

FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

PAUL E. TABOADA
(CRD No. 2033981),

Respondent.

Disciplinary Proceeding
No. 2012034719701

Hearing Officer—MAD

**EXTENDED HEARING PANEL
DECISION**

March 18, 2016

Respondent Paul E. Taboada violated (1) FINRA Rule 2010 by misappropriating investor funds and securities; (2) FINRA Rules 2150 and 2010 by misusing customer funds and securities; (3) FINRA Rule 2010 by providing false and misleading information, and failing to disclose information, to investors regarding expenses such as commissions and sales concessions; and (4) FINRA Rules 8210 and 2010 by providing false and misleading documents and testimony to FINRA. For the above misconduct, the Extended Hearing Panel barred Taboada from associating with any FINRA member firm in any capacity. Taboada is also ordered to pay the costs of this proceeding.

Appearances

For the Complainant: Gary Carleton, Esq. and Michael M. Smith, Esq.,
Department of Enforcement, Financial Industry Regulatory Authority.

For the Respondent: David A. Schrader, Esq., Moritt Hock & Hamroff LLP, New York, NY.

DECISION

I. Introduction

Respondent Paul E. Taboada created CMS FB LLC (“CMS”), a special purpose entity, to pool investor funds and purchase Facebook, Inc. shares in advance of its initial public offering (“IPO”). Taboada was CMS’s manager. He controlled CMS’s assets and liabilities, and was responsible for the distribution of CMS’s Facebook shares to its investors.

FINRA received information regarding possible irregularities relating to the operation of CMS and the distribution of its Facebook shares, which prompted FINRA to conduct an investigation. Following FINRA's investigation, the Department of Enforcement filed a four-count complaint against Taboada alleging serious violations of FINRA's rules.¹

The first cause of action alleges that Taboada violated FINRA Rule 2010 by misappropriating investor funds and securities. Specifically, the Complaint alleges that Taboada used funds belonging to certain investors to pay expenses owed by other investors and by distributing too many Facebook shares to some investors and too few shares to other investors. The second cause of action alleges that Taboada's misappropriation of investor funds and securities also violated FINRA Rules 2150 and 2010 because some of the investors were customers of Taboada's broker-dealer, Charles Morgan Securities, Inc. ("Charles Morgan"), and another broker-dealer that Taboada associated with after his firm ceased operations. The third cause of action alleges that Taboada violated FINRA Rule 2010 by providing false and misleading information, and failing to disclose information, to investors regarding expenses such as commissions and sales concessions. Lastly, the fourth cause of action alleges that Taboada violated FINRA Rules 8210 and 2010 by providing false documents and testimony to FINRA during its investigation.

Taboada filed an answer denying the alleged violations and requested a hearing.² At the hearing, Taboada explained that any irregularities regarding the use of investor funds or the distribution of Facebook shares were simply honest mistakes resulting from accounting errors. Taboada also asserted two legal defenses. First, he argued that FINRA lacked jurisdiction over his conduct because it did not involve a sufficient nexus to the securities business or the business of a broker-dealer. Second, Taboada argued that he did not misappropriate any funds and securities because the funds and securities belonged to CMS, not to its investors.

The Extended Hearing Panel did not find Taboada credible.³ It rejected Taboada's defenses and found him liable for each of the violations in the Complaint. The Panel determined that the appropriate remedial sanction for Taboada is a bar from associating with any member firm in any capacity.

¹ Enforcement filed the Complaint on May 6, 2014.

² The hearing was held in New York, New York, on September 29-October 8, 2015.

³ In this Decision, the Panel provides specific examples that demonstrate Taboada's lack of credibility.

II. Findings of Fact

A. Respondent

Taboada entered the securities industry in February 1990.⁴ From October 2005 to September 2012, Taboada was registered with Charles Morgan, a broker-dealer he created and owned.⁵

Charles Morgan became a FINRA-registered broker dealer in May 2005.⁶ It filed a Form BDW to withdraw from FINRA membership in September 2012, which was granted in November 2012.⁷ During the last two to three years that Charles Morgan was in business, it experienced financial difficulties.⁸ It lost money each month during that period and it struggled to maintain its net capital during its last year in operation.⁹

At Charles Morgan, Taboada was registered as a General Securities Representative, General Securities Principal, Operations Professional, and Investment Banking Representative.¹⁰ Taboada was also Charles Morgan's Chairman and Chief Executive Officer.¹¹ In October 2012, around the time Charles Morgan ceased operating, Taboada registered with Blackwall Capital Markets, Inc. ("Blackwall"), a FINRA-registered broker-dealer.¹² He currently holds the same registrations at Blackwall.¹³

⁴ Between 1990 and 2005, Taboada was registered with nine different FINRA member firms. CX-1, at 6-10.

⁵ CX-1, at 5. Taboada was the owner of Charles Morgan from May 2006 through February 9, 2012. Stip. ¶ 10. On February 9, 2012, CMS Global Securities, Inc. ("CMS Global Securities") became the majority owner of Charles Morgan. Stip. ¶ 11. Taboada was the majority owner of CMS Global Securities during the time that CMS Global Securities was the majority owner of Charles Morgan. Stip. ¶ 12.

⁶ Tr. 163.

⁷ Tr. 163.

⁸ Tr. 429.

⁹ Tr. 429-30.

¹⁰ Stip. ¶ 4.

¹¹ Stip. ¶ 9.

¹² Stip. ¶ 13.

¹³ Answer ("Ans.") ¶ 7. FINRA has jurisdiction over this proceeding because Taboada is registered with a FINRA member firm.

B. CMS

CMS is a Delaware “series limited liability company”¹⁴ that Taboada created in March 2011.¹⁵ He created CMS to pool investor funds and invest in pre-IPO Facebook securities.¹⁶ Taboada believed that CMS would provide a financial benefit to Charles Morgan.¹⁷ “The idea was to get a position in Facebook prior to the IPO and collect money under management that would further benefit the broker-dealer for which I owned.”¹⁸

1. CMS’s Manager

CMS is managed by CMS FB Management Associates, LLC (“Management”),¹⁹ and Taboada is its sole manager. He has complete control over CMS, making all decisions regarding CMS’s business and investments.²⁰ Initially, Taboada managed CMS from Charles Morgan’s office. After Charles Morgan ceased operating and Taboada joined Blackwall, he managed CMS from Blackwall’s office.

2. CMS’s Organization and Operation

CMS’s Offering Memorandum,²¹ which Taboada approved, informed investors how CMS was organized and how it would operate.²² The Offering Memorandum explained that investors would be issued ownership interests in a particular series within CMS.²³ According to the Offering Memorandum, each series would be “treated for most purposes as if it were a separate limited liability company.”²⁴ The Offering Memorandum further stated that “[t]he terms and conditions of each series will be identical, but they

¹⁴ Under Delaware law, a limited liability company may be composed of an individual series of membership interests. Each series can be treated as a separate entity, meaning the debts, liabilities, obligations, and expenses of one series cannot be enforced against either another series or the company as a whole. *See Section 18-215 of the Delaware Limited Liability Act.*

¹⁵ Ans. ¶ 8; Stip. ¶ 5; CX-6, at 1, 9.

¹⁶ Stip. ¶ 5.

¹⁷ Tr. 169.

¹⁸ Tr. 169.

¹⁹ CX-4; CX-5; Ans. ¶ 8.

²⁰ Tr. 169-71, 189-90; Ans. ¶ 8.

²¹ CX-6. The Offering Memorandum included a letter to investors, a description of the offering, a summary of CMS’s operating agreement, a copy of the operating agreement, and a subscription agreement. Tr. 196, 198. Taboada updated the Offering Memorandum to reflect that the placement fee increased to 10 percent. Tr. 1166-68; RX-18. The revised Offering Memorandum, dated November 14, 2011, contained no other substantive changes. *Compare CX-6 with RX-18.*

²² Tr. 197-98

²³ CX-6, at 1, 8.

²⁴ CX-6, at 1, 9.

will hold separate assets (blocks of Facebook Securities) and their profits and losses will be calculated separately for purposes of allocation and payment of distributions.”²⁵ Each series would have its own investors; books and records; assets, including its own block of Facebook securities; and expenses, including the cost of acquiring its Facebook securities.²⁶ The Offering Memorandum further explained that CMS would maintain a separate capital account for each investor in each series.²⁷ Each capital account would equal the investor’s capital contribution less his or her share of the expenses attributed to the series.²⁸ To the extent any investor had a surplus in his or her capital account when CMS wound down its business, Taboada was required to return those funds to the investor.²⁹

3. CMS’s Placement Agent

One of Taboada’s first decisions on behalf of CMS was to hire his broker-dealer, Charles Morgan, to serve as CMS’s placement agent.³⁰ Charles Morgan brokers solicited investors for CMS, including Charles Morgan customers.³¹ Charles Morgan earned at least \$407,551 in placement fees.³²

4. CMS’s Sources for Its Purchases of Facebook Shares

When CMS purchased Facebook securities, it made either (1) direct purchases from a shareholder or (2) indirect purchases from an entity affiliated with Felix Investments, LLC (“Felix”), a FINRA-registered broker-dealer that manages or otherwise controls several special purpose entities that held, or had the right to acquire, Facebook securities.³³ CMS, through Taboada, purchased ownership interests in four of Felix’s special purpose entities.³⁴

For each of CMS’s indirect purchases of Facebook securities from the Felix entities, Taboada arranged for Charles Morgan to receive sales concessions.³⁵ Beginning in March 2011, Taboada entered into three dealer agreements with Felix.³⁶ Pursuant to

²⁵ CX-6, at 6.

²⁶ CX-6, at 1, 6, 9.

²⁷ CX-6, at 9.

²⁸ CX-6, at 9, 20, 34.

²⁹ CX-6, at 33.

³⁰ Stip. ¶ 24.

³¹ CX-216.

³² Stip. ¶ 27, Table A, Column D; Ans. ¶ 10.

³³ CX-6, at 5; Stip. ¶¶ 108-111.

³⁴ Ans. ¶ 12.

³⁵ Ans. ¶¶ 12, 13.

³⁶ Stip. ¶¶ 47-52; CX-88; CX-89; CX-90.

the dealer agreements, Felix agreed to pay Charles Morgan a sales concession on each of CMS's indirect purchases equal to one-half of the commission CMS paid to Felix.³⁷ Charles Morgan received a total of \$92,721 in sales concessions from Felix.³⁸

C. CMS's Seven Series of Investors

Between March 2011 and February 2012, Taboada formed seven series of investors as CMS accepted capital contributions, which he used to purchase interests in Facebook securities for each series.³⁹

1. First Series

The First Series had eight investors (some of whom made multiple investments).⁴⁰ Six of the First Series investors were customers of Charles Morgan or Blackwall.⁴¹ The First Series investors contributed \$914,942 in capital to CMS in March and April 2011.⁴² CMS, through Taboada, paid \$863,500 to purchase interests in Facie Libre Associates II,

³⁷ Stip. ¶¶ 47-52; CX-88; CX-89; CX-90.

³⁸ Stip. ¶¶ 53-63.

³⁹ Compl. ¶ 15; Ans. ¶ 15. Taboada has changed his position regarding the number of CMS series on several occasions. During Taboada's April 2014 investigative testimony, he provided sworn testimony to Enforcement that CMS had three series of investors. Tr. 243. Taboada even identified which investors were in each series. Tr. 396-97, 1222-24. When Taboada filed his Answer in June 2014, he admitted, without qualification, that CMS had seven series of investors. Ans. ¶ 15. Taboada was represented by counsel when he filed his Answer, and he testified that he read his Answer before filing it. Ans. at 1; Tr. 213-14. Taboada never amended his Answer. When he filed his pre-hearing brief in August 2015, he admitted again that CMS had seven series of investors. In his brief, Taboada states: "Beginning in April 2011, CMS FB raised capital to invest in FB by selling interests to investors on a rolling basis in seven separate series." Taboada's Pre-Hr'g Br. at 3. However, at the hearing, Taboada changed his position and claimed that CMS had only one series. Tr. 207. Taboada testified that he "contemplated" having multiple series, but decided that CMS would have only one series because multiple series would not be practical. Tr. 204, 244. At the hearing, Taboada could not explain when or how CMS went from seven series to three series, back to seven series, and then to one series. Tr. 208, 243-50, 373-82, 387-89, 396-97. He testified that the number of series was constantly evolving, and that he did not decide that CMS would have only one series until some point between March 25 and May 1, 2014, more than two years after the last interest in CMS was issued. Tr. 206, 209-10, 249-50. Taboada's testimony does not explain why he later admitted that CMS had seven series in his Answer and in his Pre-Hearing Brief, both of which were filed after May 1, 2014. Plus, during the hearing, Taboada's own expert witness disagreed with him and testified that CMS had seven series of investors. Tr. 1608. The Hearing Panel does not find Taboada's testimony that CMS had one series to be credible. As a matter of law, Taboada's admission in his Answer is conclusive as to the number of series. *Morales v. Dep't of Army*, 947 F.2d 766, 769 (5th Cir. 1991) ("Factual assertions in pleadings are judicial admissions conclusively binding on the party that made them."); *Gibbs v. CIGNA Corp.*, 440 F.3d 571, 578 (2d Cir. 2006) ("Facts admitted in an answer, as in any pleading, are judicial admissions that bind the defendant throughout this litigation."). In addition, the documentary evidence and Taboada's expert confirm that CMS had seven series of investors.

⁴⁰ CX-128, at 50.

⁴¹ Compare Stip., Table A, with CX-211; CX-216, at 3, 5, 7; Tr. 936, 940.

⁴² Stip. ¶ 17.

LLC (“Libre II”), an entity affiliated with Felix, for the First Series.⁴³ CMS also paid Felix a 5 percent commission on the transaction, and Felix paid half of that amount to Charles Morgan as a sales concession.⁴⁴

2. Second Series

The Second Series had 15 investors (one of whom made two investments).⁴⁵ Fourteen of the Second Series investors were customers of Charles Morgan or Blackwall.⁴⁶ The Second Series investors contributed \$1,465,870.50 in capital to CMS between April and June 2011.⁴⁷ CMS paid \$1,378,226 to purchase interests in Facie Libre Associates I, LLC (“Libre I”) and Libre II for the Second Series.⁴⁸ CMS paid Felix a 5 percent commission on the transaction, and Felix paid half of that amount to Charles Morgan as a sales concession.⁴⁹

3. Third Series

The Third Series had six investors.⁵⁰ Four of the Third Series investors were customers of Charles Morgan or Blackwall.⁵¹ The Third Series investors contributed \$254,150 in capital to CMS in June and July 2011.⁵² CMS paid \$247,296.25 to purchase an interest in Libre II for the Third Series.⁵³ CMS also paid Felix a 5 percent commission on the transaction, and Felix paid half of that amount to Charles Morgan as a sales concession.⁵⁴

4. Fourth Series

The Fourth Series had ten investors.⁵⁵ Five of the Fourth Series investors were customers of Charles Morgan or Blackwall.⁵⁶ The Fourth Series investors contributed

⁴³ Stip. ¶ 29-30.

⁴⁴ Stip. ¶ 53-54.

⁴⁵ CX-128, at 50.

⁴⁶ Compare Stip., Table A, with CX-209; CX-216, at 2, 5, 7; Tr. 936, 940.

⁴⁷ Stip. ¶ 18.

⁴⁸ Stip. ¶ 31-33.

⁴⁹ Stip. ¶ 55-56.

⁵⁰ CX-128, at 51.

⁵¹ Compare Stip., Table A, with CX-212; CX-216, at 5-6, 8.

⁵² Stip. ¶ 19.

⁵³ Stip. ¶ 34.

⁵⁴ Stip. ¶ 57-58.

⁵⁵ CX-128, at 51.

⁵⁶ Compare Stip., Table A, with CX-208; CX-210; CX-214; CX-216, at 5, 7.

\$627,000 in capital to CMS between November 2011 and January 2012.⁵⁷ CMS paid \$572,428.87 to purchase an interest in Felix Multi-Opportunity II, LLC (“Opportunity”), another entity affiliated with Felix.⁵⁸

Unlike the earlier transactions, CMS paid Felix a 10 percent commission on this transaction, or \$57,242.89.⁵⁹ Under Opportunity’s offering memorandum, Felix was entitled to a 5 percent commission on the Fourth Series’ investment in Opportunity.⁶⁰ However, Taboada asked Felix to double its commission on the transaction,⁶¹ and Felix agreed.⁶² Given that Charles Morgan received half of Felix’s commission charges, the sales concession Charles Morgan received on the Opportunity transaction also doubled, increasing from \$14,310 to \$28,621.⁶³ Because of Felix’s increased commission, CMS received fewer Facebook shares from the Opportunity investment to distribute to its investors, and, as a result, the CMS investors received fewer shares.⁶⁴

Taboada did not disclose to the Fourth Series investors that Charles Morgan received a sales concession on their investment in Opportunity. The CMS Offering Memorandum did not disclose any of the sales concessions that Charles Morgan received from Felix.⁶⁵ Nor was there a supplement to the Offering Memorandum disclosing Charles Morgan’s sales concession on the transaction in connection with the Opportunity investment.⁶⁶

5. Fifth Series

The Fifth Series had 63 investors, one of whom invested twice.⁶⁷ Seven of the Fifth Series investors were customers of Charles Morgan or Blackwall.⁶⁸ The Fifth Series

⁵⁷ Stip. ¶ 20.

⁵⁸ Stip. ¶ 35.

⁵⁹ Stip. ¶ 59.

⁶⁰ CX-81, at 8 (“a 5% placement agency fee payable to Felix Investments, LLC”); Tr. 314-15.

⁶¹ CX-115; CX-116; CX-117.

⁶² Stip. ¶ 59; Tr. 328-30.

⁶³ Stip. ¶ 60; Tr. 336.

⁶⁴ Tr. 317.

⁶⁵ Tr. 957-58, 1221-22.

⁶⁶ Tr. 955. While there was a supplement to the Offering Memorandum, the supplement only disclosed the sales concessions Charles Morgan received on CMS’s investments in Libre II, not Opportunity. Tr. 958-59; RX-34. Moreover, the supplement pertained to the Offering Memorandum dated March 14, 2011 (the initial version of the Offering Memorandum), and the Fourth Series investors received the revised Offering Memorandum dated November 14, 2011. RX-18. Fourth Series investors were charged the higher 10 percent placement fee, which was imposed on investors who subscribed after November 14, 2011. See Stip. at Table A, column D, rows 33-49.

⁶⁷ CX-128, at 52.

⁶⁸ Compare Stip., Table A, with CX-213; CX-215; CX-216, at 5, 7; Tr. 936, 940.

investors contributed \$2,259,795.50 in capital to CMS in January and February 2012.⁶⁹ CMS paid \$2,010,000 to purchase 60,000 Facebook shares directly from a shareholder at \$33.50 per share.⁷⁰ Because this was a direct purchase, CMS did not pay a commission on this transaction and Charles Morgan did not receive a sales concession.⁷¹

6. Sixth Series

The Sixth Series had four investors.⁷² One of the Sixth Series investors was a customer of Charles Morgan.⁷³ The Sixth Series investors contributed \$454,980 in capital to CMS in February 2012.⁷⁴ CMS paid \$406,250 to purchase 10,350 Facebook shares directly from a shareholder at \$39.25 per share.⁷⁵ Again, this was a direct purchase so CMS did not pay a commission on the transaction and Charles Morgan did not receive a sales concession.⁷⁶

7. Seventh Series

The Seventh Series had one investor. That investor contributed \$75,000 in capital to CMS in February 2012.⁷⁷ CMS paid \$75,000 to purchase an interest in NYPA II Fund, LLC (“NYPA”) for the Seventh Series investors.⁷⁸ CMS also paid Felix a 5 percent commission on the transaction, and Felix paid half of that amount to Charles Morgan as a sales concession.⁷⁹ Taboada did not disclose Charles Morgan’s sales concession on this transaction to the CMS investors.⁸⁰

D. **Taboada’s Improper Use of Investor Funds**

Taboada did not adhere to the Offering Memorandum. He did not create and maintain a separate capital account for each investor in each series. Instead, Taboada used excess capital from the First and Second Series investors for expenses associated with the Third through Seventh Series.

⁶⁹ Stip. ¶ 21.

⁷⁰ Stip. ¶ 36.

⁷¹ Stip. ¶ 63.

⁷² CX-128, at 53.

⁷³ Compare Stip., Table A, with CX-216, at 9.

⁷⁴ Stip. ¶ 22.

⁷⁵ Stip. ¶ 37.

⁷⁶ Stip. ¶ 63.

⁷⁷ Stip. ¶ 23.

⁷⁸ Stip. ¶ 38.

⁷⁹ Stip. ¶¶ 61-62.

⁸⁰ Tr. 956.

Below we discuss the expense allocation requirements set forth in the Offering Memorandum, the allocation of the CMS expenses in accordance with the Offering Memorandum, and Taboada’s deviation from the Offering Memorandum requirements by using the First and Second Series’ capital surpluses to pay for the capital deficits among Third through Seventh Series investors.

1. The CMS Offering Memorandum’s Requirements for Allocation of Expenses

The Offering Memorandum required that any expense attributable to a particular series, *i.e.*, a “series-specific-expense,” had to be allocated to that series, and among its investors, pro rata based on their ownership interest in the series.⁸¹ Expenses that were not specifically attributed to a particular series would be allocated pro rata among all investors.⁸² While the Offering Memorandum allowed Taboada some discretion to allocate expenses not specifically attributed to a particular series, *i.e.*, “general expenses,” Taboada testified (and had previously represented to CMS investors) that he did not exercise that discretion, but rather allocated CMS’s general expenses pro rata among all of the CMS investors.⁸³

2. The Allocation of CMS Expenses Pursuant to the Offering Memorandum

Enforcement’s expert witness, Bruce Dubinsky, testified about the allocation of CMS’s expenses. Dubinsky is a Certified Public Accountant, a Certified Fraud Examiner, a Certified Valuation Analyst, a Master Analyst in Financial Forensics, and is certified in Financial Forensics.⁸⁴ Dubinsky also has extensive experience as an auditor working with private placements involving limited liability companies like CMS.⁸⁵

Dubinsky reviewed all the CMS investor contributions and expenses. He then showed what the aggregate capital accounts for the investors in each of CMS’s seven series would look like if Taboada had allocated CMS’s expenses in accordance with the Offering Memorandum. Table 1 below shows Dubinsky’s allocation of expenses.

⁸¹ CX-6, at 29, 34; *see also* Tr. 1683-84 (Q. “Let me address it this way. Mr. Radin: Do you understand that series-specific expenses are to be attributed to each individual series?” A. “Yes.”); Tr. 1690 (Q. “You understand that the series-specific costs should be subtracted from the capital in for that series, correct?” A. “Yes.”).

⁸² CX-6, at 29; Tr. 252.

⁸³ Tr. 252-53.

⁸⁴ CX-128, at 6, 30-33.

⁸⁵ Tr. 973-74.

Table 1: Dubinsky's Allocation of Expenses

A	B	C	D	E	F
	Capital In ⁸⁶	Placement Fees ⁸⁷	Securities Purchases ⁸⁸	General Expenses ⁸⁹	Balance ⁹⁰
First	\$914,942	\$22,874	\$863,500	\$13,831	\$14,737
Second	\$1,465,871	\$36,647	\$1,378,226	\$22,160	\$28,838
Third	\$254,150	\$6,354	\$247,296	\$3,842	(\$3,342)
Fourth	\$627,000	\$62,700	\$572,429	\$9,479	(\$17,607)
Fifth	\$2,259,796	\$225,980	\$2,010,000	\$34,162	(\$10,346)
Sixth	\$454,980	\$45,498	\$406,250	\$6,878	(\$3,646)
Seventh	\$75,000	\$7,500	\$75,000	\$1,134	(\$8,634)
Total	\$6,051,738	\$407,552	\$5,552,701	\$91,486	\$0

As reflected in Table 1 above, when Dubinsky allocated CMS's expenses in accordance with the Offering Memorandum, the First and Second Series investors had capital surpluses of \$14,737 and \$28,838, respectively, totaling \$43,575; and the Third through Seventh Series investors had capital deficits of (\$3,342); (\$17,607); (\$10,346); (\$3,646); and (\$8,634), respectively, totaling (\$43,575).⁹¹

3. Taboada's Use of Certain Investors' Funds to Pay Expenses Owed by Other Investors

Taboada did not return the excess capital to First or Second Series investors.⁹² Instead, he used it to pay expenses owed by the Third through Seventh Series investors.

⁸⁶ CX-128, at 21, Table 5 ("Initial Capital Contribution" column A).

⁸⁷ CX-128, at 21, Table 5 ("Placement Fee" column B).

⁸⁸ CX-128, at 21, Table 5 ("Investment in Felix SPEs and Direct Purchases" column C). The parties stipulated to these securities purchases. Stip. ¶¶ 34-38.

⁸⁹ CX-128, at 22, Table 6 ("General Expenses Allocated based on Taboada's Calculation of Ownership Percentage" column B).

⁹⁰ CX-128, at 22, Table 6 ("Taboada's Ending Capital Account Balance" column C).

⁹¹ CX-128, at 22.

⁹² Tr. 605-07, 645. Taboada admitted he did not distribute excess capital to First and Second Series investors, but claimed that those investors received equivalent amounts in additional Facebook shares. Tr. 605-07, 645. Taboada is incorrect. As reflected in Section II.E of this Decision, several First and Second Series investors did not receive *any* additional shares; in fact, they did not even receive their pro rata allotment of shares. See CX-128, at 50-53.

Beginning in late October 2012, Taboada and YS, his accountant, worked together to create the Share Calculation Spreadsheet (“Spreadsheet”).⁹³ The Spreadsheet purported to show how CMS’s expenses had been allocated among investors. A portion of the Spreadsheet is shown in Table 2 below.

Table 2: Taboada’s Allocation of Expenses

A	B	C	D	E	F	G	H
	Capital In ⁹⁴	Placement Fees ⁹⁵	General Expenses ⁹⁶	Felix Cost/5% Direct Cost/0% ⁹⁷	Net Invest ⁹⁸	Felix Cost + Net Invest ⁹⁹	Balance ¹⁰⁰
First	\$914,942	\$22,874	\$13,831	\$43,175	\$835,062	\$878,237	\$0
Second	\$1,465,871	\$36,647	\$22,160	\$68,911	\$1,338,153	\$1,407,064	\$0
Third	\$254,150	\$6,354	\$3,842	\$12,365	\$231,589	\$243,954	\$0
Fourth	\$627,000	\$62,700	\$9,479	\$28,621	\$526,200	\$554,821	\$0
Fifth	\$2,259,796	\$225,980	\$34,162	\$0	\$1,999,654	\$1,999,654	\$0
Sixth	\$454,980	\$45,498	\$6,878	\$0	\$402,604	\$402,604	\$0
Seventh	\$75,000	\$7,500	\$1,134	\$3,750	\$62,616	\$66,366	\$0
Total	\$6,051,738	\$407,552	\$91,486	\$156,822	\$5,395,878	\$5,552,700	\$0

As shown in Table 2, the Spreadsheet eliminated the surpluses and deficits among investors’ capital accounts by misrepresenting CMS’s Facebook transactions.¹⁰¹ The Spreadsheet represented that CMS, through Taboada, used \$878,237 of First Series investors’ capital to purchase Facebook securities,¹⁰² but the First Series investors paid

⁹³ Taboada tried to disclaim all responsibility for the share allocations in the Spreadsheet. He initially testified that he relied entirely on YS to create the Spreadsheet. *See, e.g.*, Tr. 445-48. However, his subsequent testimony, and the documentary evidence, revealed that he was very involved in creating and revising the Spreadsheet. Beginning in late October and continuing until late November, Taboada and YS exchanged numerous emails about the Spreadsheet; created multiple versions of the Spreadsheet; and met in person several times to discuss the Spreadsheet. CX-171 – CX-178; CX-180; RX-11; Tr. 480, 483-91. During those meetings, Taboada gave YS specific information about what information should be included in the Spreadsheet and how it should be presented. *See, e.g.*, Tr. 455, 458, 484-86, 497, 526; RX-11. The Hearing Panel did not find Taboada’s assertion that he relied entirely on YS to create the Spreadsheet to be credible.

⁹⁴ CX-177 (“Amount Original” column).

⁹⁵ CX-177 (“Commission” column).

⁹⁶ CX-177 (“Agency/Bank” + “Reg&License” + “Profession” + “Rent” columns).

⁹⁷ CX-177 (“Felix Cost/ 5% Direct Cost/ 0%” column).

⁹⁸ Column F represents Column B minus Columns C, D, and E.

⁹⁹ CX-177 (“CMS FB Net”). Column G in Table 2 represents column E plus column F (“Felix Cost/5% Direct Cost 0%” column + “Net Invest” column).

¹⁰⁰ Column H is not reflected in CX-177. Column H represents column B minus columns C, D, E, and F (“Capital In” less “Placement Fees,” “General Expenses,” “Felix Cost/5% Direct Cost/0%,” and “Net Invest” columns).

¹⁰¹ *See* CX-171 – CX-178; CX-180; RX-11; Tr. 455, 458, 484-86, 497, 526, 535-38, 552-53.

¹⁰² *See* CX-177 (“CMS FB Net” column); *see also* Table 2, Column G.

only \$863,500 to purchase interests in Libre II, which included all monies paid to Felix.¹⁰³ The Spreadsheet also represented that CMS used \$1,407,064 of the Second Series investors' capital to purchase Facebook securities,¹⁰⁴ but the Second Series investors paid only \$1,378,226 to purchase interests in Libre I and Libre II, which included all monies paid to Felix.¹⁰⁵ Together, these two misrepresentations in the Spreadsheet made it appear that First and Second Series investors paid \$43,575 more than they actually had, which eliminated their capital surpluses. Taboada and his accountant YS also misrepresented CMS's other transactions to make it appear that the Third through Seventh Series investors paid \$43,575 less than they actually had, which eliminated their capital deficits.¹⁰⁶ Because the Spreadsheet eliminated all surpluses and deficits, the Spreadsheet did not disclose accurately each investor's surplus or deficit.

The Spreadsheet also misrepresented the amount of the commission that the Fourth Series investors paid to Felix on their investment in Opportunity. The Spreadsheet represented that Fourth Series investors had paid Felix \$28,621, representing a 5 percent commission,¹⁰⁷ but, as discussed above, at Taboada's request the commission was actually \$57,242.89, representing a 10 percent commission for Felix.¹⁰⁸

E. Taboada's Improper Distribution of CMS Facebook Shares

Taboada did not distribute Facebook shares in accordance with the Offering Memorandum. Eleven First and Second Series investors did not receive their pro rata share of their respective series' Facebook stock or any additional shares to compensate them for the excess capital Taboada failed to return to them.¹⁰⁹ For example, one of the 11 investors should have received 11 additional Facebook shares *plus* his pro rata share of the First Series' excess capital, \$2,496, but he did not.¹¹⁰ Another investor should have received 71 additional Facebook shares *plus* his pro rata share of the Second Series' excess capital, \$1,966, but did not.¹¹¹ Taboada also withheld additional shares from some

¹⁰³ Stip. ¶¶ 29-30.

¹⁰⁴ See CX-177 ("CMS FB Net" column); *see also* Table 2, Column G.

¹⁰⁵ Stip. ¶¶ 31-33.

¹⁰⁶ See Stip. ¶¶ 34-38 (reflecting the payments for the securities purchased in connection with Series Three through Seven); CX-128, at 21, Table 5 ("Investment in Felix SPEs and Direct Purchases" column C). *Compare* Table 1, Column F, *with* CX-177 and Table 2, Column G.

¹⁰⁷ CX-177, at 3 (reflecting the total of the Felix Cost column, lines 45-59).

¹⁰⁸ *See supra* Section II.C.4.

¹⁰⁹ CX-128, at 50.

¹¹⁰ The investor's excess capital of \$2,496 is calculated by multiplying 16.94 percent, his series ownership percentage in the First Series, by \$14,737, the excess capital for the First Series. *See* CX-128, at 22 (reflecting the excess capital for each series), 50 (reflecting the ownership percentage for each investor).

¹¹¹ The investor's excess capital of \$1,966 is calculated by multiplying 6.82 percent, his series ownership percentage in the Second Series, by \$28,838, the excess capital for the Second Series. *See* CX-128, at 22, 50.

investors by charging them an unauthorized “carried interest” fee on their investments in CMS.

Below we discuss the Offering Memorandum requirements for distribution of Facebook shares, Taboada’s flawed distribution methodology, and his imposition of a carried interest fee.

1. The Offering Memorandum’s Requirements for the Distribution of Facebook Shares

The Offering Memorandum required Taboada to allocate all of the shares purchased by a particular series to that series, and among the series’ investors, pro rata based on their ownership interest in the series.¹¹² Dubinsky, Enforcement’s expert, allocated the CMS Facebook shares in accordance with the Offering Memorandum, employing a straightforward process. He simply allocated to each series the total number of shares that CMS received from each series’ investment in Facebook securities; then, within each series, he allocated the shares to investors pro rata based on their ownership interest in the series.¹¹³

2. Taboada’s Flawed Methodology for the Distribution of CMS’s Facebook Shares

Facebook’s IPO occurred in May 2012.¹¹⁴ The Facebook stock lockup period expired in November 2012, and CMS began receiving its Facebook shares in early December 2012.¹¹⁵ The Facebook securities CMS acquired were held in a brokerage account at Blackwall until Taboada distributed them to investors with assistance from Blackwall employees.¹¹⁶

When Taboada distributed the Facebook shares to the CMS investors, he did not adhere to the Offering Memorandum requirements. Instead, on December 11, 2012, Taboada began distributing shares to investors using the inaccurate numbers from the Spreadsheet.¹¹⁷

¹¹² CX-6, at 20.

¹¹³ CX-128, at 50-53.

¹¹⁴ Stip. ¶ 112.

¹¹⁵ Stip. ¶¶ 112, 113; Tr. 533, 541-42.

¹¹⁶ E.g., Tr. 1090-96, 1103-06; CX-75. After Taboada completed the distribution, Blackwall employees continued to assist him with CMS, providing documents and information to JL, another accountant performing work for CMS. E.g., Tr. 1396-98, 1417-18, 1483, 1492; CX-126.

¹¹⁷ Tr. 533, 541-42.

In the Spreadsheet, Taboada and YS attempted to estimate the number of shares CMS would receive and allocate the shares among investors.¹¹⁸ However, their methodology was not reliable for two reasons. First, the Spreadsheet did not accurately reflect CMS's actual Facebook transactions. The amounts of the investors' net investment in each series were not accurate because Taboada and YS had used numbers that eliminated all surpluses and deficits from investors' capital accounts. Second, the share prices in the Spreadsheet were not accurate with respect to CMS's indirect purchases of Facebook securities from the Felix entities.¹¹⁹ According to the Spreadsheet, CMS purchased Facebook securities from the Felix entities at \$31 per share for First Series investors, \$30.44 per share for Second Series investors, \$31 per share for Third Series investors, \$32 per share for the Fourth Series investors, and \$37.50 per share for the Seventh Series investor.¹²⁰

However, Felix did not promise to deliver shares to CMS at a specific price. As early as April 2011, Felix explicitly told Taboada that the number of shares CMS would receive from its investments in the Felix entities could not be determined (and thus the final price per share could not be known) until the final accounting for each entity was complete.¹²¹ Felix also told Taboada that the Felix entities would incur internal expenses, which would be passed on to CMS and reduce the number of shares delivered to CMS for its investments.¹²² Taboada testified that he understood that these expenses would reduce the number of shares CMS received from its investments in the Felix entities.¹²³ Accordingly, Taboada had no reason to believe that the Spreadsheet (1) accurately calculated the number of Facebook shares CMS would receive, or (2) properly allocated those shares among its investors.

Taboada did not have to rely on the inaccurate Spreadsheet. On December 11, the same day he began distributing shares, Felix told Taboada the exact number of shares CMS would receive from its investments in the Felix entities and identified how many shares CMS would receive from each series' investment(s).¹²⁴ Specifically, Felix sent Taboada an email stating that CMS would receive a total of 93,796 shares from its investments in the Felix entities, which was 2,287 fewer shares than Taboada and YS had calculated.¹²⁵ Taboada acknowledged that, as of December 11, with the actual share

¹¹⁸ See CX-177. The result of this calculation appeared in the "# of Shares" column.

¹¹⁹ The Fifth and Sixth Series acquired Facebook shares at fixed prices through direct purchases.

¹²⁰ See CX-177 ("Felix P/Shr Direct P/Shr" column).

¹²¹ CX-94; CX-95.

¹²² CX-94 ("The number of shares (and/or proceeds thereof) to be distributed to [] investors upon liquidation is subject to adjustment for allocation of organizational and operating expenses of the Company."); CX-95 (same); CX-101 (same); CX-105 (same).

¹²³ Tr. 286-89, 471-72.

¹²⁴ Tr. 562-63.

¹²⁵ CX-121; Tr. 562-64.

totals from Felix, he had no reason to continue using the erroneous estimated allocations from the Spreadsheet.¹²⁶ Nevertheless, he continued distributing shares using the Spreadsheet.

On December 17, Felix informed Taboada that CMS would be receiving additional shares from its investments in the Felix entities. Felix sent Taboada four emails stating that shares Felix had held back to cover transfer fees would be credited to CMS's account no later than January 15, 2013.¹²⁷ Based on these emails, Taboada understood that CMS would be receiving additional Facebook shares, but he did not tell YS about those shares to enable him to incorporate them into the Spreadsheet's share allocation.¹²⁸

On December 18, YS sent Taboada an updated spreadsheet ("Revised Spreadsheet").¹²⁹ The Revised Spreadsheet was identical to the original Spreadsheet, except that it added a new column titled "Actual Shares."¹³⁰ The "Actual Shares" column allocated shares to each series based on the share totals Felix provided to Taboada on December 11.¹³¹ However, the Revised Spreadsheet was still inaccurate because it (1) continued to misrepresent CMS's expenses by eliminating the surpluses and deficits (as the original Spreadsheet had), and (2) failed to account for the additional shares CMS would receive from Felix as stated in Felix's December 17 email to Taboada.¹³²

As soon as Taboada received the Revised Spreadsheet, he knew that the share allocations in the "Actual Shares" column were more accurate than the share allocation numbers on the original Spreadsheet he had been using until that point.¹³³ Yet, after receiving the Revised Spreadsheet, Taboada continued to rely on the inaccurate share allocation numbers from the original Spreadsheet when distributing Facebook shares to some CMS investors.¹³⁴ When deciding how many Facebook shares to distribute to a

¹²⁶ Tr. 563-64.

¹²⁷ CX-122; CX-123; CX-124; CX-125.

¹²⁸ Tr. 733, 736.

¹²⁹ CX-180.

¹³⁰ CX-180.

¹³¹ CX-180; Tr. 555-57.

¹³² CX-180; Tr. 566-69.

¹³³ Tr. 689; *see also* Tr. 695 (Q. "You considered the actual shares column to be more accurate than the prior column by which is called number of shares; correct?" A. "Yes."); Tr. 749 (Q. "Yes, and it reflects the actuals that you were using, you said were more accurate than the number of shares column; correct?" A. "Yes.").

¹³⁴ The inaccurate share allocations from the original Spreadsheets were also included in the Revised Spreadsheet. Taboada testified that he had no choice but to follow the share allocations in the original Spreadsheet because FINRA was pressuring him, through Blackwall, to distribute CMS's Facebook shares. *See, e.g.*, Tr. 535-38, 552-53. The Hearing Panel finds Taboada's assertion not credible. Blackwall's Chief Compliance Officer ("CCO") testified that he was anxious for Taboada to distribute CMS's Facebook shares because investors were calling him and complaining, but that FINRA did not pressure Blackwall to distribute CMS's Facebook shares. Tr. 1093-95, 1098-1102, 1124; CX-119.

particular investor, in most instances, Taboada chose to provide the lesser number of shares to the investor. He deviated between the share allocation numbers from the original Spreadsheet and the Revised Spreadsheet and usually provided the lesser number of shares to the investor.¹³⁵

Taboada admitted that, while he was distributing the CMS Facebook shares, he knew he was distributing too few shares to some investors. He explained that he believed he had to short these investors because he already had distributed too many shares to other investors, and thus might not have enough shares to go around.¹³⁶

3. Taboada's Imposition of a "Carried Interest" Fee

By the end of April 2013, Taboada had not distributed any Facebook shares to several investors.¹³⁷ CMS owed these investors more than 14,500 Facebook shares, based on the Revised Spreadsheet.¹³⁸ However, CMS had only 13,466 Facebook shares remaining at that time.¹³⁹ In July and August 2013, Taboada purchased an additional 900 shares of Facebook stock using outside funds;¹⁴⁰ however, that still left a shortage of more than 100 shares. To close the gap between the number of Facebook shares CMS had available and the number it owed to investors, Taboada imposed a "carried interest" charge on four of the five investors who had not yet received any shares.¹⁴¹ Taboada determined that these investors owed more than \$6,300 in "carried interest," and then withheld more than 150 shares from them to pay the fee.¹⁴²

Nothing in the Offering Memorandum authorized Taboada to impose a carried interest charge on these investors.¹⁴³ Taboada admitted that he made the decision to impose the carried interest charge and that it was not authorized under the Offering

¹³⁵ Compare CX-180 ("# of shares" and "Actual shares" columns), *with* Stip., Table A, Columns E and F (identifying the number of shares delivered and the date of delivery).

¹³⁶ Tr. 760-63.

¹³⁷ See Stip., Table A (reflecting investors who received shares after April 2013).

¹³⁸ Compare Stip., Table A, *with* CX-180.

¹³⁹ CX-75, at 36.

¹⁴⁰ Stip. ¶ 74. Taboada contends that he deposited the funds for these transactions from his personal checking account.

¹⁴¹ CX-126; CX-127, at 1-2; RX-53, at 7 n.5. Taboada did not impose a carried interest charge on one of those investors. RX-53, at 7 n.4.

¹⁴² CX-126; CX-127, at 1-2; RX-53, at 7 n.5; Tr. 180-81.

¹⁴³ Tr. 180-81.

Memorandum.¹⁴⁴ Taboada also admitted that he has not reimbursed these four investors for the carried interest that he improperly charged them.¹⁴⁵

F. Taboada's Untimely Corrective Action

Taboada failed to take timely corrective action to remedy his misallocation of Facebook shares. In December 2012, Taboada knew he had distributed too few shares to some investors, but he failed to notify all of those investors that they were owed additional shares. Thereafter, when certain investors questioned Taboada regarding their share distribution, Taboada gave them false information. He falsely told several investors that he had retained an accountant to review his share distribution. He also distributed to several investors the false and misleading Spreadsheet or the Revised Spreadsheet, representing to them that the Spreadsheet showed how their capital had been spent. When he ultimately reimbursed some investors for their shortage of shares, which occurred more than a year after Taboada realized he had not distributed enough Facebook shares to some investors,¹⁴⁶ he utilized an inaccurate and unreliable report.

Below we discuss Taboada's (1) failure to notify all investors of their shortage of Facebook shares, (2) provision of false information to certain investors, (3) reliance on an inaccurate report to reimburse investors, and (4) his untimely reimbursement to investors.

1. Taboada's Failure to Notify Investors That They Were Owed Additional Shares

Taboada admitted that he intentionally distributed too few shares to some CMS investors in December 2012. Thereafter, he took no affirmative steps to notify those investors that they were owed additional shares. By December 2012, some investors had already contacted Taboada to complain about the number of Facebook shares they received or would be receiving.¹⁴⁷ Taboada testified that he spoke with the investors who called him to complain about the number of shares they had received, but he admitted that he did nothing to notify investors who did not complain.¹⁴⁸

¹⁴⁴ Tr. 180-81.

¹⁴⁵ Tr. 819.

¹⁴⁶ Taboada waited a year before taking any corrective action, and did so only after Enforcement notified him of possible violations of FINRA Rules and subsequently filed the Complaint.

¹⁴⁷ See, e.g., CX-23; CX-30; CX-34.

¹⁴⁸ Tr. 766-67; see Tr. 790-91 ("In hindsight, I think I made an error in that time line that I should have communicated with the client and informed them of Mr. [JL]'s engagement and my pursuit to rectify the numbers. I did not make that communication.").

2. Taboada's False Statements to Investors Promising a Reconciliation of the Share Distribution

When investors complained about their share distribution, Taboada represented to them that his accountant was reviewing the share distribution and that investors would be made whole based on the accountant's report.¹⁴⁹ By mid-December 2012, he also sent emails to complaining investors assuring them that they would receive a full accounting of CMS. For example, in a December 13, 2012 email to one CMS investor, Taboada wrote:

You will also get a complete accounting of the LLC and all pertinent documents for the LLC including an accounting of the transaction[s], bank statements, escrow statements etc.¹⁵⁰

Rather than sending the investor a complete accounting, however, on January 4, 2013, Taboada sent him the inaccurate Revised Spreadsheet, which misrepresented CMS's expenses. In his January 4 email to the investor, attaching the Revised Spreadsheet, Taboada wrote:

Here is the accounting for your purchase in CMS ... a complete accounting book and audit report will be sent to you for your review but I wanted to give you something to look at this week as promised.¹⁵¹

When the investor questioned the accuracy of the Revised Spreadsheet,¹⁵² Taboada promised him an audit report showing the details of CMS's Facebook transactions:

The audit report will show the purchase dates and the funds that came in time for those purchase dates. It is very straight forward [*sic*]. If you missed the time for certain purchase price points that's an issue. But I refer you to the PPM. It states that the price can change and will change and there is no guarantee or assurance that we will get stock at any price....

You will be able to speak to the auditor and you will realize that all of the money in the LLC was managed properly. You will see at the end of the day everyone in the LLC was treated fairly and in accordance with the paperwork that each and every member signed and acknowledged.¹⁵³

¹⁴⁹ Tr. 761-62, 767-68.

¹⁵⁰ CX-30, at 3-4.

¹⁵¹ CX-34, at 3. Taboada sent the Spreadsheet or the Revised Spreadsheet to several other investors as well. See CX-23, at 5-6; CX-186; CX-188; CX-189; CX-190.

¹⁵² CX-34, at 1-2.

¹⁵³ CX-34, at 2.

Contrary to Taboada's representations, at that time there was no accountant reviewing the share distribution or auditing all of the details of CMS's Facebook transactions. Although Taboada retained an accountant, JL, to audit CMS in March 2013,¹⁵⁴ JL's assignment was expressly limited to auditing CMS's annual financial statements and preparing partnership income tax returns, not reviewing the share distribution.¹⁵⁵ JL issued his audit of CMS's financial statements in June 2013.¹⁵⁶ JL testified that an investor reviewing his audit would have no way of knowing whether he or she received the correct number of Facebook shares.¹⁵⁷ In fact, JL testified that, between March and June 2013 when he was conducting his audit, Taboada did not tell him that there were problems with CMS's Facebook share distribution.¹⁵⁸ JL further testified that Taboada's counsel, not Taboada, retained him in 2014 to perform additional work for CMS in connection with the share distribution.¹⁵⁹

3. Taboada's Reliance on Accountant JL's Unreliable Share Distribution Report

In early 2014, Taboada's counsel hired JL on behalf of CMS.¹⁶⁰ JL testified that he was not specifically retained to review the share distribution, but actually was asked "to recomputate, based upon certain Agreed Upon Procedures, what the capital accounts may have been if we looked and recalculated from day one."¹⁶¹ JL repeatedly stressed that he did not recreate CMS's books and records as part of his work.¹⁶² He explained

¹⁵⁴ CX-205. JL does not have significant experience in accounting for funds like CMS; he admitted that this type of work is only ancillary to his business, and that none of his other clients are multi-series LLCs. Tr. 1383-84, 1583-84.

¹⁵⁵ Tr. 779; CX-205.

¹⁵⁶ CX-12, at 4; Tr. 778.

¹⁵⁷ Tr. 1383-84.

¹⁵⁸ Tr. 1378-79; *see also* 1379-80.

¹⁵⁹ Tr. 1335, 1378-79. Taboada claimed that he hired JL at his own expense in the first or second quarter of 2013 to review his share distribution, and that it took JL a year to issue the first draft of his report. Tr. 786-90. The Panel does not find Taboada's testimony to be credible. As stated above, JL testified that he was not even aware of any problems with the share distribution while he was working on his audit of CMS in 2013. Taboada also testified that he retained another accountant, DB, in the fourth quarter of 2012 or the first quarter of 2013 to "[g]o over the numbers associated with the distribution of Facebook shares received and delivered through CMS []." Tr. 740-41. According to Taboada, he paid DB approximately \$6,000 out of his own pocket, and DB prepared a spreadsheet re-allocating CMS's Facebook shares. Tr. 738-41, 1288. The Hearing Panel also finds Taboada's testimony about DB not credible. The evidence shows that JL first brought DB to Taboada's attention in October 2013, when he sent an email to Taboada attaching DB's resume. Tr. 1366-67, 1370; CX-247. Other than Taboada's testimony, there is no evidence (no work product or any correspondence reflecting communications between DB and Taboada) that Taboada ever hired DB to do anything relating to CMS. Tr. 1373. In fact, on February 25, 2014, JL once again forwarded DB's resume to Taboada. CX-249.

¹⁶⁰ Tr. 1334-35; *see* CX-195, at 3 (reflecting JL's draft report dated February 18, 2014).

¹⁶¹ Tr. 1335, 1338, 1388, 1491.

¹⁶² *See, e.g.*, Tr. 1415-16, 1425.

that his Agreed Upon Procedures Report (“Report”) was a “model” that “wasn’t meant to be exact,”¹⁶³ and that his Report was based largely on assumptions and estimates rather than actual numbers.¹⁶⁴

JL’s Report contained errors that rendered all of his calculations, which he admits were estimates, unreliable. First, the Report inaccurately allocated a 5 percent Felix commission expense to the Fourth Series, but, as discussed above, the Fourth Series actually paid Felix a 10 percent commission.¹⁶⁵ JL testified that he was not aware the Fourth Series had paid a 10 percent commission.¹⁶⁶ He acknowledged that his failure to allocate the entire 10 percent commission to the Fourth Series rendered his share allocations unreliable for all of the other investors.¹⁶⁷ JL also acknowledged that the expenses that he failed to allocate to the Fourth Series investors were allocated to investors in other series, thereby reducing the number of shares allocated to those investors.¹⁶⁸

Second, JL did not know that NYPA, the entity through which the Seventh Series had acquired its Facebook shares, was a Felix entity, and that CMS had paid a commission to Felix on that transaction.¹⁶⁹ Accordingly, JL did not allocate any Felix commission expense to the Seventh Series, which meant that the expense was allocated to investors in other series, thereby reducing the number of shares allocated to them.¹⁷⁰

Lastly, JL’s Report is flawed because his methodology of allocating expenses and Facebook shares is inconsistent with a series limited liability company, regardless of whether CMS is a seven-series or a single-series limited liability company (as Taboada claimed at one point). JL agreed that, if CMS is a seven-series limited liability company, his Report did not properly allocate CMS’s expenses as a result of the errors discussed above.¹⁷¹ If CMS was a single-series limited liability company, JL’s Report did not properly allocate CMS’s Facebook shares because all investors in the purported single-

¹⁶³ See, e.g., Tr. 1461-63.

¹⁶⁴ See, e.g., Tr. 1388, 1402-03, 1411-14, 1425, 1464, 1472-73. Taboada’s expert, Arthur Radin, did not agree with JL’s extensive use of “estimates” in his Report. Radin testified that, while estimates may be suitable for financial statements, allocating CMS’s expenses and Facebook shares “is much more of a mechanical computation.” Tr. 1698-99. Radin also stated that he did not agree with JL’s assertion that accounting “is all about estimates.” Tr. 1698-99.

¹⁶⁵ RX-53, at 5; Tr. 1501-03.

¹⁶⁶ Tr. 1506, 1508-09.

¹⁶⁷ Tr. 1507.

¹⁶⁸ Tr. 1506-08.

¹⁶⁹ Tr. 1440-41, 1443-45.

¹⁷⁰ Tr. 1445-46; see Tr. 1507-08 (explaining how the failure to properly allocate a Felix commission expense to Fourth Series investors affected the number of shares allocated to other investors).

¹⁷¹ Tr. 1473.

series should have paid the same price for their Facebook shares and, under JL's allocation, they did not.¹⁷²

4. Taboada's Untimely, and in Certain Instances Inadequate, Reimbursement to Some Investors

Taboada's reimbursement to the CMS investors who received fewer Facebook shares than they were entitled to was untimely and, for certain investors, inadequate.

On May 12, 2014, more than a year after Taboada realized he had not distributed enough Facebook shares to some investors, he mailed checks to some CMS investors to reimburse them for the Facebook shares he had withheld.¹⁷³ The amounts of the reimbursement checks were derived from JL's Report. But, as discussed above, the Report was inaccurate and unreliable.

Even if JL's Report accurately determined how many additional shares Taboada owed to certain CMS investors—and the Panel finds that it did not—not all investors were made whole because Taboada sent checks to at least three investors for a lesser amount than what they were owed according to the Report. For example, JL calculated that one investor was entitled to 136 additional shares at \$56.72 per share, or \$7,313.92,¹⁷⁴ but Taboada sent a check for only \$6,288.23, which was \$1,025.69 less than the amount JL calculated.¹⁷⁵ Two other investors also received checks for less than JL calculated. Collectively, these three investors received a total of approximately \$8,000 less than JL's calculation.¹⁷⁶ Furthermore, these three investors never received *any* money from Taboada because they did not receive their checks.¹⁷⁷ Of the approximately \$40,000 in checks that Taboada mailed, only about \$24,000 in checks were received by investors.¹⁷⁸ Several mailings were returned as undeliverable.

¹⁷² Tr. 1470-72, 1073-74.

¹⁷³ Stip. ¶ 116; CX-41, at 1; RX-12; CX-1, at 27 (showing that Taboada received notification of possible charges by FINRA's Department of Enforcement on January 31, 2014). Taboada's reimbursement to the CMS investors occurred more than three months after Enforcement notified him of possible charges, and more than a week after Enforcement filed its Complaint.

¹⁷⁴ Tr. 810-12.

¹⁷⁵ CX-41, at 126-27.

¹⁷⁶ Tr. 812-13, 815-17.

¹⁷⁷ Tr. 916-17.

¹⁷⁸ Tr. 916-17.

G. Taboada's Production of False Document and Provision of False Testimony to FINRA

FINRA's Department of Enforcement began investigating Taboada's management of CMS by December 2012.¹⁷⁹ In furtherance of its investigation, Enforcement requested documents and information pursuant to FINRA Rule 8210. In a Rule 8210 request dated February 4, 2013, Enforcement specifically asked Taboada to provide all invoices from Charles Morgan to CMS.¹⁸⁰

On March 22, 2013, the day his response was due, Taboada created an invoice from Charles Morgan to CMS to support an October 2012 payment to Charles Morgan.¹⁸¹ The invoice indicated that Charles Morgan was charging CMS \$5,000 per year for use of its office space.¹⁸² Taboada dated the invoice January 2011.¹⁸³ That evening, Taboada sent an email to Enforcement attaching his response to the Rule 8210 request.¹⁸⁴ He sent the supporting documentation, including the invoice he had created from Charles Morgan to CMS reflecting a rental charge for the use of its office, to Enforcement via overnight mail.¹⁸⁵

In April 2013, a few weeks after Taboada responded to the Rule 8210 request, Taboada provided sworn testimony to Enforcement. During Taboada's investigative testimony, he falsely stated that he created the invoice in January 2011.¹⁸⁶

In April 2014, after FINRA had informed him of its preliminary determination to bring a disciplinary action against him, based, in part, on the false invoice and testimony, Taboada again provided sworn testimony to Enforcement.¹⁸⁷ During his April 2014 testimony, Taboada changed his earlier testimony and admitted that he did not create the invoice in January 2011, but in 2013, shortly after he received FINRA's Rule 8210 request.¹⁸⁸

¹⁷⁹ CX-153, at 1

¹⁸⁰ CX-153, at 5; *see* CX-155, at 3 (requesting all invoices again as a follow-up to the February 2, 2013 Rule 8210 request).

¹⁸¹ Tr. 108, 849-50; CX-196.

¹⁸² CX-196.

¹⁸³ CX-196.

¹⁸⁴ CX-156; CX-242.

¹⁸⁵ CX-156; Tr. 842-44.

¹⁸⁶ CX-236, at 5, 8-9, 10, 11-12.

¹⁸⁷ Tr. 1261-64.

¹⁸⁸ RX-54; Tr. 1262.

At the hearing, Taboada admitted that, contrary to his sworn investigative testimony in April 2013, he created the invoice on March 22, 2013.¹⁸⁹ He also admitted that, when he submitted the invoice in response to Enforcement's Rule 8210 request, he wanted Enforcement to believe that the invoice had been created in January 2011.¹⁹⁰

Taboada argued that his investigative testimony was not false because the invoice he created in March 2013 was a recreation of the original invoice purportedly created in January 2011.¹⁹¹ According to Taboada, he believes an original invoice exists but he could not find the original invoice so he recreated an "exact copy" and provided it to Enforcement.¹⁹²

The Panel did not find Taboada's testimony credible for several reasons. First, the invoice was issued to CMS, but CMS did not exist in January 2011. In fact, Taboada acknowledged that CMS did not exist in any form before March 2011.¹⁹³ He retained counsel to represent him in connection with the formation of CMS on March 4, 2011;¹⁹⁴ CMS became a limited liability company on March 9, 2011;¹⁹⁵ and Taboada disclosed CMS as an outside business activity on March 14, 2011.¹⁹⁶ Taboada also acknowledged that Charles Morgan did not provide office space to CMS until that time.¹⁹⁷

Second, the rent charge memorialized by the purported invoice did not appear as a 2011 expense in the audit that JL conducted in early 2013.¹⁹⁸ In JL's audit, the payment for the rent expense is a 2012 expense, and JL testified that he was not aware of any rent expense for 2011.¹⁹⁹

¹⁸⁹ Tr. 849-50 (Q. "Let me go back, Mr. Taboada to CX 196. Mr. Taboada, this document was created on March 22, 2013; correct?" A. "This version of it, yes." Q. "The document that appears in front of us was dated March 22, 2013; correct?" A. "Yes." Q. "The document was created on your computer that was in your office at Blackwall [Capital]; correct?" A. "Yes." Q. "You signed the document twice on March 22, 2013; correct?" A. "Yes." Q. "You created the document as you worked to file your response to the 8210 document request letter; right?" A. "Yes." Q. "And you filed that 8210 letter on that same day that you created this document; right?" A. "Yes.").

¹⁹⁰ Tr. 853.

¹⁹¹ *E.g.*, Tr. 861-62, 1247; RX-54.

¹⁹² RX-54; Tr. 1248-49.

¹⁹³ Tr. 829-31.

¹⁹⁴ CX-203.

¹⁹⁵ CX-4.

¹⁹⁶ Tr. 870-76.

¹⁹⁷ Tr. 829-31.

¹⁹⁸ JL testified that CMS used accrual accounting. As JL explained, when accrual accounting is used, an expense is identified when it occurs regardless of when a company actually pays the expense. Applying the accrual accounting methodology, CMS's rent expense should have been included as a 2011 expense in JL's audit, regardless of when CMS actually paid Charles Morgan. Tr. 1373-74.

¹⁹⁹ Tr. 1376-78; CX-12, at 6.

Lastly, while Taboada claimed to have recreated the \$5,000 rent invoice because he lost the original, he did not take this same approach with other missing invoices. For example, in his same March 22, 2013 response to Enforcement’s Rule 8210 request, Taboada wrote that he was unable to locate an invoice from YS, but would keep looking for it.²⁰⁰

III. Conclusions of Law

The Panel found Taboada liable for each of the causes of action in the Complaint. Specifically, the Panel found that Taboada violated (1) FINRA Rule 2010 by misappropriating investor funds and securities; (2) FINRA Rules 2150 and 2010 by misusing customer funds and securities; (3) FINRA Rule 2010 by providing false and misleading information, and failing to disclose information, to investors regarding expenses such as commissions and sales concessions; and (4) FINRA Rules 8210 and 2010 by providing false and misleading testimony and documents to FINRA. In doing so, we rejected Taboada’s arguments and defenses. Below we address each violation and Taboada’s defenses.

A. Taboada Violated FINRA Rule 2010 by Misappropriating Investor Funds and Securities

The first cause of action alleges that Taboada misappropriated funds and securities from CMS investors by failing to return excess capital to First and Second Series investors and by failing to distribute to certain CMS investors all of the Facebook shares to which they were entitled.

1. Legal Standard

Misappropriation is the unauthorized, improper, or unlawful use of funds or other property for a purpose other than that for which intended.²⁰¹ Misappropriation of funds or securities violates FINRA Rule 2010, which requires registered persons to “observe high standards of commercial honor and just and equitable principles of trade.”²⁰²

2. Discussion

Taboada obtained possession and control of investor funds when CMS accepted their subscriptions, and obtained possession and control over investor securities when Facebook shares were delivered to CMS. At all times, Taboada was obligated to treat investor funds and securities in accordance with the terms of the Offering Memorandum, which specified how Taboada was to handle investor funds and securities. The Offering

²⁰⁰ CX-156, at 2.

²⁰¹ *Dep’t of Enforcement v. Evans*, No. 2006005977901, 2011 FINRA Discip. LEXIS 36, at *34 n.33 (NAC Oct. 3, 2011) (citation and quotation omitted).

²⁰² FINRA Rule 2010.

Memorandum clearly contemplated that investors may have excess funds remaining in their capital accounts after paying their appropriate share of placement fees, securities purchase expenses, and general expenses. As demonstrated by Dubinsky, Enforcement’s expert, this scenario occurred with the First and Second Series investors. The Offering Memorandum required Taboada to return any such excess funds upon CMS’s dissolution. However, Taboada failed to do so. As Dubinsky calculated, Taboada used \$43,575 of excess capital from the First and Second Series investors to pay expenses that should have been paid by Third through Seventh Series investors.²⁰³ Taboada’s use of First and Second Series investor funds for this purpose violated the Offering Memorandum and was not authorized by First and Second Series investors.

With respect to investor securities, the Offering Memorandum stated that Facebook shares acquired for a particular series of investors belonged to those investors, and that any distribution of those shares had to be pro rata among all investors within the series. Taboada misappropriated securities from some investors by improperly distributing Facebook shares among CMS’s investors. Some investors received more shares than they should have, but other investors received fewer than they should have, based on their ownership percentage in their series.

Taboada’s intent to deprive investors of their funds and securities is evidenced by his conduct. He created (or caused to be created) the false and misleading Spreadsheet. The Spreadsheet falsely inflated the amount First and Second Series investors had paid to purchase ownership interests in Facebook securities, thereby erasing the surpluses from their capital accounts and giving the illusion that all of their capital had been expended. At the same time, the Spreadsheet falsely deflated the amount Third through Seventh Series investors paid to purchase ownership interests in Facebook securities, thereby erasing the deficits from their capital accounts and giving the illusion that they had paid their appropriate shares of CMS’s expenses. The evidence showed that many of these investors did not receive any extra Facebook shares to compensate them for the excess capital Taboada took from them, but actually received fewer shares than they were entitled to under the Offering Memorandum. Taboada also admitted that he made the decision to impose the unauthorized “carried interest” charge and improperly withheld more than 150 Facebook shares from four investors. Taboada admitted that those investors have not been made whole.

²⁰³ The Hearing Panel found the testimony of Enforcement’s expert, Dubinsky, helpful. The Panel accepted Dubinsky’s calculations and found them to be reliable. That said, the Panel found, and Dubinsky demonstrated, that the calculations were not complex. Rather, they entailed straightforward mathematical computations. Even Taboada’s expert stated that these calculations were mechanical computations. Tr. 1699.

Taboada received a benefit from his misappropriation.²⁰⁴ By taking funds from First and Second Series investors, Taboada avoided having to contribute his own funds to pay some of CMS's expenses, including the \$5,000 CMS paid to Charles Morgan in October 2012 for office expenses. Taboada also benefitted through Charles Morgan's receipt of the larger placement fees and "sales concessions" that were made possible by his misappropriation. For example, absent Taboada's misappropriation, Charles Morgan either would have had to reduce the placement fee it charged to the Fourth Series investors or accept a reduced sales concession on the Fourth Series' purchase of an interest in Opportunity. The Fourth Series investors contributed a total of \$627,000 in capital. Charles Morgan charged those investors a 10 percent placement fee (\$62,700), leaving \$564,300 in their capital accounts. Taboada then paid \$572,428.87 to purchase an interest in Opportunity for the Fourth Series. At Taboada's request, Felix charged a 10 percent commission on the Fourth Series transaction, half of which went to Charles Morgan as a sales concession. As structured, this transaction could not have occurred without Taboada's misappropriation of funds from First and Second Series investors because Fourth Series investors did not have sufficient capital for it. Therefore, Taboada either would have had to reduce either the size of Charles Morgan's placement fee or the size of the Fourth Series' investment in Opportunity, which would have reduced the size of the sales concession Charles Morgan received. As stated above, during the time of the Fourth Series investments, Charles Morgan was struggling to maintain its net capital.

3. Taboada's Arguments

Taboada argues that his conduct does not constitute misappropriation for several reasons. First, he argues that FINRA does not have jurisdiction to discipline him because FINRA Rule 2010 does not encompass his conduct. Second, he argues that he could not have misappropriated funds and securities from the CMS investors because the funds and securities belonged to CMS, not the individual investors. Lastly, Taboada argues that he properly allocated expenses and distributed the Facebook shares to the investors. For the reasons stated below, the Panel rejects each of Taboada's arguments.

²⁰⁴ Enforcement is not required to show that Taboada directly benefitted from his misappropriation of funds and securities in order to establish a violation of FINRA Rule 2010. *See Dep't of Enforcement v. Olson*, No. 2010023349601, 2014 FINRA Discip. LEXIS 7, at *12 n.13 (Bd. of Governors May 9, 2014) ("Even were we to assume that [respondent] did not profit from her misconduct, which we do not, it would not alter our assessment that barring [respondent] is in order."); *see also Janet Gurley Katz*, Exchange Act Release No. 61449, 2010 SEC LEXIS 994, at *47-48 (Feb. 1, 2010) (respondent misappropriated customer funds by transferring them between customer accounts without authorization in violation of NYSE Rule 476(a) prohibiting conduct inconsistent with just and equitable practice and trade); *Cathy Jean Krause Kirkpatrick*, 53 S.E.C. 918, 925 (1998) (respondent misappropriated customer funds by withdrawing customer funds to cover losses in other customers' accounts in violation of NYSE Rule 476(a) prohibiting conduct inconsistent with just and equitable practice and trade).

a. *FINRA Has Jurisdiction over Taboada’s Misconduct*

Taboada contends that FINRA lacks jurisdiction over his conduct related to CMS because his conduct is not securities-related. The National Adjudicatory Council recently addressed the scope of FINRA Rule 2010 in *Department of Enforcement v. Grivas*,²⁰⁵ a case involving similar facts to the instant case. In *Grivas*, the NAC affirmed FINRA’s jurisdiction, stating that FINRA Rule 2010 “is a broad and generalized ethical provision” that “is sufficiently wide to encompass any unethical, business-related conduct, regardless of whether it involves a security.”²⁰⁶

Similar to the respondent’s misconduct in *Grivas*, Taboada’s misconduct was both business- and securities-related, and thus within FINRA’s jurisdiction. Taboada formed CMS while he was registered at Charles Morgan. Taboada hired Charles Morgan to serve as CMS’s placement agent, and brokers at Charles Morgan solicited investors for CMS, including many Charles Morgan customers. Charles Morgan received more than \$500,000 in placement fees and sales concessions as a result of its relationship with CMS. The Facebook securities CMS acquired were held in a brokerage account at Blackwall until Taboada distributed them to investors with assistance from Blackwall employees. And, after the distribution was completed, Blackwall employees continued to assist Taboada with CMS, providing documents and information to JL while he was working on his Report. The Panel finds that Taboada’s conduct is within FINRA’s jurisdiction.

b. *Whether Investors Had a Property Interest in the Funds and Securities Is Not Relevant*

Taboada argues that he could not be liable for misappropriation because the funds and securities belonged to CMS, not the investors. This argument was also presented and rejected in *Grivas*. In *Grivas*, the hearing panel rejected the proposition that a registered person cannot misappropriate funds from investors unless the investors have a property interest in the funds. Like Taboada, the respondent in *Grivas* managed a special purpose entity organized as a limited liability company and was charged with misappropriating funds from investors. The respondent argued that he could not have misappropriated funds from investors because the funds at issue were the limited liability company’s property. The panel rejected the argument describing it as “a technical distinction without a difference in the context of this case....”²⁰⁷ The Panel finds that the same reasoning

²⁰⁵ *Dep’t of Enforcement v. Grivas*, No. 2012032997201, 2015 FINRA Discip. LEXIS 16 (NAC July 16, 2015).

²⁰⁶ *Id.* at *21-24.

²⁰⁷ *Dep’t of Enforcement v. Grivas*, No. 2012032997201, 2014 FINRA Discip. LEXIS 12, at *28 (OHO Feb. 14, 2014), aff’d, 2015 FINRA Discip. LEXIS 16 (NAC July 16, 2015).

applies here. “The gravamen of Enforcement’s complaint is that [Taboada] took monies invested in the Fund and used those monies for an unauthorized purpose.”²⁰⁸

c. *Taboada’s Allocations of Expenses and Securities Were Not Proper*

Taboada argues that he properly allocated the expenses and securities to the CMS investors. In support of his position, he argues that, as the manager of CMS, he had discretion to allocate expenses and Facebook shares. According to Taboada, he was therefore free to use monies from the First and Second Series investors to pay expenses owed by the Third through Seventh Series investors. While the Offering Memorandum allowed Taboada some discretion to allocate general expenses, Taboada testified (and told CMS investors) that he did not exercise that discretion, but rather allocated CMS’s general expenses pro rata among all of its investors.

Furthermore, the manner in which Taboada allocated expenses exceeded any limited discretion he may have had to allocate general expenses. Taboada used funds from First and Second Series investors to pay placement fees or securities purchase expenses (which are not general expenses) for investors in other series. As the above example regarding the Fourth Series reveals, the Fourth Series did not have sufficient capital to pay its placement fee to Charles Morgan and its securities purchase expense. Taboada used funds from First and Second Series investors to make up the shortfalls so the transactions could be completed. Nothing in the Offering Memorandum granted Taboada discretion to allocate to First and Second Series investors the placement fees and security purchase expenses owed by Fourth Series investors. Under the Offering Memorandum, each series was to be treated as a separate entity.

In further support of his argument that he properly allocated expenses and securities, Taboada presented expert testimony from Arthur J. Radin, a certified public accountant. Radin opined that Taboada properly allocated the CMS expenses and, when the reimbursement checks are taken into account, he also properly distributed the Facebook shares.²⁰⁹ In forming his opinions, Radin relied on JL’s Report.²¹⁰ Radin did not review any source materials, including the Spreadsheet or the Revised Spreadsheet.²¹¹ Rather, he simply accepted the numbers in JL’s Report and assumed that they were accurate.²¹²

²⁰⁸ *Grivas*, 2015 FINRA Discip. LEXIS 16, at *2.

²⁰⁹ Tr. 1607-08, 1613.

²¹⁰ Tr. 1611.

²¹¹ Tr. 1697-98, 1722.

²¹² Tr. 1676, 1693, 1722.

At the time Radin drafted his expert report and formulated his opinions, he was not aware of any errors in JL's Report.²¹³ Accordingly, Radin's report and his opinions therein do not address the errors in JL's Report. Radin acknowledged that the errors in JL's Report would impact the allocation of expenses and the distribution of shares to CMS investors.²¹⁴ For example, JL's Report imposed a carried interest charge on some investors.²¹⁵ Radin stated that this charge was appropriate, but he could not identify anything that authorized CMS to impose such a charge.²¹⁶ He acknowledged that charging carried interest had the effect of reducing the number of shares an investor would receive.²¹⁷ He further acknowledged that, if charging carried interest was improper, those investors would not have received their proper number of shares.²¹⁸

Other errors in JL's Report that impact the allocation of expenses and distribution of shares relate to the Felix commission charges. JL's Report did not reflect that (1) the Fourth Series investors paid a 10 percent commission to Felix in connection with their investment in CMS, or (2) the Seventh Series investors paid a 5 percent commission to Felix.²¹⁹ Radin was unaware of those commission charges, but acknowledged that those charges would reduce the number of shares for the Fourth and Seventh Series investors and increase the number of shares for investors in the other series.²²⁰

The Panel finds that Radin's opinions, which relied on JL's inaccurate Report, are unreliable.²²¹ Accordingly, the Panel rejects Radin's opinions.

d. *Conclusion*

The Panel concludes that Taboada violated FINRA Rule 2010 by misappropriating funds and securities from CMS investors. Specifically, Taboada failed to return excess capital to First and Second Series investors and failed to distribute to certain CMS investors all of the Facebook shares to which they were entitled.²²²

²¹³ Tr. 1664-65, 1700.

²¹⁴ Tr. 1663, 1674-75.

²¹⁵ Tr. 1645.

²¹⁶ Tr. 1645, 1647-49.

²¹⁷ Tr. 1647-48.

²¹⁸ Tr. 1663.

²¹⁹ Tr. 1670-75.

²²⁰ Tr. 1674-75.

²²¹ Tr. 1695-1700.

²²² Cf. *Lawrence R. Klein*, 52 S.E.C. 535 (1995) (respondent barred for transferring funds from one customer's account to another's without authorization).

B. Taboada Violated FINRA Rules 2150 and 2010 by Misusing Customer Funds and Securities

The second cause of action alleges that Taboada violated FINRA Rules 2150 and 2010 by misusing customer funds and securities. FINRA Rule 2150 states that “[n]o member or person associated with a member shall make improper use of a customer’s securities or funds.”²²³ Misuse of a customer’s funds occurs when a registered person fails to apply the funds or securities, or uses them for some purpose other than, as directed by the customer.²²⁴ Improper use of a customer’s funds is proscribed by FINRA Rules “without any express limitation on whether the customer is the customer of the associated person at the time of the improper use.”²²⁵

Here, 37 CMS investors, including several First and Second Series investors, were customers of Charles Morgan or Blackwall, or both. For the reasons discussed above regarding Taboada’s misappropriation of investor funds, the Panel concludes that Taboada also misused customer funds and securities by (1) improperly using excess capital from CMS investors who were also customers of Charles Morgan or Blackwall, without their authorization, to pay expenses owed by Third through Seventh Series investors, and (2) failing to distribute the proper number of Facebook shares to CMS investors who were customers of Charles Morgan or Blackwall.

C. Taboada Violated FINRA Rule 2010 by Causing Felix to Double Its Commission on CMS’s Investment to Benefit Charles Morgan; Failing to Disclose Charles Morgan’s Sales Concessions to CMS Investors; and Providing False and Misleading Information to CMS Investors

The third cause of action alleges that Taboada violated FINRA Rule 2010 in several ways when dealing with the CMS investors. Each is addressed separately below.

1. Taboada Caused Felix to Double Its Commission on CMS’s Investment in the Opportunity Transaction

Taboada asked Felix to double its commission on the Fourth Series’ investment in Opportunity, which increased the amount of Charles Morgan’s sales concession on the transaction and provided a financial benefit for Charles Morgan.

²²³ FINRA Rule 2150.

²²⁴ *Dep’t of Enforcement v. Mielke*, No. 2009019837302, 2014 FINRA Discip. LEXIS 24, at *43 (NAC Jul. 18, 2014); *Dist. Bus. Conduct Comm. v. Jones*, No. C02970023, 1998 NASD Discip. LEXIS 60, at *7 (NAC Aug. 7, 1998).

²²⁵ Cf. *Mike K. Lulla*, 51 S.E.C. 1036, 1039 (1994) (discussing the application of Section 19 of the NASD Manual prohibiting the improper use of customer funds).

Taboada argues that he did not cause Felix to double its commission because (1) he purportedly only asked about the increased commission, and (2) he did not have any authority to force Felix to double its commission. The Panel finds that Taboada not only initiated the idea, but made the final decision to have CMS pay twice the normal commission on the transaction.²²⁶

It is fundamental that a securities professional must deal with his investors and customers honestly and fairly and in accordance with the established standards of the business.²²⁷ By causing Felix to double its commission, which resulted in Charles Morgan receiving double its normal sales concession, the Fourth Series investors received fewer shares from their investment in CMS. The Panel determines that Taboada's conduct violates FINRA Rule 2010.

2. Taboada Failed to Disclose the Sales Concessions Charles Morgan Received on the Fourth and Seventh Series Facebook Transactions

Taboada did not disclose to the Fourth or Seventh Series investors the sales concessions Charles Morgan received on their investments in Opportunity and NYPA. At the time the Fourth and Seventh Series invested in CMS, Taboada was the sole owner of Charles Morgan. Charles Morgan, Taboada's broker-dealer, benefitted from the sales concessions associated with the Fourth and Seventh Series investments. The Panel determines that Taboada's failure to disclose this information was material. When deciding whether to invest in CMS, reasonable investors would have considered the fact that Taboada's financially troubled broker-dealer was receiving a sales concession as a result of their investment to be material.²²⁸ The Panel determined that Taboada's failure to disclose to the Fourth or Seventh Series investors the sales concessions Charles Morgan received constitutes a violation of FINRA Rule 2010.

3. Taboada Provided False and Misleading Information to Investors

Taboada distributed the Spreadsheet or the Revised Spreadsheet to several CMS investors. Both spreadsheets concealed Taboada's misappropriation of funds from First and Second Series investors by misrepresenting CMS's finances. Through the spreadsheets, Taboada misrepresented CMS's Facebook transactions and gave investors the false impression that (1) all CMS investors paid their appropriate share of the company's expenses, and (2) no investor had any capital surplus or deficit. Both spreadsheets also falsely represented that Fourth Series investors paid Felix a 5 percent

²²⁶ Cf. *Dep't of Enforcement v. Lipsky*, No. CAF970011, 1999 NASD Discip. LEXIS 54 (OHO June 18, 1999) (respondent violated NASD Rule 2110 by causing customers to pay excessive markups).

²²⁷ Cf. *Charles Hughes & Co., Inc. v. SEC*, 139 F.2d 434, 437 (2d Cir. 1943). According to the shingle theory, a broker-dealer impliedly represents at the outset of a securities transaction that it will deal with its customers fairly and in accordance with the standards of the industry. *Duker & Duker*, 6 S.E.C. 386, 388-89 (1939).

²²⁸ *Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988).

commission in Opportunity when, in fact, they paid a 10 percent commission at Taboada's request. As a result of the foregoing, Taboada violated FINRA Rule 2010.²²⁹

D. Taboada Violated FINRA Rules 8210 and 2010 by Providing a False Document and Testimony to FINRA

FINRA Rule 8210 requires a registered person to respond fully, completely, and truthfully to a request for information from FINRA.²³⁰ Providing false documents and testimony to FINRA violates Rule 8210.²³¹

Pursuant to Rule 8210, Taboada provided FINRA an invoice for \$5,000 from Charles Morgan to CMS dated January 2011. In April 2013, while under oath during his investigative testimony with Enforcement, Taboada falsely stated that the invoice had been created in January 2011. A year later during his investigative testimony in April 2014 and during the hearing, Taboada admitted that he actually created the invoice on March 22, 2013.

The Panel rejects Taboada's argument that his testimony was not false because the invoice he created in March 2013 was a replica of an original invoice he created in January 2011. As discussed above, the Panel did not find Taboada's testimony to be credible. Furthermore, there is no exception to Rule 8210 allowing a registered person to create a backdated replica of a document and then present that document to Enforcement as an original.²³² The Panel concludes that Taboada violated FINRA Rules 8210 and 2010 by providing false documents and testimony to FINRA.

IV. Sanctions

The Panel found Taboada liable for each cause of action in the Complaint, and determined that Taboada should be barred from association with any FINRA member firm.

A. Taboada's Violations of FINRA Rules 2150 and 2010

The Panel determined that Taboada violated FINRA Rule 2010 by misappropriating investor funds and securities as described in the first cause of action;

²²⁹ *Dep't of Enforcement v. Claggett*, No. 2005000631501, 2007 FINRA Discip. LEXIS 2, at *18 (NAC Sept. 28, 2007) ("The Commission consistently has ruled that the transmission of false documents to customers is conduct inconsistent with just and equitable principles of trade.").

²³⁰ FINRA Rule 8210.

²³¹ *Dep't of Enforcement v. Houston*, No. 2011028061001, 2015 FINRA Discip. LEXIS 21, at *16-17 (NAC Feb. 27, 2015).

²³² See *Dep't of Enforcement v. Mutual Serv. Corp.*, No. EAF0400630001, 2008 FINRA Discip. LEXIS 62, at *106-07 (OHO Dec. 16, 2008) (respondent violated FINRA Rule 8210 when it failed to disclose to Enforcement that it had provided backdated and corrected records), *aff'd*, 2010 FINRA Discip. LEXIS 12 (NAC Aug. 18, 2010), Exchange Act Release No. 65347, 2011 SEC LEXIS 3225 (Sept. 16, 2011).

and violated FINRA Rules 2150 and 2010 by misusing customer funds and securities as alleged in the second cause of action. The Panel also determined that Taboada violated FINRA Rule 2010 as alleged in the third cause of action by (1) causing Felix to double its commission on CMS’s investment in Opportunity, (2) failing to disclose the sales concessions that Charles Morgan received on the Fourth and Seventh Series Facebook transactions, and (3) providing false and misleading information to investors. The Panel imposed a unitary sanction for the first three causes of action because they all pertain to the manner in which Taboada dealt with the CMS investors.²³³ For those causes of action, the Panel determined that Taboada should be barred from associating with any FINRA member firm in any capacity. In reaching the sanctions determination, the Panel considered FINRA’s Sanction Guidelines (“Guidelines”), the Principal Considerations, and the lack of any mitigating factors.

1. The Sanction Guidelines

For the first two causes of action, misappropriation and misuse of funds and securities, the applicable guideline is “Conversion or Improper Use of Funds or Securities.” For conversion, the Guidelines recommend a bar regardless of the amount converted.²³⁴ For improper use of customer funds, the Guidelines direct adjudicators to consider a bar. Where the improper use resulted from a respondent’s misunderstanding of his customer’s use of the funds, or other mitigation exists, adjudicators should consider a suspension of six months to two years and thereafter until respondent pays restitution. The Guidelines also recommend a fine of \$2,500 to \$73,000.²³⁵

For the third cause of action, the two most analogous guidelines are “Excessive Commissions” and “Misrepresentations and Material Omissions.”²³⁶ The Guidelines for Excessive Commissions recommend a fine in the range of \$5,000 to \$146,000.²³⁷ In egregious cases, the Guidelines recommend consideration of a suspension up to two years or a bar.²³⁸ The Guidelines for “Misrepresentations and Material Omissions” draw a distinction between negligent and intentional misconduct. For negligent misconduct, the Guidelines recommend a fine of \$2,500 to \$73,000, and a suspension of up to two years.²³⁹ For intentional or reckless misconduct, the Guidelines recommend a fine of

²³³ See *Dep’t of Enforcement v. Fox & Co. Invs., Inc.*, No. C3A030017, 2005 NASD Discip. LEXIS 5, at *37 (NAC Feb. 24, 2005) (“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.”) (citation omitted), *aff’d*, Exchange Act Release No. 52697, 2005 SEC LEXIS 2822, at *36 (Oct. 28, 2005).

²³⁴ FINRA Sanction Guidelines at 36 (2015), <http://www.finra.org/industry/sanction-guidelines>.

²³⁵ *Id.*

²³⁶ *Id.* at 88, 90.

²³⁷ *Id.* at 90.

²³⁸ *Id.*

²³⁹ *Id.* at 88.

\$10,000 to \$146,000.²⁴⁰ They also recommend that the adjudicator strongly consider barring the respondent.²⁴¹ The Guidelines state that if mitigating factors predominate, an adjudicator should consider suspending the respondent for a period of six months to two years.²⁴²

2. The Principal Considerations

The Guidelines provide a list of factors that should be considered in conjunction with the imposition of sanctions with respect to all violations.²⁴³ Several aggravating factors are applicable here and support the imposition of a bar.

First, Taboada's misconduct was intentional.²⁴⁴ Taboada admitted that he made the decision to impose the unauthorized "carried interest" charge and improperly withheld more than 150 Facebook shares from four investors. Taboada also admits that those investors have not been made whole. Taboada misallocated CMS's expenses so that First and Second Series investors paid more expenses than they should have. Contrary to Taboada's assertions, many of these First and Second Series investors did not receive any extra Facebook shares to compensate them for the excess capital Taboada took from them, but actually received fewer shares than they were entitled to under the Offering Memorandum. When choosing between the "actual shares" numbers in the Revised Spreadsheet and share numbers from the original Spreadsheet, Taboada usually picked the lesser number of shares to distribute. Taboada admitted that, by early 2013, he knew that he had not distributed enough Facebook shares to many investors, but did nothing about it for over a year (until after Enforcement filed its Complaint). Rather than taking immediate corrective action, Taboada tried to conceal what he had done by sending investors the false and misleading Spreadsheet and falsely telling them that an accountant was reviewing the share distribution and that they would be made whole based on the accountant's findings.

Second, Taboada attempted to conceal his misconduct.²⁴⁵ Taboada distributed the false and misleading Spreadsheet or the Revised Spreadsheet to investors, which concealed his misappropriation of funds from the First and Second Series and the increased commission CMS paid on the Fourth Series' investment in Opportunity.

²⁴⁰ *Id.*

²⁴¹ *Id.*

²⁴² *Id.*

²⁴³ *Id.* at 6-7.

²⁴⁴ *Id.* at 7 (Principal Consideration No. 13).

²⁴⁵ *Id.* at 6 (Principal Consideration No. 10).

Third, Taboada injured investors.²⁴⁶ He misappropriated funds and Facebook shares from several investors in the First and Second Series and misappropriated Facebook shares from several other CMS investors.

Fourth, Taboada benefitted from his misappropriation.²⁴⁷ By taking excess capital belonging to First and Second Series investors and using it to pay expenses owed by Third through Seventh Series investors, Taboada avoided having to contribute his own money to pay those expenses. Moreover, the amount of the sales concessions Charles Morgan received from Felix depended on the amount of the investments in the Felix entities. The Fourth and Seventh Series could not have invested as much as they did in Opportunity or NYPA, and therefore Charles Morgan’s sales concessions would not have been as large as they were (at a time when it was struggling financially), if Taboada had not misappropriated funds belonging to other investors to cover some of the Fourth and Seventh Series’ expenses.

Fifth, Taboada engaged in a pattern of misconduct relating to CMS over an extended period of time.²⁴⁸ Between 2011 and 2013, Taboada (1) asked Felix to double its commission on CMS’s purchase of an interest in Opportunity in order to increase Charles Morgan’s sales concession on the transaction; (2) concealed, through the false and misleading Spreadsheet or the Revised Spreadsheet, the increased commission he caused Felix to charge Fourth Series investors on the investment in Opportunity; (3) failed to disclose the “sales concession” Charles Morgan received on CMS’s investments in Opportunity and NYPA; (4) misappropriated excess capital from First and Second Series investors to pay expenses owed by other investors; (5) distributed the false and misleading Spreadsheet or the Revised Spreadsheet that concealed his misappropriation of funds from First and Second Series investors; and (6) improperly withheld Facebook shares from investors by misallocating the shares and then by imposing an unauthorized “carried interest” charge.

Sixth, Taboada has not accepted responsibility for his misconduct,²⁴⁹ as demonstrated by his testimony at the hearing. Instead, he blamed his accountant, YS, for the misleading Spreadsheet. He blamed FINRA for his inadequate distribution of Facebook shares, claiming that FINRA pressured him to get the shares distributed. However, as Blackwall’s CCO explained, there was no pressure from FINRA to distribute the Facebook shares.

²⁴⁶ *Id.* (Principal Consideration No. 11).

²⁴⁷ *Id.* at 7 (Principal Consideration No. 17).

²⁴⁸ *Id.* at 6 (Principal Consideration No. 9).

²⁴⁹ *Id.* at 6 (Principal Consideration No. 2).

3. Lack of Mitigating Factors

Taboada has not presented any mitigation that warrants imposing any sanction less than a bar. First, his purported reliance on YS is not mitigating.²⁵⁰ Taboada was involved in creating the false accounting. Moreover, the calculations necessary to properly allocate CMS's expenses and distribute its Facebook shares were not complicated and did not require any level of accounting knowledge or skill. They were simple pro rata allocations based on transactions that Taboada personally negotiated. As Taboada's own expert stated, the allocation of expenses and distribution of shares were "mechanical computation[s]."²⁵¹ Most importantly, Taboada could not have reasonably relied on YS when he withheld information from him. For example, Taboada failed to inform YS about communications he had with Felix regarding the number of shares CMS would receive. On December 17, 2012, Felix emailed Taboada, informing him that CMS would be receiving additional shares; however, Taboada did not tell YS about those shares to enable YS to incorporate them into the Spreadsheet's share allocation.

Second, Taboada's distribution of cash to some investors in May 2014 is not mitigating.²⁵² This corrective action occurred *after* FINRA had issued its Wells notice and filed its Complaint, and therefore has no mitigative value.²⁵³

4. Conclusion

"Misappropriation or misuse of customer funds constitutes a serious violation of the securities laws, involving a betrayal of the basic and fundamental trust owed to a customer."²⁵⁴ The Panel concludes that a bar from associating with any FINRA member in any capacity is the appropriate remedial sanction.

B. Taboada's Violations of FINRA Rules 8210 and 2010

The Panel determined that Taboada violated FINRA Rules 8210 and 2010 by providing false information and testimony to FINRA, as alleged in the fourth cause of action. The Panel also determined that Taboada should be barred for this violation.

²⁵⁰ *Id.* (Principal Consideration No. 7).

²⁵¹ Tr. 1699.

²⁵² Guidelines at 6 (Principal Consideration No. 4).

²⁵³ See, e.g., *Raymond M. Ramos*, 49 S.E.C. 868, 871-72 (1988) ("There can be no justification for the misappropriation of a customer's funds, and the fact that [respondent] ultimately paid the money back does not warrant permitting his return to the securities business where he poses a threat to other investors."); *Daniel D. Manoff*, 55 S.E.C. 1155, 1165-66 (2002) (subsequent repayment of funds in case involving unauthorized use of co-worker's credit card is not mitigating).

²⁵⁴ *Blair Alexander West*, Exchange Act Release No. 74030, 2015 SEC LEXIS 102, at *33-34 (Jan. 9, 2015) (citations omitted).

For failing to respond to a Rule 8210 request, or failing to respond truthfully, the Guidelines recommend a fine in the range of \$25,000 to \$73,000, and state that a bar should be standard.²⁵⁵ The Guidelines direct adjudicators to consider the “[i]mportance of the information requested as viewed from FINRA’s perspective.”²⁵⁶ Here, Taboada provided false documents and testimony to FINRA regarding a \$5,000 payment he had made from CMS to Charles Morgan. This information was important because FINRA was investigating Taboada’s management of CMS, including his payment of CMS’s expenses, and whether investors had received all of the Facebook shares to which they were entitled. Taboada was aware of the nature of FINRA’s investigation when he provided the false document and testimony.

The Panel found no mitigating factors. Although Taboada later admitted that he created the invoice at the time he responded to the FINRA Rule 8210 request, his admission occurred *after* Taboada had received a Wells notice from Enforcement, indicating its intention to bring charges against Taboada, including the charge for violating Rule 8210 by providing false information and testimony to FINRA.

The Panel determines that the information Enforcement sought from Taboada was important to its investigation and Taboada’s violation of FINRA Rule 8210 was egregious. The Panel concludes that a bar is the appropriate remedial sanction.

V. Order

Respondent Paul E. Taboada violated (1) FINRA Rule 2010 by misappropriating investor funds and securities; (2) FINRA Rules 2150 and 2010 by misusing customer funds and securities; (3) FINRA Rule 2010 by providing false and misleading information, and failing to disclose information, to investors regarding expenses such as commissions and sales concessions; and (4) FINRA Rules 8210 and 2010 by providing false and misleading testimony and documents to FINRA.²⁵⁷

For the above misconduct, the Extended Hearing Panel bars Taboada from associating with any FINRA member in any capacity. In addition, Taboada is ordered to pay the costs of this proceeding in the amount of \$14,078.07, which includes an administrative fee of \$750 and hearing transcript costs of \$13,328.07.

²⁵⁵ Guidelines at 33.

²⁵⁶ *Id.*

²⁵⁷ The Hearing Panel considered all of the parties’ arguments. They are rejected or sustained to the extent that they are inconsistent with the views expressed herein.

These sanctions shall become effective on a date set by FINRA, but not earlier than 30 days after this Decision becomes the final disciplinary action of FINRA.

Maureen A. Delaney
Hearing Officer
For the Extended Hearing Panel