OHIO SECURITIES BULLETIN

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Bob Taft
Governor of Ohio

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Director of Commerce

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The Investment Adviser Compliance Program: A to Z

By Thomas E. Geyer

An investment adviser licensed, or required to be licensed, by the Ohio Division of Securities must adopt and implement written policies and procedures reasonably designed to prevent violations by the adviser (and its supervised persons[1]) of the Ohio Securities Act and the administrative rules promulgated by the Division.[2] In connection with adopting and implementing this written compliance program, an adviser must designate a person, who is a supervised person, as the "Chief Compliance Officer" ("CCO") responsible for administering the program. This compliance program requirement provides an adviser with the opportunity to establish a comprehensive – A to Z – set of standards governing its operations and compliance obligations.

Adoption and implementation of a compliance program, however, is not amenable to an "off-the-shelf" approach. Rather, an adviser must consider the scope of its services and its fiduciary duties, inventory its compliance requirements, and identify actual and potential conflicts of interest. From this starting point, an adviser must develop a program consisting of written policies and procedures that address its relevant fiduciary, operational and regulatory obligations. Following is a list of the most common fiduciary and regulatory obligations facing an adviser – a list that can serve as a checklist for a comprehensive compliance program.[3]

Advertising. Ohio law prohibits advertising by advisers that contains any untrue statement of material fact or is otherwise false or misleading.[4] Accordingly, the program must contain a procedure for the initial and periodic review of all advertising and marketing materials. The program should recognize that advertising is broadly defined to include any notice, circular, letter, or other written communication addressed to more than one person, and any notice or other announcement in any publication, on the radio, or on television.[5] The procedure should indicate who is authorized to approve materials, how such approval is memorialized, and

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provide safeguards against alteration of approved materials without approval of the alteration. The procedure also should provide for maintenance of copies of all advertising and marketing material, along with noted approvals, pursuant to the Division's recordkeeping requirements (discussed below). In addition, materials supporting any performance advertising should be thoroughly reviewed and properly maintained.

Books and Records. The Division's rules provide a detailed set of record-keeping requirements.[6] All advisers must keep records in 20 basic categories, and advisers that have custody and/or manage client assets must keep additional records. The required books and records must be maintained for not less than five years, the first two in an appropriate office of the adviser and subsequently in an easily accessible place. While the program should provide for easy accessibility to the records, it should limit access only to authorized personnel, and also provide for the reasonable safeguarding of the records from loss, alteration or destruction. For electronically-stored records, back-up files should be maintained and separately stored; for non-electronic records, it is advisable to make electronic copies that are similarly backed-up and separately stored. Records should be appropriately updated[7] and maintained in an accurate and well-organized manner. In addition to maintaining these operational records as required by the Division, as a matter of good business practice an adviser should maintain accurate and current organizational documents such as its articles of incorporation, code of regulations and minute book.

Custody. The concept of "custody" is broader than just physical possession, and means holding, directly or indirectly, client funds or securities or having any authority to obtain possession of them. Ohio licensed advisers with custody of client funds or securities must comply with a three-part standard that requires safekeeping by a "qualified custodian," notice of the custody arrangements to clients, and quarterly account statements to clients.[8] In addressing custody, a compliance program first should provide for a procedure to determine whether or not the adviser has custody. If so, the adviser must make arrangements for a qualified custodian to maintain client funds and securities either (i) in a separate account for each client under that client's name, or (ii) in accounts that contain only the adviser's clients' funds and securities under the adviser's name as agent or trustee for the clients. Second, the program must provide for notice of the custodial arrangements to clients. Third, the program must provide that clients receive an account statement, at least quarterly, that identifies (i) the amount of funds and securities in the account at the end of the quarter, and (ii) all transactions effected in the account during the quar-

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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.

Ohio Division of Securities

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ter. The adviser should receive a copy of this quarterly statement sent by the custodian. If advisory fees are to be deducted from the clients' account, it is advisable as a best practice that the adviser send deduction instructions to the custodian with a copy to the client.

Disclosure. Advisers generally are required to deliver to each client and prospective client a written disclosure statement that describes the adviser's business practices and the adviser's business and educational background.[9] This disclosure must contain the items required by Part II of Form ADV, and may be in the form of Part II or take the form of a "brochure." The program should establish a mechanism to ensure the accuracy of all information contained in the brochure. The program also should provide a procedure to ensure the initial delivery of the brochure, as well as confirmation of such delivery. In addition, the program should provide for a procedure to document the adviser's annual offer to clients to provide a copy of the brochure. Finally, the program should provide for the periodic review of the brochure and amendment as necessary.

Ethics. Closely related to the compliance program requirement is the notion that an adviser should adopt and implement a code of ethics. SEC-registered advisers are required to do so;[10] however, currently Ohio law does not contain a specific requirement that Division-licensed advisers adopt and implement a code of ethics. Nonetheless, such a code is certainly a logical extension of the adviser's fiduciary duty, and is certainly a recommended best practice. Under the SEC rule, a code of ethics must contain: standards of business conduct reflecting the adviser's fiduciary obligations; provisions requiring that the adviser's supervised persons comply with applicable federal securities laws; provisions requiring that the adviser's access persons (persons with access to nonpublic information regarding clients or recommendations) report, and that the adviser review their personal securities transactions and holdings periodically; provisions requiring that supervised persons report any violations of the adviser's code of ethics; provisions requiring that the adviser provide a copy of the code of ethics to each of the adviser's supervised persons; and provisions requiring pre-approval of access person investment in initial public offerings and private placements. The SEC rule provides a template for Ohio advisers, although like the compliance program, a code of ethics must be tailored to the business, structure, clientele and nature of the advisory firm. An adviser's code of ethics should set the tone for the conduct and professionalism of the adviser's employees, officers and directors.[11]

Form ADV. The program should provide for the regular review and update of the adviser's Form ADV. Relatedly, the program should list who is "entitled" to use the IARD system and thus make the necessary changes to the Form ADV and carry out other electronic filing obligations. In addition, the program should designate the person responsible for overseeing the annual renewal of the adviser's Form ADV, and for ensuring that the adviser's IARD financial account is properly funded in advance of the Form ADV renewal and other electronic filings.

Grievances. An adviser must maintain a copy of all written complaints received,[12] and verbal complaints should be memorialized. More importantly, the program should provide for the prompt, thorough and fair review of all complaints received. The program should outline a procedure for response to the complaint and documentation of such response.

Hyperlinks. The program should provide for the periodic review and update of the adviser's website. In addition, the program should establish a policy for e-mail, instant messaging and other electronic communications. Such electronic correspondence typically will constitute written communications subject to the Division's

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recordkeeping requirements.[13] The program also should address whether or not personal use of e-mail and other forms of electronic communication is permitted.

Insider Trading and Transactions. The program must include comprehensive policies and procedures regarding insider and personal trading. Trading on the basis of material nonpublic information must be prohibited. Division rules specifically require an adviser to establish, maintain and enforce written policies and procedures reasonably designed (taking into consideration the nature of the adviser's business) to prevent the misuse in violation of the Ohio Securities Act, the Securities Exchange Act of 1934, and the rules thereunder, of material, non-public information by the adviser or any person associated with the adviser.[14] With respect to permitted personal trading, employees must be required to identify all investment accounts in which they have a beneficial interest, report personal transactions and provide other information necessary for the adviser to comply with the Division's recordkeeping requirement on this point.[15] In addition, Ohio law prohibits "principal transactions," transactions in which an adviser acting for its own account sells securities to or purchases securities from an advisory client, without disclosure to and informed consent by the advisory client for each principal transaction.[16] Consequently, the program must establish a procedure for the necessary disclosure and consent.

Jewels. The program should provide policies and procedures governing the maintenance of any non-securities assets, such as jewels, coins, precious metals or real estate. The program should address custody of and access to such assets. In addition, the policy should address whether or not the adviser will provide any type of supervision, recommendations, or reports regarding such assets.

Know Your Customer. It is advisable for an adviser to establish a customer identification program that allows the adviser to collect information about, and verify the identities of, its clients.[17] This identification procedure may be part of a larger anti-money laundering program pursuant to which an adviser has in place procedures to detect transactions that are designed to conceal or disguise the true origin of criminally derived proceeds. Relatedly, the program should address the requirement that the adviser file a Currency Transaction Report when the adviser receives more than $10,000 in cash in a single or two or more related transactions, and the adviser's ability to file a Suspicious Activity Report for suspicious transactions involving $5,000 or more. Separately, Division-licensed advisers are subject to consumer privacy regulations promulgated by the Federal Trade Commission. In general, these standards require an adviser to develop and maintain a policy regarding the handling of non-public personal information, and provide appropriate notice of that policy. The notice generally must describe the kinds of information that the adviser collects, the categories of unaffiliated third parties with whom the information may be shared, and the adviser's policies and procedures to protect the confidentiality and security of non-public information. Further, an adviser generally is prohibited from sharing an individual's non-public personal information with non-affiliated third parties, unless the adviser has given the individual the opportunity to "opt out" of the sharing and the individual has declined to opt out. As a result, the program should not only establish the adviser's standards for sharing non-public personal information, it also should establish a mechanism to provide notice and give an opt out opportunity to clients.[18]

Legal Representation. The program should address whether or not the adviser will vote client proxies. If so, the program should detail the adviser's proxy voting processes and procedures. SEC-registered advisers that vote client proxies are required to adopt a proxy voting policy.[19] Although this SEC rule is not applicable to Division-licensed

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advisers, a Division-licensed adviser that does vote client proxies should have a policy in place because such voting is subject to statutory anti-fraud standards and the adviser's fiduciary obligations. A proxy voting policy should: (i) address conflicts of interests that may arise; (ii) be reasonably designed to ensure that the adviser votes client's securities in the best interest of the client; and (iii) disclose to clients how they may obtain information from the adviser about how the adviser voted. In addition to dealing with proxy voting, the compliance program should address whether or not the adviser will serve as a legal representative for the client in class actions, bankruptcy proceedings, or other legal proceedings involving securities held in the client's portfolio.

Matching. Under certain circumstances, an adviser may match clients in an "agency cross transaction" pursuant to which the adviser acts as a broker both for an advisory client and for another person on the other side of the transaction. Ohio law prohibits agency cross transactions without disclosure to and informed consent by the advisory client.[20] Consequently, the program must provide for agency cross transactions only in compliance with the disclosure and consent requirements specified in the Division's rules.[21] Similarly, an adviser may effect a transaction between advisory clients, known as a "cross trade," and the program must contain policies and procedures for these transactions. If an adviser receives more than an advisory fee for a cross trade, the transaction is considered an agency cross transaction that is subject to the foregoing disclosure and consent requirement.[22] If the cross trade is not considered an agency cross transaction, the adviser still has an affirmative duty of good faith and full disclosure.

New Issues. To the extent an adviser has access to new issues of securities, including initial public offerings, the program should address how shares in such offerings will be allocated among advisory clients. Of course, the program should contain a mechanism to ensure that such offerings are suitable for the accounts to which they are allocated. More generally, the program should contain policies and procedures to ensure the fair and equitable allocation of securities and recommendations among clients.

Objectives. An investment adviser has a duty to ensure that investment advice is suitable for the client to whom it is given. Accordingly, the program must require the adviser to gather and maintain appropriate information, including investment objectives and financial resources, to enable the adviser to make a suitability determination. Policies and procedures must be put in place to ensure that all securities recommendations and transactions are consistent with the client investment objectives and any client-imposed limitations or restrictions on investments. In addition, it is advisable for advisers to maintain records regarding investment decisions or recommendations, such as information about particular companies or industries, financial and economic data, and other research and periodic reports.

Portfolio Management. First, the program must put in place procedures to distinguish those portfolios that are managed on a discretionary basis from those that are managed on a non-discretionary basis. For non-discretionary accounts, procedures must be put in place to obtain client approval of proposed transactions. For all accounts, as just discussed, the program must ensure that an adviser's portfolio management strategies and execution are consistent with client investment objectives, and that management does not "drift" away from the objectives or inappropriately "chase returns." As previously mentioned, an adviser must be aware of any client-imposed investment restrictions. The program also must be designed to avoid prohibited practices like unauthorized trading, excessive trading, "scalping" (selling recently acquired securities in a market inflated by the adviser's recommendation), "cherry picking" (intentionally allocating profitable trades to per-

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sonal accounts and unprofitable trades to managed accounts) and "marking the close" (intentionally paying higher prices to buy securities at the end of a period in order to increase the value of assets under management).[23] Further, the program should contain procedures to identify and resolve trading errors in a manner that is consistent with the adviser's fiduciary duty.

Quality Control. As previously mentioned, the program must designate a CCO who is responsible for overall administration of the program. Advisers of all sizes must have a CCO – a single person operation must designate himself or herself as the CCO. The CCO may have other specific responsibilities as outlined in the program. The CCO must be competent and knowledgeable, empowered with full responsibility and authority to develop and enforce appropriate policies and procedures, and have sufficient authority within the organization to compel others to adhere to the compliance program.[24] In addition to establishing a compliance program, the Division's rules require an adviser to reasonably supervise its investment adviser representatives and other persons employed by or associated with the adviser with a view towards preventing violations of the federal securities laws.[25] For purposes of the rule, no adviser shall be deemed to have failed to satisfy its duty of reasonable supervision if the adviser has: (i) established procedures, and a system for applying the procedures, that would reasonably be expected to prevent and detect, insofar as practicable, any violation by its investment adviser representatives or other persons, employed by or associated with, the adviser; and (ii) reasonably discharged the duties and obligations incumbent on the adviser by reason of the established procedures and the system for applying the procedures without reasonable cause to believe that there was not compliance with the procedures and systems. Thus, the program must contain policies and procedures consistent with this requirement.

Reporting. The program should address regulatory and client reporting. Regulatory reporting for the firm includes the annual filing – and updating – of the Form ADV, and reporting under Section 13 of the Securities Exchange Act of 1934 if necessitated by the adviser's business. Regulatory reporting for individuals consists of the initial filing – and annual renewal – of Forms U-4 for all investment adviser representatives. Note that a single person who operates his or her advisory business in a business form (*i.e.* corporation or LLC) must be licensed as an investment adviser representative of that business, and comply with the Form U-4 filing requirements.[26] For client reporting, the program should specify the type, scope and frequency of such reports.

Soft Dollars. Soft dollar arrangements must be disclosed to clients; in addition to emphasizing this requirement, the program should set out the firm's philosophy regarding soft dollar arrangements. If the adviser engages in soft dollar relationships, the program must establish policies and procedures to ensure that such soft dollars are in compliance with the safe harbor of Section 28(e) of the Securities Exchange Act of 1934. The program should provide for the regular review of soft dollar practices, and a mechanism to make sure that soft dollar practices are consistent with disclosures made to clients.

Trading Practices. An adviser has a fiduciary obligation to obtain "best execution" of client transactions, and the program must reflect this obligation. In general, best execution means that an investment adviser must execute client securities transactions in such a manner that the client's total cost or proceeds in each transaction is most favorable under the circumstances. Soft dollar arrangements have the potential to interfere with best execution. In 1986, the SEC provided guidance – which remains sound guidance today – that in seeking best execution, an adviser should consider the full range and quality of a broker-dealer's services including, among other things,

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execution capability, the value of research provided, commission rates, financial responsibility, and responsiveness to the adviser.[27] The program should contain a best execution policy that addresses, at a minimum: the person(s) responsible for monitoring the adviser's trading practices; the criteria used to select broker-dealers; periodic and systematic review of trading practices; whether the adviser will aggregate orders; appropriate recordkeeping; and assurance of full and accurate disclosure of trading practices and soft dollar arrangements. Finally, the program should address whether or not the adviser will permit clients to direct transactions to specific broker-dealers, *i.e.* directed brokerage. Clients engaged in directed brokerage should be advised that because of their direction they may not necessarily enjoy best execution of their transactions.

Understandings. The most important understanding that an adviser has is the advisory agreement with its clients. This agreement must be in writing,[28] and at a minimum should cover: the scope of services rendered and the fees for such services; whether or not the adviser will have discretion with respect to buy and sell decisions and trade execution decisions; and custodial arrangements. The program should recognize that Ohio law prohibits assignment of an advisory contract without client consent.[29] Another important understanding is any arrangement for the referral or solicitation of clients. An adviser may pay a cash fee to a person who solicits business on behalf of the adviser only under certain circumstances, and the program must ensure that solicitation arrangements are in compliance with the Division's rule on this point.[30]

Valuation. The program should address how client portfolios will be valued both for purposes of measuring performance and calculating advisory fees. Valuation methodologies and fee calculations should be transparent and fully disclosed to clients.[31] The Division has taken the position that advisers must disclose to clients all material information regarding compensation, including a disclosure of all fees, a description of fee calculation, and whether fees are negotiable.[32] Further, additional fees imposed by mutual funds must be disclosed, and it is advisable for an adviser to ensure that clients understand that charges for transaction execution and custodial services are in addition to the advisory fee.

Wrap Fee Programs. The program should address whether or not the adviser will serve as a sponsor of wrap fee programs. If so, procedures must be put in place to ensure delivery of the required wrap fee disclosure statement (Schedule H of Form ADV).[33] In addition, the program should contain procedures to ensure that wrap fee programs are suitable for the clients to whom they are recommended.

Xtra Copies. The program should include policies and procedures to recover from natural and man-made disasters and emergencies. These policies should include, at a minimum: identification of mission critical personnel and systems; regular back-up of electronic and hard copy data; arrangements for a back-up location to conduct operations along with arrangements for back-up computer and telephone systems; and training for and periodic testing of the recovery plan.

Yearly Review. Division rules require that the compliance program be reviewed at least annually, and that a record of such review be maintained with the adviser's books and records.[34]

Zero. Zero is the number of issues relevant to an adviser's business that should *not* be addressed in the adviser's compliance program. As mentioned at the outset, the compliance program requirement provides an adviser with an opportunity to establish a comprehensive set of standards governing its operations and regulatory requirements. And rather than simply purchase a "one-size-fits-all" program, advisers should thoughtfully craft a program that addresses the issues relevant to its business. Although the program should address all compliance considerations relevant to the

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adviser's operations, the program need not specify every single action that must be taken in order to remain in compliance. In some cases, it may be sufficient for the program to allocate responsibility within the organization for the timely performance of certain obligations. Most importantly, the compliance program requirement is intended to foster a "culture of compliance;" a culture in which the highest standards of ethical behavior are practiced, and there are adequate internal controls that make it more likely that ethical behavior will be the norm throughout the organization.

Mr. Geyer is an attorney with the Bailey Cavalieri law firm in Columbus. He was Commissioner of Securities from 1996 to 2000.

(Endnotes)

[1] A supervised person is a natural person who is any of the following: (i) a partner, officer, or director of an adviser (or other person occupying a similar status or performing similar functions); (ii) an employee of an adviser; or (iii) a person who provides investment advisory services on behalf of the adviser and is subject to the supervision and control of the adviser. R.C. § 1707.01(DD).

[2] O.A.C. §1301:6-3-44(H).

[3] While this article addresses the most common issues, it is incumbent upon an adviser to consider whether there are additional issues relevant to its operations that must be addressed in its compliance program.

[4] O.A.C. §1301:6-3-44(A)(1)(e). In addition, certain other types of advertising are specifically prohibited, *see* O.A.C. §1301:6-3-44(A)(1)(a)-(d).

[5] O.A.C. §1301:6-3-44(A)(2).

[6] O.A.C. §1301:6-3-15.1(E).

[7] *See Division Guidance on Commonly Encountered Investment Adviser Issues*, Ohio Securities Bulletin 2002:2 (2002) for guidance regarding updating "primary" and "secondary" transactional records.

[8] O.A.C. §1301:6-3-44(B).

[9] O.A.C. §1301:6-3-151(G).

[10] *See* 17 C.F.R. §275.204A-1.

[11] "E" also could stand for ERISA. Advisers that serve as fiduciaries or investment managers with respect to ERISA plans are subject to additional conduct standards, a discussion of which is beyond the scope of this article. Such advisers should consult with legal counsel who is knowledgeable regarding ERISA in order to ensure compliance.

[12] O.A.C. §1301:6-3-151(E)(1)(g).

[13] O.A.C. §1301:6-3-151(E)(1)(g).

[14] O.A.C. §1301:6-3-151(F).

[15] O.A.C. §1301:6-3-151(E)(1)(l), (m).

[16] R.C. §1707.44(M)(1)(c). *See also* Ohio Investment Adviser Manual §12.33 (LexisNexis 2002 & 2005 Supp.).

[17] Broker-dealers and mutual funds are subject to federal customer identification requirements, *see* 31 C.F.R. §§103.122 and 103.131, and such requirements may be "pushed down" to advisers.

[18] For a detailed discussion of the consumer privacy rule and requirements, *see* Ohio Investment Adviser Manual, Ch. 13 (LexisNexis 2002 & 2005 Supp.).

[19] *See* 17 C.F.R. §275.206(4)-6.

[20] R.C. §1707.44(M)(1)(c).

[21] O.A.C. §1301:6-3-44(G).

[22] *See* Ohio Investment Adviser Manual §12.35 (2002 & 2005 Supp.).

[23] For a more thorough discussion of fraudulent portfolio management practices, *see* Ohio Investment Adviser Manual §12.36 (LexisNexis 2002 & 2005 Supp.).

[24] Although the CCO should have these characteristics, there is no requirement that an adviser hire a person to serve as CCO, or that a person must devote his or her full time to CCO responsibilities.

[25] O.A.C. §1301:6-3-151(D).

[26] *See* Ohio Investment Adviser Manual §§8.12, 8.13 (LexisNexis 2002 & 2005 Supp.).

[27] SEC Release No. 34-23170 (Apr. 23, 1986). The SEC supplemented this guidance in Release No. 34-43590 (Nov. 17, 2000).

[28] O.A.C. §1301:6-3-151(H)(2).

[29] O.A.C. §1301:6-3-151(H)(1)(b).

[30] O.A.C. §1301:6-3-44(C).

[31] Fees based on a percentage of capital gains or appreciation in a client's account are prohibited, except with respect to "qualified clients." O.A.C. §1301:6-3-151(H)(1)(a).

[32] *See* Ohio Investment Adviser Manual §12.30 (LexisNexis 2002 & 2005 Supp.).

[33] O.A.C. §1301:6-3-151(G)(6).

[34] O.A.C. §§1301:6-3-44(H)(1)(b); 1301:6-3-151(E)(1)(t).

Criminal Updates

Steven R. Lee of Perkins Township in Erie County, Ohio was sentenced on March 31, 2005 to four years in prison in Erie County Common Pleas Court. Lee pled guilty on February 16, 2005 to five felony counts relating to his mishandling and theft of investor funds, as well as theft of condominium association funds. An Erie County grand jury indicted Lee on 15 counts on November 14, 2003; 10 of the counts were dropped as part of a plea bargain. Lee pled guilty to the following counts: mishandling of funds as an investment adviser (third-degree felony); attempted mishandling of funds as an investment adviser (third-degree felony); attempted engaging in fraud as an investment adviser (third-degree felony); theft (third-degree felony); theft (fourth-degree felony).

The judge sentenced Lee to four years in prison for each of the third-degree felonies and 16 months for the fourth-degree felony. The sentences are to run concurrently, with Lee's sentence beginning immediately.

Lee, who had been an investment adviser since 1990 and was licensed with the State of Ohio as an investment adviser under the name of Lee Investment Services from January 1, 2000 to December 31, 2002, mishandled $90,642 in investor funds. Instead of placing the investment funds in the clients' brokerage accounts, Lee maintained the funds in a personal account in violation of the Division of Securities' investment advisory rules regarding custody of client funds. In addition, after Lee convinced his elderly neighbor to invest $6,000 through him, Lee never purchased the security for the investor.

Lee also stole $86,675.24 from the Timber Lakes Condominium Association in Perkins Township, where he once served as President and Treasurer. This portion of the case was investigated by the Perkins Township Police Department.

On March 17, 2005, **Keith W. Dominick** of Lorain, Ohio entered a guilty plea to securities fraud in U.S. District Court for the Northern District of Ohio in Cleveland. Dominick was charged with one count of securities fraud in an Information filed in U.S. District Court for the Northern District of Ohio in Cleveland on January 31, 2005. Dominick sold $1.6 million in promissory notes through his company, KNR Marketing, Inc., to 17 investors who were fellow members of the Church on the North Coast in Lorain. Dominick is not licensed to sell securities in any state and fraudulently represented that the promissory notes were risk-free and would generate extraordinary rates of return. Rather than actually investing all of the client money, Dominick used it to pay fees of other investors, pay off investors to dissuade them from contacting law enforcement, and for his business and personal expenses.

Dominick had been permanently banned from the commodities industry after the Commodities Futures Trading Commission obtained a permanent injunction against him in 1994 for operating a ponzi scheme. He also was found guilty of embezzlement and larceny in a federal criminal case in Florida in 1996 and was sentenced to 37 months in prison and was ordered to pay $4.5 million in restitution, which he hasn't done. The FBI and the Ohio Division of Securities investigated this case. Sentencing is scheduled for June 22, 2005.

On February 16, 2005, **Edmund Burke Pearson** of Montgomery County was indicted on 11 counts of securities fraud (relating to alleged violations of 1707.44(G) of the Ohio Revised Code) in Montgomery County Common Pleas Court in regards to his selling stock in Financial Solutions International Corp. Subsequently, on March 21, 2005, Mr. Pearson was indicted on 13 additional counts relating to his selling stock in Financial Solutions International Corp. (See Enforcement Section Reports, p. 10.)

Enforcement Section Reports

Edmund Burke Pearson

On March 4, 2005, the Division issued Order No. 05-041, a Cease and Desist Order, against Edmund Burke Pearson. Pearson sold preferred stock to Ohio residents on behalf of Financial Solutions International Corp. aka Brundyn Financial Group Corp. The stock involved a high degree of risk but this material fact was not disclosed to investors. Pearson also recommended the sale of this stock to one investor without reasonable grounds to believe the recommendation was suitable for the investor. Therefore, on December 13, 2004, the Division issued Order No. 04-221, a Notice of Opportunity for Hearing, against Pearson for allegedly violating Revised Code Section 1707.44(G) and Ohio Administrative Code Section 1301:6-3-19(A)(5), for failing to disclose material facts and for recommending unsuitable investments. Pearson 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. 05-041, which incorporated the allegations set forth in the Notice of Opportunity for Hearing.

Civil Actions

Joanne C. Schneider and Alan C. Schneider

In February 2005, and as a result of a hearing on the Division's motion, Cuyahoga County Common Pleas Court Judge Villanueva froze all of the assets held individually in the name of Joanne C. Schneider along with the assets she held jointly with her husband, Alan Schneider. The Court also appointed a receiver. These actions were taken so as to protect Ohio investors from harm after evidence disclosed that Joanne Schneider continued to offer promissory notes in violation of a preliminary injunction issued in December 2004 by Judge Villanueva.

Ohio Securities Conference 2005

October 21, 2005

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Securities Litigation
Venture Capital
The SEC's New Offering Rules
Ohio Division of Securities Panel

Presented by
The Ohio Division of Securities
and
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.

Additional information will be included in the next edition of the Ohio Securities Bulletin
and will be available on the Division's website at www.securities.state.oh.us

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. Consequently, for purposes of calculating an aggregate capital formation amount, each indefinite filing has been assigned a value of $1,000,000.*

Filing Type	1st Qtr 2005	YTD 2005
Exemptions		
Form 3(Q)	$32,904,380	$32,904,380
Form 3(W)	4,020,000	4,020,000
Form 3(X)	83,928,374,722	83,928,374,722
Form 3(Y)	893,000	893,000
Registrations		
Form .06	1,270,195,825	1,270,195,825
Form .09/.091	10,392,832,368	10,392,832,368
Investment Companies		
Definite	124,634,500	124,634,500
Indefinite**	587,000,000	587,000,000
TOTAL	**$96,340,854,795**	**$96,340,854,795**

Registration Statistics

The following table sets forth the number of registration, exemption, and notice filings received by the Division during the first quarter of 2005, compared to the number of filings received during the first quarter of 2004. Likewise, the table compares the year-to-date filings for 2005 and 2004.

Filing Type	1st Qtr '05	YTD '05	1st Qtr '04	YTD '04
1707.03(Q)	30	30	26	26
1707.03(W)	5	5	5	5
1707.03(X)	388	388	356	356
1707.03(Y)	5	5	2	2
1707.04/.041	0	0	0	0
1707.06	17	17	27	27
1707.09/.091	30	30	46	46
Form NF	1280	1280	1171	1171
Total	1755	1755	1633	1633

Licensing Statistics

License Type	YTD 2005
Dealers	2,355
Salespersons	126,017
Investment Adviser/Notice Filers	1,784
Investment Adviser Representatives	10,497