

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2006006518903**

RECEIVED

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REGISTRATION & DISCLOSURE

TO: Department of Enforcement
Financial Industry Regulatory Authority ("FINRA")

RE: CIG Investment Group, LLC, Respondent
CRD No. 11853

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Respondent CIG Investment Group, LLC ("CIG" or "firm") submits this Letter of Acceptance, Waiver and Consent ("AWC") for the purpose of proposing a settlement of the alleged rule violations described in Part II below. This AWC is submitted on the condition that, if accepted, FINRA will not bring any future actions against it alleging violations based on the same factual findings.

I.

ACCEPTANCE AND CONSENT

- A. CIG hereby accepts and consents, without admitting or denying the findings, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to which FINRA is a party, prior to a hearing and without an adjudication of any issue of law or fact, to the entry of the following findings by FINRA:

BACKGROUND

CIG, CRD No. 11853, is a full service broker dealer, located in Chicago, IL that has been a FINRA member since 1983. The firm is a registered municipal securities dealer. The firm has three branch offices (Boca Raton, Boston, and New York) and currently employs about 82 registered persons. CIG has relevant disciplinary history. In June 2008, the firm was censured, fined \$75,000 and agreed to an independent consultant undertaking for multiple violations, including selling shares in a private placement offering, pursuant to an offering memorandum that contained material misrepresentations or omissions in violation of NASD Rule 2110 and failing to establish, maintain, and enforce an adequate supervisory system and procedures in violation of NASD Rule 3010 and 2110.

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OVERVIEW

During the relevant period of January through November 1, 2006, CIG, failed to establish and maintain an adequate supervisory system, including written procedures, to supervise the firm's trading and market making. In addition, under the firm's supervisory system, the firm's President, GR, who worked out of CIG's headquarters in Chicago, was the direct supervisor of a registered representative, Paul Benz ("Benz"), who worked out of his home in New Jersey, and a trader, Darren White ("White"), who worked out of his home in California. The firm failed to reasonably supervise Benz and White. As a result, CIG failed to detect or prevent Benz's manipulation of the price of the thinly traded common stock of South Texas Oil Company ("STXX") between April 24 and October 31, 2006. Benz and White, who aided and abetted Benz, manipulated STXX by making trades in the account of one of Benz's customers, CIL, and by making a market in STXX from August 29 through October 31, 2006. These activities contributed to the price of STXX increasing from \$0.35 to \$4.05, a gain of over 1,000%.

CIG also failed to establish and implement an AML compliance program reasonably designed to achieve compliance with NASD Conduct Rule 3011. Between January and November 1, 2006, CIG either failed to identify or ignored red flags involving numerous instances of potentially suspicious activities, including the suspicious wiring of funds into and out of the CIL account and suspicious trading in the account, and thus failed to investigate and report these activities in accordance with the firm's own procedures and the requirements of the Bank Secrecy Act and the implementing regulations thereunder. CIG should have detected the suspicious nature of the transactions in the CIL account, investigated the activity, and made the appropriate Suspicious Activity Report ("SAR") filings. Instead, CIG permitted the suspicious activity to occur and failed to report the activity to the appropriate authorities. As a result, CIG violated NASD Conduct Rules 3011(a) and (b), and 2110 and MSRB Rule G-41.

FACTS AND VIOLATIVE CONDUCT

I. The Firm's Supervisory and AML System and Procedures

A. Supervisory System and Procedures

Between early 2004 and December 12, 2007, GR, CIG's President, worked out of CIG's headquarters in Chicago, Illinois. Under the firm's supervisory system, GR was the direct supervisor of Benz, a broker, who worked out of his home in New Jersey, and White, a trader, who worked out of his home in California. GR's supervision and contact with Benz consisted of speaking with him approximately once or twice a month. His supervision and contact with White consisted of speaking with him about twice a week.

CIG did not have a system or procedures for supervising the firm's market making activities. GR was the firm's designated principal responsible for trading/market making. GR supervised the firm's trading activities by conducting a daily review of the firm's trade blotter for any trading improprieties. Beyond this, the firm did not have a system or procedures for

collecting and reporting trade data that provided assistance to GR or any other supervisor in detecting patterns of suspicious or improper trading.

Additionally, the written supervisory procedures that were in effect until late 2006 did not contain market making procedures. GR claimed that he used separate market making procedures, which were not part of the written procedures.¹ If the procedures existed during the relevant period, it does not appear they were made available to some of the most pertinent employees. For example, White did not receive these procedures until approximately November or December 2006.

Moreover, even if the market making procedures were available during any part of the relevant period to GR or CIG traders, they failed to provide reasonable guidance on how to detect and prevent market manipulations. For example, while the procedures instructed the designated supervisor to seek out patterns of trading that may indicate manipulation, such as “parking, wash sales, marking the close or other manipulative techniques” they failed to explain these terms or describe how the supervisor should go about identifying these types of activities. Additionally, the procedures provided that a branch office manager, a role analogous to the one performed by GR in supervising Benz and White, should be “sensitive to indications of . . . [m]arket [m]anipulation” but failed to explain what market manipulation is or how to detect and prevent it.

B. AML Systems and Procedures

The firm’s AML procedures were comprised largely of boiler plate language that was not tailored to CIG’s business. For example, there were no AML procedures that addressed the firm’s market making activities. The AML procedures did not contain procedures on how to monitor for and prevent money laundering. Further, the AML procedures did not explain what additional due diligence and other potential follow-up was required if a red flag of money laundering was detected, or when a Suspicious Activity Report (SAR) needed to be filed.

GR was the firm’s AML officer between 2002 and July 2006. GR viewed his job as AML Officer as essentially ensuring that the firm was collecting the appropriate customer identification information and running it through the Office of Foreign Asset Control (OFAC) list. In his role as AML Officer, GR claimed that he continuously monitored the activity of the firm, its clients, and its associated persons for possible AML violations. In that respect, his review was limited to reviewing the daily trade blotters. He did not review account activity. Furthermore, the firm did not have a system to track or monitor for suspicious money movement or patterns of suspicious trading activity. The firm has no documentation demonstrating any type of AML reviews by GR.

II. The Trading of STXX

Between April 24 and October 26, 2006, Benz and White engaged in manipulative

¹ During the investigation, the firm produced an undated version of written market making procedures, but could not specify when they were introduced.

trading in STXX, the common stock of South Texas Oil. The trading activity occurred in the account of CIL, a customer of Benz, and through one of CIG's proprietary trading accounts.

A. South Texas Oil Company

South Texas Oil is a Texas-based oil and gas exploration company. Its common stock, STXX, is a thinly traded over-the-counter bulletin board stock. Between February 2006 and April 23, 2006, the price of STXX swung between \$0.18 and \$0.49 on relatively little volume. During this time period, the total trading volume of STXX was 84,424 shares, an average of 3,377 shares per day on the 25 days STXX traded.

During the period prior to April 24, 2006, the publicity about the company was negative. On April 6, it was reported that South Texas Oil was experiencing cash flow problems and that its Operational Cash Flow Per Share ("OPS") ranking, had been lowered. Overall during the relevant period, the news about South Texas Oil was negative.²

B. The Hedge Fund's Interest in South Texas

In July 2005, South Texas Oil entered into a subscription agreement with a hedge fund (the "Hedge Fund"), where Benz's close relative was the controlling manager and Chairman and CEO of the hedge fund's asset management company. Under the subscription agreement, the Hedge Fund received \$2.3 million in convertible debentures. The agreement provided that the convertible debentures could be exercised at a price of \$.587 per share and be convertible into the number of shares equal to 45% of the equity of the fully diluted shares of the company. On the day before the agreement, STXX closed at \$.30.

C. The CIL Account

CIL had a corporate account at CIG with Benz as the registered representative on the account. One of the authorized users was a director of the Hedge Fund. The attorney for CIL was ON, who also was the attorney for the Hedge Fund, the registered agent for the Hedge Fund's asset management company, and the attorney for South Texas.

On January 31, 2006, ON, representing himself as the attorney for CIL, explained to CIG that he was holding certain of CIL's funds in his escrow account and provided wiring instructions for \$650,000 to be wired from his escrow account into the CIL account in two separate wires, one for \$400,000 and one for \$250,000.³

Two days later, on February 2, 2006, one of the authorized users of the CIL account,

² On August 8, 2006, one of the rare positive reports indicated that STXX had a net profit during July. However, also on August 8, stockdiagnostics.com reiterated an OPS rank of 8, the lowest possible value, placing it in a group of companies with the highest risk of going out of business. On August 30, 2006, there were reports that STXX had experienced a two-year high for cash flows and a two-year low for free cash flow. There were no press reports during September and October.

³ GR was notified of the transfer of \$250,000 when an operations' employee copied him on an e-mail to Benz and White asking the reason for the third-party transfer.

wired \$675,019.75 out of CIL to a bank account in New York.⁴

D. Trading of STXX

Between April 24, 2006 and October 31, 2006, approximately 2.4 million shares of STXX traded in the market and the closing price increased from \$0.35 to \$4.05, for a gain of 1,057%. Overall, this trading constituted 35% of the total volume in STXX and the majority of this trading was for the benefit of the CIL account. Benz directed CIL's account activity in STXX and CIG's trading in STXX.

The activity in STXX can be divided into two periods. Between April 24, 2006 and August 28, 2006, Benz directed White to execute transactions for the CIL account. Beginning on August 29, Benz directed White to make a market in STXX and also to continue to execute transactions for the CIL account. Benz and White's actions caused an artificial increase in the price of STXX.

1. April 24 – August 28, 2006

On April 24, the CIL account made its initial purchase of 60,000 shares of STXX, at prices between \$0.30 and \$0.35 per share, accounting for 42% of the total trading volume that day. The purchase was notable because it was more than double the total number of shares that traded during the 30 days prior to April 24.

Between April 25 and May 31, CIL bought an additional 109,800 shares at increasing prices from \$0.535 to \$1.41, the closing price on May 31. CIL did not sell any stock during this period. However, this activity helped boost the price of STXX to a level that allowed the Hedge Fund to exercise its convertible debentures in June and take control of South Texas Oil.

From June 1 through August 28, the CIL account bought an additional 104,000 shares of STXX and sold just over 70,000 shares. Overall, from April 24 to August 28, the closing price of STXX went from \$0.35 to \$1.94. The trading volume in the CIL account, which mainly consisted of purchases, made up 32.5% of the total market activity in STXX during this time.

2. August 29 – October 31, 2006

On August 29, at Benz's request, White began making a market in STXX. Between August 29 and October 31, CIG was an active market maker in STXX both in volume traded and bid movement. During this time, CIG's influence as a market maker contributed greatly to the inside bid increasing from \$1.70 to \$3.90. Benz directed White's trading of STXX and gave him instructions on where to set his quotes and how much to trade.

Immediately after becoming a market maker, on August 30 and August 31, CIG dominated the market. CIG was at the inside bid 95% of the time and was responsible for over

⁴ The form that employee used to authorize the transfer was sent by fax from the Hedge Fund's asset management firm to the Bahamas, before the employee sent it to CIG.

80% of the total volume of STXX transactions during these last two days of August. As a result, the price increased from \$1.90 to \$2.20, an increase of approximately 16%.

During August and September, the CIL account, as directed by Benz, continued its concentrated buying pattern, buying approximately 121,000 shares while selling only 45,000 shares. In October 2006, the CIL account sold 50,000 shares of STXX, without purchasing any additional shares. At the same time, Benz directed White to continue to buy STXX in CIG's inventory account. CIG bought 58,890 and sold 68,390 with other market makers.

From August 29 through October 31, 2006, CIG was at the inside bid 52% of the time and responsible for approximately 37% of the volume. The closing price on October 31 was \$4.05

On November 1, 2006, 72,169 shares of STXX were transferred into the CIL account directly from the Hedge Fund.

3. Suspicious Activity in CIL's Account

a. Transactions Without Apparent Business Purpose

CIL's buying and selling of STXX made little economic sense. During several periods, CIL alternated between buying and selling while holding a large number of shares in the account. For example, during June 2006, it purchased 41,027 shares of STXX and sold 58,000 shares while already holding 223,827 shares in the account. In September 2006, it purchased 48,800 shares and sold 45,000 shares of STXX while holding 347,807 shares. During the six-month relevant period, the CIL account bought 398,107 STXX shares and sold 238,680 shares.

Moreover, after CIL sold shares, it frequently bought them back at a higher price. For example, from the end of June through mid-July, CIL sold 70,800 shares of STXX at an average price of \$1.52 and then bought back 70,800 at an average price of \$1.92. During these sales and repurchases, CIL maintained a position of over 200,000 shares of STXX in the account. In addition, on the last two days of September, CIL sold 45,000 STXX at \$2.015 and then bought 28,800 STXX at \$2.26, before selling 50,000 more shares during October. These sales and repurchases occurred while CIL maintained a position of more than 300,000 shares.

b. Suspicious Money Movement in the CIL Account

In addition to the wire transfers into and out of the CIL account on January 30 and February 2, 2006, by late November, ON had authorized 12 other wire transfers out of the CIL account to the same ON Trust account at a bank in California. These wires, ranging from \$20,000 to \$213,000, totaled \$1,102,203. Overall, a total of \$650,000 was wired into the CIL account and \$1,777,223 was wired out.

III. **CIG's Failure to Supervise**

CIG failed to reasonably supervise Benz and White and the trading of STXX in the CIL

account and in the CIG market making account. As described above, the firm's supervisory system was not reasonable in that it required GR, who was in Chicago, to supervise White, who was in California, and Benz, who was in New Jersey. Furthermore, GR had minimal contact with both Benz and White. He spoke with Benz once or twice each month and spoke with White approximately twice per week.

CIG did not have a system or procedures for supervising the firm's market making activities. GR, the designated principal responsible for supervising the firm's market making and trading, supervised the firm's trading and market making merely by conducting a daily review of the firm's trade blotter.

As a result of CIG's inadequate supervisory system and procedures, the manipulative trading in the CIL account and in the CIG market making account were not detected or prevented.

IV. Failure to File SAR-SF Forms

Under CIG's AML procedures, suspicious transactions involving \$5,000 or more required further investigation. Yet, CIG did not conduct any investigation of any of the wire transfers. Furthermore, CIG failed to conduct any further AML review of the CIL account, despite the suspicious nature of CIL's trading in STXX and the suspicious money movements in the account. CIG either failed to identify or ignored red flags involving numerous instances of potentially suspicious activities, and thus failed to investigate and report these activities in accordance with the firm's own procedures and the requirements of the Bank Secrecy Act and the implementing regulations thereunder. CIG should have detected the suspicious nature of the transactions in the CIL account, investigated the activity, and made the appropriate SAR filings. Instead, CIG did not report the suspicious activity to the appropriate authorities.

V. Conclusion

By virtue of the above, CIG failed to establish and maintain a reasonable supervisory system, including written procedures, in violation of NASD Rules 3010(a) and (b), and 2110. In addition, CIG violated NASD Conduct Rule 3011(a) and (b), and 2110, and MSRB Rule G-41 by failing to establish and implement AML policies and procedures that could reasonably be expected to detect and cause the reporting of suspicious securities transactions and by failing to establish and implement policies, procedures, and internal controls reasonably designed to achieve compliance with the Bank Secrecy Act and the implementing regulations thereunder.

B. CIG also consents to the imposition of the following sanctions:

1. A censure;

2. A fine of \$150,000; and
3. An undertaking that within 60 days after this AWC is accepted by FINRA, CIG shall certify to District 8, through its President, that its AML policies and procedures are in compliance with NASD Conduct Rule 3011(a) and (b), and its system and procedures for trading and market making are reasonably designed to achieve compliance with applicable federal securities laws and FINRA Rules. Thereafter, CIG, through its President, shall certify its compliance with FINRA Rule 3011 to District 8 quarterly for one year.

The sanctions imposed herein shall be effective on a date set by FINRA staff.

The firm agrees to pay the monetary sanction upon notice that this AWC has been accepted and that such payment is due and payable. The firm has submitted an Election of Payment form showing the method by which it proposes to pay the fine imposed.

The firm specifically and voluntarily waives any right to claim that it is unable to pay, now or at any time hereafter, the monetary sanction imposed in this matter.

II.

WAIVER OF PROCEDURAL RIGHTS

CIG specifically and voluntarily waives the following rights granted under FINRA's Code of Procedure:

- A. To have a Formal Complaint issued specifying the allegations against it;
- B. To be notified of the Formal Complaint and have the opportunity to answer the allegations in writing;
- C. To defend against the allegations in a disciplinary hearing before a hearing panel, to have a written record of the hearing made and to have a written decision issued; and
- D. To appeal any such decision to the National Adjudicatory Council ("NAC") and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, the firm specifically and voluntarily waives any right to claim bias or prejudgment of the

General Counsel, the NAC, or any member of the NAC, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including acceptance or rejection of this AWC.

The firm further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of FINRA Rule 9143 or the separation of functions prohibitions of FINRA Rule 9144, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including its acceptance or rejection.

III.

OTHER MATTERS

The firm understands that:

- A. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by the NAC, a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs ("ODA"), pursuant to FINRA Rule 9216;
- B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against me; and
- C. If accepted:
 - 1. this AWC will become part of CIG's permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against the firm;
 - 2. this AWC will be made available through FINRA's public disclosure program in response to public inquiries about the firm's disciplinary record;
 - 3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with FINRA Rules 8310 and 8313; and
 - 4. The firm may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. The firm may not take any position in any proceeding brought by or on behalf of FINRA, or to which FINRA is a

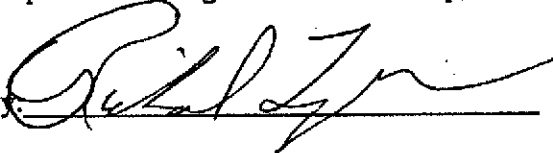
party, that is inconsistent with any part of this AWC. Nothing in this provision affects my right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.

- D. Respondent may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. The firm understands that it may not deny the charges or make any statement that is inconsistent with the AWC in this Statement. This Statement does not constitute factual or legal findings by FINRA, nor does it reflect the views of FINRA or its staff.

The undersigned, on behalf of the firm, certifies that a person duly authorized to act on its behalf has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that the firm has agreed to its provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce the firm to submit it.

April 20 09
Date

Respondent Chicago Investment Group, LLC

By 

Reviewed by:


James Kopecky, Esq.
James L. Kopecky, P.C.
190 S. LaSalle Street, Ste. 850
Chicago, IL 60603
(312) 380-6552
Counsel for Respondent

Accepted by FINRA:

5/15/09
Date

Signed on behalf of the
Director of ODA, by delegated authority

A handwritten signature in black ink, appearing to read 'Samuel L. Israel', written over a horizontal line.

Samuel L. Israel
Associate Vice President and Chief Counsel
FINRA Department of Enforcement
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Washington, D.C. 20006