

**FINANCIAL INDUSTRY REGULATORY AUTHORITY (FINRA)
OFFICE OF HEARING OFFICERS**

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

CAROLINA FINANCIAL SECURITIES, LLC,
(BD No. 41970)

and

BRUCE VICTOR ROBERTS
(CRD No. 1489110)

Respondents.

Disciplinary Proceeding
No. 2014040295201

COMPLAINT

The Department of Enforcement alleges:

SUMMARY

1. During the period from February 14, 2014 through February 21, 2014, Carolina Financial Securities, LLC (Carolina), acting through Bruce Victor Roberts (Roberts), its President, Chief Executive Officer (CEO) and Chief Compliance Officer (CCO), sold nearly \$2.5 million of 13.5 percent Senior Secured Notes in a \$5.0 million offering to 18 customers, ostensibly to raise capital for a medical and dental supply company. Carolina, acting through Roberts, failed to conduct reasonable due diligence in connection with this offering, and further created and provided to investors sales literature that misrepresented the security of the investment, the financial condition of the issuer and the value of the issuer's largest contract while also failing to disclose risks, investment fees and expenses. The \$5.0 million offering was the latest in a

\$150,000,000 fraudulent scheme which was halted only when the president of the medical and dental supply company was arrested. He subsequently pled guilty to wire fraud.

2. By engaging in the foregoing conduct, Carolina and Roberts willfully violated Section 10(b) of the Securities Exchange Act of 1934 (Exchange Act), Exchange Act Rule 10b-5 thereunder, and FINRA Rules 2010 and 2020. Alternatively, Carolina and Roberts violated FINRA Rule 2010 by acting in contravention of Section 17(a) of the Securities Act of 1933 (Securities Act), and further independently violated FINRA Rule 2010. Moreover, by failing to conduct reasonable due diligence, thereby leaving Carolina without a reasonable basis for recommending the offering to its customers, Carolina and Roberts violated FINRA Rules 2111(a) and 2010. Carolina, acting through Roberts, further provided investors with inaccurate and misleading sales literature, in violation of FINRA Rules 2210(d)(1)(A), 2210(d)(1)(B), and 2010. Finally, Carolina and Roberts failed to enforce its supervisory procedures regarding due diligence and its required suitability determination, in violation of NASD Conduct Rules 3010(a) and 3010(b) and FINRA Rule 2010.

RESPONDENTS AND JURISDICTION

3. Carolina has been a FINRA member since February 19, 1997. Carolina currently has 15 registered representatives who operate out of its main office located in Brevard, North Carolina or branch offices located in Raleigh, North Carolina, Irvine, California, and Darien, Connecticut. Carolina derives all of its revenues from private placements. Carolina is 75 percent owned by Carolina Financial Group, LLC, which is majority owned by Roberts.

4. Roberts founded Carolina and serves as its President, CEO, and CCO. Roberts entered the securities industry in March 1986, and was associated with several FINRA member firms

from March 1986 through July 1995. Roberts is registered as a general securities representative and principal, a limited representative for investment banking, and an operations professional.

5. Carolina is, and at all times relevant to the Complaint was, a FINRA member firm and Roberts is, and at all times relevant to the Complaint was, associated with Carolina. Therefore, Carolina and Roberts are subject to FINRA's jurisdiction pursuant to FINRA By-Laws Article IV, Section 1 and Article V, Section 2.

OTHER ENTITIES AND INDIVIDUALS

6. **International Manufacturing Group, Inc. (IMG)** is a wholesale and retail medical and dental supply business. IMG was owned by D.W. and his wife during the relevant period. IMG is based in Sacramento, California and was created in 1988. In May 2014, IMG filed a Chapter 11 bankruptcy petition in the U.S. Bankruptcy Court for the Eastern District of California.

7. **IMG Funding, LLC (IMGF)** was established by Carolina as a single purpose entity to raise funds and then make advances to IMG. Carolina Financial Group, LLC and Roberts served as the manager of IMGF. IMGF loaned funds to IMG purportedly for bridge financing for the establishment of Olivehurst Glove Manufacturing, LLC (Olivehurst), which is a manufacturing company affiliated with IMG. According to D.W., Olivehurst planned to manufacture high-end medical examination gloves and select lines of disposable medical supplies in the United States, which would be marketed by IMG.

8. **D.W.** served as president of IMG since it was created in 1988. D.W. was arrested on February 21, 2014, and charged in a criminal complaint in the U.S. District Court for the Eastern District of California with conspiracy, mail fraud, wire fraud and bank fraud. On May 6, 2014, D.W. entered into a Plea Agreement in which he pled guilty to one count of wire fraud, which involved a wire sent by IMGF to D.W. D.W. admitted in his plea agreement that he obtained

over \$150,000,000 by making a variety of material false representations including overstating the valuation of a contract with the U.S. Department of Veterans Affairs (VA) and overstating accounts receivable from the VA.

FACTS COMMON TO ALL COUNTS

I. Carolina, acting through Roberts, Agrees to Serve as Exclusive Placement Agent on a \$5 Million Offering Purportedly to Fund a Medical Equipment Manufacturing Facility

9. In or around late January or early February 2014, one of Carolina's registered representatives, S.R., who works out of an unregistered office in California, contacted Roberts regarding a proposal to raise funds for a California-based company, IMG. S.R. had recently discussed financing with IMG's President, D.W., and reviewed various IMG records. S.R. proposed to raise funds through the sale of one-year notes and loan the proceeds to IMG, if IMG and D.W. were willing to give security in the form of a lien on all of IMG's assets and a personal guaranty from D.W.

10. After receiving a favorable response to his proposal from Roberts, S.R. went to Sacramento, California to meet with D.W., tour the facility, and review additional financial records of IMG.

11. D.W. claimed that he needed short-term financing to expand IMG's business to include the manufacturing of medical gloves and was attempting to develop, construct, and operate a high-end medical glove manufacturing plant (Olivehurst). D.W. represented that the Olivehurst facility was on a tight construction deadline because it would lose certain U.S. Food and Drug Administration (FDA) licenses if IMG did not produce sample gloves within a certain amount of time (in 2014), and the loss of the FDA licenses would cause a significant delay in the company's expansion plans.

12. D.W. assured Carolina and Roberts, through S.R. that IMG expected additional foreign financing at a future date, but D.W. claimed the company needed at least \$750,000 to \$1,000,000 within two weeks. D.W. indicated IMG was willing to pay a higher cost for financing to meet his tight deadlines.

13. On February 3, 2014, Carolina, acting through Roberts, and D.W. signed an engagement agreement. According to the agreement, IMG engaged Carolina as its exclusive placement agent to assist in a best efforts private placement to accredited investors of up to \$5.0 million of secured loan funding (the IMGF Offering). Carolina agreed, among other things, to: (1) review various corporate documents, including IMG's business plan and financial statements, (2) advise IMG on the proposed financing, (3) solicit investors, (4) provide investors with pertinent information, (5) create and manage IMGF as a single purpose finance company for the offering, and (6) supervise the closing of the offering.

14. IMG agreed to furnish Carolina with "all information requested concerning [IMG]" and provide reasonable access to IMG's officers, directors, employees, accountants and counsel. Carolina indicated that it would "rely solely upon such information supplied by [IMG] . . . without assuming any responsibility for independent investigation or verifications thereof."

II. Carolina, Acting Through Roberts, Assigns S.R. as Lead Banker for the IMGF Offering, and Carolina Receives Incomplete and Inconsistent Documentation During its Initial Due Diligence

15. Roberts designated S.R. as the lead banker for the IMGF Offering, although S.R. had never functioned as a lead banker on any previous offering.

16. As lead banker, S.R. was responsible for gathering due diligence materials and uploading them to Carolina's internal site for supervisory review. S.R. used Carolina's due diligence

checklist as a guide in connection with his due diligence. S.R. kept Roberts apprised of his activities as lead banker for the IMGF Offering throughout the due diligence review period.

17. S.R.'s initial due diligence consisted of reviewing IMG's November 2013 financial statements, an IMG customer list, a December 2013 accounts receivable trial balance, tax forms, IMG's contract with the VA, and D.W.'s personal bank account statements.

18. S.R. then requested and reviewed IMG's financial statements for 2012. As Carolina, through S.R., was aware, the accounts receivable showed a year-over-year increase, but the accounts payable did not show a corresponding increase. This discrepancy was a red flag that the financial statements may not be accurate. When S.R. questioned D.W. about this discrepancy, D.W. claimed that the corresponding increase would be reflected in IMG's December 2013 financials.

19. S.R. requested the December 2013 financials for IMG, but D.W. never supplied them to S.R. or Carolina, which was another red flag that the financial statements and information D.W. provided were not accurate.

20. Carolina, acting through Roberts, failed to validate any receivables listed on the IMG trial balance; failed to identify IMG's accounts receivable that remained unchanged from August 2013 to December 2013; failed to validate any of the assets and liabilities on the IMG balance sheets from 2010 to November 2013; and permitted the use of the November 2013 financials in the IMGF PPM in spite of questions regarding the accuracy of the accounts payable and/or inventory accounts.

III. D.W. Falsely Claimed that IMG Had a \$94 Million Contract with the VA, which, Carolina could have Confirmed through the VA's Website, was Grossly Exaggerated

21. Prior to the IMGF Offering, D.W. represented to Carolina, S.R. and Roberts that IMG had an existing contract with the VA valued in excess of \$94 million, and that it had been extended from September 2011 to September 2016.

22. In fact, IMG conducted business with the VA in 2012 and 2013, but only had sales of \$25,102 and \$24,048, respectively. This information was publicly available at all relevant times through the VA's website (<http://www.va.gov/>).

23. Carolina, acting through Roberts, failed to obtain a complete copy of IMG's VA contract, did not question D.W. about the VA contract, and failed to have it reviewed by legal counsel.

24. Moreover, Carolina acting through Roberts, failed to contact anyone associated with the VA or review the VA's website to confirm IMG's representations regarding its contract and sales to the VA.

25. By the exercise of reasonable due diligence, Carolina and Roberts could have determined that IMG's purported \$94 million contract had an actual aggregate value of approximately \$125,000 for the five year period, not the \$94 million as D.W. had represented to Carolina, Roberts and S.R.

IV. Roberts and Carolina Performed No Due Diligence Regarding a False \$29 Million Account Receivable on IMG's December 2013 Financial Statements

26. The largest asset listed on IMG's books was an account receivable (VAM001), which showed a value of \$29,084,370 as of December 31, 2013. The VAM001 account receivable represented 79.5 percent of IMG's total accounts receivable as of December 2013 (claimed total

accounts receivable for December 2013 was \$36,569,003) and was almost 40 percent of IMG's total assets listed on its November 2013 financials.

27. Carolina, acting through S.R. and Roberts, believed that the VAM001 account receivable related to the VA contract based upon verbal representations from D.W. However, Carolina, S.R. and Roberts never confirmed that the VAM001 account receivable was actually related to the VA contract or was otherwise accurate.

28. In fact, S.R. did not contact any of the accounts listed on IMG's accounts receivable trial balance to confirm the amounts listed or the existence of the assets.

29. Additionally, Carolina, acting through Roberts, failed to independently verify any of IMG's top 50 customers included on the list of customers provided by IMG.

30. The VAM001 account receivable was grossly inflated, with IMG's financials falsely showing tens of millions of dollars in receivables from the VA.

V. IMG and D.W. Provided Incomplete and Inconsistent Financial Documents to Carolina, but Roberts and Carolina Failed to Verify or Reconcile the Information

31. IMG provided S.R. with December 2013 bank statements for five bank accounts related to IMG, one of which was a personal account for D.W. However, the statements only included the first page of each statement. The aggregate balance in the four IMG accounts at the beginning of December 2013 was approximately \$271,000.

32. S.R. requested additional bank account statements for the IMG wholesale account, which S.R. believed was IMG's main account. IMG provided statements for this account for the period of August 2013 through November 2013, but again IMG only provided the first page of each statement.

33. Although incomplete, the IMG bank account statements reflected a far lower cash position than IMG's financial statements, which was a red flag that IMG was providing false financial information in support of the IMGF Offering. The cash position as shown on the IMG wholesale account statement at the end of November 2013 was \$140,698 and the cash position from the December 2013 bank statements for all four of IMG's bank accounts showed an aggregate balance of approximately \$271,000. By contrast, IMG's November 2013 financial statements claimed the company had a cash position of \$858,591.

34. Carolina, acting through Roberts and S.R. did not attempt to reconcile the inconsistent figures or question why all four IMG accounts provided to Carolina reflected a December 2013 balance of less than one third of the cash position reflected in IMG's November 2013 balance sheet. Furthermore, Carolina did not obtain the December 2013 financial statements for IMG or complete statements for IMG's bank accounts.

35. D.W. also provided S.R. with a personal Statement of Financial Condition as of September 30, 2013. D.W.'s September 30, 2013 personal Statement of Financial Condition showed purported assets of \$70,563,239, liabilities of \$12,446,982, and a net worth of \$58,116,257. Carolina, acting through Roberts, failed to verify any of the assets, liabilities or net worth figures listed on D.W.'s personal Statement of Financial Condition.

VI. Carolina and Roberts Failed to Confirm D.W.'s Claim that a Lawsuit Against IMG's Affiliate for Defaulting on a Loan Related to the Olivehurst Facility had been Previously Settled

36. On August 15, 2013, General Electric Capital Corporation (GECC) and another entity filed a complaint in the U.S. District Court for the Eastern District of California (*General Electric Capital Corporation, et al. v. Relyaid Global Healthcare, Inc., et al.*, 2:13cv1683).

37. The GECC complaint alleged, among other things:
- a. Key Equipment Finance, Inc. (Key) agreed in December 2012 to finance the acquisition of equipment for the Olivehurst facility by RelyAid Global Healthcare, Inc. (RelyAid), which is an affiliate of IMG;
 - b. IMG executed a corporate guaranty and D.W. executed a personal guarantee of the loan;
 - c. Key advanced over \$4.4 million on behalf of RelyAid;
 - d. Key assigned the rights to the note to GECC;
 - e. RelyAid defaulted on the loan; and
 - f. IMG and D.W. failed to fulfill their guarantees.
38. On January 31, 2014, S.R. requested an explanation regarding the GECC litigation from D.W., who falsely responded that the litigation was settled in November 2013. In fact, the litigation remained pending at the time D.W. falsely claimed it had been settled and during the sales of the IMGF notes as alleged below.
39. S.R. placed D.W.'s false representation regarding the GECC litigation in Carolina's due diligence file and forwarded the false information to Roberts. No one at Carolina took any steps to verify D.W.'s claim that the GECC litigation had been settled.
40. As Carolina and Roberts could have determined through a review of publicly available records, the GECC litigation was pending at the time Carolina sold the IMGF Offering to its customers. The GECC lawsuit was not settled until March 26, 2014, and the settlement was a stipulated judgment in favor of GECC and against IMG and D.W., among others, in the amount of \$4,572,802.63.

41. Carolina, acting through S.R. and Roberts, simply relied upon the representations of D.W. and IMG regarding the resolution of the GECC litigation and failed to verify whether such representations were true.

VII. Carolina Sells Nearly Half of the \$5 Million IMGF Offering without Completing its Due Diligence, and Carolina Representatives, Including Roberts, Make Numerous Material Misrepresentations and Omissions to Investors

42. Carolina and Roberts agreed to act as placement agent for the IMGF Offering and sell up to \$5.0 million of 13.5 percent Senior Secured Notes with one-year maturities. The general purpose of the IMGF Offering was to raise capital, which would be provided to IMG for bridge financing of the Olivehurst facility.

43. Only 17 days (13 business days) elapsed from the date Carolina commenced its due diligence on January 28, 2014 until Roberts approved the IMGF Offering for sale on February 14, 2014.

44. Between February 14, 2014 and February 21, 2014, Carolina, acting through five registered representatives of the firm, sold IMGF notes to 18 customers in increments of \$25,000, raising approximately \$2.45 million.

45. During the course of these sales, Carolina, acting through Roberts and other registered representatives, made misrepresentations of material facts and omitted to disclose material facts to customers in connection with the sale of IMGF notes.

46. In the course of soliciting investors for the IMGF notes, Carolina, acting through Roberts and other registered representatives, provided customers with a flow chart, term sheet, information memorandum, and Private Placement Memorandum (PPM) (collectively, the IMGF Offering Materials), which they knew, or by exercise of reasonable diligence should have known, contained material misrepresentations and omissions. One or more of the IMGF

Offering Materials falsely represented that:

- a. IMG had a contract with the VA valued at more than \$90 million;
- b. IMG had accounts receivable as of November 2013 totaling \$36,685,772;
- c. The contemplated loan from IMGF to IMG, funded by investor proceeds, was secured by a first lien on substantially all of the assets of IMG; and
- d. The loan and interest were guaranteed by D.W.

47. None of the IMGF Offering Materials disclosed the following material facts regarding IMG and the IMGF Offering:

- e. IMG's financial statements were falsified and contained overstated accounts receivable;
- f. Carolina was provided with incomplete and inconsistent financial documentation during the course of its due diligence review, as alleged above;
- g. Carolina's due diligence review relating to the offering was ongoing; and
- h. IMG, D.W. and IMG affiliate RelyAid, were being sued by GECC in connection with RelyAid's default on a loan related to the Olivehurst facility, as alleged above.

48. Roberts personally provided the IMGF Offering Materials to at least three customers, each of which purchased IMGF notes during the relevant period. The purchases by the three customers of Roberts aggregated \$525,000.

VIII. Carolina Wires Over \$2.3 Million of Customer Funds to IMGF Before Sales are Halted Due to D.W.'s Arrest for Bank Fraud

49. The IMGF Offering was a "best efforts" offering and did not include any contingency. As a result, investor funds were immediately wired to IMG upon acceptance of the investments. Accordingly, between February 14, 2014 and February 21, 2014, Roberts directed IMGF to wire in excess of \$2.3 million of investor funds to IMG via five wires.

50. The remaining \$147,000 raised by Carolina was retained by Carolina as its placement agent fee, which was six percent of the IMGF notes sold. Carolina then paid a portion of its fee as commissions to the five representatives who sold the IMGF notes, including Roberts.

51. Carolina's due diligence review and sales of the IMGF Offering were still ongoing on February 24, 2014, when it learned of D.W.'s arrest for bank fraud and making false statements to a financial institution. The U.S. Department of Justice charged D.W. with fraud in connection with a line of credit from a bank to IMG and RelyAid to develop the Olivehurst facility.

Carolina ceased sales of the IMGF notes upon learning of D.W.'s arrest.

52. Although IMGF wired over \$2.3 million in investor funds to IMG before D.W.'s arrest, the final closing documents including the loan agreement and security agreement between IMG and IMGF, as well as the personal guaranty of D.W. were never executed.

IX. Carolina, Acting Through Roberts and S.R., Failed to Follow its Own Written Supervisory Procedures Regarding Due Diligence in Connection with the IMGF Offering

53. Carolina's Written Supervisory Procedures (WSPs) in effect during the relevant period contained numerous provisions related to the Firm's due diligence on private placements such as the IMGF Offering. Carolina, acting through Roberts and S.R., violated several WSP provisions in connection with the Firm's due diligence for the IMGF Offering.

54. First, Carolina's WSPs required that the designated principal, Roberts, conduct due diligence and approve all offerings sold by Carolina and its registered representatives.

55. Second, Carolina's WSPs required the completion of a due diligence checklist for each contemplated offering. The checklist listed items to be obtained from the issuer including, but not limited to, company overview, financial records, corporate documents, material contracts, and litigation. As alleged above, Carolina created a checklist for the IMGF Offering and

obtained certain documents. However, numerous items, such as the VA contract and bank account statements, were incomplete and many items on the checklist, such as material contracts, were still listed as pending when sales of IMGF notes were made and investor funds were released to IMG.

56. Third, Carolina's WSPs define due diligence as a reasonable investigation sufficient to form a basis for believing that the statements contained in the PPM are true and that the PPM does not omit any material facts. As alleged above, Carolina, through S.R., obtained documents that raised red flags that the PPM contained material misrepresentations and omitted material facts.

57. Fourth, Carolina's WSPs require representatives who seek to sell a particular offering to score 80 percent or higher on a Firm-designed test regarding the offering in order to sell the offering. During the period from January 31, 2013 through April 29, 2014, Carolina sold 15 offerings, including the IMGF Offering. Yet the IMGF Offering was the only offering where a test for representatives was not created and administered.

FIRST CAUSE OF ACTION — CAROLINA AND ROBERTS

Section 10(b) of the Exchange Act, Exchange Act Rule 10b-5 promulgated thereunder, and FINRA Rules 2020 and 2010 (Fraudulent Misrepresentations and Omissions in the Sale of Securities)

58. The Department realleges and incorporates by reference paragraphs 1 through 57 above.

59. Section 10(b) of the Exchange Act and Exchange Act 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.

60. 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.”

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

62. The IMGF notes are securities.

63. Between at least February 14, 2014 and February 21, 2014, Carolina, acting through Roberts and other registered representatives, made misrepresentations of material facts and omitted to disclose material facts to customers in connection with the sale of IMGF notes, as follows.

64. First, in the course of soliciting investors for the IMGF notes, Carolina, acting through Roberts and other registered representatives, provided customers with IMGF Offering Materials, which they knew, or were reckless in not knowing, contained untrue representations of material facts and omissions of material facts. One or more of the IMGF Offering Materials falsely represented that:

- a. IMG had a contract with the VA valued at more than \$90 million;
- b. IMG had accounts receivable as of November 2013 totaling \$36,685,772;
- c. The contemplated loan from IMGF to IMG, funded by investor proceeds, was secured by a first lien on substantially all of the assets of IMG; and
- d. The loan and interest were guaranteed by D.W.

65. Second, none of the IMGF Offering Materials disclosed the following material facts regarding IMG and the offering:

- a. IMG's financial statements were falsified and contained overstated accounts receivable;
- b. As alleged above, Carolina was provided with incomplete and inconsistent financial documentation during the course of its due diligence;
- c. Carolina's due diligence relating to the IMGF Offering was ongoing; and
- d. IMG, D.W. and IMG affiliate RelyAid, were being sued by GECC in connection with RelyAid's default on a loan related to the Olivehurst facility.

66. Carolina and Roberts employed the means or instrumentalities of interstate commerce, including the use of e-mail and the internet to provide the IMGF Offering Materials to customers in connection with their sales of the IMGF notes.

67. Based upon the foregoing, Carolina and Roberts effected transactions in, or induced the purchase of securities (IMGF notes) by means of the IMGF Offering Materials that were materially misleading and omitted material facts.

68. Carolina and Roberts, directly or indirectly, by the use of the means or instrumentalities of interstate commerce, or the use of e-mail, each knowingly or recklessly made untrue statements of material facts or omitted to state a 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 sale of the IMGF notes.

69. By engaging in the foregoing conduct, Carolina and Roberts willfully violated Section 10(b) of the Exchange Act and Exchange Act Rule 10b-5 thereunder and FINRA Rules 2020 and 2010.

SECOND CAUSE OF ACTION — CAROLINA AND ROBERTS

(Alternative to the First Cause of Action)

FINRA Rule 2010

**(Misrepresentations and Omissions by Respondents
in Violation of Section 17(a) of the Securities Act)**

70. The Department realleges and incorporates by reference paragraphs 1 through 69 above.
71. Section 17(a)(2) of the Securities Act prohibits, in the offer or sale of any securities using interstate commerce, obtaining “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.”
72. Section 17(a)(3) of the Securities Act prohibits, in the offer or sale of any securities using interstate commerce, engaging “in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.”
73. FINRA Rule 2010 requires associated persons in the conduct of their business to “observe high standards of commercial honor and just and equitable principles of trade.”
74. IMGF notes are securities.
75. As alleged in the First Cause of Action above, between at least February 14, 2014 and February 21, 2014, Carolina, acting through Roberts and other registered representatives, made misrepresentations of material facts and omitted to disclose material facts to customers in connection with the sale of IMGF notes.
76. In the course of soliciting investors for the IMGF notes, Carolina, acting through Roberts and other registered representatives, provided customers with IMGF Offering Materials, which they knew, or by exercise of reasonable due diligence should have known, that contained untrue representations of material facts and omissions of material facts, as alleged in the First Cause of Action above.

77. Carolina and Roberts employed the means or instrumentalities of interstate commerce, including the use of e-mail and the internet to provide the IMG F Offering Materials to customers in connection with their sales of the IMG F notes.

78. Based upon the foregoing, Carolina and Roberts effected transactions in, or induced the purchase of securities (IMG F notes) by means of the IMG F Offering Materials that were materially misleading and omitted material facts.

79. Carolina and Roberts, directly or indirectly, by the use of the means or instrumentalities of interstate commerce, or the use of e-mail, in connection with the offer or sale of the IMG F notes: (a) made untrue statements of material facts and omitted to state material facts to obtain money or property; and/or (b) engaged in transactions, practices, or a course of business which operated as a fraud or deceit upon the purchaser.

80. By engaging in the foregoing conduct, Carolina and Roberts acted in contravention of Section 17(a) of the Securities Act, thereby violating FINRA Rule 2010, and independently violated FINRA Rule 2010.

THIRD CAUSE OF ACTION — CAROLINA AND ROBERTS

FINRA Rules 2111(a) and 2010 (Reasonable Basis Suitability)

81. The Department realleges and incorporates by reference paragraphs 1 through 80 above.

82. FINRA Rule 2111 requires a member, when making a recommendation to purchase or sell a security, to have a “reasonable basis to believe that a recommended transaction ... is suitable for the customer....” A broker-dealer must first have a reasonable basis to believe, based upon a reasonable investigation, that the recommendation is suitable for at least some investors.

83. Carolina and its registered representatives have a duty to perform reasonable due diligence on securities products in order to understand the inherent risks of these products and to determine whether these products are suitable for its customers. This due diligence is especially important for alternative investments or private offerings, such as Reg. D offerings, where the securities are not registered with the U.S. Securities and Exchange Commission.

84. FINRA Regulatory Notice 10-22 reminded broker-dealers of their obligations when recommending a security, and, in particular, the regulatory requirements for Reg. D offerings. Regulatory Notice 10-22 notes that a firm's due diligence investigation must address NASD Conduct Rule 2310, which is now known as FINRA Rule 2111.

85. Carolina and Roberts knew or should have known of the following red flags in connection with the IMGF Offering:

- a. IMG failed to provide a complete copy of its VA contract;
- b. IMG's financial statements for November 2013 showed a spike in inventory;
- c. 99 percent of IMG's accounts receivable remained unchanged from August 31, 2013 to December 31, 2013;
- d. IMG failed to provide December 2013 financials despite Carolina's requests;
- e. IMG provided incomplete copies of bank account statements;
- f. IMG's cash position listed on its November 2013 financial statement did not reconcile with the balances in its bank accounts;
- g. IMG was engaged in litigation alleging that it defaulted on debts; and
- h. IMG needed immediate financing.

86. In light of these red flags, Carolina, acting as placement agent for the IMGF Offering, and Roberts failed to conduct reasonable diligence to understand the potential risks and rewards

of the IMGF Offering before recommending the IMGF notes to its customers. As a result, Carolina and Roberts were not in a position to determine whether the IMGF notes were suitable for any investors prior to recommending them to customers.

87. In short, despite numerous red flags, Carolina relied solely upon information provided by IMG and D.W. without independently verifying any of the information. Carolina, acting through Roberts, approved the sale of the IMGF notes, sold IMGF notes to customers and approved the transmittal of approximately \$2.3 million of investor funds to IMG.

88. Carolina and Roberts failed to heed the guidance provided in Regulatory Notice 10-22 and failed to conduct reasonable due diligence for the IMGF Offering before approving its sale to customers.

89. Roberts was responsible for Carolina's due diligence review, approved the IMGF Offering for sale by Carolina and approved the release of customer funds.

90. By failing to conduct reasonable due diligence to fulfill its reasonable-basis suitability obligation Carolina and Roberts violated FINRA Rules 2111(a) and 2010.

FOURTH CAUSE OF ACTION — CAROLINA AND ROBERTS

FINRA Rules 2210(d)(1)(A), 2210(d)(1)(B), and 2010 (Misleading Advertising Materials)

91. The Department realleges and incorporates by reference paragraphs 1 through 90 above.

92. Carolina prepared the IMGF Offering Materials in connection with the IMGF Offering, including, but not limited to, a flow chart, term sheet, information memorandum and a PPM. Roberts reviewed and approved the IMGF Offering Materials.

93. The flow chart, term sheet and information memorandum were provided to prospective investors.

94. The IMGF PPM, dated February 12, 2014, was not forwarded to investors, but was made available to investors on a web portal, to which customers were given access.
95. The information memorandum failed to disclose general and specific risks as well as investment fees and expenses of the IMGF Offering. The term sheet disclosed the investment fees and expenses, but failed to disclose general and specific risks associated with the IMGF Offering.
96. The IMGF PPM and information memorandum highlighted the existence of the VA contract and represented that “IMG holds a requirements contract with the Department of Veterans Affairs which contemplates the supply of \$90 mm worth of examination gloves of use in 34 VA facilities nationwide.”
97. The PPM states that a copy of the VA contract is attached, but the contract was not attached to the PPM.
98. While the PPM and the information memorandum represented that IMG had a contract with the VA valued at \$90 million, in reality the contract had a value of approximately \$125,000 and generated only about \$25,000 in annual sales.
99. The PPM and information memorandum also attached the November 2013 financial statement for IMG.
100. The November 2013 financial statement for IMG showed accounts receivable totaling \$36,685,772. The VAM001 account receivable represented almost 80 percent of the total accounts receivable for IMG.
101. In fact, as alleged above, the IMG financial statements were falsified and contained overstated accounts receivable.

102. Finally, Carolina and Roberts represented to customers in a flow chart, term sheet and the information memorandum that the loan from IMGF to IMG was secured by a first lien on substantially all of the assets of IMG, and that the loan and interest were guaranteed by D.W. While these documents were created, the documents were never executed, rendering these representations false.

103. The flow chart and information memorandum further failed to disclose that the interest payments were not guaranteed and that loss of principal was possible.

104. As a result of the foregoing conduct, Carolina and Roberts violated FINRA Rules 2210(d)(1)(A), 2210(d)(1)(B) and 2010.

FIFTH CAUSE OF ACTION — CAROLINA AND ROBERTS

NASD Conduct Rule 3010(a) and (b) and FINRA Rule 2010 (Failure to Enforce Supervisory Procedures)

105. The Department realleges and incorporates by reference paragraphs 1 through 104 above.

106. NASD Conduct Rule 3010 requires registered broker-dealers to establish, maintain and enforce a supervisory system reasonably designed to achieve compliance with applicable securities laws and regulations and FINRA rules.

107. Carolina's WSPs, in effect during the relevant period, required that the designated principal, in this case, Roberts, conduct due diligence and approve all offerings sold by Carolina.

108. FINRA Rule 2111 required Carolina to conduct reasonable due diligence of private placements such as the IMGF Offering prior to recommending such private placement to its customers.

109. As set forth in the Third Cause of Action above, Carolina, acting through Roberts, failed to conduct reasonable due diligence regarding the IMGF Offering.

110. Carolina and Roberts failed to enforce the firm's WSPs regarding its due diligence review, and its required suitability determination, in connection with the IMGF Offering.

111. As a result of the foregoing conduct, Carolina and Roberts violated of NASD Conduct Rule 3010(a) and (b) and FINRA Rule 2010.

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 that 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 Carolina and Roberts willfully violated Section 10(b) of the Exchange Act and Exchange Act Rule 10b-5.

FINRA DEPARTMENT OF ENFORCEMENT

Date: 4/29/2015


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