

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 2017052325702**

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

RE: Coastal Equities, Inc., Respondent
Member Firm
CRD No. 23769

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

I.

ACCEPTANCE AND CONSENT

- A. Respondent 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

Coastal became a FINRA member in 1989 and conducts a general securities business. The Firm is headquartered in Wilmington, Delaware, and has 104 registered representatives across 50 branches.

RELEVANT DISCIPLINARY HISTORY

Respondent does not have any relevant disciplinary history with the Securities and Exchange Commission, any state securities regulators, FINRA, or any other self-regulatory organization.

OVERVIEW

From October 2016 to July 2018, Coastal failed to reasonably supervise a registered representative, SA, who recommended excessive and unsuitable trades in the accounts of four customers. Coastal became aware of numerous red flags that SA was making unsuitable recommendations, but failed to take reasonable action to investigate them.

As a result of the foregoing, Coastal violated FINRA Rules 3110 and 2010.

FACTS AND VIOLATIVE CONDUCT

A. Applicable Law

FINRA Rule 3110 requires that a member firm take reasonable steps to: ensure that the activities of each registered representative comply with applicable securities laws, regulations, and FINRA rules; investigate red flags of potential misconduct; and take reasonable action when misconduct has occurred. A violation of FINRA Rule 3110 is also a violation of FINRA Rule 2010, which requires FINRA members to “observe high standards of commercial honor and just and equitable principles of trade.”

FINRA Rule 2111 requires member firms or their associated persons to have a reasonable basis to believe that a recommended securities transaction or investment strategy is suitable for a customer, based on information obtained through the reasonable diligence of the firm or associated person to ascertain the customer’s investment profile. A customer’s investment profile includes, but is not limited to, the customer’s age, other investments, financial situation and needs, investment objectives, investment experience, investment time horizon, liquidity needs, and risk tolerance.

Recommended securities transactions may be unsuitable if, when taken together, they are excessive and the level of trading is inconsistent with the customer’s investment profile. No single test defines when trading is excessive, but factors such as the turnover rate and the cost-to-equity ratio may provide a basis for finding that a member firm or associated person has violated FINRA’s suitability rule. Turnover rate represents the number of times that a portfolio of securities is exchanged for another portfolio of securities. The cost-to-equity ratio measures the amount an account has to appreciate just to cover commissions and other expenses; in other words, it is the break-even point where a customer may begin to see a return. A turnover rate of 6 or a cost-to-equity ratio above 20% generally indicates that excessive trading may have occurred.

In addition, recommendations to use margin to purchase securities may be unsuitable if the use of margin is inconsistent with the customer’s investment profile. Indeed, trading on margin increases the risk of loss because a customer may lose more than the amount invested and also requires the customer to pay interest on a margin loan, thereby increasing the amount the investment must appreciate before realizing a net gain.

B. Coastal’s Failure to Reasonably Supervise Representative SA

From October 2016 to July 2018, Coastal failed to reasonably supervise registered representative SA. SA’s supervisor became aware of multiple indicia that SA was recommending excessive and unsuitable trading in the accounts of four customers, and that SA was making unsuitable recommendations to purchase securities using margin in the accounts of two of those customers. The Firm failed to reasonably respond to these

red flags.¹

SA was registered through Coastal from September 2015 to July 2018. During this period, Coastal supervised securities recommendations, including those of SA, primarily through the review of daily trade blotters. Those blotters showed each trade entered by each representative, including SA, as well as the turnover rate and the amount of commissions charged to each account for the preceding 12-month period. Supervisors also would, at times, calculate the cost-to-equity ratio for certain accounts.

In September 2016, Coastal, through daily trade blotter review by SA's immediate supervisor, became aware that SA had recommended frequent transactions in preferred stock that resulted in significant losses in the account of one customer. SA's supervisor Coastal thereafter sampled other customer accounts of SA and identified additional accounts showing indicia of potential excessive trading. When asked about this trading, SA claimed that the customers approved of his trading strategy. Coastal accepted that explanation at face value and as a result took no further steps at that time.

Following that initial supervisory meeting with SA, starting in October 2016, Coastal, through supervisory review of the daily trade blotter, was on notice of additional red flags that SA was recommending unsuitable and excessive trading in the accounts of four customers, and that that he was making unsuitable recommendations to purchase securities using margin in two of those customers' accounts. Each customer was a retired, senior investor with a moderate risk tolerance, and a summary of SA's securities recommendations to those customers is set forth below.

- Customer 1 was 75 years old as of January 1, 2017, and had two accounts at Coastal, one of which was an individual retirement account. Both accounts had a moderate growth objective. From October 2016 to July 2018, SA recommended more than 100 trades in Customer 1's accounts, resulting in commissions totaling \$84,525 during this time period.
- Customer 2 was a married couple, both of whom were retired and living on a fixed income, as of January 1, 2017. They had a joint account at Coastal, which reflected a long-term growth objective. From October 2016 to April 2017, SA recommended 65 trades in Customer 2's account, including recommendations to purchase securities using margin. The commissions charged to Customer 2's account during this time period were \$97,587; the account also incurred \$11,845 in margin interest. SA's recommendations concerning the use of margin were not suitable for Customer 2 given the couple's investment profile, particularly their investment objectives and risk tolerance.
- Customer 3 was 91 years old as of January 1, 2017. Customer 3 was living on a

¹ In March 2019, SA entered into an AWC in which he agreed to a bar from associating with any FINRA member firm in any capacity for his failure to appear and provide on-the-record testimony in connection with FINRA's investigation of, *inter alia*, his recommendations of excessive and unsuitable trading, including his recommendations involving the use of margin.

fixed income and his new account paperwork listed his annual income and other investments as less than \$50,000. He had an individual account at Coastal with a moderate growth and income objective. From October 2016 to July 2018, SA recommended 31 trades in Customer 3's account, resulting in \$61,657 in commissions. The account also incurred \$580 in margin interest. SA's recommendations concerning the use of margin were not suitable for Customer 3 in light of his investment profile, particularly his limited resources to meet any potential margin call and moderate investment objective and risk tolerance.

- Customer 4 was 82 years old as of January 1, 2017, and had one account at Coastal with a moderate growth and income objective. SA recommended 39 trades in Customer 4's account from October 2016 to December 2017, resulting in \$14,126 in commissions.

From October 2016, the Firm's daily trade blotter showed SA's frequent trading and the correspondingly high turnover rates and commissions in the accounts of Customers 1 through 4. The turnover rate for each of the four customers' accounts was well over 6, while the cost-to-equity ratio was in excess of 20%, which, as noted above, are benchmarks indicating potential excessive trading. In certain of the accounts, the turnover ratio exceeded 20 and the cost-to-equity ratio exceeded 50%.

Additionally, in August 2017, the Firm began utilizing exception reports from its clearing firm as a part of its supervisory system. Those exception reports included a report for accounts with turnover rates over 6 and a report for accounts with margin-to-equity ratios over 50%. Each of the five accounts of Customers 1 through 4 generated multiple turnover exceptions, and Customer 3's account generated two margin exceptions.

Despite these red flags, from October 2016 through December 2017, no one at Coastal reviewed the accounts of Customers 1 through 4 to determine whether SA's recommendations were suitable, questioned SA about the trading in any of his customer's accounts, contacted any of SA's customers, or took any steps to reduce the commissions that SA was charging his customers or the frequency with which SA was recommending securities transactions. In December 2017, Coastal suggested that SA move some actively traded accounts to fee-based accounts, and in February 2018, Coastal began sending activity letters to some of SA's customers. Nonetheless, SA continued to recommend excessive trading and/or unsuitable use of margin to certain customers. In April 2018, Coastal sent SA a letter of admonishment, which SA did not sign until June 2018. Effective May 30, 2018, Coastal limited the commissions SA could charge to his customers' accounts. SA left Coastal in July 2018.

The Firm's failure to investigate and reasonably respond to the red flags of SA's unsuitable recommendations and to take reasonable action in response to those red flags allowed SA to solicit trading that resulted in Customers 1 through 4 paying \$257,895 in

commissions and \$12,425 in margin interest during the relevant period.²

As a result of the foregoing, Respondent violated FINRA Rules 3110 and 2010.

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

- A censure; and
- Restitution in the amount of \$270,320, plus interest in the amount of \$9,588.80.³

Restitution is ordered to be paid to the customers listed on Attachment A hereto in the total amount of \$270,320, plus interest in the amount of \$9,588.80.

A registered principal on behalf of Respondent Firm shall submit satisfactory proof of payment of restitution and pre-judgment interest (separately specifying the date and amount of each paid to each customer listed on Attachment A) or of reasonable and documented efforts undertaken to effect restitution. Such proof shall be submitted by email to EnforcementNotice@FINRA.org from a work-related account of the registered principal of Respondent Firm. The email must identify the Respondent and the case number and include a copy of the check, money order or other method of payment. This proof shall be provided by email to EnforcementNotice@FINRA.org no later than 120 days after acceptance of the AWC.

If for any reason Respondent cannot locate any customer identified in Attachment A after reasonable and documented efforts within 120 days from the date the AWC is accepted, or such additional period agreed to by a FINRA staff member in writing, Respondent shall forward any undistributed restitution and interest to the appropriate escheat, unclaimed property or abandoned property fund for the state in which the customer is last known to have resided. Respondent shall provide satisfactory proof of such action to the FINRA staff member identified above and in the manner described above, within 14 calendar days of forwarding the undistributed restitution and interest to the appropriate state authority.

Respondent specifically and voluntarily waives any right to claim an inability to pay, now or at any time hereafter, the monetary sanction imposed in this matter.

² This AWC requires Coastal to pay as restitution the commissions charged to Customers 1 through 4 as a result of SA's excessive trading, as well as the margin interest charged to Customers 2 and 3 as a result of SA's unsuitable recommendations concerning the use of margin.

³ Pursuant to the General Principles Applicable to all Sanctions Determinations contained in the *Sanction Guidelines*, FINRA imposed no fine against Coastal in this case, and agreed to assess interest on the restitution owed at a rate below that set forth in Section 6621(a)(2) of the Internal Revenue Code, after it considered, among other things, the Firm's revenues and financial resources, as well as its agreement to pay full restitution (with partial interest) to the affected customers. See Notice to Members 06-55.

The imposition of a restitution order or any other monetary sanction herein, and the timing of such ordered payments, does not preclude customers from pursuing their own actions to obtain restitution or other remedies.

Restitution payments to customers shall be preceded or accompanied by a letter, not unacceptable to FINRA staff, describing the reason for the payment and the fact that the payment is being made pursuant to a settlement with FINRA and as a term of this AWC.

As noted above, pursuant to the General Principles Applicable to all Sanction Determinations contained in the *Sanction Guidelines*, FINRA imposed no fine against the Firm in this case after it considered, among other things, the Firm's revenues and financial resources. See Notice to Members 06-55.

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

II.

WAIVER OF PROCEDURAL RIGHTS

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

- A. To have a Complaint issued specifying the allegations against it;
- B. To be notified of the 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, Respondent specifically and voluntarily waives any right to claim bias or prejudgment of the Chief Legal Officer, 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.

Respondents 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

Respondent 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 Respondent; and
- C. If accepted:
 - 1. this AWC will become part of Respondent's permanent disciplinary record and may be considered in any future action brought by FINRA or any other regulator against Respondent;
 - 2. this AWC will be made available through FINRA's public disclosure program in accordance with FINRA Rule 8313;
 - 3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with FINRA Rule 8313; and
 - 4. Respondent 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. Respondent 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 Respondent's: (i) testimonial obligations; or (ii) 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. Respondent 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 Respondent 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 it has agreed to the AWC's 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 it to submit it.

October 16, 2020
Date

Coastal Equities, Inc.
Respondent

By:  _____

Print Name: Charles F. Reiling III

Title: President

Reviewed by:



Dana Sirkis Gloor
Counsel for Respondent
Miles & Stockbridge
100 Light St.
Baltimore, MD 21202

Accepted by FINRA:

11/9/20
Date

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

K. C. Daly
Karen C. Daly
Principal Counsel
FINRA
Department of Enforcement
1601 Market St., Suite 2700
Philadelphia, PA 19103

ATTACHMENT A
to
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
COASTAL EQUITIES, INC., NO. 2017052325702

Customer #	Restitution Amount
Customer 1	\$87,586.89
Customer 2	\$113,196.95
Customer 3	\$64,486.00
Customer 4	\$14,638.96
Total	\$279,908.80