

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

JAMES C. TAO and
DONNA BOYD (f/k/a DONNA CHEN),

Defendants.

C.A. No. 4:17-cv-3678

COMPLAINT

Plaintiff Securities and Exchange Commission (the “Commission”) files this Complaint against Defendants James C. Tao (“Tao”) and Donna Boyd (f/k/a Donna Chen) (“Boyd”) (collectively, “Defendants”) and alleges as follows:

SUMMARY OF THE ACTION

1. Defendants operated a branch office of a registered investment adviser and broker-dealer in Houston, Texas (the “Registered Firm”). While associated with the Registered Firm, Defendants formed a private equity fund called PVC, LLC (“PVC”) to purportedly invest in Houston-area technology start-up companies. Without the Registered Firm’s knowledge or approval, Defendants raised approximately \$860,000 offering and selling membership units in PVC to their advisory clients and brokerage customers at the Registered Firm and to other family, friends, and contacts.

2. The Commission brings this enforcement action because Defendant Tao made material misrepresentations and omissions in connection with the offer and sale of units in the fund (*i.e.*, securities) in violation of the antifraud provisions of the federal securities laws. Tao falsely claimed that investor funds would be held in escrow and returned if PVC did not raise at least \$2.5 million, and Tao failed to timely or adequately disclose that PVC was investing in companies he owned or in which he had a personal stake, which was a clear conflict of interest. Tao also misled investors about the use of investor funds, including the use of new investor money to pay back earlier investors, and misappropriated investor funds for his personal benefit.

3. Further, Defendants Tao and Boyd acted as unregistered brokers in violation of Section 15(a) of the Securities Exchange Act of 1934 (the “Exchange Act”) when they offered and sold units in PVC. Section 15(a) requires brokers to be registered with the Commission or to be associated with a registered broker. Defendants did not register, and because they were offering and selling the PVC interests outside of their employment with the Registered Firm (a/k/a “selling away”), their association with the Registered Firm did not cover the transactions at issue.

4. As a result of this misconduct, Defendants Tao and Boyd should be enjoined from violating the relevant securities laws they violated as alleged herein, Tao should be further enjoined from soliciting or accepting funds in unregistered offerings of securities, Tao should be required to disgorge all ill-gotten gains with prejudgment interest, and both Defendants should be ordered to pay appropriate civil penalties.

JURISDICTION AND VENUE

5. This Court has jurisdiction over this action pursuant to Sections 20(b), 20(d)(1), and 22(a) of the Securities Act of 1933 (“Securities Act”) [15 U.S.C. §§ 77t(b), 77t(d)(1), &

77v(a)], Sections 21(d)(1), 21(d)(3)(A), 21(e), and 27 of the Securities Exchange Act of 1934 (“Exchange Act”) [15 U.S.C. §§ 78u(d)(1), 78u(d)(3)(A), 78u(e), & 78aa], and Sections 209(d) and 214 of the Investment Advisers Act of 1940 (“Advisers Act”) [15 U.S.C. §§ 80b-9(d) & 80b-14]. Defendants have, directly or indirectly, made use of the means or instrumentalities of interstate commerce and/or the mails in connection with the transactions, acts, practices, and courses of business alleged in this Complaint.

6. Venue is proper in this district pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)], Section 27 of the Exchange Act [15 U.S.C. § 78aa], and Section 214 of the Advisers Act [15 U.S.C. § 80b-14]. Certain of the transactions, acts, practices, and courses of conduct constituting violations of the federal securities laws occurred within this district. Among other things, Defendants offered and sold the securities at issue in this district, and they also reside in this district.

DEFENDANTS

7. Defendant James C. Tao is an individual residing in Houston, Texas.

8. Defendant Donna Boyd, who was known during some or all of the relevant time period as Donna Chen, is an individual residing in Houston, Texas.

FACTUAL ALLEGATIONS

A. Defendants “Sell Away” the PVC Offering

9. From late 2012 through March 2016, Tao and Boyd were financial advisers and registered representatives associated with the Registered Firm, which is an SEC registered investment adviser and broker-dealer based in Houston, Texas. Tao and Boyd operated a branch office of the Registered Firm located in the Westchase area of Houston, Texas, that serviced more than 120 financial advisory clients. Defendants received compensation for and were

engaged in the business of directly advising Registered Firm advisory clients as to the value of securities and the advisability of investing in, purchasing, or selling securities.

10. In August 2012, and while associated with the Registered Firm, Defendants formed and co-founded PVC, a Texas limited liability company and private equity fund that does business as Presidio Venture Capital. Defendants claimed they started PVC primarily for the purpose of investing in technology start-up companies in the Houston, Texas area.

11. Defendants' original business model was to advise their advisory clients to break off "a sleeve" of their accounts with the Registered Firm to invest in PVC as an alternative investment. The Registered Firm had a process in place for vetting and approving alternative investments, but Defendants chose not to submit PVC to the Registered Firm for consideration. Instead, Defendants solicited investments in PVC on their own and without the Registered Firm's knowledge, which is known in the industry as "selling away." Defendants then concealed the nature of their PVC activities from the Registered Firm, because they knew they would get in trouble with the Registered Firm if it found out they were "selling away" an unapproved alternative investment to firm clients. Tao and Boyd also did not register as brokers.

12. Defendants began raising funds for PVC in January 2013. After a personal falling-out with Tao, Boyd stopped her involvement with PVC in approximately mid-2013, but Tao continued to raise funds until approximately July 2016. In total, Defendants—and primarily Tao—raised approximately \$860,000 for PVC for the accounts of approximately 25 investors located in multiple states. Approximately 14 of these investors were also Defendants' advisory clients at the Registered Firm (approximately 12 of Tao's clients and 2 of Boyd's clients), and one or more of the investors were brokerage customers of the Registered Firm. In exchange for their investments, which ranged from approximately \$5,000 to \$200,000, investors received

membership units in PVC. Defendants also contributed their own capital, bringing the fund total to just over \$1 million.

13. Defendants identified and solicited potential investors from their advisory clients and brokerage customers at the Registered Firm and their personal and business contacts. Defendants conducted in-person sales meetings with potential investors, negotiated and closed the investment sales, advised the investors on the merits of the investment, and were the only points of contact between the investors and PVC. Defendants solicited investments in PVC pursuant to the terms of a Private Placement Memorandum (“PPM”) and other marketing materials that were distributed to investors. Tao was responsible for, approved and authorized, and had ultimate authority over the statements in PVC’s PPM, marketing materials, and operative documents.

14. Tao and Boyd were PVC’s initial managing members. Boyd ended her active involvement with PVC in 2013, but formally remained a managing member until April 2016. Tao has served as a PVC managing member since the company’s formation, and as the fund’s sole managing member following Boyd’s time as a managing member. Further, Tao, who acted as an investment adviser to his advisory clients at the Registered Firm, also acted as an investment adviser to the fund itself and, therefore, owed the fund and investors a fiduciary duty. Tao advised the fund on how to invest fund assets and claimed a right to receive management fees from the fund and a 20% share of the fund’s profits as compensation. The fund investors were to split the remaining 80% of the profits in accordance with their respective unit ownership interests.

15. The PVC membership units that Defendants offered and sold are investment contracts and thus securities within the meaning of the Securities Act and the Exchange Act.

The investors paid money to purchase the units, and their funds were pooled together and used by PVC to make investments. Additionally, the investors expected to receive profits from their investments based solely upon the efforts and expertise of Defendants and PVC. The units were passive investments, and the investors had no role in the operation or management of PVC. In fact, the PPM states that “the managing members will control our Company,” the investors “are not entitled to any voting rights in the Company nor any control of the Company,” and “[o]ur success will be dependent on the personal efforts of the Company’s managing members.”

B. Tao Misrepresents The PVC Offering

16. The PPM set a Minimum Offering Amount of \$2.5 million and stated that the offering was made on an “all or none” basis until the minimum was raised. Specifically, the PPM represented that, until \$2.5 million was raised, proceeds would be held in escrow with the company’s bank. The PPM further represented that “if at least 500 Units are not sold before the expiration date of this offering ... [PVC] will fully refund all of the subscription funds received, without deduction for offering expense and with the interest, if any, earned while the funds were held in trust.” These representations were material as they led investors to believe that their funds were being safeguarded and would be invested only if PVC raised sufficient capital to execute the fund’s investment plan and maintain a diverse and balanced investment portfolio.

17. The representations, however, were false. Tao did not establish an escrow account for the offering. Instead, he completely disregarded the escrow provisions and began deploying investor funds soon after they were received, starting with an initial investment of \$240,000 in a medical company in March 2013. Indeed, Tao knew PVC failed to ever raise even half of the Minimum Offering Amount, but he invested or spent substantially all of the investor funds anyway.

18. The PPM further indicated that investor funds would be used to invest in private companies and real estate developments, and Tao pitched the offering as an alternative investment that would focus on local technology start-ups. While some of the money PVC raised was invested in arms' length transactions that fit the stated business model, Tao, from the inception of the fund, intended to and did invest PVC funds in his own companies or companies in which he had a personal interest. Tao ultimately used more than \$200,000 of the funds raised to start or benefit these companies, including an EB-5 venture, a health-care company, and a concert promotion business.

19. Tao, who owed fiduciary duties to his advisory clients, failed disclose this clear conflict of interest when he solicited investments in the fund and instead falsely led investors to believe their money would be invested in independent ventures. Later, Tao buried references to certain of his personal interests in attachments to investor letters, but never made a full and appropriate disclosure of the conflicts. Tao's omissions about his conflicts of interest were material, as a reasonable investor would undoubtedly consider the fund manager's lack of independence important in deciding whether to invest.

20. Further, the PVC marketing materials that Tao used to solicit one or more of the investors touted a 12% historical rate of return. The claimed rate of return, however, was false and misleading. Tao came up with the figure by using "internet research" to calculate the average rate of return for *all* private equity funds over the past two decades—the 12% bore no connection to the historical experience of PVC or its managers. Representations about a fund's past performance are material and often critical to an investor's decision to invest.

C. Tao Misuses and Misappropriates Investor Funds

21. One of the first things Tao did with the investor funds was to pay a \$40,000 loan origination fee in 2013 to the relative of a PVC employee. Because PVC had not raised as much money as anticipated, Tao decided to seek a business loan of up to \$4 million to increase the amount of money under management in the fund. Tao planned to invest the loan proceeds in PVC and treat them as interests assigned to himself, Boyd, and three other colleagues. In other words, Tao improperly used PVC investor money in an attempt to fund a loan to increase his and other insiders' ownership interests in the fund. Tao knew that the PPM did not authorize him to use investor funds for this purpose, but he did it anyway and did not tell investors.

22. To make matters worse, after taking the \$40,000 fee, the employee's relative disappeared without ever delivering the promised loan. Tao then misled investors about the use of the funds and the reason for the \$40,000 loss. In an April 2014 Quarterly Update to investors, Tao wrote that PVC had experienced its "first and only complete loss" related to an investment in a housing community, because the sponsors of the project were not able to successfully launch the project. The housing project, as Tao knew, had nothing to do with the \$40,000 loss.

23. Then, in early 2016, the Registered Firm received a complaint from one of its clients that invested in PVC. The Registered Firm initiated an internal investigation and uncovered Defendants' outside business activities and selling away. As a result, the Registered Firm terminated Defendants in March 2016. Tao paid approximately \$75,000 as a return of principal to the disgruntled investor. Because Tao did not have enough cash on hand at PVC to return the investor's principal, Tao raised \$35,000 from two new PVC investors in 2016 and used their money to repay the earlier investor. Tao knew he intended to use the new investor funds to pay back the earlier investor at the time he solicited their investments, but he did not

disclose this material fact to the new investors and instead led them to believe their investment would be used to fund investments in accordance with the terms of the PPM. Pursuant to the PPM, the investor funds should have been used to invest in private companies, not for Tao to buyout dissatisfied investors.

24. Tao also used PVC funds to buy out at least three other PVC investors in 2016. All of these buyouts violated the “Redemption Guidelines” section of the PPM, which states that “[n]o redemptions will be permitted in the first two years after the close of the initial offering,” which had not yet occurred. Furthermore, using fund money to buy out investors reduced the amount of money in the fund and resulted in an even larger gap between the funds actually under management and the purported minimum offering amount.

25. As discussed above, Tao also misused investor funds by investing more than \$200,000 in companies he owned or in which he had a personal interest. In addition, Tao misused investor funds to pay for various expenses unrelated to uses authorized in the PPM. For example, he spent approximately \$7,500 organizing a conference on marijuana industry investing, approximately \$10,000 purchasing penny stocks, approximately \$4,600 buying products from a Vietnamese coffee company to sell online, and approximately \$1,600 paying for legal expenses and fees unrelated to PVC.

FIRST CLAIM FOR RELIEF

Violations of Section 17(a) of the Securities Act (against Defendant Tao)

26. The Commission reallages and incorporates by reference each and every allegation contained in the paragraphs above.

27. By engaging in the conduct described herein, Defendant Tao, directly or indirectly, singly or in concert with others, in the offer or sale of securities, by use of the means and instrumentalities of interstate commerce and/or by use of the mails has: (a) employed devices, schemes, and artifices to defraud; (b) obtained money or property by means of untrue statements of a material fact and omitted to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and (c) engaged in transactions, practices, and courses of business which operate or would operate as a fraud and deceit upon the purchasers.

28. With regard to his violations of Section 17(a)(1) of the Securities Act, Defendant Tao acted with scienter and engaged in the referenced acts intentionally, knowingly, and/or with severe recklessness. With regard to his violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act, Defendant Tao acted at least negligently.

29. By reason of the foregoing, Defendant Tao has violated and, unless enjoined, will continue to violate Section 17(a) of the Securities Act [15 U.S.C. § 77q].

SECOND CLAIM FOR RELIEF

Violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder (against Defendant Tao)

30. The Commission reallages and incorporates by reference each and every allegation contained in the paragraphs above.

31. By engaging in the conduct described herein, Defendant Tao directly or indirectly, singly or in concert, by the use of the means or instrumentalities of interstate commerce and/or or by use of the mails, in connection with the purchase or sale of securities, knowingly or recklessly: (a) employed devices, schemes, and artifices to defraud; (b) made

untrue statements of a material fact and omitted to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and (c) engaged in acts, practices, and courses of business which operate or would operate as a fraud and deceit upon purchasers, prospective purchasers, and any other persons.

32. Defendant Tao acted with scienter and engaged in the referenced acts intentionally, knowingly, and/or with severe recklessness.

33. By reason of the foregoing, Defendant Tao violated and, unless enjoined, will continue to violate Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

THIRD CLAIM FOR RELIEF

Violations of Sections 206(1), (2) and (4) of the Advisers Act and Rule 206(4)-8 thereunder (against Defendant Tao)

34. The Commission reallages and incorporates by reference each and every allegation contained in the paragraphs above.

35. Defendant Tao, directly or indirectly, singly or in concert, through the use of the mails or any means or instrumentality of interstate commerce, while acting as an investment adviser within the meaning of Section 202(11) of the Advisers Act [15 U.S.C. § 80b-2(11)] has (a) employed devices, schemes, and artifices to defraud any client or prospective client; (b) has engaged in acts, practices, and courses of business which operate as a fraud or deceit upon any client or prospective client; and (c) engaged in acts, practices, and courses of business which are fraudulent, deceptive, or manipulative.

36. PVC was a pooled investment vehicle under Rule 206(4)-8 of the Advisers Act, because, but for certain excluded exemptions, it falls within the definition of an investment

company, because it proposed to engage in and did engage in the business of investing, reinvesting, owning, holding, or trading in securities, and owns or proposes to acquire investment securities having a value exceeding 40% of the value of its total assets.

37. With regard to his violations of Section 206(1) of the Advisers Act, Defendant Tao acted with scienter and engaged in the referenced acts intentionally, knowingly, and/or with severe recklessness. With regard to his violations of Sections 206(2), 206(4) and Rule 206(4)-8(a)(1), Defendant Tao acted at least negligently.

38. By reason of the foregoing, Defendant Tao has violated, and unless enjoined, will continue to violate Sections 206(1), (2), and (4) of the Advisers Act [15 U.S.C. §§ 80b-6(1)-(2)] and Rule 206(4)-8 thereunder [17 C.F.R. § 275.206(4)].

FOURTH CLAIM FOR RELIEF

Violations of Section 15(a) of the Exchange Act (against Defendants Tao and Boyd)

39. The Commission reallages and incorporates by reference each and every allegation contained in the paragraphs above.

40. Defendants Tao and Boyd each acted as brokers within the meaning of Section 3(a)(4) of the Exchange Act [15 U.S.C. § 78c(4)], and made use of the mails or the means or instrumentality of interstate commerce to effect transactions in, or to induce or attempt to induce the purchase or sale of, the securities alleged above.

41. Defendants Tao and Boyd were not registered with the Commission in accordance with Section 15(b) of the Exchange Act [15 U.S.C. § 78o(b)], and Defendants' association with the Registered Firm did not exempt Defendants from registration for the transactions at issue as

such transactions were not made in the scope or course of Defendants' employment with the Registered Firm.

42. By reason of the foregoing, Defendants Tao and Boyd violated, and unless enjoined will continue to violate, Section 15(a) of the Exchange Act [15 U.S.C. § 78o(a)].

RELIEF REQUESTED

Therefore, the Commission respectfully requests that this Court:

- (a) Permanently enjoin Defendant Tao and his agents, servants, employees, attorneys and all persons in active concert or participation with him who receive actual notice of the injunction by personal service or otherwise, from violating, directly or indirectly, Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5], and Sections 206(1), (2), and (4) of the Advisers Act [15 U.S.C. §§ 80b-6(1),(2), (4)] and Rule 206(4)-8 thereunder [17 C.F.R. § 275.206(4)];
- (b) Permanently enjoin Defendant Tao and his agents, servants, employees, attorneys and all persons in active concert or participation with him who receive actual notice of the injunction by personal service or otherwise, from, directly or indirectly, including, but not limited to, through any entity owned by or controlled by Tao, soliciting or accepting funds from any person or entity for any unregistered offering of securities;
- (c) Permanently enjoin Defendants Tao and Boyd and their agents, servants, employees, attorneys and all persons in active concert or participation with them who receive actual notice of the injunction by personal service or

otherwise, from violating Section 15(a) of the Exchange Act [15 U.S.C. § 78o(a)];

- (d) Order Defendant Tao to disgorge all ill-gotten gains and/or unjust enrichment realized by him, plus prejudgment interest;
- (e) Order Defendants Tao and Boyd to each pay an appropriate civil monetary penalty pursuant to Section 20(d) of the Securities Act [15 U.S.C. § 77t(d)], Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)], and/or Section 209(e) of the Advisers Act [15 U.S.C. § 80b-9(e)]; and
- (f) Grant such further relief as this Court may deem just and proper.

Dated: December 5, 2017

Respectfully submitted,

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CERTIFICATE OF SERVICE

Defendants have waived service of summons and this complaint. *See* signed Consents attached as Exhibit A to Plaintiff's Unopposed Motion for Entry of Final Judgement against Defendant Tao and Plaintiff's Unopposed Motions for Entry of Final Judgement against Defendant Boyd filed contemporaneously herewith. I further certify that on December 5, 2017, I caused the foregoing to be served by U.S. Mail and email to the following:

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