

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

Department of Enforcement,

Complainant,

v.

Conrad R. Huss (CRD No. 2047874),

Respondent.

Disciplinary Proceeding
No. 2011027338901

Hearing Officer: DRS

**ORDER ACCEPTING OFFER OF
SETTLEMENT**

Date: October 14, 2015

INTRODUCTION

Disciplinary Proceeding No. 2011027338901 was filed on December 8, 2014, by the Department of Enforcement of the Financial Industry Regulatory Authority (FINRA) (Complainant). Respondent Conrad R. Huss submitted an Offer of Settlement (Offer) to Complainant dated October 8, 2015. Pursuant to FINRA Rule 9270(e), the Complainant and the National Adjudicatory Council (NAC), a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs (ODA) have accepted the uncontested Offer. Accordingly, this Order now is issued pursuant to FINRA Rule 9270(e)(3). The findings, conclusions and sanctions set forth in this Order are those stated in the Offer as accepted by the Complainant and approved by the NAC.

Under the terms of the Offer, Respondent has consented, without admitting or denying the allegations of the Complaint (as amended by the Offer of Settlement), and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to

which FINRA is a party, to the entry of findings and violations consistent with the allegations of the Complaint (as amended by the Offer of Settlement), and to the imposition of the sanctions set forth below, and fully understands that this Order will become part of Respondent's permanent disciplinary record and may be considered in any future actions brought by FINRA.

BACKGROUND

1. Respondent first became registered with FINRA as a General Securities Representative ("GS") through a member firm on November 1, 1989.
2. From November 1989 through December 2000, Respondent was registered as a GS through various FINRA member and former member firms.
3. From January 15, 2005 through October 31, 2006, Respondent was registered with FINRA through former member firm du Pasquier & Co., Inc. (BD No. 24750) ("DPC" or "the Firm").
4. From November 1, 2006 through December 31, 2012, Respondent was registered with FINRA through former member firms.
5. Although Respondent is no longer registered or associated with a FINRA member, he remains subject to FINRA's jurisdiction for purposes of this proceeding, pursuant to Article V, Section 4 of FINRA's By-Laws, because (1) the Complaint was filed within two years after the effective date of termination of Respondent's association with his last employer, namely, December 31, 2012; and (2) the Complaint charges him with misconduct committed while he was registered or associated with a FINRA member.

FINDINGS AND CONCLUSIONS

It has been determined that the Offer be accepted and that findings be made as follows:¹

SUMMARY

6. This case arises out of misrepresentations made by Respondent and another individual in connection with the solicitation and sale of \$1.4 million worth of promissory notes in a private offering to 14 customers between March 2006 and August 2006, while Respondent was associated with former member firm, DPC.

7. The notes (“EDFC Notes”) were issued by Economic Development Finance Corporation (“EDFC”), a real estate development company formed in 2002 in Massachusetts. In or around August 2007, EDFC defaulted under the Notes and failed to pay DPC’s customers the principal due and owing under the EDFC Notes, resulting in significant losses to many customers.

8. In connection with the sale of the EDFC Notes, Respondent negligently misrepresented to customers that the EDFC Notes were fully secured by EDFC’s pledge of proceeds from the sale of certain historic rehabilitation tax credits (“HRTCs”). In addition, Respondent provided investors with documents in which EDFC falsely stated that the EDFC Notes were secured by proceeds from the HRTCs. Respondent used these materials in connection with the sale of the EDFC Notes to prospective investors, negligently disregarding information indicating that EDFC’s statements were false.

9. In reality, there was no collateral for the EDFC Notes because (a) the HRTCs had not even been issued at the time the proceeds were purportedly pledged by EDFC; and (b) even if the

¹ The findings herein are pursuant to Respondent Huss’ Offer of Settlement and are not binding on any other person or entity named as a respondent in this or any other proceeding.

HRTCs had been issued, EDFC had no property right or interest in the purported HTRC proceeds, and therefore no ability to pledge them as collateral.

10. As set forth below, Respondent negligently made an untrue statement of a material fact in contravention of Section 17(a)(2) of the Securities Act of 1933 (“Securities Act”) and thus violated NASD Conduct Rule 2110.

FACTS

A. EDFC’s Engagement of DPC

11. EDFC was a Massachusetts real estate development company formed in 2002. Its principals were DP, President, and RS, Chief Operating Officer. EDFC focused on multi-unit housing or mixed-use development properties which could benefit from various types of governmental financial support, including historic rehabilitation tax credits (“HRTCs”), low income housing tax credits and direct subsidies available through state and federal programs.

12. HRTCs are issued by federal and state governments to encourage private developers and investors to restore historic buildings to productive use. They are essentially a form of government subsidy that developers use to raise financing for the rehabilitation of historic and older buildings. Developers use HRTCs to raise capital either by selling or syndicating the HRTCs, depending upon the type of HRTC involved, to an investor or group of investors. The investors benefit by claiming the tax credit on their income tax returns when the credits are issued.

13. In the spring of 2005, FSA, a consulting firm that was not a member of FINRA, contacted DPC on behalf of EDFC to learn whether DPC was interested in assisting EDFC in raising working capital.

14. In July 2005, Respondent began conducting due diligence concerning EDFC and its main historic property rehabilitation project at the time, known as the Hadley Building. The Hadley Building was a 45 unit apartment building to be built in a historic building in Worcester, MA that once housed a furniture company. The Hadley Building was owned by Hadley Apartments LLC, not by EDFC.

15. Beginning in 2004, EDFC sought financing for the Hadley Building from private and governmental sources, including federal, state and city grants, federal and state tax credits and low-income housing loans. In 2004 and 2006, the Massachusetts Historical Commission (“MHC”) conditionally awarded the Hadley Building state HRTCs. The final issuance of the HRTCs was contingent upon successful completion and approval of the project in accordance with state regulations.

16. In addition to meetings with EDFC and field visits, Respondent’s due diligence included reviewing, *inter alia*, documents concerning the Hadley Building, the planning and construction of the apartments, budgets, sales and rental projections, and sources of project financing, including applications for state and federal HRTCs for the Hadley Building.

17. In August 2005, Respondent recommended that DPC proceed with the transaction. On or about August 22, 2005, EDFC formally retained DPC as exclusive placement agent in connection with the proposed offer and private placement by EDFC of promissory “bridge” notes (the “Offering”). As to compensation, EDFC agreed to pay DPC a placement fee of 10% of the amount of notes sold to investors that DPC identified and a 2% expense allowance.

B. The EDFC Offering

18. The essential terms of the EDFC Offering were set forth in a Bridge Loan Promissory Note Term Sheet (the “Term Sheet”), the EDFC Notes and related agreements provided to Investors. The Term Sheet stated that “Security Issued” was “Promissory Notes in the principal amount and having other terms described” in the Term Sheet. The EDFC Notes were for a term of one year and were to pay interest at a rate of 15% per year for a term of one year, plus a 1% fee paid to the investor at closing. The principal was to be secured by proceeds from the sale of HRTCs awarded for the Hadley Building. In addition, EDFC’s two corporate officers, DP and RS, were to provide personal guarantees of EDFC’s obligations under the EDFC Notes.

19. In or around March 2006, DPC began soliciting its customers by telephone to purchase the EDFC Notes. If the customer expressed an interest, Respondent caused to be mailed to the customer a letter for prospective investors (“Investor Letter”), signed by Respondent, and the following documents (the “Offering Documents”):

- a. A Term Sheet;
- b. A sample Pledge Agreement pertaining to the collateral;
- c. A sample Assumption and Assignment Agreement pertaining to the collateral (“Assignment Agreement”);
- d. A memo summarizing the requirements for and calculations of the HRTCs pertaining to the Hadley Building (the “HRTC Memo”);
- e. A PowerPoint on the Hadley Building;
- f. An appraisal of the Hadley Building;
- g. A construction loan commitment letter from Amalgamated Bank; and
- h. DP’s and RS’s personal financial statements.

20. Respondent caused the Investment Letter and Offering Documents to be sent to 14 customers. If after receiving the Offering Documents customers decided to invest, they wired funds directly to EDFC. In return, EDFC provided the customer with an executed: (i) Note; (ii)

Pledge Agreement; (iii) Assignment Agreements from DP and HS; and (iv) Guarantees from DP and HS (collectively the “Subscription Documents”).

21. During the period March 2006 through August 2006, DPC sold \$1,400,000 worth of EDFC Notes to 14 of its customers in 18 separate transactions.

22. DPC received approximately \$168,000 in fees and expenses from the sale of EDFC Notes to Respondent’s customers.

C. Misrepresentations Concerning the HRTCs

23. In connection with the offer and sale of the EDFC Notes, Respondent made material misrepresentations to DPC’s customers concerning the terms of the EDFC Notes. Specifically, Respondent signed the Investment Letters sent to customers stating that the “proposed collateral” for the EDFC Notes included “Proceeds from the historical tax credits (federal and state).” Respondent also sent the Term Sheet, which falsely stated that the “Collateral” for the EDFC Notes included “Approved state and federal historic tax credits.”

24. In connection with the sale of the EDFC Notes, Respondent also provided investors with documents prepared by EDFC’s attorneys that falsely stated that the EDFC Notes were collateralized by HRTC, specifically the Assignment Agreement and the Pledge Agreement included in the Offering Documents.

25. The Assignment Agreement that Respondent provided to investors further reinforced the false statements concerning the collateral. Preliminarily, the Assignment Agreement falsely asserted that DP and RS were the “holders” of the HRTCs. Specifically, the Assignment Agreement drafted by EDFC’s attorneys, in the recital provisions, stated:

WHEREAS, the Assignor [DP or RS] is the holder of certain income tax credits awarded by the Government of the United States of America as well as the Commonwealth of

Massachusetts for the Assignor's work in connection with the restoration, rehabilitation and/or preservation of certain buildings and other structures recognized as "historic" by the Federal and/or State government (collectively the "Tax Credits").

26. The Assignment Agreement stated that, in connection with the Offering, EDFC was being assigned "Assignor's right, title and interest to any future proceeds upon the sale, transfer or assignment of the Tax Credits (the 'Tax Credit Proceeds')." EDFC would in turn pledge that interest in the proceeds as collateral by way of a pledge agreement, discussed below.

27. However, as discussed below, neither DP nor RS were ever "holders" of the HRTCs that they purportedly would be assigning to EDFC and, therefore, the Assignment Agreement contained untrue statements of material fact that were false and misleading.

28. Similarly, under the Pledge Agreement drafted by EDFC's attorneys, which Respondent also provided to customers, EDFC purportedly gave investors a security interest in the proceeds of the HRTCs to secure payments under the EDFC Note. In particular, the Pledge Agreement states:

WHEREAS, the Pledgor is the owner of all of the right, title and interest of the proceeds from the future sale of certain income tax credits (up to the amount of the Loan Amount) awarded by the Government of the United States of America as well as the Commonwealth of Massachusetts to [DP and RS] (principals of the Pledgor) for their work in connection with the restoration, rehabilitation and/or preservation of certain buildings and other structures recognized as "historic" by the Federal and/or State government pursuant to certain Assignment and Assumption Agreements of even date (collectively the "Tax Credit Proceeds");

NOW, THEREFORE, for good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, and in consideration of the mutual covenants and agreements herein contained, the parties hereto mutually agree as follows:

1. Pledge. As collateral security for the payment of the aforesaid Loan, the Pledgor hereby grants a security interest in and to any future Tax Credit Proceeds that Pledgor receives. The Pledgor represents and warrants that it has the right and power to pledge said Tax Credit Proceeds.

29. The representations made in the Pledge Agreement are false and misleading because, as discussed below, EDFC did not have the “right and power to pledge” the HRTCs to investors.

30. As the foregoing demonstrates, investors were repeatedly assured in the Investment Letter, in the Term Sheet, and in the Assignment and Pledge Agreements, that an investment in the EDFC Notes would be completely secured by EDFC’s pledge of the proceeds from the sale of HRTCs. These statements were materially false and misleading.

D. EDFC Could Not Legally Pledge the Proceeds from the Hadley Building HRTCs to Investors in 2006

31. EDFC never had any rights to the HRTC proceeds that it supposedly pledged as collateral. Under federal law and Massachusetts law, HRTCs can only be issued to a person or entity that holds title to the subject property. EDFC had no ownership interest in the subject property – the Hadley Building.

32. The Hadley Building was owned by an entity called Hadley Apartments LLC. Hadley Apartments LLC was 80% owned by KDN Development LLC and WesVen LLC. DP owned KDN Development LLC and RS owned WesVen LLC.

33. Neither DP nor RS owned or held title to the Hadley Building. Accordingly, neither DP nor RS could assign the HRTC proceeds to EDFC as they had represented in the Assignment Agreement. Therefore, EDFC could not pledge the HRTC proceeds to investors as represented in the Pledge Agreement.

34. The documents that Respondent provided to investors also falsely represented that the HRTC proceeds were available to secure a default under the EDFC Notes at the time they were issued because HRTCs cannot be issued until a historic rehabilitation project is completed.

The Hadley Building was not completed until 2009, at which time HRTCs for the Hadley Building were issued.

35. The assignments of the HRTC proceeds occurred in 2006, long before any Hadley Building HRTCs were issued in 2009. The Assignment Agreement purported to assign rights in the proceeds “of certain income tax credits [the HRTCs] awarded by the Government of the United States of America as well as the Commonwealth of Massachusetts”

36. In sum, EDFC could not legally pledge the proceeds of the Hadley Building HRTCs to investors. Accordingly, all of the statements representing that the EDFC Notes were secured by the proceeds of the future sale of HRTCs were false and misleading.

E. Respondent’s Negligent Misconduct Concerning the HRTCs

37. Respondent had no prior training or experience regarding tax credits. Respondent began conducting due diligence concerning EDFC and the Hadley Project in May 2005. The due diligence process included reviewing presentations concerning the planning and construction of the Hadley Project, documents concerning sources of construction financing, both existing and proposed, construction and operating budgets, sales and rental projections, applications for financing, and information concerning federal and state HRTCs (collectively, the “Due Diligence Files”). In addition, Respondent met with EDFC’s management and attorneys and made field visits to the Hadley Building.

38. The Due Diligence Files contained numerous red flags that should have made Respondent aware that EDFC could not have pledged the proceeds of the Hadley Building HRTCs as collateral for the EDFC Notes.

39. First, Due Diligence Files indicated that federal and Massachusetts HRTCs can only be issued to the person or entity that holds title to the subject property.

40. The Due Diligence Files further indicated that DP, RS and EDFC did not hold title to the subject property, i.e., the Hadley Building.

41. The Due Diligence Files further indicated, among other things, that neither federal nor Massachusetts HRTCs could be issued until a rehabilitation project was completed.

42. Accordingly, the Due Diligence Files should have indicated to Respondent that, at the time the EDFC Notes were sold, they were unsecured because EDFC could not have actually pledged the proceeds of the Hadley Building HRTCs as collateral for the EDFC Notes.

43. Respondent, however, failed to adequately conduct a follow-up investigation regarding these red flags concerning the availability of the Hadley Building HRTCs as security for the EDFC Notes. He was therefore negligent in causing the EDFC Notes to be sold by means of the misrepresentations concerning the Hadley Building HRTCs made in the Investor Letter, Term Sheet, Assignment Agreement and Pledge Agreement.

FIRST CAUSE OF ACTION
Negligent Misrepresentations of Material Facts
in Connection with the Offer or Sale of Securities
(FINRA Rule 2010, both independently and by virtue of
violating Securities Act §17(a)(2))

44. Section 17(a)(2) of the Securities Act states in relevant part that “[it] shall be unlawful for any person in the offer or sale of any securities ... by the use of any means or instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly— to obtain money or property by means of any untrue statement of a

material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.”

45. The EDFC Notes are securities.

46. During the period from March 2006 through August 2006, Respondent violated these rules in connection with the offer and sale of securities. In particular, Respondent negligently (a) misrepresented to investors (i) in the Investor Letter that the collateral for the EDFC Notes included “proceeds from the historical tax credits (federal and state);” and (ii) in the Term Sheet that collateral for the EDFC Notes included approved state and federal historic tax credits; and (b) provided investors with an Assignment and Assumption Agreement and a Pledge Agreement in which EDFC falsely stated that the HRTCs had been awarded and that the Notes would be secured by EDFC’s interest in proceeds from the HRTCs.

47. These representations were false and misleading at the time they were made.

48. The above misrepresentations were material.

49. In connection with the sale of the EDFC Notes, Respondent made use of means or instrumentalities of interstate commerce and of the mails. Specifically, Respondent made use of, among other things, the telephone, sent subscription documents to the customers using the mails and caused customers to wire funds to invest in the Offering.

50. By reason of the foregoing, Respondent acted in contravention of Securities Act §17(a)(2), thereby violating NASD Conduct Rule 2110, and also independently violated NASD Conduct Rule 2110.

SANCTIONS

It is ordered that Respondent be:

- Suspended from association with any FINRA member in all capacities for a period of two years; and
- Fined in the amount of \$20,000

The fine shall be due and payable either immediately upon reassociation with a member firm following the two year suspension noted above, or prior to any application or request for relief from any statutory disqualification resulting from this or any other event or proceeding, whichever is earlier. Respondent understands that if he is barred or suspended from associating with any FINRA member, he becomes subject to a statutory disqualification as that term is defined in Article III, Section 4 of FINRA's By-Laws, incorporating Section 3(a)(39) of the Securities Exchange Act of 1934. Accordingly, Respondent may not be associated with any FINRA member in any capacity, including clerical or ministerial functions, during the period of the bar or suspension. (See FINRA Rules 8310 and 8311.)

The sanctions imposed herein shall be effective on a date set by FINRA staff.

SO ORDERED.

FINRA

Signed on behalf of the
Director of ODA, by delegated authority



Samuel L. Barkin Senior Regional Counsel
FINRA, District 10
200 Liberty Street
New York, NY 10281-1003
(212) 858-4074
samuel.barkin@finra.org