

**FINANCIAL INDUSTRY REGULATORY AUTHORITY  
OFFICE OF HEARING OFFICERS**

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

CMG Institutional Trading, LLC  
(BD No. 47264),

and

SHAWN BALDWIN  
(CRD No. 4281564),

Respondents.

Disciplinary Proceeding  
No. 2006006890801

Hearing Officer – AWH

**HEARING PANEL DECISION**

October 14, 2008

**Respondent CMG is expelled and Respondent Baldwin, its President, is barred for violation of numerous NASD, SEC, and MSRB Rules, as alleged in a 14-cause Complaint. Respondents also assessed costs.**

Appearances:

Pamela Shu, Esq., and Richard S. Schultz, Esq., for the Department of Enforcement.

Nichole C. Patton, Esq., for CMG Institutional Trading, LLC and Shawn Baldwin.

**DECISION**

**I. Background**

On August 30, 2007, the Department of Enforcement filed a 14-Cause Complaint against Respondents CMG Institutional Trading, LLC (“CMG” or “the Firm”) and Shawn Baldwin, alleging that they violated a number of NASD, SEC and MSRB Rules. The Complaint alleges that CMG and Baldwin (1) engaged in securities-related activities without employing a qualified Financial and Operations Principal; (2) failed to maintain the minimum required net capital of an underwriter and had a net capital deficiency in

excess of \$2 million; (3) failed to prepare an accurate general ledger, trial balance, and net capital computation, as of April 30, 2005; (4) failed to prepare and file timely an accurate annual audit report for the fiscal year ending December 31, 2004; and (5) untimely filed an annual audit report for the year ending December 31, 2005, and a quarterly FOCUS report for the end of the first quarter of 2007. The Complaint also alleges that CMG and Baldwin violated NASD Rules when they (1) failed to comply with Continuing Education Requirements by permitting Baldwin to work, while unregistered, in a capacity requiring registration; (2) failed to create and maintain a Business Continuity Plan; (3) failed to apply for approval of a change in business operations; (4) failed to comply with regulations concerning communications with the public; and (5) failed to develop and implement an adequate Anti-Money Laundering (“AML”) Compliance Program. Finally, the Complaint alleges that CMG and Baldwin violated MSRB Rules when they (1) engaged in municipal securities business without a qualified municipal securities principal; (2) failed to report the primary electronic mail contact to MSRB; (3) failed to file with MSRB a list of issuers with which they had engaged in municipal securities business; (4) failed to establish, maintain, and enforce adequate written supervisory procedures for ensuring compliance with MSRB Rules; and (5) failed to establish and implement an AML Compliance Program.

Following receipt of Respondents’ Answers to the Complaint, the parties agreed to a schedule for a hearing in March 2008. At the parties’ request, the hearing date was postponed to July 2008. A hearing was held in Chicago, Illinois, beginning on July 7, 2008, before an Extended Hearing Panel consisting of the Hearing Officer and two

former members of the District 3 Committee. The parties have also filed post-hearing submissions.

## **II. The Respondents<sup>1</sup>**

Baldwin entered the securities industry in 2000 and became registered with FINRA as a general securities representative in September 2000. CMG became a registered broker/dealer in December 2001. Since that time, Baldwin has been the President, Chief Executive Officer, Chief Compliance Officer, and owner of more than 75% of CMG. He is registered through CMG as a General Securities Representative and a General Securities Principal.<sup>2</sup>

On February 20, 2008, FINRA's National Adjudicatory Council found that Baldwin and CMG failed to respond completely to requests for information related to "a suspicious capital contribution allegedly designed to bring CMG in compliance with its minimum net capital requirements." As a result, the NAC suspended CMG in all capacities for two years, suspended Baldwin from associating with any FINRA member in any capacity for two years, and imposed a \$25,000 fine upon CMG and Baldwin, jointly and severally.<sup>3</sup>

The Complaint in this case arose out of a FINRA examination of the books and records of CMG on June 21, 2005. As part of that examination, FINRA staff reviewed the previous examination of CMG that had occurred in March 2003.

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<sup>1</sup> References to the Department of Enforcement's exhibits are designated CX-; the Respondents' exhibits, as RX-; and the transcript of the hearing, as Tr.\_.

<sup>2</sup> CX-1, CX-2, CX-11.

<sup>3</sup> 2008 FINRA Discip. LEXIS 3 (Feb. 20, 2008). CMG and Baldwin have filed an application for review by the SEC of the NAC decision. The application is pending.

### **III. The Violations**

As president of CMG, Baldwin was responsible for “compliance with all the requirements imposed on his firm unless and until he reasonably delegates particular functions to another person in that firm, and neither knows nor has reason to know that such person’s performance is deficient.”<sup>4</sup> There is no evidence that Baldwin delegated ultimate responsibility for compliance with the Rules found to have been violated below. Indeed, as the Chief Compliance Officer, he was squarely responsible for those violations.

#### **A. Financial and Accounting Violations**

##### 1. Failure to Register a Qualified FINOP from March 2003 to October 19, 2005

The FINRA examination of CMG in March 2003 revealed that the Firm did not have a registered Financial and Operations Principal (“FINOP”). Robin Kole, who was registered as a FINOP with another firm at the time, was employed by CMG from July 2002 until March 10, 2003, but she was never properly registered through the Firm as a FINOP because her fingerprints were never submitted to FINRA with her Form U4.<sup>5</sup> Principal FINRA examiner Joseph Sularz determined from an internal Central Registration Depository (“CRD”) document that, from March 2003 through the third quarter of 2005, there was no FINOP registered through CMG.<sup>6</sup>

During the June 2005 examination, Sularz brought to Baldwin’s attention the fact that he did not have a registered FINOP. Baldwin replied that he was going to hire one or he would qualify for registration himself.<sup>7</sup> Following up on his examination of CMG,

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<sup>4</sup> *William H. Gerhauser, Sr.*, 53 S.E.C. 933, 941 (1998).

<sup>5</sup> CX-64; Tr. 14, 19.

<sup>6</sup> CX-23; Tr. 18.

<sup>7</sup> Tr. 21. Baldwin never passed the Series 27 examination. TR. 21-22; CX- 2, p. 7.

Sularz wrote to Baldwin on July 12, July 14, and July 22, 2005, repeatedly asking for a statement of who would be registered through the Firm as a FINOP and on what date.<sup>8</sup>

Baldwin replied on August 12, 2005, stating that, on that date, the Firm had added John O'Connell as FINOP. However, on August 30, 2005, Sularz wrote Baldwin, informing him that a U4 for O'Connell was not processed through CRD, nor did CRD show that John O'Connell ever took the Series 27 or Series 28 qualifying examination.<sup>9</sup>

On September 26, 2005, Baldwin wrote Sularz that the Firm had added Victor Samuel as FINOP. On October 13, 2005, Sularz responded in writing to Baldwin, stating that CRD did not show Victor Samuel as a person registered with CMG, nor did a search of CRD show that Victor Samuel had passed the Series 27 or Series 28 qualifying examination.<sup>10</sup> On October 19, 2005, CMG registered Lawrence Savallo as the Firm's FINOP. During the period June 22, 2005 to October 19, 2005, when the Firm had no registered FINOP, it participated in 13 underwritings that had been filed with the FINRA Corporate Finance Department.<sup>11</sup> By engaging in securities-related activities without employing a qualified FINOP, CMG, acting through Baldwin, violated NASD Membership and Registration Rule 1022 and Conduct Rule 2110.

## 2. Net Capital Deficiencies and Inaccurate Net Capital Computations

On March 23, 2005, while CMG was without a registered FINOP, the Firm entered into a firm commitment secondary offering of Genworth Financial Class A common stock. CMG Institutional Trading, LLC is listed in the prospectus as an underwriter of 597,713 shares, with a price to the public of \$26.50 a share. As an

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<sup>8</sup> CX-6, CX-7, CX-8; Tr. 26-28.

<sup>9</sup> CX-28, CX-29; Tr. 29-31.

<sup>10</sup> CX-22, CX-30; Tr. 32-33.

<sup>11</sup> CX-27, RX 25; Tr. 33-36.

underwriter, CMG committed to buying up to 597,713 shares that were not successfully sold to the public.<sup>12</sup>

According to CMG's FINRA Membership Agreement, it operated as a broker-dealer with a minimum net capital requirement of \$5,000. However, when the Firm entered into an open contractual commitment to purchase shares of Genworth Financial, its net capital requirement was raised to \$100,000, in accordance with SEC Rule 15c3-1. As Sularz testified, as of the day prior to the date of the offering, the Firm was also required to compute the "haircut," or increase in its net capital requirement, based on the valuation of the securities it was firmly committed to purchase as an underwriter. The valuation is computed using the public offering price. Accordingly, the open contractual commitment haircut was \$2,106,938.33. Based on the adjustments for the increase in minimum net capital and the amount of the haircut, CMG's net capital was deficient by

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<sup>12</sup> CX-35; Tr. 40-44. The front page ("Tombstone") of the Genworth Financial secondary offering shows Capital Management Group Securities as one of the underwriters, although the terms of the offering show that CMG Institutional Trading, LLC, made the firm commitment to buy up to 597,713 shares of the stock. Baldwin explained to Sularz that, when he was obtaining membership with NASD for the Firm, he preferred the name of the Firm to be Capital Management Group, but that name was similar to that of an existing firm. Accordingly, the Firm was named CMG Institutional Trading, LLC.

Although Capital Management Group Securities and CMG Institutional Trading, LLC are separate legal entities, the Extended Hearing Panel concludes from the evidence that the names were used interchangeably. *See* CX-34, CX-40, CX-54; Tr. 167-69, 175-77. First, CX-34, p. 2 is a trade confirmation that shows "Capital Management Group Securities," to be a member of SIPC. However, Capital Management Group Securities was not a registered broker-dealer at that time. On the same trade confirmation, CMG Institutional Trading, LLC is identified under the words "house accounts." Second, a Tombstone lists underwriting groups in alphabetically organized groupings according to the size of their participation in the offering. Capital Management Group Securities is shown on the Genworth Tombstone in the same underwriting group that CMG Institutional Trading, LLC is shown on the inside of the prospectus, i.e., with those underwriters that have committed to buy up to 597,713 shares.

The Extended Hearing Panel does not credit Baldwin's assertion that both entities were shown only as members of a selling group and were not underwriters. A selling group is governed by the selling group agreement, also called the Selected Dealer Agreement, setting forth the terms, the commissions, and the termination date which is usually 30 days from the date of the Agreement. Respondents offered no evidence of any selling group agreement or any other evidence that would corroborate Baldwin's assertion that the Firm was not an underwriter. Tr. 171-72. In any event, even members of a selling group are considered to be participants in a firm commitment offering. *See District Business Conduct Comm. v. First Colorado Financial Services, Co, and Mark P. Augustine*, No. C3A950031, 1997 NASD Discip. LEXIS 16, \*\*13-15 (NBCC March 7, 1997) (*citing Townsley Associates & Company, Inc.*, 50 S.E.C. 755 (1991) (a \$5,000 broker/dealer cannot participate in a firm commitment underwriting as a member of the selling group even if the firm's participation is riskless.)).

\$2,235,421.09.<sup>13</sup> By failing to maintain the minimum net capital of an underwriter on March 22, 2005, CMG, acting through Baldwin, violated the minimum net capital requirements of SEC Rule 15c3-1, and Baldwin violated NASD Conduct Rule 2110.

### 3. Inaccurate Books and Records

#### a). Annual Audit Report for Fiscal Year Ending December 31, 2004

On December 31, 2004, Baldwin, as a managing member, made what was described in a corporate resolution as a member's contribution of capital to CMG in the amount of \$190,000. The funds were deposited in CMG's bank account. However, on January 3, 2005, \$185,000 of the \$190,000 was withdrawn from CMG's bank account.<sup>14</sup>

CMG's auditor relied on the deposit of \$190,000 to prepare the annual audit report and compute the Firm's net capital as of December 31, 2004. The auditor's notes to the financial statement as of December 31, 2004, state that the Firm is required to maintain adjusted net capital equivalent to \$5,000 or one-eighth of aggregate indebtedness, whichever is greater. At December 31, 2004, the notes show that CMG had net capital and a net capital requirement of \$240,503. However, because \$185,000 was withdrawn one business day after the \$190,000 deposit, the firm's net capital should have been shown as \$55,503, or \$185,000 less than the stated \$240,503. To be considered an infusion of capital, the funds must remain with the firm for at least 12 months; otherwise the deposit is considered to be a payable to the person who deposited the funds.<sup>15</sup> Because of the misclassification of the \$190,000 deposit, CMG and Baldwin

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<sup>13</sup> CX-31, CX-33, CX-36, CX-37; Tr. 44-48. On the day that the haircut was required to be computed, CMG conducted securities business. CX-34.

<sup>14</sup> CX-44, CX-48; Tr. 63-66.

<sup>15</sup> CX-48, p. 2, CX-44, p. 6, CX-47, p.2; Tr. 63-69.

failed to prepare accurate books and records as mandated by SEC Rules 17a-3 and 17a-5, as well as NASD Rules 2210 and 3110.

b). Net Capital Computation as of April 30, 2005

The Complaint alleges that, by understating its expenses by approximately \$69,163, CMG failed to prepare an accurate general ledger, accurate trial balances, and accurate net capital computations. FINRA examiner Deborah Whitfield examined CMG's financial records and noted that a number of the Firm's financial documents included an accompanying statement from its certified public accountant as follows:

Management has elected to omit substantially all of the disclosures and statements of cash flows required by generally accepted accounting principles. If the omitted disclosures and statements of cash flows were included in the financial statements, they might influence the user's conclusions about the Company's financial position, results of operations, and cash flows.<sup>16</sup>

Whitfield found deficiencies in the firm's general ledger that led her to recompute the Firm's April 2005 net capital. She noted that there were zero liabilities on the firm's balance sheet and that a number of administrative types of expenses, such as salaries, rent, and utilities, were not entered on the Firm's income statement. In discussing the omission of such expenses from the financials, the Firm informed her that it had an expense sharing agreement with its affiliate, Capital Management Group Securities. However, when she reviewed that expense sharing agreement, she found that it did not include an allocation of specific expense amounts for each expense. On the basis of Notice to Members 03-63, which required such an allocation, she concluded that it was an inadequate expense sharing agreement which the Firm could not use, and it must, in any event, include all of its expenses on its own books and records. Accordingly, she

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<sup>16</sup> CX-42; Tr. 211-12.



prepared a spreadsheet summarizing the expenses she believed were reasonably allocated to the firm. By her calculations, the Firm had not booked \$60,458 in expenses which would have reduced the Firm's net capital by the same amount on April 30, 2005.<sup>17</sup>

In addition, Whitfield reviewed the Firm's checkbook and noted that five checks that had been written in April had not cleared in April. Those checks amounted to \$8,704.85, but were not reflected in the bank balance on the Firm's checkbook. Had those checks been properly reflected in the Firm's bank balance, its net capital computation for April 30 would have been reduced by the amount of those checks.<sup>18</sup>

By understating its expenses and failing to account for checks that had been written, but not yet cleared by the end of the accounting period, CMG, acting through Baldwin, failed to prepare an accurate general ledger, accurate trial balances, and accurate net capital computations as of April 30, 2005, in violation of SEC Rules 17a-3 and 17a-5, as well as NASD Rules 2210 and 3110.

#### 4. Untimely Filing of Annual Audit and FOCUS Reports

Consistent with SEC Rule 17a-5, CMG's Annual Audit Report for the year ending December 31, 2005 was due to be filed by March 1, 2006. On February 20, 2006, CMG sought an extension of time within which to file that report. The request for an extension of time was denied by letter dated February 24, 2006, based, in part, on concerns FINRA had with the currency and accuracy of the Firm's books and records. By letter dated March 17, 2006, the Firm was notified that, if it did not file its Annual

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<sup>17</sup> CX-42, p. 24; CX-43, p. 20; CX-46; Tr. 213-23. The Respondents vigorously dispute the expense amounts that Examiner Whitfield found to be reasonable. However, the Extended Hearing Panel does not need to reach a conclusion as to the specific amount of any expense. The mere absence of any amount for each of the administrative expenses is enough to conclude that the Firm's books and records were inaccurate, and that, therefore, its calculation of its net capital should have been reduced by some material number in excess of zero.

<sup>18</sup> CX-45, p.1; CX-10, p. 2; Tr. pp. 223-26.

Audit Report within 21 days of the letter, its membership in FINRA would be suspended. On April 19, 2006, FINRA notified the Firm that its membership in FINRA was suspended, as of that date, for failure to file the Annual Audit Report. CMG eventually filed the Annual Audit Report on July 24, 2006.<sup>19</sup>

CMG's Quarterly FOCUS Report for the end of the first quarter of 2007 was due to be filed by April 25, 2007. On May 10, 2007, CMG was notified that FINRA would suspend its membership in FINRA if that Report was not filed within 21 days of the receipt of the May 10 notice. CMG filed the Quarterly FOCUS Report on May 24, 2007, 29 days late, but before the date of its possible suspension.<sup>20</sup>

By filing CMG's Annual Audit Report 145 days late and its Quarterly FOCUS Report 29 days late, CMG and Baldwin violated SEC Rule 17a-5, which requires the timely filing of those reports, and, thereby violated NASD Rule 2110.

## **B. Violations of NASD Rules**

### **1. Inadequate Anti-Money Laundering Compliance Program**

NASD Conduct Rule 3011 requires each member to develop and implement a written AML compliance program on or before April 24, 2002, to ensure members' compliance with the Treasury Department's implementation of the Bank Secrecy Act, 31 U.S.C. § 5311, *et seq.* Examiner Whitfield reviewed CMG's written AML Program and found four deficiencies in that program which violate Rule 3011.

a). Although Rule 3011 and CMG's AML Program required the firm to verify each customer's identity through documentary evidence, non-documentary evidence, or both, Whitfield found no evidence that, in a sample of seven recent customer accounts,

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<sup>19</sup> CX-55-58; Tr. 315-19.

<sup>20</sup> CX-59, CX-60; Tr. 319-20.

CMG had verified any of the customer identification information it had obtained from those customers.<sup>21</sup>

b). Rule 3011(c) requires firms to provide for annual independent testing for compliance with the Bank Secrecy Act. Although CMG's AML Program identified Linda Rapacz, the Firm's auditor, as the person who would conduct, at least annually, independent testing of the AML Program, CMG, acting through Baldwin, did not have any independent testing conducted. Moreover, Whitfield found no evidence of any testing at all conducted by Linda Rapacz. Although, in its written response to the Staff's Rule 8210 request for information, the Firm asserted that its clearing firm tests its AML procedures, the response refers only to customer identification, not to independent testing of the AML Program. In any event, the clearing firm cannot conduct "independent" testing of the Firm's clearing program. Finally, the day the examiners concluded their examination, Baldwin and Kila Weaver, CMG's Managing Director, informed the Staff in writing that no suspicious activity had been detected or reported. However, the absence of suspicious activity does not satisfy the requirement that independent testing of the Program be conducted.<sup>22</sup>

c). NASD Conduct Rule 3011(d) provides that members must designate and identify to FINRA the individual(s) responsible for implementing and monitoring the AML Program and provide "prompt notification" of any change in such designation(s). CMG's written AML Program designated Baldwin as its Compliance Officer and Weaver and Ted M. Word as "Designate (sic) Officers." However, on June 20, 2005, the FINRA contact system showed that CMG had designated Anne Sprecher as an AML Primary

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<sup>21</sup> CX-24, pp. 7-8; Tr. 191-94.

<sup>22</sup> CX-22, p.1; CX-24, p. 18; RX-8; Tr. 195-200.

Compliance Contact and not Ted M. Word. The AML written program does not contain a procedure for designating an AML Compliance Officer or for transmitting contact information to FINRA.<sup>23</sup>

d.) NASD Conduct Rule 3011(e) requires that firms provide ongoing AML training for appropriate personnel. Although CMG's AML Program provides that it will develop AML training under the direction of its AML Compliance Officer and will provide such training on at least an annual basis, no such training was conducted during 2003 or 2004.<sup>24</sup>

## 2. Failure to Apply for Approval of a Change in Business Operations

Membership and Registration Rule 1017(a) requires members to file an application for approval of, among other things, any material change in business operations, which includes such operations as underwriting. CMG's Membership Agreement specifically provided that, as a broker-dealer with a \$5,000 minimum net capital requirement, it was not permitted to participate in offerings of securities as an underwriter on other than a best efforts basis. CMG, acting through Baldwin, failed to file an application for approval of a material change in its business operations although it participated in a number of firm commitment underwritings which increased its minimum net capital requirement from \$5,000 to \$100,000.<sup>25</sup>

## 3. Unapproved and Deficient Communications with the Public

As part of her examination, Whitfield asked for, and was given, advertising and sales literature used by CMG during the period April 2003 to June 2005. None of that

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<sup>23</sup> CX-24; Tr. 200-01.

<sup>24</sup> CX-24, CX-18; Tr. 201-03.

<sup>25</sup> CX-49, CX-50, CX-51, CX-52; Tr. 52-61. The Membership Agreement states that "Any activity that does not conform to the provisions set forth in this Agreement may form the basis for disciplinary action by [FINRA] against CMG Institutional Trading, LLC, its owners, or associated persons." CX-49, p.3.

material had been reviewed and approved by initial and date, nor were there any other indicia of approval by a principal or FINRA. Much of the material was contained in a “flipbook” that was provided to Examiner Sularz, who also found it available on CMG’s website. The sales literature also included prepared reprints of articles that had appeared in magazines. Written or electronic communication that is generally distributed or made available to customers or the public is considered to be “sales literature” as defined in NASD Rule 2210(a) (2). The sales literature was misleading because it represented that Capital Management Group was a broker-dealer, as well as a member of NASD, the Chicago Stock Exchange, and SIPC; it was none of those. Baldwin also admitted that there were inaccuracies on pages 1, 22, 24, 27, 30, 33, and 34 of the “flipbook” in referring to Capital Management Group, rather than CMG Institutional Trading, LLC.<sup>26</sup> By disseminating advertising and sales literature that was false or misleading, or that had not been approved by a registered principal, CMG, acting through Baldwin, violated NASD Conduct Rules 2210 and 2110, as alleged in the Complaint.

#### 4. Failure to Create and Maintain a Business Continuity Plan

NASD Conduct Rule 3510 requires members to create and maintain a written business continuity plan that addresses procedures enabling the member to meet its existing obligations to customers during an emergency or significant business disruption. The Rule specifies a number of minimum requirements for any business continuity plan. CMG’s business continuity plan failed to address the following minimum requirements of the Rule:

- Data back-up and recovery;
- Mission critical systems;
- Financial and operational assessments;

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<sup>26</sup> CX-53-54; TR. 98-102, 226-28, 487-93.

Reporting to and communications with regulators;  
Alternate communications between the firm and its customers and employees;  
Alternate physical location of employees;  
Impact of a disruption upon critical counterparts;  
Customers' prompt access to funds and securities; and  
Designation of a principal to approve the plan and his/her responsibility for  
conducting the required annual review.

In its Wells response, dated September 11, 2006, CMG acknowledged the deficiencies and stated that it submitted a revised business continuity plan, following NASD templates.<sup>27</sup> By failing to create and maintain an adequate business continuity plan, CMG, acting through Baldwin, violated NASD Conduct Rules 3510 and 2110.

#### 5. Failure to Comply with Continuing Education Requirements

The Complaint alleges, and the evidence demonstrates that Baldwin's registration was inactive for a period of 35 days, from June 6, 2003 until July 10, 2003, because he failed to complete the Regulatory Element of NASD Membership and Registration Rule 1120. During that period of time, he continued to engage actively in CMG's securities business as its President, Chief Executive Officer, and Compliance Officer. By allowing him to do so, CMG violated NASD Rules 1120, 3010, and 2110, as alleged in the Complaint.<sup>28</sup>

### **C. Violations of MSRB Rules**

#### 1. Engaging in Municipal Securities Business Without A Qualified Municipal Securities Principal

From May 22, 2004, the day after its only municipal securities principal's registration with the Firm was terminated, through October 19, 2005, CMG had no municipal securities principal. Although the June 22, 2005 MSRB Primary Electronic

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<sup>27</sup> CX-25, CX 10; Tr. 204-09. RX-12 is the revised CMG business continuity plan. Page 9 provides for approval by a senior manager; however, that page is undated and unsigned.

<sup>28</sup> CX-2, CX-17, CX-18; Tr. 190.

Mail Contact Form G-40 states that Baldwin was a Series 53 or Series 51 registered municipal securities principal, he was never registered as either. During the period that CMG was without a registered municipal securities principal, CMG participated in two municipal securities offerings: (1) the City of Chicago O'Hare International Airport General Airport Third Lien Revenue Funding Bonds (primary offering statement dated November 9, 2004), and (2) the City of Detroit, Michigan, Taxable Certificates of Participation Series 2005 (offering circular dated May 25, 2005). By participating in those offerings without having a registered municipal securities principal, CMG, acting through Baldwin, violated MSRB Rule G-3, which requires such a principal.<sup>29</sup>

Related to its failure to have a registered municipal securities principal during the 17-month period noted above, CMG, acting through Baldwin, also violated MSRB Rule G-40, which requires that it appoint such a principal as the Primary Electronic Mail Contact with MSRB. After correspondence and discussion with FINRA staff about the failure to have a registered municipal securities principal, Baldwin, as CEO and President of CMG, notified MSRB that CMG was withdrawing from MSRB membership, effective October 19, 2005.<sup>30</sup>

## 2. Inadequate Written Supervisory Procedures

From approximately April 16, 2003 through June 20, 2005, CMG, acting through Baldwin, failed to establish, maintain, and enforce adequate written supervisory procedures to ensure compliance with MSRB Rules, as required by MSRB Rule G-27. During that period of time, CMG's Compliance Policy and Procedures Manual referred

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<sup>29</sup> CX-3, CX-4, CX-5, CX-11; Tr. 72-74. In their post-hearing submission, Respondents admit that CMG participated in one of those transactions, and, CX-13, p. 48, confirms that CMG participated as an underwriter in that transaction. However, CX-13, p. 49 lists CMG as an underwriter on the other as well.

<sup>30</sup> CX-9; CX-10, p. 3; CX-11. In their post-hearing submission, Respondents admit this violation.

only to the requirement that an MSRB investor brochure be sent to any customer who filed a complaint involving municipal securities. Otherwise, the Manual contained no procedures related to MSRB Rules, including, but not limited to, municipal underwriting, political contributions, record keeping, and transaction reporting.<sup>31</sup>

### 3. Failure to File a List of Issuers

MSRB Rule G-37 governs political contributions and prohibitions on municipal securities business. To provide for public scrutiny, the Rule provides, in pertinent part, that each dealer shall, by the last of the month following the end of each calendar quarter, send to the Board a list (on Form G-37/G-38) of issuers with which the broker, dealer, or municipal securities dealer has engaged in municipal securities business, along with the type of municipal securities business. CMG, acting through Baldwin, failed to timely file with the Board a list of issuers with which it had engaged in municipal securities business for the quarters ending March 31, 2003, December 31, 2003 and December 31, 2004. At the direction of Examiner Sularz, CMG eventually filed lists for those quarters on July 5, 2005, between 155 and 797 days late.<sup>32</sup>

### 4. Failure to Establish and Implement an AML Compliance Program

MSRB Rule G-41 provides that every broker, dealer and municipal securities dealer must establish and implement an AML compliance program reasonably designed to achieve and monitor compliance with the requirements of the Bank Secrecy Act. An AML compliance program that is in compliance with NASD Rules is deemed to be in

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<sup>31</sup> CX-16, p. 51; Tr. 92-94, 142.

<sup>32</sup> CX-10, CX-13, CX-14, CX-15; Tr. 81-86, 95-96. Although, on the cover sheets of the issues, Capital Management Group Securities is listed as an underwriter, as discussed in n.11, the Extended Hearing Panel concludes that the name Capital Management Group Securities was used interchangeably with CMG Institutional Trading, LLC. CX-13, pp. 8-9, contains trade tickets for the City of Chicago bonds, showing the trader as Rick Barfield, an employee of CMG Institutional Trading, LLC. Tr. 90.



compliance with the Bank Secrecy Act for purposes of Rule G-41. As noted earlier, Examiner Whitfield reviewed CMG's written AML Compliance Program and found, on the basis of four deficiencies in the program, that it did not comply with the requirements of NASD Rule 3011. Accordingly, the deficiencies in CMG's AML Compliance Program constitute violations of MSRB Rule G-41 by CMG, acting through Baldwin.

#### **IV. Sanctions**

As set forth below, the Hearing Panel determined the sanctions that it would impose for each violation. However, giving consideration to the cumulative effect of the number and extent of the violations, the Hearing Panel determined instead to impose a single overall sanction for each Respondent: CMG will be expelled, and Baldwin will be barred in any and all capacities.

##### **A. Financial and Accounting Violations**

For two and one-half years, CMG operated without having a registered FINOP. During that time, the Firm, acting through Baldwin, (1) failed to maintain its minimum net capital requirement; and (2) failed to prepare accurate books and records by misclassifying a \$190,000 deposit as an infusion of capital, understating its expenses, and failing to account for checks that had not cleared. Following that time period, it failed to timely file its Annual Audit Report for the year ending December 31, 2005, or its Quarterly FOCUS Report for the first quarter of 2007.

For registration violations, the FINRA Sanction Guideline recommends a fine ranging from \$2,500 to \$50,000, and, in egregious cases, a suspension of the firm for up to 30 business days and a suspension of an individual for up to two years or a bar.<sup>33</sup> For net capital violations, the Guideline recommends a fine ranging from \$1,000 to \$50,000,

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<sup>33</sup> FINRA SANCTION GUIDELINES, at 48.

and a suspension of the firm and the responsible individual for up to 30 business days.<sup>34</sup> The Sanction Guideline for recordkeeping violations calls for a fine ranging from \$1,000 to \$10,000, and, in egregious cases, from \$10,000 to \$100,000. That Guideline also recommends a suspension of the firm and the responsible principal for up to 30 business days or, in egregious cases, a suspension of up to two years or expulsion of the firm and a suspension of the responsible individual for up to two years or a bar.<sup>35</sup> For late filing of FOCUS Reports, the Guideline recommends a fine ranging from \$1,000 to \$20,000 and, in egregious cases, a suspension of the firm for up to 20 business days and a suspension of the responsible individual for up to 10 business days.<sup>36</sup>

For these violations combined, Enforcement recommends that CMG be suspended for a period of six months; that Baldwin be barred in all principal capacities and suspended in any or all capacities for two years and four months; and that CMG and Baldwin be fined \$75,000 jointly and severally. The Extended Hearing Panel agrees that the sanctions recommended by Enforcement would be appropriate for those violations. CMG was without a registered FINOP for an extended period of time and continued to operate without one even after Examiner Sularz repeatedly asked the Firm and Baldwin for the name of the person who would be registered as FINOP and when that person would be registered. The necessity for a registered FINOP is made clear by the violations that occurred in the absence of one.<sup>37</sup> The net capital rule “is one of the most important tools that the SEC and [FINRA] use to protect investors because it imposes financial

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<sup>34</sup> *Id.*, at 29.

<sup>35</sup> *Id.*, at 30.

<sup>36</sup> *Id.*, at 72. While there is no specific Guideline for late filing of an Annual Audit Report, the Extended Hearing Panel will look to the analogous Guideline for late filing of a FOCUS Report.

<sup>37</sup> One of the Guidelines’ Principal Considerations in Determining Sanctions is whether the respondent engaged in numerous acts and/or a pattern of misconduct. *Id.*, at 6.

responsibility on the securities industry by: (1) establishing minimum net capital requirements for broker-dealers; and (2) defining the process used by broker-dealers to determine their net capital at all times.”<sup>38</sup> Although the net capital deficiency occurred on only one day, the deficiency exceeded \$2.2 million and followed, by less than three months, the manipulative deposit of \$190,000 as capital, of which \$185,000 was withdrawn the next business day. Moreover, the net capital computation as of the end of the month following the net capital deficiency was also inaccurate because the Respondents failed to book expenses or checks that had not yet cleared. As its certified public accountant noted, “Management has elected to omit substantially all of the disclosures and statements of cash flows required by generally accepted accounting principles.” Finally, the financial violations continued into 2006 and 2007 when the Annual Audit Report was filed 145 days late, and the quarterly FOCUS report was filed 29 days late.

#### **B. Violations of NASD Rules**

CMG and Baldwin failed to develop and implement an adequate written AML compliance program, failed to apply for approval of a change in business operations, disseminated advertising and sales literature that was inaccurate and unapproved by a principal of the firm, failed to create and maintain a Business Continuity Plan, and failed to comply with continuing education requirements.

Because there is no specific Guideline for violations of the AML Rules, the Extended Hearing Panel considered the Guideline for deficient supervisory procedures

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<sup>38</sup> *Dep’t. of Enforcement v. Inv. Mgmt. Corp. and Kevin Kunz*, No. C3A010045, 2003 NASD Discip. LEXIS 47, at \*14 (NAC Dec. 15, 2003).

which recommends a fine ranging from \$1,000 to \$25,000.<sup>39</sup> There is no evidence that the deficiencies allowed any violative conduct to occur or escape detection. Accordingly, while the Extended Hearing Panel does not find the violation to be egregious, it finds that, because there was no verification of customer identification information, no annual independent testing, no training for appropriate personnel, and no designation and identification to FINRA of the individual(s) responsible for the AML Program, the violation was serious. Enforcement recommends a fine of \$5,000; however, the Extended Hearing Panel finds that a mid-range fine of \$10,000 would be appropriate under the circumstances.

CMG and Baldwin failed to abide by CMG's Membership Agreement and failed to request a change in that Agreement to allow CMG to participate in firm commitment underwritings that raised its minimum net capital requirement from \$5,000 to \$100,000. The Sanction Guideline for member agreement violations recommends a fine ranging from \$2,500 to \$50,000. In cases involving a serious breach of the agreement, the Guideline suggests a suspension of the firm and the responsible individual for up to two years. In egregious cases, consideration should be given to expelling the firm and/or barring the responsible individual.<sup>40</sup> Enforcement characterizes the violation as serious; it requests that the Firm and Baldwin be suspended in all capacities for one month, and that they be fined \$20,000 jointly and severally. The Extended Hearing Panel, however, finds the violation to be egregious. As noted previously, a \$5,000 broker-dealer cannot participate in a firm commitment underwriting, even if its participation is riskless. Here, the Firm participated in a firm commitment underwriting when (1) it had no registered

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<sup>39</sup> FINRA SANCTION GUIDELINES, at 109.

<sup>40</sup> *Id.*, at 47.

FINOP, who might have prevented the violation of the Membership Agreement and ensured compliance with increased net capital requirements, and, (2) based on the value of the securities it was firmly committed to purchase as an underwriter, the Firm's net capital was deficient by more than \$2.2 million. Accordingly, the Extended Hearing Panel would expel the Firm and bar Baldwin in all capacities for the violation.

CMG and Baldwin maintained a website that contained inaccurate and misleading information about the Firm and failed to evidence supervisory approval of sales literature. The inaccuracies included the identification of an unregistered entity as a broker-dealer. The website was available to the public, but there was no evidence of the breadth of any sales literature circulation. The Sanction Guideline for such violations calls for a fine ranging from \$1,000 to \$20,000 and, in egregious cases, a suspension of the Firm for up to one year and a suspension of the responsible person for up to 60 days.<sup>41</sup> Enforcement does not assert that the violations are egregious; rather it requests, and the Extended Hearing Panel finds, a mid-range fine of \$10,000, jointly and severally, for the violations would be appropriate.

CMG and Baldwin failed to create and maintain a written business continuity plan that would enable them to meet its obligations to customers during an emergency or significant business disruption. There is no Sanction Guideline for such a violation. However, the Extended Hearing Panel finds that the absence of a plan by which customers would have access to their funds during an emergency or business disruption exposes those customers to potential risk or loss similar to that which the Customer Protection Rule<sup>42</sup> seeks to prevent. The Sanction Guideline for failure to comply with the

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<sup>41</sup> *Id.*, at 84.

<sup>42</sup> SEC Rule 15c3-3.

Customer Protection Rule recommends a fine ranging from \$1,000 to \$50,000 and a suspension of up to 30 business days.<sup>43</sup> The Firm did submit a revised business continuity plan that followed NASD templates. Accordingly, Enforcement requests, and the Extended Hearing Panel finds appropriate, a fine of \$5,000, jointly and severally, to remediate the violation.

Baldwin, who, as noted, was the President, CEO, and Chief Compliance Officer of CMG, acknowledged that he was non-compliant with his continuing education requirements for a period of 35 days. In their post-hearing submission, Respondents also admit that four other employees were non-compliant, although they assert that the four employees did not engage in commissionable activity. The Sanction Guideline for failure to comply with the Regulatory Element of the Continuing Education Rules calls for a fine for an individual ranging from \$1,000 to \$5,000, and for a firm, from \$2,500 to \$20,000. In cases of intentional conduct by an individual, the Guideline recommends a suspension for 30 or more days (up to two years) or consideration of a bar. Where a firm has taken no corrective action and appears unwilling to comply, the Guideline recommends consideration of a suspension for up to five business days; where the firm knowingly allowed a person to act in a registered capacity with a lapsed registration, consideration should be given to suspending the firm for up to two years or expelling the firm, and barring the responsible principal.<sup>44</sup> Enforcement requests a \$10,000 fine, jointly and severally, and a suspension of the Firm and Baldwin for one month. However, the principal considerations for this violation are the nature and extent of the responsibilities of the inactive person, and whether the respondent knowingly functioned with inactive

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<sup>43</sup> FINRA SANCTION GUIDELINES, at 28.

<sup>44</sup> *Id.*, at 45.

registration or allowed an individual to so act. Baldwin was not only the President and CEO of CMG, he was the Chief Compliance Officer upon whom the full responsibility for compliance rested. He knowingly functioned in a registered capacity for more than a month while his registration had lapsed, and the Firm, through him, allowed him to so function. Under the circumstances, the Extended Hearing Panel finds a fine of \$2,500 and a suspension in any and all capacities for two months for Baldwin, and a fine of \$10,000 and a suspension for two months for CMG would be appropriate.

### **C. Violations of MSRB Rules**

CMG, through Baldwin, violated five MSRB Rules by four courses of conduct: (1) engaging in municipal securities business without a qualified municipal securities principal, in violation of MSRB Rules G-3 and G-40; (2) failing to establish, maintain, and enforce adequate written supervisory procedures, in violation of MSRB Rule G-27; (3) failing to timely file a list of issuers with which they did business, in violation of MSRB Rule G-37; and (4) failing to establish and maintain an AML Compliance Program, in violation of MSRB Rule G-41.

As noted above, for registration violations, the FINRA Sanction Guideline recommends a fine ranging from \$2,500 to \$50,000, and, in egregious cases, a suspension of the firm for up to 30 business days and a suspension of an individual for up to two years or a bar.<sup>45</sup> Not only did CMG engage in municipal securities business without having a registered municipal securities principal, but Baldwin was identified on Form G-40 as a municipal securities principal when he never attained that designation. Accordingly, the Extended Hearing Panel finds that the appropriate sanctions for the

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<sup>45</sup> FINRA SANCTION GUIDELINES, at 48.

violations would be a \$25,000 fine, jointly and severally, and a suspension of the Firm for 30 business days, and a bar in all principal capacities for Baldwin.

The Sanction Guideline for deficient supervisory procedures recommends a fine ranging from \$1,000 to \$25,000, and, in egregious cases, consideration of a suspension of the responsible individual for up to one year and the firm for up to 30 business days.<sup>46</sup> A principal consideration is whether the deficiencies made it difficult to determine who was responsible for specific areas of supervision or compliance. Here, in the absence of any procedures (other than requiring that an investor brochure be sent to any complaining customer), it was impossible to determine who was responsible for any area of supervision or compliance. The Extended Hearing Panel finds the violation to be egregious and warrants a fine of \$25,000, jointly and severally, a suspension of CMG for 30 business days, and a suspension of Baldwin in all principal capacities for one year.

The Sanction Guideline for late filing of MSRB reports calls for a fine ranging from \$5,000 to \$10,000, with consideration of imposing a fine on a per violation basis. In egregious cases, the Sanction Guideline recommends consideration of suspending the firm from engaging in municipal securities underwriting for up to 30 business days, and suspending the responsible individual in any or all capacities for up to 30 business days. Based on the fact that CMG and Baldwin filed four reports late and that the delays ranged from 155 to 797 days, Enforcement requests a fine of \$20,000 (\$5,000 per violation), jointly and severally. The Extended Hearing Panel agrees with that recommendation.

The failure to establish and maintain an AML Compliance Program violates both MSRB Rule G-41 and, as described previously, NASD Rule 3011. However, if the Hearing Panel were imposing separate sanctions for violation of NASD Rule 3011,

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<sup>46</sup> *Id.*, at 109.



because there is a single course of conduct that violates both Rules, it would not impose additional sanctions for the violation of MSRB Rule G-41.

#### **D. Sanctions Conclusion**

In its post-hearing submission, Enforcement summarizes its sanctions requests and recommends that, in the aggregate, (1) Baldwin be barred in all principal capacities, and suspended for two years and six months in all capacities; (2) CMG be suspended in all capacities for seven months; and (3) Baldwin and CMG be fined \$170,000, jointly and severally. However, the Extended Hearing Panel notes that the violations were numerous and egregious; they occurred over almost two years in the face of repeated notification and inquiry from the Staff. The Respondents do not acknowledge or accept responsibility for any violations except the failure to notify the MSRB of CMG's primary electronic mail contact, its failure to abide by Continuing Education requirements, its untimely filing of an Annual Audit Report, and its engaging in securities related activities without employing a registered FINOP which, they claim, they did not do "knowingly." Upon consideration of the entire record, the Extended Hearing Panel concludes that CMG and Baldwin have demonstrated that they are unable and unwilling to conform their conduct to the requirements of the securities laws and regulations. Accordingly, rather than aggregating and imposing the individual sanctions set forth above, the Hearing Panel will impose a single, unitary sanction on each Respondent in order to protect the investing public. CMG will be expelled from FINRA membership and Baldwin will be barred from associating with any FINRA member in any capacity for the violations alleged in the 14-cause Complaint.

## V. Conclusion

Respondent CMG Institutional Trading, LLC is expelled from FINRA membership and Respondent Shawn D. Baldwin is barred from associating with any FINRA member in any capacity for violating NASD Rules 1017, 1022, 1120, 2110, 2210, 3010, 3011, 3110, 3510; SEC Rules 15c3-1, 17a-3, and 17a-5; and MSRB Rules G-3, G-27, G-37, G-40, and G-41. In light of the expulsion and bar, no fines will be imposed. However, CMG and Baldwin will be assessed costs, jointly and severally, in the amount of \$2,573.44, consisting of a \$750 administrative fee and a \$1,823.44 transcript fee. The expulsion and bar shall become effective immediately if this Decision becomes the final disciplinary action of FINRA.

**SO ORDERED.**

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Alan W. Heifetz  
Hearing Officer  
For the Extended Hearing Panel

Copies to:

Shawn Baldwin (*via overnight courier & first class mail*)  
CMG Institutional Trading, LLC (*via first class mail*)  
Nichole C. Patton, Esq. (*via facsimile & first class mail*)  
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