

FINANCIAL INDUSTRY REGULATORY AUTHORITY

OFFICE OF HEARING OFFICERS

Department of Enforcement,

Complainant,

v.

CSSC Brokerage Services, Inc.
(CRD No. 141630)

and

Eric S. Smith,

Respondents.

DISCIPLINARY PROCEEDING
No. 2015043646501

COMPLAINT

The Department of Enforcement alleges:

SUMMARY

1. In 2015, Respondents CSSC Brokerage Services, Inc. ("CSSC") and Eric Smith defrauded investors by offering and selling securities through a "bridge loan" offering designed to keep their floundering parent company, CSSC, Inc. ("the Parent"), afloat after more than three years of failed deals, significant business losses and mounting debts that the Parent could not pay.

2. Smith, the CEO of the Parent and also the individual that controlled CSSC and its affiliates, knew of the Parent's precarious financial condition, yet misrepresented and failed to disclose that and other material information to potential and actual investors in the bridge loan offering.

3. In connection with the bridge loan offering, CSSC and Smith repeatedly violated Section 10(b) of the Securities Exchange Act of 1934 (“Exchange Act”) and Rule 10b-5 thereunder, Section 17 (a)(2)–(3) of the Securities Act of 1933, as well as FINRA Rules 2020 and 2010, by making misrepresentations and omissions of material facts to prospective investors. Specifically, Respondents did this by intentionally:

- a. failing to disclose that the Parent could not make interest payments to existing bondholders and investors without raising additional capital;
- b. failing to disclose that by May 2015, the Parent was in default to existing bondholders and investors and was unable to repay more than \$3 million that would eventually become due;
- c. misrepresenting that the Parent had earned, was receiving and would continue to receive millions of dollars in revenue from its development of a “special purpose bank” that ultimately failed to materialize and generate any revenue;
- d. touting a significant “revenue event” resulting from the Parent’s purported association with the South Dakota Trust Company, when no such relationship existed or ever occurred; and
- e. misrepresenting Respondents’ relationship with the City of Jacksonville, Florida, including that that relationship would increase CSSC’s assets under management by nearly \$1 billion, and generate “significant revenue,” when there was no basis in fact to make any such claims.

4. Moreover, CSSC and Smith’s conduct in making the foregoing misrepresentations and omissions of material facts also constituted a failure to observe high standards of commercial honor and just and equitable principles of trade, in violation of FINRA Rule 2010.

5. Furthermore, Smith engaged in the above misconduct both individually and on behalf of CSSC, despite not being registered with the firm, as Smith: (a) was the majority owner of both the Parent and CSSC; (b) directed the payment of expenses related to CSSC’s business and home office operations, including salaries, sales incentives/commissions, rent and other expenses; (c) made all hiring decisions regarding the registered representatives of CSSC; (d) directly supervised numerous CSSC registered representatives; (e) supervised transactions made by

CSSC customers; and (f) personally met with CSSC customers to discuss their investments, including to solicit investment in the Parent's prior bond offering and the bridge loan program.

6. As a result of Smith's management, employment decisions and sales and supervision through CSSC during the period May 2010 to December 2015, both Smith and CSSC also violated NASD Rules 1021 and 1031 by failing to properly register Smith as required by those rules.

RESPONDENTS AND JURISDICTION

A. CSSC Brokerage Services, Inc.

7. CSSC is a retail broker-dealer based in Troy, Michigan. It has been a FINRA member since December 2006. Its primary branch is in Troy, Michigan, and it operates in various states through its registered representatives.

8. CSSC is a wholly owned subsidiary of the Parent, which also owns two other active subsidiaries: CSSC Insurance Services, Inc., and CSSC Investment Advisory Services.

9. The Parent and all of its subsidiaries conduct business at the same office. One accounting department services the Parent and all subsidiaries. Weekly business meetings led by Smith are held at this office and include employees and registered representatives from all the CSSC entities meeting together.

10. CSSC's registered representatives are referred to as "Affiliates" of the Parent and its various subsidiaries. CSSC's registered representatives are independent contractors who sign an "Affiliate Agreement" when they join CSSC. The Affiliate Agreement is a contract between the individual registered representative, the Parent and each of the subsidiaries, including CSSC.

11. By virtue of its current FINRA membership, FINRA has jurisdiction over CSSC under Article IV of FINRA's By-Laws.

B. Eric S. Smith

12. Smith founded the Parent in Troy, Michigan in January 1998. Prior to founding the Parent, Smith practiced law in Kentucky.

13. Smith is the CEO, majority shareholder, and President of the Parent. He is also President of CSSC Investment Advisory Services.

14. Smith formed CSSC in May 2006, when the firm became a FINRA member. Smith has been an unregistered associated person of CSSC since that time, and he has never held any securities licenses.

15. Although he is not and has never been registered with FINRA, Smith is the majority owner of CSSC and controls all aspects of CSSC's business. This includes binding the Parent and CSSC to the Affiliate Agreements with CSSC's registered representatives, agreeing to submit any disputes with Affiliates to FINRA arbitration, regularly making the decisions to hire and fire Affiliates, and supervising the securities activity of CSSC's registered representatives.

16. As alleged below, Smith also personally met with multiple CSSC customers and sold securities to those customers between 2010 and 2016.

17. By virtue of Smith's current association with and duties on behalf of CSSC, FINRA has jurisdiction over Smith under Article XIII of its By-Laws.

FACTUAL BACKGROUND

A. CSSC's May 2010 Bond Offering

18. In May 2010, the Parent initiated a bond offering with the objective of raising operating funds for it and its subsidiaries, including CSSC (the "2010 Offering").

19. The Bonds issued in connection with the 2010 Offering had a five-year term, and stated that they would pay eight percent interest to investors on a biannual basis. The 2010 Offering was initially a private offering made available to shareholders and Affiliates of the Parent, but was later expanded and offered to a number of CSSC customers.

20. In 2013, Smith personally solicited two CSSC customers, PK and SM, to invest in the 2010 Offering. They invested \$200,000 and \$20,000, respectively.

B. CSSC's Ongoing Financial Difficulties and 2014 Offering of Bridge Loan Program

21. Despite raising \$2,635,000 through the 2010 Offering, the Parent continued to have financial difficulties. The Parent was unable to generate sufficient revenue in 2013 and 2014 to cover CSSC's expenses or those of its other subsidiaries, including the payment of commissions that CSSC owed to its registered representatives.

22. Smith was acutely aware of the Parent's ongoing financial difficulties. For example, on multiple occasions in 2013 and 2014 he personally notified CSSC registered representatives that their commissions would be delayed indefinitely due to cash flow problems, and in 2013 through 2015 he also determined that the Parent was not going to pay the salaries of its senior executives for an indefinite period of time.

23. As a result of the Parent's continued financial difficulties, Smith determined to again raise working capital for the Parent, this time through an Offering of Bridge Loans in May 2014 (the "2014 Bridge Loan Program").

24. Investments in the 2014 Bridge Loan Program were evidenced by a 12-month promissory note, which paid eight percent interest at maturity.

25. Smith prepared offering documents for the 2014 Bridge Loan Program (as he had done with the 2010 Offering), including those that described the financial condition of the Parent.

26. Smith and CSSC registered representatives raised \$1,100,000, through the 2014 Bridge Loan Program, when the firm was experiencing severe difficulties. The proceeds were used, in part, to pay off the firm's overdue American Express bill, and past due commissions owed to CSSC's employees. In fact, Smith instructed the accounting department of the Parent to pay these outstanding expenses immediately after customer RRM invested \$200,000 in the Bridge Loan Program.

C. CSSC's Financial Difficulties Continue and Smith Seeks New Sources of Funding for Operations

27. Notwithstanding the 2014 Bridge Loan Program, the Parent's financial difficulties continued and, in fact, became even more acute through the spring of 2015, when the Parent's 2010 Offering obligations started to become due. In May 2015, the Parent was obligated to redeem the first bonds issued in the 2010 Offering, but the Parent did not have the necessary capital to do so.

28. The Parent did not redeem any of the bonds issued from the 2010 Offering when they came due in 2015.

29. If bondholders contacted CSSC, Smith offered to convert their bonds into interests in the Bridge Loan Program.

30. By May 8, 2015, the Parent began defaulting on its payment obligation to investors in the 2014 Bridge Loan. By July 15, 2015, CSSC had defaulted on its payment obligation to a total of at least 10 bondholders and investors in the 2014 Bridge Loan Program, and the outstanding total amount owed by the firm to existing investors exceeded \$3.3 million dollars.

31. Smith and others at CSSC were aware of these defaults and knew that Respondents did not have sufficient capital to repay those obligations as it was contractually bound to do, and knew that the Parent still needed additional capital to fund ongoing operations.

32. As a result, Smith renewed his efforts to seek private investors, through a new Bridge Loan program in June 2015 (the “2015 Bridge Loan”), which Smith and CSSC representatives offered and sold to potential investors.

D. The 2015 Bridge Loan Offering

33. On June 15, 2015, in response to the Parent’s need for operating capital and to cure its default to the 2010 bondholders and to the 2014 Bridge Loan customers, CSSC through Smith, began soliciting the 2010 bondholders and other investors to participate in the 2015 Bridge Loan program.

34. Smith and CSSC offered and sold interests in the 2015 Bridge Loan through a series of offering documents that Smith drafted and distributed (“Offering Documents”).

35. The Offering Documents consisted of four separate versions of a “Confidential Report to Shareholders,” dated June 15, September 9, October 25 and November 2, 2015 (collectively “the Reports”), as well as six different versions of a document entitled “Important

Memorandum, To: Those Who May Be Considering Make a Bridge Loan to CSSC” between June and December 2015 (collectively, the “Bridge Loan Memos”).

36. In soliciting potential investors for the 2015 Bridge Loan, Smith provided the then-current version of both the Report and the Bridge Loan Memo to those investors.

37. Smith emailed the Offering Documents to registered representatives of CSSC, and other individuals from whom he sought capital. Smith sent the Offering Documents to CSSC registered representatives whom he thought would invest in the Bridge Loan Offering, and so these registered representatives could solicit potential investors.

38. When Respondents offered and sold the 2015 Bridge Loan to potential investors through the Offering Documents, they made numerous material misrepresentations and omissions.

1. Between June 15 and December 15, 2015, Smith and CSSC failed to disclose to investors the true, and dire, financial condition of Parent and CSSC in any of the Offering Documents

39. Respondents knew that the Parent and CSSC had defaulted on payment obligations to 2014 Bridge Loan investors and 2010 bondholders as early as May 8, 2015, and that CSSC had defaulted on its payment obligation to at least 10 bondholders and Bridge Loan investors by July 15, 2015.

40. Respondents and others at CSSC were also aware that Respondents did not have sufficient capital to repay those obligations as it was contractually bound to do, and that the Parent still needed additional capital to fund ongoing operations.

41. Despite this knowledge, Smith and CSSC failed to disclose these facts to any potential investors to whom they offered and sold the 2015 Bridge Loan.

42. Smith and CSSC did not disclose in any of the Offering Documents these defaults, the approximately \$3.3 million that was due and owed to previous investors, or the fact that the ongoing operations of the Parent and CSSC were dependent upon obtaining additional capital through the 2015 Bridge Loan.

43. Information about these defaults, the outstanding amount due and owed to previous investors, the inability to repay existing investors, and the overall dire financial state of the Parent and CSSC was material information that should have been, but was not, fully disclosed to investors in the Offering Documents.

2. Between June 15 and December 15, 2015, Smith and CSSC Misrepresented and Failed to Disclose Facts Related to a Special Purpose B Program, code-named “Project X”

- a. Between June 15 and September 9, 2015, Smith and CSSC misrepresented to investors that CSSC would receive nearly \$1.4 million in consulting fees from Project X

44. In the Offering Documents that Smith sent to potential investors between June 15 and September 9, 2015, Smith misrepresented the firm’s business relationships and the development of special purpose banks, as well as the revenue that Respondents would receive as a result of establishing those banks. Respondents also omitted from the Offering Documents material information required to make Smith’s other statements not misleading.

45. Specifically, the June Report that Respondents used to offer and sell the 2015 Bridge Loan to investors stated that “CSSC is being paid a \$1 million consulting fee for its work on the design and formation of this new [Special Purpose] Bank,” and that “one half of that fee has now been earned and should be received very soon.”

46. Through the June Report, Respondents also touted the creation of additional special purpose banks that would purportedly create even more revenue for CSSC. That Report also told investors that “CSSC expects to receive the full consulting fee for the first Bank during 2015, plus

at least one half of the consulting fee for the second Special Purpose Bank amounting to \$400,000 during 2015, for a total bank design-related consulting fee-income to CSSC of \$1.4 million in 2015”, which would **“ensure that 2015 ... will be the most profitable year in CSSC’s history.”** (emphasis in the original)

47. Smith reiterated these misrepresentations to potential investors in the July 12, 2015 Bridge Loan Memo, again stating that CSSC “is being paid a \$1 million consulting fee,” and stood to earn additional fees from a second bank, both of which would **“ensure that 2015 is not only profitable, but also that it will be the most profitable year in CSSC’s history.”** (emphasis in the original)

48. These statements were false and Smith knew they were false: CSSC was not party to any consulting agreement paying a fee of \$1 million, and the bank in Florida, Project X, had not been completed. Smith was also aware there had been no development of a second bank that would pay CSSC \$400,000 in 2015.

49. At the time that Respondents made and distributed these statements to investors, CSSC had not earned, did not have any right to receive, and did not have any agreement in place allowing it to receive, consulting fees related to Project X. Indeed, there was not even a proposed schedule of fees that CSSC could conceivably be paid as a result of Project X.

50. Moreover, CSSC’s and Smith’s failure to disclose to investors that: i) CSSC did not have any agreement giving it the right to receive the touted “consulting fees,” and ii) that CSSC was unable to fund Project X without additional financing, were each omissions of material facts necessary to make Respondents’ other statements not misleading.

51. Following their receipt of these Offering Documents, investor TL invested \$50,000 in the July 12, 2015 Bridge Loan Offering on August 23, 2015. Investor TS, who was a registered representative of CSSC, invested \$20,000 on August 30, 2015.

- b. Between September and December 2015, Smith continued to misrepresent and omit material information related to the status of, and revenue generated by, Project X

52. By August 2015, CSSC had not received a single dollar of the “consulting fees” Respondents told investors “had been earned” and were “being paid.” Project X had, by that time, effectively stalled and Smith knew that no consulting agreement had been executed. Notwithstanding, Respondents prepared an updated Report in September 2015 and continued to prepare revised Bridge Loan Memos in September, October, and November 2015.

53. Each of these documents, which Respondents drafted and distributed to potential investors in offering and selling the 2015 Bridge Loan, also contained material misstatements and omissions about the financial conditions and prospects of CSSC and the Parent.

54. Rather than providing full, complete and accurate information related to Project X in the September Report and the September Bridge Loan Memo, Respondents instead claimed that the delays related to the promised Project X revenues resulted from intentional interference with the project.

55. Specifically, Respondents represented to investors in the September Report that: **“CSSC was deprived of an expected \$2.15 million in funds...”** (emphasis in the original) as a result of this interference and that CSSC **“is currently evaluating available remedies for the damage caused to the Company.”**

56. Smith, moreover, also told investors that revenue from Project X was still viable, and only delayed. **“While we believe that it may still be possible to salvage the “HealthPro” special purpose bank concept, implement it, and generate the hoped for revenue from it,**

that now appears unlikely to take place within the 4th quarter of 2015.” (emphasis in the original)

57. These statements were false and Smith knew that they were false: Smith had fired DPS, the Parent’s Manager of Financial Institutions who was principally responsible for Project X, there was no reasonable expectation that CSSC could salvage that project, CSSC had not earned and had no right to receive any consulting fees related to the project, let alone \$2.15 million, and there was no source of funding for Project X.

58. Additionally, Respondents failed to disclose in both the September Report and the September Bridge Loan Memo, both dated September 9, 2015, that DPS was terminated by Smith on that very date.

59. Smith reiterated these and similar material misstatements in, and omitted the same material information noted above from, later versions of the Reports and Bridge Loan Memos, causing those documents to be similarly inaccurate and/or misleading to investors.

60. Investor BB invested \$10,000 in the Bridge Loan offering on September 29, 2015. Investor GC, a registered representative of CSSC, invested \$50,000 on November 13, 2015.

3. Between June 15 and December 15, 2015, Respondents misrepresented to investors the Parent’s business relationship with South Dakota Trust Company and the revenue that that relationship would generate

61. From June through December 2015, Respondents also misrepresented and misled investors with respect to a touted “important new strategic alliance with the South Dakota Trust Company (“SDTC”)” and the “\$80 Billion of investment assets” that the Trust controlled.

62. Respondents stated in the June Report that: “CSSC will be the investment advisor of the [Trust’s funds], and CSSC will earn a fee based on a percentage of the assets under management With over \$80 Billion of investment assets of wealthy families across the

country in SDTC administered trust accounts, the revenue and profit potential from client referrals to CSSC could be quite substantial.”

63. Smith also told investors in the June Report that this relationship and the “substantial” profit that would result would be “up and running by year end” 2015.

64. By September, the SDTC relationship that Respondents touted had not materialized, and Smith represented to investors through the September Report that the Parent’s “relationship with [SDTC]” was in “hiatus.” Smith stated, however, that “discussions have recently recommenced regarding both a referral relationship, as well as CSSC’s assistance in the investment management of common and collective investment funds.” Respondents repeated these statements to investors in the October Report as well.

65. These statements and representations about the SDTC relationship were false and Smith knew they were false: CSSC had not developed any referral relationship with SDTC, had not reached any agreements as to when a potential relationship would commence, or come to any agreement at all to entitle CSSC to any profit, much less the “substantial” profit Respondents claimed in the Offering Documents.

4. Between June 15 and December 15, 2015, Respondents misrepresented to investors the Parent’s business relationship with the City of Jacksonville and the revenue that that relationship would generate

66. Through the Offering Documents, Respondents also represented that CSSC had a relationship with the City of Jacksonville, Florida, which they touted as providing nearly \$1 billion in assets under management for CSSC.

67. Specifically, Respondents represented to investors in the June Report that CSSC: “had a pending engagement with the City of Jacksonville, Florida . . . with regard to the investment management of Jacksonville’s [Florida] nearly \$1 billion in short-term operating funds.” (emphasis in the original)

68. According to the June Report, “[t]his engagement uniquely blends [CSSC’s] Consultant role into [an] investment advisory scenario,” which will generate revenue and “increase [CSSC’s] reportable assets under management by nearly \$1 billion.” (emphasis in the original)

69. Respondents continued to tout this consulting agreement with the City of Jacksonville while soliciting investors in later Offering Documents. Respondents represented to investors in the September Bridge Loan Memo that CSSC was “informed that [its] first such engagement, with regard to the nearly \$1 Billion in operating funds of a major southern city, is expected in early October.”

70. Respondents subsequently represented in the October and November Bridge Loan Memos that CSSC was “informed” this engagement was delayed until “the end of this calendar year [2015],” and told investors in the December Bridge Loan Memo that they were “informed” that the engagement would commence “within the first calendar quarter of 2016.”

71. At the time that Respondents made and distributed the statements about the engagement with the City of Jacksonville and the revenue that that engagement would generate, there was no basis in fact that supported them, Smith knew this and also knew that CSSC had not been engaged in any capacity to provide services to the City of Jacksonville, whether related to the City’s purported \$1 billion in assets or otherwise.

72. Moreover, at the time that Respondents made and distributed the statements about the engagement with the City of Jacksonville and the revenue that that engagement would generate, they had no reasonable expectation of this relationship or the revenue generated from it occurring by October 2015, year-end 2015, or “the first calendar quarter of 2016.”

73. Ultimately, the engagement with the City of Jacksonville, and the promised revenue derived from it, never occurred.

5. Four investors invested \$130,000 in the 2015 Bridge Loan Offerings between August 2, 2015 and November 13, 2015

74. Smith used the different versions of the Reports and Bridge Loan Memos to solicit potential investors, some of whom invested in the 2015 Bridge Loan in reliance on Respondent's false and misleading misrepresentations and omissions contained within them.

75. Smith provided these documents to potential investors by mail, including investor TL, on July 21, 2015. He also provided Offering Documents by email to at least three of CSSC's registered representatives TS, BS, and GC, knowing that those memos could be used to solicit additional investors.

76. Four investors invested in the CSSC Bridge Loan based on these fraudulent offering documents. Investor TL invested \$50,000 on August 23, 2015. TS, a registered representative of CSSC, invested \$20,000 on August 30, 2015. Investor BB invested \$10,000 on September 29, 2015. GC, a registered representative of CSSC, invested \$50,000 on November 13, 2015.

FIRST CAUSE OF ACTION
MATERIAL MISREPRESENTATIONS AND OMISSIONS

(Willful violations of Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 10b-5 thereunder, and Violations of FINRA Rules 2020 and 2010) (CSSC and Smith)

77. The Department realleges and incorporates by reference paragraphs 1–76 above.

78. Section 10(b) of the Exchange Act and Rule 10b-5 thereunder make it unlawful for any person, by the use of any means or instrumentality of interstate commerce, or of the mails, to make any untrue statement of a material fact or to omit 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, in connection with the purchase or sale of a security.

79. FINRA Rule 2020 likewise provides that: “No member shall effect any transaction in, or induce the purchase or sale of, any security by means of any manipulative, deceptive or other fraudulent device or contrivance.”

80. FINRA Rule 2010 requires members and associated persons, in the conduct of their business, to “observe high standards of commercial honor and just and equitable principles of trade.”

81. The Offering Documents CSSC, through Smith, drafted and distributed to potential investors omitted facts regarding the current financial condition of the company. Respondents failed to disclose to potential investors that the Parent was in default to past investors in the 2010 Bond and 2014 Bridge Loan, and was unable to make interest and principal payments due to those investors without raising additional capital. These omissions were material, and were omitted from each of the Offering Documents drafted by Smith, from June through December 2015.

82. The Offering Documents contained the following material misrepresentations:

- a. that the Parent was party to a consulting agreement that would pay them \$1.4 million in 2015;
- b. that the Parent would be able to salvage \$2.15 million in “expected revenue” before year end 2015;
- c. that CSSC would earn significant revenue from an association with South Dakota Trust by year end 2015; and
- d. that CSSC was in the final stages of being engaged by the City of Jacksonville, Florida to manage the city’s \$1 billion short-term operating funds, and this would occur by October 2015.

83. Each of Respondents’ statements and representations noted above were material, false and misleading, and Respondents knew they were false and misleading at the time that they prepared and distributed the Offering Documents to investors.

84. As detailed above, between June 2015 through December 2015, in connection with the offer and sales of the securities resulting from the 2015 Bridge Loan, Smith and CSSC, directly or indirectly, by the use of means or instrumentalities of interstate commerce, or of the mails, knowingly, willfully or recklessly: (i) employed devices, schemes or artifices to defraud; (ii) made untrue statement of material fact or omitted to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, concerning investments in the securities resulting from the 2015 Bridge Loan, or; (iii) engaged in acts, practices, or courses of business that operated or would operate as a fraud or deceit upon investors.

85. CSSC and Smith acted with scienter because they intentionally or at least recklessly engaged in a prolonged effort to lure investors into purchasing securities by making material misrepresentations and omitting to disclose certain material facts.

86. The misrepresentations and omissions were material because a reasonable investor would consider them important in making the decision to invest in the 2015 Bridge Loan.

87. Four investors, TL, TS, BB, and GC, invested in the 2015 Bridge Loan Offering after receiving the Offering Documents prepared and delivered by Smith.

88. CSSC is a Michigan registered company, with its principal place of business in Troy, Michigan. Smith works from the Troy, Michigan office. Investors TL and TS are residents of New York, and investor GC is a resident of Texas. Smith and CSSC delivered these documents to potential investors by employing the means or instrumentality of interstate commerce, including emails and phone calls to customers, and the use of the mails to send Bridge Loan Memos and other investment-related documents to customers. Smith also provided copies of

these documents to registered representatives of CSSC by the same methods, instructing each to provide the Offering Documents to potential investors.

89. By engaging in the foregoing conduct, Respondents Smith and CSSC willfully violated Section 10(b) of the Exchange Act and Rule 10b-5 and also violated FINRA Rules 2020 and 2010.

SECOND CAUSE OF ACTION
MATERIAL MISREPRESENTATIONS AND OMISSIONS

**(Violations of FINRA Rule 2010, by contravening
Sections 17(a)(2) and (a)(3) of the Securities Act)
(CSSC and Smith)**

(Pled in the Alternative to the First Cause of Action)

90. The Department realleges and incorporates by reference paragraphs 1-89 above.

91. Sections 17(a)(2) and 17(a)(3) of the Securities Act entitled “Fraudulent Interstate Transactions,” provide that:

- (a) It shall be unlawful for any person in the offer or sale of any securities ... by the use of any means or instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly-
- (b) to obtain money or property by means of any untrue statement of a material fact or any omission 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; or
- (c) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

92. A violation of Sections 17(a)(2) and 17(a)(3) is a violation of FINRA Rule 2010.

93. Between June and December 2015, in connection with the offers and sales of these securities by mail and telephone, CSSC and Smith obtained money (specifically the funds paid by investors for interests in the securities resulting from the 2015 Bridge Loan), either directly or indirectly: (i) by means of untrue statements of material facts and omissions to state material facts

necessary in order to make statements made, in light of the circumstances under which they were made, not misleading, or (ii) by engaging in transactions, practices, or courses of business that operated as a fraud or deceit upon investors in connection with the 2015 Bridge Loan.

94. Smith used the different versions of the Reports and Bridge Loan Memos to solicit potential investors, some of whom invested in the 2015 Bridge Loan based on Respondent's false and misleading misrepresentations and omissions contained within them.

95. Smith provided these documents to potential investors by mail, including investor TL, on July 21, 2015. He also provided Offering Documents by email to at least three of CSSC's registered representatives TS, BS, and GC, knowing that those memos would be used to solicit additional investors.

96. Four investors invested in the CSSC Bridge Loan based on these fraudulent offering documents. Investor TL invested \$50,000 on August 23, 2015. TS, an Affiliate of CSSC, invested \$20,000 on August 30, 2015. Investor BB invested \$10,000 on September 29, 2015, and GC, an Affiliate of CSSC, invested \$50,000 on November 13, 2015.

97. By engaging in the foregoing conduct, CSSC and Smith violated FINRA Rule 2010 by contravening Sections 17(a)(2) and (a)(3) of the Securities Act.

THIRD CAUSE OF ACTION
MATERIAL MISREPRESENTATIONS AND OMISSIONS

(Violations of FINRA Rule 2010)
(CSSC and Smith)

(Pled in the Alternative to the First and Second Causes of Action)

98. The Department realleges and incorporates by reference paragraphs 1 - 97 above.

99. During the Relevant Period, CSSC and Smith engaged in conduct inconsistent with just and equitable principles of trade. They obtained money from the public for four different

investments, the 2015 Bridge Loan offering described above, by making material misrepresentations and omissions of fact regarding those investments while registered with FINRA. This conduct occurred in the conduct of their business and was unethical.

100. By engaging in the foregoing conduct CSSC and Smith violated FINRA Rule 2010.

FOURTH CAUSE OF ACTION
FAILURE TO REGISTER SMITH AS AN ASSOCIATED PERSON

(Violations of NASD Rule 1031 and FINRA Rule 2010)
(CSSC and Smith)

101. The Department realleges and incorporates by reference paragraphs 1–100 above.

102. NASD Membership and Registration Rule 1031(a) provides that “[a]ll persons engaged or to be engaged in the investment banking or securities business of a member who are to function as representatives shall be registered with [FINRA]” NASD Rule 1031(b) defines a representative as follows: “Persons associated with a member . . . who are engaged in the investment banking or securities business for the member including the functions of supervision, solicitation or conduct of business in securities . . . are designated as representatives.”

103. Smith has never been registered in any capacity with FINRA, through CSSC or any other FINRA member firm.

104. Smith, and CSSC through Smith, knew that Smith was not registered as a representative during the time period May 2010 through December 2015.

105. By and through Smith’s conduct, however, Smith was acting in capacities that required his registration as a representative, including the solicitation of CSSC customers to invest in private placement offerings in the Parent company. Smith met with CSSC customers to

discuss their investments and to solicit investments in the May 2010 Bond Offering and related Bridge Loan program.

106. Smith and CSSC knew or should have known that Smith was engaged in the above conduct, despite the fact he was not registered in any capacity with the firm.

107. As a result of the above, CSSC and Smith violated NASD Membership and Registration Rule 1031(a) and FINRA Rule 2010 through the failure to register Smith.

FIFTH CAUSE OF ACTION
FAILURE TO REGISTER SMITH AS A PRINCIPAL

(Violations of NASD Rule 1021 and FINRA Rule 2010)
(CSSC and Smith)

108. The Department realleges and incorporates by reference paragraphs 1–107 above.

109. NASD Membership and Registration Rule 1021 requires all principals to be registered as such, and defines principals to include sole proprietors and partners who are “actively engaged in the management of the member’s investment banking or securities business, including supervision, solicitation, conduct of business or the training of persons associated with a member for any of these functions.”

110. Smith, and CSSC through Smith, knew that Smith was not registered as a principal during the time period May 2010 through December 2015.

111. By and through Smith’s conduct, control and ownership in connection with CSSC, Smith was acting in capacities that required his registration as a principal. He was intimately engaged in CSSC operations and its securities business, including the hiring and retaining of registered representatives, and the management of all CSSC subsidiaries’ finances.

112. Specifically, Smith was required to be registered as a principal because he:
(1) was the majority owner of both CSSC and the Parent; (2) directed the payment of expenses

related to CSSC's home office, including salaries, expenses and rent; (3) made all hiring decisions of all registered representatives working for CSSC; (4) was the direct (and in most cases only) supervisor for certain registered representatives of the firm; and (5) conducted suitability reviews for CSSC's customers who invested in private offerings sold through the firm.

113. Smith and CSSC knew or should have known that Smith was engaged in the above conduct, control and ownership of CSSC, despite the fact that he was not registered in any capacity with the firm.

114. As a result of the above, CSSC and Smith violated NASD Membership and Registration Rule 1021(a) and FINRA Rule 2010 through their failure to register Smith.

RELIEF REQUESTED

WHEREFORE, the Department respectfully requests that the Panel:

- A. make findings of fact and conclusions of law that Respondents committed the violations charged and alleged herein;
- B. order that one or more of the sanctions provided under FINRA Rule 8310(a) be imposed, including the Respondents be required to disgorge fully any and all ill-gotten gains and/or make full and complete restitution, together with interest;
- C. order that Respondents bear such costs of proceeding as are deemed fair and appropriate under the circumstances in accordance with FINRA Rule 8330; and

- D. make specific findings that Respondents willfully violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

FINRA DEPARTMENT OF ENFORCEMENT

Date:

8/4/2017



Kathryn S. Gostinger, Senior Regional Counsel
Christopher M. Burky, Deputy Regional Chief Counsel
Mark A. Koerner, Regional Chief Counsel
FINRA — Department of Enforcement
55 W. Monroe St., Suite 2700
Chicago, IL 60603
(312) 899-4400
Katie.Gostinger@finra.org
Christopher.Burky@finra.org
Mark.Koerner@finra.org