

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 66000 / December 16, 2011

ADMINISTRATIVE PROCEEDING
File No. 3-14324

In the Matter of	:	
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	:	
Capital Financial Services,	:	ORDER MAKING FINDINGS, AND
Inc. and Brian W. Boppre	:	IMPOSING REMEDIAL SANCTIONS
	:	AND A CEASE-AND-DESIST ORDER
	:	PURSUANT TO SECTIONS 15(b) AND
	:	21C OF THE SECURITIES EXCHANGE
Respondents.	:	ACT OF 1934 AS TO CAPITAL
	:	FINANCIAL SERVICES, INC.
	:	
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I.

On April 6, 2011, the Securities and Exchange Commission (“Commission”) issued an Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934, and Section 9(b) of the Investment Company Act of 1940 against Capital Financial Services, Inc. (“Respondent” or “Capital Financial”).

II.

Respondent has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order as to Capital Financial Services, Inc. (“Order”), as set forth below.

III.

On the basis of this Order and Respondent’s Offer, the Commission finds¹ that:

¹ The findings herein are made pursuant to Respondent’s Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

Summary

These proceedings arise out of Capital Financial Services, Inc.'s failure to perform reasonable due diligence on numerous private placement offerings prior to recommending them to customers where the offerings turned out to be a classic Ponzi scheme and offering fraud.

Respondent

1. Capital Financial is a wholly owned subsidiary of Capital Financial Holdings, Inc., and has been registered with the Commission and a member of the NASD (now FINRA) since 1980. Capital Financial operates as a general securities broker-dealer and is headquartered in Minot, North Dakota. Capital Financial has a network of approximately 273 offices housing over 332 registered representatives. The majority of Capital Financial's revenue is generated from the sale of mutual funds, variable insurance products, and private placements.

Other Relevant Entities

2. Provident Royalties, LLC ("Provident") was a Delaware limited liability company with its principal offices in Dallas, Texas. Provident purportedly invested in oil and gas extraction interests through a group of 23 affiliated entities (collectively the "Provident Rule 506 Entities"). Provident is a beneficial owner in each of the Provident Rule 506 Entities. On June 22, 2009, Provident and 26 affiliated entities filed a voluntary petition for Chapter 11 bankruptcy in the United States Bankruptcy Court for the Northern District of Texas. Provident is currently in receivership.

3. Provident Asset Management, LLC ("PAM") was a Delaware limited liability company which was registered with the Commission as a broker-dealer since March 9, 2004. PAM was the managing broker-dealer for the Provident offerings and exclusively sold the Provident Rule 506 Entity offerings. Capital Financial entered into a selling agreement with PAM for each Provident offering. FINRA expelled PAM from membership on March 18, 2010. PAM is currently in receivership.

4. Provident Rule 506 Entities ("Provident offerings") were a series of companies which have effected private placements claiming exemption from registration of the offered securities under Rule 506 of Regulation D. The offerings sold by Capital Financial included the following companies: Provident Energy 1, LP; Provident Energy 2, LP; Provident Energy 3, LP; Shale Royalties II, Inc.; Shale Royalties 3, LLC; Shale Royalties 4, Inc.; Shale Royalties 5, Inc.; Shale Royalties 6, Inc.; Shale Royalties 7, Inc.; Shale Royalties 9, Inc.; Shale Royalties 12, Inc.; Shale Royalties 14, Inc.; Shale Royalties 17, Inc.; Shale Royalties 18, Inc. The entities are headquartered in Provident's offices in Dallas, Texas. All the Provident Entities are controlled by a court-appointed receiver.

5. Jeffrey A. Lindsey (“Lindsey”), age 47, was a senior vice president and due diligence officer at Capital Financial until June 15, 2010. Lindsey resides in Libertyville, Illinois.

6. Brian W. Boppre (“Boppre”), age 47, was the president and a registered principal at Capital Financial until July 2010. Boppre resides in Minot, North Dakota.

Background

7. From at least September 2006 through January 2009, Capital Financial marketed, recommended to investors, and sold Provident preferred stock and limited partnership interests in a series of 14 private placements. The Provident offerings each claimed an exemption from registration of its offering pursuant to Rule 506 of Regulation D of the federal securities laws. The Provident offerings designated as Shale Royalties, Inc., numbered II through 18, offered two series of non-convertible redeemable cumulative preferred stock, while the offerings designated as Provident Energy, LP, numbered 1 through 3 offered limited partnership interests. The promised return on the Provident offerings was between 15%-18% per year depending on the term.

8. Provident Royalties’ purported business plan included the acquisition of a combination of producing and non-producing sub-surface oil and gas mineral interests, working interests and real property located within the United States. According to the Provident offerings’ Private Placement Memoranda (“PPM”), selling broker-dealers were paid commissions ranging from 5% to 9%. The sales commission varied by the offering, and by share class, with the longer term, Class A share class, paying a larger sales commission. Each PPM, with the exception of Provident Energy 1 and Provident Energy 3, disclosed the selling broker-dealer would be paid a 1% due diligence fee in addition to the sales commission.

9. Although a portion of the proceeds of the Provident offerings were used for the acquisition and development of oil and gas activities, millions of dollars of investor funds were transferred from the later Provident offerings’ bank accounts to the Provident Royalties’ operating account and then used for undisclosed and, often, undocumented loans to earlier Provident offerings. The loan proceeds were then used to pay dividends and returns of capital to investors in earlier Provident offerings in a classic Ponzi scheme.

10. Capital Financial’s due diligence process was run by Boppre and Lindsey. Boppre was responsible for reviewing new offerings and had the authority to approve the Provident offerings for Capital Financial to recommend to investors.

11. Capital Financial was first introduced to Provident during the summer of 2006 by Darren Gibson (“Gibson”), a Provident wholesaler employed by PAM. Gibson provided Lindsey with a Provident PPM and other offering materials. Lindsey had no experience or background in the oil and gas industry.

12. On August 24, 2006, PAM paid Lindsey's expenses to conduct an on-site "due diligence" visit to Provident's Dallas offices. While at Provident, Lindsey met with Provident's principals, Gibson, various Provident land men, and a Provident geologist. The meeting consisted of a presentation of Provident's business plan, followed by a question and answer session. Lindsey also took a tour of the Provident offices. Lindsey did not receive any financial information or review any of the books or records of Provident during his visit. Boppre reviewed the materials provided to Capital Financial by Provident.

13. On September 20, 2006, Capital Financial signed its first selling agreement with PAM for Shale Royalties, II ("Shale II"). Lindsey and Boppre approved Shale II based on the offering materials received from PAM, Lindsey's on-site visit, and the knowledge that other broker-dealers were selling the Provident offerings. Boppre and Lindsey eventually approved fourteen Provident offerings for sale by Capital Financial, even though they had no experience in the oil and gas industry, they only reviewed documents provided by PAM, Lindsey only visited PAM on two occasions to meet with PAM representatives and listen to a presentation on the offerings, and they had performed no independent investigation of any of the Provident offerings.

14. Capital Financial, through its registered principal, Boppre, failed to conduct due diligence on the Provident offerings sufficient to establish reasonable basis suitability before recommending the securities to its customers. Capital Financial never independently investigated any of the information in the offering materials provided by Provident. Capital Financial also never received audited or even unaudited financial statements for any of the Provident offerings. The only financial information Capital Financial received regarding Provident was an unaudited consolidated balance sheet review. However, even the unaudited consolidated balance sheet reviews were not included in the materials Capital Financial received until Shale Royalties 9. Capital Financial received this limited financial information after it approved the recommendation and sale to investors of the Provident offerings covered in those reports.

15. As each Provident offering became fully subscribed, Capital Financial signed selling agreements with PAM for later Provident offerings. In total, Capital Financial recommended and sold fourteen different Provident offerings between September 2006 and January 26, 2009 when Provident suspended sales. Lindsey and Boppre approved each Provident offering for Capital Financial registered representatives to recommend and sell to Capital Financial customers.

16. Capital Financial registered representatives placed approximately 1,087 Provident trades for roughly \$63,000,000. Capital Financial was typically paid an 8% sales commission plus a 1% due diligence fee on the amount of subscription proceeds. This resulted in Capital Financial receiving over \$5,000,000 in sales commissions, and over \$600,000 in due diligence fees on the Provident offerings.

17. Capital Financial's due diligence process for each successive Provident offering was similar to the process for Shale II. For each new Provident offering, Capital Financial received a due diligence packet from PAM. The packet typically contained; a lead broker-dealer bio, certificate of insurance, PPM, certificate of incorporation, corporate bylaws, prior activities, escrow agreement, investor subscription agreement, managing broker dealer agreement, soliciting broker dealer agreement, Form D, news articles, general industry geology reports regarding U.S. shale plays, sample mineral deed, and contact information. Lindsey did not visit Provident before approving each successive Provident offering. Capital Financial did not receive information from any other source before approving any Provident offering.

18. To assist with promoting the Provident offerings, PAM retained the third-party due diligence law firm, Mick & Associates, PC ("Mick") to draft a third-party due diligence report ("Mick report") on each Provident offering. Provident paid all fees for the due diligence reports. Upon request, Mick reports were provided at no cost to Capital Financial. Mick reports were available on all Provident offerings.

19. Capital Financial's due diligence process did not require a Mick report or any other third party due diligence prior to approving a Provident offering. Capital Financial only requested Mick reports on eight of the fourteen offerings it sold, and all eight of those Mick reports were requested by Capital Financial only after it had already approved and started recommending and selling the offering. Boppre did not review any Mick reports prior to approving Provident offerings for sale by Capital Financial.

20. The PPM's for all of the Provident offerings disclosed that the selling broker-dealer would receive a due diligence fee of 1%. However, Capital Financial did not spend any of the 1% due diligence fee conducting due diligence. Although it received over \$600,000 for due diligence fees on the fourteen Provident offerings, Capital Financial incurred no due diligence expenses. At no time did Capital Financial hire independent counsel, an accounting firm, contact third parties regarding Provident's business, or hire consultants to review the Provident offerings.

21. Along with failing to conduct any meaningful due diligence with respect to the Provident offerings prior to recommending them to investors, Capital Financial also ignored significant red flags raised by Mick. The Mick reports beginning with Shale Royalties 9 issued in March 2008, raised concerns about Provident. The Shale Royalties 9 report highlighted Provident's lack of audited financial statements, and raised questions regarding conflicts of interest. The Mick report noted that the earlier Provident offerings were collectively reporting a net operating loss and the limited financial information lacked transparency.

22. Capital Financial failed to question these red flags brought up in the Mick reports with either Provident or Mick. After receiving the Shale 9 Mick report, Capital Financial recommended and sold an additional \$32,000,000 of the Provident offerings. Capital Financial received and purportedly reviewed Mick reports for Shale Royalties 12 and Shale Royalties 18. Both reports raised the same red flags, only emphasizing those concerns by bolding or underlining the type. Although the Mick reports raised concerns about the Provident offerings,

Capital Financial failed to provide its registered representatives with copies of these reports and did not take steps to address whether this information was disclosed to customers.

23. Capital Financial's due diligence responsibility for the Provident offering was heightened by the fact that Provident was a relatively new company, Provident's management had very little experience in the oil and gas industry, Provident failed to produce audited or unaudited financial statements, and before Capital Financial entered into a sales agreement for the first time with Provident, Provident had only effected two prior offerings, both beginning in July 2006 involving a combined total of ten investors. Also, Provident paid a high dividend, and was a very risky investment.

24. Capital Financial had an obligation to conduct a reasonable investigation of a security before recommending that a customer buy that security. Instead, Capital Financial approved the Provident offerings for sale by Capital Financial registered representatives based entirely on information provided by PAM without conducting any independent investigation.

25. Capital Financial lacked information regarding the Provident offerings (e.g., financial information) because it had failed to conduct a reasonable investigation of those offerings, and did not inform customers that it lacked this information and did not inform them of the risks associated with making an investment decision while lacking such information. In addition, although the Mick reports contained significant red flags, information regarding those red flags was never passed along to customers. These failures to disclose constitute material omissions.

26. Broker-dealers cannot recommend a security without having an adequate and reasonable basis for making such recommendation, and cannot rely exclusively upon the issuer for information concerning a company. Lindsey and Boppre knew that neither they nor anyone else at Capital Financial had performed any independent investigation of the Provident offerings, yet they approved the Provident offerings for sale by Capital Financial registered representatives.

27. Lindsey and Boppre knew that they were allowing registered representatives to recommend the Provident offerings for sale without informing them that Capital Financial lacked certain information regarding the Provident offerings (e.g., information on Provident's financial situation, and Provident's relationship with other oil and gas companies) or that they failed to conduct a reasonable investigation of those offerings. Without such information, registered representatives could not have informed customers that Capital Financial was recommending the Provident offerings on the basis of limited information or the risks associated with making an investment decision with limited information.

28. Lindsey and Boppre knew that the Provident offering materials stated that selling broker-dealers would receive a 1% fee to pay for due diligence. This disclosure to investors suggested that Capital Financial conducted independent due diligence in approving the Provident offerings as appropriate to recommend and sell to Capital Financial customers. However, Capital Financial did not perform any independent due diligence.

29. Lindsey and Boppre knew Capital Financial failed to perform adequate due diligence before approving the Provident offerings for sale. Lindsey and Boppre knew they were relying exclusively on Provident for doing their due diligence. Customers were not told that although the Provident offering materials disclosed a 1% due diligence fee and Capital Financial was paid over \$630,000 in due diligence fees, Capital Financial conducted no independent due diligence.

30. Lindsey and Boppre acted at least with severe recklessness. The duty to investigate was heightened by the fact that Provident was a relatively new company operated by individuals with little or no experience in the field of oil and gas, lacked audited financial statements, and promised high returns. Lindsey and Boppre approved Provident offerings without obtaining third-party Mick reports, and failed to question red flags brought to their attention through the few Mick reports received.

Violations

31. As a result of the conduct described above, Respondent willfully violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, which prohibit fraudulent conduct in the offer and sale of securities and in connection with the purchase or sale of securities.

Undertakings

Respondent has undertaken to:

32. Within 60 days of the date of the entry of the Order, at Capital Financial's expense, retain the services of a qualified Independent Consultant ("Consultant"), not unacceptable to the staff of the Division of Enforcement, to: (i) conduct a comprehensive review of Respondent's due diligence policies, practices, and procedures; (ii) determine the adequacy of such due diligence policies and practices; and (iii) prepare a written report, referenced below, reviewing the adequacy of Respondent's due diligence policies, practices, and procedures and making recommendations regarding how Respondent should modify or supplement its due diligence policies and practices. Respondent shall provide a copy of the engagement letter detailing the Consultant's responsibilities to Commission staff;

33. Cooperate fully with the Consultant, including providing the Consultant with access to Respondent's files, books, records, and personnel as reasonably requested for the above-mentioned review, and obtaining the cooperation of respective employees or other persons under Respondent's control;

34. Require the Consultant to report to Commission staff on his/her/its activities as the staff shall request;

35. Permit the Consultant to engage such assistance, clerical, legal or expert, as necessary and at a reasonable cost, to carry out his/her/its activities, and the cost, if any, of such assistance shall be borne exclusively by Respondent;

36. Within one hundred twenty (120) days of the issuance of this Order, unless otherwise extended by Commission staff for good cause, require the Consultant to complete the review described in subparagraph 29 above and prepare a written preliminary report (“Preliminary Report”) that: (i) evaluates the adequacy of the Respondent’s due diligence policies, practices, and procedures; and (ii) makes any recommendations about modifications thereto or additional or supplemental procedures deemed necessary to remedy any deficiencies described in the Preliminary Report. Respondent shall require the Consultant to provide the Preliminary Report simultaneously to both Commission staff and Respondent;

37. Within ninety (90) days of Respondent’s receipt of the Preliminary Report, adopt and implement all recommendations set forth in the Preliminary Report; provided, however, that as to any recommendation that Respondent consider to be, in whole or in part, unduly burdensome or impractical, Respondent may submit in writing to the Consultant and Commission staff, within thirty (30) days of receiving the Preliminary Report, an alternative policy, practice, or procedure designed to achieve the same objective or purpose. Respondent shall then attempt in good faith to reach an agreement with the Consultant relating to each recommendation that Respondent considers to be unduly burdensome or impractical and request that the Consultant reasonably evaluate any alternative policy, practice, or procedure proposed by Respondent. Within fourteen (14) days after the conclusion of the discussion and evaluation by Respondent and the Consultant, Respondent shall require that the Consultant inform Respondent and Commission staff of his/her/its final determination concerning any recommendation that Respondent consider to be unduly burdensome or impractical. Respondent shall abide by the determinations of the Consultant and, within sixty (60) days after final agreement between Respondent and the Consultant or final determination by the Consultant, whichever occurs first, Respondent shall adopt and implement all of the recommendations that the Consultant deems appropriate;

38. Within fourteen (14) days of Respondent’s adoption of all of the recommendations that the Consultant deems appropriate, certify in writing to the Consultant and Commission staff that Respondent has adopted and implemented all of the Consultant’s recommendations;

39. Apply to Commission staff for an extension of the deadlines described above before their expiration and, upon a showing of good cause by Respondent, Commission staff may, in its sole discretion, grant such extensions for whatever time period it deems appropriate;

40. To ensure the independence of the Consultant, not have the authority to terminate the Consultant without prior written approval of Commission staff and shall compensate the Consultant and persons engaged to assist the Consultant for services rendered pursuant to this Order at their reasonable and customary rates;

41. Require the Independent Consultant to enter into an agreement that provides that for the period of engagement and for a period of two years from completion of the engagement, the Independent Consultant shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with Capital Financial, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity. The agreement will also provide that the Independent Consultant will require that any firm with which he/she is affiliated or of which he/she is a member, and any person engaged to assist the Independent Consultant in performance of his/her duties under this Order shall not, without prior written consent of the Division of Enforcement, enter into any employment, consultant, attorney-client, auditing or other professional relationship with Capital Financial, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such for the period of the engagement and for a period of two years after the engagement.

42. Certify, in writing, compliance with the undertakings set forth above. The certification shall identify the undertakings, provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Commission staff may make reasonable requests for further evidence of compliance, and Respondent agrees to provide such evidence. The certification and supporting material shall be submitted to Karen L. Martinez, Esq. Salt Lake Regional Office, 15 W. South Temple, Suite 1800, Salt Lake City, Utah 84101 with a copy to the Office of Chief Counsel of the Enforcement Division, no later than sixty (60) days from the date of the completion of the undertakings.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest, to impose the sanctions agreed to in Respondent Capital Financial's Offer.

Accordingly, pursuant to Sections 15(b) and 21C of the Exchange Act it is hereby ORDERED that:

A. Respondent Capital Financial cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

B. Respondent Capital Financial is censured.

C. Respondent shall comply with the undertakings enumerated in Section III above.

By the Commission.

Elizabeth M. Murphy
Secretary