FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. CANTONE RESEARCH INC. (CRD No. 26314), ANTHONY J. CANTONE (CRD No. 1066139), and RAYMOND J. DEROBBIO (CRD No. 1092310), Respondents.	Disciplinary Proceeding No. 2017055886402 Hearing Officer–LOM **EXTENDED HEARING PANEL DECISION** January 25, 2024

Respondents sold municipal bonds without a reasonable basis to believe them suitable for any investor because they conducted inadequate due diligence, in willful violation of MSRB Rule G-19. In selling the bonds, Respondents used negligent misrepresentations and omissions of material fact, in willful violation of MSRB Rule G-17 and Securities Act Sections 17(a)(2) and 17(a)(3). They also failed to disclose at or prior to the time of trade all material information about the transaction, in willful violation of MSRB Rule G-17. For these violations in the aggregate, Respondent Cantone Research Inc. is expelled from FINRA membership, and Respondents Anthony J. Cantone and Raymond J. DeRobbio are barred from associating with any FINRA member in any capacity.

Respondents sold other municipal bonds by means of fraudulent misrepresentations and omissions of material fact, in willful violation of MSRB Rule G-17 and Securities Act Section 17(a)(1), and without disclosing at or prior to the time of trade all material information about the transaction, in willful violation of MSRB Rule G-17 and MSRB Rule G-47. For these violations in the aggregate, Respondent Cantone Research is separately expelled from FINRA membership, and Respondents Cantone and DeRobbio are separately barred from associating with any FINRA member in any capacity.

Respondents are also ordered to pay their customers restitution. Each individual respondent is jointly and severally responsible with the Firm for restitution to that individual respondent's customers. The Firm is responsible for restitution to all customers who bought the bonds from any representative of the Firm.

Appearances

For the Complainant: Brody W. Weichbrodt, Esq., Mark Fernandez, Esq., Noel Downey, Esq., and Kevin Hartzell, Esq., Department of Enforcement, Financial Industry Regulatory Authority

For Respondent Raymond J. DeRobbio: Raymond J. DeRobbio, *pro se*

For Respondent Anthony J. Cantone: No appearance

For Respondent Cantone Research Inc.: No appearance

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DECISION

I. Introduction

A. Nature of the Case

This case is about two separate failed municipal bond offerings. The first offering (referred to here as the "Quad Cities" bond offering) was in 2013 for the purpose of refinancing and rehabilitating a run-down community college dormitory in rural Illinois. The dormitory was intended to serve students at Sauk Valley Community College (the "College"). The second offering (referred to here as the "Montgomery 2015" bond offering) was in 2015 for the purpose of acquiring, rehabilitating, and operating a defunct assisted-living facility in Montgomery, Alabama.

Respondent Cantone Research Inc. ("Cantone Research" or the "Firm") was the sole underwriter for both offerings. In total, it sold $2.2 million in the Quad Cities offering and a little over $6 million in the Montgomery 2015 offering. Respondents Anthony J. Cantone, the Firm's owner and chief executive officer ("CEO"), and Raymond J. DeRobbio, a registered representative and municipal bond specialist with the Firm, worked on the offerings and offering documents and were among the Firm's representatives who sold the bonds to retail customers, both in the offerings and in the secondary market.

Although a governmental body issued the bonds in each offering, the issuer was simply a conduit for the funds raised from sales of the bonds. Each governmental issuer transferred the sales proceeds to a private entity to fund the specified project. In each offering, the private entity was the borrower and sole obligor responsible for generating the revenues necessary to pay the bondholders from the specified project. The governmental entity had no responsibility to pay the bondholders.

Because investors in each project depended upon the success of the specified project for payment of their principal and interest, well-grounded financial projections were important to investors. The background of the persons and entities responsible for managing the project and repaying investors was also important as evidence of competence, trustworthiness, and likelihood of success. As discussed below, in connection with each project Respondents made misrepresentations and misleading omissions of material fact about the financial prospects of the project and the persons responsible for the project's future success. We find that they did so at least negligently in connection with the first offering (Quad Cities) and they did so fraudulently in connection with the second offering (Montgomery 2015).

Each project failed shortly after the offering closed. Neither project generated the funds necessary to pay the bondholders what they were owed. Many of the people who bought the bonds were elderly with limited resources. Although they could ill afford it, the investors lost significant life savings in the bond transactions.

Although FINRA's Department of Enforcement charged violations in connection with just these two offerings, it is necessary to understand the prior financial history of the properties to fully comprehend the nature and extent of Respondents' misconduct. Both properties were the subject of earlier failed securities offerings. In addition, Respondents chose not to disclose information about a borrower's criminal background to investors in a separate, unrelated offering. Then, when the same borrower sought investor funds in the Montgomery 2015 offering, Respondents again concealed his criminal background. The evidence revealed a pattern of misconduct in various related and unrelated earlier offerings that is relevant for purposes of sanctions.

B. The Proceeding

1. Events Prior to the Hearing

The Department of Enforcement filed the Complaint in this matter on October 26, 2021. After multiple continuances, the hearing was scheduled to begin on June 20, 2023, a date suggested by Respondents. The history of delay is summarized in a June 16, 2023 Order.

About three weeks before the hearing was scheduled to begin, counsel for DeRobbio filed a motion to withdraw from the representation and counsel for Cantone and the Firm did the same. The parties, however, did not seek another continuance of the hearing. DeRobbio said he would represent himself, and Cantone said he would represent himself and the Firm.

Following the withdrawal of counsel, Cantone asserted by email to the Office of Hearing Officers on June 8 and 9, 2023, that he was not able to participate in any pre-hearing conferences or the hearing because of an ongoing medical condition. The Hearing Officer had previously considered that condition and suggested accommodations to enable Cantone to participate in the hearing. In the June 8 and 9 emails, Cantone presented no evidence to support his claim that his current condition rendered him unable to participate regardless of any accommodations. Instead, he referred to earlier submissions that had already been found an insufficient basis for delay. The June 8 and 9 emails are attached to the June 16, 2023 Order.

On June 13, 2023, Cantone's wife, Christine Cantone, previously named the Firm's corporate representative for purposes of attending the hearing, declined by email to participate in the final pre-hearing conference. She proffered no explanation or excuse. Her email also is attached to the June 16, 2023 Order.

The Respondents' refusal to attend the pre-hearing conference or appear at the hearing was not justified. As recited in the June 16 Order, Cantone admitted that he regularly went to his office four days per week, but he claimed that his activities were very limited. Enforcement presented evidence regarding the extent of Cantone's work activities. That evidence indicated that Cantone was working much longer hours than he claimed, and that he had been entering trades and actively selling securities to customers. As for the Firm, it is a separate party from Cantone. Whatever Cantone's current condition, the Firm has its own obligations in this proceeding.

In this context, the June 16 Order informed the parties that the hearing would go forward as scheduled. It ordered all parties to appear at the hearing.

2. The Hearing

Beginning on June 20, 2023, a seven-day hearing was held in Woodbridge, New Jersey, before a three-person Extended Hearing Panel. Despite being notified that the hearing was going forward and being ordered to appear, neither Anthony Cantone nor the Firm appeared at the hearing.

Enforcement presented the testimony of Ryan Moy, a principal analyst in FINRA's Risk Monitoring program, who worked on the investigation from which this proceeding arose. It also presented testimony from five customers of the Firm and from James Swan, who worked during the relevant period for another municipal bond underwriter, Stifel Nicolaus LLC ("Stifel"). Stifel was the initial underwriter on the Quad Cities offering but, after conducting months of due diligence, it withdrew from that role. Respondents became involved in the Quad Cities offering after Stifel's withdrawal.

Respondent DeRobbio testified both in Enforcement's case and separately in his own defense. Sometimes his testimony differed from other sworn testimony he had previously given in FINRA on-the-record interviews ("OTRs") and before the Securities and Exchange Commission ("SEC"). Some excerpts from that prior testimony were read into the record and he was asked about discrepancies. The excerpts read into the record were treated as substantive testimony for purposes of the hearing.

Because Respondent Cantone refused to make himself available at the hearing for live testimony, excerpts of his previous sworn testimony in OTRs and before the SEC were read into the record. The testimony read into the record was treated as substantive testimony for purposes of the hearing.

In February 2023, before defense counsel withdrew, Enforcement and Respondents entered stipulations, filed pre-hearing briefs, and exchanged proposed exhibits. At the hearing, various exhibits that had been previously exchanged by the parties were admitted into evidence.[1]

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[1] We refer to the hearing testimony with the abbreviation for transcript "Tr." followed by the witness's last name in parentheses and then the identifying pages. For example, DeRobbio's testimony is cited "Tr. (DeRobbio) __." The five customers who testified by telephone and videoconference, however, are individually identified by their initials. So, for example, the testimony of a customer of Respondent Anthony Cantone's is cited "Tr. (KE) __." Other customers who did not testify but who were mentioned in the record are also referred to by their initials. Appendix A, which is distributed only to the parties, identifies the customers by name. To avoid a sea of initials and make this decision more readable, we identify certain other persons by first name and last initial, and sometimes also by their role. For example, the attorney who represented the developer in the Quad Cities offering and who represented the Firm as underwriter's counsel in the Montgomery 2015 offering is referred to as Attorney Brian M. A key figure in the Quad Cities offering was Steve S. These other persons are also identified in full in Appendix A.

C. The Extended Hearing Panel's Findings and Conclusions

Based on careful consideration of the entire record, we conclude that Enforcement proved the charges outlined in the Complaint. In summarizing our conclusions, we discuss specific misconduct under the separate causes of action to avoid an unending litany of misconduct that may be hard to keep in mind if it is not structured in some way. In fact, the misconduct all violates the fundamental requirement in the Municipal Securities Rulemaking Board's ("MSRB's") Rule G-17 that a municipal securities underwriter deal fairly in its business with all persons, including customers.[2]

1. Quad Cities Violations

The Quad Cities violations are negligence-based.

a. Cause I

Cause I charges Respondents with willfully violating MSRB Rule G-19. That rule is a suitability and due diligence rule. It requires that a municipal securities dealer have reasonable grounds for believing a recommended security suitable—at least for some investors and then, in addition, for the specific customer to whom it is recommended. Only through appropriate due

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We use the full names of persons registered through the Firm or through another FINRA member firm. We also use the full names of two persons important to the Montgomery 2015 offering, Christopher Brogdon and Dwayne Edwards. Brogdon was the seller in the Montgomery 2015 offering and Edwards was the buyer/conduit borrower responsible for paying investors their principal and interest. Subsequent to the Montgomery 2015 bond offering, Brogdon was found guilty of securities fraud in an SEC enforcement action relating to various bond offerings and private placements, including some that were underwritten by Respondents; and Edwards entered a consent judgment in an SEC enforcement action without admitting or denying charges of securities fraud. *See infra* at 71 n.434, 83 n.517.

We refer to Stipulations by the abbreviation "Stip." and the paragraph number cited. For example, Stip. ¶ 4 provides professional background information for Respondent Anthony Cantone.

We refer to Exhibits by a prefix (CX for Complainant's exhibits, RX for Respondents' exhibits, and JX for joint exhibits), a unique document number, and page number. For example, the Official Statement for the Quad Cities offering is cited as "JX-3, at __."

For purposes of restitution, two other appendices accompany this decision. Appendix B contains a list of customers who invested in the Quad Cities bonds and the amount by which each was injured by Respondents' misconduct. Appendix C contains the same information for investors in the Montgomery 2015 bonds. Each Appendix is organized to show the restitution owed by the Firm to each customer and the amounts for which Cantone and DeRobbio are each jointly and severally liable with the Firm for restitution to their own customers. The public versions of these appendices use the customers' initials. The versions distributed only to the parties identify the customers by full name.

Enforcement filed a pre-hearing brief, as did the three Respondents collectively through their counsel. Those briefs are referenced here as "Enf. Br." and "Resp. Br." There were no post-hearing briefs.

[2] The MSRB regulates municipal securities brokers and dealers and promulgates rules. FINRA has responsibility for enforcing MSRB rules. *See infra* at 97 & n.652.

diligence can a dealer develop reasonable grounds for believing a security suitable.[3] In the circumstances of this case, Respondents failed to perform the due diligence necessary to develop a reasonable basis for believing the Quad Cities bonds a suitable investment for any investor. This misconduct was a willful violation of MSRB Rule G-19.

- Respondents knew that Swan's underwriting firm, Stifel, had withdrawn from the underwriting, even though it had conducted months of due diligence, created a bond model, and worked on a draft of a Preliminary Official Statement ("POS"). Respondents also knew prior to the closing of the offering that Stifel would not be identified in the offering documents as having worked on the transaction and would not receive any compensation for its work, a highly unusual event. Respondents did not, however, probe the reason Stifel withdrew or treat Stifel's decision to withdraw as a red flag requiring special attention to due diligence on the offering. Instead, they treated that firm's abandoned work as sufficient basis for going forward with the offering on an accelerated basis without conducting any meaningful due diligence of their own. In fact, Stifel withdrew because it could not obtain reliable information about historical and current occupancy rates from the entity managing the dormitory, Best Management Onward Campus, Inc. ("BMOC" or the "Manager"), and Stifel did not feel comfortable with the financial projections.

- Respondents knew that municipal bonds had been previously issued in 2004 to fund construction of the dormitory and that the borrower in that earlier offering had filed for bankruptcy in 2011. The bankruptcy filings showed that the bankrupt borrower was the same entity that was the borrower on the 2013 Quad Cities bonds and the Manager of the dormitory when it went bankrupt, BMOC, was the same entity that was to manage the dormitory after the 2013 offering. The bankruptcy filing also showed that dormitory revenues had steadily declined over the three years preceding bankruptcy and that the dormitory property was abandoned by the bankruptcy trustee, who concluded that it held no value to the bankruptcy estate. But Respondents did not look at the bankruptcy filings available in public court records to analyze what happened with the earlier offering and whether the new financing would have a better chance of success. Nor did they treat the previous bankruptcy as a red flag signaling potential problems with the dormitory and the need to closely scrutinize the financial projections BMOC provided for the 2013 offering.

- Respondents knew that the dormitory needed mold remediation and that some rooms and beds were "uninhabitable"—not just in need of renovation, but "uninhabitable." Even so, Respondents never determined with any certainty how many units were "uninhabitable" and how many beds were available to support

[3] *See infra* at 99–100 & nn.665–69.

the payments due to investors. They made no on-site visit, even though the Firm's Written Supervisory Procedures ("WSPs") required one, and they did not demand unambiguous figures for habitable beds and historical and current occupancy rates. Respondents had no way of evaluating the reasonableness of BMOC's optimistic occupancy figures in the financial projections. They simply accepted the projections.

b. Cause II

Cause II charges a willful violation of MSRB Rule G-17, which requires fair dealing in the municipal securities business, along with Sections 17(a)(2) and 17(a)(3) of the federal Securities Act of 1933, which prohibit various types of unfair business conduct in the broader securities industry. MSRB Rule G-17 requires municipal securities professionals to deal fairly in their securities business with all persons and not to engage in any deceptive, dishonest, or unfair practice. This rule is understood to impose a broad duty of fair dealing that encompasses the more specific instances of misconduct specified in other MSRB rules. Scienter is not required to prove a violation of MSRB Rule G-17 or Sections 17(a)(2) and 17(a)(3).[4] We find that Respondents willfully violated their duty of fair dealing under MSRB Rule G-17 and Sections 17(a)(2) and 17(a)(3) in a host of ways, including the following:

- In the final financial projections for the dormitory project, Respondents overstated the revenues the dormitory could generate. Projected revenues were based on an occupancy rate that the dormitory historically had never achieved and was unlikely to achieve in the future, given the dormitory's uninhabitable rooms, mold problem, and other issues such as the dormitory's very poor relationship with the College upon which it depended for student renters. In overstating the revenues that the dormitory could generate, Respondents misrepresented the dormitory's financial prospects, which was deceptive and unfair to investors.

- Respondents also understated the management fees to be charged, which had the effect of lowering expenses and making it appear that the project was more profitable and less risky than it was. The BMOC contract called for a significantly higher management fee than the management fee in the disclosure documents provided to investors. In understating expenses, Respondents made another misrepresentation of the dormitory's financial prospects, which was deceptive and unfair to investors.

- In addition, Respondents misleadingly suggested that new management would operate the dormitory and be able to generate the revenues needed to pay bondholders. As noted above, the company that was to manage the dormitory after the Quad Cities offering was the same company that had previously managed the dormitory before it filed for bankruptcy, BMOC. BMOC was

[4] *See infra* at 98–99 & nn.658–64, 102 & nn.685–689.

responsible for the dormitory as it fell into disrepair and performed so poorly that the earlier bond offering failed. Respondents' misrepresentation of the company as new management was deceptive and unfair to investors.

c. Cause V

Cause V separately alleges that Respondents willfully violated MSRB Rule G-17, the fair dealing rule, by failing to disclose to their customers, at or prior to the time of trade, all material information about the transaction. We find that Enforcement proved that charge.

- The Official Statement ("OS") for the Quad Cities offering and the final financial projections presented with it were misleading. They omitted material information relating to a critical tool for evaluating the riskiness of the investment. That analytical tool, the debt service coverage ratio, is a measure of the amount by which projected net operating income exceeds the payments due to be paid to the bondholders. It indicates whether and how much financial cushion exists to enable a project to absorb unexpected negative events (such as an increase in the vacancy rate for the dormitory) and still be able to pay bondholders the principal and interest owed them.

  Stifel withdrew from the underwriting in part because the debt service coverage ratio that it calculated—and shared with Respondents—seemed too low to Swan, the lead investment banker at Stifel who worked on the transaction. He thought the risk unsuitable for retail investors.

  The OS provided a number for the debt service coverage ratio for the first few years of the project and referred the customer to an appendix to understand the financial requirements and assumptions on which the ratio was based. But the debt service coverage ratio was omitted entirely from the financial projections in the appendix given to investors, making it difficult to impossible to understand how the ratio was derived and how it related to the revenue and expense figures in the financial projections. Furthermore, in the final version of the financial projections given to investors, BMOC's name was removed as the source of the projections. This incorrectly left the impression that an independent entity was the source.

  Respondents made the disclosures opaque and misleading. They failed to disclose information necessary for customers to understand and evaluate the debt service coverage ratio and the riskiness of the investment. The misleading disclosures and omitted information were deceptive and unfair to investors.

- Respondents knew that the dormitory depended on the College for its pool of students to lease beds in the dorm and generate revenue. In the offering materials, Respondents emphasized that it was critical to the success of the project for the

College to join in the dormitory's marketing efforts. Respondents also knew that the dormitory depended on the College to provide water and sewer services. Respondents accepted at face value BMOC's description of the relationship between the dormitory and the College as a good one, with no problems. Prior to closing the offering, Respondents never contacted the College to understand its view of the relationship. In fact, the relationship was extremely poor, due in part to the dormitory's failure to pay the College for the water and sewer services that the College had previously provided the dormitory. If Respondents had examined the borrower's 2011 bankruptcy filing in connection with the first offering in 2004, they would have seen that, aside from a mortgage loan, the College was the borrower's largest bankruptcy creditor. The dormitory owed the College more than $62,000 on its water and sewer bills for 2006–2011. Respondents failed to conduct adequate due diligence and failed to disclose material information about the relationship between the College and the dormitory to investors. The resulting disclosures were deceptive and unfair to investors.

Respondents' defense. Respondents assert that they reasonably relied on Stifel and the parties interested in the transaction, along with the professionals they had retained. Respondents further assert that they were deceived by others involved in the transaction. These assertions are not a valid defense. Under MSRB rules, it was Respondents' responsibility to develop a reasonable basis for recommending the Quad Cities bonds to their customers and to deal fairly with their customers by accurately disclosing the material facts. Respondents' responsibility for complying with MSRB rules and the securities laws cannot be shifted to anyone else. And, if Respondents were deceived by others, it is only because they did not perform the due diligence necessary in the circumstances. Indeed, the circumstances made it unreasonable for Respondents to rely on Stifel. Stifel withdrew from the offering without compensation and sought not to be identified as connected to the offering. It was unwilling to recommend the bonds to its customers, which hardly created a basis on which Respondents could recommend the bonds to Cantone Research customers.

Respondents also assert that their misconduct in connection with the Quad Cities offering was not willful. They are incorrect. They chose to rely on the parties to the transaction without conducting meaningful due diligence, and they chose to present materially false and misleading information to their customers and to omit other material facts. Their misconduct was not inadvertent or accidental. It falls within the meaning of willful under the securities laws.

2. Montgomery 2015 Violations

The Montgomery 2015 violations are fraud-based.

a. Cause III

Cause III charges Respondents with selling the Montgomery 2015 bonds by means of fraudulent misrepresentations and omissions of material fact in willful violation of MSRB Rule

G-17, the fair dealing rule discussed above, and Section 17(a)(1) of the Securities Act, which prohibits any device or artifice to defraud. Fraud requires scienter; negligence is insufficient. Scienter includes knowing misrepresentations and omissions of material fact and reckless disregard for the truth.[5] We specifically find that Respondents knowingly misrepresented and omitted material facts in selling the Montgomery 2015 bonds, or, at a minimum, acted in reckless disregard for the truth.

- Respondents fraudulently and deceptively presented false information about the past financial performance of the assisted-living facility. They represented that at the time the facility closed in the summer of 2013 it was generating *monthly net income* of approximately $20,000. That was untrue. At the end of 2011 the facility had an *annual net income* of a little over $20,000. The facility had an *annual net loss* in 2012 of $115,226.50, and, by the time the facility closed in June 2013, it had a *year-to-date net loss* of $95, 931.85. Respondents either knew or were reckless if they did not know that the description of the facility's profitability was false and that it would encourage investors to believe—incorrectly—that the bonds were a sound investment. The misrepresentation of the facility's financial history was deceptive and unfair to investors.

- Respondents fraudulently and deceptively failed to disclose to customers that the person to whom investors were lending money to acquire, rehabilitate, and operate the defunct assisted-living facility, a man named Dwayne Edwards, had pled guilty to a criminal charge of misusing patients' money in connection with his nursing home business in South Carolina, lost his license to run such a facility in that state for about eight years, and been barred from the Medicare and Medicaid programs for 15 years. Although Respondents knew Edwards' troubling history, they falsely touted him as having successfully run such facilities for 35 years. Respondents' failure to disclose material facts about the borrower's criminal history and lengthy exclusion from the Medicare and Medicaid programs and their affirmative misrepresentation of the borrower's extensive successful experience were deceptive and unfair to investors.

- Respondents fraudulently and deceptively failed to disclose that the Alabama assisted-living facility had been the subject of two earlier securities offerings underwritten by the Respondent Firm that had failed to meet their payment obligations to earlier investors. Respondents Cantone and DeRobbio both were involved in the first offering (referred to here as "Montgomery 2004," a municipal bond offering), and Cantone was involved in the second (referred to here as "Montgomery 2011," a private placement offering of certificates of participation).

[5] *See infra* at 101–02 & nn.675–684.

The failure to disclose the two prior failed offerings was deceptive and unfair to investors.

- Respondents fraudulently and deceptively misled investors when they described the intended uses of the proceeds of the Montgomery 2015 offering. They failed to disclose that some of the proceeds were to be paid to investors in the two earlier failed offerings. This was contrary to representations in the OS for the Montgomery 2015 offering that all such projects were independent of each other (and also contrary to representations in the OS for Montgomery 2004). Concealing that some of the proceeds were going to be used to pay investors in the two earlier offerings enabled Respondents to sell the Montgomery 2015 bonds based on other false and misleading statements, such as that prior offerings underwritten by the Firm were successful. For some customers who previously invested in one or both of the earlier failed offerings, the failure to disclose this use of the Montgomery 2015 proceeds was particularly misleading and deceitful. The customers were unknowingly using their own funds to pay themselves what was owed in the earlier offerings. The failure to disclose that some of the proceeds of the Montgomery 2015 offering were to be used to pay investors in the prior failed offerings was deceptive and unfair to investors.

- Respondents also fraudulently and deceptively failed to disclose that some of the proceeds of the Montgomery 2015 bond offering were to be paid to the borrower in the two prior failed offerings, Montgomery 2004 and Montgomery 2011. That borrower, Christopher Brogdon, was at the time of the Montgomery 2015 offering under investigation by the SEC for fraud and other securities law violations, as Respondents knew. In fact, one of the Brogdon transactions under investigation was the Montgomery 2011 private placement offering. The SEC took Cantone's testimony in 2014 in connection with its investigation, and it took DeRobbio's testimony about three months before the closing of the Montgomery 2015 offering. Channeling some of the proceeds of the Montgomery 2015 offering to Brogdon, who had failed to pay investors in the prior offerings what he owed them, and who had no role to play in the future success or failure of the Montgomery 2015 offering, was deceptive and unfair to investors in the Montgomery 2015 bonds.

- Cantone (and through him, the Firm) also fraudulently and deceptively failed to disclose that Cantone was to receive some of the proceeds of the Montgomery 2015 offering for the purpose of repaying him for money he had loaned to Brogdon to cover the shortfall in revenues to pay earlier investors in Brogdon-related offerings. Cantone thus concealed that he knew the prior offerings had not been successful and that Cantone had been propping up earlier Brogdon-related

offerings to make it seem they were successful when they were not. This misconduct was deceptive and unfair to investors.[6]

b. Cause V

Cause V alleges that Respondents violated MSRB Rule G-47 when they sold the Montgomery 2015 bonds, both in the initial offering and in secondary market transactions. MSRB Rule G-47 requires a municipal securities dealer to disclose all material information the dealer knows (or could reasonably learn from publicly available established industry sources) about a municipal securities transaction at or prior to the time of trade. It is a codification of MSRB guidance that already existed in connection with the fair dealing rule, MSRB Rule G-17. Rule G-47 became effective on July 5, 2014, and applied to all trades in Montgomery 2015 bonds.[7] We find that Respondents willfully violated MSRB Rule G-47 by the above-cited failures to disclose material facts before or at the time of sale of the Montgomery 2015 bonds.[8]

Respondents' defense. Respondents assert that the information they failed to disclose to investors in the Montgomery 2015 bonds was not material. They further claim that they relied on advice of counsel in determining not to disclose, among other things, the borrower's criminal background and fifteen-year exclusion from the Medicare and Medicaid programs. These arguments are without merit.

3. Sanctions

As discussed below, aggravating factors predominate and justify the most stringent sanctions. In connection with each bond offering, we separately expel the Firm from FINRA membership and bar the individual Respondents from associating with a FINRA member in any capacity. The Firm is ordered to pay restitution to all customers to the extent of the customers' losses caused by the misconduct, and each individual Respondent is jointly and severally responsible with the Firm to pay restitution to his own customers who bought the Quad Cities

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[6] Cause of Action IV was pled in the alternative to Cause III. If the Extended Hearing Panel did not find that Respondents' conduct in connection with Montgomery 2015 was fraudulent, Enforcement charged in the alternative that the conduct was a negligent violation of MSRB Rule G-17. We find the Respondents' conduct was fraudulent, but, if we did not, we would find it a negligent violation of MSRB Rule G-17.

[7] *See infra* at 100–01 and nn.670–74.

[8] Cause V also charges that some sales of the Quad Cities bonds violated MSRB Rule G-47. The 2013 Quad Cities offering closed in November 2013 and almost all the secondary market trades in Quad Cities bonds occurred in the first six months of 2014, before MSRB Rule G-47 became effective. To the extent that a handful of customer trades in Quad Cities bonds occurred after July 5, 2014, they were in violation of MSRB Rule G-47 as well as MSRB Rule G-17. CX-5 shows the dates and other details of transactions in the Quad Cities bonds. In any event, all the trades in Quad Cities bonds were in violation of the fair dealing rule, MSRB Rule G-17.

and/or Montgomery 2015 bonds. The information about what is owed by whom to each customer appears in Appendix B and Appendix C to this decision.[9]

II. Findings

A. Respondents

1. Cantone Research Inc.

The Firm became a member of FINRA and the MSRB in 1990. At all times relevant here, it conducted a general securities business selling equities, mutual funds, and other securities at a single office in Eatontown, New Jersey, staffed with nine or ten registered persons.[10] In 2003, Cantone Research also entered the business of underwriting municipal revenue bond offerings and selling those bonds to its retail customers in the primary and secondary markets.[11]

In 2013, at the time of the Quad Cities bond offering, Respondent Anthony Cantone was the Chief Executive Officer ("CEO") and president; his wife, Christine Cantone, was the Chief Compliance Officer ("CCO"); and Victor Polakoff was the branch manager and municipal securities principal. Respondent DeRobbio and two adult Cantone children, John and Maryann, were also registered at the firm at that time.[12]

In 2015, at the time of the Montgomery 2015 offering, Anthony Cantone remained the CEO and president of the Firm, but Stephen King had replaced Christine Cantone as CCO. Polakoff remained the municipal principal. DeRobbio and the Cantone children, John and Maryann, also remained registered at the Firm.[13]

Polakoff agreed to a bar from the industry on September 27, 2019, for a refusal to respond to a FINRA 8210 request to appear for testimony.[14] The request for testimony was issued in connection with an investigation into the Quad Cities and Montgomery 2015 bond offerings.[15]

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[9] Statutory disqualification is not a sanction, but it follows automatically by statute from our finding that Respondents' violations were willful. 15 U.S.C. § 78c(a)(39)(F); *Robbi J. Jones*, Exchange Act Release No. 91045, 2021 SEC LEXIS 241, at *4 n.2 (Feb. 2, 2021); *Thaddeus J. North*, Exchange Act Release No. 84500, 2018 SEC LEXIS 3001, at *22–23 (Oct. 29, 2018).

[10] Stip. ¶¶ 1–2; Tr. (Moy) 70, 91, 583.

[11] Stip. ¶¶ 1–2.

[12] Tr. (Moy) 70–71, 91; Tr. (DeRobbio) 1085–86.

[13] Tr. (Moy) 91–92, 583.

[14] Tr. (Moy) 71–74; CX-54 (Letter of Acceptance, Waiver and Consent).

[15] Tr. (Moy) 71–73.

Anthony Cantone, DeRobbio, and Polakoff sold most of the bonds at issue in this case,[16] although other registered representatives at the Firm also sold the bonds. In a few instances, John and Maryann Cantone were credited for sales of Quad Cities and Montgomery 2015 bonds.[17] One of Maryann Cantone's customers testified at the hearing[18] and that customer's testimony served as a vivid example of what the Firm's salespeople told customers about the bonds. Customers of Anthony Cantone,[19] DeRobbio,[20] and Polakoff[21] also testified.

2. Anthony J. Cantone

Respondent Anthony J. Cantone has had a long career in the securities industry and has held positions of authority and responsibility. He first became registered with FINRA as a General Securities Representative through an association with a former member firm in 1982. In 1995, Cantone became registered as a General Securities Representative and General Securities Principal through an association with Cantone Research. While at Cantone Research, he subsequently became registered as a Research Analyst in 2004, a Research Principal in 2005, an Investment Banking Representative in 2010, and an Investment Banking Principal in 2018. At the time of the hearing, Cantone was registered with FINRA in the six above-referenced capacities through his association with Cantone Research. At all times relevant to this matter, Cantone was the Firm's president and majority owner.[22] He oversaw all the Firm's activities, and before the Firm committed to any underwriting, Cantone had to approve it.[23]

Cantone and the Firm have had some regulatory issues. After the completion of an examination in 2013, FINRA issued a disciplinary complaint against Cantone and the Firm charging them with fraud and other violations in connection with a series of private placements used to purchase assisted-living facilities and retirement and nursing homes. All of the private placements were related to Christopher Brogdon, his wife and family, and their business entities. The fraud charges included the Montgomery 2011 private placement relating to the same assisted-living facility as the facility involved in the Montgomery 2015 bond offering. After an August 2016 disciplinary hearing, an Extended Hearing Panel issued a May 12, 2017 decision finding that Cantone and the Firm had committed fraud and other violations.[24] On January 16,

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[16] Tr. (Moy) 353.

[17] CX-5; CX-21.

[18] Tr. (AJ) 1516–36.

[19] Tr. (KE) 909–940 and Tr. (AM) 1432–1463.

[20] Tr. (HR) 1463–1482.

[21] Tr. (CK) 1483–1511.

[22] Stip. ¶¶ 4–5.

[23] Tr. (Moy) 88–89, 93; Tr. (DeRobbio) 625. Cantone reviewed materials presented to him intently. DeRobbio testified, "Mr. Cantone has got OCD about doing his own due diligence after I presented [my due diligence materials] to him." Tr. (DeRobbio) 626.

[24] CX-42; Tr. (Moy) 65.

2019, the National Adjudicatory Council ("NAC") issued a decision largely affirming the Extended Hearing Panel decision. For the various violations, the NAC fined Cantone Research and Cantone a total of $150,000 and suspended Cantone a total of fifteen months.[25] An appeal is pending at the SEC.[26]

On June 13, 2017, about a month after the Extended Hearing Panel decision referred to above, the New Jersey Bureau of Securities entered a Consent Order and Final Judgment with the Firm, Anthony Cantone, and Christine Cantone. The Consent Order imposed a 19-month all-capacities suspension of Anthony Cantone's registrations with the New Jersey Bureau, and payment by all defendants of $1.8 million in restitution and a $300,000 civil penalty. The sanctions were imposed on defendants for making various misrepresentations to investors in a private placement, including that the relevant certificates of participation were guaranteed by issuer Cantone Office Center, LLC and Esplanade Development LLC, a Florida real estate developer.[27]

3. Raymond J. DeRobbio

Respondent Raymond J. DeRobbio first became registered with FINRA as a General Securities Representative through an association with a former member firm in 1983. At all times relevant here, DeRobbio specialized in underwriting municipal securities. Most of his business was municipal bond underwriting, and most of the bonds he worked on were conduit offerings. It was when he joined Cantone Research in 2003 that the Firm expanded to municipal securities underwritings. DeRobbio worked at Cantone Research from 2003 through much of 2006, and then he left the Firm to join another firm. He came back to Cantone Research in 2013, shortly before he was offered the opportunity to underwrite the Quad Cities offering.[28] From June 2013 through the hearing in this matter, DeRobbio was registered with FINRA through an

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[25] CX-42; CX-43. In the same proceeding, Christine Cantone, who was at the time the Firm's CCO, was found to have failed to supervise her husband, Anthony Cantone, to ensure that he accurately and completely disclosed all material facts to potential investors in the private placement transactions. She and the Firm were fined, jointly and severally, $73,000 and she was suspended in all supervisory capacities for two years, with the requirement that she requalify after the completion of her suspension. The NAC noted that she was a recidivist. She had been suspended and fined in 2012 for another supervisory violation. CX-43, at 48.

[26] *Cantone Research Inc.*, Exchange Act Release No. 99134, 2023 SEC LEXIS 3467 (Dec. 11, 2023).

[27] Stip. ¶ 6. Tr. (Moy) 1595–97; CX-28, at 23–25.

[28] Tr. (DeRobbio) 614–17, 654; 1609–10. In 2003, DeRobbio joined the Firm with his business partner, registered representative James Friar. The two of them started the Firm's municipal securities business. They left the Firm together in 2006. By the time DeRobbio rejoined the Firm in 2013, however, Friar had died. Tr. (DeRobbio) 614–16, 1017. DeRobbio said that Friar drafted the Firm's WSPs for municipal bond underwriting and "put together" one of the early offerings discussed in this decision, Montgomery 2004. Tr. (DeRobbio) 449, 618. Friar was "friendly" with Christopher Brogdon, who was the borrower in the Montgomery 2004 offering, and Friar brought Brogdon as a client to Cantone's Firm. Tr. (DeRobbio) 993–94, 1082.

association with Cantone Research as a General Securities Representative, Investment Banking Representative, Municipal Securities Representative, and Municipal Securities Principal.[29]

After DeRobbio returned to Cantone Research in 2013, he was the person at the Firm responsible for initially collecting and reviewing municipal bond due diligence.[30] He would discuss the material with Polakoff, the municipal securities principal, and then the two of them would take it to Anthony Cantone for his review.[31]

B. Jurisdiction

FINRA has jurisdiction over Cantone Research to commence and conduct this disciplinary proceeding because, starting in 1990, the Firm was a FINRA member. FINRA also had jurisdiction over Cantone and DeRobbio because they were both registered with FINRA through their association with the Firm. Respondents do not dispute FINRA's jurisdiction.[32]

DeRobbio said in a declaration filed with his counsel's motion to withdraw from the representation that he understood that the Firm was about to file a Uniform Request for Broker-Dealer Withdrawal ("Form BDW") and go out of business. But the Firm had not done so by the time of the hearing.[33] There is evidence in the record that Cantone and the Firm continued to conduct a securities business even while refusing to appear at the hearing. One of the customers testified at the hearing that he had spoken with Cantone about a potential investment within the last month or so.[34]

In any event, Enforcement commenced this proceeding while the Firm was a FINRA member and the individual Respondents were registered through it. And the proceeding concerns conduct that occurred while they held that status. Under FINRA's By-Laws, FINRA retains disciplinary jurisdiction in those circumstances for two years after the termination of membership and registration.[35]

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[29] Tr. (DeRobbio) 612–14.

[30] Tr. (DeRobbio) 620–21.

[31] Tr. (DeRobbio) 621.

[32] Stip. ¶¶ 3, 7, and 9.

[33] Tr. (DeRobbio) 1002–04.

[34] Tr. (AM) 1442–43.

[35] Art. IV, Sec. 6 (member firm); Art. V, Sec. 4 (associated person). According to records in the Central Registration Depository ("CRD"), the Firm filed a Uniform Termination Notice for Securities Industry Registration ("Form U5") for DeRobbio on July 3, 2023, saying that his position was eliminated. The Firm's registration with FINRA terminated on September 5, 2023, upon its filing of a Uniform Request for Broker-Dealer Withdrawal ("Form BDW"). On December 13, 2023, in connection with a 2022 examination of Cantone Research and investigation No. 2022073419201 (a different investigation from the one that gave rise to this proceeding), Anthony J. Cantone submitted a Letter of Acceptance, Waiver, and Consent ("AWC") to settle charges that FINRA was about to file because Cantone had refused to provide on-the-record testimony requested pursuant to FINRA Rule 8210. In

C. The Investigation Giving Rise to this Disciplinary Proceeding

Ryan Moy was the first witness to testify. Since November 2022, Moy has been a risk monitoring analyst at FINRA. In that position, he is the single point of contact for a group of trading and execution firms. He responds to questions related to their financial operations and supervision. Prior to November 2022, he was a principal examiner who was responsible for examining firms for business conduct related matters.[36]

Moy explained how this proceeding arose. He was responsible for conducting the 2013 examination of Cantone Research that ultimately led to the Extended Hearing Panel decision in May 2017 and the NAC decision in January 2019 finding that Cantone and Cantone Research had committed fraud.[37] The 2013 examination involved, among other things, review of municipal bond and private placement offerings related to Christopher Brogdon.[38] Brogdon purchased 75 to 100 assisted-living facilities in the Southeast during the early 2000s, and Cantone Research was involved with a number of the private placements in which Brogdon was the obligor or a guarantor.[39] One of the Brogdon-related private placements involved in the investigation was Montgomery 2011, which involved the same assisted-living facility in Montgomery, Alabama as the Montgomery 2015 bond offering.[40]

In 2016, Moy was assigned to a follow-up examination of Cantone Research. He was responsible for conducting a review of the due diligence documentation, supervision, and suitability of offerings. From documents requested pursuant to FINRA Rule 8210,[41] Moy saw that Montgomery 2004, Montgomery 2011, and Montgomery 2015 all related to the same assisted-living facility. He called customers who purchased the Montgomery 2015 offering from the Firm and in conversations with them he learned about the 2013 Quad Cities offering.[42]

Moy obtained and reviewed due diligence materials, which included relevant financial statements and the Firm's WSPs.[43] Moy's initial Rule 8210 request was in the context of a cycle exam, but upon his review of the Montgomery 2015 due diligence materials, he had concerns.

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the AWC, Cantone agreed to be barred. He also acknowledged that, as a result of the bar, he became subject to a statutory disqualification during the period of the bar. Cantone was represented in the AWC by the same counsel who withdrew from this proceeding shortly before the beginning of the hearing.

[36] Tr. (Moy) 56.

[37] Tr. (Moy) 62, 65; CX-42, at 6.

[38] Tr. (Moy) 62–63.

[39] Tr. (Moy) 63.

[40] Tr. (Moy) 64, 67.

[41] Tr. (Moy) 66–67.

[42] Tr. (Moy) 68, 78.

[43] Tr. (Moy) 69, 75–76; JX-1; JX-2.

The exam became a cause exam.[44] Eventually, the cause exam included the Quad Cities bond offering.[45] Moy made various Rule 8210 requests, and he believed that in response to those requests the Firm provided all its due diligence materials relating to the Quad Cities and Montgomery 2015 offerings.[46] His concerns increased when he discovered that the due diligence materials did not contain documentation that the Firm required in its WSPs.[47]

The Firm's WSPs 2013 required a due diligence memo. But there was none for Quad Cities.[48] Similarly, the Firm's WSPs in effect for 2015 required a due diligence memo, but there was none for Montgomery 2015.[49] The Firm also required, among other things, an on-site examination, but the Firm provided no evidence that anyone from Cantone Research visited the dormitory facility involved in the Quad Cities bonds before conducting the underwriting.[50]

After further scrutiny of the Firm's records, talking with customers, and taking testimony,[51] Enforcement initiated this disciplinary proceeding by filing the Complaint. We now turn to the two municipal bond offerings at issue in this case.

D. Conduit Bond Offerings

The municipal bonds in the two offerings at issue were what are known as "conduit bonds," which means that the government issuer of the bonds serves as a conduit of the funds raised in the offering and transfers the funds to a private entity to fund a project viewed as benefiting the public, such as a hospital, school, energy infrastructure, or public housing. The private entity that receives and uses the funds is the conduit borrower. The conduit borrower is responsible for paying the debt obligation. Investors who purchase conduit bonds rely on revenues generated by the conduit borrower's project for payment of the principal and interest owed on the bonds. In cases where the conduit borrower fails to make a payment, the government issuer usually is not required to pay the bondholders.[52]

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[44] Tr. (Moy) 83–84.

[45] Tr. (Moy) 84.

[46] Tr. (Moy) 78–79, 86–87.

[47] Tr. (Moy) 87–91.

[48] Tr. (Moy) 87–90; JX-1, at 30.

[49] Tr. (Moy) 92–93; JX-2, at 30.

[50] Tr. (Moy) 90–91; JX-1, at 30; JX-2, at 30.

[51] Tr. (Moy) 66–93.

[52] U.S. Securities and Exchange Commission Investor Bulletin: Municipal Bonds – An Overview (Feb. 1, 2018), https://www.sec.gov/oiea/investor-alerts-and-bulletins/ib_munibondsoverview; Speech by SEC Commissioner: Regulation of the Municipal Securities Market: Investors Are Not Second-Class Citizens, https://www.sec.gov/news/speech/2009/spch102809ebw.htm ("A conduit bond is a type of revenue bond frequently issued by a municipality on behalf of a third party, such as a college, hospital, or industrial corporation. Conduit bonds have their name because the municipality acts as a "conduit" through which investors lend money to a third party and the

Accordingly, although the issuer of the 2013 Quad Cities bonds was the Quad Cities Regional Economic Development Authority, a governmental instrumentality, neither the issuer, nor the State of Illinois, nor any municipality was obligated to make payments to bondholders. Neither the taxing power nor the faith and credit of the Quad Cities Regional Economic Development Authority, the State of Illinois, or any municipality was pledged to support the Quad Cities bonds.[53]

Similarly, the Montgomery 2015 bonds were issued by the Medical Clinic Board of the City of Montgomery-1976 East, but neither the issuer, nor the State of Alabama, nor any municipality was obligated to make payments to bondholders. No governmental entity pledged its taxing power or faith and credit in support of the bonds.[54]

In each offering, investors depended on the revenues generated by the specific project for the timely payment of principal and interest.[55] The Quad Cities bonds were payable from revenue generated by the dormitory. If the dormitory failed to generate enough revenue to pay the facility's expenses and make all scheduled principal and interest payments, then investors would incur losses.[56] And the Montgomery 2015 bonds depended on revenues generated by the assisted-living facility (once it was rehabilitated, licensed, and operational) for payment of principal and interest. If those revenues fell short, investors would suffer losses.[57]

This meant that bondholders were dependent on the competence and integrity of the borrowers and persons managing the projects. As DeRobbio agreed at the hearing, in a conduit bond offering like Quad Cities or Montgomery 2015, the background of the borrower and the operator of the project is important. Knowledge of the background of the persons who are responsible for the success of the project assists in evaluating their ability to run the project

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third party repays the debt. The credit of the third party backs the conduit bond, and the debt is generally not considered a liability of the municipality. Municipalities typically issue conduit bonds to finance the construction, purchase, or lease of dormitories, hospitals, or manufacturing and certain industrial-type facilities by the third party."). *See also* IRS Tax Exempt & Government Entities, Your Responsibilities as a Conduit Issuer of Tax-Exempt Bonds, https://www.irs.gov/pub/irs-pdf/p5005.pdf. *See also* Tr. (Swan) 1336; Tr. (DeRobbio) 630–31, 653–55.

[53] Stip. ¶ 17.

[54] Stip. ¶ 58; Tr. (DeRobbio) 656, 991.

[55] Tr. (DeRobbio) 630–31.

[56] Stip. ¶¶ 17–18.

[57] Tr. (DeRobbio) 656. In connection with the Montgomery 2015 offering, DeRobbio noted that, if revenues from the assisted-living facility fell short, investors might also recover something of what they were owed under a personal and corporate guaranty from the borrower. Tr. (DeRobbio) 656. That presumes that the borrower acts in good faith and has the resources to make up the difference. As discussed below, Brogdon and his wife did not make good on the guaranty they gave in connection with the Montgomery 2004 offering.

successfully.[58] DeRobbio testified that past success is important, and operations are "critical."[59] Most of the securities issues that DeRobbio sold were conduit bond offerings.[60]

The financial chances of being able to pay bondholders as promised also depends on the particulars of the project expected to generate revenues. As DeRobbio agreed, financial analysis is critical to investors and must be addressed in due diligence.[61]

For example, the Firm's clearing agent wrote to the Firm shortly before DeRobbio rejoined it to discourage the Firm from underwriting conduit bond deals backed by one to three nursing home facilities. The clearing agent explained in an email to Christine Cantone that such offerings were small issuances of under $5 million. From a financial perspective they were highly risky.[62]

> Any small change of occupancy, change of management or unusual expense could result in operational losses resulting in a missing interest payment [on the bonds] and causing a potential default. In case of default, the trustee could force disclosure resulting in default. Typically, bonds on the facilities drop 50% to 70% in value on the news of these events.[63]

For these reasons, the clearing agent cautioned that it was highly unlikely to approve of a small nursing home or assisted-living offering.[64] At some point after his return to Cantone Research, DeRobbio received a copy of the clearing agent's email.[65]

Each offering involved in this case was highly risky under the clearing agent's analysis. Each offering was relatively small ($2.2 million in Quad Cities bonds; a little over $6 million in Montgomery 2015 bonds) and each was backed by revenues generated from a single facility. If anything went wrong at that single facility, the bonds were subject to a potential default.

Although the two offerings at issue in this case involved different types of facilities (one a student dormitory and the other an assisted-living facility), the financial analysis was fundamentally the same because the projects were similar in how they generated revenues to pay bondholders. In simple terms, as DeRobbio agreed, both projects involved putting a resident in a

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[58] Tr. (DeRobbio) 654–56.

[59] Tr. (DeRobbio) 656.

[60] Tr. (DeRobbio) 654.

[61] Tr. (DeRobbio) 661–62.

[62] Tr. (DeRobbio) 659–62; CX-36.

[63] Tr. (DeRobbio) 659–61; CX-36.

[64] Tr. (DeRobbio) 660; CX-36.

[65] Tr. (DeRobbio) 658–61; CX-36.

bed to generate revenue.[66] Accordingly, the number of beds available for use and the occupancy/vacancy rate were critical facts to investors in both bond offerings.[67]

E. The 2013 Quad Cities Municipal Bond Offering

In late 2013, Cantone Research acted as the sole underwriter for the $2.2 million municipal revenue bond offering referred to by the parties as the Quad Cities municipal bond offering. The proceeds of that offering were supposed to be used to refinance and rehabilitate a student housing facility adjacent to the College's campus.[68] As discussed below, the 2013 Quad Cities offering quickly failed and investors incurred substantial losses.

Enforcement charges that Respondents negligently failed to conduct the due diligence necessary to develop a reasonable basis for believing the bonds a suitable investment for any investor, made negligent misrepresentations of material fact and misleading omissions of material fact, and negligently failed to disclose all material information they knew or reasonably could have known about the investment on or before the trades. Enforcement contends that this misconduct was in willful violation of MSRB Rules G-17, G-19, and G-47, and Securities Act Sections 17(a)(2) and 17(a)(3).

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[66] Tr. (DeRobbio) 664.

[67] DeRobbio acknowledged that the financial success of the Quad Cities offering was driven by paid occupancy of dormitory beds. Tr. (DeRobbio) 856-57. DeRobbio said that he analyzed offerings involving assisted-living facilities based on "debt per bed." He testified that he declined to underwrite one offering that involved $100,000 debt per bed but wanted to underwrite another that was $30,000–$40,000 debt per bed. Tr. (DeRobbio) 1039–41, 1641.

The debt-per-bed for the $2.2 million Quad Cities offering was only around $15,000 if all 142 beds were occupied and around $30,000 per bed if half the beds, 71, were occupied. This was well within DeRobbio's range of acceptability.

Curiously, however, DeRobbio also underwrote the Montgomery 2015 offering, which, on a debt-per-bed basis amounted to more than $98,000 debt per bed if all the beds were fully occupied ($6 million in debt and 61 beds). And if fewer beds were occupied the debt per bed would increase. Underwriting the Montgomery 2015 offering was inconsistent with DeRobbio's testimony that he would not go forward with an underwriting that involved that much debt per bed.

The debt-per-bed analysis also illustrates how financially risky the Montgomery 2015 offering was, even aside from other factors discussed below, like the borrower's troubling criminal background. As Respondents knew, Dwayne Edwards, the borrower in the Montgomery 2015 offering, had pled guilty to misusing patient funds in connection with his assisted-living business. As a result, he lost his license to operate such a facility in South Carolina for eight years and was precluded from the Medicare and Medicaid programs for 15 years.

[68] Stip. ¶¶ 14–16; Tr. (KE) 921–22. The College is located between the cities of Dixon, Illinois (population 15,733) and Sterling, Illinois (population 15,370). JX-3, at 45.

1. Relevant Events Prior to 2013 Quad Cities Offering

a. 2004 Dormitory Construction Financing

In August 2004, the Sauk Valley College Foundation ("Sauk Foundation") created Sauk Valley Student Housing, LLC ("Sauk Valley Housing") for the purpose of constructing a student dormitory next to the College.[69] Sauk Foundation was the sole member of Sauk Valley Housing.[70] That same year, the Illinois Finance Authority issued $7,120,000 of Variable Rate Demand Revenue Bonds (the "2004 College Bonds") to fund construction of the dormitory. The proceeds from the 2004 College Bonds were loaned to the parent company of Sauk Valley Housing, and construction was completed in 2005. Sauk Valley Housing was both the borrower and the owner of the dormitory.[71] After construction was completed, Sauk Valley Housing contracted with BMOC to manage the dormitory for a term running from August 1, 2007, to July 31, 2012.[72]

b. 2011 Borrower Bankruptcy

In February 2011, about six years after construction of the dormitory was completed, Sauk Valley Housing filed for Chapter 7 bankruptcy.[73] Respondents knew that the borrower in the 2004 bond offering had filed for bankruptcy in 2011 because it was discussed in the draft POS they received in early October 2013. From that discussion, Respondents also knew that the bankruptcy trustee had moved to abandon the dormitory as having no value or benefit for the bankruptcy estate. According to the POS, the court granted that motion.[74]

The discussion of the bankruptcy in the draft POS should have alerted Respondents to at least three potential issues requiring further study and due diligence. First, the draft POS noted that the reason the borrower in the 2004 offering had filed for Chapter 7 bankruptcy was that the rents charged for development of the earlier offering could not support the costs. This raised an issue of why the rents were insufficient and whether the rents could support the debt about to be created by the 2013 offering.[75] Second, the POS discussion suggested that the dormitory was dependent upon the College and that the College had not been helpful to the dormitory. The draft POS indicated that part of the dormitory's problem had been the lack of an adequate

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[69] JX-3, at 10, 47.

[70] JX-3, at 10, 43.

[71] Stip. ¶¶ 19–20. According to the OS for the 2013 Quad Cities offering, the borrower—Sauk Valley Housing—was owned by its "Sole Member." JX-3, at 45. In the original financing for construction of the dormitory the sole member of the Sauk Valley Housing limited liability company was the Sauk Foundation. JX-3, at 10, 43.

[72] Tr. (Moy) 599; JX-33, at 1, 9, 26, 30–32.

[73] Stip. ¶¶ 21; Tr. (Moy) 98–102; CX-1; JX-13; JX-14.

[74] CX-71, at 55–56.

[75] Tr. (DeRobbio) 676–78; CX-71, at 51.

commitment from the College to support the dormitory.[76] Third, the bankruptcy trustee's decision to abandon the property as lacking value to the bankruptcy estate could raise questions about the condition and status of the dormitory two years later.[77]

Review of the bankruptcy files was required to see what light they could shed on those issues and the reasons the first bond offering failed. Bankruptcy filings are public records.[78] However, Respondents did not examine Sauk Valley Housing's bankruptcy filings.[79] Their due diligence file did not contain a copy of any of Sauk Valley Housing's bankruptcy filings.[80]

If Respondents had reviewed the bankruptcy records, they would have learned certain significant facts. Most important, they would have learned that the borrower in the 2004 offering—the entity that filed for bankruptcy in 2011—was the same entity as the borrower in the 2013 offering, Sauk Valley Housing. They also would have learned that BMOC kept the borrower's books and records. That information would have warranted closer scrutiny of the relationships among the interested parties in the 2013 offering and whether representations in the draft POS for the 2013 offering—that the dormitory would be operated under new ownership and different management—were accurate.

In its bankruptcy filing, Sauk Valley Housing listed the dormitory as an asset with a current value of approximately $1.5 million (based on a 2009 appraisal) but reported that there was a much larger secured claim on the property, a mortgage, in the amount of more than $7.2 million, as well as other debts.[81] Among the other unsecured debts listed, Sauk Valley Housing owed the College $62,245 for water and sewer services from 2005 through 2011.[82] Aside from the mortgage, the College was the dormitory's largest creditor.[83] DeRobbio agreed at the hearing that if he had reviewed the bankruptcy filing he would have known the dormitory was not paying its water and sewer bills, and that the failure to pay those bills would put stress on the relationship between the dormitory and the College.[84]

The bankruptcy filing also showed that Sauk Valley Housing had filed a lawsuit alleging construction defects, which was settled. The terms of the settlement, however, were not disclosed

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[76] CX-71, at 55.

[77] Tr. (DeRobbio) 793–94; JX-18, at 6.

[78] Tr. (Moy) 99–100.

[79] Tr. (DeRobbio) 678–81.

[80] Tr. (Moy) 101–02.

[81] JX-14, at 6, 11.

[82] JX-14, at 15.

[83] JX-14, at 13–16.

[84] Tr. (DeRobbio) 828–30.

in the bankruptcy filing.[85] The fact of a lawsuit over construction defects might have indicated significant problems with the physical facility warranting additional due diligence.

As noted above, the bankruptcy trustee determined that the dormitory and other assets listed in the bankruptcy filing for Sauk Valley Housing had no value or benefit to the bankruptcy estate. For that reason, the trustee moved to abandon the estate's interest in the assets, including the dormitory, and the bankruptcy court granted the motion. The $7.2 million mortgage debt underlying the 2004 College bonds, which was then held by BMO Harris Bank N.A. ("Harris Bank"), was not discharged.[86] The bankruptcy trustee's abandonment of the property meant that the dormitory was excluded from the bankruptcy estate and reverted to ownership by the debtor—*i.e.*, the borrower in the 2004 offering, Sauk Valley Housing.[87] The trustee's conclusion that the dormitory had no value to the estate in 2011 would warrant additional due diligence as to its value in 2013.

The bankruptcy filing showed that the dormitory's gross income declined by approximately 25% over the course of the three school years preceding the bankruptcy filing. In the 2007–2008 school year, gross income was $409,578; in the 2008–2009 school year, gross income was $369,751; and in the 2009–2010 school year, gross income was $307,805.[88] Those declining numbers made it important to examine more closely the revenue projections for the 2013 Quad Cities offering.

Sauk Valley Housing's bankruptcy filing identified Becky P., a BMOC employee,[89] as the person who kept its books and records for the period 2008–2010.[90] As noted below, she also appears on some email correspondence in which Stifel asked BMOC about dormitory occupancy rates and other historical financial information.[91]

In its bankruptcy filing, Sauk Valley Housing was required to set forth in a financial statement the amount of each payment or transfer to any creditor within the 90-day period immediately preceding the bankruptcy filing. Sauk Valley Housing listed BMOC as the only such creditor, but it stated that the amounts paid and amount still owing to BMOC were "unknown."[92] Given that Becky P., a BMOC employee, kept the books and records for Sauk Valley Housing, this seems odd. Sauk Valley Housing should have known how much it paid to

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[85] JX-14, at 30.

[86] JX-3, at 48.

[87] *E.g.*, *Martin v. Gladstone*, D080534, 2023 Cal. App. LEXIS 813, at *11–15 (Cal. Ct. App. Oct. 19, 2023); *QDOS, Inc.*, 652 B.R. 543, 2023 Bankr. LEXIS 1896, at **11 (Bankr. Ct. C.D. Ca. July 26, 2023).

[88] JX-14, at 29.

[89] JX-14, at 30, 32.

[90] JX-14, at 32.

[91] RX-50, at 1–2.

[92] JX-14, at 30.

BMOC in the 90 days preceding the bankruptcy filing and BMOC should have known how much it received. They also should have had an understanding as to what might still be owing. Under the Bankruptcy Code, a bankruptcy trustee can act in various circumstances to avoid fraudulent transfers of property made by the debtor to related parties, as well as preferential transfers that would advantage some creditors over others.[93] The trustee "is permitted to recover, with certain exceptions, transfers of property made by the debtor within 90 days before the date the bankruptcy petition was filed."[94] If payments were made to BMOC during the 90-day period leading up to the bankruptcy filing, they should have been disclosed and may have been subject to recovery for the benefit of the bankruptcy estate.

If the bankruptcy filings had been reviewed in due diligence for the 2013 Quad Cities offering, they might have cast doubt on the wisdom of relying on Sauk Valley Housing and BMOC for historical data on the performance of the project and on BMOC's ability to manage the dormitory. At a minimum, the bankruptcy filings would have alerted Respondents to the need for deeper study of the dormitory's financial history and relationship with the College and BMOC.

c. 2011–2013 Continued Operation of Dormitory

From 2011 to 2013, the dormitory remained open, but with limited occupancy, in part due to mold contamination.[95] BMOC continued as Manager. It generated financial statements for most of the period from 2011 to the end of 2013, which Stifel produced to FINRA from its files. These financial statements were not in Respondents' files.[96] Their absence is another indication of Respondents' lack of due diligence.

After the bankruptcy, the financial statements consistently showed declining net income.[97] In the six-month period from July to December 2012, the dormitory only generated $1,500 net income, which meant that the dormitory was only generating about $3,000 a year in

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[93] *See, e.g.*, *Lange v. Inova Cap. Funding, LLC (In re Qualia Clinical Serv.*), 652 F.3d 933, 934, 941 (8th Cir. Aug. 30, 2011) (perfection of security interest within the 90-day period was avoidable preference because it would advantage one creditor over others); *Williamson v. Guardians of Travel, LLC (In re 1 Big Red LLC)*, 2023 Bankr. LEXIS 2902, at *3, 16, 18–20 (U.S. Bankr. Ct. D. Kan. Nov. 29, 2023) (noting that some trustees employ "preference mills" to pursue preference actions for the trustee from the list in the debtor's statement of affairs of all payments the debtor made in the 90 days before bankruptcy (or for insiders, within one year)); *ACF Finco I, LP v. Valley Gutter Supply, Inc. (In re Red Rose, Inc.)*, 2023 Bankr. LEXIS 2560, at *6 (U.S. Bankr. Ct. D. Nev. Sep. 11, 2023) (setting forth elements of an avoidable preference, including that it must have been made on or within 90 days before the bankruptcy case was filed).

[94] *Barnhill v. Johnson*, 503 U.S. 393, 394 (1992) (holding that check honored on 90th day prior to debtor's bankruptcy was subject to suit as avoidable preference).

[95] Stip. ¶ 22.

[96] Tr. (Moy) 165–71; RX-144; RX-145; RX-146; RX-147.

[97] Tr. (DeRobbio) 844–50; RX-144; RX-145; RX-146; RX-147.

net income.[98] As DeRobbio agreed, this was not nearly enough income to cover the debt service required for the Quad Cities bond offering.[99]

As discussed below, the OS for the Quad Cities offering projected total effective income in the first year after the offering closed, the year 2014, of $373,211 and net operating income of $133,381.[100] This was far more net operating income than actual historical results. In looking at the historical results for this period, DeRobbio admitted that the projections used in the Quad Cities offering were "excessive."[101] If Respondents had performed meaningful due diligence, they would have recognized that BMOC's financial projections were unreasonable.

2. Key Players in the 2013 Quad Cities Offering

a. Sauk Valley Housing, the Borrower, and Sugar Capital, the Mortgage Bond Purchaser

The borrower in the 2013 Quad Cities offering was Sauk Valley Housing,[102] the same entity that was the borrower in the 2004 municipal bond offering and that filed for bankruptcy in 2011. As noted above, Sauk Valley Housing remained the owner of the dormitory after the bankruptcy proceeding.

The parties stipulated that in March 2013 a man named Eric F., through his entity Sugar Valley Capital Partners, LLC ("Sugar Capital"), acquired "complete, indirect ownership" of Sauk Valley Housing.[103] It is unclear precisely what "complete, indirect ownership" means. According to the OS later issued for the 2013 Quad Cities municipal bond offering, the original sole member of Sauk Valley Housing, Sauk Foundation, assigned its membership interest to United Housing and Community Services Corporation ("United Housing") on March 21, 2013.[104] That made United Housing the sole managing member of Sauk Valley Housing, the dormitory owner. In the OS for the 2013 Quad Cities offering, neither Eric F. nor Sugar Capital was identified as a director, officer, or affiliate of United Housing.[105]

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[98] Tr. (DeRobbio) 849–50; RX-146.

[99] Tr. (DeRobbio) 850–51.

[100] Tr. (DeRobbio) 851; JX-3, at 53.

[101] Tr. (DeRobbio) 854.

[102] JX-3, at 5.

[103] Stip. ¶ 23.

[104] JX-3, at 43–44.

[105] James Swan, the investment banker who led the Stifel team on the Quad Cities underwriting until Stifel withdrew, testified that Eric F. was not the owner of the dormitory. Swan identified Eric F. as the developer of the transaction. Tr. (Swan) 1342.

The parties also stipulated that in March 2013 Eric F. acquired the existing mortgage on the dormitory from Harris Bank for $1,500,000.[106] The OS for the 2013 Quad Cities offering disclosed that Sugar Capital was the current holder of the mortgage and explained that Sugar Capital had purchased the mortgage from Harris Bank. The OS identified Eric F. as the managing member of Sugar Capital.[107]

On March 27, 2013, Sauk Foundation, which had created Sauk Valley Housing and was its sole member before United Housing replaced it, agreed to pay $600,000 to Eric F.'s entity, Sugar Capital. Sauk Foundation made the payment in return for a release of any guarantee or other obligations that it may have had relating to the dormitory in connection with the mortgage loan Sugar Capital purchased. There is no evidence in the record that Sauk Foundation in fact had any obligations in connection with the mortgage loan. This transfer of $600,000 was characterized in the agreement between Sauk Foundation and Sugar Capital as part of United Housing's acquisition of 100% membership interest in Sauk Valley Housing, with United Housing acting as Sugar Capital's "nominee."[108]

The $600,000 payment was not disclosed in the OS for the Quad Cities offering. In litigation filed by Cantone Research on behalf of bondholders after the offering failed (the "Bondholder Litigation," which is discussed in more detail below), Respondents characterized the payment as a "windfall" for Eric F.[109] According to Respondents, Eric F. led them to believe that he had acquired his interest in the dormitory for $1,500,000 and he sought to be reimbursed from the proceeds of the Quad Cities offering only for his acquisition costs. He sought no fee. Rather, he told Respondents, he would depend on eventual returns from the subordinated Series B bonds to make money on the transaction. In the Bondholder Litigation, the Firm claimed that Respondents had been unaware of the $600,000 payment that Eric F. received in addition to reimbursement of the $1,500,000 cost of acquiring the mortgage. The $600,000 payment was a profit that Eric F. made on his interest in the dormitory without waiting for payments due on the subordinated bonds.[110]

b. BMOC, the Dormitory Manager

As noted above, BMOC managed the dormitory from the time it opened through 2011 and continued to do so after Sauk Valley Housing's 2011 bankruptcy. The plan in the 2013 Quad Cities offering was for BMOC to continue to manage the dormitory.[111] Bill L. was the president

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[106] Stip. ¶ 23.

[107] JX-3, at 5, 10, 44, 52.

[108] Tr. (Moy) 109–15; CX-84.

[109] CX-85, at 14, ¶ 85.

[110] CX-85, at ¶¶ 72–73, 75, 85.

[111] JX-3, at 49–52.

of BMOC, and Steve S. was the BMOC liaison with the College.[112] Becky P. and Jason T. were two other BMOC employees who were on correspondence related to the 2013 Quad Cities bond offering.[113] Becky P., as noted above, was identified in the borrower's 2011 bankruptcy filing as the person who kept Sauk Valley Housing's books and records for 2008–2010.

BMOC was connected to United Housing, the sole member of the borrower entity in 2013, through Steve S. According to the OS for the 2013 Quad Cities offering, Steve S. served as part of BMOC's management team, but he also was Executive Director of United Housing.[114] Steve S. signed the OS that was eventually issued for the 2013 Quad Cities bonds on behalf of the borrower, Sauk Valley Housing, and its sole member, United Housing.[115] As noted above in connection with the transfer of $600,000 from Sauk Foundation to Eric F., United Housing was characterized in connection with that transaction as acting as Sugar Capital's nominee.[116]

Thus, the relationships between the borrower, BMOC, and other entities involved in the dormitory's financial history were murky. The parties involved in the Quad Cities offering do not appear to have been independent of each other, and they were not new to the dormitory project.

c. Stifel, the Original Underwriter

In spring 2013, Eric F. contacted a registered representative of Stifel to serve as underwriter for a new municipal bond offering. James Swan, the registered representative Eric F. contacted, was a managing director at Stifel and he became the lead investment banker on the Quad Cities bond offering. He was at Stifel from February 2013 through March 2021, where he held Series 7 and Series 63 licenses. He is currently with another financial services firm and holds Series 7, Series 63, Series 79, and Series 52 licenses.[117]

Swan's role in the Quad Cities offering was first to "source" the deal. He testified that he already had a relationship with the developer of the transaction, whom he identified as Eric F. In the offering, Swan said he worked with the developer, Eric F., and the property manager, BMOC. His purpose was to understand the creditworthiness of the transaction. He conferred internally at Stifel and put together the documents necessary to do the offering. His work on the offering was intended to be presented to Stifel's credit committee for decision on whether to do the deal.[118]

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[112] JX-3, at 51.

[113] RX-50; RX-66.

[114] JX-3, at 44, 51.

[115] JX-3, at 76.

[116] Tr. (Moy) 109–15; CX-84.

[117] Tr. (Swan) 1334–35, 1338.

[118] Tr. (Swan) 1336, 1341–42.

Ernest L. was Swan's analyst who helped "run the numbers."[119] He took the historical numbers presented to Stifel by the interested parties and incorporated those numbers into a pro forma, which was part of the bond model that Stifel used to understand how the dormitory had historically performed and how the property would likely perform going forward in terms of paying its debt service on a timely and current basis.[120]

At Stifel, Swan reported directly to Peter C., who was co-director of public finance. Swan said he would share with Peter C. at a high level where he was in the review process for a transaction.[121] He would consult Peter C. about whether a proposed offering was ready to present to the credit committee, and, once presented, the credit committee would then decide whether to do the underwriting.[122] The credit committee never approved the Quad Cities underwriting.[123]

d. Attorney Brian M., Counsel for Borrower and Sugar Capital

Sauk Valley Housing and United Housing (the borrower and its sole member), and Eric F.'s entity, Sugar Capital, all shared the same attorney in connection with the 2013 Quad Cities offering, Attorney Brian M.[124] Attorney Brian M. was the person who contacted Respondent DeRobbio after Stifel withdrew from the underwriting to inquire whether DeRobbio and Cantone Research might be interested in underwriting the 2013 Quad Cities offering.[125] Attorney Brian M. knew DeRobbio from working as counsel on a number of municipal bond offerings for which DeRobbio acted as an underwriter and salesperson.[126] In fact, Attorney Brian M. had been counsel for Christopher Brogdon and his entities and was involved as an attorney on the Brogdon-related Montgomery 2004 and Montgomery 2011 offerings.[127] And, as discussed below, Attorney Brian M. would later be involved in the Montgomery 2015 offering as counsel for Respondents.

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[119] Tr. (Swan) 1337–38.

[120] Tr. (Swan) 1338.

[121] Tr. (Swan) 1337–38.

[122] Tr. (Swan) 1336, 1427.

[123] Tr. (Swan) 1426–27.

[124] Stip. ¶ 25.

[125] Tr. (DeRobbio) 664–65.

[126] Tr. (Moy) 105; Tr. (DeRobbio) 664–65.

[127] Tr. (Moy) 105.

e. Attorney Vincent M., Counsel for Underwriter

While it was the underwriter for the Quad Cities offering, Stifel retained Attorney Vincent M. and his law firm as its counsel. When Respondents stepped in to underwrite the transaction, Attorney Vincent M. and his firm stayed on as underwriter's counsel.[128]

3. Stifel's Due Diligence

a. Stifel's Bond Model

As part of its due diligence, Stifel created a bond model for the Quad Cities offering[129] based on information the dormitory Manager, BMOC, provided.[130] The last draft of the bond model that Stifel worked on before withdrawing from the role of underwriter was dated August 21, 2013.[131]

i. Sources-and-Uses Page

Stifel's draft bond model included a sources-and-uses page that showed the amount of money expected from sales of the bonds and how that money was to be spent. Swan explained that the sources-and-uses page would allow the reader to see the size of the debt service and the various reserves and funding of fees.[132]

The sources-and-uses page of the August 21, 2013 draft bond model showed that the offering was composed of $2.575 million of Series A bonds (senior tax exempt) and $525,000 subordinated Series B bonds, for a total of $3.1 million. Most of the funds, a little over $2 million, were to be spent on "note acquisition." Construction costs were set at $150,000 and working capital at $30,000. A portion of the funds, $231,000, were to be set aside in a debt service reserve fund to make up any shortfall in revenues to make payments to bondholders. Most of the rest of the funds to be raised in the offering were to be spent on professional fees and other costs of the offering itself.[133]

The sources-and-uses page noted that the figures in the bond model were based on 10-month leases at 100% occupancy of 95 currently available beds in 2014, and 95% occupancy of 138 rentable beds in 2015.[134] The terms "currently available" and "rentable" were not defined. If

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[128] JX-3, at 5; Tr. (Moy) 494–95.

[129] CX-72, at 84–87.

[130] Tr. (Swan) 1356.

[131] Tr. (Swan) 1350.

[132] Tr. (Swan) 1339; CX-72, at 1, 84.

[133] CX-72, at 84.

[134] CX-72, at 84.

all 144 beds were treated as available, then the projected occupancy rate would be about 66% in 2014 and close to 96% in 2015.

ii. Pro Forma

Stifel's draft bond model also included a pro forma that projected income and expenses for the dormitory year by year, starting with 2014. With regard to projected income, the pro forma showed a "gross rent potential" of $761,724 in 2014. It projected that vacancies would result in a loss of potential rent income of $364,935. It also estimated that discounts would amount to a loss of potential rent income of $40,128. After subtraction of amounts estimated for vacancies and discounts, the "effective" income for 2014 was projected to be $373,211.[135]

This projected "effective" income was substantially higher than the dormitory's gross income reported in the borrower's bankruptcy filing for the 2009–2010 school year. As noted above, the bankruptcy filing reported gross income for that school year of $307,805.[136]

Stifel's August 2013 pro forma projected total expenses for 2014 of $263,302, which included a $38,400 management fee.[137]

Subtracting projected expenses from "effective" income, yielded a projected 2014 net operating income of $93,109.[138]

In 2015, the pro forma projected a substantial decrease in vacancies, leading to a projected increase in "effective" income of $593,931, almost twice the dormitory's gross income for the 2009–2010 school year, as reported in the borrower's bankruptcy filing. With only modest increases in expenses projected for 2015, the pro forma projected 2015 net operating income of $286,097, more than triple the projected 2014 net operating income. From 2015 through 2024, the pro forma projected steadily increasing net operating income at roughly a rate of 2% per year.[139]

iii. Payments to Bondholders

The last page of the bond model projected the principal and interest to be paid to bondholders each year. The figures were based on the projections in the pro forma for "effective" income, total expenses, and net operating income.[140]

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[135] CX-71, at 91; CX-72, at 85–86 (easier to read copy attached to different email).

[136] JX-14, at 29.

[137] CX-71, at 91; CX-72, at 85 (easier to read copy attached to different email).

[138] CX-71, at 91; CX-72, at 85 (easier to read copy attached to different email).

[139] CX-71, at 91; CX-72, at 85–86 (easier to read copy attached to different email).

[140] CX-71, at 91; CX-72, at 85–86 (easier to read copy attached to different email).

iv. Debt Service Coverage Ratio

The purpose of the bond model was to evaluate the borrower's ability to pay the debt going forward. The model would allow a reader to see whether the payments to be made to bondholders (sometimes referred to as the debt service) and the various reserves and fees were all properly funded.[141]

For that reason, a critical component of the bond model was the debt service coverage ratio. That ratio measures the ability to cover the debt service. Net operating income must exceed the debt service for a transaction to be feasible. Swan testified that excess net income was needed as a margin of safety so that if there was an increase in fixed costs, insurance, or vacancies, or if other unknowns occurred, the project would have the tolerance and ability to cover debt service in the future.[142]

The amount by which the net operating income exceeds debt service relates to the amount of risk involved. If you have a very narrow debt service coverage ratio, Swan explained, then you don't have the cushion to absorb any impact in the future for increases in costs such as utilities and insurance, or decreases in revenues, as when there are more vacancies. So that puts risk onto the bond and the bond buyers.[143] The higher the debt service coverage ratio, the less the risk to bondholders of the obligor defaulting on the debt.[144]

Stifel's draft bond model for the Quad Cities offering (as the last Stifel draft stood on August 21, 2013) showed a debt service coverage ratio of only 1.22 projected for the Series A bonds in 2015, and when the Series A bonds were combined with the subordinated Series B bonds the debt service coverage ratio projected that year for all bonds was only .91.[145] As DeRobbio admitted at the hearing, the .91 debt service coverage ratio of less than 1.0 suggested that the project was not going to generate enough money to cover all the debt service for all the bonds.[146]

Swan explained at the hearing that a change in any of the numbers for gross rent potential, vacancy, or expenses would affect the debt service coverage ratio. As DeRobbio agreed, generally the more revenue a project can generate compared to the debt it carries, the higher the debt service coverage ratio will be. And the lower the expenses of operating the property, the higher the ratio.[147] For example, if the management fee were reduced by some

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[141] Tr. (Swan) 1339.

[142] Tr. (Swan) 1339–40. DeRobbio also testified to the importance of the debt service coverage ratio. Tr. (DeRobbio) 1640.

[143] Tr. (Swan) 1339–40.

[144] Tr. (Swan) 1340–41.

[145] CX-72, at 86.

[146] Tr. (DeRobbio) 948.

[147] Tr. (DeRobbio) 673.

amount, with all other items remaining the same, the debt service coverage ratio would be higher.[148]

DeRobbio agreed in his testimony that the debt service coverage ratio is a critical measure in a municipal underwriting.[149] He said, "You want as high a debt service ratio as possible."[150] When Respondents were invited to underwrite the transaction, De Robbio hoped they could achieve a 1.5 debt service coverage ratio for the Quad Cities bonds.[151]

b. Stifel's Struggle to Obtain Consistent, Reliable Information from BMOC

In doing due diligence, Swan testified that Stifel became "uncomfortable in pursuing the transaction." Swan explained the source of discomfort. "[W]e could not get a good answer as to the number of units and the number of beds available, and that is important as we were building what I call a bond model." He said, "We just could never get a clean understanding or a solid understanding as to what the current cash flow was on that property, and, therefore, we couldn't develop the ability of a covered debt service."[152]

There was documentary evidence of the difficulty Stifel was having in obtaining reliable, consistent numbers. On August 8, 2013, Swan sent an email to Bill L. and others at BMOC, asking for information about occupancy. He copied Eric F., as well as his Stifel colleague, Ernest L. He was specific about the information he required:

> Bill,
>
> I need a detailed financial forecast with occupancy data as we know it now. So in this report I would like the number of signed leases, the number of hot leads, the number of available bed[s], the number of inhabitable beds, and below this the pro forma.[153]

Later the same day, Swan prodded Bill L. and Eric F. again by email, "When are we going to get the numbers from BMOC on Sauk Valley [the Quad Cities dormitory]?"[154] Eric F. sent an email to Becky P. at BMOC and others, including Swan and Ernest L.

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[148] Tr. (DeRobbio) 941.

[149] Tr. (DeRobbio) 671–73, 688, 949–50.

[150] Tr. (DeRobbio) 673.

[151] Tr. (DeRobbio) 670–71, 675, 688, 948–49; CX-71, at 1; JX-15, at 1.

[152] Tr. (Swan) 1337.

[153] RX-50, at 2.

[154] RX-57, at 2.

> We really need to know how many beds we ca[n] actually rent (I think it is 95 beds). And how that projects as well as the number of people we could rent to, if we had more beds.[155]

Swan's analyst, Ernest L., sent an email the evening of August 8 to Becky P. and Swan, with copies to Bill L. and Jason T., highlighting inconsistencies in the information that had been provided to Stifel.[156]

The inconsistent information was important. Swan testified that he "was trying to assemble a reliable bond model . . . and in order to put together a reliable bond model, I needed to understand the number of units and the number of beds and build off that from actual to projected."[157] The occupancy data that Stifel sought included historical information about the number of signed leases. That information would "confirm the known cash flow currently in place. In place cash flow is very pertinent."[158] Swan also had difficulty obtaining the number of "hot leads," meaning the number of students that had demonstrated interest in potentially renting at the dormitory.[159]

Historical financial information would have created a baseline for revenue. Swan explained, "[W]ith the manager telling me how many units are currently occupied, how many they have signed leases for, and what kind of rehab they're going to do to bring the balance of the units online, I could then understand how to ramp up the revenues."[160] He said, "If we're at a fraction of the total beds rented, there is going to be a process of going from a vacancy of 40% to a vacancy of 10%, and I need to connect those two dots by showing that . . . somebody will be doing renovations to those units which will allow for them to be leased, fixing mold and providing furniture, fixture, equipment and other things . . . ."[161] "It's going from actual cash flow available today, to the projected cash flow, and how do those two items connect, on a rehab need and on a signed lease basis."[162]

The following day, August 9, 2013, Swan tried again by email to obtain the information he needed from Bill L. and Eric F.:

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[155] RX-50, at 1.

[156] RX-50, at 1.

[157] Tr. (Swan) 1360.

[158] Tr. (Swan) 1360–61.

[159] Tr. (Swan) 1361.

[160] Tr. (Swan) 1381.

[161] Tr. (Swan) 1381.

[162] Tr. (Swan) 1381–82.

> Here is what I am looking for.
>
> On one page, clean and clear, please list the total available beds (143), the beds currently available, the signed leases, the committed bed[s] from the College (athletes), th[e]n that projected revenue stream, th[e]n the expenses against that number of beds . . . .[163]

After seeking information regarding the revenue stream and operating expenses, Swan also sought to understand the costs of rehabilitation.[164] Swan testified that he asked for the information to be presented "clean and clear" because he was "getting conflicting and confusing data from the manager [BMOC]."[165] He "wasn't certain whether they understood or whether they just were not providing information."[166] In any event, "the result was the same, that we were not getting what we needed."[167]

On August 14, 2013, Swan made another attempt to obtain the information he needed. He sent an email to Eric F. and Bill L. with a draft term sheet. He said that "it would be helpful if we could state truthfully that we are at 95 beds, but if not state exactly where we are (so a current number would be helpful)."[168] He sent this email "[b]ecause the numbers weren't adding up."[169]

At this point, Swan was "losing confidence" in the ability of the Manager of the dormitory—BMOC—to give him correct information.[170] Swan had been a front-line investment banker since 1997, and by 2013 he had been involved in other municipal bond underwritings, including conduit bond transactions. While there were problems with obtaining information in other offerings, he had never had problems "to this magnitude."[171] By August 14, he was contemplating the possibility of withdrawing as an underwriter in the Quad Cities offering.[172]

On the evening of August 14, 2013, Swan made a last attempt to obtain the information he needed from BMOC. He sent an email to Bill L. and Jason T. of BMOC. The format of his request was unusual. He drafted the email with blanks to be filled in. He was feeling frustrated

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[163] RX-57, at 1.

[164] RX-57, at 1.

[165] Tr. (Swan) 1363.

[166] Tr. (Swan) 1364.

[167] Tr. (Swan) 1364.

[168] Tr. (Swan) 1365; CX-77, at 1.

[169] Tr. (Swan) 1365–66.

[170] Tr. (Swan) 1366.

[171] Tr. (Swan) 1367.

[172] Tr. (Swan) 1367.

with BMOC's inability to provide the information he needed.[173] The email reads in full as follows:

> Jason and Bill,
>
> Here is exactly what I want, as of today, the Commons [dormitory] has ___ lease[s] signed, as of today BMOC expects to receive ___ athletes for housing at the Commons.
>
> Currently ___ units are habitable. The inhabitable units require the following: ___ beds (at $XXX/bed), ___ desk and bedroom furniture (at $XXX/desk and bedroom furniture), ___ common space furniture (at $XXX/common space furniture), ___refrigerators (at $XXX/refrigerator), ___ oven/ranges (at $XXX/oven/range), and ___ units needs mold remediation (at $XXXX/unit to remediate).
>
> The schedule for addressing the above will start shortly after closing (within one month) Borrower and Manager will acquire: all (or maybe a portion) of the beds totaling $XXXX; all (or maybe a portion) of the desk and bedroom furniture totaling $XXXX; all (or maybe a portion) of the common space furniture totaling $XXXX; all (or maybe a portion) of the refrigerators totaling $XXXX, and; all (or maybe a portion) of the oven/ranges totaling $XXXX. During the winter recess the Borrower and the Manager will remediate the mold in the ___ units, for a total of $XXXX.[174]

In describing the moment when he sent this email, Swan said, "I am now, yet again, telling the manager how to present back to me what is the current status of the property, and what would have been more comforting would have been if the manager understood my prior questions and delivered, on his own, something similar to this."[175]

At no point after the August 14 email did Swan receive the information he sought.[176]

c. Stifel's Determination Not to Underwrite the Offering

Swan concluded that the transaction "was not suitable for our retail investors" because there was too much risk.[177] The existing cash flow was not enough to cover the debt service on

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[173] Tr. (Swan) 1368–70; RX-66.

[174] RX-66, at 1.

[175] Tr. (Swan) 1369.

[176] Tr. (Swan) 1370.

[177] Tr. (Swan) 1383.

the bonds. The dormitory needed to be rehabilitated to get to the point that additional units could be leased, and there was risk to doing that. He did not want to put that risk into retail hands.[178]

At some point, Stifel asked some institutional investors in a general way whether they would be interested in a bond offering of around $2 million, without going into detail about the Quad Cities offering. The institutional investors were not interested in such a small deal.[179]

Having concluded that the offering was too risky for its retail investors and too small for its institutional investors, Stifel determined that it would not serve as underwriter for the Quad Cities offering.[180]

4. Stifel's September 10, 2013 Notice of Withdrawal from the Underwriting

Swan gave notice of Stifel's withdrawal from the underwriting in a September 10, 2013 email from Swan to Eric F. (Sugar Capital) and his counsel (Attorney Brian M.), Bill L. (BMOC), Steve S. (BMOC and United Housing), and others working on the Quad Cities deal.[181] In his email, he told them that Stifel was going to cancel calls on the deal until further notice. As the reason for cancelling future calls on the transaction, Swan wrote, "[T]here has been a massive amount of redemptions in the bond space . . . the project has been experiencing low occupancy. We need an improved bond market and better occupancy for this deal to be attractive to the potential bond buyer."[182]

In his testimony, Swan explained the meaning of his comments. The comment on redemptions was a way of saying that investors were pulling money out of municipal bonds and deploying it elsewhere such as in cash or equity or treasuries.[183]

The comment on low occupancy was a way of saying that the occupancy rate for the property was lower than Swan had expected, and he was uncomfortable with that. "We wanted to have a particular occupancy level before we wanted to offer this transaction, and we were not realizing that. We were asking the manager to verify the occupancy at a particular level that would give us comfort, and that event was not happening."[184] "We needed that info [on occupancy]," he said, "so that we could properly assess the current cash flow on the property to develop a net operating income and the debt service coverage ratio and the ability to cover debt

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[178] Tr. (Swan) 1383.

[179] Tr. (Swan) 1382–83, 1429–31.

[180] Tr. (Swan) 1336–37; JX-30.

[181] Tr. (Swan) 1336–37; JX-30.

[182] JX-30.

[183] Tr. (Swan) 1346–47.

[184] Tr. (Swan) 1347. Swan meant Bill L. and BMOC when he referred to the manager. Tr. (Swan) 1347.

service."[185] He concluded that the occupancy number was critical to the projections about future financial performance. "You also need that number so that we could have it as a push-off point to project forward."[186]

Swan said he wrote the September 10 email to make sure there was "no detrimental reliance" and "people did not expect that we were moving forward with the transaction."[187] "We wanted to make certain that it was officially stated that we were pulling out of the transaction."[188] "We, at this point, were essentially leaving the transaction because we were uncomfortable with the transaction."[189]

Swan explained that informing the others involved in the offering that Stifel was ceasing all calls was significant. In a typical transaction, Stifel would have weekly conference calls to go through due diligence or the drafting of documents. The developer, the manager, the trustees, and all the lawyers, including bond counsel and trustee's counsel would be on the calls with Stifel. By informing everyone that Stifel was no longer going to hold those calls, Swan said, he was informing them that the underwriting by Stifel was ended.[190]

Swan was asked about a statement in the September 10, 2013 email that could be read to contradict the notion that the September 10 date marked Stifel's withdrawal from the underwriting. In the email Swan had written "As underwriter, we continue to work on finding investors."[191] Swan explained that he was trying to withdraw in a way that would allow Eric F. to find another way to do the deal.

> This e-mail went out to the entire team, and as a courtesy to [Eric F.], I didn't want to say that we were totally abandoning this deal. It's easier for me to give a soft exit and then let him try to figure out things.
>
> We, Stifel, stopped working on this.[192]

Swan said that he wrote the email as a "soft exit" "[s]o that everyone doesn't jump off the ship."[193] As part of the "soft exit," the September 10 email said that Stifel would continue to

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[185] Tr. (Swan) 1348.

[186] Tr. (Swan) 1348.

[187] Tr. (Swan) 1343.

[188] Tr. (Swan) 1343, 1345.

[189] Tr. (Swan) 1343.

[190] Tr. (Swan) 1345–46.

[191] JX-30.

[192] Tr. (Swan) 1425.

[193] Tr. (Swan) 1425.

work on finding investors, but, in fact, Stifel did not continue to work on finding investors for the transaction.[194]

5. October 3, 2013 Identification of Another Firm to Do the Underwriting

Eric F. understood that Stifel was withdrawing from the underwriting. He looked for another firm to do the underwriting, and, when he found another firm that might do it, he told Swan in an October 3, 2013 email.[195] Swan testified,

> Eric came back to me and said, "We found a retail BD." . . . I was accepting and expecting that . . . . So, again, this [September 10 email] was written in a way to have a soft exit, and the way that you would completely tie the knot on this was when Eric said he found a BD, but that was understood between Eric and I, that I was leaving the deal.[196]

6. Eric F.'s Pressure on Swan for Assistance

In the October 3, 2013 email in which Eric F. told Swan that he had found another firm that might do the Quad Cities underwriting, Eric F. also asked Swan to send him the latest draft of the POS and Stifel's bond model. Swan did not know at the time who Eric F. was referring to as the potential underwriter, but the same day he sent both the draft POS and Stifel's August 21, 2013 draft bond model to Eric F.[197] When asked whether it was customary for one underwriter to provide its work product to a successor underwriter, Swan said no.[198] But, he said, Eric F. pressured him to provide assistance:

> Eric said "It would help me out greatly, Jim," and he leaned on me, saying "You messed me up, you aren't doing this deal, I could really use you to help me out here and make sure that I'm going forward with this transaction," so, as a courtesy, I provided that.[199]

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[194] Tr. (Swan) 1346.

[195] CX-72, at 1.

[196] Tr. (Swan) 1425.

[197] Tr. (Swan) 1349–51; CX-72.

[198] Tr. (Swan) 1419–21.

[199] Tr. (Swan) 1428–29.

7. Respondents' Introduction to the Quad Cities Bonds

Attorney Brian M., who was Eric F.'s attorney in the Quad Cities offering, was the person who contacted DeRobbio to inquire whether he and his firm, Cantone Research, would be interested in underwriting the Quad Cities bonds.[200] As noted above, Attorney Brian M. had worked with DeRobbio on other municipal bond offerings.

The morning of October 3, 2013, Eric F. sent four documents related to the offering to Attorney Brian M. The attorney then forwarded the documents to DeRobbio:[201]

- a draft POS (prepared by Stifel, the lawyers, and interested parties);[202]
- portions of the August 21, 2013 Stifel bond model showing projected revenues and expenses, the debt service coverage ratio for the Series A bonds and the subordinated Series B bonds, and the sources and uses of funds;[203]
- an appraisal of the dormitory property as of May 16, 2013 (prepared for Eric F.);[204] and
- an analysis of market potential by Tracy Cross & Associates Inc. ("Cross Associates") dated July 29, 2013 (prepared for Eric F.'s entity, Sugar Capital).[205]

By the afternoon of October 3, DeRobbio was interested in underwriting the bonds. He sent Cantone and Polakoff, the Firm's municipal bond principal, an email attaching the four documents related to the offering, saying, "When you get time peruse this deal. It is mine if I want it . . . ."[206]

The draft POS was unfinished. Information regarding the terms of the offering still needed to be added.[207] DeRobbio agreed that the offering could not be closed using that draft.[208]

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[200] Tr. (DeRobbio) 664, 681.

[201] Tr. (DeRobbio) 664–65, CX-71, at 1.

[202] CX-71, at 9–92.

[203] CX-71, at 91–92.

[204] CX-71, at 93–184.

[205] CX-71, at 185–200.

[206] Stip. ¶¶ 12, 25–26. CX-71, at 1.

[207] The missing information included the maturity date, principal amount, interest rate, and price for the bonds. CX-71, at 11. There were blank spaces for the estimated sources and uses of the funds, as well as information about the debt service requirements year-by-year and the underwriting discount. CX-71, at 64–65.

[208] Tr. (DeRobbio) 675–76; CX-71.

The financial projections in the bond model were discouraging. The debt service coverage ratio for the Series A bonds offering was only 1.22 in 2014 and 1.25 in 2015. As discussed above, Swan had concluded that the debt service coverage ratio at 1.22 was too risky for retail investors. The ratio for both Series A bonds and Series B bonds combined fell below 1.0 until 2019, which meant that the project was not projected to generate enough revenue to pay all bondholders until five or six years after the offering.[209]

The appraisal of the dormitory property and the separate Cross Associates' analysis of market potential were optimistic about how the project *could* perform, but they were vague about the details. There was reason to conduct further due diligence.

The appraisal of the property as of May 16, 2013, noted, for instance, that in April 2013 the dormitory was only 65% occupied and had 36 "offline" beds.[210] The appraisal did not define "offline" and did not indicate whether the 65% occupancy figure included or excluded the "offline" beds. Only 36% of the "rentable" units were pre-leased in May 2013 for the fall term at the College, in comparison to other similar properties that had 84%–100% occupancy for the fall.[211] According to the appraisal, the dormitory had 144 beds, but it did not indicate how many were "rentable."[212] As a result, it was impossible to interpret the percentages, but the overall impression left by the appraisal was that a substantial number of beds/rooms were unoccupied, and, perhaps, unable to be occupied or rented.

Moreover, the appraisal indicated that the pool of potential renters was small. It said that only 180–190 students were out of the district and in potential need of housing.[213]

The Cross Associates analysis of market potential completed on July 29, 2013, separately noted that the dormitory had historically "not been able to achieve stabilized occupancy of 70% or greater."[214] That analysis hinted at some of the problems with improving the dormitory's occupancy rate and revenues. It noted that the dormitory is in a rural area, meaning that students had to drive to obtain shopping, entertainment, and other services they might require. It also said that the dormitory was "susceptible to negative impressions by incoming students and especially their families,"[215] and explained that the dormitory needed improvements, including remediation of "unlivable" units, new furniture, and exterior repairs such as roof work and trim painting.[216] It concluded that the project could achieve 85%–90% occupancy in a few years, but only if a

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[209] CX-71, at 91.

[210] CX-71, at 103.

[211] CX-71, at 103.

[212] CX-71, at 102.

[213] CX-71, at 103.

[214] CX-71, at 198.

[215] JX-18, at 15.

[216] JX-18, at 15.

number of steps were taken to better market and improve the dormitory. The analysis pointedly said:

> Special attention must be given to the various renovations required at [the dormitory]. Specifically, all units should be livable; furniture/appliances must be updated as necessary; and general repairs and maintenance of the buildings must be on-going.[217]

The market analysis also disclosed another discouraging fact. It indicated that enrollment at the College had steadily declined between fall of 2008 and spring of 2013 by roughly 25%.[218] It noted that over 90% of the students at the College lived at home and commuted to school each day.[219] This information suggested that the pool of potential student renters was small and getting smaller.

The next day, on October 4, 2013, DeRobbio faxed to Cantone his recommendation for the terms under which the Firm would propose to do the underwriting. DeRobbio expressed no concern about the vacancy numbers or the debt service coverage ratio.[220] DeRobbio said nothing about any additional due diligence that Respondents would have to do.[221] He was focused on the fact that almost all the work on the offering documents had been completed and Respondents could proceed with selling the bonds almost immediately. He wrote in the fax, "All the counsel work and feasibilities are complete by respected counsel and firms."[222] He noted, "We could close 10-31!"[223] The proposed closing date was less than a month away. At the hearing DeRobbio said, "[I]t came pre-packaged and looked good."[224]

8. Stifel's Continuing Involvement

Although Stifel was no longer the underwriter on the Quad Cities offering, Swan and Ernest L. remained on the distribution list of parties involved in the offering. DeRobbio's October 9, 2013 player's list for the Quad Cities bond offering identified Cantone Research as the underwriter and Stifel as an "advisor" for the transaction. At some point, on his copy of the

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[217] CX-71, at 199.

[218] CX-71, at 193.

[219] CX-71, at 191.

[220] JX-15, at 1.

[221] Tr. (DeRobbio) 690.

[222] JX-15, at 1.

[223] Tr. (DeRobbio) 695–96; JX-15, at 1.

[224] Tr. (DeRobbio) 734.

player's list, DeRobbio struck through the advisor title for Stifel, and wrote the title "structuring agent" beside it.[225] DeRobbio said that structuring agent was the title that Swan wanted to use.[226]

Swan tried to downplay Stifel's involvement in the transaction after Cantone Research became the underwriter, saying that Stifel never agreed to serve as a structuring agent or advisor in connection with the offering.[227] "We were not interested in selling it," he said, "and we didn't feel comfortable having our name on it."[228] He admitted, however, that he and Ernest L. made changes to the bond model pursuant to Eric F.'s instructions after Respondents joined the team. He characterized these actions as a courtesy to Eric F.[229]

9. Respondents' Failure to Conduct Meaningful Due Diligence

DeRobbio worked on the transaction with the goal of closing the offering by the beginning of November, about a month after he received the call from Eric F.'s attorney.[230] This was an accelerated process.

Respondents' due diligence consisted almost entirely of telephone calls with the persons most interested in closing the Quad Cities offering—Eric F., the developer of the project, Eric F.'s attorney, and Bill L., the president of BMOC—and a review of the documents previously prepared by or for them (the appraisal, the market analysis, and an environmental report). Respondents did not verify with any independent third party what the interested parties told them.[231]

DeRobbio's assertion that he performed additional due diligence was not credible. At the hearing, DeRobbio claimed that within the first 24 hours of learning of the deal, between October 3 and October 4, he spoke to the person who prepared the Cross Associates' market analysis, the person responsible for the appraisal, and a lawyer involved in the transaction. He provided no specifics except to say he remembered having lunch with the lawyer. He claimed to have kept detailed notes on his activities, but there is no documentary evidence to corroborate his testimony.[232]

DeRobbio also claimed that in conducting due diligence he spoke to the president of the College. But he misidentified Steve S. as the president of the College. Steve S. was part of

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[225] Tr. (DeRobbio) 757–59; RX-112, at 1.

[226] Tr. (DeRobbio) 758–59.

[227] Tr. (Swan) 1374–75.

[228] Tr. (Swan) 1380.

[229] Tr. (Swan) 1372–73.

[230] JX-22, at 2.

[231] Tr. (DeRobbio) 741–46, 753; CX-75; at 6–7, ¶¶ 16–22; CX-87, at 1–2.

[232] Tr. (DeRobbio) 510, 691, 694, 1270–73.

BMOC's management and the executive director of United Housing, the borrower's sole member. Steve S. was the person who signed the Quad Cities OS on behalf of Sauk Valley Housing and United Housing.[233] There is no documentary evidence to corroborate DeRobbio's testimony about talking to a representative of the College prior to the closing of the offering. DeRobbio testified vaguely about having destroyed his due diligence notes.[234]

In fact, DeRobbio's hearing testimony is inconsistent with other evidence. DeRobbio prepared a timeline for the Bondholder Litigation that Cantone Research later filed on behalf of bondholders after the Quad Cities offering failed. DeRobbio indicated on the timeline that Respondents had their first call with someone at the College on June 2, 2015, more than a year after the offering closed.[235] And, in an affidavit filed in support of the Bondholder Litigation, DeRobbio claimed that Respondents first learned of a history of serious problems between the dormitory and the College from a lawyer for the College in late October 2015.[236]

In his OTR testimony, DeRobbio admitted that he did not conduct due diligence beyond that already done by Stifel. In that testimony, which we find more credible than his hearing testimony, DeRobbio said that he reviewed information in the draft POS he received, accepted it as it was stated, and did not conduct any additional due diligence prior to the offering.[237]

10. Stifel's Exit from the Transaction Without Compensation

At some point, Stifel stopped playing any role in the offering. It is not clear exactly when that occurred. DeRobbio's handwritten notes on his October 9 player's list indicated that Swan was out of the transaction "A/O", or as of, October 13, 2013.[238] But Ernest L. provided a revised draft bond model with financial projections to Eric F. by email a few days after that, on October 18,[239] and Eric F. forwarded that draft to Respondent Anthony Cantone. Cantone then sent it to DeRobbio and Maryann Cantone.[240]

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[233] Tr. (DeRobbio) 977–83, 1275–76; JX-3, at 76; CX-71, at 52 (the portion of the POS explaining Steve S.'s background). The president of the College was identified by name in the POS for the Quad Cities offering as someone different. His name was not one easily confused with Steve S.'s name. CX-71, at 53.

[234] Tr. (DeRobbio) 1272–75.

[235] Tr. (DeRobbio) 748–49; CX-87.

[236] CX-75, at 21–22, ¶¶ 61–65. DeRobbio testified that leading up to the offering there "had to be almost daily calls with the principals of the [C]ollege." Tr. (DeRobbio) 1272. But Respondents were not involved in those calls. They received reports from someone else on the calls. "[I]t was reported to us that, you know, relations [with the College] were never better." Tr. (DeRobbio) 1272.

[237] Tr. (DeRobbio) 739–40.

[238] Tr. (DeRobbio) 759.

[239] JX-23.

[240] JX-23.

On October 23, 2013, Swan informed his boss, Peter C., by email that Stifel would not be on the cover of the OS or listed anywhere else in the OS. But Swan also told his boss that he had asked the developer (meaning Eric F.) for a "point" as a fee for all the work they had done on the transaction.[241] On October 25, Swan seemed to contradict himself. He sent his boss another email saying that Stifel would appear on the OS as "Structuring Agent" for the transaction.[242]

The Bondholder Litigation Cantone filed after the Quad Cities bond offering defaulted alleges that Stifel suddenly withdrew from the offering completely without any explanation to Cantone Research and without any compensation from the proceeds of the offering on October 28, 2013.[243] The closing deadline had to be extended as a result. Originally, the plan was to close at the end of October or very beginning of November. In the end, it closed on November 7, 2013.[244]

In the affidavit DeRobbio submitted in support of the Bondholder Litigation, he said that he called Swan at Stifel several times to learn more about Stifel's abrupt exit, but Swan did not return the calls.[245] DeRobbio did not pursue the inquiry[246] even though he admitted at the hearing that it was "odd" and outside the norm to work on an offering and then withdraw without taking any fee.[247]

Despite Stifel's unexplained exit from the transaction without receiving any compensation, Respondents proceeded with the underwriting. There is no evidence that Respondents investigated beyond DeRobbio's fruitless telephone calls to Swan to ascertain Stifel's reasons for walking away from the transaction without compensation after months of work.

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[241] RX-104.

[242] RX-107.

[243] CX-75, at 8, ¶ 26; CX-85, at 13, ¶ 79.

[244] RX-100, at 1; CX-85, at 13, ¶ 82.

[245] Tr. (DeRobbio) 759–62.

[246] Tr. (DeRobbio) 760–62.

[247] Tr. (DeRobbio) 755; CX-85, at 18 ¶ 79. DeRobbio testified that Stifel had worked on the deal for seven months. Tr. (DeRobbio) 1270.

11. Marketing of the 2013 Quad Cities Bonds and the Closing of the Offering

On October 24, 2013, Attorney Brian M. completed the POS, and the Firm began marketing the Quad Cities bonds to its retail customers.[248] This was about three weeks from the time that Respondents first learned of the opportunity to underwrite the bonds. As DeRobbio acknowledged, once the Firm and its representatives began recommending that customers invest in the offering, the Firm should have finished its due diligence and should have had a reasonable basis for making the recommendation.[249]

Attorney Brian M. filed the POS on the MSRB's Electronic Municipal Market Access database ("EMMA")[250] on October 29, 2013. The final OS was completed and delivered to the parties to the transaction on November 1.[251] Cantone Research delivered the OS to customers who were prospective investors.[252] The OS was filed on EMMA on November 4, 2013,[253] and the offering closed on November 7, 2013.[254] It was fully subscribed.[255]

There was no mention of Stifel in the OS, and DeRobbio did not tell his customers that Stifel had once been involved and then pulled out.[256] In the Bondholder Litigation the Firm filed after the Quad Cities bonds defaulted, however, Respondents claimed that they had relied on the work that had already been done by others before Respondents became involved in the transaction, and on Stifel's relationship with the other parties to the offering.[257] None of that, however, was mentioned in the disclosure documents given to investors when they purchased the bonds.

12. Chronology of Changes to Debt Service Coverage Ratio and Management Fee in the Financial Projections

During the month of October, the calculation of the debt service coverage ratio in the draft financial projections for the 2013 Quad Cities offering fluctuated. As noted above, Stifel had calculated a ratio of 1.22, and Swan had thought it inadequate. Once Respondents stepped

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[248] Tr. (DeRobbio) 634, 695–97; CX-75, at 8, ¶ 24; Stip. ¶ 33.

[249] Tr. (DeRobbio) 698–99.

[250] EMMA is a database widely used by professionals in the municipal securities market. The database contains municipal bond filings by municipalities throughout the United States. EMMA provides the relevant documentation, official statements, and disclosures related to municipal bond offerings. Tr. (Moy) 600–01.

[251] CX-75, at 8, ¶ 27.

[252] CX-75, at 8, ¶ 27.

[253] Tr. (Moy) 142; JX-3.

[254] CX-75, at 9, ¶ 28.

[255] Tr. (DeRobbio) 969.

[256] Tr. (DeRobbio) 761–63.

[257] CX-75, at 5–6, ¶¶ 14–15.

into the underwriter role, however, the draft financial projections used various higher debt service coverage ratios. As detailed below, the management fee to be paid to BMOC was constant until October 18, when the draft financial projections circulated by email among the interested parties slashed the 2014 management fee to less than half of what it was in earlier drafts. The decrease in the management fee contributed to a favorable increase in the debt service coverage ratio in that draft of the financial projections.

a. October 3, 2013

On October 3, 2013, Swan sent Eric F. the latest draft of the Stifel pro forma, the August 21, 2013 draft. It showed the following:

- Management fee = $38,400 for both 2014 and 2015.
- Debt service coverage ratio = 1.22 for Series A in 2015.[258]

The ratio was projected to increase each succeeding year and reach 1.49 in 2024. When both the Series A and Series B (subordinated) bonds were combined, however, the debt coverage ratio for 2015 was only 0.91, which was not enough to pay the debt service on all the bonds. The ratio for all the bonds was not projected to reach 1.0 until 2019, six years after the offering. By 2024, the debt service coverage ratio for all bonds was projected to reach 1.11.[259]

b. October 9, 2013

On October 9, 2013, Swan emailed DeRobbio a copy of the Cross Associates market analysis of the dormitory completed in July. The market analysis was accompanied by a pro forma with financial projections for the offering. The cover of the pro forma was clearly labeled as prepared by BMOC and independent of the market analysis prepared by Cross Associates.[260]

The pro forma attached to this email was undated,[261] so it is unclear whether BMOC created it in July, around the same time as the market analysis, or some other time, such as early

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[258] CX-72, at 85.

[259] CX-72, at 86. As noted above, DeRobbio admitted at the hearing, a debt service coverage ratio of less than one—like the one for both the Series A and Series B bonds in Stifel's August 21, 2013 pro forma—suggests that a project will not generate enough money to cover all the debt service for all the bonds. Tr. (DeRobbio) 948. DeRobbio claimed that it did not matter to him that there was not enough money to cover the debt owed to the subordinated bonds because his customers, who bought the Series A bonds and had priority, were covered. Tr. (DeRobbio) 946–48. This unthinking statement reveals DeRobbio's lack of care regarding the overall soundness of the investment. A ratio below 1.0 for all bonds for six years suggests that the project as a whole was unsustainable. The fact that the projections showed that revenues would not cover all the payments due to the subordinated bonds for six years also should have cast some doubt on Eric F.'s claim that he intended to rely only on payments from the subordinated Series B bonds for his profit. *See supra* at 25–26.

[260] JX-18, at 19.

[261] JX-18, at 19.

October, after Respondents took on the role of underwriter. The debt service coverage ratio in this pro forma was substantially higher than in Stifel's August 21, 2013 pro forma that DeRobbio initially received.

- Management fee = $38,400 for both 2014 and 2015.[262]
- Debt service coverage ratio = 1.41 for Series A in 2015.

The ratio was projected to increase each succeeding year, reaching 1.51 in 2018 and 1.69 in 2024. When both the Series A and Series B bonds were combined, the debt coverage ratio for 2015 was 1.00. By 2024, the debt service coverage ratio for all bonds was projected to reach 1.20.[263]

c. October 10, 2013

On October 10, 2013, Eric F. sent DeRobbio an email attaching a draft of the bond model.[264] The debt service coverage ratio was still different.

- Management fee = $38,400 for both 2014 and 2015.
- Debt service coverage ratio = 1.33 for Series A in 2015.[265]

The ratio was projected to reach 2.05 by 2024. When both the Series A and Series B bonds were combined, the debt service coverage ratio was projected to range between 1.0 and 1.03 from 2015 through 2024.[266]

d. October 11–15, 2013

In mid-October, Ernest L., the analyst at Stifel who ran the numbers, was still revising the bond model and circulating it to the persons involved in the Quad Cities transaction. On October 11, 2013, he sent a revised bond model to Eric F., Swan, and Attorney Vincent M. (underwriter's counsel) as an attachment to an email.[267] Attorney Vincent M. forwarded a revised bond model to DeRobbio on October 15.[268]

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[262] JX-18, at 20.

[263] JX-18, at 20.

[264] JX-19.

[265] JX-19, at 3.

[266] JX-19, at 3.

[267] JX-22, at 3.

[268] JX-22, at 2.

At that point, the parties were planning to close the offering within two weeks. Eric F. sent Ernest L. an email telling him that they aimed to close by October 31.[269] DeRobbio sent Attorney Vincent M. an email saying, "[t]rying to close as close to November first as possible."[270]

e. October 18, 2013

Attached to an October 18, 2013 email, Ernest L. sent yet another revised bond model to Eric F., copying Swan. Eric F. sent the revised bond model to Anthony Cantone that same day. And later that day, Cantone sent the revised bond model to DeRobbio with the message, "They corrected the error that I found and discussed with you this morning in the attached."[271]

It is unclear what the error was that Cantone had identified, but this draft of the bond model used a lower management fee than any of the prior drafts of the bond model. In this draft, the management fee for 2014 was $14,928, and for 2015 was $23,757. Through 2026, the management fee was projected to be no higher than $29,539.[272] In all the earlier drafts, as noted above, the management fee was $38,400 for both 2014 and 2015, and then it rose slowly year by year after that. According to Swan, it was Eric F., the developer of the project, who directed that the management fee be set lower.[273]

Ernest L. wrote in his October 18 cover email that the management fee in the attached bond model was calculated as 6% of effective income generated by the dormitory, with 4% senior to the Series A bonds and 2% subordinate.[274]

The debt service coverage ratio was higher in this October 18 draft (1.39) than in the Stifel draft Swan sent to Eric F. on October 3 (1.22). Presumably, the lower management fee contributed to the calculation of a higher debt service coverage ratio.

To summarize, the October 18 draft contained the following projections:

- Management fee = $14,928 for 2014 and $23,757 for 2015.
- Debt service coverage ratio = 1.39 for Series A in 2015.

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[269] RX-100, at 1.

[270] JX-22, at 2.

[271] JX-23, at 1.

[272] Tr. (Moy) 128–138; JX-23, at 4; CX-4R. Moy, the FINRA analyst who testified, believed that Cantone was responsible for the change in the management fee because that was the only number that Moy identified as different from earlier drafts. Tr. (Moy) 153.

[273] Tr. (Swan) 1371–73; JX-23, at 1.

[274] JX-23, at 1.

The ratio was projected to increase each year and reach 1.50 in 2019 and 2.09 by 2024. Unlike earlier drafts, this set of financial projections did not show the debt service coverage ratio when the Series A and Series B bonds were combined.[275]

At this point, the projections for the management fee and debt service coverage ratio were inconsistent and confusing. Whatever the correct debt service coverage ratio was, it was important to investors and the inconsistencies should have been resolved so that accurate figures could be presented to investors.

f. November 4, 2013

As noted above, after Stifel's exit from the transaction, Cantone Research filed the OS with EMMA on November 4, 2013.[276] This document was given to investors.[277] Instead of clarifying and resolving the issues with the debt service coverage ratio, Respondents removed information from the forecasts and made the disclosures more opaque and misleading.

With respect to the debt service coverage ratio, the OS disclosed minimal information. It provided a number for debt service coverage ratio for a few years in the narrative body of the document without indicating whether the ratio applied to the Series A bonds only or both the Series A and Series B (subordinated) bonds. And it did not provide any of the underlying data from which the ratio was calculated. The OS said the following:[278]

Selected Forecasted Financial Data

1. Debt Service Coverage Ratio

	December 31 of each year				
Debt Service Coverage Ratio including all rents available to the borrower	2014	2015	2016	2017	2018
	---	1.33	1.34	1.39	1.41

Source: Manager and Borrower

[275] JX-23. Inexplicably, the ratio that accompanied the Cross Associates market analysis Swan sent DeRobbio on October 9 was higher (1.41) even though the management fee was the same as in the Stifel August 21 draft, $38,400 per year for 2014 and 2015. JX-18, at 20.

[276] *See supra* at 44. Tr. (Moy) 142; JX-3.

[277] CX-75, at 8, ¶ 27.

[278] JX-3, at 12.

The OS did not explain what rents might be "available" to the borrower or how the debt service coverage ratio was calculated. For more information, it referred the reader to "the entire MARKET STUDY AND FINANCIAL PROJECTIONS OF THE PROJECT, included herein as APPENDIX A."[279]

Cantone Research did not file any of the appendices, including the market analysis, on EMMA but it did send the appendices along with the OS to customers via email.[280] Appendix A contained two parts. The first was the Cross Associates market analysis completed at the end of July 2013. The second was a set of pro forma financial projections.[281]

The financial projections attached to the market analysis and sent to customers as Appendix A of the OS were different from the earlier drafts in significant ways.

First, the final financial projections attached to the Cross Associates market analysis and distributed to customers contained *no* debt service coverage ratio.[282] As a result, the only information that customers received regarding that ratio was the minimal information in the narrative body of the OS. It would be difficult if not impossible for an investor to understand how the figures in the narrative related to the figures in the financial projections. Respondents used a set of disclosure documents that conveyed far less information than any of the draft financial projections that the parties had previously exchanged among themselves.

Second, the management fee in the final financial projections was not calculated accurately.[283] The management fee as set forth in the November 1, 2013 management agreement had two components: $2,642 per month fixed fee and an additional 1.6 % of gross revenue (but not to be more than the fixed fee component). The fixed monthly component was $2,642 times 12 months, or $31,704 (before adding some percentage of gross revenue).[284] But investors were told in the final financial projections that starting in 2014 the management fee would be $14,982, a much lower figure than the management fee specified by the management contract.[285] The management fee in the final financial projections did not even meet the fixed fee component of the management fee as provided in the contract.[286]

The difference was significant. The FINRA analyst who testified, Moy, calculated that over the life of the Quad Cities bonds (2014-2043), payments to the Manager pursuant to the

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[279] JX-3, at 12.

[280] Tr. (Moy) 141.

[281] Tr. (Moy) 144; JX-4.

[282] Tr. (Moy) 144–45; JX-4, at 20–23.

[283] Tr. (Moy) 142–44, 148, 164; JX-3 at 49; JX-4.

[284] JX-11, at 8.

[285] JX-4, at 20; JX-11, at 8; CX-139, at 12.

[286] Tr. (Moy) 148.

contract would amount to $1,436,091. But working with the final financial projections distributed to customers, Moy calculated that the management fees would total only $936,525. Thus, under the contract, the management expenses would be $499,566 greater, or almost 50% greater, than the Firm told investors they would be.[287] Actual management fees paid were far closer to the calculation in the management fee agreement.[288]

Third, information identifying the source of the financial projections—BMOC—was removed from the final financial projections included in Appendix A with the Cross Associates market study. The draft market analysis DeRobbio received from Swan on October 9 had plainly identified BMOC as the source of the financial projections. In that draft, a page following the end of the Cross Associates market analysis was labeled "Appendix Table 1." The same page described the financial projections that came after it as a pro forma "Prepared by BMOC, Inc." and stated that the projections were "(Independent of the Market Analysis)."[289] In contrast, the version of the market analysis and financial projections provided to customers in Appendix A did not identify BMOC as the source of the financial projections. A slip sheet between the market analysis and the financial projections said only "Financial Projections,"[290] without making it clear that BMOC had created the projections. The slip sheet ambiguously left the impression that the financial projections may have been created independently by Cross Associates instead of a party interested in the transaction.[291] Removing the information identifying the source of the projections from Appendix A made it more difficult for investors to evaluate the information they received.

In the Bondholder Litigation Cantone filed after the offering failed, Respondents alleged with respect to occupancy figures and debt service coverage that "the POS and OS [for the Quad Cities offering] contain misleading information and omission of material information necessary to make the disclosure in the POS and OS not misleading."[292] We agree. The POS and OS were misleading and evidently designed to be obscure.

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[287] Tr. (Moy) 131–38; CX-4R. The management agreement that was sent to customers was not signed, which Moy thought odd. It was dated November 1, 2013. Tr. (Moy) 140–41; JX-11, at 8, 13–14.

[288] Tr. (Moy) 160; CX-7. In an OTR, Anthony Cantone first claimed that the difference between the figures for the management expense was not material. Then he asserted that the fees were different because the management contract was in the process of being renegotiated. But the documents provided in response to a Rule 8210 request showed that the management fee was never renegotiated. Tr. (Moy) 154–65; CX-138; CX-139; JX-11.

[289] JX-18, at 19.

[290] JX-4, at 19.

[291] While the OS did vaguely disclose in the narrative body that the financial projections were prepared by the "Manager," "Current Mortgage Holder," and the "Borrower," it did so without identifying BMOC by name and it buried the information in a discussion of the Cross Associates market analysis. JX-3, at 53.

[292] Tr. (DeRobbio) 723–34; CX-85, 16–17 ¶¶ 98–99.

13. Sales to Customers

Approximately 60 Cantone Research customers invested in the Quad Cities bonds, either in the offering or on the secondary market. FINRA analyst Moy determined that about 40 of them were 65 years old or older when they purchased the bonds. Moy used the term "approximately" when speaking of the number of customers because certain customers had multiple accounts.[293] Moy testified that in his experience this was "one of the quickest turnarounds [he had] ever seen in closing a bond [offering]."[294]

14. Failure of the Quad Cities Bond Offering

About a year after the Quad Cities offering closed, on November 5, 2014, the trustee gave bondholders notice on EMMA that there were insufficient funds in the debt service account to cover the interest that was due to be paid on November 3, 2014. Accordingly, the trustee announced that it had taken funds out of the debt service reserve fund to make up the shortfall.[295] As DeRobbio admitted, the debt service reserve fund was supposed to be an emergency fund if dormitory revenues fell short.[296] The November 5 notice meant that the dormitory was not generating enough revenues to pay bondholders.[297]

About a year later, on November 10, 2015, the trustee issued a notice of default on the Quad Cities bonds, which was filed on EMMA. In that notice, the trustee said that it had previously notified bondholders that it would not pay the interest due them on November 1, 2015.[298] The trustee could not pay the bondholders because the debt service reserve fund was already empty.[299] Evidently, the dormitory had been generating so little revenue that the emergency fund was exhausted by the second year after the offering.

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[293] Tr. (Moy) 95–96, 223, 239–40; CX-1.

[294] Tr. (Moy) 120.

[295] Tr. (DeRobbio) 701; JX-42. The notice informed bondholders that $92,250 was due on November 3, and the trustee had drawn $18,909.99 from the emergency reserve to make the full payment of interest due. JX-42.

[296] Tr. (DeRobbio) 699–700.

[297] Tr. (DeRobbio) 701. In fact, FINRA's analyst found in reviewing the dormitory's post-closing financials on EMMA that the dormitory had a negative net income in 2014 of $114,015. Tr. (Moy) 161–62; CX-07.

[298] JX-43.

[299] Tr. (DeRobbio) 700; JX-43.

15. Bondholder Litigation Claiming that Respondents Were Deceived by Parties to the Transaction

After the Quad Cities bonds defaulted in November 2015, Anthony Cantone organized and funded the Bondholder Litigation against many of the other participants in the offering. Cantone's Firm was neither a defendant nor a plaintiff, despite its central role in the offering as the sole underwriter.[300]

Cantone filed the complaint in the Bondholder Litigation in federal district court in New Jersey on September 21, 2017.[301] In general, that complaint alleged that the parties to the Quad Cities offering (Eric F., Bill L., Steve S., and their various entities (Sugar Capital, BMOC, Sauk Housing, and United Housing)) failed to disclose material information to Cantone Research and engaged in a variety of wrongdoing. Although the Bondholder Litigation purported to be brought on behalf of investors in the Quad Cities offering, the complaint focused on how the other parties to the Quad Cities offering had misled and deceived Respondents. The complaint contained no hint that Respondents had any responsibility for investors' losses.[302]

The Bondholder Litigation anticipated many of the arguments Respondents now make in their defense to this disciplinary proceeding. Respondents' overarching theme in the Bondholder Litigation was that they relied on others in connection with the Quad Cities bonds, and those other persons deceived Respondents. On that basis, Respondents claim here that they are not responsible for any problems with disclosures to investors. DeRobbio testified, "[W]e were duped, that is what I believe."[303] "[W]e were misled as a firm and by the parties to the transaction."[304] There was "deception," and there were "discrepancies" in the materials provided to the Firm.[305]

In support of the Bondholder Litigation, DeRobbio provided an affidavit identifying specific instances of other parties' alleged failures to disclose material information to DeRobbio and the Firm.[306] In his affidavit, he identified the following items of material information (among others) that Respondents allegedly did not know at the time of the Quad Cities offering:

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[300] Tr. (Moy) 108–09; Tr. (DeRobbio) 712–14; CX-85.

[301] Tr. (Moy) 108–11; Tr. (DeRobbio) 703–04; CX-85.

[302] Tr. (DeRobbio) 713; CX-85.

[303] Tr. (DeRobbio) 725.

[304] Tr. (DeRobbio) 725.

[305] Tr. (DeRobbio) 728–29.

[306] Tr. (DeRobbio) 705–07; CX-75.

- BMOC did not disclose to DeRobbio or the Firm that BMOC had managed the dormitory before and after the 2011 bankruptcy.[307]

- BMOC represented that it had good relations with the College, when, in fact, the College had threatened to terminate an affiliation agreement with the dormitory.[308] The complaint in the Bondholder Litigation asserted that the POS and OS "failed to disclose the true state of the tumultuous relationship between the college and [the dormitory] over the management and operation of the project."[309] According to DeRobbio's affidavit, it was only in October 2015 that Respondents learned of problems between BMOC and the College. That was when an attorney for the College spoke with DeRobbio and Polakoff and told them that the College "had a long history of problems with the Project and its management, dating from before the Offering." The attorney told them that the problems included "bad management, residence by persons other than College students, crime, drug use, alleged sexual exploitation of female students by the BMOC resident manager and failure to pay water and sewer bills to the College."[310]

- Cantone Research was unaware of the dormitory's dependence upon the College for water and sewer service until late October 2015.[311]

- The financial information was "limited by substantial hedging language."[312] The financial forecasts in the POS and OS failed to disclose that they were based on a "radical change" in the relationship between the dormitory and the College.[313]

If Respondents did not know these facts before the offering, it was only because they did not perform adequate due diligence. Respondents would have known that BMOC had been the Manager of the dormitory before the 2011 bankruptcy if they had looked at the Sauk Valley Housing bankruptcy file. And from the bankruptcy file they also would have learned that Sauk Valley Housing was not paying its water and sewer bills and owed the College $62,000. Furthermore, if Respondents had contacted the College directly to investigate the dormitory's failure to pay what it owed the College, they would have gained a more accurate understanding of the problems and the College's reluctance to assist in marketing the dormitory to its students. The bankruptcy filing also revealed that revenues from dormitory rentals had been declining,

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[307] CX-75, at 5, ¶ 13.

[308] Tr. (DeRobbio) 719–20; CX-75, at 7, ¶ 21, 10 ¶¶ 30–32.

[309] Tr. (DeRobbio) 719–20; CX-85, at 14–15, ¶ 88.

[310] CX-75, at 21, ¶ 63.

[311] CX-75, at 21, ¶ 64

[312] Tr. (DeRobbio) 832; CX-75, at 10, ¶ 32.

[313] Tr. (DeRobbio) 832–33.

which would have cast doubt on the optimistic projections BMOC provided for the new offering in 2013.

DeRobbio's affidavit in the Bondholder Litigation also alleged other failures to disclose material information to him and Cantone Research:

- The projected financial results in the POS and OS were based on "assumptions that have no basis in reality or the prior performance of the Project."[314]

- The POS and OS statements about "offline units" are written so vaguely that occupancy figures are "difficult, if not impossible, to decipher," and "a reader has no inkling" as to whether the debt service coverage ratio assumes the "offline units" to be back in service or not.[315]

It should have been obvious to Respondents from the outset that the POS and OS discussion of occupancy and historical performance were not well-grounded. The Cross Associates market study they received in early October 2013 said that the dormitory had never achieved a stabilized occupancy rate of more than 70%.[316] Even within the OS, statements about the number of leases signed and the number of habitable beds showed that at the time of closing the occupancy rate was less than 70%. At that time, signed leases represented no more than 40% to 57% occupancy (depending on how many beds were considered habitable). That meant that from the beginning there was a large gap between the projections in the market study and the actual occupancy rate.[317]

The Cross Associates market study done in July projected that 80-plus leases would be signed by August 2013. But, as of October 3, 2013, in fact only 44 leases had been signed. DeRobbio agreed that this short fall in signed leases was an apparent red flag.[318] Enforcement asked, "Wouldn't you agree that the fact the dorm is not meeting its projections with respect to occupancy calls into question the suitability of this deal for your investors?" He responded, "If I realized it, it would have."[319]

Respondents also knew from the outset that the POS and OS were written too vaguely to know the basis for the occupancy rate and debt service coverage ratio calculations. Prior to the offering, they could have—and should have—insisted on a clear statement of the number of "habitable" beds, expected occupancy rate for those beds, and expected revenues from those

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[314] CX-75, at 11, ¶ 33.

[315] CX-75, at 11, ¶ 34.

[316] CX-71, at 189.

[317] Tr. (DeRobbio) 874–78; JX-3, at 49.

[318] Tr. (DeRobbio) 884–86.

[319] Tr. (DeRobbio) 886.

beds. They also should have clarified issues related to the correct management fee expense and debt service coverage ratio.

Instead of nailing down precise occupancy figures, Respondents went ahead with the Quad Cities offering. They did so despite a lack of clarity about how many beds were "offline" or "uninhabitable" and how historical occupancy had been calculated. DeRobbio testified at the hearing that the language in the OS regarding offline units and offline beds "or what have you" was not clear.[320] He said at the time he was talking with the parties about structuring the Quad Cities offering he was trying to understand the occupancy figures. But, in the end, he agreed that the disclosures in the OS regarding occupancy were "convoluted." "I would agree because I personally don't understand . . . ."[321] At the time the Quad Cities offering closed, DeRobbio said he had a "slight understanding" but not a "concrete understanding" of the number of beds or units that were unavailable at the dormitory to be rented.[322]

16. DeRobbio's Effort to "Augment" his Due Diligence File

Remarkably, in 2019—after the Quad Cities offering closed in late 2013 and defaulted in 2015, and after Cantone Research filed the Bondholder Litigation in 2017—DeRobbio called Swan and asked him for Stifel's due diligence file for the Quad Cities offering. DeRobbio was specifically interested in Stifel's site visit to the dormitory. He told Swan that he would like to have the information to "augment" his files.[323]

Swan testified that he had maintained a due diligence file with his and Ernest L.'s work but he declined to provide Stifel's work to DeRobbio. The conversation made him uncomfortable. About a month before the call from DeRobbio, FINRA staff had contacted Swan regarding Stifel's role in the Quad Cities offering.[324]

By 2019, when DeRobbio made his request for Stifel's due diligence file, Respondents knew that FINRA was investigating their actions in connection with the Quad Cities offering, because it had sent them FINRA Rule 8210 requests about it.[325] And DeRobbio gave OTR testimony about the offering around the same time that he requested Stifel's file.[326]

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[320] Tr. (DeRobbio) 863.

[321] Tr. (DeRobbio) 862.

[322] Tr. (DeRobbio) 870–71. In his OTR, DeRobbio admitted that at the time of closing on the Quad Cities offering he had no true sense of the number of beds or units that were "offline." Tr. (DeRobbio) 871–72; CX-201.

[323] Tr. (Swan) 1385–87.

[324] Tr. (Swan) 1385–87.

[325] CX-136 (Mar. 4, 2019 FINRA Rule 8210 Request); CX-138 (June 18, 2019 FINRA Rule 8210 Request).

[326] Tr. (DeRobbio) 754–55.

We turn now to the other municipal bond offering charged in this case.

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F. The Montgomery 2015 Municipal Bond Offering

Cantone Research was the sole underwriter for another unrelated municipal bond offering referred to here as the Montgomery 2015 offering. Although the Montgomery 2015 offering was separate from the Quad Cities offering and unrelated to it, the two offerings together reveal a pattern at Cantone Research of opaque disclosures that misrepresented and concealed material information from investors.

Respondents sold a little over $6 million in bonds in the Montgomery 2015 offering, which closed May 29, 2015. The proceeds were supposed to be used to acquire, rehabilitate, and operate a defunct assisted-living facility in Montgomery, Alabama.[327] As disclosed in the OS for the Montgomery 2015 offering, the 61-bed facility had been closed since the end of June 2013 because of deficiencies that Alabama authorities had noted in an inspection report.[328] The facility never reopened.[329] Consequently, even though a substantial sum was raised in the Montgomery 2015 bond offering for the ostensible purpose of reviving the facility, the facility failed to generate any revenues and could not pay bond investors what they were owed.

In connection with the Montgomery 2015 offering, the Complaint charges Respondents with fraudulent violations of MSRB Rule G-17, the fair dealing rule, and MSRB Rule G-47, the rule requiring accurate disclosure of all material information at or before the time of sale, along with Securities Act Section 17(a)(1). The Complaint further charges that these violations were willful.

In connection with the Montgomery 2015 offering, Respondents were familiar with the assisted-living facility that was the subject of the Montgomery 2015 offering from two prior securities offerings underwritten by the Firm and they had previously worked with the attorneys and interested parties involved in the transaction. Respondents cannot—and do not—claim that they were misled by anyone about the facility's previous poor financial performance. Instead, as discussed below, they concealed that poor financial performance by using funds from the Montgomery 2015 offering to pay investors in the earlier offerings. They also concealed from investors in the Montgomery 2015 offering that the person to whom they were lending their money had a criminal background related to his mismanagement of such assisted-living facilities.

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[327] Tr. (DeRobbio) 990–91; JX-51, at 1.

[328] Tr. (DeRobbio) 990; JX-51, at 7, 38.

[329] Tr. (Moy) 225; Tr. (DeRobbio) 1011–12; Stip. ¶ 84.

1. Relevant Events Prior to Montgomery 2015 Offering

a. Montgomery 2004 Municipal Bond Offering

In 2004, Cantone Research was the underwriter for a $1,725,000 municipal bond offering related to the same assisted-living facility in Montgomery, Alabama, as the Montgomery 2015 bond offering.[330] The project funded by the 2004 offering was referred to as "the Cedala, LLC project,"[331] because the lessee/borrower in the Montgomery 2004 offering was Cedala, LLC ("Cedala"), a company owned and operated by Christopher Brogdon and his wife. Christopher Brogdon signed and approved the 2004 OS for the offering.[332]

The governmental entity that issued the Montgomery 2004 municipal bonds was the Medical Clinic Board of the City of Montgomery–Southside ("Montgomery Southside").[333] It represented in the OS that it was required under state law to hold title to the facility and to lease it to the lessee.[334] The lessee, Cedala, was the conduit borrower and, through an affiliated entity, was to be the manager and operator of the facility. According to the 2004 OS, the Brogdon entity, Cedala, had purchased the facility in June 2004 for $1 million, and the governmental entity issuing the bonds planned to purchase title from Cedala for $1.3 million, using some of the proceeds of the offering.[335] In this manner, Brogdon's entity, the lessee/borrower, Cedala, made a $300,000 profit immediately after the offering closed.

The OS for the 2004 offering reported that an appraisal of the facility had been completed and would be available upon request at the offices of the underwriter, Cantone Research. The OS did not identify the firm that performed the appraisal. According to the OS, the appraisal gave the facility an estimated value of $2.5 million (both "as is" and "as stabilized") as of the date March 8, 2004.[336] The credibility of that appraisal was somewhat undercut by the disclosure that the lessee/borrower had been able to purchase the facility a few months after the appraisal date for $1 million, which was less than half the appraised value. But Respondents did not make it easy for potential investors to evaluate the appraisal because they did not provide it to an investor unless the investor requested it. In fact, the record contains no copy of the appraisal.

The OS for the Montgomery 2004 offering disclosed that the assisted-living facility was 64% occupied as of July 1, 2004.[337] Elsewhere in the OS, the "current" occupancy was disclosed

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[330] JX-52, at 1, 7, 15.

[331] JX-52, at 1.

[332] JX-52, at 13, 41.

[333] JX-52, at 1, 4.

[334] JX-52, at 80.

[335] JX-52, at 7.

[336] JX-52, at 17.

[337] JX-52, at 21.

to be even lower, 59% or 36 beds.[338] Financial projections for the offering, however, were based on the assumption that the facility would be 72% occupied during the 12-month period ending June 30, 2005, and 93% occupied after that. Based on those assumptions, the OS forecasted a debt service coverage ratio of 1.25 in 2005, the first year after the offering, and 2.08 in 2006, the second year after the offering.[339]

The OS explicitly stated that bond obligations were to be paid solely from revenues generated by the facility. Revenues raised by other projects would not be available to pay the Montgomery 2004 bondholders.[340]

Cantone Research and its registered representatives sold the Montgomery 2004 bonds. Approximately 36 investors purchased the bonds.[341]

b. Financial Difficulties After Montgomery 2004 Offering

i. Brogdon's Shell Game

As discussed above in describing the investigation that led to this proceeding, the Montgomery facility involved in the 2004 bond offering was not Christopher Brogdon's only such facility. According to the SEC, from 1992 to 2014, Brogdon raised close to $190 million in in 54 separate securities offerings involving at least 60 nursing homes and assisted-living facilities throughout the Southeast and Midwest.[342] Brogdon was an important part of DeRobbio's municipal underwriting business, and even at the time of the hearing DeRobbio's customers still held some $10 million in municipal bonds connected to Brogdon.[343]

DeRobbio became concerned about Brogdon's finances, however, perhaps as early as 2009 or 2011, but certainly by the time of the Montgomery 2015 offering at issue here. He said that he had customers who invested in Brogdon-related projects who were not being timely paid.[344] This prompted him to conduct his own investigation of Brogdon's finances, which did not allay his concerns. DeRobbio blames Brogdon for difficulties DeRobbio had in his underwriting business, and, as a result, DeRobbio testified, he stopped speaking to Brogdon in

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[338] JX-52, at 86.

[339] JX-52, at 31–32.

[340] Tr. (DeRobbio) 1013–14; JX-52, at 1, 12. If the revenues generated by the facility were insufficient, certain reserves pledged under the terms of the indenture agreement could be used as a temporary bridging mechanism. JX-52, at 1, 12, 27 (debt service reserve fund); Tr. (DeRobbio) 1013–14.

[341] CX-11, at 3; CX-18R.

[342] CX-44, at 11.

[343] Tr. (DeRobbio) 1016–17.

[344] Tr. (DeRobbio) 1015–23, 1080–81.

2009.[345] He said that Brogdon's failure to make timely payments to his customers who had invested in Brogdon offerings "devastated" his underwriting business.[346]

At some point before the Montgomery 2015 offering, DeRobbio realized that Brogdon "was borrowing from Peter to pay Paul."[347] Each facility was supposed to stand on its own, but Brogdon was taking revenues from one facility to pay bondholders involved in a different facility. DeRobbio called this "fraud" and agreed that it was a "shell game."[348] DeRobbio said that he did not do any new bond issues with Brogdon after he had "been stung."[349]

ii. Financial Problems with Montgomery 2004

The Montgomery assisted-living facility is an example of how Brogdon operated and how Anthony Cantone took advantage of Brogdon's financial difficulties for his own benefit. On August 15, 2011, Brogdon approached Anthony Cantone about purchasing an interest in the facility. Brogdon wrote in an email, "The deal basically is that you would be buying a 25% interest in [an] assisted-living building that is very profitable for $550,000. The building today is worth $6,000,000. I plan on selling it or refinancing it in the next year."[350]

Cantone wrote back the next day disputing that the facility was profitable.[351] He asked, "How can you justify a value of $6 million on Cedala when the income statement and tax return shows an operating loss of $240,000 for 2009?"[352]

Cantone had asked for and received some financials on the facility. They bore out his view that it was not profitable.[353] The financials showed an operating loss of around $232,000

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[345] Tr. (DeRobbio) 1015–23, 1082.

[346] Tr. (DeRobbio) 1016.

[347] Tr. (DeRobbio) 1016.

[348] Tr. (DeRobbio) 1026, 1081.

[349] Tr. (DeRobbio) 1034. DeRobbio portrayed himself as not doing business with Brogdon after realizing that Brogdon was engaged in a "shell game." Tr. (DeRobbio) 1016. But the evidence showed something different. In December 3, 2013 email correspondence with one of his customers (CX-46), DeRobbio encouraged the customer to consider purchasing bonds in a different Brogdon-related offering "because he [Brogdon] always pays, [even if] it usually is a couple days late." Tr. (DeRobbio) 1028. DeRobbio expressed confidence in the financials for the proposed transaction because of "cross-collateralization." Tr. (DeRobbio) 1028. He wrote to the customer, "I don't mind when you have several projects that can secure a weaker sister." Tr. (DeRobbio) 1028. DeRobbio admitted at the hearing that the cross-collateralization he was referring to in the correspondence was essentially Brogdon's "shell game." Tr. (DeRobbio) 1029.

[350] Tr. (Moy) 326–28; JX-54.

[351] Tr. (Moy) 326–28; JX-54.

[352] JX-54; JX-55, at 10.

[353] Tr. (Moy) 328–29; JX-55.

for the year 2009,[354] and an operating loss of a little over $127,000 for the year 2010.[355] For the first six months of 2011, the facility showed a small positive net income of $45,239.[356] Cantone sent the financials to Victor Polakoff on August 19, 2011, and copied his two adult children, John and Maryann Cantone.[357] Accordingly, they all had information about the facility's poor financial performance before the 2011 private placement and long before they sold the Montgomery 2015 municipal bonds.

Despite the dismal financial performance of the facility, Cantone worked out a way to provide the financial support that Brogdon had requested.

c. Montgomery 2011 Private Placement

Cantone did not simply purchase 25% of the facility with his own money. Instead, he created an entity to make the purchase and offered certificates of participation in that entity in a private placement. Purchasers of the certificates of participation were required to become members of the note purchaser, Cedars Financial LLC ("Cedars Financial"), which Cantone managed.[358]

The terms of the purchase were set forth in a Confidential Disclosure Memorandum ("Disclosure Memorandum") dated August 24, 2011 (only five days after Cantone had circulated the facility's poor financials within the Firm and nine days after Brogdon's email inquiring whether Cantone would be interested in buying a share in the facility). As set forth in the Disclosure Memorandum, Cedala (the Brogdon entity) issued an unsecured promissory note which Cedars Financial purchased. In exchange for purchasing the note, Cedars Financial also received 25% of Cedala from the sole member of that company, Brogdon's wife.[359] She and her husband and the Brogdon Family LLC ("Family LLC") gave a personal guarantee on the promissory note.[360] Saint Simons Healthcare, L.L.C. ("Saint Simons"), another company owned by the Brogdon family, was identified as the manager of the facility. No attorneys or independent professionals such as an appraiser or an accountant were identified in the Disclosure

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[354] Tr. (Moy) 328–29; JX-55, at 10.

[355] JX-55, at 7.

[356] JX-55, at 4.

[357] JX-55, at 1.

[358] Tr. (Moy) 572–73; X-53, at 1, 20–21.

[359] JX-53, at 1.

[360] JX-53, at 2.

Memorandum as having worked on the transaction.[361] However, Moy, the FINRA analyst who testified, said that the Firm was assisted on this transaction by Attorney Michael G.[362]

Of the 25% interest in Cedala (the Brogdon entity) that Cedars Financial (Cantone's entity) received in exchange for purchasing the promissory note, only 15% was for the account of the investors who purchased certificates of participation. Cantone's entity retained the other 10% for itself.[363] So, even though Anthony Cantone did not contribute any money to the transaction, in effect he obtained a 10% ownership of the Brogdon company that controlled the assisted-living facility.[364] In addition, Cantone garnered certain fees that the Brogdon entity, Cedala, agreed to pay Cedars Financial, and Cedars Financial received a discount on the purchase price of the promissory note. Cedars Financial purchased the note for $511,500, which was characterized as a $38,500 discount from the $550,000 raised in the offering for the purchase. The Disclosure Memorandum specifically provided that investors in the certificates of participation would *not* share in these additional forms of compensation to Cedars Financial, Cantone's entity.[365] Those funds (fees and discount) flowed to Cantone alone.

The Disclosure Memorandum told investors that Cedala was the "equitable owner" of the assisted-living facility but explained that Alabama law required the governmental body that had issued the Montgomery 2004 bonds, Montgomery Southside, to hold legal title. The issuer leased the facility to Cedala and Cedala controlled the facility.[366]

The Disclosure Memorandum also told investors that the facility had been appraised in 2004 to have an "as is" and "as stabilized" value of $2.5 million. The Disclosure Memorandum said that the appraised value was based on certain assumptions and limiting conditions stated in the appraisal. Those assumptions and limiting conditions were not set forth in the Disclosure Memorandum. Nor was the appraisal included with the Disclosure Memorandum. Instead, investors who wanted to view the appraisal were told that they could do so "at the offices of the Company," referring to Cedala, the Brogdon entity.[367] No explanation was given for why a more current appraisal was not done. The Disclosure Memorandum did not identify the firm that performed the 2004 appraisal, and no copy of the appraisal is in the record.[368]

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[361] JX-53, at 1–2, 8–10.

[362] Tr. (Moy) 242. As discussed below, Attorney Michael G. was involved in the Montgomery 2015 offering and its precursor, a transaction the parties refer to as the Walton offering.

[363] Tr. (Moy) 573; JX-53, at 7, 21.

[364] Tr. (Moy) 573.

[365] JX-53, at 21.

[366] JX-53, at 1.

[367] JX-53, at 1, 7, 12.

[368] Once again, Cantone and the Firm made it difficult for investors to evaluate the appraisal, by withholding it and requiring investors to request it. Adding to the difficulty, they required investors in the Montgomery 2011 private placement to contact Brogdon's company to see the appraisal, not Cantone Research. Investors in the earlier

The Disclosure Memorandum forecasted more than $1.5 million in operating income for 2012 and more than $1.7 million in 2013. After operating expenses, it forecasted net income of $390,000 for 2012 and $450,000 in 2013. After paying bondholders in the Montgomery 2004 offering, the Disclosure Memorandum forecasted that the project would have more than enough money left to pay the debt service on the promissory note. It forecasted a debt service coverage ratio for the promissory note of 4.09 in 2012 and 5.24 in 2013.[369] The forecasted figures were not reasonable in light of the actual financials Brogdon had shown Cantone and the Firm.

According to FINRA's analyst, Moy, Cantone Research sold $550,000 in certificates of participation in Montgomery 2011 to approximately 24 investors.[370]

The Montgomery 2011 offering was one of a number of private placements that Anthony Cantone and his Firm underwrote in connection with Brogdon-related properties. From 2008 to 2013 they raised over $26 million for Brogdon.[371]

There is evidence in the record that, when Anthony Cantone arranged for the Montgomery 2011 offering to provide financial assistance to Brogdon, Cantone was also providing financing to Brogdon to keep other Brogdon projects afloat. On August 23, 2011, for example, Cantone sent Brogdon an email discussing a loan Cantone had made to Brogdon to stave off the failure of a bond offering another broker-dealer, not Cantone Research, had underwritten. The email indicated that Cantone had expected that bridge loan to be paid back from the proceeds of yet another offering the other broker-dealer was about to underwrite.[372] Cantone told Brogdon in an email that the Firm would only be able to close on the Montgomery 2011 private placement if Brogdon paid what was owed on the bridge loan.[373] Other email correspondence between Cantone and Brogdon discussed arrangements for Cantone to facilitate extensions of time for Brogdon to repay what he owed on three other private placements.[374]

DeRobbio was not with Cantone Research at the time of the Montgomery 2011 offering and was not involved in the Montgomery 2011 private placement.[375]

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offering, Montgomery 2004. were told they could obtain the same appraisal from Cantone Research, which would have been slightly easier for investors since they were already dealing with the Firm while they considered the investment. JX-52, at 17. In neither offering was there any explanation why the appraisal was not provided to investors from the outset.

[369] JX-53, at 16.

[370] CX-14, at 1.

[371] Tr. (DeRobbio) 1079; CX-13.

[372] CX-90.

[373] CX-90; Tr. (Moy) 1581–85.

[374] Tr. (Moy) 1586–89; CX-92.

[375] Tr. (DeRobbio) 614–17, 654; CX-32, at 3–6.

d. Financial Difficulties After Montgomery 2011 Private Placement

After the private placement closed, the assisted-living facility was unable to generate revenues sufficient to meet its obligations. For the twelve months ending December 31, 2011, the facility disclosed in an EMMA filing that it had an annual net income ending December 31, 2011, of $20,274.13.[376] For the twelve months ending December 31, 2012, the facility had a net loss of $115,226.59.[377] By the time that the facility closed in June 2013, its EMMA filing showed an income statement ending June 30, 2013, with a year-to-date net loss of $95,931.85.[378]

As summarized by FINRA's analyst, Moy, Brogdon's entity failed to make required interest payments on the Montgomery 2011 private placement on (i) December 15, 2012, (ii) June 15, 2013, and (iii) September 15, 2013.[379] Anthony Cantone wrote two checks from his personal account to his entity, Cedars Financial, to cover the first two missing interest payments owed to investors in the 2011 offering. The first check was dated December 27, 2012; the second June 28, 2013. Saint Simons, the Brogdon entity that managed the assisted-living facility, reimbursed Cantone for each check a few days after the check was written and paid Cantone an additional fee or interest payment. Cantone also wrote a third check for the September shortfall, but Brogdon's entity did not reimburse Cantone for the third check.[380] By writing the checks to cover interest payments owed the Montgomery 2011 private placement investors, Cantone concealed from those investors that the investment had failed.[381]

On September 15, 2013, repayment of the principal on the promissory note was due.[382] But the Brogdon entity that was the borrower, Cedala, made no payment. Nor did Brogdon and his wife or their Family LLC, who had guaranteed the note.[383]

In May 2014, Cantone's entity, Cedars Financial, which was the purchaser of the promissory note, sent letters to Brogdon declaring the note in default and demanding payment of principal ($550,000) and interest ($66,000).[384] In June 2014 Cedars Financial sued Brogdon and his entity, Cedala, in Georgia state court, demanding the principal and interest owed on the

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[376] CX-95, at 10.

[377] CX-95, at 46.

[378] CX-95, at 50.

[379] Tr. (Moy) 244–46; CX-14, at 3–4.

[380] (Moy) 244–46; CX-14, at 3–4.

[381] In testimony given to the SEC, excerpts of which were read into the record in this case, Cantone acknowledged that he had loaned funds to Brogdon to make interest payments on the Cedars offering, Montgomery 2011, and other Brogdon offerings as well. Tr. (Cantone) 1559–62.

[382] JX-53, at 1.

[383] Tr. (Moy) 570–72; CX-14, at 3–4; JX-53, at 17.

[384] CX-14, at 4.

Montgomery 2011 offering. And in January 2015, the court granted Cedars Financial summary judgment.[385] The court ordered the defendants to pay $682,757 to the plaintiffs.[386]

e. June 2013 Closing of Facility

In the meantime, through 2011, 2012, and early 2013, Alabama authorities received multiple complaints about the care provided at the Montgomery assisted-living facility. The authorities visited the facility numerous times and found the complaints substantiated. They identified multiple deficiencies in the management of the facility and worked with the operator on plans for correcting the deficiencies.[387]

The complaints continued in May and June 2013. Finally, after conducting a compliance assessment, the Alabama Department of Public Health issued a report dated June 13, 2013, stating that the facility had failed to operate in accord with the applicable rules.[388] Some of the deficiencies were repeat deficiencies from a report dated November 7, 2012, and some were repeat deficiencies from an even earlier 2011 inspection report.[389]

As a result of the deficiencies found in the June 13, 2013 report, the State of Alabama Health Officer issued an emergency order suspending the facility's license to operate. The emergency order required that all residents of the facility be relocated.[390] The assisted-living facility closed in June 2013.[391]

Once the facility closed in June 2013, it was not generating any revenues and the Montgomery 2004 bondholders should not have continued to receive payment. As DeRobbio agreed, the closing of the facility should have caused a default. But instead, bondholders continued to be paid, albeit late.[392] The money was coming from somewhere, but not from the assisted-living facility.

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[385] CX-14, at 4.

[386] Tr. (Moy) 196; CX-48A, at 14.

[387] JX-56.

[388] JX-56, at 1, 5–6.

[389] JX-56, at 3–9.

[390] JX-56, at 5–6.

[391] Tr. (Moy) 241–42, 340, 544.

[392] Tr. (DeRobbio) 1012–15, 1090–91; CX-95, at 1.

f. 2014 Walton Offering

i. Same Players as Montgomery 2015 Offering

In July 2014, Respondents underwrote a $3.2 million bond offering referred to here as the Walton offering, which related to a different assisted-living facility located in Georgia.[393] The Walton offering involved many of the same players as the subsequent Montgomery 2015 offering, and, in at least one important way, the Walton offering served as the precursor for the Montgomery 2015 offering.

Cantone Research was the underwriter of both offerings. Christopher Brogdon was the seller of the property in both offerings. Dwayne Edwards was the purchaser and borrower in both offerings, in each case through an entity that he owned with a business partner, Todd B.[394] Attorney Brian M. (who had been Eric F.'s counsel in the 2013 Quad Cities offering) was underwriter's counsel in the Walton offering, working for Cantone Research. And he served as underwriter's counsel for Cantone Research in the Montgomery 2015 offering.[395]

Attorney Brian M. introduced Edwards to DeRobbio in connection with the Walton transaction.[396] DeRobbio viewed Edwards as someone who could replace Brogdon by purchasing various assisted-living facilities. It would be a way of getting DeRobbio's customers out of the Brogdon deals that were not paying timely and, "[i]f it worked out," DeRobbio acknowledged that Edwards would also become a source of underwriting business for him.[397]

ii. Decision Not to Disclose Edwards' Criminal Background and Negative Professional History

The parties made an important decision in the Walton offering—not to disclose highly troubling facts about Edwards' background—and they apparently did not reconsider that decision when they later worked on the Montgomery 2015 offering.[398]

In connection with the Walton offering, DeRobbio did a LexisNexis search and learned that Edwards had a criminal background.[399] DeRobbio did the search because, as he admitted, it is important to know about the background of whoever is going to be owning and operating an

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[393] Tr. (Moy) 291–93.

[394] Tr. (Moy) 291–92. Edwards and a business partner operated through a control entity. Tr. (Moy) 291–92.

[395] Tr. (Moy) 298.

[396] Tr. (DeRobbio) 1032.

[397] Tr. (DeRobbio) 1034–36.

[398] Tr. (Moy) 293–307.

[399] JX-57. DeRobbio did the search because, as he admitted, it is important to know about the background of whoever is going to be owning and operating an assisted-living facility. Tr. (DeRobbio) 1135. DeRobbio expressed the sense that the LexisNexis search showed he had done appropriate due diligence. Tr. (DeRobbio questioning Mr. Moy) 456–57.

assisted-living facility. As discussed below, in June 2014 in connection with the Walton offering, DeRobbio and Attorney Brian M. discussed what DeRobbio had learned about Edwards' background with Edwards and his attorney, William J. Through his counsel, Edwards provided a written explanation.[400]

(a) Edwards' Troubling Background

In his explanation of his criminal background, Edwards said that on March 29, 1996, he had pleaded guilty to two criminal charges in South Carolina. He described the charges in a way that minimized their importance. He characterized the first charge as arising from an acrimonious divorce and relating to unlawful use of the telephone. He described the second charge as a claim that he had mishandled a small amount of patient funds (less than $3,000) in connection with the purchase of a nursing home. He said he settled the charges because he had run out of money to continue litigating. However, he did not deny that the alleged crimes occurred. According to Edwards, he was given three years of probation and fined $1,650. He surrendered his nursing home license and was excluded from the Medicare and Medicaid programs.[401]

Edwards did not provide the underlying documents relating to the nature of the criminal charges and his guilty pleas. From what he provided, there was no way to verify the details or evaluate how serious the charges against him were. In his explanation, Edwards claimed that his three-year probation period was terminated early, after only one year. He also provided no documents to support that claim.

Edwards did provide documents showing that eventually he was permitted once again to apply for a nursing home license in South Carolina and to participate in the Medicare and Medicaid programs.[402] Effective September 29, 2004, around eight years after his conviction, the State of South Carolina pardoned Edwards for his criminal acts, absolving him of the legal consequences of his convictions and restoring his civil rights (such as voting rights).[403] On April 2, 2012, about 15 years after he was barred from the Medicare and Medicaid programs, the U.S. Department of Health and Human Services notified him that it had reinstated his eligibility to participate in the Medicare program.[404] On May 7, 2012, the U.S. Office of Personnel Management notified him that it had terminated his debarment from submitting insurance claims to insurance carriers on behalf of federal employees.[405] Effective June 1, 2012, the South

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[400] JX-59.

[401] Tr. (DeRobbio) 1139–40; JX-59, at 1.

[402] JX-59, at 1–6.

[403] JX-59, at 2.

[404] JX-57, at 3.

[405] JX-57, at 4.

Carolina Department of Health and Human Services pronounced Edwards eligible to re-enroll and participate in the State's Medicaid program.[406]

These documents suggested that the charges against Edwards might have been more serious than he claimed. They showed that he had been disqualified for many years from various state and federal programs important to running a nursing home or assisted-living facility.[407] DeRobbio testified at the hearing that he understood that what triggered the bar from the federal programs was that Edwards had taken Medicare and Medicaid checks and used them for his own personal purposes.[408] This was significant misconduct casting doubt on Edwards' trustworthiness.

Edwards did not volunteer information relating to his criminal background at the outset of the Walton offering. He only provided the information after DeRobbio discovered Edwards' criminal background in conducting due diligence.[409] This lack of candor also gave reason for concern and warranted further investigation. There is no evidence, however, that Respondents looked at the South Carolina criminal records or did anything else to independently verify what Edwards told them.

DeRobbio testified at the hearing that there were at least three telephone calls involving Edwards and his attorney, William J., and others. Edwards' attorneys were very defensive on the subject.[410]At least as far as the bond issue was concerned, DeRobbio agreed that Edwards conveyed the sense that "he wanted to act like his criminal conviction and Medicaid/Medicare bar never happened."[411]

(b) Respondents' Decision Not to Disclose Edwards' Troubling Background

According to email correspondence among various attorneys, DeRobbio and Attorney Brian M. concluded that Cantone Research could continue to underwrite the Walton offering, and then Attorney Brian M. separately discussed with Attorney Michael G. whether any disclosures about Edwards' background had to be made in the Walton offering documents.[412]

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[406] JX-57, at 5.

[407] Tr. (DeRobbio) 1141–42.

[408] Tr. (DeRobbio) 1279.

[409] Tr. (DeRobbio) 1139.

[410] Tr. (DeRobbio) 1157–60.

[411] Tr. (DeRobbio) 1159–60.

[412] JX-57.

Attorney Michael G. had been Cantone Research's counsel when it was the underwriter in the Montgomery 2004 offering,[413] and Moy testified that Attorney Michael G. assisted the Firm in connection with Montgomery 2011.[414] But in 2013 Cantone Research sued Attorney Michael G. for malpractice in connection with another transaction.[415] It is unclear what role Attorney Michael G. could have had in the Walton offering in 2014. DeRobbio identified Attorney Michael G. at the hearing as the "structuring agent for the boilerplate of the OS [in the Walton offering]."[416] The Firm's legal malpractice suit was still pending at the time that Attorney Michael G. was consulted on the Walton offering.[417]

According to an email from Attorney Michael G. to the attorney who served as bond counsel on the Walton transaction, Attorney Brian M. and Attorney Michael G. had discussed "whether any disclosure was warranted in the [Walton] POS."[418] Attorney Michael G. wrote in the email that "[a]fter considering all the facts and circumstances" the two of them had "agreed that such disclosure was not appropriate."[419] Attorney Michael G.'s email reporting on the conclusion he and Attorney Brian M. had reached did not set forth any reasoning or basis for the conclusion that disclosure was not "appropriate." Nor did it describe the substance or type of disclosure they discussed. Attorney Michael G. copied Attorney Brian M. on the email to bond counsel. Attorney Brian M. then forwarded the email correspondence to DeRobbio on June 25, 2014, identifying it as an email to bond counsel. And DeRobbio, in turn, forwarded the email string to Christine Cantone, who was then the Firm's CCO, without comment.[420]

Notably, no attorney took clear responsibility for the conclusion that Edwards' criminal background did not require disclosure. The email that Attorney Michael G. sent bond counsel was vague. It said only that Attorney Michael G. and Attorney Brian M. had agreed that disclosure would not be "appropriate."

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[413] JX-52, at 4.

[414] Tr. (Moy) 242.

[415] Tr. (DeRobbio) 1162–63; Tr. (Moy) 227–30; CX-37.

[416] Tr. (DeRobbio) 1163.

[417] Tr. (DeRobbio) 1162–63; Tr. (Moy) 298–99.

[418] JX-57, at 1.

[419] JX-57, at 1.

[420] JX-57; JX-59; Tr. (Moy) 301; Tr. (DeRobbio) 1138–39. The correspondence from Attorney Michael G. to bond counsel did not constitute legal advice to Respondents. Attorney Michael G. was not Respondents' counsel and the email was not sent to Respondents. By implication, perhaps, Attorney Brian M.'s forwarding to DeRobbio of the other attorney's email to bond counsel was Attorney Brian M.'s advice to Respondents, but Attorney Brian M. did not label the email as such and it was not marked privileged or confidential. The email did not indicate exactly what disclosure question may have been raised and considered and did not specify any legal advice given. It merely said some disclosure of some kind would not be "appropriate."

Edwards' criminal background and long exclusion from the Medicare and Medicaid programs were not disclosed in the Walton offering.

g. DeRobbio's Promotion of Edwards' Business

As noted above, DeRobbio had investigated Brogdon and been unhappy about what he learned. In the fall of 2014, after the Walton offering closed, DeRobbio discussed underwriting other offerings in which Edwards would purchase Brogdon properties.[421] In fact, DeRobbio had thought that Edwards would "show us deals and let us have first right of refusal,"[422] and was annoyed when he learned that Edwards planned to use a different underwriter in one of those transactions.[423]

In late April 2015, DeRobbio was promoting Edwards to replace Brogdon in connection with a different assisted-living facility located in Montgomery, Alabama, one that had been previously financed by a 2010 bond offering underwritten by a different broker-dealer, not Cantone Research. DeRobbio had worked for the other broker-dealer in 2010.[424]

In email correspondence dated April 27, 2015, DeRobbio learned that the trustee for the 2010 bond offering was unlikely to make a payment due to the bondholders because Brogdon was in arrears. On April 28, 2015, DeRobbio sent an email to the trustee denouncing Brogdon's record of late payments on various bond issues and offering Edwards as a "receiver" to take over from Brogdon. DeRobbio wrote,

> FYI…..Every month for the last five months Brogdon has missed a payment or has been in default on all my issues with him. Do you want to talk to the receiver I had in mind for the Montgomery Facility? He and one of our staff have been to the facility several times. His name is Dwayne Edwards.[425]

2. Key Players in the Montgomery 2015 Offering

Cantone Research was the sole underwriter for the Montgomery 2015 bond offering, which closed on May 29, 2015.[426] Respondents sold the Montgomery 2015 bonds primarily to retail investors.[427]

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[421] Tr. (DeRobbio) 1036–44; CX-101.

[422] Tr. (DeRobbio) 1042.

[423] Tr. (DeRobbio) 1040.

[424] Tr. (DeRobbio) 1030–33; CX-50.

[425] Tr. (DeRobbio) 1030–32; CX-50.

[426] Tr. (DeRobbio) 991; JX-51, at 4, 10.

[427] Tr. (DeRobbio) 634.

a. Dwayne Edwards, the Purchaser/Borrower

Dwayne Edwards, who had been the borrower in the Walton offering in 2014, was also the borrower in the Montgomery 2015 offering. He purchased the Montgomery, Alabama assisted-living facility through a control entity he owned with his business partner, Todd B. That entity was Montgomery ALF, LLC ("ALF").[428] ALF was formed in January 2015 for the purpose of acquiring and operating the assisted-living facility, which was reported in the OS for the Montgomery 2015 offering to be ALF's only asset.[429] Another company controlled by Edwards and Todd B. was to operate and manage the facility on behalf of ALF, Oxton Place of Montgomery, LLC ("Oxton Montgomery").[430] The assisted-living facility was to generate the revenues to pay investors their principal and interest on the Montgomery 2015 bonds.[431]

b. Christopher Brogdon, the Seller

Christopher Brogdon, through his entity Cedala, was the seller of the assisted-living facility in connection with Montgomery 2015 bonds. He was previously a registered representative through a broker-dealer in the early 1980s, but he was barred from the industry in or around 1983.[432] After that, he became an important figure in the senior care industry in the Southeast. According to SEC filings and the FINRA analyst, Moy, Brogdon was involved in 75 to 100 securities transactions involving purchases of nursing and assisted-living facilities throughout the region.[433] The SEC was investigating Brogdon at the time of the Montgomery 2015 offering at issue in this case, and it filed a complaint in federal district court against him on November 20, 2015, shortly after the closing of the offering. Eventually, the district court found in favor of the SEC and entered a $48 million judgment against Brogdon and his wife.[434]

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[428] Tr. (Moy) 80, 207–08, 271; Tr. (DeRobbio) 1062; JX-51, at 4.

[429] JX-51, at 7, 15.

[430] JX-51, at 7. Edwards and Todd B. also owned other entities involved in the nursing home and assisted-living industry. JX-51, at 7, 15.

[431] JX-51, at 5–6.

[432] Tr. (DeRobbio) 992–93.

[433] Tr. (Moy) 63.

[434] The SEC said in its complaint against Brogdon that it sought emergency relief to halt ongoing fraud. The SEC alleged that since 1992 Brogdon had raised over $190 million through 54 fraudulent conduit municipal bond and private placement offerings. Among other things, according to the SEC complaint, Brogdon commingled investor proceeds from 40 conduit municipal bond offerings and secretly diverted portions to pay for his and his wife's lavish lifestyle and to prop up his various business enterprises. When payments to investors became due, the complaint alleged, he often relied on third parties to make loans to his companies to make the payments. In fact, as discussed above at 59–63, Brogdon borrowed money from Cantone to make payments owed to bondholders in various projects, including Montgomery 2004. In the lawsuit, the SEC sought to freeze the assets of Brogdon and his wife and various related entities, along with a verified accounting and the appointment of a receiver. The SEC expressed concern that if the assets were sold piecemeal by Brogdon the proceeds would be dissipated. Tr. (Moy) 269, 271; CX-44, at 2–6.

c. Attorney Brian M., Counsel for Cantone Research, the Underwriter

Attorney Brian M. and his law firm worked for Cantone Research as underwriter's counsel for the Montgomery 2015 offering.[435] As noted above, Attorney Brian M. introduced DeRobbio to Dwayne Edwards prior to the Walton offering. Attorney Brian M. served as counsel for Brogdon and his control entities in many of Brogdon's acquisitions of assisted-living facilities, and he worked as counsel on various municipal bond offerings that DeRobbio had worked on as underwriter and salesperson.[436] Attorney Brian M. also was counsel to Eric F., the developer in the 2013 Quad Cities offering, and it was Attorney Brian M. who introduced Respondents to that offering.[437]

d. Attorney William J., Borrower's Counsel

The lessee/borrower in the Montgomery 2015 offering, Edwards' entity, ALF, was represented in that transaction by Attorney William J. and his law firm.[438] William J. had represented Edwards in the Walton offering and, as discussed above, had been involved in discussions about whether it was necessary to disclose Edwards' criminal background.

e. Attorney Michael G., an Attorney for Cantone Research in Other Offerings

As noted above, by September 2013, the Cantone Research had sued Attorney Michael G. for legal malpractice.[439] But for unexplained reasons, he was involved in the Walton offering in 2014 and participated in the decision not to disclose Edwards' criminal background. The Firm's legal malpractice suit against Attorney Michael G. was still pending at the time of the Montgomery 2015 bond offering.[440]

The district court in the SEC case entered final judgment against Brogdon and the relief defendants on January 17, 2020 (not published, but discussed in later judicial orders), and the Third Circuit Court of Appeals summarily affirmed. *SEC v. Brogdon*, Nos. 21-1116 & 21-2643, 2021 U.S. App. LEXIS 39237 (3d Cir. 2021). As a result, Brogdon's properties were either sold by Brogdon or went into receivership. Tr. (Moy) 64–65. Brogdon and his wife, a relief defendant in the SEC case, did not pay the entire $48 million judgment entered against them in the SEC case. The district court then allowed the SEC to execute on its judgment by garnishing millions of dollars held by various Brogdon entities. The district court ordered the entities to remit all distributions otherwise payable to the Brogdons to the SEC. *SEC v. Brogdon*, Civ. No. 15-8173 (KM), 2021 U.S. Dist. LEXIS 125703 (D.N.J. July 2, 2021) (opinion); 2021 U.S. Dist. LEXIS 126952 (D. N.J. July 2, 2021) (order).

[435] JX-51, at 1, 4, 48.

[436] Tr. (Moy) 105.

[437] Tr. (DeRobbio) 664, 681.

[438] JX-51, at 48.

[439] CX-37.

[440] Tr. (Moy) 231, 316–17.

3. Respondents' Introduction to the Montgomery 2015 Offering

Respondents' participation in the Montgomery 2015 offering began with email correspondence in April 2015 between Edwards and DeRobbio. In that correspondence, DeRobbio sought more business from Edwards.[441] Edwards responded by sending DeRobbio a copy of a purchase contract for the assisted-living facility in Montgomery, Alabama. The facility was identified by a new name, "The Cedars."[442] In addition to a copy of the purchase contract, Edwards provided DeRobbio with an environmental report,[443] an income statement for the facility,[444] and a sources-and-uses page for a contemplated $4,725,000 offering.[445]

The purchase contract between Brogdon and Edwards (through their respective entities, Cedala and ALF) was dated January 23, 2015. The contract identified Brogdon's entity as the owner of the land, building, and all improvements and equipment.[446] The purchase price was $3 million.[447] The closing on the transaction was contingent on the ability of Edwards' entity to obtain financing sufficient to make the purchase and renovate the facility. The plan was to finance the project through the issuance of municipal bonds.[448]

The purchase contract contemplated an offering of $4.75 million,[449] a smaller financing than the Montgomery 2015 offering eventually ended up being. There is nothing in the record that explains how or why the offering increased in size. The purchase contract also contemplated that the closing would occur at the end of March 2015 or the end of April 2015.[450] The offering closed at the end of May 2015.[451]

The income statement Edwards provided DeRobbio reported year-to-date net income for the five months ending May 31, 2013, of $100,208.15.[452] It reported annual net income for the preceding year, 2012, of $258,701.55.[453]

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[441] RX-201, at 1–2.

[442] Tr. (DeRobbio) 1042–46; RX-201, at 151–72.

[443] RX-201, at 4–144.

[444] RX-201, at 145–50.

[445] RX-201, at 173.

[446] RX-201, at 151.

[447] RX-201, at 153.

[448] RX-201, at 157.

[449] RX-201, at 173.

[450] RX-201, at 151.

[451] JX-51, at 1.

[452] RX-201, at 147.

[453] RX-201, at 150.

The income figures Edwards provided were inconsistent with figures disclosed in EMMA filings. As discussed above, for the twelve months ending December 31, 2011, an EMMA filing disclosed that the facility had an *annual net income* ending December 31, 2011, of only $20,274.13.[454] According to EMMA filings, the facility showed an annual *net loss* in 2012 of over $115,000,[455] and, by the time that the facility closed in June 2013, its EMMA filing showed an income statement ending June 30, 2013, with a year-to-date *net loss* of $95,931.85.[456]

EMMA filings were available to DeRobbio, and he accessed EMMA practically every day.[457] The Firm's WSPs also required a review of EMMA filings as part of due diligence.[458] DeRobbio could (and should) have seen the inconsistencies, which would have raised questions about Edwards' truthfulness.

4. Structure of the Montgomery 2015 Offering

The Montgomery 2015 bond offering was for $6,025,000. It was structured much like the Montgomery 2004 bond offering. A different governmental body issued the bonds, however, in 2015. The issuer for the Montgomery 2004 bond offering was Montgomery Southside. The issuer for the Montgomery 2015 offering was The Medical Clinic Board of the City of Montgomery – 1976 East ("Montgomery East").[459] The OS for the Montgomery 2015 offering explained that the governmental body issuing the bonds, Montgomery East, had to hold legal title to the facility under state law, just as Montgomery Southside in the earlier bond offering said that it had to hold legal title. The OS further explained that Montgomery East would lease the property to the lessee,[460] the same as Montgomery Southside did in the Montgomery 2004 offering.

The Montgomery 2015 OS seemed to indicate that Montgomery East did not yet hold legal title to the property. It stated that the issuer "will acquire" title to the facility and "will lease" the facility to the lessee.[461] The OS did not provide any information about how Montgomery East would acquire the property.[462]

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[454] CX-95, at 10.

[455] CX-95, at 46

[456] CX-95, at 50.

[457] Tr. (DeRobbio) 1196–97.

[458] JX-2, at 31.

[459] JX-51, at 1.

[460] JX-51, at 18.

[461] JX-51, at 18.

[462] The OS for the Montgomery 2004 offering, as discussed above, indicated that Brogdon had purchased the property prior to that offering for $1 million and that the governmental body issuing the bonds, Montgomery Southside, was to purchase the property from him for $1.3 million, using proceeds of the offering. That gave Brogdon an immediate profit of $300,000. It may be that the Montgomery 2015 transaction was to function in the

The lessee in Montgomery 2015 was Edwards' entity, ALF.[463] Oxton Montgomery, another entity controlled by Edwards and his business partner, Todd B., was to manage the facility on behalf of the lessee.[464] Edwards and Todd B. guaranteed the prompt payment of lease payments and other obligations of the lessee, ALF, just as the Brogdons had guaranteed payments in the Montgomery 2004 offering.[465]

5. Appraisal

A new appraisal prepared as of February 1, 2015, estimated that the facility on that date had an "as is" value of $3.3 million.[466] According to the appraisal, Edwards' entity, ALF, planned to purchase the facility from Cedala, the Brogdon entity, for $3 million, slightly less than the appraised value.[467]

DeRobbio testified that the only way that the Montgomery 2015 offering for $6 million would make sense was if the property was projected to be more valuable than $6 million.[468] Accordingly, the appraisal for "as is" value would not by itself support the offering. But the appraisal further estimated that upon completion of renovations a few months later, in October 2015, the facility would have a market value of $8.2 million. It estimated that by two years later, in October 2017, upon achieving a stabilized occupancy rate of 95%, the property would have a value of $9.2 million.[469] The appraisal thus predicted that the property would more than double in value in the first year and nearly triple in value the second year.

There were reasons to be skeptical of the appraisal used to support the Montgomery 2015 offering. The appraisal was done by a consulting firm that had a longstanding relationship with Brogdon. It had been the appraiser for several prior Brogdon offerings, many of which had gone

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same manner, with Dwayne Edwards purchasing legal title to the facility, selling it to Montgomery East, and then leasing the facility from Montgomery East. But the OS for Montgomery 2015 did not disclose how the legal title to the facility would be transferred or the flow of funds to make that happen. The purchase and sale agreement between the Brogdon and Edwards entities, Cedala and ALF, treated the assisted-living facility as owned by Brogdon. JX-62, at 16–19.

[463] JX-51, at 1.

[464] JX-51, at 1.

[465] JX-51, at 13.

[466] JX-51, at 7; JX-62, at 3.

[467] JX-62, at 18.

[468] Tr. (DeRobbio) 1105–06.

[469] JX-51, at 7–8; JX-62, at 4, 9. The OS represented that the jump in value from $3.3 million to $8.2 million could be achieved after the expenditure of $1.185 million on renovations over the course of six months. JX-51, at 8. Elsewhere in the OS, in the independent accountant's report, the amount of money to be spent on renovations was set higher, at $1.385 million, and the timeframe set shorter, only 90 days to complete the renovations. JX-51, at 123.

into default. Furthermore, the appraisal was based on market comparisons to other Brogdon properties. It was not based on independent analysis of independent facilities.[470]

DeRobbio, however, relied on the appraisal and merely directed that his name replace the name of the original underwriter on the cover page.[471]

6. Explanation for June 2013 Closure of Facility

The OS for Montgomery 2015 explained the deficiencies that had led the State of Alabama to shut down the facility in 2013 in a way that made it seem that those deficiencies were not relevant to the new offering. The OS said that the facility was operated in the past as a specialized care assisted-living facility that had to meet a higher level of care. Going forward, the OS said, the facility was going to operate as an assisted-living facility that did not come under such stringent requirements.[472]

Investors were led to believe that the only problem with the facility was that it was unprepared to meet the strict standards for a specialized care assisted-living facility. But nothing in the record suggests that the reason the facility was closed in 2013 was narrowly focused on the requirements of a specialized care facility. In any event, elsewhere in the Montgomery 2015 OS, investors were told that the facility would operate in the future as an "assisted care/Alzheimer's facility," a type of specialized care facility, and that "continued" licensure required compliance with a host of operating and health care standards.[473] In the Montgomery 2011 offering, the facility was described as providing Alzheimer's care.[474] There was no different business model in 2015, contrary to what investors were told in the Montgomery 2015 OS.

7. Projected Debt Service Coverage

For the Montgomery 2015 offering, ALF, Dwayne Edwards' entity, prepared forecasted financial statements. ALF estimated that the debt service coverage ratio before payment of management fees would be 1.43 the first year (ending May 31, 2016) and 1.49 the next year (ending May 31, 2017). After payment of the management fees, the ratio would be 1.29 the first year and 1.28 the next year.[475]

These figures, when compared to the figures projected in the Montgomery 2004 offering, did not make sense. In Montgomery 2004, the forecasted debt service coverage ratio was 1.25 in 2005, the first year after the offering, and 2.08 in 2006, the second year after the offering. The

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[470] Tr. (DeRobbio) 1117–26; CX-9.

[471] Tr. (DeRobbio) 1113–14.

[472] JX-51, at 38.

[473] JX-51, at 23.

[474] JX-53, at 13.

[475] JX-51, at 9, 35 121.

project failed to generate the projected revenues to cover the debt service for Montgomery 2004, which was a much smaller offering ($1.75 million). It was unlikely that the same facility with the same number of beds (61) could generate revenues sufficient to cover the debt on the substantially larger offering ($6 million). As discussed above, the amount of debt on a per-bed basis for the Montgomery 2015 offering was quite large, and within a range that DeRobbio said he would decline to underwrite.[476]

8. Main False and Misleading Disclosures

a. False Financial Figures

The OS for the Montgomery 2015 offering told investors that the facility was generating monthly net income of approximately $20,000 when it closed in 2013. That was not true. In fact, the facility was losing money before it closed, as revealed in various EMMA filings.[477] As noted above, EMMA filings showed that for the twelve months ending December 31, 2011, the facility had an *annual* net income of only $20,274.13,[478] and from then until it closed it suffered net losses.[479]

The Firm produced a due diligence checklist for the Montgomery 2015 offering signed by Polakoff indicating that EMMA filings for the facility had been checked as of May 25, 2015, a few days before the offering closed.[480] DeRobbio, who checked EMMA on a regular basis in connection with his clients' holdings, knew or should have known of the discrepancies. Cantone knew from his work on Montgomery 2011 and review of financial information for the facility, along with Brogdon's failure to pay prior investors what he owed them, that the figures in the OS for Montgomery 2015 could not be correct.

The OS hedged as to who was responsible for the misinformation about the facility's net income before it closed. It said that the $20,000-per-month figure for net income was "based upon" information supplied by the "present owner"—Brogdon, who stood to gain from the sale financed by the offering and was at the time under investigation by the SEC. The nature of the information supplied was not specified. Nor did the OS explain what it meant when it said the figures were "based upon" the information supplied. There was no indication that the figures had been reviewed by an independent accountant or anyone else. The OS said that the "Lessee"—Edwards, who also was to benefit from the offering and whose trustworthiness was doubtful because of his criminal background—believed the information supplied by the present owner to be "substantially correct." Precisely what was meant by substantially correct or why Edwards

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[476] *See supra* at 20 and n.67.

[477] Tr. (Moy) 319–20, 323–24, 336–48; JX-51, at 18; CX-95.

[478] CX-95, at 10.

[479] CX-95, at 14, 18, 22, 26, 34, 38. 42, 46, 50.

[480] Tr. (Moy) 348–53; RX-233.

should be relied upon was not explained.[481] This disclosure was designed to be obscure and to make no one accountable for the accuracy of the figures.

b. Edwards' Undisclosed Troubling Background

Respondents did not disclose Edwards' criminal background and lengthy exclusion from the Medicare and Medicaid programs in connection with the Walton offering or in the OS for the Montgomery 2015 offering. In fact, the Firm's due diligence file for Montgomery 2015 contains nothing at all about Edwards' criminal background.[482] Respondents apparently felt no need to revisit the conclusion in the Walton bond offering that it was not "appropriate" to disclose the information to investors. DeRobbio testified that it was a "non-issue" in the Walton offering and "it became a non-issue in Montgomery [2015]."[483] He confirmed at the hearing that the Montgomery 2015 OS did not disclose Edwards' criminal background and that he did not orally inform investors about Edwards' background.[484]

Even so, DeRobbio acknowledged that Edwards' background created potential licensing issues and that DeRobbio thought when he researched Edwards and discovered his criminal background the information was "problematic."[485] DeRobbio nevertheless attempted to excuse the failure to disclose Edwards' background. He said,

> I was guided by two counsels and threatened by a third that if I had talked about his pardon and expungement and revealed that in either offering [Walton or Montgomery 2015] I would be charged with libel. . . . I was told not to [reveal information about Edwards' background to customers].[486]

Notably, DeRobbio did not describe seeking legal advice from his counsel, receiving legal advice, and then acting on that advice. Rather, he described being threatened with a libel lawsuit. He identified Attorney William J., the attorney for Dwayne Edwards, as the person making the threat of a libel suit. He said that Cantone Research's attorney, Brian M., "concurred."[487]

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[481] JX-51, at 18.

[482] Tr. (Moy) 306–07; Tr. (DeRobbio) 1132–33; Stip. ¶¶ 73–78.

[483] Tr. (DeRobbio) 1269.

[484] Tr. (DeRobbio) 1135.

[485] Tr. (DeRobbio) 1135.

[486] Tr. (DeRobbio) 1136. In OTR testimony, DeRobbio claimed that the Firm's counsel, identified as Attorney Brian M., and his law firm, had advised DeRobbio that Edwards' background information did not need to be disclosed, and "in fact, had it been disclosed, it could be considered libelous." In response to a Rule 8210 request, DeRobbio stated that the attorney-client relationship had begun in May 2014 in connection with the Walton offering. Tr. (DeRobbio) 1151; CX-142; CX-143, at 1–4. As previously discussed, Brian M. was the person who introduced DeRobbio to the Quad Cities offering.

[487] Tr. (DeRobbio) 1295–96.

DeRobbio also claimed that he understood the pardon to be the equivalent of expungement. He said, "[W]e were advised by counsel that we were not allowed to mention it because it's as if it didn't occur."[488] He did not identify the attorney to whom he referred and did not explain the context. But he admitted that a pardon does not mean the crime never occurred.[489] The pardon itself did not say that Edwards' record would be wiped clean or use the word expunge. Rather, it said he was granted a pardon because he had lived as a law-abiding citizen of South Carolina since "satisfying" his sentences.[490]

DeRobbio admitted that if his customers had known about Edwards' background it would have raised concerns for them and could have influenced their investment decision.[491] "[A] prudent investor would, as I did, have some discomfort."[492]

Instead of disclosing Edwards' criminal background, the OS misleadingly described Edwards as having over 35 years of experience in the assisted-living business. It described him as owning and administering many facilities in the Carolinas, Georgia, and Florida. At some point, the OS said, he operated as many as 12 facilities at one time with over 800 employees and annual revenues exceeding $30 million. It said that he performed all business functions, including exercising primary responsibility for accounts payable and receivable, reimbursement policy and procedure, quality assurance, and accounting functions.[493] The clear implication was that Edwards had been highly successful in operating this type of facility—an implication at odds with his criminal background and 15-year bars from the Medicare and Medicaid programs.[494]

DeRobbio has tried to defend the disclosure in the OS in another way. He testified in an OTR introduced as substantive evidence in this case that Edwards' family was involved in the skilled nursing home and assisted-living industry and that Edwards had worked in such facilities during the period he was barred from the Medicare and Medicaid programs. In DeRobbio's mind, this justified the claim in the OS that Edwards had worked successfully for 35 years in all aspects of the business.[495] We find that it did not.

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[488] Tr. (DeRobbio) 1268–69.

[489] Tr. (DeRobbio) 1142–44.

[490] Tr. (DeRobbio) 1146; JX-59, at 2.

[491] Tr. (DeRobbio) 1136–38.

[492] Tr. (DeRobbio) 1137.

[493] JX-51, at 15.

[494] Given Edwards' age (58), the 35 years of purported successful experience must have included the 15 years he was barred from the federal programs. Tr. (Moy) 602–05; RX-259. The disclosure misrepresented his background.

[495] Tr. (DeRobbio) 1146–50.

c. Undisclosed Failed Prior Offerings

The OS for the Montgomery 2015 offering also did not disclose the fact that the same assisted-living facility had been the subject of two previous failed offerings. As DeRobbio agreed, the OS for Montgomery 2015 did not even mention Montgomery 2004 or Montgomery 2011.[496] The inability of the facility to meet its financial obligations in the prior, smaller offerings, would have been important information to investors.

d. Undisclosed Use of Proceeds

According to the OS, the proceeds of the Montgomery 2015 offering were to be used for three purposes:

- to finance the acquisition and renovation of the 61-bed assisted-living facility;
- to make initial deposits in certain accounts, including the debt service reserve fund; and
- to pay the costs of the issuance.[497]

Investors were not told about three other uses of the proceeds:

- to pay investors in the earlier failed offerings (Montgomery 2004 and Montgomery 2011);
- to pay Brogdon (through his entity, Saint Simons); and
- to pay Anthony Cantone (through his entity, Cedars Financial).[498]

The OS for the Montgomery 2015 offering did not mention any plan to pay investors in the prior two failed offerings and did not describe itself as a refunding. But, in fact, Respondents arranged for some of the proceeds of Montgomery 2015 to be used to redeem the Montgomery 2004 bonds. Prior to the closing of Montgomery 2015, on May 18, 2015, DeRobbio sent a letter to the Bank of Oklahoma as trustee. He told the bank that he represented the majority of the bondholders in Montgomery 2004 and that the bondholders had received a redemption notice that said the redemption was to occur June 15. DeRobbio informed the bank in this correspondence that the bondholders were waiving a 20-day advance notice for redemption. He asked for the Montgomery 2004 bondholders to be paid as soon as the funds become available.

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[496] Tr. (DeRobbio) 1078.

[497] JX-51, at 1, 12.

[498] Tr. (DeRobbio) 1077.

He said that the bondholders understood that the bonds would be paid in full on May 29, 2015—the exact date the Montgomery 2015 offering was to close.[499]

In this correspondence, DeRobbio made plain that proceeds from the Montgomery 2015 offering were expected to pay prior investors in Montgomery 2004 and that the money was urgently desired as soon as it was available. The closing statement for the Montgomery 2015 offering (which investors in Montgomery 2015 did *not* receive) reflected that the exact amount DeRobbio expected to be paid to investors in Montgomery 2004, $1,562,532.06, was to be wired from the proceeds of Montgomery 2015 to the trustee bank upon closing.[500] These payments to earlier investors satisfied Brogdon's outstanding obligations related to the assisted-living facility.[501]

The closing statement also showed that Brogdon ultimately received a share of the proceeds of the Montgomery 2015 offering through his entity, Saint Simons, which had managed the assisted-living facility until it closed in 2013. The closing statement allotted $529,933.99 to Saint Simons. That payment was vaguely described on the closing statement as "repayment of funds advanced for project operations."[502] Cantone, as a minority member of Brogdon's entity, Cedala, approved the distribution through Saint Simons to Brogdon.[503]

The closing statement showed that Cantone's entity, the Cedars, received $719,882.75 from the proceeds of Montgomery 2015, which was described as a "repayment."[504] That amount covered the judgment against Brogdon for principal and interest owed to investors in Montgomery 2011.[505] Cantone and his daughter, Maryann Cantone, prepared a letter dated June 1, 2015, to be sent to investors in Montgomery 2011 informing them that the promissory note had been paid on May 29, 2015—the day the Montgomery 2015 offering closed. The letter enclosed a principal payment and told each investor an interest payment would be made within the next two weeks.[506] Investors in Montgomery 2011 were not told they were being paid by the proceeds of the Montgomery 2015 offering. They were simply informed that the promissory note had been paid.[507]

The nearly $720,000 paid to Cantone's entity, Cedars, from the proceeds of Montgomery 2015 was larger than the principal and interest owed to Montgomery 2011 investors, as reduced

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[499] Tr. (DeRobbio) 1102–05; JX-66.

[500] JX-67, at 4.

[501] Tr. (Moy) 400–01.

[502] JX-67, at 4.

[503] JX-67, at 7.

[504] Tr. (Moy) 408–09, JX-67, at 4.

[505] Tr. (Moy) 405–06.

[506] CX-112.

[507] Tr. (Moy) 410–12; CX-112.

to judgment in the suit Cantone brought against Brogdon and his entities, $682,757.[508] According to the Disclosure Memorandum for Montgomery 2011, investors in that private placement were only entitled to their principal and interest, not the other forms of compensation Cantone's entity received such as fees and discount.[509] Thus, the additional proceeds from Montgomery 2015 (the amount by which the payment to Cantone's entity exceeded the principal and interest owed to Montgomery 2011 investors) flowed to Cantone.

9. Sales to Customers

There were approximately 36 customers who purchased the Montgomery 2015 bonds, both in the offering and on the secondary market.[510]

Respondents sold some Montgomery 2015 bonds to customers who had already bought Montgomery 2004 bonds,[511] and some Montgomery 2015 bonds to customers who had purchased Montgomery 2011 certificates of participation. In fact, some customers who bought Montgomery 2015 bonds had made purchases in both prior offerings.[512] That meant that when these customers purchased bonds in the Montgomery 2015 offering they were unknowingly paying themselves what was owed in the earlier offerings. In effect, they were moving funds from one pocket to another. These sales demonstrate how the customers relied on Respondents and were too unsophisticated to sort through the various false and misleading statements Respondents made to them. These sales also show that Respondents deceived customers regarding the success of prior offerings and the benefit they could obtain from investing in Montgomery 2015.[513]

10. Failure of Montgomery 2015 Offering

The defunct assisted-living facility never reopened. DeRobbio said, "It never got off the ground, so it failed from the beginning."[514] As a result of the failure to make a payment due in

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[508] Tr. (Moy) 405–06.

[509] JX-53, at 1, 7.

[510] Tr. (Moy) 222–23; CX-11. As previously noted, Moy used the term "approximately" when speaking of the number of customers because certain customers had multiple accounts. Tr. (Moy) 223.

[511] Tr. (DeRobbio) 1063–66; Tr. (Moy) 223–24; CX-22.

[512] CX-22.

[513] Even at the hearing, DeRobbio continued to mislead customer HR, who testified. DeRobbio attempted to cultivate that customer's good will by reminding him that the Montgomery 2004 bonds were "paid off," along with other investments over the years. After reminding the customer of those ostensible successes, DeRobbio also reminded the customer that he had recommended that the customer take the proceeds from Montgomery 2004 and invest them in the "new" Montgomery offering, Montgomery 2015. Tr. (DeRobbio questioning HR) 1477–78. DeRobbio did not reveal that the Montgomery 2004 bonds were "paid off" from the proceeds invested in the Montgomery 2015 offering.

[514] Tr. (DeRobbio) 1130.

July 2016—a little over a year after the bond offering closed—the bank trustee for the Montgomery 2015 bondholders filed a notice of default on EMMA on August 1, 2016.[515]

11. SEC Suit Against Edwards

In January 2017, the SEC sued Edwards, his business partner, Todd B., and various of their entities. The SEC sought emergency relief to halt alleged ongoing fraudulent misconduct in connection with nine separate conduit municipal bond offerings, including both the Montgomery 2015 bond offering and the Walton offering discussed above. The SEC alleged that Edwards and Todd B. had raised $62 million in the nine offerings and had misused much of the money raised. According to the SEC, Edwards commingled revenues and funds raised in the offerings for various purposes and misappropriated funds for personal use. The SEC charged Todd B. with aiding and abetting that misconduct.[516] The case was resolved in June 2017, when Edwards entered into a consent judgment without admitting or denying the charges.[517]

G. Customer Testimony

As discussed below, the customers who testified said that they relied on what the Firm's representatives told them about the investments and said that they were not told anything that they would view as negative information. They consistently testified that if they had been told the undisclosed information it would have affected their decision making.

1. Customer KE—Personal, Family, and Church Investments in Quad Cities and Montgomery 2015 (registered representative, Anthony Cantone)

Customer KE is now 69 years old and retired. He worked about half of his adult life as a carpenter and much of that time he spent working for the City of Evanston, Illinois in the water department and street department.[518]

Before he became a Cantone Research customer, KE had no investing experience. When he retired, however, he received a $200,000 settlement. His father was working with Anthony Cantone at the time and introduced him to Cantone. KE then started investing with Cantone Research in around 2010.[519]

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[515] CX-17 (Moy summary), at 1; Tr. (Moy) 202, 212; CX-9.

[516] Tr. (Moy) 276–77; CX-16 at 3; CX-49, at 1–4. The SEC complaint referred to Walton as the Social Circle Offering. CX-49, at 7.

[517] SEC Litig. Release 23875, 2017 SEC LEXIS 2044 (July 7, 2017) (reporting that the U.S. District Court for the District of New Jersey had entered consent judgments against Edwards and several of his entities for securities fraud on June 9, 2017).

[518] Tr. (KE) 913.

[519] Tr. (KE) 914–16.

KE's father also referred other family members to Cantone and Cantone Research. Some invested in the Quad Cities offering and some invested in both the Quad Cities and Montgomery 2015 bonds.[520] KE's father also invested in Montgomery 2015 bonds on behalf of his church.[521] When the bond offerings failed, his father felt very bad about having caused his family and church to suffer substantial losses. His father then covered some of their losses. For example, when the Quad Cities investment "went under," KE said his father "wound up paying my son back because it was [my son's] first initial investment in any kind of thing like this and [my father] didn't want to keep him from investing in stocks or anything else for the rest of his life because of it."[522] His father also purchased the Montgomery 2015 bonds for the church and then reimbursed the church for the amount of its loss in full from his own pocket.[523]

KE's father intended to testify at the disciplinary hearing, but died before he was able to do so.[524] KE then agreed to testify.[525]

KE testified that Anthony Cantone recommended the Quad Cities bonds to him as well as his father, but KE did not purchase the Quad Cities bonds. "[Cantone] thought it was a good investment." But KE did not. "I just didn't really feel that it was. I knew the area, and I knew it was a smaller community college, where most of the people that attend there are living on farms or on a rural environment, they don't have the money to stay in a dorm setting in a junior college."[526]

KE invested $10,000 in the Montgomery 2015 bonds in May 2015 on Cantone's recommendation. That was a substantial investment for him.[527] Cantone "just encouraged me to put some money in it and thought it was a good investment . . . plus, it was a municipal bond where it was basically tax-free money you were getting, so that made it also a little more attractive for all of us across the board."[528]

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[520] Tr. (KE) 919. One of those relatives was a first cousin, NB, who invested quite heavily in the Quad Cities bonds. Tr. (KE) 923–25. Another relative was SE, KE's son, who invested $10,000 in Quad Cities bonds. Tr. (KE) 924–25.

[521] KE's father was the treasurer and an elder in the Wilmette Church of Christ. The father had been active in the church since its inception, before KE was born. Tr. (KE) 916. As treasurer, the father invested on behalf of the church based on recommendations made by Cantone. Tr. (KE) 917–18. On behalf of the church, he invested around $45,000 in Montgomery 2015 bonds. Tr. (KE) 918.

[522] Tr. (KE) 925.

[523] Tr. (Moy) 366–71; CX-21.

[524] Tr. (KE) 918. His father died on November 15, 2022, just two weeks short of his 94th birthday. Tr. (KE) 915–16.

[525] Tr. (KE) 919.

[526] Tr. (KE) 921–22.

[527] Tr. (KE) 925–26.

[528] Tr. (KE) 927.

KE did not remember receiving any negative information about the investment.[529] Cantone did not tell him about the two prior failed offerings involving the same facility.[530] He testified that knowing about the other failed offerings would have affected his decision making.[531] "It affects your ability to make wise decisions on your investment, to have the whole total picture, and we're only getting about half of the picture it looks like."[532]

Cantone also did not provide any details about the background of Dwayne Edwards, who was the lessee and owner of the management company that would run the facility.[533] KE thought that Edwards' background would have raised many red flags.[534] He would not have invested if he "would have had the total picture."[535]

KE still has two or three other investments at the Firm, and he believes one of them, a $45,000 investment, "is going to be completely under water."[536] He testified that Anthony Cantone has tried to sell him other securities within the last year, but "I think he knows pretty much that I'm pretty well done doing business with Cantone Research."[537]

2. Customer AM—Both Quad Cities and Montgomery 2015 Bonds (registered representative, Anthony Cantone)

Customer AM is now 93 years old and was around 83 to 85 when he made the investments at issue.[538] He has been retired from the postal service since 1990.[539] His wife retired before he did.[540]

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[529] Tr. (KE) 927.

[530] Tr. (KE) 927–28.

[531] Tr. (KE) 928.

[532] Tr. (KE) 928.

[533] Tr. (KE) 928.

[534] Tr. (KE) 930.

[535] Tr. (KE) 930–31.

[536] Tr. (KE) 931.

[537] Tr. (KE) 931.

[538] Tr. (AM) 1441, 1447–48.

[539] Tr. (AM) 1438.

[540] Tr. (AM) 1439.

AM's point of contact at Cantone Research was Anthony Cantone.[541] In general, Cantone would tell him how safe the bonds were and what a good investment they were. Cantone "is a pretty good talker, so after he talked to me, I trusted him."[542]

AM testified that he made "quite a few investments" with the Firm, but most of them "turned out really bad. I don't know why, but I had very bad luck."[543] "[A]ll the bonds I invested in were always built up like they were safe, you know, and that is why I invested, because, you know, I worked hard for my money and I didn't want to lose it. He always made it sound like it was – I'm not going to lose any money, I'm going to make money. So that is why I invested."[544]

AM invested a total of around $80,000 in the Quad Cities bonds, most of which he lost.[545] According to Enforcement's records, he invested $30,000 in November 2013, $25,000 in February 2014, and $25,000 in March 2014.[546]

AM did not know anything negative about the Quad Cities bonds when he made the investment. He only learned about problems after investing.[547] Cantone did not mention any names or what the money was for, and AM did not investigate. "All I know was the amount and the interest I would be getting."[548] "The only thing [Cantone] told me," AM testified, "it was a good investment."[549] But it "turned out to be the worst investment I ever made."[550] He had a loss of approximately $59,000 on the investment.[551]

AM also invested in the Montgomery 2015 bonds. "Mr. Cantone never told me anything about it except it was a wonderful building, I'm going to make a lot of money."[552] Cantone did not disclose that the proceeds from the bond offering were going to be used to pay off investors

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[541] Tr. (AM) 1437.

[542] Tr. (AM) 1461.

[543] Tr. (AM) 1439.

[544] Tr. (AM) 1441.

[545] Tr. (AM) 1439–40, 1446.

[546] Tr. (AM) 1440.

[547] Tr. (AM) 1444–45.

[548] Tr. (AM) 1442.

[549] Tr. (AM) 1445.

[550] Tr. (AM) 1445.

[551] Tr. (AM) 1446.

[552] Tr. (AM) 1446–47.

in two prior bond offerings related to the same assisted-living facility.[553] AM invested $50,000 and suffered a net loss of approximately $30,000.[554]

AM last spoke to Anthony Cantone about a month or month and a half before the hearing. Cantone called him to suggest he invest $25,000 in another investment. He had $25,000 because another bond he owned had been called. Cantone said "Well, you can put that money into [], you'll make a fortune." AM said that he told Cantone, "I had enough, I lost enough money, I can't afford to lose anymore."[555] "I says, 'Well, I made enough of a fortune with all my other investments, so I'm going to keep this 25,000.'"[556] Notably, Cantone solicited AM to purchase a security during the same period that Cantone claimed he was too ill to participate in this disciplinary hearing.

3. Customer HR—Montgomery 2015 Bonds (registered representative, DeRobbio)

Customer HR was almost 88 years old when he testified. He retired in 1995 or 1996 from working as a civil engineer with the water department in Harrisburg, Pennsylvania.[557]

HR was working with DeRobbio when DeRobbio was with another firm. He moved over to Cantone Research with his holdings when DeRobbio moved to the Firm. This would have been around 2000 or 2005. HR was already retired at that time.[558]

HR invested around $55,000 in Montgomery 2015 bonds. He knew that they were running a nursing home for seniors "and the rate of return was, you know, high." He did not know much else.[559]

"I went on Mr. DeRobbio's word that the bond was a good investment."[560] DeRobbio did not tell him any information that he would consider negative about the bonds.[561] DeRobbio did not mention Dwayne Edwards and did not mention anything about the person who would be managing the nursing home.[562] DeRobbio did not mention that the nursing home was at that time

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[553] Tr. (AM) 1448.

[554] Tr. (AM) 1447.

[555] Tr. (AM) 1442–43.

[556] Tr. (AM) 1443.

[557] Tr. (HR) 1467–68.

[558] Tr. (HR) 1469–70.

[559] Tr. (HR) 1470–71.

[560] Tr. (HR) 1472.

[561] Tr. (HR) 1472.

[562] Tr. (HR) 1472–73.

closed.[563] He did not mention that the nursing home facility had not generated net income in the months prior to its closing.[564] He did not mention that some proceeds were used to pay off a judgment that Anthony Cantone had obtained against the operator of the facility.[565] He did not say that the facility did not have a license to operate in the State of Alabama or that the nursing facility had not been consistently profitable. If DeRobbio had disclosed these facts, HR would not have invested in the bonds.[566] Similarly, if HR had been told that in the months leading up to its closure the facility had a net operating loss every month, he would not have invested.[567] He understands that his investment is now practically worthless.[568]

At the time of the hearing, HR still had an account with DeRobbio.[569] DeRobbio indicated at the hearing that he was going to talk to that customer in the next week or so.[570]

4. Customer CK—Both Quad Cities and Montgomery 2015 Bonds (registered representative, Polakoff)

Customer CK was over 65 years old when she testified.[571] She is retired from a career in television broadcasting, but she still does a weekly 5-minute segment for the Pennsylvania SPCA on pet welfare and how to take better care of pets.[572]

CK was a Cantone Research customer from 2008 until 2015.[573] Prior to that her only investment experience was in connection with her 401(k) program at work. Polakoff was her financial advisor at Cantone Research.[574] A family friend was a Cantone Research customer and her ex-husband relied on that friend's advice. She thought, "If it's good enough for him, it's probably been well vetted out, and, you know, I'll invest."[575]

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[563] Tr. (HR) 1473.

[564] Tr. (HR) 1475.

[565] Tr. (HR) 1475.

[566] Tr. (HR) 1475–76.

[567] Tr. (HR) 1476.

[568] Tr. (HR) 1476–77.

[569] Tr. (HR) 1478.

[570] Tr. (HR) 1480–81, 1482.

[571] Tr. (CK) 1487.

[572] Tr. (CK) 1488.

[573] Tr. (CK) 1489.

[574] Tr. (CK) 1489.

[575] Tr. (CK) 1490.

Generally, Polakoff recommended bonds.[576] Some of the recommendations involved Christopher Brogdon, who was held out to her as someone with whom you would certainly want to invest. She invested in municipal bonds and private placements involving Brogdon. The investments were "pitched as fabulous places for my money."[577]

CK also invested $25,000 in Quad Cities, which was a big investment for her. She thought it was a good investment and that she was lucky to be in it.[578] The information she was provided was mostly positive in nature.[579] Polakoff did not tell her about the 2011 bankruptcy filing or the decrease in the dormitory's gross income from $409,000 in 2007 to $307,000 in 2009. Nor did he tell her that the dorm had a mold-contamination problem.[580] When asked whether that information would have been important to her, she responded, "I don't buy mold, at least knowingly."[581] Polakoff also did not tell her that another broker-dealer, Stifel, was the original underwriter for the offering.[582] The undisclosed information would have affected her decision to invest in the Quad Cities bonds. "I would say, 'Vic, what are you trying to do selling me this garbage?'"[583]

In May 2015, Customer CK invested $10,000 in the Montgomery 2015 bonds, which also was a large investment to her. Polakoff told her only positive things about the investment. He did not tell her that the Firm was involved in two prior failed offerings in 2004 and 2011 involving the same facility.[584] She would not have invested if she had known. "Why would I buy that kind of debt and loss? Why would I use my money, good money, to go after bad money?"[585] Polakoff did not disclose Dwayne Edwards' guilty plea relating to mishandling funds in connection with his purchase of a nursing home, or that Edwards was required to surrender his license to own and operate assisted-living facilities in South Carolina, or that he was barred for 15 years from participating in Medicare and Medicaid programs.[586] These facts were important to her. "I wouldn't have gotten into a car driven by that guy, much less invest money into what he was doing."[587]

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[576] Tr. (CK) 1490–91.

[577] Tr. (CK) 1492.

[578] Tr. (CK) 1493.

[579] Tr. (CK) 1495.

[580] Tr. (CK) 1495.

[581] Tr. (CK) 1495.

[582] Tr. (CK) 1496.

[583] Tr. (CK) 1497.

[584] Tr. (CK) 1497–98.

[585] Tr. (CK) 1498–99.

[586] Tr. (CK) 1499–1500.

[587] Tr. (CK) 1501.

By summer 2015, CK's various investments with the Firm through Polakoff were going badly. She said that every time she went to the mailbox it seemed like there was another default notice or reason why a payment could not be made. She sensed that something was "really wrong."[588] She reached out to someone she believed she could trust, and that person did some research.[589] She testified that he "was quite alarmed by what he had found."[590] As a result, she transferred her accounts out of the Firm in summer 2015, but it was difficult. "[A]ll this stuff that wouldn't transfer, couldn't transfer, no market for, et cetera, et cetera."[591]

CK wrote an email to Polakoff complaining that he had sold her junk. "I sort of referred to all of this as, you know, eighth grade Bernie Madoff, you know, that this was some kind of a Ponzi scheme."[592] As a result of her written complaint, Polakoff wrote her a personal check for around $85,000. The money covered various investments that Polakoff had recommended to her. He told her, "[W]e understand, you know, yeah, you're a timid investor, we'll pay you back."[593] She never heard anything from the Firm with regard to her complaint about the investments Polakoff had recommended.[594]

We note that Polakoff called CK a "timid" investor. In other words, he mildly suggested that she was not sophisticated or smart and the only reason he was paying her was to be kind to her. He did not acknowledge any wrongdoing or problem with the investments he had recommended.

The Firm sold CK's Quad Cities bonds at a little bit of a loss; she still holds the Montgomery 2015 bonds.[595]

5. Customer AJ—Both Quad Cities and Montgomery 2015 Bonds (registered representative Maryann Cantone)

Customer AJ is now 35 years old. She was around 25 or 26 years old when she invested in the Quad Cities and Montgomery 2015 municipal bonds. She graduated from New York University in 2010 with a bachelor's degree in economics and math.[596]

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[588] Tr. (CK) 1502.

[589] Tr. (CK) 1502–03.

[590] Tr. (CK) 1503.

[591] Tr. (CK) 1504.

[592] Tr. (CK) 1504–05.

[593] Tr. (CK) 1505–07.

[594] Tr. (CK) 1509–10.

[595] Tr. (CK) 1507–08.

[596] Tr. (AJ) 1515, 1527.

AJ was a close childhood friend of Maryann Cantone. AJ described a deep connection with the entire Cantone family.

> [H]er and I have been best friends since we both were ten years old. We met in fifth grade when she moved to this town, and I grew up with her family. I'm very familiar with both her parents, her brother, herself. She was like a sister to me. I would spend, you know, holidays and weekends with them.[597]

The two attended different colleges.[598] After graduation, they both returned to New Jersey, reconnected, and began working. AJ has worked at multiple jobs, including as a fitness instructor, a dance teacher, and in retail. She has lived at home since college and saved the money she earned. After college, Maryann Cantone began working for her father at the Firm.[599]

As the two young women talked about their work, Maryann Cantone painted a positive picture of the Firm's success with municipal bonds. "[S]he started telling me about how well these municipal bond deals went in [Cantone Research]."[600] Maryann Cantone was enthusiastic about municipal bonds as an investment. She told AJ "[T]hey do super well, we have never had one default . . . ."[601] Maryann reiterated that "none had ever defaulted, they're so successful, they're so popular."[602] She also told AJ that municipal bonds are "as safe as you can get with doing, like investments."[603] "It, in the beginning, felt just like conversation, I can't say whether she was selling me on them or whether she was just talking, but over time it was a lot of that repeated discussion, and it absolutely gave me the impression that these were great in her company and, like I said, very popular."[604]

After working a year in retail, AJ had saved $25,000. She had no education regarding investing. She broached the subject with Maryann Cantone of investing her savings in municipal bonds:

> Like I said, she was my best friend. I knew her family very well. I trusted her family. I trusted her. She spoke so highly of these bonds, and so I told her, 'Hey, by the way you have been talking about these a ton,' I knew they were not offered constantly, so you had to wait until one became available,

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[597] Tr. (AJ) 1517–18.

[598] Tr. (AJ) 1517.

[599] Tr. (AJ) 1515–18.

[600] Tr. (AJ) 1518.

[601] Tr. (AJ) 1519.

[602] Tr. (AJ) 1529.

[603] Tr. (AJ) 1519.

[604] Tr. (AJ) 1519–20.

> and I remember saying to her, 'Hey, I got some money saved up. The next time one becomes available, let me know, I'm in.'"[605]

In April 2014, AJ became a customer of the Firm and bought Quad Cities bonds.[606] AJ set the scene for making the investment. It was an informal discussion among friends:

> So I made it clear to [Maryann] that the $25,000 at that point that I had saved, I remember she came over to my family's house, because as I was comfortable with her family, she was very comfortable with mine, and we sat in my sun room, which is where our formal dining room was, and my parents were both there with me talking to her as well . . . .[607]

AJ and her parents clearly explained that the money should be invested conservatively:

> [W]e were very clear with telling her, 'We are conservative people, risk a[]verse.' We said the 25,000 for the bond should be in the most conservative, as safe as possible, investment . . . .[608]

AJ subsequently invested another $25,000 in the Montgomery 2015 bonds.[609] She made that investment before the Quad Cities bonds had defaulted, so she thought "Wow, this is great, it's everything Maryann said it would be."[610] Once she accumulated about $20,000 in savings, she told Maryann that she would like to invest in some more bonds. Her father supplemented her savings with another $5,000.[611] The $50,000 total investment in the bonds constituted her "work life savings."[612]

Prior to making the bond investments, Maryann told AJ that Quad Cities bonds related to a college dormitory and the Montgomery 2015 bonds related to a nursing home. That was the entirety of the information conveyed.[613]

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[605] Tr. (AJ) 1520–21.

[606] Tr. (AJ) 1521.

[607] Tr. (AJ) 1521–22.

[608] Tr. (AJ) 1521–22.

[609] Tr. (AJ) 1527–28.

[610] Tr. (AJ) 1528.

[611] Tr. (AJ) 1529.

[612] Tr. (AJ) 1528. At some point, the family gave Maryann Cantone $5,000 to invest in stocks and told her that she "could play around with some riskier investments" with that money. Tr. (AJ) 1522. The record contains no further information about what happened with that money, and it is not covered by the charges in this case.

[613] Tr. (AJ) 1523.

Maryann Cantone described the Quad Cities investment in only positive terms. She never told AJ anything about the bonds that was negative.[614] She did not tell AJ about the 2011 bankruptcy filing, or the 18% decline in the dormitory's gross income between 2007 and 2009, or the decline in the College's enrollment since 2010, or the mold contamination problem with the dormitory.[615] Nor did Maryann Cantone disclose other negative information, including that the College had threatened to terminate its affiliation with the owner of the dormitory because of disputes with the management company.[616] AJ testified that she would have wanted to know about these "potentially alarming" facts.[617] She said that the undisclosed information would not only have affected her investment decision but also "I know that my father would not have allowed me to invest in this."[618]

AJ purchased the Quad Cities bonds in April 2014 on the secondary market, about five months after the original offering in November of 2013. AJ was unaware of the original offering and did not know that Stifel, the original underwriter, had withdrawn from the offering.[619] She suffered a loss of around $19,532 on the Quad Cities bonds.[620]

With respect to the Montgomery 2015 bonds, AJ said, "I distinctly remember her [Maryann Cantone] saying, 'Montgomery is a nursing home, and nursing homes, you know, are the safest bet because everyone gets old and everyone needs somewhere to go once they get old. So, in general, the nursing home municipal bond offerings do very well.'"[621] Maryann Cantone did not tell her friend about the two prior failed offerings for the same facility in 2004 and 2011.[622] AJ said that would be important information. "[T]here is no way I would have invested, even with my limited knowledge at that time, and there is absolutely no way my dad would have okayed that."[623] AJ lost $15,204 on the Montgomery 2015 bonds.[624]

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[614] Tr. (AJ) 1524.

[615] Tr. (AJ) 1524–25.

[616] Tr. (AJ) 1526.

[617] Tr. (AJ) 1525.

[618] Tr. (AJ) 1526.

[619] Tr. (AJ) 1524–25.

[620] Tr. (AJ) 1527.

[621] Tr. (AJ) 1529–30.

[622] Tr. (AJ) 1530.

[623] Tr. (AJ) 1530.

[624] Appendix C.

H. Credibility

1. Customers

We find the customers credible. They had a good general recollection of the circumstances in which Respondents recommended the bonds. They testified consistent with each other that they were not told any negative information about the investments. The customers also consistently described Respondents as enthusiastic about the bonds as secure investments yielding a good interest rate. All the customers relied on Respondents to guide them on their investments. They were not the kind of sophisticated and experienced investors that Respondents portrayed their clients to be in their pre-hearing brief.[625]

2. DeRobbio

We find DeRobbio generally not credible for several reasons. In various settings—at the hearing, in OTR testimony, and in an affidavit under oath—he gave inconsistent stories. His testimony also lacks corroborating documentary evidence. And, furthermore, throughout his testimony DeRobbio attempted to meet every perceived inconsistency or problem with a narrowly focused distinction or explanation that did not bear close scrutiny.

Without going back through the record in detail, we note a few examples. DeRobbio claimed at the hearing that he conducted extensive due diligence prior to the Quad Cities offering. He also claimed he prepared a due diligence memorandum for the Quad Cities offering, as the Firm's WSPs required.[626] But the Firm's records contain no such memorandum.[627] At the hearing, DeRobbio countered that his "memorandum" consisted of notes on his copies of the documents he was studying while conducting due diligence. But such notes do not exist either. He said at one point in the hearing that he gave the documents with his notes to Polakoff or Cantone and does not know what they did with them.[628] At another point, in discussing his detailed affidavit in support of the Bondholder Litigation that Anthony Cantone filed after the Quad Cities offering failed, DeRobbio testified that he had destroyed the notes underlying his affidavit, along with other old files, when the Firm moved its offices. He was vague about when that happened.[629] The record does not support the assertion that DeRobbio performed any independent due diligence. Indeed, in light of the short time between learning about the offering to marketing the bonds and closing, it would have been difficult for DeRobbio to conduct thorough, independent due diligence.

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[625] Resp. Br. 2.

[626] See *supra* at 39–44, 53–55.

[627] See *supra* at 17.

[628] Tr. (DeRobbio) 646–48.

[629] Tr. (DeRobbio) 1272–75, 1313–14.

DeRobbio's assertions under oath in his affidavit for the Bondholder Litigation were inconsistent with what he stated under oath at the hearing. For example, DeRobbio claimed in his affidavit that BMOC and its president, Bill L., had concealed that BMOC had managed the dormitory prior to the borrower's bankruptcy filing. The record shows, however, that Respondents received the original management contract for BMOC to manage the dormitory prior to closing, so DeRobbio and all Respondents knew that BMOC had been the manager of the dormitory for many years.[630] At the hearing, DeRobbio admitted that he knew prior to closing of the Quad Cities offering that BMOC had been the management company prior to the bankruptcy.[631]

DeRobbio's admission that he knew BMOC was the management company before the bankruptcy presented another inconsistency. In the OS for the Quad Cities offering, Respondents promoted the bonds—and discouraged investors from being concerned about the bankruptcy filing—by conveying the impression that the dormitory would be under new ownership and management. DeRobbio attempted to justify the disclosures in the OS by claiming that the owner of BMOC had told Respondents that the company was going to put a different person in charge of the dormitory, a "top gun."[632] But BMOC had the authority at any time to replace an employee who was failing at the job. DeRobbio's proffered justification for the misleading disclosure in the OS is nonsense.

We also find DeRobbio not credible because he was, at the hearing, evasive in answering many questions. He tried to avoid a yes or no answer.[633] Even when answering a straightforward question that required only a yes or no, as when shown a document and asked whether it said what it said, he would qualify his answer, by saying something like, "I would believe that to be true."[634] In other cases where a simple answer would do, DeRobbio launched into a monologue that distracted or steered widely away from a problematic issue.[635]

DeRobbio's credibility was further undermined when he asserted as fact things that were demonstrably untrue. For example, DeRobbio asserted that during his due diligence prior to the Quad Cities offering he had spoken to the president of the College, whom he identified as Steve S.[636] DeRobbio claimed that there were roughly nine calls that included the president of the College, although he retained no notes to corroborate that claim.[637] He believed that Steve S. was

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[630] Tr. (DeRobbio) 802, 805–07; CX-75, at 5, ¶ 13; JX-33, at 9, 34.

[631] Tr. (DeRobbio) 804.

[632] Tr. (DeRobbio) 804–05.

[633] Tr. (DeRobbio) 1159–60 ("That would seem the case." "I believe it to be.").

[634] Tr. (DeRobbio) 622.

[635] Tr. (DeRobbio) 615–16, 732–33.

[636] Tr. (DeRobbio) 749–52, 795.

[637] Tr. (DeRobbio) 795.

the College president.[638] It was demonstrated at the hearing that Steve S. was a member of BMOC's management team, the executive director of United Housing, and executive director of the borrower, Sauk Valley Housing. In fact, Steve S. signed the OS on behalf of the borrower.[639] The OS identified another man as the president of the College.[640] Steve S. was obviously not the president of the College.[641] At another point DeRobbio tried to say that conversations with Bill L. constituted due diligence on the College, but then was forced to admit that Bill L. was also associated with BMOC, which was going to manage the dormitory for Eric F. and his entity, Sugar Capital.[642]

DeRobbio also shifted responsibility whenever he could. In their early days at Cantone Research, DeRobbio characterized his business partner, James Friar, as the person with underwriting responsibility and tried to limit his own responsibility by calling himself a salesman.[643] It was only reluctantly that DeRobbio admitted even as a salesman he had to know the projected debt service coverage ratio disclosed in the Montgomery 2004 OS.[644] Later, when he returned to Cantone Research without Friar, DeRobbio blamed Cantone for failing to see that the financial information for the Quad Cities offering was unreliable. DeRobbio said that Cantone was the person with an investment banking license who had the expertise with the numbers.[645] DeRobbio tried to limit his due diligence on Montgomery 2015 to "[i]nitial" due diligence and identified his main job as "finding deals."[646] He was quick to say, "I was not the only one doing due diligence."[647] DeRobbio maintained that he relied on all the other professionals involved in the offerings—the accountants, lawyers, and feasibility consultants—and that he was only a salesman, without their expertise.[648] He said in connection with the Quad Cities offering that he struggled to understand "what was given to us."[649] Similarly, when DeRobbio was shown the false disclosure in the Montgomery 2015 OS that the facility was

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[638] Tr. (DeRobbio) 1275-76.

[639] JX-3, at 44–45, 51, and 76

[640] JX-3, at 46.

[641] CX-85, at 4.

[642] Tr. (DeRobbio) 1314–16.

[643] Tr. (DeRobbio) 1005, 1208–09, 1621–22, 1629.

[644] Tr. (DeRobbio) 1208–09.

[645] Tr. (DeRobbio) 736, 839–40.

[646] Tr. (DeRobbio) 1060.

[647] Tr. (DeRobbio) 908.

[648] Tr. (DeRobbio) 1257–58.

[649] Tr. (DeRobbio) 862–63.

making $20,000 per month before it shut down and was asked about what "you" told investors, he responded, "That's what *they* put in there, yes."[650]

3. Cantone

Because Anthony Cantone refused to appear at the hearing, we could not assess his credibility in person. But his refusal to appear does diminish the credibility of statements made in his behalf in the Respondents' opening brief and other filings in the case. Portions of testimony he gave elsewhere were read into the record and treated as substantive hearing testimony.[651]

III. MSRB Rules and Provisions of the Securities Act

Municipal securities and the purchase and sale of municipal securities are subject to regulation by the MSRB and its rules. Section 15B(b)(2)(C) of the Securities Exchange Act of 1934 ("Exchange Act") states that MSRB rules should be designed to prevent fraud, promote just and equitable principles of trade, and protect investors. Section 15B(c)(1) of the Exchange Act prohibits a broker-dealer from violating MSRB rules, but the MSRB does not have enforcement authority. Under Section 15B(c)(4) of the Exchange Act, the MSRB may provide guidance and assistance in the enforcement of its rules to a registered securities association like FINRA or another appropriate regulatory agency.[652]

FINRA's By-Laws provide that members and persons associated with members will abide by MSRB rules,[653] and FINRA administers and enforces its members' compliance with MSRB rules.[654] As a FINRA member, and as an underwriter of the municipal bonds at issue, Cantone Research was required to comply with the applicable MSRB rules.[655] As registered representatives and persons associated with a FINRA member, Respondents Anthony Cantone and DeRobbio were also required to comply with those rules.[656]

The Complaint charges Respondents with willful violations of three MSRB rules: MSRB Rule G-17, MSRB Rule G-19, and MSRB Rule G-47. These rules focus on investor protection because significant participation by individual investors has long been a hallmark of the

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[650] Tr. (DeRobbio) 1198 (emphasis added).

[651] Tr. (Cantone) 1542–79 (reflecting portions of Feb. 20, 2015 OTR, Oct. 22, 2015 SEC testimony, Aug. 22, 2016 disciplinary hearing testimony, Aug. 25, 2016 disciplinary hearing testimony, June 4, 2019 OTR, June 5, 2019 OTR, June 6, 2019 OTR, and June 9, 2019 OTR).

[652] 15 U.S.C. § 78o-4; *SEC v. GLT Dain Rauscher, Inc.*, 254 F.3d 852 (9th Cir. 2001). MSRB rules are found at www.msrb.org.

[653] Article IV, § 1(a)(1) and Article V, § 2(a)(1).

[654] *Anthony A. Grey*, Exchange Act Release No. 75839, 2015 SEC LEXIS 3630, at *2 n.3 (Sept. 3, 2015).

[655] Article IV, § 1(a)(1).

[656] Article V, § 2(a)(1).

municipal securities market.[657] The Complaint also charges Respondents with willfully violating the Securities Act of 1933 ("Securities Act"), Sections 17(a)(1), 17(a)(2), and 17(a)(3).

A. MSRB Rule G-17 – Fair Dealing

MSRB Rule G-17 imposes a broad duty to behave fairly in the conduct of a municipal securities business. It is at the core of the MSRB's investor protection rules. It provides that a municipal securities dealer "shall deal fairly with all persons," and it prohibits a municipal securities dealer from engaging in "any deceptive, dishonest or unfair practice." The rule contains an anti-fraud prohibition similar to the standard set forth in the SEC's Rule 10b-5, but it also establishes a general duty to deal fairly, even in the absence of fraud.[658] A violation of MSRB Rule G-17 does not require a finding of scienter.[659]

In broadly requiring fair dealing, Rule G-17 is principle-based. "All activities of dealers must be viewed in light of these basic principles, regardless of whether other MSRB rules establish specific requirements applicable to such activities."[660]

The broad duty imposed by MSRB Rule G-17 to deal fairly with all persons in the municipal securities market has been interpreted to impose various specific obligations on municipal securities dealers in their dealings with customers. Those specific duties have been the subject of MSRB guidance.[661]

One of the specific duties imposed on municipal securities dealers by MSRB Rule G-17 is an obligation to ensure that information provided to a customer is correct and not misleading.[662] A securities professional in the municipal bond market also has an obligation to

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[657] Guidance on Disclosure and Other Sales Practice Obligations to Individual and Other Retail Investors in Municipal Securities, July 14, 2009, https://www.msrb.org/Guidance-Disclosure-and-Other-Sales-Practice-Obligations-Individual-and-Other-Retail-Investors-0.

[658] Reminder of Customer Protection Obligations in Connection with Sales of Municipal Securities (Mar. 30, 2007) ("Reminder of Customer Protection Obligations (Mar. 30, 2007)"), https://www.msrb.org/Regulatory-Documents ?f%5B0%5D=msrb_publication_date%3A2007&f%5B1%5D=regulatory_documents%3A107.

[659] *Wheat, First Sec., Inc.*, Exchange Act Release No. 48378, 2003 SEC LEXIS 3155, at *25 (Aug. 20, 2003).

[660] Reminder of Customer Protection Obligations (Mar. 30, 2007).

[661] MSRB Rule G-17 Interpretations, *Interpretive Notice Concerning the Application of MSRB Rule G-17 to Underwriters of Municipal Securities*, 180 (Aug. 2, 2012), ("2012 Interpretive Notice") http://cams.ocgov.com/Web_Publisher_SAM/Agenda06_23_2020_files/images/O01520-000483A.PDF.

The 2012 Interpretive Notice has been superseded, but only as to underwriting relationships commencing after March 31, 2021. *See* MSRB Reminds Dealers of the March 31, 2021 Compliance Date for the Revised Interpretive Notice of Underwriters' Fair Dealing Obligations to Issuers (Mar. 31, 2021), https://www.msrb.org/sites/default/ files/2021-03.pdf. Accordingly, the 2012 Interpretive Notice applies to the relationships in this case. *See Walters v. J.P. Morgan Chase & Co.*, Case No. 20-12726, 2022 U.S. Dist. LEXIS 58600, at *42–48 (E.D.Mich. Mar. 29, 2022) (overview of municipal securities market).

[662] Reminder of Customer Protection Obligations (March 30, 2007).

investigate the securities offered to customers so as to have a reasonable basis for believing that key representations in the documents provided to investors are truthful and complete.[663]

In addition, a municipal securities dealer has an obligation under Rule G-17 to disclose all material information about a transaction that is known to the dealer or that is reasonably available to the dealer by accessing publicly available established industry resources. Such disclosures must be made at the time of sale or before. This disclosure obligation applies to any municipal securities transaction, either in a primary offering or on the secondary market.[664]

The overarching duty of fair dealing imposed by MSRB Rule G-17 also encompasses the more specific duties laid out in MSRB Rules G-19 and G-47. Before selling any municipal bond, a municipal securities dealer must make sure that it fully understands the bonds it is selling in order (i) to ensure that recommendations are suitable under Rule G-19 and (ii) to make appropriate disclosure of all material information to customers under Rule G-47. If a dealer violates MSRB Rules G-19 or G-47, the dealer cannot satisfy the Rule G-17 duty of fair dealing.

B. MSRB Rule G-19 – Suitability and Due Diligence

MSRB Rule G-19 is a suitability and due diligence rule. It requires that a municipal securities dealer have reasonable grounds for believing that the recommendation of a particular security is suitable for a customer, based upon (i) information about the security and (ii) facts known about the customer. The obligation arising under Rule G-19 requires a "meaningful analysis."[665] Like NASD Rule 2310, the predecessor to FINRA's suitability rule, MSRB Rule G-19's suitability obligation requires both a "reasonable basis" determination that the recommended security is suitable for at least some investors, and a "customer-specific" analysis that the security is suitable for the specific customer to whom the recommendation is made.[666] A dealer can only have reasonable grounds for believing a security to be suitable if the dealer conducts appropriate due diligence.[667]

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[663] *GLT Dain Rauscher*, 254 F.3d at 858.

[664] Guidance on Disclosure and Other Sales Practice Obligations to Individual and Other Retail Investors in Municipal Securities, July 14, 2009, https://www.msrb.org/Guidance-Disclosure-and-Other-Sales-Practice-Obligations-Individual-and-Other-Retail-Investors-0. FINRA has advised municipal securities dealers, "The MSRB has interpreted Rule G-17 to require a dealer, in connection with any transaction in municipal securities, to disclose to its customer, at or prior to the sale, all material facts about the transaction known by the dealer, as well as material facts about the security that are reasonably accessible to the market." FINRA Regulatory Notice 9-35, n. 5 (June 2009), https://www.finra.org/rules-guidance/notices/09-35.

[665] *Morgan Stanley Smith Barney, LLC*, Exchange Act Release No. 86988, 2019 SEC LEXIS 3943, at *7–8 (Sept. 17, 2019) (Order instituting administrative and cease-and-desist proceedings pursuant to Sections 15(b), 15B(c), and 21C of the Securities Exchange Act of 1934 and Section 203(e) of the Investment Advisers Act of 1940, making findings, and imposing remedial sanctions and a cease-and-desist order).

[666] FINRA Regulatory Notice 9-35, n. 5 (June 2009).

[667] *Dep't of Enforcement v. Patatian*, No. 2018057235801, 2023 FINRA Discip. LEXIS 13, at *35–37 (NAC Sept. 27, 2023), *appeal docketed*, No. 3-21796 (SEC Nov. 7, 2023).

On March 7, 2014, the SEC approved proposed rule changes to harmonize MSRB Rule G-19 with FINRA's suitability rule, FINRA Rule 2111,[668] but the general thrust of MSRB Rule G-19 remains the same. Both before and after the rule changes, MSRB Rule G-19 requires a municipal securities dealer to have a reasonable basis for a recommendation to buy or sell a municipal security. Although the revisions to MSRB Rule G-19 did not become effective until July 5, 2014, and were not applicable to the Quad Cities primary offering when it closed in 2013, none of the revisions altered Respondents' obligation under the previous version of Rule G-19 to conduct a "meaningful analysis" of the Quad Cities bond offering to ensure their suitability for customer investment. The MSRB retained its previous interpretative guidance and that guidance continues to be applicable, along with precedents established under FINRA Rule 2111. Under those Rule 2111 precedents, reasonable-basis suitability requires the exercise of reasonable due diligence sufficient to provide an understanding of the potential risks and rewards associated with a recommended security.[669]

C. MSRB Rule G-47 – Disclosure of All Material Facts Before or at Time of Trade

MSRB Rule G-47 requires a municipal securities dealer to disclose to customers at or prior to the time of trade all material facts known to it or reasonably available to it through public, established industry sources. Such sources include EMMA and publicly available bankruptcy filings. Specifically, the rule provides that a dealer must disclose at or prior to the time of trade "all material information known about the transaction and material information about the security that is reasonably accessible in the market." The rule applies whether a transaction occurs in the initial offering or on the secondary market. In particular, MSRB Rule G-47 requires disclosure of "facts that are material to assessing the potential risks of the investment."[670] Information is considered material if there is a substantial likelihood that the information would be considered important or significant by a reasonable investor in making an investment decision. Put another way, information is material if there is "a substantial likelihood that the disclosure of the omitted information would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[671]

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[668] In proposing revisions to MSRB Rule G-19 the MSRB explicitly stated that Rule G-19 "will be interpreted in a manner consistent with FINRA's interpretations of [FINRA] Rule 2111." Exchange Act Release 34-71665, 2014 SEC LEXIS 868, at *10 n.16 (Mar. 7, 2014) (Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Order Granting Approval of a Proposed Rule Change Consisting of Proposed MSRB Rule G-47, on Time of Trade Disclosure Obligations, Proposed Revisions to MSRB Rule G-19, on Suitability of Recommendations and Transactions, Proposed MSRB Rules D-15 and G-48, on Sophisticated Municipal Market Professionals, and the Proposed Deletion of Interpretive Guidance) ("SEC Order Approving MSRB Rule G-47 and Revisions to MSRB Rule G-19").

[669] *Dep't of Enforcement v. Lim*, No. 2014039091903, 2017 FINRA Discip. LEXIS 25, at *43–44 (OHO June 2, 2017) (discussing FINRA Rule 2111, Supplementary Material).

[670] MSRB Rule G-47, Supplementary Material, .01.

[671] *Basic v. Levinson*, 485 U.S. 224, 231 (1988) (quoting *TSC Indus. v. Northway*, 426 U.S. 438, 449 (1976)).

The SEC approved MSRB Rule G-47 in March 2014 and it became effective on July 5, 2014, along with the revisions to MSRB Rule G-19 discussed above.[672] Although Rule G-47 became effective after the 2013 Quad Cities offering closed, the obligation to disclose all known material facts was already an obligation under MSRB Rule 17 and its supplemental guidance.[673] In its order approving Rule G-47, the SEC noted that the MSRB did not intend for the new rule, Rule G-47, to "substantively change the current obligations" of municipal securities dealers. Rather the codification of existing obligations was merely intended to place them into "streamlined rule language."[674]

D. Section 17(a) of the Securities Act

Section 17(a) of the Securities Act contains three subsections. The first, Section 17(a)(1), prohibits the use of "any device, scheme or artifice to defraud" in the offer or sale of a security.[675] A misstatement of material fact or an omission of material fact needed to make what is said not misleading is a device or artifice to defraud. The term deceptive "encompasses a wide spectrum of conduct involving cheating or trading in falsehoods."[676] A statement or action is deceptive if it tends to give a false impression.[677] A material omission or misstatement is one which "would have been viewed by the reasonable investor as having significantly altered the total mix of information available."[678]

Proof of a violation of this subsection requires scienter.[679] Scienter is "a mental state embracing intent to deceive, manipulate, or defraud."[680] Recklessness can satisfy the scienter

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[672] SEC Order Approving MSRB Rule G-47 and Revisions to MSRB Rule G-19, Exchange Act Release No. 34-71665, 2014 SEC LEXIS 868 (Mar. 7, 2104).

[673] SEC Order Approving MSRB Rule G-47, 2014 SEC LEXIS 868, at *5–6 n.13. *See also* Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Notice of Filing of a Proposed Rule Change Consisting of Proposed MSRB Rule G-47, on Time of Trade Disclosure Obligations, Proposed Revisions to MSRB Rule G-19, on Suitability of Recommendations and Transactions, Proposed MSRB Rules D-15 and G-48, on Sophisticated Municipal Market Professionals, and the Proposed Deletion of Interpretive Guidance, Exchange Release No. 34-70593, 2013 SEC LEXIS 3077, at *3–4 (Oct. 1, 2013) ("The MSRB has interpreted Rule G-17 to require a dealer, in connection with a municipal securities transaction, to disclose to its customer, at or prior to the time of trade, all material information about the transaction known by the dealer, as well as material information about the security that is reasonably accessible to the market.").

[674] SEC Order Approving MSRB Rule G-47, 2014 SEC LEXIS 868, at *4.

[675] 15 U.S.C. § 77q(a)(1).

[676] *Dennis J. Malouf*, Exchange Act Release No. 78249, 2016 SEC LEXIS 2644, at *15 (July 27, 2016).

[677] *Id.* at n.20.

[678] *See*, *e.g.*, *SEC v. Laura*, No. 18-cv-5075 (HG) (VMS), 2023 U.S. Dist. LEXIS 111601, at *24 (E.D.N.Y. June 28, 2023).

[679] *Id. See also SEC v. Phan*, 500 F.3d 895, 907–08 (9th Cir. 2007); *SEC v. Fusion Hotel Mgmt. LLC*, No. 3:21-cv-02085-L-MSB, 2022 U.S. Dist. LEXIS 206187, at *8–9 (S.D. Cal. Nov. 10, 2022).

[680] *Dep't of Enforcement v. Smith*, No. 2015043646501, 2020 FINRA Discip. LEXIS 43, at *47 (NAC Sept. 18, 2020) (citing *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976)).

requirement.[681] Recklessness is defined as "an extreme departure from the standards of ordinary care . . . which presents a danger [of deceiving investors that] is either known to the [respondent] or is so obvious that the [respondent] must have been aware of it."[682] It is reckless disregard for the truth.[683] It may be inferred from circumstantial evidence suggesting an obvious risk of misleading investors that is so great that it is simply implausible that a respondent did not know about it.[684]

The two other subsections do not require scienter for a violation. A showing of negligence is sufficient.[685] Section 17(a)(2) makes it unlawful to offer or sell a security "by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading."[686] Section 17(a)(3) makes it unlawful to "engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser."[687] Negligent conduct under Sections 17(a)(2) and 17(a)(3) is the failure "to use the degree of care and skill that a reasonable person of ordinary prudence and intelligence would be expected to exercise in the situation."[688] As used in these provisions, negligence refers to a respondent's conduct, not respondent's state of mind.[689]

IV. Violations

We will not repeat the details of the misconduct here. Instead, we will briefly remind the reader of the nature of the misconduct and refer the reader to the previous relevant portions of this decision. Then we will explain why Respondents' arguments against liability fail.

A. Quad Cities – Negligent Misconduct

With respect to the Quad Cities offering, Enforcement's Complaint charges negligent misconduct. For purposes of MSRB Rule G-17 and Sections 17(a)(2) and 17(a)(3) of the

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[681] *Gebhart v. SEC*, 595 F.3d 1034, 1039–41 (9th Cir. 2010) (collecting cases).

[682] *City of Philadelphia v. Fleming Cos.*, 264 F.3d 1245, 1258 (10th Cir. 2001).

[683] *E.g.*, *Laura*, 2023 U.S. Dist. LEXIS 111601, at *24–25.

[684] *Smith*, 2020 FINRA Discip. LEXIS 43, at *47–48 (citing *Herman & MacLean v. Huddleston*, 459 U.S. 375, 390–91 n.30 (1983) and *Vernazza v. SEC*, 327 F.3d 851, 860–61 & n.8 (9th Cir. 2003)).

[685] *Aaron v. SEC*, 446 U.S. 680, 696–97, 701–02 (1980); *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, Exchange Act Release No. 40352, 1998 SEC LEXIS 1788, at *33 (Aug. 24, 1998); *SEC v. Wey*, 246 F. Supp. 3d 894, 912 (S.D.N.Y. 2017).

[686] 15 U.S.C. § 77q(a)(2).

[687] 15 U.S.C. § 77q(a)(3).

[688] *Dep't of Enforcement v. Cantone Research, Inc.*, No. 2013035130101, 2019 FINRA Discip. LEXIS 5, at *59 (NAC Jan. 16, 2019), *appeal docketed*, No. 3-18999 (SEC Feb. 14, 2019) (internal quotations omitted) (quoting *SEC v. True North Fin. Corp.*, 909 F. Supp. 2d 1073, 1122 (D. Minn. 2012)).

[689] *SEC v. Honig*, No. 18 Civ. 8175 (ER), 2020 U.S. Dist. LEXIS 31961, at *32 (S.D.N.Y. 2020).

Securities Act, negligent conduct is defined as "the failure to use reasonable care,"[690] or, phrased slightly differently, "the failure to use the degree of care and skill that a reasonable person of ordinary prudence and intelligence would be expected to exercise in the situation."[691] In this case, in connection with the Quad Cities offering, Respondents failed to act as a reasonably prudent person would be expected to act.

1. Cause I

In Cause I, the Complaint charges that Respondents willfully violated their duty under MSRB Rule G-19 to conduct the due diligence necessary to form a reasonable basis for believing the Quad Cities bonds a suitable investment for any investor. We find Respondents liable as charged. In their eagerness to market the bonds quickly after being presented with what DeRobbio called the "pre-packaged" offering, they ignored several red flags and relied instead on what the parties to the transaction told them.

One red flag was Stifel's unusual withdrawal from the underwriting without compensation or credit in the offering documents for the months of work it had devoted to the transaction. It did so because it could not obtain reliable information about the number of habitable beds at the dormitory and Swan did not think that the debt service coverage ratio Stifel had calculated was sufficient. Respondents' decision to go forward with the offering in reliance on the parties to the transaction was, at a minimum, negligent.[692]

Another red flag was the failure of the 2004 bond offering, which was dependent on revenues from the dormitory and which resulted in the borrower filing for bankruptcy. If Respondents had reviewed the bankruptcy filing, they would have learned many reasons to be skeptical of the viability of the 2013 Quad Cities offering. They would have learned that the same entity that was the borrower in the 2004 offering was the borrower in the Quad Cities offering. They also would have learned that BMOC was the management company for the dormitory all along, even before the bankruptcy filing. Additionally, they would have learned of the steady decline in revenues generated by the dormitory leading up to the bankruptcy, and they would have learned that, aside from a mortgage loan, the College was the dormitory's biggest creditor because the dormitory had failed to pay its water and sewer bills for years.[693]

A third red flag was the dormitory mold problem, which was serious enough that some unknown number of beds were "uninhabitable." There is no evidence that Respondents ever pressed the parties to the transaction for a precise number of uninhabitable beds, while there is

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[690] *SEC v. Jankovic*, No. 15 Civ. 1248 (KPF), 2017 U.S. Dist. LEXIS 40573, at *38 (S.D.N.Y. 2017) (quoting *SEC v. Cole*, No. 12-cv-8167 (RJS), 2015 U.S. Dist. LEXIS 132637 (S.D.N.Y. 2015)).

[691] *Id.* at *39 (quoting *SEC v. Schooler*, No. 3:12-cv-2164-GPC, 2015 U.S. Dist. LEXIS 71956 (S.D. Cal. 2015)). *See also Dep't of Enforcement v. NYPPEX, LLC*, No. 2019064813801, 2022 FINRA Discip. LEXIS 14, at *77 & n.353 (OHO Aug. 26, 2022), *appeal docketed*, (NAC Sept. 19, 2022).

[692] See *supra* at 32–36, 43–44.

[693] See *supra* at 21–24.

evidence that Swan repeatedly asked for that information. Swan's inability to get a straight answer to the question led to Stifel's withdrawal. Without reliable information regarding the number of beds available to generate revenues and support the bond offering, Respondents had no way of evaluating the financial projections for the offering. That meant they had no reasonable basis for thinking the bonds a reasonable investment for anyone.[694]

2. Cause II

In Cause II, the Complaint charges that Respondents made misrepresentations and omissions of material facts in connection with the Quad Cities offering in violation of MSRB Rule G-17, the fair dealing rule. The Complaint alleges that Respondents violated Rule G-17 both independently and by virtue of violating Sections 17(a)(2) and 17(a)(3) of the Securities Act. We find Respondents liable as charged. They made numerous misrepresentations and omissions of material fact, which were deceptive and unfair to investors.

In the final financial projections for the dormitory project, Respondents overstated the revenues the dormitory could generate. Historically, it had never achieved the occupancy rate required to make the project viable and the dormitory was unlikely to achieve the higher occupancy rate needed for the project to be successful, given the mold problem and uninhabitable rooms and the poor relationship between the dormitory and the College.[695]

Respondents also understated the management fees, which had the effect of lowering expenses and making the project appear more profitable and less risky than it was.[696]

Respondents described BMOC as though it were different from prior dormitory management, which encouraged investors to think that the 2013 Quad Cities offering was more likely to succeed than the prior offering. But BMOC had been the manager of the dormitory from the beginning and was responsible for the dormitory as its revenues declined and the borrower filed for bankruptcy.[697]

3. Cause V

Respondents also violated the fair dealing rule, MSRB Rule G-17 by failing to disclose all material facts they knew or reasonably could have known at or prior to the time of trade.[698]

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[694] See *supra* at 32–36, 43–44, 55–56.

[695] See *supra* at 23, 24–25, 32.

[696] See *supra* at 45–51.

[697] See *supra* at 22–25.

[698] In Cause V, the Complaint also charges that a handful of secondary market transactions in Quad Cities bonds violated MSRB Rule G-47. Those transactions occurred after the effective date of MSRB Rule G-47 (July 5, 2014). We find that those secondary market transactions violated both MSRB Rule G-17 and MSRB Rule G-47.

Respondents presented a critical piece of information, the debt service coverage ratio, in an opaque and misleading way. While the OS contained a few numbers for the ratio, Respondents removed any information from the financial projections regarding the debt service ratio, making it difficult if not impossible for investors to analyze and evaluate the figures. Respondents also failed to resolve issues relating to incomplete information affecting the debt service coverage ratio, such as the number of habitable beds and an accurate figure for the management fee.[699]

The financial projections themselves were changed from previous drafts so as not to identify their source clearly and accurately.[700]

Respondents misrepresented the relationship between the dormitory and the College. This was significant because the dormitory depended on the College for its pool of student renters and for water and sewer services.[701]

4. Respondents' Meritless Arguments

a. Reliance on Others

In connection with the Quad Cities offering, Respondents mainly argue in their pre-hearing brief that they reasonably relied on the due diligence already conducted by Stifel and its counsel.[702] They note that Stifel is a well-respected firm,[703] and that Stifel's counsel, who continued as counsel for Cantone Research when it became the underwriter, was "competent."[704] They rhetorically ask why they should have duplicated the due diligence those parties had already done, implying that it would have been a wasteful effort.[705] Respondents implicitly admit they conducted no meaningful due diligence themselves.

The argument that it was reasonable for Respondents to rely entirely on others must be rejected. Under the due diligence and suitability rule, MSRB Rule G-19, Respondents had a duty to understand the security and to develop a reasonable basis for believing it suitable for at least

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[699] See *supra* at 49–51.

[700] See *supra* at 51.

[701] See *supra* at 54.

[702] Resp. Br. 4–12.

[703] Resp. Br. 21 (Respondents "worked with one of the top firms in public finance (Stifel) in performing its due diligence obligations").

[704] Resp. Br. 21.

[705] Resp. Br. 4.

some investors. These obligations are "unequivocal."[706] Respondents cannot shift their responsibility under the MSRB rules for due diligence and suitability analysis to others.[707]

Furthermore, the factual support for the argument is lacking.

First, Stifel's involvement was not a basis for confidence that the Quad Cities bonds were a suitable investment for anyone. Stifel withdrew from the underwriting role and abruptly and inexplicably withdrew from any role in the offering without compensation after months of work on the transaction. Respondents should have recognized these events as a red flag and investigated the offering more thoroughly.[708]

Second, when Stifel withdrew from the offering it had not completed its due diligence. There was more to be done. Respondents could not simply rely on what Stifel had done up to the point that Respondents were introduced to the transaction.[709]

Third, although Respondents claim they relied on Stifel, DeRobbio "only talked to Mr. Swan a few times." Mostly, DeRobbio's contact was with Eric F., the party attempting to close the transaction, and Eric F.'s counsel, Attorney Brian M.[710]

Fourth, prior to the closing, Stifel did not share its due diligence file with Respondents. Respondents did not know what due diligence Stifel had done or what it knew about the proposed transaction when they marketed the Quad Cities bonds. It was only after FINRA started investigating the Quad Cities offering that DeRobbio asked Swan to give him Stifel's due diligence file, which Swan declined to do.[711]

Fifth, Respondents did not tell investors that Stifel was involved, much less that they were relying on its due diligence.[712]

Given what Respondents could have learned from the bankruptcy filing and from contacting the College, independent due diligence would not have been a wasteful effort. In these

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[706] *Dep't of Enforcement v. Wilson*, No. 2007009403801, 2011 FINRA Discip. LEXIS 67, at *49 (NAC Dec. 28, 2011).

[707] *See, e.g., William J. Murphy*, Exchange Act Release No. 69923, 2013 SEC LEXIS 1933, at *32 (July 2, 2013) (stating that applicants cannot shift to others the responsibility for their own compliance with applicable rules); *Dep't of Enforcement v. Frankfort*, No. C02040032, 2007 NASD Discip. LEXIS 16, at * 36–37 (NAC May 24, 2007) (stating that registered representative could not shift responsibility for compliance with NASD rules to others).

[708] See *supra* at 43–44.

[709] See *supra* at 39.

[710] See *supra* at 42–43.

[711] See *supra* at 56.

[712] Tr. (DeRobbio) 741–42.

circumstances, Respondents' failure to perform any meaningful due diligence was negligent at a minimum, and in violation of MSRB Rule G-19.

b. Deception Practiced by Others

Respondents also argue here, as they did in the Bondholder Litigation Cantone filed after the Quad Cities offering failed, that the parties they relied upon misled them. As DeRobbio testified, he believes Respondents were "duped" by the others involved in the offering.[713] Even if Respondents were misled by other parties involved in the transaction, this does not excuse them from liability for misleading investors. If Respondents had performed their own due diligence—as they were required to do—they would not have been misled. And, most importantly, they would not have misled their customers in violation of MSRB Rules G-17 and G-47 and Section 17(a) of the Securities Act.

c. Materiality

In their pre-hearing brief, Respondents argue that much of the information they failed to disclose to investors was not material. The standard for materiality is an objective one. A fact is material if there is a substantial likelihood that a reasonable person would have viewed it as significantly altering the total mix of information available.[714] We conclude that the information Respondents failed to disclose was material.

For instance, Respondents called the revenue data for 2007–2009, prior to the bankruptcy, irrelevant because the data was not current information and supposedly different individuals had been previously involved.[715] But the 2011 bankruptcy filing showed that the same entity owned the property before and after the bankruptcy and the same entity managed the property before and after.[716] The failure of their efforts to generate sufficient revenues from the dormitory in prior years casts doubt on their ability to turn a profit in the future.

Even aside from that, a steady decline in revenues prior to the bankruptcy would be material because it could signal problems with the building or other problems with the project that would be difficult for anyone to fix even if they were "new" to the facility. Moreover, Stifel had in its file information showing that revenues continued to decline after the bankruptcy, which would add to concern about the viability of the Quad Cities offering. Past financial performance was material to investors.[717]

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[713] See *supra* at 53.

[714] *E.g.*, *Dep't of Enforcement v. Spartan Cap. Sec., LLC*, No. 2019061528001, 2023 FINRA DISCIP. LEXIS 8, at *116–17 (OHO Mar. 28, 2023), *appeal docketed* (NAC Apr. 19, 2023).

[715] Resp. Br. 4–6.

[716] See *supra* at 21–22.

[717] See *supra* at 23–25.

Respondents also argue in their brief that the relationship between the College and the dormitory, at least as it related to the water and sewer contract, was not material because the College was required to maintain the water and sewer connections as long as the fees were paid. According to Respondents, the College could not terminate the connection.[718] But the bankruptcy filing in 2011 showed that the dormitory had not paid the fees for water and sewer services for years, and, regardless of whether the College had to continue providing services, that failure by the dormitory to pay its bills had to negatively affect the College's enthusiasm for marketing the dormitory to its students. Respondents characterized the College's cooperation in marketing the dormitory as critical to the success of the offering. But the College had little reason to encourage students to sign leases with the dormitory.[719]

d. Boilerplate Disclaimers

At the hearing, DeRobbio made several more arguments. He noted that the OS told investors that the information in it was furnished by others (including the borrower, the College, the Manager, and the issuer), not the underwriter, meaning not Cantone Research. The OS also cautioned that the information was not guaranteed to be accurate or complete.[720] These boilerplate disclaimers of responsibility did not relieve Respondents of their due diligence responsibilities and the requirement under MSRB rules and the securities laws that they not make material misrepresentations or omit material facts when selling the bonds.

e. Purported New Management for the Dormitory

DeRobbio also claimed that the representation in the OS that the dormitory would be more successful in the future because it was going to be under new management was not false. He said that BMOC had told Respondents that it was going to retain a different, more skilled employee to run the facility.[721] But the OS did not say that BMOC was going to retain a new person to manage the dormitory. Rather, the OS made it seem that the company that had managed the dormitory from the beginning, BMOC, was new. That was false.

f. Creation of Overall Misleading Impression

We believe it is important not only to explain that these individual misrepresentations and misleading omissions of material fact were by themselves violations but to understand that the overall presentation to investors was false and misleading. In conversations with customers, Respondents told them only positive things about the bonds they were buying. Although the OS for the Quad Cities offering mentioned the borrower's bankruptcy in the earlier bond offering, the OS left the impression that the project that went bankrupt was separate from the new project.

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[718] Resp. Br. 9.

[719] See *supra* at 21–22.

[720] Tr. (Moy) (questions from DeRobbio containing argument) at 568–69; JX-3, at 3.

[721] See *supra* at 95.

The new project was starting afresh with new ownership and management. The OS gave no hint that BMOC had been responsible for managing the dormitory all along, as it slid into bankruptcy, and that BMOC's management resulted in a dormitory in such disrepair that some beds/rooms were uninhabitable.

Furthermore, the arguments Respondents make as to individual details of their violations are inconsistent with each other. Their defense has no structural integrity. If Respondents were depending on Stifel, they did not tell customers that. They did not even mention Stifel to customers, either in the OS or in sales conversations. It would be a failure to disclose a material fact if Respondents were depending on Stifel to perform due diligence and they did not tell their customers that. And, although Respondents now say that the information they failed to disclose to customers was not material, they argued in the Bondholder Litigation and in DeRobbio's affidavit in support that the information *was* material.

In sum, Respondents' misconduct infected the entire underwriting process and marketing of the Quad Cities bonds. Any quibbles as to minor details cannot alter the overall conclusion that they failed to perform any meaningful due diligence and created a false impression of the dormitory's financial prospects. Respondents failed to fulfill their obligations under MSRB Rules G-19 and G-17 to conduct due diligence and deal fairly with customers.

5. Respondents' Willful Misconduct

Respondents make one other argument with respect to the Quad Cities offering that deserves attention. The Complaint charges that all of Respondents' violations were "willful," both in the Quad Cities offering and in the Montgomery 2015 offering. In their pre-hearing brief, Respondents assert that willfulness requires a level of misconduct higher than negligence,[722] citing *Robare*.[723] The Complaint charged Respondents with negligent violations in connection with the Quad Cities offering.

Whether Respondents' misconduct is found to have been willful is important. Under Section 3(a)(39)(F) of the Exchange Act, a person who willfully violates the federal securities laws or MSRB rules is subject to statutory disqualification from the securities industry.[724] Statutory disqualification is not a punishment or sanction, but, rather, a consequence imposed automatically by operation of the statute.[725]

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[722] Resp. Br. 21.

[723] *Robare Grp. Ltd. v. SEC*, 922 F. 3d 468, 479–80 (D.C. Cir. 2019).

[724] 15 U.S.C. § 78c(a)(39); *Thaddeus J. North*, Exchange Act Release No. 84500, 2018 SEC LEXIS 3001, at *22 & n.25 (2018).

[725] *North*, 2018 SEC LEXIS 3001, at *23. *See also Michael Earl McCune*, Exchange Act Release No. 77375, 2016 SEC LEXIS 1026, at *37 (Mar. 15, 2016).

It has been long held that a willful violation of the securities laws means merely "that the person charged with the duty knows what he is doing."[726] There is no requirement that the actor "also be aware that he is violating one of the Rules or Acts."[727] The act is willful if it is voluntary,[728] or, put another way, if the actor "intentionally commits the act that constitutes the violation."[729] The SEC continues to apply that definition of willful today,[730] as does the NAC.[731] The case most frequently cited for this definition of willful is *Wonsover*.[732]

In relying on *Robare*, Respondents ignore *Wonsover*.[733] In fact, *Robare* applied *Wonsover*, and *Wonsover* applies here.

Robare concerned Section 207 of the Investment Advisers Act, which makes it unlawful for any person "willfully to omit . . . any material fact" required to be stated in an application or report filed with the SEC. The issue in that case was whether the willful filing of a form that omitted required information or the willful omission of the information constituted the violation. The *Robare* court concluded that the violation defined in Section 207 was the willful omission of the information. It then held that liability under that section could only be imposed if the defendant "subjectively intended to omit material information" from the required disclosures.[734]

The *Robare* decision distinguished between the filing of the form, which was presumptively an intended act, not an accident, and the omission of the information, where the omission could have been an intentional act but also could have been inadvertent or accidental. *Robare* held in effect that the omission of required information could only be a violation of Section 207 of the Investment Company Act if it was an intentional omission, not an accident. As the SEC has said in an analogous context, "A failure to disclose is willful . . . if the [person]

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[726] *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (quoting *Hughes v. SEC*, 174 F.2d 969, 977 (D.C. Cir. 1949)).

[727] *Id.* (quoting *Gearhart & Otis, Inc. v. SEC*, 348 F.2d 798, 803 (D.C. Cir. 1965)).

[728] *Richard Allen Riemer, Jr.*, Exchange Act Release No. 84513, 2018 SEC LEXIS 3022, at *13 (Oct. 31, 2018).

[729] *Id.*

[730] *See*, *e.g.*, *Fifth Third Sec., Inc.*, Exchange Act Release No. 97937, 2023 SEC LEXIS 1837, at *10 n.10 (July 18, 2023) (willful defined for purposes of settlement of proceeding alleging violations of the Exchange Act and MSRB Rule G-27) (relying on *Wonsover*).

[731] *Dep't of Enforcement v. Henderson*, No. 2017053462401, 2022 FINRA Discip. LEXIS 15, at * 29 (NAC Dec. 29, 2022) ("A failure to disclose is willful . . . if the respondent of his own volition provides false answers on his Form U4.").

[732] *Wonsover*, 205 F. 3d 408.

[733] Resp. Br. 21.

[734] *Robare*, 922 F. 3d 468.

of his own volition provides false answers on his Form U4."[735] "An 'inadvertent filing of an inaccurate form' would not support a finding of willfulness."[736]

Robare does not require any higher standard of proof of willfulness than *Wonsover*. It does not preclude us from finding that the negligence-based violations found in connection with the Quad Cities offering were willful. Respondents engaged in negligent conduct in violation of MSRB rules and Sections 17(a)(2) and 17(a)(3) of the Exchange Act. In contrast to Section 207 of the Investment Advisers Act, these MSRB rules and provisions of Section 17(a) do not refer to willfulness in defining the violations. "In the context of Section 17(a), 'negligence' only refers to the conduct of the defendant, not the defendant's state of mind."[737] Negligence is the failure to use reasonable care regardless of a person's state of mind or reason for failing to use reasonable care. "Indeed, the distinguishing feature of Section 17(a) is the absence of a requirement that the plaintiff prove *any* state of mind."[738]

Accordingly, whether conduct is a violation of the MSRB rules and Sections 17(a)(2) and 17(a)(3) is evaluated by whether the conduct meets the standard of care. That is a separate question from whether the misconduct was willful. Under *Wonsover*, that misconduct may also be found to be willful if the conduct was no accident and the actor intended to engage in it.

We find here that Respondents underwrote the Quad Cities offering in reliance on others and without conducting the due diligence necessary in the circumstances to develop a reasonable basis for believing the securities a suitable investment for any customer. We further find that they made a host of material misrepresentations and omissions of material fact. As discussed above, their misconduct was negligent because it fell short of the standard of care they owed their customers under MSRB Rules G-19 and G-17, as well as Section 17(a) of the Exchange Act. Their acts were intentional, not accidental, so their misconduct also was willful within the meaning of *Wonsover*. As previously noted, this means Respondents are statutorily disqualified.

B. Montgomery 2015 – Fraudulent Misconduct

With respect to the Montgomery 2015 offering, the Complaint charges fraud-based violations.

1. Cause III

Cause III charges that Respondents fraudulently made misrepresentations and omissions of material fact in willful violation of MSRB Rule G-17 and Section 17(a)(1) of the Securities

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[735] *Riemer*, 2018 SEC LEXIS 3022, at *13 (quoting *Joseph S. Amundsen*, Exchange Act Release No. 69406, 2013 SEC LEXIS 1148 at *8 (Apr. 18, 2013)). *See also Spartan*, 2023 FINRA Discip. LEXIS 8, at *109 (respondents' deliberate, voluntary choice not to disclose arbitrations on their Forms U4 constituted willfulness).

[736] *Riemer*, 2018 SEC LEXIS 3022, at *13 (citing *Mathis v. SEC*, 671 F.3d 210, 218 (2d Cir. 2012)).

[737] *Honig*, 2020 U.S. Dist. LEXIS 31961, at *32 (citing *Cole*, 2015 U.S. Dist. LEXIS 132637, at *17).

[738] *Id.* (emphasis in original).

Act. The MSRB rule requires that a municipal securities dealer deal fairly with others in the conduct of its business dealings, including customers, and the statutory provision prohibits any deception or artifice to defraud. We find that Respondents acted with scienter. They knowingly or recklessly misrepresented and withheld material facts from their customers in violation of those provisions.

Respondents recklessly, if not knowingly, misrepresented the revenues that the facility was generating at the time it closed in the summer of 2013. They told customers that the facility was generating *monthly* net income of approximately $20,000. In fact, at the end of 2011 the facility had an *annual* net income of a little over $20,000. The facility had an *annual net loss* in 2012 and, by the time the facility closed in June 2013, it had a *year-to-date net loss* of $95, 931.85.[739]

Respondents knowingly failed to disclose to their customers that the person to whom investors were lending money to acquire, rehabilitate, and operate the defunct assisted-living facility had pled guilty to a criminal charge of misusing patients' money in connection with his nursing home business in South Carolina, lost his license to run such a facility in that state for about eight years, and been barred from the Medicare and Medicaid programs for 15 years. Instead, they falsely touted him as having successfully run such facilities for 35 years.[740]

Anthony Cantone (and through him, the Firm) knowingly failed to disclose that the Alabama assisted-living facility had been the subject of two earlier securities offerings underwritten by Cantone Research, Montgomery 2004 and Montgomery 2011. Cantone (and through him, the Firm) also knowingly failed to disclose that those offerings were not successful because the facility did not generate the revenues necessary to repay investors in those two offerings. DeRobbio knew that the first offering had not met its payment obligations to earlier investors. He knowingly failed to disclose that fact.[741]

Anthony Cantone (and through him, the Firm) knowingly failed to disclose that some of the proceeds of Montgomery 2015 were to be paid to investors in the two earlier failed offerings. DeRobbio knowingly arranged for some of the proceeds of Montgomery 2015 to be paid to investors in the first offering, Montgomery 2004, which he knowingly failed to disclose to investors.[742] The amount of money paid to earlier investors was significant, over $2.28 million.[743] Because some of the investors in Montgomery 2015 had also invested in one or both

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[739] See *supra* at 64, 77–78.

[740] See *supra* at 66–69, 78–79.

[741] See *supra* at 60–63.

[742] See *supra* at 80–82.

[743] CX-23.

of the earlier offerings, they unknowingly were paying themselves from the proceeds of Montgomery 2015, in effect moving money from one pocket to another.[744]

Anthony Cantone (and through him, the Firm) also knowingly failed to disclose that some of the proceeds of the Montgomery 2015 bond offering were to be paid to the borrower in the two prior failed offerings, Montgomery 2004 and Montgomery 2011. That borrower—Christopher Brogdon—had failed to pay investors in the prior offerings what he owed them and was under investigation by the SEC at the time of the Montgomery 2015 offering.[745]

Anthony Cantone (and through him, the Firm) knowingly failed to disclose that Cantone was to receive some of the proceeds of the Montgomery 2015 offering for the purpose of repaying him for money he had loaned to Brogdon to cover the shortfall in revenues to pay earlier investors in Brogdon-related offerings.[746]

2. Cause V

Cause V charges that Respondents failed to disclose at or prior to the time of trade all material facts known or reasonably accessible in the market in willful violation of MSRB Rule G-47. That rule, which became effective in July 2014, applied to all trades in Montgomery 2015 bonds. We find that Respondents willfully violated MSRB Rule G-47 by the above-cited failures to disclose material facts before or at the time of sale of the bonds.

3. Respondents' Meritless Arguments

Respondents assert that what they disclosed in the Montgomery 2015 OS was sufficient, and any information they failed to disclose to investors was not material.[747] Their argument has no merit.

As noted above in connection with the Quad Cities offering, a fact is material if there is a substantial likelihood that a reasonable person would have viewed it as significantly altering the total mix of information available.[748] We find that Respondents made multiple misrepresentations and omissions of material fact in the Montgomery 2015 offering. If any one of these misrepresentations or omissions had been fully and accurately disclosed, it would have caused a reasonable investor some concern and would have been viewed as altering the total mix of information available. If all the material information that Respondents concealed from their

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[744] CX-22.

[745] See *supra* at 80–82.

[746] Cause IV was pled in the alternative to Cause III. If the Extended Hearing Panel did not find that Respondents' conduct in connection with Montgomery 2015 was fraudulent, Enforcement charged in the alternative that the conduct was a negligent and willful violation of MSRB Rule G-17. We find the Respondents' conduct was fraudulent, but, if we did not, we would find it a negligent and willful violation of MSRB Rule G-17).

[747] Resp. Br. 12–16.

[748] *E.g.*, *TSC Indus.*, 426 U.S. at 449; *Spartan*, 2023 FINRA DISCIP. LEXIS 8, at *116–17.

customers had been combined and properly disclosed, it is doubtful that Respondents could have sold the Montgomery 2015 bonds to anyone.

First, Respondents falsely represented that the facility was generating $20,000 per month of income when it shut down in 2013, when, in fact, it had been suffering substantial losses throughout 2012 and 2013 until it closed.[749] We find this a misstatement of material fact. They argue, however, that prior operational issues suffered by prior management are not relevant to the future.[750] The very fact that Respondents misrepresented the revenue stream generated by the facility undercuts their argument. They knew that it would be easier to sell the bonds if they described the facility as having a positive cash flow instead of revealing its true dismal financial performance. That is why they concealed this information.

Second, Respondents failed to disclose Edwards' criminal history, South Carolina license suspension, and long exclusion from the Medicare and Medicaid programs.[751] We find that these were omissions of material facts. In defense, Respondents argue that Edwards' guilty plea was long ago, 19 years before the Montgomery 2015 offering, and no longer relevant.[752] But Edwards' misconduct was directly relevant to his trustworthiness to operate an assisted-living facility, and his long exclusion from the Medicare and Medicaid programs was in effect for 15 years, until 2012. The severity of the sanction was significant and it was in effect up until a few years before the Montgomery 2015 offering. Again, the fact that Edwards wanted to treat his criminal background as though it had never happened undercuts the argument that it was not material. He knew, as did Respondents, that disclosure would make it difficult to sell the bonds.

Third, with respect to the failure to disclose Edwards' criminal background, license suspension, and long exclusion from the Medicare and Medicaid programs, Respondents raise an affirmative defense. They assert that they relied upon advice of counsel in determining not to disclose the information about Edwards.[753] The burden is on Respondents to establish the defense. They must show that they (i) made complete disclosure of the relevant facts of the intended conduct to counsel; (ii) sought advice regarding the legality of the intended conduct; (iii) received advice that the intended conduct was legal; and (iv) relied in good faith on counsel's advice.[754] A respondent cannot rely on advice of counsel if the record does not show

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[749] See *supra* at 64, 77–78.

[750] Resp. Br. 13.

[751] See *supra* at 68–69, 78–79.

[752] Resp. Br. 15–16.

[753] Resp. Br. 15.

[754] *Cantone Research*, 2019 FINRA Discip. LEXIS 5, at *103–04 (citing *Markowski v. SEC*, 34 F. 3d 99, at *104–05 (2d Cir. 1994) and *Howard Brett Berger*, Exchange Act Release No. 58950, 2008 SEC LEXIS 3141, at *40–41 (Nov. 14, 2008), *aff'd*, 347 F. Appx 692 (2d Cir. 2009)).

with any specificity what advice the respondent received from counsel.[755] Vague allusions to legal advice are not sufficient.[756]

Here, Respondents have done no more than make vague allusions to legal advice. There is no evidence that Respondents requested specific legal advice on disclosure of Edwards' background or of what Respondents and their counsel might have discussed in that regard. Nor is there any evidence that Respondents' counsel gave them legal advice regarding disclosure of Edwards' criminal background. There is only an email from Attorney Michael G, the attorney Cantone Research sued for malpractice, to bond counsel in the Walton offering reporting that Attorney Michael G. and Cantone Research's counsel in that offering had agreed that disclosure (without describing disclosure of what) would not be appropriate (without explaining why or any legal basis for the conclusion). The record shows that DeRobbio was copied on the email and forwarded it to the Firm's then compliance officer, Christine Cantone, but there is no evidence demonstrating what legal advice was sought, received, or relied upon. DeRobbio revealed in his hearing testimony that he thought they should have disclosed Edwards' background but he was intimidated by Edwards' attorney's threat that DeRobbio could be sued for libel if he did disclose it.[757] Respondents have failed to establish the affirmative defense.

4. Respondents' Willful Misconduct

Respondents did not dispute in their pre-hearing brief that their misconduct in connection with the Montgomery 2015 offering was willful. We specifically find that they willfully violated MSRB Rules G-17 and G-47 in connection with that offering. Their misconduct was not inadvertent or accidental. As discussed above, this finding automatically results in statutory disqualification.

C. Summary of Findings of Violations

With respect to the Quad Cities offering, the Extended Hearing Panel finds that all Respondents committed the negligence-based violations charged in Cause I, Cause II, and Cause V. Respondents violated MSRB Rules G-17, G-19, and (to the extent transactions occurred on or after it became effective on July 5, 2014) G-47, along with Securities Act Sections 17(a)(2) and 17(a)(3). The violations were willful.

With respect to the Montgomery 2015 offering, the Extended Hearing Panel finds that all Respondents committed the fraud-based violations charged in Cause III and Cause V. All

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[755] *Eugene T. Ichinose*, Exchange Act Release No. 17381, 1980 SEC LEXIS 105, at *5 (Dec. 16, 1980).

[756] *Dan Rapoport*, Exchange Act Release No. 63744, 2011 SEC LEXIS 231, at *18 n.27 (Jan. 20, 2011).

[757] See *supra* at 66–70, 78–79.

Respondents violated MSRB Rules G-17 and G-47, along with Section 17(a)(1). The violations were willful.[758]

V. Sanctions

A. FINRA's Sanction Guidelines

In considering the appropriate sanction for a violation, adjudicators in FINRA disciplinary proceedings use FINRA's Sanction Guidelines ("Guidelines")[759] as their benchmark. Recommended sanctions range from suspensions and bars from the industry to fines, restitution, and disgorgement. They may include ordering a person to requalify and other measures as well. They distinguish between small firms and midsize or large firms and modify their recommendations for fines according to the size and resources of a respondent firm.[760] We have studied and applied the Guidelines, as we discuss below.

In addition to the Guidelines, we are conscious of judicial decisions holding that "FINRA is generally prohibited [under the Exchange Act] from imposing 'excessive or oppressive' penalties"[761] Courts have construed the statute as authorizing remedial, but not punitive, sanctions.[762]

Remedies like restitution that are directed toward correcting or undoing the effects of wrongdoing have been long recognized as equitable remedies well within the proper scope of sanctions deployed in FINRA disciplinary proceedings.[763] The Guidelines instruct that adjudicators may order restitution when an identifiable person has suffered a quantifiable loss proximately caused by a respondent's misconduct.[764]

Recent decisions explain, however, that compensating victims is not the only appropriate sanction for violations of the securities laws and regulations. Those decisions hold that even a bar from the industry is remedial, not punishment, where the purpose of the sanction is to protect the public.[765] Accordingly, our focus in considering the appropriate sanctions in this case is not

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[758] With respect to the Montgomery 2015 bonds, Enforcement pled negligent violations in Cause IV in the alternative to the fraud claims in Cause III. We have found the fraud claims in Cause III proven. If we had not, we would have found, at a minimum, that Respondents negligently committed the violations alleged.

[759] Guidelines (Sept. 2022), https://www.finra.org/sanctionguidelines.

[760] We have treated Cantone Research as a small firm for purposes of monetary sanctions such as fines.

[761] *Springsteen-Abbott v. SEC*, 989 F. 3d 4, 9 (D.C. Cir. 2021).

[762] *Siegel v. SEC*, 592 F. 3d 147, 157 (D.C. Cir. 2010).

[763] *Dep't of Enforcement v. Wicker*, No 2016052104101, 2021 FINRA Discip. LEXIS 31, at *55 (NAC Dec 15. 2021), *appeal docketed*, No. 3-20705 (SEC Jan. 13, 2022) (restitution primarily seeks to return customers to their prior position by restoring the funds of which they were wrongfully deprived).

[764] Guidelines at 2 (General Principle 1).

[765] *Springsteen-Abbott,* 989 F. 3d at 9. *See also Saad v. SEC*, 980 F. 3d 103, 107 (D.C. Cir. 2020).

only on the specifics of the Guidelines but also on the overarching purpose of protecting the public.

The Guidelines contain General Principles Applicable to All Sanction Determinations ("General Principles"), which should be considered with the imposition of sanctions in all cases, and Principal Considerations in Determining Sanctions ("Principal Considerations"), which enumerate generic factors for consideration in all cases where they might be applicable. In addition, the Guidelines contain some considerations that are particular to specific violations ("Specific Considerations"). The Guidelines recommend a range of sanctions that may be appropriate for specific types of violations, depending on the circumstances and any aggravating and mitigating factors. But the recommendations are not absolute. If appropriate, adjudicators may impose sanctions outside the ranges recommended. The Guidelines are not rigid.[766]

The Guidelines are designed to promote consistency and fairness in the resolution of FINRA disciplinary proceedings. They are also intended to protect investors and other participants in the securities markets by deterring respondents from engaging in misconduct in the future, guiding others on how to avoid similar misconduct, and remedying injuries caused by the misconduct to the extent possible. The imposition of sanctions, when necessary, builds public confidence in the financial markets. Protecting investors and building public confidence in the markets are both important to FINRA's regulatory mission.[767]

The Guidelines permit the aggregation or "batching" of violations for purposes of determining sanctions rather than imposing sanctions for each individual violation.[768] In this case, we find it appropriate to batch all the violations relating to a particular offering. The misconduct relating to a single offering was all related and part of a single selling strategy.[769] However, we do not find it appropriate to aggregate all the misconduct in both offerings for purposes of sanctions. The misconduct in the Quad Cities offering was negligent; the misconduct in the Montgomery 2015 offering was fraudulent. And the two offerings themselves were unrelated and have separate histories.

Even though we have determined that each offering should be treated separately for purposes of sanctions, much of the analysis of aggravating and mitigating factors applies equally to both offerings. In an attempt to be more efficient, we will discuss those factors in one section below. We will highlight where the second offering, Montgomery 2015, has its own additional aggravating factors.

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[766] Guidelines at 1 (Overview) and 3–4 (General Principle 3).

[767] Guidelines at 1 (Overview) and 2 (General Principle 1).

[768] Guidelines at 4 (General Principle 4).

[769] *E.g., Patatian*, 2023 FINRA Discip. LEXIS 13, at *69–70 (unitary sanction appropriate where individual transactions arose out of same strategy of recommending unsuitable REIT investments).

Finally, we recognize that some aggravating factors apply to Anthony Cantone and the Firm but not to DeRobbio, which we will also note below. DeRobbio urged at the hearing that his misconduct was different and should not be treated as harshly as Cantone's.[770] In the end, however, we conclude that DeRobbio would be a risk to the public if he were allowed to remain in the industry. That Cantone's misconduct was worse than DeRobbio's does not warrant lesser sanctions for DeRobbio.[771]

B. Sanctions Recommended in the Guidelines

1. Quad Cities

In connection with the Quad Cities bond offering, we have found that Respondents failed to perform any meaningful due diligence in violation of MSRB Rule G-19 and that led to many false and misleading misrepresentations and omissions of material fact in violation of MSRB Rule G-17 and Securities Act Sections 17(a)(2) and 17(a)(3). Respondents' misconduct proximately caused numerous customers significant losses. Customers would not have bought the bonds if they had known the truth. Enforcement proved that Respondents' conduct did not meet the standard of reasonable care and was, at a minimum, negligent.

In determining the sanctions that should be imposed in connection with the Quad Cities offering, we consulted the Guidelines for two types of violations: (i) suitability and (ii) negligent misrepresentations and omissions of material fact.

For making unsuitable recommendations, the Guidelines recommend suspending an individual respondent in any or all capacities for a period ranging from 10 business days to two years. The Guidelines recommend that adjudicators "strongly" consider a bar, however, where aggravating factors predominate. A fine of $2,500 to $40,000 may be imposed.[772] With respect to suitability violations by the Firm, the Guidelines recommend a suspension for up to three months—except where aggravating factors predominate. If aggravating factors predominate, adjudicators may suspend a firm for up to two years or even expel it. For a small firm like Cantone Research, the Guidelines also recommend a fine of $5,000 to $116,000.[773]

Where an individual is found liable for negligent misrepresentations or omissions of material fact, the Guidelines recommend suspending the respondent for a period ranging from one month to two years. A fine of $5,000 to $50,000 may also be imposed.[774] With respect to negligent misrepresentations and omissions of material fact by the Firm, the Guidelines

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[770] Tr. (DeRobbio) 1614–16.

[771] *Patatian*, 2023 FINRA Discip. LEXIS 13, at *74 (quoting *Beyn*, 2024 SEC LEXIS 980, at *19–20 ("[t]he fact that others also might have been remiss in their duties does not mitigate [the respondent's] responsibility")).

[772] Guidelines at 121.

[773] Guidelines at 69.

[774] Guidelines at 116.

recommend a suspension with respect to the relevant business lines or activities for up to three months. In addition, they recommend a fine for a small firm like Cantone Research of $5,000 to $77,000.[775]

Whether dealing with an individual respondent or a firm, and whether dealing with a suitability violation or negligent misrepresentations and omissions of material fact, the Guidelines direct adjudicators to review the Principal Considerations applicable in all cases.[776] We have done so.

2. Montgomery 2015

We find that Respondents fraudulently, with scienter, sold the Montgomery 2015 bonds in violation of their duty of fair dealing under Rule MSRB G-17, both independently and by virtue of violating Section 17(a)(1) of the Securities Act. They also failed to disclose accurately all material facts to their customers, either in the initial offering or on the secondary market, in violation of MSRB Rule G-47. Respondents' violations were willful.

In considering the appropriate sanctions for the fraud violations we have looked to the Guidelines for fraud, misrepresentations, or omissions of material fact. For the Firm, the Guidelines recommend that where aggravating factors predominate—as they do here—adjudicators should strongly consider expelling the firm. For a small firm like Cantone Research, the Guidelines recommend a fine of $25,000 to $310,000.[777] With respect to individual violators, the Guidelines recommend that adjudicators "strongly" consider barring the respondent. A suspension might be warranted if mitigating factors predominate. A fine might be imposed, ranging from $10,000 to $100,000.[778]

Whether a respondent is a firm or an individual, the Guidelines instruct adjudicators to consult the Principal Considerations applicable to all cases.[779] We have done so.

C. Analysis of Aggravating and Mitigating Factors

We find that aggravating factors predominate as to all Respondents. The following factors are aggravating:

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[775] Guidelines at 64.

[776] Guidelines at 64, 69.

[777] Guidelines at 64.

[778] Guidelines at 116.

[779] *Id.*

First, no Respondent accepts responsibility for the misconduct.[780] DeRobbio explicitly stated at the hearing regarding the Quad Cities offering, "I'm not accepting blame, no."[781] With respect to the Montgomery 2015 offering, DeRobbio took no responsibility because he claimed he was relying on advice of counsel. He argued that counsel and other Firm principals were responsible for due diligence on the transactions.[782] He said, "As a registered rep with the firm, I have the right to rely on the information provided to me by my firm and the work done by outside experts."[783] He said the words, "I fully accept responsibility for my actions."[784] But his testimony conveyed otherwise. He communicated his sense that others may have committed wrongdoing, but he did not. A respondent's failure to accept responsibility and to attempt to shift blame to others increases the likelihood that the respondent would engage in similar misconduct in the future.[785]

This aggravating factor is particularly egregious with respect to the other two Respondents. Neither Anthony Cantone nor the Firm appeared at the hearing to defend or explain their actions. Even though they agreed when they entered the industry as a FINRA member and registered representative to participate in any disciplinary proceeding and comply with any orders issued in such a proceeding, Cantone and the Firm have defied any regulatory oversight. They seek to avoid even the possibility of being held accountable for misconduct by refusing to participate in the proceeding. This refusal to be subject to discipline means that there is no reason to believe that Anthony Cantone or the Firm could be expected in the future to comply with their legal and regulatory obligations. The public would be put at risk if they were permitted to continue in the industry.[786]

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[780] Guidelines at 7 (Principal Consideration 2).

[781] Tr. (DeRobbio) 726.

[782] Tr. (DeRobbio) 1613.

[783] Tr. (DeRobbio) 1614.

[784] Tr. (DeRobbio) 1616.

[785] *Springsteen-Abbott*, Exchange Act Release 88156, 2020 SEC LEXIS 2684, at *33–34, n. 37 (Feb. 7, 2020), *petition for review dismissed in part and denied in part*, 989 F.3d 4; *Mitchell H. Fillet*, Exchange Act Release No. 79018, 2016 SEC LEXIS 3773, at *18 (Sept. 30, 2016); *Thomas D. Conrad, Jr.*, Investment Advisers Act Release No. 6467, 2023 SEC LEXIS 3123, at *11 (Oct. 20, 2023).

In fact, DeRobbio attempted to mischaracterize what happened in this case, as though a couple of offerings happened to go sour. DeRobbio asserted, "I have done hundreds of issues the same way, and they've worked out, but now we're down to two that didn't." Tr. (DeRobbio) 1257. He remained oblivious to the true character of his misconduct.

[786] Guidelines at 1 (Overview).

Second, Respondents' misconduct significantly harmed customers.[787] Customers suffered over $1.5 million in losses on the Quad Cities bonds[788] and almost $3.3 million in losses on the Montgomery 2015 bonds.[789]

Third, because many of the customers were elderly,[790] they did not have time to recoup their losses. In fact, one of the customers who was injured and who had agreed to testify at the hearing died before he was able to testify.[791]

Fourth, contrary to Respondents' assertion in their pre-hearing brief, the customers were not sophisticated investors. They had limited investment experience and relied on Respondents to evaluate the suitability and financial prospects of the investment.[792]

Fifth, there were a large number of violative transactions, more than 60 in the Quad Cities offering[793] and more than 110 in the Montgomery 2015 offering.[794] These were not isolated instances of misconduct.[795]

Sixth, Respondents attempted to conceal their own lack of due diligence in the Quad Cities offering by filing the Bondholder Litigation against various other parties to the offering, alleging that Respondents and the purchasers of the bonds had been deceived.[796] DeRobbio's affidavit was central to that litigation. In it, he complained in detail of myriad ways the parties to the offering misled Respondents. The affidavit highlighted numerous misleading aspects of the OS for the offering. DeRobbio's affidavit is inconsistent with Respondents' argument in this case that various omissions of fact were not material. The Bondholder Litigation led investors in the Quad Cities bonds to believe, incorrectly, that Respondents had all along been protecting their interests. In this way it discouraged customers from blaming Respondents for their losses.

Seventh, at least with respect to the Montgomery 2015 offering, Respondents' misconduct was the result of acts that were intentional or, at a minimum, reckless.[797]

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[787] Guidelines at 7 (Principal Consideration 11).

[788] CX-25.

[789] CX-26.

[790] Guidelines at 8 (Principal Consideration 20).

[791] Customer KE testified that his father, another customer of Anthony Cantone who purchased Quad Cities bonds, died on November 15, 2022, just two weeks short of his 94th birthday. Tr. (KE) 915–16.

[792] Guidelines at 8 (Principal Consideration 18).

[793] CX-5.

[794] CX-21.

[795] Guidelines at 8 (Principal Consideration 17).

[796] Guidelines at 7 (Principal Consideration 10).

[797] Guidelines, at 8 (Principal Consideration 13).

Eighth, in connection with both offerings, Respondents engaged in the misconduct to achieve monetary gain.[798] The Firm and the individual Respondents received commissions and fees in connection with the offerings.[799] DeRobbio received a finder's fee if a municipal bond offering closed.[800] Cantone needed to close on Montgomery 2015 to receive funds to repay him for money he had lent to Brogdon.

Ninth, in support of stringent sanctions, Enforcement argues that Cantone and the Firm are recidivists,[801] which is an aggravating factor under the Guidelines.[802] A pattern of misconduct that causes investor harm, damages market integrity, and disregards regulatory requirements may justify imposing more severe sanctions.[803]

For purposes of determining sanctions in this case, we distinguish between a person who has already been subject to disciplinary sanctions and yet, with knowledge that the conduct is condemned, persists in similar wrongdoing and a person who is shown to have engaged in a pattern of misconduct. Respondents are not recidivists in the first sense—but they are in the second sense.

To demonstrate that Anthony Cantone and the Firm are recidivists, Enforcement points to the FINRA disciplinary proceeding that resulted in a finding that they had committed fraud and other violations. The earlier FINRA disciplinary proceeding cited by Enforcement commenced with the filing of a complaint in 2013, the same year as the Quad Cities offering, but it was not resolved at the hearing level by an Extended Hearing Panel decision until 2017, after both the Quad Cities and Montgomery 2015 offerings. The New Jersey consent order that Enforcement cites was also issued in 2017, after the two offerings in this case. This means that it cannot be said that Respondents engaged in the misconduct alleged in this proceeding despite having already been subjected to prior disciplinary sanctions for similar misconduct. There had not yet been a resolution of the other matters at the time of the offerings in this case.[804]

On the other hand, even though those cases were not resolved until after the offerings at issue here, they are relevant. At the time of the two offerings charged in this case, Respondents knew that the conduct in the SEC and New Jersey cases had drawn regulatory scrutiny. And the SEC and New Jersey proceedings show a pattern of misconduct by Anthony Cantone and the

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[798] Guidelines, at 8 (Principal Consideration 16).

[799] CX-6; CX-19.

[800] Tr. (DeRobbio) 1611.

[801] Enf. Br. 34 & n.172.

[802] Guidelines at 7 (Principal Consideration 1).

[803] Guidelines at 2–3 (General Principle 2) (discussing pattern of misconduct).

[804] *Dep't of Enforcement v. Springsteen-Abbott*, Discip. Proceeding No. 2011025675501, 2015 FINRA Discip. LEXIS 15, at *145–46 (OHO Mar. 30, 2015), *aff'd*, 2016 FINRA Discip. LEXIS 39 (NAC Aug. 23, 2016), *remanded on other grounds,* 2011025675501r, 2017 FINRA Discip. LEXIS 23 (NAC July 20, 2017), *modified*, 2020 SEC LEXIS 2684.

Firm that should be considered in assessing appropriate sanctions. Furthermore, the evidence in this case has revealed a series of other offerings in which all the Respondents have engaged in misconduct. It is well-established that evidence of misconduct not charged in the complaint, but which is similar to the misconduct that is charged, is admissible in determining sanctions.[805]

We conclude that Anthony Cantone (and through him, the Firm) have engaged in a pattern of similar misconduct that inflicted harm and disregarded regulatory requirements. He and the Firm were found in the other FINRA disciplinary case to have engaged in fraud and other violations in connection with multiple private placement transactions, including the Montgomery 2011 offering. In those transactions, Cantone and the Firm failed to disclose negative financial and legal history regarding Brogdon, whose projects were supposed to generate the revenues to pay investors. Instead, Cantone and the Firm touted Brogdon's business acumen and decades of success, just as they touted Dwayne Edwards' success in this case and ignored his criminal background, license suspension, and long exclusion from the Medicare and Medicaid programs.

We also find a pattern in the evidence presented in this case. Anthony Cantone and the Firm engaged in similar misconduct in both the Quad Cities offering and the Montgomery 2015 offering. And they engaged in the same kind of misconduct in connection with the Walton offering as well. In the Walton offering, just as in Montgomery 2015, they misrepresented Dwayne Edwards' 35-year history in the assisted-living industry and failed to disclose his criminal background, suspension of his South Carolina license for eight years, and 15-year bar from the Medicare and Medicaid programs.

Although DeRobbio was not involved in the earlier FINRA disciplinary proceeding against Anthony Cantone and the Firm or the New Jersey consent order, we find that he also has engaged in a pattern of misconduct. In the Quad Cities offering, the Montgomery 2015 offering, and the Walton offering, he engaged in similar misconduct, misrepresenting material facts and failing to disclose other material facts—creating an overall misleading impression of the financial viability of the bonds. He also arranged for some of the proceeds from the Montgomery 2015 offering to be used to pay investors in Montgomery 2004 to redeem their bonds, contrary to the OS in each offering. And there was evidence that he sold bonds generally on the theory that such use of funds from one project to support another "weak sister" was appropriate.[806] It was not.

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[805] *See Dep't of Enforcement v. McCrudden*, No. 2007008358101, 2010 FINRA Discip. LEXIS 25, at *26 & n.20 (NAC Oct. 15, 2010) (citing *Wanda P. Sears*, Exchange Act Release No. 58075, 2008 SEC LEXIS 1521, at *22 n.33 (July 1, 2008) (finding, in an unauthorized trading case, that evidence of unauthorized trading, which was not alleged in the complaint, was admissible to gauge aggravating factors to assess sanctions); *Gateway Int'l Holdings, Inc.*, Exchange Act Release No. 53907, 2006 SEC LEXIS 1288, at *24 n.30 (May 31, 2006) (stating that, "[a]lthough we are not finding violations based on [other] failures [to file timely reports], we may consider them, and other matters that fall outside the [Order Instituting Proceedings], in assessing appropriate sanctions").

[806] *See supra* at 60 n.349.

There are no mitigating factors. Although Respondents argue that they were "duped" and deceived by the parties to the Quad Cities transaction, we do not find that mitigating. If they were deceived, it was because they violated their duty under MSRB Rule G-19 to conduct due diligence and develop their own reasonable basis for believing the Quad Cities bonds a suitable investment, at least for some investors. Similarly, in connection with Montgomery 2015, although Respondents argue that they did not disclose Dwayne Edwards' troubling history because they relied on advice of counsel, we have concluded that there was no reasonable reliance on advice of counsel.[807]

D. Individual Bars and Expulsion of the Firm

1. Anthony Cantone and the Firm

We conclude on this record that Anthony Cantone should be barred for the violations related to each offering and the Firm should be expelled. They have engaged in a pattern of serious misconduct. Indeed, Cantone's business model seems built on a cycle of offerings, with one being used to pay the debt of another to conceal any failures as long as possible. Cantone and the Firm also have inflicted significant harm on vulnerable, elderly, and unsophisticated investors. In connection with the Quad Cities offering, their use of the Bondholder Litigation to mislead investors and direct attention away from their own failure to perform adequate, independent due diligence adds to our concern about their future conduct. Moreover, they have been unwilling to submit to regulatory oversight. FINRA would be unable to fulfill its regulatory mission to protect investors and strengthen market integrity if they were to remain in the industry free of oversight. They would be a grave risk to the public if allowed to remain in the industry.

We acknowledge that in September, after the hearing, the Firm withdrew from the industry and at that point Anthony Cantone was no longer registered. We also acknowledge that Cantone agreed in a separate matter in December to be barred from associating with any FINRA member in all capacities.

Nevertheless, it is important that we complete, record, and make public our findings and conclusions in this disciplinary proceeding. Completion of the process ensures that Cantone and the Firm cannot in the future assert that the charges against them were never proven. If we did not make findings and conclusions in this case, Cantone would be free to reenter the industry without a disciplinary record with respect to the misconduct proven in this case. Despite the bar Cantone accepted in the AWC he signed in December, his reentry into the industry is possible if a FINRA member firm sponsors him through the Membership Continuance Application ("MC-400 Application") process. In that process, FINRA may permit a statutorily disqualified person to associate with a FINRA member firm if the firm applies for permission and agrees to certain conditions to restrict and oversee that person's activities. Barring Anthony Cantone for the misconduct proven in this case is the appropriate way to ensure that he is not allowed to resume activities that put investors at risk without significant protective conditions. Furthermore,

[807] Guidelines at 7 (Principal Consideration 7).

concluding our analysis and setting it forth on the public record protects investors by alerting and educating them as to the type of misconduct that may encounter. It encourages them to proceed cautiously and inform themselves when they invest. And completion of the disciplinary process further protects investors by deterring Respondents and others from similar misconduct in the future.

2. DeRobbio

We recognize that Anthony Cantone engaged in misconduct that DeRobbio did not. Cantone propped up Brogdon's failing projects by lending him money and using the Montgomery 2011 private placement to conceal that Montgomery 2004 had failed. Then Cantone arranged for himself to be repaid from the proceeds of Montgomery 2015. DeRobbio was not involved in that misconduct, and he argues on that basis that we should distinguish him and his actions from those of Cantone and the Firm.

Nevertheless, the misconduct in which DeRobbio did engage was extremely serious. He conducted no meaningful due diligence in the case of the Quad Cities offering. He was simply eager to market the bonds as soon as he could, ignoring numerous red flags. DeRobbio also engaged in fraudulent and deceptive misconduct in the Montgomery 2015 offering. Among other things, in connection with that offering, DeRobbio admitted that he knew that Dwayne Edwards' background was troubling and that a prudent investor would want to know about it. But he failed to disclose Edwards' background because, he claims, he was threatened with a libel suit. DeRobbio was more concerned about the risk that he might be sued than the risk that his customers might lose money investing with an unscrupulous person. DeRobbio also knew that the proceeds of the Montgomery 2015 offering were going to be used to pay earlier investors in the failed Montgomery 2004 offering. He instructed the bank trustee for the Montgomery 2004 offering to pay investors in that earlier offering with proceeds from Montgomery 2015. Using the proceeds of one offering to make payments to investors in another project was contrary to both the Montgomery 2015 OS and the Montgomery 2004 OS. These were conduit bonds that depended solely on the financial performance of the single, specified project for payment.

Although DeRobbio did participate in the disciplinary process throughout and attended the hearing, we believe he also represents a high risk to investors in the future if he is permitted to continue in the industry. He brought the Quad Cities offering to Anthony Cantone and the Firm because he was eager to market the "pre-packaged" offering. He gave no thought for conducting the independent due diligence that was his duty to do. Afterward, he accepted no responsibility for his misconduct, and he provided an affidavit that was key to the misleading Bondholder Litigation. In connection with the Montgomery 2015 offering, DeRobbio persisted in asserting that he had acted appropriately and had relied on advice of counsel, when, in fact, he was intimidated by a lawyer's threat of suing him for libel. Moreover, DeRobbio did not recognize that payment to earlier investors from the proceeds of the Montgomery 2015 offering was not permitted and did not justify calling the earlier offering successful. Throughout,

DeRobbio shifted responsibility for the violations to others. He asserted that he was not the Firm's municipal securities principal or the person who had final say on the offerings.[808]

Furthermore, DeRobbio manifested confidence that nothing was wrong with what he and the Firm had done. He emphasized that ["my clients in Montgomery 2004] got paid."[809] DeRobbio failed to appreciate the difference between payments made in compliance with applicable contractual, legal, and regulatory requirements and payments made improperly from the proceeds of one offering to investors in a different offering.

DeRobbio's registration was terminated before the Firm filed its Form BDW, but he could reenter the industry by registering with another broker-dealer. We conclude that he should be barred for his violations in connection with each offering to protect the public from any future misconduct.

Our imposition of these sanctions is consistent with the SEC's guidance on remedial sanctions. In evaluating the imposition of a bar in a FINRA disciplinary proceeding, the SEC has explained that a well-grounded finding that the sanctioned party "posed a clear risk of future misconduct" such that the bar was "necessary to protect investors" is an appropriate, remedial sanction, not a punishment.[810] Our purpose here is to protect investors from future misconduct by the Respondents.

E. Restitution

The Guidelines recommend that restitution be ordered where an identifiable person has suffered quantifiable loss that was proximately caused by the respondent's misconduct.[811] In this case, as set forth below, Enforcement has identified specific customers who purchased the Quad Cities bonds and/or the Montgomery 2015 bonds, either in the initial offering or on the secondary market. Enforcement then analyzed and memorialized the amount of each customer's losses. Those losses were proximately caused by Respondents misrepresentations and omissions of material fact, which created a false impression of the financial viability of the two bond offerings. The customers would not have bought the bonds if they had known the truth.

1. Quad Cities

Moy, the FINRA analyst who led the investigation of these transactions and testified at the hearing, prepared a chronology of the Cantone Research customer purchases and sales of the 2013 Quad Cities bonds. The chronology shows that over 60 customer accounts purchased the bonds on November 18, 2013, in the initial offering, and there were approximately 20 purchases and sales on the secondary market after that. Most of the customer purchases on the secondary

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[808] Tr. (DeRobbio) 1610–11.

[809] Tr. (DeRobbio) 1004–05.

[810] *John M. Saad*, Exchange Act Release No. 86751, 2019 SEC LEXIS 2216, at *14 (Aug. 23, 2019).

[811] Guidelines, at 5 (General Principle 5).

market occurred in the first six months of 2014. The chronology identifies each customer account, the amount of the purchase or sale, and the registered representative credited with the transaction.[812]

Moy also prepared a summary chart of customer losses on the Quad Cities bonds. It lists the customers under the name of their registered representative. So DeRobbio's customers are listed under his name, and Anthony Cantone's customers are listed under his name. For each purchase transaction by a customer, the chart identifies the date purchased, the amount invested, distributions paid out (as evidenced in EMMA), and coupon interest received. Distributions and coupon interest are totaled and subtracted from the investment amount, leaving a figure for the customer's loss on the investment.[813]

In reliance on Moy's chart of customer losses on the Quad Cities bonds, we find that DeRobbio's customers suffered total losses of $506,385.70 and that Anthony Cantone's customers suffered total losses of $456,474.22. The Firm's customers collectively suffered total losses of $1,504,184.71.[814] The losses suffered by each individual customer are set forth in Appendix B to this decision. In the public version of Appendix B, the customers are identified only by their initials. In a non-public version of Appendix B that only the parties will receive, customers are identified by name.

The Guidelines authorize adjudicators to require the payment of prejudgment interest on the base amount of restitution, and the Guidelines specify how the interest should be calculated.[815] In the Order below, we require the payment of prejudgment interest in compliance with the Guidelines.

2. Montgomery 2015

Moy, the FINRA analyst, also prepared a chronology of the Cantone Research customer purchases and sales of the Montgomery 2015 bonds. The chronology shows that approximately 110 customer accounts purchased the bonds on May 27, 2015, in the initial offering, and there were approximately 55 purchases and sales on the secondary market after that. Almost immediately, in June 2015, Respondents began repurchasing some of the bonds from customers and then selling the bonds to other customers on the secondary market. Secondary market customer purchases extended into at least May 2016. Moy's chronology identifies each customer account, the amount of the purchase or sale, whether the transaction occurred in the offering or on the secondary market, and the registered representative credited with the transaction.[816]

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[812] CX-5; Tr. (Moy) 171–78.

[813] CX-25.

[814] CX-25.

[815] Guidelines at 10.

[816] CX-21.

Moy also prepared a chart of customer losses on the Montgomery 2015 bonds. As with the chart of customer losses on the Quad Cities bonds, this chart shows the various categories of payments each customer account received and deducted those payments from the amount invested to arrive at a figure representing amount of the customer's losses. The customer accounts are grouped under the name of the registered representative who sold the bonds to the customers.[817]

In reliance on Moy's chart of customer losses on the Montgomery 2015 bonds, we find that DeRobbio's customers suffered total losses of $2,032,679.98 and that Anthony Cantone's customers suffered total losses of $741,520.92. The Firm's customers collectively suffered total losses of $3,273.240.98.[818] The losses suffered by each individual customer are set forth in Appendix C to this decision. In the public version of Appendix C, customers are identified only by their initials. In a non-public version of Appendix C that only the parties will receive, the customers are identified by name.

As with the Quad Cities bonds, we have determined to require the payment of prejudgment interest on the base amount of restitution. In the Order below, we require the payment of prejudgment interest in compliance with the Guidelines.[819]

F. Disgorgement and Fines

In connection with each offering, Enforcement requested that we award disgorgement and significant fines in addition to ordering each individual Respondent barred, the Firm expelled, and payment of restitution to the injured customers. Enforcement cites the Guidelines, General Principles 5 and 6, for authority that restitution and disgorgement may be ordered in addition to fines.[820] In support of its request for disgorgement, Enforcement submitted two exhibits that show the commissions and fees earned by Anthony Cantone, DeRobbio, and the Firm from their work on the offerings.[821]

We decline to impose these additional sanctions. While General Principles 5 and 6 permit the imposition of all these various sanctions, they do so only "where appropriate to remediate misconduct."[822] These General Principles do not encourage the imposition of all these sanctions at once. Rather, they carefully focus on the primary goal of redressing harms suffered by customers. General Principle 5, for instance, notes that restitution should be calculated based on the actual amount of the loss sustained by a victim and that restitution may be ordered even if the victim's loss exceeds the amount of the respondent's ill-gotten gain. General Principle 5 further

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[817] CX-26.

[818] CX-26.

[819] Guidelines at 10.

[820] Enf. Br. 34.

[821] CX-5; CX-19.

[822] Guidelines at 5 (General Principles 5 and 6).

provides that even if a fine is imposed, restitution should be ordered because it serves a different purpose. General Principle 6 provides that a respondent's ill-gotten gains can be ordered to be disgorged but suggests that they be used, if appropriate, to redress harms suffered by customers. General Principle 6 also states that even if a fine is imposed, disgorgement can be ordered. Nowhere do these Principles suggest, however, that once the determination is made to order restitution, an adjudicator should impose the sanctions of disgorgement and a fine in addition.

With respect to pecuniary sanctions such as fines, the Guidelines expressly state, "Adjudicators generally should not impose a fine if an individual is barred and the Adjudicator has ordered restitution or disgorgement of ill-gotten gains as appropriate to remediate the misconduct."[823] On the other hand, the Guidelines do permit imposing a fine along with restitution and disgorgement if the case involves significant and identifiable customer harm or the respondent has retained substantial ill-gotten gains.[824]

In construing the Guidelines, we are mindful that sanctions in a FINRA disciplinary case are remedial, not punitive.[825] We believe that the bars we impose on the individual Respondents and the expulsion of the Firm are necessary to protect investors in the future. We believe that ordering restitution is equitable and appropriate to remediate the harm Respondents inflicted on specific customers. We do not believe that disgorgement and fines are necessary in addition to those sanctions to further remediate the misconduct.[826]

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[823] Guidelines at 9 (Technical Matters).

[824] *Id.*

[825] *E.g.*, *Springsteen-Abbott*, 989 F.3d at 9 (FINRA is limited to remedial sanctions, but, if a bar from the industry is imposed to protect the public, the bar is remedial).

[826] This conclusion is consistent with Supreme Court holdings regarding the equitable remedies available to the SEC. The Court in *Kokesh v. SEC*, 581 U.S. 455 (2017) described disgorgement as historically a form of restitution measured by the defendant's wrongful gain. *Id.* at 458–59. But the Court determined that disgorgement as administered by the SEC was a penalty subject to a five-year statute of limitations. It did so largely because the SEC imposed disgorgement for punitive purposes and to deter violations of the securities laws by others—and also because in many cases the SEC did not use the disgorged funds to compensate victims for their losses. *Id.* at 463–65. The Court held most recently that disgorgement *can* be an equitable remedy where (i) it does not exceed the wrongdoer's net profits and (ii) is awarded for the benefit of victims. *Liu v. SEC*, 140 S. Ct. 1936, 1940 (June 22, 2020).

After the Court issued these decisions, Congress passed the National Defense Authorization Act for Fiscal Year 2021 ("NDAA"), which extends the five-year limitations period applied in *Kokesh* to ten years where alleged securities law violations are scienter-based. Congress did not otherwise change the law or overturn *Kokesh* or *Liu*. Congress left the analysis of *Kokesh* and *Liu* in place as to the appropriate circumstances in which to order disgorgement. *See generally SEC v. Sharp*, 626 F. Supp. 3d 345, 380 (D. Mass. 2022) (discussing NDAA and holding that its extension of the limitations period retroactively applied to pending case). The district court in *Sharp* described *Liu* as requiring that disgorgement be used to make victims whole. *Id.* at 380.

The Supreme Court's decisions in *Kokesh* and *Liu* indicate that disgorgement can be an equitable remedy in certain circumstances, particularly if the purpose is to compensate victims. But in this case we have already determined that

VI. Order

Cantone Research Inc.

We impose sanctions for all the violations proven in connection with the ***Quad Cities offering*** in the aggregate. Cantone Research Inc. is expelled from FINRA membership because it sold municipal bonds:

- Without a reasonable basis to believe them suitable for any investor in willful violation of MSRB Rule G-19, as charged in Cause I.

- By means of negligent misrepresentations and omissions of material fact in willful violation of MSRB Rule G-17 and, directly and indirectly, in violation of Securities Act Sections 17(a)(2) and 17(a)(3), as charged in Cause II.

- Failing to disclose at or prior to the time of trade all material information about the transaction in willful violation of MSRB Rule G-17 and MSRB Rule G-47, as charged in Cause V.

We impose sanctions for all the violations proven in connection with the ***Montgomery 2015 offering*** in the aggregate. Cantone Research Inc. is separately expelled from FINRA membership because it sold municipal bonds:

- By means of fraudulent misrepresentations and omissions of material fact in willful violation of MSRB Rule G-17 and, directly and indirectly, Securities Act Section 17(a)(1), as charged in Cause III.

- Failing to disclose at or prior to the time of trade all material information about the transaction in willful violation of MSRB Rule G-17 and MSRB Rule G-47, as charged in Cause V.

Anthony J. Cantone

We impose sanctions for all the violations proven in connection with the ***Quad Cities offering*** in the aggregate, Anthony J. Cantone is barred from associating with any FINRA member firm in any capacity because he sold municipal bonds:

- Without a reasonable basis to believe them suitable for any investor in willful violation of violation of MSRB Rule G-19, as charged in Cause I.

Respondents should compensate the victims of their misconduct by paying restitution. An additional pecuniary sanction is not necessary to remediate the harm caused by Respondents' misconduct.

- By means of negligent misrepresentations and omissions of material fact in willful violation of MSRB Rule G-17 and, directly and indirectly, Securities Act Sections 17(a)(2) and 17(a)(3), as charged in Cause II.

- Failing to disclose at or prior to the time of trade all material information about the transaction in willful violation of MSRB Rule G-17 and MSRB Rule G-47, as charged in Cause V.

We impose sanctions for all the violations proven in connection with the ***Montgomery 2015 offering*** in the aggregate. Anthony J. Cantone is separately barred from associating with any FINRA member firm in any capacity because he sold municipal bonds:

- By means of fraudulent misrepresentations and omissions of material fact in willful violation of MSRB Rule G-17 and, directly and indirectly, Securities Act Section 17(a)(1), as charged in Cause III.

- Failing to disclose at or prior to the time of trade all material information about the transaction in willful violation of MSRB Rule G-17 and MSRB Rule G-47, as charged in Cause V.

Raymond J. DeRobbio

We impose sanctions for all the violations proven in connection with the ***Quad Cities offering*** in the aggregate. Raymond J. DeRobbio is barred from associating with any FINRA member firm in any capacity because he sold municipal bonds:

- Without a reasonable basis to believe them suitable for any investor in willful violation of MSRB Rule G-19, as charged in Cause I.

- By means of negligent misrepresentations and omissions of material fact in willful violation of MSRB Rule G-17 and, directly and indirectly, Securities Act Sections 17(a)(2) and 17(a)(3), as charged in Cause II.

- Failing to disclose at or prior to the time of trade all material information about the transaction in willful violation of MSRB Rule G-17 and MSRB Rule G-47, as charged in Cause V.

We impose sanctions for all the violations proven in connection with the ***Montgomery 2015 offering*** in the aggregate. Raymond J. DeRobbio is separately barred from associating with any FINRA member firm in any capacity because he sold municipal bonds:

- By means of fraudulent misrepresentations and omissions of material fact in willful violation of MSRB Rule G-17 and, directly and indirectly, Securities Act Section 17(a)(1), as charged in Cause III.

- Failing to disclose at or prior to the time of trade all material information about the transaction in willful violation of MSRB Rule G-17 and MSRB Rule G-47, as charged in Cause V.

All Respondents

Cantone Research Inc. is ordered, to pay restitution to all customers who purchased the Quad Cities bonds from the Firm. Each such customer is identified in Appendix B to this decision, along with the amount of the customer's losses.[827] Similarly, Cantone Research Inc. is ordered to pay restitution to all customers who purchased the Montgomery 2015 bonds from the Firm. Each such customer is identified in Appendix C to this decision along with the amount of the customer's losses.[828] Restitution shall be paid to each customer in the amount of loss specified, plus interest at the rate set in 26 U.S.C. Section 6621(a)(2)[829] from October 26, 2021, the date of the Complaint in this matter, until paid in full. If this decision becomes FINRA's final disciplinary action, payment of restitution shall be due within 60 days of the date of this Decision. The Firm is responsible for restitution to all customers who bought the bonds from any representative of the Firm.

Anthony J. Cantone is jointly and severally responsible with the Firm to pay restitution plus interest as stated above to the customers to whom he sold either the Quad Cities bonds or the Montgomery 2015 bonds. The customers to whom Cantone sold the bonds are identified in the non-public versions of Appendix B and Appendix C.

Raymond J. DeRobbio is jointly and severally responsible with the Firm to pay restitution plus interest as stated above to the customers to whom he sold either the Quad Cities bonds or the Montgomery 2015 bonds. The customers to whom DeRobbio sold the bonds are identified in the non-public versions of Appendix B and Appendix C.

In the event that any customer cannot be located, unpaid restitution plus accrued interest should be paid to the appropriate escheat, unclaimed-property, or abandoned-property fund for the state of the customer's last known address.

Cantone Research Inc., Anthony J. Cantone, and Raymond J. DeRobbio are ordered, jointly and severally, to pay hearing costs in the amount of $15,209.73, which includes a $750 administrative fee and $14,459.73 for the cost of the transcript.

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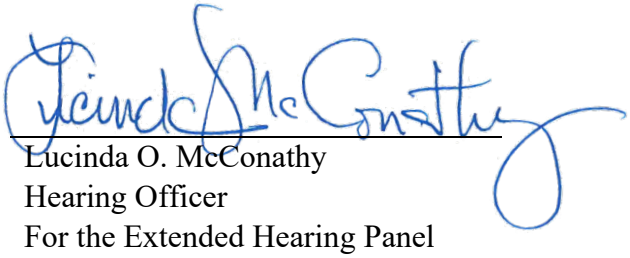
[827] The Quad Cities customers are identified in Appendix B to this decision (by initials in the public version and by full name in the non-public version served only on the parties).

[828] The Montgomery 2015 customers are identified in Appendix C to this decision (by initials in the public version and by full name in the non-public version served only on the parties).

[829] The interest rate set in Section 6621(a)(2) of the Internal Revenue Code is used by the Internal Revenue Service to determine interest due on underpaid taxes and is adjusted each quarter.

If this decision becomes FINRA's final disciplinary action, both of Cantone Research Inc.'s expulsions, both of Anthony Cantone's bars, and both of Raymond DeRobbio's bars, shall become effective immediately.[830]



Lucinda O. McConathy
Hearing Officer
For the Extended Hearing Panel

Copies to:

Cantone Research Inc. c/o Christine Cantone
(via email, overnight courier, and first-class mail)
Anthony J. Cantone (via email, overnight courier, and first-class mail)
Raymond J. DeRobbio (via email, overnight courier, and first-class mail)
Brody Weichbrodt, Esq. (via email)
Noel C. Downey, Esq. (via email)
Kevin Hartzell, Esq. (via email)
Mark Fernandez, Esq. (via email)
Jennifer L. Crawford, Esq. (via email)

[830] The Extended Hearing Panel has considered all the parties' arguments but finds additional discussion unnecessary. Those arguments are accepted to the extent they are consistent with this decision and rejected to the extent they are inconsistent with it.

Department of Enforcement v. Cantone Research, Inc., et al.
Disciplinary Proceeding No. 2017055886402
Appendix B (Public)

Quad City Customer Losses		
Customers		**Loss**
Raymond DeRobbio Customers		
BR 2 LLC (BM)	$	(3,673.70)
BR 1 LLC (BM)	$	(3,590.80)
ESV - *	$	(215,448.00)
SMP - #	$	(14,363.20)
GRK Ttee	$	(17,954.00)
GRK Ttee	$	(21,544.80)
GG	$	(43,089.60)
HPV - #	$	(17,954.00)
LCV - #	$	(10,772.40)
ML - *	$	(17,954.00)
PR TTEE	$	(140,041.20)
Total	**$**	**(506,385.70)**
Anthony Cantone Customers		
AAM	$	(22,042.20)
AAM	$	(18,932.39)
AAM	$	(18,426.83)
JB Sr	$	(7,347.40)
JES	$	(7,347.40)
MWR TTEE	$	(18,368.50)
MWR TTEE	$	(20,368.50)
PW TTEE	$	(7,347.40)
PAD	$	(18,368.50)
PR	$	(7,347.40)
RANL	$	(7,347.40)
SS	$	(18,367.50)
TCF	$	(7,347.40)
WJS	$	(33,063.30)
CAS	$	(14,694.80)
GM	$	(7,347.40)
NB	$	(129,268.80)
SE	$	(7,606.60)
WE - *	$	(35,908.00)

WE - *		$	(19,368.50)
WE - *		$	(8,147.40)
RMY		$	(14,363.20)
KC		$	(7,747.40)
	Total	**$**	**(456,474.22)**

Victor Polakoff Customers			
JR		$	(33,063.30)
AH		$	(35,908.00)
CLR		$	(35,908.00)
DB		$	(17,954.00)
FVB & - *		$	(35,908.00)
JLC		$	(35,908.00)
KB		$	(10,772.40)
PH		$	(17,954.00)
KL		$	(10,772.40)
REC- *		$	(10,772.40)
RS TTEE		$	(17,954.00)
STD		$	(3,628.30)
SC		$	(17,954.00)
SK		$	(3,590.80)
SB		$	(10,772.40)
VP		$	(17,954.00)
VP		$	(21,141.50)
WH TTEE - *		$	(10,772.40)
	Total	**$**	**(348,687.90)**

Robert Crowther Customers			
JKD		$	(35,908.00)
MSCD		$	(7,181.60)
	Total	**$**	**(43,089.60)**

Maryann Cantone Customers			
AJ		$	(19,532.39)
	Total	**$**	**(19,532.39)**

Anthony Cantone/John Cantone Customers			
WWR TTEE - *		$	(43,089.60)
	Total	**$**	**(43,089.60)**

John Cantone Customers			
AG		$	(14,363.20)
EC		$	(7,181.60)
SC		$	(7,181.60)
RK		$	(10,772.40)
JB		$	(7,181.60)
TG TTEE		$	(7,181.60)
RB		$	(18,368.50)
	Total	**$**	**(72,230.50)**

Raymond Cattonar Customers			
JKD		$	(7,347.40)
JS		$	(7,347.40)
	Total	**$**	**(14,694.80)**

Quad City Customer Total Losses	**$ (1,504,184.71)**

* - Indicates Deceased Customer

- Indicates Gift to Customer

Data source: Hearing Exhibit CX-25

Department of Enforcement v. Cantone Research, Inc., et al.
Disciplinary Proceeding No. 2017055886402
Appendix C (Public)

Montgomery 2015 Customer Losses	
Customers	**Loss**
Raymond DeRobbio Customers	
AB	$ (60,816.00)
KB, POA	$ (60,816.00)
KB, POA	$ (30,788.82)
PB TTEE	$ (30,408.00)
RAB TTEE	$ (60,816.00)
RAB TTEE	$ (36,943.99)
JD	$ (32,510.10)
JD	$ (16,866.31)
DK TTEE	$ (15,204.00)
VG	$ (6,081.60)
JL - *	$ (6,081.60)
PJR TTEE	$ (221,978.40)
PJR	$ (51,693.60)
BR 1 LLC (Dr. Bernard Miskiv)	$ (182,448.00)
BR 2 LLC (Dr. Bernard Miskiv)	$ (9,258.02)
BR 2 LLC (Dr. Bernard Miskiv)	$ (16,685.79)
BR 2 LLC (Dr. Bernard Miskiv)	$ (20,404.35)
GK TTEE	$ (152,040.00)
GK TTEE	$ (152,040.00)
GK TTEE	$ (38,730.32)
GK TTEE	$ (33,358.53)
GK TTEE	$ (33,998.61)
GK TTEE	$ (33,998.61)
GK TTEE	$ (9,245.71)
GK CUST	$ (27,367.20)
GK CUST	$ (17,037.93)
EV - *	$ (121,632.00)
HV - #	$ (121,632.00)
LV- #	$ (51,693.60)
NP - ^	$ (91,224.00)
HR	$ (33,448.80)
BM TTEE	$ (57,775.20)
SMP #	$ (36,489.60)
SMP - #	$ (558.33)
BM	$ (45,612.00)
DVP	$ (42,571.20)
JP	$ (5,902.70)

WAP		$ (54,734.40)
WAP		$ (11,788.67)
	Total	**$ (2,032,679.98)**

Anthony Cantone Customers	
AAM	$ (30,408.00)
BB	$ (45,612.00)
CL	$ (6,081.60)
DJK	$ (30,408.00)
FAE	$ (12,163.20)
FD TTEE	$ (12,163.20)
JG	$ (12,163.20)
JMW	$ (8,341.70)
JES	$ (9,122.40)
JV	$ (182,448.00)
JS - *	$ (15,204.00)
KWE	$ (6,081.60)
KZ	$ (3,040.80)
LW	$ (12,163.20)
MAC	$ (9,122.40)
MWR TTEE	$ (42,571.20)
NB	$ (45,612.00)
RM	$ (6,081.60)
RANL	$ (6,081.60)
RJB Sr TTEE	$ (21,474.25)
RLB	$ (18,244.80)
SZ - *	$ (6,081.60)
SN	$ (6,081.60)
SS	$ (9,065.70)
WE- *	$ (30,408.00)
WFL	$ (6,081.60)
CE	$ (29,471.67)
CE	$ (11,788.67)
ES	$ (32,418.83)
FD	$ (5,894.33)
JV	$ (29,471.67)
LBW	$ (5,894.33)
WCOC	$ (34,274.17)
BS	$ (9,122.40)
BN	$ (39,530.40)
DHB	$ (30,408.00)
JAY Exec	$ (24,326.40)
KAK	$ (6,081.60)
KC	$ (6,081.60)
RMY	$ (6,081.60)

TN	$	(6,081.60)
RMY	$	(5,894.33)
WBT	$	(5,894.33)
Total	**$**	**(741,520.92)**

Victor Polakoff Customers		
AH	$	(21,285.60)
BO & GI	$	(15,204.00)
CM	$	(6,081.60)
CK - ^	$	(6,081.60)
DSR	$	(12,163.20)
JLC	$	(30,408.00)
KRU TTEE	$	(15,204.00)
KRU TTEE	$	(10,222.76)
KC	$	(3,040.80)
MH	$	(9,122.40)
PK	$	(15,204.00)
REC - *	$	(9,122.40)
RSB Executor	$	(15,204.00)
RS TTEE	$	(15,204.00)
RBD A/C 2	$	(6,081.60)
STD	$	(3,040.80)
SVB - *	$	(27,367.20)
SC	$	(60,816.00)
SK	$	(9,122.40)
SP	$	(30,408.00)
TDB LP	$	(15,204.00)
WH TTEE -*	$	(6,081.60)
AA	$	(8,841.50)
BWK	$	(8,841.50)
SVB	$	(2,947.17)
Total	**$**	**(362,300.13)**

Robert Crowther Customers		
JKD	$	(36,489.60)
MSCD	$	(6,081.60)
REC	$	(10,183.00)
Total	**$**	**(52,754.20)**

John Cantone Customers		
LGL	$	(9,122.40)
LCF	$	(9,122.40)
RK	$	(12,163.20)
MC	$	(10,247.20)
Total	**$**	**(40,655.20)**

Maryann Cantone Customers			
AJ		$	(15,204.00)
PR		$	(3,040.80)
	Total	**$**	**(18,244.80)**

Anthony Cantone/John Cantone Customers			
JS		$	(15,204.00)
	Total	**$**	**(15,204.00)**

Anthony Cantone/Victor Polakoff Customers			
MAC		$	(9,881.76)
	Total	$	(9,881.76)

Montgomery 2015 Customer Total Losses	**$ (3,273,240.98)**

* - Indicates Deceased Customer

- Indicates Gift to Customer

^ - Indicates Account Transfer to Other Broker-Dealer

Data source: Hearing Exhibit CX-26