKLAHOMA CITY, OKLAHOMA 73102



In the Matter of:

Geary Securities, Inc. *aka* Capital West Securities, Inc.;
Keith D. Geary; Norman Frager; and CEMP, LLC,

Respondents.

File No. 09-141

**DEPARTMENT'S REPLY TO RESPONDENT FRAGER'S RESPONSE TO
MOTION FOR SUMMARY DECISION**

The Oklahoma Department of Securities (Department) respectfully submits this reply to the response filed by Respondent Norman Frager on December 1, 2011, in connection with the Department's motion for summary decision. As more fully set forth below, the Department contends that Respondent Frager, without reliance on any stated legal authority, other than misrepresentations of the Oklahoma Uniform Securities Act of 2004 (Act), the Administrative Rules of the Oklahoma Securities Commission and the Administrator of the Department of Securities (Rules), and Section 15(i) of the Securities Exchange Act of 1934, (1) ignores the purpose of a motion for summary decision; (2) misrepresents the role of FINRA and the United States Securities and Exchange Commission (SEC) in a state regulatory action involving net capital violation(s); and (3) fails to specifically controvert the facts set forth by the Department in its motion for summary decision and/or to provide evidence of any material factual dispute.

I. Respondent ignores the purpose of summary disposition and the requirements of the process.

The Department's prehearing proceedings and processes authorize the use of motions for summary decision in administrative matters. The provision states as follows:

A party may move for summary decision as to any substantive issue in the case. The Administrator, or the Hearing Officer, may issue a summary decision if he finds that there is **no genuine issue as to any material fact** and that the moving party is **entitled to prevail as a matter of law**. (Emphasis added.)¹

660:2-9-3(d) of the Rules.

Respondent Frager argues that the granting of a summary decision by the hearing officer would deprive him of his rights to a hearing and the opportunity to cross-examine witnesses. The argument is totally without merit as Respondent Frager's theory would render the summary disposition process meaningless.

Respondent Frager states that "[i]t is inappropriate to use deposition testimony to establish undisputed facts, when the parties are available to appear at a hearing and undergo cross examination." The very purpose of summary disposition motions is to eliminate the need for a hearing by providing the hearing officer with the opportunity to review evidentiary materials in order to determine whether there is any issue of fact to be addressed at hearing. *See Flanders v. Crane Co.*, 1984 OK 88, 693 P.2d 602, 605 (citing *Flick v. Crouch*, 434 P.2d 256, 262 (Okla. 1967)). The evidentiary materials subject to the hearing officer's review include, but are not limited to, the pleadings, depositions, admissions, and affidavits. *See State ex rel. G.E. Hettel v. Security National Bank & Trust Co.*, 922 P.2d 600, 606 (Okla. 1996). Summary disposition is proper when these

¹ While there is little case law dealing with such a motion in an administrative setting, federal and state case law in the civil context is abundant. This case law is relevant to this administrative proceeding since the language of 660:2-9-3(d) replicates that of the civil statutes and/or court rules. In Oklahoma civil proceedings, summary judgment motions are governed by Rule 13 of the Rules for District Courts of Oklahoma, 12 O.S. 2001, Ch.2, App.1 (Rule 13).

evidentiary materials establish that there is no genuine issue as to any material fact and that the movant is entitled to prevail as a matter of law. 660:2-9-3(d) of the Rules; *see also Hettel*, 922 P.2d at 606.

The party opposing a motion for summary decision must specify the material facts that the party claims to be in dispute in a written statement. *See* Rule 13(b). The opposing party must also attach evidentiary materials to contradict those facts. *Id.*; *see also Adams v. Moriarty*, 127 P.3d 621 (Okla.Civ.App. 2005).

In *Adams*, certain investors appealed the granting of a summary judgment in favor of the appointed receiver in the case. In their response to the motion, the Adamses “claimed that because discovery had not been completed they were not in a position to stipulate as to Receiver’s statements about the books and records of the Hickman Agency.” *Adams*, 127 P.3d at 623. Further, the Adamses did not attach any evidentiary materials to their objection to summary judgment. *Id.* at 624. The Court of Civil Appeals affirmed the district court’s decision granting the receiver’s summary judgment motion. The court explained:

a summary judgment motion must be decided on the record actually presented, not on a record which is potentially possible; a party opposing summary judgment therefore must present evidence, not mere contentions, justifying a trial on the merits.

Id. at 624; *see also, Polymer Fabricating, Inc. v. Employers Workers’ Compensation Ass’n*, 980 P.2d 109, 112 (Okla. 1998)(“[F]ocus in summary process is not on the facts which might be proven at trial. . . , but rather on whether the tendered material in the record reveals only undisputed facts”); *Roberson v. Jeffrey M. Waltner, M.D., Inc.*, 108 P.3d 567, 569 (Okla.Civ.App. 2005)(“[a] party resisting a motion for summary judgment may not rely on allegations of its pleadings or bald contentions that facts exist to defeat

the motion”); *Tortorelli v. Mercy Health Center, Inc.*, 242 P.3d 549, 559 (Okla.Civ.App. 2010)(“[m]ere contention that facts exist or might exist is not sufficient to withstand summary judgment”).

As demonstrated by the quotes above from *Adams and Polymer*, the scope of review in the summary disposition process is limited to the materials **in the record**. See *Adams*, 127 P.3d at 624; *Polymer*, 980 P.2d at 112; see also, *Hulsey v. Mid-America Preferred Insurance Co.*, 777 P.2d 932, 935-936 (Okla. 1989)(deposition testimony that is not part of the record “may not be used as evidentiary material in the summary judgment process”). There are numerous references in Respondent Frager’s response to his on-the-record testimony, and that of Keith Geary, before FINRA. See footnotes 10, 11, 16, 18, 19, 25 and 28 of Respondent Frager’s response. The FINRA testimony is not attached to Respondent Frager’s response and has not previously been submitted as part of the record in this case. Further, the Department was not represented at the on-the-record testimony before FINRA. Thus, the FINRA testimony should be ignored.

Like the opposing party to the summary judgment in *Adams*, Respondent Frager has expressed his inability at this time to dispute the material facts set forth by the Department in its motion. Additionally, Respondent Frager has not attached any relevant evidence supporting his objection. Rather, Respondent Frager continually states that he **expects** to provide or present contradictory testimony. Such a response is not sufficient to withstand the Department’s pending motion.

II. Respondent Frager has failed to dispute the affidavit of David Paulukaitis.

Respondent Frager questions the appropriateness of the affidavit of David Paulukaitis that is attached as supporting evidence for the Department’s motion. As

shown above, an affidavit is an appropriate tool with which to support a summary disposition motion.

Respondent Frager also questions the qualifications of Mr. Paulukaitis. The determination of Mr. Paulukaitis' qualification as an expert is within the discretion of the Hearing Officer. *See, Williams National Gas Co. v. Perkins*, 952 P.2d 483, 489 (Okla.1997)(“The qualification of an expert witness is generally within the sound discretion of the trial court[.]”). The Department supplements Mr. Paulukaitis' first affidavit with a second affidavit that fully demonstrates his competence, knowledge, skill, experience, training and education to qualify as an expert witness. *See Exhibit A*. As to substance, Mr. Paulukaitis' first affidavit sets forth facts, based on his personal knowledge, and the reasoning by which his conclusions were reached. The affidavit is evidentiary material properly considered on the Department's motion.

Finally, Respondent Frager fails to specifically counter any part of Mr. Paulukaitis' first affidavit. Respondent Frager states that while he is not prepared to contradict the affidavit, his expert disagrees with at least certain of Mr. Paulukaitis' conclusions. Respondent Frager also complains that Mr. Paulukaitis has not been deposed. The complaint is without justification. Mr. Paulukaitis' name appeared on the Department's preliminary witness list filed on December 22, 2010, on the Department's final witness list filed on March 25, 2011, and on the Department's amended final witness list filed on March 28, 2011, Furthermore, counsel for Respondent Frager received a copy of Mr. Paulukaitis' first affidavit on October 21, 2011. Yet, Respondent Frager has made no effort to depose Mr. Paulukaitis.

Again, Respondent Frager simply expects to provide contradictory testimony to that of Mr. Paulukaitis – an insufficient response to a summary disposition motion. *See* Section I above. The Paulukaitis affidavit should not be ignored as suggested by Respondent Frager.

III. Sworn testimony equates to facts.

As explained above, it is appropriate to use witness statements from depositions in support of, or in opposition to, motions for summary disposition. Deposition testimony is given under oath. During the entirety of their depositions, Keith Geary and Respondent Frager were under oath, thereby, affirming the truth of the statements made. It is inexplicable for Respondent Frager to submit that his deposition statements, made under oath, should not be considered as facts.

A. Statements of Keith Geary

Respondent Frager cites statements made by Keith Geary in his deposition that purportedly lack foundation.² At best, Respondent Frager has taken Keith Geary's words out of context. The Department responds to the claims as follows:

1. The May 28th Purchases by the Firm

Respondent Frager contends that the May 28th transactions were never completed based on an inaccurate summation of Keith Geary's testimony. Respondent Frager states that Keith Geary testified that Pershing would not provide the financing for Geary Securities, Inc. ("Geary Securities" or the "Firm") to purchase the private label collateralized mortgage obligations (PL-CMOs) involved in the transactions. Mr. Geary's actual testimony does not support Respondent Frager's contention. Geary Dep.

² It is important to note that counsel for Respondent Frager did not take advantage of the opportunity to examine Keith Geary during the deposition taken by the Department on March 22, 2011. *See* Geary Dep. 217:19-20.

60:14-67:14. For example, Mr. Geary affirmed that “[at] the end of the day, it’s their [Pershing’s] money that paid for the trade because we haven’t written tickets to sell them back out yet.” Geary Dep. 64:17-19. The following excerpts from Mr. Geary’s deposition also demonstrate the creation of the Firm’s liability to Pershing based on the purchase of the PL-CMOs:

Q. So it was on Friday that Ms. Coker received a call from Pershing that said the balance in the inventory account is too high, we are not going to fund these; is that correct?

A. I think it was – **they had already funded them**. So the question was, when are you going to move these out, what are you doing with these? (Emphasis added.)

Geary Dep. 67:10-16.

* * *

Q. But you would – the focus report was for as of May 31st, 2009?

A. Uh-huh.

Q. But you would agree that the private label CMOs were in the firm’s inventory account on that date?

A. We know that, yes. There’s no question about that. And the proof is the fact that we paid interest to Pershing to carry that inventory.

Geary Dep. 85:19-86:1.

Most telling, is the undisputed fact that Respondent Frager accounted for the interest earned on the PL-CMOs as an asset on the books of the Firm. *See* Item 33;

Fragar Answer ¶16. This accounting treatment is diametrically opposed to any claim that the Firm never owned the PL-CMOs.

2. *Entry of May 28th Trade Tickets*

Respondent Frager attempts to create a dispute regarding Item 18 in the Department's motion. Respondent Frager states that Mr. Geary admitted in his deposition that the June 1st trade tickets were not entered correctly. Respondent Frager apparently wants to believe that Mr. Geary knew on June 1st that the tickets should have been backdated to May 28th. However, that is contrary to Mr. Geary's stated intention to buy and hold the PL-CMOs. Geary Dep. 59:14-60:10, 72:15-19; Hintze Dep. 31:9-32:9. Further, the following excerpt from Mr. Geary's deposition evidences the fact that Keith Geary believed the trade tickets entered on June 1st were entered correctly at the time:

Q. Did Mr. Goodman enter those trade tickets correctly?

A. Correctly at the time, yes. Sometimes there are factor changes based on pay downs and they'll – you'll have to come back and reenter the trade ticket based on the new factors. Based on the information we had at that time, sure, yes, he entered them correctly.

Geary Dep. 74:24-75:5. Mr. Geary's response did not include an exception relating to the trade and settlement dates of the trades.

Nevertheless, the entry of the trade tickets did not create the net capital issue. Rather, it was the occurrence of the transactions, effected under Mr. Geary's direction, which created the issue. The result of the transactions was ownership by Geary Securities of the PL-CMOs until June 1, 2009 – the result intended by Mr. Geary.

3. Sale of PL-CMOs from Firm Account

Respondent Frager attempts to challenge Mr. Geary's statement that the PL-CMOs were sold from the Firm's account. In doing so, Respondent Frager claims the understanding of the parties to the transactions is outside of the knowledge or expertise of Mr. Geary. Who, other than Mr. Geary, has more knowledge about the understanding of the parties to these transactions? Mr. Geary was intimately involved (a) in the bidding process for the sale of the securities by Frontier State Bank, (b) in the decision to include the PL-CMOs in the CEMP Offering, and (c) in the purchase of the securities by the two customers of the Firm on June 1st. Mr. Geary obviously understood the purpose and intended result of the May 28th transactions. His intent for the Firm to purchase the PL-CMOs and hold them for a two or three week period could not be any more clear. *See* Item 14 of the Department's motion; Geary Dep. 72:15-19.

One only needs to look at the Firm's audit log reports to see that the PL-CMOs were owned by the Firm and then sold to the two customers. *See* Exhibit B. The reports reflect that the PL-CMOs were in the Firm's inventory account until the securities were moved into the accounts of the two customers on June 1, 2009.³ These documents speak for themselves and there is no dispute as to the ramifications of the transactions.

B. Statements of Respondent Frager

Respondent Frager complains that the Department omits testimony that would support his position from the facts presented in its motion. Yet, Respondent Frager fails to provide excerpts of his testimony that are purportedly in his favor.

In addition, Respondent Frager contends that the statements he made in his own deposition, under oath, should not be considered facts without further elaboration. While

³ The Contra Account 5KVXXXX33 is an inventory account of Geary Securities. Goodman Dep. 30:6-8.

Respondent Frager states that he is prepared to provide additional testimony, such a response is not sufficient to withstand summary disposition. *See Adams v. Moriarty*, 127 P.3d 621, 624 (Okla.Civ.App. 2005).

IV. The Department is not pre-empted from bringing an action based on violations of its net capital rule.

Throughout his response, Respondent Frager claims that the Department cannot make determinations of net capital violations. Respondent Frager improperly relies on Section 15(i) of the Securities Exchange Act of 1934 (Exchange Act) that provides as follows:

No law, rule, regulation, or order, or other administrative action of any State or political subdivision thereof shall establish capital, custody, margin, financial responsibility, making and keeping records, bonding, or financial or operational reporting requirements for brokers, dealers, municipal securities dealers, government securities brokers, or government securities dealers that differ from, or are in addition to, the requirements in those areas established under this title.

15 U.S.C. § 78o.

Admittedly, the Department cannot establish capital, recordkeeping or reporting requirements that differ from the requirements established under federal law. The pertinent rule adopted by the Administrator clearly complies with this federal mandate:

(a) All broker-dealers registered under the Securities Act shall at all times have and maintain net capital of no less than the highest minimum requirement applicable to each broker-dealer as established by the SEC in 17 CFR 240.15c3-1.

(b) As used in this subchapter, net capital shall mean the net worth of a broker-dealer calculated according to the formula established by the SEC.

660:11-5-17 of the Rules.

Section 15(i) of the Exchange Act does not prohibit or pre-empt the Administrator from bringing enforcement actions for net capital violations under 660:11-5-17 of the

Rules. The Appellate Court of Connecticut has concisely summarized the holding of the United States Supreme Court regarding preemption as follows:

[T]he laws and regulations of a state may be preempted by federal laws or regulations (footnote omitted) in three circumstances: ‘First, Congress can define explicitly the extent to which its enactments pre-empt state law. . . . Pre-emption fundamentally is a question of congressional intent . . . and when Congress has made its intent known through explicit statutory language, the courts’ task is an easy one. Second, in the absence of explicit statutory language, state law is pre-empted where it regulates conduct in a field that Congress intended the Federal Government to occupy exclusively. . . . Finally, state law is pre-empted to the extent that it actually conflicts with federal law.’

Papic v. Burke, 965 A.2d 633, 641 (2009) (citing *English v. General Electric Co.*, 496 U.S. 72, 78-79 (1990)).

Respondent Frager does not identify which of the three circumstances would pre-empt the Department from enforcing 660:11-5-17 of the Rules. In fact, the only legal authority cited by Respondent Frager in support of his pre-emption argument is Section 15(i) of the Exchange Act. The language of Section 15(i) does not explicitly pre-empt states from enforcing capital requirements that are the same as the requirements established under federal law. By the sheer fact that Section 15(i) allows states to *establish* capital requirements that are the same as the federal requirements, it is logical to assume that states can *enforce* its capital requirements if the same as the federal requirements. Further, the Department is not pre-empted from enforcing 660:11-5-17 of the Rules on the basis that it regulates conduct in a field that Congress intended the federal government to occupy exclusively. Broker-dealers are subject to a shared system of federal and state regulation as evidenced by Section 15(i), which allows states to establish capital requirements that are the same as the federal net capital requirements. *See* Section II of the brief in support of the Department’s motion. Finally, the

Department is not preempted from enforcing 660:11-5-17 of the Rules because this state's securities regulations do not conflict with federal law.

In addition, the Department's position against pre-emption is supported by the actions of other state securities regulators in enforcement of their respective capital requirements. *See Berachah Securities Corp.*, Stipulation and Consent, 1991 WL 523663 (Fla. Dept. Bank. Fin., March 20, 1991); *Pacific Growth Securities, Inc.*, Temporary Order to Cease and Desist, 1984 WL 194596 (Wash.Sec.Div., Nov. 8, 1984); *Century Pacific Int'l Corp.*, Order to Cease and Desist, 1993 WL 294230 (Ariz. Corp. Com., June 30, 1993); *Norbay Securities, Inc.*, Findings of Fact, Conclusions of Law, and Order, 1987 WL 146064 (Minn. Dept. Comm., Feb. 6, 1987); *Benham Distributors, Inc.*, Consent Order, 1991 WL 212096 (Mich.Corp.Sec.Bur. Sept. 30, 1991).

The Department brings the present action against Respondent Frager for his failure to accurately compute and report the net capital of the Firm as of May 31, 2009. The computation utilized by the Department is described in the affidavit of David Paulukaitis in a step-by-step fashion, utilizing the formula established by the SEC in Rule 15c-3-1. In addition, the Department brings this action against Respondent Frager for his failure to report the net capital deficiencies of the Firm during the month of February 2010. In this regard, the Department has not established a minimum net capital amount that differs from the federal regulators' established amount. Indeed, the Department has simply utilized the Firm's minimum net capital requirement as specified by Respondent Frager. Respondent Frager has admitted that the minimum net capital requirement for the Firm was \$250,000 at all times material hereto. *See* Item 9 of the Department's motion.

The February 2010 allegations by the Department are based solely on the net capital computations made by the Firm as compared to the minimum net capital requirement stated by Respondent Frager on behalf of the Firm on its three notices of net capital deficiencies filed with FINRA. Respondent Frager reported the deficiencies on the standard FINRA form which is aptly titled "Net capital below minimum amount required." *See* Items 59-69 of the Department's motion.

V. Respondent Frager fails to controvert the material facts of the pending motion.

As the FINOP of Geary Securities, Respondent Frager was charged with knowing the Net Capital Rule and properly applying its provisions. *See Respondent I*, 2000 WL 33407051, at *12. It was also incumbent upon Respondent Frager to inquire into all matters within the scope of his responsibilities to determine any impact on the broker-dealer's net capital position. *See Harrison Sec., Inc.*, Release No. 256, 2004 WL 2109230, at *48 (ALJ Sept. 21, 2004) (initial decision) (affirmed by *Harrison Sec. Inc.*, Exchange Act Release No. 50614, 2004 WL 2434257 (Oct. 29, 2004)). Further, the action and/or inaction of Keith Geary did not relieve Respondent Frager of his FINOP responsibilities. *See Respondent I*, 2000 WL 33407051, at *12.

Respondent Frager has not, and cannot, claim that the minimum net capital requirement for the Firm in May of 2009 and February of 2010 was anything other than \$250,000. He admitted to that fact in his Answer and his deposition testimony. His testimony is corroborated by the net capital deficiency notices he filed with FINRA in February of 2010. Respondent Frager has not successfully disputed that Geary Securities owned the PL-CMOs from May 28, 2009, through June 1, 2009, particularly, since he admits that the Firm included accrued interest on the securities as an asset of the Firm as

of May 31, 2009. Further, Respondent Frager does not dispute that he altered the Pershing inventory report dated May 29, 2009, thereby disregarding the over \$79,000,000 in PL-CMOs in the Firm's inventory account.

Additionally, Respondent Frager has not demonstrated that he performed his duties as FINOP to inquire into the PL-CMO transactions and their impact on the Firm's net capital position. In fact, Respondent Frager admits to his failures in his response to the Department's motion at pages 10, 11, 13 and 14. To wit: "Unknown to Mr. Frager until the date of Mr. Frager's testimony before FINRA in August 2010, Mr. Goodman submitted tickets for same day settlement"; "Clearly, at that time, Mr. Frager had no knowledge of the amount of the proposed transaction or the fact that trade tickets had already been submitted"; "Unknown to Mr. Frager at the time of preparing the FOCUS Report was the fact that the staff in the Operations Department allegedly did not carry out the cancelling and rebilling correctly and allegedly did not document the corrected transaction accurately"; "Mr. Frager reported the transaction as it had been described to him and as it apparently had been completed through Pershing"⁴ and "Mr. Frager was, in fact, not aware of any problem with the trade tickets until November 2009". Finally, Respondent Frager has not provided evidentiary materials to show that the June 1st trade tickets for the purchase of the PL-CMOs by the two customers of the Firm were *ever* cancelled and rebilled for settlement on May 28th.

In connection with the May 2009 net capital allegation, Respondent Frager's response to the Department's motion for summary decision provides a 7 to 8 page narrative of what transpired prior to the sale of the PL-CMOs by Frontier State Bank.

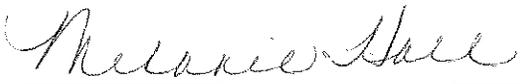
⁴ This statement by Respondent Frager is troubling due to the fact that he admits to altering the Pershing Inventory Report that reflected the Firm's ownership of the millions of dollars of PL-CMOs. Frager Dep. 78:9-14, 80:1-15.

The narrative is little more than “testimony” by his counsel and, in reality, is not material to the matter at hand. The Department has not alleged that Respondent Frager caused the Firm’s net capital to fall below \$250,000 in May of 2009. Rather, the Department’s allegations as to Respondent Frager relate to how he accounted for the PL-CMOs on the books of Geary Securities and his failure to perform his duties and responsibilities as the FINOP for the Firm – factual allegations that Respondent Frager has not disputed. In connection with the February 2010 allegations, Respondent Frager has not disputed that he failed to notify FINRA on each day of the Firm’s net capital deficiency or that the Firm did not cease operations on the days it was under capitalized.

CONCLUSION

Respondent Frager’s response to the Department’s motion for summary decision is woefully defective. Respondent Frager has failed to demonstrate, with evidence in the record, that there are material facts in dispute. The Department is entitled to prevail as a matter of law. Therefore, the Department’s motion for summary decision against Respondent Frager should be granted.

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and correct copy of the above and foregoing motion was mailed this 7th day of December, 2011, with postage prepaid, to:

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