

# OHIO SECURITIES BULLETIN

A QUARTERLY PUBLICATION OF THE OHIO DIVISION OF SECURITIES

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## Receiverships: an Important Tool for Securities Regulators

By Matthew Fornshell and Katherine Manghillis

The Ohio Supreme Court has stated that “the appointment of a receiver is the exercise of an extraordinary, drastic and sometimes harsh power which equity possesses ....” *Hoiles v. Watkins*, 117 Ohio St. 165, 174 (1927).

The concept of equity receiverships, having its roots in railroad receivership cases, is not new. However, the use of receiverships by regulators such as the Ohio Division of Securities (the “Division”) and the United States Securities and Exchange Commission (the “SEC”) has increased in recent times.

Regulators seek the appointment of a receiver in order to identify, preserve and marshal assets in extreme cases involving securities fraud. By obtaining the appointment of a receiver, the Division shuts down the scam by removing the defendants from control of the entity or enterprise. However, given the extraordinary nature of the relief being sought, the use of receiverships by securities regulators should be reserved for the most egregious incidences of fraud where assets are known to exist.<sup>1</sup>

### Statutory Authority

The Receiver is appointed as an independent officer of the court to take charge of the assets of the estate for the benefit of the creditors of the estate generally.<sup>2</sup> The appointment of a receiver in Ohio is statutory and one can be appointed only in cases where the statutes authorize it.<sup>3</sup>

The Ohio Revised Code has two sections that codify equity receiverships in Ohio and describes some of the receiver’s many powers and duties under Ohio law. Ohio Revised Code § 1707.27 is the Division’s statutory authority for motioning for the appointment of a receiver.<sup>4</sup> Ohio Revised Code §2735.04 is the general receivership statute in Ohio.<sup>5</sup>

To prevail in a motion for the appointment of a receiver, the Division must be able to demonstrate to the court that the defendant engaged in conduct resulting in a “substantial violation of sections 1707.01 to 1707.45 of the Revised Code, or of the use of any practice or transaction declared to be illegal or prohibited, or defined as fraudulent by those sections or rules adopted under those sections by the division of

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## Receiverships

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securities, to the material prejudice of a purchaser or holder of securities....”<sup>6</sup> Before a court will grant such a motion it will often conduct an evidentiary hearing where the Division will present evidence in support of its motion. At any such hearing the defendant(s) will have the opportunity to confront the Division’s witnesses and present their own evidence in opposition to the Division’s motion. Ohio Revised Code §1707.27 requires that the Court of Common Pleas make two findings before appointing a receiver: (1) the sufficiency of the application for a receivership; and (2) the sufficiency of the proof of substantial violation of the Ohio security law.<sup>7</sup> The trial court’s appointment of a receiver will not be disturbed absent an abuse of discretion.<sup>8</sup>

### The Court’s Discretion

Assuming the court has granted the Division’s motion for the appointment of a receiver, the trial court administers the estate through the receiver as its officer for the benefit of creditors generally. The Ohio Supreme Court has long recognized the broad authority which may be granted to a receiver. For example, in *State ex rel. Celebrezze v. Gibbs*, 60 Ohio St.3d 69, 572 N.E.2d 62 (1991), the Ohio Supreme Court interpreted Revised Code §2735.04 as “enabling the trial court to exercise its sound judicial discretion to limit or expand a receiver’s powers as it deems appropriate.”

Ohio Revised Code Chapter 2735 “does not contain any restrictions on what the court may authorize when it issues orders regarding receivership property.” *Quill v. Troutman Enterprises, Inc.*, Montgomery App.No.20536, 2005 Ohio2020, \*\*16-17. Likewise, Ohio Revised Code §1707.27 contains no restriction on what the court may authorize regarding receivership property. Moreover, the court appointing the receiver retains exclusive jurisdiction over the receivership and the receiver for all purposes relating to the receivership proceeding.

The court appointing the receiver protects the receiver’s custody of receivership assets against all interferences. For instance, the court requires all claimants to assets of the receivership estate to submit their claims to the receivership court.<sup>9</sup> The court may use

summary procedures to allow, disallow or subordinate claims of creditors.<sup>10</sup> The court may also authorize the sale of receivership assets free and clear of all liens, claims and encumbrances, transferring those liens, claims and encumbrances to the proceeds from the respective sales of the receivership assets.<sup>11</sup> Creditors that submit their claims to a receiver are not entitled as a matter of right to a jury trial of the issue of fact involved. Thus, while due process may not be compromised, the court need not impanel a jury to assist in the determination of facts.<sup>12</sup>

### Actions by the Receiver

The receiver’s goal in administering the receivership estate is, to the greatest extent possible, to maximize the value of the estate. Almost immediately, the receiver must assess the viability of the enterprise, understand its operations and make determinations

## OHIO SECURITIES BULLETIN

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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.

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Ohio Division of Securities

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regarding necessary personnel and whether or not to wind down the business and liquidate the assets. At the outset of any receivership it is also critical for the receiver to determine what additional professionals must be retained to administer the estate and maximize estate value. These professionals will routinely include accountants, lawyers and other individuals who may have an expertise unique to the circumstances of the receivership. Upon appointment, the defendant(s) is removed from control of the enterprise and replaced by the receiver. The receiver, pursuant to Revised Code §1707.27, must secure the books and records, including electronic records, identify and secure the assets and learn the nature of the defendant's business. The receiver reports periodically to the court regarding, among other things, the nature of the enterprise, its organizational structure and financial health, and the number and character of existing creditors. Many appointing courts require the receiver to file an initial report and an inventory detailing the assets of the defendants.<sup>13</sup>

One of the receiver's many duties is to identify and secure all of the assets of the estate, which may include personal assets as well as business assets. As defendants become more creative in finding ways to hide assets, this task consumes substantial amounts of time and resources.<sup>14</sup> An asset of the receivership estate is anything that 1) was acquired "in part or in whole, through means of a[n] act, practice, or transaction" and/or 2) was purchased with property or monies

otherwise commingled with property acquired in violation of 1707.01 to 1707.45, *et seq.* and Ohio law.

In Ponzi scheme cases, identifying and securing assets is made more difficult when the defendant has legitimate businesses in addition to the Ponzi scheme. Typically, the monies from the legitimate businesses and the Ponzi scheme are commingled and the commingled funds are expended without distinction.<sup>15</sup> The receiver is typically able to resolve most issues regarding the inter-relationship of the affiliated entities by examining business records such as bank account statements, accounting records and other corporate records of the entities. Thus, if in the process of identifying and securing the money/assets of the estate, the receiver uncovers evidence that any asset was purchased, in whole or in part, with monies or commingled monies that were acquired through the defendant's violations of Revised Code 1707.01, *et seq.*, the receiver is empowered to bring that asset into the receivership estate to protect all creditors of the defendant.

Significantly, Revised Code §1707.27 also provides the receiver with the power to "*sue for, collect, receive and take into the receiver's possession ... all [of defendant's] rights, credits, property, and choses in action*" that were acquired in violation of the Ohio Securities Act. The language explicitly empowers the receiver to bring lawsuits against third-parties in order to take possession of all the defendants'

assets. For example, in the Liberte Capital Group, LLC cases, the receiver, on behalf of the business entity, filed lawsuits against certain banks alleging, among other things, that the banks aided and abetted the defendant, that the banks were negligent in supervising the defendant's accounts and that the banks breached their duties of good faith.<sup>16</sup> In his prayer for relief the receiver requested that at a minimum the banks "should be liable to an amount equal to at least the sum total of all deposits" that defendant deposited into the various accounts. Such a recovery would become an asset of the receivership estate for the benefit of creditors.

The receiver must also identify the creditors of the receivership estate. This task is difficult and often requires the receiver to retain professionals to determine who the creditors are, what the creditors are owed and the proper classification for each creditor.<sup>17</sup> In addition, the receiver must assess the validity of those claims before disbursing funds.<sup>18</sup> At odds with the receiver's goal of maximizing the value of the receivership estate for the benefit of creditors are the necessary expenses associated with the receivership proceedings. As discussed above, among other varied tasks, the receiver must account for and liquidate the assets of the receivership estate, manage the defendant's business enterprises and determine the identity and legitimacy of creditors of the receivership estate. Performing these functions necessarily comes with costs which can be significant.

Typically, the order appointing the receiver provides that

the receiver's fees and expenses will be paid from the assets of the receivership estate or assessed as costs in the litigation.<sup>19</sup> The receiver's fees and expenses will reduce the value of the receivership estate for the creditors. Thus, securities regulators must carefully analyze the costs associated with the appointment of a receiver and determine whether or not the appointment of a receiver is in the best interests of the creditors. The ultimate function of a receiver appointed under Revised Code section 1707.27 is to liquidate the assets of the estate and distribute the proceeds to the estate's creditors. This process not only involves identifying creditors and determining the legitimacy of their claims, but also resolving priority issues by and among the creditors. Priority disputes among creditors will typically be resolved in ancillary proceedings without the participation of the receiver.

The receiver will assist the court in making a decision on distributions to creditors by proposing a "plan of distribution." Such a plan generally defines the different parties who have an interest in the liquidation proceeds and makes a recommendation to the court as to how the proceeds are to be disbursed. Following a hearing to consider any objections to the plan of distribution, the court will issue an order detailing for the receiver and all the creditors how the liquidation proceeds shall be disbursed amongst the creditors.<sup>20</sup> Assuming creditors do not appeal such an order, the receiver will disburse the liquidation proceeds to the creditors pursuant to the terms of the plan of distribution, and once

completed, depending on the status of other pending litigation in which the receiver may be a party, the receivership may be prepared to wind down its operations.

## Conclusion

The order appointing a receiver gives that receiver significant power limited only by the broad discretion of the appointing court—it is an extraordinary, drastic and sometimes harsh power.<sup>21</sup> The order often freezes the assets of the defendants, directs the receiver to take possession of the books and records of the entity and directs the receiver, upon court approval, to liquidate the assets of the estate for the benefit of creditors. The appointment of a receiver is a potent weapon, one that is used in extreme cases of securities fraud to shut down the scam and protect the assets for the benefit of the creditors. Although an important weapon in combating securities fraud that rightfully has a place in a securities regulator's quiver, the extraordinary nature of the relief, and associated costs should be reserved for the most extreme cases of securities fraud where actual assets are known to exist.

*(Editor's note: the authors are attorneys at Schottenstein, Zox and Dunn of Columbus, Ohio. Mr. Fornshell is also a former attorney-inspector of the Division.)*

### (Endnotes)

1 In 2005, the Division successfully obtained the appointment of a receiver in two cases: *Ohio Department of Commerce v. Joanne C. Schneider, et al.* Cuyahoga County Court of Common Pleas, Case No. 04-cv-548887 and *Ohio Department of Commerce v. Westhaven Group, LLC, et al.*, Lucas County Court of Common Pleas, Case No. 05-cv-6857. In both cases, the defendants

violated, among other statutes, §1707.44(C)(1) by selling unregistered promissory notes to investors. Many of the promissory notes were unsecured.  
2 See 80 Ohio Jurisprudence Receivers §82.

3 See *Hoiles v. Watkins*, 117 Ohio St. 165 (1927)

4 Ohio Revised Code §1707.27 states as follows:

If a court of common pleas is satisfied with the sufficiency of the application for a receivership, and of the sufficiency of the proof or substantial violation of sections 1707.01 to 1707.45 of the Revised Code, or of the use of any act, practice or transaction declared to be illegal or prohibited, or defined as fraudulent by those sections or rules adopted under those sections by the division of securities, to the material prejudice of a purchaser or holder of securities, or of a client of an investment adviser or investment adviser representative, the court may appoint a receiver, for any person so violating sections 1707.01 to 1707.45 of the Revised Code or rule adopted under those sections by the division, with the power to sue for, collect, receive and take into the receiver's possession all of the books, records, and papers of the persons and all rights, credits, property, and choses in action acquired by the person by means of any such act, practice or transaction, and also all property with which the property has been mingled, if the property cannot be identified in kind because of the commingling, and with the power to sell, convey, and assign the property, and to hold and dispose of the proceeds under the direction of the court of common pleas. The court shall have jurisdiction of all questions arising in the proceedings and may make orders and decrees therein as justice and equity require.

5 Ohio Revised Code §2735.04 states as follows:

Under the control of the court which appointed him, as provided in section 2735.01 of the Revised Code, a receiver may bring and defend actions in his own name as receiver, take and keep possession of property, receive rents,

collect, compound for, and compromise demands, make transfers, and generally do such acts respecting the property as the court authorizes.

6 R.C. 1707.27.

7 *Ohio Department of Commerce v. Condo-Mobile, Inc.*, 1978 Ohio App. LEXIS 10505 (1978).

8 *State ex rel Montgomery v. Gold*, Franklin App. No. 04AP-863, 2006-Ohio-943 at P65 citing *Victory White Metal Co. v. N.P. Motel Sys.*, Mahoning App. No. 04MA-245, 2005-Ohio-2706 at P55-56.

9 *Frye, Receiver v. MacWilson*, 39 Ohio App. 158, 161 (1931).

10 *United States v. Arizona Fuels Corp.* (C.A.9, 1984), 739 F.2d 455, 458, the Ninth Circuit Court of Appeals held that “[s]uch abbreviated procedures (including the use of a single receivership proceeding to resolve all claims) advance the government’s interest in judicial efficiency by reducing the time needed to resolve disputes, decreasing the costs of litigation, and preventing the dissipation of the receiver’s assets.”

11 See *Quill v. Troutman Enterprises, Inc.*, Montgomery App. No. 20536, 2005-Ohio-2020.

12 *Burch Construction Co. v. Atlantic Homes, Inc.*, 119 Ohio App. 464, 466 (1963).

13 See e.g. Cuyahoga County Court of Common Pleas, General Division, Rule 26; Montgomery County Court of Common Pleas, General Division, Rule 2.29.

14 See Dana J. Lesemann & Peter B. Zlotnick, *Receiverships and Other Shark Tales*, Litigation Fall 2005, at 48-52, 70-71 discussing duties of receivers appointed in Federal Trade Commission actions.

15 See *In re Taubman* (Bankr. S.D. Ohio 1993), 160 B.R. 964, 978 discussing the commingling of funds from the Ponzi scheme with funds from other business activity.

16 The Liberte Capital Group, LLC cases are related to a pending viatical insurance fraud action. The receiver’s cases against the banks are captioned as *Wuliger v. Star Bank*, Case No. 02-

cv-01513 (N.D. Ohio Aug. 1, 2002); *Wuliger v. KeyBank*, Case No. 02-cv-02160 (N.D. Ohio Nov. 1, 2002); and *Wuliger v. Liberty Bank*, Case No. 02-cv-01378 (N.D. Ohio July 17, 2002) the complaints in these cases have survived motions to dismiss and are still pending.

17 See *Keith v. Black Rose, Inc.*, 1984 Ohio App. LEXIS 12150 (1984), stating that in receivership actions, general creditors should share the common fund on a pro rata basis.

18 See *Tomb v. Mathews*, 1992 Ohio App. LEXIS 3958 (1992), \*2 “In addition, the receiver was given the authority to hear, decide and determine any amounts Winding Books, Inc. owed to admitted creditors or alleged creditors.”

19 See Dana J. Lesemann & Peter B. Zlotnick, *Receiverships and Other Shark Tales*, Litigation Fall 2005, at 50.

20 Any such order issued by the court may be the subject of appeals by creditors who disagree with the court’s plan. Short of a court-approved settlement among the creditors and the receiver, until such appeals are resolved it will likely impair the receiver’s ability, to make distributions to the creditors.

21 See *Hoiles*, 117 Ohio St. 165, 174.

## Licensing Statistics

License Type	YTD 2006
Dealers	2,376
Salespersons	131,130
Investment Adviser/Notice Filers	1,911
Investment Adviser Representatives	12,558

# Ohio Securities Conference 2006

**October 13, 2006**

**Executive Conference and Training Center  
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Federal and Ohio Litigation Update  
Ethical Considerations in Securities Transactions  
Corporate Governance Developments  
Ohio Division of Securities Panel

Presented by  
**The 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.

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](http://www.securities.state.oh.us)

## Criminal Updates

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On March 7, 2006, a Bill of Information was filed in U.S. District Court for the Northern District of Ohio, charging **Richard A. Daniels** of Chagrin Falls, Ohio with one count of securities fraud. According to the filing, Daniels conducted his securities fraud scheme from approximately 1997 through approximately December 2005, resulting in losses to investors of approximately \$2,254,138. During this same period, Daniels was employed by Lincoln Financial Advisors Corp. and held Ohio securities salesperson and investment adviser representative licenses. The Bill of Information alleges that Daniels gained access to client funds by selling them promissory notes in an Ohio corporation that he formed, First Capi-

tal Group. The notes promised fixed returns from between four percent to seven percent. The Bill of Information states that Daniels used the funds of his clients to make payments to earlier investors, and to support his own personal debts and expenses.

Moreover, the Bill of Information states that Daniels did such things as the following in furtherance of his scheme: transferred funds from his existing clients at Lincoln to accounts that he controlled by forging client signatures on withdrawal requests and wire transfer authorizations and provided some investors fictitious account statements, falsely showing positive growth in their accounts. Also, he did not pro-

vide account statements or investment documentation to some investors. Instead, he merely provided them verbal representations that their investments were achieving positive returns. The Division investigated this matter and referred it to the U.S. Attorney's Office. In their release, the U.S. Attorney for the Northern District of Ohio credited the Division as the investigative agency on this case. (*See also, Enforcement Section Reports.*)

## Enforcement Section Reports

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### Richard A. Daniels

On March 22, 2006, the Division issued Division Order 06-081 against Richard A. Daniels of Chagrin Falls, Ohio, revoking his Ohio securities salesperson and investment adviser representative licenses.

The Division found that Daniels violated Ohio Revised Code Section 1707.44(G), and Ohio Administrative Code Rules 1301:6-3-19(A)(19), 1301:6-3-16(C), and 1301:6-3-16.1(C), and he was found not to be of "good business repute" pursuant to Ohio Administrative Code Rules 1301:6-3-19(D)(8) and (D)(9) and Ohio Revised Code Section 1707.19(A)(1). The Division found that Daniels violated Ohio

Revised Code Section 1707.44(G) by fraudulently selling promissory notes in First Capital Group, an Ohio corporation organized by Daniels, and in other entities created by him. Daniels was found to have misappropriated approximately \$2.1 million from nine of his clients from 1998 through 2005. He was employed by Lincoln Financial Advisors Corp. during that same time as a financial advisor. Daniels gained access to his clients' funds by selling them promissory notes or by embezzling funds from their accounts at Lincoln and other entities. Daniels forged his clients' signatures to wire transfer requests and withdrawal authorizations and had the money deposited in accounts that he controlled. The Division found that Daniels used the money from promissory note investors and

the money that he embezzled to make payments to earlier investors and to support his own personal expenses and debts.

In furtherance of his scheme, Daniels was found to have set up Individual Retirement Accounts ("IRA") for some of his clients at Equity Trust Company, a self-directed IRA custodian, located in Elyria, Ohio. In some cases, Daniels' clients were not even aware that they had an IRA at Equity Trust Company, as Daniels forged their signatures to account applications and account-related forms and listed his address as the address of record. Moreover, Daniels would have the funds, which he misappropriated from his clients, sent to Equity Trust Company. He would then direct Equity Trust Company to pur-

## Enforcement Section Reports

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chase a promissory note for the clients' IRA from him, and to wire the money to an account that he controlled.

The Division found that Daniels failed to update his Form U-4, as required by Ohio Administrative Code Rules 1301:6-3-16(C) and 1301:6-3-16.1(C), to disclose a \$410,016.41 federal tax lien filed against him on February 23, 2005. In addition, Daniels was found to have violated Ohio Administrative Code Rule 1301:6-3-19(A)(19) for "selling away" related to the sale of the promissory notes of First Capital Group.

One occurrence that bore on whether or not Daniels was of "good business repute" was Daniels being permanently enjoined from violating the registration and anti-fraud provisions of the Federal securities laws in the offer and sale of securities in an action brought by the U.S. Securities and Exchange Commission in 1978. In addition, for the same set of facts that led to the SEC civil action, Daniels plead guilty to two counts of mail fraud in U.S. District Court for the Northern District of Ohio and was sentenced on March 31, 1983 to five years of probation and fined \$5,000.

On February 16, 2006, the Division issued Division Order 06-047, a Suspension of Ohio Securities Salesperson License, Suspension of Ohio Investment Adviser Representative License, Notice of Intent to Revoke Ohio Securities Salesperson License, Notice of Intent to Revoke Ohio Investment Adviser Representative License, and Notice of Opportunity for Hearing to Daniels.

Daniels failed to timely request an administrative hearing pursuant to Chapter 119 of the Ohio Revised Code, and Division Order No. 06-081 was issued on March 22, 2006. (See *Criminal Updates*.)

### James E. Upshaw

On February 16, 2006, the Division issued Division Order 06-046, a Cease and Desist Order, to James E. Upshaw of Bellwood, Illinois and Upshaw and Associates, LLC, a business controlled by Upshaw.

The Division found that Upshaw and Upshaw and Associates violated the provisions of Ohio Revised Code sections 1707.44(C)(1), 1707.44(B)(4), and 1707.44(G). From January 2003 through April 2004, Upshaw sold promissory notes of Upshaw and Associates to at least seventeen Ohio investors totaling \$685,000. Investors were promised guaranteed returns of up to ten percent per month and that Upshaw would use their money to invest in large-cap U.S. stocks, Treasury bills, commercial paper, and silver and gold. The investors were not given any disclosure documents regarding their investments, Upshaw, or Upshaw and Associates. In addition, investors were not informed of Upshaw's criminal record of two Illinois criminal convictions for theft or his bankruptcy filings. Upshaw defaulted on the investors' promissory notes as he used little of investor funds in the manner he promised. Instead, he used investor funds to pay returns to earlier investors and converted the remainder to his own use. Upshaw, an African-

American, targeted members of the African-American community and the churches where they worshipped. Moreover, he held himself out as a church minister and made references to religion to gain the trust of others to invest with him.

The Division notified Upshaw and Upshaw and Associates of their right to an adjudicative hearing pursuant to Chapter 119 of the Revised Code with the issuance of a Notice of Opportunity for Hearing on January 5, 2006. A hearing was not requested by either Upshaw or Upshaw and Associates and the Cease and Desist Order described above was issued to them.

On December 1, 2005, Upshaw was convicted of theft and securities fraud in the Circuit Court of Cook County, Illinois related to the sale of Upshaw and Associates' promissory notes and was sentenced to seven and a half years in prison and ordered to pay \$3,249,842 restitution to victims from several states. The Illinois Secretary of State credited the Division with contributing to the investigation that led to Upshaw's conviction.

### Gilbert L. Warner ; Entity Investing, Inc.

On January 5, 2006, the Division issued Order No. 06-001, a Cease and Desist Order, against Gilbert L. Warner and Entity Investing Inc. of Brunswick, Ohio. Throughout 2003, Gilbert L. Warner, through his company, Entity Investing, Inc., an Ohio corporation, sold to at least

five Ohio residents member interests in limited liability companies. These member interests in limited liability companies are securities under the Ohio Securities Act but were not registered with the Division. Therefore, on November 30, 2005, the Division issued Order No. 05-206, a Notice of Opportunity for Hearing, against Gilbert L. Warner and Entity Investing Inc. for allegedly violating Revised Code Section 1707.44(C)(1), which prohibits the unregistered sale of securities. Gilbert L. Warner and Entity Investing 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. 06-001 which incorporated the allegations set forth in the Notice of Opportunity for Hearing.

**James T. Garrett; Carolinas First Investments, Inc.**

On February 1, 2006, the Division issued Order No. 06-018, a Cease and Desist Order, against James T. Garrett and Carolinas First Investments, Inc. of North Carolina. In 2002 and 2003 Garrett, then a licensed salesperson and president of Carolinas First Investments, Inc., a licensed dealer, sold promissory notes on behalf of The Thaxton Group, Inc. and through the employees of The Thaxton Group Inc.'s subsidiaries. On December 28, 2004, the Division issued Order No. 04-238 against James T. Garrett and Carolinas First Investments, Inc. for allegedly selling the promissory notes without reasonable grounds to believe that the transactions were suitable for Ohio investors in violation of Ohio Administrative Code Section 1301:6-3-19(A)(5). Carolinas First Invest-

ments Inc. was also accused of allegedly violating Ohio Administrative Code Section 1301:6-3-19(B)(9) for failing to reasonably supervise the individuals it used to conduct its sales in Ohio. An administrative hearing was held pursuant to Chapter 119 of the Revised Code. The Hearing examiner's report and recommendation in the Division's favor was issued on November 21, 2005, and subsequently approved by the Division in its Cease and Desist Order No. 06-018.

**Samuel G. Morocco**

On February 6, 2006, the Division issued Order No. 06-023, a Cease and Desist Order, against Samuel G. Morocco of North Lima, Ohio. From April 2003 through November 2004, Morocco, while licensed as a securities salesperson with National Planning Corporation, sold to Ohio investors promissory notes issued by Joanne and Alan Schneider. These promissory notes are securities under the Ohio Securities Act but were not registered with the Division or exempt from registration and therefore sold by Morocco in violation of Revised Code Section 1707.44 (C)(1). Mr. Morocco also violated Ohio Administrative Code Section 1301:6-3-19(A)(19) as he failed to obtain written authority from his employer at the time prior to selling the notes which were also not recorded on the broker/dealer's regular books or records. Mr. Morocco entered into a consent agreement with the Division wherein he waived the issuance of a Notice of Opportunity for Hearing, as well as his right to such a hearing in accordance with Revised Code Chapter 119, thereby allowing the Division to issue its Cease and Desist Order No. 06-023.

**Allen O. Snyder**

On January 20, 2006, the Division issued a Cease and Desist Order, Division Order No. 06-006, to Allen O. Snyder and HiTech Co. Accounting Services of Indianapolis, Indiana. Snyder, dba HiTech Co. Accounting Services, induced Ohio investors to invest money or roll-over funds from IRA accounts into a purported IRA created by Snyder, which would contain government bonds that he guaranteed at seven percent interest for five years. Snyder then falsified account statements, indicating profits, and never invested investor funds in anything. Snyder's actions constituted violations of R.C. sections 1707.44(C)(1), 1707.44(B)(4), 1707.44(G) and 1707.44(K).

The Division notified Snyder and HiTech Co. Accounting Services of their right to an administrative hearing pursuant to Chapter 119 of the Ohio Revised Code. Snyder and HiTech Co. Accounting Services did not request a hearing in a timely matter, resulting in the issuance of the Cease and Desist Order.

**National Capital 1, Inc.;**  
**Thomas John Schnippel**

On January 31, 2006, the Division issued a Consented Cease and Desist Order (No. 06-014) against National Capital 1, Inc. and Thomas John Schnippel, of Botkins, Ohio.

The Division found that the Respondents violated Revised Code sections 1707.44(C)(1), 1707.44(B)(4) and 1707.44(G), which prohibit, respectively, the sale of unregistered securities, misrepresentation in the sale of securities,

and engaging in fraudulent acts in the sale of securities. The Division had previously issued a Notice of Opportunity for Hearing against the Respondents on November 4, 2005 alleging the above-cited violations. The violations stemmed from National Capital 1, Inc.'s sales of promissory notes to 48 investors in an effort to raise approximately \$1,400,000. Schnippel participated in some of the later sales. Sales to the 48 investors occurred between July 2002 and March 2005. The money was to be used to promote and build a gambling casino that would be operated by an Oklahoma Indian tribe. The Order alleged that, in selling the notes, the Respondents failed to disclose to investors that principal and interest payments would almost exclusively come from the investors' own contributions and that National Capital 1, Inc. had no other identifiable source of income to make such payments. They also guaranteed investors that their principal was safe, despite the fact that the corporation had no guaranteed ongoing source of income.

Upon receiving the Notice of Opportunity for Hearing, the Respondents requested a hearing pursuant to Chapter 119 of the Revised Code. The Division and the Respondents entered into a Consent Agreement on January 31, 2006. The Respondents waived their rights to further appeals guaranteed in Chapter 119 of the Revised Code, and consented, stipulated and agreed to the findings, conclusions and orders set forth in the accompanying Cease and Desist Order.

**A Piece of the Action, LLC;  
Thomas R. Holtsberry;  
Robert Bollinger**

On February 9, 2006, the Division issued a Consented Cease and Desist Order, Order No. 06-036, against A Piece of the Action, LLC, Thomas R. Holtsberry and Robert Bollinger. The three Respondents conduct business out of Harrod, Ohio.

The Division found that Bollinger violated the provisions of Revised Code section 1707.44(C)(1), which prohibits the sale of unregistered securities, as well as Revised Code section 1707.44(A)(1), which prohibits unlicensed persons from selling securities. The Division also found that A Piece of the Action, LLC and Thomas R. Holtsberry violated the provisions of Revised Code sections 1707.44(C)(1) and 1707.44(B)(1) which prohibits any person from knowingly making a false representation concerning a material and relevant fact in any written statement for the purpose of exempting securities or transactions for registration. Those findings appeared as allegations in a Notice of Opportunity for Hearing the Division had previously issued against the Respondents on November 4, 2005. Holtsberry had formed A Piece of the Action, LLC, bringing in Bollinger as a partner who would be responsible for obtaining investors in order to raise revenue in support of National Capital 1, Inc. (See *preceding summary*). National Capital 1, Inc.'s purpose was, in turn, to promote and build a gambling casino to be operated by an Oklahoma Indian tribe.

Holtsberry had filed a Form 3-Q on behalf of A Piece of the Action, LLC, which asked for information concerning commissions paid for the sale of securities. Holtsberry stated on the form that no one had been paid a commission to sell securities issued on behalf of the company. The Division asserted that Bollinger was paid a commission to sell eleven investment contracts totaling \$275,000, thereby making Holtsberry's statement false and triggering a violation of R.C. 1707.44(B)(1). The Division also asserted that Bollinger had acted as a dealer in selling securities in violation of R.C. 1707.44(A)(1). The Division also asserted that, since the Form 3-Q filing was deemed defective, the Respondents had not effectively registered or claimed a valid exemption, thereby triggering a violation of R.C. 1707.44(C)(1).

Upon receiving the Notice of Opportunity for Hearing, the Respondents requested a hearing pursuant to Chapter 119 of the Revised Code. The Division and the Respondents entered into a Consent Agreement on February 9, 2006. The Respondents waived their rights to any further appeals guaranteed in Chapter 119 of the Revised Code, and consented, stipulated and agreed to the findings, conclusions and orders set forth in the accompanying Cease and Desist Order.

## 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 2006	YTD 2006
<b>Exemptions</b>		
Form 3(Q)	\$46,305,324.00	\$46,305,324.00
Form 3(W)	4,000,000	4,000,000
Form 3(X)	104,791,302,982	104,791,302,982
Form 3(Y)	12,475,000	12,475,000
<b>Registrations</b>		
Form .06	1,103,891,612	1,103,891,612
Form .09/.091	1,945,517,401	1,945,517,401
<b>Investment Companies</b>		
Definite	130,630,391	130,630,391
Indefinite**	553,000,000	553,000,000
<b>TOTAL</b>	<b>\$108,587,122,710</b>	<b>\$108,587,122,710</b>

## Registration Statistics

The following table sets forth the number of registration, exemption, and notice filings received by the Division during the first quarter of 2006, compared to the number of filings received during the first quarter of 2005. Likewise, the table compares the year-to-date filings for 2005 and 2006.

Filing Type	1st Qtr '06	YTD '06	1st Qtr '05	YTD '05
1707.03(Q)	37	37	30	30
1707.03(W)3	4	4	5	5
1707.03(X)	467	467	388	388
1707.03(Y)	3	3	5	5
1707.04/.041	1	1	0	0
1707.06	27	27	17	17
1707.09/.091	36	36	30	30
Form NF	1329	1329	1280	1280
<b>Total</b>	<b>1904</b>	<b>1904</b>	<b>1755</b>	<b>1755</b>