

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

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

AVENIR FINANCIAL GROUP  
(CRD No. 148490),

MICHAEL TODD CLEMENTS  
(CRD No. 1702071),

and

KARIM AHMED IBRAHIM,  
a/k/a CHRIS ALLEN  
(CRD No. 5983439),

Respondents.

Disciplinary Proceeding  
No. 2015044960501

Hearing Officer–DRS

**EXTENDED HEARING PANEL  
DECISION**

September 20, 2016

**Avenir is censured, fined \$229,000, ordered to offer rescission to defrauded customers, and suspended for two years from engaging in any self-offerings of securities for willfully engaging in fraud, failing to make required disclosures and related regulatory filings concerning self-offerings of securities, and for failing to supervise. Clements is barred from association with any FINRA member firm in all capacities and ordered to offer rescission to defrauded customers for willfully engaging in fraud. Ibrahim is suspended for two years in all capacities from association with any FINRA member firm, ordered to offer rescission to a defrauded customer, ordered to disgorge his commission and to relinquish any claim to an equity interest in Avenir based on his sale to the defrauded customer for willfully engaging in fraud. Respondents are also ordered to pay costs.**

**The aiding and abetting and misuse of customer funds charges are dismissed.**

## Appearances

For the Complainant: Michael J. Watling, Esq., Carolyn O’Leary, Esq., and Jeffrey D. Pariser, Esq., Department of Enforcement, Financial Industry Regulatory Authority.

For Respondents Avenir Financial Group and Michael Todd Clements: Robert C. Harris, Esq., Hunter Taubman Fischer LLC.

Respondent Karim Ahmed Ibrahim (also known as Chris Allen), Pro Se.

## DECISION

### I. Introduction

This case arose from equity and debt self-offerings by Avenir Financial Group (“Avenir” or “Firm”), a financially troubled FINRA member firm, and Bull Run Capital Holdings, LLC (“BRCH”), a holding company that owned an Avenir branch office. In connection with those offerings, the Department of Enforcement brought fraud and other charges against Avenir, its Chief Executive Officer and Chief Compliance Officer, Michael Todd Clements, and one of its registered representatives, Karim Ahmed Ibrahim (also known as Chris Allen).<sup>1</sup> The gravamen of the fraud-related charges is that Respondents omitted and misrepresented material information to investors in connection with the self-offerings. Specifically, Respondents are charged with failing to disclose that the Firm was in poor financial condition and that it had ceased its securities business for two weeks because of net capital deficiencies. Avenir and Clements are also charged with failing to disclose that the owner of BRCH planned to use a portion of the offering proceeds for his personal benefit.<sup>2</sup>

Respondents denied all charges, maintaining that they tried to comply with their obligations, did not make misrepresentations or omissions, or, to the extent any violations occurred, the violations were technical or not their fault. An Extended Hearing Panel held a

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<sup>1</sup> The investigation that led to this proceeding resulted from a FINRA cycle examination of the Firm as well as a review by FINRA’s Department of Corporate Financing of filings made by the Firm. Tr. 1682–85, 1725–30.

<sup>2</sup> In addition to filing the instant disciplinary proceeding, Enforcement also sought a temporary cease and desist order (“TCDO”) against Respondents in a separate proceeding under FINRA Rule 9810 (Proceeding No. 2015044960501) (“TCDO Proceeding”). On May 6, 2015, a FINRA Hearing Panel in the TCDO Proceeding issued, upon consent of the parties, a TCDO against Respondents. The TCDO ordered, among other things, that: (1) Respondents cease and desist from committing fraud in violation of Section 10(b) of the Securities Exchange Act of 1934, SEC Rule 10b-5, and FINRA Rules 2020 and 2010; (2) Clements cease and desist from aiding and abetting violations of those provisions; (3) Respondents cease and desist from soliciting, or causing Avenir to solicit, sales of Avenir equity unless Avenir fully discloses the true financial condition of the firm; (4) Avenir and Clements cease and desist from selling equity in the firm or its branch offices and from selling promissory notes unless Avenir and its branch offices fully disclose the true use of the proceeds; and (5) Avenir and Clements cease and desist from using the proceeds of such equity raises or promissory notes for purposes not fully disclosed to individuals who purchased the equity or made loans in connection with the promissory notes. The TCDO remained in effect until the Extended Hearing Panel issued this Extended Hearing Panel Decision.

seven-day hearing. And, after considering the evidence and the parties' arguments, we make findings of fact and conclusions of law and impose the sanctions set forth below.

## **II. Findings of Fact**

### **A. The Respondents**

#### **1. Avenir Financial Group**

Avenir was established in 2008 by Michael Todd Clements and David Allen, the Firm's co-owners and principals.<sup>3</sup> In March 2012, Avenir became a FINRA member.<sup>4</sup> Since its inception, Avenir has engaged in a general securities business and maintained its principal place of business in New York.<sup>5</sup> At all relevant times, Avenir had between seven and eight branch offices and employed approximately 17 to 24 registered persons.<sup>6</sup>

#### **2. Michael Todd Clements**

Michael Todd Clements entered the securities industry in or around 1988.<sup>7</sup> At all relevant times, he owned an approximately 38 percent interest in Avenir.<sup>8</sup> Clements's registrations with the Firm included General Securities Representative, General Securities Principal, General Securities Sales Supervisor, Investment Banking Representative, and Operations Professional Research Principal.<sup>9</sup> Clements is based in Avenir's Florida office.<sup>10</sup>

Since Avenir's inception, Clements served as the Firm's Chief Executive Officer ("CEO") and Chief Compliance Officer ("CCO").<sup>11</sup> As Avenir's CCO, he was the principal responsible for overseeing the Firm's supervision system,<sup>12</sup> and was responsible for supervising

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<sup>3</sup> Complainant's Exhibit 73 ("CX-\_\_").

<sup>4</sup> Avenir and Clements Response to the Amended Expedited Complaint, ¶ 10, ("Avenir and Clements Answer ¶ \_\_").

<sup>5</sup> Avenir and Clements Answer ¶¶ 10, 113; Ibrahim Answer to the Amended Statement of Claim ¶¶ 10, 120 ("Ibrahim Answer ¶ \_\_").

<sup>6</sup> Avenir and Clements Answer ¶ 10. Avenir is, and at all times relevant to this proceeding was, a member of FINRA and remains subject to FINRA's jurisdiction under Article IV, Section 1 of FINRA's By-Laws. Avenir and Clements Answer ¶ 10.

<sup>7</sup> Avenir and Clements Answer ¶ 11.

<sup>8</sup> Hearing Transcript 112 ("Tr. \_\_").

<sup>9</sup> Avenir and Clements Answer ¶ 11. Clements is, and at all times relevant to this proceeding was, associated with a FINRA member firm and remains subject to FINRA's jurisdiction under Article V, Section 2 of FINRA's By-Laws. Avenir and Clements Answer ¶ 11; CX-82, at 6-7.

<sup>10</sup> Avenir and Clements Answer ¶ 113.

<sup>11</sup> Avenir and Clements Answer ¶ 11; Ibrahim Answer ¶ 134; Tr. 78; CX-73, at 8.

<sup>12</sup> Tr. 129-37.

the Firm’s investment banking activities, including any Avenir self-offerings of securities.<sup>13</sup> Clements was also responsible for supervising the Firm’s regulatory filings, including filings made under FINRA Rule 5122, which governs self-offerings of securities by a member firm.<sup>14</sup> Also, as CCO, Clements was responsible for reviewing the Firm’s regulatory responses before the Firm submitted them to regulators, including FINRA.<sup>15</sup>

During the relevant period, Clements was solely responsible for providing training to Avenir registered representatives regarding private sales of equity, as well as ensuring due diligence on these investments, investor suitability, and that “the transaction was completed properly with the client.”<sup>16</sup> Clements was the direct supervisor of certain registered representatives, including Cesar Rodriguez,<sup>17</sup> the owner of BRCH.

### **3. Karim Ibrahim**

Karim Ibrahim<sup>18</sup> first became associated with a FINRA member firm in 2011<sup>19</sup> and became associated with Avenir as a General Securities Representative in April 2013.<sup>20</sup> Ibrahim was registered with the Firm throughout the hearing in this case.<sup>21</sup> Ibrahim worked in Avenir’s New York Office<sup>22</sup> and his supervisor was David Allen.<sup>23</sup>

#### **B. Avenir’s Capital Crises**

From inception, Avenir was thinly capitalized.<sup>24</sup> Eventually, Avenir needed to raise additional capital. Thus, in late 2013 and early 2014, Avenir raised \$388,000 from four investors in separate self-offerings.<sup>25</sup> These self-offerings were prompted by the Firm’s need to stave off net capital problems—not just to expand operations. Despite its net capital problems, Avenir increased its capital risk by permitting its registered representatives to open margin accounts for

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<sup>13</sup> Tr. 227–29; CX-61, at 1–3.

<sup>14</sup> Tr. 237–43; CX-61, at 7–8.

<sup>15</sup> Tr. 2263, 2318–23.

<sup>16</sup> Ibrahim Answer ¶ 83.

<sup>17</sup> Tr. 166–68.

<sup>18</sup> When interacting with customers, Ibrahim used the name “Chris Allen.” Tr. 716–17.

<sup>19</sup> CX-81, at 8.

<sup>20</sup> Avenir and Clements Answer ¶ 12; Ibrahim Answer ¶ 12; CX-81.

<sup>21</sup> Tr. 698; CX-81, at 5.

<sup>22</sup> Avenir and Clements Answer ¶ 113; Ibrahim Answer ¶ 113

<sup>23</sup> Tr. 1838.

<sup>24</sup> CX-115; CX-116; CX-117; CX-118; CX-119; CX-120; CX-121; CX-122; CX-123 (FOCUS filings from October 2012 through October 2013 reflecting that the Firm’s cash reserves never exceeded \$25,855).

<sup>25</sup> Avenir and Clements Answer ¶ 2.

customers and recommend that those customers trade on margin.<sup>26</sup> These activities increased the Firm's capital risk because if a margin transaction resulted in a margin call and the customer failed to make a timely payment, the Firm was secondarily liable to its clearing firm.<sup>27</sup>

Ibrahim was one of the registered representatives who was permitted to open and trade margin accounts. From August through December 2013, Ibrahim solicited several customers to trade on margin.<sup>28</sup> Avenir suffered a net capital deficiency in October 2013 when two of Ibrahim's customers, GD and HR, faced margin calls from Avenir's clearing firm.<sup>29</sup> Because they failed to make full and timely payments to cover their debit balances, Avenir became liable for those unpaid balances. The charge to Avenir for covering these debits created a net capital deficiency of \$223,000. And on the morning of October 23, 2013, the Firm filed a notice with FINRA reporting that its net capital had fallen below the minimum amount required by the Securities and Exchange Commission ("SEC").<sup>30</sup> Later that morning, Clements emailed Avenir's employees instructing them to immediately stop conducting a securities business until the Firm could comply with the SEC's net capital rules.<sup>31</sup>

To comply with the net capital rules, the Firm needed an immediate capital infusion. So, Clements decided to seek funds from outside investors through an Avenir equity self-offering.

The first investor to purchase an equity interest was Clements's mother, JC.<sup>32</sup> Under her Purchase Agreement, signed on October 30, 2013,<sup>33</sup> she purchased a five percent ownership interest in the Firm for \$13,000 (i.e., \$2,600 for each one percent interest).<sup>34</sup> Along with her investment, JC executed a disclosure document prepared by Clements stating that JC's investment would be used for "operating expenses and net Capitalization [sic]."<sup>35</sup> Neither her payment, nor an additional capital deposit on November 1, 2013, by Clements was sufficient to return the Firm to net capital compliance.<sup>36</sup>

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<sup>26</sup> Tr. 182–83; CX-62, at 70–72.

<sup>27</sup> Tr. 184–85; 1846–48.

<sup>28</sup> CX-145, at 6–14; CX-162; Tr. 876.

<sup>29</sup> Tr. 732–34, 738–40; CX-138.

<sup>30</sup> CX-10. *See* SEC Rule 17a-11(b).

<sup>31</sup> Tr. 286–90; CX-139.

<sup>32</sup> Tr. 256.

<sup>33</sup> CX-19, at 3.

<sup>34</sup> Avenir and Clements Answer ¶ 19.

<sup>35</sup> Avenir and Clements Answer ¶ 21.

<sup>36</sup> CX-123, at 4; Tr. 1174–75, 1856–62.

A few days later, however, another investor, AC,<sup>37</sup> supplied additional capital, which brought the Firm back into net capital compliance. Avenir registered representative Cesar Rodriguez solicited AC's investment in Avenir.<sup>38</sup> On November 4, 2013, AC executed a Purchase Agreement and Private Transaction Customer Disclosure Acknowledgment ("AC Purchase Documents") reflecting that he would pay \$25,000 in exchange for a one percent ownership interest in Avenir.<sup>39</sup> AC's initial payment of \$15,000 was deposited into the Firm's bank account on November 4, 2013.<sup>40</sup> As a result, the Firm was able to resume its securities business on November 5, 2013, after having been precluded from conducting that business since October 23.<sup>41</sup>

Two weeks after the Firm reopened, Ibrahim placed customer trades that triggered a second financial crisis for Avenir. On November 19, 2013, Ibrahim solicited customer RF to purchase, on margin, more than \$500,000 worth of shares of two securities.<sup>42</sup> The Firm permitted Ibrahim to enter the trades because RF had made a \$300,000 opening deposit into his account the day before the trades were executed.<sup>43</sup> But on November 22, RF's check was returned for insufficient funds.<sup>44</sup> This caused the clearing firm, that day, to email Clements (and the Firm's other co-owner, David Allen) demanding a \$300,000 wire transfer by the next business day or else it would sell out RF's account.<sup>45</sup> In the email, the clearing firm also informed them that RF's account "has \$190,000 due" by November 27 for his trades and that it would not grant any extensions.<sup>46</sup>

Clements knew that the Firm would again have a net capital deficiency if the clearing firm forced a sell-out of the RF trades and Avenir booked the related liability.<sup>47</sup> Thus, on November 25, Clements sent the clearing firm a "Plan of Action" addressing the RF-related crisis and how the Firm intended to remedy it and place itself on a path to financial stability and

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<sup>37</sup> CX-22.

<sup>38</sup> Tr. 1329–30.

<sup>39</sup> CX-22, at 1; CX-23; Tr. 1331–32.

<sup>40</sup> CX-13, at 1; CX-11, at 6; Tr. 329–30. AC's Purchase Documents did not reflect the intended use of the proceeds or Rodriguez's selling compensation for the transaction. *See* CX-22; CX-23. Later, however, AC acknowledged in writing that before investing in Avenir he had been orally advised that the funds would be used for the growth of the broker-dealer and for operational purposes. AC also acknowledged that before executing the Purchase Documents, he was orally advised that Rodriguez would receive a 10 percent commission for his investment. Respondents Avenir and Clements Exhibit 6 ("RX-\_\_").

<sup>41</sup> CX-143; Tr. 304, 1860–63.

<sup>42</sup> CX-162, at 10.

<sup>43</sup> Ibrahim Answer ¶ 28(a); CX-148, at 8 ¶ 1.

<sup>44</sup> CX-162, at 10; Ibrahim Answer ¶ 28(c).

<sup>45</sup> CX-146.

<sup>46</sup> CX-146.

<sup>47</sup> Tr. 368.

growth.<sup>48</sup> The Plan of Action included a section entitled “Proposed Heightened Supervision for Karim Ibrahim,”<sup>49</sup> which contained detailed provisions about how the Firm would supervise Ibrahim. This section ended with an assurance that Avenir would terminate its association with Ibrahim if necessary to maintain the clearing firm’s “comfortability” with the Firm.<sup>50</sup>

The Firm’s precarious financial situation and its desire to avert another closure set the stage for Ibrahim’s sale of Avenir equity to customer NL, discussed below. The Amended Expedited Complaint charges that Ibrahim, Avenir, and Clements defrauded NL in connection with the sale.

## **C. Ibrahim’s Sale of Avenir Equity to Customer NL**

### **1. Respondents’ Omission of Information**

Clements provided “Private Transaction training” to Ibrahim in August 2013 and approved and supervised his capital-raising efforts.<sup>51</sup> After Clements received the above-referenced November 22, 2013 email from the clearing firm, he asked Ibrahim if he had any customers who would be interested in investing in the Firm.<sup>52</sup> He also directed Ibrahim to offer investors a one percent interest in Avenir for every \$50,000 invested,<sup>53</sup> and to tell them that their funds would be used for Avenir’s day-to-day operations and growth.<sup>54</sup>

But there was much information that Clements did not tell Ibrahim. For example, he did not tell Ibrahim (1) the basis for the valuation of the equity interest; (2) the prices paid for recent investments in Avenir, including the fact that there had been recent capital raises at a fraction of the price that Ibrahim would be offering to other investors; (3) about the Firm’s financial condition, including its regulatory capital situation; and (4) about the Plan of Action submitted to the clearing firm.<sup>55</sup>

Based on Clements’s directives, Ibrahim solicited Avenir Customer NL to invest in the Firm.<sup>56</sup> NL was a wealthy, self-employed, 92 year-old new customer.<sup>57</sup> In soliciting the

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<sup>48</sup> CX-148, at 8–9.

<sup>49</sup> CX-148, at 8–9.

<sup>50</sup> CX-148, at 9.

<sup>51</sup> Ibrahim Answer ¶ 96; CX-58. During the period August 2013 through November 2013, Clements asked Ibrahim to solicit his customers to invest in Avenir. Ibrahim Answer, ¶ 96. Ibrahim solicited investors to do so between October 30 and December 19, 2013. Ibrahim Answer ¶ 18.

<sup>52</sup> Tr. 815–21.

<sup>53</sup> Ibrahim Answer ¶ 105.

<sup>54</sup> Ibrahim Answer ¶ 124.

<sup>55</sup> Ibrahim Answer ¶¶ 3, 29, 98, 100, 105.

<sup>56</sup> Ibrahim Answer ¶ 29; Tr. 737–38, 819–25.

<sup>57</sup> Ibrahim Answer ¶ 27; CX-1, at 1–2.

investment, Ibrahim told NL that Avenir was a small start-up company; that Avenir was seeking an equity investment to grow the Firm and fund its day-to-day operations;<sup>58</sup> and that one day NL's investment would be returned "in a very large amount."<sup>59</sup> Ibrahim also provided NL with a Purchase Agreement, under which NL would receive a five percent ownership interest in Avenir for a payment of \$250,000 (i.e., \$50,000 per one percent interest).<sup>60</sup> (Clements set the price for NL's equity investment,<sup>61</sup> drafted the Purchase Agreement, and was responsible for approving the terms of the investment.)<sup>62</sup>

But other than this three-page Purchase Agreement,<sup>63</sup> Ibrahim provided NL with no written materials, including any written information about the Firm.<sup>64</sup> Moreover, although Ibrahim admitted in this proceeding that he was aware that the Firm faced a dire regulatory capital situation,<sup>65</sup> he did not disclose any information to NL about Avenir's financial condition.<sup>66</sup>

More specifically, Ibrahim did not tell NL (1) that Avenir had ceased conducting a securities business within the past month for insufficient net capital; (2) that the Firm was facing an imminent margin-call-related liability of \$190,000 and that unless the firm raised funds from new investors to cover the liability, it would again be net capital deficient;<sup>67</sup> or (3) about the Firm's regulatory capital situation.<sup>68</sup> And, not knowing about the terms of the Plan of Action or that there had been recent capital raises at a fraction of the price paid by NL, Ibrahim was not able to—and in fact did not—disclose this information to NL.<sup>69</sup>

On November 26, 2013, NL signed the Purchase Agreement,<sup>70</sup> agreeing to invest \$250,000 for a five percent interest in Avenir.<sup>71</sup> In connection with the transaction, Ibrahim received a 10 percent sales commission (\$25,000) and an unvested five percent equity interest in

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<sup>58</sup> Tr. 912, 2050–51.

<sup>59</sup> Tr. 889.

<sup>60</sup> CX-2.

<sup>61</sup> Ibrahim Answer ¶ 3.

<sup>62</sup> Tr. 406–12. Avenir and Clements Answer ¶ 108.

<sup>63</sup> CX-2.

<sup>64</sup> Tr. 891–92; CX-8B, at 18.

<sup>65</sup> Ibrahim Answer ¶ 3.

<sup>66</sup> Tr. 892; CX-8B, at 19–24; CX-94, at 2, ¶ 1(g) (responding to FINRA's information request).

<sup>67</sup> CX-8B, at 21–24; Tr. 889–91. At the time Clements asked Ibrahim to solicit investors, Ibrahim knew that RF was not "making good on" the margin debt. Tr. 823.

<sup>68</sup> Ibrahim Answer ¶ 30.

<sup>69</sup> Avenir and Clements Answer ¶ 99; Ibrahim Answer ¶¶ 99–100.

<sup>70</sup> CX-2.

<sup>71</sup> Ibrahim Answer ¶¶ 27, 30, 31, 106; Avenir and Clements Answer ¶ 106.



Avenir.<sup>72</sup> The Firm used part of NL’s investment to cover the liability it incurred as a result of RF’s trades.<sup>73</sup>

## **2. Respondents’ Arguments Regarding NL’s Avenir Equity Purchase and Witness Credibility**

Respondents denied any wrongdoing in connection with NL’s equity purchase. We considered and rejected their arguments. First, Ibrahim argued that he did not know that Avenir was in financial trouble at the time NL purchased his equity interest.<sup>74</sup> This assertion was not credible. Ibrahim admitted during his investigative on-the-record testimony (“OTR”) that he knew that the Firm was in “dire financial straits” at the time RF’s \$300,000 check bounced and could “go under” as a result of the unsecured debt.<sup>75</sup> Ibrahim also admitted in his Answer to the Amended Expedited Complaint that he was aware at that time that the Firm was in dire financial circumstances.<sup>76</sup> Moreover, Ibrahim was well aware of the Firm’s recent and serious financial problems because he had been unable to work as a registered representative during the Firm’s suspension of business for net capital deficiencies.

Second, Respondents characterized NL as uninterested in learning any information about Avenir before he purchased the equity interest. NL, who testified via a pre-hearing video OTR played at the hearing, conceded that he did not ask for Avenir’s financials, did not ask how long the Firm had been in business, did not perform a Google search on the Firm, and did not ask any friends about the Firm.<sup>77</sup> In fact, according to Ibrahim, NL declined Ibrahim’s offer to let him review Avenir’s books and records before making the investment.<sup>78</sup> But, as discussed below in the Conclusions of Law, regardless of whether NL asked Ibrahim for information about Avenir, Ibrahim had an independent obligation to provide him with material information. In any event, even if NL had reviewed the Firm’s financials at the time, they would not have revealed Avenir’s looming financial crisis as a result of RF’s unpaid margin liabilities, as the Firm did not book the liability until December 5, 2013<sup>79</sup>—after NL’s funds for his equity purchase had cleared. Nor did

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<sup>72</sup> CX-149; CX-152. Ibrahim never received the five percent equity interest in Avenir. Tr. 862, 1906–09.

<sup>73</sup> Tr. 417–18, 438; CX-11, at 7; CX-12, at 4. Ibrahim, Clements, and the Firm’s co-owner all testified that at the time of NL’s investment they believed RF would pay for the trades and that NL’s investment would not be used to cover RF’s negative debit balance. RF, however, never paid for the trades. Tr. 1875–76, 2050, 2180–81.

<sup>74</sup> Karim Ibrahim’s Post-Hearing Brief at 8 (“Ibrahim Br. at \_\_\_”).

<sup>75</sup> Tr. 746–49, 801–04, 893–94.

<sup>76</sup> Ibrahim Answer ¶ 16.

<sup>77</sup> CX-8B, at 55–56.

<sup>78</sup> Tr. 2051–52.

<sup>79</sup> CX-11, at 7; *see also* Tr. 437–38.

the Firm's November 2013 FOCUS report, which contained the Firm's balance sheet as of November 30, 2013, reflect the liability associated with RF's trades.<sup>80</sup>

Third, Ibrahim claimed that the Panel should reject NL's testimony because his video OTR was conducted by Enforcement in a biased manner. We do not agree. The Panel watched the OTR and found no evidence to substantiate Ibrahim's assertion. NL testified under oath; the Respondents were present at the OTR; and they had the opportunity to—and did in fact—question him.

Fourth, Respondents attacked NL's credibility (although at times they relied on his OTR testimony). They claimed that his memory was poor,<sup>81</sup> that he was biased against Respondents because he had a pending arbitration against them, and that he falsely portrayed himself as an unsophisticated investor.<sup>82</sup> The Panel recognizes that NL appeared physically weak during his OTR; that at times he had trouble remembering various details surrounding his investment;<sup>83</sup> and that he appears to have down-played his level of sophistication. (For example, he actively monitored his investment portfolios and maintained an office with three computer screens that allowed him to review and track his investment portfolios.<sup>84</sup> NL was also a founding member of a bank and conducted his own due diligence before investing in it.)<sup>85</sup> But on the key details, including what NL said about what Ibrahim did not tell him—namely, information about the Firm's financial condition and difficulties—NL's testimony was clear and credible, and was not undermined by cross examination.<sup>86</sup> Significantly, the Respondents did not dispute that they failed to tell NL about the Firm's financial difficulties.

By contrast, when questioned at the hearing by Enforcement about his dealing with NL, Ibrahim was frequently combative and evasive; his testimony was often impeached and needed refreshing by reference to his earlier OTR testimony. These factors undercut his credibility. When Ibrahim's hearing testimony conflicted with his OTR testimony, the Hearing Panel

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<sup>80</sup> CX-124, at 3.

<sup>81</sup> In support of their argument that NL's memory was poor, they point to Ibrahim's testimony that NL asked him about his commission on the investment and that Ibrahim then disclosed it (Tr. 2050–51, 2432–36)—a claim that NL denied. CX-8B, at 26–27. Also, Avenir and Clements cite Ibrahim's testimony that he disclosed to NL how his Avenir investment would be used (Tr. 2432–36), while NL testified that he did not recall if Ibrahim told him that his investment proceeds would be used for day-to-day operations. CX-8B, at 28. Ibrahim offered no corroboration for his claims that he made these statements to NL. And given the concerns the Panel has regarding Ibrahim's credibility, the evidence is inconclusive as to whether he did so.

<sup>82</sup> CX-8B, at 47.

<sup>83</sup> CX-8B, at 17–18.

<sup>84</sup> Ibrahim's Exhibit 12 (“IX-\_\_”); CX-8B, at 84–85.

<sup>85</sup> CX-8B, at 53–54.

<sup>86</sup> See, e.g., CX-8B, at 19–23. In addition to Enforcement, NL was questioned at his OTR by Clements and Ibrahim's then-counsel.

credited the OTR testimony, which was given closer in time to the events at issue and likely before he fully appreciated how certain answers could affect his potential liability.

#### **D. Rodriguez’s Sale of Avenir Equity to KK**

In addition to the Avenir equity sale to NL, the Amended Expedited Complaint charges Avenir and Clements with wrongdoing in connection with sales of equity and promissory notes in self-offerings by Cesar Rodriguez. Rodriguez was associated with Avenir from June 2013 through April 2015 at several Avenir branch or OSJ offices near Chicago.<sup>87</sup> From approximately October 2013 through April 2015, Clements was Rodriguez’s direct supervisor.<sup>88</sup>

We address, first, the sale of Avenir equity to KK, a customer and long-time friend of Rodriguez.<sup>89</sup> On Thanksgiving Day 2013, KK’s adult daughter was killed in a car accident, leaving behind a six-year old child.<sup>90</sup> KK received \$125,000 in life insurance proceeds from a policy he had purchased on her behalf.<sup>91</sup> Soon afterwards, KK asked Rodriguez for advice about how to invest the proceeds.<sup>92</sup> Rodriguez, in turn, sought help from Clements on how to advise KK.<sup>93</sup> Rodriguez then visited KK’s home and, while there, placed a conference call to Clements to discuss investing KK’s insurance proceeds.<sup>94</sup>

#### **1. Rodriguez’s and Clements’s Misrepresentations and Omissions**

During the conference call, KK told Rodriguez and Clements that he wanted a safe, long-term investment that would provide for his granddaughter’s future.<sup>95</sup> In response, Clements recommended that KK buy an equity interest in Avenir.<sup>96</sup> He assured KK that Avenir was a “growth company,”<sup>97</sup> that it was doing “exceptionally well,”<sup>98</sup> and was “growing exponentially.”<sup>99</sup> Clements also told KK that Avenir was a long-term investment, “safer than a

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<sup>87</sup> Tr. 1257–58; CX-80, at 13–14.

<sup>88</sup> Tr. 1258.

<sup>89</sup> Tr. 1303.

<sup>90</sup> Tr. 1591–93.

<sup>91</sup> Tr. 1591–93.

<sup>92</sup> Tr. 1334–35, 1593–94.

<sup>93</sup> Tr. 1335–40, 1594–96.

<sup>94</sup> Tr. 1334–42, 1461, 1595–1602, 1635–36, 1640.

<sup>95</sup> Tr. 1334–42, 1461, 1595–1602, 1635–36, 1640.

<sup>96</sup> Tr. 1334–42, 1461, 1595–1602, 1635–36, 1640.

<sup>97</sup> Tr. 1340–41.

<sup>98</sup> Tr. 1598.

<sup>99</sup> Tr. 1340, 1596.

mutual fund and a bank,” and that the Firm was financially supported by a billionaire “Wall Street Investor,” whom he referred to as “Noel” (an apparent reference to NL).<sup>100</sup>

Afterward, KK agreed to purchase a two percent interest in the Firm for \$100,000.<sup>101</sup> KK made the investment in two payments of \$50,000 on December 18, 2013, and March 3, 2014.<sup>102</sup> The only document KK received in connection with his December 2013 investment was a Purchase Agreement, drafted by Clements, which KK signed on December 18, 2013.<sup>103</sup> It contained no investment risk disclosure.<sup>104</sup>

In connection with his March 2014 investment, KK received a Purchase Agreement and Risk Disclosure, but these documents also failed to include investment-specific risk disclosures.<sup>105</sup> Further, these documents did not disclose the use of proceeds and selling compensation associated with KK’s equity purchase.<sup>106</sup> (As discussed below, however, KK later executed and returned an undated letter to Avenir stating that he was orally advised before investing that his investment in Avenir would be used for the operations and growth of the Firm and that Rodriguez would receive 10 percent selling compensation for his solicitation of KK’s two Avenir investments).<sup>107</sup>

Finally, when KK made these investments, neither Rodriguez nor Clements provided him with any financial statements or other documents or information concerning the Firm’s financial condition.<sup>108</sup> And, specifically, Clements did not tell KK that Avenir had recently been prohibited from conducting a securities business due to insufficient capital.<sup>109</sup>

## **2. Respondents’ Defenses and Witness Credibility**

Clements disputes making misrepresentations or omissions to KK. In fact, he denied any involvement in soliciting KK’s Avenir equity investment,<sup>110</sup> maintaining that he first spoke to

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<sup>100</sup> Tr. 1339, 1595–96.

<sup>101</sup> Tr. 1600; CX-26; CX-27; CX-28.

<sup>102</sup> Tr. 1600; CX-26; CX-27; CX-28. Also on March 3, 2014, KK executed an Avenir Financial Group, Inc. Equity Purchase Agreement disclosing that he had done his own due diligence on the Firm and was aware of the liquidity risks of his investments. CX-29.

<sup>103</sup> CX-26; *see also* CX-66; CX-71; Tr. 1733–34.

<sup>104</sup> CX-26; Tr. 463.

<sup>105</sup> CX-27; CX-28; CX-29.

<sup>106</sup> Respondents Michael Todd Clements and Avenir Financial Group’s Post-Hearing Brief at 8 (“Avenir and Clements Br. at \_\_”).

<sup>107</sup> RX-8; CX-72.

<sup>108</sup> *See* CX-94, at 2 (responding to FINRA information request. *See* CX-92, at 2 ¶ (1(g)); Tr. 1598–99.

<sup>109</sup> Tr. 1599–1600.

<sup>110</sup> Tr. 464, 2192–95.

KK in March 2014, after KK made his second investment in Avenir.<sup>111</sup> Also, Avenir and Clements argue that Rodriguez's and KK's testimony was self-serving and should be rejected. Generally, they challenge KK's recollection of events because he admitted taking medication that affected his memory in December 2013.<sup>112</sup> And, further, they suggest that KK simply had "buyer's remorse when Avenir did not generate large returns."<sup>113</sup> They also specifically challenge KK's testimony that he was not informed of the selling compensation associated with his Avenir investment and the intended use of proceeds. They argue that KK signed a letter acknowledging those representations. And, although he claimed not to have read the letter before signing it, they urge the Panel to reject that testimony because the letter was only six lines long and KK sent it from his business fax number.<sup>114</sup>

We reject these arguments, as we found KK's testimony not only credible, but compelling. He movingly related the story of the loss of his daughter, his desire to provide for his young granddaughter's future, and his discussions with Rodriguez and Clements about how to invest his deceased daughter's insurance proceeds. His memory about key events was clear and was corroborated by Rodriguez's testimony. Regarding KK's letter acknowledging that Rodriguez made intended use and compensation disclosures to him, while we considered it, we gave it minimal weight in assessing KK's credibility: Given his close relationship with Rodriguez, we found it credible that KK may have simply followed Rodriguez's instructions to sign the letter, doing so either without reading it, without reading it closely, or irrespective of its contents. On balance, we credited KK's version over Clements's.

Avenir and Clements also attack Rodriguez's credibility, claiming that his testimony is undermined by his ulterior motives. According to Clements, after Rodriguez was barred from the securities industry, Rodriguez told Clements that "one way or the other" he would obtain the return of the Avenir equity investments made by KK and another investor, AC.<sup>115</sup> This testimony was uncorroborated; Rodriguez was not asked during his testimony whether he made this alleged statement to Clements; and, generally, the Panel did not find Clements particularly credible. Still, we recognize that Rodriguez might have wanted to help KK and AC. But this did not cause us to reject his testimony, which, overall, we found credible, as it was corroborated by KK's testimony and was not undercut by cross-examination.

#### **E. Rodriguez's Sales of BRCH Promissory Notes and Equity Interests**

In addition to selling Avenir equity interests, Rodriguez also solicited investments in BRCH. From April 2014 through January 2015, Rodriguez raised \$173,800 for BRCH from six

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<sup>111</sup> Tr. 2192–95.

<sup>112</sup> Tr. 1638–39.

<sup>113</sup> Avenir and Clements Br. at 20.

<sup>114</sup> Tr. 1639; RX-8; CX-72.

<sup>115</sup> Tr. 2364–66.

customers by selling promissory notes and BRCH equity interests.<sup>116</sup> In selling the promissory notes and equity interests, he used as a model the purchase agreements that Clements created.<sup>117</sup>

## 1. BRCH Promissory Notes Offering

In April 2014, Rodriguez sought and obtained permission from Clements for BRCH to raise up to \$500,000 in a self-offering of promissory notes issued by BRCH.<sup>118</sup> Clements approved the issuance of the promissory notes in writing on April 10, 2014, noting that Rodriguez had “Completed Private Transaction training” two days earlier.<sup>119</sup> Clements drafted and provided Rodriguez with the promissory notes that Rodriguez sold to BRCH investors.<sup>120</sup> Each of these notes stated that the selling compensation related to the offering and included a disclosure limiting the use of funds to general operating expenses and growing BRCH.<sup>121</sup> Thereafter, between April 2014 and January 2015, Rodriguez sold \$99,300 in BRCH-issued promissory notes to four investors: KK, the Ss (CS and AS), and ES.<sup>122</sup>

In connection with the BRCH sale of promissory notes, Clements prepared a Private Transaction Customer Disclosure Acknowledgment that at least two investors signed.<sup>123</sup> This document contained two misstatements: “Avenir has no direct or indirect involvement whatsoever in this offering” and “this investment . . . is not supervised by [Avenir].”

## 2. Rodriguez’s Sale of BRCH Equity Interests

From May 2014 through October 2014, Rodriguez also sold equity interests in BRCH in the amount of \$74,500 to four investors, namely, KK, CS, AC, and RD.<sup>124</sup> As discussed above, the promissory notes described how BRCH planned to use investor proceeds. By contrast, the

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<sup>116</sup> CX-31; CX-34.

<sup>117</sup> Tr. 539, 1302–07.

<sup>118</sup> CX-38; CX-59; CX-153, at 5; Tr. 168, 1299–1302; RX-11, at 1; Avenir and Clements Answer ¶ 57.

<sup>119</sup> Avenir and Clements Answer ¶ 57.

<sup>120</sup> Tr. 508–09; 1299–1305.

<sup>121</sup> Avenir and Clements Answer ¶¶ 55, 60, 72, 78; CX-38; CX-49; CX-51; CX-57.

<sup>122</sup> CX-31; CX-34; Tr. 1310–12. On April 15, 2014, KK purchased a BRCH promissory note in the amount of \$45,000. Avenir and Clements Answer ¶ 60; (CX-38); the Ss purchased a BRCH promissory note in the amount of \$25,000 on August 8, 2014 (CX-49), and on October 3, 2014, they purchased an additional BRCH promissory note in the amount of \$10,000 (CX-51); and ES purchased a BRCH promissory note in the amount of \$19,300 on January 14, 2015 (CX-57).

<sup>123</sup> See, e.g., CX-37 (KK); CX-56 (ES); Tr. 1376–77, 1384.

<sup>124</sup> CX-31; CX-34; Tr. 1310–12. KK purchased an equity interest in BRCH on May 9, 2014, and paid \$8,000 (CX-39; CX-34, at 1); CS purchased an equity interest in BRCH on May 16, 2014, and made payments totaling \$36,000 (CX-41; CX-34, at 1–3, 5); AC purchased an equity interest in BRCH on June 20, 2014, for \$7,500; (CX-45; CX-34, at 2); and RD purchased an equity interest in BRCH on September 5, 2014, and made payments totaling \$23,000. (CX-52; CX-34, at 5, 6).

equity purchase agreements did not contain a similar representation.<sup>125</sup> Rodriguez, however, orally informed the BRCH equity investors that he would use their investment proceeds to expand BRCH's operations in Chicago and New York as well as for "day to day operations [and] expenditures."<sup>126</sup>

### **3. Clements's Knowledge of the BRCH Equity Interest Sales**

Unlike the BRCH promissory notes offering, it is not clear that Clements had advance or contemporaneous knowledge of Rodriguez's sale of BRCH equity interests. Rodriguez and Clements gave conflicting testimony on this subject. Rodriguez testified that soon after Clements approved Rodriguez's sale of BRCH notes, he sought Clements' permission to sell equity shares issued by BRCH, and that Clements told him to use the same purchase agreement used in connection with the Avenir equity self-offering in the fall of 2013. Rodriguez also testified that during their discussions about the BRCH equity offering, Clements told him that he could sell "personal shares" of BRCH and could use the proceeds for personal expenses as long as he recorded the sales, and all personal expenses, in BRCH's books and records and reported them to his firm's CPA.<sup>127</sup>

Clements disputes this version. He testified that Rodriguez never informed him or Avenir that Rodriguez intended to solicit individuals to purchase BRCH equity and never sought permission to do so.<sup>128</sup> In fact, Clements claims that he was unaware of the BRCH equity offering until approximately March 2015, some five months after the last sale.<sup>129</sup> Further, Clements specifically denied providing Rodriguez with a form to conduct the BRCH equity solicitations. Rather, according to Clements, Rodriguez already had a copy of the form Avenir used for the sale of Avenir equity interests.<sup>130</sup> Moreover, Clements argues that Rodriguez's version of events is not believable because the purchase agreement that Clements allegedly provided to Rodriguez, or suggested he use, was not for the sale of "personal shares." (And, in fact, the purchase agreements Rodriguez actually used in connection with the BRCH equity raises reflected an agreement between the issuer (BRCH) and the investor, and not between Rodriguez and the investor).<sup>131</sup>

Avenir and Clements also attack Rodriguez's testimony on the grounds that Rodriguez intentionally concealed the BRCH equity offering from them. As proof, they point to the manner

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<sup>125</sup> CX-39; CX-41; CX-45; CX-52.

<sup>126</sup> Tr. 1313-14; CX-111, at 3-6.

<sup>127</sup> Tr. 1309-10, 1324.

<sup>128</sup> Tr. 495-96, 2206.

<sup>129</sup> Tr. 2206-07.

<sup>130</sup> Tr. 2220-21.

<sup>131</sup> CX-39; CX-41; CX-45; CX-52.

in which Rodriguez handled a June 16, 2014 FINRA Rule 8210 request for information.<sup>132</sup> Respondents note that Rodriguez sent a draft response to Clements for his review,<sup>133</sup> but the draft omitted any reference to the BRCH offering. And Clements's response to Rodriguez after his review did not mention that offering.<sup>134</sup> Also, when Rodriguez responded to the request on June 30, 2014,<sup>135</sup> and informed FINRA that he had previously solicited investors to purchase BRCH equity,<sup>136</sup> he did not send a copy of his response to Avenir.<sup>137</sup> Avenir and Clements contend that taken together, these facts show that Rodriguez concealed the BRCH equity offering from them<sup>138</sup> and that Clements was unaware of the offering.<sup>139</sup>

We were not convinced, however, that Rodriguez deliberately concealed the equity offering from Avenir and Clements. It is implausible that he would try to conceal the offering from Respondents, while at the same time disclose the existence of the offering to FINRA. Moreover, Rodriguez knew that Clements helped draft the response, which noted that the Firm was providing FINRA with BRCH bank statements and general ledgers—documents that reflect deposits of equity investor funds.<sup>140</sup>

Nevertheless, we find that Clements probably lacked advance or contemporaneous knowledge of the offering, at least with respect to the offering of shares other than Rodriguez's personal shares. Rodriguez's testimony about Clements's advance knowledge was uncorroborated. And we view it as unlikely that Clements would have specifically advised Rodriguez that he could use investor funds for his personal expenses (except perhaps funds from the sale of his own personal BRCH holdings). Further, even if Rodriguez and Clements did discuss a forthcoming BRCH equity offering, the particulars of those discussions remain murky. For example, it is not clear what, if anything, Rodriguez may have said to Clements about the proposed details of the offering, including whether the upcoming offering was limited to only Rodriguez's personal shares of BRCH, or what disclosures should be made to investors about the intended use of the proceeds. In short, the evidence of Clements's advance knowledge was conflicting, unclear, and inconclusive.

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<sup>132</sup> CX-85.

<sup>133</sup> RX-42.

<sup>134</sup> RX-42, at 2–3.

<sup>135</sup> CX-87.

<sup>136</sup> CX-87.

<sup>137</sup> Tr. 1815–17.

<sup>138</sup> Avenir and Clements Br. at 21.

<sup>139</sup> Tr. 2206–07.

<sup>140</sup> RX-42, at 3–4. As we discuss later, the general ledger's entries contained red flags that placed, or should have placed, Clements on notice that Rodriguez was conducting a BRCH equity offering.



## F. Rodriguez Misuses Investor Funds

From April 2014 through February 2015, Rodriguez raised \$173,800 from investors in the BRCH equity and promissory notes offerings.<sup>141</sup> The offering funds were deposited into the BRCH bank account. Also during this period, Rodriguez withdrew \$77,287.55 from that account to pay personal expenses.<sup>142</sup> At the time of each BRCH equity and debt sale, Rodriguez represented to investors either orally or in writing that their investment proceeds would be used for general operating expenses and growing BRCH.<sup>143</sup> Contrary to these representations, Rodriguez misused a portion of the funds to pay for his personal expenses. This much is undisputed.

The parties disagree, however, about the amount of investor funds Rodriguez used for personal expenses, and whether he used both promissory notes funds and equity funds to pay for those expenses. Enforcement contends that Rodriguez admitted to using more than \$77,000 of the investors' \$173,800 investment to pay personal expenses (i.e., expenses unrelated to BRCH's business operations).<sup>144</sup> And, in fact, Rodriguez admitted spending \$77,000 on personal expenses,<sup>145</sup> and conceded that he "used some of the monies that [he] raised from the equity that [he] sold of [his] portions of the shares for Bull Run."<sup>146</sup> But he denied misusing funds from the BRCH promissory notes offering.<sup>147</sup>

For their part, Respondents Avenir and Clements concede that Rodriguez misused investor funds, but deny that he misused funds totaling \$77,287.55 or that he misused any promissory notes funds. Respondents argue that "Enforcement failed to account for Rodriguez's

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<sup>141</sup> CX-34, at 7.

<sup>142</sup> CX-31; CX-34. For example, funds were withdrawn to pay for expenses attributed to "Kay Jewelers" (CX-34, at 1); "Build a Bear" (CX-34, at 1); "Great Clips" (CX-34, at 2); Petco (CX-34, at 3); "Perfumania" (CX-34, at 4); and "Vitamin Shop" (CX-34, at 4).

<sup>143</sup> Avenir and Clements Answer ¶ 55.

<sup>144</sup> Department of Enforcement's Post-Hearing Brief at 37 ("Enf's Opening Br. at \_\_") (citing CX-31; Tr. 1265–1266; CX-84). On April 27, 2015, FINRA barred Rodriguez from association with any FINRA member firm based on a Letter of Acceptance, Waiver and Consent ("AWC") which he submitted. Under the terms of the AWC, Rodriguez consented to findings that he defrauded investors by misusing for personal expenses approximately \$77,000 of the \$173,800 raised from six investors in equity and/or promissory note offerings. (CX-84, at 3). Enforcement relies upon this AWC as proof that Rodriguez used investor funds to source the personal expense withdrawals. The Panel considered the AWC, but gave it little weight because Rodriguez accepted and consented to the findings without admitting or denying them (CX-84, at 1). And, although he was precluded under a provision in the AWC from taking positions in any proceeding brought by or on behalf of FINRA that are inconsistent with the AWC, that provision also states that it does not "effect" his "testimonial obligations," so he was free to testify differently than his AWC, if necessary to comply with his testimonial obligation to provide truthful testimony.

<sup>145</sup> Tr. 1271–72.

<sup>146</sup> Tr. 1265.

<sup>147</sup> Tr. 1310, 1478, 1551.

personal funds that were deposited into the Bull Run bank account.”<sup>148</sup> By subtracting Rodriguez’s personal fund deposits (\$42,185.78)<sup>149</sup> from the personal expense withdrawals (\$77,287.55) during the period April 8, 2014 through February 27, 2015, they conclude that “his misuse of investor funds is actually \$35,101.77.”<sup>150</sup>

Further complicating the misuse calculation, neither party traced the source of the funds used for each personal expense payment withdrawal. Nor is the Hearing Panel readily able to do so based on its review of the evidence because Rodriguez did not segregate into separate bank accounts the funds raised in each offering. Instead, he comingled in one account the funds raised in the offerings along with unrelated funds he and others deposited. This comingling makes it unclear whether a specific withdrawal was funded by a deposit of promissory notes funds, equity interest funds, or unrelated funds.

Nevertheless, we do not believe that Enforcement’s failure to trace, or our inability to trace, the source of funds for the expense payment withdrawals precludes us from finding that Rodriguez paid those expenses from funds raised in both the equity and promissory notes offerings. First, it is clear that without the investor funds, Rodriguez would have been unable to use the BRCH account to pay all of the listed personal expenses, as that account otherwise lacked sufficient funds to do so. As reflected on BRCH’s general ledger and the summary exhibit derived from it, the personal expense withdrawals substantially exceeded the deposits unrelated to the offerings.<sup>151</sup> From April 8, 2014, through February 27, 2015, deposits by Rodriguez and others —unrelated to the capital raises—totaled \$54,516.42. The withdrawals for personal expenses exceeded these deposits by \$22,771.13. Second, it was Rodriguez, himself, who made it difficult—if not impossible—to trace the source of the personal expense withdrawals: it was his decision to comingle in one account the investors’ funds with other funds and to then withdraw funds from that account to pay for personal expenses. Thus, fairness requires that our calculation of customer fund misuse be construed against him.

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<sup>148</sup> Avenir and Clements Br. at 22 n.143

<sup>149</sup> This amount was derived from CX-34, a summary exhibit based on BRCH’s general ledger, which reflected all deposits made in, and withdrawals for personal expenses made from, the BRCH bank account during the period April 8, 2014, through February 27, 2015. Rodriguez disputes the accuracy of this figure, claiming that he deposited additional funds beyond \$42,185.78 into the account. He testified that those additional funds consisted of the proceeds from the sale of his personal shares in BRCH. Tr. 1270, 1272. Indeed, BRCH’s general ledger reflects two unlabeled additional deposits into the account totaling \$11,400, made in January 2014, before the period reflected in CX-34. One of the deposits was made by Rodriguez in the amount of \$2,100.

<sup>150</sup> Avenir and Clements Br. at 22 n.143. *See also* CX-34, at 7. Their calculation fails to account for, i.e., subtract, non-investor funds deposited during the period April 8, 2014, through February 27, 2015, by other individuals and third parties totaling \$12,330, as well as the January 2014 deposits totaling \$11,400 referenced in footnote 149, above.

<sup>151</sup> Also, it appears that the infusion of investor funds may well have precipitated Rodriguez’s personal expense withdrawals. In January 2014, the bank account’s balance rose to \$11,293.95. CX-31, at 1. Yet, he withdrew no funds from the account that month, or during the next two months. But in April, only after he began depositing the proceeds from the promissory note and equity interest sales, Rodriguez started withdrawing funds, including funds to pay for personal expenses. CX-31, at 1; CX-34, at 1.

Therefore, the Hearing Panel did not consider the inability to trace funds in this instance as an impediment to finding that Rodriguez misused \$77,287.85 in investor funds.<sup>152</sup>

### **G. Avenir Fails to Provide Written Disclosures to Investors or Make Appropriate Filings with FINRA**

Avenir failed to provide written disclosures regarding the use of proceeds or selling compensation to any investor or prospective investor (except JC) regarding any equity self-offering by either Avenir or BRCH before December 2014. Nor, prior to that date, did it file the written disclosures with FINRA.<sup>153</sup> And, with respect to the BRCH equity offerings, Avenir did not provide these written disclosures to investors or prospective investors and did not file the written disclosures with FINRA.<sup>154</sup>

### **H. Supervision**

#### **1. Avenir and Clements Fail to Adequately Supervise Avenir and BRCH's Capital Raising**

Clements was primarily responsible for supervising the capital raising activity at Avenir and its branch offices.<sup>155</sup> He was also Rodriguez's direct supervisor and was required to supervise all of BRCH's capital raising activity, including conducting due diligence before any

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<sup>152</sup> Cf. *Drexel Highlander Ltd. P'ship v. Edelman (In re Edelman)*, 2014 Bankr. LEXIS 2013, at \*90–92 (Bankr. N.D. Tex. May 6, 2014), *aff'd*, *Edelman v. Drexel Highlander L.P.*, 2015 U.S. Dist. LEXIS 130115 (N.D. Tex. Sept. 28, 2015) (finding no impediment to calculating amount of funds paid to debtor, or used for his direct or indirect benefit, notwithstanding inability to trace funds paid for these purposes because of comingling) (citing *In re Colson*, 2013 Bankr. LEXIS 4001, 2013 WL 5352638, at \*33 (Bankr. S.D. Miss. Sept. 23, 2013)) (“The Court agrees with Colson that the question of what happened to the money was not answered definitively at Trial. The Court rejects, however, Colson’s attempt to use Fidelity’s inability to trace the escrow funds as a defense to his breach of the fiduciary duty he owed the lenders. It was Colson who structured the accounts in a way that allowed him to play hide-and-seek with escrow funds. To allow Colson to benefit from the complexity of that structure by requiring Fidelity to untangle the commingled funds would reward him for how well he succeeded in breaching his fiduciary duty to the lenders.”).

<sup>153</sup> In December 2014, the Firm made untimely filings with FINRA representing that it made oral disclosures to Avenir investors JC, AC, KK, and NL regarding the use of proceeds and selling compensation. CX-63; CX-65; CX-66; CX-67; CX-68; CX-96, at 1–2, ¶ 3 (responding to FINRA information request dated December 11, 2014. CX-95, at 2, ¶ 3); Tr. 1728–36.

<sup>154</sup> As discussed below, Avenir has conceded in this proceeding that it failed to make the required written disclosures or filings in connection with both the Avenir and BRCH equity self-offerings. *See also* Tr. 1312–13; 1482–83 (Rodriguez testifying that he told BRCH equity investors that he would use their funds for day to day operations and, in part, to expand the operations of two branch offices (located in Chicago and New York), but making no reference to having done so in writing).

<sup>155</sup> Tr. 227–29; CX-61, at 7–8.

BRCH offering.<sup>156</sup> One of Clements’s responsibilities was to audit the use of proceeds raised in these offerings.<sup>157</sup>

We find that Avenir and Clements failed to exercise reasonable supervision in connection with their supervision of the Avenir and BRCH capital raisings. First, as to both Ibrahim’s sale of an Avenir equity interest to NL, and Rodriguez’s sale of an Avenir equity interest to KK, Clements took no steps to ensure that they disclosed the Firm’s precarious financial condition. As discussed below in the Conclusions of Law section, this was material information that should have been disclosed to prospective investors.

Second, it is undisputed that Clements (1) failed to advise Rodriguez that the BRCH equity raises were member private offerings subject to FINRA Rule 5122’s disclosure and filing requirements;<sup>158</sup> (2) failed to ensure that Rodriguez made adequate and accurate written disclosures about the use of proceeds to BRCH investors; and (3) failed to file any such written disclosures with FINRA. Collectively, these failures resulted in the Firm’s continued non-compliance with those provisions.

Third, Clements failed to ensure that the appropriate filings and disclosures were made in a timely fashion by Avenir regarding its equity offerings.

Fourth, Clements failed to detect, or ignored, red flags contained in BRCH’s bank statements and general ledger that Rodriguez may have been conducting an equity offering and misusing investor funds. Clements was aware of FINRA’s Rule 8210 request and helped draft and review Rodriguez’s response, which attached BRCH bank statements and the general ledger. Clements should have reviewed these documents by at least June 2014. Had Clements reviewed these documents, he would have seen deposits and withdrawals from the BRCH bank account—the same account into which Rodriguez deposited investor funds and made withdrawals that were, on their face, for personal expenses. And, thus, he would have seen—and should have pursued—indications of an equity offering and misuse of funds.

Fifth, Clements drafted a “PRIVATE TRANSACTION CUSTOMER DISCLOSURE ACKNOWLEDGEMENT,” containing misstatements and errors, which Rodriguez used in connection with the BRCH promissory notes offering.<sup>159</sup> Two investors in that offering, KK and ES, represented on the Acknowledgement that through their “own independent due diligence, review of the Offering Document, all other addendums, financials and disclosures, [they were] fully aware of the various risks and liquidity issues associated with this start-up company

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<sup>156</sup> CX-58, at 2; Tr. 685–86.

<sup>157</sup> Tr. 240–43.

<sup>158</sup> *See, e.g.*, Tr.1342– 3 (Rodriguez testifying that he was not familiar with Rule 5122 until he prepared for his OTR).

<sup>159</sup> The version of the Acknowledgements admitted into evidence was prepared by Clements (Tr. 1376–77, 1384) and contained language similar, but not identical, to the language alleged in the Amended Expedited Complaint. Compare CX-37 and CX-56 with Amended Expedited Complaint ¶¶ 89, 90.

investment and have deemed it a suitable investment for my portfolio.” Given his involvement in the BRCH promissory note offering, Clements knew, or should have known, that there were no “addendums” for the capital raise. Also, to the extent that any BRCH “financials” even existed, he knew, or should have known, that Rodriguez never provided them to investors. Thus, Clements was, or should have been, aware that the Acknowledgement contained false statements. Therefore, it was a red flag that KK and ES either did not understand the Acknowledgement or executed it without review. This is especially true in connection with investor ES, who signed his Acknowledgement on December 16, 2014.<sup>160</sup> Clements had visited the BRCH-owned Avenir Chicago branch the prior month and was acutely aware that financial documentation was not available to review.

Finally, Avenir never investigated or disciplined Rodriguez, placed him on heightened supervision, or terminated his association with the Firm, even after learning of his misconduct.<sup>161</sup>

## **2. Avenir and Clements’s Defense of Their Supervision of Rodriguez**

Clements and Avenir defend their supervision of Rodriguez, maintaining that they acted reasonably but that Rodriguez concealed the equity offering from them. In support of this position, they point out that Clements conducted two branch audits of Rodriguez’s Avenir branch near Chicago, one in March and the other in November 2014.<sup>162</sup> According to Clements, during the March 2014 visit to the Chicago branch, he reviewed the documents on file and the books and records.<sup>163</sup> Following this audit, as discussed above, they assert that Rodriguez failed to give them a copy of his June 2014 Rule 8210 response disclosing the equity offering.

Clements also conducted a November 2014 audit. During that audit, he reviewed, among other things, the documents relating to the BRCH promissory note offerings.<sup>164</sup> At that time, according to Clements, he sought financial information from BRCH and observed numerous deficiencies, including a lack of financials and missing account documents. In fact, with the exception of a few bank statements, Rodriguez did not have BRCH financial information at his Avenir branch office in Chicago.<sup>165</sup> Still, according to Allen and Clements, they pressed Rodriguez for financial documents beginning in the fall of 2014 and received them the next month.<sup>166</sup> And in July 2015, they also received BRCH financial documents from Rodriguez’s

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<sup>160</sup> CX-56.

<sup>161</sup> Tr. 2314–15.

<sup>162</sup> Tr. 520, 2222–26.

<sup>163</sup> Tr. 2195–96.

<sup>164</sup> Tr. 2222–24.

<sup>165</sup> Tr. 2222–26.

<sup>166</sup> Tr. 1909–13. *See also* Tr. 2226–27 (in which Clements references the receipt of financial information in December 2015, apparently misspeaking and meaning, instead, 2014).

accountant.<sup>167</sup> In sum, according to Avenir and Clements, these circumstances show that they properly supervised Rodriguez, but that he evaded supervision.

We reject this view of the evidence. First, by June 30, 2014, Rodriguez produced certain BRCH bank statements, financial statements, and a general ledger to FINRA, all of which were available for Clements's review as discussed above.<sup>168</sup> These documents showed that Rodriguez was withdrawing funds from the BRCH bank account for personal expenses and should have caused Clements to inquire further and require satisfactory responses from Rodriguez or take prompt corrective action to address the irregularities. But it does not appear that he ever reviewed those documents or, if he did, that he ever took any follow-up actions based on them. Instead, five months later, he audited Rodriguez's Chicago branch in November 2014 and was stymied by the lack of financial documentation available for his review. By that time, Rodriguez had been selling BRCH notes since April 2014 and equity interests since May 2014, raising over \$154,000.<sup>169</sup> Yet, in the face of the deficiencies Clements observed during the November audit, he took no action to stop Rodriguez from conducting capital raises, which continued, unabated, until January 2015.<sup>170</sup>

Accordingly, we find that the above-described failures, in their totality, constituted a failure by Avenir and Clements to reasonably supervise Rodriguez.

### **3. The Panel Rejects Certain Alleged Failures to Supervise by Clements**

While we find that Clements failed in a number of respects to reasonably supervise the Avenir and BRCH capital raises, we reject certain allegations of unreasonable supervision. First, Enforcement alleged that Avenir and Clements failed to supervise Ibrahim's capital raising because he did not explain to Ibrahim (a) the basis for the valuation of equity interests in Avenir; (b) the Plan of Action; or (c) the prices paid for recent investments in Avenir. As we explain below, we did not find that this information was material to investors. And, therefore we do not find that reasonable supervision required Clements to explain this information to Ibrahim and ensure that he disclosed it to investors.

Second, Enforcement alleged that Clements did not reasonably supervise Rodriguez because he did not confirm that Rodriguez was soliciting only accredited investors to invest in BRCH, notwithstanding certain alleged information in Avenir's own records indicating that

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<sup>167</sup> RX-18. There was conflicting evidence about the frequency with which Rodriguez provided BRCH financial information to Avenir. Rodriguez testified it was his practice to provide Allen, Avenir's co-owner, with BRCH's financials, including its general ledger. Tr. 1281. Allen disputed this version, testifying that although he asked Rodriguez for the financials on numerous occasions, he found evidence of BRCH having provided Avenir with financial documents on only two occasions, the first time being in December 2014. Tr. 1909–11. We found the evidence inconclusive and were therefore unable to resolve this disputed issue.

<sup>168</sup> CX-87.

<sup>169</sup> CX-31; CX-34.

<sup>170</sup> CX-34, at 6.

certain investors were not accredited.<sup>171</sup> The record, however, did not demonstrate that he failed to supervise reasonably in this regard. The parties largely ignored this issue at the hearing and did not address it in their pre- or post-hearing briefs.

Third, according to Enforcement, Clements failed to conduct reasonable due diligence regarding BRCH to determine whether the prices charged for equity in BRCH bore a reasonable relationship to the actual equity value in the firm. We make no finding on this specific allegation, given our broader finding that, after June 2014, he failed to reasonably supervise the BRCH equity offering.

Finally, Enforcement alleged that Clements failed to supervise Rodriguez because he advised him that he could treat the proceeds of the BRCH equity raises as his personal funds. But as we discussed above, on this point the evidence was inconclusive.

### **III. Conclusions of Law**

#### **A. Avenir, Clements, and Ibrahim Willfully Violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, and Violated FINRA Rules 2020 and 2010 (First Cause of Action)**

Enforcement charges that all Respondents made material omissions to NL in connection with his purchase of an Avenir equity interest, thereby willfully violating Section 10(b) of the Securities Exchange Act of 1934 (“Exchange Act”) and Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010. Enforcement also charges that Avenir and Clements violated these provisions by making material misrepresentations and omissions to KK in connection with his Avenir equity interest purchase.

Exchange Act Section 10(b) and Exchange Act Rule 10b-5 prohibit fraudulent and deceptive acts and practices in connection with the purchase or sale of a security.<sup>172</sup> To establish that Respondents violated Exchange Act Section 10(b) and Rule 10b-5 thereunder, Enforcement must prove by a preponderance of the evidence that they made material misrepresentations or omissions in connection with the purchase or sale of a security and that they acted with scienter.<sup>173</sup> FINRA Rule 2020 is FINRA’s anti-fraud rule and prohibits members from

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<sup>171</sup> Rodriguez was permitted to solicit only accredited investors for any private offering. Avenir and Clements Answer, ¶ 91.

<sup>172</sup> Exchange Act Section 10(b) makes it “unlawful for any person . . . [t]o use or employ, in connection with the purchase or sale of any security . . . , any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe.” 15 U.S.C. § 78j(b). Exchange Act Rule 10b-5 makes it unlawful “[t]o employ any device, scheme, or artifice to defraud; to make any untrue statement of material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.” 17 C.F.R. § 240.10b-5.

<sup>173</sup> *Dep’t of Enforcement v. Fillet*, No. 2008011762801, 2013 FINRA Discip. LEXIS 26, at \*18 (NAC Oct. 2, 2013), *aff’d in relevant part*, Exchange Act Release No. 75054, 2015 SEC LEXIS 2142 (May 27, 2015). Enforcement must

“effect[ing] any transaction in, or induc[ing] the purchase or sale of, any security by means of any manipulative, deceptive or other fraudulent device or contrivance.”<sup>174</sup> Respondents violated Rule 2020 if, acting with scienter, they induced the purchase or sale of a security “by means of” a material false statement or omission.<sup>175</sup> A violation of the SEC’s or FINRA’s anti-fraud rules also violates FINRA Rule 2010.<sup>176</sup>

“Whether information is material ‘depends on the significance the reasonable investor would place on the . . . information.’”<sup>177</sup> “Information is material ‘if there is a substantial likelihood that a reasonable [investor] would consider it important in deciding how to [invest] . . . [and] the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the ‘total mix’ of information made available.’”<sup>178</sup> There is a substantial likelihood that a reasonable investor would consider it important if the issuer is experiencing financial difficulty as this may well impact the investor’s ability to obtain a positive return on the investment.<sup>179</sup>

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also prove that Respondents used “any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange.” 17 C.F.R. § 240.10b-5. Enforcement satisfied this requirement because Ibrahim communicated with NL by “[p]hone, email fax,” Tr. 887, and because all Avenir sales made to KK were initially solicited by telephone. Tr. 1593–98. *See Fillet*, 2013 FINRA Discip. LEXIS 26, at \*19 n.7 (citing *SEC v. Softpoint, Inc.*, 958 F. Supp. 846, 865 (S.D.N.Y. 1997) (determining that the jurisdictional requirements of the federal antifraud provisions are interpreted broadly and are satisfied by intrastate telephone calls or the use of the U.S. mail), *aff’d*, 159 F.3d 1348 (2d Cir. 1998)).

<sup>174</sup> *Dep’t of Enforcement v. Ahmed*, No. 2012034211301, 2015 FINRA Discip. LEXIS 45, at \*88–89 (NAC Sept. 25, 2015). *See Fillet*, 2013 FINRA Discip. LEXIS 26, at \*38 (explaining that FINRA Rule 2020 “captures a broader range of activity than [Exchange Act] Rule 10b-5(b)”).

<sup>175</sup> *Dep’t of Enforcement v. Akindemowo*, No. 2011029619301, 2015 FINRA Discip. LEXIS 58, at \*29 (NAC Dec. 29, 2015), *appeal docketed*, No. 3-17076 (SEC Jan. 29, 2015); *Dep’t of Enforcement v. Davidofsky*, No. 2008015934801, 2013 FINRA Discip. LEXIS 7, at \*31 n.31 (NAC Apr. 26, 2013) (“NASD Rule 2120 [now FINRA Rule 2020] requires a showing of scienter, similar to Exchange Act Rule 10b-5.”).

<sup>176</sup> *Ahmed*, 2015 FINRA Discip. LEXIS 45, at \*89 n.83 (“Conduct that violates the Commission’s or FINRA’s rules, including the antifraud rules, is inconsistent with ‘high standards of commercial honor and just and equitable principles of trade’ and violates FINRA Rule 2010.”). “FINRA Rules 2020 and 2010, which generally apply to FINRA ‘members,’ are applicable to associated persons pursuant to FINRA Rule 0140(a).” *Id.*

<sup>177</sup> *Akindemowo*, 2015 FINRA Discip. LEXIS 58, at \*32 (quoting *Basic Inc. v. Levinson*, 485 U.S. 224, 240 (1988)).

<sup>178</sup> *Fillet*, 2013 FINRA Discip. LEXIS 26, at \*29 (quoting *Basic*, 485 U.S. at 240).

<sup>179</sup> *See, e.g. Dep’t of Enforcement v. Donner Corp. Int’l*, No. CAF020048, 2006 NASD Discip. LEXIS 4, at \*34 (NAC Mar. 9, 2006), *aff’d in relevant part*, Exchange Act Release No. 55313, 2007 SEC LEXIS 334 (Feb. 20, 2007) (finding that “[a] reasonable investor . . . would consider significant information pertaining to an issuer’s financial condition, profitability, solvency, and potential for success); *Kevin D. Kunz*, 64 F. App’x 659, 665, 2003 U.S. App. LEXIS 6011, at \*12 (10th Cir. Mar. 28, 2003) (citing *SEC v. Murphy*, 626 F.2d 633, 683 (9th Cir. 1980) (holding that “the materiality of information relating to financial condition, solvency and profitability is not subject to serious challenge”)); *Dep’t of Enforcement v. John Carris Invs.*, No. 2011028647101, 2015 FINRA Discip. LEXIS 32, at \*116–18 (OHO Jan. 20, 2015) (finding that failure to disclose in connection with a self-offering that a broker-dealer was not in net capital compliance was a material omission).



“Scienter is defined as ‘a mental state embracing intent to deceive, manipulate, or defraud.’”<sup>180</sup> “Scienter is established if a respondent acted intentionally or recklessly.”<sup>181</sup> “Reckless conduct includes ‘a highly unreasonable omission, involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it.’”<sup>182</sup>

### **1. Avenir, Clements, and Ibrahim Willfully Failed to Disclose Material Information to NL**

Enforcement established that Respondents omitted information in connection with the equity interest sale to NL. Clements drafted and approved the NL Purchase Agreement,<sup>183</sup> thereby making statements to NL. And Ibrahim spoke directly to NL. Both Clements and Ibrahim were obligated to refrain from withholding material information from NL in connection with the equity interest sale to him.<sup>184</sup> But neither of them disclosed the Firm’s precarious financial condition, including the Firm’s recent 13-day stoppage of its securities business due to a net capital deficiency and the risk of another such event.

The omitted information was material, as a reasonable investor would want to know that Avenir had recently experienced financial difficulties so serious that the Firm was, for a time, unable to conduct a securities business due to insufficient net capital and that it teetered on the edge of another shut down of that business; such information bears significantly on the likely profitability of the investment.

We also find that Clements and Ibrahim acted with scienter. It is beyond dispute that Clements was fully aware of the Firm’s finances,<sup>185</sup> yet he disclosed only minimal information

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<sup>180</sup> *Akindemowo*, 2015 FINRA Discip. LEXIS 58, at \*33 (quoting *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976)).

<sup>181</sup> *Id.* (citing *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 319 n.3 (2007)). See also *Ahmed*, 2015 FINRA Discip. LEXIS 45, at \*77 n.78 (“Scienter also is established through a heightened showing of recklessness.”).

<sup>182</sup> *Fillet*, 2013 FINRA Discip. LEXIS 26, at \*35 (quoting *Sundstrand Corp. v. Sun Chem. Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977) (internal quotation omitted)); *Dep’t of Enforcement v. Reynolds*, No. CAF990018, 2001 NASD Discip. LEXIS 17, at \*45 n.28 (NAC June 25, 2001) (finding that the proper standard for a fraud claim based on SEC Rule 10b-5 is intent or recklessness and not gross negligence, although the line between recklessness and gross negligence is a fine one) (citing *Bd. of Cnty. Comm’rs v. Liberty Group*, 965 F.2d 879, 883–84 (10th Cir. 1992), *cert denied*, 506 U.S. 918 (1992)).

<sup>183</sup> CX-2; Tr. 410–12.

<sup>184</sup> See FINRA Regulatory Notice 10-22, 2010 FINRA LEXIS 43, at 15–16 (Apr. 2010) (reminding firms and registered representatives that broker-dealers that prepare private placement memoranda or other offering documents have an affirmative duty to, among other things, ensure that there are no material omissions in the offering documents disseminated to investors).

<sup>185</sup> Avenir’s financial situation remained dire through the end of 2013. The Firm’s FOCUS reports filed for the fourth quarter of 2013 reflected a quarterly loss of \$313,356. CX-125, at 6.

in the Purchase Agreement.<sup>186</sup> Ibrahim also knew of the Firm's precarious financial situation. At the time he solicited NL's investment, Ibrahim knew that the Firm had recently stopped conducting a securities business because of a net capital deficiency resulting from client negative equity balances<sup>187</sup> and that the Firm "was in a dire financial situation" and "could potentially go under" as a result.<sup>188</sup> The suspension of business at Avenir had a direct and personal impact on Ibrahim's ability to conduct securities business with his clients and earn a living during that time. Ibrahim also knew that days earlier, his customer, RF, had bounced a \$300,000 check and faced a substantial margin call.<sup>189</sup> And, as a result, the Firm potentially faced another capital crisis.<sup>190</sup> But he, too, failed to disclose the Firm's financial plight. The omitted information was so obviously material that Clements and Ibrahim's failure to disclose it was, at a minimum, reckless.

Accordingly, based on the foregoing, Avenir (acting through Clements and Ibrahim), and Clements and Ibrahim violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. They also violated FINRA Rules 2010 and 2020.

Enforcement also charges that Respondents' violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder were willful. A violation is deemed willful if "the person charged with the duty knows what he is doing."<sup>191</sup> To find that Avenir, Clements, and Ibrahim acted willfully, we need only find that they "voluntarily committed the act that constituted the violation."<sup>192</sup> Here, their violative acts were voluntary and, hence, their violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder were willful.

Avenir and Clements argue that material information was not withheld from NL. They submit that Ibrahim told NL that Avenir was trying to grow its operations and offered NL access to Avenir's books and records and provided him with the contact information for Clements and Allen. Further, according to Ibrahim, NL told Ibrahim that he did not want this information.<sup>193</sup> In other words, they blame NL for not learning about material information regarding the Firm's finances. Ibrahim also blames Clements and Allen. He points out that at the time of the NL

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<sup>186</sup> CX-8B, at 29; Tr. 406, 410-13.

<sup>187</sup> CX-139; CX-140; CX-141; Tr. 740-41, 766-77.

<sup>188</sup> Tr. 745-50.

<sup>189</sup> CX-162, at 10; CX-147; Tr. 795-801. Tr. 801-04.

<sup>190</sup> Tr. 801-04.

<sup>191</sup> *Dep't of Enforcement v. McCune*, No. 2011027993301, 2015 FINRA Discip. LEXIS 22, at \*11 (NAC July 27, 2015) (quoting *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000)), *aff'd*, Exchange Act Release No. 77375, 2016 SEC LEXIS 1026 (Mar. 15, 2016), *appeal docketed*, No. 16-9527 (10th Cir. May 12, 2016).

<sup>192</sup> *Dep't of Enforcement v. Gallagher*, No. 2008011701203, 2012 FINRA Discip. LEXIS 61, at \*25 (NAC Dec. 12, 2012); *Arthur Lipper Corp. v. SEC*, 547 F.2d 171, 180 (2d Cir. 1976) (holding that finding of willfulness does not require intent to violate the law, but merely intent to do the act that constitutes a violation of the law).

<sup>193</sup> Tr. 890-92, 2051-52.

investment, he had only been in the securities industry for about two years; that he relied on Clements and Allen as his supervisors to assure that regulatory requirements were met;<sup>194</sup> and that they were responsible for omitted facts in the offering document.<sup>195</sup>

These arguments fail. It is well established that youth and inexperience are not defenses to securities laws violations.<sup>196</sup> Nor may broker-dealers and their associated persons shift to others their obligation to comply with the duties imposed on them under the securities laws.<sup>197</sup> More specifically, a “respondent cannot shift responsibility for compliance to supervisors.”<sup>198</sup> In short, Respondents were obligated to disclose all material information to NL, and they failed to do so.

On the other hand, Enforcement failed to demonstrate that certain non-disclosed information was material. The Amended Expedited Complaint charges that Clements failed to explain to Ibrahim (thus failed to ensure that Ibrahim told NL): (1) the basis for the price of the equity offered to NL; (2) that there had been recent investments in Avenir at far lower prices than the price offered to NL; (3) that the Firm had submitted a Plan of Action to its clearing firm; and (4) the potential impact to the Firm of RF’s \$190,000 margin call.

The Panel does not find that this omitted information was material in the context of NL’s purchase.<sup>199</sup> Although a reasonable investor may have some interest in knowing what other investors had paid, in the total mix of information here, this information would not likely have impacted a reasonable investor’s decision given that a number of factors may have affected the terms that Avenir offered to any particular potential investor.

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<sup>194</sup> Ibrahim Br. at 3, 6, 13–15.

<sup>195</sup> Ibrahim Br. at 14.

<sup>196</sup> See *SEC v. Hasho*, 784 F. Supp. 1059, 1108 (S.D.N.Y. 1992) (“Those who hold themselves out as professionals with specialized knowledge and skill to furnish guidance cannot be heard to claim youth or inexperience when faced with charges of violations of the anti-fraud provisions of the securities laws.”); *Scott Epstein*, Exchange Act Release No. 59328, 2009 SEC LEXIS 217, at \*73 (Jan. 30, 2009) (rejecting youth and inexperience and lack of adequate supervision as defenses to allegations of unsuitable recommendations); *Dep’t of Enforcement v. Neaton*, No. 2007009082902, 2011 FINRA Discip. LEXIS 13, at \*20 (NAC Jan. 7, 2011), *aff’d*, Exchange Act Release No. 65598, 2011 SEC LEXIS 3719 (Oct. 20, 2011) (finding that respondent’s inexperience in the securities industry was not a defense to his failure to disclose material information on a Form U4); *Dep’t of Enforcement v. White*, No. 2012033128703, 2015 FINRA Discip. LEXIS 48, at \*70 (OHO June 30, 2015) (finding that, although new and inexperienced in the securities industry, the respondent must accept responsibility for his own actions, which cannot be excused by lack of knowledge, understanding, or appreciation of the rules).

<sup>197</sup> *Dep’t of Enforcement v. Zaragoza*, No. E8A2002109804, 2008 FINRA Discip. LEXIS 28, at \*28 (NAC Aug. 20, 2008).

<sup>198</sup> *Dep’t of Enforcement, v. Mielke*, No. 2009019837302, 2014 FINRA Discip. LEXIS 24, at \*25 n.21 (NAC July 18, 2014) (quoting *Gluckman*, 54 S.E.C. 175, 184 n.29 (July 20, 1999)), *aff’d*, Exchange Act Release No. 75981, 2015 SEC LEXIS 3927 (Sept. 24, 2015).

<sup>199</sup> In any event, even if material, Enforcement did not prove that Respondents acted with scienter when they failed to disclose this information.

Second, as to the Plan of Action, this, too, was not material, as its non-disclosure was simply part of an overarching, material non-disclosure. That the Firm had recently shut down its securities business for two weeks and was struggling financially was material information that should have been disclosed—not the particulars of a Plan of Action designed to overcome a recent financial crisis and avert another one. Likewise, we do not find that RF’s debit balance and its potential impact on the Firm was material information that required disclosure, as this, too, is subsumed in the broader non-disclosure about the Firm’s finances.

## **2. Avenir and Clements Willfully Made Material Misstatements and Omissions to KK**

As we found above, Clements falsely represented to KK that the Firm was doing “exceptionally well,” “growing exponentially,” and that KK’s investment was safe. Further, he failed to disclose the Firm’s financial troubles. The misstated and omitted information was material because, for the reasons discussed above regarding NL’s investment, it would likely have been important to a reasonable investor’s investment decision.<sup>200</sup> Also, for the reasons stated above in connection with NL’s investment, Clements made the misstatements and omissions at least recklessly and, therefore, with scienter. Clements’ violative acts were voluntary and, hence, the violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder were willful.

Accordingly, Avenir, acting through Clements, and Clements willfully violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. They also violated FINRA Rules 2020 and 2010.

### **B. Avenir Willfully Violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and violated FINRA Rules 2020 and 2010 in the Sale of Debt and Equity Interests in BRCH (Second Cause of Action)**

Enforcement charged that prior to, and in connection with, the sales of equity or debt investments in BRCH, Avenir, acting through Rodriguez, knowingly misrepresented to KK, CS, AC, RD, the Ss, and ES the intended use of their investment proceeds. As a result, Enforcement claims that Avenir willfully violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and violated FINRA Rules 2020 and 2010.

Enforcement proved that Rodriguez misrepresented to the debt and equity investors, either orally or in writing, that their investment proceeds would be used for general operating expenses and growing BRCH.<sup>201</sup> In fact, he misused a portion of the funds to pay for his personal expenses. The misrepresentations were made in connection with the sale of securities and

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<sup>200</sup> The Amended Expedited Complaint also charges that as part of the fraud against KK, Clements failed to disclose (1) that Avenir had permitted others to purchase Avenir equity interests at much lower prices than offered to him or (2) the details of the Plan of Action. For the reasons stated above, we do not find this information material or that Clements made these omissions with scienter.

<sup>201</sup> Avenir and Clements Answer ¶ 55.

through the use of the instrumentalities of interstate commerce.<sup>202</sup> Rodriguez's misrepresentations were material because the use of proceeds would be important to a reasonable investor's investment decision.<sup>203</sup> Also, because Rodriguez began using the funds for personal expenses shortly after he made the misrepresentations, we find he knew that his statements about the intended use of the proceeds were false at the time he made them.<sup>204</sup> Thus, we find that he made the misrepresentations with scienter.<sup>205</sup>

Therefore, we conclude that in the sale of debt and equity interests in BRCH, Rodriguez violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and violated FINRA Rules 2020 and 2010.<sup>206</sup> We also find that Rodriguez's actions were willful, as alleged in the Amended Expedited Complaint. In this context, the term "willful" means intentionally committing the act which constitutes the violation.<sup>207</sup> There is no requirement that the actor be aware that he or she is violating a particular rule or regulation.<sup>208</sup> Rodriguez intentionally committed the acts which constitute the violations.

Enforcement argues that Rodriguez's misconduct is attributable to Avenir through the doctrine of respondeat superior.<sup>209</sup> Under this doctrine, "the wrongful acts of an employee

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<sup>202</sup> We draw the interstate commerce inference from the fact that customers were located in New York, Illinois, and Ohio.

<sup>203</sup> See *Hasho*, 784 F. Supp. at 1108; *NASD v. Prendergast*, No. C3A960033, 1999 NASD Discip. LEXIS 19, at \*35 (NAC July 8, 1999) (holding that intended use of proceeds was material), *aff'd*, Exchange Act Release No. 44632, 2001 SEC LEXIS 2767 (Aug. 1, 2001).

<sup>204</sup> We properly considered Rodriguez's post-sale conduct in assessing his intent at the time of the sales. See *NASD v. Clark*, No. C3A930010, 1994 NASD Discip. LEXIS 57, at \*26–27 (NBCC May 18, 1994) (finding that it is appropriate to consider post-sale conduct that occurs shortly after the sale in assessing whether respondent acted with scienter).

<sup>205</sup> *Ahmed*, 2015 FINRA Discip. LEXIS 45, at \*78 (concluding that respondent acted with scienter because he diverted the investor funds and therefore knew that the proceeds of the offering were being used for undisclosed purposes); *Prendergast*, 1999 NASD Discip. LEXIS 19, at \*16–17 (holding that scienter was established by a showing that the registered representative invested funds in a manner inconsistent with the specific uses proscribed in the private placement memorandum); *Clark*, 1994 NASD Discip. LEXIS 57, at \*26–27 (holding that the representative acted with scienter in making misrepresentations to customers when the significant deviations from the use of proceeds described in sales to customers began almost immediately after the sales closed) (citing 5B A. Jacobs, *Litigation and Practice Under Rule 10b-5* § 61.01[c][iii] at 3-78 & nn. 24 & 25 (2d ed. & 1992 Supp.) ("the more pronounced the alteration from the original intent and the shorter the period between the representation and the change, the stronger the inference that the original representation was false"))).

<sup>206</sup> In its Pre-Hearing Brief at 19 n.95, Enforcement announced that for each cause of action it "is holding Avenir liable for the actions of its employees and registered representatives through the theory of respondeat superior." Enforcement took a more limited position, however, in its Opening Post-Hearing Brief at 36, specifically invoking the doctrine as a basis for liability only in connection with the Second and Fourth Causes of Action.

<sup>207</sup> *Mathis v. SEC*, 671 F.3d 210, 216–18 (2d Cir. 2012).

<sup>208</sup> *Id.*; see also *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (holding that the term "willful" means that the person with the duty knows what he is doing, but does not require that one know that he is breaking the law).

<sup>209</sup> Enf's Opening Br. at 36.

undertaken within the scope of employment can be imputed to the employer.”<sup>210</sup> “An employee acts within the scope of employment when performing work assigned by the employer or engaging in a course of conduct subject to the employer’s control.”<sup>211</sup> By contrast, “[a]n employee’s act is not within the scope of employment when it occurs within an independent course of conduct not intended by the employee to serve any purpose of the employer.”<sup>212</sup>

Avenir and Clements argue that Avenir cannot be liable for Rodriguez’s fraud in connection with the BRCH equity sales because Rodriguez concealed the offering from the Firm, and he acted outside the scope of his employment and without authorization.<sup>213</sup> And, regarding the BRCH promissory notes offering, they claim Rodriguez did not misrepresent the intended use of proceeds because he testified that he did not misuse promissory notes funds.<sup>214</sup>

We reject Avenir and Clements’s arguments. Concerning the equity offering, irrespective of whether Rodriguez deliberately concealed the offering from Avenir—and we made no finding that he did so—Rodriguez acted within the scope of his employment when making the misrepresentation. Rodriguez owned BRCH, the holding company that owned an Avenir branch office. BRCH’s capital raising was subject to Avenir’s supervision and control. With Avenir’s knowledge and approval, Rodriguez undertook capital raising through the sale of BRCH promissory notes, which was intended to benefit Avenir, through BRCH’s branch office ownership.<sup>215</sup> We find that, similarly, Rodriguez’s BRCH equity interest sales were designed to benefit Avenir. For these reasons, the sale of BRCH equity interests was an activity within the scope of his employment at Avenir. Finally, although Avenir argues that Rodriguez did not

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<sup>210</sup> *SEC v. Sells*, No. C 11-4941 CW, 2012 U.S. Dist. LEXIS 112450, at \*24 (N.D. Cal. Aug. 10, 2012) (concluding, for purposes of an SEC civil enforcement action for fraud, that an officer’s “knowledge may be imputed to [his firm] by application of the doctrine of respondeat superior under which wrongful acts of an employee undertaken within the scope of employment can be imputed to the employer”). See also *Ahmed*, 2015 FINRA Discip. LEXIS 45, at \*80; *Kirk A. Knapp*, 50 S.E.C. 858, 860 n.7 (1992) (explaining that FINRA properly attributed scienter of firm’s owner to firm and thereby found primary antifraud violation by firm based on owner’s conduct). See also *Kirlin Sec., Inc.*, Exchange Act Release No. 61135, 2009 SEC LEXIS 4168, at \*59 (Dec. 10, 2009) (affirming FINRA disciplinary action against member firm for the manipulation of a security sold to public investors by the firm’s co-chief executive and head trader).

<sup>211</sup> *Vanderwall v. Marriott*, Civil No. 2012-84, 2013 U.S. Dist. LEXIS 117764, at \*35–36 (D.V.I. Aug. 20, 2013) (quoting Restatement (Third) of Agency § 7.07(2)).

<sup>212</sup> *Id.* The NAC observed that the SEC has “long recognized the doctrine of respondeat superior in enforcement or disciplinary actions.” *Dep’t of Mkt. Regulation v. Yankee Fin. Group, Inc.*, No. CMS030182, 2006 NASD Discip. LEXIS 21, at \*59 (NAC Aug. 4, 2006). Yet the Hearing Panel could only find a handful of reported FINRA decisions in the last 20 years that specifically reference the doctrine. Importantly, we are mindful that a generalized application of respondeat superior could transform many cases—such as those involving a failure to supervise a broker who committed fraud—into fraud actions against firms. The Hearing Panel, therefore, was circumspect in approaching the issue of the doctrine’s applicability to this case.

<sup>213</sup> Avenir and Clements Br. at 22.

<sup>214</sup> Avenir and Clements Br. at 22 (citing Tr. 1310, 1478).

<sup>215</sup> See n. 156.

misuse promissory note funds and therefore made no misrepresentations to the promissory note investors regarding the use of their funds, we found otherwise, as discussed above.

Based on the above, we conclude that under the doctrine of respondeat superior, Rodriguez's misconduct is imputed to Avenir. Accordingly, Avenir willfully violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and violated FINRA Rules 2020 and 2010 in the sale of debt and equity interests in BRCH.

### **C. Enforcement Failed to Establish that Avenir Misused Customer Funds in Violation of FINRA Rules 2150 and 2010 (Fourth Cause of Action)**

The Amended Expedited Complaint alleges that BRCH customers KK, CS, AC, the Ss, RD, and ES invested funds in BRCH through debenture and equity sales, and that Rodriguez misused at least a portion of these funds for personal purposes. Based on Rodriguez's alleged misuse, Enforcement charges Avenir with violating FINRA Rules 2150 and 2010.

FINRA Rule 2150(a) provides that neither a FINRA member firm nor a "person associated with a member shall make improper use of a customer's securities or funds." An associated person improperly uses customer funds and violates this provision by failing to apply the customer's money as the customer has directed.<sup>216</sup> Here, the offering proceeds were to be used in connection with BRCH. There is no evidence that the customers authorized Rodriguez to use their funds for his personal expenses. Nevertheless, Rodriguez used a portion of the funds for an unauthorized purpose, namely, for his personal expenses. Therefore, he violated Rule 2150(a). His misconduct also violated Rule 2010 because it "reflects directly on [his] ability both to comply with regulatory requirements fundamental to the securities business and to fulfill his fiduciary responsibilities in handling other people's money."<sup>217</sup> And, thus, it is "patently antithetical" to Rule 2010's exacting ethical standards.<sup>218</sup> Also, "[a] violation of any FINRA rule ... violates NASD Rule 2110 and FINRA Rule 2010."<sup>219</sup>

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<sup>216</sup> *Dep't of Enforcement v. Patel*, No. C02990052, 2001 NASD Discip. LEXIS 42, at \*24–25 (NAC May 23, 2001) (affirming a hearing panel decision barring a representative for misusing customer funds by using them for his own purposes rather than investing them as directed by the customers); *Dep't of Enforcement v. Triggs*, No. C04020006, 2002 NASD Discip. LEXIS 20, at \*8 (NAC Dec. 13, 2002) (use of customer funds for any purpose not directed by the customer violates NASD Rule 2330(a), the predecessor of FINRA Rule 2150(a)).

<sup>217</sup> *James A. Goetz*, 53 S.E.C. 472, 477 (1998).

<sup>218</sup> The SEC has recognized that the misuse of customer funds is "patently antithetical to the high standards of commercial honor and just and equitable principles of trade that the NASD seeks to promote." *Joel Eugene Shaw*, 51 S.E.C. 1224, 1226–27 (1994) (quoting *Wheaton D. Blanchard*, 46 S.E.C. 365, 366 (1976) (internal quotation marks omitted)). Improper use of customer funds also can support an independent charge of violating NASD Conduct Rule 2110 and its successor, FINRA Rule 2010. *Dist. Bus. Conduct Comm. v. Roach*, No. C02960031, 1998 NASD Discip. LEXIS 3, at \*14 (NBCC Jan. 20, 1998). In this case, however, an independent violation was not separately or alternatively charged. Here, the Rule 2010 charge is based on the alleged violation of Rule 2150.

<sup>219</sup> *Mielke*, 2014 FINRA Discip. LEXIS 24, at \*8 n.3.

But it does not necessarily follow that Avenir automatically violated FINRA Rules because Rodriguez misused customer funds. Enforcement argues, as it did in connection with the Second Cause of Action for fraud, that Rodriguez’s misconduct is imputed to Avenir through respondeat superior. Enforcement asserts that this doctrine applies because Rodriguez was associated with the Firm when he engaged in his misconduct.<sup>220</sup> That is not sufficient, however, because Enforcement must show that Rodriguez’s conduct was within the scope of his employment. And, as we quoted above, “[a]n employee’s act is not within the scope of employment when it occurs within an independent course of conduct not intended by the employee to serve any purpose of the employer.”<sup>221</sup> Enforcement neither alleged nor proved that Rodriguez intended his misuse of funds to benefit Avenir, and, clearly, his misuse did not benefit the Firm. Accordingly, we conclude that Enforcement failed to establish that Avenir violated FINRA Rules 2150 and 2101, and these charges are dismissed.

**D. The Panel Dismisses the Aiding and Abetting Charge Against Clements (Third Cause of Action)**

The Amended Expedited Complaint charges Clements with aiding and abetting Ibrahim’s fraud against NL, and with aiding and abetting Rodriguez’s fraud in connection with the BRCH equity and debt offering. We dismiss this charge, as explained below.

**1. The Hearing Panel Declines to Impose Liability on Clements for Aiding and Abetting Ibrahim’s Fraud in the Sale of Avenir Equity Interests to NL (Third Cause of Action)**

To find Clements liable as an aider and abettor, Enforcement must prove the following: (1) a primary securities law violation committed by another party or parties, namely, Ibrahim and Rodriguez; (2) that Clements rendered substantial assistance in furtherance of the violative conduct; and (3) that Clements provided such assistance with scienter (namely, knowingly or recklessly).<sup>222</sup>

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<sup>220</sup> Enf’s Opening Br. at 36.

<sup>221</sup> *Vanderwall*, 2013 U.S. Dist. LEXIS 117764, at \*35–36 (quoting Restatement (Third) of Agency § 7.07(2)); *CFTC v. Byrnes*, 13-CV-1174 (VSB), 58 F. Supp. 3d 319, 327 (S.D.N.Y. Sept. 30, 2014) (same). *See also Burlington Indus., Inc. v. Ellerth*, 524 U.S. 742, 756–57 (1998) (noting that an intentional tort is generally outside the scope of an employee’s employment unless motivated by a desire to serve the employer’s purposes); *In re Ivan F. Boesky Sec. Litig.*, 36 F.3d 255, 265 (2d Cir. 1994) (“While an employer may be liable for even intentional and criminal acts committed by its employee, those acts must in some way further the interests of the employer, and not solely benefit the employee.”).

<sup>222</sup> *Dep’t of Enforcement v. Brokaw*, No. 2007007792902, 2012 FINRA Discip. LEXIS 53, at \*26 n.20 (NAC Sept. 14, 2012) (citing *Dep’t of Mkt. Regulation v. Proudian*, No. CMS040165, 2008 FINRA Discip. LEXIS 21, at \*22 (NAC Aug. 7, 2008)), *aff’d*, Exchange Act Release No. 70883, 2013 SEC LEXIS 3583 (Nov. 15, 2013). *See also In the Matter of Bernard E. Young*, Investment Company Act Release No. 32050, 2016 SEC LEXIS 1123, at \*76–77 (Mar. 24, 2016) (citing *SEC v. Apuzzo*, 689 F.3d 204, 206 (2d Cir. 2012)) (“Aiding and abetting liability can be established by: (1) a primary violation of the securities laws; (2) the aider and abettor’s knowledge or recklessness



Above, we concluded that Clements and Ibrahim engaged in willful fraud in the sale of Avenir equity interests to NL (First Cause of Action). Our findings in support of that conclusion also established the elements of aiding and abetting liability against Clements. Specifically, there was a securities law violation committed by another party, namely, Ibrahim. Also, Clements rendered substantial assistance in furtherance of Ibrahim's violative conduct by (1) directing Ibrahim to solicit investors in the Firm and to state that the invested funds would be used for Avenir's day-to-day operations; (2) drafting NL's Purchase Agreement, which omitted material information about the Firm's financial difficulties, including that without a capital contribution by NL, the Firm would likely fall below its net capital requirements; and (3) never disclosing this information to NL and never making sure that Ibrahim did so. Finally, given his involvement and awareness of Ibrahim's conduct, he provided this assistance knowingly or recklessly.

In making these findings, we reject Clements arguments that Enforcement failed to establish that he aided and abetted the fraud against NL. While Clements admits that he drafted the Avenir equity offering documents, he maintains that he did not aid and abet a violation because Ibrahim offered the Firm's financials to NL and NL declined to review them. This argument fails for the reasons we set forth above in connection with our analysis of liability under the First Cause of Action. Also, Clements claims that he ensured that each Avenir representative was properly trained to solicit Avenir equity investments because this training program ensured that Avenir representatives provided investors with appropriate disclosures.<sup>223</sup> This argument also fails. Training aside, Clements directed the Avenir equity offering and took no steps to ensure that all appropriate disclosures were made. Worse, he drafted the offering documents that omitted material information. Accordingly, Clements provided substantial assistance to Ibrahim's fraudulent sale to NL knowing, or recklessly disregarding that Ibrahim was engaged in improper conduct. As a result, Clements aided and abetted Ibrahim's fraud.

Nevertheless, in light of our finding that Clements directly engaged in willful fraud in connection with the equity sale to NL, we decline to impose aiding and abetting liability on him based on the same nucleus of facts.<sup>224</sup>

## **2. Enforcement Failed to Establish that Clements Aided and Abetted Rodriguez's Fraudulent Sale of Equity and Debt Interests in BRCH (Third Cause of Action)**

The Amended Expedited Complaint's Third Cause of Action also charges Clements with aiding and abetting Rodriguez's fraud in the sale of BRCH equity interests and promissory notes. Enforcement alleged that (1) before Rodriguez solicited investors to purchase equity interests or

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as to the violation; and (3) the aider and abettor's substantial assistance in the achievement of the primary violation.").

<sup>223</sup> Avenir and Clements Br. at 23; CX-58, at 2-4.

<sup>224</sup> *Larry C. Grossman and Gregory J. Adams*, Initial Decision Release No. 727, 2014 SEC LEXIS 4979, at \*102 n.43 (Dec. 23, 2014) (initial decision) (declining to impose aiding and abetting liability in light of a finding of primary liability).

promissory notes in BRCH, Clements advised Rodriguez that he could treat investor funds as his own; (2) Clements knew, from his review of the promissory notes issued to KK, the Ss and ES, that Rodriguez promised to use the proceeds for general operating expenses and growing BRCH; (3) Clements was, or should have been, aware, from his review of the BRCH financial records, that Rodriguez was using proceeds from BRCH equity investments and promissory notes for Rodriguez's personal needs; and (4) the use of BRCH investment proceeds for Rodriguez's personal expenses was a material fact to investors.

Clements maintains that Enforcement failed to show that he aided and abetted a fraud in connection with the BRCH offerings. As to the equity offering, Clements argues that he was unaware of the offering at the time and lent no assistance to it.<sup>225</sup> He also argues, regarding the notes offering, that Rodriguez did not misuse any promissory note funds, so there was no fraud for him to aid and abet.<sup>226</sup>

The evidence did not establish this violation. First, as to the equity offering, Enforcement failed to prove either that Clements knew of the offering in advance or that he advised Rodriguez that Rodriguez could treat investor funds as his own. Additionally, as to both the equity and promissory notes offering, Enforcement did not demonstrate that Clements provided substantial assistance to Rodriguez while knowing (or recklessly disregarding) that Rodriguez planned to misrepresent, or was misrepresenting, to investors in the offerings that he intended to use a portion of their funds to pay his personal expenses.

Enforcement did establish that by June 2014, Clements learned, or should have learned, that Rodriguez misused a portion of investor funds raised in the BRCH offerings. As discussed previously, Clements helped prepare and was responsible for regulatory responses to FINRA about BRCH's self-offerings,<sup>227</sup> including a June 30, 2014 response identifying BRCH debt and equity investors that attached BRCH's bank statements, its general ledger, and financial statements.<sup>228</sup> These documents contained withdrawals to pay for personal expenses, which would have been apparent to Clements had he reviewed the documents before (or around the time that) Rodriguez provided the documents to FINRA.<sup>229</sup> But Clements' after-the-fact knowledge of Rodriguez's wrongdoing (or reckless disregard of it) does not, by itself, constitute

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<sup>225</sup> Avenir and Clements Br. at 24.

<sup>226</sup> Avenir and Clements Br. at 23–24.

<sup>227</sup> CX-87; CX-88; Tr. 1315–16.

<sup>228</sup> CX-87, at 2–3, ¶¶ 19, 23, 25.

<sup>229</sup> In November 2014, Clements audited Rodriguez's Chicago branch and reviewed BRCH financials and other documentation. These documents, according to Clements, showed "the break out of the expenses, how the money was spent." Tr. 514–17. Also, Clements testified that it was not until December 2014 that he received expense sheets from BRCH that detailed in their entirety the nature of the expenses. Tr. 516–20, 526. Similarly, he claimed that it was not until the end of 2014 that he received complete bank statements for BRCH for the time period that Rodriguez was raising capital for BRCH, receiving them also only at the end of 2014. Tr. 531–32. Notwithstanding this evidence, as we explained above, we find that Clements knew, or should have known, of the misuse earlier, namely, in June 2014.

aiding and abetting by Clements. Enforcement failed to show (1) that Clements substantially assisted Rodriguez's wrong doing or (2) that Clements did so with knowledge of, or in reckless disregard of the fact that, Clements planned to misuse, or was misusing, investor funds. Consequently, Enforcement did not prove that Clements aided and abetted Rodriguez's fraudulent sale of BRCH equity interests or promissory notes.

We therefore find that Enforcement failed to establish aiding and abetting liability in connection with Rodriguez's fraud. And, because we also decline to impose liability against Clements for aiding and abetting Ibrahim's fraud on NL, we dismiss the Third Cause of Action.

**E. Avenir Violated FINRA Rules 5122 and 2010 by Not Providing Written Disclosure Regarding Selling Compensation and Use of Proceeds and Not Making Related Filings (Sixth Cause of Action)**

Avenir is charged with violating FINRA Rules 5122 and 2010 in connection with any Avenir and BRCH equity self-offering conducted before December 2014. FINRA Rule 5122 "established standards on disclosure, use of proceeds and a filing requirement for private placements issued by a member firm or a control entity."<sup>230</sup> Its purpose is to provide every investor in a member private offering with "basic information concerning the offering."<sup>231</sup> A member private offering is "a private placement of unregistered securities issued by a member or a control entity."<sup>232</sup> Avenir is a member firm and BRCH is a "control entity."<sup>233</sup>

Under FINRA Rule 5122(b)(1), a member firm must provide each prospective investor with "an offering document" that discloses the "intended use of the offering proceeds" and "the offering expenses and the amount of selling compensation that will be paid to the member and its associated persons." FINRA Rule 5122(b)(2) requires member firms to submit to FINRA's Corporate Financing Department the offering document required by FINRA Rule 5122(b)(1) at or before the first time it is provided to any prospective investor.

The Hearing Panel finds that Avenir violated FINRA Rules 5122 and 2010 in connection with the Avenir equity self-offering and the BRCH equity self-offerings. Both offerings were "member private offerings" which made them subject to the requirements of FINRA Rule 5122. Regarding the Avenir self-offering, the Firm did not provide investors or prospective investors

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<sup>230</sup> FINRA Regulatory Notice 12-40, 2012 FINRA LEXIS 59, at \*3 (Sept. 2012).

<sup>231</sup> FINRA Regulatory Notice 09-27, 2009 FINRA LEXIS 89, at \*7 (May 2009).

<sup>232</sup> FINRA Rule 5122(a)(1).

<sup>233</sup> A "control entity" is "any entity that controls or is under common control with a member, or that is controlled by a member or its associated persons." *See* FINRA Rule 5122(a)(2). Rodriguez controlled BRCH and was an associated person of Avenir.

(other than JC) with written disclosures regarding the use of proceeds or the amount of selling compensation and also failed to make the required filings with FINRA.<sup>234</sup>

Avenir does not dispute that FINRA Rule 5122 applied to its equity self-offerings or that it failed to make the required disclosures and filings. Instead, Avenir argues, that while it failed to comply with what it characterized as “the technical aspects of FINRA Rule 5122,”<sup>235</sup> it nevertheless made all required disclosures orally and the Firm had sought guidance from Corporate Finance before engaging in the self-offerings.<sup>236</sup>

To support its defense, the Firm points to a training program that Clements developed to conduct the Avenir equity offering and the Avenir branch office debt offering, during which he advised Ibrahim and Rodriguez that selling compensation and the use of proceeds for the investment needed to be communicated.<sup>237</sup> Further, Clements testified that he sought confirmation in writing from investors that these disclosures had been made to them.<sup>238</sup> In particular, Clements notes that AC<sup>239</sup> and KK<sup>240</sup> signed letters acknowledging that use of proceeds and selling compensation were disclosed prior to their respective Avenir equity purchases. Also, according to Ibrahim, he orally advised NL as to the use of proceeds and selling compensation associated with NL’s equity investment in Avenir.<sup>241</sup>

Nevertheless, these actions do not constitute compliance with the Rule’s written disclosure and filing requirements. Accordingly, we conclude that Avenir violated FINRA Rules 5122 and 2010, as charged, in connection with an Avenir self-offering conducted before December 2014.

The Firm also failed to make the required written disclosures and filings for the BRCH equity self-offerings. As discussed above, Enforcement failed to demonstrate that Avenir knew of the BRCH equity offerings while they were ongoing. Nevertheless, by June 2014, Avenir should have discovered that BRCH was conducting an equity offering (which continued through October 2014) and made the appropriate disclosures and filings thereafter. We therefore conclude that Avenir violated FINRA Rules 5122 and 2010.

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<sup>234</sup> As noted above at n. 153, in December 2014, the Firm made untimely filings purportedly reflecting that it made oral disclosures about the use of proceeds and selling compensation to four Avenir equity investors.

<sup>235</sup> Avenir and Clements Br. 27.

<sup>236</sup> Avenir and Clements Br. at 11, 27; Tr. 1813–15, 2101–02.

<sup>237</sup> CX-58, at 2–4.

<sup>238</sup> Tr. 2134–35.

<sup>239</sup> RX-6.

<sup>240</sup> RX-8.

<sup>241</sup> Tr. 2050–51.

**F. Avenir and Clements Violated NASD Rule 3010(b) and FINRA Rules 3110(b) and 2010 (Fifth Cause of Action)**

The Amended Expedited Complaint charges Avenir and Clements with failing to supervise Avenir and BRCH's capital raising efforts, in violation of NASD Rule 3010(b) and FINRA Rules 3110(b) and 2010. NASD Rule 3010(b) provides, in pertinent part, that "[e]ach member shall establish, maintain, and enforce written procedures ... to supervise the activities of registered representatives, registered principals, and other associated persons that are reasonably designed to achieve compliance with applicable securities laws and regulations, and with the applicable Rules of NASD." On December 1, 2014, NASD Rule 3010(b) was re-codified as FINRA Rule 3110(b) to apply to FINRA Rules.<sup>242</sup>

Compliance with the supervision rule requires that a supervisor exercise "reasonable" supervision.<sup>243</sup> Whether supervision is reasonable depends on the particular circumstances of each case.<sup>244</sup> But procedures alone are "not enough. Without sufficient implementation, guidelines and strictures do not assure compliance."<sup>245</sup> Additionally, "[t]he duty of supervision includes the responsibility to investigate 'red flags' that suggest that misconduct may be occurring and to act upon the results of such investigation."<sup>246</sup> More specifically, "[o]nce indications of irregularity arise, supervisors must respond appropriately."<sup>247</sup> Ultimately, "responsibility for proper supervision of a member's business rests with the member."<sup>248</sup>

A violation of NASD Rule 3010 is also a violation of NASD Rule 2110.<sup>249</sup> NASD Rule 2110, FINRA's ethical standards Rule, states that "[a] member, in the conduct of his business, shall observe high standards of commercial honor and just and equitable principles of trade." Effective December 15, 2008, NASD Rule 2110 was re-codified, without change, as FINRA

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<sup>242</sup> FINRA Regulatory Notice 14-10, 2014 FINRA LEXIS 17, at \*10 (March 2014).

<sup>243</sup> *Dep't of Enforcement v. Rooney*, No. 2009019042402, 2015 FINRA Discip. LEXIS 19, at \*60 (NAC July 23, 2015). Pursuant to NASD Rule 0115, now FINRA Rule 0140(a), persons associated with a member shall have the same duties and obligations as a member under NASD Rules.

<sup>244</sup> *Id.*

<sup>245</sup> *Id.*

<sup>246</sup> *Rooney*, 2015 FINRA Discip. LEXIS 19, at \*61 (quoting *Ronald Pellegrino*, Exchange Act Release No. 59125, 2008 SEC LEXIS 2843, at \*33).

<sup>247</sup> *Id.*

<sup>248</sup> *Dep't of Enforcement v. Brookstone Securities, Inc.*, No. 2007011413501, 2015 FINRA Discip. LEXIS 3, at \*104 (NAC Apr. 16, 2015).

<sup>249</sup> *Dep't of Enforcement v. ACAP Financial*, No. 2007008239001, 2012 FINRA Discip. LEXIS 55, at \*13 n.9 (NAC Sept. 26, 2012), *aff'd*, Exchange Act Release No. 70046, 2013 SEC LEXIS 2156 (July 26, 2013), *aff'd*, 783 F.3d 763 (10th Cir. 2015).

Rule 2010.<sup>250</sup> “A violation of any FINRA rule . . . violates NASD Rule 2110 and FINRA Rule 2010.”<sup>251</sup>

As addressed above, Avenir and Clements failed in numerous respects to reasonably supervise Avenir and BRCH’s capital raising activities. While we find that Avenir and Clements are also directly responsible for misconduct involving activities they were required to supervise, according to the SEC, there is no “inherent inconsistency in finding a respondent both substantively responsible and a deficient supervisor with respect to the same misconduct. Participating in misconduct is itself a supervisory failure.”<sup>252</sup> Accordingly, we find that Avenir and Clements violated NASD Rule 3010(b) and FINRA Rules 3110(b) and 2010.

#### **IV. Sanctions**

In considering the appropriate sanctions to impose on Respondents, the Extended Hearing Panel looked to FINRA’s Sanction Guidelines (“Guidelines”).<sup>253</sup> The Guidelines contain General Principles Applicable to All Sanction Determinations (“General Principles”), overarching Principal Considerations in Determining Sanctions, as well as guidelines for specific violations. The General Principles explain that “sanctions should be designed to protect the investing public by deterring misconduct and upholding high standards of business conduct.”<sup>254</sup> 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.”<sup>255</sup> Further, sanctions should “reflect the seriousness of the misconduct at issue,”<sup>256</sup> and should be “tailored to address the misconduct involved in each particular case.”<sup>257</sup>

##### **A. Fraud**

The Hearing Panel concluded that (1) Avenir and Clements willfully violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, and violated FINRA Rules 2020 and 2010 in connection with sales of Avenir equity to NL and KK (First Cause of Action); (2) Avenir willfully violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, and violated FINRA Rules 2020 and 2010 in connection with the sale of equity and debenture investments in BRCH to KK, CS, AC, RD, the Ss, and ES (Second Cause

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<sup>250</sup> See FINRA Regulatory Notice 08-57, 2008 FINRA LEXIS 50, at \*32–33 (Oct. 2008).

<sup>251</sup> *Mielke*, 2014 FINRA Discip. LEXIS 24, at \*8 n.2.

<sup>252</sup> *John Montelbano*, Exchange Act Release No. 47227, 2003 SEC LEXIS 153, at \*28–29 (Jan. 22, 2003). *Dep’t of Enforcement v. The Dratel Group, Inc.*, No. 2008012925001, 2014 FINRA Discip. LEXIS 6, at \*84 n.58 (NAC May 2, 2014), *aff’d*, 2016 SEC LEXIS 1035 (Mar. 17, 2016).

<sup>253</sup> FINRA Sanction Guidelines (2015) (“Guidelines”), <http://www.finra.org/industry/sanction-guidelines>.

<sup>254</sup> Guidelines at 2 (General Principles Applicable to All Sanction Determinations, No. 1).

<sup>255</sup> *Id.*

<sup>256</sup> *Id.*

<sup>257</sup> Guidelines at 3 (General Principles Applicable to All Sanction Determinations, No. 3).

of Action), (3) Ibrahim willfully violated Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, and violated FINRA Rules 2020 and 2010 in connection with sales of Avenir equity to NL (First Cause of Action).

The Sanction Guidelines for intentional or reckless misrepresentations or omissions of material fact provide for a fine of \$10,000 to \$146,000. For a firm, the Guidelines direct the Panel to consider a suspension “with respect to any or all activities for up to two years.” But, where “aggravating factors predominate,” the Panel should “strongly consider expelling the firm.” For an individual respondent, they also recommend that the Hearing Panel “[s]trongly consider barring an individual.” Where “mitigating factors predominate,” however, the Panel should “consider suspending an individual in any or all capacities for a period of six months to two years.”<sup>258</sup>

### **1. Avenir and Clements—Avenir Equity Sales**

In applying the principal considerations applicable to Avenir and Clements’ fraudulent conduct regarding the Avenir equity raises from NL and KK (First Cause of Action) and Avenir’s fraud in connection with, the sales of equity and debt investments in BRCH (Second Cause of Action), we find that numerous aggravating factors are present.

Regarding the Avenir equity raises: Avenir and Clements failed to accept responsibility for their misconduct;<sup>259</sup> injured two customers, namely, NL and KK;<sup>260</sup> acted recklessly, not just negligently;<sup>261</sup> and benefitted monetarily (through the equity sales to NL and KK, Avenir raised \$350,000 and was able to avert another financial crisis and remain open for business).<sup>262</sup> Also, they victimized a vulnerable customer, KK, who, at the time of their misconduct, had recently experienced the death of his adult daughter and was concerned about providing for her young child’s future. Clements took full advantage of the trust KK placed in Rodriguez, with whom he had a lengthy friendship.<sup>263</sup> We also considered that the size of the transactions was large, as NL

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<sup>258</sup> Guidelines at 88.

<sup>259</sup> Guidelines at 6 (Principal Considerations in Determining Sanctions, No. 2).

<sup>260</sup> Guidelines at 6 (Principal Considerations in Determining Sanctions, No. 11). NL and KK were injured in the sense that they were defrauded, collectively, out of \$350,000. But there was no evidence offered showing the present value of their equity interests.

<sup>261</sup> Guidelines at 7 (Principal Considerations in Determining Sanctions, No. 13).

<sup>262</sup> Guidelines at 7 (Principal Considerations in Determining Sanctions, No. 17).

<sup>263</sup> Cf. *Dep’t of Enforcement v. Smith*, No. 2011029152401, 2013 FINRA Discip. LEXIS 16, at \*22 (OHO Feb. 19, 2013), *aff’d*, 2014 FINRA Discip. LEXIS 2 (NAC Feb. 21, 2014) (finding aggravating that the respondent “preyed” on a “particularly vulnerable” recently widowed customer and took “advantage of the trust established through a lengthy previous friendship, under the pretext of providing financial advice to help [her] secure her future retirement”); *Dep’t of Enforcement v. Brookstone Sec., Inc.*, No. 2007011413501, 2012 FINRA Discip. LEXIS 52, at \*108 (OHO May 31, 2012), *aff’d*, 2015 FINRA Discip. LEXIS 3 (NAC Apr. 16, 2015).

invested \$250,000 and KK invested \$100,000, and, while the misconduct was not widespread,<sup>264</sup> it was not isolated.

Finally, the Panel considered that at the time of the misconduct, Clements held a senior position of responsibility at the Firm: he was not just its co-owner, but its CEO and CCO. Also, he drafted the offering documents and directed Avenir's capital raising. And, while both Rodriguez and Ibrahim were, themselves, responsible for disclosing all material information to their customers, they looked to Clements for guidance. And, specifically in connection with the sale to KK, Rodriguez brought Clements into his discussions with KK to assist in advising the customer about how to invest the insurance proceeds he had just received—an opportunity that Clements promptly used to defraud KK.

## **2. Avenir—BRCH Equity Interest and Note Sales**

Regarding Avenir's fraud in connection with the BRCH equity and debt investments (Second Cause of Action), we apply the considerations in the Sanction Guidelines and find that numerous aggravating factors exist. First, Avenir did not express remorse for the misconduct; instead, it tried to shift blame to Rodriguez, claiming that he acted outside the scope of his employment, without authority, and tried to conceal the existence of the equity sales. Second, the misconduct injured others in the amount of \$173,800 (the funds raised from investors in the equity and notes offerings), while benefitting Avenir branch offices headed by Rodriguez. Third, Rodriguez's misconduct was more than reckless, it was intentional. Fourth, his misconduct occurred over an extended period of time (April 2014 through January 2015—period of nine months).<sup>265</sup> Fifth, the misconduct was pervasive, involving customers KK, CS, AC, the Ss, and ES;<sup>266</sup> and (6) Rodriguez's wrongdoing was not limited to one type of instrument, but encompassed both equity and debt instruments.<sup>267</sup>

Nevertheless, two factors are mitigative. First, the wrongdoing did not directly benefit Avenir, but, rather, a holding company that owned the Chicago branch. Second, Rodriguez's fraud was not directed by Avenir senior management. And it was not until his fraud had gone on for several months that Clements and Avenir discovered, or should have discovered, his misuse of investor funds. Second, Avenir's liability was based on an imputation of Rodriguez's misrepresentations about the intended use of funds through the doctrine of respondeat superior. But its misconduct was more in the nature of a failure to supervise, rather than fraud.

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<sup>264</sup> Guidelines at 6 (Principal Considerations in Determining Sanctions, No. 8).

<sup>265</sup> Guidelines at 6 (Principal Considerations in Determining Sanctions, No. 9).

<sup>266</sup> Guidelines at 6, 7 (Principal Considerations in Determining Sanctions, Nos. 8, 18).

<sup>267</sup> Guidelines at 7 (Principal Considerations in Determining Sanctions, No. 18).



### 3. Ibrahim—Avenir Equity Sale

As to Ibrahim’s fraudulent sale to NL of an Avenir equity interest, the Panel considered the following facts as aggravating: (1) he failed to express remorse; (2) Ibrahim engaged in conduct that injured a customer, namely, NL; (3) his actions were reckless, not merely negligent; and (4) he benefitted financially from his misconduct, as the sale resulted in a gain to Ibrahim of a \$25,000 commission and a pledged five percent equity stake in the Firm. On the other hand, we also took into account that the misconduct was isolated, as it involved one customer, and was reckless, rather than intentional.

We reject, however, a number of Ibrahim’s mitigation arguments. As discussed above, Ibrahim asks that the Panel take into account that at the time he engaged in the sale to NL, he was young and inexperienced. We rejected this argument as a defense to liability. We also reject it as mitigative of sanctions.<sup>268</sup> Further, we reject as mitigative Ibrahim’s purported reliance on Clements to train and supervise him and to ensure he complied with his disclosure obligations.<sup>269</sup> In fact, Ibrahim’s blame-shifting arguments do more than fail to mitigate his misconduct; they demonstrate that he fails to accept responsibility for his actions. And, finally, regarding Ibrahim’s assertion that NL was a sophisticated investor, that circumstance, even if true, provides only limited mitigation.<sup>270</sup>

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<sup>268</sup> *Dep’t of Enforcement v. Cuzzo*, No. C9B050011, 2007 NASD Discip. LEXIS 12, at \*37 (NAC Feb. 27, 2007) (“[Y]outh and inexperience do not shield registered representatives from liability and we do not consider such factors as evidence of mitigation.”).

<sup>269</sup> *Dep’t of Enforcement v. Epstein*, No. C9B040098, 2007 FINRA Discip. LEXIS 18, at \*97 (NAC Dec. 20, 2007), *aff’d*, Exchange Act Release No. 59328, 2009 SEC LEXIS 217 (Jan. 30, 2009), *petition denied*, 416 F. App’x 142 (3d Cir. 2010) (“Neither a respondent’s claimed ignorance of the securities laws, nor a respondent’s attempt to shift responsibility for a failure to comply with the securities laws inadequate training or incompetent supervision, will serve to lessen the sanction imposed.”); *Dep’t of Enforcement v. Grafenauer*, No. C8A030068, 2005 NASD Discip. LEXIS 29, at \*15 (NAC May 17, 2005) (“[N]either a respondent’s claimed ignorance of the securities laws, nor a respondent’s attempt to shift responsibility for a failure to comply with the securities laws to incompetent supervision, will serve to lessen the sanction imposed.”).

<sup>270</sup> Guidelines, at 7 (Principal Considerations in Determining Sanctions, No. 19); *Dep’t of Mkt. Regulation v. Lane*, No. 20070082049, 2013 FINRA Discip. LEXIS 34, at \*85–86 (NAC Dec. 26, 2013), *aff’d*, Exchange Act Release No. 74629, 2015 SEC LEXIS 558 (Feb. 13, 2015) (finding that uncontradicted claims that customers were sophisticated provided “some mitigation” but this did not give respondent “free reign to fraudulently omit” a material fact); *Dep’t of Enforcement v. Glodek*, No. E9B2002010501, 2009 FINRA Discip. LEXIS 1, at \*24 (NAC Feb. 24, 2009) (same), *aff’d*, Exchange Act Release No. 60937, 2009 SEC LEXIS 3936 (Nov. 4, 2009), *petition denied*, 416 F. App’x 95 (2d Cir. 2011). *But see Dep’t. of Enforcement v. Scholander*, No. 2009019108901, 2014 FINRA Discip. LEXIS 33, at \*81–82 (NAC Dec. 29, 2014), *aff’d*, Exchange Act Release No. 77492, 2016 SEC LEXIS 1209 (Mar. 31, 2016), *appeal docketed*, No. 16-1739 (2d Cir. May 31, 2016) (quoting *Dolphin and Bradbury, Inc.*, Exchange Act Release No. 54143, 2006 SEC LEXIS 1592, at \*36 (July 13, 2006), *petition denied*, 512 F.3d 634 (D.C. Cir. 2008)) (rejecting as mitigative respondents’ assertion that “their customers were sophisticated and thus in no need of disclosure,” explaining that even if true, “[T]he protection of the antifraud provisions of the securities laws extends to sophisticated investors as well as those less sophisticated.”).

#### 4. Conclusion

We find that aggravating factors predominate as to Avenir, and that as to Clements and Ibrahim, mitigating factors do not predominate. Therefore, as directed by the Guidelines, we strongly considered expelling the Firm and barring Clements and Ibrahim. While the fraudulent misconduct did result in serious injury to a number of customers, the wrongdoing was limited to one business activity—self-offerings—and was not committed by a large number of associated persons compared to the total associated persons in the Firm. Also, it was not proven that the fraud committed by Rodriguez concerning his intended use of investor proceeds was directed by Avenir management or was accomplished with its knowledge or approval. Therefore, while strong sanctions are appropriate, we do not find that expelling the Firm is necessary to remediate its misconduct, protect investors, and deter others from engaging in similar misconduct.

Not so as to Clements. His conduct was egregious, especially toward KK, and showed an utter disregard for his regulatory obligations in his quest to raise funds for his struggling firm. We conclude that permitting Clements to remain in the industry would pose too great a risk to the investing public; he should be barred.

Ibrahim's misconduct, on the other hand, was serious and reckless but not egregious or intentional, and involved one customer. We do not believe that barring him is a necessary remedial sanction.

Accordingly, we impose the following sanctions, based on the fraud violations.<sup>271</sup>

(1) Avenir is censured; fined \$146,000; ordered to offer rescission to NL's estate<sup>272</sup> and to KK of their Avenir equity interests at the original purchase price (minus any dividends or interest payments received), plus interest from the date of purchase;<sup>273</sup> ordered to offer rescission to KK, CX, AC, the Ss, and ES of their BRCH equity interests and promissory notes at the original purchase price (minus any dividends or interest payments received), plus interest from

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<sup>271</sup> The Panel finds that the fraud violations are related and that the sanctions imposed should be designed and tailored to deter the same underlying misconduct, namely, a failure by Avenir to appreciate and adhere to its obligation to disclose material information and to refrain from making material misrepresentations in connection with capital raises. Accordingly, the Panel imposes a unitary sanction for the two fraud violations (First and Second Causes of Action). *See Mielke*, 2014 FINRA Discip. LEXIS 24, at \*55 (citing *Dep't of Enforcement v. Fox & Co. Inv., Inc.*, No. C3A030017, 2005 NASD Discip. LEXIS 5, at \*37 (NAC Feb. 24, 2005) (finding that "where multiple, related violations arise as a result of a single underlying problem, a single set of sanctions may be more appropriate to achieve [FINRA's] remedial goals"), *aff'd*, Exchange Act Release No. 52697, 2005 SEC LEXIS 2822, at \*36 (Oct. 28, 2005)).

<sup>272</sup> NL passed away after the hearing in this case.

<sup>273</sup> Guidelines at 4 (General Principles Applicable to All Sanction Determinations, No. 5) ("Where appropriate, Adjudicators may order that a respondent offer rescission to an injured party."). Interest shall run from the purchase date of the equity interests at the rate established for the underpayment of federal income tax in Section 6621 of the Internal Revenue Code, 26 U.S.C § 6621(a)(2). *Cf.* Guidelines at 11.

the date of purchase; and suspended for a period of two years from engaging in any self-offerings, either directly or through any branch offices;

(2) Clements is barred from association with any FINRA member firm in all capacities and ordered to offer rescission to NL's estate and to KK of their Avenir equity interests at the original purchase price (minus any dividends or interest payments received), plus interest from the date of purchase; and

(3) Ibrahim is suspended for a period of two years in all capacities from association with any FINRA member firm; ordered to offer rescission to NL's estate of NL's Avenir equity interest at the original purchase price (minus any dividends or interest payments received), plus interest from the date of purchase;<sup>274</sup> ordered to disgorge his \$25,000 commission,<sup>275</sup> plus prejudgment interest,<sup>276</sup> and ordered to relinquish any claim to a five percent interest in Avenir based on his equity interest sale to NL.

#### **B. Avenir's Failure to Provide Written Disclosure Regarding Selling Compensation and Use of Proceeds and to Make Appropriate Filings with FINRA**

There is not a specific sanction guideline for violations of FINRA Rule 5122. But we found somewhat instructive the guideline for violations of MSRB Rule G-26, which governs the late filing and failing to file offering documents with the MSRB.<sup>277</sup> This guideline recommends that for a late filing, in egregious cases, the Hearing Panel should consider suspending the firm from engaging in all municipal underwriting activities for up to 30 business days, imposing a fine of \$5,000 to \$15,000, and imposing a fine on a per violation basis. And, for failure to file, in egregious cases, the Hearing Panel should consider suspending the firm from engaging in all municipal underwriting activities for up to 30 business days, fining the firm \$5,000 to \$29,000

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<sup>274</sup> NL and KK entered into agreements with Avenir—and not with Clements or Ibrahim—to purchase equity interests in Avenir. But the investors' lack of privity of contract with Clements and Ibrahim does not prevent these Respondents from being ordered to offer rescission to NL and KK. *See Pinter v. Dahl*, 486 U.S. 622, 647 (1987) (“When rescission is predicated on fraud, rather than based on contract theory, privity is not essential”) (quoting *Gordon v. Burr*, 506 F.2d 1080, 1085 (2d Cir. 1974) (“[A]s between the innocent purchaser and the wrongdoer who, though not a privy to the fraudulent contract, nonetheless induced the victim to make the purchase, equity requires the wrongdoer to restore the victim to the status quo.”)).

<sup>275</sup> Guidelines at 4–5 (General Principles Applicable to All Sanction Determinations, No. 6). Ibrahim shall not be obligated to disgorge his commission if his rescission offer to the estate of NL is accepted and completed.

<sup>276</sup> *Davidofsky*, 2013 FINRA Discip. LEXIS 7, at \*43 (“When assessing disgorgement, FINRA adjudicators should require payment of prejudgment interest on the amount to be disgorged, or explain in their decision why the payment of prejudgment interest is not appropriate to effectuate the purposes of equitable disgorgement. The rate of prejudgment interest is the rate established for the underpayment of income taxes in the Internal Revenue Code, which is the same rate we use when ordering interest on a restitution award.”). Interest shall be calculated at the rate established for the underpayment of federal income tax. *See* n. 273.

<sup>277</sup> Guidelines at 71.

and consider imposing a fine on a per violation basis. The relevant consideration under this guideline includes the average number of days late the filings were made.<sup>278</sup>

Looking to this Guideline and the relevant general and principal considerations in the Guidelines, there are various factors we took into account in determining the appropriately remedial sanctions. Some of these factors are aggravating: (1) numerous investors did not receive the required written disclosure—three investors (AC, KK, and NL) in connection with the Avenir equity offerings and four investors (KK, CS, AC, RD) in connection with the BRCH equity self-offering; (2) the Firm never made any filings regarding the BRCH equity offerings; (3) regarding the Avenir equity offerings, it made no filings until December 2014, seven months after the Avenir equity offerings began; and (4) the failure or late filing violations related to two offerings, the Avenir equity offering and the BRCH equity offering.

By way of mitigation, we considered that (1) the Firm conceded it did not comply with Rule 5122 and expressed remorse (although it did not do so prior to detection by FINRA); (2) it appears—although it is not conclusive—that the Firm made oral disclosures about the use of proceeds and selling compensation to Avenir equity investors JC, AC, NL, and KK; (3) the wrongdoing was not intentional; and (4) that until June 2014, the Firm was likely neither aware, nor reckless in not being aware, that BRCH was conducting equity raises.

On balance, we find that a sufficiently remedial sanction for the violation of FINRA Rules 5122 and 2010 is a censure and a \$10,000 fine.

### **C. Avenir and Clements Failure to Supervise**

The Sanction Guidelines for failure to supervise<sup>279</sup> recommend a fine in the range of \$5,000 to \$73,000 and that the Panel consider suspending the responsible individual in all supervisory capacities for up to 30 business days and limiting the activities of the appropriate branch office or department for up to 30 business days.

In egregious cases, the Guidelines direct the Panel to consider limiting the activities of the branch office or department for a longer period or suspending the firm with respect to any or all activities or functions for up to 30 business days. The Panel is also directed to consider suspending the responsible individual in any or all capacities for up to two years or barring the responsible individual.

Finally, when a firm has engaged in systemic supervision failures, the Guidelines ask us to consider a longer suspension of the firm with respect to any or all activities or functions (of up to two years) or expulsion of the firm.

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<sup>278</sup> The Guideline also contains several other considerations which we did not find relevant here.

<sup>279</sup> Guidelines at 103.

The guideline for failure to supervise contains these principal considerations: (1) whether the respondent ignored “red flag” warnings that should have resulted in additional supervisory scrutiny; (2) whether the individuals responsible for the underlying misconduct attempted to conceal the misconduct from the respondent; (3) the nature, extent, size and character of the underlying misconduct; and (4) third, the quality and degree of the supervisor’s implementation of the firm’s supervisory procedures and controls.

The supervision failures in this case were egregious and systemic. Avenir, acting through Clements, failed to adequately supervise Avenir’s capital raising. Clements was responsible for supervising the Firm’s capital raises and was also Rodriguez’s direct supervisor. He not only failed in numerous respects to adequately supervise the capital raises and Rodriguez, but was, himself, an active participant in the underlying wrongdoing committed against NL and KK. The supervisory failures involved both equity and promissory notes offerings that raised nearly \$562,000 over a two-year period (from approximately December 2013 through January 2015). The Firm, through Clements, also ignored red flags that Rodriguez was engaged in an equity raise for BRCH and was misusing investor funds. His failure to take action in the face of these red flags resulted in the continuation of Rodriguez’s misuse of customer funds and the failure to provide Rule 5122 written disclosures to investors in the equity raises.

“Assuring proper supervision is a critical component of broker-dealer operations.”<sup>280</sup> And given that the supervision violations in this case are egregious and systemic, and in the absence of mitigation, we find that the Firm and Clements should be fined, jointly and severally, \$73,000<sup>281</sup> and that Clements should be barred in all principal capacities. Further, the Firm should be censured and suspended for two years from engaging in any self-offerings, either directly or through any branch offices.<sup>282</sup>

In light of the sanctions imposed upon Clements for his fraud violations, however, we impose no additional sanctions on him for his failure to supervise.

## **V. Order**

The Extended Hearing Panel imposes the following sanctions:

- A. For willfully violating Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, and for violating FINRA Rules 2020 and 2010:

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<sup>280</sup> *Rooney*, 2015 FINRA Discip. LEXIS 19, at \*59 (quoting *Ronald Pellegrino*, Exchange Act Release No. 59125, 2008 SEC LEXIS 2843, at \*33 (Dec. 19, 2008)).

<sup>281</sup> See Guidelines at 9 (“Fines may be imposed individually as to each respondent in a case, or jointly and severally as to two or more respondents.”).

<sup>282</sup> The two-year suspension from engaging in any self-offerings shall run concurrently with the identical suspension imposed in connection with the fraud violations.

(1) Avenir is censured; fined \$146,000; ordered to offer rescission to NL's estate and to KK of their Avenir equity interests at the original purchase price (minus any dividends or interest payments received), plus interest from the date of purchase; ordered to offer rescission to KK, CX, AC, the Ss, and ES<sup>283</sup> of their BRCH equity interests and promissory notes at the original purchase price (minus any dividends or interest payments received), plus interest from the date of purchase; and suspended for two years from engaging in any self-offerings, either directly or through any branch offices;

(2) Clements is barred from association with any FINRA member firm in all capacities and ordered to offer rescission to NL's estate and to KK of their Avenir equity interests at the original purchase price (minus any dividends or interest payments received), plus interest from the date of purchase,<sup>284</sup> and

(3) Ibrahim is suspended for two years in all capacities from association with any FINRA member firm; ordered to offer rescission to NL's estate of NL's Avenir equity interest at the original purchase price (minus any dividends or interest payments received), plus interest from the date of purchase; ordered to disgorge his \$25,000 commission based on his equity interest sale to NL,<sup>285</sup> plus prejudgment interest, and ordered to relinquish any claim to a five percent interest in Avenir based on that sale to NL.<sup>286</sup>

B. For violating FINRA Rules 5122 and 2010, Avenir is censured and fined \$10,000.

C. For violating NASD Rule 3010(b) and FINRA Rules 3110(b) and 2010, Avenir is censured, fined \$73,000, and suspended for two years from engaging in any self-offerings, either directly or through any branch offices.<sup>287</sup>

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<sup>283</sup> These customers are identified in the Addendum to this Decision, which is served only on the parties.

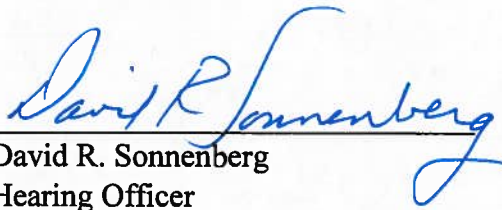
<sup>284</sup> We considered imposing a fine but in the exercise of our discretion, decline to do so, as we find that the other sanctions imposed are sufficient and appropriately tailored to respond to the misconduct at issue. *See* Guidelines at 3 (General Principles Applicable to All Sanction Determinations, No. 3) (“Adjudicators should tailor sanctions to respond to the misconduct at issue. Sanctions in disciplinary proceedings are intended to be remedial and to prevent the recurrence of misconduct. Adjudicators therefore should impose sanctions tailored to address the misconduct involved in each particular case.”) & 10 (“Adjudicators may exercise their discretion in applying FINRA’s policy on the imposition and collection of monetary sanctions as necessary to achieve FINRA’s regulatory purposes.”). *But see* Guidelines at 10 (“Adjudicators generally should impose a fine and require payment of restitution and disgorgement even if an individual is barred in all sales practice cases if: the case involves widespread, significant and identifiable customer harm; or the respondent has retained substantial ill-gotten gains.”).

<sup>285</sup> Ibrahim shall not be obligated to disgorge his commission if his rescission offer to the estate of NL is accepted and completed.

<sup>286</sup> We considered imposing a fine but in the exercise of our discretion decline to do so, as we find that the other sanctions imposed are sufficient and appropriately tailored to address the misconduct at issue.

<sup>287</sup> The two-year suspension from engaging in any self-offerings shall run concurrently with the identical suspension imposed in connection with the fraud violations.

- D. The aiding and abetting charges (Third Cause of Action) and the misuse of customer funds charges (Fourth Cause of Action) are dismissed.
- E. Respondents are ordered, jointly and severally, to pay hearing costs in the amount of \$19,130.96, consisting of an administrative fee of \$750.00 and the cost of the transcript.
- F. If this decision becomes FINRA's final disciplinary action, the suspensions shall become effective with the opening of business on Monday, November 21, 2016, and end at the close of business on Tuesday, November 20, 2018. The fines and assessed costs shall be due on a date set by FINRA, but not sooner than 30 days after this decision becomes FINRA's final disciplinary action in this proceeding.<sup>288</sup>

  
David R. Sonnenberg  
Hearing Officer  
For the Extended Hearing Panel

Copies to: Avenir Financial Group (via overnight courier and first class mail)  
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Robert C. Harris, Esq. (via email and first-class mail)  
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Michael J. Watling, Esq. (via email and first class mail)  
Carolyn O'Leary, Esq. (via email)  
Jeffrey D. Pariser, Esq. (via email)

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<sup>288</sup> The Extended Hearing Panel considered all of the parties' arguments. Arguments not specifically discussed herein are rejected or sustained to the extent that they are inconsistent or in accord with this Decision.