

**ADMINISTRATIVE PROCEEDING
BEFORE THE
SECURITIES COMMISSIONER OF MARYLAND**

IN THE MATTER OF: *

Capital Investment Group, Inc. * Securities Division No. 2012-0297

RESPONDENT *

* * * * *

CONSENT ORDER

WHEREAS, the Securities Division of the Office of the Maryland Attorney General (the "Securities Division"), pursuant to the authority granted in section 11-701 of the Maryland Securities Act, Title 11, Corporations and Associations Article, Annotated Code of Maryland (2014 Repl. Vol. and 2016 Supp.) (the "Securities Act"), undertook an investigation into Capital Investment Group, Inc.'s ("CIG" or "Respondent") supervision of Joseph Giordano ("Giordano"), a registered representative formerly affiliated with CIG, and

WHEREAS, on the basis of that investigation, the Maryland Securities Commissioner (the "Commissioner") has found that grounds exist to conclude that CIG violated the Securities Act by failing to reasonably supervise Giordano who offered and sold unregistered securities and sold securities that were unsuitable for some investors; and

WHEREAS, the Commissioner and Respondent have reached an agreement in this action whereby Respondent without admitting or denying any findings of fact or conclusions of law except to admit to the jurisdiction of the Commissioner in this matter and over it in this matter, consents to the terms of this Consent Order; and

WHEREAS, Respondent waives its right to a hearing and any rights it may have to seek judicial review or otherwise challenge or contest the terms and conditions of this Consent Order; and

WHEREAS, the Commissioner has determined that it is in the public interest to issue this Consent Order;

NOW, THEREFORE, THE COMMISSIONER FINDS, CONCLUDES, AND ORDERS:

I. JURISDICTION

1. The Commissioner has jurisdiction in this proceeding pursuant to section 11-701.1 of the Securities Act.

II. RESPONDENT

2. CIG maintains its principal place of business in North Carolina but, through its registered representatives, also maintains branch and/or non-branch offices in Maryland. At all times relevant to this matter, Giordano worked out of a CIG-office in Annapolis, MD. CIG has been registered as a broker-dealer with the Financial Industry Regulatory Authority ("FINRA") and the Securities and Exchange Commission since 1984 and with the Securities Division since January 1990.

III. FINDINGS OF FACT

A. Offer and Sale of Unregistered Securities

3. In or about October 1992, Giordano joined CIG. CIG registered him as a registered representative with the FINRA and as an agent with the Securities Division. A few years later, he became a principal for CIG.

4. During the early 1990s, Giordano met Wilfred Azar III ("Azar") and developed both a personal and a business relationship with him.

5. A few years later, Azar became a brokerage client of CIG and Giordano.
6. In or about 1999, Azar purchased from his grandfather a majority interest in Empire Corporation, a real estate management and development company.
7. That same year, Azar approached Giordano about custodying bonds issued by Empire Corporation, known as Empire Corporation Senior Subordinated Debenture - Interest Compounded Monthly @ 10% ("Empire debentures" or "debentures").
8. Azar's sister-in-law and brother-in-law wanted to purchase bonds issued by Empire Corporation to hold in their individual retirement accounts, and Azar was looking for a custodian to hold the bonds.
9. According to Giordano, at that time he approached CIG and Sterne, Agee & Leach, Inc. ("SAL"), CIG's clearing broker-dealer, to determine if and how the Empire debentures could be custodied with SAL, and SAL provided Giordano with the procedures for establishing individual retirement accounts to hold the Empire debentures.
10. CIG states that it has no record of being approached by Giordano during this time period; however, the bonds were processed through CIG's clearing broker-dealer, SAL.
11. Giordano assisted Azar's sister-in-law and brother-in-law in purchasing and establishing accounts at SAL to hold the Empire debentures. Subsequently, Giordano assisted other clients in establishing accounts at SAL and purchasing the Empire debentures.
12. Giordano initially offered the Empire debentures only to those who had a pre-existing relationship with Azar, such as friends and family of Azar.
13. During the Winter of 2006, CIG conducted an on-site audit of Giordano's office which, at the time of the audit, was an OSJ branch office of CIG.

14. Following the on-site visit, Bill Portwood, CIG's former Chief Compliance Officer ("CCO"), sent Giordano a deficiency letter dated February 14, 2006 noting the sale of Empire debentures.

15. At that time, Giordano had effected approximately six Empire securities transactions totaling \$322,501 for Azar and Azar's referrals.

16. In his deficiency letter to Giordano, Portwood noted that Giordano's sales of Empire Corporation debentures had not been approved by Portwood, when he wrote: "All private placements require my prior approval before any sales are made or offers made to prospective clients. Prior approval was not received for this private placement unless it was received prior to my arrival."

17. In a February 16, 2006 e-mail to Portwood, responding to Portwood's issue regarding the Empire debentures, Giordano, in part, wrote:

For your records, we have made these bonds available to our clients since October 2002. Lisa Brittain (formerly of Capital Investment Group) and Frank Powell (Sterne Agee & Leach) have each given us their permission and have helped us develop procedures to process these transactions and maintain these securities . . . Furthermore, **we do not receive compensation of any kind for handling these transactions.** I am the only investment representative in our office permitted to provide the availability these bonds to our clients and **I do not solicit them.** *Emphasis added.*

18. Giordano also informed Portwood that the securities would be listed on clients' CIG brokerage statements.

19. A few days later, on February 21, 2006, in an email to Giordano, Portwood wrote: "I have no further questions. I understand. You can continue to sell such bonds on an **unsolicited basis.**" *Emphasis added.*

20. In a January 5, 2010 email to CIG's current CCO, Ronald King, Portwood recalled that the bonds were to be offered to limited investors who were accredited and sophisticated, Portwood wrote, in part:

Based on recollection, it was roughly about 2006 when we discussed him potentially offering the debt security to family, friends, and those individuals close to Empire Corporation (in other words **accredited/sophisticated investors**). As I recall, we worked with Sterne Agee to ensure the security could be custodied there if so chosen by the client. I am also confident that I conversed with . . . [management] to receive [management's] ok, given the nature and characteristics of the security and Joe's length of tenure with Capital.

To the best of my knowledge, the approval was granted after a thorough examination of the offering, conversations with . . . [management] and the knowledge that the broker in question (Giordano) had a reputation of being very ethical, honest, and forthright in his dealings with clients and Capital, including Compliance. Regardless, I know Joe was previously given the ok to offer the security. *Emphasis added.*

21. There is no evidence to indicate that Portwood or CIG took reasonable steps to determine if the debentures being offered by Giordano were registered or subject to an exemption from registration.

22. Despite CIG's stipulation that the securities continue to be offered on an unsolicited basis only, beginning in or about the Spring of 2006, Giordano began offering the debentures to investors not previously associated with Azar, including Giordano's friends and his CIG brokerage clients. Despite Giordano's representations to Portwood that he did not "receive compensation of any kind for the handling these transactions," Giordano began receiving compensation in connection with the Empire debentures, and didn't seek CIG's approval for the changed circumstances. Giordano did not disclose to his broker-dealer, CIG, the substantial payments he received from Empire Corporation and Azar.

23. Between Spring of 2006 and 2009, Giordano raised more than \$2,000,000 from more than 30 investors.

24. Despite the significant increase in sales of the debentures during that time, CIG failed to take any additional steps to determine if Giordano was abiding by the restrictions imposed by CIG and the representations made by Giordano.

25. In December 2009, Giordano's branch office was again audited by CIG's home office. The audit was conducted by CIG's current CCO, Ronald King ("King").

26. During the audit, King discovered that Giordano was offering the Empire debentures to CIG's clients.

27. King asked Giordano why he was offering the debentures. Giordano told King that Portwood had approved the offering on an unsolicited basis. Giordano further told King that he was not getting any compensation in connection with the debenture offering. However, as noted above, Giordano offered the debentures on a solicited basis and received compensation in connection with the debenture offering.

28. King expressed concerns regarding the Empire debenture offering including, but not limited to, the lack of financial statements provided and the lack of registration, and instructed Giordano to immediately cease offering and selling the Empire debentures.

29. Empire Corporation began experiencing difficulty making payments to investors.

30. In October 2010, Empire Corporation's parent company, Empire Holdings Corporation, filed for bankruptcy.

B. Unsuitable Investment Recommendations

31. The Empire debentures were not suitable investments for some of CIG's clients.

32. The debentures were high-yield unsecured subordinated debt investments.

33. In sworn testimony before the SEC, Giordano was asked if he considered making an individual investment in the bonds. Giordano responded, "I'm not an accredited investor. I was not eligible."

34. Yet, Giordano solicited and sold the debentures to several non-accredited and/or unsophisticated investors.

35. Based upon information contained in client new account forms, Giordano should have known that the debentures were unsuitable for some of his clients.

36. For example, the new account form for one investor showed that he had a net worth of \$400,000 and a liquid net worth of \$250,000. He worked as a produce manager for a grocery store and had an annual net income of \$58,000. His prior investment experience was limited to investing in mutual funds. The client was neither accredited nor sophisticated, yet he was solicited to invest \$30,000, more than 10% of his liquid net worth.

37. Another investor was a self-employed artist with an annual income of \$6,000. Her husband's income was listed at \$70,000. Her net worth and liquid net worth were listed as \$200,000 and \$10,000, respectively. She purchased \$5,000 worth of Empire debentures.

38. Other investors solicited by Giordano did not meet the accredited or sophisticated investor standard.

39. Giordano recommended investments that were unsuitable for some investors, and CIG failed to reasonably supervise those recommendations.

C. Investor Losses

40. At the time of Empire's bankruptcy filing, many of Giordano's clients who invested in the Empire debentures had not been repaid and, in the aggregate, incurred losses exceeding \$2 million.

41. Since that time, Respondent has made payments of approximately \$930,000 to some of those investors, while some investors have not been repaid.

IV. CONCLUSIONS OF LAW

The Commissioner concludes that:

42. Respondent failed to reasonably supervise Giordano's securities activities including Giordano's offering and selling of unregistered securities in violation of section 11-501 of the Securities Act and Giordano's dishonest and unethical practices of making unsuitable recommendations to clients; thereby grounds exist under section 11-412(a)(10) of the Securities Act for the Commissioner to issue an order to suspend or revoke Respondent's broker-dealer registration if she finds the order is in the public interest.

V. SANCTIONS

NOW THEREFORE, IT IS HEREBY ORDERED, and Respondent expressly consents and agrees:

43. Respondent shall cease and desist from failing to reasonably supervise its agents, which provides the Commissioner with grounds under section 11-412(a)(10) of the Securities Act to issue an order to suspend or revoke Respondent's broker-dealer registration if she finds the order is in the public interest.

44. Respondent is assessed a civil penalty pursuant to section 11.701.1(b)(4) of \$500,000 for the violations set forth in this Order. This civil penalty shall be reduced dollar for dollar by the amount of restitution made by Respondent to the investors that purchased Empire debentures through CIG and its former representative, Giordano ("Empire investors"). Payment of the civil penalty shall be made

in installments, as follows: \$75,000.00 contemporaneous with the issuance of this Order; and payments of \$75,000.00 each payable on or before January 1, 2017, April 1, 2017, July 1, 2017, October 1, 2017, January 1, 2018, and the balance on or before April 1, 2018, unless the \$500,000.00 is paid in full sooner. Payments shall be by check made payable to the “Office of the Attorney General” in accordance with the terms of this paragraph. These funds shall be distributed pro rata to the Empire investors by the Office of the Attorney General in a manner within its discretion subject to the receipt by Respondent of an acceptable release of civil liability from the Empire investors receiving payment from the Office of the Attorney General. The civil penalty imposed herein shall be waived completely if investors are repaid in full in accordance with the terms of this paragraph.

45. Respondent shall comply fully with the Securities Act and the regulations promulgated thereunder.

46. This Consent Order concludes the investigation by the Securities Division and any other action that the Commissioner could commence against the Respondent under applicable law as it relates to the Findings of Fact and violations set forth in this Consent Order.

47. This Consent Order is not intended to subject Capital Investment Group, Inc. or any of its affiliated entities or individuals, past and present, except for Joseph Giordano referenced herein (“Affiliates”) to any disqualifications contained in the federal securities laws, the rules and regulations thereunder, the rules and regulations of self regulatory organizations or various states’ or U.S. territories’ securities laws, including, without limitation, any disqualifications from relying upon the registration exemptions or safe harbor provisions. In addition, this Order is not intended to form the basis for any such disqualifications.

48. This Consent Order is entered into solely for the purpose of resolving this investigation, and is not intended to be used for any other purpose. For any person or entity not a party to the Consent Order, this Consent Order does not limit or create any private rights or remedies against Respondent or its Affiliates, limit or create any liability of Respondent or its Affiliates, or limit or create defenses of Respondent or its Affiliates to any claims. Nor does this Consent Order affect Respondent's or its Affiliates' right to take positions in litigation to which neither the Securities Division nor the Commissioner is a party.

VI. JURISDICTION RETAINED

49. Jurisdiction shall be retained by the Commissioner for such further orders and directions as may be necessary or appropriate for the construction or enforcement of this Consent Order.

50. If Respondent fails to materially comply with any term of this Consent Order, the Commissioner may institute administrative or judicial proceedings against Respondent to seek to enforce this Consent Order, to sanction Respondent for violating an Order of the Commissioner or for making a misrepresentation of material fact upon which this Consent Order was based, and may take any other action authorized under the Securities Act or under any other applicable law, including the issuance of fines or penalties as provided by the Securities Act. In any such proceeding in which, after an opportunity for a hearing, the Securities Commissioner or the court finds that Respondent has violated this Consent Order or made any material misrepresentations in their dealings with the Securities Division, the Securities Division may also seek other sanctions for the violations that initiated this matter. For the purpose of determining those sanctions, the Findings of Fact and violations of the Securities Act set forth in this Consent Order shall be deemed admitted, and may be introduced into evidence against Respondent.

51. In the event that judicial intervention in this matter is sought by the Commissioner or Respondent, subject matter jurisdiction will lie in the Circuit Court for Baltimore City pursuant to section 11-702 of the Securities Act. The Circuit Court for Baltimore City will have personal jurisdiction over Respondent pursuant to section 6-103(b) of the Courts and Judicial Proceedings Article, Title 6, Annotated Code of Maryland (2013 Repl. Vol. and 2016 Supp.). Venue will be properly in that Court pursuant to Section 6-201(a) and 6-202(11) of that article.

52. The terms of this Consent Order may be vacated or modified only by a subsequent order issued by the Commissioner.

SO ORDERED:

Commissioner's Signature on File
w/Original Document

Date: November 29, 2016

Melanie Senter Lubin
Securities Commissioner

BY CONSENT:

Capital Investment Group, Inc
by: Richard K. Bryant, Chief Executive Officer

_____, 2016
Date

Subscribed and sworn to before me
this ____ day of _____, 2016.

Notary Public
My Commission expires _____