OPEN MEETING ITEM

ORIGINAL

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CARL J. KUNASEK
CHAIRMAN
JIM IRVIN
COMMISSIONER
WILLIAM A. MUNDELL
COMMISSIONER

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AZ CORP COMMISSION

BRIAN C. McNEIL
EXECUTIVE SECRETARY

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ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission
DOCKETED
DOCUMENT CONTROL
FEB 11 2000
DOCKETED BY

DATE: February 11, 2000

DOCKET NO.: S-03177A-98-0000

TO ALL PARTIES:

Enclosed please find the recommendation of Hearing Officer Barbara M. Behun. The recommendation has been filed in the form of an Opinion and Order on:

FOREX INVESTMENT SERVICES CORPORATION, EASTERN VANGUARD FOREX LTD., EASTERN VANGUARD GROUP LIMITED, K. (DAVID) SHARMA, SAMMY LEE CHUN WING, PETER SUEN SUK TAK, MICHAEL E. CHO, TO FAI CHENG, JEAN YUEN, Y & T INC. DBA TOKYO INTERNATIONAL INVESTMENT LTD, WING MING TAM, GUO QUAN ZHANG, AND JAMES CHARLES SIMMONS, JR.
(NOTICE OF OPPORTUNITY)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Hearing Officer by filing an original and ten (10) copies of the exceptions with the Commission's Docket Control at the address listed below by **4:00** p.m. on or before:

FEBRUARY 22, 2000

The enclosed is NOT an order of the Commission, but a recommendation of the Hearing Officer to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Working Session and Open Meeting to be held on:

MARCH 1, 2000 AND MARCH 2, 2000

For more information, you may contact Docket Control at (602) 542-3477 or the Hearing Division at (602) 542-4250.

BRIAN C. McNEIL
EXECUTIVE SECRETARY

This document is available in alternative formats by contacting Cynthia Mercurio-Sandoval, ADA Coordinator, voice phone number 602/542-0838, E-mail csandoval@cc.state.az.us

BEFORE THE ARIZONA CORPORATION COMMISSION

CARL J. KUNASEK
CHAIRMAN
JIM IRVIN
COMMISSIONER
WILLIAM A. MUNDELL
COMMISSIONER

IN THE MATTER OF:

FOREX INVESTMENT SERVICES CORPORATION
2700 N. Central Ave., Suite 1110
Phoenix, AZ 85004

EASTERN VANGUARD FOREX LTD.
2700 N. Central Ave., Suite 1110
Phoenix, AZ 85004

c/o HWR Services Limited, Registered Agent
P.O. Box 71, Craigmuir Chambers
Road Town, Tortola
British Virgin Islands

EASTERN VANGUARD GROUP LIMITED
c/o AMS Trustees Limited, Registered Agent
Creque Building, Main Street, P.O. Box 116
Road Town, Tortola
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K. (DAVID) SHARMA
Eastern Vanguard Forex Ltd.
P. O. Box 71, Craigmuir Chambers
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British Virgin Islands

SAMMY LEE CHUN WING
Eastern Vanguard Group Limited
Creque Building, Main Street, P.O. Box 116
Road Town, Tortola
British Virgin Islands

PETER SUEN SUK TAK
Eastern Vanguard Group Limited
Creque Building, Main Street, P.O. Box 116
Road Town, Tortola
British Virgin Islands

JAMES CHARLES SIMMONS, JR.
5045 N. 58th Ave. #23A
Glendale, AZ 85301

. . .

DOCKET NO. S-03177A-98-0000

DECISION NO. _____

OPINION AND ORDER

MICHAEL E. CHO
839 Faxon Avenue
San Francisco, CA 94112

TO FAI CHENG
1800 Van Ness, 2nd Fl.
San Francisco, CA 94109

JEAN YUEN
439 3rd Avenue
San Francisco, CA 94118

Y & T INC. and TOKYO
INTERNATIONAL INVESTMENT LTD.
1800 Van Ness Ave., 2nd Fl.
San Francisco, CA 94109

WING MING TAM
c/o Tokyo International Investment Ltd.
1800 Van Ness Ave., 2nd Fl.
San Francisco, CA 94109

GUO QUAN ZHANG
O/o Tokyo International Investment Ltd.
1800 Van Ness Ave., 2nd Fl.
San Francisco, CA 94109

Respondents.

DATE OF HEARING:	August 27, 28, September 1, 9-11, 14, 16, 17, 22, 28, October 8, 9, 13-16, 21, and 23, 1998 Oral argument July 8, 1999
PLACE OF HEARING:	Phoenix, Arizona
PRESIDING OFFICER:	Barbara M. Behun
APPEARANCES:	Mr. Alan S. Baskin, ROSHKA HEYMAN & DEWULF, PLC, on behalf of Forex Investment Services Corporation; Eastern Vanguard Forex Ltd.; Eastern Vanguard Group Limited; K. (David) Sharma; Sammy Lee Chun Wing; Peter Suen Suk Tak; Michael E. Cho; To Fai Cheng; Jean Yuen; Y & T Inc. dba Tokyo International Investment Ltd.; Wing Ming Tam; and Guo Quan Zhang; and Mr. Mark C. Knops, Special Assistant Attorney General, and Mr. Robert A. Zumoff, Assistant Attorney General, on behalf of the Securities Division of the Arizona Corporation Commission.

BY THE COMMISSION:

On February 6, 1998, the Securities Division ("Division") of the Arizona Corporation Commission ("Commission") filed a Notice of Opportunity for Hearing Regarding Proposed Order

for Relief ("Notice") against Forex Investment Services Corporation ("FISC"); Eastern Vanguard Forex Ltd. ("EVFL"); Eastern Vanguard Group Limited ("EVGL"); K. (David) Sharma ("Sharma"); Sammy Lee Chun Wing ("Wing"); Peter Suen Suk Tak ("Tak"); Michael E. Cho ("Cho"); To Fai Cheng ("Cheng"); Jean Yuen ("Yuen"); Y & T Inc. dba Tokyo International Investment Ltd. ("Tokyo"); Wing Ming Tam ("Tam"); Guo Quan Zhang ("Guo"); and James Charles Simmons, Jr. ("Simmons") All Respondents requested a hearing. Ultimately, All Respondents except for Simmons ("Collective Respondents") were represented by counsel at the hearing. Simmons represented himself and appeared in a pre-trial matter, but did not appear or participate in the hearing.

A hearing was held before a duly authorized Hearing Officer of the Commission at the Commission's offices in Phoenix, Arizona. On November 25, 1998, Collective Respondents filed a Motion to Dismiss re: Lack of Jurisdiction and Motion to Dismiss Securities Division's Claim for Restitution ("Motion"). On January 4, 1999, the Division filed a Response to the Motion, and on January 29, 1999, Collective Respondents filed a Reply. Oral argument on the Motion was held on July 8, 1999.

On March 8, 1999, the Division filed a notice of withdrawal of allegations contained in paragraphs 29, 30, 34 and 35 of the Notice. Also on March 8, 1999, the Division filed a Motion for Sanction of Evidentiary Inference against Certain Respondents.

Collective Respondents and the Division filed post-hearing memoranda and response memoranda on April 26, 1999 and June 1, 1999, respectively. Collective Respondents' response to the Motion for Sanction was contained within their post-hearing memorandum.

DISCUSSION

Introduction

FISC advertised for foreign currency traders and enrolled individuals in a course to trade foreign currency. Trainees recruited friends, family, conducted general solicitation and frequently would invest their own money in foreign currency contracts. Leveraged trading on accounts was conducted by relaying through Tokyo to an EVFL office in Macau. Currency dealers in Macau contracted directly with international monetary companies without using a regulated exchange or board of trade. Prices were set by EVFL, and positions tracked through internal accounts. Currency

contracts were kept open until ordered sold by the investor or there were insufficient funds in the account to cover the contract. Generally, traders and customers lost money.

Interest was charged or paid on positions left open overnight. The interest charged was greater than the interest EVFL paid. FISC compensated salesmen for each trade closed on behalf of an account holder by paying a portion of its share of the trading commission charged to the account by EVFL.

The Division alleged a violation of A.R.S. § 44-1841, offer or sale of unregistered securities, against FISC, EVFL, Simmons and Cho. The Division claimed that FISC, EVFL, Simmons and Cho offered to sell or sold securities within or from Arizona in the form of commodity investment contracts, within the meaning of A.R.S. §§ 44-1801(3), (6), (13), (19) and (23), and 44-2003(A). The Division initially alleged that Cheng, Yuen, Tokyo, Tam, Guo, Sharma, EVGL, Wing and Tak were jointly and severally liable under A.R.S. § 44-1999, but subsequently withdrew those allegations.

The Division alleged a violation of A.R.S. § 44-1842, transactions by unregistered dealers or salesmen, against FISC, EVFL, Simmons and Cho, claiming that they acted as dealers or salesmen in or from Arizona within the meaning of A.R.S. § 44-1801(9) and (20), although not registered pursuant to the provisions of Article 9 of the Securities Act of Arizona, 44 A.R.S. § 1801, *et seq.* ("Act" or "SAA"). The Division initially alleged that Cheng, Yuen, Tokyo, Tam, Guo, Sharma, EVGL, Wing and Tak were jointly and severally liable under A.R.S. § 44-1999, but subsequently withdrew those allegations.

The Division alleged a violation of A.R.S. § 44-1991 against FISC, EVFL, Simmons and Cho for directly or indirectly making untrue statements of material fact and omitting to state material facts which were necessary in order to make the statements made not misleading in light of the circumstances under which they were made. The Division alleged that FISC, EVFL, Simmons and Cho directly or indirectly engaged in transactions, practices or courses of business which operated or would operate as a fraud or deceit upon offerees and investors within the meaning of A.R.S. § 44-1991.

The Division alleged that during the violations of A.R.S. § 44-1991, Cheng, Yuen, Tokyo, Tam and Guo directly or indirectly controlled FISC; and Sharma, EVGL, Wing and Tak directly or

indirectly controlled EVFL within the meaning of A.R.S. § 44-1999, and therefore were jointly and severally liable to the same extent as FISC and EVFL, respectively, for violations of A.R.S. § 44-1991.

Jurisdiction

Collective Respondents claimed that Congress amended the Commodity Exchange Act, 7 U.S.C. § 1, *et seq.* ("CEA") in 1974 to exclude regulation of off-exchange transactions in foreign currency. According to Collective Respondents, Congress created the Commodity Futures Trading Commission ("CFTC") to develop the expertise to regulate commodity trading, and gave the CFTC broad, extensive, and exclusive jurisdiction over investments involving commodities.

Collective Respondents claimed that the following Section of the CEA eliminated state jurisdiction over the type of foreign currency trading that occurred in this matter:

> Section 2. Accounts, agreements, and transactions subject to jurisdiction of Commodity Futures Trading Commission relation to jurisdiction of Securities and Exchange Commission and Federal and State courts; excepted transactions
>
> (i) The Commission shall have exclusive jurisdiction, except to the extent otherwise provided in section 2a of this title, with respect to accounts, agreements (including any transaction which is of the character of, or is commonly known to the trade as, an "option", "privilege", "indemnity", "bid", "offer", "put", "call", "advance guaranty", or "decline guaranty"), and transactions involving contracts of sale of a commodity for future delivery, traded or executed on a contract market designated pursuant to section 7 of this title or any other board of trade, exchange, or market, and transactions subject to regulation by the Commission pursuant to section 23 of this title. Except as hereinabove provided, nothing contained in this section shall (I) supersede or limit the jurisdiction at any time conferred on the Securities and Exchange Commission or other regulatory authorities under the laws of the United States or of any State, or (II) restrict the Securities and Exchange Commission and such other authorities from carrying out their duties and responsibilities in accordance with such laws. Nothing in this section shall supersede or limit the jurisdiction conferred on courts of the United States or any State.
>
> (ii) Nothing in this chapter shall be deemed to govern or in any way be applicable to transactions in foreign currency, security warrants, security rights, resales of installment loan contracts, repurchase options, government securities, or mortgages and mortgage purchase commitments, unless such transactions involve the sale thereof for future delivery conducted on a board of trade.

Collective Respondents alleged that the Commission lacks jurisdiction to (1) require that transactions in foreign currency be registered as securities under Arizona law; (2) require Respondents to register with the State in connection with these foreign currency transactions; and (3)

initiate proceedings for other alleged violations of the Act in connection with transactions in foreign currency.

Collective Respondents alleged that the United States Supreme Court, in *Dunn v. Commodity Futures Trading Commission*, 519 U.S. 465, 117 S. Ct. 913, (1997) and the United States Court of Appeals for the Ninth Circuit, in *Commodity Futures Trading Commission v. Frankwell Bullion, Ltd.*, 99 F.3d 299 (9th Cir. 1996) determined that Section 2 of the CEA prohibited regulation of off-exchange foreign currency trading. Similarly to FISC, Frankwell sold standardized lots of certain currencies in which the customer could either open a "long" or a "short" position at a price based on the Interbank spot market. Customers did not pay the purchase price for the currency or accept delivery for it. Customers would take a profit or loss when a position was closed with an offsetting contract. A carrying charge was assessed for each day that a contract was left open. According to Collective Respondents, the Court of Appeals held that Congress intended to exclude all off-exchange transactions from regulation. The Court of Appeals also rejected the argument that Frankwell was a board of trade as an association of persons engaged in the business of selling commodities.

Collective Respondents alleged that in *Dunn*, 117 S. Ct. 913 at 918, the United States Supreme Court held that Congress had not authorized the CFTC to regulate off-exchange trading in options to buy or sell foreign currency. Collective Respondents claimed that as Congress specifically prohibited the CFTC from regulating transactions in foreign currency, Congress's mandate must logically be construed to extend to the states. Collective Respondents argued that under the doctrine of negative preemption, the fact that Congress has not regulated certain activity in a subject matter manifests intent that the activity should not be regulated by the states.

The Division claimed that the savings clause in Section 2(i) frame and limit the excepted transactions in Section 2(ii). According to the Division, the initial grant to the CFTC of exclusive subject matter jurisdiction over certain transactions displaced the jurisdiction of state securities and commodities agencies over transactions within its ambit. The Division alleged that except for those items specifically within the CFTC's exclusive jurisdiction, Congress specified that nothing in "this section" shall "supersede or limit the jurisdiction at any time conferred on ... other regulatory

authorities under the laws of ... any State" or "restrict ... such other authorities from carrying out their duties and responsibilities in accordance with such laws."

The Division argued that the phrase "this section" included all of Section 2, including subsection (ii) and its excepted transactions. The Division claimed that except where in contravention of the exclusive jurisdiction of the CFTC, the duties and responsibilities conferred by the SAA on the Commission to enforce the state law fall within the Section 2(i) preservation of state regulatory authority.

The Division argued that Section 2(ii) preserves transactions in the listed items from federal regulation under the CEA unless they involve the sale of futures on a board of trade. As support, the Division indicated the existence of widespread and established state securities regulation of items in Section 2(ii), such as security warrants and rights and government securities.

The Division distinguished *Dunn* and *Frankwell* by indicating that they expressly apply to CFTC jurisdiction. The Supreme Court in *Dunn* ruled that foreign currency options are transactions in foreign currency within the meaning of the CEA. The Court of Appeals in *Frankwell* determined that foreign currency transactions are exempted from CFTC jurisdiction because they are not transactions involving sales on a board of trade.

The Division disputed the application of the negative preemption doctrine where jurisdiction was withheld from the CFTC. The Division claimed that the negative preemption doctrine was expressly inapplicable according to Section 16.e of the CEA, which states:

> Section 16. Commission operations
>
> (e) Relation to other laws, departments, or agencies
>
> Nothing in this chapter shall supersede or preempt –
>
> (1) criminal prosecution under any Federal criminal statute;
>
> (2) the application of any Federal or State statute, including any rule or regulation thereunder, to any transaction in or involving any commodity, product, right, service, or interest (A) that is not conducted on or subject to the rules of a contract market, or, in the case of any State or local law that prohibits or regulates gaming or the operation of "bucket shops" (other than antifraud provisions of general applicability), that is not a transaction or class of transactions that has received or is covered by the terms of any exemption previously granted by the Commission under subsection (c) of section 6 of this title, or (B) (except as otherwise specified by the Commission by rule or regulation) that is not conducted on or subject to the rules of any board of trade,

> exchange, or market located outside the United States, its territories or possessions, or (C) that is not subject to regulation by the Commission under section 6c or 23 of this title...

The Division claimed that Respondents failed to bear their burden of overcoming the presumption of jurisdiction in the Commission to enforce the SAA against Respondents.

We agree with the Division that Respondents have not established that the Commission does not have jurisdiction over them. The Commission will exercise its jurisdiction pursuant to the SAA.[1]

Arbitration

Collective Respondents claimed that the Federal Arbitration Act ("FAA"), 9 U.S.C. § 2, has mandated that arbitration clauses should be enforced:

> A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction ... shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

Collective Respondents stated that each customer for whom the Division is seeking restitution signed an agreement with EVFL containing an arbitration clause:

> EVF has the right at its sole election to refer any dispute arising from or relating to this agreement or to any transaction/s contract effected hereunder to arbitration in accordance with the rules or regulations of EVF and/or other appropriate bodies.

After the Division filed the Notice, Respondents sent letters to each customer demanding arbitration of any claims that they might have against Respondents. Only one letter was returned. Customers elected to have the Division pursue potential claims on their behalf in this proceeding.

Collective Respondents alleged that the FAA pre-empted state law authorizing rescission in securities fraud claims, citing *Olde Discount Corporation v. Tupman*, 1 F.3d 202 (3rd Cir. 1993), and *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 1007 S. Ct. 2332, 96 L.Ed. 2d 185 (1987).

The Division claimed that Arizona followed the doctrine of separability, in which the arbitration clause is considered to be an agreement independent and separate from the principal

[1] We note that Collective Respondents' argument would allow for unsupervised transactions. The CEA limits the jurisdiction of the CFTC to boards of trade. Collective Respondents' allegations would eliminate state jurisdiction over the foreign currency trade, although the CEA, including amendments, speaks solely to the jurisdiction of the CFTC over foreign currency trading. Collective Respondents would also eliminate jurisdiction over securities that involve foreign currency. Presumably, the ban would include the other items specified in Subchapter (ii), such as security warrants, security rights, government securities, and mortgages.

contract, in *U.S. Insulation, Inc. v. Hilro Construction Company, Inc.* 146 Ariz. 250, 253, 705 P.2d 490, 493 (App. 1985), citing *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 87 S. Ct. 1801, 1805, 18 L.Ed. 2d 1270 (1967), and *Stevens/Leinweber/Sullens, Inc. v. Holm Development and Management, Inc.*, 165 Ariz. 25, 795 P.2d 1308 (App. 1990). The Division asserted that *Holm* applied the Arizona Uniform Arbitration Act ("AUAA"), 12 A.R.S. § 1501 *et seq.*, which used policy identical to the FAA, giving force and effect to arbitration provisions in contracts. According to the Division, an analysis of the arbitration provision must be conducted to determine whether there exist grounds for its revocation. The Division concluded that the arbitration provision herein is void for lack of consideration and repudiation and waiver.

Collective Respondents claimed that *Holm* was no longer good law, based upon *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 115 S. Ct. 834, 130 L.Ed. 2d 753 (1995) and *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681, 116 S. Ct. 1652, 134 L.Ed. 2d 902 (1996). Collective Respondents cited *Allied-Bruce Terminix*, 513 U.S. at 281, as follows:

> States may regulate contracts, including arbitration clauses, under general contract law principles and they may invalidate any arbitration clause "upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. What States may not do is decide that a contract is fair enough to enforce all its basic terms (price, service, credit), but not fair enough to enforce its arbitration clause. The [Federal Arbitration] Act makes any such state policy unlawful, for that kind of policy would place arbitration clauses on an unequal "footing," directly contrary to the Act's language and Congress' intent.

The Division argued that *Holm* is still the law in Arizona. The Division claimed that *Allied-Bruce Terminix* and other recent United States Supreme Court opinions did not refute the doctrine of separability. The Division asserted that the AUAA and *Holm* were in compliance with the FAA. According to the Division, Arizona law that a contract can fail for lack of mutuality of obligation, when applied to the arbitration clause, invalidates the clause. The Division also claimed that the arbitration provision failed on other grounds, such as the doctrine of reasonable expectations, unconscionability, repudiation, and prejudice.

We agree with the Division that the arbitration clause, and Collective Respondents' use of the clause in this matter, is not valid. We will allow the claim of restitution.

Request for Evidentiary Inference

On March 8, 1999, the Division filed a Motion for Sanction of Evidentiary Inference against Certain Respondents ("Motion for Sanction") in the form of an adverse inference that records neither produced nor disclaimed by EVFL and EVGL pursuant to Commission ruling would tend to show that Sharma, EVGL, Wing and Tak were controlling persons of EVFL within the meaning of A.R.S. § 44-1999 and violations of A.R.S. § 44-1991 alleged in this matter against EVFL by the Division. The Division requested records regarding direct or indirect benefit to EVGL, Sharma, Wing, Tak and Cheng from EVFL assets. As detailed in the Division's Motion, the Division filed a Motion to Compel production of records, and later requested an adverse inference. By rulings on September 11, 1998, October 23, 1998 and November 4, 1998, Respondents were required to provide the requested information. On December 9, 1998, Collective Respondents filed an affidavit of Alwin Yam dated December 2, 1998. The Division claimed that the affidavit was not responsive to the inquiries.

In their Post-Hearing Memorandum filed April 26, 1999, Collective Respondents alleged that the affidavit of Mr. Yam was responsive to the Division's request. Collective Respondents claimed that due to the delay in the Division rearguing the Motion, they were deprived of the opportunity to explain the rationale behind the affidavit. Collective Respondents also argued that the affidavit responds to the request to the extent that it is relevant to this matter. Collective Respondents asserted that the affidavit responds to the operation of EVFL solely as it pertains to FISC. Collective Respondents requested that any adverse inference should be limited to an inference that the relevant Respondents received a benefit from operations of EVFL other than operations related to FISC, and that the operation of EVFL solely as it pertains to FISC is relevant to this proceeding.

We agree with the Division that Respondents EVFL and EVGL, through Alwin Yam, failed to respond to discovery requested by the Division and ordered by the Commission. We will grant the Division's motion for a sanction in the form of an adverse inference that records neither produced nor disclaimed by EVFL and EVGL would tend to show that Sharma, EVGL, Wing and Tak were controlling persons of EVFL within the meaning of A.R.S. § 44-1999, for purposes of EVFL violations of A.R.S. § 44-1991 alleged in this matter by the Division.

Controlling Persons

In connection with A.R.S. § 44-1991 violations alleged against EVFL and FISC, the Division

alleged that certain Respondents directly or indirectly controlled those persons within the meaning of A.R.S. § 44-1999, making the controlling Respondents jointly and severally liable for violations. Respondents argued that the interpretation of primary liability in A.R.S. § 44-2003 and *Standard Chartered PLC v. Price Waterhouse*, 190 Ariz. 6, 17-23, 945 P.2d 317, 328-34 (App. 1996), requires participating in or inducing the unlawful sale of securities. Respondents assert that control liability allegations must be dismissed under the control test in *Paracor Finance, Inc. v. General Electric Capital Corp.*, 79 F.3d 878 (9th Cir. 1996). According to Respondents, control liability requires actual participation in the specific violative activity.

The Division pointed out that its allegations of primary liability are based upon A.R.S. §§ 44-1841, 1842 and 1991, and distinguished the differing statutory liability and judicial interpretation. The Division claimed that the Ninth Circuit interpretations of federal securities laws have not always comported with the construction mandated by our legislature for the SAA. The Division requested that we adopt the Fifth Circuit's control test in which liability accompanies possession of actual power to directly or indirectly influence the general affairs and policy of the primary violator. *See G. A. Thompson Co., Inc. v. Partridge*, 636 F.2d 945, 958 (5th Cir. 1981).[2]

The Division asserted that a rebuttable presumption of vicarious liability arises under A.R.S. § 44-1999, which may be defeated upon a showing, according to § 44-1999, that "the controlling person acted in good faith and did not directly or indirectly induce the act underlying the action." Respondents claimed that the Division did not establish that the alleged controlling Respondents directed anyone to make false and misleading statements.

The Division claimed that to meet the affirmative defense, Respondents must establish that they did not act intentionally, recklessly or negligently, and did not directly or indirectly induce the violations, by action or inaction. The Division asserted that Respondents did not provide any affirmative evidence, claiming that evidence indicated no control liability also proves the good faith defense. The Division claimed that Respondents did not establish a prima facie good faith defense.

We agree with the Division that a strict interpretation of the Ninth Circuit test is too restrictive

[2] In *Nutek Information Sytems v. Arizona Corporation Commission,* 977 P.2d 826 (App. 1998), our Court of Appeals rejected a Ninth Circuit liability test in favor of a less burdensome Fifth Circuit test.

to guard the public interest as directed by our state legislature, although we will not bar its use in the broader sense of requiring power to control the type of action causing the fraud. Whether under the Fifth or Ninth Circuit tests, the Division has satisfied its burden that certain Respondents should be subject to control liability for actions of FISC and EVFL. The general affairs and specific policies of the primary violators were controlled by the controlling persons. In addition, Respondents have not satisfied the burden of proof of an affirmative defense regarding control liability.

* * * * * * * * * *

Having considered the entire record herein and being fully advised in the premises, the Commission finds, concludes, and orders that:

FINDINGS OF FACT

1. On February 6, 1998, the Division filed a Notice against Respondents.

2. Respondents requested a hearing.

3. Commencing on August 27, 1998, a hearing was held before a duly authorized Hearing Officer of the Commission.

4. On November 25, 1998, Collective Respondents filed a Motion.

5. On January 4, 1999, the Division filed a Response to the Motion.

6. On January 29, 1999, Collective Respondents filed a Reply to the Motion.

7. Oral argument on the Motion was held on July 8, 1999.

8. The above discussion of the Motion is incorporated herein, as is the ruling that the Motion is denied in its entirety.

9. On March 8, 1999, the Division filed a notice of withdrawal of allegations contained in paragraphs 29, 30, 34 and 35 of the Notice.

10. On March 8, 1999, the Division filed a Motion for Sanction.

11. Collective Respondents and the Division filed post-hearing memoranda on April 26, 1999. Collective Respondents' response to the Division's Motion for Sanction was included within its post-hearing memorandum.

12. Collective Respondents and the Division filed response memoranda on June 1, 1999.

13. The above discussion and ruling regarding the Motion for Sanction are incorporated

herein.

14. The Division alleged that in connection with the offer or sale of securities within and/or from Arizona described above, Respondents directly or indirectly made untrue statements of material fact and omitted to state material facts which were necessary in order to make the statements made not misleading in light of the circumstances under which they were made, in violation of A.R.S. § 44-1991, including but not limited to the following:

(a) Respondents made untrue statements that EVFL or FISC salesmen were professional currency traders able to make sound investment decisions on behalf of investors, while in fact such salesman had insufficient training and experience in Forex-related trading and made unsound investment decisions that caused substantial losses by investors;

(b) Respondents failed to disclose the business experience of EVFL and its principals;

(c) Respondents failed to disclose financial statements reflecting the financial condition of EVFL;

(d) Respondents failed to disclose how customer Forex orders were executed by EVFL;

(e) Respondents failed to disclose the terms under which interest was charged or paid on overnight positions, or the risk of loss to a customer account due to adverse interest or "premium" charges resulting from maintaining an overnight position;

(f) Respondents failed to disclose the location and use of investor funds after deposit with FISC and EVFL and while such funds were credited to investor accounts; and

(g) Respondents failed to disclose the EVFL and FISC policy that their offer or sale of FOREX trading accounts were not subject to state or federal securities laws, and the attendant risks to investors of non-compliance with the investor protection provisions of those laws.

15. The Division alleged that in connection with their offers or sales of securities through FISC, Respondents directly or indirectly engaged in transactions, practices or courses of business which operated or would operate as a fraud or deceit upon offerees or investors within the meaning of A.R.S. § 44-1991, including but not limited to presenting EVFL and FISC salesmen as professional currency traders able to make sound investment decisions on behalf of investors, while such salesmen had insufficient training and experience in Forex-related trading and made unsound investment decisions that caused substantial losses by investors.

16. The Division alleged that during the foregoing violations of A.R.S. § 44-1991, Respondents Cheng, Yuen, Tokyo, Tam and Guo directly or indirectly controlled FISC within the meaning of A.R.S. § 44-1999, and therefore are jointly and severally liable to the same extent as FISC for its violations of A.R.S. § 44-1991.

17. The Division alleged that during the foregoing violations of A.R.S. § 44-1991, Respondents Sharma, EVGL, Wing and Tak directly or indirectly controlled EVFL within the meaning of A.R.S. § 44-1999, and therefore are jointly and severally liable to the same extent as EVFL for its violations of A.R.S. § 44-1991.

18. The Division and Collective Respondents stipulated to the following facts, which Respondent Simmons has not opposed:

(a) According to sales literature provided to prospective investors, an investor engages in leveraged trading on the international foreign currency spot market ("Forex") through an EVFL account by buying or selling on margin fixed amounts of four foreign currencies: the German Mark (DM 125,000), the Swiss Franc (SF 125,000), the British Pound (£62,500) and the Japanese Yen (¥12,500,000). Each foreign currency lot or "contract" is priced in U. S. dollars based on fluctuating currency exchange rates reported on the Interbank Network, a global communication network of international banks.

(b) Investors opened EVFL trading accounts through FISC by paying at least $10,000 as "Guarantee Money" and executing an EVFL "Customer's Agreement" and other documents. Investor funds were deposited into an EVFL bank account in California as "initial margin" to "secure" trading transactions. The "Customer's Agreement" and related documents were retained indefinitely by FISC, with copies provided to EVFL. ...

(c) Leveraged trading on an account was conducted by relaying investor buy or sell orders through the FISC and TOKYO offices to an EVFL office in Portuguese Macau on the Pacific coast of China, with all buy or sell contract prices set by EVFL. Trading was leveraged because less than five percent of the price to buy or sell each currency contract was reserved in the account as an earnest deposit or initial margin. EVFL imposed a minimum "day trade" margin of $1,000 for each contract (or "position") entered into ("opened") and then liquidated ("closed") by an offsetting contract during the same business day. For each contract opened but not closed until another business day, EVFL required a $2,000 minimum "overnight trade" margin. ...

(d) The currency contracts bought or sold through EVFL trading accounts provided no settlement or delivery dates. Overnight positions could be maintained indefinitely through successive business days, with only one trading commission charged by EVFL upon position liquidation. Additional margin was required to maintain open positions if adverse changes in currency prices rendered the minimum margin insufficient. EVFL charged or paid daily interest on overnight positions depending on the currency and whether the position was buy or sell. The interest charged was greater than the interest

EVFL paid. Whether a day trade or an overnight trade resulted in investor gain was determined by the price difference between the opening position and the offsetting contract closing a position, together with commission cost and daily interest charged or paid by EVFL on overnight positions.

(e) The leveraged trading accounts offered or sold by EVFL through FISC were promoted as a speculative investment. The EVFL Customer's Agreement expressly required an account holder to specially instruct EVFL in writing and receive confirmation for any order placed for actual delivery. EVFL reserved the right to determine the time and place of such delivery at its discretion. Orders placed without such instruction and confirmation were deemed not for delivery.

19. Paragraph 1 of the Customer's Agreement provided in part that EVFL "is hereby requested and authorized by customer to act as broker or as agent or as principal to execute customer's Investment order/s."

20. The "Addendum to Customer's Agreement" ("Addendum") declared that the Customer Agreement is governed by Arizona law.

21. According to an Agreement between FISC and EVFL dated January 1, 1997, EVFL agreed to pay FISC $20,000 monthly plus $50 per position closed in return for FISC providing "adequate facilities", "telephone and communication equipment," and "training courses as well as training facilities" for EVFL "employees." FISC was also to receive and distribute EVFL funds as directed for commission payments to EVFL "employees." EVFL was "responsible for all taxes, and withholdings, and must comply with all local, state and federal regulations." FISC was to provide "reasonable advertisements" for EVFL's "business" and "financial market information related to" EVFL's "business."

22. Tam stated that FISC was a branch office of EVFL, "like a McDonald's, kind of like a part of the company but, you know, an individual location."

23. FISC's Better Business Bureau application signed July 30, 1996 by Dionisio Meneses identified its business as "foreign exchange broker" and listed EVFL as its parent company.

24. FISC opened for business in April 1996, with Mr. Meneses as its marketing manager from inception until November 1996.

25. Cho was FISC marketing manager from early January 1997 until October 31, 1997.

26. Cho's compensation as marketing manager included a monthly salary; a monthly commission package based upon a percentage of new investor deposits, an override per closed

trading position; plus a bonus if investor deposits reached a monthly threshold.

27. During his tenure as marketing manager, Cho received between $16,000 and $17,000 from the commission package.

28. Simmons entered a FISC trader training class in January 1997, after interviewing with Cho.

29. Cho helped Simmons learn FISC trading procedures and assisted him with clients.

30. In Spring 1997, Cho hired Simmons as assistant marketing manager, after recommending him to Tam and getting Tam's approval.

31. Cho trained Simmons as his assistant, and gave him instructions not to make any decisions about the trainees, that Cho was the one who made those decisions.

32. As assistant marketing manager, Simmons received a monthly compensation and an override per position closed by any trader under his supervision.

33. Simmons replaced Cho as marketing department manager for FISC on November 1, 1997, until the office closed on December 18, 1997, with a monthly compensation and an override per position closed by any trader in the office.

34. FISC advertised for foreign currency traders and enrolled interested individuals in two-month training courses to be currency traders.

35. The training included instruction on how to recruit customers.

36. Towards the end of the course, trainees were encouraged to recruit customers.

37. Cho questioned trainees about obtaining clients.

38. On numerous occasions, trainees invested their own money, or funds of their relatives or friends, in trading accounts at the conclusion of the training course.

39. FISC telemarketed trading accounts in 1996.

40. Traders were provided FISC business cards and a "standard" introductory FISC letter recommended by Cho.

41. Traders had access to a FISC computer, and were allowed to compose and send letters using FISC letterhead.

42. At least twenty-one EVFL commodity investment contract securities were offered and

sold within or from Arizona through FISC.

43. Blank Customer's Agreements to be executed by clients were received by FISC with the EVFL signature block already signed by an EVFL authorized person.

44. Customers opened accounts by checks payable to EVFL that were directly deposited by FISC to an EVFL account at Citibank in San Francisco.

45. FISC prepared and mailed EVFL account statements to investors.

46. Cho personally sold EVFL accounts to two investors through FISC, and participated while marketing manager in the sale of accounts to sixteen other investors.

47. As a trader, Simmons personally offered and sold four EVFL accounts.

48. As marketing manager, Simmons participated in the sale of two EVFL accounts.

49. Cho testified that the marketing manager "is the one who's making decisions," and that his job was "to generate business" for FISC.

50. Cho placed the FISC newspaper advertisements for foreign currency trader applicants.

51. Cho taught two training classes and participated in another one, taught by Simmons.

52. Cho reviewed the Customer's Agreement with the trainees.

53. Cho supervised traders after the training course, and assisted in talking with potential and actual clients.

54. Cho informed the traders that he would help close accounts with potential clients.

55. Cho conducted the signing of the new Customer's Agreements, received investor funds, and explained procedures to investors.

56. In late February 1997, Cho purchased $500 worth of leads for use in the office by trainees and traders.

57. Cho told the traders and trainees about the leads, and invited them to use the leads.

58. At a party with the traders in late summer 1997, Cho queried each trader about investor recruitment.

59. EVFL Forex accounts offered or sold through FISC were never registered as securities under the SAA.

60. No Respondent has claimed any exemption from registration under the SAA.

61. FISC, EVFL, Simmons and Cho offered and sold EVFL Forex accounts.

62. FISC, EVFL, Simmons and Cho were not registered to sell securities under the SAA.

63. FISC, EVFL, Simmons and Cho acted as securities dealers or salesmen while unregistered under the SAA.

64. Respondents made untrue statements that EVFL or FISC salesmen were professional currency traders able to make sound investment decisions on behalf of investors, while in fact such salesmen had insufficient training and experience in Forex-related trading and made unsound investment decisions that caused substantial losses by investors.

65. A FISC brochure entitled "Foreign Exchange Services" declared: "Forex Investment Services Corp. research team also provides its traders and clients with in-depth fundamental and technical analysis. With this wealth of experience and knowledge, Forex Investment Services Corp.'s traders have the discipline and ability to make sound investment decisions."

66. The FISC brochure was given to prospective investors and to FISC trainees for marketing.

67. The standard FISC introductory letter claimed that high returns on investments could be achieved, but omitted mention of any risk of loss.

68. The FISC brochure stated that "Foreign currency trading has inherent advantages over traditional forms of investment," and "100% return on investment in a given year is not uncommon due to the volatility of the spot market."

69. Simmons stated that he has not personally achieved 100 percent return, and indicated that he did not add a disclaimer to prospective clients regarding that statement.

70. To induce Alan Davis to invest with FISC, Simmons claimed that he had been a commodities trader in the east coast; that he traded his uncle's $200,000 account at FISC so that it made $15,000 monthly to send to the uncle; that he was trading his own and his mother's account at FISC; that he doubled his mother's account; that seven out of ten trades he did were profitable; that he placed a $300 stop loss on every trade and never lost more than $320 at a trade; and that Mr. Davis would make three to five percent return per month and double his account every two years.

71. FISC employees intimated that Cho was a master trader. Simmons told Alan Davis

prior to his investment that Cho made $20,000 monthly trading in Forex, and was "one of the best in the business;" that Cho was brought from the San Francisco office to "pick this office up" because of how well he did over there; and that he fired 17 out of the 25 traders at FISC "because they wouldn't obey how he wanted the trading practices done at the office there."

72. When Alan Davis opened his account through FISC, Cho told him that he would make three to five percent per month on his investment, and double it in two years.

73. Alan Davis testified that based upon what he had been told, he believed that Simmons and Cho were professional currency traders who could make sound investment decisions on his behalf.

74. Alan Davis relayed the information to his retired parents, F. Dean and Melba Davis, who relied on it to make their decision to invest through FISC.

75. When F. Dean, Melba, Alan and Debbie Davis met with Simmons at FISC to open F. Dean Davis' account, Simmons repeated that the account would earn three to five percent per month and double in two years; that they could lose no more than $300 per trade because of his use of stop loss orders; and that seven of ten trades he did made money.

76. Cho told F. Dean and Melba Davis that their money would earn three to five percent per month and double in two years, and told them that he would make sure that their account was traded properly.

77. Nineteen of twenty-one EVFL investor accounts opened through FISC lost money.

78. Experience as a commodity trader was not a prerequisite to enrolling in the training course.

79. Most trainees had no prior experience as commodity traders.

80. Generally, trainees lost money in the practice trading conducted as part of their training.

81. Simmons had never traded in commodities or commodity futures or options, nor was he ever registered to sell such products.

82. Simmons did not have a background or experience in foreign currency trading when he entered the FISC training class in January 1997.

83. Simmons never traded any EVFL accounts for any family relative.

84. Simmons never managed an account worth over $200,000 belonging to his uncle in the Midwest.

85. Simmons admitted that he knew of no blanket stop loss or limit order; that a stop loss order can only be placed on a specific buy or sell order; and that an order might not get executed in a volatile market.

86. Cho managed only seven or eight investor clients before he was employed by Tokyo.

87. Most of Cho's previous investors had lost money.

88. Cho managed less than ten investors while at Tokyo.

89. Most of Cho's investors at Tokyo had lost money.

90. Both of Cho's personal investor clients at FISC lost money.

91. Cho admitted that it was "probably not" likely that a Forex investor could make a three to five percent monthly return from trading.

92. FISC trader Dan Hoesch did not disclose to an offeree that Hoesch's only other client at FISC had just lost his entire $28,000 investment one month prior.

93. Respondents failed to disclose information about the business background and experience of EVFL and its principals to offerees.

94. Cho stated that FISC trader trainees were told that FISC does business with EVFL in Macau, and that EVFL does business with other offices in the United States and other countries.

95. According to Cho, if traders requested more information, he would provide them with a list of the names and titles of EVFL and EVGL officers and directors.

96. FISC trader Dan Hoesch testified that the list of names and titles was the only information about EVFL and its principals that he provided to the approximately thirty offerees he solicited.

97. Respondents failed to disclose financial statements reflecting the financial condition of EVFL.

98. Respondents failed to disclose how customer Forex orders were executed by EVFL.

99. Simmons stated that he was not sure what happened to a customer order relayed from

FISC to Macau because no one ever explained it to him.

100. Simmons told investor Alan Davis that orders from FISC were placed on the Chicago exchange.

101. Percy Lung Siu Hung ("Lung"), chief dealer at the EVFL Macau office since it opened in 1994, testified that he was responsible for order execution. Mr. Lung stated that every order received is sent outside EVFL, and that most orders from FISC were placed with only one company in Macau.

102. Lung claimed that he never placed a transaction for EVFL with a bank, and that there is an ordinance in Hong Kong restricting them from placing that type of order with any Hong Kong bank.

103. Respondents failed to disclose the terms under which interest was charged or paid on overnight positions, or the risk of loss to a customer account due to adverse interest or "premium" charges resulting from maintaining an overnight open position.

104. Respondents charged EVFL accounts with an overnight buy position in Deutsche marks, Swiss francs and Japanese yen, or an overnight sell position in Pound sterling would be charged interest each calendar day on a fixed percentage basis.

105. Accounts with an overnight sell position in the first three currencies would earn daily interest at a lesser rate than charged.

106. Respondents failed to explain that an overnight position on Wednesday is charged for three days, to cover weekend costs, even if a position was not held during a weekend.

107. Respondents failed to disclose that interest rates assessed were higher than interest rates paid by EVFL.

108. Respondents failed to disclose the risk of loss to investments from interest charges.

109. Cho was not aware of any trader explaining the FISC account statement to a prospective investor.

110. Respondents failed to disclose the location and use of investor funds after deposit with FISC and EVFL, while the funds were credited to investor accounts.

111. Investor funds were deposited into an EVFL account with Citibank in San Francisco,

California.

112. Respondents did not provide information regarding investor funds in the Citibank account between FISC's opening in 1996 and June 13, 1997, and after November 5, 1997.

113. Between June 13, 1997 and November 5, 1997, all wire transfers from the account were deposited in an EVFL Marine Midland Bank account in New York, New York, which received funds from companies throughout the world who have their accounts serviced by EVFL.

114. According to testimony, EVFL primarily used the account to receive and/or pay funds related to trading gains and/or losses at the companies it serviced and to pay other business-related expenses. EVFL stated that once investors' funds were deposited into that account, it became impossible to trace the funds.

115. Respondents failed to disclose EVFL and FISC policy that offers or sales of Forex trading accounts were not subject to state or federal securities law, and the risks to investors of non-compliance with investor protection provisions of those laws.

116. According to testimony, in 1996, when questioned by a trainee, a FISC marketing manager said that someone was in contact with the Commission, the Commission decided to take no action, and they were free to solicit.

117. The trainee stated that a week or so after his inquiry, the marketing manager showed him a no-action letter allegedly from the Division on Commission letterhead.

118. The Division presented evidence that the only Division letter regarding FISC or EVFL was a denial of a no-action request on October 17, 1997.

119. The no-action request, dated August 23, 1996, referred to "FISC's Proposed Business", failing to disclose that FISC was already offering and selling EVFL accounts in Arizona.

120. Respondents' no-action request was not disclosed to investors while it was pending or after its denial.

121. Tam assured Cho that there was "no problem" regarding the no-action letter.

122. One of the traders testified that when he was a FISC trainee in Summer 1996, he told Tam and the FISC marketing manager that FISC traders had to be licensed to solicit investors.

123. The trainee stated that Tam disagreed with him, and argued with him, so he brought in

a lawyer to talk with Mr. Tam regarding a licensing requirement.

124. Cho assured FISC trainees "that there is no direct regulation" and that they needed no license to trade currency.

125. Cho admitted that he did not explain the risks of non-regulation to traders or prospective clients.

126. Cho averred that if people asked specific questions, he admitted that EVFL could go out of business and take their money, but added that they probably would not; that they have been doing business for a long time, and they would not take off with the client's money.

127. Simmons admitted that he was not aware of insurance or other protection available for an account holder if FISC or EVFL closed down, or registration or licensing required for making the trading accounts available to the public.

128. Simmons stated that he never inquired why FISC was not licensed, and he was told that they did not need one.

129. Simmons stated that he did not volunteer to a prospective client that there was no licensing or registration requirement, or that deposits were not protected by any kind of regulatory insurance required for investors putting money on deposit.

130. Simmons did not know anything about the financial condition of EVFL.

131. In connection with their offers or sales of securities through FISC, Respondents directly or indirectly engaged in transactions, practices or courses of business which operated or would operate as a fraud or deceit upon offerees or investors within the meaning of A.R.S. § 44-1991, including but not limited to presenting EVFL and FISC salesman as professional currency traders able to make sound investment decisions on behalf of investors, while such salesmen had insufficient training and experience in Forex-related trading and made unsound investment decisions that caused substantial losses by investors.

132. Respondents operated FISC to raise investor funds for trading through EVFL.

133. Trainee traders were encouraged to raise funds from family and friends.

134. The recruiting of investors required continual recruiting of trader trainees.

135. Cho was brought in to run the FISC office to get clients for FISC.

136. Cho admitted that the purpose of the training program was to develop traders who would bring in new accounts.

137. These new accounts included investments from traders.

138. The classified advertisements placed by FISC referred to an expanding international firm – which was EVFL, not FISC with its one office in Phoenix.

139. The printed materials provided to trainees included an item stating in part:

> The odds of making money from Forex Trading are inconsistent. A fairly high proportion stop trading within 6 months because of excessive losses. Some traders are fortunate to do well at the beginning. Invariably, they become over confident and lose all their early profits. Because they have tasted limited success, they are likely to keep trading longer and lose more than somebody who has lost consistently from the beginning.
>
> Other than gambling, there is probably no human endeavor with such a low success rate that continue to attract such a large number of participants. (sic)

140. Cho agreed with the above extract.

141. Cho admitted that there was a high risk of traders losing money on their first accounts.

142. Cho admitted that he did not advise his trainees to disclose to prospective clients the likelihood that a new trader would lose investor money for the first accounts traded, either by copy of the above information or orally.

143. Cho stated that prospective investors were provided with the Brochure, which states that traders have the discipline and ability to make sound investment decisions, because he was told to do it that way. The Brochure was very similar to Tokyo's brochure, and Tam told him that it was basically the same thing as Tokyo's brochures.

144. Cho did not inform Alan and Debbie Davis, and F. Dean and Melba Davis, that their accounts were Simmons' first and second, respectively, and that there was a high risk that Simmons would lose money trading the accounts.

145. Cho did not inform F. Dean and Melba Davis at the time of their investment that Simmons had lost money in their son's account.

146. Cho did not inquire of F. Dean and Melba Davis whether they could afford to lose the money they had invested.

147. Cho told trainees that they could tell prospective investors that "we would try to make

3 to 5 or 4 to 5 percent a month" on their investment.

148. Cho told Tam on December 2, 1997 about Simmons' untrue representations regarding his trading history to Alan Davis.

149. Simmons was retained as FISC marketing manager until the office was closed on December 18, 1997.

150. Cheng has been the president, a director and one of two shareholders of FISC at all times relevant to this matter, and Executive Director of EVGL.

151. Cheng has been an EVGL director since May 2, 1994.

152. EVGL took over direct ownership of EVFL as its sole shareholder on August 1, 1997.

153. In 1994, DPS Global Management Ltd. ("DPS") purchased a one-half interest in Tokyo, which was assigned to Cheng as owner of DPS.

154. Tam testified that FISC came into being because Cheng and Yuen, two investors, were interested in owning an investment service company of the same type as Tokyo.

> And they want to invest and they asked us to try to manage it for them to make a profit.... So we promise to help them to build up the business office herein Phoenix because we feel that it is a potential market here in Phoenix. And they agreed that there is a potential market. So they invest the money and set up a company.

155. FISC's owners, Cheng and Yuen, provided $100,000 for start-up costs.

156. FISC's lease was signed on September 13, 1995, and FISC opened for business in April 1996.

157. Cheng and Scott Yuen, Yuen's husband, "loaned" $145,000 to FISC in 1996 to support the operation of FISC.

158. Tam consulted with FISC owners on major decisions, included hiring and terminating personnel.

159. Tam consulted with FISC owners on how business was doing.

160. Cheng possessed the actual power to directly or indirectly control or influence the general affairs and policy of FISC as officer, director and half-owner of FISC, and through DPS's half ownership of Tokyo.

161. Cheng exercised power over FISC by consulting with Tam and approving major

decisions affecting FISC.

162. Yuen was the secretary, treasurer, director, and one of two shareholders of FISC at all times relevant to this matter.

163. Yuen signed articles of incorporation and income tax returns on behalf of FISC.

164. Yuen signed the January 1, 1997 Agreement between FISC and Tokyo, and the Amendment to Agreement dated December 17, 1997, that terminated all agreements between FISC and EVFL.

165. As officer, director and half owner of FISC, Yuen possessed the actual power to directly or indirectly control or influence the general affairs and policy of FISC.

166. Yuen actually exercised that power over FISC by consulting with Tam and approving major decisions affecting FISC.

167. Tokyo was incorporated in California on November 21, 1991, and began operations on March 1, 1992.

168. Tam described Tokyo as a branch of EVFL.

169. Tokyo provided to FISC's prospective landlord a letter of reference from Tokyo's banker, and its federal and state tax returns for 1994.

170. Tokyo managed FISC from its inception until its closing.

171. Pursuant to the January 1, 1997 agreement between Tokyo and FISC, Tokyo received $3 per order settlement from FISC plus housing and travel expenses for Tam in return for providing management consulting services to FISC and handling settlement of FISC orders.

172. From March 1996 until January 1997, Garrett Tsang, a Tokyo employee, trained and supervised FISC operations personnel.

173. The January 1997 training class at FISC was taught by Tony Taniguchi, a Tokyo employee.

174. Tokyo twice loaned $10,000 to FISC to keep FISC in business.

175. The fixed employee compensation Tam received from Tokyo included his work for FISC.

176. Cho's duties at FISC were the same as at Tokyo, to generate business.

177. FISC's brochure and Addendum were substantially the same as that used by Tokyo.

178. The standard FISC introductory letter was the same as that used by Tokyo.

179. As manager of FISC, Tokyo was a controlling person by itself and collectively with Cheng, Yuen, Tam and Guo.

180. Tam was an employee and general manager of Tokyo.

181. Tam helped incorporate FISC, and was in charge of it from its inception.

182. Tam delivered paychecks to FISC and supervised the FISC operations clerks.

183. Tam made decisions on day-to-day operations of FISC without consulting its owners.

184. Tam consulted with FISC's investor-owners on major decisions.

185. Tam was Cho's only superior while Cho worked at FISC.

186. Tam told Cho when to place newspaper advertisements for trader applicants.

187. Cho stated that he talked with Tam before making every decision, that he never did anything without consulting Tam.

188. Tam monitored closely Cho's activities at FISC, and was aware of FISC's marketing and operations department activities.

189. During the period Simmons was marketing manager for FISC, Simmons reported to Tam and received direction from him.

190. Written complaints from investors were forwarded by Simmons to Tam.

191. As corporations act through agents, FISC was under management by Tokyo through Respondent Tam, who was a controlling person of FISC individually and collectively with Cheng, Yuen, Tokyo and Guo.

192. Guo has been Chief Executive Officer, Secretary, Chief Financial Officer and a Director of Tokyo.

193. Guo signed the 1992 and 1997 Statement by Domestic Stock Corporation filings by Tokyo with the California Secretary of State.

194. Guo signed the Fictitious Business Name Statement filings by Tokyo with the City and County of San Francisco.

195. Guo owned half of Tokyo's stock, and devoted 100 percent of his time to the business

of Tokyo.

196. Guo was a controlling person over FISC, individually and collectively with Cheng, Yuen, Tokyo and Tam.

197. Firgal Consultants Limited, a British Virgin Islands company originally incorporated in September 1993, was renamed EVFL on August 9, 1994, the same day that Sharma became its sole director.

198. Lung, chief dealer at the EVFL Macau office since it opened in 1994, stated that Wing, Tak and Cheng have been his superiors since before his company told him to move to Macau.

199. No evidence of the existence of any EVFL corporate officers was disclosed, and EVFL's Articles of Association do not mandate the appointment of officers.

200. Sharma was a Director of EVFL until August 1, 1997.

201. Sharma was sole shareholder of EVFL until August 1, 1997, when he resigned as EVFL Director and all his shares were transferred to EVGL.

202. On behalf of EVFL, Sharma signed the agreement between it and FISC dated January 1, 1997.

203. The Customer Agreements signed by investors Alan and Debbie Davis and F. Dean and Melba Davis and Michael Noriega were executed on behalf of EVFL by Sharma.

204. Sharma and Tak had signatory power on all of EVFL's bank accounts.

205. Investor withdrawals of funds from EVFL trading accounts required written authorization from Sharma and Tak.

206. Sharma was a controlling person of EVFL at all relevant times, individually and collectively with EVGL.

207. EVGL was incorporated in the British Virgin Islands as an International Business Company on March 16, 1994.

208. EVGL has issued only one share of stock in the form of a bearer stock certificate dated May 1, 1994, and has not disclosed the identity of the holder or custodian of the bearer certificate.

209. Cheng and Wing have been EVGL's directors since May 2, 1994.

210. On August 9, 1994, EVFL was incorporated in Hong Kong and renamed Eastern

Traders (HK) Ltd; and Firgal Consultants Ltd., a British Virgin Islands company, was renamed EVFL, with Sharma as its director and sole shareholder.

211. EVGL directors Cheng and Wing became the two directors of the Hong Kong EVFL, with Cheng as its corporate secretary.

212. The EVFL Company Profile brochure describes EVFL as a member of the Eastern Vanguard Group.

213. Cheng became President, a director and one of two shareholders of FISC.

214. EVGL and EVFL share the same chief administrator, Alwin Yam.

215. Mr. Yam replaced Sharma as EVFL Director on August 1, 1997, and replaced Sharma as a signatory on all EVFL bank accounts in October 1997.

216. Wing, as chairman of EVGL, appointed Mr. Yam as EVFL director, and authorized the share transfer.

217. Mr. Yam described EVGL as a holding company for EVFL, among others.

218. Tam described Wing to Cho as the "big boss".

219. Wing was chairman of EVGL at all relevant times.

220. Wing was EVGL director since May 2, 1994.

221. Tak was deputy Chairman of EVGL at all relevant times, and became EVGL Secretary on August 1, 1994.

222. As corporations act through their agents, EVGL was a controlling person of EVFL through Sharma, Wing, and Tak, who were controlling persons individually and collectively.

223. In connection with the offer or sale of securities within and/or from Arizona described above, Respondents directly or indirectly made untrue statements of material fact and omitted to state material facts which were necessary in order to make the statements made not misleading in light of the circumstances under which they were made, in violation of A.R.S. § 44-1991, including but not limited to the following:

(a) Respondents made untrue statements that EVFL or FISC salesmen were professional currency traders able to make sound investment decisions on behalf of investors, while in fact such salesman had insufficient training and experience in Forex-related trading and made unsound investment decisions that caused substantial losses by investors;

(b) Respondents failed to disclose the business experience of EVFL and its principals;

(c) Respondents failed to disclose financial statements reflecting the financial condition of EVFL;

(d) Respondents failed to disclose how customer Forex orders were executed by EVFL;

(e) Respondents failed to disclose the terms under which interest was charged or paid on overnight positions, or the risk of loss to a customer account due to adverse interest or "premium" charges resulting from maintaining an overnight position;

(f) Respondents failed to disclose the location and use of investor funds after deposit with FISC and EVFL and while such funds were credited to investor accounts; and

(g) Respondents failed to disclose the EVFL and FISC policy that their offer or sale of FOREX trading accounts were not subject to state or federal securities laws, and the attendant risks to investors of non-compliance with the investor protection provisions of those laws.

224. In connection with their offers or sales of securities through FISC, Respondents directly or indirectly engaged in transactions, practices or courses of business which operated or would operate as a fraud or deceit upon offerees or investors within the meaning of A.R.S. § 44-1991, including but not limited to presenting EVFL and FISC salesmen as professional currency traders able to make sound investment decisions on behalf of investors, while such salesmen had insufficient training and experience in Forex-related trading and made unsound investment decisions that caused substantial losses by investors.

225. The Division recommended that pursuant to A.R.S. § 44-2032, FISC, EVFL, Simmons and Cho should be ordered to permanently cease and desist from violating A.R.S. §§ 44-1841, 1842 and 1991, and Sharma, Cheng, Yuen, Tokyo and Tam should be ordered to permanently cease and desist from violating A.R.S. § 44-1991.

226. The Division recommended that pursuant to A.R.S. § 44-2032(1) and A.A.C. R14-4-308(C)(1) and (B)(1)(b), Respondents should be ordered to pay monetary restitution to investors as follows:

FISC and EVFL, jointly and severally together with controlling persons Cheng, Yuen, Tokyo, Tam, Guo, Sharma, EVGL, Wing and Tak should pay the total amount of $336,086.41 to those investors who suffered losses as shown on Exh. S-138, together with interest pursuant to A.A.C. R14-4-308 from the dates of investment at the statutory rate of ten percent per annum;

Simmons should pay the total amount of $99,447.69, together with interest pursuant to A.A.C. R14-4-308 from the dates of investment at the statutory rate of ten percent per annum, or which $3,753.80 plus interest should be paid jointly and severally with the above Respondents to Peter Baker, who invested while Simmons was FISC marketing manager, and $95,693.80 plus interest should be paid jointly and severally with Cho and the above Respondents to Simmons' investor clients Alan and Debbie Davis, Dean and Melba Davis, Michael Noriega, and Van and Ruth Shumway, for their losses as shown on Exh. S-138;

Cho should pay the total amount of $320,872.58, together with interest pursuant to A.A.C. R14-4-308 from the dates of investment at the statutory rate of ten percent per annum, of which $225,178.69 plus interest should be paid jointly and severally with the above Respondents to all except Simmons' clients who invested while Cho was FISC marketing manager, and $95,693.89 plus interest should be paid jointly and severally with the above Respondents and Simmons to Simmons' clients, all for their losses as shown on Exh. S-138.

227. The Division recommended that pursuant to A.R.S. § 44-2032 and to correct the conditions resulting from Respondents' violations of the SAA, all written agreements between EVFL and its accountholders who invested through FISC should be ordered rescinded.

228. The Division recommended that pursuant to A.R.S. § 44-2036(A), Respondents should be assessed administrative penalties in an amount not to exceed five thousand dollars for each SAA violation.

229. The Division claimed that FISC, EVFL, Simmons and Cho violated the antifraud and both registration provisions of the SAA in connection with each sale of an EVFL security for which the Division is seeking restitution.

230. The Division claimed that Sharma, Cheng, Yuen, Tokyo and Tam repeatedly violated the SAA's antifraud provision in connection with multiple sales of EVFL securities. The Division alleged eight separate acts that each constituted a separate violation of the SAA antifraud provision in connection with each sale of an EVFL security.

231. The Division alleged that FISC and EVFL made untrue statements of material fact to the Commission in their no-action letter request to the Division dated August 23, 1996.

232. The Division requested the following administrative penalties:

(a) Twenty-one investors purchased EVFL securities through FISC, each purchase in violation of the antifraud and both registration provisions of the SAA. The Division alleged eight separate acts that each violated the antifraud provision alone in connection with each sale. The Division requested administrative penalties against FISC and EVFL in the amount of $150,000 each;

(b) For eight antifraud violations in connection with each sale of an EVFL security

to fifteen investors through FISC before August 1, 1997, Sharma should be assessed $100,000;

(c) For eight antifraud violations in connection with each sale of an EVFL security to six investors, together with two non-registration violations for each sale, Simmons should be assessed $25,000;

(d) For eight antifraud violations in connection with each sale of an EVFL security to eighteen investors, together with two non-registration violations for each sale, Cho should be assessed $100,000;

(e) For eight antifraud violations in connection with each sale of an EVFL security to twenty one investors, Cheng should be assessed $100,000;

(f) For eight antifraud violations in connection with each sale of an EVFL security to twenty one investors, Yuen should be assessed $100,000;

(g) For eight antifraud violations in connection with each sale of an EVFL security to twenty one investors, Tokyo should be assessed $100,000;

(h) For eight antifraud violations in connection with each sale of an EVFL security to twenty one investors, Tam should be assessed $100,000; and

233. Any other relief the Commission deems appropriate and authorized by law.

CONCLUSIONS OF LAW

1. The Commission has jurisdiction over this matter pursuant to Article XV of the Arizona Constitution and A.R.S. § 44-1801, *et seq*.

2. For purposes of the SAA, "Security" includes a "commodity investment contract". A.R.S. § 44-1801(23).

3. "Commodity investment contract" is defined in relevant part as "any account, agreement or contract for the purchase or sale, primarily for speculation or investment purposes and not for use or consumption by the offeree or purchaser, of one or more commodities ... Any commodity investment contract offered or sold, in the absence of evidence to the contrary, is presumed to be offered or sold for speculation or investment purposes." A.R.S. § 44-1801(6).

4. "Commodity" is defined in relevant part to include "any foreign currency." A.R.S. § 44-1801(3).

5. A commodity investment contract security under the SAA includes any account, agreement or contract for the purchase or sale, primarily for speculation or investment purposes, of any foreign currency.

6. The investments offered by FISC, EVFL, Simmons and Cho were securities within the

meaning of A.R.S. § 44-1801.23.

7. The securities were not registered under A.R.S. §§ 44-1871 through 44-1875, 44-1891 through 44-1900 or 44-1902; were not exempt securities under A.R.S. § 44-1843 or § 44-1843.01; were not offered or sold in exempt transactions under A.R.S. § 44-1844 and were not securities exempt under any rule or Order promulgated by the Commission.

8. The actions and conduct of FISC, EVFL, Simmons and Cho constitute the offer and/or sale of securities within the meaning of A.R.S. §§ 44-1801.13 and 44-1801.19.

9. FISC, EVFL, Simmons and Cho offered and sold unregistered securities within or from Arizona in violation of A.R.S. § 44-1841.

10. FISC, EVFL, Simmons and Cho offered and/or sold securities within or from Arizona without being registered as a dealer or salesman in violation of A.R.S. § 44-1842.

11. In connection with the offer and sale of the above securities, FISC, EVFL, Simmons and Cho violated the antifraud provisions of A.R.S. § 44-1991.

12. During the foregoing violations, Cheng, Yuen, Tokyo, Tam and Guo directly or indirectly controlled FISC within the meaning of A.R.S. § 44-1999, and are jointly and severally liable with FISC for violations of A.R.S. § 44-1991.

13. During the foregoing violations, Sharma, EVGL, Wing and Tak directly or indirectly controlled EVFL within the meaning of A.R.S. § 44-1999, and are jointly and severally liable for violations of A.R.S. § 44-1991.

14. Pursuant to A.R.S. § 44-2032 and to correct the conditions resulting from Respondents' violations of the SAA, all written agreements between EVFL and its accountholders who invested through FISC should be rescinded.

15. FISC, EVFL, Simmons and Cho should be restrained pursuant to A.R.S. § 44-2032 from any future violations of A.R.S. §§ 44-1841, 44-1842, and 44-1991, and all other provisions of the Act.

16. Sharma, Cheng, Yuen, Tokyo and Tam should be restrained pursuant to A.R.S. § 44-2032 from any future violations of A.R.S. § 44-1991, and all other provisions of the Act.

17. Respondents should be ordered to pay restitution in the manner set forth below

pursuant to A.R.S. § 44-2032 and A.A.C. R14-4-308.

18. Respondents should be assessed administrative penalties pursuant to A.R.S. § 44-2036 for violations of the Act.

ORDER

IT IS THEREFORE ORDERED that pursuant to the authority granted to the Commission under A.R.S. §§ 44-2032, 44-1972 and A.A.C. R14-4-307, Respondents Forex Investment Services Corporation, Eastern Vanguard Forex Ltd., Simmons and Cho, their agents, servants, employees, successors, assigns, and those persons in active concert or participation with them, shall cease and desist from the following and any other violations of the Arizona Securities Act:

> 1. Offering to sell or selling securities within or from the State of Arizona, unless the securities are registered with the Commission pursuant to Articles VI or VII of the Act, an exemption under the Act is applicable, or a notice filing has been made under A.R.S. § 44-3321;
>
> 2. Offering to sell or selling securities within or from the State of Arizona unless prior registration as a dealer or salesman is obtained under Article IX of the Act, or an exemption from registration is applicable; and
>
> 3. Offering to sell or selling securities within or from the State of Arizona through material misrepresentations or omissions, and/or through courses of business that would operate as a fraud or deceit, in violation of A.R.S. § 44-1991.

IT IS FURTHER ORDERED that pursuant to the authority granted to the Commission under A.R.S. §§ 44-2032, 44-1972 and A.A.C. R14-4-307, Respondents Sharma, Cheng, Yuen, Tokyo and Tam, their agents, servants, employees, successors, assigns, and those persons in active concert or participation with them, shall cease and desist from the following and any other violations of the Arizona Securities Act:

> Offering to sell or selling securities within or from the State of Arizona through material misrepresentations or omissions, and/or through courses of business that would operate as a fraud or deceit, in violation of A.R.S. § 44-1991.

IT IS FURTHER ORDERED that all written agreements between Eastern Vanguard Forex Ltd. and its accountholders who invested through Forex Investment Services Corporation shall be rescinded.

IT IS FURTHER ORDERED that pursuant to the authority granted to the Commission under A.R.S. § 44-2032,

Forex Investment Services Corporation and Eastern Vanguard Forex Ltd., jointly and severally together with controlling persons Cheng, Yuen, Tokyo, Tam, Guo, Sharma, Eastern Vanguard Group Limited, Wing and Tak shall pay the total amount of $336,086.41 to those investors who suffered losses, together with interest pursuant to A.A.C. R14-4-308 from the dates of investment at the statutory rate of ten percent per annum;

Simmons shall pay the total amount of $99,447.69, together with interest pursuant to A.A.C. R14-4-308 from the dates of investment at the statutory rate of ten percent per annum, or which $3,753.80 plus interest should be paid jointly and severally with the above Respondents to Peter Baker, who invested while Simmons was Forex Investment Services Corporation marketing manager, and $95,693.80 plus interest shall be paid jointly and severally with Cho and the above Respondents to Simmons' investor clients Alan and Debbie Davis, Dean and Melba Davis, Michael Noriega, and Van and Ruth Shumway, for their losses;

Cho shall pay the total amount of $320,872.58, together with interest pursuant to A.A.C. R14-4-308 from the dates of investment at the statutory rate of ten percent per annum, of which $225,178.69 plus interest should be paid jointly and severally with the above Respondents to all except Simmons' clients who invested while Cho was Forex Investment Services Corporation marketing manager, and $95,693.89 plus interest shall be paid jointly and severally with the above Respondents and Simmons to Simmons' clients, all for their losses.

Restitution shall be made jointly and severally with any other Respondent who may be ordered to pay restitution to investors, as set forth in the records obtained by the Securities Division, pursuant to A.A.C. R14-4-3408, subject to any set off for repayments or income received upon the sale of the security made prior to the effective date of this Decision, as verified by the Director of the Securities Division, pursuant to A.A.C. R14-4-308.C; payments are to be made in full within ninety days from the effective date of this Decision.

IT IS FURTHER ORDERED that restitution funds shall be paid to the Arizona Attorney General's Office, and shall be deposited in a trust account with a federally insured financial institution. The funds shall be disbursed pro rata in accordance with the outstanding balances to those investors entitled to restitution.

IT IS FURTHER ORDERED that pursuant to the authority granted to the Commission under A.R.S. § 44-2036, administrative penalties shall be made as follows, with payment to be made in full within one hundred eighty days from the effective date of this Decision, payable to the State Treasurer for deposit in the General Fund of the State of Arizona:

(a) For eight antifraud violations in connection with each sale of an Eastern Vanguard Forex Ltd. security to twenty-one investors in violation of the antifraud and both registration provisions of the SAA in connection with purchases of Eastern Vanguard Forex Ltd. securities through Forex Investment

Services Corporation, Forext Investment Services Corporation and Eastern Vanguard Forex Ltd. shall be assessed $150,000 each;

(b) For eight antifraud violations in connection with each sale of an Eastern Vanguard Forex Ltd. security to fifteen investors through Forex Investment Services Corporation before August 1, 1997, Sharma shall be assessed $100,000;

(c) For eight antifraud violations in connection with each sale of an Eastern Vanguard Forex Ltd. security to six investors, together with two non-registration violations for each sale, Simmons shall be assessed $25,000;

(d) For eight antifraud violations in connection with each sale of an Eastern Vanguard Forex Ltd. security to eighteen investors, together with two non-registration violations for each sale, Cho shall be assessed $100,000;

(e) For eight antifraud violations in connection with each sale of an Eastern Vanguard Forex Ltd. security to twenty one investors, Cheng shall be assessed $100,000;

(f) For eight antifraud violations in connection with each sale of an Eastern Vanguard Forex Ltd. security to twenty one investors, Yuen shall be assessed $100,000;

(g) For eight antifraud violations in connection with each sale of an Eastern Vanguard Forex Ltd. security to twenty one investors, Tokyo shall be assessed $100,000; and

(h) For eight antifraud violations in connection with each sale of an Eastern Vanguard Forex Ltd. security to twenty one investors, Tam shall be assessed $100,000;

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IT IS FURTHER ORDERED that if restitution is made within ninety days, administrative penalties shall be reduced to $20,000 for each Respondent.

IT IS FURTHER ORDERED that this Decision shall become effective immediately.

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

CHAIRMAN COMMISSIONER COMMISSIONER

IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive Secretary of the Arizona Corporation Commission, have hereunto set my hand and caused the official seal of the Commission to be affixed at the Capitol, in the City of Phoenix, this _____ day of _____, 2000.

BRIAN C. McNEIL
EXECUTIVE SECRETARY

DISSENT _____
BMB:bbs

SERVICE LIST FOR: FOREX INVESTMENT SERVICES CORPORATION, EASTERN VANGUARD FOREX LTD., EASTERN VANGUARD GROUP LIMITED, K. (DAVID) SHARMA, SAMMY LEE CHUN WING, PETER SUEN SUK TAK, MICHAEL E. CHO, TO FAI CHENG, JEAN YUEN, Y & T INC. DBA TOKYO INTERNATIONAL INVESTMENT LTD, WING MING TAM, GUO QUAN ZHANG, AND JAMES CHARLES SIMMONS, JR.

DOCKET NO. S-03177A-98-0000

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