

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

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

WILFREDO FELIX
(CRD No. 2693672)

and

PRIMEX PRIME ELECTRONIC
EXECUTION, INC. d/b/a PRIMEX
(CRD No. 29394),

Respondents.

Disciplinary Proceeding
No. 2018058286901

Hearing Officer—MJD

**EXTENDED HEARING
PANEL DECISION**

July 1, 2020

Respondent Wilfredo Felix is barred in all capacities for failing to provide a personal tax-related document during the investigation of this matter.

Felix and Primex made and preserved inaccurate and false expense records, causing Primex to maintain an inaccurate general ledger and file inaccurate quarterly FOCUS Reports. Primex also responded to a FINRA request for information and documents in an untimely manner. For this misconduct, the firm is censured and fined \$40,000. In light of the bar, no additional sanctions are imposed against Felix for the books and records violations.

Enforcement failed to prove that Felix provided false or misleading information and testimony during the investigation. Those charges are therefore dismissed.

Appearances

For the Complainant: Michael J. Newman, Esq., Gabrielle G. Hirz, Esq., Jeff Fauci, Esq., and Lisa M. Colone, Esq., Department of Enforcement, Financial Industry Regulatory Authority

For the Respondents: John K. Wells, Esq.

DECISION

I. Introduction

FINRA's Department of Enforcement filed a six-cause Complaint against Respondents Primex Prime Electronic Execution, Inc. ("Primex" or the "Firm") and the Firm's sole owner, chief executive officer, and financial and operations principal ("FINOP"), Wilfredo Felix ("Felix"). The central allegation is that, from 2013 to 2015 (the relevant period), Felix misclassified hundreds of thousands of dollars in personal expenses as Firm business expenses on the Firm's general ledger, causing Primex to have inaccurate books and records and to file inaccurate quarterly Financial and Operational Combined Uniform Single ("FOCUS") Reports. Primex's outside auditor required Respondents to reclassify as compensation certain 2014 and 2015 expenses that the auditor had determined were personal.

Cause one of the Complaint charges Felix with violating FINRA Rule 2010 by making false expense entries in Primex's books and records. Specifically, cause one alleges that Felix recorded hundreds of personal expenses as Firm business expenses on the general ledger. Cause two charges Felix and Primex with violating FINRA Rules 4511 and 2010 by failing to make and preserve accurate books and records as a result of Felix's false expense entries, and failing to file accurate FOCUS Reports. Cause two also charges Primex with willfully violating Section 17(a) of the Securities Exchange Act of 1934 ("Exchange Act") and Exchange Act Rules 17a-3 and 17a-5.

Causes three through six of the Complaint charge Felix and Primex with violating FINRA Rules 8210 and 2010. Cause three alleges that the Firm responded in an untimely manner—more than three months late—to a request for information and documents related to expenses Felix entered in the general ledger. Causes four and five charge Felix with giving FINRA staff false or misleading information—first in writing, and again a few months later at an on-the-record interview ("OTR")—about why the Firm's auditor required that his personal expenses be reclassified as compensation. Cause five further charges that Felix gave false testimony during an OTR by stating that Primex's auditor was responsible for preparing two slightly different versions of his personal 2013 Internal Revenue Service ("IRS") Form 1099-MISC ("1099") to report his Primex compensation. Cause six charges Felix with failing to produce a copy of his 2013 IRS Wage and Income Transcript ("IRS Transcript"), which he could have obtained by submitting IRS Form 4506-T (Request for Transcript of Tax Return) to the IRS.

Respondents filed separate Answers denying the allegations and requesting a hearing.¹ They claim that Felix did not intentionally misclassify personal expenses as Firm business expenses or try to conceal them. They argue that the expenses at issue were reflected on

¹ A five-day hearing took place in New York, New York, beginning January 9, 2020. In addition to Felix, Enforcement called Primex's outside auditor, a FINRA investigator, and a FINRA examination manager to testify. Felix also testified in Respondents' case.

Primex's general ledger and could be reviewed by regulators. Respondents say that Felix recorded expenses on the general ledger as he reasonably believed they should have been entered, but they also concede in their Answers that, on occasion, Felix inadvertently used the wrong debit card when paying for personal items.

Respondents acknowledge that the Firm's auditor directed the Firm to reclassify certain expenses in 2014 and 2015 as distributions, or compensation, to Felix, rather than as Firm business expenses. Respondents argue that Felix reluctantly agreed to the auditor's reclassifications, rather than argue over each expense, to avoid subjecting Primex to penalties for filing the annual audit late.² Primex concedes that it responded late to one of FINRA's requests for information but states that the tardiness was excusable under the circumstances. Felix denies giving false or misleading information to FINRA and disputes that Rule 8210 obligates him to produce his IRS Transcript or sign a form to get a copy.

A majority of the Extended Hearing Panel finds that, by failing to produce a copy of his IRS Transcript, Felix violated FINRA Rules 8210 and 2010, as alleged in cause six. For this misconduct, the majority bars Felix from associating with any member firm in any capacity.³

The Panel finds that Felix violated FINRA Rule 2010, as alleged in cause one, by misrepresenting his personal expenses as business expenses on Firm records. The Panel finds that Enforcement proved by a preponderance of the evidence that Respondents improperly classified \$248,893 in personal expenses, but not \$437,654, as Enforcement charges. Respondents violated FINRA Rules 4511 and 2010, and Primex willfully violated Section 17(a) of the Exchange Act and Exchange Act Rules 17a-3 and 17a-5 by making and preserving inaccurate Firm books and records and filing inaccurate FOCUS Reports, as alleged in cause two.

We censure and fine Primex \$25,000 for books and records violations and for filing inaccurate FOCUS Reports. The firm is also censured and fined \$15,000 for its untimely response to FINRA staff's request for information, as alleged in cause three.⁴

² Answer of Respondent Primex ("Primex Ans.") 3-4; Answer of Respondent Wilfredo Felix ("Felix Ans.") 3-4. Respondents' Answers did not differ materially.

³ One panelist dissents from the majority's findings that Felix violated Rules 8210 and 2010, as alleged in cause six. With respect to causes four and five, the Panel finds that Enforcement failed to meet its burden of proof that Felix violated FINRA Rules 8210 and 2010. We accordingly dismiss causes of action four and five.

⁴ In light of the bar we impose for misconduct under cause six, we do not impose additional sanctions on Felix for misconduct under causes one and two. Had we not barred Felix under cause six, for the misconduct alleged in causes one and two we would fine Felix \$25,000, suspend him for 30 business days as a FINOP and thereafter until such time as he requalifies as a FINOP.

II. Findings of Fact

A. Background of Respondents

1. Felix

Felix first became registered with a FINRA member firm in 1995. In 2001, he purchased Primex. Felix is the sole shareholder of Primex, which he owns through its parent company, Advantage Trading LLC (“Advantage Trading”). Advantage Trading is a passive holding company with no business activity.⁵

During the relevant period, Felix was Primex’s chief executive officer, chief financial officer, and chief compliance officer. He was registered with the Firm as a general securities principal, introducing broker-dealer FINOP, operations professional, and corporate securities representative.⁶

As the Firm’s FINOP, Felix was the only person at Primex who made entries in the Firm’s general ledger and prepared and submitted FOCUS Reports. He was also the only person with signatory authority over Primex’s bank account and the only person who had a debit card associated with the account. Felix did not maintain bank accounts in his own name because he “didn’t trust the banking system.”⁷

Felix had no formal compensation agreement with Primex during the relevant period. He testified that he determined what to compensate himself each month based on the level of Firm revenues.⁸ At the time of the hearing, Felix had not filed personal income tax returns at least since 2013 because of a “personal preference.” He explained that he “would rather not file [a] tax

⁵ Hearing Transcript (“Tr.”) 811-12, 1098; Joint Exhibit (“JX-”) 13. Felix bought Primex with two other persons. He became Primex’s sole owner in 2003 when he bought out the other two persons. Tr. 1103-07. Felix also used an Advantage Trading bank account for personal expenses. Tr. 813, 940, 1536-37.

⁶ Complaint (“Compl.”) ¶ 8; Felix Ans. ¶ 8; Primex Ans. ¶ 8; Tr. 794-95, 803, 811-12, 1098, 1117-18; JX-1, at 6-7; JX-2, at 4-16. Felix also has his own retail clients. Tr. 1112-13, 1529-30.

⁷ Compl. ¶ 8; Felix Ans. ¶ 8; Primex Ans. ¶ 8; Tr. 814. Felix cited the 1907 banking crisis in the United States as a reason he did not maintain a personal bank account. “I watch the banking system,” Felix testified, and he predicted that “we are going to have some problems with the economy [in the] third quarter” of 2021. Tr. 815. At the time of the hearing, Felix still had no personal bank account. Tr. 816. Felix’s wife did not have a bank account either. Tr. 808.

⁸ Compl. ¶¶ 8, 12; Felix Ans. ¶¶ 8, 12; Primex Ans. ¶¶ 8, 12; Tr. 807-08, 1208-09.

[return] and take the penalty for not filing it, rather than file a false tax return.”⁹ Felix is married and has four children, three of whom were between approximately three and 12 years old at the beginning of the relevant period.¹⁰

FINRA has jurisdiction over Felix because he was registered with FINRA when the Complaint was filed and is charged with committing misconduct while registered.

2. Primex

Primex became a FINRA member in 1992. Between 2013 and 2015, it had approximately 30 registered representatives and operated five branch offices. At the time of the hearing, it had 14 registered representatives and operated out of two branch offices.¹¹ During most of the relevant period, Primex’s principal office was located in Elmsford, New York. In approximately September 2015, Felix relocated the office to New York City.¹² During the relevant period, the Firm sold equities, bonds, mutual funds, and variable annuities to retail customers, but a majority of the Firm’s business consisted of facilitating its customers’ exchanges of investment property pursuant to Section 1031 of the Internal Revenue Code to lawfully defer payment of capital gains taxes.¹³ During the first decade that Felix owned the Firm, Primex was not very profitable. As a result, Felix invested Firm revenues into the operations of the Firm.¹⁴ By approximately 2010, Primex’s revenues started to increase. It had revenues of nearly \$1.1 million in 2013, \$1.8 million in 2014, and \$3.5 million in 2015.¹⁵

⁹ Tr. 792-94, 1122. *See also* JX-43, at 16. Felix testified that he paid no taxes for tax years 2013 through 2015. He believes he had a personal loss carry forward that would minimize his taxes for those years. Tr. 794, 813-14, 1123-24. He also testified that he has income from sources in Russia and China from developing game applications, so he has “to make sure [he] report[s] all that information and tax deductions” and is “waiting for the correct information and verified information so [he] could properly file.” Tr. 1122-23. Felix testified that he has outside business activities, including an online retailer, and has developed or owns 50 computer or cellphone applications. He also owns 40 registered trademarks, three patents, and 500 Internet domains. Most of these ventures, Felix testified, are not profitable. Tr. 1119-23, 1530-31.

¹⁰ Tr. 1525-26. The fourth child was 19 years old at the beginning of the relevant period.

¹¹ Compl. ¶ 10; Felix Ans. ¶ 10; Primex Ans. ¶ 10; Tr. 1108-09.

¹² Tr. 1109-11, 1128-29, 1316; JX-1, at 3.

¹³ Tr. 1111, 1528. Felix estimated that, during 2013, 2014, and 2015, 60 percent of the Firm’s business involved facilitating Section 1031 exchanges and 40 percent involved transactions in stocks and bonds with retail customers. Tr. 1527-30. Under the Internal Revenue Code Section 1031, a taxpayer is generally not required to recognize a gain or loss in a transaction involving an exchange of one business or investment property for another business or investment property of the same nature or character. *See* <https://www.irs.gov/businesses/small-businesses-self-employed/like-kind-exchanges-real-estate-tax-tips>.

¹⁴ Tr. 1176-77.

¹⁵ JX-132, at 5; JX-133, at 2; JX-167, at 5.

FINRA has jurisdiction over Primex because the Firm was registered with FINRA when the Complaint was filed and is charged with committing misconduct while it was registered.

B. Origin of Proceeding

FINRA began a cycle examination of Primex in early 2015 covering the period between September 2013 and March 2015. FINRA staff saw entries on the Firm's general ledger that it suspected were Felix's personal expenses. Such entries could be improper, FINRA's exam manager testified, if Felix had the Firm pay for his personal expenses without recording or classifying them as disbursements or compensation to himself.¹⁶ FINRA staff was concerned that Felix was using Firm funds to pay his personal expenses as a means of avoiding personal tax liability.¹⁷ The examiners asked for the Firm's bank records and copies of invoices, sales receipts, and other evidence to determine if the expenses Felix had incurred between 2013 and 2015 were in fact Firm business expenses.¹⁸

C. Primex's Outside Auditor

Primex's outside auditor ("CPA"), a certified public accountant who owns and operates his own accounting firm, conducted the Firm's annual audits from 2002, one year after Felix acquired the Firm, until 2016. CPA has audited broker-dealers for more than 40 years. During the relevant period, CPA audited about 60 FINRA-registered broker-dealers each year.¹⁹ CPA also provided tax preparation services for Primex, but never for Felix individually.²⁰

CPA dealt primarily with Felix to perform the Firm's audits. According to CPA, they had "a good relationship."²¹ Felix testified that he had a "great, great relationship" with CPA until about 2019. He trusted CPA's judgment and considered him a "father figure."²²

As Primex's revenues grew, CPA noticed that Felix's personal spending began to increase.²³ In early 2014, CPA suggested to Felix that he change Primex's tax filing status from a

¹⁶ Tr. 352, 357, 376-77. The cycle examination resulted in a referral to Enforcement in April 2016. JX-182, at 4.

¹⁷ Tr. 363-64, 375, 381.

¹⁸ Tr. 352-57, 363-65, 374-76; JX-14; JX-15; JX-18.

¹⁹ Tr. 78, 83, 1156; Respondents' Exhibit ("RX-") 3.

²⁰ Tr. 1159. *See, e.g.*, JX-132; JX-133; RX-4.

²¹ Tr. 83-86.

²² Tr. 816-17, 920.

²³ Tr. 86-87.

C Corporation to an S Corporation effective January 1, 2014. Felix agreed.²⁴ The switch in tax status did not change how Primex was supposed to record business expenses, according to CPA.²⁵ The expense reclassifications CPA required had nothing to do with Primex's change in tax status from a C Corporation to an S Corporation.²⁶

In early March 2015, after completing the 2014 audit, CPA wrote Felix that he could no longer perform Primex's audits because of the amount of work involved in examining Felix's expenses. At the hearing, CPA explained that he thought Felix's explanations about the business purpose of certain expenses were not "plausible."²⁷ But CPA later reconsidered and agreed to perform the 2015 and 2016 audits.²⁸

D. Classifications of Felix's Expenses

CPA performed the 2014 and 2015 audits immediately after the end of each year and had multiple communications with Felix about his expenses. He required Respondents to reclassify \$174,066 for 2014 and \$140,492 for 2015 as distributions to Felix when he conducted Primex's audits for those years. Primex adopted CPA's calculations in its general ledger and filed amended FOCUS Reports for the fourth quarters of 2014 and 2015 to correct the purported misclassifications.

Enforcement relied on CPA's calculations for 2014 and 2015 as the amounts Respondents wrongly classified in those years. Enforcement's investigator testified that he relied on CPA's work because CPA performed the audits immediately after the end of each fiscal year and had discussions with Felix about the charges. Also, Primex had adopted CPA's calculations, incorporated them into its general ledger, and filed amended FOCUS Reports for the fourth quarters of 2014 and 2015 to correct the purported misclassifications. Enforcement's investigator testified that he did not see any utility in making adjustments to CPA's conclusions.²⁹

²⁴ Tr. 88-89, 93, 1205-07; JX-112; JX-133, at 10-12; RX-17 at 243, 245, 251, 253. CPA testified that he recommended Primex switch its tax status because the Firm no longer had a net operating loss carry forward. Pursuant to Internal Revenue Code Sections 1363 and 1366, an S Corporation, rather than paying income tax itself, passes its income through to its shareholders, who report their pro rata share of the corporation's income or loss on their individual income tax returns. Therefore, as an S Corporation beginning with tax year 2014, all of Primex's losses or profits would flow through to Felix as its sole owner. *See* Tr. 88-89; JX-112.

²⁵ Tr. 89-90.

²⁶ Tr. 170, 175-76.

²⁷ Tr. 161, 824, 1382; JX-129, at 1.

²⁸ Tr. 83. CPA testified that he agreed to do the 2015 audit after Felix gave him assurances that his recordkeeping would improve. Tr. 164-65. CPA testified that he decided to stop conducting audits for Primex after 2016 because Felix had not improved the state of the Firm's books and records, and Felix delivered needed materials to perform the audits late, causing CPA to adjust the Firm's financial filings many times. Tr. 87-88. After 2016, CPA continued to provide limited accounting services to Primex until 2019. Tr. 824, 1159-60.

²⁹ Tr. 643-44, 661-62, 743.

For 2014, Enforcement sorted Felix's personal spending into general categories. It calculated that, of the \$174,066 in expenses that CPA had Respondents reclassify, \$64,000 in cash was withdrawn by Felix using ATMs or counter withdrawals at a bank using a Firm check. He spent more than \$33,000 at general retailers (such as Amazon, Costco, J.C. Penney, Macy's, Marshalls, Sears, Target, and Walmart); \$17,700 at clothing or shoe stores; \$11,300 for entertainment (including Chuck E. Cheese, Disney Store, Luna Park, Sesame Place, and movie theatres); \$7,144 for furniture (at Wayfair and Ikea, for example); and another \$5,626 for medical and pharmacy expenses.³⁰ He also spent more than \$13,800 in loan repayments and \$5,571 for car insurance and related charges. Felix spent lesser amounts on other categories of expenses during 2014—from \$336 to \$1,762—on food, toys, cosmetics, tuition, dry cleaners, fitness, and pets, for example.³¹

For 2015, based on Enforcement's calculations, the \$140,492 in expenses that CPA had Respondents reclassify included Felix's withdrawal of more than \$19,000 in cash from ATMs. Enforcement also estimated that Felix spent \$30,618 at general retailers; \$15,168 for travel; more than \$13,060 on furniture; \$7,432 at clothing stores; nearly \$7,000 for entertainment; more than \$7,000 at hardware stores (mostly at Home Depot); more than \$8,500 at Amazon Marketplace and PayPal; and \$4,570 on electronics (primarily at Best Buy).³² Felix spent nearly \$3,000 on pharmaceutical and medical services in 2015. Enforcement also identified spending in smaller amounts that ranged from \$353 for pet care to \$2,483 for fitness or sporting goods. Felix also charged nearly \$1,100 on food and more than \$1,600 on his children's tuition to Primex's bank account, in excess of \$900 on cleaning services, and more than \$1,000 for cosmetics and personal grooming items.³³

Enforcement also alleges that Respondents had engaged in similar misconduct in 2013, even though CPA did not require Primex to reclassify Felix's expenses for that year.³⁴ Enforcement generally applied the methodology CPA used in his 2014 and 2015 audits to its review of Felix's 2013 expenses. After reviewing the different sorts of expenses, including vendors, associated with CPA's 2014 and 2015 reclassifications, Enforcement calculated that in 2013 Felix had spent \$123,096 on personal expenses using Firm funds that he incorrectly classified as business expenses on Primex's general ledger.³⁵

³⁰ Complainant's Exhibit ("CX-_") 2, at 1, 17-30. Enforcement relied in part on Felix's classifications or descriptions of expenses in a response to a request for information made under Rule 8210. *See* Tr. 637-38; JX-38, at 61-72.

³¹ CX-2, at 1, 17-30.

³² CX-3, at 1, 17-31.

³³ CX-3, at 1, 17-31.

³⁴ In 2013, CPA adjusted Primex's financials but the corrections did not involve reclassifying Felix's expenses. *See* Tr. 104-07; JX-115. CPA asked for supporting documentation for certain 2013 expenses, the largest of which involved property improvements that exceeded \$2,000. Tr. 112-14; JX-112; JX-113.

³⁵ CX-1, at 1.

Based on a careful review of the documentary evidence and testimony, the Panel finds that Enforcement failed to prove that \$437,654 in allegedly misclassified personal expenses from 2013 to 2015 were incorrectly recorded as business expenses in Primex's books and records. Instead, we find that Felix misclassified a total of \$248,893. We set forth below in detail our findings as to these expenses. In making these determinations, the Panel carefully considered witness testimony, together with the available documents, and the parties' arguments about the expenses.

We first discuss the expense reclassifications CPA required for the 2014 and 2015 audits. We then discuss the calculations Enforcement performed that led to the 2013 allegations. Lastly, we provide the Panel's findings concerning Felix's expenses.

1. CPA's 2014 Audit

CPA began working on Primex's 2014 audit in early 2015.³⁶ CPA noticed that entries were recorded on the general ledger as property or leasehold improvements and, in particular, as "miscellaneous expenses," that he thought were "inordinately high" for a small firm.³⁷ When CPA saw what he thought were personal expenses, he decided "to look at everything," including Primex's monthly bank statements.³⁸

On February 28, 2015, as the filing deadline was approaching, CPA emailed Felix asking for corroboration that certain items identified in the general ledger as "miscellaneous expenses" were in fact for the Firm.³⁹ CPA was concerned that the expenses could have been personal. Felix does not dispute that he charged personal expenses to Primex. He testified that he recorded

³⁶ During the audits before 2014, CPA did not question whether any expenses were wrongly recorded as business expenses. CPA took a closer look at Primex's expenses in the 2014 audit because of new standards that were imposed on broker-dealer audits during the year. In anticipation of conducting the 2014 audit, CPA wrote Felix on November 25, 2014 that 2014 was "a transitional year for [broker-dealer] audits as the audits convert to PCAOB standards." JX-122, at 2; RX-17, at 414. Beginning in 2014, PCAOB accounting standards applied to registered broker-dealers in addition to public companies. CPA testified that, with the transition, the PCAOB "want[ed] everything to be perfect basically to public company standards." Tr. 176. According to CPA, beginning in 2014, auditors were "just auditing in more depth than we were in 2013." Tr. 108. "[I]t was no longer a matter of getting net capital right. It was a matter of getting all the numbers right." Tr. 125.

³⁷ Tr. 148-49.

³⁸ Tr. 125-26.

³⁹ CPA reminded Felix that the PCAOB had warned auditors that the proper accounting for personal expenses is to treat them as distributions, or compensation. CPA wrote, "Note that a new day has dawned for BD audits as they converted to PCAOB standards effective 06/01/14. Any unsubstantiated amounts or amounts that are deemed to be personal expenses . . . will be reclassified as distributions [to Felix]." JX-123, at 1. *See also* Tr. 99. Felix testified that, in the February 28, 2015 email, CPA changed his guidance for the first time and required Primex to treat personal expenses as compensation to Felix. *See* Tr. 1221-22, 1228.

According to CPA, the reclassifications were unrelated to new PCAOB standards applied to broker-dealers beginning in 2014, and the proper classification of personal expenses on a general ledger did not change in 2014 with the onset of PCAOB standards. Tr. 177.

his personal expenses on the general ledger during the relevant period as he always had—most often under “miscellaneous expenses”—which he said was the “guidance” CPA gave him.⁴⁰ CPA contradicted Felix. He testified that Felix understood the difference between a personal and a business expense.⁴¹ Given the advice CPA gave Felix in his February 28 email, the Panel credits CPA and does not find Felix credible on this point.

CPA invited Felix to contest his reclassifications before completing the audit. He would tell Felix if he was missing evidence to support claimed business expenses.⁴² Felix provided receipts if he could locate them, which CPA would review to determine if they represented “a reasonable and necessary” business expense. In one example that CPA gave at the hearing, Felix sent him a photograph of some furniture to demonstrate that the expense was for the Firm’s office. As a result, CPA considered it to have been correctly classified as a business expense.⁴³ If a receipt was for an expense that had a possible business purpose, CPA would generally agree it was correctly classified. According to CPA, Felix admitted some expenses were personal—for example, charges for women’s clothing—but there were some Felix wanted to argue about.⁴⁴ If Felix explained what an expense was for, even without a receipt, CPA would accept it if it seemed “legitimate.”⁴⁵

Felix did not provide CPA with documentation for many expenses CPA questioned—more than 600 in 2014.⁴⁶ Generally, if Felix had no receipt for an expense, or failed to provide a plausible explanation for it, CPA treated it as a personal expense. Also, if a receipt was illegible, CPA would not treat the item as a business expense.⁴⁷ In addition to sending emails with explanations and receipts, Felix had telephone conversations with CPA over disputed expenses. CPA acknowledged that, given the late start to the audit, Felix may not have had enough time to provide him support for business expenses before the audit had to be filed.⁴⁸

CPA said he applied his “professional judgment” as an “experienced auditor[]”⁴⁹ of broker-dealers in determining which expenses were personal and did not constitute “ordinary and

⁴⁰ Tr. 810-11, 941-42, 1180.

⁴¹ Tr. 141-42.

⁴² JX-125 (CPA email on March 1, 2015, telling Felix, “[W]e need original receipts, invoices, bills, etc. in support of the disbursements or these items will need to be reclassified to owner’s distributions.”). *See also* JX-124, at 2 (February 27, 2015 email from CPA to Felix attaching list of disputed expenses).

⁴³ Tr. 163-64.

⁴⁴ Tr. 137-38.

⁴⁵ Tr. 158-59.

⁴⁶ Tr. 135-36, 204-05.

⁴⁷ Tr. 156. *See also* JX-126, at 1, 7-8.

⁴⁸ Tr. 139-41.

⁴⁹ Tr. 195.

necessary” expenses of operating Primex.⁵⁰ He conceded that there were “lots of close calls” in deciding whether to allow an item as a business expense, even in instances for which Felix produced a receipt.⁵¹ If it was close, however, CPA would give Felix the benefit of the doubt. If Felix gave him a reasonable explanation, he would allow it as a business expense.⁵² It was also difficult for CPA to challenge many expenses because he was not in New York. CPA said he could not walk around the office to see whether certain items Felix said he purchased for Primex were in the office.⁵³

After reviewing entries on the general ledger, mostly under “miscellaneous expenses,” CPA required that Respondents reclassify 642 individual expenses totaling \$174,066 as distributions to Felix for 2014. The expense reclassifications, or adjustments, were “very unusual” for a broker-dealer, CPA testified. He had no other broker-dealer clients for whom he had to make similar adjustments.⁵⁴ CPA testified that, without the corrections he insisted on, the expense entries on Primex’s books and records would have been inaccurate.⁵⁵

On March 26, 2015, CPA sent Felix a governance letter to formally communicate his audit findings. He wrote that he had “encountered significant difficulties in dealing with management in performing and completing [the 2014] audit related to [the] classification of personal expenses paid by [Primex].”⁵⁶ In the letter, CPA told Felix that accounting standards require that CPA inform the Firm of non-trivial misstatements uncovered in the audit. He warned Felix, “It is imperative that [Primex] maintain accurate books and records throughout the year. Personal expenses paid by [Primex] on behalf of the stockholder should be charged to distributions.”⁵⁷

⁵⁰ Tr. 101.

⁵¹ Tr. 204.

⁵² Tr. 206.

⁵³ Tr. 224.

⁵⁴ Tr. 136, 149; JX-28, at 3.

⁵⁵ Tr. 171. *See also* JX-28, at 3; JX-130, at 3. Felix reflected the \$174,066 reclassifications on the general ledger as an adjustment to distributions as of December 31, 2014. Tr. 521-22, 843; JX-14, at 37. Felix filed the annual audit report incorporating CPA’s reclassifications of \$174,066. Tr. 845-46; JX-53.

⁵⁶ JX-134, at 3. CPA testified that he was required to send Felix a governance letter pursuant to the standards established by the American Institute of Certified Public Accountants (“AICPA”). Tr. 177-78. AICPA Statement on Auditing Standards No. 114 directs accountants to send a governance letter to communicate to those charged with the governance of a corporate entity significant findings from an audit, including disagreements with management and audit adjustments, which are not otherwise contained in the audited financial statement. *See* <https://www.aicpa.org/content/dam/aicpa/research/standards/auditattest/downloadabledocuments/au-00380.pdf>.

⁵⁷ JX-134, at 3. CPA had never before sent a broker-dealer client a similar governance letter concerning the payment of personal expenses. Tr. 181.

2. CPA's 2015 Audit

CPA conducted Primex's 2015 audit using the same methodology he had used for the 2014 audit. He reviewed expenses that appeared on the Firm's general ledger and bank statements. If he questioned whether an expense was appropriately charged to the Firm, he asked Felix for supporting evidence.

On February 29, 2016, for example, one of CPA's assistants emailed Felix for "[r]eceipts, descriptions for the circled items on the attached [general ledger] detail for leasehold improvements and fixed assets."⁵⁸ CPA testified that he decided to ask for evidence supporting these entries Felix made in the general ledger. The questioned expense entries in this instance ranged from \$3,300 to more than \$22,000.⁵⁹

The same day, in another email, CPA asked Felix to provide a "breakout" for monthly entries under the "miscellaneous expenses" category in the general ledger, covering January to June 2015 and ranging in amounts from \$9,213 to \$15,246. CPA needed the information so he could cross-reference the expenses to Primex's bank statements.⁶⁰ The bank statements identify the vendor and individual dollar amounts charged. CPA testified that, for a "miscellaneous expenses" category, these were "big amounts" and he needed details of the expenses to "form an opinion as to whether or not they were ordinary and necessary business expenses" of Primex.⁶¹

On March 1, 2016, CPA emailed Felix copies of Primex's 2015 monthly bank account statements he had marked up by identifying individual expenses that he considered personal, based on the vendor or description. He instructed Felix to send receipts and explanations of the business purpose for those items with which Felix disagreed.⁶² CPA did this for hundreds of debit card and cash withdrawal entries on the bank statements. These included, for example, expenses for karate classes, movie tickets, department stores, electronics stores, and hardware stores. CPA testified that he thought numerous Home Depot charges did not "sound plausible" and suspected they were instead for personal home remodeling.⁶³ CPA testified that he was also "highly skeptical" that Felix's ATM cash withdrawals were for business expenses because they were "unsubstantiated disbursements" from Primex.⁶⁴ Between January and October 2015, Felix withdrew more than \$19,000 in cash from Primex's bank account using ATMs.⁶⁵

⁵⁸ JX-136, at 1.

⁵⁹ Tr. 186-87; JX-136, at 2-3.

⁶⁰ JX-137.

⁶¹ Tr. 188.

⁶² See JX-139; JX-140.

⁶³ Tr. 193.

⁶⁴ Tr. 203-04.

⁶⁵ CX-3, at 1, 18-19.

On March 2, 2016, Felix responded by emailing CPA copies of about a dozen receipts he said represented spending on fixtures. The receipts were from high-end furniture stores, BestBuy, and Staples.⁶⁶ On March 5, 2016, Felix sent about another 30 receipts. These were from Home Depot, Costco, Walmart, Rite Aid, Walgreens, and other vendors.⁶⁷ CPA ended up accepting Felix's explanations that many expenses represented legitimate leasehold improvements because he was not in a position to challenge them even though, in his experience, it was rare for a broker-dealer to spend the amounts Felix had claimed on leasehold improvements.⁶⁸ In the end, CPA allowed many Home Depot charges to remain classified as Primex expenses based on Felix's representations that they were for Primex's office.⁶⁹

A few days later, CPA emailed Felix marked-up copies of Primex's 2015 monthly bank statements and general ledger to show him which expenses he had accepted, based on Felix's representations, as legitimate Primex expenses and those he still contended were personal.⁷⁰ In one example CPA gave at the hearing, he questioned travel charges and asked Felix for the names of the persons on the trip to support that the charges were for business purposes. In another case, CPA accepted Felix's representation that a \$226 expense was for a vacation plan for Primex brokers.⁷¹

On March 7, 2016, CPA emailed Felix a revised list of items he had determined were for personal expenses, after reviewing the supporting materials Felix had provided and listening to his explanations.⁷² After further reviewing expenses for which Felix provided supporting material or explanations, CPA made more changes. On March 9, 2016, CPA emailed Felix his final audit adjustments to the 2015 audit. The adjustments reclassified \$140,492⁷³ as

⁶⁶ JX-141.

⁶⁷ JX-143.

⁶⁸ Tr. 197-98; JX-107.

⁶⁹ CPA also allowed many Best Buy receipts because he "felt confident" they were reasonable. Tr. 224. *See also* Tr. 1359. CPA testified that "you cannot challenge every thing [sic] someone tells you." Tr. 201.

⁷⁰ *See* JX-144; JX-145; JX-146; JX-150. For items CPA identified as personal, he asked Felix to produce a "MEANINGFUL receipt" if Felix still believed that the item represented a business expense. JX-144, at 1. CPA said that a "meaningful" receipt was one that was created by the vendor that showed what was purchased. Tr. 219. *See also* JX-151, at 1.

⁷¹ Tr. 201; JX-144, at 2.

⁷² Tr. 211-12; JX-149.

⁷³ JX-28, at 1. According to Enforcement, Felix's personal expenses decreased during 2015. It calculated that he improperly classified \$30,106 and \$11,937 in personal expenses in the third and fourth quarters, respectively. Tr. 559; CX-3, at 1.

distributions to Felix. CPA instructed Felix to post the required adjustments to the general ledger.⁷⁴

After completing the 2015 annual audit, CPA sent Felix an email on March 11, 2016, stating that the “numerous audit entries arising during the [2015] audit constitute a material weakness under [Securities and Exchange Commission (“SEC”)] rules.”⁷⁵ He told Felix that Primex had to formally disclose this development to the SEC within 48 hours. CPA provided Felix with proposed language to use, which included a statement that Primex had “misclassified personal expenses.”⁷⁶ The same day, Felix filed the required notice with the SEC. However, instead of citing “misclassified personal expenses” as the cause of the material weakness, Felix informed the SEC that the deficiency involved “misclassification of shareholder distributions.”⁷⁷

While CPA was conducting the 2015 audit, the SEC was conducting its own cycle examination of Primex. SEC staff arrived on site unannounced in January 2016 and, according to Felix, looked at a wide range of the Firm’s operations and records.⁷⁸ The SEC completed its examination in June 2016. It summarized its findings in a letter to Felix. It had identified “numerous expenses” totaling \$136,027 between July and September 2015 that SEC staff thought were “not typical” for a firm the size of Primex. The SEC asked Respondents for validation of over \$100,000 of the recorded business expenses, but received receipts for less than \$40,000 of the expenses. The SEC’s letter noted that a review of the receipts “revealed that although certain items included on the receipts could reasonably be business expenses, the relevance of many items was unclear and in numerous instances they appear[ed] to be commingled with personal expenses.”⁷⁹

During its investigation, Enforcement staff asked Felix to provide a written statement explaining whether a sample of 96 expenses incurred throughout 2015 were for personal or

⁷⁴ Tr. 226-27; JX-153, at 1, 12. Felix recorded the reclassification of \$140,492 in expenses as distributions on the general ledger as of December 31, 2015. Tr. 564-65; JX-37, at 19. He also reflected CPA’s reclassifications in the 2015 audit he filed. Tr. 914-17; JX-54.

Felix presented evidence that by the middle of 2015 he was recording entries on the general ledger reflecting greater distributions to himself. These items were not reclassified by CPA. *See* Tr. 1308-12, 1317-19; JX-106; JX-172, at 24-25.

⁷⁵ JX-155, at 1. CPA relied on Exchange Act Rule 17a-11(e), which states that when a broker-dealer discovers or is notified by its accountant of the existence of any material weakness, as defined in Exchange Act Rule 17a-5(d)(3)(iii), it must give notice to the SEC and transmit a report within 48 hours. JX-155, at 2.

⁷⁶ Tr. 230-31; JX-155, at 1, 4.

⁷⁷ Tr. 928; JX-55, at 2. Felix’s notice also stated that the deficiencies occurred between September 30, 2015, and December 31, 2015, when in fact they occurred throughout the year. Felix testified that he spoke to CPA about the changed language before filing the notice. Tr. 928.

⁷⁸ Tr. 1375-77. The SEC did not take any action against Respondents as a result of its examination. Tr. 1086, 1373.

⁷⁹ JX-58, at 6. The SEC informed Felix in its examination letter that it had determined Primex was not in compliance with Exchange Act Rules 17a-3(a)(11) and 17a-5(a)(2)(iii). JX-58, at 6.

business purposes. The expenses ranged from \$8 to more than \$4,600, and included multiple ATM withdrawals.⁸⁰ Felix did not provide the requested statement addressing each item. Through counsel, Felix answered that “it [was] impossible to determine whether the listed charges (particularly ATM withdrawals) represent[ed] personal expenditures or expenses of Primex.”⁸¹ He also told Enforcement that he sometimes inadvertently used a Primex debit card instead of an Advantage Trading debit card to purchase items. According to Felix, to the extent that personal expenses appeared on Primex’s general ledger, they were reclassified as distributions as a result of CPA’s audit.⁸²

Respondents disputed the staff’s preliminary findings, set forth in an exception letter to the Firm at the conclusion of the cycle examination, that Primex had misclassified Felix’s personal expenses. In a written response dated February 16, 2016, Primex disagreed that it maintained an inaccurate general ledger: “The firm’s financial records are audited by a third-party [Public Company Accounting Oversight Board] (“PCAOB”) accountant [*i.e.*, CPA], and no irregularities were recorded. All expenses were recorded correctly on the firm’s books and records. Every transaction was recorded fully. There were no missing or excluded off-balance sheet transactions. Primex has not failed to maintain its books and records.”⁸³

3. Enforcement’s Review of Felix’s 2013 Expenses

After seeing entries that could represent Felix’s personal expenses in Primex’s 2014 and 2015 general ledger, FINRA staff obtained from Respondents copies of Primex’s 2013 general ledger and the Firm’s monthly bank statements. Enforcement’s investigator testified that he saw, in particular, expense activity and ATM cash withdrawals that appeared to be personal in nature and other expenses with many of the same vendors that appeared on the general ledger in 2014 and 2015.⁸⁴

In December 2017, Enforcement asked Respondents to explain the business purpose of a sample of 100 expenses Felix had incurred throughout 2013. The expenses ranged from \$260 to nearly \$3,800, and included multiple ATM withdrawals.⁸⁵ Felix responded that, because of the passage of time, he could “not recall whether any particular expense . . . was a personal expenditure or a business expense, nor [did] he have receipts or documentation or other information for such expenses.”⁸⁶

⁸⁰ JX-43, at 1-13.

⁸¹ JX-43, at 17.

⁸² JX-43, at 17.

⁸³ JX-21, at 13.

⁸⁴ Tr. 527-29, 547-48, 570, 588-91. *See also* JX-27; JX-36; JX-38, at 19-58. CPA testified that his audits before 2014 focused on the accuracy of the Firm’s stated net capital. Tr. 99-100.

⁸⁵ Tr. 590-91; JX-41, at 1-7.

⁸⁶ JX-41, at 15.

FINRA staff applied a standard similar to what CPA had used to determine which 2014 and 2015 expenses were personal. Enforcement compared Felix's spending at vendors in 2013 with vendors in 2014 and 2015 that CPA reclassified as personal expenses. As a result, Enforcement's investigator calculated that Respondents incorrectly classified more than 500 of Felix's personal expenses, totaling \$123,096, as Primex business expenses in 2013.⁸⁷

Of the \$123,096 Enforcement determined was wrongly reclassified in 2013, more than \$50,000 was attributable to Felix's cash withdrawals. Felix also spent more than \$27,000 at retailers, including Costco, Macy's, Walmart, Marshalls, and Target. He spent in excess of \$11,000 on entertainment, which included karate lessons, Netflix, Amazon Video On Demand, and movie theatres. Clothing expenses came to nearly \$11,000 at, for example, children's clothing stores, shoe stores, Men's Wearhouse, and TJ Maxx.⁸⁸ Felix spent between approximately \$800 and \$5,300 on makeup or cosmetics, pet care, medical services, fitness and sporting goods, toys, loan repayments, car-related expenses, and hardware.⁸⁹

4. The Panel's Findings Concerning Felix's Expenses

Based on a careful review of the documentary evidence and testimony, the Panel finds that Enforcement failed to prove that a total of \$437,654 in allegedly misclassified personal expenses from 2013 to 2015 were incorrectly recorded as business expenses in Primex's books and records. We did not accept Enforcement's decision to treat all of CPA's 2014 and 2015 reclassifications as improper expense classifications by Respondents. Instead, we find that Felix misclassified a total of \$248,893. In making these determinations, the Panel carefully considered witness testimony, together with the available documents, and the parties' arguments about the expenses.

At the outset, the Panel finds that Felix and CPA were racing to file the audits on time to avoid sanctions against Primex. SEC rules requires a broker-dealer to file its year-end audit within 60 calendar days of the end of its fiscal year. Primex's fiscal year ends on December 31 of each year. Accordingly, Primex's audit was due on or about March 1 of each year. If a broker-dealer misses the 60-calendar day deadline, it faces a \$100 fine for each day it is late. If a broker-dealer does not file its annual audit within 10 business days of the deadline, the SEC has the authority to order a broker-dealer to cease operations until it files the audit.⁹⁰ Felix testified that, even though he disagreed with CPA's reclassifications, he had no choice but to accept the final

⁸⁷ CX-1.

⁸⁸ CX-1, at 1, 14-25.

⁸⁹ CX-1, at 14-25.

⁹⁰ See Exchange Act Rule 17a-5(d)(5), FINRA Rule 4140, and Schedule A, Section 4(g)(1), of FINRA's By-Laws. See also Tr. 318, 1215.

adjustments CPA provided to him on March 9, 2015, or subject Primex to penalties if he filed the audit late.⁹¹

We recognize that it was Felix's responsibility to show CPA which questioned items were business expenses, and we find that CPA reasonably applied his professional judgment given the circumstances. The Panel also applied its own judgment as to which 2013 expenses (none of which was reclassified as compensation by CPA) Felix improperly recorded as Firm expenses.

Felix explained the purpose of many expenses—conceding that many were personal, while insisting that others were business. Questioned about hundreds of different expenses during two days of testimony, Felix often was unable to recall whether an expense was personal or business. In some instances, he changed his testimony from one day to the next about the purpose of an expense. The Panel credits Felix's testimony that, given the Firm's small size, he was the person responsible for making most, if not all, of the purchases required to operate Primex. We also conclude, however, that, without a personal bank account, Felix's principal source of money to purchase household necessities for himself, his wife, and young children was the Primex bank account, in addition to the Advantage Trading bank account.

The Panel accepts Felix's business justifications for some expenses. In other instances, the Panel finds that Felix's explanations were not credible given the nature and amount of the expense, and the vendor involved. Sometimes Felix could not recall if a purchase was business-related.⁹² At other times, he claimed that purchases were gifts for his employees and brokers and therefore appropriate business expenses.⁹³

We set forth below in detail our findings as to these expenses.

a. Cash Withdrawals

During the relevant period, Felix withdrew \$133,901 in cash from Primex accounts at ATMs or by using a Firm check at the bank. From 2013 to 2015, he took \$50,777, \$64,091

⁹¹ Tr. 1262-63.

⁹² For example, Felix testified that he could not recall if a purchase of women's shoes at DSW for \$61.97 in October 2014 was personal. Tr. 1465-66; CX-2, at 20; JX-93. He said he could not recall if two dresses bought online for \$258.06 at Macy's in June 2015 were personal. Tr. 1477-78; CX-3, at 26; JX-161. The Panel does not find Felix's representations credible.

⁹³ For example, Felix claimed a \$677.71 charge for Xbox games bought in mid-December 2013 was not for his children. Tr. 1435-37; CX-1, at 24; JX-69. He said that a pair of women's boots he bought for \$128.84 online from Macy's was a business-related gift because his wife does not wear the size purchased. Tr. 1443-44; CX-2, at 3; JX-71. A \$54.06 online purchase of two girls' toddler-sized sweat suits at Macy's in January 2015, Felix testified, were business-related gifts even though he could not recall for whom. Tr. 1471-73; CX-3, at 19; JX-158. In another instance, only after being shown the receipt for a women's sweater, did Felix concede that an online purchase for \$61.50 at Macy's in December 2014 was personal. He had originally described the expense as office supplies. Tr. 1468-69; JX-96.

(\$53,591 of which was from ATM withdrawals), and \$19,033, respectively, in cash from Primex's bank account.⁹⁴ At the hearing, Felix acknowledged using the cash to pay for personal items.⁹⁵ Felix estimated that, in 2013, between \$5,000 and \$10,000 of the cash he obtained was for personal use. He testified that he used 30 percent of the \$53,591 he withdrew from ATMs in 2014, or \$16,077, and 20 percent of the \$19,033 he withdrew in 2015, or \$3,807, for personal expenses.⁹⁶ In a written response to a Rule 8210 request for information, Felix acknowledged that \$6,500 in counter withdrawals at Primex's bank between September and December 2014 also were for personal expenses.⁹⁷

Accepting Felix's admissions, the Panel finds that, in addition to the \$6,500 in counter withdrawals in 2014, he obtained \$5,000, \$16,077, and \$3,807 in cash from Primex's bank account for personal expenses, respectively, in 2013, 2014, and 2015. Thus, the Panel finds that Felix used a total of \$31,384 in cash withdrawals for personal expenses between 2013 and 2015.

b. General Retailers

Felix made hundreds of purchases totaling \$91,264 from vendors that Enforcement categorized as "general retailers"—\$27,284, \$33,362, and \$30,618, respectively, from 2013 to 2015. The retailers included Costco, J.C. Penney, Macy's, Marshalls, Overstock, Target, and Walmart, among others.⁹⁸

Felix testified that such purchases represented office expenses. These include over 120 purchases at Costco—totaling approximately \$15,000 each year.⁹⁹ In 2015, there were 41 purchases totaling more than \$5,800 from a website called HauteLook.¹⁰⁰ He made more than 50 purchases at Macy's totaling in excess of \$8,700 during the relevant period.¹⁰¹ Lesser amounts were spent at other retailers. Felix provided no reasonable or credible explanation and provided no evidence supporting his claim that these purchases were for business purposes. Accordingly,

⁹⁴ CX-1 at 1, 14-15, 24; CX-2, at 1, 17-19, 30; CX-3, at 1, 18-19. With the exception of two ATM withdrawals totaling \$1,300 in October 2015, Felix made all the ATM withdrawals in 2015 by June 1. CX-3, at 18-19.

⁹⁵ See Tr. 1274. Two Home Depot receipts for more than \$200 showed that Felix paid with cash. Tr. 1275-76; RX-1, at 20, 22. Felix testified that he withdrew \$4,000 from Primex's bank to pay cash for a sofa for the office, however, this withdrawal was not reclassified by CPA. Tr. 1278-79; CX-3, at 11; JX-172, at 57.

⁹⁶ Tr. 1540-41, 1550-51, 1556-57. Earlier in the hearing, Felix disputed that any 2013 ATM withdrawals were for personal expenses. See Tr. 1003-04.

⁹⁷ JX-24, at 3. See also CX-2, at 1, 30.

⁹⁸ CX-1, at 1, 21-23; CX-2, at 1, 24-27; CX-3, at 1, 23-26.

⁹⁹ CX-1, at 21-22; CX-2, at 24-25; CX-3, at 24-25. One purchase at Costco was for \$3,793 and another was for \$2,105. CX-1, at 21-22; CX-3, at 24-25.

¹⁰⁰ CX-3, at 25. Felix testified that HauteLook purchases were for the office, without providing detail. Tr. 1152.

¹⁰¹ CX-1, at 22; CX-2, at 25-26; CX-3, at 26.

the Panel finds that Felix's \$91,264 in purchases under the category general retailers were personal expenses and therefore not properly recorded in Primex's books and records.

c. Clothing Retailers and Other Online Vendors

Felix spent \$35,990 at clothing stores or online clothing retailers—\$10,858, \$17,700, and \$7,432, respectively, between 2013 and 2015. He made purchases at multiple retailers, including Lord & Taylor, Burlington Coat Factory, Cole Haan, Salvatore Ferragamo, The Gap, Louis Vuitton, Nike, Neiman Marcus, and Timberland, among many others.¹⁰² Clothing purchases included, for example, spending at discount shoe retailers DSW and Zappos, totaling \$2,929, which Felix did not dispute were for personal items.¹⁰³

Felix claimed that some clothing purchases were business gifts—for example, of \$1,909 spent at Men's Wearhouse in 2013, Felix said only \$1,078 was personal and the rest, or \$831, was for business gifts.¹⁰⁴ For one of the retailers, Felix credibly explained that \$607 that appeared to have been spent at a clothing store in 2013 and 2014 was actually for office plants.¹⁰⁵ Felix testified that purchases at online retailer Zulily were not clothes but items for the office. In 2014 and 2015, he spent \$4,977 on 63 purchases at Zulily.¹⁰⁶ Because Zulily sells items for the office, the Panel finds that these expenses were plausibly business-related.

Felix testified that two items totaling \$2,163 purchased from Louis Vuitton were for a monogrammed gift to the Firm's highest producing broker (\$397) and pictures, or decorative screens, displayed in the office (\$1,766).¹⁰⁷ Another purchase for \$1,742, in November 2014, according to Felix, was for a fur throw he bought for the office.¹⁰⁸ The Panel finds that the Louis Vuitton items and the fur were business-related expenses.

Accordingly, the Panel finds that \$25,670 Felix spent at clothing retailers (excluding \$831 at Men's Wearhouse, office plant expenses, all purchases at Zulily, and the Louis Vuitton and fur expenses) were personal expenses and improperly recorded as business expenses.¹⁰⁹

¹⁰² CX-1, at 1, 15-16; CX-2, at 1, 20-21; CX-3, at 1, 19-20. Felix's single largest clothing expense was a \$2,692 purchase at a fur store in New Jersey in January 2013. *See* CX-1, at 16.

¹⁰³ Tr. 1020-21, 1444-45; CX-1, at 15; CX-2, at 20-21; CX-3, at 20.

¹⁰⁴ Tr. 1541-42; CX-1, at 16.

¹⁰⁵ A store called H&M, Felix testified, actually referred to a plant or gardening store, not the clothing retailer. These expenses totaled \$607, which the Panel finds relate to Primex's business. Tr. 1142; CX-1, at 15; CX-2, at 20.

¹⁰⁶ CX-2, at 21; CX-3, at 20.

¹⁰⁷ Tr. 1143, 1335-37, 1561; CX-2, at 20; CX-3, at 20.

¹⁰⁸ Tr. 881, 1133-34; CX-2, at 20; JX-24, at 4; RX-2, at 4.

¹⁰⁹ CX-2, at 20-21; CX-3, at 19-20.

In 2015, Felix also made 86 purchases on Amazon or with Amazon Marketplace, totaling \$5,403. He also made 45 purchases totaling \$3,136 at multiple retailers using PayPal.¹¹⁰ Felix did not explain the business purpose of any of these purchases, although he disputed one of the expenses, for \$878, that CPA reclassified.¹¹¹ The Panel finds these expenses, totaling \$8,539, were personal and therefore were not correctly recorded in Primex's books and records.

d. Entertainment

Felix spent \$29,755 on entertainment: \$11,482, \$11,308, and \$6,965, respectively, from 2013 to 2015. This spending includes more than 100 individual charges at Amazon Video on Demand and Amazon Kindle, ranging from \$1.99 to \$35.99. It also includes multiple movie theatre ticket purchases; Netflix purchases; tickets to Ringling Brothers circus; and visits to bowling alleys, Luna Park, SeaWorld, Chuck E. Cheese, and Sesame Place. Additionally, Felix used Primex's funds to pay for approximately 90 karate lessons (costing between \$29 and \$376 each).¹¹²

Felix concedes that all the karate charges were for his son's lessons and therefore were personal. He contends that they were recurring charges he made "inadvertently" using a Primex debit card.¹¹³ He also testified that \$700 spent at Luna Park at Coney Island was personal, as were the visits to the circus and Sesame Place.¹¹⁴ In a written response to Enforcement staff, Felix also said that a \$102.35 charge at SeaWorld in October 2014 was personal.¹¹⁵

Felix testified that the movie tickets were for brokers, "for them to do something outside of the office."¹¹⁶ Felix also testified that all the Amazon Video On Demand charges were business expenses because Primex brokers would watch videos in the office if they stayed late.¹¹⁷ Given the frequency and number of the movie ticket and video purchases, the Panel does not find this credible. Felix also spent \$1,072 at an indoor baseball batting cage in June 2014, which he testified was a business expense because he had taken brokers. The Panel does not find this credible. The visits to the batting cage occurred near his son's birthday, he placed an order for a birthday cake with the same establishment, and he spent another \$300 at the batting cage in

¹¹⁰ CX-3, at 1, 17-18, 28.

¹¹¹ Tr. 666; CX-3, at 1, 17-18.

¹¹² CX-1, at 1, 16-20; CX-2, at 1, 21-23; CX-3, at 1, 21-22.

¹¹³ Tr. 890-92.

¹¹⁴ Tr. 1561; CX-1, at 19; CX-2, at 22; CX-3, at 22. Earlier in his testimony, Felix insisted the Luna Park expenses were work-related because he took brokers to the boardwalk to talk. Tr. 896.

¹¹⁵ JX-24, at 4. At the hearing, Felix said the SeaWorld and Sesame Place expenses were personal. Tr. 1545-46.

¹¹⁶ Tr. 1022.

¹¹⁷ Tr. 1543.

June 2015.¹¹⁸ Felix also insisted that \$212 he spent at Chuck E. Cheese was a business expense because he “may have” also taken a broker when he took his children there.¹¹⁹ The Panel rejects this as a justification for classifying a Chuck E. Cheese charge as a business expense.

The Panel finds that all \$29,755 in entertainment expenses incurred by Felix were personal.

e. Travel Expenses

Felix charged \$16,455 in travel expenses to Primex in 2014 and 2015.¹²⁰ He acknowledged that \$1,287 he spent in 2014 for passports and on travel to a resort was personal.¹²¹ Felix offered no explanation or purported business purpose for the remaining travel expenses. The Panel accordingly finds that Felix’s \$16,455 in travel-related expenses were personal and therefore improperly classified as Firm expenses.

f. Loan Repayments and Car Expenses

Felix made loan payments of \$18,038 in 2013 and 2014. Felix acknowledged that \$8,281 in loan expenses in 2014 to Ocwen Financial were mortgage payments for a personal investment property.¹²² He claimed that other loan payments of \$4,198 and \$5,558 to Santander Bank in 2013 and 2014, respectively, were for a Mercedes the Firm owned that he drove “at times” and that “other brokers drove it.”¹²³ The car was not identified in the Firm’s annual audit as a Primex asset, and Felix also admitted to owning “a few” Mercedes himself.¹²⁴ Accordingly, we find that all loan payments, totaling \$18,038, were personal.¹²⁵

In 2014, Felix charged \$4,674 on a Primex card for car insurance for the Mercedes. Because the Panel determines the Mercedes is personal, we also find that the insurance payments were personal expenses.¹²⁶

¹¹⁸ Tr. 883-86; CX-2, at 22; CX-3, at 21; JX-30; JX-85. Felix testified that his son’s birthday was in June. Tr. 1525-26. He also testified that because June was the anniversary of the date he purchased Primex he would hold an office celebration in June as well. Tr. 999-1000. The Panel rejects this explanation, too.

¹¹⁹ Tr. 895-96; CX-2, at 22.

¹²⁰ CX-2, at 1, 29; CX-3, at 1.

¹²¹ Tr. 1555-56; CX-2, at 1, 29.

¹²² Tr. 861-63; CX-1, at 1, 23; CX-2, at 1, 27; JX-24, at 4.

¹²³ Tr. 1010-15, 1547, 1554-55; CX-1, at 23; CX-2, at 27.

¹²⁴ Tr. 855-58. Primex’s annual audit did not reflect any assets or liabilities relating to an automobile. Tr. 950; CX-52, at 6-8. Felix paid \$755.55 for auto repairs to a Mercedes he said was in the Firm’s name. Tr. 856; CX-2, at 19. The Panel does not find it credible that the Mercedes was a Firm car.

¹²⁵ Tr. 858-61; CX-1, at 1, 23; CX-2, at 1, 27.

¹²⁶ CX-2, at 19.

g. Fitness-Related Expenses

Felix spent \$5,425 of Primex's funds on items related to fitness or health between 2013 and 2015. Of this amount, he spent \$1,328 on health or dietary supplements and at least \$318 on visits to a gym, which Felix admitted were personal.¹²⁷ Other expenditures of \$555 for a "Flex Belt," \$318 at Planet Fitness, and \$133 at Weight Watchers, Felix specifically acknowledged, were personal.¹²⁸ He claimed that other items, including exercise-related goods from Modell's and Beachbody Fitness, totaling \$651, were placed in the office for brokers to use.¹²⁹

Felix testified that he operates Primex in "a totally different way" from other broker-dealer owners to ensure that "the environment is correct" because a broker's job is stressful. He bought some items for the office, he said, "to provide the brokers with certain things to do," which included a stationary bicycle so "they could run things off," and a "dummy" so brokers could punch it instead of "screaming in the office."¹³⁰ The Panel does not find these explanations sufficiently credible to demonstrate a business purpose for the fitness-related items. Furthermore, Felix provided no corroborating evidence to substantiate this claim that these were business-related expenses.

Accordingly, the Panel finds that Felix's \$5,425 in fitness spending was personal and incorrectly classified as Primex expenses.

h. Medical and Pharmacy Expenses

Felix incurred \$4,950 in medical expenses from 2013 to 2015. Although Felix used Firm funds for these expenses, he acknowledged these were personal.¹³¹

i. Toys and Children's Tuition

In 2013 and 2014, Felix spent \$4,242 of Primex's funds at toy and game stores, such as Toys R Us, Babies R Us, and GameStop, and on products like Sony PlayStation and Nintendo.¹³² Felix testified that some toy purchases were actually gifts for his brokers or their children. Given that Felix had young children at the time of the purchases, the Panel does not find this explanation credible and determines that the entire \$4,242 represents personal expenses that he improperly recorded as business expenses.

¹²⁷ Tr. 995-96, 1430, 1546, 1561; CX-1, at 1; CX-2, at 1; CX-3, at 1. The \$1,328 in dietary supplements includes purchases from GNC, Maxx Test 300, and Superbalife. CX-1, at 20; CX-3, at 22; JX-65.

¹²⁸ Tr. 1546-47, 1562; CX-1, at 20-21. Felix also did not dispute that \$50.95 for a health supplement was a personal expense. Tr. 1430-31; CX-1, at 20; JX-65.

¹²⁹ Tr. 989, 1561; CX-3, at 22.

¹³⁰ Tr. 990-91.

¹³¹ Tr. 1549, 1562; CX-1, at 1, 23; CX-2, at 1, 27; CX-3, at 1, 27.

¹³² CX-1, at 1, 24; CX-2, at 1, 29.

Felix paid his children's private school tuition using the Primex bank account. He acknowledged spending \$547 and \$1,605 on tuition in 2014 and 2015, respectively.¹³³ Accordingly, the Panel finds that Felix's \$2,152 in tuition spending was incorrectly recorded as business expenses.

j. Jewelry, Cosmetics, and Personal Care Expenses

Felix testified that a \$3,745 jewelry purchase in August 2014 was for gifts to sponsors of securities products Primex sold to its customers.¹³⁴ The Panel does not find this explanation credible. It is not plausible that a broker-dealer would provide gifts to product sponsors, particularly in the amounts Felix claims. Respondents maintained no record of gifts to third persons and had no receipts for these items. Felix could not even recall to which sponsors he purportedly gave the jewelry.¹³⁵ Felix also made another jewelry purchase for \$375 at approximately the same time, for which he provided no reasonable explanation.¹³⁶ The Panel therefore finds that Felix's \$4,120 in jewelry purchases were personal expenses incorrectly recorded as Firm expenses.

Felix also spent \$3,194 of Primex's funds on items Enforcement categorized as cosmetics (or makeup) and personal care from 2013 to 2015.¹³⁷ At the hearing, he claimed that even though he purchased items from cosmetics stores or similar vendors, they were not all cosmetics products. The items included, for example, candles, shaving kits, jewelry, and other items that he said he gifted to brokers.¹³⁸ Of the \$3,194 total, Felix spent \$336 on dental supplies in 2015.¹³⁹

The Panel finds that, with the exception of \$336 spent on dental products, Felix's explanations are plausible given the amount he spent on these items and the number of persons who worked at Primex. The Panel therefore finds that \$2,858 in purchases of makeup, cosmetics, and personal care items from 2013 to 2015 were properly classified as business expenses. The \$336 spent on dental products was incorrectly classified.

¹³³ Tr. 979-80; CX-2, at 1, 30; CX-3, at 1, 30; JX-24, at 3-4. The \$547 payment in 2014 was made to the same third-party payment service used to pay \$1,605 in tuition in 2015.

¹³⁴ Tr. 862-63.

¹³⁵ Tr. 862. In a response to a Rule 8210 request for information during the investigation, Felix said the jewelry was a personal expense. CX-24, at 4.

¹³⁶ CX-2, at 1, 27. Felix acknowledged that he had not recorded any gifts on Primex's books and records. Tr. 1482, 1485; RX-17, at 29, 405, 1139.

¹³⁷ CX-1, at 1, 23; CX-2, at 1, 27; CX-3, at 1, 27-29.

¹³⁸ Tr. 984-85 (regarding Sephora purchases), 1462-63, 1474, 1548-49.

¹³⁹ CX-3, at 28-29. In a written response to a Rule 8210 request for information, Felix stated a dental care expense was personal. *See* JX-24, at 4.

k. Pet Care

Felix spent \$3,019 on pet care from 2013 to 2015, some of which was for the care of his dog and some of which represented the costs of keeping a fish tank that Felix testified he had at Primex's office. The fish tank expenses (at Petco) totaled \$1,130, which the Panel finds were reasonable business expenses.¹⁴⁰

The Panel finds that the dog-care expenses of \$1,889 were personal and improperly classified as business expenses.¹⁴¹

l. Hardware, Furniture, and Electronics

In 2013, Felix spent \$5,281 of Primex's funds at kitchen and bath stores and a tile store. In 2014, he spent \$578 at Home Depot and Lowe's for "office fixup" or "office supplies."¹⁴² In 2015, he spent an additional \$7,022 at Home Depot and at the same tile and kitchen stores.¹⁴³ Felix testified that his purchases at Home Depot and the tile and kitchen stores were for Primex's offices in Elmsford and later New York City. This testimony was consistent with the explanations that Felix offered CPA during his audits. At the hearing, Felix entered into evidence photographs of items he said were purchased at these stores, including for example, a ladder.¹⁴⁴ The Panel finds it plausible that these expenses were business-related and therefore concludes they were correctly classified.

During 2014 and 2015, Felix spent \$20,205 of Primex's funds on furniture items, according to Enforcement's categorizations—\$7,144 and \$13,061, respectively. Felix testified that he bought furniture and related items, including plants, for Primex's office to create a certain mood, or "[wow] factor" for his clients and employees.¹⁴⁵ The Panel credits Felix's testimony and, in the absence of persuasive countervailing evidence, finds that these expenses were business-related.

Felix also spent \$5,901 of Primex's funds on electronics in 2014 and 2015, primarily at Best Buy and HP Homestore. He testified that he purchased a television, monitors, and a computer for Primex's office.¹⁴⁶ The Panel credits Felix's testimony and finds that the expenses were properly classified as business-related.

¹⁴⁰ Tr. 889-90, 1139, 1151; CX-1, at 1, 23-24; CX-2, at 1, 28; CX-3, at 1, 29.

¹⁴¹ In response to a Rule 8210 request for information, Felix described dog-care expenses as personal and acknowledged they should be treated as shareholder distributions. JX-24, at 4.

¹⁴² CX-1, at 1, 23; CX-2, at 1, 27.

¹⁴³ CX-3, at 1, 26-27.

¹⁴⁴ Tr. 1151, 1458-61.

¹⁴⁵ Tr. 1140; CX-2, at 1, 24; CX-3, at 1, 23.

¹⁴⁶ Tr. 1141, 1146, 1354; CX-2, at 1, 21; CX-3, at 1, 21.

m. Cleaning Services and Food Expenses

Felix charged \$1,775 to Primex's credit or debit cards for dry cleaning or other cleaning services in 2014 and 2015. He credibly testified that this was primarily for dry cleaning office items and "office cleanup."¹⁴⁷ The Panel finds these expenses to be business-related.

Felix spent \$1,418 on food in 2014 and 2015, according to Enforcement's estimates. Felix testified that he frequently purchased food for the office and bought lunches for brokers.¹⁴⁸ The Panel credits Felix's testimony and finds that Enforcement failed to prove that these expenses were personal. Accordingly, the Panel finds the food expenses were properly recorded as business expenses.

* * *

After carefully considering all the evidence, the Panel finds that Enforcement proved by a preponderance of the evidence that between 2013 and 2015 Respondents improperly recorded \$248,893 of Felix's personal expenses as business expenses on Primex's general ledger.

E. Respondents' Incorrect Focus Reports

Felix filed Primex's FOCUS Report for the fourth quarter of 2014 in January 2015, before CPA directed Respondents to reclassify Felix's expenses.¹⁴⁹ In July 2015, Respondents filed an amended FOCUS Report for the fourth quarter of 2014 to reflect the reclassification of \$174,066 of Felix's expenses as compensation.¹⁵⁰ Enforcement reviewed each of Primex's four quarterly FOCUS Reports for 2014. It calculates that the FOCUS Reports for the first three quarters of 2014 understated distributions, or compensation, to Felix by \$48,153, \$40,459, and \$42,231, respectively. The amended FOCUS Report for the fourth quarter overstated Felix's compensation by \$149,143 because the entire \$174,066 in adjustments was booked as of December 31, 2014.¹⁵¹

Similarly, Felix filed Primex's FOCUS Report for the fourth quarter of 2015 in January 2016. He filed two amendments in mid-March 2016 to reflect that he had reclassified \$140,492 in personal expenses as compensation.¹⁵² Enforcement calculates that the FOCUS Reports for the first three quarters of 2015 understated distributions to Felix by \$40,374, \$58,076, and \$30,106, respectively. The amended FOCUS Report for the fourth quarter of 2015 overstated

¹⁴⁷ CX-2, at 1, 19-20; CX-3, at 1, 19.

¹⁴⁸ Tr. 1138, 1154, 1258; CX-2, at 1, 24; CX-3, at 1, 22-23.

¹⁴⁹ FOCUS Reports are due within 17 business days after the end of each calendar quarter. Exchange Act Rule 17a-5(a)(2)(iii).

¹⁵⁰ Tr. 697-99; JX-56, at 57-64.

¹⁵¹ Tr. 708-12; CX-2, at 1; CX-6.

¹⁵² Tr. 699-702; JX-56, at 89-96.

Felix's compensation by \$128,556 because the \$140,492 correction was made as of December 31, 2015, making up for the understatements in the FOCUS Reports filed for the first three quarters.¹⁵³

Respondents did not file any amended FOCUS Reports in 2013 because CPA did not require them to reclassify any expenses.¹⁵⁴ Enforcement calculates that in each quarterly FOCUS Report—based on \$123,096 of expenses it determined were personal—Respondents understated the amount of compensation Felix had actually received. According to Enforcement, the 2013 FOCUS Reports understated Felix's compensation by \$23,618, \$10,637, \$44,810, and \$44,031 for each quarter, respectively.¹⁵⁵

Enforcement's investigator acknowledged that, if Felix's personal expenses were in fact less each year than what CPA and Enforcement calculated, the understatement of compensation in the FOCUS Reports would be incorrect by smaller amounts than those set forth above.¹⁵⁶

F. Primex's Late Response to November 2015 Requests for Information

On November 3, 2015, FINRA staff sent Primex a written request for information, pursuant to FINRA Rule 8210. It asked the Firm to "provide an explanation of the business purpose" for a sample of 73 checks, debit card charges, and electronic funds transfers that Felix effected through the Firm's bank account between January 2014 and March 2015. It also asked the Firm to produce "copies of all invoices and/or supporting documentation relating to the payment" associated with each listed transactions.¹⁵⁷ FINRA staff selected these charges because they "appeared to be blatantly not firm-related."¹⁵⁸ When the Firm failed to respond by the due date (November 10, 2015), FINRA staff sent the Firm another, substantially similar request on November 17, asking for a response by November 27, 2015.¹⁵⁹

On December 24, 2015, FINRA sent Primex an "exception letter" setting forth the staff's findings resulting from the cycle examination. One of the exceptions, or violations, was the Firm's failure to respond to FINRA's November 3 and November 17, 2015 Rule 8210 requests asking about the way it classified Felix's expenses on Primex's general ledger. The letter stated

¹⁵³ Tr. 716-20; CX-3, at 1; CX-7.

¹⁵⁴ Tr. 738-39.

¹⁵⁵ Tr. 704-07; CX-1, at 1; CX-5.

¹⁵⁶ Tr. 776-78.

¹⁵⁷ Tr. 383-84; JX-19. Felix called FINRA staff to request an extension of time to respond to the November 3 request for information and was instructed to put his request in writing. According to FINRA, he failed to do so. In a second request, FINRA staff acknowledged that, on about November 9, 2015, Felix called a staff member to ask for an extension. Tr. 386-87; JX-20, at 2.

¹⁵⁸ Tr. 384.

¹⁵⁹ JX-20. Felix did not ask for an extension of time to respond to the November 17, 2015 Rule 8210 request. Tr. 391.

that the Firm's failure to respond "has limited staff's ability to fully identify all potential personal expenses."¹⁶⁰ Another exception was for recordkeeping irregularities concerning Felix's expenses.

Primex responded to the exception letter in writing on February 26, 2016. The Firm said that it had not responded to the November Rule 8210 requests because Felix had sought guidance from FINRA staff and was waiting to hear back, but that it would respond.¹⁶¹ At the hearing, FINRA's examination manager testified that Felix had contacted him to ask what FINRA or SEC rule prohibited a firm from paying personal expenses. The examination manager told Felix that there was no such rule but, citing basic accounting principles, a broker-dealer's books and records must reflect expenditures of the firm accurately or otherwise record that it was paying personal expenses. Because the examination manager believed he adequately answered Felix's question, the manager did not get back to Felix with more guidance.¹⁶²

Felix also told the examination manager that Primex was in the process of moving to its new offices in New York City, and he needed time to go through boxes to find the materials responsive to the Rule 8210 requests.¹⁶³ On January 15, 2016, Felix emailed FINRA staff, "As discussed a response from Primex is forthcoming for the outstanding requests. As per my prior conversations with [staff], I was awaiting guidance (and still am) regarding the rules per the request and the relevance from your end."¹⁶⁴ Felix testified that during this period he was also busy attending to SEC staff who had initiated an unannounced on-site examination of the Firm in January 2016.¹⁶⁵

Because the Firm still had not responded to the November 3 and November 17, 2015 Rule 8210 requests, on February 26, 2016, FINRA staff issued a Notice of Suspension pursuant to FINRA Rule 9552 informing Felix he would be suspended from associating with any member firm and Primex that it would be suspended from FINRA membership unless they produced the requested information by March 21, 2016. The Notice of Suspension also informed Respondents the suspensions would not take effect if they produced the information before March 21, 2016.¹⁶⁶

¹⁶⁰ JX-21, at 5.

¹⁶¹ JX-21, at 12.

¹⁶² Tr. 401-02.

¹⁶³ Felix Ans. ¶ 87; Primex Ans. ¶ 87; Tr. 468, 955, 1374-75.

¹⁶⁴ JX-22, at 1. Within days of receiving Felix's email, FINRA staff responded that the requests "were made pursuant to FINRA Rule 8210 and relate to FINRA's examination of your firm." JX-22, at 1.

¹⁶⁵ Tr. 1374-76.

¹⁶⁶ Tr. 414-15; JX-23, at 1-3. The FINRA Rule 9550 series provides for expedited proceedings under certain circumstances. FINRA Rule 9552(a) through (h) sets forth expedited procedures specifically designed for instances in which associated persons or member firms fail to provide any information, report, material, data, or testimony required, or required to be filed, pursuant to FINRA's By-Laws or Rules.

Respondents submitted a written response to the Rule 8210 requests on March 17, 2016, thereby averting the suspensions.¹⁶⁷ The response included a short description (but no explanation) of the purpose of each of the 73 expenses FINRA had identified (for example, “Wil Felix Salary,” “Shareholder Distribution,” “Furniture and Fixtures,” and “Leasehold Improvements”) and produced copies of some canceled checks, receipts, and other documentation relating to some of the transactions listed in the Rule 8210 requests.¹⁶⁸ Even though FINRA staff deemed the response deficient, FINRA withdrew the Notice of Suspension against Respondents.¹⁶⁹

G. Felix’s Allegedly False and Misleading Testimony and Written Responses to FINRA Staff’s Information Requests

During Enforcement’s investigation of this matter, FINRA staff asked Felix to explain why CPA had required Respondents to reclassify certain of his expenses as compensation. The staff also asked Felix who prepared his 1099s for 2013 reflecting compensation from Primex. Enforcement alleges in causes four and five that Felix gave false or misleading answers to these questions. For the reasons set forth below, the Panel finds that as a factual matter Felix did not provide false or misleading information about these two subjects.

1. Felix Did Not Provide False Statements about the Reason CPA Reclassified His Expenses

FINRA staff sent Felix a Rule 8210 request for information on December 12, 2017, asking that he explain the purpose for 100 purchases from vendors on Primex’s books or ATM cash withdrawals from Primex’s bank account in 2013. FINRA asked that, for items Felix identified as legitimate Firm expenses, he describe the business purpose of each expense.¹⁷⁰

Through counsel, Felix answered the request in writing on January 5, 2018. The Complaint alleges that a portion of Felix’s answer was false or misleading.¹⁷¹ In his response, Felix wrote that he could not recall whether the 100 charges were business-related because with the passage of time he no longer had the relevant receipts or other documentation. He further claimed that Primex’s change in tax structure from a C Corporation to an S Corporation caused Respondents to change how they classified Primex’s expenses.¹⁷² The Complaint alleges that the following statements in Felix’s written response were false or misleading:

¹⁶⁷ Tr. 419, 437-38; JX-24.

¹⁶⁸ JX-24, at 3-51.

¹⁶⁹ Tr. 437-38, 469-70, 479.

¹⁷⁰ JX-41, at 2-7.

¹⁷¹ See Compl. ¶¶ 44, 96-98.

¹⁷² JX-41, at 15.

Primex changed its tax structure in 2014 from a C corporation to an S corporation, which necessitated a change in the manner in which Primex expenses were classified, and the manner in which Mr. Felix's compensation was noted for accounting purposes. This led to the reclassification of expenses by [CPA] for 2014 noted in your letter. Because this change was implemented in 2014 and on a 'going forward' basis, there was no effort to go back in time and 'reclassify' expenses for any prior year, as the 'reclassification' was done solely in conjunction with the change in tax structure implemented for 2014 and future years. At all times, Primex and Mr. Felix have followed the advice of certified public accountants in the maintenance of the corporate records of Primex.¹⁷³

Felix repeated this explanation four months later during his OTR on May 24, 2018. Enforcement alleges that Felix's testimony was untruthful and therefore he violated Rule 8210. The Complaint charges that Felix provided false or misleading answers in the following exchange with FINRA staff.¹⁷⁴

Q: Why did you continue to use a firm bank account and credit card to pay personal expenses in 2015 in light of the result of this, the 2014 audit?

A: I don't know what you're talking about.

Q: Did you use the – do you understand that in 2014, [CPA] had you reclassify \$200,000 in expenses?

A: That's because we changed from a C corp. to an S corp.¹⁷⁵

The Complaint contends that Felix's statements are false or misleading because, even though Primex's tax structure changed in 2014 from a C Corporation to an S Corporation, Felix knew that was not why CPA had him reclassify Primex's expenses for 2014 and 2015. The Complaint alleges that CPA required Respondents to reclassify the expenses because Felix had failed to demonstrate to CPA that the expenses were incurred for a legitimate business purpose.¹⁷⁶

Later during the same OTR, Felix provided the following additional answers concerning the reclassification of Primex's expenses. The Complaint does not cite this testimony as false or misleading.

¹⁷³ Compl. ¶¶ 44, 97. *See also* JX-41, at 15.

¹⁷⁴ Compl. ¶¶ 45-46, 100.

¹⁷⁵ JX-5, at 149.

¹⁷⁶ Compl. ¶ 46.

- Q: Why did this continue [allegedly improperly classifying expenses in 2015]?
- A: There was nothing that continued. We purchased things for the firm. We expensed them for the firm. And [CPA] disagreed what we bought for the firm was for the firm.
- Q: In 2014 and 2015?
- A: To 2014, [CPA] adjusted things due to the fact we went from an S Corp. to -- from a C to an S Corp. [CPA] said this is what we need to do, take them as expenses.
- Q: [CPA] told you expenses you put on your firm's books and records in your general ledger as business expenses were not, in fact, business expenses? They were personal expenses, correct?
- A: That's incorrect. That's an incorrect statement.¹⁷⁷

At the hearing, Felix offered his explanation as to why his written statement and OTR testimony were truthful.¹⁷⁸ He testified that the fact that the tax structure change coincided with CPA's first ever instruction to reclassify his expenses caused him to think of the two developments as linked. He testified that his written statement was truthful because the change in tax structure was the only thing that CPA and he discussed at the time the expenses were reclassified for 2014.¹⁷⁹ He contended that when he "was speaking to [CPA] at that time [early 2015], that [was] all we spoke about [—] the C-Corporation, S Corp., C-Corporation Corp., S Corp. Even through the whole [2014] audit . . . that's all we spoke about."¹⁸⁰ He added, "[T]hat is how I associated--that is the only thing that had actually changed at that time for us That is the reason that stuck in my mind."¹⁸¹

When specifically asked by Enforcement at the hearing if the reason for CPA's expense reclassifications for 2014 and 2015 was the change to S Corporation status, Felix answered, "That is still my understanding, correct."¹⁸² Felix testified, "We reclassified it from miscellaneous expense to shareholder distributions. That is my understanding why we did that."¹⁸³ Felix conceded that there did not exist any communication from CPA stating that the tax

¹⁷⁷ JX-5, at 187-88.

¹⁷⁸ See Tr. 1035-37.

¹⁷⁹ Tr. 1030-31.

¹⁸⁰ Tr. 1394-95.

¹⁸¹ Tr. 1395.

¹⁸² Tr. 1037. See also Tr. 1395-98.

¹⁸³ Tr. 1035-36.

structure change necessitated the reclassifications, but repeated that he “associated” the switch with the expense reclassifications “[b]ased upon multiple conversations [with CPA], based upon all of the things going on at the time [early 2015].”¹⁸⁴

After a careful review of the evidence, the Panel finds that Felix did not provide false or misleading written statements or investigative testimony about the reasons for the expense reclassifications, as alleged in causes four and five. As Felix argued at the hearing,¹⁸⁵ the allegation does not involve an independently verifiable statement of fact but calls on a factfinder to peer into Felix’s mind to determine if he really believed that the reclassifications were caused by a change in Primex’s tax structure. The Panel finds it was not unreasonable for Felix to connect the reclassifications with the fact that the Firm had just switched from a C Corporation to an S Corporation in 2014, which was the first year that CPA instructed Respondents to reclassify certain personal expenses as distributions to Felix. Even if Felix was wrong about the reasons for the reclassification of expenses, it does not lead to the conclusion that he provided false or misleading testimony and written responses.

2. Felix Did Not Give False Testimony about His Personal 1099s

In addition to alleging that Felix gave false testimony about the reasons for the expense reclassifications in 2014 and 2015, cause five alleges that, during the investigation, Felix gave false or misleading testimony that CPA had prepared two personal 1099s for him (one in the amount of \$42,200 and another one for \$42,849) to report compensation Primex paid Felix in 2013.¹⁸⁶ At the hearing, Felix stood by his investigative testimony that CPA prepared his 1099s for 2013 and denied he gave false testimony on the subject.¹⁸⁷ He said that no one besides CPA ever prepared a 1099 for him.¹⁸⁸

Respondents produced Felix’s two 1099s covering tax year 2013—on August 4, 2014 (in connection with the prior cycle examination), and April 30, 2015—in response to requests made pursuant to FINRA Rule 8210.¹⁸⁹ Enforcement cites a series of emails between Felix and CPA as evidence that CPA did not prepare the 1099s. Enforcement argues it is inculpatory that the two exchanged emails containing compensation information and copies of 1099s for the Firm’s

¹⁸⁴ Tr. 1425.

¹⁸⁵ Tr. 65-66 (Respondents’ opening statement). *See also* Respondents’ Post-Hearing Brief (“Respondents’ Post-Hrg. Br.”) 25-26.

¹⁸⁶ *See* Compl. ¶¶ 53, 55-56, 101-02.

¹⁸⁷ Tr. 1054, 1400-01.

¹⁸⁸ Tr. 1401.

¹⁸⁹ Tr. 1049-50; JX-11, at 1, 7; JX-16, at 1, 32. The Complaint does not allege that Felix provided FINRA with false or fabricated 1099s in response to the requests—only that his testimony that CPA prepared them was false or misleading. Although not explicitly alleged, the implication is that Felix’s testimony was false or misleading because, if CPA did not create the two 1099s, Felix knew that someone else did, or he created them himself. *See* Compl. ¶¶ 49-58, 101.

brokers for 2013 but no emails concerning Felix's 1099s.¹⁹⁰ On March 24, 2014, as part of CPA's tax preparation work and 2013 audit of Primex, Felix emailed CPA the names and compensation amounts for 19 Primex registered representatives so CPA could prepare their 1099s. Felix did not include his own name or the amount of his 2013 compensation in the email.¹⁹¹ The next day, March 25, 2014, CPA responded via email with copies of the 1099s that Felix had requested for the 19 brokers. CPA said he would file the forms with the IRS once Felix approved them. CPA did not include a 1099 for Felix in the email.¹⁹²

On July 18, 2014, FINRA staff sent the Firm a Rule 8210 request for copies of 1099s or W-2s reflecting compensation Primex paid Felix in 2012 and 2013, and documents supporting the compensation calculations.¹⁹³ Felix responded on August 4, 2014, by including a 1099 showing Primex paid him \$42,200 in 2013. Felix also produced an IRS Form 1125-E (Compensation of Officers) for Primex also reflecting that the Firm had paid him \$42,200 that year.¹⁹⁴

On April 24, 2015, FINRA staff made another Rule 8210 request to Respondents for compensation information for Firm brokers. The request asked Primex to produce copies of all 1099s and W-2s issued to Firm contractors or non-employees for 2013 and 2014.¹⁹⁵ On April 30, 2015, Felix produced 1099s for 2013 and 2014. Nineteen of the 1099s for 2013 were for Firm brokers or consultants whom Felix had previously identified to CPA.¹⁹⁶ With this production to FINRA, Felix included a copy of a 1099 for 2013 for himself showing compensation of \$42,849, instead of \$42,200.¹⁹⁷

At the hearing, CPA testified that his firm did not prepare either of the 1099s for Felix. CPA said he searched his firm's electronic records and they showed that he had not prepared a

¹⁹⁰ Tr. 724-25, 732-34, 778-79.

¹⁹¹ JX-116.

¹⁹² Tr. 245-46; JX-118.

¹⁹³ JX-11, at 1-2.

¹⁹⁴ JX-11, at 4, 6-7. In April 2019, a few months before Enforcement filed the Complaint, CPA produced to FINRA staff a Form 1125-E reflecting that Primex paid Felix \$35,849 in compensation in 2013. *See* Tr. 249-51; JX-50, at 1, 5. CPA acknowledged under cross-examination that the Form 1125-E for \$35,849 was not the final version and therefore was not filed with the IRS. On July 9, 2014, CPA emailed Felix for his review and approval draft copies of Primex's 2013 federal and state tax returns, which included a Form 1125-E showing compensation to Felix of \$35,849. Tr. 302-04; JX-119. A month later, on August 6, 2014, CPA emailed Felix a revised Form 1120 showing Felix's compensation in 2013 was \$42,849. Tr. 294-95; JX-120. On April 10, 2015, CPA emailed Felix a copy of Primex's 2013 corporate tax return which showed \$35,849 in compensation to Felix. JX-133, at 1-2. *See also* Tr. 1204-05.

¹⁹⁵ JX-16, at 1.

¹⁹⁶ JX-16.

¹⁹⁷ JX-16, at 32.

1099 for Felix for 2013.¹⁹⁸ In August 2018, at Enforcement's request, CPA signed a Declaration stating, among other things, that his firm had prepared 1099s for Primex's brokers for about 10 years until 2016, but that neither he nor anyone at his firm prepared a 1099 for Felix for 2012 or 2013.¹⁹⁹ At the hearing, CPA acknowledged that certain statements in his Declaration were incorrect. Since signing the Declaration in 2018, CPA said that he was able to determine that his firm had in fact created and filed a 1099 for Felix, but this had occurred only on one occasion sometime in the early 2000s, according to CPA. He reiterated at the hearing that he did not prepare one for Felix in 2012 or 2013.²⁰⁰

During cross-examination by Felix's counsel, CPA was shown multiple 1099s for Felix for 2003, 2004, 2006, 2007, 2010, 2011, and as recently as 2015. After being shown the forms, CPA did not dispute that he or someone at his firm had, in fact, generated 1099s for Felix for those years. In each instance, CPA had mailed hard copies of the 1099s to Felix instead of emailing them as he had with the 1099s for the brokers for 2013.²⁰¹ At the hearing, Enforcement's investigator acknowledged that before the hearing he had reviewed 1099s for Felix for the various years cited above, together with envelopes. He did not dispute the evidence indicating that CPA would sometimes mail Felix's 1099s to him.²⁰²

Felix testified that no one other than CPA had ever prepared tax forms for Primex.²⁰³ Felix said that he would not provide CPA with a specific dollar figure for his own compensation as he would for the Firm's brokers and independent contractors. Felix explained that CPA had a procedure to calculate his compensation.²⁰⁴ CPA would go through the Firm's general ledger and bank statements to independently verify the amount of Felix's annual compensation to include on a 1099.²⁰⁵ Felix's testimony on this issue is supported by an email he sent CPA in early March 2015 transmitting 2014 compensation figures for 20 brokers and consultants. Felix

¹⁹⁸ Tr. 251-52.

¹⁹⁹ JX-173, at 11-12.

²⁰⁰ Tr. 254. CPA further testified that, as a C Corporation, Primex should not have filed a Form 1099 for Felix in 2013. Instead, the proper reporting method, according to CPA, was to file a Form W-2 for him. CPA filed a Form 1099 for Felix in the early 2000s because Felix had asked him to do so. CPA stated that there was no harm in using a Form 1099 instead of a Form W-2 because Primex reported to the IRS that it had paid Felix compensation. Tr. 260-61.

²⁰¹ RX-8; RX-9; RX-10; RX-11; RX-12; RX-13; RX-17, at 1554. Felix testified that CPA prepared the 1099s for the years cited. Tr. 1169. CPA testified that, because Primex was an S Corporation in 2015, he prepared a Form K-1 for Felix that year, but he also acknowledged preparing a 1099, which he said was an error. Tr. 282-85; JX-174, at 2. CPA also prepared a Form K-1 for Felix for 2014 because Primex was an S Corporation. According to a Firm response to a Rule 8210 request for information, no 1099 (or W-2) was issued to Felix for 2014. *See* JX-17.

²⁰² Tr. 779-80.

²⁰³ Tr. 1059-60.

²⁰⁴ Tr. 1172-73.

²⁰⁵ Tr. 1171-74.

included in the list his own name and address but not a compensation amount. The space where the compensation figure was provided for the brokers was left blank under Felix's name.²⁰⁶

At the hearing, Felix offered an explanation as to how CPA created two conflicting 1099s for 2013, which the Panel finds reasonable. According to Felix, CPA started with a figure of \$35,849 that appeared in the Firm's general ledger, under the year-end entry for a subaccount called "Salary & Wages (Officers)."²⁰⁷ This figure was not correct, according to Felix, because CPA had failed to include withdrawals of \$2,000 and \$5,000 Felix made on September 23, 2013, which were recorded on a different general ledger subaccount called "Salary & Wages." Adding \$7,000 to \$35,849 results in compensation of \$42,849, the amount that appeared on one of the 2013 1099s. At some point, Felix explained, CPA corrected his calculations by subtracting \$648.89 that had been mistakenly allocated on the general ledger on July 27, 2013, as compensation to Felix that should have been allocated instead to Felix's brother, who also worked at Primex. This correction resulted in the other, corrected 1099 showing Primex compensated Felix \$42,200 in 2013.²⁰⁸

Enforcement also claims that Felix fabricated a third version of his 1099 for 2013 showing compensation of \$271,833.08. (The Complaint does not charge Felix with providing false or misleading testimony that this 1099 was created by CPA. But Enforcement presented evidence at the hearing concerning the third 1099 apparently to undermine Felix's sworn statements that CPA had created the other two 1099s.²⁰⁹) In late 2014, Felix sought to purchase a BMW from an automobile dealership. In connection with the purchase, on November 20, 2014, he emailed an application form to the dealership in which he stated that his annual income exceeded \$250,000.²¹⁰ The same day, he also emailed the dealership a copy of a 1099 for 2013 showing that Primex had paid him \$271,833.08.²¹¹ Felix testified that at some point CPA had made a mistake—that he had created an incorrect 1099 that was supposed to be for another

²⁰⁶ JX-127, at 3. CPA also prepared Primex's 2013 annual corporate tax documents, including Forms 1120 and 1125-E. These forms call for the disclosure of compensation paid to officers of the corporation. *See* JX-120, at 4; JX-50, at 5. It would have been reasonable and logical that, to prepare the two Primex tax forms, CPA would have had to calculate Felix's 2013 compensation first before including the amount on the Forms 1120 and 1125-E.

²⁰⁷ Tr. 1201; JX-27, at 48. Felix testified that \$35,849, a figure that CPA used on a Form 1120 he prepared for Primex for 2013, was incorrect. Tr. 1203-05; JX-133, at 2.

²⁰⁸ Tr. 1201-03; JX-27, at 47-48. Felix testified that \$42,200 was the amount of compensation that Primex reported to the IRS in 2013. Tr. 1051-52.

²⁰⁹ Compl. ¶¶ 59-60.

²¹⁰ JX-102. Felix said the BMW was intended to replace another car for Primex. He also said the dealership's application form was a "formality," and that he was not applying for a bank loan. Tr. 1062-64.

²¹¹ JX-103.

Primex broker. In March 2014, CPA in fact had created a 1099 for 2013 in the same amount for the other broker.²¹² Felix denied altering the 1099 to replace the other broker's name with his.²¹³

In addition to the fact that at least two different 1099s existed and CPA did not include Felix's 1099 in emails containing Primex brokers' 1099s, the Complaint specifically cites as evidence that the font for "2013" on his two 1099s was different from the font that appeared on the 1099s CPA created for the brokers.²¹⁴ The "2013" at the upper right of Felix's two 1099s was hollow (~~2013~~); in contrast, the font on the brokers' 1099s was filled in (**2013**). In all other respects, the 2013 1099s for Felix and the registered representatives were indistinguishable. FINRA's investigator testified that the different fonts contributed to his conclusion that Felix had fabricated the two 1099s.²¹⁵

Based on a review of the evidence, including the conflicting testimony of Felix and CPA on the issue, the Panel finds that Enforcement failed to prove that Felix's investigative testimony—that it was CPA who prepared two 2013 1099s—was false or misleading. The Panel finds the apparently different font used in the forms to be immaterial.²¹⁶ It could have been caused by printing or photocopying irregularities or the existence of different 1099 forms that the IRS made available at the time. We also are persuaded by Felix's explanations about how CPA may have calculated the two different compensation amounts which led to his creation of two 2013 1099s. We also credit Felix's testimony that there was a process for calculating his compensation that was different from the manner in which brokers' compensation was determined. This explains why his 1099 was not mentioned or included in emails between Felix and CPA that discussed brokers' compensation and their 1099s. Given the totality of the evidence, and CPA's acknowledgement that he was mistaken about what he originally told Enforcement in 2018, we do not credit CPA's testimony or his Declaration that he did not create Felix's 1099s in 2013. The Panel finds it likely that CPA in fact created Felix's two 1099s for 2013.

²¹² JX-16, at 17; JX-118, at 6. Enforcement did not ask CPA about the 2013 1099 reflecting \$271,833.08 in earnings for Felix, which would have helped shed light on the issue. However, the Panel notes that CPA had to make a small correction to the other broker's 1099, which may have led to his inadvertently creating an additional 1099 in Felix's name instead of the other broker's name. *See* Tr. 247-48; JX-169, at 2, 4, 24.

²¹³ Tr. 1071-73, 1414.

²¹⁴ *See* Compl. ¶ 55.

²¹⁵ Tr. 723-26. *See also* JX-16, at 16-32.

²¹⁶ On the IRS Forms 4868 (Application for Automatic Extension of Time to File U.S. Individual Income Tax Return) and 1120 (U.S. Corporation Income Tax Return) that were admitted into evidence, half of the year was in hollow font and the other half was filled in. *See* JX-29; JX-43, at 21-22; JX-133, at 2. One version of IRS Form 1125-E printed the number of the form (not the year) in hollow font and another version displayed it in solid font. *See* JX-11, at 6, 8.

H. Felix's Failure to Produce His 2013 IRS Wage and Income Transcript

Cause six charges Felix with failing to produce his IRS Transcript for 2013. There is no dispute that Felix did not produce the IRS Transcript or instruct the IRS to provide it to him. According to the IRS, a "tax return transcript shows most line items including [adjusted gross income] from an original tax return (Form 1040, 1040A or 1040EZ) as filed, along with any forms and schedules. It doesn't show changes made after the filing of the original return."²¹⁷

During the investigation, FINRA staff asked Felix on five occasions in 2016 and 2018 to produce his IRS Transcripts for various years, including 2013, or sign IRS Form 4506-T instructing the IRS to send them to him. On each occasion, through his counsel, Felix responded that he was not obligated to produce his IRS Transcripts or sign the Form 4506-T because the information sought was beyond the scope of Rule 8210.

FINRA asked Felix to produce IRS Transcripts for tax years 2013 to 2015 three times in 2016: on May 26, July 7, and October 17, 2016.²¹⁸ Staff conducting the cycle examination made these three requests. The Complaint does not charge Felix with failing to respond to the three 2016 requests but to two later requests made in 2018.

In 2018, Enforcement staff renewed the 2016 requests for the IRS Transcripts because Felix had not responded to the earlier requests. On August 17, 2018, FINRA staff sent its fourth request that Felix submit a signed Form 4506-T to the IRS.²¹⁹ FINRA staff sent its fifth and final request for the IRS Transcripts on September 7, 2018.²²⁰ With this request, Enforcement also cited authority for the proposition that a person subject to FINRA jurisdiction "must make records available when that person 'controls [such records] or has a right to demand them.'"²²¹ Unlike the three requests sent in 2016, in the last two requests, Enforcement informed Felix that

²¹⁷ See <https://www.irs.gov/newsroom/how-to-get-tax-transcripts-and-copies-of-tax-returns-from-the-irs>. IRS Transcripts may be ordered online, by telephone, or by mail. *Id.*

²¹⁸ See JX-26, at 2-3; JX-33; JX-34. Each of the three 2016 requests asked that Felix fax a signed Form 4506-T to the IRS and provide FINRA evidence that he sent it. On the three Forms 4506-T sent to Felix in 2016, FINRA checked the box marked "Account Transcript."

²¹⁹ JX-48, at 1-8.

²²⁰ JX-49. In the August and September 2018 Rule 8210 requests, Enforcement added tax years 2016 and 2017 to its request. JX-48, at 7; JX-49, at 9. Thus, the 2018 requests asked for IRS Transcripts for tax years 2013 through 2017. FINRA's Rule 8210 letters warned Felix that he was obligated to respond "fully, promptly, and without qualification" and a failure to respond "could expose him to sanctions, including a permanent bar . . . from the securities industry." JX-48, at 3; JX-49, at 4.

²²¹ JX-49, at 2 (citing FINRA Rule 8210, Supplementary Material .01, and a FINRA Office of Hearing Officers pre-hearing order in a prior, unrelated disciplinary proceeding.). See OHO Order 17-08 (No. 2014038847602) (Mar. 21, 2017), https://www.finra.org/sites/default/files/OHO_Order_17-08_2014038847602_0.pdf.

he could also request his IRS Transcripts online using the IRS website.²²² Enforcement's investigator testified that he asked for the IRS Transcripts in 2018 to verify if a 1099 had been filed for Felix in any of the identified tax years and, if filed, what was the amount of income reported.²²³

At the hearing, Felix testified that he declined FINRA's request to sign the Form 4506-T because "[i]t is a matter of princip[le] And after providing hundreds of thousands of documentation [sic], we took a legal position on the 8210 request as far as compelling an individual to sign documentation."²²⁴ He also said that during the investigation he tried, through his attorney, to accurately set forth his legal position about the IRS Transcripts. He further asserted, "I don't think FINRA has the right to compel me to sign documentation," and that his objection to doing so was made in good faith.²²⁵

III. Conclusions of Law

We address first the allegations in causes one and two that Respondents falsified Firm books and records and failed to file accurate quarterly FOCUS Reports in 2013, 2014, and 2015, in violation of FINRA Rules 4511 and 2010 and, in the case of Primex, in willful violation of Section 17(a) of the Exchange Act and Exchange Act Rules 17a-3 and 17a-5.

We then address Respondents' alleged violations of FINRA Rules 8210 and 2010: (i) Primex's untimely response to FINRA's request for information (cause three), and (ii) Felix's failure to produce his IRS Transcript for 2013 (cause six).

Lastly, we address the fact that Enforcement failed to prove that Felix provided false or misleading information to FINRA during its investigation, as alleged in causes four and five.

²²² On the two Forms 4506-T sent to Felix in 2018, Enforcement checked the box labeled "Form W-2, Form 1099 series, Form 1098 series, or Form 5498 series transcript." Enforcement's investigator testified that he checked that box to get information on any 1099 that was filed for Felix. Tr. 728. According to the form, "The IRS can provide a transcript that includes data from these information returns. State or local information is not included with the Form W-2 information. The IRS may be able to provide this transcript information for up to 10 years. Information for the current year is generally not available until the year after it is filed with the IRS Most requests will be processed within 10 business days." See JX-48, at 5, 7; JX-49, at 7, 9.

²²³ Tr. 726, 738.

²²⁴ Tr. 1402-03. Felix denied that he was motivated by wanting to avoid alerting the IRS to his failure to pay taxes. Tr. 1085.

²²⁵ Tr. 1403, 1411.

A. False Books and Records and Misleading or False FOCUS Reports (Causes One and Two)

1. Felix Violated FINRA Rule 2010 (Cause One)

The evidence establishes, and Respondents do not dispute, that Felix recorded personal expenses as Primex business expenses in the general ledger. Respondents concede that Felix used Primex's bank account for personal expenses.²²⁶ The expenses included many categories of spending that had no business connection to Primex, including payments for Felix's children's school tuition, toys, movie tickets, and clothing, monthly mortgage payments, and miscellaneous cash withdrawals.

Respondents argue that no one, including CPA and regulators, ever advised them before the 2014 audit that they needed to account for Felix's personal expenses differently on the Firm's general ledger.²²⁷ Once CPA required that Respondents reclassify the expenses, they did so, but only because they had no choice as the audit was late and the Firm risked penalties. Implicit in their argument is that had Felix known that the way he classified his expenses was wrong he would have treated them as Firm dividends or distributions. Respondents further contend that Enforcement failed to present legal authority that the manner of classification they used was improper.²²⁸ As they put the issue, "Enforcement never established as fact what [accounting for personal expenses] was proper. Indeed, it is still entirely unclear . . . what the law requires with regard to the classification of expenses (if anything), because Enforcement made no effort to present any evidence of what the law is or what the law says."²²⁹

The Panel rejects Felix's argument. The Panel finds that Enforcement, by reference to FINRA and SEC rules and citation to legal authorities, established how a broker-dealer should properly reflect payment of personal expenses to officers and employees on its books and records, including the general ledger.

Cause one alleges that Felix violated FINRA Rule 2010 by falsifying Primex's books and records from 2013 to 2015 by misclassifying his personal expenses as business expenses of the

²²⁶ Tr. 810-11, 1538; Respondents' Post-Hrg. Br. 2 ("It was established at the hearing that, from time to time, Mr. Felix used the Primex bank account to make personal purchases.").

²²⁷ Respondents' Post-Hrg. Br. 3-4.

²²⁸ Respondents go so far as to contend that the Complaint "contains no reference to any legal authority concerning the classification of personal expenses, nor any citation to a law, rule, regulation or policy that would suggest (much less establish) that what Mr. Felix was doing was wrong. To the extent that Enforcement asserts that Mr. Felix was doing something wrong or improper, it has never provided notice to him of any authority for that assertion, such that he could challenge that authority or the basis for Enforcement's position." Respondents' Post-Hrg. Br. 10 n.61.

²²⁹ Respondents' Post-Hrg. Br. 10. They add that "[n]o witness testified about any established law, rule, regulation, policy or guidance that requires the personal expenses of an officer of a broker dealer to be classified in any particular manner," and, therefore, "the Panel is left with no benchmark or standard against which to judge Mr. Felix's conduct." Respondents' Post-Hrg. Br. 9-10.

Firm on its general ledger.²³⁰ Rule 2010 obligates members and associated persons in the conduct of their business to “observe high standards of commercial honor and just and equitable principles of trade.”

An associated person violates FINRA Rule 2010 by violating another FINRA or SEC rule, or by engaging in business-related conduct unethically or in bad faith.²³¹ A finding of scienter is not needed to establish a violation of the Rule.²³² The Rule establishes an ethical standard that requires associated persons to act with integrity and honesty in the course of their business even though the misconduct may not be illegal.²³³ FINRA’s disciplinary authority under Rule 2010 is “broad enough to encompass business-related conduct that is inconsistent with just and equitable principles of trade, even if that activity does not involve a security.”²³⁴ The principal consideration is whether the misconduct reflects on an associated person’s ability to comply with regulatory requirements necessary to the proper functioning of the securities industry and protection of the public.²³⁵ Falsifying records is an example of misconduct that adversely reflects on a person’s ability to comply with regulatory requirements and has been held to be a practice inconsistent with just and equitable principles of trade.²³⁶ Accordingly, an associated person who falsifies Firm documents engages in unethical conduct that violates FINRA Rule 2010.²³⁷

The Panel finds that it should have been obvious to Felix that recording his personal expenses as business expenses, thereby understating his income and overstating Primex’s expenses, was wrong. As Primex’s FINOP, Felix should have understood the importance of maintaining an accurate general ledger. Felix had an ethical obligation to record the expenses

²³⁰ Compl. ¶ 68.

²³¹ *Calvin David Fox*, 56 S.E.C. 1371, 1376-77 (2003).

²³² *Robert E. Kauffman*, 51 S.E.C. 838, 839 n.5 (Nov. 18, 1993) (To establish this violation, “[t]he most that is required is a finding of bad faith or unethical conduct.”), *petition for review denied*, No. 94-3011, 1994 U.S. App. LEXIS 43727(3d Cir. Oct. 20, 1994).

²³³ See *Robert Marcus Lane*, Exchange Act Release No. 74269, 2015 SEC LEXIS 558, at *21 n.20 (Feb. 13, 2015) (stating that this “general ethical standard . . . is broader and provides more flexibility than prescriptive regulations and legal requirements. [FINRA Rule 2010] protects investors and the securities industry from dishonest practices that are unfair to investors or hinder the functioning of a free and open market, even though those practices may not be illegal or violate a specific rule or regulation.”).

²³⁴ *Daniel D. Manoff*, 55 S.E.C. 1155, 1162 (2002) (quoting *Vail v. SEC*, 101 F.3d 37, 39 (5th Cir. 1996) (per curiam)).

²³⁵ See *James A. Goetz*, 53 S.E.C. 472, 477 (1998).

²³⁶ *Ramiro Jose Sugranes*, 52 S.E.C. 156, 157 (1995); *Jeffrey Michael Miller*, 51 S.E.C. 1027, 1029 (1994); see also *Dep’t of Enforcement v. Salaverria*, No. C07040077, 2005 NASD Discip. LEXIS 10, at *16-17 (NAC Dec. 12, 2005) (providing employer firm with a fictitious score report falsely representing that respondent passed a registration examination is conduct that falls within the broad ethical principle included in FINRA Rule 2010).

²³⁷ *Dep’t of Enforcement v. Mielke*, No. 2009019837302, 2014 FINRA Discip. LEXIS 24, at *5, *40 (NAC July 18, 2014) (misstatements on firm compliance questionnaires violated NASD Rule 2110, the predecessor to FINRA Rule 2010), *aff’d*, Exchange Act Release No. 75981, 2015 SEC LEXIS 3927 (Sept. 24, 2015).

accurately. Personal, living, or family expenses generally do not qualify as business expenses, and certain personal expenses that may serve some business purpose, such as clothing or eyeglasses, have been held to be “so inherently personal” that they do not qualify as a business expenses.²³⁸

The Panel finds that, by recording personal expenses as business expenses, Felix’s conduct was unethical and in bad faith,²³⁹ and therefore he failed to “observe high standards of commercial honor and just and equitable principles of trade” as required by FINRA Rule 2010.

2. Respondents Violated FINRA Rules 4511 and 2010 and Primex Willfully Violated Section 17(a) of Exchange Act and Exchange Act Rules 17a-3 and 17a-5 (Cause Two)

Cause two charges that both Respondents violated FINRA Rules 4511 and 2010. Rule 4511(a) requires FINRA members to “make and preserve books and records as required under FINRA’s rules, the Exchange Act and the applicable Exchange Act rules.”²⁴⁰ The Complaint charges that Felix and Primex (acting through Felix) misclassified Felix’s personal expenses on the general ledger from 2013 to 2015, causing Primex’s books and records to be inaccurate by overstating its business expenses and understating distributions, or compensation, paid to Felix. Cause two further alleges that, by misclassifying his expenses, Felix also caused Primex to file inaccurate FOCUS Reports.²⁴¹

Entering inaccurate information in a member firm’s general ledger and FOCUS Reports violates both Rule 4511’s requirement to keep accurate books and records and Rule 2010’s requirement that members observe high standards of commercial honor and just and equitable

²³⁸ *Fred W. Amend Co. v. Comm’r*, 55 T.C. 320, 326 (Tax Ct. 1970), *aff’d*, 454 F.2d 399 (7th Cir. 1971). *See also* I.R.C. § 162(a) (defining “trade or business expenses” as the “ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business”) and § 262(a) (stating that, with limited exceptions, no deduction shall be allowed for “personal, living, or family expenses”).

²³⁹ Causing a firm to violate its recordkeeping obligations is a violation of FINRA Rule 2010. *See James S. Pritula*, 53 S.E.C. 968, 976-77 (1998) (FINOP’s failure to maintain accurate trial balances and firm books and records caused the firm’s net capital and recordkeeping violations, in violation of NASD Rule 2110, the predecessor to FINRA Rule 2010). *See also Dep’t of Enforcement v. Taylor*, No. 20070094468, 2011 FINRA Discip. LEXIS 17, at *15 (NAC Aug. 5, 2011) (Associated persons who cause their firms to violate an SEC rule “can be held liable under NASD Rule 2110,” the predecessor to FINRA Rule 2010); *Robert Tretiak*, 56 S.E.C. 209, 223-26 (2003) (affirming finding that respondent violated NASD Rule 2110 by causing a violation of an SEC rule).

²⁴⁰ *Dep’t of Enforcement v. Ortiz*, No. E0220030425-01, 2007 FINRA Discip. LEXIS 3, at *14 n.14 (NAC Oct. 10, 2007), *aff’d*, Exchange Act Release No. 58416, 2008 SEC LEXIS 2401 (Aug. 22, 2008).

²⁴¹ Compl. ¶¶ 76-78.

principles of trade.²⁴² A finding of scienter is not required to establish a violation of Rule 4511, nor is it necessary to prove that inaccuracies in a member's records are material.²⁴³

Cause two further charges that Primex willfully violated Section 17(a)(1) of the Exchange Act and Exchange Act Rules 17a-3 and 17a-5.²⁴⁴ Section 17(a) requires broker-dealers to make and keep records as prescribed by the SEC. Exchange Act Rule 17a-3(a)(2) requires firms to make and keep current “[l]edgers (or other records) reflecting all assets and liabilities, income and expense and capital accounts.” Exchange Act Rule 17a-5(a)(2)(iii) requires broker-dealers like Primex that do not clear transactions or carry customer accounts to file FOCUS Reports containing Part IIA of Form X-17A-5 at least on a quarterly basis. FOCUS Reports enable periodic monitoring of a broker-dealer's financial soundness.²⁴⁵

Compliance with recordkeeping rules is essential to the proper functioning of the regulatory process. As the SEC has noted, provisions of the Exchange Act protect the public interest and investors by “requir[ing] that member firms conduct their business operations with regularity and that their records accurately reflect those operations.”²⁴⁶ The SEC “has stressed the importance of the records that broker-dealers are required to maintain pursuant to the Exchange Act, describing them as the ‘keystone of the surveillance of brokers and dealers by our staff and by the securities industry’s self-regulatory bodies.’”²⁴⁷ The obligation to maintain records and file reports includes a requirement that such records and reports be true and

²⁴² Conduct that violates FINRA Rule 4511 also violates FINRA Rule 2010's requirement that members observe high standards of commercial honor and just and equitable principles of trade in the conduct of their business. See *Dep't of Enforcement v. Trevisan*, No. E9B2003026301, 2008 FINRA Discip. LEXIS 12, at *27-29 (NAC Apr. 30, 2008) (finding that an associated person who entered inaccurate information into firm's records violated NASD Rules 3110 and 2110 (the predecessors to FINRA Rules 4511 and 2010, respectively)); *Dep't of Enforcement v. N. Woodward Fin. Corp.*, No. 2011028502101, 2016 FINRA Discip. LEXIS 35, at *14 n.16 (NAC July 19, 2016) (“A violation of any FINRA rule is also a violation of FINRA Rule 2010.”).

²⁴³ *Joseph G. Chiulli*, 54 S.E.C. 515, 522 (2000) (NASD Rule 3110, the predecessor to FINRA Rule 4511, “has no scienter requirement.”). See also *Palm State Equities, Inc.*, 52 S.E.C. 333, 336 (1995) (“Exchange Act Rule 17a-3 requires that a broker-dealer keep and maintain current books and records. It does not permit a broker-dealer to avoid this requirement merely because, in retrospect, the resulting adjustments prove to be immaterial.”)

²⁴⁴ Compl. ¶¶ 77, 79-80. A violation of an SEC Rule is also a violation of FINRA Rule 2010. See *L.H. Alton & Co.*, 53 S.E.C. 1118, 1121-22 (1999) (upholding violation of NASD Rule 2110, the predecessor to FINRA Rule 2010, where respondent filed inaccurate FOCUS Reports in violation of Exchange Act Rule 17a-5), *petition for review denied*, No. 99-70383, 2000 U.S. App. LEXIS 17926 (9th Cir. July 14, 2000); *Fox & Co. Invs., Inc.*, 58 S.E.C. 873, 890-93 (2005).

²⁴⁵ *Meyers Assocs., L.P.*, Exchange Act Release No. 86497, 2019 SEC LEXIS 1869, at *42 n.75 (July 26, 2019) (citing *E. Magnus Oppenheim & Co., Inc.*, 58 S.E.C. 231, 232 n.3 (2005)).

²⁴⁶ See *Meyers Assocs., L.P.*, 2019 SEC LEXIS 1869, at *46-47 & n.82 (citing *Mielke*, 2015 SEC LEXIS 3927, at *51).

²⁴⁷ *Trevisan*, 2008 FINRA Discip. LEXIS 12, at *36 (quoting *Edward J. Mawod & Co.*, 46 S.E.C. 865, 873 n.39 (1977), *aff'd*, 591 F.2d 588 (10th Cir. 1979)).

correct.²⁴⁸ Although there is no allegation that Felix’s use of Primex’s funds was improper, Respondents were required to record the expenses accurately in the general ledger and FOCUS Reports. The SEC has specifically held that it is a violation of FINRA Rules 4511 and 2010 and Section 17(a) of the Exchange, together with Exchange Act Rules 17a-3 and 17a-5, to record a firm’s payment of personal expenses as business expenses. Instead, according to the SEC, such payments should be recorded as payment of compensation to the recipient.²⁴⁹

Therefore, it was improper for Respondents to record Felix’s expenses on the general ledger as Firm business expenses instead of compensation to Felix. By classifying payments made to Felix for his personal expenses as business expenses, Primex inaccurately recorded his compensation on its general ledger and FOCUS Reports.²⁵⁰ Accordingly, the Panel finds that Respondents failed to maintain adequate books and records. Felix caused Primex to inaccurately record \$248,893 in personal expenses in its general ledger and to file FOCUS Reports that inaccurately reported such expenses as business expenses. As a result of this conduct, Respondents violated FINRA Rules 4511 and 2010²⁵¹ and Primex violated Section 17(a)(1) of the Exchange Act and Exchange Act Rules 17a-3 and 17a-5.

3. Primex is Subject to Statutory Disqualification

The Complaint alleges that Primex’s violations of Section 17(a) of the Exchange Act and Exchange Act Rules 17a-3 and 17a-5 were willful.²⁵² If it acted willfully, Primex is subject to statutory disqualification.²⁵³ Article III, Section 3 of FINRA’s By-Laws provides that no member shall continue as a member if it becomes subject to disqualification. Article III, Section 4 of FINRA’s By-Laws states that a member is subject to disqualification if the member is subject to

²⁴⁸ *Dep’t of Enforcement v. Inv. Mgmt. Corp.*, No. C3A010045, 2003 NASD Discip. LEXIS 47, at *20 (NAC Dec. 15, 2003). See also *Dep’t of Enforcement v. Siesennop*, No. 2010025132201, 2012 FINRA Discip. LEXIS 67, at *29 (OHO Oct. 22, 2012) (citing *Voss & Co., Inc.*, 47 S.E.C. 626, 632 n.16 (1981)).

²⁴⁹ See *Meyers Assocs., L.P.*, 2019 SEC LEXIS 1869, at *45-46 & n.80 (finding that respondent firm’s recording of reimbursements of two employees’ personal expenses exceeding \$60,000 as firm business expenses violated FINRA Rules 4511 and 2010 and Section 17(a)(1) of the Exchange Act and Exchange Act Rules 17a-3, 17a-4, and 17a-5) (citing 26 U.S.C. § 61(a)(1) (defining “gross income” as “all income from whatever source derived,” including “fringe benefits”)); see also Internal Revenue Service, Executive Compensation-Fringe Benefits Audit Techniques Guide (02-2005), 2005 WL 1500302, at *3 (Feb. 2005) (“Personal expenses paid on behalf of executives are taxable fringe benefits that should be included in wages.”)).

²⁵⁰ See *Orlando Joseph Jett*, 57 S.E.C. 350, 396-97 (2004) (finding that a firm’s misstatement of profits in general ledger and FOCUS Reports violated Section 17(a)(1) of the Exchange Act and Exchange Act Rules 17a-3 and 17a-5).

²⁵¹ Primex’s violations of the Exchange Act and Exchange Act Rules also violate FINRA Rule 2010. See *L.H. Alton & Co.*, 53 S.E.C. at 1121-22 (upholding violation of predecessor to FINRA Rule 2010 where respondent filed inaccurate FOCUS Reports in violation of Exchange Act Rule 17a-5).

²⁵² Compl. ¶ 79.

²⁵³ *Dep’t of Enforcement v. Merrimac Corp. Sec., Inc.*, No. 2007007151101, 2010 FINRA Discip. LEXIS 41, at *55 n.48 (OHO Dec. 8, 2010) (recordkeeping violation was willful even if firm was attempting to comply with rules), *aff’d*, 2012 FINRA Discip. LEXIS 43 (Bd. of Governors May 2, 2012).

one of the disqualifying events listed in Section 3(a)(39) of the Exchange Act. One such disqualifying event identified in Section 3(a)(39)(F) and Section 15(b)(4)(D) of the Exchange Act is a finding that a violation of any provision of the Exchange Act was willful.

We find that the evidence shows that Primex, acting through Felix, acted willfully. Felix testified that he intentionally used Primex funds for his personal expenses and recorded them as Firm business expenses. In any event, willfulness does not require intent to commit misconduct or knowledge of committing an error. “Willfulness” is defined broadly and means intentionally committing the act that constitutes the violation—not knowingly committing a rule violation.²⁵⁴ “[A]s used in the federal securities laws, ‘willful’ means something other than involving ‘deliberate or reckless disregard of a regulatory requirement.’”²⁵⁵ A violation is deemed willful if “the person charged with the duty knows what he is doing.”²⁵⁶ The person need not be aware that he is violating the Exchange Act or an Exchange Act Rule.²⁵⁷

The Panel therefore finds that Primex’s violations of Section 17(a) of the Exchange Act and Exchange Act Rules 17a-3 and 17a-5 were willful. Primex is accordingly subject to statutory disqualification.

B. Respondents Violated FINRA Rules 8210 and 2010 (Causes Three and Six)

FINRA Rule 8210(a)(1) provides that, for purposes of an investigation, complaint, examination, or proceeding, FINRA staff may require a member, person associated with a member, or any other person subject to FINRA’s jurisdiction to provide information orally, in writing, or electronically and to testify at a location specified by FINRA staff, with respect to any matter involved in the investigation, complaint, examination, or proceeding. Subsection (a)(2) of the Rule further gives FINRA the authority to inspect and copy the books, records, and accounts of a member firm and associated person with respect to any matter involved in the investigation, complaint, examination, or proceeding that are in the firm’s or associated person’s possession, custody, or control. FINRA Rule 8210(c) provides that no member or person shall fail to provide information or testimony pursuant to the Rule. A failure to provide documents or information requested pursuant to FINRA Rule 8210 is a violation of FINRA Rules 8210 and 2010.²⁵⁸

²⁵⁴ *Mathis v. SEC*, 671 F.3d 210, 217 (2d Cir. 2012); *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000); *Tager v. SEC*, 344 F.2d 5, 8 (2d Cir. 1965); *Leaddog Capital Mkts., LLC*, Initial Decision Release No. 468, 2012 SEC LEXIS 2918, at *38-39 (Sept. 14, 2012) (collecting cases).

²⁵⁵ *Next Fin. Grp., Inc.*, Initial Decision Release No. 349, 2008 SEC LEXIS 1393, at *59 (June 18, 2008).

²⁵⁶ *Wonsover*, 205 F.3d at 414. *See also Dep’t of Enforcement v. Jones*, No. 2015044782401, 2018 FINRA Discip. LEXIS 37, at *57-59 (OHO Oct. 17, 2018) (finding firm’s violations of SEC recordkeeping rules were willful and therefore the firm was subject to statutory disqualification), *appeal docketed* (NAC Nov. 13, 2018).

²⁵⁷ *Mathis*, 671 F.3d at 217 (interpreting Sections 3(a)(39)(F) and 15(b)(4)(A) of the Exchange Act).

²⁵⁸ *Dep’t of Enforcement v. Gallagher*, No. 2008011701203, 2012 FINRA Discip. LEXIS 61, at *11 n.9 (NAC Dec. 12, 2012).

1. Primex Responded Untimely to November 2015 Requests for Information and Documents (Cause Three)

Cause three alleges that Primex violated FINRA Rules 8210 and 2010 by responding in an untimely manner to Enforcement's November 3 and November 17, 2015 requests for information.²⁵⁹ Respondents acknowledge that Primex did not respond until March 17, 2016, more than three months after the original due date of November 10, 2015, and after FINRA had initiated suspension proceedings under FINRA Rule 9552. Respondents do not dispute receiving the requests.²⁶⁰ The information was directly material to FINRA's investigation into Respondents' recordkeeping practices. FINRA was trying to determine if Felix spent Firm money on himself and whether the expenses were recorded properly in Firm records. Primex acknowledges that the information FINRA sought was "undoubtedly important" but claims that the late response "does not appear to have materially affected" the investigation.²⁶¹ Primex notes that more than three years passed before Enforcement filed the Complaint, during which time FINRA continued to send Rule 8210 requests to which Felix and Primex responded.

Primex argues that under the circumstances the three-month delay was excusable and does not rise to the level of a Rule 8210 violation. Primex contends that it did not ignore Enforcement's two requests and remained in contact with FINRA. Felix phoned the staff shortly after receiving the first request and orally asked for an extension of time to respond. Respondents contend that, unlike a request for copies of specific documents, the November 2015 requests were not easy to respond to. The requests required locating documents and describing the purpose of 73 of Felix's purchases spanning 15 months. Respondents also argue that Felix was waiting for a response from FINRA to his request for an explanation of which rule or regulation Respondents may have violated in connection with Felix's expenses.²⁶² The tardiness, they say, was also caused in part by the SEC's surprise on-site examination in January 2016. Felix also spent time responding to FINRA's examination report, issued in December 2015. They further argue that they had just moved Primex into new offices in New York City, and Felix could not immediately put his hands on the materials needed to respond to the requests.²⁶³ Finally, Primex argues that its delay in responding was exacerbated by Felix's preparation of Primex's 2015 year-end FOCUS Report and shortly thereafter the 2015 annual audit.²⁶⁴

Since FINRA lacks subpoena power, it must rely upon Rule 8210 "to police the activities of its members and associated persons."²⁶⁵ "The failure to respond to [FINRA's] information

²⁵⁹ Compl. ¶¶ 86-88, 93.

²⁶⁰ See Felix Ans. ¶¶ 86-88, 90-92; Primex Ans. ¶¶ 86-88, 90-92.

²⁶¹ Respondents' Post-Hrg. Br. 19.

²⁶² Respondent's Post-Hrg. Br. 19-20.

²⁶³ Felix Ans. ¶ 87; Primex Ans. ¶ 87; Respondents' Post-Hrg. Br. 19-20.

²⁶⁴ Respondents' Post-Hrg Br. 21.

²⁶⁵ *Joseph Patrick Hannan*, 53 S.E.C. 854, 858-59 (1998).

requests frustrates [FINRA's] ability to detect misconduct, and such inability in turn threatens investors and markets.”²⁶⁶ The National Adjudicatory Council has stated that member firms and associated persons should “assign the utmost priority to responding to FINRA’s Rule 8210 requests.”²⁶⁷

Primex’s efforts to justify its delay in responding do not excuse its failure. FINRA Rule 8210 does not require that FINRA explain the purpose or relevance of a request for information.²⁶⁸ Felix could not condition Primex’s response on FINRA staff’s justifying its need for the information requested. His apparent initial belief that FINRA did not need the information provides no excuse for his delay in producing it.²⁶⁹ As the SEC has stated, a FINRA “member may not second guess or impose conditions on” a request for information.²⁷⁰ In any event, FINRA staff had explained to Felix the basis of its request even though it had no obligation to do so.

The Panel finds that, notwithstanding Respondents’ various explanations, a delay of three months is not excusable. Accordingly, the Panel finds that by providing a late response to two FINRA requests for information and documents Primex violated FINRA Rules 8210 and 2010, as alleged in cause three of the Complaint.²⁷¹

²⁶⁶ *PAZ Sec., Inc.*, Exchange Act Release No. 57656, 2008 SEC LEXIS 820, at *13 (Apr. 11, 2008), *petition for review denied*, 566 F.3d 1172 (May 29, 2009).

²⁶⁷ *Dep’t of Enforcement v. Plunkett*, No. 2006005259801, 2012 FINRA Discip. LEXIS 1, at *27 (NAC Feb. 21, 2012), *remanded for reconsideration of sanctions*, Exchange Act Release No. 69766, 2013 SEC LEXIS 1699 (June 14, 2013).

²⁶⁸ *See Morton Bruce Erenstein*, Exchange Act Release No. 56768, 2007 SEC LEXIS 2596, at *13 (Nov. 8, 2007) (Rule 8210 “does not require that [FINRA] explain its reasons for making the information request or justify the relevance of any particular request.”), *petition for review denied*, 316 F. App’x 865 (11th Cir. 2008).

²⁶⁹ *Michael David Borth*, 51 S.E.C. 178, 181 (1992) (FINRA’s “Rules do not permit second guessing of [FINRA’s] requests.”).

²⁷⁰ *Hannan*, 53 S.E.C. at 859 (citations omitted).

²⁷¹ *See Erenstein*, 2007 SEC LEXIS 2596, at *23-24 (rejecting respondent’s argument that his counsel’s initial objections to Rule 8210 request excused his initial failure to comply); *CMG Inst’l Trading, LLC*, Exchange Act Release No. 59325, 2009 SEC LEXIS 215, at *29-30 (Jan. 30, 2009) (finding that respondent firm and its president did not respond completely and in a timely manner to a request for information); *Dep’t of Enforcement v. Evansen*, No. 2010023724601, 2014 FINRA Discip. LEXIS 10, at *27-28 (NAC June 3, 2014) (finding that a response to a Rule 8210 request made after FINRA pursued expedited proceedings under Rule 9552 was untimely), *aff’d*, Exchange Act Release No. 75531, 2015 SEC LEXIS 3080 (July 27, 2015).

2. Felix Violated Rule 8210 by Failing to Produce His 2013 IRS Transcript (Cause Six)

Cause six charges Felix with failing to respond to two FINRA Rule 8210 requests dated August 17 and September 7, 2018, to produce his IRS Transcript for tax year 2013.²⁷² The requests asked Felix, if he did not have a copy of the IRS Transcripts, to request them from the IRS by submitting a Form 4506-T that Enforcement had completed and enclosed with each request, or to do so online using the IRS website. Enforcement contends that the information in the IRS Transcript was material to its investigation of Respondents.²⁷³ There is no dispute that Felix failed to produce any IRS Transcripts. For the reasons set forth below, the Panel majority finds that Felix violated FINRA Rules 8210 and 2010 by not producing the 2013 IRS Transcript or asking the IRS for it.

FINRA has consistently interpreted “books, records, and accounts” to include records such as tax returns.²⁷⁴ Furthermore, whether a requested record is “with respect to any matter involved in” a FINRA investigation, is a determination made by the FINRA staff.²⁷⁵ Rule 8210 does not require that FINRA “explain its reasons for making the information request or justify the relevance of any particular request.”²⁷⁶ As the SEC has stated, “The determination of when it is appropriate for an investigation to proceed is a matter for [FINRA] to decide, not the respondent.”²⁷⁷ The requirement to respond fully and completely to a Rule 8210 request is “unequivocal,” “unqualified,” and “mandatory.”²⁷⁸

Supplementary Material .01 to Rule 8210 states that a member firm, associated person, or person under FINRA’s jurisdiction must make available “books, records or accounts” even in instances when those materials are in the possession of another person or entity when the firm, associated person, or person under FINRA’s jurisdiction “controls or has a right to demand them.” Supplementary Material .01 also states that materials within the ambit of Rule 8210 include records relating to a member’s “operation as a broker-dealer or relating to the person’s association with the member.”

²⁷² Compl. ¶¶ 107-09; FINRA staff’s Rule 8210 letters included requests that Felix also produce IRS Transcripts for 2012 to 2017, but the Complaint does not charge him with failing to provide IRS Transcripts for all of those years. See JX-48, at 5-7; JX-49, at 7-9.

²⁷³ Compl. ¶¶ 107-09. FINRA asked Felix to produce IRS Transcripts on at least three earlier occasions than those alleged in the Complaint: May 26, July 7, and October 17, 2016. See JX-26, at 3; JX-33; JX-34.

²⁷⁴ See *Erenstein*, 2007 SEC LEXIS 2596, at *12.

²⁷⁵ *Id.*

²⁷⁶ *Id.* at *13.

²⁷⁷ *Michael J. Markowski*, 54 S.E.C. 838, 838 (2000).

²⁷⁸ *Dep’t of Enforcement v. Lundgren*, No. FPI150009, 2016 FINRA Discip. LEXIS 2, at *12 (NAC Feb. 18, 2016) (collecting cases).

In December 2012, the SEC approved FINRA’s proposed amendments to Rule 8210 that broadened its reach to include information and documents within a member’s or associated person’s “control.”²⁷⁹ The SEC noted that, in proposing the revisions to include the word “control,” in addition to possession and custody, FINRA intended to require members or persons covered by Rule 8210 “to provide, for example, records that they have the legal right, authority, or ability to obtain upon demand.”²⁸⁰ The language change, the SEC noted, “parallels the Federal Rules of Civil Procedure regarding document requests and subpoenas for documents.”²⁸¹

In early 2013, FINRA informed members and associated persons in Regulatory Notice 13-06 that the SEC had approved the amendments to Rule 8210. The revised Rule and Supplementary Material .01, FINRA said, “indicate[] that all aspects of the relationship between a broker-dealer and its associated persons are potentially the subject of a Rule 8210 request.”²⁸²

During the investigation, Felix offered justifications for his decision to not produce the IRS Transcripts. He repeated these explanations at the hearing. In response to FINRA’s first request, made in May 2016, Felix’s attorney told FINRA that he did not have the IRS Transcripts and “respectfully decline[d]” to sign the Form 4506-T that Enforcement had enclosed with its request.²⁸³ In July 2016, again through his counsel, Felix followed up in response to a second Enforcement request (dated July 7, 2016) that he sign the IRS form. His attorney wrote, “[I]t is unclear to us at this point how this request for IRS account transcripts relates to FINRA’s investigation and enforcement of the federal securities laws.” Because Felix had demonstrated to FINRA that he had not filed tax returns for the years in question, Felix’s attorney added, “[W]e are not sure what information FINRA seeks to glean from an IRS account statement.”²⁸⁴

²⁷⁹ *Order Granting Accelerated Approval of a Proposed Rule Change*, Exchange Act Release No. 68386, 2012 SEC LEXIS 3798, at *25 (Dec. 7, 2012).

²⁸⁰ *Id.* at *5 n.10 (citing *Camden Iron & Metal v. Marubeni Am. Corp.*, 138 F.R.D. 438, 441 (D.N.J. 1991) (“Federal courts construe ‘control’ very broadly under [Federal] Rule [of Civil Procedure] 34.”). *See also* *FINRA Notice of Filing of Proposed Rule Change to Amend Rule 8210*, 74 Fed. Reg. 54614, 54615 n.4 (Oct. 22, 2009).

²⁸¹ *Order Granting Accelerated Approval of a Proposed Rule Change*, 2012 SEC LEXIS 3798, at *5 & n.11 (citing Fed. R. Civ. P. 34).

²⁸² The revisions to FINRA Rule 8210 went into effect on February 25, 2013. FINRA Regulatory Notice 13-06, at 2 (Jan. 2013), <https://www.finra.org/rules-guidance/notices/13-06>. FINRA noted that the rule change was prompted by an adverse 2006 SEC opinion, in which the SEC expressed skepticism regarding FINRA’s argument that an associated person was required to provide documents because they were in his possession and control. *See Jay Alan Ochanpaugh*, Exchange Act Release No. 54363, 2006 SEC LEXIS 1926, at *19 (Aug. 25, 2006). The SEC accepted, for the purpose of its decision, that a “possession and control” standard applied, but concluded that “[FINRA] ha[d] not met its burden of proof to meet even that standard.” *Id.* at *22. FINRA said that amending the rule to add the phrase “possession, custody or control” removed this uncertainty identified in the *Ochanpaugh* opinion. FINRA Regulatory Notice 13-06, at 2 n.3.

²⁸³ JX-26, at 11. Felix provided FINRA with copies of IRS forms he had filed to show that he had applied for extensions to file his returns from for years 2013 to 2015. JX-26, at 11.

²⁸⁴ JX-33, at 18.

After receiving the third request (dated October 17, 2016) that Felix submit the Form 4506-T to the IRS, Felix’s counsel wrote that “[they were] not aware of any authority for the proposition that FINRA could use Rule 8210 to compel an individual to sign his name to an IRS form” to obtain IRS Transcripts. He disputed the legal authorities Enforcement had previously cited in support of its request because they did not concern IRS Transcripts and did not involve compelling a person to sign a form granting permission to obtain records “that were not made or kept by the individual.”²⁸⁵ Felix argued that he produced “the equivalent of his [tax] returns” when he produced copies of his extension applications. Asking him to produce the IRS Transcripts, counsel wrote, is “a different matter entirely.”²⁸⁶

Felix further disputed Rule 8210’s reach in his October 31, 2016 letter to Enforcement staff. Relying on Supplementary Material .01, Felix’s attorney wrote that IRS Transcripts are not books, records, or accounts “of” Felix for the purposes of Rule 8210. The information Enforcement sought, counsel wrote, “are IRS records, created and maintained solely by the IRS,” adding that Felix “played no role in the creation or maintenance of those records, nor has he ever seen them, or, prior to the instant dispute, ever heard of them.”²⁸⁷ Felix argued that there is a “significant difference between records ‘of’ Mr. Felix (records that associated persons ‘make or keep,’ such as tax returns) and records created solely by the IRS (such as account transcripts).”²⁸⁸ Felix’s attorney concluded by saying that his client had not “failed to produce” his IRS Transcripts, as FINRA claimed in its Rule 8210 letter, because he had not seen any legal authority that FINRA had the power to compel the production of such a record under Rule 8210.²⁸⁹

In response to FINRA’s fourth request, dated August 17, 2018, Felix’s counsel repeated his argument that an IRS Transcript is an IRS document and not one “created, signed, utilized, owned or maintained by” Felix. Felix had never seen such a document, the attorney wrote, “much less had possession, custody or control over it.”²⁹⁰ Felix’s counsel added that since exchanging correspondence with Enforcement in 2016 about the requested materials, he had not received any new compelling authority that FINRA was entitled to the information.²⁹¹

FINRA staff sent its final request for the IRS Transcripts on September 7, 2018. Felix’s counsel refined his argument that Felix was not lawfully obligated to produce the IRS Transcripts. In a September 14, 2018 letter, he said that they are beyond the scope of FINRA’s

²⁸⁵ JX-34, at 7.

²⁸⁶ JX-34, at 8. Felix did not dispute FINRA’s right, under Rule 8210, to obtain a registered person’s personal tax returns. JX-34, at 8.

²⁸⁷ JX-34, at 8.

²⁸⁸ JX-34, at 8.

²⁸⁹ JX-34, at 8.

²⁹⁰ JX-48, at 12.

²⁹¹ JX-48, at 12.

authority because an IRS Transcript is not a record of the member or associated person and they do not relate to the member firm's or associated person's "operation as a broker-dealer or relat[e] to the person's association with the member."²⁹² Felix conceded that the scope of Rule 8210 is "broad" but countered that it is "not all-encompassing, and it does have limits."²⁹³

Felix argues in his post-hearing brief that he was not "in possession" of the IRS records, and therefore objected to Enforcement's use of Rule 8210 to compel him to submit an IRS form to obtain the records.²⁹⁴ He again contended that "the scope of Rule 8210 does not extend to IRS Transcripts, nor can it be used [to] force him to sign an IRS form."²⁹⁵

Enforcement sees things differently. It argues that the plain text of Rule 8210 obligates Felix to produce the 2013 IRS Transcript because he had "control" over its production by simply asking the IRS for it. According to Enforcement, the request was directly connected with its investigation of the misclassification of Felix's expenses as business expenses on Primex's books and records. The IRS Transcript for 2013 was material to the investigation because it would have shown the amount of income Respondents determined that Felix earned that year, an issue that was at the heart of the disagreement between FINRA and Respondents over what constituted personal versus business expenses. Enforcement also says that the IRS Transcript may have led to evidence relevant to whether any of the 1099s Felix produced, including the one he provided to the car dealership, was fabricated.²⁹⁶

The Panel majority finds that Rule 8210 obligated Felix to obtain his 2013 IRS Transcript. FINRA sought in its Rule 8210 requests records that relate to the compensation Felix received from Primex in his capacity as an associated person. Even though the IRS maintained the tax information, the information was personal to Felix and related to his association with a FINRA member firm. The 2013 IRS Transcript FINRA wanted therefore was "of" Felix because it concerned his own tax-related information even though the IRS stored it—just as a person's phone calls are maintained as records of the phone company. The information in the 2013 IRS Transcript was based on information about Felix that Respondents provided to the IRS. The

²⁹² JX-49, at 19 (quoting Supplementary Material .01).

²⁹³ JX-49, at 20. Felix also disputed Enforcement's reliance on a 2017 pre-hearing disciplinary order for the authority that IRS Transcripts fall within Rule 8210's scope. *See* JX-49, at 20. In *Dep't of Enforcement v. Graetz*, the assigned hearing officer ordered respondent to submit a Form 4506-T to the IRS in a case alleging that he had knowingly failed to disclose federal tax liens on his Form U4 (Uniform Application for Securities Industry Registration or Transfer). OHO Order 17-08 (2014038847602) (Mar. 21, 2017), https://www.finra.org/sites/default/files/OHO_Order_17-08_2014038847602_0.pdf. Felix argued that the *Graetz* pre-hearing order was not proper authority because that case turned on whether respondent had notice of tax liens, and tax liens are not at issue in this case. JX-49, at 20.

²⁹⁴ Respondents' Post-Hrg. Br. 31-32.

²⁹⁵ Respondents' Post-Hrg. Br. 32.

²⁹⁶ Department of Enforcement's Post-Hearing Brief ("Enforcement's Post-Hrg. Br.") 27.

Panel majority does not agree, as Felix argues, that the records are solely IRS records and therefore Felix had no role in creating them.

The Panel majority further finds that Felix had “control” of the information maintained by the IRS, within the meaning of Rule 8210, because he had the authority to ask the IRS to produce the 2013 IRS Transcript.²⁹⁷ The Panel majority notes that Felix informed staff that he had not filed income tax returns. Accordingly, under the circumstances, the next best thing to get a picture of income reported to the IRS was the IRS Transcript. Obtaining the 2013 IRS Transcript was not burdensome. Though Felix objected to the idea of having to sign and submit a Form 4506-T, it is in effect no different than making a similar request to a bank or phone company for a person’s records. That Enforcement provided Felix with the form to make the request is not intrusive or violative of a person’s rights. Nor is it relevant to the Panel majority that the request involves obtaining information maintained by a government agency.

Accordingly, the Panel majority finds that Felix violated FINRA Rules 8210 and 2010, as alleged in cause six, by failing to produce his IRS Transcript for tax year 2013 or submit Form 4506-T to the IRS to obtain it.

C. Felix Did Not Provide False or Misleading Information to FINRA (Causes Four and Five)

Providing false or misleading information to FINRA during the course of an examination or investigation in response to a request for information or during testimony violates FINRA Rules 8210 and 2010.²⁹⁸

Causes four and five charge Felix with giving FINRA false or misleading information and testimony about the reasons CPA required Respondents to reclassify Felix’s expenses as compensation. As we discuss above, the Panel finds that it was not unreasonable for Felix to believe that the reason for the reclassifications was the change in Primex’s tax status in 2014 from a C Corporation to an S Corporation. Cause five further charges that Felix falsely testified that CPA prepared his two 2013 1099s. As set forth above, the Panel finds that CPA likely created the 1099s, and therefore Felix’s testimony was truthful.

Accordingly, the Panel dismisses causes four and five, alleging that Felix engaged in additional violations of FINRA Rules 8210 and 2010 because Enforcement failed to meet its burden of proof.

²⁹⁷ *Dep’t of Enforcement v. DreamFunded Marketplace, LLC*, No. 2017053428201, 2019 FINRA Discip. LEXIS 27, at *252 (OHO June 5, 2019) (finding that records held by respondents’ accountant were in their control because they could direct that they be produced), *appeal docketed* (NAC July 1, 2019); *Dep’t of Enforcement v. Biney*, No. 20140425550-02, 2016 FINRA Discip. LEXIS 43, at *30 (OHO Aug. 31, 2016) (rejecting respondent’s argument that delay in producing telephone records was because they were not within his custody or control).

²⁹⁸ *Ortiz*, 2008 SEC LEXIS 2401, at *23 (citing *John Montelbano*, 56 S.E.C. 76, 78 (2003)).

IV. Sanctions

The Panel imposes sanctions for Respondents' violations of causes one through three of the Complaint and the Panel majority imposes sanctions for Felix's failure to produce his 2013 IRS Transcript, as alleged in cause six. In determining the appropriate sanctions, the Panel consulted FINRA's Sanction Guidelines ("Guidelines"), specifically, the General Principles Applicable to All Sanction Determinations ("General Principles"), Principal Considerations in Determining Sanctions ("Principal Considerations"), as well as guidelines for specific violations.²⁹⁹

The General Principles explain that disciplinary sanctions "should be designed to protect the investing public by deterring misconduct and upholding high standards of business conduct."³⁰⁰ Adjudicators are therefore instructed to "design sanctions that are meaningful and significant enough to prevent and discourage future misconduct by a respondent and deter others from engaging in similar misconduct."³⁰¹ Sanctions should also be "more than a cost of doing business." They should be "a meaningful deterrent and reflect the seriousness of the misconduct at issue."³⁰² Adjudicators should impose sanctions "tailored to address the misconduct involved in each particular case."³⁰³

A. Respondents' Books and Records Violations (Causes One and Two)

As alleged in causes one and two, Felix falsified Primex's books and records, in violation of FINRA Rule 2010, and caused the Firm to misclassify his expenses as business expenses and thus file inaccurate FOCUS Reports, in violation of FINRA Rules 4511 and 2010. The Guidelines state that, in certain instances, it is appropriate to aggregate violations for purposes of imposing sanctions.³⁰⁴ The Panel finds it appropriate in this instance to assess a unitary sanction for Felix's books and records violations in causes one and two because they relate to his inaccurate recording of expenses in the Firm's general ledger.³⁰⁵

To determine the appropriate sanctions for Felix's inaccurate or false recording of his expenses, the Panel considered the guideline for forgery, unauthorized use of signatures or falsification of records in violation of FINRA Rule 2010,³⁰⁶ together with the guideline for

²⁹⁹ FINRA Sanction Guidelines at 2-8, 29, 37, 70 (2019), <http://www.finra.org/sanctionguidelines>.

³⁰⁰ Guidelines at 2 (General Principles, No. 1).

³⁰¹ Guidelines at 2 (General Principles, No. 1).

³⁰² Guidelines at 2 (General Principles, No. 1).

³⁰³ Guidelines at 3 (General Principles, No. 3).

³⁰⁴ Guidelines at 4.

³⁰⁵ See *Taylor*, 2011 FINRA Discip. LEXIS 17, at *21-26 (applying a single sanction for providing firm false information and causing firm to maintain inaccurate books and records).

³⁰⁶ Guidelines at 37.

recordkeeping violations of FINRA Rules 4511 and 2010.³⁰⁷ The Panel also consulted the guideline for filing false or misleading FOCUS Reports.³⁰⁸ The guideline for falsification of records instructs adjudicators to consider a fine of \$5,000 to \$11,000 and a suspension of 10 business days to six months in cases where the falsification is done with authorization and in the absence of other violations or customer harm. Where the falsification is not authorized, and in the absence of other violations or customer harm, adjudicators should consider a fine as high as \$155,000.³⁰⁹

The guideline for recordkeeping violations of FINRA Rule 4511 and the SEC's recordkeeping rules, including Exchange Act Rule 17a-3, instructs adjudicators to consider a fine of \$1,000 to \$16,000 and suspend the responsible individual in any or all capacities for a period of 10 business days to three months. In cases where aggravating factors predominate, adjudicators should consider a fine of \$10,000 to \$155,000 and a longer suspension of an individual (of up to two years) or a bar.³¹⁰ Where significant aggravating factors predominate, consideration should be given to a fine higher than \$155,000. Factfinders should consider suspending a firm for a period of 10 business days to two years or expelling the firm in cases where aggravating factors predominate.³¹¹

The guideline for filing false or misleading FOCUS Reports instructs adjudicators to consider imposing a fine between \$10,000 and \$77,000 and suspending the financial and operations principal or other responsible principal in any or all capacities for up to two years. In addition to imposing a fine, adjudicators should also consider suspending a firm from all solicited retail business for up to 30 business days and thereafter until it corrects all deficiencies.³¹²

The relevant principal considerations for recordkeeping violations and falsification of records recommend that the Panel consider the nature and materiality of the inaccurate or missing information and the nature of the falsified documents. Other considerations include the nature, proportion, and size of the firm records at issue, and whether the respondent entered or omitted the inaccurate or missing information intentionally, recklessly, or as the result of negligence.³¹³

³⁰⁷ Guidelines at 29.

³⁰⁸ Guidelines at 70.

³⁰⁹ Guidelines at 37. When a respondent falsifies a document without authorization resulting in customer harm or if the misconduct is accompanied by significant aggravating factors, a bar should be considered standard. Guidelines at 37.

³¹⁰ Guidelines at 29.

³¹¹ Guidelines at 29.

³¹² Guidelines at 70.

³¹³ Guidelines at 29, 37. *See also* Guidelines at 8 (Principal Considerations, No. 13) (whether respondent's misconduct was the result of an intentional act, recklessness or negligence).

Here, Felix acknowledged that he knowingly recorded personal expenses as Primex's expenses in some instances. He also testified that he did so inadvertently in other instances. The Panel finds that Felix acted intentionally when he misclassified his expenses.³¹⁴ The Panel considered that the improper classifications did not involve a limited number of violative acts committed in a short period, but many hundreds of expenses spanning three years and a significant amount of money that represented a substantial percentage of Primex's annual revenues each year. This resulted in Primex's filing FOCUS Reports for three years that had incorrect or misleading information about the Firm's business expenses and the amount of compensation it paid to its sole owner and most important principal. Given the length of time, the number of transactions, and the sizeable amount of money involved, the Panel finds that this misconduct demonstrates a pattern of behavior.³¹⁵

The Panel finds that Felix's misconduct was not egregious, however. Because he owned Primex, he was spending his own money and the expense misclassifications did not affect the Firm's net capital. Felix also agreed to reclassify the 2014 and 2015 expenses as CPA had instructed. Therefore sanctions at the low end of the Guidelines' proposed ranges are appropriate. We therefore assess a fine of \$25,000 against Felix. The Panel concludes that it is also necessary to suspend Felix from associating with any member firm as a FINOP (including introducing broker-dealer financial and operations principal) for 30 business days and thereafter until he requalifies as a FINOP.³¹⁶ The Panel finds it appropriate that Felix be required to requalify as a FINOP because his conduct demonstrates a lack of knowledge or familiarity with certain rules concerning the securities industry.³¹⁷ Thus, Felix may not re-register in a FINOP capacity until he requalifies as a FINOP.³¹⁸

To determine the appropriate sanction for Primex's books and records violations, alleged in cause two, the Panel applied the same guidelines for recordkeeping violations, together with the guideline for filing false or misleading FOCUS Reports in violation of Exchange Act Rule

³¹⁴ Guidelines at 29.

³¹⁵ Guidelines at 29. *See also* Guidelines at 7-8 (Principal Considerations, Nos. 8, 9, 17) (whether the respondent engaged in numerous acts and/or a pattern of misconduct) (whether the respondent engaged in the misconduct over an extended period of time) (the number, size and character of the transactions at issue).

³¹⁶ Guidelines at 3 (General Principles, No. 3) (adjudicators "should impose sanctions tailored to address the misconduct involved in each particular case" including suspending an individual "from functioning in any or all capacities").

³¹⁷ Guidelines at 6 (General Principles, No. 8) ("The remedial purpose of disciplinary sanctions may be served by requiring an individual respondent to requalify by examination as a condition of continued employment in the securities industry."). *See, e.g., Dist. Bus. Conduct Comm. v. First Colo. Fin. Servs. Co.*, No. C3A950031, 1997 NASD Discip. LEXIS 16, at *18 (NBCC Mar. 7, 1997) (imposing 10-business-day suspension against FINOP in financial and operations principal capacities for causing firm to operate under net capital deficiency).

³¹⁸ As discussed in more detail below, under cause six, we bar Felix for violating FINRA Rules 8210 and 2010. In light of this, we do not impose the suspension or fine against Felix or the requirement that he requalify as a financial and operations principal.

17a-5.³¹⁹ Applying the same violation-specific factors considered in determining Felix’s sanctions, the Panel finds that an appropriate sanction for Primex is also a \$25,000 fine, together with a censure.

B. Respondents’ Violations of FINRA Rule 8210 (Causes Three and Six)

Below, the Panel addresses sanctions against Primex for its late response to FINRA staff’s requests for information (cause three) and Felix’s failure to produce his 2013 IRS Transcript (cause six), in violation of FINRA Rules 8210 and 2010.

1. Primex’s Untimely Response to FINRA Rule 8210 Request (Cause Three)

In cases involving a firm’s failure to respond in a timely manner to a Rule 8210 request for information, the Guidelines provide for suspending the firm with respect to any or all activities or functions for up to 30 business days. The Guidelines also instruct adjudicators to consider a fine between \$2,500 and \$39,000 for an untimely response to a request for information and documents.³²⁰

The principal considerations in determining sanctions for a failure to timely respond are (i) the importance of the information requested as viewed from FINRA’s perspective, (ii) the number of requests made and the degree of regulatory pressure required to obtain a response, and (iii) the length of time it took the respondent to respond.³²¹ The Panel finds, and Primex concedes, that the information FINRA sought was important. Primex was asked to explain the business purpose of 73 randomly selected expenses incurred by Felix in 2014 and 2015. At that early stage of the investigation, documentation and prompt answers from Primex would have assisted FINRA staff in understanding what personal expenses Felix may have had the Firm pay without recording them properly on the Firm’s general ledger.

Respondents contend that the November 2015 request was just one of many requests for information that FINRA served on Respondents over a five-year investigation. It was an “anomaly,” they say, because, after responding to the request in March 2016, there were no other instances of Primex “responding in a similar or materially late fashion to any Rule 8210

³¹⁹ Guidelines at 29, 70. The Panel also applied Principal Considerations Nos. 8 and 9.

³²⁰ Guidelines at 33. The Complaint alleges that Primex failed to respond to two requests for information. Compl. ¶ 93. *See also* Enforcement Post-Hrg. Br. 24. Because the November 3 and November 17, 2015 Rule 8210 requests were identical in substance, the Panel treats them as one request that Enforcement sent to Primex twice.

³²¹ Guidelines at 33.

requests.”³²² Respondents also argue that Primex has no disciplinary history.³²³ However, the absence of disciplinary history is not mitigating.³²⁴

In light of the significance of the information requested, Primex’s three-month delay in responding, requiring the staff to initiate a Rule 9552 expedited proceeding to obtain compliance, makes a meaningful sanction necessary. The Panel finds that an appropriate sanction given all the circumstances is a censure and fine of \$15,000. The fine falls just below the middle of the range suggested by the Guidelines for an untimely response to a request for information. The Panel determines that the fine amount is sufficiently remedial to deter future violations and impress upon the Firm the importance of complying with Rule 8210.

2. Felix’s Failure to Produce His 2013 IRS Transcript (Cause Six)

The Guidelines provide that, where an individual fails to respond at all to a FINRA Rule 8210 request, a bar is standard. The Guidelines further provide that a bar is the standard sanction for a partial but incomplete response, unless the person can demonstrate that the information provided substantially complied with all aspects of the request. A lesser sanction of a suspension of up to two years may be warranted where mitigation exists or the response was untimely.³²⁵ The imposition of a bar as the standard sanction for a complete failure to respond to information requests “reflects the judgment that, in the absence of mitigating factors, a complete failure to cooperate with [FINRA] requests for information or testimony is so fundamentally incompatible with [FINRA’s] self-regulatory function that the risk to the markets and investors posed by such misconduct is properly remedied by a bar.”³²⁶

Enforcement’s requests for the IRS Transcripts concerned an investigation into potentially serious wrongdoing—whether Respondents properly classified Felix’s expenses to ensure that Primex’s books and records correctly recorded his compensation and what amount of compensation, if any, Primex ultimately reported to the IRS. While Felix did not entirely ignore FINRA’s requests for the IRS Transcripts, he nonetheless failed to respond by providing the requested document, thereby impeding FINRA’s investigation into violative conduct. The Panel majority finds that he did not provide a valid explanation for his refusal to obtain the IRS Transcripts, and we have rejected his legal arguments about the limited scope of Rule 8210 as baseless. FINRA was entitled to the information, and entitled to ask that Felix submit a form to

³²² Respondents’ Post-Hrg. Br. 22.

³²³ Respondents’ Post-Hrg. Br. 19.

³²⁴ *Allen Holeman*, Exchange Act Release No. 86523, 2019 SEC LEXIS 1903, at *48 (July 31, 2019).

³²⁵ Guidelines at 33. The Guidelines also provide for consideration of a fine between \$25,000 and \$77,000 in cases involving a failure to respond or to respond truthfully. In light of the bar, we do not impose a fine against Felix. Guidelines at 33.

³²⁶ *Howard Brett Berger*, Exchange Act Release No. 58950, 2008 SEC LEXIS 3141, at *16 (Nov. 14, 2008) (quoting *Charles C. Fawcett, IV*, Exchange Release No. 56770, 2007 SEC LEXIS 2598, at *21-22 (Nov. 8, 2007)), *petition for review denied*, 347 F. App’x 692 (2d Cir. 2009).

obtain the IRS Transcript. A response would have assisted FINRA's investigation and may have led to other areas of investigation.

The Panel majority is troubled by Felix's questioning FINRA's need for the information, effectively asking the staff to justify its request. As we have already stated, an associated person may not second-guess an information request and the obligation to respond is unequivocal. The Guidelines specifically state that the importance of any Rule 8210 request is assessed from FINRA's perspective.³²⁷ The SEC has stated that barring a respondent for violations of Rule 8210 "protects investors by encouraging the timely cooperation that assists in the prompt discovery and correction of wrongdoing."³²⁸

Because Felix failed to produce his IRS Transcript for 2013, the Panel majority finds that he failed to respond at all to FINRA's Rule 8210 request. The appropriate sanction is therefore a bar in all capacities. The Panel majority finds barring Felix is appropriately remedial, not punitive, and will serve as a deterrent to others who may wish to avoid complying with requests for information and documents. It is "critically important to the self-regulatory system that members and associated persons cooperate with [FINRA] investigations."³²⁹

V. Order

Felix is barred from associating with any member firm in any capacity for violating FINRA Rules 8210 and 2010, as alleged in cause six of the Complaint.

For Felix's violations of FINRA Rules 4511 and 2010 as alleged in causes one and two, the Panel finds that a \$25,000 fine and a suspension for a period of 30 business days from associating with any member firm as a FINOP, and remaining suspended until such time as he requalifies as a FINOP, is appropriate. In light of the bar for the violation of FINRA Rules 8210 and 2010 under cause six, however, the Panel does not impose the suspension and fine against Felix or the requirement that he requalify as a FINOP.

Primex is censured and fined \$25,000 for its violations of FINRA Rules 4511 and 2010 and its willful violations of Section 17(a) of the Exchange Act and Exchange Act Rules 17a-3 and 17a-5, as alleged in cause two. It is also subject to statutory disqualification for the willful violations of the Exchange Act. Primex is censured and fined \$15,000 for violations of FINRA Rules 8210 and 2010, as alleged in cause three of the Complaint.³³⁰ Thus, in total, Primex is censured and fined \$40,000.

³²⁷ Guidelines at 33.

³²⁸ *Elliot M. Hershberg*, 58 S.E.C. 1184, 1189 (2006), *aff'd*, 210 F. App'x 125 (2d Cir. 2006).

³²⁹ *Evansen*, 2015 SEC LEXIS 3080, at *63 (quoting *Erenstein v. SEC*, 316 F. App'x 865, 871 (11th Cir. 2008)).

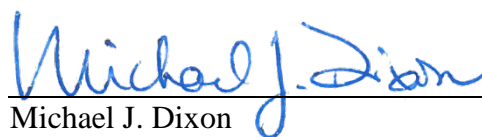
³³⁰ The Hearing Panel has considered and rejects without discussion all other arguments of the parties.

The Hearing Panel dismisses causes four and five of the Complaint alleging that Felix engaged in additional violations of FINRA Rules 8210 and 2010 because Enforcement failed to meet its burden of proof.

If this decision becomes FINRA's final disciplinary action, Felix's bar shall become effective immediately.

Respondents are each ordered to pay half of the total costs in the amount of \$12,585.39, which includes a \$750 administrative fee and \$11,835.39 for the cost of the hearing transcript. The costs shall be due on a date set by FINRA, but not sooner than 30 days after this decision becomes FINRA's final action.

The fines shall be due on a date set by FINRA, but not sooner than 30 days after this decision becomes FINRA's final action.


Michael J. Dixon
Hearing Officer
For the Extended Hearing Panel

DISSENT

Panelist dissenting, in part, from the majority of the Panel regarding cause six of the Complaint:

I respectfully disagree with my fellow panelists' conclusions. I am unable to join in the Panel majority's finding that Enforcement proved that, as a matter of law, Felix violated FINRA Rules 8210 and 2010 by failing to provide a copy of his 2013 IRS Transcript or, in the alternative, to sign and submit Form 4506-T to the IRS to obtain it.

I find that Rule 8210 is not intended to compel an associated person to produce the sort of information preserved in an IRS Transcript that is only indirectly created by the taxpayer and sign and submit a form to the IRS to obtain a copy. This, to me, is different from asking a person to produce copies of bank statements, telephone records, or accounting papers for an outside business, to give a few typical examples. Bank and telephone statements are representative of the sorts of records a person customarily thinks of as records that he or she knowingly and intentionally causes to be generated and maintained by a third party.

FINRA has ruled in the past that under certain circumstances an associated person's tax returns also are subject to Rule 8210 because the taxpayer prepared the returns. However, the

IRS records of a taxpayer, such as the 2013 IRS Transcript sought in this case, fall just over the line and into a different category to my mind. They are not “of” the associated person. I am aware that Rule 8210 obligates a person to produce records from a third party so long as he or she has “control” over their production. But, applying principles of fairness, I do not think that IRS Transcripts are the sort of records that were contemplated as being within the reach of Rule 8210 or within a firm’s or an associated person’s “control.”

I understand that Rule 8210 has been held to require that associated persons may not question the purpose of a FINRA request for information and documents, as that would undermine FINRA’s ability to fulfill its regulatory function. That is an essential proposition that must be preserved. But based on the central allegations made in this case, and after hearing the testimony and reviewing the documents admitted into evidence, I am troubled by FINRA’s request. The IRS Transcript would not have revealed whether CPA, or someone else, prepared Felix’s 2013 1099s, as Enforcement suggests. They also would not have shed light on whether any individual expense was personal or business, which is at the heart of the allegations in the Complaint. Such determinations can be made only by evaluating each expense.

I therefore dissent from the Panel majority’s finding that Felix violated Rules 8210 and 2010, as alleged in cause six.

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