

# OHIO SECURITIES BULLETIN

A QUARTERLY PUBLICATION OF THE OHIO DIVISION OF SECURITIES

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Governor of Ohio

Gary C. Suhadolnik  
Director of Commerce

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Commissioner of Securities

## Division Guidance on Commonly Encountered Investment Adviser Issues

By Tom Geyer and Caryn Francis

March 18, 2002, marked the three year anniversary of the effective date of the Ohio investment adviser laws. In these three-plus years, the Division has licensed over 550 investment advisers and over 8,900 investment adviser representatives, and received notice filings from nearly 900 SEC-registered investment advisers operating in Ohio. In connection with this licensing program, the Division launched a field examination program with the goal of conducting on-site examinations of all Division-licensed investment advisers for compliance with Ohio law. In addition, the Division has initiated enforcement efforts in the investment advisory area, and in February 2002 the Division secured the first criminal conviction under the Ohio investment adviser laws.

As the Division's investment adviser regulatory program continues to mature, the Division wishes to provide guidance on the following commonly encountered issues. Since Ohio law is based on the federal Investment Advisers Act of 1940, the Division believes that federal law and Securities and Exchange Commission interpretations provide persuasive guidance in the following areas.

### 1. Custody

R.C. 1707.44(M)(2) prohibits an investment adviser or investment adviser representative that is licensed (or required to be licensed) by the Division from taking or having custody of funds or securities of any person, except as provided in rules adopted by the Division. The Division's custody rules are set out in O.A.C. 1301:6-

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## IARD MANDATE: Investment Adviser Representatives

On January 1, 2002, the first mandate of a two-prong initiative by the Division of Securities to use the Investment Adviser Registration Depository (IARD) became effective. Investment advisers licensed, or seeking to be licensed, in Ohio achieved entitlement from the National Association of Securities Dealers, Inc., transitioned onto the IARD, and submitted Forms ADV to the Division via the online IARD throughout the first two quarters of 2002. At this juncture, no paper filings can be submitted by investment advisers to the Division for initial licensure, to renew licensure, or for purposes of updating information—all filings must be submitted via the IARD.

Beginning January 1, 2003, the Division will implement the second prong of the IARD initiative and require all representatives or agents of investment advisers—known in Ohio as investment adviser representatives—to submit all initial, renewal and associated filings to the Division via the IARD. As with the 2002 mandate, investment adviser representatives will be given until the end of the second quarter 2003 to transition onto the IARD. This deadline must be met by current Ohio licensees in order to continue to offer investment advisory services in Ohio. After January 1, 2003, those persons *initially* seeking investment adviser representative licensure can only file their applications via the IARD.

In anticipation of the Division's upcoming IARD mandate for investment adviser representatives, investment advisers should visit the IARD web site at [www.iard.com](http://www.iard.com) or contact the IARD hotline at 240-386-4848 for additional information.

# OHIO

DEPARTMENT OF  
COMMERCE

## DIVISION OF SECURITIES

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Ohio Securities Bulletin

Issue 2002:2

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## Adviser Issues

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3-44(B), and impose a series of safekeeping, notice and audit requirements. The rules are designed to provide a minimum level of protection and security for client funds and securities. While the six steps established by the Division's custody rules are black and white, the issue of what constitutes "custody" has presented some gray areas. Further clouding this area is the fact that it is possible for an adviser to have custody with respect to some accounts, and not have custody with respect to other accounts.

### *General Definition of "Custody"*

The Form ADV defines custody as directly or indirectly holding client funds or securities, having authority to obtain possession of client funds or securities, or having the ability to appropriate client funds or securities.<sup>1</sup> Physical possession is the classic case of custody. However, custody also can arise without physical possession. In this regard, the Division shares the view of the SEC that an adviser has custody when the adviser:

- has a general power of attorney over a client's account
- has signatory power over a client's checking account
- maintains an omnibus-type account in its own name at a broker or a bank in which client securities are maintained after trades settle
- obtains advisory fees by directly billing client custodians without effective oversight by the client or an independent party
- serves as a trustee of client trusts.
- acts as the general partner of a limited partnership client.<sup>2</sup>

This list describes situations where an adviser has the authority to obtain client funds or securities, or has the ability to appropriate the funds or securities, whether or not the adviser has physical possession of the funds or securities. In these situations, the adviser must comply with the Division's

custody rules, except in the limited circumstances described below. Specifically, described below are certain situations in which the adviser does not have physical possession of client funds or securities, and may put in place certain safeguards in order to avoid being deemed to have custody.

### *Alternate Safeguards When the Adviser Has the Authority to Deduct Fees From Client Accounts*

The authority to deduct fees from a client account represents the ability to appropriate client funds, and thus falls within the general definition of custody. However, where a client account is held by an independent custodian, an adviser may deduct fees from the account and not be deemed to have custody if the adviser follows one of the following two alternative sets of safeguards:

• *Alternative One:* (1) The client provides written authorization permitting the adviser's fees to be paid directly from the client's account held by an independent custodian; (2) the adviser sends to the client, and to the custodian at the same time, a bill showing the amount of the fee, the value of the client's assets on which the fee was based, and the specific manner in

which the adviser's fee was calculated; and (3) the custodian agrees to send the client a statement, at least quarterly, indicating all amounts disbursed from the account including the amount of advisory fees paid directly to the adviser.<sup>3</sup>

• *Alternative Two:* (1) The client provides written authorization permitting the adviser's fees to be paid directly from the client's account held by an independent custodian; (2) the adviser sends a bill to the custodian indicating only the amount of the fee to be paid by the custodian; (3) at the same time the bill is sent to the custodian, the adviser sends to the client a separate statement showing the amount of the fee, the value of the client's assets on which the fee was based, and the specific manner in which the adviser's fee was calculated; (4) the adviser discloses to clients that it is the client's responsibility to verify the accuracy of the fee calculation and that the custodian will not determine whether the fee is properly calculated; and (5) the custodian agrees to send the client a statement, at least quarterly, indicating all amounts disbursed from the account including the amount of advisory fees paid directly to the adviser.<sup>4</sup>

## OHIO SECURITIES BULLETIN

Desiree T. Shannon, Esq., Editor

The *Ohio Securities Bulletin* is a quarterly publication of the Ohio Department of Commerce, Division of Securities. The primary purpose of the *Bulletin* is to (i) provide commentary on timely or timeless issues pertaining to securities law and regulation in Ohio, (ii) provide legislative updates, (iii) report the activities of the enforcement section, (iv) set forth registration and licensing statistics and (v) provide public notice of various proceedings.

*The Division encourages members of the securities community to submit for publication articles on timely or timeless issues pertaining to securities law and regulation in Ohio. If you are interested in submitting an article, contact the Editor for editorial guidelines and publication deadlines. The Division reserves the right to edit articles submitted for publication.*

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### Ohio Division of Securities

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*All listings are area code (614)*

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*Alternate Safeguards When an Investment Adviser Serves as Both General Partner of, and Investment Adviser to, a Limited Partnership*

When an investment adviser serves as both the general partner of, and investment adviser to, a limited partnership, the adviser generally has the authority to dispose of funds and securities of the limited partnership, and collect advisory fees from the limited partnership. This authority falls within the general definition of custody. However, if an investment adviser/general partner puts in place the following safeguards, the investment adviser/general partner may make certain withdrawals without being deemed to have custody.<sup>5</sup>

If the limited partnership account is held by an independent custodian,<sup>6</sup> the investment adviser/general partner may receive advisory fees directly from the account of the limited partnership, provided that: (1) an attorney or an independent certified public accountant for the partnership (“independent representative”)<sup>7</sup> provides written authorization, in each case, permitting the advisory fees to be paid directly from the partnership’s account; (2) the investment adviser sends to the independent representative and to the custodian at the same time, a bill showing the amount of the fee, the value of the partnership’s assets on which the fee was based, and the specific manner in which the adviser’s fee was calculated; and (3) the custodian sends to the independent representative and to the partnership a statement, at least quarterly, indicating all amounts disbursed from the account including the amount of advisory fees that are paid directly to the investment adviser.

In addition to receiving advisory fees from the limited partnership account held by an independent custodian, the investment adviser/general partner may make withdrawals representing (i) bona fide reductions in its capital investment in the limited partnership; (ii) its pro rata share of income or capital gains; or (iii) operating and administrative expenses, provided that in each case: (1) the investment adviser sends to the independent representative information sufficient for such representative to calculate the correct amount of the capital account balances; (2) the independent representative authorizes the custodian in writing to make such a transfer; and

(3) the custodian sends to the independent representative and to the limited partnership, at least quarterly, a statement indicating all amounts disbursed from the limited partnership’s account.<sup>8</sup>

*Determining the Existence of a “Client Trust”*

As mentioned above, serving as the trustee of a client trust constitutes custody and requires compliance with the custody rules. Like the SEC, the Division will find that a trust constitutes a “client trust” if any of the following apply: (1) there is an investment advisory contract between the adviser and the trust; (2) the grantor is a current client<sup>9</sup> of the adviser; or (3) the trust agreement provides that the trustee will be compensated and that the trustee will render advice regarding securities to the trust.<sup>10</sup>

*Alternate Safeguards When the Adviser Serves as the Trustee of a Client Trust*

When an adviser serves as a trustee of a client trust, and the trust assets are held by an independent custodian, the adviser may establish alternate safeguards by giving certain instructions to the custodian and a notice to the client.<sup>11</sup> An adviser that establishes and follows the following safeguards will not be deemed to have custody with respect to client trusts held by an independent custodian and covered by the safeguards.

First, the adviser must provide written instructions to the custodian as follows:

- (1) You will not deliver trust securities to any officer or employee of the investment adviser, nor will you transmit any funds to the investment adviser or to any of its employees, except that you may pay trustee fees to the trustee and investment management fees to the investment adviser, provided that:
  - (a) the grantor of the trust, the attorneys for the trust (if it is a testamentary trust), the co-trustee of the trust (other than an officer or employee of the investment adviser), or a defined beneficiary of

the trust has authorized you in writing to pay those fees;

(b) the statements for those fees show the amount of the fees for the trustee, and in the case of statements for investment management fees, show the value of the trust assets on which the fee is based and the manner in which the fee was calculated; and

(c) you agree to send to the grantor of the trust, the attorneys for a testamentary trust, the co-trustee (other than an officer or employee of the investment adviser), or a defined beneficiary of the trust, at least quarterly, a statement of all disbursements from the account of the trust, including the amount of investment management fees paid to the investment adviser and the amount of trustee fees paid to the trustee.

(2) Other than as set forth in (1)(a) above, you may transfer funds or securities (or both) of the trust only upon the direction of an officer or employee of the investment adviser whom you have duly accepted as an authorized signatory for such instructions to you, and only to the following:

(a) a trust company, bank trust department, or brokerage firm independent of the investment adviser, for the account of the trust to which the assets relate;

(b) the named grantors or to the named beneficiaries of the trust;

(c) a third person independent of the investment adviser in payment of the fees or charges of the third person, including, but not limited to: (i) attorney’s, accountant’s, or custodian’s fees for the trust; and (ii) taxes, interest, maintenance or other expenses, if there is property other than securities or cash owned by the trust;

(d) third persons independent of the investment adviser for any other purpose legitimately associated with the management of the trust; or

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## Adviser Issues

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(e) a broker-dealer in the normal course of portfolio purchases and sales, provided that the transfer is made on payment against delivery basis or payment against trust receipt.

Second, if the custodian agrees to these instructions and is authorized to pay the fees, the adviser must send to the grantor of the trust, the attorney for the trust if it is a testamentary trust, the co-trustee (other than an officer or employee of the investment adviser), or a defined beneficiary of the trust, at the same time that it sends any statement to the custodian, a statement showing the amount of the trustee fee or investment management fee, the value of the assets on which the fees were based, and the specific manner in which the fees were calculated.

### 2. Use of "Registered Investment Adviser"

A person that is properly licensed as an investment adviser with the Division, or properly registered as an investment adviser with the SEC, may use the phrase "Registered Investment Adviser." In addition, a person may state that such person is licensed by the Division, by another state, or registered with the SEC, if such statement is true and the effect of such licensure or registration is not misrepresented.<sup>12</sup>

However, a person is prohibited from using the initials "R.I.A." or "RIA."<sup>13</sup> Since these initials have no generally understood meaning, and initials appearing after a name usually indicate a degree or licensed professional position, use of these initials would be misleading.<sup>14</sup> Further, no person may represent or imply in any manner that such person has been sponsored, recommended or approved, or that such person's abilities or qualifications have in any respect been passed upon by the State of Ohio, the Ohio Department of Commerce, the Division, or any other state or federal agency.<sup>15</sup>

### 3. Record-keeping

Every investment adviser licensed by the Division is required to make and keep true, accurate and current copies of certain specified books and records.<sup>16</sup>

#### *The Meaning of "Current"*

The Division recognizes that "current," as used in the record-keeping rule, will vary with the circumstances of the advisory business and the nature of the records being kept. As a general rule:

- *Primary records* of transactions, such as order memoranda, confirmations, invoices, journal entries and logs, must be created concurrently with the transaction, or as soon as practicable thereafter. *Primary records* of transactions must be kept up-to-date at all times.<sup>17</sup>

- *Secondary records* of transactions, such as ledgers and other comparable records to which transactional information is posted, generally must be updated within a few days after transactions occur.<sup>18</sup> In the case of a small adviser, with a few clients, posting transactional data to *secondary records* within ninety days of the transaction may be sufficient.

#### *Applicability of Books and Records Rules*

The Division's books and records rules apply to *all* investment advisers licensed by the Division. There is no exception for sole proprietorships or other small businesses. Every Division licensed investment adviser must keep the sixteen items required by O.A.C. 1301:6-3-151(C)(1). Advisers with custody of client funds or securities also must keep the additional five items required by O.A.C. 1301:6-3-151(C)(2). Finally, advisers that manage client assets, must, in addition to the items required by O.A.C. 1301:6-3-151(C)(1) and (2), keep the two items required by O.A.C. 1301:6-3-151(C)(3).

### 4. Hedge Clauses

Since advisers are required to act in the best interests of their clients, advisers may not use a "hedge clause" or similar contractual provision to attempt to limit the adviser's

liability. Examples of typical hedge clauses that are impermissible include those with language excusing the adviser from liability except in cases of "gross negligence," "wanton malfeasance," "reckless misconduct" or "willful misconduct." O.A.C. 1301:6-3-44(E)(1)(d) prohibits the use of, and declares void, any condition, stipulation, or provision binding any person to waive compliance with the Ohio Securities Act or any rule promulgated thereunder.

### *Endnotes*

1 Item 6 in the Glossary of Terms of Form ADV.

2 SEC Letter from the Office of Compliance Inspections and Examinations to Registered Investment Advisers on Areas Reviewed and Violations Found During Inspections (May 1, 2000), available at [www.sec.gov/divisions/ocie/advltr.htm](http://www.sec.gov/divisions/ocie/advltr.htm).

3 SEC Release IA-1000 (Dec. 3, 1985), Item II.C.5.

4 John B. Kennedy, SEC No-Action Letter (June 5, 1996).

5 *See, e.g.*, Bennett Management Company, Inc., SEC No-Action Letter (Feb. 26, 1990).

6 The independent custodian(s) can be a bank (Bennett Management Company, Inc., SEC No-Action Letter (Feb. 26, 1990); an independent broker-dealer (GBU, Inc., SEC No-Action Letter (April 22, 1993)); or a combination of both (PIMS Incorporated, SEC No-Action Letter (Oct. 21, 1991).

7 The purpose of the independent representative is to address any potential conflicts of interest. An accountant or attorney for the general partner is *not* an independent representative. *See* GBU, Inc., SEC No-Action Letter (April 22, 1993).

# OHIO SECURITIES CONFERENCE 2002

NOVEMBER 22, 2002

**Executive Conference and Training Center  
Vern Riffe Center  
77 South High Street, 31st Floor  
Columbus, Ohio 43215**

Investment Adviser Update  
Securities Law in Cyberspace  
Ohio Control Share Acquisition Act: Northrop Grumman v. TRW  
Private Placements  
Sarbanes-Oxley Act Overview  
Ohio Division of Securities Panel

presented by

**Ohio Division of Securities**

**The Cybersecurities Law Institute at the University of Toledo College of Law**

The meetings of the Ohio Division of Securities Advisory Committees  
will be held in conjunction with this Conference.

In September, a Conference Brochure with detailed information and registration  
instructions will be sent to all Ohio subscribers to the Ohio Securities Bulletin.

8 *See, e.g.*, Bennett Management Company, Inc., SEC No-Action Letter (Feb. 26, 1990); Lend Lease International, SEC No-Action Letter (Sept. 11, 1991); Canyon Management Company, SEC No-Action Letter (Oct. 15, 1991).

9 A client is a "current client" for each year in which the client either receives advice from the adviser or pays for advice received, or to be received, from the adviser. SEC Release IA-1000 (Dec. 3, 1985), Item II.C.4.

10 Melville G. MacKay, SEC No-Action Letter (May 27, 1997).

11 Blum Shapiro Financial Services Inc., SEC No-Action Letter (April 16, 1993).

12 O.A.C. 1301:6-3-44(E)(2).

13 Securities & Syndication Review, SEC No-Action Letter (Feb. 16, 1984).

14 *Id.*

15 O.A.C. 1301:6-3-44(E)(1)(a).

16 O.A.C. 1301:6-3-151(C).

17 American Asset Management Company, SEC No-Action Letter (Aug. 24, 1987).

18 *Id.*

### **Duncan Hill, Inc.**

On May 9, 2002, Duncan Hill, Inc. entered into a Consent Agreement with the Division and consented to the issuance of a Cease and Desist Order, Division Order No. 02-134. Respondent's business address is in Ohio.

The Division found that Duncan Hill, Inc. violated the provisions of Ohio Revised Code section 1707.44(C)(1) by selling unregistered convertible promissory notes that did not meet the qualifications for the requested exemption for private placements pursuant to R.C. 1707.03(Q). The Final Order to Cease and Desist was issued on May 9, 2002.

### **Edward Eugene Hawkins**

On May 29, 2002, the Division issued Division Order No. 02-147, a Cease and Desist Order, against Edward Eugene Hawkins. Respondent is an Ohio resident.

On August 8, 2001, the Division issued a Notice of Opportunity for Hearing, Division Order No. 01-231, to Edward Eugene Hawkins. After an administrative hearing held on January 16, 2002 in which the Hearing Officer ultimately found in the Division's favor, the Division issued its final Cease and Desist Order. The Division held that the Respondent violated the provisions of Ohio Revised Code section 1707.44(C)(1) by selling unregistered investments in a bank debenture trading program for Meyah Investment Group. The Division also held that the investments were sold in violation of Ohio Administrative Code Section 1301:6-3-19(A)(19) since they were not authorized by his employing dealer, Securities Management and Research, Inc.

### **Ivan A. Shepard**

On April 2, 2002, the Division issued Division Order No. 02-106, a Cease and Desist Order, to Ivan A. Shepard of Bay Village, Ohio.

The Division found that Shepard, an Ohio-licensed insurance agent, violated the provisions of Ohio Revised Code section 1707.44(C)(1) and Ohio Administrative Code 1301:6-3-19(A)(19) by, respectively,

selling unregistered securities in the form of pay telephone and related service agreements for National Communications Marketing, Inc. and Communications Marketing Associates, Inc., and failing to obtain prior authorization from securities dealer Signator Investors, Inc. whom he was licensed with at the time of the sales, i.e. "selling away". ETS Payphones, Inc. was the exclusive supplier of the customer-owned coin operated telephones. The Securities and Exchange Commission obtained a permanent injunction against ETS for securities law violations. On March 1, 2002, the Division issued a Notice of Opportunity for Hearing, Division Order 02-079, to Shepard.

The Division notified Shepard of his right to an adjudicative hearing pursuant to Chapter 119 of the Revised Code. A hearing was not requested and the Cease and Desist Order was issued on April 2, 2002.

### **Joseph Sirilla, Jr.**

On April 10, 2002, the Division issued Division Order No. 02-113, a Cease and Desist Order to Joseph Sirilla, Jr. of Campbell, Ohio.

The Division found that Sirilla, an Ohio-licensed insurance agent, violated the provisions of Ohio Revised Code section 1707.44(C)(1) and Ohio Administrative Code 1301:6-3-19(A)(19) by, respectively, selling unregistered securities in the form of pay telephone and related service agreements for National Communications Marketing, Inc. and Communications Marketing Associates, Inc., and failing to obtain prior authorization from securities dealer Conseco Securities, Inc. whom he was licensed with at the time of the sales, i.e. "selling away". The Division found that he was paid commissions of 12% for selling the securities. ETS Payphones, Inc. was the exclusive supplier of the customer-owned coin-operated telephones. The Securities and Exchange Commission obtained a permanent injunction against ETS for securities law violations. On March 6, 2002, the Division issued a Notice of Opportunity for Hearing, Division Order 02-083, to Sirilla.

The Division notified Sirilla of his right to an adjudicative hearing pursuant to

Chapter 119 of the Revised Code. A hearing was not requested and the Cease and Desist Order was issued on April 10, 2002.

### **George A. Price**

On April 16, 2002, the Division issued Division Order No. 02-118, a Cease and Desist Order to George A. Price of Shadyside, Ohio.

The Division found that Price, an Ohio-licensed insurance agent, violated the provisions of Ohio Revised Code sections 1707.44(A)(1) and 1707.44(C)(1) by selling unregistered securities in the form of pay telephone and related service agreements for National Communications Marketing, Inc. and Communications Marketing Associates, Inc. while he was unlicensed as a securities salesperson. The Division found that he was paid commissions of 10% to 12% for selling the securities. ETS Payphones, Inc. was the exclusive supplier of the customer-owned coin-operated telephones. The Securities and Exchange Commission obtained a permanent injunction against ETS for securities law violations. On March 13, 2002, the Division issued a Notice of Opportunity for Hearing, Division Order 02-091, to Price.

The Division notified Price of his right to an adjudicative hearing pursuant to Chapter 119 of the Revised Code. A hearing was not requested and the Cease and Desist Order was issued on April 16, 2002.

### **William G. Burkett**

On April 30, 2002, the Division issued Division Order No. 02-129, a Cease and Desist Order to William G. Burkett of Powell, Ohio.

The Division found that Burkett, an Ohio-licensed insurance agent, violated the provisions of Ohio Revised Code sections 1707.44(A)(1), 1707.44(B)(4), 1707.44(C)(1) and 1707.44(G) and Ohio Administrative Code 1301:6-3-19(A)(5) by selling unregistered securities in the form of pay telephone and related service agreements for National Communications Marketing, Inc. and Communications Marketing Associates, Inc. while he was unlicensed as a secu-

rities salesperson. He also misrepresented the risks and suitability of investing in the securities. The Division found that he shared commissions of at least 14% with another salesperson from the securities sales. ETS Payphones, Inc. was the exclusive supplier of the customer-owned coin-operated telephones. The Securities and Exchange Commission obtained a permanent injunction against ETS for securities law violations. On March 28, 2002, the Division issued a Notice of Opportunity for Hearing, Division Order 02-104, to Burkett.

The Division notified Burkett of his right to an adjudicative hearing pursuant to Chapter 119 of the Revised Code. A hearing was not requested and the Cease and Desist Order was issued on April 30, 2002.

### **Ronald A. Thompson**

On May 9, 2002, the Division issued Division Order No. 02-135, a Cease and Desist Order to Ronald A. Thompson of Boca Raton, Florida.

The Division found that Thompson violated the provisions of Ohio Revised Code sections 1707.44(A)(1), 1707.44(C)(1) and Ohio Administrative Code 1301:6-3-19(A)(19) by selling unregistered securities in the form of pay telephone and related service agreements for National Communications Marketing, Inc. and Communications Marketing Associates, Inc., some of which were made while he was unlicensed as a securities salesperson, and he shared commissions with someone who wasn't licensed as a salesperson at the time of some of the sales. The Division found that he shared commissions of at least 14% with another salesperson from the securities sales. ETS Payphones, Inc. was the exclusive supplier of the customer-owned coin-operated telephones. The Securities and Exchange Commission obtained a permanent injunction against ETS for securities law violations. On March 28, 2002, the Division issued an Amended Notice of Opportunity for Hearing, Division Order 02-063, to Thompson.

The Division notified Thompson of his right to an adjudicative hearing pursuant to Chapter 119 of the Revised Code. A hearing request was made and then with-

drawn, and the Cease and Desist Order was issued on May 9, 2002.

### **Combined Agency, Inc.; James E. Ady**

On May 9, 2002, the Division issued a Cease and Desist Order, Division Order No. 02-137, to Combined Agency, Inc. and James E. Ady of Spokane, Washington.

The Division found that Combined Agency and Ady violated the provisions of Ohio Revised Code sections 1707.44(A)(1) and 1707.44(C)(1) by selling unregistered viatical settlements while unlicensed as a securities dealer and salesperson. The Division's investigation stemmed from the sale of viatical settlements of Robin Hood International, Ltd. to Ohio investors. The Division found that commissions of 10% were paid to Combined Agency and Ady for the viatical settlements. On April 4, 2002, the Division issued a Notice of Opportunity for Hearing, Division Order 02-111, to Combined Agency and Ady.

The Division notified Combined Agency and Ady of their right to an adjudicative hearing pursuant to Chapter 119 of the Revised Code. A hearing was not requested and the Cease and Desist Order was issued on May 9, 2002.

### **Keith A. Votaw**

On May 9, 2002, the Division issued Division Order No. 02-138, a Cease and Desist Order to Keith A. Votaw of Bellefontaine, Ohio.

The Division found that Votaw, an Ohio-licensed insurance agent, violated the provisions of Ohio Revised Code sections 1707.44(A)(1) and 1707.44(C)(1) by selling unregistered securities in the form of pay telephone and related service agreements for National Communications Marketing, Inc. and Communications Marketing Associates, Inc. while he was unlicensed as a securities salesperson. The Division found that he was paid commissions of 10% to 12% for selling the securities. ETS Payphones, Inc. was the exclusive supplier of the customer-owned coin-operated telephones. The Securities and Exchange Commission obtained a permanent injunction against ETS for securities law violations. On April 4, 2002, the Division issued a Notice of Opportunity

for Hearing, Division Order 02-110, to Votaw.

The Division notified Votaw of his right to an adjudicative hearing pursuant to Chapter 119 of the Revised Code. A hearing was not requested and the Cease and Desist Order was issued on May 9, 2002.

### **Beneficial Assistance**

On May 24, 2002, the Division issued a Final Order to Cease and Desist, Division Order No. 02-144, to Beneficial Assistance of Baltimore, Maryland.

The Division found that Beneficial Assistance violated the provisions of Ohio Revised Code section 1707.44(C)(1) by selling unregistered viatical settlements totaling approximately \$1,504,037.08 to Ohio investors through local salespeople which the company recruited and paid sales commissions.

On October 26, 2001, the Division issued a Notice of Opportunity for Hearing, Division Order 01-284, to Beneficial. An administrative hearing was requested and held on February 4, 2002. The hearing officer issued a report containing recommendations that were favorable to the Division. The report was accepted by the Division, and the Final Order to Cease and Desist was issued on May 24, 2002.

### **Delbert R. Cogar**

On June 3, 2002, the Division issued Division Order No. 02-151, a Cease and Desist Order to Delbert R. Cogar of Ada, Ohio.

The Division found that Cogar, an Ohio-licensed insurance agent, violated the provisions of Ohio Revised Code sections 1707.44(A)(1) and 1707.44(C)(1) by selling unregistered securities in the form of pay telephone and related service agreements for National Communications Marketing, Inc. and Communications Marketing Associates, Inc. while he was unlicensed as a securities salesperson. The Division found that he was paid commissions of 10% to 12% for selling the securities. ETS Payphones, Inc. was the exclusive supplier of the customer-owned coin-operated telephones. The Securities and Exchange Commission obtained a permanent injunction against ETS for securities law violations. On April 23, 2002,

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## Enforcement Reports

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the Division issued a Notice of Opportunity for Hearing, Division Order 02-122, to Cogar.

The Division notified Cogar of his right to an adjudicative hearing pursuant to Chapter 119 of the Revised Code. A hearing was not requested and the Cease and Desist Order was issued on June 3, 2002.

### Robert A. Tennant

On June 12, 2002, the Division issued Division Order No. 02-164, a Cease and Desist Order to Robert A. Tennant of Akron, Ohio.

The Division found that Tennant, an Ohio-licensed insurance agent, violated the provisions of Ohio Revised Code sections 1707.44(A)(1) and 1707.44(C)(1) by selling unregistered securities in the form of pay telephone and related service agreements for National Communications Marketing, Inc. and Communications Marketing Associates, Inc. while he was unlicensed as a securities salesperson. The Division found that he was paid commissions of 12% for selling the securities. ETS Payphones, Inc. was the exclusive supplier of the customer-owned coin-operated telephones. The Securities and Exchange Commission obtained a permanent injunction against ETS for securities law violations. On May 9, 2002, the Division issued a Notice of Opportunity for Hearing, Division Order 02-139, to Tennant.

The Division notified Tennant of his right to an adjudicative hearing pursuant to Chapter 119 of the Revised Code. A hearing was not requested and the Cease and Desist Order was issued on June 12, 2002.

### Jeffrey W. Fleming

On May 15, 2002, the Division issued a Cease and Desist Order, Division Order No. 02-143, to Jeffrey W. Fleming of Boardman, Ohio.

On April 4, 2002, the Division issued a Notice of Opportunity for Hearing, Division Order No. 02-108, to Jeffrey W. Fleming pursuant to Revised Code Chapter 119. The Division alleged that Fleming violated Ohio Revised Code sections

1707.44(A)(1) and 1707.44(C)(1) by selling securities to Ohio residents without a license and selling or causing to be sold unregistered securities to Ohio residents in the form of investment contracts of ETS Payphones Inc. and Phoenix Telecom Inc. The Division also notified Fleming of his right to an adjudicative hearing pursuant to Chapter 119 of the Revised Code. A hearing was not requested and a final Cease and Desist Order was issued to Fleming on May 15, 2002.

### John Zimmerman

On January 14, 2002, the Division issued Order No. 02-019, a Cease and Desist Order, against John Zimmerman. Throughout 1999 Zimmerman sold to Ohio residents, on behalf of Accelerated Benefits Corporation, fractionalized interests in viatical settlements. These interests in viatical settlements are securities under the Ohio Securities Act but were not registered with the Division. Furthermore, Respondent's conduct with respect to selling the fractionalized interests in viatical settlements constituted his acting as a dealer, as defined by Ohio Revised Code Section 1707.01(E)(1), even though he was not licensed as such. Therefore, on December 10, 2001, the Division issued Order No. 01-326, a Notice of Opportunity for Hearing, against John Zimmerman for allegedly violating Ohio Revised Code Section 1707.01(C)(1), *i.e.*, the unregistered sale of securities, along with Ohio Revised Code Section 1707.44(A)(1), *i.e.*, selling securities to Ohio residents without being licensed as a dealer. The Respondent did not request a hearing pursuant to Chapter 119 of the Ohio Revised Code, thereby allowing the Division to issue its Cease and Desist Order No. 02-019, which incorporated the allegations set forth in the Notice of Opportunity for Hearing.

### William Griffioen

On January 14, 2002, the Division issued Order No. 02-018, a Cease and Desist Order against William Griffioen. From October of 1999 through December of 1999, Griffioen sold to Ohio residents, on behalf of Accelerated Benefits Corporation, fractionalized interests in viatical settlements.

These interests in viatical settlements are securities under the Ohio Securities Act but were not registered with the Division. Furthermore, Respondent's conduct with respect to selling the fractionalized interests in viatical settlements constituted his acting as a dealer, as defined by Ohio Revised Code Section 1707.01(E)(1), even though he was not licensed as such. Therefore, on December 10, 2001, the Division issued Order No. 01-325, a Notice of Opportunity for Hearing, against William Griffioen for allegedly violating Ohio Revised Code Section 1707.01(C)(1), *i.e.*, the unregistered sale of securities, along with Ohio Revised Code Section 1707.44(A)(1), *i.e.*, selling securities to Ohio residents without being licensed as a dealer. The Respondent did not request a hearing pursuant to Chapter 119 of the Ohio Revised Code, thereby allowing the Division to issue its Cease and Desist Order No. 02-018, which incorporated the allegations set forth in the Notice of Opportunity for Hearing.

### David Barnes

On January 14, 2002, the Division issued Order No. 02-020, a Cease and Desist Order against David Barnes. From August of 1999 through October of 1999, Barnes sold to Ohio residents, on behalf of Accelerated Benefits Corporation, fractionalized interests in viatical settlements. These interests in viatical settlements are securities under the Ohio Securities Act but were not registered with the Division. Furthermore, Respondent's conduct with respect to selling the fractionalized interests in viatical settlements constituted his acting as a dealer, as defined by Ohio Revised Code Section 1707.01(E)(1), even though he was not licensed as such. Therefore, on December 10, 2001, the Division issued Order No. 01-323, a Notice of Opportunity for Hearing against David Barnes for allegedly violating Revised Code Section 1707.01(C)(1), *i.e.*, the unregistered sale of securities, along with Revised Code Section 1707.44(A)(1), *i.e.*, selling securities to Ohio residents without being licensed as a dealer. The Respondent did not request a hearing pursuant to Chapter 119 of the Ohio Revised Code, thereby allowing the Division to issue its Cease and Desist Order No. 02-020, which incorporated the allegations set forth in the Notice of Opportunity for Hearing.



## Timothy D. Austin

On January 14, 2002, the Division issued Order No. 02-021, a Cease and Desist Order, against Timothy D. Austin. From December of 1998 through August of 2000, Austin sold to Ohio residents, on behalf of Accelerated Benefits Corporation, fractionalized interests in viatical settlements. These interests in viatical settlements are securities under the Ohio Securities Act but were not registered with the Division. Therefore, on December 10, 2001, the Division issued Order No. 01-324, a Notice of Opportunity for Hearing against Timothy D. Austin for allegedly violating Ohio Revised Code Section 1707.01(C)(1), i.e., the unregistered sale of securities. The Respondent did not request a hearing pursuant to Chapter 119 of the Ohio Revised Code, thereby allowing the Division to issue its Cease and Desist Order No. 02-021, which incorporated the allegations set forth in the Notice of Opportunity for Hearing.

## Kevin L. Lawrence

On May 28, 2002, the Division issued Order No. 02-146, a Cease and Desist Order, against Kevin L. Lawrence. From July 2000 through April 2001, Lawrence, as president of Health Maintenance Centers, Inc., sold to Ohio residents shares of common stock in Health Maintenance Centers, Inc. These shares of stock are securities under the Ohio Securities Act but were not registered with the Division. Therefore, on March 8, 2002, the Division issued Order No. 02-087, a Notice of Opportunity for Hearing against Kevin L. Lawrence for allegedly violating Ohio Revised Code Section 1707.44 (C)(1), i.e. the unregistered sale of securities. Mr. Lawrence consented to the issuance of Order No. 02-146, which incorporated the allegations set forth in the Notice of Opportunity for Hearing.

## Health Maintenance Centers, Inc.

On May 9, 2002, the Division issued Order No. 02-136, a Cease and Desist Order against Health Maintenance Centers, Inc. From July 2000 through April 2001, Health Maintenance Centers, Inc. sold to Ohio residents shares of common stock in said corporation. These shares of stock are

securities under the Ohio Securities Act but were not registered with the Division. Therefore, on March 8, 2002, the Division issued Order No. 02-087, a Notice of Opportunity for Hearing, against Health Maintenance Centers, Inc. for allegedly violating Revised Code Section 1707.44 (C)(1), i.e. the unregistered sale of securities. Health Maintenance Centers, Inc. did not request a hearing pursuant to Chapter 119 of the Ohio Revised Code, thereby allowing the Division to issue its Cease and Desist Order No. 02-136 which incorporated the allegations set forth in the Notice of Opportunity for Hearing as findings.

## Caribbean Treasure Hunters, Inc.

On June 19, 2002, the Division issued Division Order No. 02-167, a Cease and Desist Order against Caribbean Treasure Hunters, Inc., which conducted business from Deerfield Beach, Florida.

The Division found that the Respondent had violated the provisions of Ohio Revised Code section 1707.44(C)(1) by selling unregistered securities. The Division's allegations stem from the offer for sale in August 2001 by means of a "cold call" convertible preferred stock. The Division notified Respondent of its right to an administrative hearing pursuant to Chapter 119 of the Revised Code, which Respondent waived by failing to timely request a hearing. Therefore, the Division issued Cease and Desist Order No. 02-167.

## James F. Crawford

On June 6, 2002, the Division issued Division Order No. 02-162, a Cease and Desist Order, by Consent, against James F. Crawford. Respondent conducted business from North Canton, Ohio.

The Division found that Respondent violated Ohio Revised Code section 1707.44(C)(1) by selling unregistered securities, and that Respondent further violated Ohio Administrative Code Rule 1301:6-3-19(A)(19) by "selling away" while employed by Lincoln Financial Advisors Corporation.

The Division's allegations stem from the sale of promissory notes, investment contracts and limited liability company

membership interests for Allstate Finance, Inc., Alpha Telecom, Inc. and Hotel Connect #600, LLC.

The Division notified Respondent of his right to an administrative hearing pursuant to Chapter 119 of the Revised Code, which Respondent waived by entering into the Consent Agreement. Therefore, the Division issued Cease and Desist Order No. 02-162.

## Criminal Updates

On April 15, 2002, **Essam A. Mikhail** was sentenced to four years in prison and ordered to pay \$29,123 in restitution. Mikhail was indicted on May 25, 2001, and pled guilty on February 11, 2002, in Franklin County Common Pleas Court to one felony count of acting as an unlicensed investment adviser and one felony count of improperly maintaining custody of a client's funds or securities. This case represents the Division's first conviction under the new investment adviser provisions to the Ohio Securities Act enacted in March 1999.

On April 22, 2002, **D. Gerald Lach** pled guilty in the Clermont County Common Pleas Court to 12 counts of selling unregistered securities to Ohio residents. He was sentenced to four years in prison and given credit for the approximately one year he has already served. Lach was originally indicted on August 30, 2000, on 55 felony counts in connection with sales of securities in several companies that he owned or controlled including Cincinnati Regional Initiative Inc., Midwest Regional Authority, Community Concerned Citizens Inc., and Storehouse Malachai 3:10 Inc. Four additional counts, including one count of selling unregistered securities, two counts of false representations in the sale of securities, and one count of fraudulent activity in the sale of securities were added on January 25, 2001, after authorities learned that Lach had attempted to sell \$200,000 in stock in early January 2001.

**Paul A. Rendina** was arraigned in Willoughby Municipal Court on June 27, 2002 on seven securities counts (all second degree felonies) filed against him on May 20th. The counts include one count of the

*Continued on page 12*

## Licensing Statistics

| License Type                      | YTD 2001 |
|-----------------------------------|----------|
| Dealer                            | 2,337    |
| Salesmen                          | 123,694  |
| Investment Adviser                | 1,448    |
| Investment Adviser Representative | 8,933    |

## Final Order Summaries

*The following is a summary of recent final orders issued by the Division in response to salesperson and investment adviser representative license applications.*

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| PARTY                             | DECISION | ORDER SENT/NO.   | ALLEGATIONS<br>H.O. RECOMMENDATIONS  |
|-----------------------------------|----------|------------------|--|
| Charles William Sheets            | Denied   | 5/2/02<br>02-130 | ADM 1301:6-3-19(D)<br>(2),(7), and (9)<br>1707.19(A)(1)<br>Findings Approved |
| Horizon Investment Advisors, Inc. | Denied   | 6/6/02<br>02-161 | ADM 1301:6-3-19(D)(9)<br>R.C. 1707.19(F)<br>Hearing Not Requested            |

## Registration Statistics

The following table sets forth the number of registration, exemption, and notice filings received by the Division during the second quarter of 2002, compared to the number of filings received during the second quarter of 2001. Likewise, the table compares the year-to-date filings for 2002 and 2001.

| Filing Type  | 2nd Qtr '02 | YTD '02 | 2nd Qtr '01 | YTD '01 |
|--------------|-------------|---------|-------------|---------|
| 1707.03(Q)   | 34          | 68      | 31          | 70      |
| 1707.03(W)   | 4           | 12      | 1           | 9       |
| 1707.03(X)   | 275         | 524     | 262         | 563     |
| 1707.03(Y)   | 1           | 5       | 4           | 4       |
| 1707.04/.041 | 1           | 3       | 0           | 1       |
| 1707.06      | 17          | 48      | 17          | 40      |
| 1707.09/.091 | 49          | 85      | 34          | 84      |
| Form NF      | 1144        | 2225    | 1109        | 2517    |
| 1707.39/.391 | 11          | 24      | 27          | 50      |
| Total        | 1536        | 2993    | 1485        | 3340    |
|              |             |         |             |         |

## Capital Formation Statistics\*

Because the Division's mission includes enhancing capital formation, the Division tabulates the aggregate dollar amount of securities to be sold in Ohio pursuant to filings made with the Division. As indicated in the notes to the table, the aggregate dollar amount includes a value of \$1,000,000 for each "indefinite" investment company filing. However, the table does not reflect the value of securities sold pursuant to "self-executing exemptions" like the "exchange listed" exemption in R.C. 1707.02(E) and the "limited offering" exemption in R.C. 1707.03(O). Nonetheless, the Division believes that the statistics set out in the table are representative of the amount of capital formation taking place in Ohio.

\*Categories reflect amount of securities registered, offered, or eligible to be sold in Ohio by issuers.

\*\*Investment companies may seek to sell an indefinite amount of securities by submitting maximum fees. Based on the maximum filing fee of \$1100, an indefinite filing represents the sale of a minimum of \$1,000,000 worth of securities, with no maximum. For purposes of calculating an aggregate capital formation amount, each indefinite filing has therefore been assigned a value of \$1,000,000.

| Filing Type                 | Second Qtr 2002         | YTD 2002                 |
|-----------------------------|-------------------------|--------------------------|
| <b>Exemptions</b>           |                         |                          |
| Form 3(Q)                   | 317,264,737             | 386,431,935              |
| Form 3(W)                   | 8,832,580               | 22,494,580               |
| Form 3(X)                   | 41,696,877,829          | 179,903,333,032          |
| Form 3(Y)                   | 1,000,000               | 409,751,000              |
| <b>Registrations</b>        |                         |                          |
| Form .06                    | 192,879,463             | 445,925,862              |
| Form .09/.091               | 3,506,807,790           | 17,000,017,216           |
| <b>Investment Companies</b> |                         |                          |
| Definite                    | 92,165,700              | 2,211,110,799            |
| Indefinite**                | 613,000,000             | 1,141,000,000            |
| <b>TOTAL</b>                | <b>\$46,428,828,099</b> | <b>\$201,307,064,424</b> |

## Enforcement Reports

*continued from page 9*

unregistered sale of securities, three counts of securities fraud and three counts of false representations in the sale of securities. The charges relate to the sale of securities by Rendina, a C.P.A., to Ohio investors in his entities, Willowlake Rental Partnership #197 and 34101 GP, Inc. Rendina's preliminary hearing is scheduled for July 25, 2002.

### Theresa Stencil

Theresa Stencil was indicted on two counts of engaging in a pattern of corrupt activity, 14 counts of theft, 19 counts of selling unregistered securities, two counts of securing writings by deception, and one count of tampering with records by a Lorain County grand jury on April 10, 2002. Stencil owned and operated Augar-Lane Development Co. Ltd, Western Reserve Arabian Ltd., Merit Financial Services, Inc. and Fam-

ily Focus Center. The Division of Securities Suspended Stencil's securities salesperson license for the sale of Augar-Lane promissory notes to Ohio investors on October 19, 2001, and subsequently revoked her securities license on January 28, 2002.

### John H. Rodeman

On April 16, 2002, John H. Rodeman pled guilty to a four count Information in U.S. District Court in Akron. The four counts included conspiracy, securities fraud, mail fraud and filing a false income tax return. Rodeman is a former salesman and participant in Andrew P. Bodnar's \$41 million ponzi scheme. In August 1998, the Division filed a motion asking the Summit County Court of Common Pleas to appoint a receiver to recover the assets of Bodnar and his affiliated entities. The court approved the application, appointed the Receiver and the Receivership is still ongoing.

## Civil Actions

### George J. Fiorini II dba The Fiorini Agency and Guardian Investments, LLC.

An agreed permanent injunction was entered against Guardian Investments on April 8, 2002, in Hamilton County Common Pleas Court. A contempt hearing was held by the court and Fiorini was found guilty of contempt on April 19, 2002, and ordered to provide all documents and information to a CPA appointed by the court. On April 20, 2001, the Division filed a complaint requesting preliminary and permanent injunctions in Hamilton County Common Pleas Court against George J. Fiorini II dba The Fiorini Agency and Guardian Investments, LLC. Fiorini advertised and sold his "10% Plus Income Plan" to Ohio residents and represented the plan as a low risk investment opportunity. In fact, Fiorini offered high risk, unsecured promissory notes in Guardian Investments. On September 4, 2001, the court entered an order granting the Division a preliminary injunction.

# OHIO SECURITIES BULLETIN

Ohio Department of Commerce  
Division of Securities  
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22nd Floor  
Columbus, Ohio 43215

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