FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT, Complainant, v. CANTONE RESEARCH INC. (BD No. 26314), ANTHONY J. CANTONE (CRD No. 1066139), and CHRISTINE L. CANTONE (CRD No. 2687618), Respondents.	Disciplinary Proceeding No. 2013035130101 Hearing Officer–MC **EXTENDED HEARING PANEL DECISION** May 12, 2017

Respondents Cantone Research Inc. and Anthony J. Cantone intentionally made material omissions and a misrepresentation in connection with the sales of securities in a series of private placements, in violation of Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010. They negligently made additional material omissions in connection with the sales of securities, in violation of Sections 17(a)(2) and (3) of the Securities Act of 1933, and FINRA Rule 2010. For these violations, Anthony J. Cantone is suspended in all capacities for 15 months and he and CRI are fined $150,000 jointly and severally.

Respondent Cantone Research Inc., through Christine Cantone, failed to supervise Respondent Anthony J. Cantone reasonably, in violation of NASD Rule 3010 and FINRA Rule 2010. Christine Cantone is suspended in all capacities for six months and she and CRI are fined $75,000 jointly and severally.

Enforcement failed to establish that Cantone Research Inc. and Anthony J. Cantone made improper use of customer funds and recommended an unsuitable investment. The causes of action alleging these violations are dismissed.

Appearances

For the Complainant: Noel C. Downey, Esq., Mark Maldonado, Esq., Robert A. Fisher, Esq., and Christopher Kelly, Esq., Department of Enforcement, Financial Industry Regulatory Authority.

For the Respondent: Michael Gross, Esq., and Heidi E. VonderHeide, Esq., Ulmer & Berne LLP, Chicago, Ill.

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DECISION

I. Introduction

This case originated in 2013 with a routine FINRA cycle examination of Respondent Cantone Research Inc. ("CRI"). The examination focused on sales of a series of private placements by CRI and Anthony J. Cantone ("Cantone"). They offered high-risk investments to accredited investors. The funds raised were used to purchase notes from a real estate developer, Christopher F. Brogdon, a central figure in the offerings, who specialized in developing and selling assisted living facilities and retirement and nursing homes. Investors received securities that Cantone called Certificates of Participation ("Brogdon-related COPs" or "COPs"). From 2008 through 2012, CRI and Cantone made eight Brogdon-related COP offerings.

From 2010 to 2013, CRI and Cantone sold Brogdon-related COPs to approximately 100 investors for more than $8 million, earning more than $1 million in fees, commissions and other payments.[1] Although Cantone structured all eight offerings almost identically, with offering documents containing similar features and terms, the Department of Enforcement charged only five of them as fraudulent.[2] The thrust of the Complaint is that in those offerings, made over three years, CRI and Cantone knowingly defrauded investors by failing to disclose, or misrepresenting, more than a dozen negative events in the developer's lengthy business background. Enforcement insists that each undisclosed event constituted a material fact, and that CRI and Cantone's egregious conduct caused investors to lose more than $6 million. Enforcement argues that CRI should be expelled from FINRA membership and that Cantone should be barred from the securities industry.

For the reasons given in detail below, the Extended Hearing Panel sustains some of the fraud charges. The Panel concludes that CRI and Cantone's misconduct was serious but not egregious. The Panel also finds that the evidence does not support Enforcement's claim of $6 million in investor losses.

The Complaint also charges CRI and Christine Cantone with failing to supervise Cantone to ensure that he accurately and completely disclosed all material facts to potential investors in the COPs. Describing their supervisory violations as egregious, Enforcement seeks to bar Christine Cantone from the securities industry and expel CRI from FINRA membership.[3] The Panel concludes that although CRI and Christine Cantone failed to supervise appropriately, the evidence does not support imposing sanctions as severe as Enforcement recommends.

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[1] Enforcement's Pre-Hr'g Br., at 1-2; Complaint ("Compl.") ¶ 1.

[2] Enforcement did not explain why it elected to charge fraud in some offerings but not others.

[3] Enforcement's Pre-Hr'g Br., at 3.

Finally, the Complaint also charges CRI and Cantone with misusing customer funds and making unsuitable recommendations. The Panel finds the evidence insufficient to support these charges and dismisses them.

The Decision begins with a review of the details of the charges.

II. The Charges

The Complaint contains five causes of action. The first cause of action alleges that CRI and Cantone knowingly or recklessly made fraudulent misrepresentations and omissions of material facts in connection with the offer and sale of five Brogdon-related COPs from 2010 to April 2013, thereby willfully violating Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and SEC Rule 10b-5, as well as FINRA Rules 2020 and 2010.[4] Specifically, cause one of the Complaint alleges that CRI and Cantone failed to disclose that:

- Cantone, through Cantone Office Center, LLC, which he owned, failed to honor guarantees to pay interest and principal to investors in two promissory notes related to condominium projects, which defaulted in 2007 and 2009, respectively. The projects had no nexus to the Brogdon-related COPs.[5]
- The NASD twice barred Brogdon, in 1984 and 1985.[6]
- Brogdon was indicted for fraud in 1999.[7]
- An appellate court in 2003 affirmed a civil judgment filed against Brogdon holding that he had failed to honor a stock repurchase guarantee.[8]
- Several entities controlled by Brogdon were sued for fraud, subjected to tax liens, or filed for bankruptcy.[9]
- Brogdon missed or made numerous late interest payments to investors in three COPs.[10]

[4] Compl. ¶¶ 1, 88-89.

[5] *Id*. ¶¶ 26-29, 87e.

[6] *Id*. ¶¶ 31-32, 87a.

[7] *Id*. ¶ 87b.

[8] *Id.* ¶ 87c.

[9] *Id*. ¶¶ 33, 87d.

[10] *Id*. ¶ 87f.

- Brogdon failed to make required principal payments to investors in February and August 2012, and February 2013.[11]
- Cantone, Christine Cantone, and CRI covered Brogdon's late or missed interest payments to investors in violation of the terms of the prospectus, called a Confidential Disclosure Memorandum ("CDM"), for each of these offerings, which stated that payments of interest and principal were to come from the operation of the facility or from Brogdon, his wife, and Brogdon Family, LLC.[12]
- Cantone negotiated "secret terms" in extension agreements with Brogdon for two of the offerings, whereby he increased interest rates on the underlying promissory notes and charged additional fees without informing investors.[13]
- As of May 2013, Brogdon's entities owed interest payments and late fees amounting to approximately $350,000.[14]
- One of the projects had significant net losses for 2008, 2009, and 2010.[15]
- In 2012, Brogdon entities involved in three COP offerings lost more than $2 million.[16]
- Cantone misused $64,500 owed to investors in one offering to pay investors in a separate offering.[17]

The second cause of action charges, in the alternative, that CRI and Cantone made the alleged fraudulent misrepresentations or omissions negligently, violating Sections 17(a)(2) and (3) of the Securities Act of 1933 ("Securities Act"), and thereby violating FINRA Rule 2010.[18]

The third cause of action charges that CRI and Cantone made improper use of customer funds, in violation of FINRA Rules 2150 and 2010.[19]

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[11] *Id*. ¶ 87g.

[12] *Id*. ¶¶ 24, 87h. Brogdon managed the Brogdon Family, LLC, an entity held by Brogdon, his wife, his children, and a trust for his grandchildren that owns and operates healthcare facilities. Joint Exhibit ("JX")-6, at 21-22.

[13] Compl. ¶ 87i.

[14] *Id*. ¶ 87j.

[15] *Id*. ¶ 87k.

[16] *Id*. ¶ 87l.

[17] *Id*. ¶ 87m.

[18] *Id*. ¶¶ 91-95.

[19] *Id*. ¶¶ 97-104.

The fourth cause of action alleges that in recommending the eighth and last Brogdon-related COP offering, CRI and Cantone failed to conduct reasonable due diligence into the underlying real estate project and ignored multiple "red flags" about Brogdon and the financial soundness of Brogdon's entities, and therefore lacked a reasonable basis for believing that the offering was suitable for any investor. By recommending the investment, CRI and Cantone allegedly violated FINRA Rules 2111(a) and 2010.[20]

The fifth cause of action alleges that CRI, and Christine Cantone, as CRI's Chief Compliance Officer ("CCO") and responsible for supervising Cantone, while aware of the negative facts material to the Brogdon-related COP offerings, failed to supervise Cantone reasonably and ensure he disclosed all material facts concerning the COP offerings to prospective investors, in violation of NASD Rule 3010 and FINRA Rule 2010.[21]

Respondents deny the charges. CRI and Cantone also assert the affirmative defense that they relied upon the advice of legal counsel in determining what information to disclose to investors.

III. Respondents

A. Cantone Research Inc.

CRI has its main office in Tinton Falls, New Jersey, a branch office in New York City, and has been a FINRA member since 1990. It employs 28 people and operates a general securities business.[22]

B. Anthony J. Cantone

Cantone is CRI's owner, president, and chief executive officer ("CEO"), and has been registered as a General Securities Representative since 1982. He acquired additional registrations as a General Securities Principal, Research Analyst, Research Principal, and Investment Banking Representative.[23] He describes himself as an equity analyst specializing in high-risk small-cap equities.[24]

C. Christine L. Cantone

Christine Cantone is Cantone's spouse. She began her career in the securities industry with CRI in 1996 as a registered General Securities Representative. She acquired additional

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[20] *Id*. ¶¶ 106-09.

[21] *Id*. ¶¶ 110-13.

[22] Hearing Transcript ("Tr.") 147; Compl. ¶ 8; Answer ("Ans.") ¶ 8.

[23] Compl. ¶ 10; Ans. ¶ 10; JX-2, at 6.

[24] Tr. 613, 761.

registrations as an Introducing Broker-Dealer Financial and Operations Principal, Financial and Operations Principal, General Securities Principal, Municipal Securities Principal, Registered Options Principal, and Operations Professional. Except for a three-month hiatus from March through June 2012,[25] Christine Cantone was CRI's CCO and Cantone's supervisor from 2010 until 2014 when she resigned her position as CCO. She also managed the books for the Brogdon-related COP offerings. She now handles administrative tasks at CRI.[26]

Being currently registered, all three Respondents are subject to FINRA's jurisdiction.

IV. Facts

A. Cantone's First Dealings with Brogdon

Cantone met Brogdon and began a business relationship with him approximately five years before the first offering at issue here. We begin with a brief description of their initial dealings, a series of municipal bond offerings, and what Cantone learned about Brogdon's past.

1. The Municipal Bond Transactions

Cantone engaged in his first municipal bond deal with Brogdon in 2003.[27] He met Brogdon through James Friar, a registered representative Cantone hired that year.[28] Friar was a financial analyst and investment banker specializing in high-yield municipal bonds, an area outside Cantone's area of expertise.[29] Friar knew Brogdon from previous municipal bond deals and vouched for him, affirming "his personal experience with Brogdon had all been positive," Friar had "never had a problem" with Brogdon, and Brogdon had always paid interest and principal to bond investors when due.[30]

Friar also introduced Cantone to attorney Michael Gardner, who prepared the prospectuses for the bond deals.[31] Like Friar, Gardner had a prior long-term relationship with

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[25] During this period, Christine Cantone was suspended in all capacities pursuant to a Letter of Acceptance, Waiver and Consent for failing to properly supervise a registered representative who misappropriated $1.6 million in customer funds. She also agreed to pay a fine and restitution. Tr. 1205-6; JX-3, at 24-26.

[26] Compl. ¶ 12; Ans. ¶ 12; Tr. 1202, 1204-08, 1881; JX-3, at 6.

[27] Tr. 231.

[28] Tr. 231.

[29] Tr. 231-32.

[30] Tr. 233, 238.

[31] Tr. 341, 767-69.

Brogdon preceding Friar's move to CRI, and had represented other broker-dealers in Brogdon-related deals.[32]

Cantone participated in nine municipal bond offerings with Brogdon that Friar brought to CRI from 2003 to 2008.[33] Brogdon, his wife, and the Brogdon Family, LLC, guaranteed the offerings.[34] According to Cantone, although one offering had to be extended to pay investors, and there was a late payment in another, all were successful ventures—investors were repaid principal and earned interest.[35]

2. Cantone's Due Diligence on Brogdon

When Friar brought Cantone the first municipal bond deal in 2003, Cantone put him in charge of conducting due diligence. It was Friar who informed Cantone of Brogdon's history.[36] Cantone testified that Friar told him that there were red flags on Brogdon's record, including a bar from the securities industry imposed by the NASD in the early 1980s,[37] a 1990 bankruptcy filing by a company Brogdon managed,[38] and an indictment in 1999 for Medicaid fraud.[39]

According to Cantone, he and Friar discussed the materiality of these negative events, and Friar told Cantone he had spoken about them with Gardner.[40] Cantone claims he relied on Friar and Gardner— his "two trusted advisors"—and their advice that an NASD bar more than 20 years before was not relevant and need not be disclosed. Cantone stated that he thought Gardner, "this very competent, very qualified attorney," would disclose all required material information about Brogdon's past.[41]

For three of the bond offerings, the borrower was National Assistance Bureau, Inc. ("NAB"), a nursing home management company with which Brogdon was associated.[42] The

[32] Tr. 767-68, 1196-97.

[33] Tr. 305, 765, 786.

[34] Tr. 779.

[35] Tr. 768-69.

[36] Tr. 234-235.

[37] Tr. 257.

[38] Tr. 278-80.

[39] Tr. 292, 807; Respondent's Exhibit ("RX")-5.

[40] Tr. 233-35, 775-76.

[41] Tr. 269, 342.

[42] RX-280; RX-283; RX-286. Cantone testified that Brogdon told him NAB was a non-profit entity for which he served as an advisor to its board of directors. According to an SEC complaint filed against him, Brogdon controlled NAB. Tr. 277-81.

prospectuses Gardner drafted for these offerings disclosed that NAB filed for bankruptcy in 1990. However, they did not disclose other negative events in Brogdon's background that are the subject of the Complaint in this case, such as the NASD bars, criminal charges, civil suits, and tax liens filed against Brogdon or entities with which he was associated.[43]

B. Overview of the Brogdon-Related COPs

The first seven COP offerings involved nursing homes and assisted living facilities Brogdon acquired, developed, and managed.[44] The eighth involved a residential real estate project on land Brogdon purchased, the sole project whose operation was not managed by Brogdon, but by a realtor/builder experienced in constructing single-family homes.[45]

The eight Brogdon-related COPs had common features and terms. In addition, each had a CDM and a guaranty committing either Brogdon or another entity he owned and managed to make prompt payments of interest and principal.

1. Structure and Financing

As discussed in more detail below, the Brogdon-related COPs are almost identical in structure. For each, Cantone created a limited liability company ("issuing LLC") to issue the COPs that he sold to investors, raising capital for Brogdon to acquire, develop, and sell real estate and facilities. Each COP required a minimum investment of $10,000.

When an issuing LLC raised the required capital, it purchased a promissory note from an entity Brogdon controlled. Seven of the notes were to mature in two or three years; the eighth in five years.[46] The notes earned 10% interest annually, payable quarterly. At maturity, investors were to receive their principal and, when Brogdon sold or refinanced the project, a share of any profit or capital gain realized by Brogdon.[47]

2. The Confidential Disclosure Memoranda

For each offering, Cantone provided investors with a CDM that described the features of the offering. Each CDM was similar in format and content. The CDMs stated that principal and

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[43] Tr. 767-74; RX-280–RX-282; RX-285–RX-288.

[44] Tr. 226-27; JX-6, at 6 (Hoover); JX-7, at 7 (Columbia); Tr. 887-90 (Country Club); Tr. 896-99 (Limestone); JX-12, at 7 (Chestnut); JX-18; at 7 (Oklahoma); JX-23, at 7 (Cedars).

[45] JX-28, at 7-8.

[46] JX-7, at 1-2; JX-12, at 1; JX-18, at 1; JX-23, at 1; JX-28, at 1.

[47] Tr. 96.

interest were to be paid solely from revenues generated from the operation of the underlying facility or payments pursuant to the guaranty.[48]

The CDMs stated that COP holders might receive funds in addition to payments of principal and interest. These included contingent semi-annual payments starting after the maturity date of the note, if the facility generated sufficient cash.[49] Furthermore, upon the sale or refinancing of the facility, investors were to receive a proportionate share of any capital gain realized by the sale or refinancing. This is what Cantone referred to as the "very important" equity component of all of the Brogdon-related COPs.[50]

The CDMs for the Brogdon-related COPs at issue all contained a section with a favorable biographical sketch of Brogdon. They described him as co-founder in 1987 of Winter Haven Homes, Inc., a company that "developed, owned and operated assisted living and nursing homes primarily in the Southeastern United States." The CDMs represented that Brogdon had worked in the "assisted living, nursing home and retirement community business for more than 20 years," and that he served as Chairman of the Board of Retirement Care Associates ("RCA"), which also operated assisted living and retirement homes, from 1991 to 1998. The CDMs stated that, from 1994 to 1998, Brogdon was chairman of a Nasdaq-listed medical supply company, and from 1998 to 1999, he was the chairman of NewCare Health Corporation ("NHC"), also a Nasdaq-listed company. According to Cantone, the biographical sketches of Brogdon in the CDMs had the same information as those in the offering materials for the municipal bond offerings he had previously conducted with Brogdon.[51]

The CDMs described risks, warning investors they should purchase Brogdon-related COPs only if they were able to bear the risk involved, which was commensurate with the potential for high yield.[52] In the section describing contingent payments, the CDMs had a bold-font paragraph in capital letters warning investors that there was no assurance that cash flow would generate contingent payments.[53]

Although he acknowledged he was ultimately responsible for the contents of the CDMs, Cantone testified that he applied a "hands-off policy" about deciding what should be disclosed in the CDMs, having delegated that decision to Friar and Gardner.[54]

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48 JX-6, at 15-16; JX-7, at 21-22; JX-12, at 24-25; JX-18, at 29-30; JX-23, at 19-20; JX-28, at 18.

49 *See, e.g.,* JX-6, at 14; JX-7, at 19-20.

50 Tr. 95-97.

51 Tr. 335-40.

52 *See, e.g.,* JX-6, at 3, 17; JX-7, at 4, 25.

53 *See, e.g.,* JX-6, at 2; JX-7, at 2.

54 Tr. 338.

3. The Brogdon Guaranty

Except for the last offering, a common feature of the COPs was the Brogdon Guaranty Agreement. The terms of the Guaranty were straightforward. It named Brogdon, his wife, and the Brogdon Family, LLC as guarantors. It stated that the guarantors provided the Guaranty as a "condition precedent" to the purchase of the underlying note. The Guaranty pledged that the guarantors, for the benefit of the issuing LLC and the holders of the COPs, "absolutely and unconditionally" guaranteed the "prompt payment and performance, as and when due, of all . . . obligations" pursuant to the note to the extent the venture succeeded in generating cash flow, achieved capital gains, or successfully refinanced. The guarantors also agreed to pay all expenses, including legal fees the issuing LLC might incur to enforce the Guaranty. Brogdon signed it personally, and as manager of Brogdon Family, LLC.[55]

According to Cantone, after completing the municipal bond offerings and before issuing the Brogdon-related COPs, he conducted additional due diligence to evaluate the strength of the Brogdon Guaranty. This included a review of Brogdon's financial statements and tax returns.[56] Cantone testified he "wouldn't have done those [Brogdon-related] deals without the guaranty."[57] Cantone further testified that he required Brogdon to provide the Brogdon Guaranty because he wanted Brogdon to have "skin in the game," *i.e.*, a personal commitment to pay investors if a project floundered.[58] Cantone testified that the Brogdon Guaranty "was an important selling point" for the COPs.[59]

C. The Eight Brogdon-Related COPs

Below we discuss the eight Brogdon-related offerings. The offerings are organized chronologically beginning with the earliest, issued in 2008. Although there are similarities among the eight offerings, Enforcement's charges of fraudulent and negligent misrepresentations and omissions relate only to five.

1. Hoover, Issued December 8, 2008

Hoover Financial LLC ("Hoover") was the first issuing LLC Cantone created to offer Brogdon-related COPs.[60]

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[55] JX-9; JX-15; JX-20; JX-25.

[56] Tr. 230.

[57] Tr. 101.

[58] Tr. 101-02.

[59] Tr. 229.

[60] Tr. 306.

The Hoover CDM stated that the plan was for Hoover to purchase a $1.5 million secured promissory note from a Brogdon entity, Ridgeview Assisted Living LLC ("Ridgeview").[61] A second mortgage lien on the underlying assisted living facility secured the note and the Brogdon Guaranty guaranteed prompt payment of interest and principal.[62] Ridgeview was to use the proceeds from its sale of the promissory note to pay part of the cost of acquiring an assisted living facility located in Hoover, Alabama. Investors were to receive 12 percent interest annually and return of their principal when the note matured. After maturity, until the sale of the facility, investors were to receive additional payments of interest at 8 percent until Brogdon sold or refinanced the facility. Upon sale or refinancing, investors would receive a share of any gain proportional to their investment, as would Cantone.[63]

Friar, who had recently left CRI, brought the proposal to Cantone at the end of 2008.[64] According to Cantone, Friar brought him the due diligence materials he had collected on the project, and they spent two or three days reviewing the materials together.[65] Cantone testified that they reviewed Ridgeview's state-issued operating license, drawings of the facility, a realtor's memorandum describing the property, a menu of meals served to residents,[66] and 2007 real estate tax bills giving an assessed market value.[67]

Cantone testified that he also updated himself on Brogdon's financial status, reviewing tax returns and a financial statement.[68] Cantone claimed he "wanted to revisit" the negative background Friar had disclosed to him prior to the municipal bond offerings in 2003, including the criminal charges, the NASD disciplinary proceedings, and the class action suit. According to Cantone, he asked Brogdon to explain these events. In response, Brogdon provided a copy of a May 2008 letter, written by his attorney to a third party, containing a brief explanation.[69]

The letter stated that Brogdon's law firm had investigated and determined the criminal charges were "utterly groundless" and had convinced the prosecutor to drop them. It stated that in 1984 the NASD filed a complaint and imposed a bar for net capital violations. The letter claimed that Brogdon had decided to ignore the complaint because he lacked funds to litigate and had decided not to return to the securities business. The letter stated that in 1994, when Brogdon

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[61] JX-6, at 1.

[62] JX-6, at 1.

[63] JX-6, at 2.

[64] Tr. 784-85.

[65] Tr. 787-788.

[66] Tr. 789-91; RX-28–RX-32.

[67] Tr. 791-92; RX-37.

[68] Tr. 806.

[69] Tr. 807-09; RX-5.

was chairman of the board, CEO, and a major stockholder of Retirement Care Associates, RCA applied for listing on Nasdaq. According to the letter, the application was initially denied because of the NASD bar. Brogdon then obtained a hearing for an exception and the Nasdaq Listing Qualifications Committee approved the application. Finally, the letter stated that in 1997, securities class action lawsuits were filed against RCA and Brogdon when a merger of RCA with Sun Healthcare, Inc. was to occur, but the suits settled with Brogdon receiving a full release.[70] According to Cantone, Sun Healthcare then proceeded with the merger and purchased RCA.[71]

As with later Brogdon-related COPs, Cantone testified that he required Brogdon to provide "his personal guaranty" to make payments of interest and principal promptly.[72]

The Hoover note was to mature in January 2010.[73] Cantone testified that after only nine months investors received repayment of principal and a full year's interest. According to Cantone, investors have subsequently received additional payments amounting to 16 percent of their investment, for a total return thus far of 28 percent. Cantone testified that he expects investors to share in an additional payment from Brogdon of at least $645,000 when the facility is sold.[74]

Although the Hoover CDM contained the same representations about Brogdon as the other Brogdon-related CDMs, with the same negative facts omitted, Enforcement did not include the Hoover offering in the Complaint.

2. Columbia, Issued In February 2010

Cantone created Columbia Financial, LLC ("Columbia") to conduct the second Brogdon-related COP offering. It is the first offering Enforcement included in the Complaint. Cantone solicited investors to buy COPs to participate in the purchase of a secured promissory note for $1.75 million from a Brogdon entity, Polo Road Assisted Living, LLC ("Polo Road").[75] Columbia offered 10 percent interest and a share of any capital gains, with the note to mature in two years.[76] Cantone raised the $1.75 million from approximately 70 investors over a three-week period in February 2010.[77]

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[70] RX-5, at 2-3.

[71] Tr. 809.

[72] Tr. 228-29.

[73] JX-6, at 2.

[74] Tr. 805-06.

[75] JX-7, at 1.

[76] JX-7, at 2.

[77] Complainant's Exhibit ("CX")-24.

When Brogdon proposed the project, the property consisted of an unoccupied assisted living facility and independent living apartments.[78] It was in foreclosure, and the required operating licenses had expired.[79] It had a $6 million mortgage, but its assessed value was only $4 million. Brogdon, through Polo Road, was to use the investor funds Cantone raised to pay part of the $3.1 million purchase price, almost $1 million less than the assessed value. The goal was eventually to sell it for more than $6 million.[80]

Cantone testified that for Columbia, as for every offering guaranteed by Brogdon, his due diligence included reviews of Brogdon's then-current financial status.[81] In addition, his due diligence for the Columbia offering included review of a detailed real estate appraisal,[82] numerous other documents relating to Polo Road's planned purchase of the facility,[83] and an on-site visit.[84] Cantone was favorably impressed with the project, particularly with the low purchase price. He directed Gardner to prepare a CDM reflecting the terms he negotiated with Brogdon.[85] Cantone testified that he and Gardner exchanged numerous emails during Gardner's drafting of the Columbia CDM.[86] As with other offerings, Cantone described the offering in the CDM as a high-risk investment with a potential for a high rate of return.[87]

The CDM stated the payment of principal and interest was secured by a second mortgage lien on the facility and guaranteed by the Brogdon Guaranty.[88]

If the facility generated sufficient cash flow, investors would receive a share proportionate to their investment through additional semi-annual payments.[89] Furthermore, upon the sale or refinancing of the facility, investors were to receive a proportionate share of any capital gain realized by the sale or refinancing.

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[78] JX-7, at 11.

[79] JX-7, at 10.

[80] Tr. 834-35; JX-7, at 12.

[81] Tr. 825-27, 878-79.

[82] Tr. 833-36; RX-42.

[83] Tr. 836-39; RX-44−RX-54.

[84] Tr. 828-29; RX-43.

[85] Tr. 859-62.

[86] RX-360 is an exhibit Cantone testified consists of the email exchanges with Gardner relating to the drafting of the Columbia CDM; in hardcopy form, it is more than 1,000 pages. Tr. 859.

[87] Tr. 829-30.

[88] JX-7, at 1.

[89] JX-7, at 2.

The first interest payment came due on May 1, 2010.[90] Brogdon sent a check six days late.[91] It was not for the full amount due. According to Cantone, Brogdon explained the payment was short because of a "bookkeeping error."[92] The Cantones provided funds to enable Columbia to pay investors their interest in full.[93] Brogdon reimbursed the Cantones the following month.[94]

Enforcement calls Brogdon's failure to pay on time and in full a default and argues that Cantone should have disclosed it to Columbia investors, as well as to investors in subsequent COPs.[95] The Columbia promissory note defined default as a failure to make payment within five days of receiving notice from the issuing LLC that interest was not paid when due.[96] Cantone did not deem Brogdon's late payment to be a material issue.[97] To him, it was a bookkeeping error, corrected quickly, and unnecessary to disclose to Columbia investors or to investors in subsequent offerings.[98]

The Columbia note matured on February 1, 2012. Polo Road did not repay the principal.[99] On April 20, Cantone complained in an email that Brogdon's failure to pay the principal on time and his tardiness in making an equity payment in the completed Hoover offering made it difficult to solicit investments in other upcoming Brogdon-related COPs.[100]

Brogdon failed to make the interest payment that was due on May 1.[101] Cantone wired his own funds to Columbia to make this interest payment to investors; the wire memo described the payment as a "personal investment in private placement."[102] When Brogdon missed the next

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[90] Tr. 402-03.

[91] Tr. 404.

[92] Tr. 195, 406-07, 519, 532.

[93] Tr. 404-06; CX-25.

[94] Tr. 407.

[95] Enforcement's Post-Hr'g Br., at 8-9.

[96] JX-8, at 2.

[97] Tr. 406-07, 531-32.

[98] Respondents' Post-Hr'g Br., at 43-44.

[99] Tr. 409-10.

[100] CX-27.

[101] CX-28.

[102] CX-29, at 2.

interest payment on August 1, 2012, Cantone notified Brogdon that he was in default.[103] Cantone "loaned" the money to Columbia to pay interest to investors.[104]

On October 1, 2012, Cantone agreed to extend the Polo Road note maturity to February 1, 2013. The extension agreement stated that Polo Road had been unable to pay principal because the facility had not achieved sufficient occupancy.[105] The agreement increased Brogdon's interest on the note to 14 percent, added $68,000 more in principal, an extension fee of more than $80,000, and attorney's fees of $3,000.[106] The letter Cantone sent to Columbia investors to inform them of the extension did not inform them of Brogdon's missed interest and principal payments or of the additional fees and interest.[107]

When questioned at his on-the-record testimony ("OTR"), Cantone testified that the additional 4 percent interest was to be paid to him, not to investors, who would continue to receive 10 percent interest. He testified that he did not disclose this to Columbia investors.[108]At the hearing, Cantone changed his story, and testified that he disclosed the increased interest rate and offered investors the 14 percent interest rate in writing. But this written disclosure occurred more than a year after the fact, in February 2014, after the 2013 FINRA examination cited him and CRI for their failure to disclose these facts.[109]

In January 2013, Brogdon informed Cantone he would be unable to pay Columbia investors their principal due on February 1 because of the facility's low occupancy. On February 5, Cantone told Brogdon he was willing to extend the due date again. He noted that he had to buy out four investors who were unwilling to agree to the first one-year extension, and told Brogdon to pay $68,000 to cover interest to investors, plus $1,000 in attorney's fees. Brogdon replied, "It's on the way."[110]

On February 12, 2013, Cantone sent Brogdon the second extension agreement, postponing the maturity date to February 1, 2014.[111]After the extension, Brogdon continued to

[103] CX-31.

[104] CX-32.

[105] CX-33, at 1.

[106] CX-33, at 2.

[107] Tr. 450-54, CX-34.

[108] Tr. 444-47.

[109] Tr. 444-47, 487-91; CX-46, at 3; CX-102, at 19. Cantone testified at the hearing that he never collected 14 percent interest from Polo Road but claimed that if he had, he would have given investors the benefit of the higher rate. Tr. 1105.

[110] CX-35−CX-36.

[111] CX-37, at 1-2.

miss interest payment deadlines. As a result, Cantone loaned Columbia funds to cover interest payments in May, August, and November 2013, and February 2014.[112]

On November 7, 2014, Columbia sued Polo Road, Brogdon, his wife, and the Brogdon Family, LLC for the unpaid principal, interest, and attorney's fees.[113] On January 4, 2016, the court granted summary judgment in favor of Columbia.[114]

In December 2016, after the hearing in this proceeding, the property sold for $5 million as Cantone expected. Columbia received more than $2.8 million and has paid the investors their principal and all interest due, making their investment profitable.[115]

Enforcement charges that Cantone's and CRI's failures to inform Columbia investors of these late and missed interest payments by Brogdon constitute fraudulent material omissions.[116]

3. Country Club, Issued July 22, 2010

The Country Club, LLC ("Country Club") offering was issued on July 22, 2010, shortly after the Columbia offering.[117] The underlying facility was a functioning assisted living residence.[118] The CDM promised investors annual interest at 10 percent, and a potential share of any capital gains.[119] The CDM Gardner prepared included the Brogdon Guaranty, and the same disclosures that were in the Columbia and Hoover CDMs.[120] According to Cantone, the due diligence he performed for Country Club included visiting the property twice and obtaining an appraisal and environmental study. Cantone characterized it as "very similar" to the due diligence he performed before issuing the Columbia offering.[121]

The original maturity date was in August 2012. Brogdon failed to make required interest payments, and defaulted on the principal.[122] Cantone claimed he discussed the matter with all of

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112 Tr. 174-75, 1330-31, 1336-39; CX-42−CX-44.

113 Tr. 876-77.

114 RX-301.

115 Tr. 871-73; RX-382; RX-383; Respondents' Motion to Reopen Record to Have Additional Exhibits Admitted into Evidence.

116 Compl. ¶¶ 87-89.

117 Tr. 893-94.

118 Tr. 890.

119 Tr. 888.

120 Tr. 891.

121 Tr. 890-91.

122 Tr. 892.

the investors when the note matured and extended the maturity date to give Brogdon additional time to sell the facility. Investors continued to receive interest at 10 percent per year for the extension period, and when Brogdon succeeded in selling the facility, investors received "capital gain close to 25 percent"[123] and an equity distribution of eight percent.[124]

4. Limestone, Issued December 1, 2010

Cantone created Limestone Financial, LLC ("Limestone") to raise $500,000 to lend to Brogdon to assist in the completion of constructing, furnishing, and equipping a new assisted living facility.[125] Cantone issued the Limestone offering on December 1, 2010, and purchased the note on December 31.[126] It contained the Brogdon Guaranty.[127] Limestone offered interest at 10 percent, return of principal on maturity in two years, and a 20 percent share in any capital gain upon sale of the facility.[128] According to Cantone, the due diligence he conducted tracked that of the earlier offerings, and, as previously, Gardner prepared the CDM.[129]

Brogdon did not repay principal when due in January 2013. Cantone testified that he "had to extend" the note's maturity date to February 1, 2014. The extension agreement increased Brogdon's interest from 10 percent to 14 percent, charged an extension fee of 20 percent, and assessed attorney's fees of $3,000.[130] Brogdon sold the property in 2014. Although investors received return of their principal and accrued interest, Brogdon has not provided an accounting of realized gain or loss; Cantone testified that he was contemplating filing suit against Brogdon to require Brogdon to pay any shared equity due under the COP.[131]

Despite the similarities in the CDMs, containing the same disclosures and omissions to disclose facts about Brogdon's business history, Enforcement did not charge CRI and Cantone with fraud in connection with sales of Country Club or Limestone COPs and neither offering is mentioned in the Complaint.

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[123] Tr. 893-95.

[124] Tr. 896.

[125] RX-72, at 1.

[126] Tr. 898-99; RX-73, at 1.

[127] Tr. 109-10.

[128] Tr. 898-900; RX-73, at 1.

[129] Tr. 900.

[130] Tr. 900-03; RX-73.

[131] Tr. 900-02.

5. Chestnut, Issued February 24, 2011

The next project Brogdon proposed to Cantone, and the second one included in the Complaint, involved another purchase of assisted living apartments and independent living homes. Friar referred Brogdon and this project to Cantone after first trying to raise the funds at another firm.[132] Cantone created Chestnut Financial, LLC to offer COPs to purchase two notes issued by two Brogdon entities: a $1.175 million note issued by Chestnut Independent Living, LLC, and a $775,000 note issued by Highlands Assisted Living, LLC. According to the CDM, the two entities would use investors' funds to pay part of the cost of buying two senior living facilities. The notes were unsecured but contained the Brogdon Guaranty.[133] Brogdon was to manage the properties and pay principal and interest from revenues realized from the ownership and operation of the living units, or from his own funds as guarantor.[134] In contrast to the Columbia promissory note's definition of default as payment later than five days after notice, the Chestnut promissory notes defined default as failure to pay within 15 days of a due date.[135]

Cantone visited the facility as part of his due diligence review. He testified that he was originally concerned about Brogdon's valuation of the facilities because they had a negative cash flow at the time.[136] He asked Brogdon how he expected to be able to pay interest and principal from revenues as the CDM required him to do, given the poor cash flow for 2009 and 2010.[137] Brogdon told Cantone the project would break even when it achieved 50 percent occupancy.[138]

After further review, Cantone concluded that the Chestnut project was "an exceptional value."[139] Brogdon had a contract to purchase the property for approximately $7 million. Cantone learned from a local real estate broker that the individual homes, constituting the independent living part of the project, could be sold for $10 million, without including the assisted living apartments and clubhouse.[140] Cantone reviewed a 2010 bank appraisal that valued the property at

[132] Tr. 915-16, 918-19.

[133] Tr. 528-29; JX-12, at 1-2.

[134] Tr. 521-22.

[135] Tr. 527-28; JX-13, at 2.

[136] Tr. 906.

[137] Tr. 914; RX-77.

[138] Tr. 921-22; RX-86.

[139] Tr. 562.

[140] Tr. 906-07.

$8.4 million.[141] He learned that the prior owner had paid $22 million to acquire the facility and Brogdon's proposed purchase price was only about a third of that amount.[142]

Cantone solicited investors, sending a number of them an email providing a four-point summary that highlighted the following: (i) 10 percent interest per year for three years, paid quarterly; (ii) principal repaid in three years; (iii) the Brogdon Guaranty; and (iv) equity ownership, entitling investors to additional payments from the cash flow of up to 8 percent of each investor's initial investment, and a share of any capital gain realized at the end.[143] Cantone told one prospective investor that Chestnut was less risky than other private placements Cantone was working on because it involved the purchase of distressed real estate on which the mortgagor bank was willing to take a loss, and was guaranteed by Brogdon, with whom Cantone stated he had been working "for 12 years on 14 projects with not a single default."[144]

Cantone raised nearly $1.8 million.[145] Brogdon did not make the first quarterly interest payment for Chestnut when it was due on June 1, 2011,[146] but paid it within the 15-day grace period as provided in the Chestnut CDM.[147] Nonetheless, Cantone told Brogdon the late payment impeded his ability to convince prospective investors to put money in other Brogdon-related projects.[148]

At about the same time, to help Brogdon avoid damage to his reputation, Cantone gave Brogdon a loan to prevent a default on an unrelated bond deal offered by another firm.[149]

The next interest payment for Chestnut came due on September 1, 2011. Brogdon failed to pay it, and Cantone covered it so Chestnut could pay investors their interest.[150]

In February 2012, Cantone sent an email to Brogdon reminding him that an interest payment was due March 1, and expressing concern over whether he would be able to pay it on time. On March 8, Cantone sent another email with an invoice stating the interest payment was past due, complaining that investors were calling him about Brogdon's failure to pay principal to

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[141] RX-75, at 2-3.

[142] Tr. 906, 909.

[143] Tr. 533-34; CX-53a, at 3; CX-53b, at 1; CX-53c; CX-53d.

[144] CX-53a, at 2.

[145] Tr. 535.

[146] CX-55, at 3.

[147] Tr. 540.

[148] Tr. 537-39, 547.

[149] Tr. 550; CX-55, at 2; CX-109.

[150] Tr. 553-4; CX-57.

Columbia investors, and stating he did not want prospective investors to start worrying about the timeliness of payments on other projects like Chestnut. Cantone reminded Brogdon that if he did not pay interest by March 15, he would be in default, and the interest rate would rise to 18%. On March 20, Cantone deposited a check with the notation "bridge loan" to cover Chestnut investors' interest.[151] On March 29, past the 15-day grace period, Brogdon made the interest payment.[152]

The next interest payment was due on June 1, 2012. Again, Brogdon failed to pay. On June 8, Cantone loaned the funds, at no interest, to Chestnut to pay investors.[153] On July 12, Cantone sent Brogdon an email reminding him the June interest payment was still outstanding, and the previous quarter's interest had been late enough to give Chestnut the right to declare it in default.[154]

The next interest payment was due on September 1, 2012. In a September 11-12 email exchange, Cantone reminded Brogdon he had not made the payments due on June 1 and September 1 despite his personal guarantee.[155] On September 12, Cantone again loaned Chestnut funds for the September interest,[156] and again on December 4, 2012.[157] Later, on December 17, Chestnut received a payment from Brogdon for the December interest.[158]

On March 19, 2013, Brogdon sent Cantone an email saying he was "scrounging" for the then-due Chestnut interest payment. The next day, Cantone replied that he had gotten "many phone calls from investors" about late interest payments, and told Brogdon to send the payment by the end of the week.[159] Cantone testified that by this time he was "getting concerned" that Brogdon was overextended.[160]

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[151] Tr. 567-69; CX-60, at 4.

[152] Tr. 569; CX-60, at 3.

[153] Tr. 577; CX-62, at 1.

[154] Tr. 578-79; CX-61.

[155] CX-63, at 1-2.

[156] Tr. 581-82; CX-64.

[157] Tr. 582-84; CX-65.

[158] Tr. 584-85; CX-65.

[159] CX-67, at 2-3.

[160] Tr. 596.

A May 24, 2013 Chestnut invoice to Brogdon reflected unpaid interest payments for March, June, and September 2012, and March 2013, and interest that would come due on June 1, 2013, plus administrative fees, for a total of $350,025.[161]

In December 2013 and March 2014, Cantone again loaned the funds to Chestnut to make interest payments to investors that Brogdon should have paid.[162] Cantone did not disclose to Chestnut investors that he was providing the funds.[163]

Principal came due on March 1, 2014. On June 24, 2014, Chestnut notified Brogdon that the note was in default and demanded payment. On August 12, Chestnut filed suit to enforce the Brogdon Guaranty.[164]

Chestnut obtained a judgment against Brogdon.[165] At the hearing in this disciplinary proceeding, Cantone testified that the property was on the market, with the assisted living facility listed at $5.7 million and the homes being sold by a realtor who has informed him she expects to sell eight to ten homes annually. Cantone estimates the value of the property at completion will be $13 to $15 million, which is $5 million to $7 million more than Brogdon had paid to acquire and improve the property.[166] Cantone testified that the unanticipated need for extensive improvements required to ready the facility for sale caused the problems encountered in the offering.[167] Currently, the Chestnut project remains in default and investors have not yet received full interest or principal from Brogdon.[168]

Enforcement argues that Cantone's representation to a prospective Chestnut investor that Brogdon had not defaulted on a single project was false, because when he made that statement in February 2011, Brogdon had already defaulted on the first payment of interest to Columbia.[169] Cantone, however, testified that Columbia had not declared the May 2010 payment a default because it was just a "bookkeeping error" Brogdon corrected within a month.[170]

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[161] CX-69.

[162] Tr. 619-21; CX-70; CX-71.

[163] Tr. 587.

[164] Tr. 620-22; CX-73.

[165] Tr. 607, 926.

[166] Tr. 926-29.

[167] Tr. 927-28.

[168] Tr. 604.

[169] Tr. 531-32; Enforcement's Post-Hr'g Br., at 14.

[170] Tr. 531-32.

6. Oklahoma, Issued July 22, 2011.

Cantone created Oklahoma Financial, LLC ("Oklahoma") to offer $2.8 million in COPs to purchase a promissory note issued by Oklahoma Operating, LLC, a Brogdon entity. Like the note in the Chestnut offering, this one was guaranteed by the Brogdon Guaranty.[171] This is the third offering included in the Complaint.

Brogdon was to use the funds raised to purchase five nursing homes operating in separate Oklahoma locations.[172] The fact that the purchase price of each of the nursing homes was significantly below the appraised value of the homes, even though the real estate market had hit bottom, impressed Cantone.[173]

Cantone testified that he did not need to visit the Oklahoma nursing homes as part of his due diligence. The facilities were operating successfully, and he was satisfied with the appraisals, the facilities' cash flow, their financial statements, and Brogdon's documentation of his finances. Cantone gathered documents similar to those he had reviewed in the due diligence for the previous COP offerings: environmental assessments; appraisals prepared by the same real estate appraiser who prepared the Chestnut appraisal, in whom he had confidence;[174] and operating agreements for all five of the nursing homes.[175] Brogdon sent Cantone eight months of financial statements from the previous owner of the five nursing homes.[176] Cantone and Brogdon also exchanged emails discussing details of the operation of the homes, including consideration of the differing daily rates Medicaid and Medicare paid for nursing home services.[177]

As with the previous offerings, Cantone testified that attorney Gardner was "in charge" of ensuring the offering documents contained appropriate disclosures and complied with securities regulations.[178] Gardner drafted the Oklahoma CDM, dated July 22, 2011. Its terms tracked those of the previous offerings: 10 percent interest, payable quarterly, maturity in two years, semi-annual equity payments to be generated by operating proceeds, and a proportionate share of any capital gains earned when the nursing homes were sold or refinanced.[179] Like the Chestnut CDM,

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[171] JX-18, at 1-2. In addition, Brogdon and his wife signed a certification stating the representations in the Oklahoma CDM about Brogdon, his wife and the Brogdon Family, LLC were accurate, and that there were no material omissions. Tr. 950-51; RX-111.

[172] Tr. 932-33; JX-18, at 1.

[173] Tr. 942-43; RX-95.

[174] Tr. 935-42; RX-95.

[175] Tr. 957; RX-114–RX-18.

[176] Tr. 948-49; CX-109.

[177] Tr. 946-48; RX-108.

[178] Tr. 958.

[179] Tr. 624-26; JX-18, at 1-3.

the Oklahoma CDM provided for a 15-day grace period from the due date of interest and principal payments before a missed payment would be considered a default.[180] The risk warnings stated that there was no assurance that the homes would generate sufficient revenues to pay investors the semi-annual contingent payments, and no assurance investors would receive capital gains.[181]

Cantone solicited investors for Oklahoma from June through August 2011 to raise $2.8 million to purchase the note from Oklahoma Operating, LLC.[182] In some communications with prospective investors, Cantone identified the Brogdon Guaranty as a selling point, and extolled Brogdon's "highly successful" accomplishments.[183]

These solicitations occurred at the same time that Cantone told Brogdon that investors in earlier COPs were concerned about his inability to honor his guarantee on another project and that he was "stretched too thin."[184]

When an Oklahoma investor who had sent Cantone a $25,000 down payment raised questions about the Oklahoma COP, Cantone responded that while the Brogdon Guaranty "has significant merit," it did not eliminate the risk involved. Cantone offered to let the investor withdraw his funds.[185]

Cantone testified that at this point, in July 2011, despite some investors' concerns about the Brogdon Guaranty, and despite having provided Brogdon a bridge loan to help him avoid default on an unrelated project, he was still "comfortable" with Brogdon.[186]

According to Cantone, Brogdon managed to make interest payments to Oklahoma investors "pretty timely."[187] However, Brogdon did not pay the principal when it came due in July 2013. Consequently, Cantone extended the maturity date of the note to January 15, 2014, increasing the interest rate Brogdon was to pay Oklahoma from 10 to 14 percent, charging an extension fee of $56,000 and attorney's fees of $2,000.[188]

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180 Tr. 627; JX-19, at 2.

181 JX-18, at 2, 3.

182 Tr. 624, 628-29; CX-74.

183 CX-75b, CX-75c, CX-76.

184 Tr. 631; CX-55.

185 Tr. 635-38; CX-76.

186 Tr. 639.

187 Tr. 960.

188 Tr. 642-43; CX-78.

Cantone testified that he did not mail a copy of the extension agreement to his investors.[189] And Cantone did not disclose the extension fees to Oklahoma's investors. However, he testified that he "fully disclosed" the increase in the interest rate.[190] The credible evidence conflicts with this testimony. In a letter Cantone sent to Oklahoma investors describing the extension agreement, he wrote that Brogdon had agreed to continue paying 10 percent interest. The letter does not disclose the increase to 14 percent.[191] When asked about this in his OTR, Cantone testified that investors were "not interested in my 4 percent extra I'm getting"—they just wanted to know they would continue to receive the promised 10 percent. Cantone later acknowledged, in response to the 2014 FINRA letter summarizing the findings of the 2013 FINRA examination, that the letter "contained an error of fact regarding the actual interest rate the borrower agreed to pay."[192]

Pursuant to the terms of the extension agreement, Brogdon owed interest and fees of $112,000; however, Brogdon paid only $84,000, the amount due prior to the extension.[193] Cantone did not inform Oklahoma investors of the underpayment.[194]

Brogdon defaulted on the principal payment that came due on January 15, 2014, the extended maturity date. Cantone then filed suit against Brogdon, his wife, and the Brogdon Family, LLC, and obtained a judgment for return of principal and interest. Cantone testified at the hearing in this disciplinary proceeding that the homes were listed for sale for $14 million and that two potential buyers have shown interest. Since Brogdon paid $11.5 million, and did not need to invest in any significant capital improvements, Cantone believes if they are sold for the asking price, investors will obtain a substantial capital gain.[195]

7. Cedars, Issued August 24, 2011

The Cedars CDM offered investors $550,000 in COPs to purchase a promissory note maturing in two years, issued by Cedala, LLC ("Cedala"), an entity owned by Brogdon's wife, Connie Brogdon, and managed by Brogdon. Cedala was an equity owner of an assisted living facility; Connie Brogdon was to use the proceeds from the sale of the note to redeem 25 percent of her membership in Cedala, which she would convey to Cedars Financial, LLC, Cantone's

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[189] Tr. 646-49.

[190] Tr. 641-44, 651-52.

[191] CX-77.

[192] Tr. 652. Cantone testified that his practice was to offer to buy out investors who did not agree to extend the maturity date of the note, but when he bought out an investor, the investor lost the opportunity to receive contingent equity payments and any share of the capital gains realized on sale of the homes. Tr. 649.

[193] Tr. 653-54.

[194] Tr. 654.

[195] Tr. 960-63; RX-346.

issuing LLC, to hold on behalf of the COP purchasers. The COPs offered 10 percent annual interest and return of principal at maturity.[196] The note was unsecured but payments of principal and interest were guaranteed by the Brogdon Guaranty.[197] Brogdon was the project manager.[198]

Brogdon had first proposed the project in an August 15, 2011 email, writing that Cantone could purchase a 25 percent interest in a "very profitable" assisted living facility worth $6 million. Brogdon wrote that he intended to sell or refinance the facility the following year.[199] Cantone responded the same day, asking Brogdon for ownership history, including financial statements, Cedala's 2010 tax return, and other information about the condition of the facility.[200]

Cantone questioned Brogdon about his estimate of the value of the property, noting that the income statement and tax return showed the facility lost about $240,000 in 2009.[201] Brogdon responded with income statements showing losses for 2008, 2009, and 2010, but increased revenues and profitability for the first six months of 2011. This information gave Cantone confidence that the property had begun to generate enough money to enable Brogdon to pay the interest on the note.[202]

Cantone testified that his due diligence for Cedars was similar to the due diligence he conducted for the other offerings. He did not ask for a new appraisal because it was not a new facility, but obtained a 2004 appraisal, and sought information on sales of comparable properties.[203] Cantone asked Brogdon for a list of all the projects Brogdon and his wife had guaranteed.[204] Cantone also asked for evidence of the facility's revenues from private payments, Medicaid, and Medicare.[205] Again, Gardner drafted the CDM and other offering documents.[206] The CDM did not disclose the facility's losses in 2008, 2009, and 2010.[207]

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196 Tr. 682-683; JX-23, at 1.

197 JX-23, at 2, JX-24, at 2.

198 Tr. 978; RX-135.

199 CX-90.

200 Tr. 688-89; CX-82.

201 Tr. 690; CX-90.

202 Tr. 970-74; CX-91. Enforcement claims in its pre-hearing brief that "Notwithstanding his expressed concerns, and before receiving any response to those concerns from Brogdon, on or around August 22, 2011, Cantone went ahead with the Cedars Financial Offering." Enforcement's Pre-Hr'g Br., at 30. This is incorrect. Before issuing the Cedars COPs, Cantone obtained the most recent income statement for the underlying facility showing revenues through June 2011, which he forwarded to a colleague on August 19. RX-127. On August 24, Brogdon pointed out this was an increase of approximately $50,000 per month over the revenues in June 2009. RX-129.

203 Tr. 967-68; RX-124.

204 Tr. 975-76; RX-128; RX-131.

205 Tr. 976-77; RX-130.

As with the previous offerings, the Cedars CDM stated that interest and principal payments would be solely derived from operating revenues and backed by the Brogdon Guaranty.[208] However, Cantone covered for Brogdon's failures to make interest payments as they came due in December 2012 and June 2013; each time, Brogdon repaid Cantone four days after the Cantones used their funds to cover the interest due.[209] In October 2013, Cantone made a third payment with the notation "short term loan" on the check."[210]

When asked if he informed Cedars investors that he, not Brogdon, made these payments, Cantone answered inconsistently.[211] Still, Cantone acknowledged that CRI had agreed with the FINRA examination's conclusion that the firm should have disclosed this information to Cedars investors.[212]

The Cedars note matured in September 2013.[213] In a February 2013 email, noting that Brogdon needed extensions to repay principal on two other projects, Cantone warned Brogdon that if he failed to repay principal when due, Cantone would "have no choice" but to sue.[214]

Brogdon defaulted on Cedars, and in June 2014, Cedars sued Brogdon as Cantone had promised.[215] The court granted summary judgment, awarding Cedars almost $700,000 in principal, interest, and costs,[216] and investors received their principal and outstanding interest.[217]

After the Cedars offering, Cantone testified, he decided that he would conduct no further offerings containing the Brogdon Guaranty.[218]

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[206] Tr. 979.

[207] Tr. 692-93.

[208] Tr. 109-10; JX-23, at 19-20.

[209] Tr. 694-698; CX-92; CX-93.

[210] Tr. 698-99; CX-94.

[211] First, he said he could not recall when, but insisted that all his clients "were given information" that he made the payments. Tr. 172. Then he testified that he "could not confirm" whether he informed the investors, but he did not have a "specific recollection that it wasn't discussed." Tr. 698.

[212] Tr. 703.

[213] JX-23, at 1.

[214] CX-38.

[215] Tr. 704; CX-96.

[216] Tr. 711; CX-97.

[217] Cantone testified that, at the time of the hearing in this disciplinary proceeding, Brogdon had repaid their principal to Cedars investors, plus interest, upon selling the facility. However, Brogdon has not provided an accounting of the net capital gain, and Cantone is considering suing him to obtain Cedars' equity share. Tr. 982-83.

8. Cherokee, Issued May 28, 2013

a. The Offering

Cherokee was the last of Cantone's Brogdon-related COPs. Cantone insists it was "completely different" from the other Brogdon-related COPs because it was not a nursing home or assisted living project. Cantone testified the only reason Brogdon was involved was that he "brought the project to [Cantone's] attention and . . . we couldn't cut him out."[219]

Cantone testified that Brogdon first approached him in April 2012 about land located next to a retirement facility he had previously developed. Brogdon explained that a bank had agreed to sell him the land at a 45 percent discount. Brogdon's partner was a real estate developer, Bruce Alexander, who worked with him at RCA and the Chestnut facilities renovations.[220]

At first, Cantone was uninterested in Brogdon's proposal and "shrugged it off." Brogdon proposed to guarantee the offering, but Cantone had lost confidence in the Brogdon Guaranty because of all the late payments and defaults.[221] At this time, early 2012, the market for new homes was weak because of an oversupply of homes for sale. By January 2013, however, Cantone began noticing news reports that home sales nationally were recovering, and he decided to take another look at Brogdon's project.[222]

Brogdon owned and managed Arcadia Partners, LLC, the entity that owned the land for the project. Brogdon had the property subdivided into lots on which he planned to build age-restricted townhomes with a clubhouse and common areas. Cantone created Cherokee to issue COPs to purchase a promissory note from Arcadia for $1.825 million.[223] Arcadia planned to use the proceeds for constructing the first phase of the project.[224] With the note purchase, Cherokee and its investors acquired an ownership interest in Arcadia. Arcadia was to retain Alexander's company to construct the homes and manage the project.[225]

The plan was to build and sell a few homes, and use the proceeds to build more, until all homes were completed. Arcadia would pay interest and principal to investors from home sale

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218 Tr. 201.

219 Tr. 1011.

220 RX-153.

221 Tr. 1022.

222 Tr. 1023.

223 JX-28, at 1.

224 Tr. 719-20; JX-28, at 2.

225 Tr. 716-17; JX-28, at 1-2.

proceeds. Cantone described the Cherokee project as a "self-sustaining" real estate development that "had nothing to do with the previous offerings."[226] The promissory note was secured by a deed, subordinate to a senior deed held by participants in a bond issue by Brogdon's entity, Chelsea Investments, LLC ("Chelsea"), which raised the funds for the purchase of the land.[227] The CDM did not mention the Brogdon Guaranty.[228] Instead, Chelsea guaranteed the prompt payment of interest and principal.

In other respects, the Cherokee offering resembled the previous Brogdon-related COPs, except the note was to mature in five years, not two. Arcadia was to pay Cherokee investors 10 percent in quarterly payments and a share of profits generated by sales of the homes.[229] The minimum share of profits for investors was to be $5,000 per home, and after the first 15 were sold, the minimum profit was to increase to $9,000.[230]

Cantone testified that his due diligence included reviewing the certificate of organization for Arcadia, documentation for the first mortgage on the property, and the money Brogdon borrowed to develop infrastructure.[231] He asked Brogdon for details on the economics of the project, including Brogdon's expected cash flow and projected profits.[232] Cantone also reviewed a personal financial statement Alexander had submitted to his bank, dated July 2, 2012, showing that Alexander's net worth exceeded $8 million.[233]

Cantone made a site visit before issuing the Cherokee CDM.[234] He saw that the infrastructure was 75 percent complete; the roads were built, as were most of the sewers, drainage, and utility infrastructure.[235] By this time, the spring of 2013, he had met and worked successfully with the builder, Alexander, on another project.[236] Cantone was impressed by Alexander's estimate that he could build a home for $175,000 and sell it for $275,000, and that later in the project, he expected to sell the homes for $325,000. He was also impressed by the fact that Alexander was a real estate agent as well as a builder, and had an existing sales

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[226] Tr. 728.

[227] JX-28, at 2.

[228] Tr. 102-103, 728; JX-28, at 2.

[229] JX-29, at 1.

[230] Tr. 1012.

[231] Tr. 1023-26.

[232] Tr. 1027.

[233] Tr. 1020; RX-143, at 1.

[234] Tr. 1019.

[235] Tr. 1013.

[236] Tr. 1015-16.

organization to market the homes.[237] Cantone testified that he reviewed a real estate appraisal giving the property a market value of $3.6 million, and noted that Brogdon expected to purchase it at a significant discount.[238]

Cantone testified that he asked Brogdon for information on nearby comparable home sales, documentation of the bank's willingness to discount the mortgage, and financial statements for 2012 for the other Brogdon-related COPs Cantone had funded. Those statements showed net losses for Cedars, Chestnut, Columbia, and Country Club.[239] The Cherokee CDM did not disclose those losses. When asked why not, Cantone testified that Gardner drafted the CDM and it was his decision not to include that information. Furthermore, Cantone testified, Cherokee was unrelated to the previous offerings.[240]

Cantone solicited investors for Cherokee from the end of April through June 2013, and raised more than $1.8 million. In one email to a prospective customer, Cantone attached a property appraisal and a list of four selling points.[241] They did not mention Brogdon or any guaranty.[242] Cantone testified that he did not believe the Chelsea Guaranty was material.[243]

When asked if he informed prospective investors in the Cherokee offering of Brogdon's missed payments of interest and principal in the previous offerings, Cantone said he could not confirm that he did, but that "a lot" of the Cherokee investors had invested in them and would have known, because he had "multiple discussions" with investors.[244] In any event, Cantone did not think the fact that Brogdon was unable to make the payments was material to Cherokee.[245]

Cantone testified at the hearing that six homes had been sold, the clubhouse was finished, and two other homes were under construction.[246] Investors have received their interest payments in addition to their profit shares from the sales.[247] The note's maturity date is May 2018.

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[237] Tr. 1032-33.

[238] Tr. 1028-29.

[239] CX-99.

[240] Tr. 728-29.

[241] Tr. 735.

[242] Tr. 735-37.

[243] Tr. 744.

[244] Tr. 699-700.

[245] Tr. 700-02.

[246] Tr. 1058.

[247] Tr. 1057-58.

b. The Chelsea Guaranty

Cantone insists the Cherokee offering is "a lot different" from the other Brogdon-related COPs,[248] partly because he did not require Brogdon to provide his personal guarantee. According to Cantone, the Brogdon Guaranty was superfluous because the project was to be self-sustaining.[249] However, the offering did have a guarantor: Chelsea.[250]

Cantone claims to have had several reasons for not requiring Brogdon personally to guarantee payment of interest and principal for Cherokee investors. First, Brogdon had proven to be an unreliable guarantor by failing to make multiple interest payments on time and by defaulting in previous offerings.[251] Cantone testified he had lost confidence in Brogdon's guarantee.[252]

Second, Cantone emphasized that the project underlying Cherokee was different from the other projects involving nursing home or assisted living facilities Brogdon managed.[253] Brogdon's expertise was in the assisted living industry, not building and selling homes, which was the purpose of Cherokee.[254] That is why Alexander, not Brogdon, managed the project.[255]

Significantly, Cantone also testified that when Gardner began drafting the Cherokee CDM, he told Cantone if he included the Brogdon Guaranty, he would have to disclose Brogdon's "multiple failures to perform under previous guaranties."[256] Cantone and Gardner thus agreed not to include a Brogdon Guaranty in the Cherokee CDM.[257] Cantone testified that he also instructed Gardner to "de-emphasize the [Chelsea] guaranty" in the Cherokee CDM.[258]

According to Cantone, this is why Gardner included a warning in the CDM in bold, capital letters stating, "potential investors should make their investment decision based upon

[248] Tr. 90, 102.

[249] Tr. 747.

[250] Tr. 102-03; JX-30, at 1.

[251] Tr. 191.

[252] Tr. 1022, 1037.

[253] Tr. 191.

[254] Tr. 192.

[255] Tr. 464.

[256] Tr. 746-47, 1036-37; CX-126.

[257] Tr. 748.

[258] Tr. 748.

their evaluation of the development project, and not in reliance upon the Chelsea Guaranty Agreement."[259]

Given these reservations about the worth of the Chelsea Guaranty, Cantone could not explain the reason he included it in the CDM. Cantone claimed the point was to emphasize to Brogdon "that he had a fiduciary responsibility" to transfer Cherokee investor funds to Alexander.[260] But Cantone testified that he was *not* concerned that Brogdon would fail to transfer investor funds as required.[261]

D. Undisclosed Negative Background

The central charge of the Complaint is that when CRI and Cantone solicited investors in the Brogdon-related offerings, they fraudulently failed to inform investors of Brogdon's extensive negative business history, and when they solicited investors in the offerings after Columbia, they fraudulently failed to disclose Brogdon's accumulation of late payments of interest and principal, Cantone's loans to cover them, Cantone's extensions of note maturity dates, and Brogdon's financial setbacks. In addition, the Complaint charges CRI and Cantone with fraudulently failing to disclose a significant failed business venture Cantone suffered shortly before the Columbia offering.

1. Brogdon's History[262]

The CDMs for the Brogdon-related COPs contain no negative background information about Brogdon and do not describe the adverse events in his business past that Cantone should have known about because they were easily accessed by internet and public records research.

a. The NASD Bars

The NASD barred Brogdon from the securities industry twice. The NASD filed the first of two complaints against Brogdon in January 1984. It alleged that he engaged in unauthorized purchases of corporate and municipal bonds in the account of an institutional customer. A hearing was held in May 1984, but Brogdon did not appear. The NASD District Business Conduct Committee issued its decision in July, finding that Brogdon engaged in unauthorized transactions "for his own nefarious purposes," and imposed a censure, a fine of $10,000, and a bar.[263]

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[259] Tr. 748; JX-28, at 23.

[260] Tr. 745, 1046-48.

[261] Tr. 1145.

[262] Not subject to FINRA jurisdiction, Brogdon did not testify at the hearing. Facts about him come from documents in evidence and the testimony of Cantone and his wife.

[263] CX-3.

In July 1984, the NASD filed a second complaint against Brogdon and his firm for violating books and records and net capital rules. Again, Brogdon did not appear at the hearing. In January 1985, the District Business Conduct Committee, finding that Brogdon concealed municipal bond transactions from his clearing firm to circumvent credit limitations on his firm, imposed a censure, a $50,000 fine, and a second bar.[264]

b. The Criminal Charges

The Complaint alleges that Brogdon was indicted for fraud.[265] In actuality, in January 1999, a Florida state prosecutor filed a criminal information[266] charging Brogdon with racketeering, theft, abuse of an elderly or disabled adult, and Medicaid fraud. Brogdon entered a plea of not guilty and was released on a bond of $10,000. The case was closed in January 2000 with the entry of a *nolle prosequi*.[267] Thus, no trial was held and there was no finding of guilt on any of the charges.

c. Civil Judgment for Failure to Honor Stock Repurchase

In 1998, Brogdon was CEO of NHC. To induce another entity to purchase a significant number of shares of NHC, Brogdon agreed to buy back the shares if the purchaser requested he do so within one year. Before the year ended, the purchaser invoked the repurchase agreement. Brogdon refused to honor it. The purchaser sued for breach of contract, and moved for summary judgment. The court granted the motion and enforced the agreement. Brogdon appealed, claiming the repurchase agreement was legally unenforceable. In March 2003, the Georgia Court of Appeals upheld the lower court decision. The court found that Brogdon, to induce the purchase of NHC stock, had created "essentially a personal guaranty" and, having benefitted from the agreement, held that he could not renege by later claiming it was unenforceable.[268]

d. Brogdon Companies' Bankruptcies, Tax Liens and Civil Suits

In 1990, NAB, the nursing home management company "partially controlled by Brogdon," filed for bankruptcy.[269] In 1999, NHC also filed for bankruptcy.[270]

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[264] CX-4.

[265] Compl. ¶¶ 3, 34, 87(b).

[266] An information is a formal criminal charge filed by a prosecutor without a grand jury indictment. *Black's Law Dictionary*, 899 (10th ed. 2014)

[267] CX-10, at 29. A *nolle prosequi* is a formal notice on the record of a criminal case that the prosecutor has elected not to prosecute. *Black's Law Dictionary*, 1210 (10th ed. 1990).

[268] CX-14a, at 1, 4.

[269] Compl. ¶ 33a.

[270] *Id*. ¶ 33d.

In 1996, while Brogdon was Chairman of RCA, the Internal Revenue Service filed liens against RCA for "at least" $4 million.[271] Brogdon was still RCA's Chairman in 1997 when class action lawsuits were filed against the company and Brogdon, claiming they had misrepresented the financial condition of RCA in an effort to sell it. The suits settled in 1999.[272]

2. Brogdon's Failures to Pay Interest Timely, and Cantone's Loans to Cover Them

Cantone and CRI failed to inform investors in the COPs when Brogdon failed to pay interest payments to investors on time. Also, on numerous occasions, Cantone paid the interest owed to Columbia, Chestnut, and Cedars investors, without informing them, or the investors in the other offerings, of Brogdon's delinquent payments.

3. Cantone's Extensions of Note Maturity Dates

When Brogdon defaulted on repayment of principal to Columbia and Oklahoma, Cantone negotiated extensions of maturity dates with Brogdon, increased the interest rates on the underlying promissory notes, and charged additional principal and fees, without informing investors of the increased interest and fees.[273]

4. Brogdon's Financial Setbacks

Cantone issued Cherokee, the last Brogdon-related COP, in May 2013. Prior to its issuance, Brogdon provided Cantone with financial statements for several of his businesses. The statements reflected losses of more than two million dollars for the Brogdon entities managing three of the COP projects. Cantone and CRI did not mention these losses in the Cherokee CDM and did not otherwise inform prospective investors of the setbacks.[274]

5. Cantone's Failed Prior Business Venture

CRI and Cantone also did not disclose information about a failed Cantone business venture.

Cantone and his wife Christine Cantone owned Cantone Office Center, LLC ("COC"). In November 2005, before any of the Brogdon-related COPs were issued, COC issued $2.6 million in two series of certificates, one guaranteed and the other not. The funds raised were to purchase a promissory note issued by an entity called Esplanade Development, LLC to develop Esplanade

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[271] *Id*. ¶ 33b.

[272] *Id* ¶ 33c.

[273] Tr. 487-89 (Columbia extension); Tr. 650-51 (Oklahoma extension). Cantone extended the maturity date of the note in a third offering, Country Club, Tr. 894-95, but it was not one of the offerings for which Enforcement charged Cantone and CRI with fraudulent misconduct.

[274] Tr. 726-27.

I, a Florida condominium complex. COC was a guarantor for the timely payment of interest and repayment of principal to investors who purchased the guaranteed certificates. The note was to mature in two years.[275]

In February 2007, COC issued a second offering of certificates, again in two series, one guaranteed and the other not.[276] The offering raised $5.1 million to purchase a note to finance the construction of the Esplanade II. Again, COC guaranteed timely payment of interest and principal to investors. This note also was to mature in two years.[277]

Cantone testified that 90 percent of the completed condominiums were sold. However, the buyers walked away from their purchases when the real estate market collapsed.[278] The developer defaulted on both notes.[279] According to Cantone, although COC has paid investors "all that [it] could afford," it has not been able to fully honor its guarantee to the investors owning the guaranteed certificates.[280]

CRI and Cantone did not disclose any information regarding COC's failure to honor its guarantees to investors in the Brogdon-related COPs.[281]

V. Discussion

A. The Fraud Charges

1. Legal Standards

The first cause of action charges CRI and Cantone with violating Section 10(b) of the Exchange Act of 1934, Rule 10b-5 promulgated thereunder, and FINRA Rules 2020 and 2010, by making material misstatements and omissions in connection with the sales of five of the eight Brogdon-related COPs. Rule 10b-5 prohibits making any "untrue statement of a material fact" as well as failing "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."

To prove violations of Exchange Act Section 10(b) and Rule 10b-5, Enforcement must establish by a preponderance of the evidence[282] that CRI and Cantone: "(1) made a material

[275] Tr. 306-10, 315; JX-4, at 1-2.

[276] Tr. 313-14; JX-5, at 1-2.

[277] Tr. 316; JX-5, at 1.

[278] Tr. 326.

[279] Tr. 312-15.

[280] Tr. 318.

[281] Tr. 328-29.

[282] *Mitchell H. Fillet*, Exchange Act Release No. 75054, 2015 SEC LEXIS 2142, at *18 (Mar. 27, 2015).

misrepresentation or omission (2) in connection with the purchase or sale of a security (3) with scienter (4) in interstate commerce."[283] Rule 2020, FINRA's anti-fraud rule, is similar to Exchange Act Rule 10b-5, providing that no member shall effect any transactions, or induce the purchase or sale of any security, by means of any manipulative, deceptive or fraudulent device.

Scienter is a "mental state embracing intent to deceive, manipulate, or defraud."[284] It may be proven by evidence that CRI and Cantone actually knew their misrepresentations and omissions would mislead investors, or by evidence that they recklessly disregarded a substantial risk of misleading, a risk "so obvious that any reasonable man would be legally bound as knowing."[285] When the fraud involves an omission, the element of scienter is satisfied by proof that the respondent had actual knowledge of the omitted material information.[286]

To prove the violations of Section 17(a) (2) and (3) of the Securities Act, pleaded in the alternative in the second cause of action, Enforcement must establish that CRI and Cantone made material misrepresentations or omissions in the offer or sale of securities, but need not prove scienter.[287] In place of scienter, Enforcement must prove that Cantone acted negligently. It is negligent to fail "to exercise the standard of care that a reasonably prudent person would have exercised in a similar situation . . . [Negligence] connotes culpable carelessness."[288] This standard of care imposes a duty to take reasonable steps to become informed about a recommended security, and to do much more than to rely unquestioningly on information an issuer provides.[289] Omitting material information violates this standard of care, and is inconsistent with the high standards of commercial honor and the just and equitable principles of trade mandated by FINRA Rule 2010.

Respondents CRI and Cantone do not dispute that they employed instrumentalities of interstate commerce to solicit investments in the Brogdon-related COPs, and that the COPs are securities. However, they challenge: (i) the materiality of the facts that were allegedly

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[283] *SEC v. Platforms Wireless Int'l Corp.*, 617 F.3d 1072, 1092 (9th Cir. 2010); *SEC v. Wolfson*, 539 F.3d 1249, 1256 (10th Cir. 2008) (citing *Geman v. SEC*, 334 F.3d 1183, 1192 (10th Cir. 2003)).

[284] *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 (1976).

[285] *Dep't of Enforcement v. Abbondante*, No. C10020090, 2005 NASD Discip. LEXIS 43, at *28 (NAC Apr. 5, 2005), *aff'd*, 58 S.E.C. 1082 (2006), *aff'd*, 209 F. App'x 6 (2d Cir. 2006).

[286] *GSC Partners CDO Fund v. Washington*, 368 F.3d 228, 239 (3d Cir. 2004) (quoting *Fenstermacher v. Philadelphia Nat'l Bank*, 493 F.2d 333, 340 (3d Cir. 1974)).

[287] *SEC v. Merchant Capital, LLC, et al.,* 483 F.3d 747, 770-71 (11th Cir. 2007) (citing *Aaron v. SEC*, 446 U.S. 680, 702 (1980)).

[288] *John P. Flannery*, Initial Decisions Release No. 438, 2011 SEC LEXIS 3835, at *104 (Oct. 28, 2011) (quoting *Black's Law Dictionary,* 1056 (7th ed. 1999)), *rev'd in part, on other grounds,* Exchange Act Release No. 9689, 2014 SEC Lexis 4981 (Dec. 15, 2014), *petition granted and vacated on other grounds*, 810 F.3d 1 (1st Cir. 2015).

[289] *Dep't of Enforcement v. Reynolds*, No. CAF990018, 2001 NASD Discip. LEXIS 17, at *42-43 (NAC June 25, 2001).

misrepresented or not disclosed to investors in the COPs; (ii) the charge that the omissions or misrepresentations of fact were made in connection with the sales of the COPs; and (iii) the existence of scienter.

We begin by examining each of the alleged omissions or misrepresentations of fact to determine whether the evidence establishes they are material. If a fact is material, we must then determine whether it was omitted or misrepresented in connection with the sale of the COPs, and, if so, whether CRI and Cantone acted intentionally, or recklessly, or negligently.

2. Materiality

Whether a fact is material must be determined by analysis of the particular facts of a case.[290] An omitted fact is material if there is a substantial likelihood that a reasonable investor, deciding whether to invest, would find disclosure of the fact would significantly alter the "total mix" of available information.[291] An omitted fact may render a statement incomplete or false, but if the omitted fact is "otherwise insignificant," the omission is immaterial.[292] The standard for determining materiality of a fact is an objective one, and it is to be applied by the Panel.[293]

a. Time and Materiality

Respondents argue that the negative events in Brogdon's business history are not material because they occurred years before the Brogdon-related COPs were issued. Cantone and CRI issued the first Brogdon-related COP included in the Complaint, the Columbia offering, in February 2010. The oldest negative event in Brogdon's business history, the 1984 NASD bar, occurred 26 years earlier. Respondents argue that "the more time that has passed since a particular event, the less material the event is to a reasonable investor."[294]

Enforcement, in opposition, asserts that "the negative events concerning Brogdon and his negative business history are all material irrespective of their age." Enforcement notes "there is no statute of limitations" to determine the materiality of past negative events.[295] Enforcement also points out that the CDMs for the Brogdon-related COPs positively portray Brogdon's business successes dating back to 1987, 21 years before the Columbia offering was issued.[296] Enforcement

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[290] *Basic Inc. v. Levinson*, 485 U.S. 224, 238-39 (1988).

[291] *Id*., at 231-32 (quoting *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)).

[292] *Id*., at 238.

[293] *Worlds of Wonder Sec. Litig*., 1992 U.S. Dist. LEXIS 10503, at *12 (N.D. Cal. July 9, 1992) ("Under the federal securities laws, materiality is determined by an objective standard: the hypothetical 'reasonable investor' is the yardstick used to measure materiality . . . and it is for the trier of fact to decide whether defendants' omissions were, in fact, material") (citing *Basic, supra*, at 231).

[294] Respondent's Post-Hr'g Br., at 28.

[295] Enforcement's Post-Hr'g Br., at 42.

[296] *E.g.*, JX-7, at 7-8.

cites a recent Office of Hearing Officers panel decision in a Rule 10b-5 fraudulent omission case for the proposition that a respondent may not present only positive business successes while omitting negative information necessary to allow a fair overall evaluation of a person's business history.[297]

Upon careful consideration, the Panel finds that the age of an event in Brogdon's past, although not dispositive, is a factor to weigh in determining its materiality. Common sense suggests that a reasonable investor would consider, in circumstances like those here, recent adverse events more significant than similar events occurring a quarter century before. Facts weighed for materiality must be viewed in context. That is part of the rationale leading courts to consider the passage of time as a relevant factor in making materiality determinations involving undisclosed facts.[298]

However, the age of an event is not the only factor to consider. As Cantone testified, and the CDMs reflected, Brogdon's long experience in the business of developing assisted living and nursing home facilities was a selling point for the COPs. Cantone presented Brogdon's past business successes, his role in managing the projects underlying the offerings, and the Brogdon Guaranty, as positive factors boosting the likelihood of the success of the offerings.[299] Cantone's representations portrayed Brogdon as being one of "those . . . responsible for the success or failure" of the offerings.[300] The choice to disclose only positive achievements in Brogdon's background may make omitted negative events material.[301] Although this does not necessarily make every single one of Brogdon's business adversities material, it requires us to examine each of the omitted negative events in Brogdon's background to determine, in context, if there is "a substantial likelihood that a reasonable [investor] would consider it important in deciding how to [invest] . . . [and] the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[302]

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[297] Enforcement's Post-Hr'g Br., at 43, citing *Dep't of Enforcement v. Louis Ottimo*, No. 2009017440201, 2015 FINRA Discip. LEXIS 42, at *32 (OHO July 10, 2015), *aff'd*, 2017 FINRA Discip. LEXIS 10 (NAC Mar. 15, 2017).

[298] *See, e.g., Hollinger v. Titan Capital Corp.*, 914 F.2d 1564 (9th Cir. 1990), cert. denied, 499 U.S. 976 (1991); *Fisher v. Ross*, 1996 U.S. Dist. LEXIS 15091, at *31-32 (S.D.N.Y. Oct. 11, 1996).

[299] *See, e.g., Brian Prendergast,* 55 S.E.C. 289, 302 (2001) (respondent's claimed financial acumen important to potential investor, and therefore material).

[300] *Ottimo*, 2017 FINRA Discip. LEXIS 10, at *14 (quoting *Thomas J. Fittin, Jr.*, 50 S.E.C. 544, 546 (1991)).

[301] *Ottimo*, 2017 FINRA Discip. LEXIS 10, at *15-16.

[302] *Dep't of Mkt. Regulation v. Burch*, No. 2005000324301, 2011 FINRA Discip. LEXIS 16, at *29 (NAC July 28, 2011) (citing *Basic*, 485 U.S. at 231-32 (quoting *TSC Indus.,* 426 U.S. at 449)).

i. Brogdon's 1984 and 1985 NASD Bars

The NASD barred Brogdon in two separate disciplinary actions, in 1984 and 1985. Cantone testified that he learned from Friar in 2003 that Brogdon had a disciplinary history.[303] Cantone testified that Friar told him, and Brogdon later confirmed, that the NASD imposed a bar after Brogdon elected not to appear at a hearing because he had no interest in remaining in the securities industry.[304] From Friar and Brogdon, Cantone understood that the disciplinary action stemmed from a large business deal that caused Brogdon to lose his firm's capital, and that one of the allegations against Brogdon related to unauthorized trading.[305] Cantone did not conduct any follow-up investigation.[306]

When he decided to participate with Brogdon in the municipal bond offerings in 2003, Cantone testified that he was not concerned about the NASD bars when he learned that Brogdon had not been accused of stealing client funds.[307] This was partly because the disciplinary actions against Brogdon were almost 20 years old, partly because Cantone believed Brogdon's business successes since then "trumped" his having been barred,[308] and partly because he relied on the advice of Gardner, an experienced securities attorney, who knew Brogdon's background and had prepared earlier offerings involving Brogdon before he did so for CRI.[309] Cantone testified that Friar and Gardner, "two trusted advisors," told him the bars were not material.[310] If the bars were material, Cantone testified, he believed his lawyer would have included them in the CDMs.[311]

In 2008, after the municipal bond deals, when Cantone prepared to issue the Brogdon-related COPs, he continued to rely on Friar's earlier due diligence. As discussed above, Cantone testified that, to update his due diligence file, he asked Brogdon for documentation to "put to rest" Brogdon's past history. Brogdon provided the letter his lawyer wrote to a third party to explain several negative events in Brogdon's background. Cantone testified that the letter

[303] Tr. 256.

[304] Tr. 258, 266. Brogdon appealed the original District Business Conduct Committee decision, an indication that he was not as uninterested in the outcome as Cantone had been led to believe. Tr. 266-67; CX-5.

[305] Tr. 258-59, 263. It is unclear from Cantone's testimony whether he understood from Friar that Brogdon was barred twice.

[306] Tr. 259-60, 264.

[307] Tr. 258.

[308] Tr. 264.

[309] Tr. 341-42.

[310] Tr. 269.

[311] Tr. 267.

reinforced what Friar had previously disclosed to him.[312] Cantone also asked Brogdon to provide a personal financial statement when preparing each offering.[313]

Enforcement insists Brogdon's bars are material facts that Cantone and CRI should have disclosed to investors in the COPs. Enforcement reasons that "Brogdon was the central participant in each of the COP offerings" because he "controlled" them and guaranteed payments of interest and principal to investors. Hence, "adverse facts that cast doubt on Brogdon, his competence, or his reliability unquestionably would be material to investors" and being barred twice "is just such a fact."[314] Although the bars were imposed more than two decades before the Columbia offering, Enforcement contends that the conclusion in the NASD disciplinary decisions that Brogdon's continued presence in the securities industry would pose a substantial threat to investors "is a material fact that any reasonable investor would want to know regardless of its age."[315]

CRI and Cantone argue that the NASD bars are immaterial based on their age alone.[316] They argue further that subsequent events diminished their materiality. Respondents represent that in 1994, a decade after the first bar, Brogdon, as the president of RCA, submitted an application to Nasdaq for the company to be listed on the Nasdaq National Market, and in 1997, the application was approved.[317] They assert that this demonstrates that the NASD had satisfied itself that Brogdon's regulatory history did not pose a threat to the public interest.[318]

The argument has merit. The SEC, the NASD, and Nasdaq have affirmed the propriety of weighing the disciplinary history of a company's officers and directors when reviewing a Nasdaq

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[312] Tr. 347-48; RX-5.

[313] Tr. 372.

[314] Enforcement's Post-Hr'g Br., at 33, citing *LeadDog Capital Markets,* Initial Decisions Release No. 468, 2012 SEC LEXIS 2918 (Sept. 14, 2012) (holding that a majority owner of a hedge fund who intentionally failed to disclose his disciplinary history from a private placement memorandum acted fraudulently).

[315] Enforcement's Post-Hr'g Br., at 42.

[316] Respondent's Post-Hr'g Br., at 29.

[317] *Id.*, at 36 and n.221.

[318] *Id.* at 36. CRI and Cantone also argue that because the NASD owned Nasdaq, and Nasdaq approved the application, the NASD deemed the bars to be immaterial, and FINRA should be "estopped," pursuant to the doctrine of equitable estoppel, from now arguing the bars are material, because CRI and Cantone could justifiably rely on that determination. *Id.*, at 37, n.221, citing *Kosakow v. New Rochelle Radiology Assocs., P.C.*, 274 F.3d 706, 725 (2d Cir. 2001) ("where the enforcement of the rights of one party would work an injustice upon the other party due to the latter's justifiable reliance upon the former's words or conduct" the doctrine of equitable estoppel can be raised). We do not need to address the question of estoppel, raised for the first time in a footnote in Respondents' Post-Hearing Brief, with no testimony or evidence establishing CRI and Cantone acted on justifiable reliance upon Nasdaq's grant of Brogdon's listing application. The only evidence relating to this matter is the language in the CDMs touting Brogdon's responsibility for obtaining Nasdaq Market listing for RCA, and his chairmanship of NHC, a Nasdaq-listed company. *See, e.g.*, JX-7, at 7-8.

listing application. In a 1994 release, the SEC stated, "In recent years, the NASD has received an increasing number of applications for inclusion in the Nasdaq System from companies in which an officer, director . . . or other person in a position to influence management decisions has been enjoined, barred or suspended from participation in the securities industry for violation(s) of state or federal securities laws, self-regulatory organizations ('SRO') rules and regulations."[319] The release goes on to say, "On a case-by-case basis, the NASD has denied the applications of such issuers" under the authority of NASD's Qualifications Requirements By-Law.[320] Part II, Subsection 3(a)(3) of Schedule D of the By-Laws, in effect in 1994, provided that the NASD may deny inclusion whenever it "deems it necessary to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, or to protect investors and the public interest."

In a 1996 case, *DHB Capital Group, Inc.*, the SEC upheld an NASD denial of a company's application for Nasdaq listing based in part on the disciplinary history of the company's director and controlling shareholder, who had been barred four years earlier, pursuant to the Qualification Requirements By-Law. The NASD found the respondent had, among other things, aided and abetted a registered representative who engaged in insider trading.[321] The SEC noted, "the NASD has expressed quite plainly that it is troubled by [Respondent's] prior misconduct. We find that the NASD's concerns . . . are legitimate . . . [and] the underlying conduct undermines both the regulation of securities firms and its registered representatives, and the protection of investors."[322]

Thus, when Nasdaq was considering RCA's application for Nasdaq Market listing, it could have denied the application under the Qualification Requirements By-Law. The By-Law authorized Nasdaq to refuse applications for listing by companies with an officer or director who had been disciplined under the By-Law's mandate to "prevent fraudulent and manipulative acts and practices" and "protect investors and the public interest." Nevertheless, Nasdaq approved Brogdon's application, listed the company, and permitted Brogdon to serve as its Chairman and majority stockholder. He subsequently served as director of other publicly listed companies.[323] Respondents argue that Nasdaq's approvals, and Brogdon's business successes in the 1990's, erode the materiality of the bars.[324]

[319] SEC Release No. 34-33899, 59 FR 18171 (Apr. 15, 1994).

[320] *Id.*

[321] Exchange Act Rel. No. 34-37069, https://www.sec.gov/litigation/opinions/34-37069.txt, 61 SEC DOCKET 1758 (Apr. 5, 1996).

[322] *Id.*

[323] Respondents' Post-Hr'g Br., at 36; JX-23 at 8.

[324] Respondents' Post- Hr'g Br., at 36-37.

Taking all of these facts into consideration, the Panel concludes that the age of the bars and Nasdaq's approval of Brogdon's company's listing application vitiate their materiality. The record supports Respondents' contentions that Gardner and Friar both knew the NASD had barred Brogdon, and in Gardner's judgment, the bars did not have to be disclosed in the CDMs for the Brogdon-related COPs. The record also supports Cantone's testimony that he did not hide Brogdon's bars from inquiring customers; for example, one customer confirmed that he and Cantone discussed these negative events, and Cantone sent him a copy of the letter from Brogdon's attorney explaining the negative information.[325]

For these reasons, we conclude that there is not a substantial likelihood that a reasonable investor, deciding whether to invest in the COPs, would find disclosure of the 1984 and 1985 NASD bars to significantly alter the total mix of available information. Therefore, failure to disclose them was not a material omission.

ii. The Criminal Charges

CRI and Cantone argue that the passage of time since Brogdon's 1999 criminal charges, dropped in 2000, and Cantone's reliance on his lawyer's advice,[326] made it unnecessary to disclose the events in the CDMs.[327] They cite *Barron Partners, LP v. LAB123, Inc.* in support.[328] *Barron* involved a guilty plea entered 17 years earlier. The court held that its "temporal remoteness" rendered the nondisclosure "at most, of marginal relevance."[329]

CRI and Cantone also cite *Hollinger v. Titan Capital Corp.*[330] At issue there was whether it was reckless for Titan not to have disclosed to clients an 11-year-old forgery conviction of its registered representative.[331] One factor the court considered was that the NASD, aware of the conviction, had approved the representative's application for registration. The court concluded that Titan's failure to disclose its representative's conviction to clients was not reckless, noting that a "broker-dealer is not required to inform investors of every negative fact it knows about its registered representatives."[332]

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325 Tr. 1854.

326 Tr. 819-20.

327 Respondents' Post-Hr'g Br., at 30-31.

328 593 F. Supp. 2d 667, 673 (S.D.N.Y. 2009).

329 *Id.*

330 914 F.2d 1564.

331 The court noted that the trial court held that the omission was not material; the appellate court, for the purposes of its decision, assumed without deciding that "a jury could reasonably find the omission to be material" and proceeded to decide whether Titan acted recklessly. *Id.*, at 1570, n.12.

332 *Id.*, at 1571-72.

Enforcement asserts that it is "self-evident that the criminal indictment of a person central to an investment's success is a material fact that must be disclosed." Enforcement argues that the dropping of the 1999 charges against Brogdon did not make them immaterial. For authority, Enforcement cites the case of *SEC v. Electronics Warehouse, Inc.*[333] Enforcement claims that the *Electronics Warehouse* court "considered this precise issue and concluded that 'any investor . . . would have wanted to know that [the principal] had been charged with fraud, *even if the charges were not prosecuted.*'"[334] (Emphasis added).

However, *Electronics Warehouse* did not consider and resolve "this precise issue." The indictment in *Electronics Warehouse* was pending at the time of the offering. The court noted that the prospectus given to investors in *Electronics Warehouse* stated: "The Company is completely dependent upon the personal efforts and abilities of its CEO, [the principal], who is devoting and will devote his entire time to the Company's day-to-day activities . . . the loss or unavailability of the services of [the principal] . . . would have a materially adverse effect on the Company's business and /or potential earning capacity."[335] In contrast, Brogdon's charges were terminated a decade before the Columbia offering.

In *Electronics Warehouse* the court stated: "Any investor in Warehouse would have wanted to know that [the principal] had been charged with fraud, even if the charge were not prosecuted *by reason of his cooperation in a fraud investigation*." (Emphasis added). The court concluded that the "*pendency* of the criminal proceeding was, therefore, a material fact." (Emphasis supplied). The court observed that the pending indictment "was likely to make [the principal] 'unavailable' to Warehouse, either through his proposed resignation, his need to prepare a defense and stand trial, or through the possibility of incarceration."[336] Unlike the indictment in *Electronics Warehouse*, the dropped criminal information posed no threat to Brogdon's availability to manage the projects underlying the COPs.[337]

Other cases Enforcement relies upon are also distinguishable. In *Mitchell H. Fillet*,[338] the issuer of a private placement offering had two separate criminal convictions that the respondent failed to disclose to an investor. One, in 1987, was for filing a false affidavit to a state court and converting client funds, issuing bad checks, refusing to return client funds, and possessing stolen

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[333] 689 F.Supp. 53 (D. Conn. 1988).

[334] Enforcement's Post-Hr'g Br., at 35. *Electronics Warehouse,* 689 F.Supp. at 66-67.

[335] *Electronics Warehouse,* at 66.

[336] *Id.*

[337] The Panel is not persuaded by Enforcement's reliance upon another case it cites for the proposition that a failure to disclose a dismissed indictment was material. In *SEC v. Freeman*, the indictment at issue had been dismissed after a mistrial. There were three additional civil court proceedings, in one of which a court found the respondent had made intentional misrepresentations with the intent to defraud purchasers of franchises. All four proceedings had occurred within the previous ten years. 1978 U.S. Dist. LEXIS 19237, at *11-12 (N.D. Ill. 1978).

[338] Enforcement's Post-Hr'g Br., at 35, n.213.

property. The second, in 2003, just four years before the period relevant to the violations alleged in the case, was for possession of stolen property. The issuer served prison time for both convictions.[339] In *Dep't of Enforcement v. Craig*, a case involving Form U4 disclosure failures, at issue were five *pending* felony charges and a conviction for misdemeanor larceny.[340] In these cases the criminal charges resulted in convictions, were pending, or were more recent than Brogdon's dismissed charges.

The Panel finds that Brogdon's dropped criminal information from 1999 is not the equivalent of a conviction following a guilty plea because it is neither an admission of guilt nor an adjudication of any of the facts alleged in the allegations. We also find that its temporal remoteness diminishes its materiality. Considering all the circumstances, we find that nondisclosure of the criminal information was not a material omission.

iii. Class Action Suit, Bankruptcies and Tax Liens

In 1996, when Brogdon was chairman of RCA, the IRS filed tax liens totaling "at least $4 million" against the company. In 1997, ten civil class action lawsuits were filed against RCA, Brogdon, and others, alleging misrepresentations relating to the financial condition of RCA. The suits were settled in July 1999.[341] In 1990, NAB, described in the Complaint as a "nursing home management company partly controlled by Brogdon," filed for bankruptcy,[342] and in 1999, NHC, described as a "public corporation that managed assisted living facilities and nursing homes," filed for bankruptcy while Brogdon was its chairman.[343]

CRI and Cantone argue that the NAB and NHC bankruptcies are not material because they occurred years before the COP offerings, were corporate, not personal bankruptcies, and had no nexus to the financial condition of the entities involved in the COP offerings.[344] Furthermore, Cantone's lawyer Gardner knew of at least the 1990 bankruptcy, and advised Friar in 2002 that it was then "well beyond any period of relevancy."[345] Respondents cite cases holding that a six-year old bankruptcy and a nine-year old bankruptcy were not material facts requiring disclosure by officers of newly formed businesses absent evidence of wrongdoing in connection

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339 *Fillet*, 2015 SEC LEXIS 2142, at *5-6, 11-12. The issuer, an attorney, had been disbarred and had 87 tax and judgment liens filed against him.

340 *Dep't of Enforcement v. Craig*, No. E8A2004095901, 2007 FINRA Discip. LEXIS 16, at *12 (NAC Dec. 27, 2007), aff'd, Exchange Act Release No. 59137, 2008 SEC LEXIS 2844 (Dec. 22, 2008).

341 CX-9, at 1-2.

342 Compl. ¶ 33a.

343 *Id.*, ¶ 33d.

344 Respondents' Post-Hr'g Br., at 22, n.156, 32, n.205

345 *Id.*, at 21-22.

with the bankruptcies, when the bankrupt businesses were entirely unrelated to the currently operating businesses.[346]

Enforcement insists that each bankruptcy is a material fact that Cantone and CRI should have disclosed to prospective investors in the Brogdon-related COPs. Enforcement argues that a "reasonable investor would want to know" about these events, particularly in light of the "glowing review of Brogdon's business acumen and supposedly successful business history" in the CDMs distributed with the offerings.[347]

After carefully considering the arguments of the parties and relevant precedents relating to materiality,[348] the Panel concludes that CRI and Cantone were not required to disclose the NAB bankruptcy and class action suits, but were required to disclose the NHC bankruptcy and the tax liens.

The temporal remoteness of the NAB bankruptcy, combined with the fact that it was neither a personal bankruptcy filing by Brogdon, nor a bankruptcy of a company controlled by Brogdon, make it non-material.

The 1999 NHC bankruptcy is different, however. The business of NHC was to manage assisted living facilities and nursing homes, facilities like those involved with the first four Brogdon-related COPs at issue here. The CDMs describe Brogdon's extensive relevant business experience and success in positive terms, and point out: "In 1998 and 1999, Mr. Brogdon was also Chairman of NewCare Health Corporation, a Nasdaq-listed company in the assisted living and nursing home business."[349] In this context, NHC's 1999 bankruptcy, under Brogdon's chairmanship, is a material fact CRI and Cantone should have disclosed.

With regard to the class actions filed in 1997 against RCA, Brogdon and others, 13 years before the Columbia offering, we find that they are not material and Cantone and CRI were not required to disclose them. First, we note their temporal remoteness. Second, the suits were settled. We are persuaded that these "unadjudicated allegations . . . should not automatically be

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[346] *Id.*, at 31-32, citing *Fisher*, 1996 U.S. Dist. LEXIS 15091, at *31-32; *Feinberg v. Leighton*, 1987 U.S. Dist. LEXIS 580, at *32-33 (S.D.N.Y. Jan. 30, 1987).

[347] Enforcement's Post-Hr'g Br., at 37-38.

[348] *SEC v. Carriba Air*, 681 F.2d 1318, at 1320, 1323-24 (11th Cir. 1982) (defendants selling stock in a new airline were required to disclose that the principals had been involved in a string of airline company failures including a nearly identical venture, an airline that declared bankruptcy only one month before the formation of the new venture, with the same routes, and employees); *SEC v. Merchant Capital*, 483 F.3d at 770-71 (holding that "failure to disclose the bankruptcy of a similar predecessor company is a material omission" particularly when the defendant "put his experience in issue" by touting his past business successes and the bankruptcy was "very recent"); *SEC v. Kirkland*, 521 F.Supp. 2d 1281, 1286-87, 1302-03 (M.D. Fla. 2007) (defendant soliciting investments was required to disclose that the state issued two cease-and-desist orders and a temporary restraining order prohibit him from selling the securities).

[349] JX-7, at 8 (Columbia CDM); JX-12, at 8 (Chestnut CDM); JX-18, at 8 (Oklahoma CDM); JX-23, at 8 (Cedars CDM); JX-28, at 8 (Cherokee CDM).

deemed material" and find that a reasonable investor in the Brogdon-related COPs would not "place much stock in the bald, untested allegations in a civil complaint" unrelated to the COPs.[350]

We do not, however, come to the same conclusion in considering the materiality of CRI and Cantone's non-disclosure of the filing of the substantial federal tax liens against RCA in 1996. Even though the liens were not filed against Brogdon personally, and despite their temporal remoteness from the COP offerings at issue here, as Chairman of RCA, Brogdon was responsible for its operation. Failure to pay taxes of nearly $4 million is significant. FINRA deems a tax lien filed against a FINRA member firm material under any circumstance—liens are required to be disclosed promptly on an associated person's Uniform Application for Securities Industry Registration or Transfer,[351] and on a member firm's Form BD.[352] We find that a reasonable investor would consider millions of dollars in tax liens against RCA, under Brogdon's chairmanship, significant, with the potential to alter the total mix of information available relating to Brogdon's ability to manage the COPs sold by CRI and Cantone. This is especially so considering the statements in the CDMs touting Brogdon's business acumen and success over two decades in managing similar retirement, assisted living, and nursing home facilities and projects.

In sum, the Panel concludes that the NHC bankruptcy and the multi-million dollar federal tax liens filed against RCA under Brogdon's stewardship are material, and CRI and Cantone should have disclosed them in the CDMs circulated to prospective purchasers of the Brogdon-related COPs.

iv. The 2003 Georgia Appellate Decision

One of the omissions charged against CRI and Cantone concerned the 2003 Georgia appellate decision in a breach of contract suit filed against Brogdon described above. To induce a company to purchase a significant amount of NHC stock when Brogdon was NHC's CEO and a stockholder, he agreed to buy the stock back if the company requested he do so within a year. The company made a timely request. Brogdon refused. The company took him to court to enforce the agreement. The court ruled in the company's favor and Brogdon appealed.[353] On

[350] *GAF Corp. v. Heyman,* 724 F.2d 727, 739-40 (2d Cir. 1983).

[351] *Robert D. Tucker*, Exchange Act Release No. 68210, 2012 SEC LEXIS 3496, at *29-33 (Nov. 9, 2012); *Mathis v. SEC*, 671 F.3d 210, 219-20 (2d Cir. 2012) (approving of the SEC application of the Supreme Court's established "proper and familiar test for materiality" in determining that tax liens were material in part based on large dollar amount, number of liens, indicating broker had serious financial problems and was under financial pressure).

[352] *Dep't of Enforcement v. The Dratel Group, Inc.*, No. 2009016317701, 2015 FINRA Discip. LEXIS 10, at *12 (NAC May 6, 2015).

[353] Compl. ¶ 35; CX-14a.

appeal, the Georgia appellate court refused to allow Brogdon to "render void" what it deemed to be "essentially a personal guaranty."[354]

Cantone testified that he does not recall if Friar informed him of this court decision when he provided Cantone with Brogdon's background information.[355] Enforcement argues that regardless of whether Friar told Cantone, the information was easily accessible by a simple internet search.[356]

Respondents argue that this event, like many others in the Complaint, "happened years before the first Offering was sold in 2010," and there is no substantial likelihood a reasonable investor would consider it to significantly alter the extensive mix of information CRI and Cantone provided.[357]

The Panel finds it troubling that Cantone does not recall whether he even was aware of this event. And while Brogdon's breach of his contractual obligation to repurchase the NHC stock occurred nine years before the first COP offering, the Panel finds that Respondents should have disclosed it.

As discussed above, the Brogdon Guaranty was an important selling point for the first four COP offerings at issue. Given the importance of the Brogdon Guaranty, there is a substantial likelihood that a reasonable investor deciding whether to purchase a COP would consider the court's decision that Brogdon refused to honor a similarly binding personal guarantee to be an important fact that could alter the mix of available information. By conducting reasonable due diligence, CRI and Cantone should have known of the court decision, and should have disclosed it to prospective investors who may have made their decision partly relying upon the Brogdon Guaranty.

v. Late First Interest Payments: Columbia, Chestnut, and Cedars

The Complaint alleges that "[o]n more than ten separate occasions, [the Brogdon entities responsible for making interest payments to Columbia, Chestnut, and Cedars investors] failed to make a required interest payment . . . [and] CRI and Cantone did not inform investors of any of

[354] CX-14a, at 4. The court rejected Brogdon's argument that the agreement was unenforceable because it was wrong for him to make it in the first place.

[355] Tr. 304-05.

[356] Enforcement's Post-Hr'g Br., at 3. Respondents did not address the 2003 Georgia appellate court decision in their post-hearing brief.

[357] Respondents' Pre-Hr'g Br., at 9, 27-28. Respondents point out that the suit leading to the appellate decision was filed in 2001, and the alleged failure to honor the guarantee occurred well before the 2003 decision.

these defaults. Instead, Cantone and Christine Cantone secretly 'covered' the interest payments to investors even though the underlying CDMs prohibited them from doing so."[358]

As discussed above, the first interest payment for the Columbia offering was due on May 1, 2010.[359] Brogdon did not pay it on time. He made a partial payment nine days late.[360] The Cantones covered the shortfall.[361]

Noting the Columbia promissory note defined a default as a failure to make payment within five days of the due date, Enforcement argues this constituted a default by Brogdon,[362] and Cantone's failure to inform investors who had already invested in Columbia, as well as the prospective investors in the subsequent Chestnut, Oklahoma, Cedars and Cherokee COP offerings, was a material omission.[363]

The first interest payment for Chestnut investors was due on June 1, 2011. Brogdon made the payment late, but within the allotted grace period.[364] The Chestnut promissory note defined default as a failure to make a payment within 15 days of the due date.[365]

Enforcement argues that CRI and Cantone wrongly failed to inform prospective Chestnut investors of the late payment. Enforcement also contends that Cantone made a material misrepresentation by telling an investor on February 23, 2011, that in the 12 years Cantone had worked on projects with Brogdon, they completed "14 projects with not a single default."[366] Enforcement asserts this was false because Brogdon had "defaulted on the promissory note issued to Columbia."[367] But, as discussed above, that "default" was the tardy partial payment of Columbia's first interest payment.

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358 Compl. ¶¶ 46-47. Even though the CDMs identified the "sole sources" of the payments of interest and principal, nothing in the CDMs expressly prohibited Cantone from covering the interest payments.

359 JX-7, at 2.

360 CX-25, at 1. Early in the hearing, at Tr. 195-96, Cantone testified that Brogdon's payment was $7,000 less than required, but later calculated that the amount due, consisting of interest plus a facility fee, was $51,000, which would make the shortfall $17,000. Tr. 392-94.

361 Tr. 195-96; CX-25, at 1.

362 Enforcement's Post-Hr'g Br., at 8-9.

363 Enforcement's Pre-Hr'g Br., at 12 ("CRI and Cantone failed to disclose this default to investors."); Enforcement's Post-Hr'g Br. at 14, 18-19, 21-22, 24.

364 Tr. 536-37, 540; CX-56.

365 JX-14, at 2.

366 Enforcement's Pre-Hr'g Br., at 18-19; CX-53a, at 2.

367 Enforcement's Pre-Hr'g Br., at 19.

Viewing the totality of the circumstances surrounding the first interest payments for both the Columbia and Chestnut offerings, we conclude that they do not constitute material facts that CRI and Cantone needed to disclose to the COP investors.

First, Cantone testified without contradiction that Brogdon's tardy first Columbia interest payment was not intentional, and not caused by an inability to pay. Cantone accepted Brogdon's explanation that it was a bookkeeping error, corrected shortly thereafter. Furthermore, Columbia investors had already made their investments, so the omission did not induce, and was not in connection with, their decisions to invest. The lack of materiality made it unnecessary for CRI and Cantone to disclose the tardy payment to investors in the other COP offerings that followed Columbia: Country Club, Chestnut, Cedars, and Cherokee.

As for the late first Chestnut interest payment, it was not a default; it was paid in full before the expiration of the grace period as provided by the terms of the Chestnut promissory note.[368] It was not a material event occurring in connection with the sale of the Chestnut offering, and it was not fraudulent for CRI and Cantone to fail to disclose it to investors in the succeeding offerings.

Cedars was the fourth of the five allegedly fraudulent offerings. The first Cedars interest payment was due on December 15, 2011.[369] On December 27, the Cantones paid the interest, noting it as a temporary loan.[370] Brogdon's payment, by check dated December 24, was deposited into the Cedars account on December 31.[371] Like Chestnut, the Cedars promissory note set a 15-day grace period for payments of interest, so the Brogdon check, dated within and deposited one day after the grace period, was not significantly late, and we do not deem the late payment to be material.[372] Therefore, we do not agree with Enforcement's argument that Cantone was required to disclose it to Cedar investors and prospective investors in the last offering at issue, Cherokee.

In sum, the Panel concludes that the late first interest payments Brogdon made in Columbia, Chestnut, and Cedars are not material facts that CRI and Cantone wrongfully failed to disclose.

vi. Late Interest Payments Before Extensions of Maturity Dates for Columbia and Oklahoma Notes

The Columbia note matured on February 1, 2012. As discussed above, Cantone initially offered Brogdon a six-month extension. Although Columbia continued to receive interest from

368 JX-13, at 2-3.

369 JX-23, at 1.

370 Tr. 694; CX-92, at 4.

371 Tr. 695-96; CX-92, at 4.

372 Compl. ¶ 87f.

him, Brogdon did not repay the principal by September 2012. On October 1, Cantone agreed to extend the maturity date of the note to February 1, 2013.[373] Later in October, Cantone sent a letter notifying Columbia investors of the extension.[374] Cantone offered to buy back COPs from Columbia investors who wanted their principal returned on the original maturity date.[375]

By the time of the extension, Brogdon had made two more late interest payments to Columbia, and three late payments to Chestnut. Cantone did not disclose these facts in his letter to investors, and did not disclose that the extension agreement raised the annual interest rate from 10 percent to 14 percent and charged an extension fee.

After Brogdon told Cantone in January 2013 that he was unable to repay the principal because of low occupancy of the assisted living facility and independent living apartments, Cantone offered a second extension. Cantone noted that he had bought out four investors who were unwilling to agree to the previous extension. The second extension agreement, dated February 1, 2013, was for another year, with the new maturity date February 1, 2014. By the time of the second extension agreement, Brogdon had been unable to make two more interest payments—one to Chestnut, the other to Cedars—but Cantone did not disclose these to Columbia investors. The Panel finds these missed payments to be material facts that should have been disclosed to the Columbia investors contemplating whether to continue to participate in the extended offering.

As previously discussed, Brogdon was also unable to repay principal when the Oklahoma note matured in July 2013. Cantone agreed to extend the maturity date to January 15, 2014. The agreement had the same terms as the Columbia extension agreements: it increased the annual interest rate from 10 to 14 percent, and added fees. As he had done with the first Columbia extension, Cantone sent a letter to the Oklahoma investors announcing the extension. In this letter, too, Cantone did not inform investors of the additional fees or the increased interest rate. Instead, he erroneously represented that Brogdon had agreed to continue to pay 10 percent.[376] As with Columbia, Cantone offered to repurchase COPs from investors who wanted the return of their principal.[377]

The Oklahoma extension agreement was dated July 10, 2013. By then, Brogdon had failed to make additional timely interest payments to investors in other COPs: one to Columbia, one to Chestnut and two to Cedars that Cantone did not disclose.

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[373] CX-33.

[374] CX-34.

[375] Tr. 992-94. Cantone repurchased COPs from several Columbia investors.

[376] CX-77.

[377] Tr. 992-96.

Enforcement argues that Brogdon's failures to pay interest, inability to repay principal, and the changes Cantone made to the interest rate and fees in the extension agreements, are material facts that CRI and Cantone were required, but failed, to disclose to Columbia and Oklahoma investors, and that Cantone's letter to Oklahoma investors materially misrepresented the interest rate Brogdon was to pay when the extension was granted.[378]

CRI and Cantone argue, first, that even though they were under no obligation to inform investors of the missed interest payments, the investors knew about them. They claim Cantone "regularly called his investors to advise them of the late interest payment and to let them know when it would be received."[379] Second, Respondents argue they were not obligated to disclose to investors on an ongoing basis that Brogdon was late in making their interest payments because, even if the information might be material, the disclosure requirements of Section 10(b), Rule 10b-5, and Section 17(a) apply only to misrepresentations and omissions made in connection with the purchase or sale of securities, and not to post-sale communications.[380]

We address these two arguments in order.

Three customers testified that Cantone discussed Brogdon's late payments with them.[381] Cantone testified that he told "most of these clients" that he was paying the interest,[382] and informed investors who were "interested."[383] However, there is no documentary evidence that Cantone informed investors that Brogdon missed payments in other offerings before extending the maturity dates for the Columbia and Chestnut notes. To the contrary, the FINRA examination found that CRI and Cantone "did not disclose to investors of Columbia that [Brogdon] failed to make several timely interest payments." Respondents agreed with the examiners "that Columbia ought to have made disclosures to investors" of these failures.[384] In response to a similar examination finding concerning Chestnut, Respondents replied they "should have made this disclosure to the investors at the time Chestnut granted the extension."[385] Thus, the evidence does not support Cantone's assertion that he informed Columbia and Chestnut investors of Brogdon's failures to make interest payments on time.

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[378] Enforcement's Post-Hr'g Br., at 40-41.

[379] Respondents' Post-Hr'g Br., at 40.

[380] *Id.*, citing, at 41 n.247, *U.S. v. Harris*, 919 F.Supp. 2d 702, at 709 (E.D. Va. 2013).

[381] Tr. 1845; RX-349; RX-350.

[382] Tr. 175-176.

[383] Tr. 205.

[384] Tr. 174-75.

[385] Tr. 176-77.

Furthermore, in his OTR, when asked if he informed Columbia investors that he had made interest payments that Brogdon missed, Cantone testified "I don't know the answer to that question, but I don't think it's that pertinent."[386] He also testified he "probably did not mention . . . that I was lending the money to Columbia out of my pocket. I'm not sure that I did."[387] When asked during the OTR to explain what he told clients about having paid interest to COP investors, Cantone replied: "It was irrelevant. I don't think I discussed it with too many people. Maybe one or two people that asked."[388]

The Panel agrees with Respondents that some of the disclosure omissions Enforcement claims to be fraudulent were irrelevant because they were not made "in connection with" the purchase of COPs by some investors. For example, when Brogdon missed the Columbia interest payment in May 2012, Chestnut, Oklahoma and Cedars investors had purchased their COPs at least nine months previously, so disclosure could have had no impact on their investment decisions.

The extensions for Columbia and Oklahoma make them different. Cantone gave investors a choice. They could continue to participate in the offerings or he would buy them out to let them redeem their investments. As one court has held in a case involving previously purchased securities, misrepresentations that included "lulling statements about . . . delayed interest payments as well as misrepresentations intended to induce delayed redemptions" of investment certificates, were sufficiently "in connection with" securities purchases to fall within the scope of Section10(b) and Rule 10b-5. The court held, as we do here, that "reliable payment of interest . . . would have played a large role in an investor's decision to cash out."[389] Mindful that courts have broadly construed the meaning of the phrase "in connection with the purchase or sale of securities,"[390] we hold that CRI and Cantone's failure to disclose the missed payments were omissions made in connection with the purchase or sale of the COPs.

Finally, we find that there is a substantial likelihood that reasonable Columbia and Oklahoma investors deciding whether to continue to participate in the offerings would consider

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[386] Tr. 210-11.

[387] Tr. 213-14.

[388] Tr. 220. Cantone claimed that during the OTR his memory was impaired because he was taking medication for a head cold. Tr. 380-81. However, at the interview, he testified "I'm just taking some cold medication" and he believed he was able to understand and answer questions. Tr. 244-45.

[389] *U.S. v. Durham*, 766 F.3d 672, 682-83 (7th Cir. 2014), *cert. denied*, *Durham v. U.S.*, 136 S. Ct. 92, 2015 U.S. LEXIS 5240 (Oct. 5, 2015). See also, *Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 85 (2006) (endorsing broad interpretation of the meaning of "in connection with the purchase or sale" for the purpose of §10(b) fraud claims, stating that it does not apply only to purchasers and sellers, but also to holders affected by fraudulent manipulation of stock prices).

[390] *See, e.g.*, *SEC V. Zandford*, 535 U.S. 813, at 819, 822 (2002) (approving of broad interpretation of the phrase and holding that it requires only that a misrepresentation "coincide" with a purchase or sale); *Superintendent of Ins. v. Bankers Life & Casualty Co.*, 404 U.S. 6, 12-13 (1971) (it is enough if a misrepresentation touches a transaction).

the terms of the extension agreements that Cantone failed to disclose, and misrepresented to Oklahoma investors, to significantly alter the total mix of available information. The first Columbia extension agreement forthrightly stated that Brogdon was unable to make required payments, but Cantone did not send the extension agreement to investors. Instead, he sent them a letter after the fact stating only that he had granted the extension because Brogdon had a prospective purchaser for the underlying facility.[391] The first Columbia extension agreement charged additional fees to Brogdon and increased the interest rate from 10 to 14 percent, and Cantone determined the additional 4 percent would go to him, not to the investors. Cantone did not disclose these changes to the investors.[392]

The Oklahoma extension agreement made similar changes, increasing the interest rate from 10 to 14 percent and charging Brogdon additional fees. As with the Columbia extension, Cantone did not send the extension agreement to investors. In the letter he sent to them, he falsely stated the 10 percent interest rate would continue, and did not disclose the additional four percent he was charging. Cantone justified this in his OTR when he testified that the investors were "not interested in my 4 percent extra I'm getting."[393] The omissions and the misrepresentation in the extension agreements are material.

vii. Subsequent Late Payments Before the Cherokee Offering

Cantone issued the Cedars offering in August 2011. Almost two years passed before Cantone issued the last Brogdon-related offering, Cherokee, on May 28, 2013. By then, as noted above, Brogdon:

- was unable to repay the Columbia investors their principal, and the note maturity date was postponed twice;
- had missed making prompt interest payments on the Columbia note four times, and on the Chestnut note six times;
- owed $350,000 to Chestnut in missed interest payments and fees; and
- had missed making an interest payment when due to Cedars.

[391] Enforcement's Post-Hr'g Br., at 40; CX-33, at 1 (Columbia's first extension agreement); CX-34 (letter to Columbia investors). Cantone testified that his lawyer, Gardner, prepared the extension agreements and "never told" him to send a copy to investors. Tr. 492. He also testified that he does not recall discussing the question with Gardner. Tr. 493.

[392] Tr. 445-47.

[393] Tr. 648.

In addition, at the end of 2012, Brogdon provided Cantone with income statements showing negative income estimates for the year of more than $800,000 for Columbia, more than $1,000,000 for Chestnut, and more than $115,000 for Cedars.[394]

Cantone gave conflicting testimony about whether he informed prospective Cherokee investors of these facts. Initially, Cantone testified that disclosure would have been "irrelevant." He then hedged, saying, "Actually, they all knew" and claimed that every time he sent a check for interest, he called the investors, and told them "by the way, this money didn't come from Brogdon. It came from me. I loaned the money to Brogdon."[395] He insisted there was no need to disclose prior Brogdon payment problems to prospective Cherokee investors because Cherokee "had nothing to do with the previous offerings."[396] Finally, he admitted that, with prospective Cherokee investors, "I don't think we discussed . . . any of the Brogdon deals . . . because those were a completely different animal"[397] and "I don't think we discussed anything prior to Cherokee because it was a different deal."[398] In other words, Cantone considered the many prior Brogdon missed payments and defaults irrelevant to Cherokee investors. The Panel finds that he did not disclose them to prospective Cherokee investors.

Enforcement argues that Brogdon's repeated failures to pay interest and principal to investors in the COPs prior to the Cherokee offering constitute material information CRI and Cantone were required to disclose to prospective Cherokee investors.[399]

CRI and Cantone insist that Brogdon's missed payments to investors in prior offerings would not be material to prospective Cherokee investors.[400] Cantone, recognizing by then that Brogdon was an unreliable guarantor, did not require Brogdon to personally guarantee the offering, and did not include the Brogdon Guaranty in the Cherokee CDM. Respondents argue that without the Brogdon Guaranty, Brogdon's "finances and past conduct became immaterial."[401]

The Panel disagrees. The terms of the Chelsea Guaranty track those of the Brogdon Guaranty. The Chelsea Guaranty's numbered paragraphs have the same headings and content as

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[394] CX-99, at 5, 11, 14.

[395] Tr. 169-70.

[396] Tr. 728.

[397] Tr. 1118.

[398] Tr. 1119.

[399] Enforcement's Post-Hr'g Br., at 23-25, 38-39.

[400] Respondents' Post-Hr'g Br. at 45-46.

[401] *Id*., at 45-47.

the Brogdon Guaranty.[402] Like the Brogdon Guaranty, the Chelsea Guaranty states that providing the Guaranty was a prerequisite for the note purchase to occur.[403]

The Cherokee CDM did not de-emphasize, as Cantone said he intended it to, the significance of the Chelsea Guaranty and Brogdon's role in the project. The CDM provided the same biographical information about Brogdon as the CDMs for the other offerings, touting his long and successful business experience.[404]

It is true that a section addressing the "Value of the Chelsea Guaranty Agreement" warned investors, in bold capital letters, that they should not make their investment decisions in reliance on the Chelsea Guaranty.[405] However, on the next page the CDM stated, "Brogdon is the central participant in the transactions," and reiterated that Chelsea was managed and controlled by Brogdon, and owned by Brogdon Family, LLC.[406]

Considering all of these circumstances, the Panel finds unpersuasive the argument that the Chelsea Guaranty made the Cherokee offering completely different from the other Brogdon-related COPs. Cantone may not have used Brogdon's name or guarantee as a selling point in the same manner that he had in the previous offerings, but the description of Brogdon in the CDM as "the central participant" represented that he had a significant role in the offering and was important to its potential for success.

We also find that Cantone's explanation of why he included the Chelsea Guaranty in the Cherokee CDM, discussed in detail earlier, is not credible. He testified, unconvincingly, that his only purpose was to impress upon Brogdon his fiduciary responsibility to transfer investor funds to the project's construction manager. Rather, the evidence suggests that the Chelsea Guaranty was a way to keep Brogdon's name prominent in the Cherokee CDM without having to disclose—as Gardner told him a Brogdon Guaranty would have required—Brogdon's numerous failures to honor his commitment to make prompt payments in prior offerings. Cherokee investors were entitled to disclosure of these negative facts.

Taking all of these factors into consideration, we conclude that there is a substantial likelihood that reasonable prospective Cherokee investors would consider the number of missed interest and principal payments occurring after the Cedars offering was issued, and the

[402] The only difference is that the Brogdon Guaranty specifically stated the guarantee provided was for the benefit of the note purchaser and the holders of COPs, but the Chelsea Guaranty stated it was for the benefit of the note purchaser. JX-9, at 2; JX-30, at 2.

[403] JX-30, at 1.

[404] JX-28, at 7-8.

[405] JX-28, at 23. The CDMs for the other COPs contained a similar disclaimer titled "Value of the Brogdon Guaranty" with similar language, albeit without the bold, capitalized sentence relating to the Chelsea Guaranty. *See, e.g.*, JX-18, at 36.

[406] JX-28, at 23-24.

information about Brogdon's negative income at the end of 2012 for the operation of the Columbia, Chestnut, and Cedars projects, to be facts that would have significantly altered the mix of available information relevant to deciding whether to participate in the Cherokee offering.

viii. The Failure to Honor the Esplanade Guarantees

The Complaint also charges CRI and Cantone with fraudulently omitting to disclose another business failure—not Brogdon's but Cantone's—involving the defaults of the Esplanade I and II offerings in 2007 and 2009 respectively.

Enforcement argues that Cantone's failure, through Cantone Office Center, to honor the guarantee to pay interest and principal to the Esplanade I and II investors was a material fact that should have been disclosed to all prospective investors in the Brogdon-related COPs. Enforcement reasons that the "role of Cantone Office Center in the Esplanade offerings was similar to the role of the Cantone-controlled LLCs in the Brogdon-related COPs": Cantone was central to the Brogdon-related COPs; he solicited the investors; he controlled the entities that solicited investments and sent them to Brogdon; he enforced the terms of the promissory notes; and he pressed Brogdon to repay investors their principal and interest. Thus, Enforcement concludes, the failure of COC, owned and managed by Cantone, to honor its guarantees in Esplanade I and II, was something a reasonable prospective investor in the Brogdon-related COPs would want to know.[407]

CRI and Cantone counter that COC's failure to honor the guarantee to pay interest and principal to the investors in Esplanade I and II, which took place during the financial crisis of 2008, had no connection to Brogdon or the Brogdon-related COPs. The COPs involved different projects in different locales, with a different developer. Therefore, Respondents argue, the Esplanade failure would not have been material to a reasonable investor.[408]

The Panel agrees that the Esplanade offerings unquestionably constituted a significant business failure in Cantone's history. However, they were unrelated to the Brogdon-related COPs. Courts have established that not every failed business venture in a person's background must be disclosed.[409] Just because Cantone experienced a business failure with Esplanade does not mean it was material to later, unrelated ventures, and does not compel the conclusion that Cantone was obligated to disclose the failure to prospective investors in the Brogdon-related COPs. We note that neither Cantone nor any of his entities assumed the role of guarantor in the Brogdon-related COPs.

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[407] Enforcement's Post-Hr'g Br., at 36

[408] Respondents' Post-Hr'g Br., at 38-40.

[409] *Fisher*, 1996 U.S. Dist. LEXIS 15091, at *31-32 (six-year-old bankruptcy of prior employer of directors of company making an offering held immaterial absent evidence that the executives had committed wrongdoing, and no evidence the bankruptcy had any bearing on financial prospects of offering company); *Feinberg*, 1987 U.S. Dist. Lexis 580, at *32 (omission by defendant to disclose he was involved in a company, with no connection to the business at issue, that went bankrupt nine years earlier, was not material); *Hollinger*, 914 F.2d at 1572.

Because the Brogdon-related COPs were entirely unrelated to the Esplanade COPs, the Panel concludes that Cantone and COC's failure to honor the guarantees in the Esplanade ventures is not material, and they were not obligated to disclose it to prospective investors in the Brogdon-related COPs.

b. Independent and Collective Materiality

Enforcement argues that although each of the facts reviewed above is "separately and independently . . . material and required disclosure," we must consider them collectively, asserting that "[t]he question is whether his 1984 bar *and* his 198[5] bar *and* his criminal indictment *and* [NHC'S] bankruptcy *and* the class action lawsuits against RCA *and* Brogdon's repeated failure to make required principal and interest payments, etc., collectively, are material."[410]

As Enforcement accurately states, "[n]ondisclosed facts are not viewed in isolation. Materiality depends upon all the circumstances of the case."[411] This means "whether an alleged misrepresentation or omission is material necessarily depends on all relevant circumstances of the particular case"[412] and that the Panel must "focus on . . . whether defendants' representations, taken together and in context, would have misled a reasonable investor."[413]

This does not mean, however, that non-material factual omissions become material simply because there are a number of them. We have, therefore, necessarily considered "whether *all* of the misrepresentations" (which were in this case primarily omissions), are material in the context of the CDMs.[414] We have concluded that the NASD bars, the dropped criminal charges, the NAB bankruptcy and the class action lawsuits, each of which we have found not material individually, are also not material collectively.

c. Summary

The Panel concludes that there are three material events from Brogdon's business history that should have been disclosed to prospective investors in all five of the Brogdon-related COPs:

- the approximately $4 million in federal tax liens filed in 1996 against RCA while Brogdon was its chairman;

[410] Enforcement's Post-Hr'g Br., at 45 (emphasis in original).

[411] *Id*., at 44-45, n.261, quoting *Oleck v. Fischer*, 1979 U.S. Dist. LEXIS 11785, at *36 (S.D.N.Y. 1979) and citing *Perez v. Higher One Holdings, Inc*., 2016 U.S. Dist. LEXIS 123919, at *29 (D.Conn. 2016), quoting *Manavazian v. Atec Grp., Inc.*, 160 F.Supp. 2d 468, 478 (E.D.N.Y. 2001).

[412] *Ganino v. Citizens Utils. Co*., 228 F.3d 154, 162 (2d Cir. 2000).

[413] *Initial Pub. Offering Sec. Litig*., 241 F.Supp. 2d 281, 379 (S.D.N.Y. 2003) (quoting *Demaria v. Andersen*, 318 F.3d 170, 180 (2d Cir. 2003)).

[414] *Id.,* at 380 (emphasis in original).

- the 1999 NHC bankruptcy filing while Brogdon was its chairman; and
- the 2003 court decision concerning Brogdon's failure to honor a personal guarantee that he had originally proposed to induce a stock sale.

In addition, we find two events to be material to Columbia and Oklahoma investors when presented with the option of agreeing to the extensions of maturity dates of the notes in those offerings:

- Brogdon's undisclosed and increasingly frequent missed payments of interest and principal; and
- the undisclosed increase in the interest rate and additional fees Cantone charged Brogdon for the extensions.

We also find material the misrepresentation made in the letter to Oklahoma investors of the interest rate Cantone charged Brogdon.

Similarly, we find there are three omissions of material fact that CRI and Cantone should have disclosed to prospective Cherokee investors before the Cherokee offering was issued in May 2013:

- Brogdon's numerous missed or late payments of principal and interest to investors in the previous offerings;
- Brogdon's arrearage of more than $350,000 owed to Chestnut; and
- the negative income for 2012 for the facilities Brogdon was managing for Columbia, Chestnut, and Cedars.

3. Scienter

We must now consider whether Respondents made these misrepresentations and omissions with scienter, that is, either knowingly or recklessly, as the first cause of action alleges, or negligently, as the second cause of action alleges.

CRI and Cantone argue there is no evidence they acted with scienter or negligently. They posit three main grounds for their position. First, they claim to have "acted on good faith reliance on the advice of their counsel.[415] Second, they assert that investing more than half a million dollars of the Cantones' own funds in the COPs, and recommending the COPs to family members, is evidence of their lack of fraudulent intent.[416] Third, they argue that the thorough due

[415] Respondents' Post-Hr'g Br., at 48.

[416] *Id.*, at 49.

diligence they conducted on each project shows they did not act with fraudulent intent or negligence.[417]

a. Reliance on Advice of Counsel

Generally, a claim of reliance on the advice of counsel requires a respondent to provide evidence that the respondent consulted with and made full disclosure to counsel; asked for advice on the legality of a proposed course of action; received advice that it was legal; and relied on the advice in good faith. Even when a respondent satisfies these requirements, it has been held that the reliance is "not a complete defense, but only one factor for consideration."[418]

Enforcement argues that CRI and Cantone failed to satisfy their burden of establishing a defense of reliance on counsel because they failed to prove that they specifically asked for an attorney's advice on whether to disclose Brogdon's negative business background, his failures to make timely interest and principal payments, and the changes in the terms of the extension agreements for the Columbia and Oklahoma offerings.[419]

CRI and Cantone contend that they established the elements of good faith reliance on the advice of counsel.[420] They claim they relied on Gardner's advice as to what facts in Brogdon's background to disclose to investors in the COP CDMs. They describe Gardner as an "experienced, well-reputed counsel," and assert that in addition to Gardner, when they were soliciting investors for the Cherokee COPs, they sought the advice of a second attorney to review and approve the documents Gardner had drafted.[421]

There were three emails Gardner sent relating to advice concerning Brogdon's background. CRI and Cantone argue that, in conjunction with Cantone's testimony, the emails are evidence of their reasonable good faith reliance on counsel. One is the email Gardner wrote to Friar in 2002, relating to a municipal bond offering, suggesting that Brogdon's 1990 bankruptcy was "well beyond any period of relevancy."[422] Another is a 2008 email in connection with the Hoover offering, in which Gardner expressed his view that the NASD bar imposed on Brogdon for net capital violations was not relevant.[423] The third is the email Gardner sent to

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[417] *Id.*, at 49-51.

[418] Enforcement's Post-Hr'g Br., at 48-49, quoting *Markowski v. SEC*, 34 F.3d 99, at 104-05 (2d Cir. 1994). *See also Dep't of Enforcement v. Fox*, *et al.*, No. 2012030724101, 2017 FINRA Discip. LEXIS 3, at *34 (NAC Jan. 6, 2017) quoting *Howard Brett Berger*, Exchange Act Release No. 58950, 2008 SEC LEXIS 3141, at *40 (Nov. 14, 2008), *aff'd*, 347 F. App'x 692 (2d Cir. 2009), *cert. denied*, 559 U.S. 1102 (2010).

[419] Enforcement's Post-Hr'g Br., at 49-55.

[420] Respondents' Post-Hr'g Br., at 17-18.

[421] *Id*.

[422] RX-367.

[423] RX-368.

Cantone before preparing the Cherokee CDM, warning that if Cantone wanted to include the Brogdon Guaranty, the CDM would have to recite all the prior Brogdon failures to pay promised interest and principal when due.[424]

The only other document in the record prepared by a lawyer relating to Brogdon's negative history was the letter to a third party, prepared not by Gardner, but by Brogdon's lawyer, that purported to explain away the dropped criminal charge and the RCA class action lawsuits.[425]

Respondents argue that these documents establish that Gardner reasonably determined the NASD bars, the 1990 NAB bankruptcy, the dropped criminal charges and the RCA class action suits did not need to be disclosed, and that CRI and Cantone "reasonably relied upon his advice when it distributed the CDMs."[426] Respondents argue, further, that this good faith reliance negates any possibility they acted with scienter or negligently, and the first and second causes of action therefore should be dismissed "as a matter of law."[427]

The Panel disagrees. We find that the evidence falls short of establishing CRI and Cantone relied in good faith on counsel.

First, as discussed above, Cantone testified that he delegated to Gardner the responsibility for ensuring that CRI and he complied with securities laws and FINRA rules, and made all necessary disclosures of material facts in connection with the sales of the COPs. CRI and Cantone represent that they relied on the familiarity with Brogdon and his background that Gardner and Friar possessed from their prior years of working with him.[428] When asked about the drafting of the contents of the biographical background information in the CDMs, Cantone testified he had taken "a hands-off policy. Jim Friar and the lawyer put the CDM together and these disclosures. Whatever they thought was relevant would have been disclosed."[429] Emphasizing that he did not prepare the CDMs,[430] Cantone insists that Gardner, "aware of certain events" in Brogdon's background, advised him that those events did not need to be disclosed in the CDMs.[431]

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[424] CX-126.

[425] RX-5.

[426] Respondents' Post-Hr'g Br., at 23.

[427] *Id*., at 23-24.

[428] Tr. 341-42.

[429] Tr. 337-40.

[430] Tr. 203.

[431] Respondent's Post-Hr'g Br., at 18-19.

Retaining Gardner to prepare offering documents did not relieve CRI and Cantone of their obligation to comply with securities laws and regulations.[432] The NAC recently held it is not enough for respondents to retain counsel to prepare offering documents and then argue they "thus reasonably relied on competent legal advice" with regard to the contents.[433] The record establishes that Cantone read and approved the biographical description of Brogdon in the CDMs.[434] Respondents, not their attorney, were ultimately responsible for the material omissions in that description, common to all of the COP CDMs.

Furthermore, the absence of documentation of the specific advice Gardner provided is problematic. To establish good faith reliance on advice of counsel ordinarily requires proof of the advice given, either through the testimony of the lawyer who gave the advice,[435] or written documentation of the actual advice.[436] Gardner did not testify. We deem Cantone's testimony that he reasonably relied on Gardner for advice on disclosures insufficient.[437] There is no evidence establishing that he sought Gardner's advice specifically on whether to disclose Brogdon's 1996 tax liens, the 1999 NHC bankruptcy, the 2003 Georgia appellate decision, Brogdon's failures to pay interest and principal, the changes in the interest rate and fees he charged Brogdon for the extensions, and arrearages Brogdon owed to Chestnut investors.

CRI and Cantone failed to establish good-faith reliance on the advice of their counsel in determining what to disclose, and, more important, what not to disclose, to COP investors about the negative facts in Brogdon's background. We find their claim of reliance does not negate, as they insist it should, a finding of scienter.

b. Respondents' Personal Investments in the COPs

Turning to Respondents' second contention relating to scienter, we reject the claim that Cantone's personal and family investments in the COPs negate scienter. CRI and Cantone cite no authorities in support of this claim. They base it on the testimony of the Cantones that they

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[432] *SEC v. Savoy Indus., Inc.*, 665 F.2d 1310, 1315 n.28 (D.C. Cir. 1981) (rejecting denial of responsibility by respondent for false and misleading documents prepared by law firm, when respondent was in charge of firm and responsible for its disclosure obligations).

[433] *Ottimo*, 2017 FINRA Discip. LEXIS 10, at *37-39.

[434] Tr. 338.

[435] *Dep't of Enforcement v. Kesner*, No. 2005001729501, 2010 FINRA Discip. LEXIS 2, at *42-43 (NAC Feb. 26, 2010), citing *Berger*, 2008 SEC LEXIS 3141, at *40.

[436] *Fox*, 2017 FINRA Discip. LEXIS 3, at *34-35 (noting respondents' failure to provide an opinion letter or written documentation of the advice upon which they purportedly relied).

[437] *SEC v. McNamee*, 481 F.3d 451, 456 (7th Cir. 2007) (Respondent "offered nothing other than his say-so," insufficient to establish reliance on advice of counsel without any letter containing advice or testimony of "an actual lawyer").

would never have personally invested, or recommended close family members to invest, if they did not believe in the viability of the offerings and the accuracy of the CDMs.[438]

It has long been settled that a broker's willingness to speculate with his personal assets, despite knowing adverse information about an investment, does not excuse failure to disclose the information.[439] This is so even if the broker honestly believes in the investment.[440]

c. Due Diligence on the Underlying Projects

Respondents' third argument to negate scienter, and to rebut the alternative allegation that they acted negligently, is that Cantone conducted extensive due diligence on the offerings. The record supports the claim that Cantone gathered and reviewed substantial data including property appraisals, environmental studies, financial information, real estate appraisals, and made personal visits to some of the facilities. Respondents argue that to find scienter or negligence requires evidence they knew, or should have known, their omissions could mislead investors. Cantone claims he possessed a good-faith belief that, in light of his in-depth review of each project, the information at issue was immaterial, and Gardner agreed. Thus, the materiality of the omitted facts and the misrepresented fact was at least questionable, and far from obvious, and Respondents' belief they were immaterial "undercuts any argument that they acted with scienter."[441]

These arguments miss the mark. The due diligence Cantone conducted concerning the economics of the underlying projects is not relevant here. Rather, it is the due diligence, or lack of it, concerning Brogdon and his background that is relevant. As we noted above, Cantone admitted he did little investigation into Brogdon's background, instead relying on the knowledge of Friar and Gardner from their past association with Brogdon. And as we have seen, Cantone, and possibly Gardner, were probably unaware of some of the significant events we deem material: the Georgia appellate decision, the federal tax liens, and the NHC bankruptcy.

As we have also seen, when Cantone extended the Columbia and Oklahoma note maturity dates and changed the interest rate for Brogdon, and solicited investments in Cherokee, he knew Brogdon had missed numerous interest and principal payments, and that he had increased the interest rate. Yet Cantone chose not to disclose these matters when it could have mattered to the investors. It is on these facts that we must focus to determine whether Cantone, and CRI through him, acted with scienter, or negligently.

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[438] Respondents' Post-Hr'g Br., at 49.

[439] *Richard J. Buck & Co.,* 43 S.E.C. 998, 1008 n.20 (1968).

[440] *Burch*, 2011 FINRA Discip. LEXIS 16, at *31-32 (citing *Dane s. Faber*, 57 S.E.C. 297, 310 (2004)).

[441] Respondents' Post-Hr'g Br., at 49-51.

4. Conclusions

a. CRI and Cantone Made Negligent Omissions of Material Fact in Connection with the Sales of Five COP Offerings (Second Cause of Action)

We turn now to the three events from Brogdon's business history that we have determined to be material, and that should have been disclosed, to investors in all five COPs.

The evidence does not establish whether CRI and Cantone knew of the 1999 NHC bankruptcy. Cantone testified that he does not recall whether Friar informed him of the tax liens or the Georgia appellate decision.[442] However, there was a significant amount of publicly available information about the negative events in Brogdon's past.[443]

Although Cantone claimed he conducted his own due diligence in 2008 "to update [his] due diligence file on the old issues of Brogdon" before issuing the COPs, the only example of documentation relating to Brogdon's checkered past that he produced was the copy of the letter Brogdon's attorney wrote to a third party explaining away some of Brogdon's disciplinary history. Cantone testified that Brogdon gave it to him after Cantone asked him for "anything that . . . puts to rest the issues" of Brogdon's past history.[444] Cantone referred to the letter as "part of my own due diligence in 2008."[445] Because he relied on Friar and Gardner's familiarity with Brogdon's background, Cantone testified he did not review Brogdon's business history in connection with each COP offering, although he asked for a "personal financial statement on every deal," including updated tax returns.[446]

For example, Cantone obtained a financial statement for Brogdon and his wife dated December 31, 2009.[447] Cantone did not recall contacting the accountant who prepared it.[448]

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[442] Tr. 292-94 (Cantone has no recollection of Friar informing him of the tax liens); Tr. 296-97 (Cantone does not recall Friar informing him of contents of articles describing NHC bankruptcy and other negative events); Tr. 304-05 (Cantone cannot recall Friar informing him of the Georgia appellate court decision).

[443] *E.g.*, CX-6 (1996 New York Times article describing questions concerning Brogdon's actions as chairman of RCA and negative history he had failed to disclose to shareholders); CX-7 (1993 Forbes Magazine article critical of Brogdon's ethics in municipal bond deals); CX-8 (May 1999 Atlanta Business Chronicle article describing shareholder suits filed against Brogdon and RCA); CX-11 (July 1999 Atlanta Journal article describing "scandal" in closing of NHC office in Atlanta); CX-12 (1999 Associated Press article alleging NHC misuse of escrow fund); Tr. 1672-74 (FINRA examiner testimony describing easily accessible, publicly available, background information on Brogdon's business record).

[444] Tr. 342-43, 348-49; RX-5.

[445] Tr. 343.

[446] Tr. 371-73.

[447] Tr. 377-78; CX-19a.

[448] Tr. 378.

Although it was titled "Statement of Financial Condition," its preface explained that it was a "compilation" limited to "the representation of the individuals whose financial statements are presented," and an acknowledgment that the accounting firm had "not audited or reviewed" it.[449] Thus, it consisted merely of the Brogdons' unaudited representations of their assets, liabilities, and net worth.

Cantone apparently did not dig deeper. He testified that he does not know if he conducted an internet search on Brogdon, even though he "used Google all the time."[450] During FINRA's 2013 examination of CRI, the examiner asked for and received all of CRI's records pertaining to the due diligence conducted for the COP offerings. CRI produced drafts of the offering documents and financial reports relating to the underlying facilities of the offerings—but no background information, and no negative history, on Brogdon.[451]

It is negligent for a registered representative to fail "to exercise the standard of care that a reasonably prudent person would have exercised in a similar situation . . . [Negligence] connotes culpable carelessness."[452] This standard of care imposes a duty on a registered representative to take reasonable steps to become informed about a recommended security, and to do more than to rely unquestioningly on information provided, in this case, by Brogdon, Friar, and Gardner.[453] CRI and Cantone had a duty to take reasonable steps to become informed about Brogdon, who was central to the potential success or failure of the offerings. Respondents had an obligation "to investigate and verify" Brogdon's background.[454] It was not enough for CRI and Cantone to gather information only about the underlying facilities and not Brogdon.

CRI and Cantone did not fulfill this obligation. Consequently, they were unaware of the tax liens, the Georgia court decision, and the NHC bankruptcy, which we have found to be material facts that should have been disclosed to investors in the COPs. By omitting this material information, they violated the requisite standard of care, violated Section 17(a)(2) and (3) of the

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[449] CX-19a, at 1-2.

[450] Tr. 349.

[451] Tr. 1670-71, 1673-74, 1690-96.

[452] *Flannery*, 2011 SEC LEXIS 3835, at *104 (quoting *Black's Law Dictionary* 1056 (7th ed. 1999)).

[453] *Reynolds*, 2001 NASD Discip. LEXIS 17, at *42-43.

[454] *Id.*

Securities Act, and failed to comply with the high standards of commercial honor and just and equitable principles of trade that NASD Rule 2110 and FINRA Rule 2010 mandate.[455]

b. CRI and Cantone Made Knowing or Reckless Omissions and a Misrepresentation of Material Fact in Connection with the Maturity Date Extensions of Two Investments, and in Connection with Sales of the Cherokee COP (First Cause of Action)

We now turn to the remaining material omissions, and the misrepresentation, that we have found material to Columbia and Oklahoma investors when Cantone extended the maturity dates of their notes, and the material omissions in the CDMs for prospective Cherokee offering investors. The question is whether these omissions and misrepresentation were made with scienter, either knowingly or recklessly, as the Complaint's first cause of action alleges.

As noted above, in cases involving failure to disclose material facts, evidence that a respondent "had actual knowledge of the material information" that he did not disclose, establishes scienter.[456] CRI and Cantone knew of Brogdon's missed and late payments of interest and principal prior to the date of the extension agreements, and prior to the issuance of the Cherokee offering, and they knew of the changes to the terms of the loans, specifically the additional fees and higher interest rate they charged Brogdon. There is also no question that Cantone understood the materiality of Brogdon's missed and late payments. As the number of Brogdon's failures to pay timely interest and principal increased, so did Cantone's complaints to Brogdon that he was injuring his reputation and making it difficult for Cantone to find additional investors for upcoming offerings.[457]

For these reasons, the Panel finds that Respondents acted with scienter, intentionally failing to disclose Brogdon's missed or late payments, and the changes to the interest rate, to Columbia and Oklahoma investors, and misrepresenting the changed interest rate to be paid after the extension to Oklahoma, thereby depriving the investors of material facts when deciding whether to continue to participate in the offerings with extended maturity dates.

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[455] *Id.*, at *44. In July 2007, NASD consolidated with the member regulation and enforcement functions of NYSE Regulation. The consolidated entity began operating under a new corporate name, the Financial Industry Regulatory Authority (FINRA). References to FINRA include, where appropriate, NASD. When the first phase of the new consolidated rules became effective on December 15, 2008, *see* Regulatory Notice 08-57 (Oct. 2008), FINRA Rule 2010 superseded NASD Rule 2110. In this case, the Complaint's second cause of action alleges negligent misconduct beginning when NASD Rule 2110 was effective and ending after the adoption of FINRA Rule 2010. The two rules are identical.

[456] *See, e.g.*, *GSC Partners CDO Fund,* 368 F.3d at 239, quoting *Fenstermacher v. Phila. Nat'l Bank*, 493 F.2d 333, 340 (3d Cir. 1974).

[457] *See, e.g.*, CX-55, at 1 (complaining to Brogdon that his failure to pay principal impairs Cantone's ability to obtain funds for future projects); at 2 (complaining to Brogdon that late payment to investors in prior bond issue led three investors to question his guarantee).

For the same reasons, the Panel finds that CRI and Cantone acted with scienter when they failed to inform prospective Cherokee investors of Brogdon's growing number of missed interest and principal payments to investors in the prior offerings. Worse, they revealed an intent to manipulate Cherokee investors by replacing the Brogdon Guaranty with the Chelsea Guaranty in the Cherokee CDM. As we found above, Cantone substituted the Chelsea Guaranty for the Brogdon Guaranty to avoid disclosing Brogdon's record of missed payments, as Gardner told Cantone he would need to do if the CDM contained the Brogdon Guaranty.

These facts and circumstances establish that, in the offers to Columbia and Oklahoma investors to continue participating in offerings with extended note maturity dates, and the offer and sale of the Cherokee COPs, Cantone, and through him CRI, willfully violated Section 10(b) of the Exchange Act, SEC Rule 10b-5, and FINRA Rules 2020 and 2010, as charged in the Complaint's first cause of action. Because their actions were willful, CRI and Cantone are subject to statutory disqualification.[458]

5. Sanctions

For an individual charged with intentional or reckless omissions of material fact in the sales of securities, the Sanction Guidelines strongly recommend first considering a bar. If there are mitigating circumstances, the Guidelines recommend suspension in any or all capacities for six months to two years, and a fine of $10,000 to $146,000. For a firm, the Guidelines recommend suspension of any or all activities for up to two years, and strong consideration of expulsion from FINRA membership if there are aggravating circumstances. For negligent omissions, the Guidelines recommend suspension of an individual in any or all capacities for 31 days to two years, and consideration of suspending a firm with respect to a limited set of activities for 90 days.[459]

Enforcement characterizes the misconduct we have found CRI and Cantone responsible for under the first cause of action—the misrepresentation and omissions in connection with the extensions of the Columbia and Oklahoma notes, and the omissions in connection with the sale of the Cherokee COPs—as egregious, and argues that expelling CRI and barring Cantone are the appropriate sanctions. For Cantone, Enforcement identifies as aggravating factors the repeated nature of the fraudulent omissions and misrepresentation to investors, the intentionality of the misconduct, the duration of the course of the misconduct over approximately three years, the

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[458] Under Sections 3(a)(39)(F) and 15(b)(4)(D) of the Exchange Act, broker-dealers and associated persons are subject to disqualification from the securities industry for willful violations of the federal securities laws. See 15 U.S.C. § 78c(a)(39)(F); 15 U.S.C. § 78o(b)(4)(D). The Complaint alleges that CRI and Cantone willfully violated Exchange Act Section 10(b) and Rule 10b-5. Our finding of scienter is an implicit finding that Cantone, and CRI through him, knew what they were doing when they made the material misrepresentation to Oklahoma investors and omitted material information relating to Brogdon's missed interest and principal payments to prospective Cherokee investors and Columbia and Oklahoma investors considering the proposed maturity extensions. Thus, these violations were willful, and CRI and Cantone are statutorily disqualified by operation of the Exchange Act. *See, e.g., Ottimo*, 2017 FINRA Discip. LEXIS 10, at *24 n.9.

[459] FINRA Sanction Guidelines at 89 (April 2017), http://www.finra.org/industry/sanction-guidelines.

defaults of four of the notes at issue and claimed losses of $6 million of investor funds, and Cantone's failure to accept responsibility.[460]

The recommendation to expel CRI is based on Enforcement's contention that CRI is responsible for the fraud charges as well as improper use of customer funds, unsuitable recommendations and failing to supervise Cantone. Noting that the firm's violations occurred through Cantone and Christine Cantone, Enforcement argues that the Cantones' failure to accept responsibility and CRI and Christine Cantone's disciplinary history are aggravating factors.[461]

CRI and Cantone argue that Enforcement's recommendations are inordinately harsh and punitive, and would unfairly injure CRI's 28 employees and its customers. They contend it is mitigating that they "did everything they could have to ensure the accuracy of the CDMs" and reasonably relied on the advice of counsel after providing him with "all requisite information." Thus, they assert there is no misconduct to deter by imposing sanctions. Respondents also argue that mitigating factors exist, including Cantone's offer to repurchase COPs from investors when he extended note maturity dates, paying interest when Brogdon was late, and obtaining judgments against Brogdon. Respondents also claim the sophistication of the investors—all accredited, who attested in their subscription agreements for the COPs that they understood the risks—militates against imposing sanctions. Respondents argue further that they intended no harm, should not be faulted for failing to accept responsibility simply because they defended themselves in this proceeding, and demonstrated their desire to improve by changing their policies in response to the FINRA staff's findings from the 2013 examination.[462]

Although the Panel finds the fraudulent misconduct of CRI and Cantone to be serious, we find neither the egregious degree of aggravation argued by Enforcement, nor the sweeping mitigation advocated by Respondents.

First, we do not find that CRI and Cantone's intentional fraudulent misconduct occurred in connection with all of the offerings. Rather, we find it occurred only in connection with the extensions of the Columbia and Oklahoma offering notes and the solicitation of investments in the Cherokee offering. The intentional or reckless nature of the misconduct is an aggravating factor.[463]

Second, the Panel concurs with Enforcement that CRI and Cantone's fraudulent conduct involved numerous acts, constituting a pattern, and occurred over a significant period, also

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[460] Enforcement's Post-Hr'g Br., at 60.

[461] Enforcement's Post-Hr'g Br., at 62-63.

[462] Respondents' Post-Hr'g Br., at 57-61.

[463] Guidelines at 8 (Principal Considerations No. 13 (misconduct resulting from intentional or reckless acts)). We have found CRI and Cantone's failures to disclose the NHC bankruptcy, the federal tax liens, and the appellate court decision to have been negligent omissions to disclose to all COP investors.

recognized as aggravating for the purposes of determining sanctions.[464] Cantone notified Columbia investors of the first extension of the note's maturity in October 2012, of the second in February 2013, and he notified Oklahoma investors of the extension of their note in July 2013, a span of ten months. When Cantone notified Columbia investors of the first extension, he failed to inform them of Brogdon's three late payments to Chestnut investors and two late interest payments to Columbia investors, with missed deadlines in March, May, August, and September 2012. When Cantone notified Columbia investors of the second extension in February 2013, Brogdon had missed two additional interest payments in December 2012, one to Chestnut investors and another to Cedars investors. When Cantone notified Oklahoma investors of the extension of their note, Brogdon had missed an additional interest payment deadline in Columbia, Chestnut, and Cedars. As we discussed in the description of the Cherokee offering, Cantone solicited investors in Cherokee from April through June 2013, failing to disclose these missed payments to prospective investors.

Third, the Panel finds that Cantone has not acknowledged responsibility for his misconduct.[465] To the contrary, he repeatedly attempted to shift responsibility by testifying that his lawyer was responsible for determining the materiality of facts to include in the CDMs, at one point asserting this justified his adoption of a "hands-off policy" about the contents of the CDMs. He provided little evidence of substantive consultation with his lawyer on what disclosures should have been included. When his lawyer pointed out the need to disclose Brogdon's many missed payments if there were to be a Brogdon Guaranty in the Cherokee CDM, Cantone substituted the Chelsea Guaranty. Under these circumstances, Cantone's claim that it was the lawyer's responsibility, rather than his, rings hollow.

The Panel also finds that Cantone was deceptive when examiners questioned him at the outset of the June 2013 FINRA examination.[466] The examiners asked him if there had been any defaults in the private placements during the review period, and he said no. They asked him if there had been any late payments, and he again said no.[467] Yet by then, Brogdon had made a number of late interest payments and had failed to pay the Columbia note principal when due, and Cantone had extended the maturity date twice. Although by covering Brogdon's missed payments Cantone had not formally declared Brogdon to be in default and had ensured that investors received interest, it was disingenuous of him to simply deny there had been any late payments.

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[464] Guidelines at 7 (Principal Considerations No. 8 (numerous acts or pattern of misconduct) and No. 9 (misconduct over extended time)).

[465] Guidelines at 7 (Principal Considerations No. 2 (acceptance of responsibility prior to detection by regulator)).

[466] Guidelines at 7 (Principal Considerations No. 10 (attempt to conceal misconduct to deceive regulatory authorities)).

[467] Tr. 1580-81, 1666-67.

The evidence does not support Enforcement's claim that the misconduct resulted in economic injury to the investing public of almost $6 million. Rather, the evidence establishes that Cantone acted to prevent investors from loss. He used his own funds to make up for a number of Brogdon's missed payments, and obtained court judgments against Brogdon on behalf of Cedars, Oklahoma, Chestnut, and Columbia, requiring Brogdon to repay principal and interest he owes. Cantone's efforts have been successful in significant measure, with investors in Columbia and Cedars, including himself, receiving repayment of principal and interest.[468] Thus we do not find present the aggravating factor of significant economic loss.

For these reasons the Panel concludes that for Cantone, a one-year suspension in all capacities, and for Cantone and CRI a joint and several fine of $100,000, as the Guidelines permit,[469] are appropriately remedial sanctions for their knowing, material omissions and misrepresentation in connection with the Columbia and Oklahoma extensions and the sales of Cherokee COPs.

For negligently failing to disclose to investors in all five of the offerings three material events in Brogdon's history—the federal tax liens, the NHC bankruptcy, and the court decision finding Brogdon failed to honor a guarantee—the Panel concludes that it is appropriate to impose an additional three-month suspension on Cantone in all capacities, and an additional joint and several fine on Cantone and CRI in the amount of $50,000.

B. Supervision

1. The Charges

The Complaint's fifth cause of action alleges that CRI and Christine Cantone failed to fulfill their supervisory obligations in violation of NASD Rule 3010 and FINRA Rule 2010. The Complaint charges that although Christine Cantone was aware of "numerous red flags concerning Cantone's sales of the COP Offerings," she did not take reasonable steps to ensure that Cantone disclosed "all material facts" to investors and prospective investors.[470]

The Complaint identifies four "red flags" Christine Cantone allegedly failed to act upon:

- Cantone's failure to honor the guarantee he made in the Esplanade I and II offerings;
- Brogdon's bars from the securities industry;

[468] Enforcement does not seek restitution or disgorgement.

[469] Guidelines at 9 ("Fines may be imposed individually . . . or jointly and severally as to two or more respondents."). We impose the fines jointly on CRI and Cantone because it was through Cantone that the misconduct for which CRI is liable occurred.)

[470] Compl. ¶ 112-13.

- Cantone's interest payments to investors when Brogdon was late or defaulted on them; and
- Cantone's extension of the maturity dates of notes after Brogdon missed due dates for payments of principal, and Cantone's acceptance of undisclosed fees and increased interest.

The Complaint alleges that by not responding appropriately to these red flags, Christine Cantone did not ensure that her husband "accurately and completely" disclosed these facts to investors in the Brogdon-related COPs, and thereby she, and CRI through her, failed to fulfill their supervisory responsibilities in violation of NASD Rule 3010 and FINRA Rule 2010.[471]

2. Facts

Christine Cantone has 21 years of experience in the securities industry, including 12 years in compliance. During the relevant period of this case, she was CRI'S CCO, with the exception of a three-month period from March to June of 2012.[472] She resigned as CCO in 2014 and currently performs mostly administrative tasks at CRI.[473]

As CCO, under the firm's written supervisory procedures, Christine Cantone's responsibilities included reviewing emails and correspondence, maintaining CRI's written supervisory procedures, and ensuring that representatives under her supervision conducted thorough due diligence.[474] She also supervised her husband[475] and handled the books for the Brogdon-related COPs.[476] When it came to supervising her husband's conduct of due diligence for the Brogdon-related COPs, Christine Cantone testified that she "made sure he did his due diligence,"[477] but she did not "judge the merits of the deal."[478]

Christine Cantone testified that she discussed with Gardner whether Brogdon's 1984 NASD bar should have been disclosed in the Hoover CDM,[479] but had no discussions about revisiting the question during the preparation of the Columbia CDM.[480] This was her only

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[471] *Id.*

[472] Tr. 1202; JX-3, at 4.

[473] Tr. 1207-08.

[474] Tr. 1209, 1214.

[475] Tr. 1209.

[476] Tr. 1203.

[477] Tr. 1215.

[478] Tr. 1887.

[479] Tr. 1890, 1893-94.

[480] Tr. 1889-90.

testimony about reviewing the CDMs for the Brogdon-related COPs to ensure they contained the necessary disclosures.

She testified that she knew first-hand that Cantone had failed to honor the guarantees he made to investors of Esplanade I and II.[481] She was also aware that the NASD had barred Brogdon and he had been charged with Medicaid fraud in the past.[482] Christine Cantone also knew when Brogdon failed to make timely interest payments in the Columbia, Chestnut and Cedars offerings and missed principal payments in the Columbia offering. She participated with Cantone in directing funds from their joint bank account to make interest payments when Brogdon failed to do so in Columbia,[483] Chestnut,[484] and Cedars.[485] She knew when Cantone extended the maturity dates of the notes in the Columbia and Oklahoma offerings and changed the terms by increasing the interest rate Brogdon was to pay and assessing him additional costs.[486] Christine Cantone also knew that Cedala, the Brogdon entity involved in the Cedars offering, sustained losses in 2008, 2009, and 2010;[487] that by May 2013, Brogdon owed more than $350,000 in interest to investors in the Chestnut offering;[488] and that by the end of 2012, the Brogdon entities involved in the Chestnut, and Cedars offerings had sustained losses of more than $2 million.[489]

Christine Cantone's unchallenged testimony established that she reviewed CRI's emails daily,[490] was privy to the email exchanges between Cantone and Gardner,[491] and monitored Cantone's conduct of due diligence for the Brogdon-related COPs to ensure he received and reviewed the documents he requested.[492] She was also copied on numerous emails exchanged

[481] Tr. 1266; Enforcement's Post-Hr'g Br., at 29.

[482] Tr. 1229.

[483] Tr. 1327-28, 1331, 1336-41, 1343.

[484] Tr. 1350-53, 1357-67.

[485] Tr. 1386-88.

[486] Tr. 1379-81, 1900.

[487] Tr. 1383-84.

[488] Tr. 1365.

[489] Tr. 1392-94.

[490] Tr. 1885-86.

[491] Tr. 1889.

[492] Tr. 1887.

between Gardner, Cantone and Brogdon, relating to drafts of offering documents,[493] and she testified she reviewed the drafts of documents Gardner prepared.[494]

3. Arguments

Enforcement points out that despite knowing Esplanade defaulted on principal and interest payments to investors and that COC did not honor its guarantee in the Esplanade COPs, Christine Cantone did not require Cantone to disclose these facts to investors in the Brogdon-related COPs.[495] Enforcement stresses that she should also have ensured that Cantone informed investors of Brogdon's late and missed interest payments to Columbia, Chestnut, and Cedars; his failure to pay principal due in Columbia; the interest payments made by CRI and the Cantones to Columbia, Chestnut, and Cedars; the extensions of maturity dates in Columbia and Oklahoma; the increased interest rate Cantone required from Brogdon; the losses suffered by Cedala, Polo Road, Chestnut Independent Living, and Highlands Assisted Living; and the misuse of $64,500 of funds of Oklahoma investors.[496]

Aware of all of these negative facts, Enforcement argues, it was incumbent upon Christine Cantone to require Cantone to disclose these matters to investors in the Brogdon COPs, and her failure to do so constituted a failure to perform her supervisory responsibilities.[497]

CRI and Christine Cantone contend the facts Cantone failed to disclose were not material, and therefore Cantone and CRI were not required to disclose them to prospective investors, and furthermore, Christine Cantone reasonably relied on the advice of her counsel to conclude that they did not need to be disclosed.[498]

4. Conclusions

NASD Rule 3010(a), the supervision rule in effect at the time relevant to this case, requires member firms to establish and maintain supervision systems "reasonably designed to achieve compliance" with securities laws and NASD and FINRA rules. Reasonable efforts to achieve compliance include responding to "red flags," which are suspicious circumstances that suggest there is an "indication of irregularity" or a potential for legal or regulatory violations.[499]

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[493] E.g., RX-361, at 7, 14, 16, 52, 99, 138, 224, 301, 306, 340, 346, 364.

[494] Tr. 1889.

[495] Enforcement's Post-Hr'g Br., at 29.

[496] *Id*., at 29-30.

[497] *Id*., at 29-30, 58-59.

[498] Respondents' Post-Hr'g Br., at 55.

[499] *Quest Capital Strategies, Inc*., 55 S.E.C. 362 (2001); *Ronald Pellegrino*, Exchange Act Release No. 59125, 2008 SEC LEXIS 2843, at *33 (Dec. 19, 2008).

The Panel carefully considered the evidence and the arguments of the parties. Starting with the failure to honor the guarantee in the Esplanade offerings and Brogdon's bars from the securities industry, we have found that they are not material facts requiring disclosure to prospective investors in the five COP offerings at issue. Furthermore, we have found that Enforcement failed to prove that investor funds from the Oklahoma offering were misused. Therefore, we conclude that Christine Cantone's failure to ensure that these matters were disclosed to investors in the Brogdon COPs, by inclusion in the CDMs or otherwise, did not violate NASD Rule 3010 and FINRA Rule 2010.

However, the Panel has found that Cantone's failure to inform prospective investors in the Columbia and Oklahoma offerings—to whom he proposed extending the maturity dates of their notes—of the changes in the interest rate and other fees assessed against Brogdon, and his failure to inform them and prospective Cherokee investors of Brogdon's late interest payments and missed principal payments in earlier offerings, constitute material omissions. Christine Cantone should have exercised her supervisory authority by directing Cantone to inform investors appropriately. By not doing so, she failed her supervisory obligations as CCO of CRI and Cantone's supervisor. Therefore she, and through her, CRI, violated NASD Rule 3010 and FINRA Rule 2010.

5. Sanctions

FINRA's Sanction Guidelines for failing to supervise recommend a fine of $5,000 to $73,000, and consideration of imposing fines separately on a firm and a responsible individual. They recommend considering a suspension for individuals in all supervisory capacities for up to 30 business days, and limiting a firm's activities for up to 30 business days. For egregious cases, the Guidelines recommend considering suspension for individuals in any or all capacities for up to two years, or a bar, and suspension of a firm with respect to any or all activities for up to two years, or expulsion. The applicable Principal Consideration is whether a supervisory failure allowed misconduct to occur or escape detection.[500]

Enforcement insists Christine Cantone's supervisory failure was so egregious she should be barred from the securities industry, and CRI should be expelled from FINRA. Enforcement argues that the aggravating factors include her ignoring numerous red flags, participating in her husband's misconduct by transferring funds at his direction, her disciplinary history of a previous suspension for supervisory failures, and her refusal to accept responsibility. Citing the Guidelines' Principal Considerations in Determining Sanctions, Enforcement also emphasizes as significant aggravating factors that the Cantones' overall misconduct involved selling investors more than $8 million in COPs, and causing more than $6 million in losses to investors.[501]

[500] Guidelines at 105.

[501] Enforcement's Post-Hr'g Br., at 60-62, and n.343 (citing Guidelines, Principal Considerations No.11).

Enforcement also argues that Christine Cantone's failure to ensure that Cantone informed investors involved repeated instances of misconduct, extending over a lengthy period.[502]

As set forth in detail above, Enforcement has not proven that purchasers of Brogdon-related COPs lost $6 million. Rather, the evidence shows that investors in two of the five offerings included in the Complaint—Columbia and Cedars—and the three Brogdon-related COPs offerings not included in the Complaint but indistinguishable from the others, have received their principal and interest in full. Two of the three remaining offerings included in the Complaint—Chestnut and Oklahoma—are currently listed for sale, and the third, Cherokee, is proceeding according to plan. Thus, one of the chief aggravating factors on which Enforcement relies—economic injury to investors—is absent.

Nonetheless, the Panel finds that Christine Cantone's supervision failures are serious. First, the Guidelines require us to consider her relevant disciplinary history.[503] She and CRI were recently sanctioned for a supervision violation, involving her failure to detect serious misconduct by a registered representative under her supervision who was misappropriating customer funds. Her failure to direct her husband to make disclosures to investors in the COPs in this case extended more than a year. Christine Cantone was fully aware of Brogdon's late and missed payments. She also knew the note maturity extension agreements included changed terms not communicated to investors.[504]

Considering all of the facts and arguments of the parties, the Panel concludes that sanctions less severe than Enforcement recommends will achieve the remedial goals established by the Sanction Guidelines, and will serve to deter similar future misconduct by CRI, Christine Cantone, and others. Therefore, we suspend Christine Cantone in all capacities for six months, and impose a fine of $75,000 jointly and severally on her and on CRI. We impose the fine jointly rather than separately on her and CRI because it was through her that the misconduct attributable to CRI occurred.[505]

C. The Misuse of Customer Funds

1. The Charge

The Complaint's third cause of action alleges that CRI and Cantone misused $64,500 of investor funds in the Oklahoma offering that were to have been used to purchase nursing homes. The charge is that Cantone withheld the funds to pressure Brogdon to make payment on a separate note unrelated to Oklahoma, then wired the funds to Brogdon, who "wired the same

[502] *Id.*, at n.342, citing Principal Considerations No. 9 (misconduct over an extended period) and No. 18 (number, size and character of the transactions at issue).

[503] Guidelines at 2 (General Principle No. 2).

[504] Guidelines at 7 (Principal Considerations Nos. 8, 9).

[505] Guidelines at 9 (fines may be imposed jointly and severally as to two or more respondents).

$64,500 to CRI and Cantone, who then used those funds" to repay investors in an unrelated offering.[506] The Complaint charges that CRI and Cantone thereby violated FINRA Rule 2150(a), which prohibits "making improper use of a customer's . . . funds."

2. Facts

The Oklahoma CDM provided that the offering was to raise $2.8 million to assist a Brogdon entity to purchase five nursing homes.[507] Oklahoma purchased the note at a discount, and was to send Brogdon $2,547,500.[508] However, on July 28, 2011, Cantone wired $2,483,000 to Brogdon—$64,500 less than the full amount owed. An entry in Oklahoma's books stated $64,500 "held for amt Brogdon owes Hoover."[509] This was a reference to Brogdon's obligation to make a semi-annual equity payment of $64,500 to the investors in the Hoover offering, which was due on July 1, 2011, but not paid.[510]

In an August 15, 2011 email to Brogdon, Cantone referred to a need to "settle up on Hoover," and went on to state that "we still have $64,500 in the escrow account" for Oklahoma "that you had me withhold at the time of closing. We can use these funds to make the monthly payments you suggest below."[511]

On August 17, 2011, about three weeks after Cantone wired $2,483,000 to Brogdon to purchase the $2.8 million note, CRI wired $64,500 from the Oklahoma bank account to a Brogdon bank account;[512] and Brogdon wired the same amount from the same Brogdon bank account to Hoover that Cantone then distributed to Hoover investors.[513]

3. Arguments

Enforcement contends that these transactions prove Cantone and CRI misused investor funds allocated for the purchase of nursing homes.[514] By withholding $64,500 of Oklahoma investor funds from the original wire to purchase the note, and later sending that amount to

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[506] Compl. ¶¶ 99-103.

[507] Tr. 625; JX-18, at 1.

[508] Tr. 654-58; JX-18, at 30.

[509] Tr. 1730-31; CX-81.

[510] Tr. 1732-33; JX-6, at 2.

[511] Tr. 1732; CX-82. This was in response to a comment Brogdon made about making Oklahoma interest payments on a monthly, instead of quarterly, basis. CX-82, at 2.

[512] Tr. 676; CX-84.

[513] Tr. 673-76.

[514] Enforcement's Post-Hr'g Br., at 26, 56-57; JX-18, at 1.

Brogdon to send to Hoover, Enforcement argues, Cantone and CRI failed to apply the funds as the customers directed, in violation of Rule 2150(a).[515]

Respondents disagree. They argue that Brogdon directed Cantone to withhold the funds at the closing of the note purchase, as Cantone mentioned to Brogdon in an email.[516] They point out that Respondents did not send the $64,500 to Hoover but wired the funds to the Brogdon SunTrust Bank account Brogdon designated.[517] Cantone testified the funds consisted of "leftover money in the escrow account that needed to be wired to Brogdon . . . [f]or the Oklahoma project."[518] Documentation of the wire transfer from the Oklahoma account reflects the transfer to the Brogdon Family, LLC Sun Trust Bank account with a notation "FBO [for benefit of] Oklahoma Financial."[519] Thus, the Oklahoma funds went where they were supposed to go. It was not Respondents, but a holder of the Brogdon account, who directed $64,500 to Hoover.[520]

Consequently, Respondents argue, the evidence does not establish that Respondents misused Oklahoma investor funds; rather, the evidence shows that Respondents appropriately sent funds from Oklahoma's escrow account to a Brogdon account as directed, at which point the funds were in Brogdon's control. Finally, because there was more than $80,000 already in the account, there is no evidence that the $64,500 transferred from the Brogdon account was, as the Complaint alleges, "the same $64,500" coming from the Oklahoma escrow account.[521]

4. Conclusion

The evidence shows a delay in the payment of $64,500 from the Oklahoma escrow account to Brogdon, apparently at Brogdon's direction. The delay was not lengthy; CRI wired the funds approximately three weeks after the date of the purchase of the note. The delay did not impede the acquisition of the note by Oklahoma. The evidence does not establish, as required to prove misuse of customer funds, that the funds sent from Brogdon's account to Hoover were the same dollars that originated in the Oklahoma escrow account. Any misdirection of funds that may have occurred was from the Brogdon account, not an account controlled by the Cantones.

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515 Enforcement Post-Hr'g Br., at 56, citing *Alderman v. SEC*, 104 F.3d 285 (9th Cir. 1997), holding that respondent wrongfully prevented the prompt return of customer funds that had been mistakenly deposited to his firm's account.

516 Respondents' Post-Hr'g Br., at 48; CX-82.

517 Respondents' Post-Hr'g Br., at 47-48; CX-83, at 6.

518 Tr. 664-65.

519 CX-84, at 1, 4.

520 Respondents' Post-Hr'g Br., at 47. Respondents also point out that the Cantone family invested more than $100,000 in Oklahoma. *Id.*, at 48; CX-74, at 1. Thus, they argue, there is no way to determine whether the $64,500 was their own money; even if they had used it for a purpose other than for the benefit of Oklahoma, there is no proof that it was the money of other investors, an essential element of misuse of funds.

521 Respondents' Post-Hr'g Br., at 48; CX-85, at 3.

The evidence does not establish that the funds sent from Brogdon's account to Hoover were Oklahoma investors' funds.

D. Unsuitable Recommendations to Invest in Cherokee

1. The Charge

The Complaint's fourth cause of action charges CRI and Cantone with violating FINRA Rule 2111(a), FINRA's suitability rule, and thereby also Rule 2010. FINRA Rule 2111(a) requires a member to have a reasonable basis to believe a recommended investment is suitable, based on the member acquiring an understanding of the customer's investment profile by reasonable diligence. Rule 2111.05(a) provides further guidance as to what the suitability requirement means. It states there are three suitability obligations: reasonable-basis suitability, customer-specific suitability, and quantitative suitability. Reasonable-basis suitability, the Rule explains, "requires a member . . . to have a reasonable basis to believe, based on reasonable diligence, that the recommendation is suitable for at least *some* investors . . . A member's . . . reasonable diligence must provide the member . . . with an understanding of the potential risks and rewards associated with the recommended security . . . The lack of such an understanding when recommending a security . . . violates the suitability rule."

The Complaint alleges that CRI and Cantone lacked a reasonable basis to believe their recommendation of the Cherokee COPs was suitable for any investor, including any of the 46 customers to whom they recommended investing, because Cantone failed to conduct a reasonable due diligence investigation into the real estate project that was the underpinning for the investment, and to take into consideration "multiple 'red flags'" concerning Brogdon and his entities.[522]

2. Arguments

Enforcement argues that because of Brogdon's failure to make interest and principal payments to Columbia and Chestnut investors, the Cherokee offering "was not suitable for any investor, regardless of their individual characteristics."[523]

CRI and Cantone counter Enforcement's argument by asserting that Cantone conducted an extensive due diligence investigation into the real estate project Cherokee was helping to fund, and that Brogdon's problems in paying his obligations to investors in the prior offerings were irrelevant to the viability of the Cherokee offering. They also point out that at the conclusion of the hearing, the Cherokee homes were still under construction and progressing as planned: six homes had been sold at prices consistent with the projections in the Cherokee CDM, and investors had received their 10 percent interest annually for the first three years as well as

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[522] Compl. ¶¶ 107-08.

[523] Tr. 2006-07; Enforcement's Post-Hr'g Br., at 57-58.

their shares in the profits from the sales. In addition, construction had been completed on the community clubhouse and four more homes were listed for sale.[524]

3. Conclusion

As discussed in the description of the Cherokee offering above, Cantone testified about his due diligence into the underlying construction project, including obtaining documentation on the first mortgage Arcadia held on the property subdivided for development. Cantone testified that he visited the property and confirmed that the infrastructure for the development was largely completed. As previously discussed, Cantone testified he obtained information on comparable home sales near the development and reviewed an appraisal of the value of the real estate. Cantone's testimony is unrebutted.

The evidence supports the conclusion that Cantone satisfied himself that the Cherokee project, managed by a real estate developer with whom he had dealt in prior successful projects, was likely to do well. The progress of the project so far appears to justify his assessment. Furthermore, we have seen that the Cherokee CDM informed investors that they were exposed to high risk in the hope of obtaining an expected high return. The Cherokee subscription agreement, like those for the other COPs, required investors to attest they were accredited.[525] Although Cantone should have informed Cherokee investors of Brogdon's missed interest and principal payments in prior offerings, he had concluded that the sales of homes in the Cherokee project would generate funds sufficient to pay investors.

Considering these facts, the Panel concludes that Enforcement did not prove by a preponderance of the evidence that CRI and Cantone failed to conduct reasonable due diligence to investigate the viability of the real estate home construction project underlying the Cherokee offering, and did not prove that Cantone lacked a reasonable basis for believing that the Cherokee COPs were suitable for the investors in Cherokee, or any investor. We therefore dismiss the fourth cause of action.

VI. Order

For violating Section 10(b) of the Exchange Act, Rule 10b-5 thereunder, and FINRA Rules 2020 and 2010 by knowingly making a material misrepresentation and omissions in the sales of securities, as alleged in the first cause of action, Cantone is suspended in all capacities for one year, and CRI and Cantone are fined $100,000, jointly and severally.

For violating Sections 17(a) (2) and (3) of the Securities Act of 1933, and FINRA Rule 2010, by negligently failing to disclose material facts in the sales of securities, as alleged in the second cause of action, Cantone is suspended in all capacities for an additional three months, and CRI and Cantone are fined an additional $50,000, jointly and severally.

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[524] Respondents' Post-Hr'g Br., at 53-54; Tr. 1057-64; RX-365; JX-28, at 11.

[525] *See* JX-32 ¶ 8, JX-11 ¶ 8, JX-17 ¶ 9.

For failing to supervise to reasonably ensure that Cantone and CRI informed investors appropriately of material facts in connection with the sales of securities, as alleged in the fifth cause of action, Christine Cantone is suspended in all capacities for six months, and CRI and Christine Cantone are fined $75,000, jointly and severally.

Cantone, Christine Cantone, and CRI are jointly and severally assessed hearing costs in the amount of $17,201.27, including an administrative fee of $750 and $16,451.27 for the hearing transcripts.

The third and fourth causes of action are dismissed.

If this Decision becomes FINRA's final disciplinary action, Anthony Cantone's suspension shall become effective on July 1, 2017, and end on September 30, 2018; Christine Cantone's suspension shall become effective on July 1, 2017, and end on December 31, 2017. The fines shall be due on a date set by FINRA, but not sooner than 30 days after this decision becomes FINRA's final disciplinary action in this proceeding.[526]

Matthew Campbell
Hearing Officer
For the Extended Hearing Panel

Copies to:
- Anthony J. Cantone (via first-class mail and overnight courier)
- Christine L. Cantone (via first-class mail and overnight courier)
- Michael Gross, Esq. (via email and first-class mail)
- Alan Wolper, Esq. (via email)
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- Walter L. Baumgardner, Esq. (via email)
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- Mark Maldonado, Esq. (via email)
- Robert Fisher, Esq. (via email)
- Jeffrey D. Pariser, Esq. (via email)

[526] The Extended Hearing Panel has considered and rejects without discussion all other arguments of the parties.