

ORIGINAL

NEW APPLICATION



0000076275

RECEIVED

2007 SEP 13 P 4: 13

AZ CORP COMMISSION
BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

MIKE GLEASON, Chairman
WILLIAM A. MUNDELL
JEFF HATCH-MILLER
KRISTIN K. MAYES
GARY PIERCE

Arizona Corporation Commission

DOCKETED

SEP 13 2007

DOCKETED BY

In the matter of:
KENNETH HOWARD FRALEIGH and LINDA
JEAN FRALEIGH, husband and wife
Respondents.

DOCKET NO. S-20551A-07-0521

NOTICE OF OPPORTUNITY FOR
HEARING REGARDING PROPOSED
ORDER TO CEASE AND DESIST,
ORDER FOR RESTITUTION, FOR
ADMINISTRATIVE PENALTIES AND
FOR OTHER AFFIRMATIVE ACTION

NOTICE: EACH RESPONDENT HAS 10 DAYS TO REQUEST A HEARING

EACH RESPONDENT HAS 30 DAYS TO FILE AN ANSWER

The Securities Division ("Division") of the Arizona Corporation Commission ("Commission") alleges that KENNETH HOWARD FRALEIGH ("FRALEIGH" or "RESPONDENT") has engaged in acts, practices and transactions, which constitute violations of the Securities Act of Arizona, A.R.S. § 44-1801 *et seq.* ("Securities Act").

I. JURISDICTION

1. The Commission has jurisdiction over this matter pursuant to Article XV of the Arizona Constitution and the Securities Act.

II. RESPONDENTS

2. At all times material hereto, FRALEIGH was a resident of Arizona and was not registered as a securities salesperson.

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26

1 McCleod, James Duncan, Hendrix Montecastro and Charlie Choi, organized and attended the
2 seminars.

3 8. RESPONDENTS agreed to invest with PWM in May 2005. By August 2006,
4 RESPONDENTS had purchased five properties through PWM.

5 9. To become a client of PWM required adherence to PWM's three rules which, according to
6 FRALEIGH, were, "They make all decisions, whatever they say I do, and it's a three-year
7 commitment."

8 10. After agreeing to invest, FRALEIGH began to offer family members, co-workers, members
9 of his church and others an opportunity to invest through PWM and its related entities.

10 11. At all times material hereto, FRALEIGH was employed as a facility manager by the United
11 States Air Force at Davis-Monthan Air Force Base in Tucson, Arizona.

12 12. FRALEIGH was designated as a "referral partner" by PWM and he provided prospective
13 investors with PWM business cards printed with his name. As part of his responsibilities as a
14 referral partner, FRALEIGH acted as a liaison between California representatives of PWM and
15 investors whom FRALEIGH had recruited into the program.

16 13. FRALEIGH's sales activities included sharing with prospective investors that he had
17 invested with PWM, assisting with organizing the investment seminars, recruiting prospective
18 investors to attend and providing his own testimonial at the seminars to those in attendance.

19 14. FRALEIGH's ability to recruit prospective investors from Tucson resulted in him becoming
20 PWM's primary source for Tucson area investors.

21 15. In exchange for FRALEIGH's services as a "referral partner," he was compensated by PWM
22 and its related entities.

23 16. FRALEIGH failed to inform prospective investors that he was being compensated for his
24 recruitment and referral of prospective investors.

25

26

1 17. The security initially offered to prospective investors by FRALEIGH was an investment
2 contract comprised of residential real estate (“real estate program”) through a company known as
3 Stonewood Consulting, Inc. (“Stonewood”). Beginning in early 2006, as a result of Stonewood’s
4 poor reputation in the real estate community, FRALEIGH directed prospective investors to purchase
5 securities issued by PWM. Prospective investors were offered an opportunity to participate in a
6 program in which PWM (either directly or through an affiliated entity) would use the investor’s
7 credit to buy real estate.

8 18. PWM and its related entities located the real estate to be purchased, arranged the financing,
9 obtained the appraisals and ultimately purchased the residential real estate to be held in the investor’s
10 name. FRALEIGH told prospective investors that the properties being purchased would be rented
11 until such time as their value appreciated to the point that they could then be sold with the investors
12 realizing the increase in the value of the real estate.

13 19. Prospective investors had no input into the initial selection of the properties to be purchased,
14 the renters who would occupy the properties, the property maintenance company, the title company,
15 the mortgage company or the appraiser. Likewise, investors were not responsible for deciding when
16 the homes would be sold. In most instances, prospective investors did not see the appraisals
17 performed on the properties being purchased in their names. The lack of investor input resulted from
18 investors’ adherence to PWM’s three rules.

19 20. FRALEIGH told prospective investors that PWM would make monthly payments to the
20 investor to cover mortgage payments and expenses. The majority of individuals who invested in the
21 real estate program purchased multiple residences.

22 21. FRALEIGH had not obtained nor sought any financial information from PWM and its related
23 entities that would have allowed him to represent to prospective investors that PWM or its related
24 entities were in a position to continue to make the monthly payments to cover mortgage payments
25 and expenses on properties purchased in the names of new investors.

26

1 22. FRALEIGH also offered prospective investors an opportunity to invest cash, which they were
2 encouraged to obtain by refinancing the existing mortgages on their primary residence. FRALEIGH
3 informed prospective investors that this cash would be invested in securities such as stocks, bonds,
4 precious metals, or other unspecified investments. Prospective investors were again promised
5 monthly payments in an amount sufficient to cover the monthly payments on these newly refinanced
6 mortgages. Several investors refinanced the existing mortgages on their primary residence and some
7 investors obtained second mortgages on their primary residence.

8 23. The transactions to close the purchase of real estate by investors through the real estate
9 program and the refinancing by investors of their principal residence were structured to generate
10 excess funds that would be wired directly to PWM or its related entities.

11 24. PWM and its related entities ceased making payments to investors to cover their debt
12 payments in late 2006. Numerous investors now face foreclosure proceedings on the multiple
13 properties purchased in their names as well as their principal residences.

14 25. In addition to residential real-estate investments and in an effort to raise additional cash to
15 offset the effects of the slowing real estate market, PWM representatives created an investment fund
16 called Total Return Fund, L.L.C. ("TRF"). In the summer of 2006, PWM began to apply for credit
17 cards and/or lines of credit in investors' names. In many instances, application was made without the
18 prior consent of the investor. FRALEIGH then offered prospective investors an opportunity to invest
19 in securities through TRF. To generate the cash required to invest with TRF, FRALEIGH
20 encouraged investors to obtain cash advances against the credit cards or the lines of credit, and to
21 invest the cash in TRF. TRF was described to investors as a short-term investment opportunity
22 offering an extremely high return. Several investors opened credit card accounts and lines of credit
23 and requested cash advances and loan amounts which were subsequently forwarded to PWM and it
24 related entities such as TRF.

25
26

1 26. FRALEIGH also offered securities in the form of unspecified foreign currency through an
2 entity known as Jovane Investments. Toward the end of 2006, investors were asked to liquidate their
3 retirement savings and to use those funds to purchase an investment involving foreign currency.
4 Among other things, Jovane representatives told investors that the opportunity promised an 8:1
5 return in six months. To date, investors have not received the promised return on their investment in
6 foreign currency.

7 **IV. VIOLATION OF A.R.S. § 44-1841**

8 **(Offer or Sale of Unregistered Securities)**

9 27. From on or about May 2005, FRALEIGH offered and sold securities in the form of
10 investment contracts, within or from Arizona, in violation of A.R.S. §44-1841.

11 28. The securities referred to above were not registered pursuant to the provisions of Articles 6 or
12 7 of the Securities Act.

13 29. This conduct violates A.R.S. § 44-1841.

14 **V. VIOLATION OF A.R.S. § 44-1842**

15 **(Transactions by Unregistered Dealers or Salesmen)**

16 30. FRALEIGH offered or sold securities within or from Arizona, while not registered as a dealer
17 or salesman pursuant to the provisions of Article 9 of the Securities Act.

18 31. This conduct violates A.R.S. §44-1842.

19 **VI. VIOLATION OF A.R.S. § 44-1991**

20 **(Fraud in Connection with the Offer or Sale of Securities)**

21 32. In connection with the offer or sale of securities within or from Arizona, FRALEIGH directly
22 or indirectly: (i) employed a device, scheme or artifice to defraud; (ii) made untrue statements of
23 material fact or omitted to state material facts which were necessary in order to make the statements
24 made not misleading in light of the circumstances under which they were made; and (iii) engaged in
25
26

1 transactions, practices or courses of business which operated or would operate as a fraud or deceit
2 upon offerees and investors. FRALEIGH's conduct includes, but is not limited to, the following:

3 a) Failing to inform prospective investors that he was being compensated for his sales
4 activities; and

5 b) Failing to provide prospective investors with any salient financial and/or other
6 background information about the companies offering the investment opportunities he was
7 promoting; and

8 c) Failing to fully disclose to prospective investors the risks associated with the
9 investment programs he was promoting; and

10 d) Failing to inform prospective investors that Maurice McCleod, the managing member
11 of Pacific Wealth Management, was his son in law.

12 33. This conduct violates A.R.S. § 44-1991.

13 **VII. REQUESTED RELIEF**

14 The Division requests that the Commission grant the following relief against
15 Respondents:

16 1. Order FRALEIGH to permanently cease and desist from violating the Securities Act,
17 pursuant to A.R.S. §44-2032;

18 2. Order FRALEIGH to take affirmative action to correct the conditions resulting from
19 his acts, practices or transactions, including a requirement to make restitution pursuant to A.R.S.
20 §44-2032;

21 3. Order FRALEIGH to pay the state of Arizona administrative penalties of up to five
22 thousand dollars (\$5,000) for each violation of the Securities Act, pursuant to A.R.S. §44-2036;

23 4. Order that the marital community of FRALEIGH and RESPONDENT SPOUSE be
24 subject to any order of restitution, rescission, administrative penalties, or other appropriate
25 affirmative action pursuant to A.R.S. §25-215; and
26

1 Notice. Filing instructions may be obtained from Docket Control by calling (602) 542-3477 or on
2 the Commission's Internet web site at <http://www.azcc.gov/Divisions/Hearings/Docket.asp>

3 Additionally, RESPONDENT or RESPONDENT SPOUSE must serve the Answer upon
4 the Division. Pursuant to A.A.C. R14-4-303, service upon the Division may be made by mailing
5 or by hand-delivering a copy of the Answer to the Division at 1300 West Washington, 3rd Floor,
6 Phoenix, Arizona, 85007, addressed to William W. Black.

7 The Answer shall contain an admission or denial of each allegation in this Notice and the
8 original signature of each Respondent or Respondents' attorney. A statement of a lack of sufficient
9 knowledge or information shall be considered a denial of an allegation. An allegation not denied
10 shall be considered admitted.

11 When RESPONDENT or RESPONDENT SPOUSE intends in good faith to deny only a
12 part or a qualification of an allegation, RESPONDENT or RESPONDENT SPOUSE shall specify
13 that part or qualification of the allegation and shall admit the remainder. RESPONDENT and
14 RESPONDENT SPOUSE waive any affirmative defense not raised in the answer.

15 The officer presiding over the hearing may grant relief from the requirement to file an
16 Answer for good cause shown.

17 Dated this 13th day of September, 2007.

18 

19 _____
20 Mark Dinell
21 Assistant Director of Securities
22
23
24
25
26