BEFORE THE NATIONAL ADJUDICATORY COUNCIL

FINANCIAL INDUSTRY REGULATORY AUTHORITY

In the Matter of Department of Enforcement, Complainant, vs. Craig Scott Taddonio New York, NY, Brent Morgan Porges New York, NY, and Edward Beyn New York, NY, Respondents.	DECISION Complaint Nos. 2015044823501 2015044823502 Dated: January 29, 2019

Registered representative excessively traded and churned customer accounts and made unsuitable recommendations to a customer. Registered representative and principal failed to exercise reasonable supervision in light of red flags that registered representatives were, or might be, excessively trading customer accounts, and he gave false testimony to FINRA in an on-the-record interview. Held, findings affirmed and sanctions modified.

Appearances

For the Complainant: Leo F. Orenstein, Esq., Danielle I. Schanz, Esq., Carlos A. Lopez, Esq., Vaishali Shetty, Esq., Artur M. Wlazlo, Esq., Department of Enforcement, Financial Industry Regulatory Authority

For the Respondents: Pro Se

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Decision

Craig Scott Taddonio and Edward Beyn appeal the bars imposed on them in a July 31, 2017 Extended Hearing Panel Decision. The Extended Hearing Panel (the "Hearing Panel") found that Beyn excessively traded customer accounts, in violation of NASD Rule 2310 and FINRA Rules 2111 and 2010, and churned customer accounts, in violation of Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act"), Exchange Act Rule 10b-5, and FINRA Rules 2020 and 2010.[1] The Hearing Panel further found that Beyn made qualitatively unsuitable recommendations to a customer, in violation of NASD Rule 2310 and FINRA Rules 2111 and 2010. For these violations, the Hearing Panel barred Beyn from associating with any FINRA member firm in any capacity.

The Hearing Panel found that Taddonio failed to exercise reasonable supervision, in violation of NASD Rules 3010 and FINRA Rule 2010, in light of red flags that indicated Beyn and several other registered representatives at his firm were excessively trading customer accounts. The Hearing Panel also found that Taddonio gave false testimony to FINRA in a sworn on-the-record interview, in violation of FINRA Rules 8210 and 2010. For the supervisory violations, the Hearing Panel barred Taddonio from associating with any FINRA member firm in any principal or supervisory capacity. For giving false testimony, the Hearing Panel barred Taddonio from associating with any FINRA member firm in any capacity.

On appeal, both Taddonio and Beyn deny any wrong-doing. Beyn argues that his customers were sophisticated and were aware of and approved all the trading in their accounts. Beyn also denies the sale of unsuitable investments to one customer. Taddonio primarily argues that he delegated all supervisory responsibilities to the firm's chief compliance officers and that he himself had no supervisory duties. Taddonio also argues that the trading at the firm was approved by the customers and not excessive.

After an independent review of the record, we affirm the Hearing Panel's findings of violation and the sanction imposed on Beyn. With respect to Taddonio, we affirm the findings of violation, but modify the sanctions to impose a bar in all capacities for Taddonio's egregious supervisory violations. Our findings, and the sanctions we impose, are supported by the record and the Hearing Panel's extensive credibility findings.

I. Background

A. Craig Scott Taddonio

Taddonio first registered with FINRA in March 2004 as a general securities representative with FINRA member GunnAllen Financial, Inc. Taddonio had graduated from

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[1] The conduct rules that apply in this case are those that existed at the time of the conduct at issue.

high school less than three years earlier and dropped out of college in his freshman year for personal reasons. Taddonio testified that he was very successful as a salesman at GunnAllen. In December 2005, Taddonio left GunnAllen to join Pointe Capital, LLC. While at Pointe Capital, Taddonio obtained his general securities principal license. In May 2010, Taddonio left Pointe Capital to join Brookstone Securities, Inc., where he owned his own branch office. In January 2012, Taddonio and Brent Morgan Porges co-founded Craig Scott Capital, LLC. ("CSC"). Taddonio had worked with Porges for various periods at GunnAllen, Pointe Capital, and Brookstone. Taddonio was CSC's majority owner and served as its Chief Executive Officer ("CEO") and President. Taddonio is not currently associated with any FINRA member firm.

B. Craig Scott Capital, LLC

Taddonio and Porges co-founded CSC and owned approximately 80% and 20% of the firm, respectively.[2] CSC began the FINRA membership process in 2011, was approved as a member in January 2012, and began operating in February 2012. CSC operated out of the same location as the Brookstone branch office Taddonio owned prior to founding CSC. Many of the registered representatives who initially joined CSC were previously registered with Brookstone, including the four brokers whose trading is at issue in this case: Beyn, ZB, DC, and MV. During the relevant time period, Taddonio served as CSC's CEO and President and Porges served as its Chief Operating Officer ("COO"). CSC ceased operations in December 2015, shortly before it was suspended by FINRA for failure to pay outstanding fees.

At its height, CSC employed approximately 35-40 registered representatives and operated with what Taddonio described as a model of senior and junior brokers. Junior brokers were new to the industry and primarily cold called leads obtained from Dunn & Bradstreet or other sources. Junior brokers attempted to convince potential investors to open an account and make an initial trade, usually the purchase of a modest amount of a listed or widely traded NASDAQ stock with a $99 fee charged for the trade. Once the account was opened, and the initial trade made, the account was transferred to a "senior" broker, with at least some additional experience in the industry, who would attempt to persuade the customer to invest more money with CSC and continue trading.[3]

CSC's management consisted of Taddonio, Porges, and a chief compliance officer ("CCO"). Initially, CSC's CCO was RC. RC assisted CSC with the membership application process and served as its CCO until February 2013, when he was terminated by Taddonio and Porges. Taddonio subsequently hired JG to serve as CCO. JG remained CCO of CSC until September 2015, shortly before CSC ceased operations.

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[2] Their ownership interests were reduced slightly later, when an ownership interest was granted to an investor that provided financing for CSC.

[3] Several of the "senior" brokers had very little experience. ZB, for example, graduated from college in 2010, started working at Brookstone in 2011, and worked at CSC until he was terminated in August 2013.

Many CSC brokers employed what Taddonio referred to as the "earnings play" strategy and touted this strategy to their customers. The earnings play strategy involved purchasing a stock shortly before it was expected to release an earnings announcement in the hope that the announcement would cause an increase in the stock price. The stock would then be sold at a gain. Taddonio provided lists to the registered representatives of companies expected to make earnings announcements in the near future. The earnings play strategy was used by the four registered representatives whose trading is at issue in this case—Beyn, ZB, DC, and MV—often for securities identified by Taddonio. All four registered representatives used the strategy to make numerous, frequent, short-term trades in customer accounts. Taddonio testified that no one at CSC did an analysis to determine whether the strategy was successfully used at the firm.

Taddonio testified that most of CSC's revenue was generated by commissions (including mark-ups and mark-downs) paid by customers. CSC charged a flat $99 fee for every trade, all of which was retained by the firm (the "Firm Commission"). Additionally, CSC charged a commission on each trade, a portion of which was paid to the firm and a portion to the broker. The individual broker was given considerable latitude to decide the amount of this commission as long as it did not exceed the firm's general limits or an individual limit that may have been placed on a particular account.[4]

The individual broker also had the authority to decide whether a trade would be executed on a riskless principal basis, in which case the customer would be charged a mark-up or mark-down instead of a commission.[5] Again, as long as the mark-up or mark-down did not exceed the 5% (and later 3.2%) firm limits, the individual broker was authorized to set the amount of the mark-up or mark-down. The broker would be paid a portion of the mark-up or mark-down, and the firm would retain a portion. The brokers whose trading is at issue in this case executed their trades on a riskless principal basis and, accordingly, their customers were charged mark-ups and mark-downs in addition to the $99 Firm Commission on each trade.

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[4] At the beginning of the relevant time period, the firm limit was 5%. Later, the general firm limit was reduced to 3.2%. Smaller percentages were imposed on selected accounts based on the recommendations of the CCO.

[5] A "riskless principal" transaction is one in which, after receiving an order to buy or sell from a customer, the broker-dealer buys or sells the security to another person in its principal capacity for or from its proprietary account to cover the customer's order. *See Dennis Todd Lloyd Gordon*, Exchange Act Release No. 57655, 2008 SEC LEXIS 819, at *39 n.47 (Apr. 11, 2008). Such trades are riskless "in that the stock is acquired [or sold] by the firm only after [the customer] had agreed to buy [or sell] the stock." *Id.* at *38-39. For a buy transaction, the firm will charge the customer more than it paid to buy the stock for its proprietary account—a mark-up. For a sale, the firm pays the customer a lower price for the stock that it received from the sale from its proprietary account—a mark-down. Ordinarily, riskless principal transactions have small mark-ups and mark-downs.

CSC's clearing firm sent trade confirmations to customers. Every confirmation included basic information about the trade, including the name of the stock, the trade date, the number of shares purchased or sold, and the price per share. The confirmation also set out the "Principal" amount of the trade (the price per share multiplied by the number of shares purchased or sold), the $99 "Firm Commission," and the "Net Amount" (calculated by adding the $99 Firm Commission to the Principal amount).

The trade confirmations also included a section entitled "[s]pecial remarks for this transaction." This section was located on the bottom left of the trade confirmation and was in smaller type than the rest of the information. When a trade was executed on a riskless principal basis, this section contained several pieces of information. First, this section would note that the trade was executed on a "Riskless Principal" basis. Second, this section noted the "Reported Price"—i.e., the price per share *including* the mark-up or mark-down for the transaction. Finally, this section would set out the "Commission Equivalent . . . per share"—i.e., the amount per share charged as a mark-up or mark-down. In order to calculate the total cost of a riskless principal trade, a customer would have to multiply the number of shares traded by the "Commission Equivalent" and then add the $99 Firm Commission. CSC did not provide customers with a written explanation of mark-ups and mark-downs or how to calculate the costs of a trade from the confirmation.

Taddonio functioned as the firm's sales manager, closely monitored the brokers' sales activities, and actively encouraged brokers to raise revenue by trading accounts. Taddonio acknowledged the he had access to daily sales activity on his work laptop and could monitor sales from anywhere. Taddonio encouraged brokers to open and trade accounts. For example, in November 2012, Taddonio emailed CSC brokers:

> We HAVE to treat the next 2 weeks like the last 2 weeks of the month and try to raise as much money as possible and open as many accounts as we can the next 2 weeks!! It is IMPERATIVE that you work harder the next 2 weeks than you ever have!! Remember this is your Christmas paycheck and I know everyone wants to have an amazing Christmas even better than we did last year!

[Emphasis in original.] Taddonio went on to caution brokers that they did not "want to be embarrassed and have to apologize to [] families and friends" if the brokers "couldn't get them what they wanted." Taddonio told brokers that if they "pitch[ed] accounts the second you walk in [to the office] for 2 hours, open one account and then trade and raise money for the next two hours you will be shocked at how much you accomplish the next two weeks." Taddonio instructed that after taking a short lunch, brokers should again "pitch new accounts for another hour and a half to two hours and finish the day trading and raising money." Taddonio sent this email shortly after Hurricane Sandy and included in the email a sales pitch for Home Depot based on the damage caused by the hurricane. Taddonio closed his email by promising a list of recommended stocks would follow and saying, "[l]et's raise some $$$$!"

Taddonio encouraged sales by rewarding top producing brokers with awards, including trophies and, in some cases, cash awards. Award categories included "Top Producing Broker," "Most Money Raised," "Most New Accounts," and "Biggest Producer."

C. Edward Beyn

Beyn began working at Pointe Capital in 2007, while still in high school, and registered with the firm as a general securities representative in May 2008. Beyn worked with Taddonio at Pointe Capital, and Taddonio was one of the brokers at that firm who trained Beyn. With the exception of a brief period during which he moved to another FINRA member, Beyn worked at Pointe Capital until May 2010, when he registered with Taddonio's Brookstone branch office. Beyn transferred his registration to CSC when it commenced operations in February 2012. He remained with CSC until September 2015, when he joined another FINRA member for several months. Beyn is not currently associated with any FINRA member.

II. Procedural History

This case arose out of a May 2014 FINRA examination of CSC. On December 30, 2015, FINRA's Department of Enforcement ("Enforcement") filed a complaint against CSC, Taddonio, and Porges, followed by the filing, on January 5, 2016, of a five-cause corrected complaint.[6] In the corrected complaint, Enforcement charged that "from the day [CSC] opened its doors in January 2012 through at least December 2014," CSC, Taddonio, and Porges "fostered a culture of aggressive, excessive trading of customer accounts" and "encourag[ed] the firm's registered representatives to use upcoming earnings announcements as a catalyst for recommending hundreds, and in some cases thousands, of short-term trades in customer accounts." Enforcement alleged that, as a result of this culture, CSC, Taddonio, Porges, and the firm's registered representatives "earned more than $5 million in commissions (including mark-ups and mark-downs) while customers suffered more than $9 million in losses in accounts where the annualized turnover rates were as high as more than 200 and the annualized cost-to-equity ratios

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[6] CSC did not file an answer to the corrected complaint, and on November 15, 2016, the Hearing Officer entered an order holding CSC in default and deeming all the allegations against CSC as admitted. On August 10, 2017, the Hearing Officer issued a default decision with respect to CSC. The Hearing Officer found that CSC: (1) engaged in excessive trading of customer accounts, in violation of NASD Rule 2310, NASD IM-2310-2, and FINRA Rules 2111 and 2010; (2) engaged in churning of customer accounts, in violation of Exchange Act Section 10(b), Exchange Act Rule 10b-5, and FINRA Rules 2020 and 2010; and (3) made false statements in written responses to FINRA requests for information, in violation of FINRA Rules 8210 and 2010. For these violations, the Hearing Officer expelled CSC from FINRA membership. The Hearing Officer also found that CSC: (1) failed to supervise and failed to maintain adequate written supervisory procedures, in violation of NASD Rule 3010 and FINRA Rule 2010; and (2) failed to comply with telemarketing rule requirements, in violation of FINRA Rules 3230 and 2010. The Hearing Officer did not impose any sanctions for these violations in light of the expulsion imposed for CSC's excessive trading, churning, and false statements.

were as high as more than 800%." The corrected complaint further alleged that CSC, Taddonio, and Porges failed to establish and implement a reasonable supervisory system designed to prevent excessive trading and churning, and did "little to nothing" to respond to numerous red flags indicating excessive trading and churning. Enforcement also alleged that Taddonio and Porges gave false testimony to FINRA in sworn on-the-record interviews concerning whether registered representatives used recording devices to record conversations with customers.

Two causes were alleged against Taddonio and Porges. Cause three of the corrected complaint alleged that CSC, Taddonio, and Porges failed to establish, maintain, and enforce a reasonable supervisory system, including written supervisory procedures, designed to prevent excessive trading and churning in customer accounts, in violation of NASD Rule 3010(a) and (b) and FINRA Rule 2010.[7] Cause five alleged that CSC, Taddonio, and Porges violated FINRA Rules 8210 and 2010 by giving false testimony to FINRA in on-the-record interviews concerning the firm's use of recording devices to record conversations with customers. On February 22, 2016, Taddonio's and Porges's counsel filed an answer denying the alleged violations against his clients.[8]

On March 16, 2016, Enforcement filed a three-cause complaint against Beyn. Enforcement alleged that, during the period from March 2012 through May 2015, Beyn exercised control over the accounts of six customers and excessively traded and churned those accounts. Enforcement alleged that, based on the frequency of trading and the commissions charged, "there was little to no possibility that the customers would profit from [the] trading" and Beyn "abused [his customers'] trust by excessively and fraudulently trading the accounts."

Cause one of the complaint against Beyn alleged that Beyn churned the accounts of six customers, in violation of Exchange Act Section 10(b), Exchange Act Rule 10b-5, and FINRA Rules 2020 and 2010. Cause two alleged that Beyn excessively traded the accounts, in violation of NASD Rule 2310 and FINRA Rules 2111 and 2010. Cause three alleged that Beyn recommended investments in exchange traded notes to a customer without reasonable grounds for believing that the investment was suitable for that customer, in violation of NASD Rule 2310

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[7] Causes one, two, and four were asserted against CSC only. Cause one of the corrected complaint alleged that CSC, acting through three of its registered representatives, exercised control over several customer accounts and excessively traded those accounts, in violation of FINRA Rules 2111 and 2010 and NASD Rule 2310 and IM-2310-2. In cause two, Enforcement alleged that CSC, through its registered representatives, churned customer accounts, in willful violation of Exchange Act Section 10(b) and Exchange Act Rule 10b-5, and in violation of FINRA Rules 2020 and 2010. Court four alleged that CSC violated FINRA Rules 3230 and 2010 by failing to establish a reasonable system and procedures to prevent cold calls to persons on the national do-not-call list.

[8] Taddonio's and Porges's counsel withdrew shortly thereafter, and Taddonio and Porges proceeded pro se.

and FINRA Rules 2111 and 2010. After being granted an extension of time to do so, Beyn's counsel filed an answer denying the alleged violations against Beyn.[9]

On April 14, 2016, Enforcement moved pursuant to FINRA Rule 9214(b) to consolidate the case against CSC, Taddonio, and Porges with the case against Beyn on the grounds that both cases "arose out of the same set of operative facts."[10] On June 1, 2016, the Chief Hearing Officer granted the motion to consolidate the cases.

A twelve-day hearing was held during January and February 2017, at which Taddonio, Porges, and Beyn testified. The Hearing Panel also took testimony from 13 other witnesses, including both of CSC's CCOs, former CSC employees, several CSC customers, and FINRA staff. The Hearing Panel admitted more than 250 exhibits into evidence, and it allowed the record to remain open for a month after the conclusion of the hearing to allow the respondents to introduce additional evidence.[11] The parties also submitted post-hearing briefs.

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[9] Beyn's counsel withdrew prior to the hearing, and Beyn proceeded pro se.

[10] FINRA Rule 9214(b) provides that a "[p]arty may file a motion to consolidate two or more disciplinary proceedings if such consolidation would further the efficiency of the disciplinary process, if the subject complaints involve common questions of law or fact or one or more of the same Respondents, or if one or more of the factors favoring consolidation . . . appear to be present." FINRA Rule 9214(a) lists the factors favoring consolidation, which include: "(1) whether the same or similar evidence reasonably would be expected to be offered at each of the hearings; (2) whether the proposed consolidation would conserve the time and resources of the Parties; and (3) whether any unfair prejudice would be suffered by one or more Parties as a result of the consolidation."

[11] On appeal, Taddonio and Beyn argue that the Hearing Officer improperly denied their request to adjourn the hearing and allow them more time to review documents for possible exculpatory evidence. We have considered and reject this argument. The record shows Enforcement complied with its obligations to produce documents in discovery and provided Taddonio and Beyn with substantial assistance in accessing those documents. Taddonio and Beyn had months prior to the hearing to review documents. After knowing of the upcoming hearing for months, they waited until the last minute to request the adjournment. Both respondents participated actively in the hearing, asking many questions of the witnesses, referring to various documents, and filing written arguments. While the Hearing Officer denied the adjournment, he gave respondents considerable leeway in introducing documents and left the record open for a month after the conclusion of the hearing to allow them to introduce additional evidence. Only Taddonio availed himself of the opportunity, and submitted documents that the Hearing Panel accepted into the record. Significantly, the documents that respondents complain they had an insufficient opportunity to review were CSC's own documents, and respondents have failed either during the hearing or this appeal to identify any category of documents produced that may have assisted in their defense, but which they were denied an opportunity to introduce. Our review of the record confirms that the parties were given ample opportunity to introduce all of the evidence that was relevant to their claims. *See* FINRA Rule 9263(a).

On July 31, 2017, the Hearing Panel issued its decision. The Hearing Panel found that Beyn controlled the trading in nine accounts belonging to six customers, and that he excessively traded those accounts, in violation of NASD Rule 2310 and FINRA Rules 2111 and 2010. The Hearing Panel also found that Beyn churned these accounts, in violation of Exchange Act Section 10(b), Exchange Act Rule 10-b5, and FINRA Rules 2020 and 2010. The Hearing Panel also found that Beyn made unsuitable recommendations to a customer of exchange traded notes, in violation of NASD Rule 2310 and FINRA Rules 2111 and 2010. For these violations, the Hearing Panel barred Beyn from associating with any FINRA member firm in any capacity.

With respect to the allegations against Taddonio and Porges, the Hearing Panel found that both Taddonio and Porges failed to exercise reasonable supervision in light of numerous red flags confronting them that Beyn and other CSC registered representatives were excessively trading customer accounts. The Hearing Panel found that Taddonio's and Porges's supervisory failures violated NASD Rule 3010(a) and (b) and FINRA Rule 2010. For these supervisory violations, the Hearing Panel barred Taddonio and Porges from associating with any FINRA member firm in a principal or supervisory capacity. Finally, the Hearing Panel found that Taddonio and Porges gave false testimony to FINRA in sworn on-the-record interviews concerning CSC brokers' use of devices to record conversations, in violation of FINRA Rule 8210 and 2010. For these violations, the Hearing Panel barred Taddonio and Porges from associating with any FINRA member firm in any capacity.

Taddonio, Porges, and Beyn each filed a notice of appeal challenging the Hearing Panel's factual findings, legal conclusions, and the sanctions it imposed. Porges moved to withdraw his appeal on March 11, 2018. On April 23, 2018, the National Adjudicatory Council ("NAC") advised Porges that it had determined not to call his case for review and, as a result of the withdrawal of his request for appeal, the Hearing Panel's decision is FINRA' s final disciplinary decision with respect to Porges.

After an independent review of the record, we affirm the Hearing Panel's findings of violation. We also affirm the bar in any capacity imposed on Beyn for excessive trading and churning, and the bar imposed on Taddonio for giving false testimony to FINRA. For Taddonio's supervisory violations, however, we modify the sanction and impose a bar in all capacities. As discussed in more detail below, we find that Taddonio's supervisory violations were egregious, and they reflect a fundamental lack of understanding of and willingness to abide by the regulatory requirements required of individuals in the securities industry. We find that Taddonio poses a danger to the industry and the investing public and, accordingly, a bar in all capacities is appropriate for his supervisory violations.

III. Discussion

A. Beyn Excessively Traded and Churned Customer Accounts and Recommended Unsuitable Investments to a Customer

1. Facts

The allegations of violations against Beyn involve the trading in nine accounts which belonged to six customers—EK, BM, TP, EH, WR, and JB. Four of these customers—EK, BM, TP, EH—testified at the hearing. Beyn employed the earnings play strategy in trading these accounts, and he effected the transactions in the accounts on a riskless principal basis, charging the customers mark-ups and mark-downs rather than commissions.

a. EK

When EK opened his account, he was almost 70 years old and semi-retired. In addition to social security, he earned approximately $26,000 from a construction business. EK testified that, after high school, he had attended less than a year of college and two years at a trade school. Prior to trading at CSC, EK's investment experience was limited to a single trade he had made decades earlier. EK testified that he lost money on that trade and never traded again.

EK testified that he was contacted by CSC through a cold call. EK agreed to open an account and invest $5,000 with CSC. Soon after opening the account, it was transferred to Beyn. EK testified that he and Beyn spoke frequently and often had long talks. EK said he came to trust Beyn and consider him a friend. EK said that Beyn told him he would make a lot of money for him.

Based on his conversations with Beyn, EK agreed to invest an additional $350,000 in his CSC account. Beyn explained to EK that he would be using the earnings play strategy for the account. EK testified that he told Beyn this money was all he had for retirement and that he would rely on Beyn to make recommendations for his account. EK testified: "I told [Beyn] I had none, no investment experience at all. And if I was going to do this, that I would have to rely on him and Mr. Beyn assured me not to worry he would make us lots of money." EK testified that Beyn recommended all the trades in his account, and EK simply agreed to Beyn's recommendations.

EK testified that he signed his account opening documentation even though it contained certain errors because Beyn told him it was just a formality. At Beyn's request, EK also signed a margin agreement because Beyn claimed margin would make his account "more flexible."

EK testified that Beyn never explained the meaning of riskless principal trades to him and that they never discussed the mark-ups and mark-downs EK would be charged for these trades. EK testified that Beyn told him that he would pay a fee of $99 for each trade. EK acknowledged that he received trade confirmations for his account, but he testified that he did not understand that he was being charged more than the $99 commission, which he understood was the sole cost for each trade.

EK's account was actively traded from March 1, 2012, through August 31, 2013. During that period, there were 115 trades in EK's account, which had a realized net loss of more than $230,000. EK's costs for the account totaled more than $188,000, including more than $166,000 in mark-ups and mark-downs, $11,000 in Firm Commissions, and $10,000 in margin interest. Beyn received more than $116,000 from the mark-ups and mark-downs charged to EK.

The annualized cost-to-equity ratio for EK's account during the period it was actively traded was more than 70%, and the account had an annualized turnover rate of more than 18.[12] The 70% cost-to-equity ratio meant that EK's account would have to realize annual gains of 70% just to break even. The turnover ratio indicates that over the course of a year, EK's portfolio of securities was exchanged more than 18 times.

b. BM

BM testified that he is college-educated and self-employed as a sales representative for aviation companies, earning approximately $200,000 per year. At the time he opened his account with CSC, BM was 60 years old, married, and had a disabled adult daughter whom he supported.

BM testified that, after receiving approximately 3-5 cold calls from a CSC broker over a period of several months, he agreed to open an account and make a small investment. BM's investment experience consisted of a Prudential annuity, a managed account that he had previously liquidated and closed, a few aviation stocks he had purchased in a self-directed account because he was familiar with the companies through his business, an investment in Garmin stock because he knew one of the company's founders, and an investment in a company that made body cameras for police because he thought that would be a growing business. At the time BM opened his CSC account, he had $700,000 in his Prudential annuity and $400,000 in a Schwab account.

BM testified that he initially agreed to invest $10,000 with CSC in an IRA account to "test it out." He testified that shortly after completing his new account paperwork and making his initial investment, he was contacted by Beyn, who told him that his account had been transferred to him because he had more experience as a broker. BM testified that Beyn told him

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[12] An account's cost-to-equity ratio is the percentage the account would have to appreciate just to break even given the costs of trading and is calculated by dividing the total expenses by the average monthly equity in an account. *Ralph Calabro*, Exchange Act Release No. 75076, 2015 SEC LEXIS 2175, at * 31 (May 29, 2015). Turnover rate refers to the number of times the securities in the account were exchanged for a different portfolio of securities and is calculated by dividing the total purchases in the account by the average account equity and annualizing the number. *Id.*

The cost-to-equity ratio for EK's account for the active period only (not annualized) was more than 106% and the turnover rate for this period was almost 28.

that he could not be effective with an investment of only $10,000, but that if BM invested a larger amount of money, Beyn could make him an additional $40,000 in only three to four months. BM testified that Beyn did not explain how he would achieve these gains.

After speaking with Beyn, BM agreed to invest an additional $240,000 with Beyn. When he received the transfer paperwork from CSC, however, BM saw that the amount of the transfer was listed at $400,000—the entire amount in the brokerage account from which he was making the transfer. BM said he changed the amount to $240,000, returned the paperwork, and only $240,000 was transferred.

BM testified he told Beyn that, although he wanted his money to grow, he also did not want to lose it. BM also testified that Beyn never asked him about the level of risk he was willing to bear, and he told Beyn he was supporting an adult, disabled child. The account opening documents for BM's IRA account lists his investment objective as "maximum growth," which was defined as "[m]aximum capital appreciation with higher risk and little to no income." BM testified that the new account documents were largely prefilled with information when he received the documents from CSC to sign.

BM testified that he spoke frequently to Beyn and relied on Beyn's recommendations. In making recommendations, Beyn would refer to earnings reports and estimate the gains they would "stand to book" from a trade. BM testified that he often responded to Beyn's recommendations by saying "you're the expert" and "I have to rely on you." BM testified that, when his account started to experience losses, Beyn would always have an excuse and would reassure him that they "would make it up on the next one."

While BM acknowledged that he received trade confirmations and account statements, he testified that he was not fully aware of the level of trading in the account. He also testified that he was not aware that he had signed a margin agreement and did not understand what margin means.

BM testified that he and Beyn never discussed mark-ups and mark-downs, and it was BM's understanding that he was paying only a commission of $99 per trade—an amount BM thought was high in comparison to the $18 he had previously paid for self-directed trades. BM testified that, when the account started experiencing losses, he tried to use the trade confirmations to calculate the amount of the loss. Based on his calculation, BM thought his account had lost approximately $25,000. When he closed his account and transferred the balance to another broker-dealer, he realized his losses were almost three times as much. BM testified that he could not understand the discrepancy until an attorney he consulted for help explained that he had been paying mark-ups and mark-downs in addition to the $99 Firm Commission.

BM's account was actively traded from January 2015, through May 2015. During that period, there were 80 trades in BM's account, and the account realized net losses of more than $65,000. The total costs of the trading in the account were more than $52,000, including mark-ups and mark-downs of more than $44,000 and almost $8,000 in Firm Commissions. Beyn's share of the mark-ups and mark-downs paid by BM was more than $15,000.

The annualized cost-to-equity ratio in BM's account was more than 70%, and the account had an annualized turnover rate of more than 23. Based on the level of trading and fees charged to BM's account, he would have had to realize gains of more than 70% to break even. Moreover, in the course of just five months, the portfolio of securities in BM's account was completely exchanged almost 10 times, an average of almost twice per month.[13]

c. TP

TP is 80 years old and an engineer. He co-owned a construction company with another Beyn customer, EH. He first opened an account with Beyn when Beyn was associated with Brookstone. EH became involved with Brookstone when he responded to a Brookstone solicitation to buy stock in Facebook's IPO. When Beyn joined CSC, TP transferred his accounts to CSC.

TP had two accounts at CSC, an individual account and an IRA valued at approximately $1.4 million. TP testified that while he hoped to grow his IRA to $5 million, he told Beyn he did not want to speculate in that account, but was willing to speculate in his individual account. The investment objective for the CSC IRA was "growth," defined as "capital appreciation through quality equity investments and little or no income." The investment objective for TP's individual account was "speculation." TP testified that he expected the individual account and IRA to be invested differently.

TP testified that Beyn told him he was using the earnings play strategy and that he accepted all of Beyn's recommendations. TP testified that Beyn selected which stock to trade, when to buy and sell it, and determined how many shares to trade. TP testified that Beyn assured him on multiple occasions that he would "win 12 of every 15 trades." TP also testified that his understanding was that he was paying $99 for each trade and that it was not until he was contacted by FINRA that he understood that he was also paying mark-ups and mark-downs on his trades.

TP's individual account was actively traded from May 2012, through December 2013. During that period, there were 154 trades in the account, the account had a net realized loss of more than $66,000, and incurred costs of almost $81,000, including mark-ups and mark-downs of more than $65,000 and Firm Commissions of more than $15,000. Beyn received almost $23,000 of the mark-ups and mark-downs charged to TP's individual account. The account had an annualized cost-to-equity ratio of more than 70% and an annualized turnover rate of more than 22.[14]

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[13] The non-annualized cost-to-equity ratio for the period the account was actively traded was almost 30%, and the non-annualized turnover rate was almost 10.

[14] The non-annualized cost-to-equity ratio for the period TP's individual account was actively traded was more than 119%, and the non-annualized turnover rate was more than 37.

TP's IRA was actively traded from April 2012, through December 2013. During this period, there were 662 trades in the IRA (an average of more than 31 trades per month) and realized net losses of almost $787,000. For this period, the IRA incurred costs of almost $600,000. Of these costs, more than $533,000 were mark-ups and mark-downs, and more than $65,000 were Firm Commissions. Beyn received more than $186,000 of the mark-ups and mark-downs charged to TP's IRA. The IRA had an annualized cost-to-equity ratio of almost 34% and an annualized turnover rate of almost 11.[15]

d. EH

EH was TP's partner in a construction company. EH became Beyn's customer at Brookstone after he was referred by TP to that firm to purchase Facebook stock. Like TP, EH transferred his account to CSC when Beyn joined CSC. Prior to investing at CSC, EH had several individual and IRA investment accounts and had invested in silver and gold.

EH had two accounts at CSC—an IRA account and an account held in the name of a limited partnership EH used to invest (the "LP Account"). The initial account opening form for the LP Account included a preprinted account objective of "speculation." It also included, however, a handwritten note indicating that EH's objective was "maximum growth." In an updated account form completed a year later, EH's objective for the LP Account was listed as "maximum growth." EH's IRA account objective was listed as "growth." EH transferred $1.4 million from an existing IRA into his CSC IRA.

EH testified that he and Beyn spoke often and that he followed Beyn's recommendations. EH also testified that he continued to pursue his interest in silver and gold and suggested to Beyn that they invest in gold and silver exchange traded funds ("ETFs").[16] Instead of investing in a silver and gold ETFs, however, Beyn recommended that EH invest in exchange traded notes

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[15] The non-annualized cost-to-equity ratio for the period TP's IRA account was actively traded was more than 59%, and the non-annualized turnover rate was almost 19.

[16] ETFs are "SEC-registered investment companies that offer investors a way to pool their money in a fund that invests in stocks, bonds, or other assets. In return, investors receive an interest in the fund. Most ETFs are professionally managed by SEC-registered investment advisers. Some ETFs are passively-managed funds that seek to achieve the same return as a particular market index (often called index funds), while others are actively managed funds that buy or sell investments consistent with a stated investment objective." *See Fast Answers, Exchange Traded Funds (ETFS)*, U.S. Sec. Exch. Comm'n, https://www.sec.gov/fast-answers/answersetfhtm.html (last modified Dec. 6, 2017). EFTs "combine features of a mutual fund, which can only be purchased or redeemed at the end of each trading day at its NAV per share, with the ability to trade throughout the day on a national securities exchange at market prices." *Id.*

("ETNs").[17] EH testified that Beyn—not EH—recommended investing in an ETN and he did not understand anything about ETNs.

Beyn recommended three ETNs to EH. In June 2012, EK invested $63,000 in the iPath S&P 500 VIX Short Term Futures ETN ("VXX"), which he held until June 2013, and sold for a loss of $42,500. In August 2013, EH invested $120,000 in Velocity Shares 3X Long Gold ETN ("UGLD") and Velocity Shares 3X Long Silver ETN ("USLV"), which EH transferred to another firm when he closed his CSC accounts in October 2013.

VXX, UGLD, and UDLV were all highly complex and speculative investments intended for highly sophisticated investors. According to the issuer, VXX was intended as a "short-term tactical vehicle[] to express views on the direction of volatility or as [a] customizable solution[] to manage or hedge risk in a portfolio." The issuer also warned that ETNs like VXX "are riskier than ordinary unsecured debt securities" and could result in the loss of some or all of an investor's principal. Similarly, the issuer of UGLD and USLV cautioned that "ETNs are intended to be daily trading tools for sophisticated investors to manage daily trading risks" and are designed to "achieve their stated investment objectives on a daily basis." The issuer further cautioned that ETNs "should be purchased only by knowledgeable investors," and investors "should actively and frequently monitor their investments in ETNs, even intra-day." Finally, the issuer cautioned that "it is possible [investors] will suffer significant losses in the ETNs" even if the long-term performance of the underlying index is favorable.

EH's IRA was actively traded from April 2012, through July 2014. During this period, there were 398 trades in the IRA, and it sustained net realized losses of $985,000. Also during this period, the IRA incurred costs of more than $426,000, including $387,000 in mark-ups and mark-downs and almost $39,000 in Firm Commissions. Beyn's share of the mark-ups and mark-downs charged to this account was more than $135,000. EH's IRA had an annualized cost-to-equity ratio of more than 18% and an annualized turnover rate of more than 8.[18]

EH's LP Account was actively traded from March 2012, through July 2014. During that period, there were 323 trades in the account, and the account had more than $571,000 in net realized losses. During the period it was actively traded, the LP Account incurred more than $261,000 in costs, including almost $224,000 in mark-ups and mark-downs and almost $32,000 in Firm Commissions. Beyn's share of the mark-ups and mark-downs charged for this account

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[17] ETNs are unsecured debt obligations for which the issuer promises to pay an amount as determined by an underlying index or benchmark on a specified maturity date. *See Investor Bulletin: Exchange Traded Notes (ETNs)*, U.S. Sec. Exch. Comm'n, https://www.sec.gov/oiea/investor-alerts-bulletins/ib_etn.html (Dec. 1, 2015). ETNs do not actually buy or hold any assets listed on the underlying index. *Id.*

[18] The non-annualized cost-to-equity ratio for the period EH's IRA was actively traded was more than 42%, and the non-annualized turnover rate was more than 19.

was more than $78,000. EH's LP account had an annualized cost-to-equity ratio of more than 21% and an annualized turnover rate of more than 8.[19]

e. WR and JB

Beyn's customers, WR and JB, did not testify at the hearing.[20] WR had two accounts at CSC with Beyn. WR's first account was actively traded from June 2013, through September 2013, during which there were 94 trades (an average of more than 23 trades per month). Beyn marked 77 of these 94 trades as "solicited." During the relevant period, the account had a net realized loss of more than $86,000 and incurred costs of more than $46,000, including more than $36,000 in mark-ups and mark-downs (of which Beyn received more than $25,000) and more than $9,000 in Firm Commissions. The annualized cost-to-equity ratio for this account was more than 182% and it had an annualized turnover of more than 52.[21] WR closed this account in September 2013.

WR's second CSC account with Beyn was actively traded from April 2014, through July 2014. During this period, there were 88 trades in the account (an average of 22 trades per month), all of which were marked "solicited" by Beyn. This account suffered a realized net loss of more than $52,000 and incurred costs of almost $49,000. The costs included almost $40,000 in mark-ups and mark-downs (of which Beyn received almost $28,000) and almost $9,000 in Firm Commissions. The account had an annualized cost-to-equity ratio of more than 546% and an annualized turnover rate of more than 177.[22]

JB's account was actively traded from April 2014, through July 2014. During this period, there were 106 trades in the account (an average of approximately 26 trades per month), and the account had net realized losses of almost $66,000. Beyn marked 105 of the 106 trades in JB's account "solicited." The costs incurred in the account during this period were almost $66,000, including almost $55,000 in mark-ups and mark-downs (of which Beyn received more

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[19] The non-annualized cost-to-equity ratio for the period EH's LP Account was actively traded was more than 51%, and the non-annualized turnover rate was more than 20.

[20] Enforcement offered the testimony of a FINRA examiner who had spoken to WR and JB. The Hearing Panel, however, did not give substantial weight to the examiner's hearsay testimony concerning his conversations with these customers because the examiner was only able to relate the general content of the conversations but could not recall them in detail. We agree, and do not rely on the examiner's testimony in this decision. Instead, we rely solely on the documentary evidence concerning WR's and JB's accounts.

[21] The non-annualized cost-to-equity ratio for the period WR's first account was actively traded was more than 60%, and the non-annualized turnover rate was almost 53.

[22] The non-annualized cost-to-equity ratio for the period WR's second account was actively traded was more than 182%, and the non-annualized turnover rate more than 59.

than $38,000) and more than $10,000 in Firm Commissions. The account had an annualized cost-to-equity ratio of more than 573% and an annualized turnover rate of more than 188.[23]

2. Discussion

a. Beyn Was Not a Credible Witness

The Hearing Panel made detailed findings concerning the relative credibility of Beyn and the customers who testified during the hearing. With respect to the customers, the Hearing Panel found "these customers' testimony generally credible." The Hearing Panel explained that "[e]ach customer answered questions in a straightforward, direct manner; each customer's testimony was internally consistent; and the testimony of each customer was consistent with the testimony of the other customers."

On the other hand, the Hearing Panel found Beyn not credible. The Hearing Panel "observed Beyn as he testified at the hearing." It concluded that "Beyn was evasive, avoiding direct responses to clear questions; his testimony was inconsistent; and his demeanor suggested that he was formulating answers that he thought might be helpful to his case rather than providing candid responses to the questions." The Hearing Panel concluded that Beyn's testimony was self-serving and not credible.

While we conduct a de novo review of the Hearing Panel's decision, we give substantial weight and deference to the Hearing Panel's credibility findings. *See Eliezer Gurfel*, 54 S.E.C. 56, 62 n.11 (1999), *aff'd*, 205 F.3d 400 (D.C. Cir. 2000). It is well settled that the "credibility determinations of an initial fact-finder, which are based on hearing the witnesses' testimony and observing their demeanor, are entitled to considerable weight and deference, and can be overcome only where the record contains substantial evidence for doing so." *See, e.g.*, *John Montelbano*, 56 S.E.C. 76, 89 (2003); *Daniel D. Manoff*, 55 S.E.C. 1155, 1161-62 & n.6 (2002); *Dep't of Enforcement v. Elgart*, Complaint No. 2013035211801, 2017 FINRA Discip. LEXIS 9, at *24-25 (FINRA NAC Mar. 16, 2017), *aff'd*, Exchange Act Release No. 81779, 2017 SEC LEXIS 3097 (Sept. 29, 2017), *aff'd*, 2018 U.S. App. LEXIS 26627 (11th Cir. Sept. 19, 2018). We find no substantial evidence in the record to warrant overturning the Hearing Panel's credibility determinations. To the contrary, the record amply supports those findings, and we affirm them.

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[23] The non-annualized cost-to-equity ratio for the period JB's account was actively traded was more than 191%, and the non-annualized turnover rate was almost 63.

b. Beyn Excessively Traded the Accounts of Six Customers

The Hearing Panel found that Beyn excessively traded nine accounts of six customers, in violation of FINRA's suitability rules—NASD Rule 2310 and FINRA Rule 2111—and FINRA Rule 2010.[24] We agree.

NASD Rule 2310 requires that "[i]n recommending to a customer the purchase, sale or exchange of any security," a broker "shall have reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts . . . disclosed by such customer as to his other security holdings and as to [the customer's] financial situation and needs." FINRA Rule 2111 similarly provides that a "member or an associated person must have a reasonable basis to believe that a recommended transaction or investment strategy involving a security or securities is suitable for the customer." Recommendations violate the suitability rule if "(i) the representative's understanding of the investment is insufficient to establish a reasonable basis for making a recommendation; (ii) the representative inadequately assesses whether the recommendation is suitable for the specific investor to whom the recommendation is directed; or (iii) the level of trading recommended by the representative is excessive in light of the customer's investment needs and objectives." *Richard G. Cody*, Exchange Act Release No. 64565, 2011 SEC LEXIS 1862, at *26 (May 27, 2011), *aff'd*, 693 F.3d 251 (1st Cir. 2012); *see also John M. Reynolds*, 50 S.E.C. 805, 806 (1991) (explaining that the suitability rule includes the requirement that the trading in an account be quantitatively suitable) (internal quotations omitted).

Quantitative suitability means that the broker has "reasonable grounds to believe that the number of recommended transactions within a particular period is not excessive." *Dep't of Enforcement v. Medeck*, Complaint No. E9B2003033701, 2009 FINRA LEXIS Discip. 7, at *31 (FINRA NAC July 30, 2009). Quantitative suitability "focuses not on the underlying characteristics of a particular security but on whether the number of transactions within a given timeframe is suitable in light of the customer's financial circumstances and investment objectives." *Id.* at *32. "Excessive trading occurs when a registered representative has control over the trading in an account and the level of trading in that account is inconsistent with the customer's objectives and financial situation." *Cody*, 2011 SEC LEXIS 1862, at *40-41.

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[24] FINRA Rule 2111 replaced NASD Rule 2310 effective July 9, 2012. *See FINRA Regulatory Notice 11-25*, 2011 FINRA LEXIS 45 (May 2011). Accordingly, NASD Rule 2310 applies to transactions prior to July 9, 2012, and FINRA Rule 2111 applies to transactions on or after July 9, 2012. A violation of NASD Rule 2310 or FINRA Rule 2111 is also a violation of FINRA Rule 2010, which requires registered representatives to observe high standards of commercial honor and just and equitable principles of trade. *Cody*, 2011 SEC LEXIS 1862, at *26.

i. Control

The accounts at issue were not discretionary accounts. In addition to having formal discretionary authority over an account, however, a broker can control an account if he has de facto control of the account. *Medeck*, 2009 FINRA Discip. LEXIS 7, at * 33-34. De facto control may be established when the customer relies on the representative such that the representative controls the volume and frequency of the account. *Clyde J. Bruff*, 53 S.E.C. 880, 883 (1998), *aff'd*, 1999 U.S. App. LEXIS 27405 (9th Cir. Oct. 25, 1999); *see also Calabro*, 2015 SEC LEXIS 2175, at *18 (explaining that de facto control may be established (1) "when the customer relies on the representative such that the representative controls the volume and frequency of transactions" or (2) "where a customer routinely follows a registered representative's recommendations" and the customer does not have "sufficient understanding to make an independent evaluation of the broker's recommendations") (internal quotations omitted).

Beyn argues that his customers were sophisticated, understood the trading in their accounts, and controlled that trading. The four customers who testified all claimed that they relied on Beyn to recommend the trading in their accounts and that they routinely followed his recommendations. Moreover, all the customers testified that they did not understand the level of trading in the accounts and did not understand the costs they were paying for that trading. The Hearing Panel found the customers' testimony credible and Beyn's testimony not credible and concluded that Beyn controlled the customers' accounts. We agree.

EK testified that, prior to opening his CSC account, his investment experience was limited to a single trade on which he lost money. He testified that he trusted Beyn and relied on him completely to determine all the trading in his account. EK also testified that Beyn never discussed the costs of the trading with him and he did not understand mark-ups and mark-downs. The Hearing Panel found that EK "reasonably believed that he was only being charged $99 per trade" and rejected as "not credible" Beyn's claim that EK was a sophisticated investor. To the contrary, the Hearing Panel found that EK was an inexperienced and unsophisticated investor who trusted Beyn. We find that the record supports these findings and there is no evidence in the record, much less substantial evidence, to disturb these credibility findings.

BM testified that his investment experience was limited to an annuity, a managed account, and a handful of stocks—mostly aviation stocks, the business in which he worked. BM also testified that he relied on Beyn completely for the trading in his account. BM did not understand what margin was and, despite reviewing trade confirmations and trying to calculate his losses, he did not understand what mark-ups and mark-downs were and did not know how to calculate them. Until he consulted an attorney after experiencing heavy losses, BM believed that he was paying $99 per trade. The Hearing Panel found BM credible and rejected "Beyn's self-serving statements" that the customers were sophisticated and understood the risks of the trading as not credible. The record supports the Hearing Panel's determination to credit BM's testimony over Beyn's.

TP testified that he relied on Beyn for the trading in his accounts and accepted all his recommendations. The Hearing Panel concluded, based on its assessment of TP's credibility as a witness, that while TP had sophistication as a businessman, he was more focused on running his

construction business than managing the trading in his CSC accounts. Instead, he relied on Beyn to do so. The Hearing Panel also credited TP's testimony that, while he wanted to speculate in his individual account, he expected his IRA account to be treated more conservatively. Beyn, however, pursued the same frequent short-term trading strategy in both accounts. We find no substantial evidence in the record to disturb the Hearing Panel's decision to credit TP's testimony rather than Beyn's.

EH testified that he followed all Beyn's recommendations. EH also testified that he wanted to invest in ETFs, not ETNs, and that he did not understand ETNs at all. The Hearing Panel credited EH's testimony and found Beyn's claims that EH was a "sophisticated investor" with "vast knowledge" of investment products not credible. The Hearing Panel stated that "having observed EH during his testimony, [it] does not find [EH] to be a sophisticated investor." The Hearing Panel credited EH's testimony that he that he did not understand he had purchased ETNs rather than ETFs and pointed to this as evidence of his lack of sophistication. The Hearing Panel also credited EH's testimony that he did not understand the costs he was paying for the trading in his account.

The Hearing Panel found that Beyn exercised control over the accounts of the two customers who did not testify, WR and JB. This conclusion was based on the fact that Beyn marked the vast majority of the trades in both customers' accounts "solicited" and the "outrageously" high cost-to-equity ratios and turnover rates in the accounts. WR's accounts had annualized cost-to-equity ratios of more than 546% and 182% and annualized turnover rates of almost 178 and 53. JB's account had an annualized cost-to-equity of more than 573% and annualized turnover of more than 188. These cost-to-equity ratios guaranteed that there was no way WR's and JB's accounts could break even, much less be profitable, and we agree that no customer who understood the trading in the account would agree to this trading, which could only benefit Beyn and CSC at the customer's expense. We therefore find that Beyn controlled WR's and JB's accounts.

Beyn makes much of the fact that his customers received confirmations for all the trading in their accounts. A customer's receipt of confirmations, however, does not demonstrate that the customer controls his or her account. *See, e.g.*, *Michael David Sweeney*, 50 S.E.C. 761, 765-66 (1991) (stating that the fact customers received confirmations and monthly statements did not change the Commission's view that the broker controlled the accounts where the broker initiated nearly all the transactions in the accounts and the customers did not fully understand the trading or the costs of the trading); *Jack H. Stein*, 56 S.E.C. 108, 119 n.31 (2003) (rejecting the argument that a customer was estopped from objecting to excessive trading because she had received confirmations and statements and was thus aware of the trading activity).

The record shows that Beyn chose the investments, including the volume and frequency of the trading, in his customers' accounts and that Beyn's customers, who did not have sufficient investment experience and understanding to make an independent evaluation of Beyn's recommendations, routinely followed those recommendations. *See, e.g.*, *Cody*, 2011 SEC LEXIS 1862, at *43 (finding that registered representative had de facto control because the customers "did not independently evaluate his recommendations but rather acquiesced in his trades"); *Gerald E. Donnelly*, 52 S.E.C. 600, 604 (1996) (finding control where customers

"approved individual transactions simply on the basis of [the registered representative's] recommendations"); *Joseph J. Barbato*, 53 S.E.C. 1259, 1272-77 (1999) (finding control where the registered representative chose the investments in the customer's account and the customer "habitually followed [his] recommendations"). We find, accordingly, that Beyn controlled the trading in EK's, BM's, TP's, EH's, WR's, and JB's accounts.

ii. Quantitative Unsuitability

We find that the level of trading by Beyn in EK's, BM's, TP's, EH's, WR's, and JB's accounts was grossly inconsistent with the customers' investment objectives and financial and personal circumstances. Beyn traded all the accounts the same, regardless of the listed investment objective and the customer's age or stated financial condition. Indeed, with respect to TP's IRA account, Beyn admitted that he ignored the growth objective listed for the account. We agree with the Hearing Panel that the trading in the accounts was excessive even assuming that all the customers wanted to speculate, given the costs Beyn was charging for the trading.

A determination of whether trading is quantitatively unsuitable "does not rest on any magical per annum percentage." *Donnelly*, 52 S.E.C. at 603 (internal quotations omitted). In determining quantitative unsuitability, however, we consider turnover rate, cost-to-equity ratio, and the number and frequency of trading, including the use of in-and-out trading. *See Calabro*, 2015 SEC LEXIS 2175, at *32; *Dep't of Enforcement v. Newport Coast Sec., Inc.*, Complaint No. 2012030564701, 2018 FINRA Discip. LEXIS 14, at *99 (FINRA NAC May 23, 2018), *appeal docketed*, SEC Admin. Proceeding No. 3-18555 (June 22, 2018). "While there is no definitive turnover rate or cost-to-equity ratio that establishes excessive trading, [the Commission has] held that a turnover rate of 6 or a cost-to-equity ratio in excess [] of 20% generally indicates that excessive trading has occurred." *Calabro*, 2015 SEC LEXIS 2175, at *32.

We agree with the Hearing Panel that the turnover rates and cost-to-equity ratios here are outrageously high and demonstrate that Beyn traded the accounts without any regard for the best interest or investment objectives of his customers. Rather, the level of trading demonstrates that Beyn traded the accounts to generate revenue for himself and CSC.

WR's accounts had annualized turnover rates of 52 and 177 and annualized cost-to-equity ratios of 182% and 546%, respectively. In just four months of trading, WR's accounts together contained an average of 45 trades per month, the vast majority of which Beyn marked "solicited." In the four months it was actively traded, JB's account had an average of 26 trades per month, an annualized turnover rate of 188, and an annualized cost-to-equity ratio of 573%. EK's account had an annualized turnover rate of 18 and an annualized cost-to-equity of 70%. BM's account contained 80 trades in the five months is was actively traded, an annualized turnover rate of 23, and an annualized cost-to-equity ratio of 70%. TP's individual account had an annualized turnover rate of 22 and an annualized cost-to-equity ratio of 70%, and his IRA, which averaged 31 trades per month, had an annualized turnover of 11 and an annualized cost-to-equity ratio of 34%. EH's accounts both had annualized turnover rates of 8 and annualized cost-to-equity ratios of 18% and 21%, respectively.

We find that the accounts of all six customers were excessively traded. All the accounts exceeded the turnover rates and cost-to-equity ratios that the Commission has held are indicative of excessive trading—6 and 20%, respectively. And all except EH's account exceeded these benchmarks by very large amounts. Given the costs charged by Beyn and CSC, the accounts had virtually no chance of breaking even, much less realizing any gains for the customers no matter how the underlying investments performed. Even in the case of EH's accounts, which had cost-to-equity ratios on the lower end, the accounts would have had to realize gains of 18% and 21% just to break even, given the costs of trading Beyn and CSC were charging to the accounts.

Under these circumstances, we can reach no other conclusion than the trading in the accounts Beyn controlled was quantitatively unsuitable, in violation of NASD Rule 2310 and FINRA Rules 2111 and 2010.

c. Churning

"Churning occurs when a securities broker enters into transactions and manages a client's account for the purpose of generating commissions and in disregard of his client's interests." *Donald A. Roche*, 53 S.E.C. 16, 22 (1997) (internal quotations omitted). Excessive trading constitutes churning when it is done with scienter, and churning violates Exchange Act Section 10(b), Exchange Act Rule 10b-5, and FINRA Rules 2020 and 2010.[25] *Newport Coast Sec.*, 2018 FINRA Discip. LEXIS 14, at *80, 109. Scienter is "a mental state embracing an intent to deceive, manipulate or defraud" and can be established by showing the broker's trading was intentionally for the purpose of generating commissions in disregard of the customer's interest or in reckless disregard of the customer's interests. *Calabro*, 2015 SEC LEXIS 2175, at *55. Churning "does not require proof of a specific or invidious intent to defraud." *Dzenits v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 494 F.2d 168, 171 n.2 (10th Cir. 1974). Rather, "scienter may be inferred from the amount of commissions charged by the registered representative." *Calabro*, 2015 SEC LEXIS 2175, at *55-56. It is sufficient that a broker acts with reckless disregard for the customer's interests. *See Studer*, 57 S.E.C. at 1020.

We find that Beyn acted with at least reckless disregard of his customers' interests. The turnover rates and cost-to-equity ratios demonstrate that Beyn acted with scienter. For all but EH's accounts, the customers' accounts would have to appreciate from 34% to 573% just to break even given the costs Beyn and CSC were charging and the levels of trading.[26] *See*

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[25] Churning is a manipulative and deceptive device within the meaning of Exchange Act Section 10(b) and Exchange Act Rule 10b-5. *See Michael T. Studer*, 57 S.E.C. 1011, 1020-23 (2004), *aff'd*, 260 F. App'x 342 (2d Cir. 2008). That same conduct also violates FINRA 2020, FINRA's antifraud rule, and is a violation of just and equitable principles of trade under FINRA Rule 2010. *See Davidofsky*, Complaint No. 2008015934801, 2013 FINRA Discip. LEXIS 7, at *26 n.27 (FINRA NAC Apr. 26, 2013).

[26] We agree with the Hearing Panel that although the turnover rates and cost-to-equity ratios for EH's accounts were lower than for Beyn's other customers, the trading in EH's accounts

[Footnote continued on next page]

Newport Coast Sec., Inc., 2018 FINRA Discip. LEXIS 14, at *109-10 (finding that the "exceptionally high trading volume, the in-and-out trading, the exorbitant turnover rates, and the sky-high returns that [the broker's] trading would have needed to generate for the . . . customers to break even evidence [the broker's] scienter"); *Davidofsky*, 2013 FINRA Discip. LEXIS 7, at *33 (finding that "[t]he cost-to-equity ratio and the turnover rate for [the customer's] account were so high that [the broker] must have known that he was acting in reckless disregard of [the customer's] interests," where the cost-to-equity ratio was nearly 45%).

Furthermore, while Beyn's customers experienced total losses of almost $3 million, Beyn earned almost $650,000 from the trading in the accounts—all in the form of mark-ups and mark-downs that all the customers testified they did not understand. Beyn's earnings further support the finding that he acted with the requisite scienter. *See Newport Coast Sec., Inc.*, 2018 FINRA Discip. LEXIS 14, at *109-10 (finding that the commissions a broker generated from his excessive trading "demonstrates that he acted with scienter"); *Davidofsky*, 2013 FINRA Discip. LEXIS 7, at *33 (same).

We find, accordingly, that Beyn churned EK's, BM's, TP's, EH's, WR's, and JB's accounts, in violation of Exchange Act Section 10(b), Exchange Act Rule 10b-5, and FINRA Rules 2020 and 2010.

d. Beyn Recommended Unsuitable ETNs to EK

NASD Rule 2310, and its successor, FINRA Rule 2111, require that, "[i]n recommending the purchase, sale, or exchange of any security," a broker "must have reasonable grounds for believing that the recommendation is suitable for that customer based on the facts . . . disclosed by the customer as to his other securities holdings and the customer's financial situation and needs"—i.e., that the recommendation is *qualitatively* suitable. *Dep't of Enforcement v. Xagoraris*, Complaint Nos. 20080127674 & 20080133768, 2014 FINRA Discip. LEXIS 34, at *18 (FINRA NAC Aug. 1, 2014). There are two types of analysis under NASD Rule 2310 and FINRA Rule 2111, known as "reasonable basis" suitability and "customer-specific" suitability. *See Dep't of Enforcement v. Luo*, Complaint No. 2011026346206, 2017 FINRA Discip. LEXIS 4, at *27-28 (FINRA NAC Jan. 13, 2017). To satisfy reasonable-basis suitability a broker must conduct a reasonable investigation and conclude that a recommendation could be suitable for at least some investors. *Id.* at *18-20; *see also Cody*, 2011 SEC LEXIS 1862, at *26-32. Customer-specific suitability requires that a broker must assess whether an investment recommendation is suitable for the specific customer to whom it is made, and to tailor recommendations to a customer's financial profile. *See Xagoraris*, 2014 FINRA Discip. LEXIS 34, at *18-20.

[cont'd]

must be viewed in the context of the pattern of excessive trading by Beyn across several accounts. We find that the trading in EH's accounts was also excessive.

The Hearing Panel found that the ETNs were unsuitable for EK. We agree. As the disclosure documents indicated, ETNs are speculative investments intended for highly sophisticated investors primarily to hedge intraday risks. The ETNs were not suitable for an individual investor, like EK, who purchased and held them for long periods of time.

Beyn did not argue at the hearing that the ETNs were suitable. Rather, he argued that EK purchased the ETN's on an unsolicited basis and against Beyn's advice. The Hearing Panel did not credit Beyn's account. Beyn marked one of the ETN purchases "solicited," and EK testified that while he inquired about investing in gold and silver ETFs, he knew nothing about ETNs and the ETNs were recommended by Beyn. The Hearing Panel credited EK's testimony over Beyn's and we see no evidence in the record to overturn this credibility determination.

We find, therefore, that Beyn recommended investments to EK which were qualitatively unsuitable for him, in violation of NASD Rule 2310 and FINRA Rules 2111 and 2010.

B. Taddonio Failed to Exercise Reasonable Supervision in Light of Numerous Red Flags Indicating Excessive Trading and Churning

1. Facts

The record contains evidence concerning the trading in 37 accounts (belonging to 30 customers) which were traded by Beyn, ZB, DC, and MV, including all but one of the accounts which we have found Beyn excessively traded and churned.[27] A FINRA examiner testified that Beyn, ZB, DC, and MV were the top producing brokers at the firm and these accounts were the firm's most actively traded and most profitable.[28] During the periods these accounts were actively traded,[29] there were more than 9,000 trades in the accounts, the accounts had total net losses of almost $9.2 million, and CSC earned more than $4.7 million from the accounts.[30] The majority of the trades were marked solicited by the brokers. The annualized turnover rates for these accounts ranged from 6.6 to 212.25, with 13 accounts having annualized turnover rates

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[27] The evidence relating to Taddonio's failure to supervise excludes BM's account, which was opened and traded in 2015, after the time period during which Enforcement alleged Taddonio failed to exercise reasonable supervision—i.e., January 2012 to December 2014.

[28] For example, the record contains evidence that, in June 2013, Taddonio approved an award for ZB for "most money raised," for DC for most new accounts opened, and for Beyn for "biggest producer."

[29] Enforcement presented data for the accounts for the specific period during which each account was actively traded.

[30] The total costs charged to these customers, including margin interest, exceeded $5.9 million. Taddonio testified that he received a salary of $500,000 per year and capital distributions based on CSC's profitability.

over 100. The annualized cost-to-equity ratios ranged from 18.1% to 824.6%, with 25 of the accounts having annualized cost-to-equity ratios over 100%.

During the period from January 2012, to January 2013, RC served as CSC's CCO. RC testified that Taddonio reviewed the commissions (including mark-ups and mark-downs) and revenue generated by CSC's registered representatives on a daily, weekly, and monthly basis. RC also testified that Taddonio reviewed account activity and discussed accounts with registered representatives regularly. RC's testimony is corroborated by emails Taddonio sent indicating that he was aware of the registered representatives' trading and could access trading information on his desktop from anywhere.

While he was CCO, RC developed a document titled "active account worksheet" that he had registered representatives complete. The first active account worksheets were completed in May or June 2012 for approximately 30 actively-traded and poorly performing accounts, including accounts on which Beyn, ZB, DC, and MV were the brokers.

The active account worksheet required the brokers to provide information about realized and unrealized gains and losses and commissions and fees charged to the accounts. The worksheet also asked the registered representatives to estimate (on a percentage basis) the extent to which the customer relied on the broker for investment advice, the percentage of trades that were solicited or unsolicited, and to describe the investment strategy for the account. RC provided a list of these active accounts, along with the completed active account worksheets, to Taddonio, who signed the worksheets on behalf of "Sales Management." RC followed the same procedure for approximately 50-60 actively traded and poorly performing accounts in the fall of 2012.

In February 2013, CSC hired JG to replace RC as the CSC's CCO. JG remained CSC's CCO until September 2015, shortly before the firm closed.

After he became CCO, JG arranged for CSC's clearing firm to begin providing a monthly active account exception report. The report included accounts that met certain criteria, including: (1) monthly commissions (including mark-ups or mark-downs) totaling $2,500 or more; (2) 10 or more trades per month in the account; (3) commission-to-equity ratios of 5% or more; or (4) a loss in the account of 20% or more of its value. Accounts included in the report were organized by registered representative and showed: (1) the account value as of the end of the current month and previous month and the percentage of change; (2) the number of solicited and unsolicited trades for the month; (3) the total commissions and commission-to-equity ratio for the current month, the last three months, and the last 12 months; (4) the number of trades and commissions charged in each of the prior 12 months; and (5) the annualized turnover rate for the current month, the last three months, and the last 12 months.

JG and Taddonio received the active account exception reports from the clearing firm electronically. Additionally, JG forwarded a hard copy of the report, along with other exception reports, to Taddonio. JG testified that he explained the active account exception reports to Taddonio and expected Taddonio to review the report in his role as a sales manager. JG testified

that, after a few months, he noticed a pattern of the same accounts and same brokers appearing on the active account exception reports, including Beyn, ZB, DC, and MV.

The record includes copies of the monthly active account exception reports for each month from February 2013, to April 2014. Beyn and MV had multiple accounts appear on the report every single month. DC had multiple accounts on the report every month except August 2013.[31] ZB had multiple accounts appear on active account exception reports until he left CSC in August 2013.

With respect to Beyn's accounts, EH's account appeared on the report every month from February 2013, through August 2014. EH's LP Account also appeared on the report for 10 months. TP's accounts appeared on the report for nine months, and EK's account appeared four times—in one instance for three consecutive months. WR's and JB's accounts also appeared on the active account report.

WR's account appeared on the report for the month of July 2013. The report reflected a loss in WR's account during the month of July of 56%. The report also showed that Beyn had executed 58 trades in WR's account, 54 of which he marked solicited. The report showed an annualized turnover rate for the account of more than 226 and annualized cost-to-equity ratio of more than 46%. The record contains similarly large numbers for other accounts for which Beyn, ZB, DC, and MV were the brokers. This pattern continued to be reflected on the active account exception reports month after month.

JG also continued utilizing the active account worksheet process that RC had initiated. JG's worksheets called for basic information concerning losses, commissions (including mark-ups and mark-downs) charged, and the number of transactions, and also contained a section where the registered representative would provide a narrative explaining the performance of the account and the extent to which the customers were relying on the broker for investment strategies and advice. Often the brokers included comments that the customers were aware of the activity in their accounts and were satisfied. JG did not contact customers to confirm statements in these narratives indicating that the customers were aware of losses, commissions, and the trading in the accounts. JG testified that at least for some time, he provided copies of these active account worksheets to Taddonio.

Beginning in 2013, Taddonio was also aware of a number of customer complaints and arbitrations alleging excessive trading. The record contains evidence of at least six complaints from and arbitrations filed by customers during the period from July 2013, through December 2014. The complaints were filed by customers of Beyn, ZB, and DC, and the arbitrations named

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[31] For example, the April 2013 report listed 40 active accounts, of which approximately 27 were either managed exclusively by Beyn, DC, MV, or ZB, or for which commission credits were shared between one of them and another broker. The same pattern recurs in the other active account exception reports introduced by Enforcement.

CSC, Taddonio, or both as respondents. Many of the complaints included allegations of excessive trading and churning.

2. Discussion

NASD Rule 3010(a) provides that members "shall establish and maintain 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 securities laws and regulations." NASD Rule 3010(b) provides that members "shall establish, maintain, and enforce written procedures . . . to supervise the activities of registered representatives, registered principals, and other associated persons that are reasonably designed to achieve compliance with applicable securities laws and regulations." A member must implement and enforce its supervisory system and written procedures reasonably in light of the circumstances presented. *See Ronald Pellegrino*, Exchange Act Release No. 59125, 2008 SEC LEXIS 2843, at *33 (Dec. 19, 2008). The supervisory duties imposed under NASD Rule 3010 include a responsibility to investigate and act upon "'red flags' that suggest that misconduct may be occurring and to act upon the results of such investigation" with an appropriate response. *Id.*; *see also Christopher J. Benz*, 52 S.E.C 1280, 1283 n.13 (1997), *aff'd*, 168 F.3d 478 (3d Cir. 1998) (explaining that supervisors must respond to red flags and other indications of irregularities).

We find that Taddonio was made aware of numerous red flags that Beyn, ZB, DC, and MV were, or might be, excessively trading customers' accounts. Taddonio owned CSC and was its CEO. He was heavily focused on promoting sales activity and monitored production, commissions (including mark-ups and mark-downs), and the revenues CSC was generating. He had access to data regarding these facts daily from his laptop, and the record supports finding that he regularly monitored them. Taddonio met with CSC's registered representatives and reviewed accounts regularly.

While RC was CCO, he provided and reviewed with Taddonio the active account worksheets on at least two occasions—in May or June of 2012, and in the fall of 2012. If he was not already aware of it, the active account worksheets brought to Taddonio's attention the activity in accounts assigned to Beyn, ZB, DC, and MV that were being actively traded but performing poorly. The active account worksheets contained information about the losses in the accounts, the frequency of trading (including the percentage of solicited trades), and the mark-ups and mark-downs charged.

When JG took over as CCO, he arranged for CSC's clearing firm's monthly active account exceptions report to be provided directly to Taddonio. JG himself also provided Taddonio with a hard copy of this report. The active account exception report contained substantial information about the actively traded accounts, including the outrageously high turnover rates and cost-to-equity ratios in the accounts. Additionally, JG provided Taddonio with his own version of the active account worksheets implemented by RC, which were another source of information about trading. Even a cursory review of the active account exception reports shows the pattern of excessive trading by accounts of these four brokers. We conclude that Taddonio was either aware of this pattern of excessive trading or reckless in not becoming aware of it.

The active account worksheets and active account exceptions reports, along with the stream of complaints coming from customers, provided Taddonio with ample red flags that Beyn, ZB, DC, and MV were, or might be, excessively trading customer accounts.

Taddonio's primary arguments on appeal are that CSC took steps to address the red flags and, to the extent those steps were insufficient, he was not responsible because supervisory duties had been delegated to CSC's CCOs, RC and JG. Taddonio's arguments are without merit.

a. CSC's Supervisory Responses Were Insufficient

CSC's supervisory structure consisted of Taddonio, Porges, and CSC's CCOs, RC and JG. While RC was CCO, he had brokers complete active account worksheets, provided them to Taddonio, and suggested to certain brokers that they lower commissions on certain actively traded accounts. RC testified that he did not have the authority to force brokers to lower commissions and that his authority was limited to lowering the commission on a single trade if it exceeded the firm's 5% limit. RC testified that he gave Taddonio a list of accounts for which he thought commissions should be reduced, but Taddonio took no steps to do so.

When JG became CCO, he recommended, and Taddonio approved, the reduction of the firm-wide maximum commission from 5% to 3.2%. JG also recommended, and Taddonio approved, the further reduction of commissions for accounts that were being excessively traded. Other than reducing commission for certain specific accounts, however, no steps were taken to discipline or educate brokers, limit trading volume by brokers, alter sales practices, or correct past excessive trading.

JG also began a practice in which the firm sent selected customers a document entitled the "Active Account Letter." For a time, Taddonio signed the letters, and they were later signed by Porges. The letters were sent to customers with accounts that JG was concerned might be being excessively traded. The letters asked customers to confirm, by signing and returning a copy, the customer's financial profile and investment objective and "to confirm our understanding that the orders we have executed for you are in accordance with your objectives and risk capital limits; and that you are fully aware of the nature, frequency, risk factors, profits or losses associated with the transactions in your account."

In some cases, rather than sending an "Active Account Letter," CSC asked customers to execute a sworn document CSC called an "Affidavit of Support." Affidavits of Support were sent to customers at the request of the brokers, and Taddonio or Porges communicated to JG when a broker wanted to send one to a particular customer. The Affidavit of Support asked customers to swear that the customer "understood that there was a good chance that [the customer] would lose money in [his] account," that the broker "reviews the frequency of the

transactions with [the customer] including turnover ratio issues and cost-equity considerations," and that the customer did not "feel the trading in the account is excessive."[32]

We find that these supervisory responses were insufficient to address the red flags indicating excessive trading in CSC's accounts. The Active Account Letters and Affidavits of Support prepared by JG demonstrate that Taddonio was aware that excessive trading was, or might be, occurring in certain accounts, but those responses were directed at attempting to protect the firm from claims by the customers, rather than preventing violative conduct. There is no evidence that Taddonio undertook any investigation of particular accounts or brokers or counseled any broker about his activity. Significantly, the firm took no meaningful steps to restrict the trading by brokers for whom there were repeated red flags indicating that they were engaged in excessive trading and the excessive trading continued unabated. Supervisors did not regularly contact any customer to verify representations being made by salespersons regarding their investment sophistication or experience or the suitability of the investment strategies being employed by the brokers. The reliance of self-serving representations by brokers claiming that customers were satisfied despite heavy losses and high costs, was far from a sufficient response to the red flags indicating excessive trading.

b. Taddonio Is Responsible for a Failure to Supervise

Taddonio argues that he is not responsible for any supervisory failures because he delegated all supervisory responsibilities to CSC's CCOs. The record contradicts Taddonio's claims.

It is well established that "the president of a broker-dealer . . . is responsible for compliance with all of the requirements imposed on his firm unless and until he reasonably delegates particular functions to another person in that firm, and neither knows nor has reason to know that such person's performance is deficient." *Michael Ben Lavigne*, 51 S.E.C. 1068, 1071 (1994). Taddonio did not effectively delegate all supervisory responsibilities to the CCOs. Moreover, even if he had delegated these responsibilities, he was aware from the data provided by the CCOs that the excessive trading was not being controlled and that the compliance efforts were insufficient. Accordingly, he was responsible for intervening. *See John Busacca*, Exchange Act Release No. 3-13750, 2010 SEC LEXIS 3787, at *33-34 (Nov. 12, 2010), *aff'd*, 449 F. App'x 886 (11th Cir. 2011) (finding that firm president had obligation to act because he was aware of red flags of misconduct).

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[32] TP, EH, and EK signed affidavits of support. TP and JB signed active account letters. All the customers credibly testified that they trusted and relied on Beyn, and that they did not understand the costs of trading in their accounts. The customers testified that Beyn urged them to sign these documents. The letters and affidavits contained no information about the frequency or costs of trading in any of the accounts, and CSC permitted the brokers to contact customers concerning these documents when they were sent. Accordingly, we give limited weight to the customers' decision to sign these documents.

First, CSC's written supervisory procedures ("WSPs") did not say that supervisory responsibility for sales practices rested with the CCOs. Instead, the WSPs only said the responsibility rested with the "Designated Supervisor." Taddonio was listed as CSC's president, CEO, sales manager, and branch manager. The WSPs did not include an organizational chart or other explanation of the "Designated Supervisors" for particular functions.

Both RC and JG testified that Taddonio ran the firm and that they reported to him and Porges. RC testified that he had no responsibility for supervising brokers and he did not have the authority to hire, fire, or determine commissions and salaries (other than the modest reductions discussed above). He testified that Taddonio and Porges managed the sales force. JG similarly testified that he did not supervise brokers. JG testified that he had no authority to fire brokers or set commissions or salaries. RC testified that he was not to speak with clients – all client contact was handled by the brokers or by Taddonio. Like RC, JG testified that Taddonio and Porges supervised the brokers.

RC's and JG's testimony concerning their limited ability to supervise brokers, along with Taddonio's claims that all supervisory duties were delegated to RC and JG lays bare the true situation at CSC—there was essentially no supervision at CSC. Taddonio, while monitoring production and encouraging brokers to continuously generate revenue, disclaimed any responsibility for responding to red flags indicating that that revenue was being generated by excessive trading and churning in violation of FINRA rules and the securities laws. CSC's limited disciplinary efforts were ineffectual.

Even if Taddonio had delegated supervisory responsibility, however, (which we find he did not), he was aware of the plethora of red flags indicating that accounts were being excessively traded. Taddonio was also aware of the insufficient steps the CCOs had taken to address those red flags and, accordingly, had a duty to intervene to ensure that the red flags were investigated and appropriate steps were taken to address the unsuitable and excessive trading.

We find that Taddonio, the firm's president, CEO, and sales manager, acted as a supervisor for the sales force. Taddonio monitored sales activity, communicated with brokers on a daily basis, and actively encouraged them to open new accounts and trade to make money for the brokers and the firm. Taddonio knew of red flags indicating that certain brokers were excessively trading accounts, but he took no steps to investigate those red flags and respond to the possible excessive trading. To the contrary, he encouraged brokers to, in his words, "raise $$$$."[33] Accordingly, Taddonio failed to reasonably supervise the trading in customer accounts to ensure that they were not excessively traded, in violation of NASD Rule 3010(a) and (b) and FINRA Rule 2010.

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[33] For example, Taddonio created a lengthy sales pitch on Apple stock which said that a customer "could not wait another minute before putting money into Apple before it is too late." Taddonio instructed brokers on creating a sense of urgency and offered strategies to overcome a customer's reluctance to invest.

C. Taddonio Gave False Testimony to FINRA

1. Facts

During a February 13, 2015 on-the-record interview ("OTR"), ZB testified that CSC routinely recorded telephone calls to customers. ZB reiterated this testimony in a second OTR on February 26, 2015. In a March 18, 2015 OTR, Porges denied that the firm recorded calls. On March 20, 2015, Taddonio appeared for an OTR pursuant to FINRA Rule 8210. During his OTR, Taddonio was asked whether CSC or anyone associated with CSC had recorded conversations or calls, including with customers. Taddonio denied that any such recordings were made and testified that "I don't know of any recordings, anything."

On March 26, 2015, FINRA conducted an unscheduled visit to CSC's offices. During this visit, FINRA copied 10 hard drives on nine firm computers, including Taddonio's, Porges's, Beyn's, ZB's, CD's, and other brokers' computers. Enforcement did not find recorded telephone calls on any of the copied hard drives.

Enforcement, however, established by a preponderance of the evidence that there were such recordings at CSC at some time. First, in the OTR that was taken prior to Taddonio's OTR, ZB testified that calls with customers were recorded.[34] DC also testified, in a FINRA arbitration hearing, that some of his calls with CSC customers were recorded. Another CSC broker, NM, testified that the firm recorded calls for training purposes, and he also testified that he discussed one such call with Taddonio.

Enforcement also introduced several invoices showing purchases of recording equipment by CSC in 2014, including an invoice attached to an email sent to Taddonio. Photographs taken in CSC's office showed recording equipment in plain sight on brokers' desks. Enforcement introduced evidence that Taddonio's work computer contained audio files created on a USB recorder which were created while CSC was in business and some of which referred to customers. The record also contains an email between NM and Taddonio referring to their discussion about a recorded call with a customer and another email from Taddonio to Porges with a recorded call attached. The recorded call was with a customer who had filed a complaint. NM testified that he discussed this call with Taddonio.

2. Discussion

Providing false testimony to FINRA in an OTR is a violation of FINRA Rules 8210 and 2010. *See Montelbano*, 56 S.E.C. at 98 (finding that respondents violated Rule 8210 by giving false testimony during an OTR); *Dep't of Enforcement v. Hedge Fund Capital Partners, LLC*, Complaint No. 2006004122402, 2012 FINRA Discip. LEXIS 42, at *64-68 (FINRA NAC May

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[34] The Hearing Panel gave no weight to ZB's testimony because he did not appear before the panel and for other reasons pertaining to his conduct and his dismissal from the firm. On this issue, however, ZB's testimony was corroborated by other evidence and thus has some value.

1, 2012) (finding that respondents violated NASD Rules 8210 and 2110 by providing false and misleading information and testimony to FINRA).

We agree with the Hearing Panel that the record supports that at least some calls with CSC customers were recorded. We also find that a preponderance of the evidence establishes that Taddonio was aware that brokers were recording calls. The Hearing Panel found Taddonio's testimony that he did not know about recordings or recording equipment not credible and the record supports this finding. The Hearing Panel also found credible NM's testimony that he discussed a recorded call with Taddonio credible. The other documentary evidence, including photographs showing recording devices in plain sight, demonstrates that Taddonio knew calls were being recorded and, accordingly, testified falsely at his OTR, in violation of FINRA Rules 8210 and 2010.

IV. Sanctions

In determining the appropriate sanctions for respondents' misconduct, we considered FINRA's Sanction Guidelines ("Guidelines"), including the Principal Considerations in Determining Sanctions.[35] After a careful review of the record, and applying the Guidelines, we affirm the bar in any capacity imposed on Beyn for quantitatively and qualitatively unsuitable trading and churning, and the bar in any capacity imposed on Taddonio for giving false testimony to FIRNA. With respect to Taddonio's supervisory violation, we find the principal and supervisory bar imposed by the Hearing Panel inadequate given the egregious nature of Taddonio's violations, and his continued inability or unwillingness to recognize the seriousness of his misconduct or appreciate his regulatory responsibilities under industry rules. Accordingly, we modify the sanction the Hearing Panel imposed for Taddonio's supervisory violations, and we impose a bar in all capacities.

A. Beyn Is Barred in All Capacities for His Excessive Trading and Churning of Customer Accounts and His Unsuitable Recommendations

The Guidelines for excessive trading and churning recommend monetary sanctions of $5,000 to $110,000.[36] The Guidelines also instruct us to consider a suspension in any or all capacities for one month to two years, or where aggravating factors predominate, a longer suspension of up to two years or a bar.[37] The Guidelines further provide that we should "[s]trongly consider barring an individual for reckless or intentional misconduct (*e.g.*, churning)."[38]

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35 *See FINRA Sanction Guidelines* (2017), http://www.finra.org/sites/default/files/2017_Sanction_Guidelines.pdf [hereinafter *Guidelines*].

36 *Guidelines*, at 79.

37 *Id.*

38 *Id.*

For making unsuitable recommendations, the Guidelines recommend a fine of $2,500 to $110,000, and a suspension in any or all capacities for a period of 10 business days to two years.[39] Where aggravating factors predominate, the Guidelines urge us to "strongly consider a bar for an individual respondent."[40]

We agree with the Hearing Panel that it is appropriate to impose a unitary sanction on Beyn because his violations arose out of the same trading. The Hearing Panel imposed a bar in all capacities. We agree that this is an appropriately remedial sanction for Beyn's misconduct.

There are numerous aggravating factors, and no mitigating factors, that support this sanction. Beyn's excessive trading and churning of customer accounts involved a pattern of numerous, intentional acts of misconduct over an extended period of time.[41] Beyn induced his customers to repose complete trust in him to advance their interests. Beyn's misconduct, however, caused the accounts of his customers to be replete with transactions that were high in cost, highly risky, and had little prospect to be profitable, thereby causing injury to his customers, who suffered substantial losses, and resulting in substantial financial gains to Beyn.[42] Beyn has taken no responsibility for his misconduct, has shown no remorse, and still argues that his customers approved the trading in the accounts despite their ignorance of the actual costs of their trading, the outrageous turnover rates, and cost-to-equity ratios which virtually assured that Beyn and CSC would benefit from the trading, but the customers would not.[43] Beyn has taken no steps to provide any restitution to customers.[44]

Under these circumstances, the Guidelines and investor protection considerations support the imposing a bar in all capacities. Beyn has shown that he is a danger to investors, cannot comply with rules and regulations intended to protect investors, and has no place in the securities industry.

B. Taddonio Is Barred in All Capacities for His Supervisory Violations

The Guidelines for failure to supervise recommend suspending a responsible individual in any or all capacities for up two years or barring the responsible individual in egregious

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39 *Id.* at 96.

40 *Id.*

41 *See id.* at 7-8 (Principal Considerations in Determining Sanctions, Nos. 8, 9, 13).

42 *See id.* at 7-8 (Principal Considerations in Determining Sanctions, Nos. 11, 16).

43 *See id.* at 7 (Principal Considerations in Determining Sanctions, No. 2).

44 *See id.* at 7 (Principal Considerations in Determining Sanctions, No. 4).

cases.[45] The principal considerations specific to failure to supervise include whether the responsible individual ignored red flags, the nature and extent of the underlying misconduct, and the quality and degree of the supervisor's implementation of procedures and controls.[46] All of these factors are aggravating here and support imposing a bar. Taddonio was aware of numerous red flags indicating excessive trading by CSC brokers, yet with the exception of taking the CCO's advice to reduce commissions in specific cases, he took no steps to prevent violative trading. To the contrary, CSC's business model encouraged this trading. The potential excessive trading affected at least 30 CSC customers.

Several of the principal considerations that apply to all violations also apply to Taddonio and are aggravating. Taddonio has taken no responsibility for the misconduct and took no corrective action, including by offering customers restitution.[47] Taddonio failed to ensure that procedures and controls were put into place to prevent excessive trading by brokers.[48] Taddonio's failure to supervise was a pattern of conduct over an extended period of time that involved numerous acts.[49] Finally, Taddonio's failure to supervise resulted in significant injuries to customers and substantial gains to CSC and Taddonio as the majority owner of the firm.[50]

For his supervisory violations, the Hearing Panel imposed a bar in all principal and supervisory capacities on Taddonio. We find this sanction insufficient given Taddonio's egregious supervisory violations and modify the sanction to impose a bar in all capacities. *See, e.g.*, *William J. Murphy*, Exchange Act Release No. 69923, 2013 SEC LEXIS 1933, at *112 & n.155 (July 2, 2013) (sustaining an all-capacities bar imposed for egregious supervisory violations and noting that "[b]ecause proper supervision serves such an important role in protecting investors, egregious violations of supervisory rules often warrant the most severe sanctions"); *Studer*, 57 S.E.C. at 1026 (affirming a bar in all capacities for failure to supervise.

The record demonstrates that Taddonio played a key role in creating a culture at the firm that allowed, and even encouraged, excessive trading by brokers. Taddonio's communications with brokers emphasized generating revenue, and he gave monthly awards to brokers for accomplishments such as opening more accounts and generating the most revenue. This focus, combined with Taddonio's complete failure to respond to numerous red flags that brokers were excessively trading customer accounts to generate that revenue, demonstrates that Taddonio is

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45 *Id.* at 105.

46 *Id.*

47 *See id.* at 7 (Principal Considerations in Determining Sanctions, Nos. 2, 3, 4).

48 *See id.* at 7 (Principal Considerations in Determining Sanctions, No. 5).

49 *See id.* at 7 (Principal Considerations in Determining Sanctions, Nos. 8, 9).

50 *See id.* at 7-8 (Principal Considerations in Determining Sanctions, Nos. 11, 16).

unable to comply with the standards of conduct expected of securities industry professionals. We find that Taddonio presents a danger to the investing public and that a bar in all capacities is the appropriately remedial sanction for his violations.

C. Taddonio Is Barred in All Capacities for Giving False Testimony to FINRA

The Guidelines for failing to respond truthfully to a FINRA Rule 8210 request recommend a bar.[51] The specific principal consideration is the importance of the requested information from FINRA's perspective.[52] In this case, FINRA was investigating possible excessive trading and churning of customer accounts and the existence and content of taped conversations was important to determining whether these violations had occurred. Taddonio's false testimony obstructed FINRA's investigation.

Providing false information to FINRA is a serious violation, which is routinely sanctioned with the imposition of a bar in all capacities. *See, e.g.*, *Geoffrey Ortiz*, Exchange Act Release No. 58416, 2008 SEC LEXIS 2401, at *32 (Aug. 22, 2008) (stating that "failure to provide truthful responses to requests for information renders the violator presumptively unfit for employment in the securities industry"); *Dep't of Enforcement v. David Harari*, Complaint No. 2011025899601, 2015 FINRA Discip. LEXIS 2, at *34 (FINRA NAC Mar. 9, 2015) (imposing bars in all capacities for providing false documents and information to FINRA).

The record contains substantial evidence that conversations were taped at CSC. Taddonio's testimony to the contrary at his OTR was false and, for this misconduct, we impose a bar in all capacities.

V. Conclusion

Beyn excessively traded customer accounts, in violation of NASD Rule 2310 and FINRA Rules 2111 and 2010, and churned customer accounts, in violation of Exchange Act Section 10(b), Exchange Act Rule 10b-5, and FINRA Rules 2020 and 2010. Beyn also made an unsuitable investment recommendation to a customer, in violation of NASD Rule 2310 and FINRA Rules 2111 and 2010. For these violations, Beyn is barred from associating with any FINRA member firm in any capacity.

Taddonio failed to exercise reasonable supervision in light of red flags indicating that registered representatives at his firm were, or might be, excessively trading customer accounts, in violation of NASD Rule 3010 (a) and (b) and FINRA Rule 2010. For these violations, Taddonio is barred from associating with any FINRA member firm in any capacity. Taddonio also gave false testimony to FINRA, in violation of FINRA Rules 8210 and 2010. For these violations, Taddonio is barred from associating with any FINRA member firm in any capacity.

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51 *Id.*, at 33.

52 *Id.*

The bars imposed on Beyn and Taddonio are effectively immediately upon the service of this decision.

On behalf of the National Adjudicatory Council,

Jennifer Piorko Mitchell,
Vice President and Deputy Corporate Secretary