

UNITED STATES OF AMERICA  
Before the  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

In the Matter of  
  
PAUL EDWARD "ED" LLOYD, JR., CPA

INITIAL DECISION  
July 27, 2015

APPEARANCES: Robert F. Schroeder and Brian M. Basinger, representing the Division of Enforcement, Securities and Exchange Commission

Frederick K. Sharpless, Sharpless & Stavola, P.A., representing Respondent Paul Edward "Ed" Lloyd, Jr., CPA

BEFORE: Cameron Elliot, Administrative Law Judge

### SUMMARY

This Initial Decision finds that Respondent Paul Edward "Ed" Lloyd, Jr., CPA, violated Section 206(4) of the Investment Advisers Act of 1940 (Advisers Act). This Initial Decision orders Lloyd to cease and desist from violating Advisers Act Section 206(4), and imposes an associational bar, disgorgement of \$105,750, and civil penalties of \$100,000 against Lloyd.

### I. INTRODUCTION

#### A. Procedural Background

The Securities and Exchange Commission (Commission) issued an Order Instituting Administrative and Cease-and-Desist Proceedings (OIP) on September 30, 2014, pursuant to the Securities Act of 1933 (Securities Act) Section 8A, Securities Exchange Act of 1934 (Exchange Act) Sections 15(b) and 21C, Advisers Act Sections 203(f) and 203(k), and Investment Company Act of 1940 (Investment Company Act) Section 9(b). Lloyd answered on October 22, 2014.

A hearing was held on March 19-20 and 23-25, 2015, in Charlotte, North Carolina. The admitted exhibits are listed in the Record Index issued by the Office of the Secretary. The

Division of Enforcement (Division) and Respondent filed post-hearing briefs and briefing was complete on May 29, 2015.<sup>1</sup>

## **B. Summary of Allegations**

This proceeding concerns alleged unregistered broker-dealer activity, fraudulent offer and sale of investments in land conservation easements, and misappropriation of investor<sup>2</sup> funds. OIP at 2. More specifically, the OIP alleges that Lloyd created and controlled three business entities in which he pooled investor funds to purchase units of unrelated entities, offered privately pursuant to Regulation D (Reg D) (17 C.F.R. § 230.501 *et seq.*), which planned to acquire controlling interests in land to be set aside for conservation. *Id.* at 2-3. It further alleges that in connection with one of these pooled fund entities, Forest Conservation 2012 (FC12), Lloyd misappropriated \$130,000 of investor assets, made various misrepresentations to a securities broker, and later took steps to conceal his scheme. *Id.* at 2-3, 9. The OIP alleges that Lloyd willfully violated Securities Act Section 17(a) and Exchange Act Section 10(b) and Rule 10b-5 thereunder, which prohibit fraudulent conduct in the offer and sale of securities and in connection with the purchase or sale of securities; Advisers Act Sections 206(1), 206(2), and 206(4), and Rule 206(4)-8 thereunder, which prohibit fraudulent conduct by an investment adviser; and Exchange Act Section 15(a), which prohibits an unregistered broker-dealer from effecting transactions in securities unless an exemption from registration applies. *Id.* at 10-11.

Lloyd disputes that he dealt in securities, and instead asserts that he arranged tax deductions for his clients through their participation in conservation easements. Answer at 7; Resp. Br. at 16. He further denies misappropriation of investor assets and concealment of any scheme. Resp. Br. at 14, 23-24.

## **C. Summary Disposition Ruling**

Prior to the reassignment of this proceeding to me, the presiding administrative law judge ruled on Respondent's motion for summary disposition. *Paul Edward "Ed" Lloyd, Jr., CPA*, Admin. Proc. Rulings Release No. 2366, 2015 SEC LEXIS 767 (Feb. 27, 2015) (Summary Disposition Order); *see Paul Edward "Ed" Lloyd, Jr., CPA*, Admin. Proc. Rulings Release No. 2425, 2015 SEC LEXIS 968 (Mar. 16, 2015). The Summary Disposition Order held that any interests Lloyd sold were not securities, and that Lloyd's alleged activities therefore did not

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<sup>1</sup> Citations to the hearing transcript are noted as "Tr. \_\_\_\_." Citations to exhibits offered by the Division and Respondents are noted as "Div. Ex. \_\_\_\_" and "Resp. Ex. \_\_," respectively. The Division's and Respondent's post-hearing briefs are noted as "Div. Br. \_\_\_\_." and "Resp. Br. \_\_\_\_.", respectively. The Division's and Respondent's post-hearing reply briefs are noted as "Div. Reply \_\_\_\_" and "Resp. Reply \_\_," respectively.

<sup>2</sup> This Initial Decision uses the term "investor" interchangeably with similar terms, such as "participant." The term "investor" is used in many exhibits to refer to persons contributing money to the ventures at issue, and its use in this Initial Decision is not meant to imply that the interests at issue were securities. *E.g.*, Div. Ex. 56 at 2035.

involve securities transactions. Summary Disposition Order, 2015 SEC LEXIS 767, at \*5, \*12-14. Accordingly, the Summary Disposition Order determined that “[w]hether he sold any such interests to advisory clients and engaged in prohibited practices in doing so remains at issue,” and that only the charges of violations of Advisers Act Sections 206(1), 206(2), and 206(4) would proceed. *Id.* at \*5, \*15. Upon reassignment of the case to me, I stated that I would not reconsider the Summary Disposition Order because doing so would “prejudice the Respondent[] unduly.” Mar. 16, 2015, Prehearing Tr. 24-25. However, I permitted both parties to make offers of proof during the hearing. Tr. 139, 213, 1079.

## II. FINDINGS OF FACT

The findings and conclusions herein are based on the entire record and on facts officially noticed pursuant to Rule 323 of the Commission’s Rules of Practice (Rules), 17 C.F.R. § 201.323. The parties’ motion papers and all documents and exhibits of record have been fully reviewed and carefully considered. I have determined all facts based on a preponderance of the evidence standard of proof. *See Steadman v. SEC*, 450 U.S. 91, 102 (1981). I have considered and rejected all arguments, proposed findings, and conclusions that are inconsistent with this Initial Decision.

### A. Background

#### 1. Lloyd

Lloyd is about fifty years of age and lives in North Carolina. Div. Ex. 185. He has run a Certified Public Accountant practice, Ed Lloyd & Associates, PLLC, since late 1993. Tr. 692-93; Div. Ex. 185 at 5. His CPA practice, located in Charlotte, provides tax planning, accounting, and consulting services to individuals and small business. Tr. 693, 824-25. He regularly prepares federal and state tax returns for clients, but does not audit public companies. Tr. 632, 694, 824. Ed Lloyd & Associates employs a small number of other accountants and an administrative assistant. Tr. 693-94. Lloyd obtained his CPA license in 1990 following his graduation from the University of North Carolina at Charlotte. Div. Ex. 185 at 3-4.

Lloyd until recently also maintained an investment advisory business. Tr. 306-07, 551, 695, 826-29; Paul Edward Lloyd Jr. BrokerCheck Report at 3-4 (data current as of Jan. 20, 2015) (BrokerCheck Report).<sup>3</sup> Lloyd operated Ed Lloyd Wealth Management through an association with registered broker-dealer and investment adviser firm LPL Financial LLC (LPL) from late 2006 to March 2013. Tr. 274, 551, 695, 771, 826-29; BrokerCheck Report at 4, 7. A non-registered administrative assistant was also involved in Lloyd Wealth Management. Tr. 274, 292. Prior to 2006, Lloyd controlled an entity called Ed Lloyd Investments LLC and was affiliated with two other brokerage firms. Tr. 698-99; BrokerCheck Report at 4. Lloyd first became involved in the securities industry no later than 2000, and passed five industry exams,

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<sup>3</sup> Official notice was taken of this document pursuant to 17 C.F.R. § 201.323. *Paul Edward “Ed” Lloyd, Jr., CPA*, Admin. Proc. Rulings Release No. 2560, 2015 SEC LEXIS 1452 (Apr. 20, 2015).

including the Series 7 (General Securities Representative Examination) and the Series 65 (Uniform Investment Adviser Law Examination). Tr. 695; BrokerCheck Report at 3. He currently is not listed as associated with a broker-dealer or investment adviser. BrokerCheck Report at 1.

Beyond his tax practice and securities industry involvement, Lloyd has also controlled or been involved in a number of business entities in the insurance or captive insurance industry, including Benefit Administrative Services LLC. Tr. 1035, 1038-44; *see* Div. Ex. 102. Lloyd did not disclose his affiliation with these insurance entities to Commission staff in the course of its pre-OIP investigation of Lloyd. Tr. 1036, 1038; Div. Ex. 185. His explanation of why he did not disclose his affiliation with them when asked to fill out a background questionnaire, asking for educational and employment history, was hard to comprehend. *See* Div. Ex. 185. Specifically, he testified that he did not think he needed to disclose affiliations with business entities he owned because he did not consider himself an employee of them. Tr. 1037. Lloyd is also affiliated, through his wife, with Corporate Solutions, Inc., which provides registered agent services for state-registered business entities. Tr. 856-57, 1045-46; *see* Div. Ex. 67.

## 2. LPL Policies and Procedures

Relevant to this proceeding are a number of policies maintained by LPL in the 2011-12 timeframe. These policies were communicated in LPL's Advisor Compliance Manual. Tr. 285, 717-18; *see* Div. Exs. 154, 155. Financial advisors associated with LPL, like Lloyd, are required to be familiar with the manual and copies of it are made available to them. Tr. 319-20. Lloyd received both the manual and training in connection with it. Tr. 717-18.

Selling away and outside business activities. LPL forbids financial advisors from selling away, meaning selling a security not in connection with LPL, without LPL's knowledge of the existence of those securities sales and LPL's approval. Tr. 307-08; Div. Ex. 154 at 4681, 4683, 4720; Div. Ex. 155 at 7948, 7950, 7995.<sup>4</sup> LPL's selling away policy is designed to ensure compliance with FINRA Rule 3270 and NASD Rule 3040. Tr. 276; Div. Ex. 154 at 4681, 4683; Div. Ex. 155 at 7948, 7950. It further seeks to understand all outside business activities of its financial advisors to make certain that those outside business activities are suitable for LPL's financial advisory clients. Tr. 276.

LPL's selling away policy in the Advisor Compliance Manual states:

[A]ll associated persons must provide written notice to the member with which he is associated describing in detail the proposed transaction and the person's proposed involvement therein (i.e., playing a role in the private securities transaction or personally investing in it, etc.) and stating whether he has received or may receive selling compensation in connection with the transaction.

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<sup>4</sup> Page citations referring to the Bates stamp on the page only use the last four digits of the Bates stamp. For example, a page of Div. Ex. 9 with Bates stamp "SEC-LLOYD-P-0000015" is referred to simply as "Div. Ex. 9 at 0015."

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If an advisor wishes to engage in a private securities transaction, then he/she must submit the following to the LPL Financial AI Ops department: Alternative Investment—Accommodation Purchase Unsolicited Private Transaction Form[;] Prospectus or offering circular[;] Original application or subscription agreement[;] Sample certificate[;] Lien letter[;] 30-day assurance statement.”

Div. Ex. 154 at 4683; Div. Ex. 155 at 7950 (formatting altered). It then states: “[a]dvisors must state whether they received or may receive selling compensation in connection with the transaction”; “[a]dvisors may not solicit any clients for these types of investments”; and “[a]dvisors are strictly forbidden from investing in a private securities transaction with their clients.” Div. Ex. 154 at 4683; Div. Ex. 155 at 7950.

Erin Dethlefsen (Dethlefsen), an LPL senior branch examiner, testified regarding LPL’s selling away policy. Tr. 271-72, 314-15. She testified that LPL expects to be informed if an associated person is involved in pooling investor funds, including LPL client funds. Tr. 314-15. She also stated that an LPL advisor’s investment in a private securities transaction alongside the advisor’s clients is a violation of the Advisor Compliance Manual. Tr. 319.

Document signature policy. LPL has a policy forbidding the use of non-original or non-authentic client signatures on forms. “All documents requiring customer signatures and/or initials must bear original customer signature and initials” and “[c]utting or pasting previously provided customer’s signature or initials to any documents” is prohibited. Div. Ex. 154 at 4727; Div. Ex. 155 at 7995.

Tax advice and primary business of financial advisors. LPL financial advisors “are not permitted to give tax advice to customers.” Div. Ex. 154 at 4727; Div. Ex. 155 at 7995. LPL’s manual states that “[c]ustomers should be advised to consult their own tax advisor or accountant.” Div. Ex. 154 at 4727; Div. Ex. 155 at 7995. LPL also requires that any associated financial advisor is primarily in the business of being a financial advisor. Tr. 276; Div. Ex. 154 at 4688; Div. Ex. 155 at 7955. Despite these policies, throughout the time Lloyd was associated with LPL, Lloyd also maintained a CPA practice and LPL was aware that Lloyd maintained a CPA practice, and there is no evidence that LPL ever objected to his maintaining one. Tr. 287, 289, 320; BrokerCheck Report at 4.

## **B. Conservation Easements**

A conservation easement is a permanent legal restriction placed by a property owner on a piece of property. Tr. 97-98; Div. Ex. 94. The terms of the easement, recorded in the land deed, restrict the property from being developed and require that it be conserved for a stated purpose, e.g., animal habitat preservation. Tr. 97-98. Where a piece of land is granted a conservation easement, a federal tax deduction based on a charitable contribution, greater than the cost of the membership units purchased by the investor in the land, may be available; this means that the investor may enjoy a tax deduction, in dollars, far greater than the dollars invested in the land. Answer at 2 (admitting certain facts alleged in OIP ¶ 2); Tr. 212, 453; *see, e.g.*, Div. Ex. 94. If a

property owner wishes to pursue a conservation easement, the owner may elect to bring in partners in the ownership of the property. Tr. 99, 443-46; *see, e.g.*, Div. Ex. 94 at 0602.

Each of the three conservation easements in suit involved a property owner who created a limited partnership which issued membership units pursuant to Reg D. Tr. 99-100, 445-46; Div. Exs. 151, 152, 153. The three limited partnerships/issuers and their associated Reg D offerings were named Maple Equestrian, LLC (Maple Equestrian), Piney Cumberland Holdings, LLC (Piney Cumberland), and Meadow Creek Holdings, LLC (Meadow Creek). Div. Exs. 151, 152, 153. The offering documents portrayed the offerings as exempt from registration pursuant to Reg D because the issuers believed the offerings constituted securities. Tr. 442-44, 454, 495, 517-21.

Offering documents were prepared for each of the offerings. Tr. 99-100, 104, 462; Div. Ex. 9; Div. Ex. 55 Div. Ex. 56 at 1808-2025. Maple Equestrian was a 2011 offering of membership units in a property located in Alabama; Piney Cumberland was a 2012 offering of membership units in a property located in Tennessee; and Meadow Creek was a 2012 offering of membership units in a property also located in Tennessee. Tr. 129, 456-57, 489, 496-97; Div. Ex. 9 at 0006-07, 0015; Div. Ex. 55 at 0685-86, 0695; Div. Ex. 56 at 1808-09, 1818-19.

For each of the offerings, the decision to place the underlying land into conservation was not made, and could not be made, until after the offering closed, and the identity of the new landowners had been determined. Tr. 101, 130, 155, 182; Div. Ex. 9 at 0015, 0037; Div. Ex. 55 at 0696-97; Div. Ex. 56 at 1820, 1841. Each offering's Private Offering Summary contemplated that the underlying land might be developed rather than conserved, or used for some other purpose altogether. Tr. 448; Div. Ex. 9 at 0015, 0036; Div. Ex. 55 at 0696, 0717; Div. Ex. 56 at 1819, 1826, 1841. The decision to place each property under a conservation easement required the approving vote of the majority of interest holders. Tr. 213, 476-81; Div. Ex. 9 at 0015, 0021-22, 0026; Div. Ex. 55 at 696, 703, 0717; Div. Ex. 56 at 1819, 1840-41.

The offerings were each sold to investors via broker-dealer Strategic Financial Alliance (SFA), and specifically Nancy Zak (Zak), who was a registered representative of SFA between October 2011 and May 2013 and who earned commissions on her sales of membership units. Tr. 96-99, 101, 129, 132-33, 263. Lloyd became acquainted with Zak in 2011, after learning about the tax deduction strategy of investing in land to be placed under a conservation easement. Tr. 211, 557, 724, 836. Throughout their business relationship, Lloyd and Zak always conferred by email or phone; the two never met in person. Tr. 115.

### **C. Forest Conservation 2011 and Forest Conservation 2012 II**

Lloyd created Forest Conservation 2011, LLC (FC11) for the purpose of investing in the Maple Equestrian offering, and made himself the manager of FC11. Tr. 115, 130, 458-59; Div. Ex. 22 at 2250; Div. Ex. 23 at 2103-18; Resp. Ex. 58 at 1052. Lloyd had his clients<sup>5</sup> invest in

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<sup>5</sup> References in this Initial Decision to Lloyd's "clients" without a modifier mean clients of Lloyd's tax practice but not his investment advisory practice. When a distinction between tax

Maple Equestrian through FC11—versus having his clients interact directly with SFA and invest individually in Maple Equestrian—because he wanted to maintain control of his clients’ activities and wanted all SFA communications to go through him. Tr. 125-27; Div. Ex. 7. Lloyd directed Zak to “communicat[e] through him directly.” Tr. 125.

In late 2011, Lloyd collected client funds in FC11, and FC11 in turn invested \$377,480 in the Maple Equestrian offering, giving FC11 a 20 percent ownership stake in Maple Equestrian. Tr. 491; Div. Ex. 5; Div. Ex. 121 at 3 of 50 pages; Div. Ex. 122 at 3 of 10 pages. Lloyd put his own money into FC11, as did ten of his tax clients. Div. Ex. 121 at 1, 3 of 50 pages; Div. Ex. 122 at 3 of 10 pages. Three of those tax clients were also advisory clients: Timothy (“Tim”) Goss, Leslie (“Lee”) Powell, and Larry Price. Tr. 573-74, 710-11; Div. Ex. 123 at 5 of 80 pages.

Lloyd created Forest Conservation 2012 II, LLC (FC12-II) for the purpose of investing in the Meadow Creek offering, and made himself the manager of FC12-II. Div. Ex. 99; Div. Ex. 100 at 23; Div. Ex. 123 at 1-2 of 80 pages; Div. Ex. 179 at 1137-66. In late 2012, Lloyd collected client funds in FC12-II, and FC12-II in turn invested \$164,220 in the Meadow Creek offering. Tr. 478; Div. Ex. 123 at 6, 79 of 80 pages. Six of Lloyd’s tax clients contributed funds to FC12-II; none were also advisory clients. Div. Ex. 123 at 6 of 80 pages. Lloyd did not contribute any of his own funds to FC12-II. *Id.*

1. Fees Charged for Participation in Forest Conservation 2011 and Forest Conservation 2012 II

The clients who put money into FC11 made contributions ranging from \$21,500 to \$67,980. Div. Ex. 122 at 3 of 10 pages. For their participation, Lloyd charged fees ranging from \$4,500 to \$5,000, with most clients being charged \$4,500. Div. Exs. 2, 3, 4, 5; Div. Ex. 122 at 3 of 10 pages. Thus, Lloyd’s fee amounted to 6.21% to 13.42% percent of each client’s contribution. A smaller contribution typically resulted in a fee consuming a larger percentage of the contribution. *See* Div. Ex. 122 at 3 of 10 pages.

Lloyd made his fees clear in writing before his clients put money into FC11. Div. Exs. 2, 3, 4, 5, 156. At the time he was collecting assets in FC11, he described his fee as a “program fee.” Div. Ex. 156. Some of the clients who contributed to FC11 wrote separate checks for funds to be invested in Maple Equestrian and for Lloyd’s fee. Div. Exs. 14, 15, 16, 17.

The clients who put funds in FC12-II made contributions ranging from \$20,000 to \$50,000. Div. Ex. 123 at 76 of 80 pages. For their participation, Lloyd charged fees ranging from \$4,500 to \$7,500. Tr. 582; Div. Ex. 123 at 76 of 80 pages. Thus, Lloyd’s fee amounted to 15 to 22.5 percent of each client’s contribution. As with FC11, a smaller contribution typically resulted in a fee consuming a larger percentage of the contribution. *See* Div. Ex. 123 at 76 of 80 pages. In contrast to FC11, clients did not write separate checks for funds to be invested in

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and investment advisory clients is made, clients are described as “tax clients” or “advisory clients,” as appropriate.

Meadow Creek and the program fee; instead, each client wrote one single check covering the Meadow Creek investment and the program fee. Div. Ex. 123 at 77 of 80 pages.

2. Tax Deductions for Participation in Forest Conservation 2011 and Forest Conservation 2012 II

Following the close of both the Maple Equestrian and Meadow Creek offerings, conservation easements on the underlying land were proposed; the landowners (including, respectively, FC11 and FC12-II) voted in favor of the proposed easements; and the easements were granted and recorded. Tr. 473-74, 501-02; Div. Ex. 108. The grant of these conservation easements caused the Maple Equestrian and Meadow Creek partnerships to issue to FC11 and FC12-II, respectively, Internal Revenue Service (IRS) Schedule K-1s reflecting losses as to the underlying, conserved property, and thereafter Lloyd created K-1s for each investor in the Forest Conservation entities reflecting losses, which were the basis of the deductions his clients took on their annual tax returns. Tr. 493-94, 502-04, 559; Div. Ex. 28; Div. Ex. 121 at 22-50 of 50; Div. Ex. 129.

**D. Forest Conservation 2012**

In late 2012, after collecting funds in FC11 and before collecting funds in FC12-II, Lloyd collected client funds in FC12 for the purpose of investing those funds in Piney Cumberland. Answer at 1; Div. Ex. 123 at 1 of 80 pages. Lloyd was the manager of FC12. Tr. 175, 458; Div. Ex. 81 at 0837; Div. Ex. 189 at 1278. At the time of the FC12 offering, the potential tax deduction if the underlying land were granted a conservation easement—that is, the potential return to investors in the Piney Cumberland offering—was greater than each investor’s investment. Tr. 156, 453; Div. Ex. 56 at 1806.

1. Requirements for Investment in Piney Cumberland

In September 2012, Zak wrote Lloyd to explain SFA’s new requirements for LLCs, such as FC12, to invest in SFA-sponsored private offerings. Div. Ex. 44 at 0001. She explained that SFA required that any LLC participating in the offering had to have an operating agreement and could charge no management fees, and that all members of the participating LLC had to complete SFA client account forms “to be sure they are all accredited.” *Id.* This SFA requirement accorded with the requirement of the Piney Cumberland issuer that each individual—whether investing funds directly in an offering, or pooling assets in an LLC to be invested in the offering—had to submit complete accredited investor paperwork approved by the issuer. Tr. 454, 463-65, 517, 811.

Zak had provided Lloyd with instructions on completing SFA client and accredited investor paperwork the previous December, in connection with FC11. Tr. 117; Div. Ex. 6. The paperwork included a Client Account Form, which “establishe[d]” each participating person as a client of “Nancy Zak, registered representative of the Strategic Financial Alliance.” Div. Ex. 6 at 2158. The Client Account Form contained a field entitled Primary Investment Goal, where participants were required to indicate “Real Estate Investment.” *Id.* at 2160. The Client Account Form also contained a field under Financial Information titled Previous Investment Experience,

with boxes to check, or leave unchecked, next to these options: none; previous investment experience; bonds; stocks; mutual funds; LP; REITS; alt. investments. Div. Ex. 6 at 2163.

The Client Profile section of the Client Account Form contained yes/no boxes next to this question: “Is the client or any member of the client’s immediate family employed by a bank, insurance company, investment advisor, broker/dealer or FINRA?” Div. Ex. 6 at 2162. Zak explained that “[i]f you are a [r]egistered [r]epresentative, you must answer ‘Yes’ to” this question. Div. Ex. 6 at 2158. If a Client Account Form showed that the person or the person’s immediate family member was in the securities industry, SFA required that a “407 letter” be provided for that person before that person would be eligible to participate in the SFA-sponsored private offering. Tr. 106; Div. Ex. 6 at 2159. A 407 letter ensured that the affiliated broker-dealer or investment adviser was aware of the person’s participation in the private offering, and documented that the affiliated entity approved the person’s participation in the offering through SFA. Tr. 107-08. SFA’s affiliation question on the Client Account Form and its rule regarding 407 letters were designed to ensure compliance with selling away regulations. Tr. 105-07; *see, e.g.*, Div. Ex. 193 at 347.

In November 2012, an SFA colleague of Zak’s provided Lloyd with customized paperwork that SFA needed for Piney Cumberland. Div. Ex. 56. One of these forms required each investor in Piney Cumberland to acknowledge that:

I, the undersigned Investor, intend to subscribe in a private offering for Units of membership interest in . . . a limited liability company owning undeveloped real estate . . . . I have been advised, understand and acknowledge that this investment in real estate involves various tax and legal consequences that may be particular to me. I further understand and acknowledge that [SFA], its registered representatives, and their respective employees do not offer or give tax or legal advice and that it is my responsibility to seek out and obtain my own independent tax and/or legal advice regarding an investment in the Company.

Div. Ex. 56 at 2035.

## 2. Assembly of Funds in Forest Conservation 2012

Between October 1, 2012, and December 7, 2012, Lloyd deposited funds into FC12’s account from seventeen clients, totaling \$632,500. Div. Ex. 123 at 67-74 of 80 pages. These seventeen contributors included Christopher (“Chris”) Brown, James (“Rusty”) Carson, and Michael (“Mike”) Malloy, none of whom were Lloyd’s advisory clients at the time. Tr. 793; Div. Ex. 123 at 5 of 80 pages. Brown’s \$50,000 check made out to FC12 was deposited in FC12’s account on October 1, 2012<sup>6</sup>; Carson’s \$30,000 check on December 4, 2012; and Malloy’s \$50,000 check on November 14, 2012. Div. Ex. 123 at 67-70, 72-73 of 80 pages.

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<sup>6</sup> Brown’s check was dated August 30, 2012, because Lloyd was having conversations with Brown regarding FC12 in the summer of 2012. Tr. 976; Resp. Ex. 17 at 9510.

The seventeen contributors also included five of Lloyd's advisory clients: Vernon ("Ray") Branch, who contributed \$40,000; Tim Goss, who contributed \$35,000; Ashley Hooks (Hooks), who contributed \$35,000; Lee Powell, who contributed \$60,000; and Larry Price, who contributed \$40,000. Tr. 710-11, 828, 1057, 1076-77, 1084; Div. Ex. 123 at 5, 67-70 of 80 pages.

On December 7, 2012, Lloyd deposited \$16,802 of his own funds in FC12, making him the final person to commit funds. Div. Ex. 123 at 72-73 of 80 pages. A total of \$649,302 was thus ultimately put in FC12, by a total of eighteen individuals.

FC12 invested \$543,552 in Piney Cumberland, giving FC12 a 23.76 percent ownership interest in the offering. Tr. 184, 474; Div. Ex. 81; Div. Ex. 123 at 5, 72-73, 75 of 80 pages. The transfer from FC12's bank account to the bank account of the escrow agent for the Piney Cumberland offering was made on December 7, 2012, the same day as Lloyd's deposit into the FC12 account. Tr. 456; Div. Ex. 123 at 72-73, 75 of 80 pages.

### 3. Completion of SFA Paperwork and Piney Cumberland Closing

On December 3, 2012, Lloyd sent Zak completed client and accredited investor paperwork, filled out by both himself and some of his clients. Div. Ex. 75. The Client Account Form he completed for himself indicated that he did *not* work in the securities industry and was *not* affiliated with a broker-dealer or investment adviser. Tr. 158-61, 786; Div. Ex. 75 at 0688. Specifically, "No" was selected next to "Are you or your spouse, or any other immediate family members, including parents, in-laws, siblings and dependents, employed by or associated with the securities industry or a financial services regulator?" Tr. 159-60; Div. Ex. 75 at 688. Nor did Lloyd's Client Account Form reveal his investment experience as a financial advisor and participant in the securities industry. Div. Ex. 75 at 0689 (leaving bonds, stocks, and mutual funds unchecked in the Previous Investment Experience section). Lloyd had also, in 2011, filled out a separate Client Account Form that failed to reveal his securities industry experience and affiliation with an investment adviser. Div. Ex. 174 at 0419-20. Although these entries on his Client Account Form were false—or, as Lloyd put it, "not correct"—Lloyd denied that he intended to conceal information from LPL. Tr. 748, 786-89. When asked why he answered the Client Account Form the way he did, all he could say was: "I do not recall. I have no idea. There's no reason for it." Tr. 786.

Also on December 3, 2012, Lloyd sent Zak for the first time FC12's Operating Agreement, showing that FC12 was structured as an LLC under Wyoming law. Div. Ex. 75 at 0694-721. The Operating Agreement did not include a list of the members of FC12. *Id.* It also stated that the FC12 membership interests were not registered as securities "in reliance upon exemptions" to the registration provisions of the Securities Act, among other laws, and that "sale or disposition of the membership interest is restricted." Tr. 789-90; Div. Ex. 75 at 0694, 0714, 0719. Later that same day, Zak emailed Lloyd, reiterating that each of his clients participating in Piney Cumberland through FC12 would need to complete SFA paperwork. Tr. 162-63; Div. Ex. 76 at 0015.

On December 5, 2012, Lloyd sent Zak more completed SFA paperwork. Div. Ex. 79. Among these papers was the completed Client Account Form for Lloyd's tax client Rusty Carson, which Carson himself had completed and signed on December 3, 2012. Tr. 167, 800-01; Div. Ex. 79 at 0738. The Client Account Form disclosed that Carson worked in the securities industry and was affiliated with broker-dealer Merrill Lynch. Tr. 166; Div. Ex. 79 at 0738.

On December 6, 2012, Lloyd conveyed to Zak that FC12 would invest \$543,552 in Piney Cumberland. Div. Ex. 81 at 0837. On December 7, 2012, Zak asked Lloyd to obtain a 407 letter for Carson, and attached a sample 407 letter to her email. Tr. 167; Div. Ex. 193. Lloyd never spoke to Carson about Zak's request or the need for a 407 letter. Tr. 813-14, 913-14. Instead, on December 7, 2012, Lloyd answered Zak's email by stating simply that Carson was now "OUT." Tr. 179; Div. Ex. 84 at 879-80. Zak responded the same day requesting confirmation: "Carson is not participating, correct?" Div. Ex. 84 at 878. Lloyd responded: "Correct." *Id.*

Also on December 7, 2012, Lloyd sent Zak FC12's Operating Agreement again. Div. Ex. 86. This time a Schedule I to the Operating Agreement was included, which showed Lloyd as the only member of FC12, controlling a 100 percent membership interest. *Id.* at 934. Later that day, Lloyd emailed Zak confirming that the wire transfer from FC12 to the escrow agent was complete. Tr. 182; Div. Ex. 87.

On December 10, 2012, Lloyd emailed Zak a "schedule" of fifteen members of FC12, including himself, and their corresponding contribution amounts. Div. Ex. 88. Brown, Carson, and Malloy—all of whom had deposited a total of \$130,000 in FC12—were not on this list. Div. Exs. 88, 123 at 67-72 of 80 pages. Lloyd listed the amount of each client's check as that client's contribution or "contribution received," without deduction of any fees. Div. Ex. 88 at 0940, 0942. Lloyd also stated that his personal investment in FC12 was \$41,052—\$24,250 more than the mere \$16,802 he had deposited in FC12 a few days earlier. Div. Ex. 88 at 940.

Later on December 10, 2012, Zak forwarded to Lloyd comments from Peter Hardin (Hardin), the attorney representing the issuer of the Piney Cumberland offering. Tr. 185, 250-51, 485; Div. Ex. 89. Hardin had received the FC12 Operating Agreement with the Schedule I reflecting Lloyd as the only member. Div. Ex. 86 at 934; Div. Ex. 89 at 377. Hardin wrote:

I do not understand. The Operating Agreement show[s] that there is only one member, Ed Lloyd, who owns 100% of the entity. I need to see the current Operating Agreement that shows all current members. Are you [Zak] saying that all of the persons listed on the "investor list" that was attached are all new members of Forest Conversation 2012? If so, they need to amend their Operating Agreement to reflect that new ownership on Schedule I and resend to us. I would also like to see a certificate of the Manager stating that the Operating Agreement as attached is true and correct as of the date hereof. If something else was meant, please explain.

Div. Ex. 89 at 377. Hardin explained "[t]here was a disconnect between the proposed investor list for [FC12] and the individuals who were represented to . . . be members of the entity pursuant to the operating agreement," which "showed only one member." Tr. 461.

In response to Hardin’s concerns, Lloyd sent Zak the Operating Agreement with a revised Schedule I in the evening of December 10, 2012. Div. Ex. 90 at 956. The revised Schedule I listed fifteen members of FC12—the same fifteen people, not including Carson, Brown, or Malloy, that Lloyd had provided to Zak earlier that same day. Div. Ex. 90; *see also* Div. Ex. 88. The revised Schedule I listed each member’s ownership stake in FC12 as follows (Div. Exs. 90, 187):

	<u>Name</u>	<u>Ownership Stake</u>
1	Gary Appel	5.52%
2	Raymond Bouley	5.98%
3	Ray Branch	7.36%
4	Jarrett Clay	8.28%
5	Jesse Garrett	5.52%
6	Tim Goss	6.44%
7	Dennis Hall	5.06%
8	Ashley Hooks	6.44%
9	Steve Kezman	4.14%
10	Michael Knight	5.52%
11	Paul Edward Lloyd, Jr.	7.55%
12	Mark Losby	7.36%
13	William Mitchell	6.44%
14	Lee Powell	11.04%
15	Larry Price	7.36%

Upon his receipt of the updated Schedule I, Hardin was satisfied with FC12’s documentation for investment in Piney Cumberland, and was ready to approve FC12 and its (represented) fifteen members as investors, upon receipt of a signed Manager’s Certificate from Lloyd. Tr. 464, 468; Div. Ex. 189. FC12 was the final investor in Piney Cumberland, meaning that the issuer was waiting on information from FC12 to close the offering. Tr. 464, 472. Hardin testified that if the issuer had discovered an omission or inaccuracy in Schedule I, it would not have allowed FC12 to invest in Piney Cumberland. Tr. 469.

On December 11, 2012, Lloyd sent an executed Manager’s Certificate to SFA, attaching a “true, complete and correct copy of the [FC12] Operating Agreement,” which included the revised Schedule I provided the prior day. Div. Ex. 191 at 1019, 1047. This Manager’s Certificate was then forwarded to Hardin. Tr. 467. Accordingly, on December 11, 2012, FC12 became a member of the Piney Cumberland offering, with 228 membership units, or 23.76 percent of the offering. Div. Ex. 192. At no time following the closing of the Piney Cumberland offering did Lloyd inform SFA or Hardin that Schedule I to the FC12 Operating Agreement, as provided on December 10 and 11, 2012, was inaccurate, or that Carson, Brown, and Malloy should have been included on Schedule I. Tr. 194-95, 484; *see* Div. Exs. 90, 91, 191.

Following the close of the Piney Cumberland offering, a conservation easement on the land was proposed. Tr. 473; Div. Ex. 94. Consistent with the terms of the Private Offering

Summary, on December 13, 2012, Lloyd voted in favor of the conservation proposal on behalf of FC12. Tr. 480; Div. Ex. 93. In the end, the majority of ownership units voted in favor of the conservation approach, and an easement was granted and recorded on the property. Tr. 476-82; Div. Ex. 56 at 1819; Div. Ex. 92. After the easement was granted, Piney Cumberland's issuer issued a K-1 to FC12, listing the tax deduction to which FC12 was entitled: approximately \$2.2 million. Tr. 482-83; Div. Ex. 129 at 0005-06.

#### 4. Fees Charged for Participation in Forest Conservation 2012

In November and December 2012, Lloyd withdrew funds totaling \$105,750 from FC12 and directed those funds to other personal and business accounts he controlled. Div. Exs. 67, 102, 109, 110, 187. Specifically, Lloyd's withdrawals were \$2,000 to Corporate Solutions Inc., on November 28, 2012, \$22,750 to Benefit Administrative Services LLC on December 20, 2012, \$22,000 to Benefit Administrative Services on December 30, 2012, and \$59,000 to Ed Lloyd and Associates LLC on December 31, 2012. Div. Exs. 67, 102, 109, 110, 187. Lloyd maintains that these funds were his "tax service fees," and this Initial Decision refers to them as fees. *E.g.*, Div. Ex. 123 at 67 of 80 pages.

Although Brown, Carson, and Malloy were not initially identified as members of FC12 and investors in the Piney Cumberland offering, Lloyd apportioned to each of them, as well as his other fourteen participating clients, fees in connection with FC12. Div. Ex. 123 at 67, 69, 72 of 80 pages; Div. Ex. 187. The fees ranged from \$4,750 to \$8,500 per client. Div. Ex. 123 at 67, 69, 72 of 80 pages; Div. Ex. 187. Thus, Lloyd's fee amounted to 14.17 to 21.11 percent of each client's payment to Lloyd. *See* Div. Exs. 123, 187.

As with FC12-II, a smaller contribution resulted in a fee comprising a larger percentage of the contribution. For instance, Steve Kezman's \$4,750 fee constituted 21.11 percent of his total contribution of \$22,500. *See* Div. Exs. 123, 187. However, unlike with FC11, fees charged in connection with FC12 were not separately assessed from funds destined for investment in the Reg D offering; instead, each client made one single deposit in FC12. Div. Ex. 123 at 67-70 of 80 pages. There is no evidence that Lloyd ever sent a client an invoice, receipt, or other writing documenting any FC12 fees. *See* Div. Exs. 2, 3, 4.

#### 5. Tax Deductions for Participation in Forest Conservation 2012

After Lloyd received FC12's K-1, he prepared K-1s for FC12's members. Tr. 559; Div. Ex. 128 at 0012-29. Lloyd issued the K-1s around May 2013, although the precise date is uncertain; the Division maintains that the K-1s were created in "May 2013," a fact Lloyd has not disputed, and the K-1s clearly had not been created as of March 14, 2013, one week after Lloyd resigned from LPL. *See* Div. Br. 5, 15; Div. Ex. 123 ("K-1 forms have not been yet been completed for Forest 2012."); BrokerCheck Report at 7. He prepared a total of eighteen such K-1s, including for Brown, Carson, Malloy, and himself. Div. Ex. 128 at 0012-29; *see supra* §

II(D)(3). The K-1s assumed that each contributor to FC12 held the following ownership interests in FC12's profits<sup>7</sup>:

<u>Name</u>	<u>Profits Stake</u>
Gary Appel	4.51%
Raymond Bouley	4.92%
Ray Branch	6.16%
Chris Brown	7.82%
Rusty Carson	4.51%
Jarrett Clay	6.99%
Jesse Garrett	4.51%
Tim Goss	5.34%
Dennis Hall	4.09%
Ashley Hooks	5.33%
Steve Kezman	3.27%
Michael Knight	4.51%
Paul Edward Lloyd, Jr.	3.09%
Mark Losby	6.16%
Michael Malloy	7.82%
William Mitchell	5.34%
Lee Powell	9.47%
Larry Price	6.16%

Div. Ex. 187 (citing Div. Ex. 128 at 0012-29). These interests were inconsistent with the interests Lloyd listed on the revised Schedule I to the Operating Agreement shared with SFA and the issuer on December 10 and 11, 2012. *See supra* § II(D)(3). Indeed, most clients had their interests diluted relative to what Lloyd had represented earlier; Brown, Carson, and Malloy, however, saw their interests increased from naught:

<u>Name</u>	<u>Ownership Stake Based on Dec. 2012 Schedule I</u>	<u>Profits Stake Based on May 2013 K1s</u>	<u>Comparison Dec. 2012 vs. May 2013</u>
Gary Appel	5.52%	4.51%	-1.01%
Raymond Bouley	5.98%	4.92%	-1.06%
Ray Branch	7.36%	6.16%	-1.20%
Chris Brown	0.00%	7.82%	7.82%
Rusty Carson	0.00%	4.51%	4.51%

<sup>7</sup> The K-1s assumed pro rata shares in FC12's losses and capital as to each FC12 participant except for Garrett, with a 5.34% interest in loss/capital, and Goss, with a 4.51% interest in loss/capital. Div. Ex. 128 at 0012-29.

Jarrett Clay	8.28%	6.99%	-1.29%
Jesse Garrett	5.52%	4.51%	-1.01%
Tim Goss	6.44%	5.34%	-1.11%
Dennis Hall	5.06%	4.09%	-0.97%
Ashley Hooks	6.44%	5.33%	-1.11%
Steve Kezman	4.14%	3.27%	-0.88%
Michael Knight	5.52%	4.51%	-1.01%
Paul Edward Lloyd, Jr.	7.55%	3.09%	-4.46%
Mark Losby	7.36%	6.16%	-1.20%
Michael Malloy	0.00%	7.82%	7.82%
William Mitchell	6.44%	5.34%	-1.11%
Lee Powell	11.04%	9.47%	-1.57%
Larry Price	7.36%	6.16%	-1.20%

See Div. Ex. 187.

Following the seventeen clients' receipt of K-1s, each client took a federal tax deduction as each anticipated. Tr. 936, 965, 1060, 1108, 1172; *see generally* Resp. Ex. 39. Lloyd's clients who testified at the hearing were Jennifer Parker Brown (wife of Chris Brown), Branch, Goss, Hall, Hooks, Losby, Price, and Powell. Tr. *passim*. Thus, eight of Lloyd's seventeen clients who put funds in FC12 testified. Affidavits prepared by Lloyd's counsel and signed by Goss and Hooks were also admitted into evidence. Tr. 1068-70, 1078; Resp. Ex. 39. Testifying clients generally reported being satisfied with Lloyd's services in connection with FC12. Tr. 622-26, 628, 965, 1060-61, 1110, 1135, 1174; *see also* Resp. Ex. 39 ("I am very satisfied with Ed Lloyd's tax planning and tax preparations services.").

#### 6. Lloyd's Testimony Regarding Forest Conservation 2012

Lloyd testified during the Division's investigation on February 6, 2014, and again on June 12, 2014. Div. Exs. 144, 147. Both investigative transcripts were admitted in evidence, although the latter generally pertains to matters not material to this proceeding.

In Lloyd's investigative testimony, when he was asked whether his clients knew the fees he charged before they invested in FC12, Lloyd stated, "[y]es, I communicated that to them" by telephone. Div. Ex. 144 at 69, 71. When he was asked whether he intentionally left Brown, Carson, and Malloy off Schedule I to the FC12 Operating Agreement that he sent Zak on December 10, 2012, he stated "[n]ot to my recollection. It looks like I've got an error." *Id.* at 111; *see* Div. Ex. 88. When asked why his own contribution to FC12 was listed as \$41,052, \$24,250 more than the \$16,802 he actually deposited in FC12's account, Lloyd stated, "I'm not sure." Div. Ex. 144 at 114-15. When asked why each client's "contribution received" was the total of the client's contribution and tax service fee, rather than just the client's contribution, Lloyd stated, "I don't know." *Id.* at 116; *see* Div. Ex. 88 at 0940, 0942. When asked to explain

how in one set of documents Lloyd had documented total deposits from eighteen investors of \$649,302, and in another set of documents Lloyd had documented total contributions from fifteen investors of \$543,552, a difference of \$105,750—exactly what Lloyd asserted was his aggregate tax service fee—he stated, “I guess it was an error.” Div. Ex. 144 at 117-19, 139-40.

When asked for his “theory” of why he listed his own contribution as \$41,052 in one document and \$16,802 in another, Lloyd stated, rather non-responsively, “I do not recall at this time.” Div. Ex. 144 at 120-21; *see also* Tr. 728; Div. Ex. 144 at 125. When the Division pointed out that an SFA account form Lloyd filled out, dated December 3, 2012, listed his contribution as \$41,052, and then asked if he was “anticipating to purchase \$41,052 at this time on December the 3rd, 2012,” Lloyd stated, “[b]ased upon this, I would assume so.” Div. Ex. 144 at 147-48. When asked again whether “the fee for each individual was discussed up front before a check was written,” Lloyd was notably evasive, and ultimately stated both “[y]es” and “[t]o the best of my recollection, I followed this practice in everything that I do.” *Id.* at 122-23. The Division showed Lloyd the paperwork for Appel, and asked, “when Mr. Appel here indicates that he’s purchasing \$30,000, does that not represent that he’s saying he’s anticipating purchasing \$30,000 in the easement as opposed to \$24,500?” *Id.* at 158. Lloyd replied, “I don’t know.” *Id.*

The Division eventually asked, “[d]id you intentionally fail to notify Piney Cumberland or Nancy Zak that Chris Brown, James Carson and Mike Malloy were providing money and were going to invest in this?” Div. Ex. 144 at 150. Lloyd first responded, “I don’t recall,” and then stated,

I’m saying I don’t know exactly what happened with—you’re asking about these documents, so I have to be very careful what I’m saying because there are a ton of documents floating around, being submitted by different people in different ways, and I have to be very careful to answer your question in a way that is correct. And we’re also talking about stuff that happened in 2012 and I can’t recall everything that happened in 2012 during a time when I’m working an enormous amount of hours. So I’m just being very clear as far as what I can say that I do and do not recall.

*Id.* at 150-51.

During the hearing, Lloyd’s memory remained poor as to certain issues. He admitted that his answer to the question on his Client Account Form regarding his association with the securities industry was “not correct,” although when asked why he answered it incorrectly, he stated, “I do not recall. I have no idea. There’s no reason for it.” Tr. 785-86. Similarly, when asked to explain why he failed to indicate his previous investment experience on his Client Account Form, he stated, “I have no idea. I don’t know if I was thinking in the context of what—I don’t know.” Tr. 788.

On some issues, however, Lloyd demonstrated a markedly improved memory, because he “spent a tremendous amount of time trying to recreate what happened and jog [his] memory.” Tr. 920. He agreed that he normally issued written invoices to his clients, but that he did not disclose his fees for FC12 to his clients in writing. Tr. 767-68, 1051. When asked if the

“amount of money that was put on the form as the amount of purchase was the amount of money that was being contributed towards the respective offering by the prospective investor,” he stated, “I believe you’re correct, yes.” Tr. 778.

Lloyd also remembered why he omitted Carson from the list of participants he forwarded to Zak and Hardin. Lloyd agreed that in Carson’s Client Account Form, which Lloyd sent to Zak on December 5, 2012, Carson himself had indicated that he was associated with Merrill Lynch. Tr. 800-01. Lloyd further agreed that for Carson to participate in FC12’s purchase of Piney Cumberland units, a 407 letter would have to be submitted to Carson’s “broker-dealer,” and then transmitted to SFA so that SFA could approve Carson. Tr. 803-05. Lloyd understood that if he could not obtain Carson’s 407 letter in time for the Piney Cumberland closing, FC12 would not be able to participate in it. Tr. 808-09, 812-13. Lloyd believed that he could not obtain Carson’s 407 letter in time, and never explained to Carson that a 407 letter was needed. Tr. 808-10, 812. Lloyd again explained that he was very busy at the time—“physically and mentally exhausted.” Tr. 810.

Lloyd then explained his own state of mind at the time:

Q And you led Mr. Carson to believe that he was still a member of Forest Conservation 2012 with respect to the Piney Cumberland Holdings offering. Right?

A He was still a member of 2012.

Q So you considered him to be a member even though you purposefully did not provide SFA with the paperwork it needed in order for it to deem him as an accredited investor. Right?

A He wrote the check. I mean, I was—I guess from a—he wrote the check, therefore he was in, but I was taking him out.

Q So did you say to Ms. Zak, James Rusty Carson is a member of Forest Conservation 2012, but I don’t want to share the paperwork with him because I think it would be too difficult to get?

A No. I made the decision that I was going to take him out. And again that’s the decision that I made.

Q So you made a decision to take him out even though you’re saying he was still actually in because he gave you a check. Right?

A I think he was in because he gave me a check and I think he was out because I was going to take him out.

Q Okay. So he’s out in your mind, but you’re still—you think he’s an investor and he’s in. Correct?

A I don't agree with that.

Q Well, you just said that he was out, you took him out, you withdrew him from something. What did you take him out from?

A I was going to take him out of his position and write him a check and pay him out.

Q Well, he was certainly out of Forest Conservation 2012. He was certainly not someone who could be in an investor in Forest Conservation 2012 because he did not provide the requisite paperwork to SFA. Correct?

A I guess so.

Q When you said the word "out" to Ms. Zak, what did you mean by the word "out" to Ms. Zak? You meant that he wasn't going to participate in the offering. Correct?

A Yes. That was my intention, that he was not going to participate.

Q So you never shared with Mr. Carson your determination that he was going to be out of the offering. Right?

A Correct.

Q And you kept his money. Right?

A Correct.

Q And even so much so that you ultimately, when all is said and done and when you received a K-1 for the membership units that were held by Forest Conservation 2012, you issued him a K-1 indicating that he in fact was an investor in the Forest Conservation 2012 offering?

A Correct, because his money was in there.

JUDGE ELLIOT: I have—I have got to say I am completely baffled. I have no idea what's going on here. What do you mean? I thought you said he wasn't in. He gave you the money. You didn't give it back.

THE WITNESS: I didn't give it back. My intention was to give it back to him, sir. I did not do that. He gave me the money and therefore he was entitled to the K-1 for the charitable contribution and I gave that to him.

JUDGE ELLIOT: No, he wasn't. Why didn't you just give him his money back instead of the K-1?

THE WITNESS: Because I had gone through and I explained to him what the tax benefits were. I promised these things to him and I didn't feel that it was right.

Tr. 813-16; *see also* Tr. 868, 885, 912-22.

Lloyd's memory of his own contribution to FC12 also improved. Lloyd deposited his own contribution of \$16,802 into FC12's account on December 7, 2012, three days after he deposited Carson's \$30,000 check, and the same day he wired FC12's funds. Tr. 1054; Div. Ex. 123 at 72-73 of 80 pages. On December 10, 2012, Lloyd told Zak that his contribution had increased to \$41,052, an amount Lloyd "always wanted." Tr. 1054; Div. Ex. 88. Ultimately, Lloyd issued a K-1 to himself corresponding to a contribution of only \$16,802. Div. Ex. 128 at 0024; Div. Ex. 187. I asked Lloyd at least four times when he made the decision to reduce his contribution back to \$16,802, and he testified, at least four times, that he made the decision either when he received Carson's check (i.e., December 3 or 4, 2012) or when he wired FC12's funds (i.e., December 7, 2012). Tr. 1052-55. Thus, notwithstanding that Lloyd actually desired an increased contribution, Lloyd's December 10, 2012, email to Zak, telling her that his own contribution to FC12 had increased, was knowingly false when he sent it.

#### **E. LPL Examination**

LPL had last examined Lloyd's practice in 2012. Tr. 279. On February 7, 2013, LPL sent Dethlefsen to conduct a regular, unannounced examination of Lloyd's investment advisory practice. Tr. 274, 277-78, 292; Div. Ex. 120. Lloyd acted unusually agitated by Dethlefsen's arrival, and expressed annoyance because she arrived during tax season. Tr. 295-96, 343. Lloyd, however, did not interfere with Dethlefsen's workflow and did not prevent her from pulling advisory client files for inspection. Tr. 343.

During the exam, Dethlefsen discovered two instances of cut and paste signatures in Lloyd's advisory client files, in violation of LPL's policies. Tr. 298-99, 324; *see supra* § II(A)(2). This discovery caused Dethlefsen to broaden her exam. Tr. 304-05. Despite the broadened exam, she was not aware, and was not made aware, of the existence of FC11, FC12, and FC12-II. Tr. 311, 313, 315. When she inspected Lloyd's desk area by opening and looking in drawers, Lloyd told her that certain files related to his tax clients were confidential, and that LPL had no reason to look at them. Tr. 328.

The participation in SFA-brokered private offerings by his clients and himself, and Lloyd's failure to inform LPL of them, were inconsistent with LPL's compliance policies relating to selling away, outside business activities, and providing tax advice. Tr. 307-23; Div. Ex. 155 at 7949-92; *see supra* § II(A)(2).

#### **F. OCIE Examination**

In March 2013, staff in the Commission's Office of Compliance Inspections and Examinations (OCIE) conducted an examination of Lloyd's LPL branch office, with a focus on

the Forest Conservation entities. Tr. 553, 610; *see* Div. Ex. 123. OCIE’s exam of Lloyd was apparently spurred by an earlier exam of SFA by which it was looking at documents relating to the Maple Equestrian offering. Tr. 549-52. FC11 drew the attention of OCIE because “it’s unusual to have an investor who is also pooling funds from other investors into another investment[;] [i]t’s just unusual to see.” Tr. 550.

When OCIE examiners visited Lloyd on March 6, 2013, Lloyd told the examiners that he had no LPL advisory clients who deposited funds in FC11. Tr. 555-56. He also “indicated he did not receive compensation for the investment in Maple Equestrian,” mentioning a “flat tax planning fee” instead. Tr. 558; *see also* Div. Ex. 121 at 4 of 50 pages (“fee for the broader tax planning”). The examiners asked him whether he disclosed his involvement with the Forest Conservation entities to LPL, and Lloyd answered that he had not. Tr. 561.

On March 7, 2013, Lloyd resigned as a registered representative of LPL. Tr. 892, 895; BrokerCheck Report at 4, 7.

On March 6, 2013, OCIE requested documents relating to the Forest Conservation entities. Div. Ex. 123 at 1 of 80 pages. On March 12, 2013, Lloyd, through counsel, produced to OCIE paperwork relating to FC11. Div. Ex. 121. That production revealed that Lloyd’s representation that no LPL advisory clients had deposited funds in FC11 was false. Tr. 564-65, 567-68; Div. Ex. 121 at 1, 3 of 50 pages. Another production on March 13 2013, revealed Lloyd’s fees associated with FC11. Div. Ex. 122 at 3 of 10 pages.

On March 14, 2013, Lloyd made another production through counsel, providing a list of FC12 contributors—eighteen, not the fifteen revealed to SFA—as well as a copy of FC12’s Operating Agreements (dated March 16 and December 19, 2012). Tr. 573; Div. Ex. 123 at 1-2, 5, 9-65 of 80 pages. The March 16, 2012, Operating Agreement he provided included the original Schedule I Hardin rejected, that listed Lloyd with a 100 percent interest. Tr. 575; Div. Ex. 123 at 36 of 80 pages. Lloyd did not provide OCIE with the revised Schedule I, listing fifteen members, that he had provided to SFA and the Piney Cumberland issuer on both December 10 and 11, 2012. *See* Div. Ex. 88 at 0942. Lloyd’s production also listed his fee (“tax service fee”) and the “Conservation Contribution” as to each client. Div. Ex. 123 at 67, 69, 72 of 80 pages. This appears to have been the first written record of Lloyd’s fees for FC12. Tr. 611. Also, each client’s listed contribution was different from the contribution listed in the revised Schedule I supplied to Zak and the Piney Cumberland issuer. *See* Div. 88 at 0942.

In the course of the OCIE examination, Lloyd disclosed four advisory clients who participated in FC12, but never indicated that Hooks was an advisory client. *See* Div. Ex. 123 at 5 of 80 pages. As a result, the OIP alleges that only four of Lloyd’s advisory clients invested in FC12. OIP at 7. In fact, the hearing record shows that five advisory clients invested in FC12; Hooks testified that she was also Lloyd’s advisory client, starting in 2011 or 2012 and continuing until Lloyd’s resignation from LPL. Tr. 1057, 1076-77. Specifically, Hooks had an LPL IRA through Lloyd. Tr. 1076. Lloyd apparently denies that Hooks was an advisory client. *See* Resp. Br. at 14.

### **G. Lloyd's Wells Submission**

On July 18, 2014, Lloyd through counsel sent the Division a Wells submission. Div. Ex. 149. In the submission, Lloyd averred that his failure to include Brown, Carson, and Malloy in the revised Schedule I provided to SFA “was simply a clerical error,” explaining that the bank records produced to OCIE showed the true deposits in FC12. *Id.* at 9; *see also id.* at 10, 12.

In contrast to Lloyd's hearing testimony, his Wells submission said nothing about choosing to take Carson “out” of FC12, failing to inform Carson of this choice, declining to return Carson's deposit, and then putting Carson back “in” FC12 without informing Zak or Hardin. Tr. 807-16, 868-70, 873-84, 912-20. Nor did it say that he decided that his own contribution would be \$16,802, and then informed Zak a few days thereafter that it was \$41,052. Tr. 1052-55.

The Wells submission also explained that Lloyd prepared K-1s for the eighteen persons who deposited funds in FC12, the K-1s showed the “correct” interests of those eighteen in the conservation easement deduction, and the K-1s allowed them to receive their “intended tax benefit” to which “they were entitled.” Div. Ex. 149 at 3, 10, 13. However, the K-1s were prepared only after OCIE had examined Lloyd.

Before making his Wells submission, Lloyd amended the FC12 Operating Agreement, which required obtaining his seventeen clients' signatures. Tr. 626, 942-43, 966-69, 1090, 1124-26; Resp. Ex. 16; *see* Resp. Br. at 13 (amendment occurred “[i]n the summer of 2014”). The amendment included these statements:

Whereas, in preparing the revision of *December 7, 2012*, Paul Edward Lloyd, Jr., caused to be attached schedules of interests and percentages that, *through a scrivener's error*, omitted the names of three members and *misstated percentages as of that date*; and

...

Whereas, the members of Forest Conservation 2012 LLC wish to ratify and confirm the Operating Agreement, *and to correct the scrivener's error by replacing the erroneous schedules of December 7, 2012* with the schedules attached as Exhibit “B” (as of December 7, 2012) and Exhibit “C” (at all times after payment of the fee).

Resp. Ex. 16 at 2 (emphasis added). In fact, the December 7, 2012, Schedule I showed Lloyd as the only FC12 participant. Div. Ex. 86 at 0934.

### **H. Hearing Testimony of Lloyd's Clients**

#### **1. Ray Branch**

Branch, a technology-company owner from Raleigh, NC, has been a tax client of Lloyd for about six years. Tr. 1084, 1093-94. He also receives investment advice from Lloyd through Ed Lloyd Wealth Management. Tr. 1085-86.

Branch received a document subpoena from the Commission about FC12. Tr. 1096-97. Branch spoke to Lloyd about the subpoena, and Lloyd directed Branch to speak to Lloyd's attorneys about the investigation. Tr. 1097-99. Branch and Lloyd's attorneys discussed the fees Lloyd charged, among other things. Tr. 1102. Branch acknowledged that, while Lloyd sent Branch invoices for tax planning services over the years, Branch was never sent an invoice in connection with FC12. Tr. 1100.

## 2. Jennifer Parker Brown

Jennifer Parker Brown (J. Brown) is the wife of Chris Brown. Tr. 961, 969, 972. The Browns, from Durham, NC, were referred to Lloyd by Malloy, and have been Lloyd's tax clients for about four years. Tr. 960-61. Lloyd interacted exclusively with J. Brown on behalf of both Browns. Tr. 972. J. Brown testified that she and her husband have participated in conservation easement programs with Lloyd "every year" since 2012. Tr. 966.

J. Brown testified that she and her husband contributed funds to FC12 after a general discussion with Lloyd about the size of the tax deduction a \$50,000 contribution to FC12 would yield. Tr. 992. At the time, she had a "pretty simplistic" understanding of how a tax deduction would be secured. Tr. 962. She said she knew there would be a fee, but does not remember discussing the size of the fee. Tr. 965, 989-91. At the hearing, she did not remember what fee Lloyd charged for FC12. Tr. 989.

## 3. Tim Goss

Goss, from Waxhaw, NC, is in the restaurant franchise business and has been a client of Lloyd's for about eight years. Tr. 1127-28, 1135-36. Goss was an advisory client of Lloyd's in the past, but is not currently. Tr. 1128, 1137, 1153.

Goss testified that the fees charged by Lloyd did not matter much to him:

Well, I really didn't have a discussion with him about the [FC12] fees. The fees are what the fees are. . . . I've had enough trouble with accountants in North Carolina to last me a lifetime. . . . [J]ust to be honest with you, that's really never been an issue for me. I am more worried about the quality of the work and [getting] it right.

Tr. 1140-41. However, he knew there would be a fee before contributing funds. Tr. 1156-57, 1164. Also, when he prepared an affidavit supporting Lloyd, as requested by Lloyd's counsel, he did not remember what fees he had been charged in connection with FC11 and FC12. Tr. 1160-63; Resp. Ex. 39 at 17-18 of 62 pages.

When Goss learned that Commission staff were investigating Lloyd, he was concerned how it might affect him personally. Tr. 1145. His “biggest concerns” were whether he would be audited by the IRS and whether what Lloyd did with the Forest Conservation entities was “legit.” Tr. 1145. When Goss first received a document subpoena from Commission staff, he discussed it with Lloyd. Tr. 1139, 1142-43.

#### 4. Dennis Hall

Hall, an architect from Charlotte, NC, has been a tax client of Lloyd’s for about six years. Tr. 1168-69, 1182. Hall viewed his participation in FC11 and FC12 as charitable; as “an Old Boy Scout [he’s] always interested in the conservation of forestland.” Tr. 1170.

Hall could not recall what fee Lloyd charged him for his participation in FC11 and FC12. When asked whether Lloyd discussed “his fee” with Hall before Hall wrote a check to FC12, Hall said Lloyd “probably did. I—I—I would certainly think he did. I don’t have a memory of that right now.” Tr. 1173. His understanding at the hearing was that the single check he wrote to FC12 included a fee to Lloyd, but he did not know whether he knew that fact in 2012. Tr. 1173-74.

When Lloyd sent Hall the amended FC12 Operating Agreement in the summer of 2014, Lloyd “seemed to be in a little bit of a hurry to get a signature on it.” Tr. 1175. Hall “wasn’t concerned with the words in it,” and discussed the document with Lloyd only after he had already signed and returned it to Lloyd. Tr. 1175-76. Hall accepts Lloyd’s explanation that there were clerical errors in the FC12 Operating Agreement, but acknowledges that he might not have a full understanding of what ensued with FC12. Tr. 1181-82.

Hall has participated in other conservation easement programs with Lloyd since he participated in FC11 and FC12. Tr. 1174. Hall has been happy with Lloyd’s tax-related services and has recommended Lloyd to others. Tr. 1174.

#### 5. Ashley Hooks

Hooks, from Marietta, GA, has been a tax client of Lloyd’s for about four years. Tr. 1056-57, 1061-62. As noted, Hooks was also Lloyd’s advisory client. Tr. 1057, 1076-77.

Hooks testified that she knew, before contributing to FC12, that she would be charged a fee for participation in FC12, but did not know at that time how much that fee would be. Tr. 1059-60, 1066, 1072-74. She acknowledged that Lloyd’s fee for her participation in FC12 was higher than his typical “accounting” services fees. Tr. 1074-75. She believed that she learned what the fee would be in an email between her and Lloyd. Tr. 1063-66, 1072-74. However, no such email was ever produced by Lloyd or Hooks to the Division, or offered in evidence, and Hooks generally does not converse with Lloyd over the phone. Tr. 1076.

Hooks conversed with Lloyd after she first received a document subpoena from Commission staff, but did not remember the specifics of that conversation. Tr. 1064-66. When Hooks received the subpoena, it made her nervous about her own exposure. She testified that

“[Lloyd] calmed my nerves a little bit. . . . I asked him if I should get an attorney, and he said that would be up to me.” Tr. 1065. She was “really concerned about what [she] needed to do to protect [her]self.” Tr. 1065.

#### 6. Mark Losby

Losby, from Columbia, SC, runs a chiropractic office with his wife. Tr. 928. He has been a tax client of Lloyd’s since 2012. Tr. 928. Losby did not fully appreciate that as a member of FC12, he would be investing in a real estate offering; he understood the tax deduction strategy “at a very macro level,” not “the inner workings.” Tr. 946-47.

Losby testified that he understood, before he wrote his \$40,000 check to FC12, that Lloyd would take a portion of this contribution as a fee. Tr. 930-31, 937, 945. He testified that he knew upfront that the fee would be \$6,500. Tr. 939-41. However, Losby also testified that he turned to Lloyd when he first received a document subpoena from Commission staff, meaning Lloyd had the opportunity to influence Losby’s memory of his FC12 participation. Tr. 937-38, 942-43.

#### 7. Larry Price

Price, a lawyer from Charlotte, NC, has been a tax client of Lloyd’s for at least ten years. Tr. 1105-06, 1111-12. Price is also an advisory client of Lloyd’s, and had an LPL account in at least 2011 and 2012. Tr. 1106, 1114. Price participated in FC11 and FC12, and at the hearing described them as “[i]nvestments to get a tax deduction.” Tr. 1114. Price was satisfied with the results of his FC11 and FC12 participation. Tr. 1107-08.

Price testified that Lloyd told him, prior to his contributing \$40,000 to FC12, that there would be a fee of \$6,500 taken from that amount. Tr. 1108. Like Losby, however, Price was in contact with Lloyd just after receiving a document subpoena from Commission staff. Tr. 1117-19.

#### 8. Lee Powell

Powell, a “partially retired” independent consultant from Mooresville, NC, has been Lloyd’s tax client since 2011. Tr. 614. Goss introduced Powell to Lloyd. Tr. 614, 629. Powell is “a CPA by background.” Tr. 615, 642. Since around 2012, Powell has also been an advisory client of Lloyd’s. Tr. 632-33. Lloyd managed an IRA for Powell; the existing IRA was moved to LPL when Powell became an advisory client. Tr. 633-34, 636, 676-77. Powell was satisfied with his participation in both FC11 and FC12. Tr. 622, 625. He has since participated in two other conservation easement programs through Lloyd. Tr. 625.

Powell described Lloyd’s conservation easement strategy as “to essentially procure land and then with other limited partners donate that land as part of a conservation and receive a tax deduction for that.” Tr. 615. Powell expected to receive tax deductions, and no other financial gains, from participating in the Forest Conservation entities through Lloyd. Tr. 615. He

recognized that to make a qualified conservation contribution warranting a federal tax deduction, he would need a qualified real property interest. Tr. 648-50.

Powell testified that he was aware that the checks he wrote to FC11 and FC12 would each include a fee. Tr. 620, 625; Resp. Ex. 4 at 11-12 of 14; Resp. Ex. 58. He testified before seeing any documents that he believed he was charged a fee between \$4,000 and \$5,000 in connection with FC12, and that his actual fee of \$8,500 seemed high. Tr. 641, 670. After seeing his fee in writing, he testified that the first time he knew that the fee charged in connection with FC12 was \$8,500 was when the Operating Agreement was amended. Tr. 677; Resp. Ex. 16 at 2220. Powell also acknowledged that for FC11 he was charged a much smaller fee of \$4,500, and that he received invoices for tax services Lloyd provided to him, but not for an FC12 fee. Tr. 640, 645.

After Powell received a document subpoena from Commission staff, he spoke to Lloyd. Tr. 643. Powell “would have felt personally exposed” and likely spoke to Lloyd about whether the conservation easement strategy was “a valid tax strategy.” Tr. 643.

Powell did not recall the details of his 2014 conversation with Lloyd about signing the amended FC12 Operating Agreement. Tr. 626-27, 653-54. Powell only recalled that an error had been made that needed to be corrected; he “didn’t have any understanding what the problem was.” Tr. 654.

### **III. DISCUSSION AND CONCLUSIONS OF LAW**

#### **A. Legal Standards**

Following the Summary Disposition Order, only the charges under Advisers Act Section 206 remain to be decided. *See supra* § I(C).

Advisers Act Section 206(1) makes it unlawful for an investment adviser to employ any device, scheme, or artifice to defraud any client or prospective client. 15 U.S.C. § 80b-6(1). Section 206(2) makes it unlawful for an investment adviser to engage in any transaction, practice, or course of business that operates as a fraud or deceit upon any client or prospective client. 15 U.S.C. § 80b-6(2). Advisers Act Section 206(4) prohibits investment advisers from engaging in any act, practice, or course of business which is fraudulent, deceptive, or manipulative, whether or not the victim is a client or prospective client. 15 U.S.C. § 80b-6(4). The Advisers Act does not define “client” or “prospective client.” *See* 15 U.S.C. § 80b-2; Rules Implementing Amendments to the Inv. Advisers Act of 1940, Advisers Act Release No. 1601, 1996 WL 734264, at \*15 (Dec. 20, 1996) (“The term ‘client’ is not defined in the Advisers Act.”); *SEC v. DiBella*, 587 F.3d 553, 568 n.11 (2d Cir. 2009).

An investment adviser is defined in relevant part as “any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing or selling securities.” 15 U.S.C. § 80b-2(a)(11). “Investment adviser” is distinguished from “person associated with an investment adviser” in the Advisers Act. *Compare* 15 U.S.C. § 80b-2(a)(11) *with* 15 U.S.C. § 80b-2(a)(17). The latter “means any partner, officer, or director of [an] investment adviser (or

any person performing similar functions), or any person directly or indirectly controlling or controlled by such investment adviser, including any employee of such investment adviser.” 15 U.S.C. § 80b-2(a)(17).

A material misrepresentation or omission, made in connection with the business of being an investment adviser, using jurisdictional means, is enough to establish a violation of Section 206(4); the material misrepresentation or omission must defraud, or operate as a fraud or deceit upon, a client or prospective client to establish a Section 206(1) or 206(2) violation. 15 U.S.C. § 80b-6(1), (2), (4); *see SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 197-99 (1963); *Montford & Co.*, Advisers Act Release No. 3829, 2014 WL 1744130, at \*13 (May 2, 2014); *David Henry Disraeli*, Advisers Act Release No. 2686, 2007 WL 4481515, at \*9 (Dec. 21, 2007). In the context of a Section 206 violation, a misrepresented or omitted fact may be deemed material if it would be significant to a reasonable client or prospective client’s evaluation of the adviser’s integrity or fidelity to his clients. *See Delta Global Advisors, Inc.*, Advisers Act Release No. 3282, 2011 WL 4364106, at \*4 (Sept. 20, 2011); *Interpretation of Section 206(3) of the Inv. Advisers Act of 1940*, Advisers Act Release No. 1732, 1998 WL 400409, at \*3 & n.11 (July 17, 1998); Tamar Frankel & Ann Taylor Schwing, *The Regulation of Money Managers*, § 13.01[B][2][c].

Section 206(1) requires a showing of scienter, meaning an “intent to deceive, manipulate, or defraud,” while Sections 206(2) and 206(4) do not. *SEC v. Steadman*, 967 F.2d 636, 641, & n.3, 643 & n.5, 647 (D.C. Cir. 1992). Scienter may be established through “a heightened showing of recklessness.” *John P. Flannery*, Securities Act Release No. 9689, 2014 WL 7145625, at \*10 n.24 (Dec. 15, 2015).

Primary liability for violations of Advisers Acts Section 206(1), 206(2), and 206(4) may only rest with an investment adviser, as distinguished from a non-controlling employee of an investment adviser. *See SEC v. Berger*, 244 F. Supp. 2d 180, 193 (S.D.N.Y. 2001) (“Because [defendant] effectively controlled [the investment advisory firm] and its decisionmaking, [defendant] is also properly labeled an investment adviser within the meaning of the Advisers Act.”); *John J. Kenny*, 56 S.E.C. 448, 485 n.54 (2003) (“An associated person may be charged as a primary violator under Section 206 where the activities of the associated person cause him or her to meet the broad definition of ‘investment adviser.’ . . . [C]ourts have found that an associated person is liable under Section 206 where the investment adviser is an alter ego of . . . or is controlled by the associated person.”); *Russell W. Stein*, Exchange Act Release No. 47504, 2003 WL 1125746, at \*3-4 (Mar. 14, 2003) (mere employee of Merrill Lynch did not qualify as an investment adviser and could not be held primarily liable for violation of Advisers Act Section 206).

## **B. Misrepresentations**

The “misrepresentations” alleged against Lloyd in connection with FC12 fall into three categories: (1) misrepresentations to SFA (OIP at ¶¶ 48, 49); (2) issuance of false K-1s to FC 12 participants (OIP at ¶¶ 50, 51); and (3) misappropriation of funds from Brown, Carson, and Malloy (OIP at ¶¶ 46, 47). *See* OIP at 9; Div. Br. at 19-21. As described below, the record supports only the allegations of misrepresentations to SFA.

## 1. Material Misrepresentations to SFA

The OIP alleges that Lloyd did not reveal to SFA that Brown, Carson, or Malloy had provided investment funds to FC12, and that when Zak asked Lloyd specifically about Carson, Lloyd informed Zak that Carson was “OUT.” OIP at 9. Lloyd does not dispute that he “made a misrepresentation to Ms. Zak and SFA” regarding Carson’s participation in FC12. Resp. Br. at 15; *see* Resp. Reply at 24. Lloyd agreed at the hearing that the “amount of money that was put on the form as the amount of purchase was the amount of money that was being contributed towards the respective offering by the prospective investor.” Tr. 778. Thus, Lloyd’s omission of Brown and Malloy on the list of FC12 investors also constituted a misrepresentation to SFA. Tr. 194-95, 484.

Lloyd’s misrepresentations, although made to a broker-dealer rather than to a client or prospective client, were plainly material; both SFA and Piney Cumberland needed to know the identities of individual investors to ensure suitability and to comply with disclosure requirements, among other considerations. Tr. 106-08, 453-54, 519. Additionally, anyone considering trusting Lloyd as a financial advisor would surely want to know that he was willing to mislead a brokerage firm about Carson’s placement of funds in FC12.

## 2. False K-1s

The OIP alleges that Lloyd issued false K-1s to Brown, Carson, and Malloy, because those clients were not actually invested in FC12 and were not entitled to a share of FC12’s tax deduction, and that by issuing the false K-1s, Lloyd understated the tax deductions to which the other participants were entitled. OIP at 9. Although the Division repeats the OIP’s allegations in its post-hearing briefing, its principal argument on this point is not that the K-1s independently violated Section 206, but that the K-1s were intended to cover up Lloyd’s overall scheme, and therefore support a finding of scienter. Div. Br. at 30.

The issuance of the K-1s was not an independent violation of Section 206. There is insufficient evidence that Brown, Carson, and Malloy were not, in fact, members of FC12. Each participant, including Brown, Carson, and Malloy, paid Lloyd for a share of FC12, and each received a share of FC12’s tax deduction, roughly on a pro rata basis. FC12, as an unincorporated limited liability company, was treated for tax purposes as a partnership. *See* 26 U.S.C. § 761(a). Partnerships file “information returns” which must include the identities of the partners. *See* 26 U.S.C. § 6031(a); *Mathia v. Comm’r of Internal Revenue*, 669 F.3d 1080, 1082 n.1 (10th Cir. 2012). FC12’s information return (Form 1065) included K-1s for all of its participants, including Brown, Carson, and Malloy. Resp. Ex. 26. Piney Cumberland held title to the underlying real estate, and nothing in the record suggests that FC12 or the members of FC12 had to appear on the deed for Piney Cumberland’s tax deduction to pass to FC12, or that Brown, Carson, and Malloy lost the right to a tax deduction because they were not on the deed. Similarly, nothing in the record demonstrates that SFA’s treatment of interests in Piney Cumberland—by, for instance, failing to forward the identities of Brown, Carson, and Malloy to a transfer agent—caused the FC12 participants to lose their interests in FC12.

Certainly the overall manner in which Lloyd managed FC12 was, at a minimum, highly irregular. But there is no reason to think that Lloyd's failure to inform SFA and Piney Cumberland that Brown, Carson, and Malloy were participants in FC12 meant that Brown, Carson, and Malloy were not, in fact, participants in FC12. There is evidence that Lloyd did not communicate his FC12-related fees to his clients beforehand, that the size of each client's contribution to FC12 was both excessive (because it included Lloyd's fees) and not accurately communicated to SFA, and that the FC12 membership list was not properly documented in its Operating Agreement until after OCIE started examining Lloyd's records. But in the end each client received a share of FC12's tax deduction that was more or less what each client expected, there is no basis for concluding that the inaccurate information conveyed to SFA affected the extent to which each client actually participated in FC12, and the OIP does not allege a violation based on non-disclosure of advisory fees, charging excessive advisory fees, or failing to keep accurate books and records. In sum, given the state of the evidence, the record is insufficient to establish that the eighteen K-1s issued to the eighteen participants in FC12 were false.

### 3. Misappropriation

The Division maintains that Lloyd "stole" Brown, Malloy, and Carson's money. Div. Br. at 5, 14-15, 20, 30, 32, 34. It argues that the full \$130,000 that Brown, Carson, and Malloy together deposited in FC12 was stolen, and Lloyd diverted \$105,750 to accounts he controlled while using the remaining \$24,250 to inflate his personal investment in FC12. *See, e.g.*, Div. Br. at 32 ("Lloyd stole \$130,000 from Brown, Malloy and Carson."); *see also* OIP at 3, 9.

This may have been Lloyd's actual intention. If Lloyd had not issued a K-1 to himself, tied to his actual \$16,802 contribution to FC12, and K-1s to Brown, Carson, and Malloy, tied to their actual combined \$130,000 contributions to FC12, the evidence for the alleged misappropriation would be much stronger. But Brown, Carson, and Malloy gave their money to Lloyd in the expectation of receiving K-1s, and Lloyd issued them K-1s in approximately the amounts they should have received. Again, Lloyd's management of FC12 was at least highly irregular, but it did not amount to theft.

Make no mistake, Lloyd may not have issued true and correct K-1s absent the focus on him in early 2013 by LPL and OCIE. *See* Resp. Reply at 9-10. It is entirely possible that, had LPL and OCIE never examined Lloyd, he would have stolen \$130,000 from his clients outright. But it is at least as possible that Lloyd was simply "physically and mentally exhausted," and that he intended all along to straighten everything out once tax season was over. Tr. 810. The many falsehoods he conveyed to SFA and Piney Cumberland, and his failure to keep his clients informed of his inattentive and unprofessional stewardship of their money, may have merely been part of a scheme to cut corners and muddle through, rather than a scheme to steal or convert his clients' assets. On the facts of this case, misappropriation has not been proven by a preponderance of the evidence.

## C. Liability for Fraud

### 1. Lloyd Was an Investment Adviser

Lloyd argues that he is not liable because he “was acting as an accountant, and such conduct is not within the enforcement jurisdiction of the Commission.” Resp. Br. at 16; *see* Resp. Reply at 20-21. To be sure, an accountant “whose performance of [investment advisory] services is solely incidental to the practice of his profession” is not considered an investment adviser. 15 U.S.C. § 80b-2(a)(11)(B). But Lloyd passed multiple securities examinations, intentionally associated himself with LPL, provided both tax and advisory services simultaneously to at least five clients, and, as particularly relevant here, commingled those five clients in FC12, an LLC he set up to invest in a private (non-securities) offering through a registered broker-dealer. His investment advisory work in this proceeding was in no sense “solely incidental” to his accounting practice—to the contrary, they were inextricably intertwined.

Respondent further argues that under *Russell W. Stein*, 2003 WL 1125746, Lloyd can only be considered an associated person of an investment adviser, and not an investment adviser himself. *See* Resp. Reply at 19-20. In *Russell W. Stein*, however, the respondent was clearly working merely as an associated person of an investment adviser. “There [was] no evidence . . . that Stein acted in any capacity other than as a Merrill Lynch employee in his dealings with Merrill Lynch clients.” 2003 WL 1125746, at \*3. Further, Stein headed a team of Merrill Lynch employees providing investment consulting services and held himself out as an employee of Merrill Lynch. *See Russell W. Stein*, Initial Decision Release No. 150, 1999 SEC LEXIS 1982, at \*5-7 (Sept. 27, 1999).

Lloyd, by contrast, admitted to having about twenty advisory clients through his own investment advisory firm, Ed Lloyd Wealth Management, while associated with a distinct registered investment adviser, LPL. Tr. 697-98, 771. The independent contractor-like autonomy he possessed while associated with LPL made him much more like a controlling person of an investment adviser than an employee of an investment adviser. *See Donald L. Koch*, Exchange Act Release No. 72179, 2014 WL 1998524, at \*18 & n.196 (May 16, 2014) (citing in part *John J. Kenny*, 56 S.E.C. at 485 n.54), *pet. denied on relevant grounds*, --- F.3d ---, 2015 WL 4216988 (D.C. Cir. July 14, 2015). Further, with respect to his advisory clients, Lloyd engaged in conduct virtually indistinguishable from that of an unregistered investment adviser. It would be anomalous if Lloyd could only be held secondarily liable for conduct that would warrant primary liability for an unregistered investment adviser. *See Koch*, --- F.3d ---, 2015 WL 4216988, at \*8 (D.C. Cir. July 14, 2015); *Teicher v. SEC*, 177 F.3d 1016, 1017-19 (D.C. Cir. 1999). Most important, LPL cannot be held primarily liable here because it knew nothing about FC12. Lloyd purposefully kept LPL in the dark about all three Forest Conservation entities, and his deceitful conduct toward SFA was purely his own, not LPL’s. It would be particularly anomalous if he could avoid primary liability by the simple expedient of selling away. Lloyd was therefore an investment adviser at all relevant times.

## 2. Lloyd Acted With Scienter

The evidence of scienter is overwhelming, and conclusively refutes Lloyd’s contention that his misrepresentations to SFA were mere “scrivener’s error[s].” *See* Div. Br. at 20; Resp. Br. at 23 (“three participants . . . were not listed on Schedule I in December 2012 due to a scrivener’s error”). First, if his misrepresentations were mere scrivener’s errors, one would have

expected Lloyd to inform SFA of the errors as soon as he learned of them. But he made no such correction. Second, Lloyd misled SFA in other ways—such as hiding his association with LPL and misrepresenting his personal contribution to FC12—at the same time he was omitting Brown, Carson, and Malloy from FC12’s Schedule I. *See supra* § II(D)(3). Notably, he not only failed to list Brown and Malloy on the Schedule I, he also did not transmit their Client Account Forms to SFA. Third, Lloyd chose not to produce to OCIE the Schedule I to the FC12 Operating Agreement in effect in March 2013, showing just fifteen participants (and not Brown, Carson, or Malloy), which Lloyd had sent to SFA and the Piney Cumberland offering’s issuer a mere three months earlier. Since Lloyd also, accurately, told OCIE that eighteen participants contributed funds to FC12, providing the most recent Schedule I to OCIE would have immediately revealed his misconduct. Fourth, Lloyd failed to inform LPL of the existence of the Forest Conservation entities, which were outside business activities, and of his and his tax and advisory clients’ participation in private offerings brokered by SFA. Lloyd’s failure was clearly intentional, because he had been trained in LPL’s compliance policies. Last, Lloyd’s own testimony was that he purposely did not tell Carson that a 407 letter was needed, and purposely did not refund Carson’s FC12 contribution, to honor his promise to Carson of a tax deduction. Tr. 807-16, 868-84, 911-20.

Although I have credited Lloyd’s testimony on numerous issues, his credibility on this subject is low. His demeanor in the hearing was poor overall; he was non-responsive and evasive when asked difficult questions, and sometimes provided very confusing answers. That Lloyd changed his account from the narrative he provided in his Wells Submission (i.e., “scrivener’s error”), then changed it back in his post-hearing briefing, further undermines his credibility on this subject. That he omitted telling his clients of his many failures, including his failure to tell SFA that Brown, Carson, and Malloy had deposited money in FC12, and that Lloyd provided false information to SFA regarding his own FC12 contribution to compensate for Carson’s omission, similarly erodes his credibility.

As it happens, though, Lloyd’s credibility is not crucial to resolving the issue of scienter with respect to Carson, because even Lloyd conceded that his Carson-related paperwork was “very sloppy.” Tr. 1019. That is, Lloyd’s own testimony establishes that at a minimum he acted highly unreasonably, and departed from an investment adviser’s standard of care to an extreme degree, by telling SFA that Carson was “OUT.”

Accordingly, at a minimum Lloyd acted with extreme recklessness, and therefore with scienter, by misleading SFA regarding Carson. He also acted intentionally, and therefore with scienter, by omitting any mention of Brown and Malloy to SFA. The Division has met its burden of proving that Lloyd committed at least two acts of deception against SFA charged in the OIP, with scienter.

### 3. Lloyd Committed Primary Violations of Advisers Act Section 206(4)

Lloyd’s communications with SFA were generally by email between North Carolina and Georgia, and were therefore in interstate commerce. *E.g.*, Tr. 263; Div. Ex. 88. Lloyd made at least two material misrepresentations or omissions to SFA. Lloyd was an investment adviser at all relevant times. This is sufficient to demonstrate two violations of Section 206(4).

Section 206(4) is worded broadly to make unlawful *any* fraudulent or deceptive act, practice, or course of business by an investment adviser. 15 U.S.C. § 80b-6(4). The act, practice, or course of business need not be in connection with providing investment advice. See *SEC v. DiBella*, No. 304-cv-1342, 2005 WL 3215899, at \*8 (D. Conn. Nov. 29, 2005); *Marc N. Geman*, Exchange Act Release No. 43963, 2001 WL 124847, at \*8 (Feb. 14, 2001). It also need not be made in the course of the advisory relationship. See *Mysore S. Sundara*, Exchange Act Release No. 28419, 1990 WL 312172, at \*3 (Sept. 10, 1990) (fraudulent investment advisory activities included investment adviser's borrowing funds from individuals who were his advisory clients); *Ronald B. Donati, Inc.*, Advisers Act Release No. 683, 1979 WL 174199 (July 2, 1979) (finding violations in connection with personal loan from investment advisory client as alleged in Advisers Act Release No. 666, 1979 WL 173632). The misrepresentations Lloyd made to SFA fall within the scope of Section 206(4), and Lloyd is primarily liable for violating it.

4. Lloyd did not Violate Advisers Act Sections 206(1) and 206(2)

As noted, the record does not establish violations involving fraud upon Lloyd's individual clients or prospective clients, whether advisory or not. The Division argues that Lloyd defrauded FC12, as well as his individual advisory clients. See Div. Br. at 20. But FC12 never invested in securities, nor was it likely to, and it was therefore neither a client nor a prospective client. Thus, Lloyd did not violate Sections 206(1) or 206(2).

5. Connection to Now-Dismissed Allegations

The Division urges that I reverse the summary disposition ruling and construe FC12 as a security. See Div. Br. at 21-27. As I iterated before the hearing, I decline to reverse the ruling of the law judge previously assigned to this proceeding. Mar. 16, 2015, Prehearing Tr. 24-25. However, were the summary disposition ruling reversed, the record would likely support violations under the Securities and Exchange Acts.

Lloyd's misrepresentations to SFA would have been material under the Securities and Exchange Acts because a reasonable investor in FC12—again, assuming FC12 was a security—would surely want to know that Lloyd was concealing the identity of FC12 investors from the broker-dealer and the issuer. See *Basic Inc. v. Levinson*, 485 U.S. 224, 231-32, 240 (1988); *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449-50 (1976); *Flannery*, 2014 WL 7145625, at \*20-22. Lloyd also acted with scienter. See *Aaron v. SEC*, 446 U.S. 680, 697 (1980); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 (1976). Thus, violations of Securities Act Section 17(a) and Exchange Act Section 10(b) and Rule 10b-5 could likely be made out. In particular, Lloyd's omissions regarding Brown, Carson, and Malloy would likely constitute false statements in the offer, purchase, and sale of securities under Securities Act Section 17(a)(2), by which Lloyd obtained money in the form of fees, and under Exchange Act Rule 10b-5(b). See 15 U.S.C. § 77q(a)(2); 17 C.F.R. § 240.10b-5(b). Advisers Act Rule 206(4)-8 prohibits similar material misstatements by an investment adviser to investors in a pooled investment vehicle. See 17 C.F.R. § 275.206(4)-8(a)(1); *Prohibition of Fraud by Advisers to Certain Pooled Inv. Vehicles*, Advisers Act Release No. 2628, 2007 WL 2239114, at \*3 (Aug. 3, 2007). Lastly, it is virtually

undisputed—but for the fact that the interests at issue were not securities—that Lloyd was selling away from LPL in violation of 15 U.S.C. § 78o(a)(1). *See* Div. Br. at 28-29.

#### **D. Constitutional Issues**

Lloyd argues that this proceeding denies him due process because the administrative setting lacks the type of discovery and evidentiary rules found in federal practice, and appears to argue that the Commission’s law judges and the Commission itself are biased in favor of the Division. *See* Answer at 13; Resp. Br. at 18-20.

Lloyd cites no cases or other authority holding that the Commission’s Rules violate due process, nor am I aware of any such authority. *Cf. Atlas Roofing Co. v. Occupational Safety & Health Review Comm’n*, 430 U.S. 442, 450 (1977) (“[I]n cases . . . in which the Government sues in its sovereign capacity to enforce public rights created by statutes within the power of Congress to enact the Seventh Amendment does not prohibit Congress from assigning the factfinding function and initial adjudication to an administrative forum with which the jury would be incompatible.”); *Mitchell M. Maynard*, Advisers Act Release No. 2875, 2009 WL 1362796, at \*8 & n.21 (May 15, 2009) (“The fundamental requirement of due process is the opportunity to be heard at a meaningful time and in a meaningful manner.”) (*citing Matthews v. Eldridge*, 424 U.S. 319, 333 (1976)); *see also SEC. v. Jett*, 514 F. Supp. 2d 532, 536 (S.D.N.Y. 2007) (due process fulfilled where service complied with Commission’s Rules of Practice). It is entirely consistent with due process for the Commission to act as both charging body and appellate reviewer. *See* 5 U.S.C. § 554; *Blinder, Robinson, & Co., Inc. v. SEC*, 837 F.2d 1099, 1107 (D.C. Cir. 1988); *Whole Foods Mkt.*, Docket No. 9324, 2008 WL 4153583, at \*3 (F.T.C. Sept. 5, 2008) (“Respondent cites no authority for the proposition that the [Federal Trade] Commission, having sought preliminary relief, may not adjudicate the merits, and we are aware of none. To the contrary, the Administrative Procedure Act envisions agencies acting in the dual roles that [Respondent] objects to.”). Lloyd’s due process claim is therefore meritless.

Lloyd’s evidence of bias is entirely unpersuasive. That the presiding law judge changed for no stated reason and at an inconvenient time for all parties is not evidence of bias. *See* Resp. Br. at 19. That I overruled some but not all of Lloyd’s evidentiary objections is no more evidence of bias than that I overruled some but not all of the Division’s evidentiary objections. *See id.* at 20. Even assuming that I have “rarely, if ever, found in favor of the Respondent in the past two years,” that is not evidence of bias against Lloyd. *See id.* Lloyd cites various statements I made during his testimony as evidence of bias. *See id.* at 21. How the cited statements show bias is a complete mystery, however.

Lloyd further argues that I had no authority to conduct the hearing because I am not an officer of the Commission. Resp. Br. at 17-18 (citing 15 U.S.C. § 80b-12). But when the Commission instituted this proceeding it ordered a hearing “before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission’s Rules of Practice, 17 C.F.R. § 201.110.” OIP at 11. Under such circumstances, “the Chief Administrative Law Judge shall select . . . the administrative law judge to preside.” 17 C.F.R. § 201.110. On March 16, 2015, the Chief Administrative Law Judge designated me to “preside at the hearing in these proceedings and to perform other and related duties in accordance with the Commission’s Rules of Practice.” *Paul Edward “Ed” Lloyd, Jr., CPA*, 2015 SEC LEXIS 968.

To the extent the Advisers Act requires that the hearing “be held before the Commission . . . or any officer or officers of the Commission designated by it,” I am perforce the designated officer. 15 U.S.C. § 80b-12. Lloyd cites no authority for the proposition that the term “officer” has the same meaning in the Advisers Act as it does in the Constitution, and so whether or not I am an officer within the meaning of Article II of the Constitution is immaterial. Resp. Br. at 17-18.

#### **IV. Sanctions**

The Division requests a cease-and-desist order, a bar from association with an investment adviser, broker, dealer, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization (associational bar), disgorgement with prejudgment interest, and second-tier civil penalties against Lloyd.<sup>8</sup> Div. Br. at 31-35. I conclude in this section that a cease-and-desist order, associational bar, disgorgement with prejudgment interest, and second-tier civil penalties should be imposed against Lloyd.

##### **A. The Public Interest**

The appropriateness of remedial sanctions in this proceeding is guided by the public interest factors set forth in *Steadman v. SEC*, 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981), namely: the egregiousness of the respondent’s actions; the isolated or recurrent nature of the infraction; the degree of scienter involved; the sincerity of the respondent’s assurances against future violations; the respondent’s recognition of the wrongful nature of his or her conduct; and the likelihood that the respondent’s occupation will present opportunities for future violations (*Steadman* factors). *Gary M. Kornman*, Exchange Act Release No. 59403, 2009 SEC LEXIS 367, at \*22 (Feb. 13, 2009), *pet. denied*, 592 F.3d 173 (D.C. Cir. 2010). The Commission also considers the extent to which the sanction will have a deterrent effect, the degree of harm to investors, the likelihood of future violations, and the combination of sanctions against the respondent. *See Schield Mgmt. Co.*, 58 S.E.C. 1197, 1217-18 & n.46 (2006); *KPMG Peat Marwick LLP*, 54 S.E.C. 1135, 1184-85, 1191-92 (2001). The Commission’s inquiry into the appropriate sanction to protect the public interest is a flexible one and no one factor is dispositive. *KPMG*, 54 S.E.C. at 1192; *see Gary M. Kornman*, 2009 SEC LEXIS 367, at \*22.

Lloyd deceived SFA regarding Brown and Malloy’s participation in FC12. He further misrepresented to SFA Carson’s placement of funds in FC12. These misrepresentations constitute two violations of the Advisers Act, making Lloyd’s fraudulent misconduct recurrent.

Lloyd’s misconduct was also egregious and involved a fair degree of scienter. Fundamentally, it is simply wrong to deceive one’s counterparty about material matters. More specifically, Lloyd’s failure to inform SFA and Piney Cumberland of the identities of their ultimate customers undermined those entities’ compliance efforts, created a risk that they might

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<sup>8</sup> In post-hearing briefing, these remedies were exclusively sought under the Advisers Act, presumably because of the Summary Disposition Order. Div. Br. at 31-35. *But see* OIP at 11 (contemplating remedies under other securities statutes).

violate the suitability and disclosure provisions of the securities laws, and, in Carson's case, potentially created a conflict of interest between SFA and Merrill Lynch. Moreover, Lloyd took a number of calculated steps to make SFA unaware of his background and LPL unaware of his handling of the Forest Conservation entities, and was obstructive and unforthcoming when LPL and OCIE turned their attention to his dealings.

Lloyd accepts no responsibility that he has done anything at all wrong, or even at all connected to his investment advisory practice, and expresses no remorse for misleading SFA and the Piney Cumberland offering's issuer. At the same time, it is clear that Lloyd has continued to set up opportunities for his clients to earn tax deductions via conservation easements, even since OCIE and the Division turned their focus on Lloyd and the Forest Conservation entities. Tr. 625, 966, 1174. Although he is no longer associated with a registered investment adviser, and his profession therefore does not presently afford him opportunities to recidivate, he has otherwise offered no assurances against future violations. Indeed, now that he is no longer an investment adviser, the Advisers Act no longer prohibits him from deceiving the broker-dealers and issuers with which he continues to deal. The *Steadman* factors, except for his occupation, all weigh in favor of a heavy sanction.

Admittedly, no investors were harmed by Lloyd's misconduct, and his violations were neither recent nor remote, but a heavy sanction will have a strong deterrent effect and there is no evidence that the requested combination of sanctions is unduly severe. Overall, robust sanctions against Lloyd are appropriate in the public interest.

### **B. Cease-and-Desist**

Advisers Act Section 203(k), 15 U.S.C. §§ 80b-3(k), authorizes the Commission to impose cease-and-desist orders for violations of the Advisers Act. Some likelihood of future violation is a prerequisite for the imposition of such an order. *KPMG Peat Marwick LLP*, 54 S.E.C. at 1185. However, "a finding of [a past] violation raises a sufficient risk of future violation," because "evidence showing that a respondent violated the law once probably also shows a risk of repetition that merits . . . ordering [a] cease-and-desist order." *Id.* In evaluating the propriety of a cease-and-desist order, the Commission considers the *Steadman* factors, as well as the recency of the violation, the resulting harm to investors in the marketplace, and the effect of other sanctions. *Id.* at 1192.

A cease-and-desist order is appropriate here, particularly because Lloyd shows no remorse for his misconduct and continues to set up conservation easement programs for clients.

### **C. Associational Bar**

Advisers Act Section 203(f), 15 U.S.C. §80b-3(f), authorizes imposition of an associational bar against a person, if: (1) at the time of misconduct he was associated with an investment adviser; (2) such a bar is in the public interest; and (3) the person willfully violated any provision of the Advisers Act.

As discussed above, Lloyd was an associated person of LPL in December 2012, and thus was associated with an investment adviser within the meaning of Advisers Act Section 203(f) at the time of his misconduct. His violations were committed with scienter, and were therefore willful. *See Donald L. Koch*, 2014 WL 1998524, at \*13 n.139. As with a cease-and-desist order, the public interest clearly weighs in favor of an associational bar.

#### **D. Disgorgement with Prejudgment Interest**

Advisers Act Section 203(j), 15 U.S.C. § 80b-3(j), authorizes disgorgement of ill-gotten gains, including reasonable interest, in any proceeding in which a civil money penalty could be imposed. “Disgorgement is an equitable remedy, imposed to force a defendant to give up the amount by which he was unjustly enriched.” *SEC v. Contorinis*, 743 F.3d 296, 301 (2d Cir. 2014) (internal quotation omitted). Disgorgement does not serve a punitive function, but is designed to force wrongdoers to return the fruits of illegal conduct. *Id.*; *see also Brendan E. Murray*, Advisers Act Release No. 2809, 2008 WL 4964110, at \*12 (Nov. 21, 2008). The amount of disgorgement should include all gains flowing from the illegal activities, but calculating it requires only a reasonable approximation of profits causally connected to the violation, and once the Division shows that its disgorgement figure is a reasonable approximation of the amount of profits, the burden shifts to the respondent to demonstrate that the Division’s estimate is not a reasonable approximation. *Donald L. Koch*, 2014 WL 1998524, at \*22.

I am unconvinced by the Division’s argument that \$130,000, reflecting the total of Brown, Carson, and Malloy’s contributions to FC12, is a reasonable approximation of the amount of profits. *See Div. Br.* at 32. This is because, as explained above, the Division has not established Lloyd’s theft of those clients’ funds. *See supra* III(B)(3). Instead, the Division has shown that Lloyd violated the Advisers Act by making two misrepresentations to a broker-dealer in connection with Lloyd’s investment advisory practice. Lloyd’s own testimony establishes that, but for his deceit of SFA, his clients could not have participated in FC12 and he would not have been entitled to his fees. Tr. 809, 812-13. Thus, the amount he was enriched as a result of his deceit—\$105,750—should be disgorged. Div. Exs. 67, 102, 109, 110, 187.

Advisers Act Section 203(j) also contemplates an award of reasonable prejudgment interest on a disgorgement amount. Lloyd will be required to pay prejudgment interest on the \$105,750 disgorgement amount, calculated from January 1, 2013, to the last day of the month preceding the month in which disgorgement is paid, consistent with 17 C.F.R. § 201.600.

#### **E. Civil Penalties**

Advisers Act Section 203(i) authorizes the imposition of civil penalties where, as here, the respondent has violated the Advisers Act. *See* 15 U.S.C. § 80b-3(i)(1)(B). A three-tier system establishes the maximum civil money penalty that may be imposed for each violation: a first-tier penalty is permissible for each statutory violation; a second-tier penalty is permissible where the respondent’s unlawful act or omission involves fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement; and a third-tier penalty is permissible where the misconduct, in addition to involving fraud, deceit, manipulation, or

deliberate or reckless disregard for a regulatory requirement, resulted in substantial losses, created a significant risk of substantial losses to other persons, or resulted in substantial pecuniary gain to the person who committed the misconduct. 15 U.S.C. § 80b-3(i)(2). The number of violations must be determined when imposing civil penalties. *See Rapoport v. SEC*, 682 F.3d 98, 108 (D.C. Cir. 2012). In determining whether a penalty is in the public interest, the Commission may consider (1) whether the violation involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement, (2) the resulting harm to other persons, (3) any unjust enrichment and prior restitution, (4) the respondent's prior regulatory record, (5) the need to deter the respondent and other persons, and (6) such other matters as justice may require. 15 U.S.C. § 80b-3(i)(3); *Anthony Fields, CPA*, Exchange Act Release No. 74344, 2015 WL 728005, at \*24 (Feb. 20, 2015).

The Division asks for second-tier penalties against Lloyd. Div. Br. at 34. Because Lloyd engaged in violations involving fraud or deceit two times—by omitting mention of Brown and Malloy's FC12 participation to SFA, and by affirmatively misrepresenting Carson's participation in FC12 to SFA—second-tier penalties are justified. As for the other public interest factors, Lloyd has a clean regulatory record. On the other hand, although there was no demonstrated harm to Lloyd's clients, and the Piney Cumberland interests were not securities, by circumventing the compliance processes at SFA and Piney Cumberland, Lloyd created a risk that those entities would violate the securities laws. Moreover, Lloyd received substantial unjust enrichment in the form of fees—substantial enough, in fact, to warrant third-tier penalties. *See Ralph Calabro*, Exchange Act Release No. 75076, 2015 WL 3439152, at \*47 (May 29, 2015) (\$55,000 in gains from churning found to warrant third-tier penalties). Also, civil penalties are an effective deterrent, particularly because Lloyd is no longer a regulated person.

On balance, civil penalties less than the maximum are warranted. The Division requests a total of \$100,000, which is reasonable under the circumstances. Lloyd will thus be ordered to pay second-tier penalties of \$50,000 for each of his two fraudulent misrepresentations, totaling \$100,000 in civil penalties. *See* 17 C.F.R. § 201.1004, Subpt. E, Table IV (for violations occurring between March 2009 and March 2013, the maximum amount of civil penalty for each violation is \$75,000 for a natural person).

## V. Record Certification

Pursuant to 17 C.F.R. § 201.351(b), I certify that the record includes the items set forth in the Corrected Record Index issued by the Commission's Office of the Secretary on July 23, 2015.<sup>9</sup>

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<sup>9</sup> Resp. Ex. 123 was admitted at the hearing, but just a small number of pages were admitted: an April 5, 2013, letter from Lloyd's counsel to the Division; and the December 10, 2012, version of the FC12 Operating Agreement, which is duplicative of part of Div. Ex. 90. Tr. 895, 899-900; *see* Resp. Ex. 123 at 1-3, 601-29 of 1204 pages; *see also surpa* § II(D)(3). These pages were part of a larger collection of documents provided by Lloyd to the Division in April 2013, which collection was admitted as Resp. Ex. 124. Tr. 1194-95. Following the hearing, however, Respondent filed with the Commission's Office of the Secretary a 1,204-page document as Resp.

## VI. Order

IT IS ORDERED that, pursuant to Investment Advisers Act of 1940 Section 203(f), Paul Edward “Ed” Lloyd, Jr., CPA, is permanently BARRED from association with any investment adviser, broker, dealer, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization.

IT IS FURTHER ORDERED that, pursuant to Investment Advisers Act of 1940 Section 203(k), Paul Edward “Ed” Lloyd, Jr., CPA, shall CEASE AND DESIST from committing any violations or future violations of Investment Advisers Act of 1940 Section 206.

IT IS FURTHER ORDERED that, pursuant to Investment Advisers Act of 1940 Section 203(i), Paul Edward “Ed” Lloyd, Jr., CPA, shall PAY A CIVIL MONEY PENALTY in the amount of \$100,000.

IT IS FURTHER ORDERED that, pursuant to Investment Advisers Act of 1940 Section 203(j), Paul Edward “Ed” Lloyd, Jr., CPA, shall DISGORGE \$105,750 and shall pay prejudgment interest on that amount, calculated from January 1, 2013, to the last day of the month preceding the month in which disgorgement is made, consistent with 17 C.F.R. § 201.600.

Payment of disgorgement, prejudgment interest, and civil penalties shall be made no later than twenty-one days following the day this Initial Decision becomes final, unless the Commission directs otherwise. Payment shall be made in one of the following ways: (1) transmitted electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request; (2) direct payments from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or (3) by certified check, United States postal money order, bank cashier’s check, wire transfer, or bank money order, payable to the Securities and Exchange Commission.

Any payment by certified check, United States postal money order, bank cashier’s check, wire transfer, or bank money order shall include a cover letter identifying the Respondent and Administrative Proceeding No. 3-16182, and shall be delivered to: Enterprises Services Center, Accounts Receivable Branch, HQ Bldg., Room 181, AMZ-341, 6500 South MacArthur Blvd., Oklahoma City, Oklahoma 73169. A copy of the cover letter and instrument of payment shall be sent to the Commission’s Division of Enforcement, directed to the attention of counsel of record.

This Initial Decision shall become effective in accordance with and subject to the provisions of Rule 360 of the Commission’s Rules of Practice, 17 C.F.R. § 201.360. Pursuant to that Rule, a party may file a petition for review of this Initial Decision within twenty-one days

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Ex. 123, and did not file Resp. Ex. 124. It appears that the filed version of Resp. Ex. 123 is the same as the admitted (but not filed) version of Resp. Ex. 124. The variance is immaterial; all of the admitted version of Resp. Ex. 123 is contained within the filed version of Resp. Ex. 123, the admitted version of Resp. Ex. 124 is duplicative of the filed version of Resp. Ex. 123, and I have not relied on any version of either exhibit.

after service of the Initial Decision. A party may also file a motion to correct a manifest error of fact within ten days of the Initial Decision, pursuant to Rule 111 of the Commission's Rules of Practice, 17 C.F.R. § 201.111. If a motion to correct a manifest error of fact is filed by a party, then a party shall have twenty-one days to file a petition for review from the date of the undersigned's order resolving such motion to correct manifest error of fact. The Initial Decision will not become final until the Commission enters an order of finality. The Commission will enter an order of finality unless a party files a petition for review or motion to correct manifest error of fact or the Commission determines on its own initiative to review the Initial Decision as to a party. If any of these events occur, the Initial Decision shall not become final as to that party.

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Cameron Elliot  
Administrative Law Judge