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

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| DEPARTMENT OF ENFORCEMENT,<br><br>Complainant,<br><br>v.<br><br>JOHN CARRIS INVESTMENTS, LLC (CRD No. 145767),<br><br>GEORGE CARRIS, (CRD No. 3079577),<br><br>ANDREY TKATCHENKO, (CRD No. 2712245),<br><br>JASON BARTER, (CRD No. 2552583),<br><br>and<br><br>RANDY HECHLER, (CRD No. 2292597),<br><br>Respondents. | Disciplinary Proceeding No. 2011028647101<br><br>Hearing Officer–MAD<br><br>**AMENDED EXTENDED HEARING PANEL DECISION**[1]<br><br>January 20, 2015 |

**Respondents John Carris Investments, LLC ("JCI") and George Carris: (1) willfully violated Securities Exchange Act of 1934, Section 10(b), Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by knowingly or, at a minimum, recklessly selling securities issued by JCI's parent company on the basis of false statements of material fact and misleading omissions of material fact (Second Cause of Action); (2) violated NASD Rule 2310, and FINRA Rules 2111 and 2010, by recommending the purchase of securities issued by JCI's parent company to customers without a reasonable basis (Fifth Cause of Action); and (3) willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by manipulating the price of Fibrocell Science, Inc. stock through prearranged trading and improperly placing stock in customer accounts to maintain the price at an artificial level (First Cause of**

[1] The Extended Hearing Panel Decision is amended to reflect the correct CRD numbers of the Respondents.

**Action). For the above misconduct, JCI is expelled from FINRA membership and Carris is barred from association with any FINRA member firm in any capacity.**

**JCI and Carris also committed the following violations for which additional sanctions are not ordered in light of the sanctions ordered in connection with the fraud and suitability violations:**

- **Respondent Carris violated NASD Rule 3110, and FINRA Rules 4511 and 2010, from January 1, 2010 through December 31, 2011, by causing JCI to create and maintain inaccurate books and records in violation of Section17(a) of the Exchange Act and Rule 17a-3 thereunder; and JCI violated NASD Rule 3110, and FINRA Rules 4511 and 2010, and willfully violated Exchange Act Section 17(a) and Rule 17a-3 thereunder, by creating and maintaining inaccurate books and records (Sixth Cause of Action);**

- **JCI and Carris violated FINRA Rule 2010, by failing to remit employee payroll taxes to the United States Treasury and other taxing authorities (Eleventh Cause of Action);**

- **Carris violated FINRA Rule 2010, by causing JCI to operate without sufficient net capital; and JCI willfully violated Exchange Act Section 15, Rule 15c-3, *et seq.* thereunder, and FINRA Rule 2010, by operating without sufficient net capital (Tenth Cause of Action);**

- **JCI and Carris violated FINRA Rules 3310 and 2010, by failing to implement Anti-Money Laundering policies and procedures that can be reasonably expected to detect and cause the reporting of suspicious transactions (Eighth Cause of Action); and**

- **JCI and Carris violated FINRA Rules 3010 and 2010, by failing to establish, maintain, and enforce a reasonable supervisory system (Ninth Cause of Action).**

**Respondent Andrey Tkatchenko violated NASD Rule 2310, and FINRA Rules 2111 and 2010, by recommending the purchase of securities issued by JCI's parent company to customers during the ongoing offerings without a reasonable basis (Fifth Cause of Action). For this misconduct, he is fined $10,000 and suspended from association with any FINRA member in all capacities for two years.**

**Respondent Jason Barter willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by manipulating the price of Fibrocell stock through prearranged trading (First Cause of Action). For this misconduct, he is fined $5,000, suspended from association with any FINRA member in all capacities for 18 months, and required to re-qualify by examination as a registered representative before he re-enters the securities industry in any capacity.**

**The evidence did not support the following charges, which are dismissed:**

- **The Third Cause of Action alleging that JCI willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by failing to disclose material, adverse conflict of interest information to JCI customers who were purchasing Fibrocell stock.**

- **The Fourth Cause of Action alleging that Carris willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by aiding and abetting securities fraud in connection with JCI's sale of Fibrocell stock.**

- **The Seventh Cause of Action alleging that Carris and JCI violated FINRA Rule 2010, by (i) failing to issue year-end tax forms, Forms W-2, for years 2009 and 2010; and (ii) issuing a false Form W-2 for 2011 that underreported Carris' compensation.**

- **The Ninth Cause of Action alleging that Hechler violated FINRA Rules 3010 and 2010, by failing to establish, maintain, and enforce a reasonable supervisory system. This charge is dismissed solely with respect to Respondent Hechler.**

**Respondents JCI, Carris, Tkatchenko, and Barter are ordered to jointly and severally pay the costs of this proceeding.**

## Appearances

Michael J. Watling, Esq., Kristina Juntunen, Esq., Mark Maldonado, Esq., Susan Light, Esq., for the Department of Enforcement, Complainant.

Christopher P. Greeley, Esq., for Respondents John Carris Investments and George Carris.

Michael P. Gilmore, Esq., for Respondents Andrey Tkatchenko and Jason Barter.

Respondent Randy Hechler, pro se.

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## DECISION

### I. INTRODUCTION

FINRA's Department of Enforcement brought this proceeding against the above five Respondents: former FINRA member firm John Carris Investments, LLC ("JCI"); George Carris, JCI's president and Chief Executive Officer ("CEO"); Jason Barter, JCI's trader; Andrey Tkatchenko, a JCI registered representative; and Randy Hechler, JCI's Chief Compliance Officer ("CCO") during the last year and a half that the firm was in operation. Enforcement alleges that Respondents violated certain FINRA and NASD Rules, and provisions of the Securities Exchange Act of 1934 (Exchange Act), which included securities fraud.

### II. BACKGROUND AND PROCEDURAL HISTORY

Carris founded and controlled JCI, a small broker dealer. He also simultaneously founded and controlled JCI's parent company, Invictus Capital, Inc. (Invictus). Invictus' sole purpose was to raise capital for JCI through self-offerings of debt and equity securities. JCI was the only source of revenue for Invictus.

Carris established JCI to operate as a broker-dealer that would retail corporate equity securities and provide investment banking services to development stage companies. From June 2009 through October 2012, JCI provided investment banking services for Fibrocell Science, Inc. (Fibrocell). JCI acted as an exclusive placement agent or lead placement agent on several private placements for Fibrocell. During a portion of that time, Fibrocell was publicly traded on the Over-the-Counter Bulletin Board ("OTCBB") system.

This disciplinary proceeding arose after an examination of the firm that led to an investigation into FINRA's concerns regarding: (i) JCI's sale of Invictus securities

through the use of offering documents that FINRA believed contained false statements and material omissions; and (ii) JCI's trading in Fibrocell. FINRA staff concluded from its investigation that JCI committed securities fraud when selling Invictus securities and trading Fibrocell securities.

Upon completion of its investigation, Enforcement filed a nine-count Complaint on June 7, 2013. Each Respondent filed an Answer and requested a hearing. Enforcement requested expedited treatment of the case, and, at the suggestion of the parties, the hearing was set in January 2014.

On September 17, 2013, Enforcement filed a motion to amend the Complaint, seeking to add two new causes of action: (i) another fraud cause of action against JCI relating to sales of Fibrocell securities held by firm principals while representatives of JCI were soliciting customers to purchase Fibrocell, and (ii) an aiding and abetting charge against Carris relating to the new fraud cause of action. In addition, Enforcement sought to add Hechler, the CCO at the time of the Fibrocell sales, as a respondent and supplement its supervisory cause of action to include allegations of supervisory failures by Hechler. The Hearing Officer granted Enforcement's motion,[2] and Enforcement filed

[2] Enforcement understood that, although they requested expedited treatment of the case, the filing of the Amended Complaint, which added a respondent, required postponing the hearing to ensure that the new respondent could have a sufficient opportunity to review the discovery and participate in the complete pre-hearing process.

the Amended Complaint on September 30, 2013.[3] All of the Respondents filed answers to the Amended Complaint.

The Amended Complaint contains 11 causes of action, relating to the following topics: (i) the operation of JCI, (ii) Invictus securities, (iii) Fibrocell, and (iv) anti-money laundering ("AML") and supervisory systems and procedures at JCI. Regarding the operation of JCI, the Amended Complaint alleges that JCI and Carris: (i) used firm funds to pay personal expenses of firm principals, (ii) failed to provide tax forms and provided inaccurate tax forms to a firm principal, (iii) failed to remit employee payroll taxes to the government after representing to its employees that it had withheld those funds from their pay, and (iv) operated a securities business without sufficient net capital. Regarding Invictus securities, the Amended Complaint alleges securities fraud in connection with the Invictus Offerings and that the firm sold Invictus securities without a reasonable basis. Regarding Fibrocell securities, the Amended Complaint alleges securities fraud in connection with the trading and sales of Fibrocell stock. Lastly, regarding JCI's supervisory system and policies, the Amended Complaint alleges that JCI failed to establish, maintain, and enforce a reasonable supervisory system and an AML compliance program. Each of the charges in the Amended Complaint is delineated below.

JCI's Operations

- Carris violated NASD Rule 3110, and FINRA Rules 4511 and 2010, from January 1, 2010 through December 31, 2011, by causing JCI to create and maintain inaccurate books and records in violation of Section 17(a) of the Exchange Act

[3] When filing the Amended Complaint, Enforcement also filed a request for a temporary cease and desist order ("TCDO"). Respondents consented to the request, and the Panel issued the Consent Order for the TCDO on October 14, 2013. The TCDO ordered Respondents to cease soliciting customer purchases of securities in which JCI or its principals have an economic interest unless JCI fully discloses such interest. The TCDO remains in place. On April 28, 2014, during the hearing, JCI ceased operations completely and filed a Uniform Request for Broker-Dealer Withdrawal ("Form BDW").

and Rule 17a-3 thereunder. JCI also violated NASD Rule 3110, and FINRA Rules 4511 and 2010, and willfully violated Exchange Act Section 17(a) and Rule 17a-3 thereunder, by creating and maintaining inaccurate books and records. (Sixth Cause of Action).

- Carris and JCI violated FINRA Rule 2010, by failing to issue year-end tax forms, Forms W-2, for the years 2009 and 2010; and issuing a false Form W-2 for 2011 that underreported Carris' compensation. (Seventh Cause of Action).

- Carris and JCI violated FINRA Rule 2010, from May 2010 through December 2012, by failing to remit employee payroll taxes to the United States Treasury and other taxing authorities. (Eleventh Cause of Action).

- Carris violated FINRA Rule 2010, by causing JCI to operate without sufficient net capital. JCI willfully violated Exchange Act Section 15, Rule 15c-3, *et seq*. thereunder, and FINRA Rule 2010, by operating without sufficient net capital between November 1, 2011 and August 6, 2012. (Tenth Cause of Action).

Sales of Invictus Securities

- Carris and JCI willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, from October 2010 through September 2012, by defrauding customers in connection with the sale of Invictus stock and notes. The Amended Complaint alleges that Carris failed to disclose the financial condition of Invictus and JCI, failed to disclose his personal use of firm funds, and misled investors regarding Invictus' financial condition by paying dividends to Invictus investors with funds contributed by new investors. (Second Cause of Action).[4]

- Carris, Tkatchenko, and JCI violated NASD Rule 2310, and FINRA Rules 2111 and 2010, from October 2010 through the filing of the Amended Complaint (the "Offering Period"), by recommending the purchase of Invictus stock and notes to customers during the ongoing offerings without a reasonable basis. (Fifth Cause of Action).

Trading and Sales of Fibrocell

- Carris, Barter, and JCI willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by engaging in manipulative stock trading of Fibrocell while JCI was acting as a placement agent for Fibrocell. Specifically, the Amended Complaint alleges that, from May 1, 2010 through September 30, 2010 (the "Manipulation Period"), Carris and Barter manipulated

[4] The failure to disclose the poor financial condition of JCI included Carris' failure to inform investors that JCI was out of net capital compliance. Amended Complaint ("Am. Compl.") ¶¶ 59, 152.

the price of Fibrocell in order to create the false appearance of trading volume and to maintain the share price at an artificial level. (First Cause of Action).

- JCI willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by failing to disclose material, adverse conflict of interest information to JCI customers who were purchasing Fibrocell. Specifically, the Amended Complaint alleges that, from May 3 through May 21, 2013 (the "Liquidation Period"), JCI committed securities fraud by failing to notify its customers that Carris and DB, another principal at JCI, were selling personally held shares of Fibrocell common stock while representatives of JCI were soliciting its customers to buy shares of Fibrocell common stock. (Third Cause of Action).

- Carris willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by aiding and abetting the securities fraud during the Liquidation Period. (Fourth Cause of Action).

AML and Supervisory Systems and Procedures

- Carris and JCI violated FINRA Rules 3310(a) and 2010, from May 2010 through May 2011 (the "AML Period"), by failing to establish and implement AML policies and procedures that can be reasonably expected to detect and cause the reporting of suspicious transactions. (Eighth Cause of Action).

- Carris, Hechler, and JCI violated FINRA Rules 3010 and 2010, by failing to establish, maintain, and enforce a reasonable supervisory system. (Ninth Cause of Action).

The Extended Hearing Panel (Panel) conducted a hearing in New York, New York, from April 28 through May 15, 2014. On August 1, 2014, the parties filed post-hearing briefs and findings of fact with the Office of Hearing Officers.

Based on a preponderance of the evidence, the Hearing Panel makes the following findings of fact and conclusion of law.

## III. FINDINGS OF FACT

### A. Respondents[5]

#### 1. John Carris Investments

In May 2009, Carris purchased a defunct broker-dealer and changed the name to John Carris Investments, LLC.[6] Carris established JCI to: (i) operate as a broker-dealer retailing corporate equity securities in the over-the-counter market, and (ii) offer private placements of securities.[7] JCI was a small broker dealer; and initially, Carris was the only employee.[8] JCI was a FINRA-registered broker-dealer from June 2009 through April 2014, when it filed a Form BDW with FINRA.[9]

#### 2. George Carris

Carris has worked in the securities industry for 15 years.[10] From June 2009 through April 2014, Carris was registered with FINRA as a General Securities Representative and a General Securities Principal through his association with JCI.[11]

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[5] JCI was a FINRA member firm at the time of the alleged misconduct and remained a FINRA member firm until the end of April 2014. CX-4; CX-5; Tr. (Carris) 450. Carris, Barter, Tkatchenko, and Hechler were registered with FINRA through their association with JCI through the end of April 2014. CX-8, CX-10, CX-12, CX-13. Accordingly, FINRA has jurisdiction over all of the Respondents as they were registered with FINRA at the time of the alleged misconduct. *See* FINRA By-Laws Art. IV, Sections 1, 6; By-Laws Art. V, Sections 2, 4.

[6] CX-8; CX-3, at 2.

[7] CX-3, at 2, 7-8.

[8] Tr. (Carris) 944. By the end of 2010, JCI had approximately ten employees, including approximately six registered representatives. Tr. (Tkatchenko) 1618; CX-150A, at 20. In April 2011, JCI had 23 employees. CX-141, at 2. By 2014, JCI grew to approximately 60 employees. Tr. (Tkatchenko) 1618.

[9] Tr. (Carris) 450; CX-4; CX-5.

[10] CX-8, at 10. Prior to his employment at JCI, Carris was registered with at least three other FINRA member firms. CX-8, at 4-7.

[11] CX-8, at 3.

At JCI, Carris held a number of supervisory roles. Carris was the president through September 2012, and the CEO until at least mid-March 2014.[12] As president and CEO, Carris was responsible for ensuring overall supervision of JCI.[13] He required JCI employees, including himself, to read and sign a new-hire compliance agreement.[14]

Carris was also the CCO and Anti-Money Laundering Compliance Officer ("AMLCO") from JCI's inception through August 23, 2010.[15] As CCO, he was responsible for JCI's compliance program.[16] His AMLCO compliance duties included reviewing trading activity in low-priced securities.[17] Carris was also the designated supervisor for retail sales through mid-August 2011.[18] In his capacity as CCO, Carris supervised ten registered representatives, and as the supervisor for retail sales, he supervised seven registered representatives.[19]

Despite Carris' important supervisory roles at JCI, throughout the hearing, he attempted to distance himself from the operation of JCI and claimed to be unaware of many of the issues alleged in the Amended Complaint. The Hearing Panel did not find Carris credible.[20]

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[12] CX-5, at 4-5; CX-8, at 7; Tr. (Carris) 177-78.

[13] Tr. (Carris) 214.

[14] Tr. (Carris) 695-99; CX-8A, at 52-60; CX-12A, at 2-10.

[15] Tr. (Carris) 178-79, 211, 213-14. Thereafter, Brian Simmons, another principal at JCI, replaced Carris as CCO and held that position until JCI hired Hechler in December 2012. Tr. (Carris) 230-31, 241-42, (Hechler) 3104.

[16] CX-150, at 269.

[17] Tr. (Carris) 241-42.

[18] CX-150, at 19; CX-150A, at 20; CX-150B, at 21 (identifying another principal as head of Retail Sales beginning in mid-August 2011); Tr. (Carris) 225.

[19] CX-150, at 19; Tr. (Carris) 225-26.

[20] In the Decision, the Hearing Panel provides specific examples that demonstrate Carris' lack of credibility.

### 3. Andrey Tkatchenko

Tkatchenko entered the securities industry in 1996.[21] From October 2010 through April 2014, he was registered with FINRA as a General Securities Representative and a General Securities Principal through his association with JCI.[22] Tkatchenko joined JCI after discussions with Carris.[23] Carris agreed to pay Tkatchenko a $300,000 signing bonus, and Tkatchenko agreed to work for Carris at JCI for four years.[24]

### 4. Jason Barter

Barter first became registered in the securities industry as a General Securities Representative through his association with a FINRA member firm in June 1995.[25] In 1999, he obtained his Series 55 license, which enabled him to be an Equity Trader Limited Representative.[26] Barter has been employed as an Equity Trader since 2001.[27] From July 2009 through April 2014, Barter was registered with FINRA as a General Securities Representative, Equity Trader, and General Securities Principal through his association with JCI. [28]

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[21] CX-10, at 14; Tr. (Tkatchenko) 1305.

[22] CX-10, at 2-3; Tr. (Tkatchenko) 1305-06. Tkatchenko's firm representative code was JI14. Tr. (Tkatchenko) 1313.

[23] Tr. (Tkatchenko) 1308-09.

[24] Tr. (Tkatchenko) 1324-25.

[25] CX-12, at 13.

[26] CX-12, at 13.

[27] Tr. (Barter) 2051; CX-12, at 4.

[28] CX-12, at 3; Tr. (Barter) 2052-53.

Barter was JCI's first employee; Carris hired him to be JCI's head trader.[29] Shortly after Barter began working at JCI, he signed JCI's new-hire compliance agreement, in which he agreed not to enter orders of substantially the same size, at substantially the same time and substantially the same price, for the purpose of creating a false or misleading appearance of active trading in a security or a false or misleading appearance with respect to the market security.[30] At JCI, registered representatives did not have the ability to enter orders for purchases or sales of securities directly. Rather, they had to complete trade tickets and deliver them to Barter, who reviewed the tickets and sent the orders to market makers for execution.[31] JCI did not have an active Trading Department. Typically, Barter entered 15 or fewer trades per day relating to a handful of securities.[32] Barter was JCI's only trader.[33]

[29] Tr. (Carris) 947, (Barter) 2060-62; CX-150, at 19, 282 (identifying Barter as "head trader" responsible for equity trading); CX-150A, at 19 (listing Barter as "head trader"). Carris had known Barter for approximately 13 years before he hired him. Tr. (Carris) 945-46.

[30] CX-12A, at 4, 10; Tr. (Carris) 695-98, (Barter) 2054-59.

[31] Tr. (Carris) 667-69. In the case of OTCBB stocks, a manager such as Carris needed to review and initial the order ticket after the registered representative prepared it. Tr. (Carris) 668-69. The order ticket would be delivered to Barter after the manager's review. Tr. (Carris) 669. After Barter sent orders to a market maker, JCI received a trade confirmation including the customer's name, the broker representative number, the date and time of the transaction, and the security and price. The confirmation was sent to the customer and a copy was retained by JCI. Tr. (Carris) 675-76.

[32] *See generally* RX-39; *see also* CX-141, at 2 ("the firm executed approximately 15 trades a day"); Tr. (Carris) 661-62 (stating JCI sent 5 to 10 order tickets to the market maker a day).

[33] Tr. (Barter) 2049 (Barter "was the firm's sole trader."); Tr. (Barter) 2087-94 (acknowledging his prior sworn testimony that he was the only person entering trades until Simmons began working at JCI on August 23, 2010). Although one of Simmons' licenses was a Series 55, enabling him to be an Equity Trader, his only roles at JCI were CCO, AMLCO, and municipal securities principal. PX-1, at 15; Tr. (Simmons) 2200.

Barter was also responsible for supervising all over-the-counter equity trading.[34] Pursuant to JCI's written supervisory procedures ("WSPs"), Barter had an obligation to monitor trading activity to prevent market manipulation, which could include prearranged trades, wash sales, or parking of securities.[35] Barter was responsible for identifying "fictitious sales" and "transactions of the same security at the same time for the same price."[36]

### 5. Randy Hechler

Hechler has been registered in the securities industry for more than 20 years.[37] Hechler has worked in a compliance function for more than ten years, and has spent almost ten years as a CCO.[38]

From December 2012 through April 2014, Hechler was registered with FINRA through his association with JCI. [39] At JCI, he was the CCO and was responsible for overall supervision of JCI's compliance programs.[40] His registrations included: General Securities Representative, General Securities Principal, Equity Trader, Investment Banking Representative, Research Analyst, and Operations Professional.[41]

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[34] CX-150, at 19; CX-150A, at 20; CX-150B, at 21; CX-150C, at 23; CX-150D, at 23; CX-150E, at 23; Tr. (Barter) 2062-63.

[35] CX-150, at 19, 282, 344-45; CX-150A, at 20; Tr. (Barter) 2062-64, 2075-78.

[36] CX-12A, 4; CX-150, at 344-45; Tr. (Barter) 2059, 2075-78.

[37] CX-13, at 2-7; Tr. (Hechler) 3111.

[38] CX 13, at 8; Tr. (Hechler) 3111.

[39] Tr. (Hechler) 3104; CX-13, at 2-3.

[40] Tr. (Hechler) 3128-29.

[41] CX-13, at 2-3, 15-16; Tr. (Hechler) 3112-16.

### B. JCI's Parent Company: Invictus

Invictus was JCI's parent company from June 2009 through April 2014.[42] Until at least April 2013, Carris owned 100% of the issued and outstanding common shares of Invictus and was its sole officer and director. [43]

As a typical holding company, Invictus had no employees, generated no independent revenue, and owned no physical assets.[44] Its only business purpose was to raise capital for JCI through self-offerings of debt and equity securities; and JCI, the subject of the Invictus self-offerings, was the sole source of revenue for Invictus. [45] Carris controlled both entities and he considered their funds to be "the same basket of cash."[46]

[42] On or about June 11, 2009, Carris, acting on behalf of both Invictus and Invictus Capital LLC ("Invictus LLC"), entered into a Membership Purchase Agreement whereby Invictus became the sole indirect owner of JCI. CX-14; CX-5, at 5; Tr. (Carris) 187-88 (Carris was JCI's CEO, COO and CCO at the time JCI's parent company Invictus acquired JCI on June 11, 2009), 196-98 (Carris signed on behalf of all entities as 100% owner). After executing this agreement, there were three distinct entities in the ownership structure of JCI. Carris owned 100% of Invictus, while Invictus became the sole owner of Invictus LLC, and Invictus LLC became the sole owner of JCI. CX-14; Tr. (Carris) 200-02 (Carris was issued 800,000 shares of Invictus common stock).

[43] Tr. (Carris) 201-04; CX-95, at 23, 51. Carris personally established bank accounts for Invictus using his home address. Tr. (Carris) 206-08; CX-108, CX-109. Carris controlled these Invictus bank accounts by possessing signature, wire, and check writing authority. Tr. (Carris) 210.

[44] Tr. (Carris) 203, 209-10, 256.

[45] Tr. (Carris) 203-04, 210-11 (admitting that there were no other revenues going into the Invictus bank accounts other than capital deposits and that those deposits were transferred into the JCI account), 253-54, 256, 399-400 (money raised by Invictus offerings went to JCI), 1015; CX-104 – CX-106.

[46] Tr. (Carris) 1016.

### C. JCI's Financial Condition

JCI generated revenues from the sale of Invictus self-offerings and its investment banking and trading.[47] From JCI's inception, its operating expenses exceeded its total revenues, resulting in annual net losses, which increased every year except 2013. In 2009, JCI had a net loss of $2,328.[48] In 2010, its net loss was $785,292.[49] In 2011 and 2012, JCI's net loss was $3,106,664 and $3,660,715 respectively.[50] JCI's net loss decreased to $2,155,394 in 2013.[51]

#### 1. JCI's Inaccurate Books and Records as a Result of Carris' Use of JCI Funds

Carris personally established a business bank account for JCI that gave him signature, wire, check writing, and debit card authority.[52] He used the JCI bank account to receive JCI business revenue and pay JCI expenses.[53] Carris also established a JCI corporate credit card for his sole use.[54]

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[47] Tr. (Carris) 209-10 (admitting that the Invictus 2010 and 2011 bank accounts at CX-108 and CX-109 were used to deposit funds gained from investors who paid for Invictus securities and the funds were then transferred to JCI bank accounts to pay for JCI operating expenses), 406 (affirming that any earnings from Fibrocell were deposited into the JCI bank account, not the Invictus accounts, and no monies were transferred from the JCI account to the Invictus accounts).

[48] CX-112, at 6.

[49] CX-113, at 5.

[50] CX-114, at 7; CX-114A, at 8.

[51] CX-114B, at 8.

[52] Tr. (Carris) 204-05.

[53] Tr. (Carris) 205.

[54] Tr. (Carris) 205-06.

Carris used JCI's debit and credit cards for his personal expenses.[55] He began this practice from the time he established JCI and continued it through the end of 2013.[56] As expenses were incurred, they were entered into JCI's general ledger, which was organized by coded business expense categories.[57]

This activity was uncovered when FINRA conducted an examination of JCI's books and records in 2011.[58] In July 2011, FINRA staff questioned numerous expenses that appeared on JCI's general ledger that had no apparent business purpose.[59] For example, FINRA questioned the business purpose for expenses incurred at motorcycle retailers, firearms retailers, tattoo parlors, pet grooming establishments, dry cleaners, clothing retailers, and numerous other vendors whose business was not related to the operation of a broker-dealer. In response, in mid-2012, JCI provided FINRA with a spreadsheet of expenses incurred in 2010 and 2011 that were initially booked as business expenses, but were later "reclassified" as "owner's draws."[60] In total, JCI reclassified over $590,000 of business expenses, which were actually Carris' personal expenses that were paid by JCI, in part from revenues attributable to the Invictus offerings.[61]

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[55] Tr. (Carris) 468-69, 494-96; CX-97, CX-98. From October 2010 through December 2011, Carris used over $454,882 of JCI funds for non-business purposes, including making cash withdrawals or writing checks to cash. CX-99, at 1; *see generally* CX-99.

[56] Tr. (Carris) 469-75, 494-96.

[57] Tr. (Carris) 467-68. At the end of the year, the general ledger was provided to JCI's auditor to prepare the audited financial statements. Tr. (Carris) 468.

[58] Tr. (Carris) 494.

[59] CX-220, at 2. In the July 2011 Rule 8210 request letter, FINRA staff also inquired about Invictus, its finances, and the Series A and B self-offerings. CX-220, at 4-6. The letter was hand-delivered to JCI. CX-220, at 1. Both Carris and Simmons, the CCO, acknowledged receipt of the letter by signing it on July 12, 2011. CX-220, at 7.

[60] CX-99; Tr. (Carris) 512, 1094-95.

[61] CX-97 – CX-99; Tr. (Carris) 209-10, 465-68, 517.

Carris explained that, from June 2009 through the third quarter of 2011, MG, a JCI employee who handled administrative matters in the back office, was responsible for properly characterizing charges in JCI's general ledger.[62] Carris stated that he expected MG to properly characterize his personal charges on the JCI credit card in JCI's general ledger.[63] He stated that the credit card statement provided her with a basis to characterize the charge in JCI's general ledger.[64] There was no evidence that Carris completed expense reports and Carris admitted that he provided MG with "very few" receipts because MG "should have a very clear understanding" from the credit card statement.[65] However, the JCI corporate credit card statement only identified a vendor and an amount.[66]

### 2. JCI's Failure to Issue Tax Forms and Issuance of an Inaccurate Tax Form

From JCI's inception in May 2009, through May 2012, Carris received compensation, wages, and advances from JCI, as well as distributions from Invictus totaling approximately $757,288.[67] As discussed above, separate and apart from those monies were Carris' non-business expenses that JCI paid in 2010 and 2011, totaling over $590,000.[68]

In 2009 and 2010, JCI failed to issue Carris any Forms W-2 for wages or other compensation, and Carris reported no wage income on his federal and state tax returns for

[62] Tr. (Carris) 1087-88.

[63] Tr. (Carris) 1089-90.

[64] Tr. (Carris) 1266-68.

[65] Tr. (Carris) 1267-68.

[66] Tr. (Carris) 1267-68.

[67] CX-100, at 1.

[68] CX-100, at 1.

those two years.[69] In 2011, JCI issued a Form W-2 to Carris that reported his total wages and other compensation as $150,416.[70]

Carris explained that, although he signed his personal tax returns, he did not review them.[71] He stated that, for each tax year between 2009 and 2011, the JCI office staff organized his tax materials and an accountant prepared his tax returns.[72]

### 3. JCI's Failure to Pay Employee Payroll Taxes

JCI withheld payroll taxes, including Social Security and Medicare taxes, from its employees.[73] During 2009 through 2011, JCI issued Forms W-2 to its employees notifying them that their payroll taxes, including Social Security and Medicare taxes, had been withheld from their income.[74] Carris acknowledged that JCI withheld such taxes for all its employees and understood that JCI was responsible for collecting and paying these taxes for all JCI employees to the appropriate taxing authorities.[75]

In early 2011, JCI stopped making full payments to various taxing authorities for its employees' payroll taxes. On August 29, 2011, JCI's payroll service provider sent an email to MG, alerting her that JCI had not been paying payroll taxes and could be "open

[69] See CX-126 (containing no Forms W-2 issued to Carris for 2009 and 2010); Tr. (Carris) 557.

[70] CX-126, at 64.

[71] Tr. (Carris) 543-45.

[72] Tr. (Carris) 541-45, 1099-100. Carris also stated that he has not been audited or received any correspondence from the Internal Revenue Service ("IRS") regarding his personal tax returns for years 2009 through 2011. Tr. (Carris) 1100.

[73] *See generally* CX-126.

[74] CX-126.

[75] Tr. (Carris) 565-66.

to liabilities from your employees, fed and state."[76]

On October 17, 2011, Carris and MG received an email from the payroll service provider, titled "Overdue Payroll Taxes," stating that JCI was still not paying its employees' payroll taxes and the unpaid balance at that point in time exceeded $634,000.[77]

On December 2, 2011, and January 5, 2012, the payroll service provider again emailed Carris and another JCI employee regarding the unpaid payroll taxes.[78] On January 19, 2012, the payroll service provider emailed JCI's Chief Financial Officer ("CFO") to schedule a conference call with Carris and the CFO.[79]

In early April 2012, JCI's accountant emailed the CFO inquiring if JCI had received any IRS notices for the unpaid taxes and informing him about the IRS's calculation of penalties for unpaid payroll taxes.[80]

Although Carris was aware of JCI's obligation to pay its employees' payroll taxes, Carris failed to ensure that JCI paid the taxes.[81] Instead, JCI continued to carry the deficiency as a liability on its balance sheet.[82] At the end of 2012, JCI had an outstanding

[76] CX-131; Carris stated that, in 2009, 2010, and the first three quarters of 2011, MG was responsible for the payment of JCI's payroll taxes. Tr. (Carris) 1101. Carris claims that MG did not inform him that JCI was delinquent in paying federal payroll taxes, state payroll taxes, or MCTMT payroll taxes. Tr. (Carris) 1103, 1105.

[77] CX-132; *see* CX-114, at 6 (JCI's 2011 year-end liabilities in the amount of $626,360 approximates the payroll taxes owed by JCI).

[78] CX-133; CX-134. The December 2, 2011 email also included MG. The January 5, 2012 email included JCI's CFO.

[79] CX-135.

[80] CX-136; Tr. (Carris) 593-95.

[81] Tr. (Carris) 565-66, 588-89.

[82] Tr. (Carris) 596.

payroll tax liability of $536,930,[83] and at the end of 2013, the payroll tax liability was $611,529.[84]

Carris stated that he did not receive any emails sent by JCI's payroll service provider regarding JCI's failure to properly remit employee payroll taxes, and the payroll service company never contacted him directly by telephone to inform him that JCI was delinquent in satisfying its payroll tax obligations.[85] While Carris admitted the October 17, 2011 email was sent to his business email address at johncarrisinvestments.com, he claimed that he first learned that JCI was delinquent in satisfying its payroll obligations in the first or second quarter of 2012 when he was shown JCI's audited financial statement.[86] Although Carris maintained business and personal email accounts, and gave those email addresses to outside service providers, he claimed that it was not his practice to read or send emails.[87] Carris stated that other JCI employees had access to his JCI email account and would send and receive emails on his behalf.[88] The Panel did not find

[83] CX-114A.

[84] CX-114B.

[85] Tr. (Carris) 1102-03, 1105.

[86] Tr. (Carris) 572-73, 1107-08.

[87] Tr. (Carris) 1117, 1122.

[88] For example, Carris explained that other individuals sent a July 12, 2010 email, which was sent from his JCI email account. Tr. (Carris) 812-16 (referring to email at CX-81).

Carris credible.[89]

### 4. JCI's Net Capital Deficiencies

JCI was required to maintain a minimum net capital of $100,000.[90] At all relevant times, JCI designated a Financial and Operations Principal ("FINOP").[91] JCI's WSPs stated that its FINOP was responsible for calculating and monitoring JCI's net capital, as well as filing any Rule 17a-11(b) Net Capital Deficiency Financial Notices (Deficiency Notices) if necessary.[92]

JCI, through its designated FINOP, filed several Deficiency Notices indicating that it was out of net capital compliance.[93] JCI never ceased operations when it was net

[89] The evidence does not support Carris' assertion that he never received or read his emails. First, the July 12, 2010 email, referenced in footnote 85 above, was sent to one of Carris' customers and referenced a conversation between Carris and the customer. Tr. (Carris) 814-16; CX-81. Second, the evidence also showed that Carris used a personal email address to conduct business. In June 2009, Carris used his personal email to send a customer information concerning Fibrocell. CX-84. On September 9, 2010, one of Carris' customers sent him an email regarding a Fibrocell transaction, which was sent to Carris at both his business and personal email accounts. CX-220, at 12. In October and December 2011, Carris received messages from JCI's payroll service provider at both his business and personal email addresses. CX-132, CX-133; Tr. (Carris) 1102-04. When confronted with these emails, Carris claimed that a friend set up the personal email account in 2004 or 2005 so that Carris could "get on the Play Station and also some other games that I was playing at the time." Tr. (Carris) 1104. Third, Carris used an iPhone to send emails. CX-84, CX-270. On December 30, 2010, he sent an email message from his Iphone, signing the email "Love you -G." CX- 270.

[90] Tr. (Carris) 883. JCI acknowledged its obligation to maintain this level of net capital in its regularly filed FOCUS reports. Tr. (Carris) 879-80.

[91] Tr. (Carris) 3526. Carris did not serve as CFO or FINOP. *See* CX 150, at 19 (BZ designated as CFO and FINOP); CX-150A, at 20 (SH designated as CFO and FINOP); CX-150B, at 21 (RK designated as CFO and SH designated as FINOP).

[92] CX-150A, at 80; CX-150B, at 58; CX-150C, at 99; CX-150D, at 99; CX-150E, at 100.

[93] CX-157 – CX-159E. Carris was not identified on any Deficiency Notices as a JCI member contact.

capital deficient.[94] Instead, JCI filed Deficiency Notices once it cured the deficiency.[95] Each Deficiency Notice is addressed separately below.

First Deficiency Notice: *November 1, 2011 – March 19, 2012*

On March 23, 2012, JCI filed the first Deficiency Notice with FINRA stating JCI operated with insufficient net capital from November 1, 2011 through March 19, 2012.[96] The amount of the deficiency was $332,266.[97] JCI corrected the deficiency by infusing $788,000 into the firm; it raised the $788,000 through Invictus self-offerings.[98]

The filing of the Deficiency Notice originated from frustration on the part of JCI's FINOP. On March 22, 2012, JCI's FINOP sent an email to JCI's CFO, titled "Concerned FINOP," informing him that JCI was out of net compliance and "has been since at least the end of February maybe earlier."[99] The FINOP stated, "[u]nless you call me with the reasons why you believe this is not the case the rules also require that the firm immediately ***CEASE*** all security business until the net capital has been restored."[100] The FINOP told the CFO that he had "tried to discuss this with George [Carris] and he was non responsive."[101] The next morning on March 23, the FINOP forwarded the "Concerned FINOP" email to JCI's FINRA Regulatory Coordinator stating that he was giving him a "heads up" and letting him know that he was "deeply disturbed at the lack

[94] Tr. (Carris) 908-09.

[95] CX-157 – CX-159E.

[96] CX-157.

[97] CX-157, at 3.

[98] CX-157, at 3; Tr. (Carris) 883-88.

[99] CX-156, at 3-4.

[100] CX-156, at 4 (emphasis in original).

[101] CX-156, at 4.

of response as of this morning to my letter [email] to JCI."[102] The FINRA Regulatory Coordinator then forwarded the email to his supervisor, the surveillance manager within FINRA Regulation.[103] The FINRA surveillance manager then forwarded the "Concerned FINOP" email chain to JCI's CFO requesting that JCI's net capital computation be provided that day, along with documentary evidence that funding came into the firm to cure any deficiency.[104] JCI's CFO replied to FINRA's surveillance manager attaching the following supporting documentation: Invictus bank activity, JCI bank deposits, and meeting minutes for the capital contributions.[105]

The documents provided by JCI's CFO reflected that Carris was aware of the net capital deficiency and participated in restoring JCI's net capital position by authorizing the capital contributions using monies raised from the Invictus investors. The $788,000 used to cover the net capital deficiency came into the firm from Invictus investors between March 2 and March 15, 2012. As each investment flowed into Invictus, Carris used the funds for capital contributions to correct JCI's net capital deficiency. On March 2, 2012, two Invictus investors jointly purchased a $188,000 note issued by Invictus.[106] On March 9, 2012, Carris, as the "sole director" of JCI, held a special meeting and authorized the funds to be used as a capital contribution for JCI.[107] On March 9 and March 12, 2012, two Invictus investors each purchased $50,000 of preferred shares in an

[102] CX-156, at 3.

[103] CX-156, at 2-3.

[104] CX-156, at 2.

[105] CX-156, at 1.

[106] CX-107A.

[107] CX-156, at 6.

Invictus Offering.[108] Then, Carris authorized the $100,000 to be used as capital contributions for JCI on March 12 and March 13.[109] On March 15, an Invictus investor purchased $500,000 of preferred shares in an Invictus Offering; four days later, Carris authorized the infusion of the $500,000 into JCI as a capital contribution.[110]

Although the March 23 Deficiency Notice stated that JCI first discovered the net capital deficiency on March 22, 2012, Carris' infusions of capital to correct the deficiency began on March 9, 2012.[111] Indeed, instead of ceasing operations as JCI's FINOP stated in his email, Carris caused the firm to continue operating and used the monies generated from the sales of Invictus securities to cure JCI's net capital deficiency.[112]

Second Deficiency Notice: *July 1 - 24, 2012*

On August 14, 2012, JCI filed a second Deficiency Notice with FINRA stating JCI operated with insufficient net capital from July 1 through July 24, 2012.[113] JCI's management made a capital infusion of $147,000 to bring JCI into compliance.[114] The source of funds for the $147,000 infusion was raised through an Invictus investor.[115]

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[108] CX-107, at 8.

[109] CX-156, at 7-8.

[110] CX-107, at 8; CX-156, at 9.

[111] *See* CX-156 (JCI informing FINRA that capital infusion began on March 9, 2012).

[112] Tr. (Carris) 893-94, 908-09.

[113] CX-158.

[114] CX-158, at 3.

[115] CX-106, at 1; Tr. (Carris) 893-94.

Third Deficiency Notice: *August 6, 2012*

On August 17, 2012, JCI filed a third Deficiency Notice with FINRA stating JCI operated with insufficient net capital on August 6, 2012.[116] JCI's management made a capital infusion of $75,000 to bring JCI into compliance.[117] Again, JCI used $75,000 of Invictus funds to restore its net capital position.[118]

Additional Deficiency Notices

JCI filed additional retrospective Deficiency Notices with FINRA on the following dates: October 15, 2013, November 22, 2013, January 27, 2014, and February 4 and 11, 2014.[119] Those Deficiency Notices reflected that JCI continued to conduct a securities business when out of net capital compliance during the following time periods: (i) January 1 through October 14, 2013; (ii) June 1 through October 22, 2013; (iii) October 22, 2013 through January 23, 2014; (iv) February 3, 2014; and (v) February 10, 2014.[120]

Even as JCI was undercapitalized, it raised money through its Invictus offerings.[121] Over $1 million of the funds used to correct the net capital deficiencies were directly attributable to Invictus investors.[122]

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[116] CX-159.

[117] CX-159, at 3.

[118] CX-106, at 1; Tr. (Carris) 895-97.

[119] CX-159A – CX-159E.

[120] CX-159A – CX-159E. CX-159B states that JCI was out of net capital compliance from June 11, 2011 (not 2013); however, that appears to be a typographical error in light of the prior Deficiency Notices.

[121] Tr. (Carris) 911-12; *see* CX-107, at 4, 8; CX-107A.

[122] Tr. (Carris) 910-11.

### D. Issuance and Sales of Invictus Securities

JCI sold a series of securities offerings issued by its parent company Invictus, including offerings of notes.[123] Funds raised through the private offerings were used to operate JCI. When investors purchased shares of Invictus, the money was deposited in an Invictus bank account and then transferred to a JCI bank account in order to satisfy obligations at the broker-dealer level.[124]

For each Invictus offering, JCI was the exclusive placement agent.[125] Carris caused the Invictus offering materials to be prepared, and Carris reviewed and approved them prior to their use to solicit investors.[126] Carris also created a financial incentive for his registered representatives to sell Invictus. JCI registered representatives got a 60% payout on commissions that ranged from zero to three percent.[127] However, when selling the Invictus offerings, JCI registered representatives received 10% of the gross proceeds as commissions.[128] JCI retained the remaining 90% of the gross proceeds from the Invictus sales.[129]

The Invictus private debt and equity self-offerings raised approximately $11 million for Carris and JCI.[130]

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[123] All of the offering documents identified the investments as securities. CX-92, at 8; CX-93, at 9; CX-94, at 26; CX-95, at 29; CX-96, at 25.

[124] Tr. (Carris) 1015.

[125] Tr. (Carris) 257; *see, e.g.*, CX-95, at 44; CX-96, at 29.

[126] Tr. (Carris) 255 (Series A private placement memorandum); Tr. 276-77 (all offering documents); Tr. 383 (Series B private placement memorandum); Tr. 422-23 (Bridge Offering subscription documents).

[127] Tr. (Tkatchenko) 1327-28, 1363-64.

[128] Tr. (Carris) 257, (Tkatchenko) 1474.

[129] Tr. (Carris) 257.

[130] Tr. (Carris) 3615-16.

### 1. Series A Offering

In June 2009, Carris created a Confidential Private Offering Memorandum ("PPM") that offered accredited investors shares of Series A Preferred Stock of Invictus.[131] The Series A PPM described JCI as a "financial services company that specializes in high growth opportunities" focusing on retail brokerage services and investment banking and advisory services for small companies.[132] The Series A Offering offered investors convertible preferred shares priced at $25.00 per share, with a minimum purchase of 10,000 shares.[133] The Series A Offering contained a conversion provision that allowed investors to convert preferred shares to common stock on a dollar-for-dollar basis with no preferential treatment in the event of a liquidation.[134] Carris owned 800,000 common shares of Invictus when the Series A Offering opened; the liquidation provision made all preferred shareholders subordinate to Carris.[135] From October through December 2010, JCI raised approximately $822,975 from 16 investors in the Series A Offering.[136]

Risk Factors

In the section titled "Risk Factors," the Series A PPM stated that "[w]e have incurred and may continue to incur losses and our business will have no revenue unless and until operations commence."[137] Later, the PPM described JCI as a "development stage company, and we have had no revenue from operations" and that "[s]ince inception,

[131] CX-92; Tr. (Carris) 255.

[132] CX-92, at 7.

[133] CX-92, at 2; Tr. (Carris) 257-58, 259 (Carris intended to raise a minimum of $250,000 and a maximum of $5 million in the Series A Offering).

[134] CX-92, at 8; Tr. (Carris) 265-66.

[135] Tr. (Carris) 267.

[136] CX-107; Tr. (Carris) 283.

[137] CX-92, at 12.

we have incurred a substantial net loss" and "we expect that we will incur losses at least until we are fully operational as a broker-dealer . . . We may not realize any revenue unless and until we successfully begin to operate as a broker-dealer. . . . [o]ur business is difficult to evaluate because we have no operating history."[138]

These statements were not accurate at the time the first customer invested in the Series A Offering on October 5, 2010, nearly 16 months after Carris prepared the Series A PPM**.** [139] Contrary to the statements in the PPM, JCI was generating revenue and incurring operating expenses. Eight months earlier, in February 2010, JCI received its 2009 audited financial statements.[140] The 2009 financial statements reported $649,012 in revenues and $651,273 in operating expenses.[141] In addition, JCI's monthly FOCUS reports, filed with the Securities and Exchange Commission ("SEC") by its FINOP, reflected revenues and operating expenses each month in 2010.[142] None of the information from the 2009 audited financial statements or the year-to-date FOCUS reports for 2010 was provided to investors in the Series A PPM.[143]

JCI's net losses were also increasing. Its 2009 financial statement reported a net loss of $2,328.[144] In the third quarter of 2010, JCI incurred a net loss of $54,000; and in

[138] CX-92, at 12.

[139] CX-107; Tr. (Carris) 289-90 (JCI solicited customers to invest in the Series A Offering from October 5 through December 29, 2010), 293.

[140] CX-112; Tr. (Carris) 297-99 (admitting that an accounting firm provided the 2009 audited financial statements to JCI on February 19 and April 30, 2010, prior to the first Series A Offering sale on October 5, 2010).

[141] CX-112, at 6.

[142] CX-264, at 33-96.

[143] Tr. (Carris) 299; *see generally* CX-92.

[144] CX-112, at 6.

October 2010, when JCI made its first sale of the Series A Offering, JCI's monthly net loss was greater than $283,000.[145]

Use of Proceeds

The "Use of Proceeds" section in the Series A PPM stated that investor funds would be used "primarily for additional working capital and other general corporate expenses."[146] Instead, Carris used investor funds for his personal expenses and dividends for the Series A Offering investors (discussed more fully below under "Dividends").[147]

While investors contributed capital through the Series A Offering, Carris used investor funds for personal expenses, including expenses at wine and liquor stores, clothing store, dry cleaners, as well as numerous expenses described in JCI's books only as "cash."[148] By mid-November 2011, Carris knew that numerous personal expenses were improperly booked on JCI's general ledger as business expenses.[149] Despite that knowledge, Carris continued to charge his personal expenses to JCI and to use his JCI-issued credit and debit cards for non-business purposes.[150]

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[145] CX-264, at 70, 78.

[146] CX-92, at 24; Tr. (Carris) 529-30 (Carris admitted that the Use of Proceeds section did not include non-business expenses.

[147] CX-97; CX-98; CX-99; CX-100.

[148] CX-97; CX-98; CX-99; CX-100; Tr. (Carris); Tr. 527-28 (Carris affirming that during 2010 and 2011, JCI was selling the Series A, Series B, and Bridge Notes Offerings and simultaneously reclassifying the personal expenses that had been coded as business expenses).

[149] Tr. (Carris) 1215, 1217-18.

[150] Tr. (Carris) 506-07 (acknowledging that he used JCI corporate credit and debit cards to make cash withdrawals from ATM machines, to stream movies through a Playstation in an office conference room, and to charge personal non-business meals); Tr. 1213-15.

Dividends

The Series A, and each of the subsequent preferred stock offerings, contained two dividend features.[151] First, the PPM provided for a 4% cash dividend, payable at the discretion of Invictus' board of directors (i.e., Carris).[152] Second, the PPM provided for a discretionary cash dividend tied to profit derived from the securities received by JCI as part of its compensation for investment banking activity.[153] The PPM stated that any determination to pay dividends would be dependent upon "our financial condition, results of operations, capital requirements and such other factors as the Board deems relevant."[154] It further stated that dividends would only be paid from "legally available funds."[155] All dividend payments were made at Carris' sole discretion.[156]

On January 15, 2011, Carris determined that Invictus would pay a 1% per-share dividend to the Series A investors.[157] Carris acknowledged that JCI was unprofitable when he decided that Invictus would make the initial dividend payment to the Series A investors.[158] The January 2011 dividends were: (i) paid from an Invictus bank account; and (ii) funded entirely by Series A Invictus investors' investment contributions.[159] Money was not moved from JCI to Invictus to pay those dividends because the entities were under common control, and the funds were considered to be "the same basket of

[151] CX-92, at 26.

[152] CX-92, at 8, 26.

[153] CX-92, at 8; Tr. (Carris) 263-64.

[154] CX-92, at 26.

[155] CX-92, at 26.

[156] CX-92, at 8; Tr. (Carris) 263-64, 282.

[157] CX-107, at 1; Tr. (Carris) 289-90, 301-02, 381.

[158] Tr. (Carris) 379-81.

[159] Tr. (Carris) 209-10, 302, 1016.

cash."[160] After Carris made all the January 2011 dividend payments, the balance in the Invictus account was $667.08.[161]

On February 25, 2011, Carris received JCI's audited financial statements for 2010.[162] In 2010, JCI had total revenues of $1,935,064, but a total net loss of $785,292.[163] Nonetheless, Carris paid dividends to the Series A investors on four additional dates: April 15, 2011, July 15, 2011, October 15, 2011, and January 15, 2012.[164] In addition to Carris' knowledge of JCI's finances, when he made the decision to pay the January 15, 2012 dividend, he was also aware (as discussed above) that FINRA had recently questioned the classification of certain expenses on JCI's general ledger.

**2. Series B Offering**

Carris created a PPM for Series B preferred shares of Invictus, dated January 24, 2011.[165] The Series B PPM contained the same two dividend features as Series A, but changed the preferred-to-common stock conversion ratio to significantly reduce the Series B investors' ownership interest upon conversion.[166] JCI began selling shares of the Series B Invictus self-offering on March 8, 2011.[167] From that date through November 17,

[160] Tr. (Carris) 1016.

[161] *Compare* CX-107, at 1 *with* CX-109, at 4-6 (payments were made through the end of February 2011); Tr. (Carris) 302.

[162] Tr. (Carris) 379.

[163] CX-113, at 5; Tr. (Carris) 379-81.

[164] CX-107, at 1.

[165] CX-93; Tr. (Carris) 383.

[166] CX-93, at 9. The effect of this change in conversion ratio meant that a Series B investor who purchased $80,000 of preferred shares and then converted them to common shares would own the same number of common shares as a Series A investor who only paid $10,000. Tr. (Carris) 384-89.

[167] CX-107, at 2.

2011, JCI raised approximately $3,324,500 from 43 investors in the Series B offering.[168] Over $1.2 million raised in the Series B offering was from Series A investors who had been receiving dividends from the Series A offering.[169]

Risk Factors

Similar to the Series A PPM, the section titled "Risk Factors" in the Series B PPM stated, "[w]e have incurred and may continue to incur losses and our business will have no revenue unless and until operations commence."[170] Later, the PPM described JCI as a "development stage company", having "no revenue from operations."[171] The PPM also stated that "[s]ince inception, we have incurred a substantial net loss" and "we expect that we will incur losses at least until we are fully operational as a broker-dealer."[172]

Even though JCI had been in operation for 19 months, and it had the 2010 audited financial statements in its possession prior to the opening of the Series B offering, the Series B PPM contained no financial statements or other detailed financial information concerning JCI.[173] Series B investors were not provided JCI's 2009 or 2010 audited financial statements, which showed that it incurred net losses of $2,328 and $785,292, respectively.[174]

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[168] CX-107, at 3-4; Tr. (Carris) 394.

[169] *Compare* CX-107, at 1 *with* CX-107, at 2-4; Tr. (Carris) 401.

[170] CX-93, at 13.

[171] CX-93, at 13.

[172] CX-93, at 13.

[173] *See generally* CX-93; Tr. (Carris) 390-94, 421.

[174] CX-112, at 6; CX-113, at 5.

Use of Proceeds

The section titled "Use of Proceeds" stated that Series B investor funds would be used "primarily for additional working capital and other general corporate expenses."[175] However, Carris used investor funds in the Series B offering for personal expenses, including expenses described in its books only as "cash" and undescribed expenses classified as employee gifts.[176] All of these expenses were falsely classified as business expenses in JCI's books and records, and none were among the uses disclosed to investors.[177] In addition, despite the fact that JCI was operating at a loss at the end of 2010 and every month during 2011, Carris nonetheless paid dividends to the Series A and B investors.[178]

Dividends

When drafting the Series B PPM, Carris changed the Dividend section from the same section in the Series A PPM by stating that the Series A investors had received dividend payments.[179] The rest of the Dividends section in the Series B PPM was identical to the Series A PPM.[180] As reflected in JCI's FOCUS reports, JCI was not profitable in any single month during 2011.[181] In addition, its 2011 audited financial

[175] CX-93, at 26.

[176] CX-99; CX-100; Tr. (Carris) 506-07.

[177] CX-97 – CX-99.

[178] CX-113, at 5; CX-107, at 1-3.

[179] CX-93, at 28.

[180] CX-93, at 28.

[181] CX-264, at 102, 110, 118, 126, 134, 150, 158, 166, 174, 190, 246; Tr. (Carris) 1206-12. The November 2011 FOCUS report is not contained in CX-264. CX-264 mistakenly contains the November 2010 FOCUS report. Accordingly, the losses described above for November 2011 are estimated based on the October 2011 FOCUS report and the FOCUS report of the last quarter of 2011.

statements reflected a net loss of $3,106,664.[182] Despite JCI's bleak financial situation, Carris paid dividends to the Series B investors on April 15, 2011, July 15, 2011, October 15, 2011, and January 15, 2012, totaling $72,290.[183] As Carris acknowledged, these dividends were not paid from JCI profits but rather from funds deposited by new Invictus investors.[184]

### 3. Bridge Offering

In mid-July 2011, FINRA was investigating JCI and had inquired about Invictus and its Series A and B self-offerings.[185] In the midst of FINRA's open investigation, Carris created another offering for Invictus: the issuance of promissory notes (the "Bridge Offering"), dated December 1, 2011.[186] The Bridge Offering provided investors with a one-year 9% annual interest promissory note plus 20% of the investors' principal investment at the one year purchase anniversary.[187]

Unlike the Series A and B PPMs, the Bridge Offering subscription documents contained updated financial information for JCI.[188] When soliciting investors for the Bridge Offering, Invictus, through JCI, sent letters to the Series B investors.[189] The letters described the Bridge Offering and enclosed the Bridge Offering subscription

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[182] CX-114, at 7; Tr. (Carris) 408-09.

[183] *See* CX-107, at 2; Tr. (Carris) 412-15 (JCI's salaries and related expenses for 2011 were $2.1 million and commission expenses were $888,000. Carris admits that salary and commission expenses alone exceeded total Firm revenue for 2011 and dividends were still paid).

[184] Tr. (Carris) 405-06.

[185] CX-220.

[186] *Compare* CX-220 (dated July 11, 2011) *with* CX-234 (Rule 8210 response letter dated June 20, 2012); CX-96.

[187] CX-96, at 25; Tr. (Carris) 424-26.

[188] CX-96.

[189] *See, e.g.*, RX-6, at 3-7.

documents.[190] The letters also advised investors that it had "determined that there were purported deficiencies in certain disclosures set forth in the B Memorandum which could be considered insufficient and/or misleading disclosure."[191] The letters included a confirmation letter for the Series B investors to return, indicating that they confirmed their previous investment in the Series B Offering. [192] When the Series B investors received the letter and Bridge Offering documents, they had already received at least three dividend payments in connection with their prior Invictus preferred stock investments.[193]

While the Bridge Offering documentation contained updated financial information about JCI, neither the letter nor the subscription documents disclosed that JCI was out of net capital compliance.[194] Carris created the Bridge Offering on December 1, 2011, and JCI had been out of net capital compliance since November 1, 2011.[195] The Series A and B Offerings contained a section titled "Net Capital Requirements."[196] However, when Carris created the Bridge Offering, he removed the net capital section.[197] Indeed, throughout the time that JCI sold the Bridge Offering notes, it was out of net capital compliance.[198]

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[190] RX-6, at 3-7.

[191] RX-6, at 4.

[192] RX-6, at 6.

[193] CX-107, at 1-4; CX-107A. Many Bridge Offering investors were prior Series A and Series B investors who had received dividends in connection with their prior Invictus preferred stock investments. *Compare* CX-107, at 1-4 *with* CX-107A.

[194] RX-6; CX-96.

[195] CX-96, at 1; CX-157.

[196] CX-92, at 23; CX-93, at 25.

[197] *Compare* CX-92, at 23 and CX-93, at 25 *with* CX-96.

[198] *Compare* CX-157 *with* CX-107A.

The Use of Proceeds section also continued to omit information regarding how the proceeds would be used. According to the Bridge Offering documents, the proceeds of the Bridge notes were only to be used for business expenses.[199] However, Carris used the Bridge Offering investors' funds for his personal expenses and for personal expenses of other JCI employees.[200] While investors contributed capital through the Bridge Offering, Carris spent their investment funds on personal expenses, such as expenses at toy stores and clothing stores, as well as expenses described in JCI's books only as "cash."[201] Despite the fact that JCI continued to incur even greater losses, Carris also used Bridge Offering investors' funds to pay dividends to the Series A and B investors.[202] And, as discussed above, Carris used funds from Invictus investors to cure JCI's net capital deficiencies.[203] The description of expected uses of proceeds did not mention that proceeds would be used for personal expenses, dividend payments to investors of previous offerings, or capital contributions to cure JCI's net capital deficiencies.[204]

From December 5, 2011, through March 2, 2012, JCI sold approximately $2 million Bridge Offering notes to 27 investors.[205] As of March 31, 2013, all Bridge

[199] CX-96, at 24; Tr. (Carris) 449-50.

[200] CX-97; CX-98; CX-99; Tr. (Carris) 506-07.

[201] CX-97; CX-98; CX-99.

[202] *Compare* CX-107A (reflecting Bridge note investments from December 5, 2011 through March 2, 2012) *with* CX-107, at 1-4 (reflecting dividend payments to Series A and B investors on January 15, 2012). JCI's FOCUS report for the last quarter of 2011 reflected a net loss of greater than $1.2 million. CX-264, at 190. JCI's 2012 audited financials reflected a net loss of greater than $3.6 million. CX-114A, at 8.

[203] *See supra* footnotes 105 and 106 and accompanying text reflecting $188,000 from Bridge Offering investors applied to net capital deficiency.

[204] CX-96, at 24.

[205] CX-107A; Tr. (Carris) 433-34.

Offering notes had matured and were in default.[206] As previously noted, JCI filed a Form BDW on April 29, 2014.[207]

#### 4. Series C Offerings

Carris created two separate sets of subscription documents for two Series C preferred stock offerings of Invictus: the First Series C PPM, dated March 9, 2012, and the Second Series C PPM, dated April 3, 2013.[208]

First Series C Offering

The First Series C Offering was structured similarly to the Series A and Series B offerings. It contained the same eight-for-one conversion formula as the Series B Offering.[209]

Like the Bridge Offering subscription documents, the First Series C PPM contained updated financial information about JCI.[210] However, it too failed to include a net capital requirements section. When Carris created the first Series C Offering on March 1, 2012, and JCI made its first sale on March 9, 2012, JCI had been out of net capital compliance since November 1, 2011.[211] As of the date of the first Series C Offering sale, Carris was clearly aware that JCI was out of net capital compliance

[206] CX-95, at 8; Tr. (Carris) 450 (the Bridge Offering notes went into default and remain in default as of the date of his hearing testimony).

[207] Tr. (Carris) 450 (there was an open Series C Offering through the date JCI filed the Form BDW).

[208] CX-94, CX-95; Tr. (Carris) 452.

[209] CX-94, at 27; Tr. (Carris) 459-60.

[210] CX-94, at 1.

[211] CX-94, at 1; CX-107, at 8; CX-157.

because that day he had authorized a capital infusion of $188,000 using funds from an investor in the Bridge Offering.[212]

The Use of Proceeds section stated that investor funds would be used for general corporate expenses, and notified investors that proceeds could be used to pay dividends to investors in the Series A and B Offerings.[213] While Carris added the new language to inform potential investors that proceeds could be used for dividend payments, he continued to omit any reference to the use of proceeds for personal expenses or capital contributions to cure JCI's net capital deficiencies. From March 9 to May 1, 2012, Carris' expenses included, but were not limited to, funds described in JCI's books as "cash" and home improvement store expenses.[214] These expenses were classified as business expenses in JCI's books but were not among the uses disclosed to investors.[215] As discussed above, Carris applied the proceeds from the first Series C Offering sales between March 9 and March 15, 2012, totaling $600,000, to JCI's net capital deficiencies.[216]

The First Series C Offering contained the same two dividend features that were present in the Series A and Series B offerings, but with differences in the amount of the quarterly dividend.[217] Series C investors could also be paid cash dividends or additional shares of Series C stock at Carris' discretion.[218] Despite JCI's unprofitability in 2010 and

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[212] *See supra* footnotes 105 and 106 and accompanying text.

[213] CX-94, at 29; Tr. (Carris) 455-57.

[214] Tr. (Carris) 506-07; CX-98.

[215] CX-94; CX-98.

[216] *See supra* footnotes 105 through 109 and accompanying text.

[217] CX-94; CX-95; Tr. (Carris) 453-54.

[218] CX-94, at 47; Tr. (Carris) 458-59.

2011, dividend payments were made to Series C investors beginning on April 15, 2012—just one month after the first investor purchased Series C preferred shares.[219]

From March 9, 2012 through March 31, 2013, JCI raised $3,820,500 in the First Series C Offering.[220]

Second Series C Offering

Similar to the First Series C Offering, the Second Series C Offering of preferred shares contained the same eight-for-one conversion formula as the Series B Offering.[221]

The Second Series C PPM also contained updated financial information about JCI.[222] The 2012 audited financial statement stated that, during 2010 and 2011, JCI had not generated sufficient cash to cover its obligations.[223] The audited financial statement and the Second Series C PPM warned investors that there was substantial doubt that JCI could continue as a "going concern."[224] The Second Series C PPM also informed investors that, as of March 31, 2013, all $1,960,000 of the Bridge Offering notes had matured and were in default.[225]

The Second Series C Offering was ongoing when Enforcement filed the Complaint.[226]

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[219] CX-107, at 8; Tr. (Carris) 464-65 (acknowledging that one customer was paid a dividend on April 15, 2012, only two days after first investing on April 13, 2012, and admitting that "… for the year 2012 [JCI] was not profitable").

[220] CX-95, at 6; Tr. (Carris) 460-63.

[221] CX-95, at 30; Tr. (Carris) 459-60.

[222] CX-95, at 1, 52-78.

[223] CX-95, at 65.

[224] CX-95, at 39, 66.

[225] CX-95, at 39.

[226] Carris – JCI Amended Answer ("Am. Ans.") ¶ 71.

### E. Tkatchenko's Due Diligence Prior to Recommending the Invictus Securities

In late 2010, shortly after Tkatchenko joined JCI, he learned about Invictus from Carris, and began recommending Invictus securities to his clients. [227] Tkatchenko obtained most of his JCI customers through cold-calling.[228]

By the end of December 2010, Tkatchenko had begun soliciting his customers to invest in Invictus and his customers had invested approximately $200,000 in the Series A Offering.[229] From March 2011 through November 2011, Tkatchenko solicited his customers to invest over $1.3 million in the Series B Offering.[230] From December 2011 through February 2012, Tkatchenko solicited his customers to invest approximately $145,000 in the Bridge Offering.[231] From March 2012 through October 2013, Tkatchenko solicited his customers to invest at least $220,000 in the Series C Offerings.[232] In total, Tkatchenko solicited 28 customers to invest over $1.8 million in the Invictus Offerings over a three-year period.

Like other JCI registered representatives, Tkatchenko received higher commissions for selling Invictus than any other security.[233] Commissions for sales of Invictus securities were 10% of the gross proceeds and Tkatchenko retained the entire commission amount.[234]

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[227] CX-10, at 11; Tr. (Tkatchenko) 1373-79.

[228] Tr. (Tkatchenko) 1310.

[229] Tr. (Tkatchenko) 1376-80; CX-107.

[230] Tr. (Tkatchenko) 1380-06; CX-107.

[231] Tr. (Tkatchenko) 1408-13; CX-107A.

[232] Tr. (Tkatchenko) 1414-23; CX-107.

[233] Tr. (Tkatchenko) 1474-75.

[234] Tr. (Tkatchenko) 1474-75.

Prior to recommending Invictus, Tkatchenko testified that he: (i) reviewed the Invictus PPMs; (ii) relied on JCI's investment banking department; (iii) observed the daily activity at JCI, including speaking to members of its "management team"; (iv) recalled his knowledge of self-raising activities at other firms; and (v) conducted internet research on another broker-dealer that had done a self-offering.[235]

Although Tkatchenko testified that he reviewed the Series A and B PPMs, neither document contained any financial data for JCI. Prior to recommending the Series A and B Offerings, Tkatchenko did not review any JCI financial information.[236] Had he done so, he would have learned that: (i) JCI was operating at a net loss when he joined the firm in October 2010 (JCI had a net loss of $283,560 for the month of October 2010); and (ii) JCI continued to operate with a net loss for each month throughout 2011.[237] Tkatchenko stated that JCI's finances did not matter because "[f]or the start-up company, financial [statements are] not going to be a critical factor."[238] However, Tkatchenko recommended the Series B Offering through November 2011; and, at that point, JCI had been operating for two and a half years.[239]

Regarding Tkatchenko's asserted reliance on the JCI investment banking department, Tkatchenko knew that Carris was responsible for the creation of the Series A

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[235] Tr. (Tkatchenko) 1431-33, 1618, 1820-22.

[236] The Panel found that Tkatchenko was not credible. For example, at the hearing, Tkatchenko claimed to have reviewed JCI financial information on Edgar. Tr. (Tkatchenko) 1439. However, during his investigative testimony, he stated that he never looked at any outside source for financial information. Specifically, he stated that he only looked at the PPM. He explained that he looked at both JCI's and Invictus' balance sheet in the PPM and never obtained a balance sheet from any outside source. Tr. (Tkatchenko) 1453-54. In addition, at the hearing, Tkatchenko acknowledged that Invictus does not even have a balance sheet. Tr. (Tkatchenko) 1455.

[237] CX-264, at 78, 97-192.

[238] Tr. (Tkatchenko) 1620.

[239] CX-107, at 4.

and B PPMs. Thus, Tkatchenko knew or should have known that JCI's investment banking department was not a trusted independent source of information regarding Invictus.

Although Tkatchenko testified that he relied on JCI's "management team," the Series A and B PPMs identified Carris as "Management."[240] Aside from Simmons, the CCO who had joined JCI approximately six weeks before Tkatchenko, Carris was the only member of "management" when Tkatchenko joined JCI.[241] Accordingly, with regard to Tkatchenko's recommendations of the Series A and B Offerings, resulting in greater than $1.5 million from investors, Tkatchenko's reliance on "management" was also simply a reliance on Carris.

Tkatchenko asserted that both his prior experience at a broker-dealer that engaged in a self-offering and his internet search of another firm that had done a self-offering were relevant to his determination of Invictus' suitability. However, he failed to demonstrate how the success or failure of an offering at another broker-dealer related to whether he had a reasonable basis to recommend a different self-offering at a different broker-dealer.

Tkatchenko ignored warning signs regarding the Invictus investments. First, when Tkatchenko read the Bridge Offering subscription documents and learned of JCI's precarious financial condition, he did not inquire about JCI's net capital position. Had he done so, he would have learned that JCI was out of net capital at the time Carris created the Bridge Offering. Indeed, the entire time Tkatchenko recommended the Bridge

[240] CX-92, at 32; CX-93, at 34.

[241] *See* CX-150A, at 2.

Offering to his customers, JCI was out of net capital compliance.[242] JCI was also out of net capital compliance when Carris created the First Series C Offering. Because Tkatchenko failed to inquire about the net capital position, he also recommended the First Series C to customers during the time when JCI was out of net capital compliance.[243]

Second, when the Bridge Offering opened on December 1, 2011 (less than two weeks after Tkatchenko completed his last sale from the Series B Offering), Tkatchenko's customers who had invested in the Series A and B Offerings had received at least three dividend payments, the last of which occurred six weeks before the Bridge Offering opened.[244] Despite Tkatchenko's recent knowledge of JCI's poor financial condition from the Bridge Offering documentation, Tkatchenko did not inquire about the source of funds used to pay the dividends before continuing to recommend Invictus securities to his customers. Had he done so, he would have learned that the dividends paid to the Invictus investors came from new Invictus investors' funds.

Third, from December 2011 through February 2012, Tkatchenko had customers who had invested in the Bridge Offering but had never received any principal and interest on their investments.[245] With that knowledge, Tkatchenko recommended the First Series C Offering to his customers in March 2012.[246]

Fourth, in April 2013, Carris created offering documents for the Second Series C Offering, which disclosed that as of March 31, 2013, all $1,960,000 of the Bridge

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[242] CX-107A; Tr. (Tkatchenko) 1374-75.

[243] Sales of Invictus securities through March 22, 2012, occurred at a time when JCI was out of net capital compliance. CX-107, at 8, Tr. (Tkatchenko) 1374-76.

[244] CX-94, at 1 (Bridge Offering); CX-107, at 1-4.

[245] Tr. (Tkatchenko) 1470.

[246] CX-107, at 8.

Offering notes, including $145,000 of Bridge Offering notes held by Tkatchenko's customers, had matured and were in default.[247] By April 2013, JCI received its 2012 audited financial statements that posted an annual operating loss of $3,660,715.[248] As noted above, the auditors provided a very bleak description of JCI's financial condition.[249] Nonetheless, Tkatchenko continued to recommend that his customers invest in Invictus.[250] Tkatchenko explained that he "strongly believe[d] that [JCI was] going to overcome the difficulties and eventually [was] going to prevail and be victorious, and in exchange reward the participants in Invictus Capital, reward them with -- you know, it's going to be monetary rewards."[251]

### F. Fibrocell Science, Inc.

Fibrocell is a biotech company focused on the development of various products for aesthetic, medical, and scientific applications.[252] Carris had a long history of working with Fibrocell. In 2002, when Carris worked for another broker-dealer, he raised funds for Fibrocell's predecessor, and Fibrocell has been a JCI client since Carris established the firm in 2009.

#### 1. JCI's Investment Banking Services for Fibrocell

JCI provided investment banking services to Fibrocell from June 2009 through at least October 2012.[253] On September 1, 2009, JCI entered into an Investment Banking

[247] CX-95, at 39; Tr. (Tkatchenko) 1742.

[248] CX-114A, at 8. The 2012 financial statements were included with the Second Series C PPM. CX-95, at 1, 39, 52-78.

[249] CX-114A, at 13.

[250] Tr. (Tkatchenko) 1474.

[251] Tr. (Tkatchenko) 1742-43.

[252] Tr. (Carris) 599-600. The stock symbol is "FCSC." Tr. (Carris) 678.

[253] CX-17, at 1-2; Tr. (Carris) 608-09.

Agreement with Fibrocell to provide banking and advisory services, which (i) included a retainer payment of options to purchase one million shares of Fibrocell at $0.75 per share, and (ii) established that JCI would receive placement agent fees ranging from 8% to 10% for acting as Fibrocell's placement agent.[254] In addition to cash compensation, Fibrocell also paid JCI, Carris, and other firm principals warrants to purchase shares of Fibrocell common stock.[255] Beginning in September 2009, JCI acted as a placement agent for nine Fibrocell offerings, including Fibrocell's Series B Private Investment in Public Equity ("PIPE") [256] Offering from July through November 2010.[257] The PIPE Offering generated $4.6 million for Fibrocell, and $354,000 in commissions and fees for JCI.[258]

Fibrocell represented the largest single source of JCI's revenue.[259] From August 2009 through June 2012, JCI received $3,405,391 of revenue in connection with investment banking services provided to Fibrocell.[260] Since 2009, as compensation for investment banking services performed for Fibrocell, Carris received significant amounts of Fibrocell stock and warrants, and over $600,000 in net proceeds from the sale of Fibrocell stock.[261]

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[254] CX-15, at 2.

[255] CX-15; Tr. (Carris) 621.

[256] "In a PIPE offering, investors commit to purchase a certain number of restricted shares from a company at a specified price. The company agrees, in turn, to file a resale registration statement so that the investors can resell the shares to the public." www.sec.gov/answers/pipeofferings.htm.

[257] CX-17; Tr. (Carris) 601-04.

[258] CX-17; CX-18; Tr. (Carris) 601-04.

[259] Tr. (Carris) 625-30 (stating Fibrocell was JCI's primary and largest investment banking client from 2009 through 2011); Tr. 608-09 (Carris) (affirming 12 of the 17 transactions listed in CX-17 related to Fibrocell where JCI acted either as the investment banker, reseller, or syndicate member); CX-114A, at 12 ("For the year ended December 31, 2012, revenues from one customer accounted for 93 percent of investment banking revenues and 51 percent of total revenues.").

[260] CX-18, at 1; Tr. (Carris) 623-25.

[261] CX-23; CX-24; CX-120; CX-123; Tr. (Carris) 604-07.

### 2. Trading in Fibrocell Securities

Fibrocell was a "very illiquid," "thinly traded" stock that was publicly traded on the OTCBB system during the Manipulation Period.[262] Both prior to and throughout the Manipulation Period, JCI was a placement agent for Fibrocell in its PIPE Offering.[263] Carris understood that the PIPE Offering would be more attractive to investors if the price for Fibrocell was as high as possible in the market.[264] When JCI engaged in investment banking activity and conducted capital raises like the Fibrocell PIPE Offering, it notified its head trader, Barter.[265]

During the Manipulation Period, JCI dominated the trading of Fibrocell in the OTCBB market.[266] JCI was responsible for approximately 76% of Fibrocell's total OTCBB market trading volume.[267] On 48 of 106 trading days during the Manipulation Period, JCI accounted for 50% or more of the day's total Fibrocell trading volume, and on 29 of 106 trading days JCI accounted for 90% or more of the day's trading volume.[268] When Barter sent Fibrocell orders to the market maker for execution, he was aware of the Fibrocell OTCBB market volume; he knew that JCI dominated the trading in Fibrocell.[269]

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[262] Tr. (Carris) 630-31, 712; Tr. (Barter) 2781; CX-1A; CX-1B; CX-1E; CX-1J.

[263] Tr. (Carris) 601-04, 630-31, 662-67; CX-17; CX-18; CX-23; CX-24.

[264] Tr. (Carris) 853-54.

[265] Tr. (Barter) 2671-72.

[266] Tr. (Barter) 2671; CX-1B; CX-1J.

[267] CX-1J.

[268] CX-1A; CX-1H.

[269] Tr. (Barter) 2670-71.

JCI's Fibrocell trading activity during the Manipulation Period consisted of unfunded customer purchases (typically initiated in response to mandated Regulation T[270] sell-out notices from JCI's clearing firm). These were interspersed with reported matched trades. Attachment A to this Decision reflects 60 reported matched trades (primarily limit orders placed less than one minute apart) executed during the Manipulation Period. [271] Barter admitted that he sent buy and sell orders for the same number of Fibrocell shares within seconds of each other to the same market maker,[272] which constituted virtually all of the 60 reported matched trades to JCI's market maker for execution.[273]

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[270] The Federal Reserve Board's Regulation T pertains to an investor's obligation when a security is purchased. Specifically, an investor is given a maximum of five business days to pay for securities purchased in a cash or margin account. If payment due exceeds $1,000 and is not received by the end of this time period, the broker-dealer must either liquidate the position or apply for and receive an extension from its designated examining authority. NASD Notice to Members 99-102 (Dec. 1999), *available at* http://www.finra.org/Industry/Regulation/Notices/1999/P004028.

[271] Attachment A was created from CX-1B and RX-39. The Panel included 3 trades that were partial executions, which are indicated by an asterisk (*). In those instances, Barter sent a 10,000 share sell limit order and then sent buy orders (one market order and two limit orders) to the same market maker. RX-39, at 11, 27. The market maker filled the buy orders with the pending 10,000 share sell order. Barter was aware of the market volume of the Fibrocell trading on days when JCI traded Fibrocell. Tr. (Barter) 2670-71. Barter also acknowledged that he could see transactions entered in specific securities, including the time, price, and volume. Tr. (Barter) 2137.

[272] Tr. (Barter) 2137. Barter identified his initials on numerous Fibrocell trades. Tr. (Barter) 2105-08, 2119-22, 2149, 2156, 2158-59, 2162-63, 2540, 2545-46, 2553-55.

[273] Barter had the only login for JCI's trading system. Tr. (Barter) 2624-25. Although Barter stated that he had his passwords written on a piece of paper under his keyboard (information he never provided during his investigative testimony), he admitted that he never shared his login or password with anyone. Tr. (Barter) 2102-03. Barter testified that he was out of the office for a vacation from August 2 through 9, 2010. Tr. (Barter) 2447-53. However, his emails suggest he was in the office or had remote access JCI's systems because he used his JCI email on August 2 and 3. Tr. (Barter) 2646-64; CX-266. Several emails were exchanged between Barter's JCI email and the clearing firm regarding a "trading apparatus." Tr. (Barter) 2651-62; CX-266. Moreover, Barter initialed and processed a trade ticket dated August 3, 2010 for the sale of 1,000 shares of Fibrocell in a same-day settlement from his son's account. RX-36. Barter testified that the purpose of the sale was to obtain spending money for the impending vacation. *Id*. Although he stated he was out of the office, he placed a trade for himself. *Id*. Even removing the two trades occurring during August 4-9, 2010, there are still 58 matched trades that Barter caused to be executed during the Manipulation Period.

During the Manipulation Period, the closing price for Fibrocell gradually declined each month from $.90 to $.55.[274] Within each month, the daily closing price fluctuated.[275]

Below we discuss examples of unfunded purchases of Fibrocell stock, the movement of large blocks of Fibrocell stock, and reported matched limit orders at prices above the last trade in the market.[276] The examples below contain some overlap as JCI employed a combination of trading strategies simultaneously during the Manipulation Period.

Unfunded Fibrocell Stock Purchases

During most of the Manipulation Period, JCI was not profitable.[277] On May 17, 2010, the balance in JCI's checking account was negative $19,575.55.[278] Carris was aware of this and took steps to infuse money into JCI. On May 18, 2010, Carris sold a block of 80,000 Fibrocell shares from his personal account for approximately $74,000.[279] Carris' sell order settled on the same day he sold the stock; he made a capital contribution to JCI that same day.[280] Carris sold an additional block of 80,000 shares for $79,980 on

[274] CX-1A, at 1.

[275] CX-1A, at 2-6.

[276] Barter admitted that he would be concerned about such trading activity. Tr. (Barter) 2176-79 ("If it came across my desk and it was laid out in the manner that you just showed me then, yes, I would take concern with it.").

[277] *See* CX-264, at 46 (reflecting a second quarter loss of $255,087 for 2010), 54 (reflecting net income of $110,337 for July 2010), 62 (reflecting a net loss of $121,347 for August 2010), 70 (reflecting a net loss of $54,328 for September 2010).

[278] CX-97, at 19.

[279] CX-248A, at 13.

[280] CX-248A, at 13; CX-97, at 19.

May 21, 2010.[281] On May 26, 2010, the settlement date, Carris infused the entire proceeds of $79,980 into JCI.[282]

Carris' sales of Fibrocell were paired with Fibrocell purchases. On May 18, 2010, Barter sent Carris' 80,000 share sell order for execution as a limit order paired with a 80,000 share buy order.[283] He sent both orders to the same market maker within less than one minute of each other.[284] That same day, Barter sent a 35,900 share sell limit order paired with a 35,900 share buy limit order to the same market maker within 15 seconds of each other.[285] JCI's clearing firm's blotter ("Blotter") reflected that, on May 18, Carris' customer NM purchased 115,900 shares of Fibrocell, an amount equal to the two sell orders.[286] On May 21, 2010, Barter received another 80,000 share sell order from Carris. Barter sent the sell order for execution as a market order paired with a 80,000 share buy market order; he placed both orders within 45 seconds of each other with the same market maker.[287] The Blotter reflected that customer NM purchased an additional 109,000 shares of Fibrocell that day.[288]

Although JCI described NM's purchase as "unsolicited,"[289] NM never paid for the Fibrocell shares. Soon after NM's purchases, JCI's clearing firm began sending daily sell-out notices to Carris, Barter, and others at JCI instructing the firm to arrange for

[281] CX-1B, at 9; CX-248A, at 14.

[282] CX-97, at 20 ; CX-248A, at 14.

[283] CX-1B, at 7; RX-39, at 20-21.

[284] CX-1B, at 7; RX-39, at 20-21.

[285] CX-1B, at 7; RX-39, at 20-21.

[286] CX-248A, at 13.

[287] CX-1B, at 9; RX-39, at 24.

[288] Tr. (Carris) 714-17; CX-248A, at 13-14.

[289] CX-248A, at 13-14.

NM's purchases to be funded.[290] Customer NM never funded the purchases. Instead, JCI distributed NM's Fibrocell position to other JCI customers who, like NM, never paid for the shares they purportedly purchased.[291]

This cycle repeated itself throughout the Manipulation Period. Specifically, Fibrocell shares passed through the accounts of at least 26 Carris customers who never funded the purchases.[292] In each case, just as the clearing firm was about to require a sell-out into the market,[293] JCI sold the unfunded shares to another customer or a JCI firm account.[294] JCI marked these unfunded purchases and sales as "unsolicited," and generally did not charge a commission.[295] Trade tickets and trade confirmations created by JCI, and the Blotter provided by its clearing firm, identified Carris or a JCI firm account as the broker associated with these transactions.[296] Carris' customers, in whose accounts these

[290] CX-261, at 103-06, 110-11, 113-14, 134-35, 137, 139-41, 146-53, 160-67, 172-73. Carris and Barter received the notices from the clearing firm at their JCI email addresses, and Barter forwarded some to others at the firm. *See generally* CX-261 (compilation of sell-out emails indicating Carris and "Trading" as recipients); Tr. (Barter) 2105-117, 2129-37, 2141-47. Barter stated that he "received them pretty much every single day up until about a week ago." Tr. (Barter) 2142.

[291] CX-248A, at 15-16; CX-1E (tracing Carris' sale of 160,000 shares of Fibrocell through the account of customer NM, and into accounts of customers JC and SM on June 7, 2010, and then to the accounts of customers LL and MG on June 9, 2010 (time stamp on Blotter reflects a June 10, 2010 trade date)).

[292] CX-261.

[293] CX-65; CX-66; CX-68; CX-72; CX-74 – CX-79. The clearing agent sent approximately 112 emails to JCI concerning unfunded transactions. CX-261.

[294] CX-1D; CX-1F; CX-1G; CX-1J; CX-1K; CX-1L; CX-248A; CX-261.

[295] *See* CX-1K, at 11-27.

[296] CX-248A; CX-27 – CX-35; CX-37; CX-38; CX-41 – CX-49; CX-52 – CX-56; Tr. (Carris) 676-81 (Carris' representative code was J101), 681-82, (Barter) 2139 (J199 was the code for the firm), 2143 (Carris was the broker for the transactions).

Fibrocell trades occurred, were unaware of and never paid for the Fibrocell purchases.[297] For example, on July 29, 2010, customer DE, after receiving a trade confirmation from JCI reflecting a Fibrocell trade for 133,000 shares, sent an email to JCI's Trading Department:[298]

> I have a question for you or George [Carris]. I received some Trade Confirmation letters in the mail recently regarding the purchase of some stock for Fibrocell Science Inc. What is this letter exactly and what does it mean … The total net amount on the statements is pretty nice but I am assuming that the money being shown on the Trade Confirmation letter is not really mine? I am asking because I really have no idea. I am completely clueless and would like to understand more.[299]

Movement of Blocks of Fibrocell Stock

Two distinct blocks of Fibrocell shares moved through JCI customer accounts in July and August 2010: one block in the amount of 133,000 shares and the other for 85,900 shares that grew to 109,900 shares.[300] As Carris acknowledged, all of the unfunded purchases, generally marked unsolicited, involved his customers.[301]

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[297] Carris admitted that DE did not authorize the multiple buy and sell transactions for 133,000 Fibrocell shares. CX-80; Tr. (Carris) 788, 791-94, 798-99.

[298] CX-80; Tr. (Carris) 775, 788-92. Although the email salutation stated MG, DE only sent the email to trading@johncarrisinvestments.com; there were no other recipients listed on the email. CX-80. Barter acknowledged that trading@johncarrisinvestments.com was his email address at JCI. Tr. (Barter) 2108. He received emails sent to trading@johncarrisinvestments.com, and at times forwarded them to other JCI employees. *See, e.g.*, CX-261, at 242. He used his JCI email for both personal and business purposes. CX-266. In fact, within two business days from the July 29 email, Barter was emailing JCI's clearing firm using the trading@johncarrisinvestments.com email address. CX-266, at 1.

[299] CX-80; Tr. (Carris) 788-92. When DE sent the above email, JCI had already received a week's worth of emails from its clearing firm stating that the July 12 transactions from DE's account were not funded. Tr. (Carris) 791-92.

[300] CX-248A; Tr. (Carris) 762-851. Barter admitted that the trading activity from July through August 2010 detailed above shows a distinct block of shares moving through very specific and similar customer accounts. Tr. (Barter) 2175-76.

[301] Tr. (Carris) 849-51.

*133,000 Fibrocell Share Block*

The 133,000 share block movement began on July 12, 2010, when the clearing firm sent JCI a sell-out email instructing it to sell 45,000 shares out of customer JC's account as unfunded.[302] In the same email, the clearing firm instructed JCI to sell an unfunded purchase of 160,450 shares of Fibrocell out of customer JK's account.[303] Within minutes, in transactions that were not reported to the market, JCI purchased 205,450 shares and placed them in two other customer accounts.[304] The 205,450 shares represented the unfunded shares from customers JC and JK.[305] Customer VP received 72,450 shares and DE (the author of the above email) received 133,000 shares.[306] As the clearing firm demanded that Barter, Carris, and JCI sell the unfunded purchases into the market,[307] JCI moved the 133,000 shares between customer DE's account and JCI's accounts on July 13, July 23, and July 29.[308] None of this activity was reported to the market.[309] However, JCI, through Barter, traded the 133,000 share block in the OTCBB market several times.[310] Barter placed the 133,000 share buy and sell orders as limit orders, sending them to the same market maker within minutes (typically less than

[302] CX-261, at 257.

[303] CX-261, at 257.

[304] CX-248A, at 19.

[305] CX-248A, at 19.

[306] CX-248A, at 19.

[307] CX-261, at 4, 7, 11, 15, 17, 20, 25, 29, 38, 40, 64, 72, 80, 97, 101, 126, 129, 309, 312, 317, 322, 327, 330, and 337.

[308] CX-248A, at 19-21.

[309] *Compare* CX-248A *with* CX-1B and RX-39.

[310] CX-1B, at 18-22; RX-39, at 76, 79, 84, 87, 92.

one minute) of each other.[311] The market maker then executed the orders within seconds of each other and within a fraction of a penny of each other on each of the following dates: August 3, August 11, August 19, August 25, and September 3, 2010.[312] On each of those dates, JCI's trading constituted 96-100% of the total OTCBB market volume in Fibrocell.[313]

*85,900 Fibrocell Share Block*

During July and August 2010, similar activity took place for the block of 85,900 Fibrocell shares, which grew to 109,900 shares when combined with additional shares.[314] Similar to the 133,000 share block, JCI, through Barter, traded the 85,900 share block in the OTCBB market. On August 2 and August 10, Barter placed the 85,900 share buy and sell orders as limit orders, sending them to the same market maker within approximately 30 seconds of each other.[315] The market maker then executed the orders within seconds of each other and within a penny of each other.[316] JCI's trading constituted 83% of the total OTCBB market volume in Fibrocell on August 2, and 99% on August 10.[317]

On August 18, 2010, the Blotter reflected that one of Carris' customers sold the 85,900 share block and another Carris customer sold 24,000 shares, totaling 109,900 shares.[318] That day, JCI, through Barter, sent the 109,900 share sell order to the market

[311] CX-1B, at 18-22; RX-39, at 76, 79, 84, 87, 92.

[312] CX-1B, at 18-22; RX-39, at 76, 79, 84, 87, 92.

[313] CX-1H, at 3-4.

[314] CX-248A, at 19-24.

[315] CX-1B, at 17-18; RX-39, at 75, 78.

[316] CX-1B, at 17-18; RX-39, at 75, 78.

[317] CX-1B, at 17-18; CX-1H, at 3.

[318] CX-248A, at 23.

paired with a buy order for 109,900 shares.[319] Barter placed the buy and sell orders as limit orders, sending them to the same market maker within 30 seconds of each other.[320] Within minutes, the market maker executed the orders within seconds of each other and within a fraction of a penny of each other.[321] JCI, through Barter, again traded the 109,900 share block in the OTCBB market, sending both buy and sell limit orders within 30 seconds to the same market maker, which executed the orders within seconds of each other and within a fraction of a penny of each other, on August 27 and September 1.[322] On August 18, August 27, and September 1, 2010, JCI's trading in Fibrocell comprised 83-99% of the total OTCBB market volume.[323]

Reported Matched Limit Orders Priced Above Last Trade in the Market

Barter caused Fibrocell trades to be sent for execution at limit prices above the last trade in the market. On July 27, 2010, Carris' customer TM bought 72,450 shares and his customer VP sold 72,450 shares.[324] Customer TM's purchase was unfunded and VP's sale was the subject of a sellout notice that day demanding the sale from a prior unfunded purchase.[325] Barter submitted the buy and sell Fibrocell orders as limit orders to the same market maker within 30 seconds of each other.[326] Despite the fact that Fibrocell traded at $.73-.74 just prior to this order, Barter sent this order to the market priced at $.785 per

[319] CX-1B, at 19; RX-39, at 83.

[320] CX-1B, at 19; RX-39, at 83.

[321] CX-1B, at 19.

[322] CX-1B, at 20-21; RX-39, at 89-90. The trading took place in the customer accounts of KC, AO, VP, PC, SQ, and JCI accounts. CX-248A, at 24.

[323] CX-1B, at 19-21; CX-1H, at 3.

[324] CX-248A, at 21.

[325] CX-261, at 78; CX-262, at 96-97.

[326] CX-1B, at 16; CX-27.

share.[327] The Fibrocell trading at JCI on July 27 represented approximately 93% of the total OTCBB market volume.[328] Approximately one hour after JCI's matched Fibrocell orders, the market reported the next Fibrocell trade at $.75.[329]

On July 29, 2010, Carris' customer RS bought 30,000 Fibrocell shares and his customer DE sold 30,000 shares.[330] That day, Carris, Barter, and JCI received a notice from JCI's clearing firm demanding that DE's earlier 30,000 share purchase be sold out because there were not enough funds in the account for the purchase.[331] Barter sent the 30,000 buy and sell orders as limit orders to the same market maker within 30 seconds of each other.[332] While the market reflected the preceding trade at $0.73, the sell side of this trade was $0.805 and the buy side was $0.81.[333] The matched buy side trade at $0.81 represented the closing price for the day.[334] The next day, the first sell in the market was reported at $.80.[335] JCI's Fibrocell trading on July 29 represented approximately 88% of the total OTCBB market volume.[336]

The day after effecting the July 29 matched trades, Barter sent matched 4,000 share limit orders for execution, within 30 seconds of each other to the same market

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[327] CX-207 (row 878 and 879 reflect the matched trades priced at $.785, rows 873-77 reflect the trades priced at $.73-.74); CX-211 (row 780).

[328] CX-1B, at 16.

[329] CX-207 (row 880).

[330] CX-248A, at 22.

[331] CX-261, at 30.

[332] CX-1B, at 16; CX-28.

[333] CX-207 (rows 900-902).

[334] CX-211 (row 778).

[335] CX-207 (row 903).

[336] CX-1B, at 16-17; CX-1H, at 3.

maker, priced at $.795-.80.[337] Carris was the registered representative for the sell order, which was marked "unsolicited" and reflected that no commission was charged.[338]

### 3. Liquidation of Fibrocell Securities

In October 2012, Fibrocell issued Carris and DB, a JCI principal, each 1.9 million restricted Fibrocell shares as compensation for JCI's work on a Fibrocell capital raising campaign.[339] Because the shares were restricted, neither Carris nor DB could sell their shares until the end of April or early May 2013.[340] Following a reverse stock split of Fibrocell's common shares on April 30, 2013,[341] Carris owned 74,636 shares of Fibrocell stock, and DB owned 73,969 shares of Fibrocell stock.[342] Both Carris and DB held these shares in their personal brokerage accounts at JCI.[343] At about the same time the reverse-split occurred, the restricted shares issued to Carris and DB became freely tradable.[344]

Over 13 trading days during the Liquidation Period, Carris and DB sold their 148,605 Fibrocell shares.[345] To sell their shares, Carris and DB orally gave Barter a "limit not held" order at or before the opening of the market.[346] Barter then completed their

[337] CX-248A, at 22; CX-207 (rows 904 and 905); CX-1B, at17; RX-39, at 74.

[338] CX-248A, at 22; CX-29, at 1-2.

[339] Tr. (Carris) 857-59.

[340] Tr. (Carris) 857-59.

[341] CX-118; Tr. (Carris) 860-61.

[342] CX-120, at 5-6; CX-121, at 5; Tr. (Carris) 862.

[343] Tr. (Carris) 862-63.

[344] These shares were subject to a six-month selling restriction, pursuant to SEC Rule 144(d)(1).

[345] Tr. (Carris) 864-71, 1126; CX-1N; CX-120; CX-121. Carris and DB sold their shares throughout the Liquidation Period "to get the best price possible." Tr. (Carris) 914-15.

[346] Tr. (Carris) 1234, 1277, (Barter) 2636-38, (Hechler) 3267.

trade tickets and immediately routed the orders to the market maker.[347] The total proceeds from their sales were approximately $700,000. [348]

During the Liquidation Period, similar to the Manipulation Period, Fibrocell was still thinly-traded, and JCI continued to dominate the Fibrocell market.[349] However, JCI was not providing investment banking or advisory services to Fibrocell and did not have Fibrocell on a restricted list.[350] In addition, JCI was not acting as a market maker for Fibrocell, writing research reports, or engaging in proprietary trading.[351]

JCI registered representatives solicited customers to purchase Fibrocell shares when Carris and DB were selling their shares during the Liquidation Period, as well as prior to the Liquidation Period.[352] However, there is no evidence that either Carris or DB (i) solicited any customer to purchase shares of Fibrocell, or (ii) directed or incentivized any registered representative to solicit purchases of Fibrocell.

Although Carris knew that JCI registered representatives solicited customers to purchase Fibrocell throughout the time that he and DB sold their Fibrocell shares,[353] none of the registered representatives knew that Carris and DB were selling their Fibrocell shares.[354] According to Hechler, JCI's CCO during the Liquidation Period, providing such information to the JCI registered representatives is contrary to the WSPs he created

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[347] Tr. (Barter) 2637-38.

[348] CX-1N; CX-249A; Tr. (Carris) 869-71.

[349] Tr. (Carris) 712, 922-23, (Barter) 2781; CX-1M (JCI accounted for as much as 94% of total market volume on a single day).

[350] Tr. (Carris) 1172-73, (Tkatchenko) 1796, (Barter) 2641-42, (Hechler) 3267.

[351] Tr. (Carris) 1170, 1172, (Barter) 2641, (Hechler) 3267.

[352] Tr. (Carris) 714-15, 871-72; CX-249A; CX-1, *et seq*.

[353] Tr. (Carris) 871-72.

[354] Tr. (Hechler) 3267-68, 3274; Stipulations ("Stip.") ¶ 2.

for JCI and what the rules and regulations required.[355] Hechler believed that had he provided this type of information to the registered representatives he could have created an environment for front running, prearranged trading, and possibly manipulation.[356] Neither JCI nor the registered representatives who solicited Fibrocell purchases informed the customers that Carris and DB were simultaneously selling their shares.[357]

### G. JCI's Anti-Money Laundering Compliance Program

During the AML Period, Carris was JCI's AMLCO until he hired Simmons on August 23, 2010.[358] JCI's AML compliance program consisted of AML procedures, dated March 31 and September 22, 2010, both of which incorporated the firm's WSPs.[359] Carris and Simmons were responsible for reviewing and monitoring customer account activity on a daily and monthly basis for unusual patterns indicative of potentially suspicious activity.[360] They stated that they reviewed trade tickets and reports from their clearing firm.[361] JCI, through Carris, also required each employee to review and sign the new-hire compliance agreement.[362]

Although JCI's AML materials did not (i) identify specific firm reports to be used, or clearing firm reports to be requested, to enable JCI to conducts its AML compliance reviews, or (ii) provide specific procedures of how employees should review

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[355] Tr. (Hechler) 3274.

[356] Tr. (Hechler) 3274.

[357] Tr. (Carris) 871-72; Stip. ¶ 1.

[358] CX-139; CX-140; CX-141; Tr. (Carris) 211, 213-14, (Simmons) 2226.

[359] CX-139; CX-140; CX-150; CX-150A.

[360] CX-139, at 2; CX-141, at 6; Tr. (Carris) 235-38, 241-42, 246-48.

[361] Tr. (Carris) 241-42, 245-49; CX-141, at 6.

[362] CX-8A, at 52-60; Tr. (Carris) 695-97.

trading and accounts for red flags,[363] the materials did identify specific red flags that are indicative of suspicious activity, including, among others:

- A customer wishes to engage in transactions that lack business sense or apparent investment strategy, or are inconsistent with the customer's stated business strategy.

- The customer engages in suspicious activity involving the practice of depositing penny stocks, liquidating them, and wiring proceeds.

- For no apparent reason, the customer has multiple accounts under a single name or multiple names, with a large number of inter-account or third-party transfers.

- The customer maintains multiple accounts, or maintains accounts in the name of family members or corporate entities, for no apparent business purpose or other purpose.[364]

A review of several customer accounts (and related accounts) revealed red flags indicative of suspicious activity such as: (i) transactions that lack business sense or apparent investment strategy; and (ii) the practice of depositing penny stocks, liquidating them, and wiring proceeds.[365] Below we discuss five customer accounts and examples of suspicious trading in those accounts.

Customers PB and DB

From May 12, 2010 through May 10, 2011, customer PB and his relative DB controlled three accounts at JCI.[366] During the above time period, PB and DB purchased

[363] Tr. (Simmons) 2231.

[364] CX-150, at 180-81; Tr. (Simmons) 2227-30 (cknowledging JCI's September 22, 2010 WSPs (CX-140) identified several red flags, including "trading that constitutes a substantial portion of all trading for the day in a particular security; trading or journaling between/among accounts, particularly between related owners; late day trading; heavy trading in low-priced securities …").

[365] *See generally* CX-142 – CX-149.

[366] CX-143.

and sold millions of shares of low-priced securities, including Fibrocell.[367]

On May 17, 2010, PB sold 19,400 Fibrocell shares.[368] On May 18, 2010, PB sold 35,900 Fibrocell shares paired with a matched limit order that Barter sent to the market.[369] PB's May 18 sale and a sale of 80,000 shares of Fibrocell by Carris that same day were offset by a Carris customer's unfunded purchase of 115,900 shares.[370] On May 19, PB wired the proceeds from his May 17 and May 18 sales out of his account.[371]

On June 8, 2010, PB purchased 130,000 Fibrocell shares in five transactions in an individually named account; and on the same day, he sold 130,000 Fibrocell shares in five transactions through one of the accounts in the name of an entity. The buys and sells were in the same quantities, and each corresponding buy and sell had the same price.[372] On June 9, 2010, PB wired $64,250 out of his account.[373]

During this time period, PB, DB, and their related corporate entity cancelled at least 14 buy or sell transactions involving Fibrocell.[374]

Customer SF

From May 11, 2010 through March 28, 2011, customer SF deposited and sold over three million shares of five low-priced securities and wired over $250,000 from the account.[375] He also entered eight buy-side orders for the low-priced securities, which he

[367] CX-143.

[368] CX-143.

[369] CX-143; *see supra* footnote 284 and accompanying text.

[370] *See supra* footnote 285 and accompanying text.

[371] CX-143.

[372] CX-143.

[373] CX-143.

[374] CX-143 at 1-2.

[375] CX-144.

then cancelled.[376] Each cancelled buy order corresponded with a sell order on the same day in the same share amount, and usually at the same price.[377]

Customer JF

From October 15, 2010 through March 31, 2011, customer JF sold several million shares of low-priced securities and wired out, or received payments by check, a total of $14,749.[378] JF also entered seven buy-side orders, all of which he cancelled.[379] Each cancelled buy order corresponded with a sell order that took place on the same day or within one day.[380] The cancelled buy orders were in the same share amounts and at the same prices as the corresponding sell orders.[381]

Customer ES

From November 9, 2010 through May 4, 2011, customer ES deposited, purchased, and sold several million shares of low-priced securities, including Fibrocell.[382] For example, on November 15, 2010, ES bought 100,000 shares of Polymedix, Inc. for $1.03 per share.[383] That same day, he sold the same amount of shares at the same price.[384] Then, he cancelled his buy order.[385] The sale of the 100,000 Polymedix shares generated

[376] CX-144.

[377] CX-144.

[378] CX-145.

[379] CX-145.

[380] CX-145.

[381] CX-145.

[382] CX-146.

[383] CX-146.

[384] CX-146.

[385] CX-146.

$102,590 for ES.[386] Throughout this period, ES wired approximately $425,000 from his account.[387]

Customer HG

From November 17, 2010 through April 15, 2011, customer HG purchased and sold hundreds of thousands of shares of low-priced securities.[388] Like the above JCI customers, HG's transactions included buy-side cancellations paired with sales in the same amount at the same price.[389] In nine separate transactions, she wired approximately $79,500 out of her account.[390]

In addition to the trading in the five customer accounts above, the Fibrocell trading during the Manipulation Period was also suspicious because it appeared to lack business sense. Time and time again, JCI entered purchase orders in customer accounts for blocks of Fibrocell shares. These orders were marked unsolicited. They were also unfunded and unreported transactions. Five to seven days later, when JCI received sell-out notices from its clearing firm, it then sold the same block of shares to another customer or JCI account. This activity also occurred within the review period of the auditor's AML report.

Despite the above red flags of suspicious activity, JCI failed to identify suspicious activity during the AML Period. JCI's annual AML audit report, dated April 18, 2011, reviewed JCI's AML program for the period of April 2010 through March 2011. In conducting the audit, the auditor reviewed "all the documentation deemed relevant to

[386] CX-146.

[387] CX-146.

[388] CX-147.

[389] CX-147.

[390] CX-147.

assist in making an informed determination as to the level of compliance the Firm maintained."[391] The auditor also interviewed Simmons, who had overall responsibility for firm-wide AML compliance.[392] When reporting his results, the auditor stated that "[f]rom the completion of the last AML audit to date, the Firm has *not identified* unusual or suspicious activity or patterns of activity that required further inquiry, and/or the filing of a Suspicious Activity Report ("SAR")."[393]

### H. JCI's Supervisory System

As identified above, Carris held several significant supervisory roles at JCI. From the creation of JCI through the filing of the Form BD, Carris served as JCI's president. In that role he was responsible for overall supervision of JCI. He also supervised registered representatives in his capacity as the CCO and supervisor of retail sales. Below we address the supervisory failures in connection with JCI's (i) Fibrocell trading during the Manipulation Period, (ii) sales of Invictus securities, (iii) books and records relating to the payment of Carris' personal expenses, (iv) net capital deficiencies, and (v) employee payroll taxes.

#### 1. Fibrocell Trading During the Manipulation Period

During the Manipulation Period, JCI, through Carris and Barter, repeatedly bought and sold Fibrocell shares between customer accounts and firm accounts. Most, if not all, of the customers involved in the trading (both reported and unreported) were customers of Carris. Throughout the Manipulation Period, Carris ignored red flags that would have alerted him that the trading activity in his customers' accounts was improper.

[391] CX-141, at 3.

[392] CX-141, at 3.

[393] CX-141, at 6.

For example, Carris received repeated emails from JCI's clearing firm notifying him that (i) his customers' transactions were unfunded, and (ii) firm accounts were improperly receiving and holding Fibrocell securities.[394] In fact, one of Carris' customers sent an email to JCI questioning why Fibrocell stock appeared in her account when she never purchased it.[395] Although Carris acknowledged that he reviewed trading data similar in content to the information found on a trade blotter,[396] and JCI was only entering between 5 and 15 trades per day,[397] he did not detect or investigate the irregularities above.

**2. Sales of Invictus Securities**

As stated above, Carris caused the Invictus offering materials to be prepared, and he reviewed and approved them prior to their use to solicit investors.[398] In connection with the Series A and B Offerings alone, JCI sold Invictus shares valued at over $4.1 million.[399] JCI and its registered representatives sold Invictus Series A and Series B shares using offering materials that made false statements and misleading omissions. Carris failed to ensure that investors received current, accurate financial information for JCI and Invictus. Here, the Invictus sales provided a financial benefit to Carris and JCI. Despite his responsibilities as the firm's president, CCO, supervisor of retail sales, and supervisor of registered representatives, Carris took no supervisory steps to ensure that (i) JCI's registered representatives conducted adequate due diligence prior to selling

[394] CX-261.

[395] CX-80.

[396] Tr. (Carris) 638-42, 660-62.

[397] Tr. (Carris) 662; CX-141, at 1-2.

[398] *See supra* footnote 125 and accompanying text.

[399] CX-107, at 1-4.

Invictus, and (ii) customers were not sold an unsuitable product. Instead, without regard to JCI's bleak financial condition, he continued to promote Invictus.[400]

### 3. Books and Records Relating to the Payment of Carris' Personal Expenses

Carris knew that he was using his JCI corporate credit and debit cards for his personal expenses. When his personal and business expenses were processed by JCI, Carris never submitted any expense form to substantiate the expense. There is no evidence that Carris or any other JCI principal took any supervisory action to ensure that his expenses were properly characterized on JCI's books and records.

### 4. Net Capital Deficiencies

Carris knew that JCI operated with insufficient net capital as of March 9, 2012, when he caused Invictus investor monies to be infused into JCI. At that point, he knew that the monies he infused were not sufficient to bring the firm back into net capital compliance, so he continued to make additional capital contributions into JCI as investment funds came from Invictus investors. He did not cease JCI's operations, but continued to seek more funds from the Invictus investors. Certainly, as of March 9, he was on notice of JCI's net capital problems, yet he did not reasonably supervise JCI's FINOP and CFO who were both involved in handling JCI's net capital compliance. After March 23, 2012 (the date of the First Net Capital Deficiency), JCI operated with a net capital deficiency between July 1, and July 24, 2012, and on August 6, 2012, as described in the Amended Complaint, as well as during the additional time periods described above.

[400] CX-256 (recording of conversation with JCI customer).

### 5. Employee Payroll Taxes

JCI's payroll service provider informed Carris that JCI was delinquent in its obligations to pay its employees' payroll taxes no later than October 17, 2011, the date of the payroll service provider's first email directly to Carris informing him of the unpaid payroll taxes.[401] Throughout the end of 2011 and into 2012, the payroll service provider repeatedly reminded Carris and JCI that JCI was behind in its payroll tax obligations. In addition, Carris received articles and other resource materials explaining the significance of failing to pay employee payroll taxes.

Despite this knowledge, Carris took no steps to supervise the CFO and other JCI employees responsible for the payment of the payroll taxes. Instead, knowing that JCI had not satisfied its obligation to its employees, he determined to pay dividends to Invictus investors.

## IV. CONCLUSIONS OF LAW

### A. JCI's Inaccurate Books and Records (Cause Six)

The Sixth Cause of Action alleges that, from January 1, 2010 through December 5, 2011, Carris violated NASD Rule 3110, and FINRA Rules 4511 and 2010, by causing JCI to create and maintain inaccurate books and records, in violation of Section 17(a) of the Exchange Act and Rule 17a-3 thereunder. The Sixth Cause of Action also charges JCI with violating NASD Rule 3110, and FINRA Rules 4511 and 2010, and willfully violating Exchange Act Section 17(a) and Rule 17a-3 thereunder, by creating and maintaining inaccurate books and records.

NASD Rule 3110, now FINRA Rule 4511, requires member firms to "make and preserve books, accounts, records, memoranda, and correspondence in conformity with

[401] CX-132.

all applicable laws, rules, regulations and statements of policy promulgated thereunder and with the Rules of [FINRA] and as prescribed by SEC Rule 17a-3." Entering inaccurate information in a member firm's books or records violates NASD Rule 3110 and FINRA Rule 4511, and also violates FINRA Rule 2010's requirement that members observe high standards of commercial honor and just and equitable principles of trade in the conduct of their business.[402]

Compliance with these recordkeeping rules is essential to the proper functioning of the regulatory process. "Indeed, the SEC has stressed the importance of the records that broker-dealers are required to maintain pursuant to the Exchange Act, describing them as the 'keystone of the surveillance of brokers and dealers by our staff and by the securities industry's self-regulatory bodies.'"[403]

From January 1, 2010 through December 5, 2011, Carris used his JCI corporate credit and debit cards for his personal expenses.[404] As a result of Carris' use of JCI funds for personal purposes, the firm's books and records were manifestly inaccurate. After FINRA questioned the business purpose of the expenses on JCI's general ledger, JCI reclassified the personal expenses that had been identified as business expenses. The reclassified expenses totaled more than $590,000.

Carris argued that the inaccurate books and records were due to the incompetence of MG, a JCI back office employee, who did not know how to record the expenses.

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[402] *See, e.g.*, *Fox & Co. Inv., Inc.*, Exchange Act Release No. 52697, 2005 SEC LEXIS 2822, at *30-32 (Oct. 28, 2005).

[403] *Dep't. of Enforcement v. Trevisan*, Complaint No. E9B2003026301, 2008 FINRA Discip. LEXIS 12, at *35 (NAC Apr 30, 2008) (quoting *Edward J. Mawood & Co.*, 46 S.E.C. 865, 873 n.39 (1977), *aff'd*, 591 F.2d 588 (10th Cir. 1979)).

[404] Carris continued this practice until at least the end of 2013, and continued despite FINRA asking questions about Carris' personal expenses during a 2010 sales practice examination. Tr. (Carris) 494-96.

However, the Panel is not persuaded by Carris' attempt to shift the blame to a low-level employee. Carris incurred the expenses on the JCI corporate credit and debit cards, yet he never completed an expense report or delineated the expenses as personal.

"A central purpose of the requirement for maintaining a general ledger … is to … facilitate the preparation of financial statements showing the broker's or dealer's financial condition." [405] Here, Carris' extensive use of JCI funds for personal expenses caused not only the general ledger to be inaccurate but also corresponding FOCUS reports, audited financial statements, and tax returns that JCI had prepared prior to its reclassification of the expenses.

The Panel finds that, from January 1, 2010 through December 5, 2011, Carris and JCI violated NASD Rule 3110, and FINRA Rules 4511 and 2010. The Panel also finds that JCI, through Carris, violated Exchange Act Section 17(a) and Rule 17a-3 thereunder, by creating and maintaining inaccurate books and records.

The Panel further finds that JCI's violation of Exchange Act Section 17(a), and Rule 17a-3 thereunder, was willful. A finding of willfulness does not require intent to violate the law, but merely intent to do the act that constitutes a violation of the law.[406] A failure to act may be willful even though it was inadvertent.[407] Applying these principles, the Panel concludes that JCI acted willfully in creating and maintaining inaccurate books and records.

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[405] *North Woodward Financial Corp*., Securities Exchange Release No. 60505, 2009 SEC LEXIS 2796, at *26-27 (Aug. 14, 2009).

[406] *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000); *Arthur Lipper Corp. v. SEC*, 547 F.2d 171, 180 (2d Cir. 1976).

[407] *Stonegate Sec. Inc.*, 55 S.E.C. 346, 351, at *9 (Oct. 15, 2001) (citing *Hammon Capital Mgmt. Corp*., 48 S.E.C. 264, 265 (1985)); *Jesse Rosenblum*, 47 S.E.C. 1065, 1067 & n.9 (1984); *Oppenheimer & Co.*, 47 S.E.C. 286, 287-88 (1980) (citing *Haight & Co., Inc*., 44 S.E.C. 481, 507 (1971), *aff'd without opinion* (D.C. Cir. 1971)).

### B. JCI's Failure to Issue Tax Forms and Issuance of an Inaccurate Tax Form (Cause Seven)

The Seventh Cause of Action alleges that Carris and JCI violated FINRA Rule 2010, by failing to issue year-end tax forms, Forms W-2, for years 2009 and 2010, and issuing a false Form W-2 for 2011 that underreported Carris' compensation.

FINRA Rule 2010 is broadly applied to sanction unethical conduct by members of the securities industry. Members violate Rule 2010 when they violate established ethical business standards or undertake conduct in bad faith.[408]

Here, Enforcement introduced Forms W-2 gathered from JCI, as well as Carris' personal tax returns for 2009 and 2010. There was also evidence of the personal expenses that Carris charged to JCI during 2010 and 2011. However, there was no evidence that Carris caused, or participated in, the firm's failure to issue Forms W-2 in 2009 and 2010, or the firm's issuance of an inaccurate Form W-2 in 2011. In addition, there was no evidence of what the appropriate tax and accounting treatment for the reclassified general ledger entries (i.e., wages, owner distributions, etc.) should have been.

In light of the foregoing, the Panel finds that Enforcement failed to prove the Seventh Cause of Action by a preponderance of the evidence. The Seventh Cause of Action is dismissed.

### C. JCI's and Carris' Failure to Pay Employee Payroll Taxes (Cause Eleven)

The Eleventh Cause of Action alleges that Carris and JCI violated FINRA Rule 2010, by failing to remit employee payroll taxes to the United States Treasury and other taxing authorities. In *Department of Enforcement v. Shvarts*, the National Adjudicatory

[408] *Thomas Woodley Heath, III v. SEC*, 586 F.3d 122, 134, 2009 U.S. App. LEXIS 24128, at *34 (2d Cir. 2009).

Council ("NAC") applied a two-part test to determine whether the conduct at issue violated NASD Rule 2110 (now FINRA Rule 2010): (i) the misconduct must occur "in the conduct of" the respondent's business; and (ii) the misconduct must violate just and equitable principles of trade.[409]

The Panel finds that JCI"s failure to remit employee payroll taxes clearly relates to the conduct of JCI's business. Securities firms are required to collect and pay employee payroll taxes, and the willful failure to do so is a crime.[410] During 2011, JCI issued Forms W-2 to its employees notifying them of (i) their gross compensation and (ii) the portion of their compensation that JCI withheld to pay their payroll taxes. Carris admitted that JCI was responsible for collecting and paying these taxes for all JCI employees. Contrary to its obligation, JCI stopped making full payments to various taxing authorities for its employees' payroll taxes in early 2011. Although JCI and Carris received notifications from their payroll service provider regarding the payroll tax arrearage to the taxing authorities, neither Carris nor any other JCI representative ensured that the monies were paid to the IRS. Instead, JCI used the monies for other purposes.[411]

The Panel finds that Carris and JCI violated FINRA Rule 2010 by failing to remit employee payroll taxes to the United States Treasury and taxing authorities.

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[409] *Dep't of Enforcement v. Shvarts*, Complaint No. CAF980029, 2000 NASD Discip. LEXIS 6, at *18 (NAC June 2, 2000) (citations omitted); *see Dep't of Enforcement v. DiFrancesco*, Complaint No. 2007009848801, 2010 FINRA Discip. LEXIS 37, at *15-16 (NAC Dec. 17, 2010) (analyzing respondent's conduct under Rule 2110 (now Rule 2010) to determine if his conduct was: (i) business-related; and (ii) inconsistent with high standards of commercial honor and just and equitable principles of trade).

[410] "Willful failure to collect or pay over tax" is a felony offense punishable by a maximum of five years' imprisonment and a $10,000 fine. 26 U.S.C. § 7202.

[411] During the time period when JCI failed to pay its employees' payroll taxes, Carris authorized the payment of dividends to Invictus investors even though JCI was operating at a net loss during 2011 and 2012. CX-107; CX-107A; CX-114, at 7; CX-114A, at 8.

### D. JCI's Net Capital Deficiencies (Cause Ten)

The Tenth Cause of Action alleges that JCI willfully violated Section 15 of the Exchange Act, Rule 15c-3 thereunder, and FINRA Rule 2010, by operating without sufficient net capital between November 1, 2011 and August 6, 2012. The Tenth Cause of Action also charges Carris with violating FINRA Rule 2010, by causing JCI to operate without sufficient net capital.

A firm's net capital is a measure of its liquidity and its ability to meet its financial obligations. Through Exchange Act Rule 15c3-1,[412] the SEC imposes minimum net capital requirements on broker-dealers in order to protect customers and other market participants from broker-dealer failures.[413] The net capital rule "is designed to insure that a broker-dealer will have sufficient liquid assets to satisfy its indebtedness, particularly the claims of its customers."[414] The net capital rule involves "fundamental safeguards" and is "one of the most important weapons in the [regulatory] arsenal to protect investors."[415]

Although the net capital rule can be complex to apply, since it requires various calculations in various circumstances, certain basic principles are well-known, including that a broker-dealer is required to maintain a minimum level of net capital at all times.[416]

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[412] 17 C.F.R. § 240.15c3-1.

[413] *Fox & Co. Inv., Inc.*, 2005 SEC LEXIS 2822, at *18.

[414] *Dep't of Enforcement v. Block*, Complaint No. C05990026, 2001 NASD Discip. LEXIS 35, at *32 (NAC Aug. 16, 2001).

[415] *Fox & Co. Inv., Inc.*, 2005 SEC LEXIS 2822, at *40 (quoting *Blaise D'Antoni & Associates, Inc. v. SEC*, 289 F.2d 276, 277 (5th Cir. 1961)).

[416] The net capital rule begins with the statement that a securities broker-dealer must maintain its minimum net capital "at all times." 17 C.F.R. § 240.15c3-1(a); *see also* NASD Notice to Members 07-16 (Apr. 2007) (SEC's net capital rule requires a broker-dealer to maintain its required net capital continuously), *available at* http://www.finra.org/Industry/Regulation/Notices/2007/P018898.

JCI was subject to a minimum net capital requirement of $100,000. The net capital rule prohibited JCI from continuing to engage in a securities business if its net capital fell below that amount.[417] As reflected in the First, Second, and Third Deficiency Notices discussed above, JCI operated with deficient net capital between November 1, 2011 and March 19, 2012, between July 1 and July 24, 2012, and on August 6, 2012. All of the Deficiency Notices state that JCI learned of the net capital deficiency the day before the filing of the Deficiency Notices; however, at least with regard to the First Deficiency Notice, the infusions of capital contributions reflect that JCI was aware of the problem approximately two weeks before the filing of the Deficiency Notice.

Carris argues that he cannot be held personally liable under SEC Rule 15c-3 for JCI's net capital violations because he was not JCI's FINOP and did not insert himself into the process of calculating JCI's net capital position.[418] However, the SEC has held that even if there has been an effective delegation of financial compliance responsibilities, a controlling executive who is directly involved in net capital violations incurs responsibility for those violations.[419]

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[417] *Dep't of Enforcement v. Inv. Management Corp.*, Complaint No. C3A010045, 2003 NASD Discip. LEXIS 47, at *13-14 (NAC Dec. 15, 2003).

[418] Carris-JCI Post-Hrg Br. at 46-48.

[419] *Block*, 2001 NASD Discip. LEXIS 35, at *16 (NAC Aug. 16, 2001) (citing *William H. Gerhauser*, 53 S.E.C. 933 (1998) and *Kirk A. Knapp*, 51 S.E.C. 115 (1992)). In *Gerhauser*, the SEC found the firm's president liable for the net capital violation because he had given the FINOP incorrect information about the firm's net capital obligations. *Gerhauser*, 53 S.E.C. at 940-42. In *Knapp*, the SEC found respondent liable for the firm's net capital and recordkeeping violations because he had proposed many of the violative transactions and, as chief shareholder and executive, he controlled the FINOP and dictated the operations of the firm. *Knapp*, 51 S.E.C. at 126.

Carris was the president and CEO of JCI. As such, he was responsible for ensuring that JCI complied with all applicable rules and regulations.[420] Here, by at least March 9, 2012, Carris was aware of the first net capital deficiency. With that knowledge, he did not cease JCI's operations. Rather, he continued operating JCI and used the monies flowing into JCI from sales of Invictus securities to cure the net capital deficiency. It is also clear that he knew the amount of the net capital deficiency because he continued making capital contributions with Invictus investor funds through March 19, when an Invictus investor purchased a sufficient amount of Invictus securities to cover the net capital deficiency. At that point, Carris' authorizations of the capital contributions also stopped. Carris' actions were deliberate.

The Panel finds that, between March 9 and March 19, 2012, Carris violated Rule 2010 by causing JCI to operate without sufficient capital. The Panel also finds that JCI violated Section 15 of the Exchange Act, and Rule 15c-3 thereunder, and Rule 2010, by operating without sufficient net capital between November 1, 2011 and March 19, 2012, between July 1 and July 24, 2012, and on August 6, 2012.[421] Applying the willfulness standard delineated above, the Panel finds JCI's violation was willful.[422] Instead of ceasing operations, JCI used Invictus investors' monies that it recently secured through sales of Invictus securities to cure JCI's net capital deficiencies and continue operating.

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[420] *See Block*, 2001 NASD Discip. LEXIS 35, *25 (stating that it is well settled that presidents of securities firms bear a heavy responsibility to ensure that broker-dealers comply with all applicable rules and regulations); *see also James Michael Brown*, 50 S.E.C. 1322 (1992) (rejecting defense that president of firm should be excused because he lacked a meaningful role in firm's management), *aff'd*, *Brown v. SEC*, 21 F.3d 1124 (11th Cir. 1994) (unpublished table decision).

[421] Section 15 of the Exchange Act, and Rule 15c-3 thereunder do not require proof of intent or scienter. *Harrison Securities, Inc*., 2004 SEC LEXIS 2145, at *124 (Sept. 21, 2004).

[422] *See supra* footnotes 405 and 406 and accompanying text discussing the willfulness standard.

### E. JCI's and Carris' Securities Fraud in Connection with Invictus (Cause Two)

The Second Cause of Action alleges that Carris and JCI willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, from October 2010 through September 2012, by defrauding customers in connection with the sale of Invictus stock and notes. The Amended Complaint alleges that Carris failed to disclose the poor financial condition of Invictus and JCI, failed to disclose Carris' personal use of firm funds, and misled investors regarding Invictus' financial condition by paying dividends to Invictus' early investors with funds contributed by new investors.

#### 1. Legal Standard

Section 10(b) of the Exchange Act broadly proscribes securities fraud in violation of rules promulgated by the SEC, including Rule 10b-5. Section 10(b) provides, "[i]t shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails … [t]o use or employ, in connection with the purchase or sale of any security … any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."[423] Rule 10b-5 makes it unlawful "[t]o make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading."[424] A Rule 10b-5 violation requires proof of the following: (i) a false statement or a misleading

[423] 15 U.S.C. § 78j.

[424] 17 C.F.R. § 240.10b-5.

omission; (ii) of a material fact; (iii) made with the requisite scienter or state of mind; (iv) using the jurisdictional means; (v) in connection with the purchase or sale of a security.[425]

FINRA Rule 2020 proscribes fraud in language similar to Section 10(b), stating: "No member shall effect any transaction in, or induce the purchase or sale of, any security by means of any manipulative, deceptive or other fraudulent device or contrivance."[426] A violation of Section 10(b) is also a violation of FINRA Rule 2020.[427] Committing fraud and other violations of law and FINRA Rules is inconsistent with the high standards of ethical conduct required by Rule 2110.[428]

### 2. JCI and Carris Made Material Misstatements and Omissions in Connection with the Sale of Invictus Securities

Enforcement established the elements of securities fraud under Section 10(b) of the Exchange Act, and Rule 10b-5 thereunder.

#### (a) False Statements and Misleading Omissions

The false statements and misleading omissions in the Invictus Offerings related to the following areas: (i) the financial condition of Invictus and JCI, (ii) the use of

[425] *Gebhart v. SEC*, 595 F.3d 1034, 1040 and n.8 (9th Cir. 2010) (affirming SEC decision in NASD (now FINRA) disciplinary case charging Rule 10b-5 fraud and distinguished enforcement action from private securities fraud action).

[426] Unlike Exchange Act Rule 10b-5(b), FINRA's antifraud rule language under Rule 2020 does not require that a respondent be the "maker" of a false statement or misleading omission. *See Dep't of Enforcement v. Fillet*, 2013 FINRA Discip. LEXIS 26, at *37-38 (NAC Oct. 2, 2013) (discussing the distinction between Rule 10b-5 and NASD Rule 2120 (now FINRA Rule 2020)).

[427] *Dep't of Enforcement v. Thomas Weisel Partners, LLC*, Complaint No. 2008014621701, 2013 FINRA Discip. LEXIS 1, at *15 (NAC Feb. 15, 2013).

[428] *Colonial Realty Corp. v. Bache & Co.*, 358 F.2d 178, 182 (2d Cir.), *cert. denied*, 385 U.S. 817 (1966).

proceeds, (iii) and the payment of dividends.[429]

**(1) Financial Condition of Invictus and JCI**

The Panel concludes that Carris made false statements and omissions in the Invictus PPMs and subscription documents regarding JCI's revenues and operating history. In both the Series A and B Offerings, the PPMs stated that JCI was a "development stage company" with "no revenue from operations" and "no operating history." These statements were false. When JCI first sold the Series A Offering, it had been in operation for nearly sixteen months, was generating revenue, and incurring operating expenses. Its 2009 audited financial statements reflected $649,012 in revenues and $651,273 in operating expenses. When JCI sold the Series B Offering, it had been in operation for 19 months. At that time, it possessed both the 2009 and 2010 audited financial statements, which reflected revenues and operating expenses.

The SEC has held that the fact that a recommended security had incurred losses was important to a reasonable investor and thus a material fact that was required to be disclosed.[430] In this case, not only was JCI fully operational, it had incurred losses that were steadily increasing. For example, JCI's 2009 financial statement reported a net loss of $2,328. In the third quarter of 2010, it incurred a net loss of $54,000. In October 2010, when JCI made its first sale of the Series A Offering, its monthly net loss was greater

[429] To the extent that Respondents Carris and JCI argue that certain disclosures in the PPMs and subscription documents corrected any false or misleading statement, they are wrong. For example, the disclosure that the "Company will retain broad discretion in the allocation of the net proceeds of the Offering" was not sufficient to inform investors that Carris was already using investor proceeds to pay his personal expenses that were charged to JCI's credit and debit cards. CX-96, at 24; *cf., Deng v. 278 Gramercy Park Group, LLC*, 2014 U.S. Dist. LEXIS 74156, at *15-16 (S.D.N.Y. May 30, 2014) (disclosure in PPM for real estate project that manager had "complete discretion" on how to apply the net proceeds of an offering did not reveal that proceeds were used for non-project purposes).

[430] *Dane S. Faber*, 57 S.E.C. 297, 306-07 (2004).

than $283,000. And, the 2010 audited financial statements reflected net losses of $785,292. The Series A and B PPMs omitted any specific information on JCI's finances, including its losses. Neither PPM contained any financial statements or FOCUS reports for JCI.

Carris also failed to disclose that JCI was not in net capital compliance. Although JCI was out of net capital compliance prior to Carris' creation of the Bridge Offering and throughout every sale of the Bridge Offering notes, the subscription documents omitted any reference to JCI's net capital deficiencies.

**(2) Use of Proceeds**

Carris omitted important information in the Use of Proceeds section in the Offerings relating to personal expenses, payments to prior Invictus investors, and capital contributions. First, all of the Offerings neglected to disclose that a portion of the proceeds were applied to personal expenses. Second, the Series A, Series B, and Bridge Offerings failed to disclose that investor funds would be used to pay dividends to previous Invictus investors. Third, the Bridge and Series C Offerings failed to disclose that investor funds would be applied to JCI's net capital deficiencies.

**(3) Dividends**

The Dividends section in the Series A, B, and C Offerings omitted information that made the Offerings misleading. The Series A and B PPMs stated that any determination to pay dividends would be dependent upon "our financial condition, results of operations, capital requirements and such other factors as the Board [(i.e., Carris)] deems relevant" and that dividends would only be paid from "legally available funds." While the Offerings stated that Carris had discretion to pay dividends, the Series A and B Offerings did not state that Invictus would pay dividends if it or JCI was losing money or

was out of net capital compliance. Accordingly, investors receiving a dividend payment could easily but erroneously assume that Invictus and the broker-dealer JCI were financially sound. Despite JCI's negative financial condition, Carris paid dividends to the Series A and B investors. Dividend payments were also made to Series C investors beginning in April 2012 despite JCI's persistent unprofitability. The Panel finds that the payment of dividends was used as a means to attract additional investments in the Invictus Offerings.

**(b) Materiality**

The question of materiality is an objective one, involving the significance of an omitted or misrepresented fact to a reasonable investor.[431] A fact is material if there is a substantial likelihood that a reasonable investor would have considered the fact important in making an investment decision, and disclosure of the omitted fact would have significantly altered the total mix of information available.[432] Carris made misstatements and omissions regarding the financial condition of Invictus and JCI, the use of proceeds, and the payment of dividends. The materiality of such facts relating to a company's "financial condition, solvency and profitability is not subject to serious challenge."[433] The Panel finds that the false statements and omissions were material. Although the PPMs

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[431] *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 445 (1976). *Amgen, Inc. v. Conn. Ret. Plans & Tr. Funds*, 133 S. Ct. 1184, 1195-96 (Feb. 27, 2013); *Matrixx Initiatives, Inc. v. Siracusano*, 131 S. Ct. 1309, 1318 (2011).

Materiality can be evaluated under this objective standard, considering how a reasonable investor would view the false statement or misleading omission, without testimony from any particular customer. *Dep't of Enforcement v. Scholander*, Complaint No. 2009019108901, 2013 FINRA Discip. LEXIS 37, at *64-65 and n.122 (OHO Aug. 16, 2013) *appeal docketed* (Aug. 30, 2013) (citing *RichMark Capital Corp.*, Exchange Act Release No. 48758, 2003 SEC LEXIS 2650, at *15 (Nov. 7, 2003)), *aff'd*, 86 F. App'x 744 (5th Cir. 2004).

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

[433] *SEC v. Murphy*, 626 F.2d 633, 653 (9th Cir. 1980).

warned investors that the securities were speculative and an investment in Invictus could result in losses, the PPMs were insufficient to notify potential investors of JCI's specific, significant financial and operational issues.

**(c) Scienter**

There is substantial evidence supporting the Panel's conclusion that Carris intentionally omitted material information when he created the Offering PPMs. However, at a minimum, he acted recklessly, thereby satisfying the scienter requirement under the antifraud rules.[434] The courts have defined recklessness as "an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it."[435]

Carris was an experienced broker who knew or should have known the material significance of his misstatements and the facts he withheld from the Invictus investors. He was fully familiar with the Invictus Offerings. In fact, he acknowledged that he was responsible for the content of the offering documents. Carris intentionally, or at least recklessly, withheld specific information regarding the actual financial condition of JCI in the Invictus Offerings. For example, although the Series A and B PPMs were similar to the Bridge Offering subscription documents, when issuing the Bridge Offering, Carris

[434] *Hollinger v. Titan Capital Corp.*, 914 F.2d 1564 (9th Cir. 1990) (en banc).

[435] *See, e.g., Howard v. Everex, Inc.*, 228 F.3d 1057, 1063 (9th Cir. 2000).

removed the section discussing the firm's net capital requirements.[436] This coincided with the time period that JCI was out of net capital compliance—a fact that Carris hid from the investors in the Bridge Offering. Carris omitted the same information when issuing the First Series C Offering. JCI was still out of net capital compliance when Carris created the First Series C Offering. Even when Carris was using Invictus investor funds to cure JCI's net capital deficiencies, there is no evidence that Carris took any steps to ensure that the investors in the Bridge Offering, and the initial investors in the First Series C Offering, were aware that JCI was out of net capital compliance and should not have been conducting a securities business at all.[437] Carris' scienter is attributable to JCI.[438]

**(d) Jurisdictional Means**

Carris and JCI marketed and sold the Invictus Offerings through the PPMs and subscription documents, using the U.S. mail and telephone calls.[439]

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[436] As noted in Section IV, subpart D, the Panel found that, at least as of March 9, 2012, Carris was aware of the first net capital deficiency; however, the Panel also notes that the Bridge Offering documents, dated December 1, 2011, and issued one month after the start of the first net capital deficiency period, did not contain a section on the net capital requirements.

[437] *Kenneth R. Ward*, Exchange Act Release No. 47535, 2003 SEC LEXIS 687, at *39 (Mar. 19, 2003) (finding scienter established when representative was aware of material information and failed to make appropriate disclosures to customers), *aff'd*, 75 F. App'x 320 (5th Cir. 2003).

[438] *See Stratocomm Corp.*, 2014 U.S. Dist. LEXIS 20855, at *38 (N.D. N.Y. Feb. 19, 2014) (scienter of company officer attributed to company where officer acting within apparent authority) (citing *Adams v. Kinder-Morgan, Inc.*, 340 F.3d 1083, 1106-07 (10th Cir. 2003)); *Kirk A. Knapp*, 50 S.E.C. 858, 860 n.7 (1992) (noting that NASD properly attributed scienter of firm's owner to firm); *SEC v. Blinder, Robinson & Co.*, 542 F. Supp. 468, 477 (D. Colo. 1982) (holding, for purposes of establishing scienter, that president and principal shareholder's mental state is imputed to the firm).

[439] *See SEC v. Softpoint, Inc.*, 958 F. Supp. 846, 865 (S.D.N.Y. 1997) (determining that the jurisdictional requirements of the federal antifraud provisions are interpreted broadly and are satisfied by intrastate telephone calls or the use of the U.S. mail), *aff'd*, 159 F.3d 1348 (2d Cir. 1998).

#### (e) Sale of a Security

All of the false statements and omissions occurred in connection with the sale of a security. Each of the offering documents described the Invictus shares and notes as securities.[440]

### 3. Conclusion

The Panel finds that Carris and JCI willfully[441] violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, from October 2010 through September 2012, by defrauding customers in connection with the sale of Invictus stock and notes.[442]

## F. JCI, Carris, and Tkatchenko Recommended Invictus Securities Without a Reasonable Basis (Cause Five)

The Fifth Cause of Action alleges that Carris, Tkatchenko, and JCI violated NASD Rule 2310, and FINRA Rules 2111 and 2010, during the Offering Period by recommending the purchase of Invictus stock and notes to customers during the ongoing offerings without a reasonable basis.

FINRA Rule 2111 and its predecessor NASD Rule 2310 require a member recommending an investment to have reasonable grounds for believing that the investment is suitable for a customer. However, prior to making a customer-specific suitability determination, a registered representative must ensure that he has a reasonable

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[440] *See supra* footnote 122.

[441] The Panel finds that Carris' and JCI's misconduct was willful. *See supra* footnotes 405 and 406 and accompanying text discussing the willfulness standard.

[442] The Panel finds that Carris was the "maker" of the misstatements as required under Exchange Act Rule 10b-5(b). Under Rule 2020, Carris is liable if he induced the purchase or sale of a security through the "use" of a false statement, even if it was made by another. The Panel finds that Carris and JCI also violated Rule 2020 by inducing investors to purchase Invictus securities through the "use" of false statements and material omissions.

basis for recommending the investment product to his client.[443] "A recommendation may lack 'reasonable-basis' suitability if the broker: (i) fails to understand the transaction, which can result from, among other things, a failure to conduct a reasonable investigation concerning the security; or (ii) recommends a security that is not suitable for any investors."[444] When conducting a reasonable-basis suitability analysis, a registered representative "must perform appropriate due diligence to ensure that [he] understands the nature of the product, as well as the potential risks and rewards associated with the product."[445] A violation of FINRA Rule 2111, or NASD Rule 2310, is also a violation of FINRA Rule 2010.[446]

As discussed above, the Panel determined that Carris and JCI committed securities fraud through their false statements and material omissions made in connection with the sale of Invictus securities. Securities sold through fraudulent means are not suitable for any investor. Regarding Tkatchenko, the Panel finds that he failed to conduct a reasonable investigation into the Invictus Offerings and JCI prior to recommending the Invictus securities.

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[443] *Dep't of Enforcement v. Cody*, Complaint No. 2005003188901, 2010 FINRA Discip. LEXIS 8, *19 (NAC May 10, 2010), *aff'd*, 2011 SEC LEXIS 1862 (May 27, 2011) (citing *Michael Frederick Siegel*, Exchange Act Release No. 58737, 2008 SEC LEXIS 2459, at *28 (Oct. 6, 2008), *aff'd in relevant part*, 592 F.3d 147 (D.C. Cir. 2010)).

[444] *Dep't of Enforcement v. Siegel*, Complaint No. C05020055, 2007 NASD Discip. LEXIS 20, at *38 (NAC May 11, 2007), *aff'd*, Exchange Act Release No. 58737, 2008 SEC LEXIS 2459 (Oct. 6, 2008), *aff'd in relevant part*, 592 F.3d 147 (D.C. Cir. 2010).

[445] NASD Notice to Members 03-71 (Nov. 2003), *available at* http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p003070.pdf. The type of due diligence that is appropriate will vary from product to product. *Id*. Common features that members must understand include, but are not limited to, the following: (i) tax consequences of the product; and (ii) principal, return, and interest rate risks and the factors that determine those risks. *Id*.

[446] *See Cody*, Admin. Proc. File No. 3-13932, 2011 SEC LEXIS 1862, at *26 (May 27, 2011).

FINRA has reminded brokers of their obligation to conduct a reasonable investigation of issuers and the securities recommended in offerings.[447] In recommending an investment in a private placement, a registered representative represents to a potential investor "that a reasonable investigation has been made and that his recommendation rests on the conclusions based on such investigation."[448]

Here, Tkatchenko primarily relied on Carris. When doing so, he knew that Carris held dual roles. Carris created the Invictus Offerings, and he was the sole principal of Invictus. Carris was also the president and CEO of JCI, Invictus' exclusive placement agent. Tkatchenko's reliance on Carris did not constitute a reasonable investigation of the Invictus securities. Tkatchenko was not entitled to rely on Carris as the primary source of information about the Invictus Offerings in light of Carris' obvious self-interest. In addition, Carris was Tkatchenko's supervisor. As the SEC stressed, "statements made by a salesman's superiors [are not] an adequate basis for representations made to investors"[449]

A registered representative is required to disclose material facts that are "reasonably ascertainable."[450] JCI's financial condition, and in particular its losses and net capital position, were reasonably ascertainable by Tkatchenko. Despite his access to JCI's financial documentation, Tkatchenko recommended that his customers purchase over $1.5 million of Invictus securities in the Series A and B Offerings without reviewing

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[447] *See* FINRA Regulatory Notice 10-22 (Apr. 2010), *available at* http://www.finra.org/Industry/Regulation/Notices/2010/P121299.

[448] *Hanly v. SEC*, 415 F.2d 589, 597 (2d Cir. 1969); *see* FINRA Regulatory Notice 10-22.

[449] *Dan King Brainard*, 47 S.E.C. 991, 997 (1983); *see J. Stephen Stout*, 54 S.E.C. 888, 911-12 & n.53, 2000 SEC LEXIS 2119, at *49 (2000) (stating that a broker "cannot excuse his failure to conduct [a suitability] inquiry by claiming that he blindly relied on his firm's recommendations").

[450] *Hanly*, 415 F.2d at 597.

any of JCI's financial records. As the SEC has held, a registered representative "cannot recommend an unknown or little known security unless he has seen reliable financial data that supply him with a reasonable basis for his recommendation."[451] Tkatchenko could and should have requested and reviewed such information.

Tkatchenko explained that JCI's finances were not relevant because JCI was a "start-up company," but a broker's personal belief in an investment does not excuse a failure to disclose material information.[452] When Carris disclosed JCI's bleak financial condition by providing financial statements with the Bridge Offering subscription documentation, Tkatchenko failed to determine how Invictus could pay dividends to the investors in light of JCI's losses. Nevertheless, Tkatchenko recommended Invictus securities to investors in the Bridge Offering and the First Series C Offering.

The Panel concludes that Carris, Tkatchenko, and JCI violated NASD Rule 2310 and FINRA Rules 2111 and 2010, during the Offering Period, by recommending the purchase of Invictus securities to customers without a reasonable basis.

### G. JCI, Carris, and Barter Manipulated Fibrocell Stock (Cause One)

The First Cause of Action alleges that Carris, Barter, and JCI willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by engaging in manipulative stock trading of Fibrocell while JCI was acting as a placement agent for Fibrocell. Specifically, the First Cause of Action alleges that, during the Manipulation Period, Carris and Barter manipulated the price of Fibrocell by

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[451] *Dan King Brainard*, 47 S.E.C. at 997 n.18 (citations omitted).

[452] *See Alexander Reid & Co.*, 40 S.E.C. 986, 990-91 (1962) (stating that "it is not a sufficient excuse that a dealer personally believes the representation for which he has no adequate basis"); *Faber,* 57 S.E.C. at 309 (noting that a personal belief in an investment does not excuse a failure to disclose material information to customers).

engaging in pre-arranged trading and improperly placing shares of Fibrocell stock in the accounts of JCI customers, in order to create the false appearance of trading volume and to maintain the share price at an artificial level.

Exchange Act Section 10(b), Rule 10b-5, and FINRA Rule 2020 prohibit fraudulent and deceptive acts and practices in connection with the offer, purchase, or sale of a security.[453] Manipulation "connotes intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities."[454] "A person contemplating or making a distribution has an obvious incentive to artificially influence the market price of the securities in order to facilitate the distribution or to increase its profitability."[455] The SEC has held that "where a person who has a substantial interest in the success of a distribution takes active steps to increase the price of the security, a prima facie case of manipulative purpose exists."[456]

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[453] In addition to prohibiting nondisclosure and false and misleading statements, Exchange Act Rule 10b-5 prohibits "any device, scheme, or artifice to defraud" or any conduct "which operates or would operate as a fraud or deceit upon any person." Violations of Section 10(b) and Exchange Act Rule 10b-5 must involve the use of any means or instrumentalities of transportation or communication in interstate commerce, or the mails, or any facility of any national securities exchange. *See, e.g., SEC v. Hasho*, 784 F. Supp. 1059, 1106 (S.D.N.Y. 1992). In this case, the requirement of interstate commerce is satisfied. The Fibrocell trades at issue were traded on the OTCBB, and JCI used the U.S. mail to send trade confirmations to its customers for both the reported and unreported trades.

[454] *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 199 (1976); *Swartwood Hesse, Inc*., 50 S.E.C. 1301, 1307 (1992) ("Manipulation is the creation of deceptive value or market activity for a security, accomplished by an intentional interference with the free forces of supply and demand."); *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 476 (1977) (explaining that manipulation refers to conduct intended to mislead investors "by artificially affecting market activity").

[455] *Bruns, Nordeman & Co*., 40 S.E.C. 652, 660 n.11 (1961).

[456] *Id*. As early as 1949, the SEC found manipulation based on the purpose behind the actions of a market participant. *Halsey, Stuart & Co*., 30 S.E.C. 106, 124 (1949) ("purpose must be inferred when hope, belief, and motive are implemented by activity objectively resulting in market support, price raising, sales at higher prices and the protection of inventory").

The Panel has considered the factual details here, and the possible inferences to be drawn from them, and finds that Carris, Barter, and JCI engaged in a manipulation.[457] Fibrocell was a thinly-traded stock, and JCI dominated the market for Fibrocell. The Fibrocell trading activity (both reported and unreported) occurred in conjunction with the Fibrocell PIPE offering. JCI was the placement agent for the offering, and Carris had a financial interest in ensuring the success of the offering.

At the start of the Manipulation Period, JCI was not in sound financial condition. To alleviate JCI's financial problems, Carris sold 160,000 of his Fibrocell shares and infused money into JCI. Carris knew that liquidating his Fibrocell shares or shares of his customers would cause the share price to decline sharply because Fibrocell was illiquid and thinly traded. This in turn would threaten the success of the PIPE Offering. In response to this problem, Carris intentionally employed manipulative and deceptive practices to create artificial demand for, and restrict the supply of, Fibrocell stock in the market. Carris restricted the supply of Fibrocell by purchasing and selling Fibrocell stock for his customers without their knowledge or authorization. Because the Fibrocell stock purchases were unauthorized, the customers never paid for the trades. When Carris, Barter, and JCI received sell-out notices from JCI's clearing firm for the unfunded purchases, Carris either (i) avoided selling the shares into the market by buying and selling Fibrocell shares via unreported trades into other customer accounts, or (ii) when forced to sell into the market, paired sell orders with corresponding buy orders, the majority of which were limit orders sent to the same market maker with no commission

[457] *See, e.g., Brooklyn Capital & Sec. Trading, Inc.*, 52 S.E.C. 1286, 1290 (1997) ("In determining whether a manipulation has occurred, we have depended on inferences drawn from a mass of factual detail including patterns of behavior, apparent irregularities, and from trading data." (internal quotations omitted)).

charged to the customer. Through these trades, the Fibrocell market appeared active. Because Barter sent the orders to the market as matched orders, there was little risk of a sharp decline in the price of Fibrocell.

Carris claims he had no involvement in the manipulative trading of Fibrocell. He believes that MG, a back office administrative employee, did the manipulative trading.[458] The Panel does not credit Carris' self-serving explanation. Carris was the registered representative for all of the customers who purportedly traded Fibrocell. Carris' direct involvement is seen from the beginning of the Manipulation Period when he personally sold 80,000 shares on May 18, and another 80,000 shares on May 21, 2010. Another Carris customer also sold 35,900 shares on May 18. When submitting these trades for execution on the market, Carris paired them with corresponding buy orders. On May 18, another one of Carris' customers bought 115,900 shares in an unsolicited, unreported, and unfunded transaction. That trade equaled Carris' 80,000 share sell order and the customer's 35,900 share sell order. After execution of the May 18 and May 21 orders, he used the proceeds from those sales to infuse money into JCI. The use of matching orders and unfunded, unauthorized customer purchases to support the price of Fibrocell, and prevent a sharp price decline, occurred repeatedly throughout the Manipulation Period.

Barter was instrumental in the Fibrocell manipulation. During the Manipulation Period, he knew that JCI was the placement agent for the Fibrocell PIPE Offering. He also knew that JCI dominated the market in Fibrocell. With that knowledge, he caused approximately 58 matched orders, the majority of which were limit orders, to be executed

[458] Tr. (Carris) 3525-26, 3549.

in the OTCBB market.[459] He sent these orders to the same market maker generally within less than one minute of each other. Time and time again, he observed that the orders were immediately executed.

Barter also ignored several red flags that should have alerted him that the Fibrocell orders he sent to the market were not *bona fide* orders. First, all of the 58 buy and sell orders were for identical share amounts and virtually all were marked "unsolicited." In addition, most of the matched orders did not result in the charging of a commission. Second, on July 29, the trading department received an email from a JCI customer indicating that she was unaware of how Fibrocell shares appeared in her account. Third, Barter repeatedly traded the same large blocks of Fibrocell stocks, typically in matched limit orders. In August and September 2010, he traded the 133,000 share block five times in a five week period.[460] The repeated buys and sells of the 133,000 share block coincided with Regulation T sell-out notices from JCI's clearing firm. Although Barter claimed not to have read any of the sell-out notices from the clearing firm, he was at least aware that the clearing firm was sending such notices regarding unfunded purchases during the Manipulation Period.[461] Barter knew or should have known that such activity was suspicious. By signing the new-hire compliance agreement, Barter agreed that he would not enter orders of substantially the same size, at

[459] The day after effecting the July 29 matched trades, Barter supported the new $.80 market price by sending 4,000 share matched limit orders for execution, within 30 seconds of each other to the same maker, priced at $.795-.80. CX-248A, at 22; CX-207 (rows 904 and 905); CX-1B, at17; RX-39, at 74.

[460] *See* CX-1B; RX-39; Attachment A. Barter also repeatedly traded blocks of Fibrocell in the amount of 85,900 shares (which grew to 109,900 shares) and 57,201 shares. CX-1B; RX-39; Attachment A.

[461] In the beginning of the Manipulation Period, Barter forwarded some of the sell-out notices to MG. Tr. (Barter) 2141-47. Barter also acknowledged receiving such notices as recently as the week before the hearing. Tr. (Barter) 2142.

substantially the same time and substantially the same price, for the purpose of creating a false or misleading appearance of active trading in a security or a false or misleading appearance with respect to the market security. In this instance, the prearranged Fibrocell trading was not *bona fide* and was thus done to support the price during the PIPE Offering. At a minimum, Barter acted recklessly, thereby satisfying the scienter requirement under the antifraud rules.

In light of the foregoing, the Panel concludes that Carris, Barter, and JCI willfully[462] violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by engaging in manipulative stock trading of Fibrocell while JCI was acting as a placement agent for Fibrocell.[463]

### H. JCI Did Not Commit Fraud In Connection With Sales of Fibrocell By Carris and Another JCI Principal (Cause Three); Carris Did Not Aid and Abet the Alleged Fraud (Cause Four); and Hechler Did Not Fail to Provide Guidance Regarding the Alleged Conflicts of Interest (Cause Nine in part)

The Third Cause of Action alleges that JCI willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by failing to disclose material adverse conflict of interest information to JCI customers who were purchasing Fibrocell. Specifically, the Amended Complaint alleges that, during the Liquidation Period, JCI committed securities fraud by failing to notify its customers that Carris and DB were selling personally held shares of Fibrocell common stock while JCI representatives were soliciting customers to buy shares of Fibrocell common stock. The Panel determines that the evidence fails to support this cause of action.

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[462] The Panel finds that Carris' and JCI's misconduct was willful. *See supra* footnote 405 and 406 and accompanying text discussing the willfulness standard.

[463] Carris' scienter is attributable to JCI. *See supra* footnote 439.

When an investor is presented with a recommendation to purchase or sell a security, the registered representative making the recommendation is required to provide, amongst other things, a disclosure of material adverse facts, including "self-interest that could influence a salesman's recommendation."[464] The disclosure requirement requires that there be a conflict of some sort – a competing economic interest that would affect the recommendation being made by a registered representative. The competing interest must be disclosed so that an investor can weigh the registered representative's motivations for making such a recommendation.[465] The focus is on the registered representative's knowledge when soliciting customers to purchase securities.[466] The instances where a conflict of interest or failure to disclose material facts has been found involve a direct correlation between the solicitation and the adverse interest.[467]

Here, there is no evidence that Carris or DB solicited any orders of Fibrocell during the Liquidation Period. There is also no evidence that anyone making a recommendation to a JCI customer to purchase shares of Fibrocell suffered from a

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[464] *Zwetsch and Evans*, 50 S.E.C. 816, 818 (1991); *see Chasins v. Smith, Barney & Co*., 438 F.2d 1167, 1172 (2d Cir. N.Y. 1970) (noting that an investor "must be permitted to evaluate overlapping motivations through appropriate disclosures, especially where one motivation is economic self-interest").

[465] *See Chasins*, 438 F.2d at 1172 ("An investor who is at least informed of the possibility of such adverse interests, due to his broker's market making in the securities recommended, can question the reasons for the recommendations.").

[466] *Dept. of Market Reg. v. Jerry William Burch*, Complaint No. 2005000324301, 2011 FINRA Discip. LEXIS 16 *27 (NAC July 28, 2011).

[467] *See id*. at *27 (finding a conflict of interest where a registered representative solicited customers to purchase securities his wife was contemporaneously selling and noting that "it was implausible that [the registered representative] did not know [his wife] was selling [the] stock while he was recommending and buying it for customers…"); *Zwetsch and Evans*, 50 S.E.C. 816, at 818 (finding a conflict where two brokers were soliciting customers to purchase shares while simultaneously selling their own shares or recommending that their families sell shares); *Chasins*, 438 F.2d at 1172 (finding a conflict where the firm recommended a security while also making a market in the recommended security) (citations omitted).

conflict or an adverse interest. The registered representatives who solicited purchases of Fibrocell did so without (i) any knowledge that Carris and DB were selling shares, or (ii) any incentive to solicit purchases while Carris sold his shares. During the Liquidation Period, JCI was neither engaged in proprietary trading nor providing investment banking services for Fibrocell.[468]

The Panel concludes that JCI did not violate Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by failing to disclose purportedly adverse conflict of interest information to JCI customers who were purchasing Fibrocell. Accordingly, the Panel dismisses the Third Cause of Action.

The Fourth Cause of Action alleges that Carris willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by aiding and abetting the securities fraud during the Liquidation Period. In light of the fact that the Panel dismissed the Third Cause of Action, the Panel also dismisses the Fourth Cause of Action.[469]

The Ninth Cause of Action, in part, alleges that Hechler violated FINRA Rules 3010 and 2010, by failing to establish, maintain, and enforce a reasonable supervisory system and procedures to detect violations of securities laws and rules concerning conflicts of interest. Specifically the Amended Complaint alleges that Hechler failed to provide any guidance in JCI's January 2013 WSPs concerning disclosure of potential conflicts of interest when registered representatives solicit customers to purchase

[468] *RichMark Capital Corp,* 57 S.E.C. 1, 5, 8-9 (Nov. 7, 2003) (finding a conflict where customers who were solicited to purchase stock were not told that the firm was incentivized to solicit them because of an investment banking agreement).

[469] *See Dep't of Market Regulation v. Proudian*, Complaint No. CMS040165, 2008 FINRA Discip. LEXIS 21, *22-23 (NAC Aug. 7, 2008) (stating that aiding and abetting requires a finding of a primary securities law violation committed by another party or parties).

securities that JCI principals are simultaneously selling.[470] As discussed above, because the Panel determined that there was not a conflict of interest, it also determined that Hechler did not violate FINRA Rules 3010 and 2010. Accordingly, the Panel dismisses this portion of the Ninth Cause of Action.

### I. JCI and Carris Failed to Implement AML Policies and Procedures (Cause Eight)

The Eighth Cause of Action alleges that Carris and JCI violated FINRA Rules 3310(a) and 2010, during the AML Period, by failing to establish and implement AML policies and procedures that can be reasonably expected to detect and cause the reporting of suspicious transactions.

Conduct Rule 3310 requires each member firm to "develop and implement a written anti-money laundering program reasonably designed to achieve and monitor the member's compliance with the requirements of the Bank Secrecy Act [("BSA")] … , and the implementing regulations promulgated thereunder by the Department of the Treasury." Conduct Rule 3310(a) requires each member to establish and implement policies and procedures "that can be reasonably expected to detect and cause the reporting of" suspicious activity and transactions.

Notice to Members ("NTM") 02-21, which provides guidance to member firms concerning AML compliance programs, emphasizes each firm's duty to detect red flags and, if a firm detects any, to "perform additional due diligence before proceeding with the

[470] Am. Compl. ¶¶ 255, 256.

transaction."[471] NTM 02-47,[472] which sets forth the provisions of the final AML rule for suspicious transaction reporting promulgated by Treasury for the securities industry, advises broker-dealers of their duty to file a SAR form for certain suspicious transactions occurring after December 30, 2002. The types of suspicious activity that broker-dealers must report include market manipulation, prearranged or other non-competitive trading, securities fraud, significant wire or other transactions without economic purpose, and wash or other fictitious trading.

The trading at JCI raised red flags during the AML Period, which should have prompted an investigation. During the Manipulation Period, the suspicious trading included market manipulation, prearranged trading through both reported and unreported matched trades, and transactions without an economic purpose such as the numerous unfunded purchases. As exemplified by the trading in the accounts of PB and DB, SF, JF, ES, and HG, which occurred throughout the AML Period, the trading in JCI's customers' accounts included the purchase of penny stocks, the liquidation of those stocks, and the wiring out of the proceeds. At times, the sales of the stock were paired with buy orders, on the same day, in the same amount, and at the same price. Then, the buy order was cancelled leaving only the sell order and the proceeds from that sale. All of the above activity should have triggered an inquiry. However, despite the above suspicious activity (described more fully in section III, subsections F and G), as noted in the April 2011 auditor's annual AML report, JCI, through Carris and Simmons, did not identify any unusual or suspicious activity.

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[471] NASD Notice to Members 02-21 (Apr. 2002), *available at* https://www.finra.org/Industry/Regulation/Notices/2002/p003703

[472] NASD Notice to Members 02-47 (Aug. 2002), *available at* https://www.finra.org/Industry/Regulation/Notices/2002/p003512.

The Panel concludes that Carris and JCI violated FINRA Rules 3310(a) and 2010, throughout the AML Period, by failing to implement AML policies and procedures that can be reasonably expected to detect and cause the reporting of suspicious transactions.

### J. JCI and Carris Failed to Supervise and Implement a Reasonable Supervisory System (Cause Nine)

The Ninth Cause of Action alleges that, from May 2009 through April 2012, JCI and Carris failed to establish, maintain, and enforce an adequate supervisory system, in violation of NASD Rule 3010 and FINRA Rule 2010.[473] The Ninth Cause of Action also alleges that, from January 2010 through the filing of the Amended Complaint, Carris and JCI violated NASD Rule 3010 and FINRA Rule 2010, by failing to adequately supervise the activities of JCI's registered representatives, principals, and associated persons in a manner reasonably designed to achieve compliance by detecting the misconduct in the First Cause of Action (manipulation of Fibrocell), the Second Cause of Action (misstatements and misleading omissions of material fact in connection with the sale of Invictus), the Fifth Cause of Action (no reasonable-basis suitability in connection with the sale of Invictus), the Sixth Cause of Action (books and records violations in connection with Carris' personal charges), the Tenth Cause of Action (net capital violations), and the Eleventh Cause of Action (failure to remit payroll taxes).

"Assuring proper supervision is a critical component of broker-dealer operations."[474] NASD Rule 3010 requires JCI and Carris to establish a "system to supervise the activities of each registered representative, registered principal, and other associated person that is reasonably designed to achieve compliance with applicable

[473] Am. Compl. ¶ 10.

[474] *Richard F. Kresge*, Exchange Act Release No. 55988, 2007 SEC LEXIS 1407, at *27 (June 29, 2007).

securities laws and regulations, and with applicable NASD Rules."[475] "The standard of 'reasonable' supervision is determined based on the particular circumstances of each case."[476] A violation of NASD Rule 3010 is also a violation of FINRA Rule 2010.[477]

"It is especially imperative that those in authority exercise particular vigilance when indications of irregularity reach their attention."[478] As president and CEO, as well as CCO for a portion of time, Carris was in a position of authority. "The duty of supervision includes the responsibility to *investigate 'red flags'* that suggest that misconduct may be occurring and to *act* upon the results of such investigation."[479] Carris failed to do so. During the Manipulation Period, Carris ignored red flags, such as unfunded customer purchases and matched trades, that would have alerted him that the trading activity in his customers' accounts was improper. Regarding the sales of Invictus securities, Carris failed to ensure that (i) the Invictus offering materials were accurate and complete, and (ii) JCI and its registered representatives had a reasonable basis for recommending them. He used JCI's corporate credit and debit cards, but then failed to submit expense reports or monitor how the expenses were characterized in the firm's books and records. Carris failed to properly supervise JCI's net capital compliance even though he had to infuse significant sums of money into JCI. Lastly, Carris ignored

[475] NASD Rule 3010(a).

[476] *Ronald Pellegrino*, Exchange Act Release No. 59125, 2008 SEC LEXIS 2843, at *32-33 (Dec. 19, 2008) (internal quotation marks and brackets omitted); *Christopher Benz*, 52 S.E.C. 1280, 1284 (1997) (citing *Consol. Inv. Servs., Inc.*, 52 S.E.C. 582 (1996)).

[477] *Dep't of Enforcement v. Midas Sec, LLC*, Complaint No. 2005000075703, 2011 FINRA Discip. LEXIS 62, at *21-23 (N.A.C. Mar. 3, 2011).

[478] *Dennis S. Kaminski*, Exchange Act Release No. 65347, 2011 SEC LEXIS 3225, at *25-26 (Sept. 16, 2011).

[479] *Id.* at *25 (quoting *Michael T. Studer*, 57 S.E.C. 1011, 1023-24 (2004)) (emphasis added).

notifications from JCI's payroll service provider regarding unpaid employee payroll taxes.

The Panel concludes that Carris and JCI failed to establish, maintain, and enforce a reasonable supervisory system. They also failed to supervise JCI's registered representatives, principals, and associated persons in a manner reasonably designed to achieve compliance by preventing and detecting the misconduct in the First Cause of Action (manipulation of Fibrocell), the Second Cause of Action (misstatements and misleading omissions of material fact in connection with the sale of Invictus), the Fifth Cause of Action (no reasonable-basis suitability in connection with the sale of Invictus), the Sixth Cause of Action (books and records violation in connection with Carris' personal charges), the Tenth Cause of Action (net capital violations), and the Eleventh Cause of Action (failure to remit payroll taxes).[480] Accordingly, the Panel finds that Carris and JCI violated NASD Rule 3010 and FINRA Rule 2010.

## V. SANCTIONS

In considering the appropriate sanction for a violation, adjudicators in FINRA disciplinary proceedings look to FINRA's Sanction Guidelines. The Guidelines contain a range of sanctions for particular violations, depending on the circumstances. They also contain General Principles, applicable in all cases, and overarching Principal Considerations.[481]

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[480] *See Dep't of Enforcement v. The Dratel Group, Inc.*, Complaint No. 2008012925001, 2014 FINRA Discip. LEXIS 6, at *84 n.58 (NAC May 2, 2014), *appeal docketed*, No. 3-15869, 2014 SEC LEXIS 2362 (SEC July 2, 2014) (holding president responsible both for the underlying misconduct and the lax supervisory and compliance structure at his firm) (citing *John Montelbano*, 56 S.E.C. 76, 93 (2003) (finding a respondent both substantively responsible and a deficient supervisor with respect to the same misconduct)).

[481] FINRA Sanction Guidelines (2011) ("Guidelines"), available at www.finra.org/oho (then follow "Enforcement" hyperlink to "Sanction Guidelines").

### A. JCI and Carris

The Panel determined that stringent sanctions were appropriate for JCI and Carris. Consequently, the Panel concludes that expulsion of JCI and an order barring Carris from association with any FINRA member firm in any capacity best serve the remedial purposes of disciplinary oversight.

#### 1. Securities Fraud in Connection with Invictus (Cause Two) and Sales of Invictus Without a Reasonable Basis (Cause Five)

Because the Second and Fifth Causes of Action involve much of the same conduct, they are aggregated for purposes of sanctions, as authorized by the Guidelines.[482] The Guidelines set forth a range of sanctions for misconduct involving misrepresentations or omissions of material fact. If the misconduct is intentional or reckless an individual may be suspended in any or all capacities, and a firm may be suspended with respect to any or all activities or functions, for anywhere between ten business days and two years. In egregious cases, it may be appropriate to bar an individual and expel a firm.[483] The Guidelines for unsuitable recommendations of all types (including both reasonable-basis suitability and customer-specific suitability) provide that an individual respondent may be suspended in all capacities for a period ranging from 10 business days to one year, and may be fined from $2,500 to $75,000. In egregious cases, a longer suspension of up to two years or a bar may be appropriate.[484]

The Panel finds that Carris' misconduct was intentional, or at least extremely reckless.[485] Carris created the Invictus Offerings, and he made the false statements and

[482] Guidelines, at 4 (General Principle No. 4).

[483] *Id*. at 88.

[484] *Id*. at 94.

[485] *Id*. at 7 (Principal Consideration No. 13).

material omissions. His sales of the fraudulent securities continued for well over two years through multiple offerings.[486] And, at no time did Carris accept responsibility for the Invictus fraud.[487]

Carris' financial gain from the misconduct was large and was absolutely necessary for the survival of JCI.[488] Throughout the time he sold the Invictus securities, he knew that he was operating Invictus in a Ponzi-like manner using monies from new investments to pay dividends to existing investors. Other than his own personal belief, Carris had no realistic indication that Invictus could or would repay investors what it owed them. The Invictus securities were clearly unsuitable investments for anyone.

For all of the above reasons, the Panel believes it is necessary for the protection of the investing public that JCI be expelled and Carris be barred from associating with any FINRA member firm in any capacity.

### 2. Manipulation of Fibrocell (Cause One)

The Guidelines do not contain specific guidelines applicable to market manipulation.[489] Accordingly, the Panel reviewed SEC precedent regarding the gravity of the violation and the Principal Considerations in determining sanctions, as set forth in the Guidelines. As the SEC has emphasized, "there are few, if any, more serious offenses

[486] *Id*. at 6 (Principal Considerations Nos. 8 and 9).

[487] *Id*. (Principal Consideration No. 2).

[488] *Id*. at 7 (Principal Consideration No. 17).

[489] The most relevant Guideline for manipulation addresses misrepresentations or material omissions of fact. That Guideline recommends a fine of $2,500 to $50,000 and a suspension of up to 30 days in cases involving negligence; a fine of $10,000 to $100,000 and a suspension of 10 days to two years for intentional or reckless misconduct; and, in egregious cases, a bar, or, in the case of a firm, expulsion. Guidelines, at 88.

than manipulation. Such misconduct is a fraud perpetrated not merely on particular customers but on the entire market."[490]

Upon review of the Principal Considerations, the Panel concludes that this violation involves several aggravating factors. First, Carris' conduct was intentional.[491] He engaged in manipulative stock trading of Fibrocell while JCI was acting as a placement agent for Fibrocell. His manipulative trading was accomplished through pre-arranged trading and improperly placing shares of Fibrocell stock in the accounts of JCI customers in order to create the false appearance of trading volume and to maintain the share price at an artificial level. Not only did Carris orchestrate the manipulative scheme, he was, as the president and CEO of JCI, in a position to prevent the manipulation and did not do so. Second, Carris refused to accept responsibility for the manipulation violations relating to Fibrocell.[492] Instead, he blamed the manipulative scheme on MG, a non-registered, back office employee. Third, the Panel considered the time period for manipulative misconduct.[493] The manipulative purchase and sale orders relating to Fibrocell occurred over a five-month period. Finally, Carris' misconduct resulted in the potential for monetary and other gain.[494] JCI was the placement agent for the Fibrocell PIPE Offering, and it had done significant investment banking work for Fibrocell in the past. Because Carris received Fibrocell stock and held a majority interest in JCI and its

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[490] *Kirlin Securities*, Exchange Act Release No. 61135, 2009 SEC LEXIS 4168, at *85 (Dec. 10, 2009) (quoting *John Montelbano*, 56 S.E.C. 76, 105 (2003)).

[491] Guidelines, at 7 (Principal Consideration No. 13).

[492] *Id*. at 6 (Principal Consideration No. 2).

[493] *Id*. (Principal Consideration No. 9).

[494] *Id*. at 7 (Principal Consideration No. 17).

parent company, he stood to profit from increased investments in the offering, as well as from fees and commissions.

As the NAC has emphasized: "The integrity of the securities markets is paramount, and those who engage in activities that manipulate markets cause great harm not only to investors who are involved in the manipulated markets, but to the overall public perception that the markets are driven by the free forces of supply and demand."[495] After careful consideration of Carris' misconduct and the above specific considerations, the Panel determined that the Fibrocell manipulation was egregious and warrants a bar for Carris and an expulsion for JCI.

### 3. JCI's and Carris' Remaining Violations

In light of JCI's expulsion and Carris' bar, the Panel determined not to impose additional sanctions for the following violations. However, below the Panel discusses the violations and appropriate remedial sanctions for the violations.[496]

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[495] *Mkt. Surveillance Comm. v. Markowski*, Complaint No. CMS920091, 1998 NASD Discip. LEXIS 35, at *56-57 (N.A.C. July 13, 1998), *aff'd*, Exchange Act Release No. 43259, 2000 SEC LEXIS 1860 (Sept. 7, 2000), *aff'd*, 274 F.3d 525 (D.C. Cir. 2001).

[496] At the hearing, Carris provided testimony and documentation to demonstrate his inability to pay a fine. Tr. (Carris) 3578-98; RCX-5. Here, because of the scope and severity of Carris' misconduct, and the fact that inability to pay is but one factor to consider and is not dispositive of the sanctions determination, the Panel determined that a monetary penalty, albeit not imposed in light of the bar, is an appropriate remedial sanction. *See Johnny Clifton*, Admin. Proc. File No. 3-14266, 2013 SEC LEXIS 3151, *10 (Oct. 9, 2013) (finding monetary penalty appropriate in light of the pattern and self-serving nature of respondent's misconduct); *Philip A. Lehman*, Exchange Act Release No. 54660, 2006 SEC LEXIS 2498, *15 (Oct. 27, 2006) ("Even when a respondent demonstrates an inability to pay, we have discretion not to waive the penalty, particularly when the misconduct is sufficiently egregious."); *Charles Trento*, Exchange Act Release No. 49296, 2004 SEC LEXIS 389, at *14 (Feb. 23, 2004) ("Even accepting [respondent's] financial report at face value, we find that the egregiousness of his conduct far outweighs any consideration of his present ability to pay a penalty.").

**a) Inaccurate Books and Records (Cause Six)**

For recordkeeping violations, such as violations of NASD Conduct Rule 3110 and Exchange Act Rule 17a-3, the Guidelines recommend a fine of $1,000 to $10,000, and a suspension for firms and responsible individuals for up to 30 business days. Where the violations are egregious, the Guidelines recommend a fine ranging between $10,000 and $100,000, and consideration of individual bars and firm expulsions. In addition to the Principal Considerations, the Guidelines direct adjudicators to consider the nature and materiality of the inaccurate or misleading information in the records.

Here, for approximately two years, Carris caused JCI to maintain inaccurate books and records by failing to properly characterize his personal expenses on JCI's books and records. Carris' mischaracterization of his expenses impacted not only JCI's general ledger but also the corresponding FOCUS reports, audited financial statements, and tax returns. JCI did not correct the inaccuracies until FINRA brought them to its attention. Carris did not accept responsibility for the mischaracterized expenses. Instead, he again blamed MG.

The Panel determines that the following are appropriate sanctions: (1) a $100,000 fine for JCI and (2) a $100,000 fine and a one-year suspension from association with any FINRA member in all capacities for Carris.

**b) Failure to Pay Employee Payroll Taxes (Cause Eleven)**

There is no Guideline for the failure to pay employee payroll taxes. However, the Panel determined that the Guidelines for "Improper Use of Funds" were the most analogous. The Guidelines for Improper Use of Funds recommend a fine of $2,500 to $50,000, and consideration of a bar. Where the improper use results from a

misunderstanding of the intended use of the funds, or other mitigating factors exist, the Guidelines recommend that adjudicators consider suspending the respondent for six months to two years.

Here, there was no misunderstanding of the intended use of the funds. JCI was obligated to hold the payroll tax funds in trust for payment to the taxing authorities. Carris admitted that he understood JCI's obligation. Yet, JCI, through Carris, chose to use the funds for its own purposes.

JCI's and Carris' misuse of funds in this case warrants a significant sanction. Accordingly, the Panel determines that the following sanctions are appropriate: $50,000 fine for JCI, and $50,000 fine and a three-month suspension from association with any FINRA member in all capacities for Carris.

**c) Net Capital Deficiencies (Cause Ten)**

FINRA's Guidelines for net capital violations recommend a fine of $1,000 to $50,000, and a suspension for up to 30 business days, or, in egregious cases, a longer suspension or bar, for an individual respondent.[497] For firms, the Guidelines recommend suspending the firm with respect to any and all activities for up to 30 days, or, in egregious cases, a longer suspension or expulsion. The Guidelines set forth the following considerations when determining the appropriate sanction for net capital violations: (1) whether the firm continued in business while knowing of deficiencies/inaccuracies or voluntarily ceased conducting business because of the deficiencies/inaccuracies, and (2) whether respondent attempted to conceal deficiencies or inaccuracies by any means, including "parking" of inventory and inflating "mark-to-market" calculations.

[497] Sanction Guidelines, at 28.

Here, the Panel determined that it was necessary to assess sanctions above the Guidelines because the net capital violations at JCI were extremely egregious. JCI did not cease operating when it was out of net capital compliance. Instead, its continued sale of Invictus securities provided the funds needed for JCI to cure its net capital deficiencies. JCI's net capital violations occurred over and over again. In addition to the periods referenced in the Amended Complaint, after the filing of the initial Complaint on September 17, 2013, JCI continued to operate when it was out of net capital compliance on five separate occasions.[498] The Panel determines that the appropriate sanctions are: a $100,000 fine for JCI, and a $75,000 fine and a nine-month suspension from association with any FINRA member in all capacities for Carris.

**d) Failure to Implement AML Policies and Procedures (Cause Eight)**

The Guidelines do not specifically address violations of NASD Conduct Rule 3011. However, in substance, the rules requiring firms to implement AML programs are supervisory requirements. Accordingly, the Panel considered the Guidelines for

[498] Respondents JCI and Carris objected to the admissibility of the additional net capital deficiencies because they occurred after the relevant period described in the Amended Complaint. The Panel admitted the testimony and exhibits for the purposes of sanctions. Evidence of misconduct that is not alleged in the complaint, but is similar to the misconduct charged in the complaint, is admissible to determine sanctions. *See Dep't of Enforcement v. McCrudden*, Complaint No. 2007008358101, 2010 FINRA Discip. LEXIS 25, at *26, n.19 (NAC 2010) (citing *Wanda P. Sears*, Exchange Act Release No. 58075, 2008 SEC LEXIS 1521, at *22 n.33 (July 1, 2008) (finding, in an unauthorized trading case, that evidence of unauthorized trading, which was not alleged in the complaint, was admissible to gauge aggravating factors to assess sanctions); *Gateway Int'l Holdings, Inc*., Exchange Act Release No. 53907, 2006 SEC LEXIS 1288, at *24 n.30 (May 31, 2006) (stating that, "[a]lthough we are not finding violations based on [other] failures [to file timely reports], we may consider them, and other matters that fall outside the [Order Instituting Proceedings], in assessing appropriate sanctions")).

supervisory violations (delineated below) in determining the appropriate remedial sanction in this case.[499]

It is important as a matter of national policy that every FINRA member implements an effective AML program. During the AML Period, extensive suspicious trading occurred at JCI that should have prompted an investigation. The suspicious trading included, but was not limited to, the following: prearranged trading through both reported and unreported matched trades, transactions without an economic purpose such as the numerous unfunded purchases, and the liquidation of penny stock purchases and the wiring out of the proceeds. The Panel found that JCI's and Carris' misconduct was very serious.

The Panel concludes that the appropriate sanction under the facts and circumstances of this case is a $50,000 fine for JCI, and a $25,000 fine and a three-month suspension from association with any FINRA member in all principal capacities for Carris. This sanction will remediate JCI's and Carris' violations and deter others from engaging in similar misconduct.

**e) Failure to Supervise and Implement a Reasonable Supervisory System (Cause Nine)**

For the violation of NASD Conduct Rule 3010(a), the Guidelines recommend a fine of $5,000 to $50,000, suspension of the responsible individuals in all supervisory capacities for up to 30 business days, and limiting the activities of appropriate branch offices or departments for up to 30 business days. In egregious cases, the Guidelines suggest limiting activities of the branch office or department for a longer period or

[499] *See Dep't of Enforcement v. Domestic Sec., Inc.*, Complaint No., 2005001819101, 2008 FINRA Discip. LEXIS 44, at *21 n.9 (NAC Oct. 2, 2008).

suspending the firm with respect to any or all activities or functions for up to 30 business days, and suspending the responsible individual in any or all capacities for up to two years or barring the responsible individual.[500] The Guidelines set forth the following considerations when determining the appropriate sanction for a failure to supervise: (1) the quality and degree of the supervisor's implementation of the firm's supervisory procedures and controls; (2) whether respondent ignored "red flag" warnings that should have resulted in additional supervisory scrutiny; and (3) the nature, extent, size, and character of the underlying misconduct.[501]

The Panel found no evidence of any effective supervisory controls at JCI. Misconduct occurred throughout every area of JCI's operations. As discussed above, Carris routinely ignored red flags. Worse yet, throughout the hearing, Carris either claimed to be unaware of the violations at issue or blamed others, such as employee MG or the outside payroll service contractor, for the misconduct.

In light of JCI's and Carris' abdication of their supervisory responsibilities, the Panel majority finds that the appropriate remedial sanction for JCI and Carris exceeds the Guidelines. Accordingly, the Panel majority determines that JCI's sanction is $100,000 fine, and Carris' sanctions are a $100,000 fine and a bar from association with any FINRA member in all principal capacities.

**B. Tkatchenko**

In determining the appropriate sanction for Tkatchenko, the Panel reviewed the Sanction Guidelines for reasonable-basis suitability violations described above.

[500] Guidelines, at 103.

[501] *Id.*

Tkatchenko's Invictus sales occurred over two years and involved multiple Invictus Offerings. His sales generated substantial profits for both himself and JCI. When selling the Invictus securities, Tkatchenko ignored his duty to investigate the Invictus Offerings prior to recommending them to his customers. Not only did he fail to investigate Invictus, but he disregarded obvious warning signals that should have alerted him to the need for an immediate and searching inquiry. Even when presented with hard facts regarding JCI's dismal financial condition, such as its net losses and defaults on the Bridge Offering notes, Tkatchenko willingly accepted Carris' promotion of Invictus and continued to recommend Invictus.

The Panel also considered Tkatchenko's disciplinary history. In May 2012, Tkatchenko entered into a settlement with FINRA. Without admitting or denying, he consented to the entry of factual findings that he caused more than 24 solicited trade tickets or trade confirmations to be falsely marked "unsolicited."[502] Tkatchenko agreed to a $10,000 fine and a 15-day suspension from association with any FINRA member in any capacity.[503]

After careful consideration, the Panel concludes that the appropriate sanctions for Tkatchenko are a $10,000 fine and a two-year suspension from association with any

[502] CX-10, at 22-26.

[503] CX-10, at 26.

FINRA member in all capacities.[504]

### C. Barter

When determining the appropriate sanction for Barter, the Panel relied on the same factors discussed above for JCI's and Carris' manipulation of Fibrocell.

The Fibrocell manipulation could not have occurred without Barter's participation. He knew JCI was a placement agent for Fibrocell. He also knew JCI dominated the OTCBB market for Fibrocell. With that knowledge, he caused matched Fibrocell orders to be executed during the Manipulation Period, the majority of which were limit orders. He also repeatedly entered orders for identical large block trades that were submitted to him as the clearing firm sent Regulation T sell-out notices.

Barter was JCI's Head Trader, with supervisory duties over the trading at JCI. He failed to fulfill his duty to review the orders to ensure that this type of activity did not occur. He ignored the red flags indicative of wrongdoing. The frequent matched orders were indicative of pre-arranged trading. Plus, on July 29, 2010, he received an email from one of Carris' customers after she received a trade confirmation reflecting a Fibrocell

[504] At the hearing, Tkatchenko testified about his inability to pay a fine. Tr. (Tkatchenko) 3634-38. The Guidelines require that, when raised by a respondent, we consider such claims when determining an appropriate level of monetary sanctions. Barter, "like any respondent raising the issue of his or her personal financial circumstances as they affect ability to pay a restitution order, has the burden of producing evidence in support of the claim and proving bona fide insolvency." *Toney L. Reed*, 52 S.E.C. 944, 947 n.12 (1996). Proof of bona fide insolvency requires that the accuracy of all financial information be verified "through the submission of signed and notarized documents evidencing financial hardship." *Dep't of Enforcement v. Levitov*, Complaint No. CAF970011, 2000 NASD Discip. LEXIS 12, at * 33-34 (NAC June 28, 2000). Tkatchenko failed to submit any supporting documentation, and there is no way to verify his assertions. Accordingly, we do not find that he established an inability to pay a monetary fine. Here, the Panel imposed a light fine of $10,000 because we believe that the two-year suspension in all capacities will more effectively serve the public interest than would the imposition of a larger fine.

trade. In the July 29 email, she questioned how the Fibrocell stock appeared in her account when she never purchased it.

The integrity of the market depends on traders such as Barter. Barter was in a position to prevent the manipulation of Fibrocell and did not do so. Instead, he focused his attention on the mechanics of order entry without any qualitative assessment of the trading activity.

The Panel concludes that the appropriate sanction for Barter is a $5,000 fine and an 18-month suspension from association with any FINRA member in all capacities.[505] Barter's misconduct reveals that he was unfamiliar with the legal requirements of a trader and important responsibilities of a securities professional. Accordingly, the Panel requires Barter to re-qualify by examination as a registered representative before he re-enters the securities industry in any capacity.

## VI. ORDER

Based on careful consideration of all the evidence, the Hearing Panel imposes the following sanctions:[506]

### A. John Carris Investments, LLC and George Carris

Respondent John Carris Investments, LLC is expelled from FINRA and Respondent George Carris is barred from association with any FINRA member firm in any capacity for the following violations:

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[505] At the hearing, Barter also testified about his inability to pay a fine. Tr. (Barter) 3627-33. Like Tkatchenko, Barter also failed to provide the Panel with any supporting documentation of his financial condition. *See supra* footnote 503. Accordingly, he failed to establish an inability to pay a monetary fine. Here, the Panel imposed a light fine of $5,000 because we believe that the 18-month suspension in all capacities and the requirement to requalify will more effectively serve the public interest than would the imposition of a larger fine.

[506] The Panel considered all of the parties' arguments. They are rejected or sustained to the extent that they are inconsistent with the views expressed herein.

(1) Willfully violating the Securities Exchange Act of 1934, Section 10(b), Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by knowingly or, at a minimum, recklessly selling securities issued by JCI's parent company on the basis of false statements of material fact and misleading omissions of material fact as alleged in the Second Cause of Action;

(2) Violating NASD Rule 2310, and FINRA Rules 2111 and 2010, during the Offering Period, by recommending the purchase of securities issued by JCI's parent company to customers without a reasonable basis as alleged in the Fifth Cause of Action; and

(3) Willfully violating Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, during the Manipulation Period, by manipulating the price of Fibrocell Science, Inc. stock through prearranged trading and improperly placing stock in customer accounts to maintain the price at an artificial level as alleged in the First Cause of Action.

The Hearing Panel concluded that JCI and Carris committed the following additional violations as alleged in the Amended Complaint; however, in light of the sanctions ordered in connection with the above fraud and suitability violations, sanctions are not imposed.

(1) Respondent Carris violated NASD Rule 3110, and FINRA Rules 4511 and 2010, from January 1, 2010 through December 31, 2011, by causing JCI to create and maintain inaccurate books and records in violation of Section17(a) of the Exchange Act and Rule 17a-3 thereunder; and JCI violated NASD Rule 3110, and FINRA Rules 4511 and 2010, and willfully violated Exchange Act Section 17(a) and Rule 17a-3 thereunder,

by creating and maintaining inaccurate books and records, as alleged in the Sixth Cause of Action;

(2) JCI and Carris violated FINRA Rule 2010, from May 2010 through December 2012, by failing to remit to the United States Treasury and other taxing authorities hundreds of thousands of dollars in employee payroll taxes as alleged in the Eleventh Cause of Action;

(3) Carris violated FINRA Rule 2010, by causing JCI to operate without sufficient net capital; and JCI willfully violated Exchange Act Section 15, Rule 15c-3, et seq. thereunder, and FINRA Rule 2010, by operating without sufficient net capital between November 1, 2011 and August 6, 2012, as alleged in the Tenth Cause of Action;

(4) JCI and Carris violated FINRA Rules 3310 and 2010, during the AML Period, by failing to implement Anti-Money Laundering policies and procedures that can be reasonably expected to detect and cause the reporting of suspicious transactions, as alleged in the Eighth Cause of Action; and

(5) JCI and Carris violated FINRA Rules 3010 and 2010, by failing to establish, maintain, and enforce a reasonable supervisory system as alleged in the Ninth Cause of Action.

The evidence did not support the following charges, which are dismissed.

(1) The Third Cause of Action alleging that, during the Liquidation Period, JCI willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by failing to disclose material, adverse conflict of interest information to JCI customers who were purchasing Fibrocell stock.

(2) The Fourth Cause of Action alleging that Carris willfully violated Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, by aiding and abetting the securities fraud during the Liquidation Period.

(3) The Seventh Cause of Action alleging that Carris and JCI violated FINRA Rule 2010, by (i) failing to issue year-end tax forms, Forms W-2, for years 2009 and 2010; and (ii) issuing a false Form W-2 for 2011 that underreported Carris' compensation.

**B. Andrey Tkatchenko**

Respondent Andrey Tkatchenko is fined $10,000 and suspended from association with any FINRA member in all capacities for two years for violating NASD Rule 2310, and FINRA Rules 2111 and 2010, during the Offering Period, by recommending the purchase of securities issued by JCI's parent company to customers during the ongoing offerings without a reasonable basis as alleged in the Fifth Cause of Action.

If this Decision becomes FINRA's final disciplinary action in this proceeding, the foregoing suspension shall begin on March 16, 2015.

**C. Jason Barter**

Respondent Jason Barter is fined $5,000, suspended from associating with any FINRA member firm in all capacities for 18 months, and required to re-qualify by examination as a registered representative before he re-enters the securities industry in any capacity for willfully violating Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010, during the Manipulation Period, by manipulating the price of Fibrocell stock through prearranged trading as alleged in the First Cause of Action.

If this Decision becomes FINRA's final disciplinary action in this proceeding, the foregoing suspension shall begin on March 16, 2015.

**D. Randy Hechler**

The Hearing Panel concluded that Respondent Randy Hechler did not violate FINRA Rules 3010 and 2010, by failing to establish, maintain, and enforce a reasonable supervisory system as alleged in the Ninth Cause of Action. Accordingly, the Ninth Cause of Action is dismissed solely with respect to Respondent Hechler.

Except for the expulsion, bars, and suspensions detailed above, the remaining sanctions shall become effective on a date set by FINRA, but not earlier than 30 days after this Decision becomes FINRA's final disciplinary action.

In addition, JCI, Carris, Tkatchenko, and Barter are jointly and severally ordered to pay $28,864.79 in costs.[507]

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Maureen A. Delaney
Hearing Officer
For the Extended Hearing Panel

[507] The costs are composed of an administrative fee of $750 and transcript costs of $28,114.79.