BEFORE THE NATIONAL ADJUDICATORY COUNCIL

FINANCIAL INDUSTRY REGULATORY AUTHORITY

In the Matter of Department of Enforcement, Complainant, vs. Richard Gomez Jackson Heights, NY Respondent.	DECISION Complaint No. 2011030293503 Dated: March 28, 2018

Associated person sold securities away from his member firm, recommended unsuitable securities transactions, and fraudulently misrepresented material facts. Held, findings and sanctions modified.

Appearances

For the Complainant: Michael Smith, Esq., Thomas Kuczajda, Esq., Department of Enforcement, Financial Industry Regulatory Authority

For the Respondent: Pro Se

Decision

I. Introduction

Richard Gomez ("Gomez") appeals a June 10, 2016 Hearing Panel decision. The Hearing Panel found that Gomez violated FINRA rules when he engaged in the private sale of securities without notifying his member firm and recommended those securities to investors, including his firm's customers, without having a reasonable basis for his recommendations. The Hearing Panel barred Gomez from associating with any FINRA member in any capacity for this misconduct.

The Department of Enforcement ("Enforcement") cross appeals the Hearing Panel's decision. Although the Hearing Panel found that Gomez misrepresented material facts while recommending and selling the securities in question to investors, it concluded that he lacked scienter and dismissed a claim that Gomez engaged in fraud.

After a thorough review of the entire record, we find that Gomez impermissibly sold securities away from the FINRA member with which he was associated without providing his

firm with prior written notice, and he violated his duty to ensure that he possessed a reasonable basis to recommend the securities to his customers. We, however, reverse the Hearing Panel's finding that Gomez lacked the requisite scienter to commit fraud. We therefore find that he also violated the federal securities laws and FINRA rules by misrepresenting material facts to investors.

We modify the sanctions imposed by the Hearing Panel by imposing a bar for the fraud violation and separate bars for each of the other violations.

II. Background

Gomez entered the securities industry in 2003. During his career, Gomez associated or registered as a general securities representative with 20 different broker-dealers. Gomez left the securities industry in late 2015, and he is not currently associated with a FINRA member.

The conduct at issue in this case occurred while Gomez was registered as a general securities representative of Legend Securities, Inc. ("Legend"). He associated with Legend from June 1, to December 2, 2011.

III. Procedural History

Enforcement commenced disciplinary proceedings on April 8, 2015, when it filed a three-cause complaint that alleged Gomez engaged in misconduct for which FINRA should impose sanctions. The first cause alleged that Gomez fraudulently misrepresented or omitted material facts in connection with his sale of securities offered or issued by two entities—Praetorian Global Fund, Ltd. ("Praetorian") and U.S. Coal Corporation, Inc. ("U.S. Coal")—in violation of Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act"), Exchange Act Rule 10b-5, and FINRA Rules 2020 and 2010.[1] The second cause alleged that Gomez recommended those securities to investors without possessing a reasonable basis to conclude that the securities were suitable for his customers, in violation of NASD Rule 2310 and FINRA Rule 2010. The third cause alleged that Gomez privately participated, for compensation, in the sale of the securities away from Legend without notifying the firm, in violation of NASD Rule 3040 and FINRA Rule 2010.

Gomez filed an answer on June 26, 2015, in which he admitted the claim that he impermissibly sold securities away from his firm, but he denied the remaining allegations that his conduct violated the federal securities laws and FINRA rules. On June 10, 2016, the Hearing Panel issued its decision after conducting a one-day hearing.

The Hearing Panel found that Gomez violated NASD Rule 3040 and FINRA Rule 2010 when he participated in the private sale of Praetorian and U.S. Coal securities for compensation without notifying his firm. The Hearing Panel found also that Gomez violated NASD Rule 2310 and FINRA Rule 2010 when he recommended the securities to investors, including Legend

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

customers, without having a reasonable basis for believing that those securities were suitable for them. Finally, the Hearing Panel dismissed Enforcement's claim that Gomez engaged in fraud after concluding that, although negligent, he acted neither recklessly nor intentionally when he misrepresented or omitted material facts while selling the securities to investors. The Hearing Panel imposed a single bar for Gomez's selling away and suitability violations.

The parties timely appealed and cross-appealed, respectively, the Hearing Panel's decision.

IV. Facts

A. Gomez is Introduced to Praetorian and John Mattera

Praetorian was registered in the British Virgin Islands as a professional mutual fund. It sold unregistered securities of several limited liability companies, the "Praetorian G" entities, that claimed to offer investors the opportunity to acquire interests in privately held, pre-initial public offering ("pre-IPO") shares of coveted stock in internet and technology companies, including Groupon, Inc. ("Groupon"), Facebook, Inc. ("Facebook"), and Zynga, Inc. ("Zynga").[2]

A former colleague, HG, introduced Gomez to David Howard ("Howard") when Gomez registered with Legend in June 2011. Howard told Gomez that he worked for Praetorian, and he emailed Gomez subscription documents for one of the Praetorian G entities, Praetorian G Power V, LLC ("G Power V"), which were in an editable, Microsoft Word format.

G Power V purported to offer investors the opportunity to purchase interests entitling them to shares of Groupon stock. The subscription documents nevertheless contained obvious typographical errors and a number of conflicting statements about the number and class of Groupon shares available to investors through G Power V. For example, the subscription documents claimed that G Power V offered investors access to 10 million shares of Groupon stock, but elsewhere the documents stated that Praetorian capitalized G Power V with only one million Groupon shares. Similarly, the first page of the subscription documents stated that G Power V offered investors an interest in Series E preferred Groupon stock, but elsewhere the documents referred to Series F preferred stock of the company.

The subscription documents also included wire transfer instructions for Praetorian's supposed "escrow agent," First American Service Transmittals, Inc. ("FAST"). Although Praetorian was ostensibly located in the British Virgin Islands, the wire transfer instructions directed investors to send their funds to a FAST account held at a Fort Lauderdale, Florida branch of a regional bank.[3] According to information publicly available on the Florida Secretary of

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[2] Praetorian never registered with the Securities Exchange Commission ("Commission") in any capacity. None of the Praetorian G entities ever registered any of their securities or offerings with the Commission.

[3] The wire instructions also told investors to fax their completed subscription documents to a number that Gomez knew to be a south Florida phone number.

State's website, "Johnny R. Arnold" ("Arnold") was an officer and director of FAST, and the company listed its address as an apartment at a residential address in Boca Raton, Florida.

In late June 2011, Gomez met Howard at a New York City restaurant, and he introduced Gomez to John Mattera ("Mattera") by telephone. During their conversation, Mattera told Gomez that he was Praetorian's "fund manager," and he explained that the Praetorian G entities offered investors the means to acquire interests in pre-IPO shares of "hot" companies like Groupon, Facebook, and Zynga.

After speaking with Mattera, Gomez agreed to solicit investors for Praetorian, which he concluded was a hedge fund. Gomez and Howard decided to split a ten percent commission on the gross investments that Gomez procured for the Praetorian G entities, with Gomez receiving eighty percent of this sum.[4] Howard agreed to pay Gomez his share of these commissions directly, which meant that Praetorian would not be involved with the payment of Gomez's commissions.

B. Gomez Conducts Little Independent Investigation of Praetorian

Gomez had no prior experience with private placement securities offerings before his involvement with Praetorian. He nevertheless acknowledges that he had an obligation to perform reasonable due diligence before recommending that investors, including Legend customers, purchase securities offered by Praetorian.

Gomez conducted little meaningful, independent investigation of Praetorian, or the individuals and entities involved with it, before he began selling the securities. Gomez claimed that he "did as much as [he] could," but in his hearing testimony he could not recall with any specificity the steps he took to perform his diligence or whether he kept any files or materials detailing the scope of the investigation he performed.[5] Gomez claimed also that he read thoroughly the G Power V subscription documents that Howard provided him, but he did not find anything in the documents that concerned him. As he testified, although the documents contained inconsistencies and raised a number of questions, the documents "looked fine" to him.[6]

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[4] As Gomez testified, this commission rate was well above the norm that Gomez had experienced during his time in the securities industry.

[5] In an April 2012 response to a FINRA request for information, Gomez identified several websites he claimed to have looked at while performing his research. None of these websites contained any information relating to Praetorian or the suitability of any investment in the Praetorian G entities. They instead dealt with an entity called "The Mattera Reserve" and Mattera's purported philanthropic endeavors.

[6] The G Power V subscription documents referenced certain exhibits and a non-disclosure agreement that Howard did not send to Gomez. Gomez never asked for or received these attachments.

Gomez instead relied largely on information and assurances provided to him by Mattera and Howard as the basis for his recommendations. Gomez claimed that Praetorian "was private, [and] information regarding the company, its activities and financials were limited," and he thus "relied on the professional review and due diligence of [Mattera] and provided by [Praetorian's] public relations personnel." For instance, when Gomez tried to verify that the Praetorian G entities owned the pre-IPO shares in which they purported to offer investors an interest, he was rebuffed and accepted at face value Howard's assurances—"We do own it. It's private. We cannot show it." Gomez never asked to review any stock certificates or other evidence showing ownership of or access to shares, and he did not otherwise take, prior to soliciting investors, any steps to verify independently that any Praetorian G entity owned any pre-IPO shares of Groupon, Facebook, or Zynga.

Indeed, the limited due diligence Gomez performed failed to uncover material, adverse information that was publicly available to him from a search of the Commission's website, or an internet search engine, about Mattera, Howard, Arnold, Praetorian, or FAST. For instance, by the end of 2010, Mattera possessed a lengthy criminal history and the Commission had sued him in federal court for fraud.

Between 1998 and 2003, Mattera pleaded guilty in four separate Florida criminal cases for, among other things, operating as an unlicensed mortgage broker and multiple instances of grand theft. His criminal activities included taking fees for loans that he never provided, taking stock from a seller without ever paying for the stock, and failing to deliver securities for which customers had paid. For these criminal offenses, Mattera served probation and was ordered to pay restitution.

In 2009, the Commission charged Mattera, and others, including Arnold, in a civil enforcement action filed in Florida alleging that he disseminated false information and participated in a fraudulent scheme to avoid registration requirements by issuing bogus promissory notes to obtain and sell illegally unrestricted shares of a penny stock company. In 2010, Mattera consented to the entry of a permanent injunction against future violations of Exchange Act Section 10(b), Exchange Act Rule 10b-5, and Sections 5(a) and 5(c) of the Securities Act of 1933 ("Securities Act"), a permanent penny stock bar, and an order to disgorge $140,000, plus prejudgment interest. Arnold defaulted by failing to answer the Commission's complaint, and the court permanently enjoined him and barred him from participating in the offering of penny stocks.

In addition to these criminal and regulatory enforcement actions, Gomez failed to uncover numerous civil judgments that state and federal courts had entered against Mattera. In 2000, for example, a federal court in Texas entered a default judgment against Mattera and his d/b/a, "Praetorian Corporation," for $1,197,500. In its order, the court found that Mattera's conduct was "intentional and fraudulent as alleged" in the plaintiff's complaint. In 2002, a federal court in California entered a default judgment against Mattera for $115,000. In that case, the plaintiff alleged that Mattera had agreed to buy stock for $104,000, but after receiving the shares, never delivered the funds to pay for them.

On June 17, 2011, at about the time that Gomez claimed to research Praetorian, plaintiffs filed a federal lawsuit in Florida against Mattera, Arnold, and another of Arnold's "escrow services," First American Reliable Escrow, Inc. ("FARE"). The plaintiffs alleged that FARE had acted as escrow agent for a private placement of securities, but FARE and Mattera improperly diverted funds from the escrow account. On July 18, 2011, the defendants agreed to a settlement in which Mattera and Arnold agreed to pay the plaintiffs $340,000 and deliver the securities the plaintiffs had purchased.[7]

Finally, Gomez also failed to uncover that, at the time Howard was recruiting him to engage in sales efforts for Praetorian, Howard was facing securities fraud allegations for his involvement in an unrelated boiler-room scheme. In March 2011, the Commission sued Howard and several others in California alleging that they had "engaged in a scheme to defraud almost 200 investors located in approximately 38 states, resulting in customer losses of over $3 million."

C. Gomez Begins Selling Praetorian Securities Away from His Firm

Legend did not permit its brokers to participate in private securities transactions. Gomez, who was aware of this restriction, did not notify Legend in any manner of his plan to participate in securities transactions and solicit investments for Praetorian away from the firm for compensation.

On June 22, 2011, Gomez telephoned DB and recommended that he invest in G Power V. DB was not aware of Praetorian or G Power V before Gomez contacted him. Gomez sent DB the G Power V subscription documents that Gomez had received from Howard. Gomez told DB that G Power V owned or had access to pre-IPO shares of Groupon stock and that an investment in this Praetorian G entity would give DB an interest in Groupon's securities. Because of Gomez's solicitation, DB wired $44,000 to FAST to invest in G Power V. Howard paid Gomez $3,200 as a commission for DB's investment.[8]

D. Gomez Solicits Other Investors While Ignoring Potential Red Flags

On the day of DB's G Power V investment, Gomez discovered a potential discrepancy in the fund's subscription documents. When Gomez reviewed Groupon's Form S-1 Registration Statement, dated June 2, 2011, he discovered that Groupon had authorized fewer than 5 million shares of Series E preferred stock, far less than the 10 million shares Praetorian claimed that G

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[7] By June 2011, in addition to the several criminal and civil judgments against him, the Internal Revenue Service had recorded at least three unsatisfied federal tax liens against Mattera totaling more than $7 million. Copies of these liens were available on the Palm Beach County Clerk's website.

[8] Howard routinely paid Gomez his Praetorian-related commissions by issuing a personal check drawn on a bank account that was not his.

Power V was offering, and the Form S-1 did not identify Praetorian or G Power V as a Groupon shareholder.[9]

Gomez emailed Howard on June 23, 2011. He asked Howard how Praetorian acquired the Groupon shares that G Power V purported to offer its investors, and why G Power V claimed to own more than the number of Series E preferred stock that Groupon had authorized. Gomez stated in his email, "[t]he clients are reading the S1, & these are the questions I am getting."

Howard emailed his response later that day. Howard avoided answering Gomez's questions directly, and he instead told Gomez that, "if you want verification for all this, please realize this is the kind of due diligence for institutions. . . . We are audited by kpmg and that should be good enough. . . . If [Praetorian] didn't have the stock it would be big trouble for not only us, but the second largest accounting firm in the world."

Gomez testified that, after he received Howard's response, he spoke to Howard, and Howard told him that Praetorian was "working the shares" through another private company. Howard assured Gomez that G Power V had the 10 million shares of Series E preferred shares that Praetorian was purporting to offer investors.[10]

Gomez attempted to verify the limited information that Howard provided him, but he was unable to do so. He called KPMG's office in the British Virgin Islands, but it would not give Gomez any information.[11] Gomez also called two private equity firms identified as stockholders in Groupon's Form S-1 to inquire about Praetorian's claimed ownership of Groupon stock. These entities too declined to provide Gomez any information. Finally, Gomez called Mattera's assistant, who told him that Praetorian obtained Groupon stock through one of Mattera's associates, who was affiliated with a private equity firm listed in Groupon's Form S-1 as a shareholder. When Gomez called this entity, however, no one would speak with him.

A few days later, on June 28, 2011, Mattera's assistant unexpectedly emailed Gomez new subscription documents for G Power V.[12] The first page of these G Power V subscription

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[9] Gomez did not recall reviewing Groupon's Form S-1 before June 22, 2011.

[10] Gomez testified that Howard said he would show Gomez how Praetorian had acquired Groupon shares, but he never fulfilled his promise.

[11] Gomez did not recall ever asking for a copy of any audit report for Praetorian or the Praetorian G entities.

[12] On the day that Gomez received the new G Power V documents, Mattera's assistant also sent Gomez subscription documents for another Praetorian G entity, Praetorian G Power IV, LLC ("G Power IV"). G Power IV claimed to own and offer to investors Series B preferred shares in Facebook. The documents, however, contained several obvious errors. For example, the first line of the documents stated, in a bold font, that G Power IV owned stock in "Facebook, Inc., Inc." The first paragraph of the documents described Facebook as a "Social Medial Company." In addition, elsewhere the documents stated that G Power IV allowed investors to

documents stated that Praetorian was offering investors ownership in Groupon Series B-1 preferred stock rather than Series E preferred shares. Nevertheless, elsewhere the documents stated that an investment in G Power V entitled investors to ownership of Series F preferred stock, not Series B-1 preferred shares. When Gomez inquired about this apparent discrepancy, Howard or Mattera's assistant told him that the Series B-1 preferred shares were within the Series F preferred shares.[13] Gomez admits he did nothing to verify this claim. Ultimately, Gomez "trusted" Howard, the subscription documents he received for Praetorian "seemed fine," and he "kept moving forward" to solicit investors for Praetorian.

On July 4 and 5, 2011, Gomez sold interests in G Power V to four investors—TD, JG, RW, and AM—away from Legend. Gomez recommended G Power V's securities to each of these investors, and none of them had heard of Praetorian or G Power V before Gomez solicited their investments and sent them subscription documents.[14] Gomez told each of the investors, two of whom (TD and RW) were also his customers at Legend, that G Power V owned or had access to Groupon shares and that an investment in G Power V gave them an ownership interest in the company's stock. TD, JG, RW, and AM invested $50,000, $120,000, $40,000, and $40,000 in G Power V, respectively, with each wiring money to FAST in accordance with the subscription documents' wiring instructions. Howard paid Gomez commissions totaling $18,400 for these four transactions.

E. Gomez's Sales Efforts Continue Despite a Pay Dispute

On July 5, 2011, Mattera's assistant emailed Gomez two additional sets of Praetorian subscription documents. Both sets of documents were ostensibly for the same Praetorian G entity, Praetorian G Power VIII, LLC ("G Power VIII"). The documents, however, claimed to offer investors the opportunity to purchase interests in two different companies, with one offering Series B preferred shares of "Twitter, Inc." and the other Series B preferred shares of Zynga. A review of the documents raised still other issues: the wire transfer instructions in one set of the documents referred to "Praetorian G Power VIII, LLC (Twitter)", but the instructions included with the other set referred to "Praetorian G Power XII (Zynga)."

On July 8, 2011, Mattera's assistant emailed Gomez a third set of subscription documents, this time for Praetorian G Power VI, LLC ("G Power VI). These documents, like one of the sets of documents that Gomez received for G Power VIII, claimed to offer investors the opportunity to purchase interests in Series B preferred shares of Zynga. Gomez did not recall noticing any of the inconsistencies in the three set of documents that he received in early July 2011. He assumed that investors would simply pick one set of documents over the others

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purchase Series B preferred shares of "Facebook Automotive, Inc." Gomez testified that these errors gave him no pause.

[13] According to Groupon's Form S-1, the company had not authorized or issued any shares of Series B-1 preferred stock.

[14] The record is unclear as to which version of the G Power V subscription documents Gomez sent to these investors.

depending on whether they intended to invest in Twitter or Zynga. These discrepancies did not cause Gomez to conduct any additional due diligence.

On July 21, 2011, Gomez solicited MB to purchase an interest in G Power VI away from Legend. MB was not familiar with Praetorian or G Power VI before Gomez recommended the investment to him. Gomez told MB that G Power VI owned Zynga stock and that investing in G Power VI would give him ownership of Zynga stock. On July 22, 2011, MB, who was also a Legend customer, wired $50,000 to FAST's bank account to purchase an interest in G Power VI.

Unlike the earlier transactions he had arranged for Praetorian, Gomez did not promptly receive from Howard payment of his portion of the commissions earned from his sale to MB. Gomez therefore emailed Howard on July 27, 2011, to complain about Howard's lack of payment. Howard replied by email that day. He told Gomez "he had a citi fraud detection freeze [his] accounts," but he assured Gomez that he would "get it [done] in the afternoon." On July 31, 2011, Gomez complained again because he had not received his commissions for MB's purchase. A few days later, on August 2, 2011, Howard told Gomez by email, "[w]e need to meet." Howard said he was "in a meeting with [his] attorney now," but would call Gomez later. On August 3, 2011, Gomez emailed Howard again and stated, "I do not understand what is going on, I get my clients to wire the funds to escrow & you pay. Why are you holding out on me this time[?]." On August 4, 2011, Howard replied and wrote that he had "been under the gun on several issues that [he] would rather discuss in person."

Gomez testified that he was not concerned with Howard's lack of payment or with Howard's statements that his accounts had been frozen, that he was meeting with his attorney, or that he had been under pressure and needed to talk in person.[15] Yet, problems persisted. On approximately August 5, 2011, Howard paid Gomez $2,000, half the amount Gomez believed he was due, as a commission for MB's investment in G Power VI. Howard again explained to Gomez that he was having personal problems, and he assured Gomez that he would pay him the remaining $2,000 the following week.

Howard never paid Gomez the additional $2,000. On August 22, 2011, Gomez sent an email to Howard and other individuals associated with Praetorian complaining that Howard had paid a portion of his MB commission to another party. This complaint proved effective. On August 23, 2011, Gomez entered into a new "Consulting Agreement" with Praetorian. Under the agreement, Praetorian agreed to pay Gomez directly a commission of ten percent for his Praetorian G sales. Howard would therefore no longer be involved in paying his commissions. With the new commission arrangement in place, Gomez resumed soliciting investors for Praetorian.

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[15] In hindsight, Howard's statements to Gomez had a backstory. On July 27, 2011, the Commodity Futures Trading Commission ("CFTC") had sued Howard and others in federal court for fraudulently soliciting customers to trade off-exchange foreign currency. According to the CFTC's complaint, Howard and his co-defendants falsely claimed significant profits spanning several years and falsely assured customers, who lost more than $700,000, that their accounts bore minimal risk. Gomez testified that he was unaware of the CFTC's action against Howard.

F. Gomez Sells to One More Customer as Praetorian's Fraud Becomes Apparent

On September 16, 2011, several Praetorian investors sued Praetorian, FAST, Mattera, Arnold, and others in a Florida federal court. They claimed that Mattera, and others associated with Praetorian, engaged in a fraud, breach of contract, and conversion in connection with Praetorian G Power II, LLC ("G Power II"). The investors, who had invested a total of $4.525 million in G Power II, claimed that Mattera and his co-defendants fraudulently induced them to purchase their interests by falsely claiming that G Power II owned pre-IPO shares in Fisker Automotive, Inc. ("Fisker") and that investors would be purchasing ownership interests in Fisker stock. The investors asserted also that Arnold and FAST, which had acted as "escrow agent" for their investments in G Power II, improperly distributed funds to Mattera and others, in breach of their fiduciary duties as escrow agents.

The *Miami Herald* published an article about the September lawsuit on October 13, 2011. The article stated, in part, that the money investors "shipped to a Fort Lauderdale title company to be held in escrow until the deal was completed, appears gone," and that Mattera had admitted that G Power II never owned the Fisker shares that it was purporting to offer investors. The article explained that, "[f]or Mattera, it's not the first time he has been accused of business malfeasance," and it recounted Mattera's criminal history and several of the lawsuits, including the Commission's 2009 action for penny stock fraud, that had been filed against him and alleged that he had engaged in fraudulent business practices. Finally, the article noted, "[t]he common thread" in many of the actions against Mattera was that "Mattera used a title company owned by longtime associate Johnny Ray Arnold." Gomez testified that he was unaware of the lawsuit against the individuals and entities with which he had been dealing the last several months, and he does not recall ever seeing the *Miami Herald's* article.

Later in October 2011, when it became clear that Groupon would price its IPO below $40 a share, the price investors in G Power V thought they had paid for their shares, Praetorian took the unusual step to allow investors to "convert" their interests. Investors were told that they could exchange their interests in G Power V and Groupon stock for interests in Praetorian's Zynga-related offering, G Power VI. Gomez arranged these "conversions" for several investors, including DB, JG, RW, TD, and AM. Gomez did not find the offer of a conversion strange.

Gomez made his final Praetorian sale on November 16, 2011, when he sold an interest in G Power VI to TS, who had been Gomez's customer at a broker-dealer other than Legend. TS was not familiar with Praetorian or G Power VI before Gomez solicited him and recommended that he consider an investment. As he had with the other investors, Gomez told TS that G Power VI owned Zynga stock and that, by investing in this Praetorian G entity, TS would acquire an ownership interest in Zynga stock. TS wired $50,000 to FAST's bank account to purchase an interest in G Power VI.

G. The Commission Exposes Praetorian's Fraud

On November 17, 2011, the day after Gomez sold TS an interest in G Power VI , the Commission charged in a civil enforcement action filed in New York that Mattera, Praetorian, several of the Praetorian G entities, including G Power IV, V, and VI, Howard, Arnold, and

FAST were engaged in a fraud. According to the Commission's complaint, Mattera and several other individuals used Praetorian and the Praetorian G entities to commit fraud by falsely claiming that they owned shares worth tens of millions of dollars in privately-held companies that were expected to soon hold initial public offerings, including Groupon and Facebook. In reality, the Commission alleged, Mattera and his associates never owned the promised pre-IPO shares in these companies and the investment vehicles were a sham. The purported escrow service for investor funds, FAST, merely transferred those funds to Mattera's personal accounts, after Arnold took a cut for himself first. Mattera then used investor funds for private jets, luxury cars, fine art, jewelry, and other personal uses.[16]

In total, the investors that Gomez solicited to purchase interests in the Praetorian G entities lost $394,000.

H. Gomez Also Participates in Sales of U.S. Coal Stock Away from Legend

U.S. Coal was a private company that, as its name suggested, produced coal in central Appalachia. Gomez learned about U.S. Coal from HG at about the same time he introduced Gomez to Howard and Praetorian. HG, through an associate, CF also introduced Gomez to LF, a founder of U.S. Coal.

LF told Gomez that he was the manager of a private investment fund, Blackstone Capital Advisors ("Blackstone"). HG, CF, and LF also told Gomez that U.S. Coal was planning an IPO of stock in the "near future," that Merrill Lynch was U.S. Coal's second-largest shareholder, and that Blackstone had acquired shares of U.S. Coal from company retirees who needed money but were unwilling to wait for the purported IPO. They thus asked Gomez to find investors to purchase Blackstone's U.S. Coal stock.

As with his Praetorian-related efforts, Gomez conducted minimal due diligence about Blackstone's sale of U.S. Coal stock, and the limited information he obtained raised questions about an impending IPO. For example, Gomez claimed that he spoke with U.S. Coal's investor relations department, but he admits that they told him only that an IPO was a "possibility" and that the company had no current plans to go public. He claimed also to have reviewed documents that HG sent him in August 2011, including a presentation that appeared to have been prepared by a broker-dealer concerning a possible U.S. Coal IPO. The presentation, however, was more than one year old and included a target date that had already passed. Nevertheless, Gomez concluded that Blackstone's sale of U.S. Coal stock "seemed reasonable," though he could not recall the facts that lead him to conclude that U.S. Coal securities would be suitable for any investors.

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[16] On December 6, 2013, the court entered judgments against Mattera and Howard. The court permanently enjoined Mattera from participating in any manner in the issuance, offer, or sale of any security, and it ordered Howard to disgorge $34,575, plus prejudgment interest. It is unclear from the record whether judgments have been entered against the remaining defendants. Mattera also pleaded guilty to federal criminal charges for conspiracy, securities fraud, wire fraud, and money laundering related to Praetorian's offerings. The court in that action sentenced Mattera to 11 years in prison and ordered that he pay more than $13 million in restitution.

Blackstone offered to sell its U.S. Coal shares in 10,000 share units for $3.50 a share. Gomez "thought that was a fair price," and he agreed to find buyers for Blackstone's U.S. Coal stock in exchange for a 13 percent commission, a rate Gomez understood to exceed industry norms. Gomez did not notify Legend that he intended to participate in sales of U.S. Coal stock away from the firm for compensation.

Beginning on August 24, 2011, and ending on September 13, 2011, Gomez sold U.S. Coal shares to three investors, MB, TD, and RW, away from Legend. None of these investors was aware of U.S. Coal prior to hearing Gomez's solicitation. Gomez told each of them that U.S. Coal would conduct an IPO in the "near future," and based on Gomez's recommendations, they each agreed to purchase 10,000 shares of U.S. Coal stock from Blackstone for $35,000. For his efforts, Gomez received commissions totaling $14,950. Gomez instructed RW, who was a Legend customer, to withdraw funds from his brokerage account to pay for his purchase of U.S. Coal shares.

As time went on, Gomez received conflicting information about U.S. Coal. Gomez testified that CF "would tell [him] one thing and then another thing and then another thing." As the months went by, "[i]t was frustrating to get a real answer." Gomez felt frustrated by his inability to speak with LF directly. When a U.S. Coal IPO did not occur, Gomez tried to contact LF. Although Gomez thought he had set up a call with LF, it never happened.

Despite harboring some reservations, Gomez continued his efforts to solicit investors for Blackstone's U.S. Coal shares. On December 12, 2011, Gomez solicited Legend customer JH, who agreed to purchase $105,000 worth of U.S. Coal stock. The record is unclear as to whether this transaction was completed.

An IPO of U.S. Coal stock never happened. In 2014, the company's creditors forced it into bankruptcy. MB, TD, and RW lost the entirety of their U.S. Coal investments.

V. Discussion

A. Gomez Engaged Impermissibly in Private Securities Transactions

NASD Rule 3040 prohibits a person associated with a FINRA member from participating "in any manner" in a "private securities transaction" unless that person provides prior written notice to his employer that describes the proposed transaction and his proposed role.[17] NASD

[17] FINRA interprets the phrase "in any manner" broadly to further the regulatory purpose of the rule. *See Dep't of Enforcement v. Love*, Complaint No. C3A010009, 2003 NASD Discip. LEXIS 17, at *30 (NASD NAC May 19, 2003) ("[B]oth the SEC and we have found that even very limited involvement by an associated person is sufficient to trigger the requirement that the person give written notice to his or her employer."), *aff'd*, 57 S.E.C. 315 (2004). NASD Rule 3040 defines a "private securities transaction" as "any securities transaction outside the regular course or scope of an associated person's employment with a member." NASD Rule 3040(e)(1).

Rule 3040(a), (b). In the case of a transaction involving "selling compensation," the rule requires further that the associated person receive written approval from the member before engaging in the transaction.[18] NASD Rule 3040(b), (c)(1).

The record supports conclusively the Hearing Panel's findings that Gomez participated in private securities transactions outside the scope of his employment with Legend without ever notifying the firm of his role in those transactions or receiving from the firm its written approval to participate in them for compensation. Gomez admits that he solicited, recommended, and sold to investors away from Legend, including customers of the firm, the securities offered or issued by Praetorian and U.S. Coal. Gomez further admits that he did so without disclosing, at any point during his period of registration with the firm, either orally or in writing, his proposed or actual role in those securities transactions and the compensation, in the form of commissions, he planned to and did receive for his efforts.[19] Legend did not permit its brokers to engage in the private sales of securities, and Gomez clearly denied the firm the vital opportunity to approve or disapprove his selling of securities away from the member for compensation.

Given these uncontroverted facts, and his admission that he is liable for the misconduct alleged in cause three of the complaint, we affirm the Hearing Panel's findings that Gomez violated NASD Rule 3040 and FINRA Rule 2010.[20]

B. Gomez Recommended Securities Without a Suitable Basis

NASD Rule 2310 requires, "[i]n recommending to a customer the purchase, sale, or exchange of any security," that a member or associated person "have reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts, if any, disclosed by such customer as to his other securities holdings and as to his financial situation and needs." *See* NASD Rule 2310(a); *see also* FINRA Rule 0140. Consequently, any recommendation to engage in a securities-related transaction must have both a "reasonable basis" and be suitable for the specific customer to whom it is directed. *See Richard G. Cody*, Exchange Act Release No. 64565, 2011 SEC LEXIS 1862, at *26 (May 27, 2011), *aff'd*, 693 F.3d 251 (1st Cir. 2012).

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[18] NASD Rule 3040 defines "selling compensation" as "any compensation paid directly or indirectly from whatever source in connection with or as a result of the purchase or sale of a security, including, though not limited to, commissions . . . ." NASD Rule 3040(e)(2).

[19] Gomez does not dispute that the investment interests in the Praetorian G entities and U.S. Coal involved in this case were securities within the meaning of Securities Act Section 2(a)(1) and Exchange Act Section 3(a)(10). *See* 15 U.S.C. §§ 77b(a)(1), 78c(a)(10).

[20] FINRA Rule 2010 requires FINRA members, in the conduct of their business, to observe high standards of commercial honor and just and equitable principles of trade. This rule applies with equal force to persons associated with a member. *See* FINRA Rule 0140(a) ("Persons associated with a member shall have the same duties and obligations as a member under the Rules"). A violation of one FINRA rule is also a violation of FINRA Rule 2010. *See Dep't of Enforcement v. Luo*, Complaint No. 2011026346206, 2017 FINRA Discip. LEXIS 4, at *20-21 (FINRA NAC Jan. 13, 2017).

"Reasonable basis" suitability requires that a registered representative possess an "adequate and reasonable" understanding that the recommended transaction could be suitable for at least some customers before he can conclude that it is suitable for any particular customer. *See F.J. Kaufman and Co.*, 50 S.E.C. 164, 168 (1989) (quoting *Hanly v. SEC*, 415 F.2d 589, 597 (2d Cir. 1969)). A representative violates this element of suitability when he fails to conduct a reasonable investigation to comprehend fundamentally the consequences of his recommendation and the potential risks and rewards that inhere to it. *See Michael Frederick Siegel*, Exchange Act Release No. 58737, 2008 SEC LEXIS 2459, at *28 (Oct. 6, 2008), *aff'd in relevant part*, 592 F.3d 147 (D.C. Cir. 2010).

For a recommendation involving the private placement of securities, a registered representative should conduct reasonable diligence of the issuer and the individuals involved with it; the issuer's purported business and prospects; the assets the issuer claims to hold or intends to acquire; any claims made about the securities at issue; and the handling and use of the offering's proceeds. *See FINRA Regulatory Notice 10-22*, 2010 FINRA LEXIS 43, at *12-13 (Apr. 2010) (discussing due diligence required for reasonable-basis suitability in context of recommended private offerings). As FINRA warned prior to the recommendations that Gomez made in this case, securities offerings involving purported pre-IPO shares of "hot" companies are, in particular, fraught with risk and often marked with the potential for fraud. *See FINRA Investor Alerts: Pre-IPO Offerings—These Scammers Are Not Your Friends* (Mar. 15, 2011), http://www.finra.org/Investors/ProtectYourself/InvestorAlerts/FraudsAndScams/P123316. In connection with any offering that claims to involve pre-IPO securities, it is necessary to vet fully the promoters of the offering, including internet research for history or news of any fraudulent or criminal activity, understand what individuals or firms will handle investment monies, and verify the terms and legitimacy of the investment by enlisting the aid of professionals who are in no way connected to it. *See id.* ("The bottom line is that many pre-IPO scams involve unlicensed individuals selling unregistered securities—that's why it's critical to check out both the promoter and the investment.").

Although Gomez had never been involved in a private placement or conducted his own due diligence, he knew that he was solely responsible for conducting his own investigation of the securities transactions that he recommended. The Hearing Panel, however, found that Gomez recommended the securities of two little-known entities, Praetorian and U.S. Coal, to investors, including Legend customers, without possessing an adequate and reasonable basis for believing these securities offerings were suitable for them. We agree.

Gomez recommended Praetorian's securities to investors and told them that the Praetorian G entities owned or had access to pre-IPO shares of hot companies like Groupon and Zynga. Gomez, however, had no direct knowledge that these claims were true. Although he attempted to verify Praetorian's ownership of the pre-IPO shares in which it claimed to offer investors an interest, Gomez was unable to validate these claims. He thus accepted at face value assurances from Howard and Mattera that the Praetorian G entities did in fact own the shares they claimed to possess, while thoughtlessly ignoring Praetorian's claim that this information was private. Gomez's reliance on such assurances highlights the arbitrary nature of his suitability investigation; as the registered representative who recommended the securities,

Gomez had an independent obligation to ensure he understood them. *See Cody*, 2011 SEC LEXIS 1862, at *34 ("[A] representative must have a reasonable understanding of the risks and benefits of the investment before he can recommend it."). He could not blindly rely, as he did here, on information provided by individuals involved with Praetorian as the basis for his recommendations. *See id.* (finding a registered representative's reliance on another's familiarity with the securities he recommended did not excuse his violation).

Gomez claimed that he read thoroughly the various subscription documents that Howard and others from Praetorian sent him concerning the offerings of the Praetorian G entities. Gomez, however, recognized that these documents contained obvious errors and inconsistencies that called into question the validity of the offerings and raised numerous questions about the amount and class of the pre-IPO shares the Praetorian G entities purported to own. Though he claimed the documents "looked fine," these documents could not have provided Gomez a reasonable basis for recommending Praetorian's securities to investors. *See Siegel*, 2008 SEC LEXIS 2459, at *30 (finding, even if a registered representative read them, offering documents that provided conflicting or confusing information about the details of a private placement could not provide evidence of reasonable basis suitability).

Gomez also claimed that he conducted due diligence on Praetorian. Gomez provided FINRA some internet-based research that he conducted before recommending the securities of the Praetorian G entities to investors. We agree with the Hearing Panel that this diligence was insufficient. The information Gomez acquired concerned an entity, The Mattera Reserve, that was not Praetorian, and Gomez never conducted a search of sites that would have provided important information to him and his customers, including the Commission's website. Gomez therefore failed to discover significant, adverse public information about the past criminal or fraudulent activities of Mattera, Arnold, and Howard that would have caused any reasonable securities industry professional to pause and question Praetorian's legitimacy, and the authenticity of FAST's purported "escrow services," before he recommended the securities. Gomez's recommendations concerning Praetorian and the Praetorian G entities were thus decidedly unreasonable. *See Dep't of Enforcement v. McGee*, Complaint No. 2012034389202, 2016 FINRA Discip. LEXIS 33, at *60-61 (FINRA NAC July 18, 2016) (finding, where a registered representative reviewed a company's website and marketing materials, visited the company's office, and met with representatives of the company, these activities were insufficient to satisfy the due diligence requirements of reasonable basis suitability where he failed to gain an understanding of the company and the investments it offered), *aff'd*, Exchange Act Release No. 80314, 2017 SEC LEXIS 987 (Mar. 27, 2017).

Gomez's investigation of U.S. Coal was similarly flawed. Gomez relied here primarily on information provided to him by HG, CF, and LF. For instance, when they told him that U.S. Coal planned an IPO in the "near future," he accepted these statements as fact, despite information he received from the company that it had no plan for an IPO of its shares at the time. Gomez also accepted without question a year-old, purported presentation about a U.S. Coal IPO, which he received from HG and never bothered to authenticate. Although Gomez believed that Blackstone's sale of U.S. Coal stock seemed reasonable, he could not recall in his testimony any of the facts that led him to this conclusion. Rather, he admittedly never questioned how Blackstone and LF sourced the U.S. Coal shares they were offering to sell investors, or why

Blackstone would not offer these securities through a registered broker-dealer, but away from such a firm for commissions that must have seemed too good to be true.

Based on the preponderance of this evidence, we conclude that Gomez had no basis, and certainly not an adequate and reasonable basis, for his belief that his recommendations regarding investments in Praetorian and U.S. Coal securities could be suitable for at least some investors. With offerings like those at issue here, concerning the private sale of interests that purport to involve pre-IPO shares, the spectrum of risks is wide. *See FINRA Investor Alerts: Pre-IPO Offerings—These Scammers Are Not Your Friends*. These risks include, at one end of the spectrum, the risk that an IPO will never occur, and at the other end, that the unregistered shares are part of a fraud in which the promoter does not have the shares he is offering. *Id.* The limited diligence that Gomez claims to have performed prior to soliciting investors for Praetorian, as well as for Blackstone's U.S. Coal shares, failed meaningfully or realistically to investigate or confront these risks. We therefore affirm the Hearing Panel's findings that Gomez violated NASD Rule 2310 and FINRA Rule 2010.

C. Gomez Fraudulently Misrepresented Facts to Investors

Exchange Act Section 10(b) makes it "unlawful for any person, directly or indirectly . . . [t]o use or employ, in connection with the purchase or sale of any security . . . , any manipulative or deceptive device or contrivance in contravention" of Commission rules. 15 U.S.C. § 78j(b). Exchange Rule 10b-5(b) makes it unlawful for any person "directly or indirectly" to "make any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made . . . not misleading."[21] 17 C.F.R. §240.10b-5(b). FINRA Rule 2020, FINRA's antifraud rule, prohibits FINRA members and their associated persons from effecting "any transaction in, or induc[ing] the purchase or sale of, any security by means of any manipulative,

[21] Exchange Act Rule 10b-5 implements the Commission's authority under Section 10(b) of the Exchange Act through three subsections that are not mutually exclusive. *See John P. Flannery*, Exchange Act Release No. 73840, 2014 SEC LEXIS 4981, at *29 (Dec. 15, 2014), *vacated on other grounds*, 810 F.3d 1 (1st Cir. 2015) (rejecting the Commission's key factual determinations on substantial evidence grounds); *see also Lorenzo v. SEC*, 872 F.3d 578, 588 (D.C. Cir. 2017) ("Rules 10b-5(a) and (c) . . . may encompass certain conduct involving the dissemination of false statements even if the same conduct lies beyond the reach of Rule 10b-5(b)."). Exchange Act Rules 10b-5(a) and (c), make it unlawful for any person directly or indirectly to, respectively, "employ any device, scheme, or artifice to defraud" or "engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security." 17 C.F.R. §240.10b-5(a), (c).

deceptive or other fraudulent device or contrivance."[22] Proof of scienter is required to establish a violation of each of the foregoing provisions.[23] *See Luo*, 2017 FINRA Discip. LEXIS 4, at *20.

Enforcement alleged, and the Hearing Panel found, that Gomez made material misstatements of fact when he solicited investors to purchase securities issued by the Praetorian G entities and U.S. Coal. We agree.

Gomez admits that he told the investors he solicited for Praetorian that the Praetorian G entities owned or had access to pre-IPO shares of Groupon or Zynga stock and that, by investing in the securities of the Praetorian G entities, they would acquire an ownership interest in Groupon's or Zynga's stock. Gomez also admits that he told investors to which he recommended the purchase of Blackstone's U.S. Coal securities that U.S. Coal would conduct an IPO in the "near future." These statements of fact were demonstrably false.[24] Praetorian and the Praetorian G entities were fraudulent and they did not own the pre-IPO shares they purported to own. With respect to U.S. Coal, the company had no plans to undertake an IPO at the time Gomez told investors that it was. Indeed, the company eventually went bankrupt without ever conducting an IPO of its securities.

We find also that these misstatements were material. "[M]ateriality depends on the significance the reasonable investor would place on the withheld or misrepresented information." *Basic v. Levinson*, 485 U.S. 224, 239 (1988). A fact is therefore material if there is a substantial likelihood that a reasonable investor would have viewed it as significantly altering the total mix of information made available. *Id.* at 231-32 (quoting *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)). The truth that Praetorian and the Praetorian G entities did not own pre-IPO shares of Groupon or Zynga, and that U.S. Coal had no plans to pursue an IPO, would have undoubtedly been material to the investors Gomez solicited. Gomez's false statements to the contrary significantly altered the total mix of information available to these investors and any reasonable investor. *See, e.g.*, *Kenny Akindemowo*, Exchange Act Release No. 79007, 2016 SEC

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[22] Although it proscribes fraud with language similar to Exchange Act Section 10(b) and Exchange Act Rule 10b-5, FINRA Rule 2020 captures a broader range of activities. *See Dep't of Enforcement v. Fillet*, Complaint No. 2008011762801, 2013 FINRA Discip. LEXIS 26, at *38 (FINRA NAC Oct. 2, 2013), *aff'd in relevant part*, Exchange Act Release No. 75054, 2015 SEC LEXIS 2142 (May 27, 2015).

[23] Section 10(b) of the Exchange Act and Exchange Act Rule 10b-5 include jurisdictional elements that prohibit fraud by "any means or instrumentality of interstate commerce." *See* 15 U.S.C. § 78j; 17 C.F.R. 240.10b-5. Gomez admits that his conduct in this case occurred by means or instrumentality of interstate commerce.

[24] Gomez is liable for his oral misstatements under Exchange Act Rule 10b-5(b) if he made these statements with scienter, which we conclude below he did. *See SEC v. McDuffie*, Civ. Action No. 12-cv-02939, 2014 U.S. Dist. LEXIS 128664, at *23 (D. Colo. Sept. 15, 2014) ("A defendant is liable for his or her own oral misstatements and omissions."); *cf. Janus Capital Grp., Inc. v. First Derivative Traders*, 564 U.S. 135, 143 (2011) ("[I]t is the speaker who takes credit—or blame—for what is ultimately said.").

LEXIS 3769, at *17 (Sept. 30, 2016) ("[A] reasonable investor would want to know how their funds were actually being used."); *Dane S. Faber*, 57 S.E.C. 297, 307 (2004) (finding registered representative's false statement that an offering was an IPO was a material misrepresentation).

Having found that Gomez misrepresented material facts to investors, the Hearing Panel nevertheless dismissed the claim that Gomez engaged in fraud. Citing Gomez's "inexperience and ignorance," the Hearing Panel concluded that Gomez was "negligent" and his conduct "did not rise to the level of scienter required by the anti-fraud provisions." We do not concur in the Hearing Panel's assessment of the evidence and find that Gomez acted at least recklessly when he misrepresented material facts to investors. *See Joseph Abbondante*, Exchange Act Release No. 53066, 58 S.E.C. 1082, 1104 (2006) ("[T]he NAC acted within its authority in reviewing the Hearing Panel's dismissal of scienter-based fraud allegations.").

Scienter is "a mental state embracing intent to deceive, manipulate, or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976). It includes intentional or reckless conduct. *See Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 319 n.3 (2007). Reckless conduct includes "a highly unreasonable omission, involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known . . . or is so obvious that the actor must have been aware of it."[25] *Sundstrand Corp. v. Sun Chem. Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977).

Affirmative statements concerning the purchase or sale of a security come with the "ever-present duty not to mislead." *See Basic*, 485 U.S. at 241 n.18. A registered representative is required to give honest and complete information when he recommends the purchase or sale of a security. *See De Kwiatkowski v. Bear Stearns & Co.*, 306 F.3d 1293, 1302 (2d Cir. 2002). A broker is under a duty to investigate, and "[h]e cannot recommend a security unless there is an adequate and reasonable basis for such recommendation." *Hanly v. SEC*, 415 F.2d 589, 595-96 (2d Cir. 1969). As we note above, in the context of a private placement of securities, a registered representative has an obligation to conduct a reasonable investigation of the issuer and the securities offering. *See FINRA Regulatory Notice 10-22*, 2010 FINRA LEXIS 43, at *10-13. He may not simply ignore facts about which he has a duty to know or recklessly state those facts about which he is ignorant. *See Luo*, 2017 FINRA Discip. LEXIS 4, at *20 (quoting *Dep't of Enforcement v. Cipriano*, Complaint No. C07050029, 2007 NASD Discip. LEXIS 23, at *34 (NASD NAC July 26, 2007)).

With respect to the Praetorian sales, we conclude that Gomez failed to perform a meaningful investigation of the securities and their promoters, and he did not respond to red flags and other factors relating to Praetorian's claim of ownership of pre-IPO stock. *See Alvin W. Gebhart*, Exchange Act Release No. 58951, 2008 SEC LEXIS 3142, at *27-28 (Nov. 14, 2008) (finding respondents recklessly made critical representations related to the safety of notes without performing any reasonable investigation into the actual securitization of the notes), *aff'd*, 595 F.3d 1034 (9th Cir. 2010). This created the substantial risk, which would have been obvious

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[25] Proof of recklessness may be inferred from circumstantial evidence. *Herman & MacLean v. Huddleston*, 459 U.S. 375, 390 n.30 (1983).

to any reasonable securities professional, and must have been obvious to Gomez, that his representations to investors were not true. *See id.* at *28 ("We remain convinced that the Gebharts' conduct satisfies this definition of recklessness.").

Without having performed any significant, independent investigation, Gomez recommended Praetorian and told investors that Praetorian owned or had access to pre-IPO stock in which they would acquire an interest. Gomez knew that, in making this representation, he was relying on what Howard and Mattera told him. Gomez had no knowledge that this was true, and when he attempted to investigate, he was unable to verify the validity of their claims. His failure to conduct a purposeful investigation regarding the availability of pre-IPO shares, as well as his inability to fully research and detect the questionable backgrounds of Mattera and his associates, was reckless. *See SEC v. Milan, Inc.*, 00 CIV. 108 (DLC), 2000 U.S. Dist. LEXIS 16204, at *17 (S.D.N.Y. Nov. 9, 2000) ("Cope had ample opportunity to question the availability of the shares to Milan, and Milan's bona fides in executing the transactions.").

Moreover, reckless conduct can occur where a "variety of circumstances may raise enough questions about the legitimacy of an investment to make a person's failure to investigate before recommending that investment reckless." *See id.* at *15. Here, while continuing to solicit investors, Gomez was aware of numerous red flags that he encountered, including that the Praetorian subscription documents often contained discrepancies, he could not receive a satisfactory answer when he inquired about those inconsistencies, and Praetorian often simply sent Gomez new documents that removed problematic information and references. For example, after soliciting DB's investment, Gomez noticed that G Power V claimed to own more Series E preferred stock than Groupon had issued. When Gomez questioned Praetorian about this discrepancy, it simply sent him new subscription documents that changed the offering to reflect that Praetorian owned Series B-1 preferred shares, which Praetorian claimed were somehow subsumed within Series F shares. Gomez admits he did nothing to verify these claims, and days later he solicited the investments of TD, JG, RW, and AM.

Gomez knew also that he was receiving commissions at a rate that exceeded brokerage industry norms, Howard paid his commissions by personal check, and Praetorian ultimately changed his commission agreement when he complained. Gomez failed to absorb Howard's statements concerning his inability to pay his commissions, that his accounts were frozen, and that he was talking to an attorney. Finally, Gomez knew that Praetorian allowed his customers to convert their unprofitable Groupon investments into investments in Zynga without cost. Despite this, Gomez made a final Praetorian sale to TS. Continuing with a sale to TS, despite numerous red flags and a lack of independent verification, was undoubtedly reckless.

Similarly, with respect to U.S. Coal, Gomez knew that LF was trying to sell shares through private securities transactions, rather than through a registered broker-dealer, and was paying Gomez commissions well above industry norms. Gomez knew too that the purported IPO presentation he received was more than a year old, and a statement from a company representative contradicted the claim that U.S. Coal planned an IPO in the "near future." Although he harbored reservations because of these circumstances, Gomez solicited U.S. Coal investments from MB, TD, and RW. Indeed, his admitted frustration with the lack of a U.S.

Coal IPO and his inability to obtain any information from CF and LF did not stop him from soliciting JH to purchase Blackstone's U.S. Coal shares.

Under these circumstances, Gomez's "refusal to see the obvious, or to investigate the doubtful," gives rise to an inference of reckless misconduct. *See South Cherry St., LLC v. Hennessee Group LLC*, 573 F.3d 98, 109 (2d Cir. 2009). The Hearing Panel based its finding of negligence on Gomez's reliance and belief in Howard, Mattera, HG, CF, and LF. His misplaced confidence in these individuals, however, must be evaluated in light of the obvious warning signs that further investigation was necessary. *See Gebhart*, 2008 SEC LEXIS 3142, at *31-32 ("[T]he Gebharts ignored these facts, performed no investigation, and asserted the truth of critical matters with no objective, independent basis for doing so."). Gomez "made no meaningful attempts to confirm the validity of [his] assertions to clients . . . . [and] made these unsupported representations to clients despite not knowing whether they were true or false and despite having several and varied reasons to doubt the truth of [his] own statements." *See id.* at *37-38. We find Gomez's claim that he conducted all the diligence necessary for him to recommend Praetorian and U.S. Coal securities to investors to be obviously unreasonable. Contrary to his assertions, Gomez must have known that, when he made his misrepresentations, his actions presented an unacceptable danger of misleading investors that was reckless. *See Gebhart*, 2008 SEC LEXIS 3142, at *35 ("A respondent's asserted good faith belief is not plausible if he ignores facts that place him on notice of misleading clients.").

A registered representative cannot shift to others his responsibility to refrain from committing fraud. *See SEC v. Hasho*, 784 F. Supp. 1059, 1107 (S.D.N.Y. 1992) ("Salesmen or registered representatives have certain duties that they cannot avoid by reliance on either their employer or issuer."); *see also Faber*, 57 S.E.C. at 309-10 (rejecting argument that respondent did not possess the scienter necessary to establish liability for fraudulent misrepresentations and omissions where respondent argued that he relied on information provided by his firm). Gomez may not invoke his inexperience as a defense for his fraud.[26] *See Hasho*, 784 F. Supp. at 1108 ("Those who hold themselves out as professionals with specialized knowledge and skill to furnish guidance can not be heard to claim youth or inexperience when faced with charges of violations of the anti-fraud provisions of the securities laws.").

We therefore conclude that Gomez made material misrepresentations during the offer and sale of the Praetorian and U.S. Coal securities. We also conclude that Gomez failed to make necessary investigations, ignored obvious risks, and made his recommendations based primarily on the statements of others, and he therefore acted recklessly and with scienter. His conduct was an extreme departure from the standard of care for a meaningful investigation such that Gomez must have been aware that he was putting investors in danger. We therefore find that Gomez

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[26] Gomez claims as evidence of his purported good faith that his brother, JG, invested in Praetorian's Groupon entity. It is well established, however, that investing one's own funds, or the funds of friends or family members, does not negate scienter. *See Gebhart*, 2008 SEC LEXIS 3142, at *37; *see also John R. Brick*, 46 S.E.C. 43, 49 n.16 (1975) (respondent's "willingness to gamble with his own money and with that of his father-in-law did not give him a license to make unfounded recommendations to clients").

violated Exchange Act Section 10(b), Exchange Act Rule 10b-5, and FINRA Rules 2020 and 2010.

VI. Sanctions

The Hearing Panel imposed a unitary sanction, a single bar, for Gomez's selling away and suitability violations. In light of our finding that Gomez engaged also in fraud, we modify the sanctions imposed by the Hearing Panel and assess sanctions by cause for Gomez's several, serious violations.

A. Selling Away

For violations involving private securities transactions, the Guidelines instruct us to assess first the extent of the selling away.[27] Gomez sold away from Legend in securities transactions totaling $499,000 to seven investors over a period of approximately five months. The Guidelines recommend, as a starting point, a suspension of three to six months for this level of activity.[28]

The Guidelines further instruct us, however, to consider the presence of one or more aggravating factors that may raise or lower the sanction imposed.[29] We find present a number of aggravating factors that warrant a significantly higher sanction in this case.

First, the Praetorian securities that Gomez sold away from Legend resulted from fraudulent and criminal activities.[30] Second, his selling away directly injured members of the investing public, with the investors he solicited losing at least $499,000 as a result of their investments in the Praetorian G entities and U.S. Coal.[31] Third, Gomez sold away to customers of his firm.[32] Fourth, Gomez participated directly in the selling away of Praetorian and U.S. Coal securities.[33] Fifth, the evidence in the record shows that Gomez recruited at least one other

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27 *See FINRA Sanction Guidelines* 14 (2017), http://www.finra.org/sites/default/files/Sanctions_Guidelines.pdf [hereinafter *Guidelines*].

28 *See id.* The Guidelines also recommend a fine of $5,000 to $73,000. *Id.*

29 *Id.*

30 *See id.* (Principal Considerations in Determining Sanctions, No. 4).

31 *See id.* at 15 (Principal Considerations in Determining Sanctions, No. 7).

32 *See id.* (Principal Considerations in Determining Sanctions, No. 8).

33 *See id.* (Principal Considerations in Determining Sanctions, No. 11).

broker at another firm to sell Praetorian securities.[34] Finally, Gomez concealed his activities from his firm, while understanding that the firm prohibited private securities transactions.[35]

Gomez acknowledges that, despite Legend's prohibition on private securities transactions, he understood, at the time of the transactions that are at issue in this case, he had a duty to notify Legend that he intended to sell securities away from the firm. Gomez nevertheless consciously decided that he would not notify Legend of the Praetorian and U.S. Coal securities transactions in which he planned to participate, knowing that he could suffer repercussions for his decision to conceal his activities from the firm. We therefore conclude that Gomez exhibited a troubling, intentional disregard of a fundamental obligation imposed on him as securities industry professional.[36]

"[S]elling away is a serious violation." *Jim Newcomb*, 55 S.E.C. 406, 417 (2001). The Commission "repeatedly [has] stated that the prohibition on private securities transactions is fundamental to any associated person's duty to his customers and his firm." *Harry Friedman*, Exchange Act Release No. 64486, 2011 SEC LEXIS 1699, at *35 (May 13, 2011). NASD Rule 3040 "protect[s] investors from unsupervised sales and securities firms from exposure to loss and litigation from transactions by associated persons outside the scope of their employment." *Chris Dinh Hartley*, 57 S.E.C, 767, 775 n.17 (2004). The rule therefore plays a crucial role in the regulatory scheme, and its abuse calls for significant sanctions. *See Ronald W. Gibbs*, 52 S.E.C. 358, 365 (1995).

In light of these aggravating factors, and in the absence of any mitigating factors, we bar Gomez from associating in any capacity with any FINRA member firm for violating NASD Rule 3040 and FINRA Rule 2010.

B. Suitability Violations

The Guidelines for suitability violations recommend suspending an individual respondent in any or all capacities for a period of 10 days to two years.[37] Where aggravating factors predominate, the Guidelines recommend that we strongly consider a bar.[38]

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34 *See id.* (Principal Considerations in Determining Sanctions, No. 12).

35 *See id.* (Principal Considerations in Determining Sanctions, Nos. 10, 13). Gomez went to Legend's office only a few times while registered with the firm, and he typically worked at his or a friend's apartment. He concealed his activities from Legend by avoiding the firm's office and using his personal email account for any Praetorian-related business.

36 *See id.* at 8 (Principal Considerations in Determining Sanctions, No. 13).

37 *Guidelines*, at 95. The Guidelines also recommend a fine of $2,500 to $110,000. *Id.*

38 *Id.*

We conclude that a bar is an appropriate sanction in this case. Gomez breached an important duty that is fundamental to the relationship between a registered representative and his customers when he recommended that investors, including Legend customers, invest in Praetorian and U.S. Coal securities, without possessing a reasonable basis for his recommendations. *See Dep't of Enforcement v. Wilson*, Complaint No. 2007009403801, 2011 FINRA Discip. LEXIS 67, at *47 (FINRA NAC Dec. 28, 2011) ("Wilson's unsuitable transactions were in serious breach of his duty to his customers."). He engaged in a decidedly risky course of conduct that was without any apparent concern for investors or of the risks involved with his recommendations.

We consider it aggravating that Gomez engaged in a clear pattern of misconduct, and he abused the trust and confidence placed in him by investors and his customers, by recommending a significant number of unsuitable transactions over an extended period.[39] *See Dep't of Enforcement v. Epstein*, Complaint No. C9B040098, 2007 FINRA Discip. LEXIS 18, at *94 (FINRA NAC Dec. 20, 2007) ("Given that Epstein made unsuitable recommendations to at least 12 customers over a period of several months, we find that Epstein systematically failed to uphold high standards of commercial honor."), *aff'd*, Exchange Act Release No. 59328, 2009 SEC LEXIS 217 (Jan. 30, 2009), *aff'd*, 416 F. App'x 142 (3d Cir. 2010). He did so for his own monetary gain, while investors suffered substantial, direct losses because of his actions.[40]

Gomez's failure to accept responsibility for his actions is particularly disturbing.[41] Throughout these proceedings, Gomez regularly defended his conduct by asserting that the investors he solicited to invest in Praetorian and U.S. Coal securities never questioned his recommendations. A broker, however, has a duty to refrain from making unsuitable recommendations, regardless of a customer's desire or interest to invest in the recommended security. *See James B. Chase*, 56 S.E.C. 149, 159 & n.23 (2003) (stating the "test for whether [respondent's] recommendations were suitable is not whether [customers] acquiesced in them"). The duty Gomez possessed to ensure that he had a reasonable basis for his recommendations was his alone. *See Cody*, 2011 SEC LEXIS 1862, at *34 ("Cody, as the broker who recommended the securities, had an independent obligation to ensure that he understood them."). His failure to recognize the inadequacy of his examination of Praetorian and U.S. Coal, or the red flags that made his suitability determinations inherently suspect, supports imposing a bar. *See Luo*, 2017 FINRA Discip. LEXIS 4, at *34 ("We are particularly troubled by Luo's continuing failure . . . to recognize the inadequacy of his investigation . . . ."). In light of our duty to protect the investing public and ensure the integrity of the market, we find we must act decisively in this case, as we have done in similar cases, where the evidence demonstrates that a respondent proved himself indifferent to his duty to ensure that he recommend suitable transactions to his customers. *See Epstein*, 2007 FINRA Discip. LEXIS 18, at *100-01 ("Epstein's demonstrated

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[39] *See Guidelines*, at 7 (Principal Considerations in Determining Sanctions, Nos. 8, 9).

[40] *See Guidelines*, at 8 (Principal Considerations in Determining Sanctions, Nos. 16, 17, 18).

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

insouciance and indifference towards his responsibilities under NASD rules poses a serious risk to the investing public.").

Accordingly, we bar Gomez from associating in any capacity with any FINRA member firm for violating NASD Rule 2310 and FINRA Rule 2010.

C. Fraudulent Misrepresentations of Material Facts

Fraud violations, such as those that Gomez committed, are "especially serious and subject to the severest of sanctions under the securities laws." *See Marshall E. Melton*, 56 S.E.C. 695, 713 (2003). The Guidelines for intentional or reckless misrepresentations or omissions of material fact therefore recommend that we strongly consider barring an individual respondent, unless mitigating factors predominate.[42]

We conclude that there are aggravating factors, and no mitigating factors, that support a decision to bar Gomez for his fraud. Gomez recklessly misrepresented facts that he must have known would persuade investors to purchase Praetorian and U.S. Coal securities and the pre-IPO shares in which they claimed to offer investors an interest.[43] As we note above, Gomez also profited from his misconduct, while the investors he solicited to invest in the Praetorian G entities and U.S. Coal lost the entirety of their investments.[44] Although Gomez claimed as mitigation his lack of a disciplinary history, this argument is without merit. On January 18, 2017, Gomez entered into a Letter of Acceptance, Waiver and Consent ("AWC") to settle a FINRA disciplinary action. The AWC included findings that Gomez, among other things, exercised discretion without prior written authorization, excessively traded customer accounts, and engaged in qualitatively unsuitable and unauthorized trading, in violation of FINRA rules. For this misconduct, Gomez received a one-year suspension from associating with any FINRA member in any capacity. To the extent Gomez claims that he did not engage in any misconduct before the activities that are at issue in this case, his lack of a prior disciplinary history is not mitigating for purposes of assessing sanctions. *See Fillet*, 2013 FINRA Discip. LEXIS 26, at *62.

Gomez also claimed that he is a "good" and "honest person." We conclude, however, that his willingness to place his personal interests deceitfully before those of his firm, and the investors and customers he solicited, reinforces the conclusion that a bar is the correct sanction in this case. *Cf. Janet Gurley Katz*, Exchange Act Release No. 61449, 2010 SEC LEXIS 994, at *92 (Feb. 1, 2010) ("Katz's assertions that she was a nice person who did a good job for her clients similarly do not warrant a lesser sanction . . . ."). Indeed, Gomez claimed frequently

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42 *See Guidelines*, at 89. They also recommend a fine of $10,000 to $146,000. *Id.*

43 *See id.* at 8 (Principal Considerations in Determining Sanctions, No. 13); *see also Fillet*, 2013 FINRA Discip. LEXIS 26, at *52-53 ("Fillet recklessly misrepresented . . . important information . . . that he knew would be used to persuade potential investors to purchase units in the . . . offering.").

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

during these proceedings that he too is a casualty of the misconduct of others and complained regularly that FINRA's disciplinary action hindered his ability to conduct business—"I feel I have suffered enough through all this." His claim that he is a "victim" is not mitigating. *See Dep't of Enforcement v. Ortiz*, Complaint No. 2014041319201, 2017 FINRA Discip. LEXIS 5, at *37 (FINRA NAC Jan. 4, 2017). As a registered securities industry professional, Gomez flouted the high standards of conduct that FINRA expects of its members and their associated persons when they participate in the sale of privately placed securities. *See FINRA Regulatory Notice 10-22*, 2010 FINRA LEXIS 43, at *1 ("FINRA reminds broker-dealers of their obligation to conduct a reasonable investigation of the issuer and the securities they recommend in offerings . . . known as private placements."). His conduct demonstrates that he is fundamentally unfit to continue as an associated person of a FINRA member. *See Akindemowo*, 2016 SEC LEXIS 3769, at *39 ("Akindemowo defrauded investors with false statements about securities and pocketed funds entrusted to him—this conduct demonstrates a fundamental unfitness for association in the securities industry.").

Accordingly, we bar Gomez from associating with any FINRA member in any capacity for violating Exchange Act Section 10(b), Exchange Act Rule 10b-5, and FINRA Rules 2020 and 2010.

VII. Conclusion

We find that Gomez sold securities away from his member firm without providing the firm prior written notice, in violation of NASD Rule 3040 and FINRA Rule 2010. We find also that Gomez recommended securities to investors, without a reasonable basis as to the suitability of those securities, in violation of NASD Rule 2310 and FINRA Rule 2010. Finally, we find that Gomez fraudulently misrepresented material facts to investors, in violation of Exchange Act Section 10(b), Exchange Act Rule 10b-5, and FINRA Rules 2020 and 2010. Accordingly, we bar Gomez from associating with any FINRA member in any capacity for each of the foregoing violations. The three bars are effective immediately upon issuance of this decision. We also affirm the Hearing Panel's order that Gomez pay hearing costs of $3,498.16 and impose appeal costs of $1,480.66.[45]

On behalf of the National Adjudicatory Council,

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Jennifer Piorko Mitchell, Vice President and
Deputy Corporate Secretary

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[45] Pursuant to FINRA Rule 8320, FINRA will revoke for non-payment the registration of any person associated with a member who fails to pay any fine, costs, or other monetary sanctions after seven days' notice in writing.