

WILLIAM A. MUNDELL
CHAIRMAN

JIM IRVIN
COMMISSIONER

MARC SPITZER
COMMISSIONER



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ARIZONA CORPORATION COMMISSION

OPEN MEETING ITEM
MEMORANDUM

TO: Chairman William A. Mundell
Commissioner Jim Irvin
Commissioner Marc Spitzer

FROM: Mark Sendrow *MS*
Director of Securities

DATE: September 18, 2001

RE: Kenneth Eugene Schaub, *et al.*, S-03443A-01-0000

CC: Brian C. McNeil, Executive Secretary

NEW

AZ CORP COMMISSION
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Accompanying this memorandum is a proposed Order to Cease and Desist, Order of Revocation, Order for Administrative Penalties, and Consent to Same ("Consent Order"), regarding Kenneth Eugene Schaub and Investment Planners of America, Inc. ("IPA").

Mr. Schaub has been a Arizona-licensed mortgage broker for approximately 25 years. He is president, chief executive officer and 49% owner of IPA, an Arizona corporation formed in 1993, which has been and is in the business of managing real estate limited liability companies.

Mr. Schaub became an Arizona-registered securities salesman in or about 1988. During the period relevant to the Consent Order, Mr. Schaub was associated with Royal Alliance Associates, Inc. ("Royal Alliance") for about three months, then with Raymond James Financial Services, Inc. ("Raymond James") for about nine months, until his termination on or about March 23, 2000.

Between April and December 1999, Mr. Schaub and IPA raised about \$7 million from (mostly Arizona) investors, for a company known as American Business Funding Corporation ("ABF"). ABF was in the business of factoring accounts receivable for small to medium-sized businesses. ABF presented its proposal as a "business opportunity," but in fact ABF was issuing unregistered securities in the form of investment contracts. ABF filed for reorganization under Chapter 11 of the United States Bankruptcy Code on February 24, 2000, amid allegations that about \$17 million had been misappropriated from the company by one or more of its three owners, and that

the business was operating as a Ponzi scheme. This event led to Mr. Schaub's termination by Raymond James, for having engaged in undisclosed outside business ("selling away").

The Division first received information concerning the above facts on or about July 5, 2000, when Mr. Schaub filed an application to become a licensed investment adviser representative in Arizona. Mr. Schaub disclosed his involvement with ABF, and ABF's bankruptcy, as part of his investment adviser representative application. Mr. Schaub fully cooperated with the Division's subsequent investigation regarding ABF, which revealed the additional facts summarized here.

Mr. Schaub and IPA sold about \$7 million in ABF investment contracts to 18 investors. Mr. Schaub supplied documentation to the Division supporting the conclusion that his investors were wealthy persons with substantial experience evaluating various kinds of investments, including securities and real estate loans, although they appear to have had no prior experience with accounts receivable factoring. Mr. Schaub did not receive or control any investor money; checks were made payable to and delivered to ABF. The investors were told to expect a return of approximately 12% per annum on their invested funds, an expectation that appeared reasonable in light of the company's claimed performance. Mr. Schaub investigated the business, including making visits to ABF's offices and examining the documents allegedly created and used in effecting particular factoring transactions, both before beginning to raise funds for ABF and during the period when he was raising funds. In addition to selling the investment to others, Mr. Schaub invested \$164,000 of his own money in ABF investment contracts.

In early 2000, Mr. Schaub and others learned that one of ABF's owners might have been perpetrating a fraud. Among other things, ABF's controller and "independent" CPA (whose only client was ABF) both executed affidavits admitting that they had cooperated with Angelo Tullo, one of ABF's three owners, in fabricating documentation concerning factoring business that never had existed. As mentioned above, discovery of the alleged fraud led to a Chapter 11 filing and reorganization of the business under new management.

Prior to the filing of the bankruptcy petition, Mr. Schaub's investors had received returns on their investments from ABF, leaving a net \$6.4 million invested. Pursuant to the plan of reorganization approved by the Bankruptcy Court on November 20, 2000 (the "Plan"), this net amount was treated as "Allowed Investor Claims." The holders of Allowed Investor Claims received an interest in a promissory note issued by the reorganized entity, New Horizon Capital, LLC ("NHC"), which is expected to pay the Allowed Investor Claims in full over a period of ten years from the effective date of the Plan, including interest at an annual rate of 7%. The investors also own 55% of the equity interests in NHC, and they are beneficiaries of a litigation trust that was formed to pursue, among other things, the investors' claims against Angelo Tullo and others. NHC is to advance all attorneys' fees and costs of prosecuting the claims.

During the pendency of the Chapter 11 case, Mr. Schaub provided debtor-in-possession financing to enable the company to continue as a going concern and to expand its profitable factoring business. Mr. Schaub borrowed approximately \$1.8 million, secured by his personal guarantee, liens on virtually all of his personal assets, and a term life insurance policy on his life naming the lender as beneficiary. Mr. Schaub used the \$1.8 million to fund a loan to the debtor-

in-possession, pursuant to terms approved as "fair" by the Bankruptcy Court. He is obligated to pay about \$29,000 per month in interest with respect to this financing.

In addition, prior to and during the pendency of the Chapter 11 case, Mr. Schaub retained the law firm of Cochran & Dahl, P.C., to represent the interests of his investors. The total amount billed by the firm for this representation was approximately \$83,240. Mr. Schaub still owes about \$25,000 in legal fees to the firm on account of this representation, and he is obligated to pay approximately \$3,000 per month on account of this debt.

The proposed Consent Order would order Mr. Schaub and IPA to cease and desist from violating the Arizona Securities Act, and would revoke Mr. Schaub's securities salesman registration. In addition, both respondents agree not to apply to the state of Arizona for registration as a securities dealer or salesman, or for licensure as an investment adviser or investment adviser representative, at any time in the future. Further, the proposed Consent Order would direct Mr. Schaub, IPA, and the marital community of Ken and Donna Schaub, jointly and severally, to pay an administrative penalty of \$25,000: \$2,500 on the effective date of the Consent Order and the remainder in installments over a period of 36 months.

The Division believes that the proposed Consent Order, together with the actions already taken by the Bankruptcy Court, protect the interests of investors and serve the best interests of the people of Arizona. The Division requests that the Commission approve the proposed Consent Order.

Originator: Amy Leeson

AG: Moira McCarthy

I.

FINDINGS OF FACT

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3 1. KEN SCHAUB, CRD #1601008, has been a registered securities salesman in Arizona
4 since at least January 1999. He was associated with Royal Alliance Associates, Inc. ("Royal
5 Alliance"), until his termination on or about June 25, 1999. Thereafter he was associated with
6 Raymond James Financial Services, Inc. ("Raymond James"), until his termination on or about
7 March 23, 2000. Since his termination by Raymond James, KEN SCHAUB has not been
8 associated with a dealer firm.

9 2. At all times relevant to this Order, KEN SCHAUB has resided in Arizona. His last
10 known business address is that of his office at IPA, 4518 N. 32nd Street, Suite #100, Phoenix,
11 Arizona 85018.

12 3. At all times relevant to this Order, KEN SCHAUB has been married to DONNA
13 LOUISE SCHAUB, whose last known address is 2943 E. Melody Lane, Gilbert, Arizona 85234.
14 All actions of KEN SCHAUB have been taken in furtherance of the marital community of KEN
15 AND DONNA SCHAUB. DONNA LOUISE SCHAUB is not a respondent in this matter, but she
16 acknowledges that all actions of KEN SCHAUB, as described in this Order, have been taken in
17 furtherance of the KEN AND DONNA SCHAUB marital community.

18 4. KEN SCHAUB holds an Arizona license to engage in business as a mortgage broker.

19 5. IPA is an Arizona corporation, formed on January 20, 1993, of which KEN SCHAUB
20 is president, chief executive officer and a 49% owner. The address of IPA is 4518 N. 32nd Street,
21 Suite #100, Phoenix, Arizona 85018.

22 6. IPA has never been registered or licensed as a securities dealer in Arizona or elsewhere.
23 Apart from the securities sales activity that will be described below in this Order, IPA has been and
24 is in the business of managing real estate limited liability companies.
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1 7. Between April 1999 and December 1999, KEN SCHAUB and IPA sold unregistered
2 securities. The securities took the form of investment contracts, entered into by and between
3 investors and American Business Funding Corporation ("ABF").

4 8. The principal business of ABF was factoring accounts receivable for small to medium-
5 sized businesses in Arizona and California.

6 9. RESPONDENTS sold the securities from their Phoenix office and other locations in
7 Arizona.

8 10. RESPONDENTS raised approximately \$6,954,000 in invested funds for ABF, from 18
9 investors.

10 11. In addition, KEN SCHAUB invested a total of \$164,000 of his own money in ABF
11 investment contracts -- \$134,000 from his retirement fund and \$30,000 from the Ken and Donna
12 Schaub Revocable Trust.

13 12. KEN SCHAUB neither sought nor received approval from Royal Alliance or Raymond
14 James to offer or sell the ABF investment contracts.

15 13. The sales of ABF investment contracts were not recorded on the books and records of
16 the dealer firm with which KEN SCHAUB was associated at the time of the sales.

17 14. On or about February 24, 2000, ABF filed a petition for reorganization under Chapter
18 11 of the United States Bankruptcy Code (11 U.S.C. § 101 *et seq.*) in the United States Bankruptcy
19 Court for the District of Arizona.

20 15. Prior to the filing of the bankruptcy petition, the investors who had purchased
21 investment contracts through KEN SCHAUB had received from ABF a total of \$553,997.64 as
22 returns on their investments, leaving a net amount invested of \$6,400,002.36.

23 16. The Bankruptcy Court approved a plan of reorganization for ABF, pursuant to
24 Bankruptcy Code § 1129, on or about November 20, 2000 (the "Plan").

25 17. Pursuant to the Plan, ABF dissolved and a newly-formed limited liability company,
26 New Horizon Capital, LLC ("NHC"), succeeded to its business.

1 18. Under the Plan, those persons who had purchased ABF investment contracts, and who
2 had timely filed proofs of claim in the Bankruptcy Court, were treated as “holders of Allowed
3 Investor Claims.” (Their claims were “allowed” to the extent of their principal invested, less
4 amounts that had been paid to them as returns on investment pre-bankruptcy filing by ABF.)

5 19. Under the Plan, each holder of an Allowed Investor Claim received the following:

- 6 a. An undivided interest in a Term Note delivered by NHC, which bears 7% per
7 annum interest, payable quarterly in arrears from the effective date of the Plan.
8 Principal is due annually, beginning on December 1, 2002, until paid in full.
- 9 b. A pro rata share of fifty-five percent of the equity interests in NHC.
- 10 c. An interest as beneficiary in a trust that was formed to litigate certain claims
11 that ABF possessed prior to the bankruptcy, and claims that holders of Allowed
12 Investor Claims had elected to assign to the litigation trust. NHC is to advance
13 all attorneys’ fees and costs of prosecuting the claims, and will be reimbursed
14 out of any litigation recoveries realized by the trust. The beneficiaries were
15 entitled to select the trustee.

16 20. Financial projections that were appended to the Plan approved by the Bankruptcy Court,
17 indicate that Allowed Investor Claims are expected to be paid in full, with interest as stated above,
18 over a period of approximately ten years.

19 21. More than 70% of the holders of Allowed Investor Claims, both in number and in dollar
20 value of claims, voted for the Plan. All but one of the investors who had purchased investment
21 contracts through KEN SCHAUB, voted for the Plan.

22 22. During the pendency of the Chapter 11 case in Bankruptcy Court, ABF required debtor-
23 in-possession financing to continue as a going concern and to expand its profitable factoring
24 business. KEN SCHAUB borrowed approximately \$1.8 million, secured by his personal
25 guarantee, liens on his personal assets, and a term life insurance policy on his life naming the
26 lender as beneficiary. KEN SCHAUB then used the \$1.8 million he had borrowed, to fund a loan

1 to the debtor-in-possession, pursuant to terms approved by the Bankruptcy Court. He is obligated
2 to pay approximately \$29,000 per month in interest with respect to this financing.

3 23. In addition, prior to and during the pendency of the Chapter 11 case, KEN SCHAUB
4 retained the law firm of Cochran & Dahl, P.C., to represent the interests of the investors who had
5 purchased their investment contracts through KEN SCHAUB. The total amount billed by the firm
6 for this representation was approximately \$83,240. KEN SCHAUB still owes approximately
7 \$25,000 in legal fees to the firm on account of this representation, and he is obligated to pay
8 approximately \$3,000 per month on account of this debt.

9 **II.**

10 **CONCLUSIONS OF LAW**

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

13 2. RESPONDENTS offered and sold securities, within the meaning of A.R.S. §§ 44-
14 1801(15), 44-1801(21), and 44-1801(26).

15 3. RESPONDENTS violated A.R.S. § 44-1841 by offering and selling, within or from
16 Arizona, securities that were neither registered nor exempt from registration.

17 4. IPA violated A.R.S. § 44-1842 by offering and selling securities while neither
18 registered as a dealer nor exempt from registration.

19 5. KEN SCHAUB's conduct subjects KEN SCHAUB to an order of revocation pursuant
20 to A.R.S. § 44-1962(A). Specifically, KEN SCHAUB:

21 a. Has engaged in conduct specified by A.R.S. § 44-1962(A)(2), in that he violated
22 a provision of the Securities Act by selling unregistered securities within or
23 from Arizona; and

24 b. Has engaged in conduct specified by A.R.S. § 44-1962(A)(10) and Ariz.
25 Admin. Code R14-4-130(A)(17), by effecting sales of securities that were not
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1 recorded on the books and records of the dealer firm with which he was
2 associated at the time of the sales.

3 6. RESPONDENTS' conduct is grounds for a cease and desist order pursuant to A.R.S. §
4 44-2032.

5 7. RESPONDENTS' conduct is grounds for administrative penalties under A.R.S. § 44-
6 2036.

7 **III.**

8 **ORDER**

9 THEREFORE, on the basis of the Findings of Fact, Conclusions of Law, and the
10 RESPONDENTS' and DONNA LOUISE SCHAUB's consent to the entry of this Order, the
11 Commission finds that the following relief is appropriate, in the public interest, and necessary for
12 the protection of investors:

13 IT IS ORDERED, pursuant to A.R.S. § 44-2032, that RESPONDENTS, their agents,
14 employees, successors and assigns, shall permanently cease and desist from violating the
15 Securities Act.

16 IT IS FURTHER ORDERED, pursuant to A.R.S. § 44-2036, that IPA, KEN SCHAUB,
17 and the marital community of KEN AND DONNA SCHAUB, jointly and severally, shall pay an
18 administrative penalty in the amount of \$25,000. Payment shall be made by cashier's checks or
19 money orders payable to the "State of Arizona" in installments as follows: \$2,500.00 on the date
20 of this Order; and at least \$726.00 per month on or before the 1st day of each month beginning on
21 November 1, 2001. Any amount outstanding shall accrue interest at the rate of 10% per annum
22 from the date of this Order until paid in full. If at any time IPA, KEN SCHAUB, or the marital
23 community of KEN AND DONNA SCHAUB does not comply with this order for administrative
24 penalties, any outstanding balance shall be in default and shall be immediately due and payable.
25 For the purposes of this Order, a bankruptcy filing by either of RESPONDENTS, and/or by
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1 DONNA LOUISE SCHAUB, that seeks discharge of this obligation to pay administrative
2 penalties shall be an act of default.

3 IT IS FURTHER ORDERED, pursuant to A.R.S. § 44-1962, that KEN SCHAUB's
4 securities salesman registration is revoked.

5 IT IS FURTHER ORDERED that this Order shall become effective immediately.

6 BY ORDER OF THE ARIZONA CORPORATION COMMISSION

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CHAIRMAN

COMMISSIONER

COMMISSIONER

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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
_____, 2001.

BRIAN C. McNEIL
Executive Secretary

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DISSENT

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This document is available in alternative formats by contacting Shelly M. Hood, ADA Coordinator,
voice phone number 602-542-3931, E-mail shood@cc.state.az.us.

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(AJL)

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CONSENT TO ENTRY OF ORDER

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2 1. RESPONDENTS and DONNA LOUISE SCHAUB admit the jurisdiction of the
3 Commission over the subject matter of this proceeding. RESPONDENTS and DONNA LOUISE
4 SCHAUB acknowledge that they have been fully advised of their right to a hearing to present
5 evidence and call witnesses, and RESPONDENTS and DONNA LOUISE SCHAUB knowingly
6 and voluntarily waive any and all rights to a hearing before the Commission and all other rights
7 otherwise available under Article 11 of the Securities Act and Title 14 of the Arizona
8 Administrative Code. RESPONDENTS and DONNA LOUISE SCHAUB acknowledge that this
9 Order to Cease and Desist, Order of Revocation, Order for Administrative Penalties, and Consent
10 to Same ("Order") constitutes a valid final order of the Commission.

11 2. RESPONDENTS and DONNA LOUISE SCHAUB knowingly and voluntarily waive
12 any right they may have under Article 12 of the Securities Act to judicial review by any court by
13 way of suit, appeal, or extraordinary relief resulting from the entry of this Order.

14 3. RESPONDENTS and DONNA LOUISE SCHAUB acknowledge and agree that this
15 Order is entered into freely and voluntarily and that no promise was made or coercion used to
16 induce such entry.

17 4. RESPONDENTS and DONNA LOUISE SCHAUB acknowledge that they have
18 reviewed this Order and understand all terms it contains.

19 5. RESPONDENTS and DONNA LOUISE SCHAUB neither admit nor deny the
20 Findings of Fact and Conclusions of Law contained in this Order. RESPONDENTS and DONNA
21 LOUISE SCHAUB agree that they shall not challenge their validity in any present or future
22 administrative proceeding before the Commission or any other state agency concerning the denial
23 or issuance of any license or registration required by the State to engage in the practice of any
24 business or profession.

25 6. By consenting to the entry of this Order, RESPONDENTS and DONNA LOUISE
26 SCHAUB agree not to take any action or to make, or permit to be made, any public statement

1 denying, directly or indirectly, any Finding of Fact or Conclusion of Law in this Order or creating
2 the impression that this Order is without factual basis. RESPONDENTS and DONNA LOUISE
3 SCHAUB will undertake steps necessary to assure that all of their agents and employees
4 understand and comply with this agreement.

5 7. While this Order settles this administrative matter between RESPONDENTS and the
6 Commission, RESPONDENTS and DONNA LOUISE SCHAUB understand that this Order does
7 not preclude the Commission from instituting other administrative proceedings based on violations
8 that are not addressed by this Order.

9 8. RESPONDENTS and DONNA LOUISE SCHAUB understand that this Order does not
10 preclude the Commission from referring this matter to any governmental agency for
11 administrative, civil, or criminal proceedings that may be related to the matters addressed by this
12 Order.

13 9. RESPONDENTS and DONNA LOUISE SCHAUB understand that this Order does not
14 preclude any other agency or officer of the state of Arizona or its subdivisions from instituting
15 administrative, civil or criminal proceedings that may be related to matters addressed by this
16 Order.

17 10. RESPONDENTS agree that they will not apply to the state of Arizona for registration
18 as a securities dealer or salesman, or for licensure as an investment adviser or investment adviser
19 representative, at any time in the future.

20 11. RESPONDENTS agree that they will not exercise any control over any entity that
21 offers or sells securities or provides investment advisory services, within or from Arizona.

22 12. RESPONDENTS and DONNA LOUISE SCHAUB agree that until the administrative
23 penalty has been paid in full, RESPONDENTS and DONNA LOUISE SCHAUB will notify the
24 Director of the Securities Division within 30 days of any change in home address or any change in
25 RESPONDENTS' or DONNA LOUISE SCHAUB's ability to pay amounts due under this Order.

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1 13. RESPONDENTS and DONNA LOUISE SCHAUB understand that default shall render
2 them liable to the Commission for its costs of collection and interest at the maximum legal rate.

3 14. KEN SCHAUB agrees that he will continue to cooperate with the Securities Division
4 including, but not limited to, providing complete and accurate testimony at any hearing in this
5 matter and cooperating with the state of Arizona in any related investigation or any other matters
6 arising from the activities described in this Order.

7 15. KEN SCHAUB and DONNA LOUISE SCHAUB acknowledge that the administrative
8 penalty imposed by this Order is an obligation of KEN SCHAUB, as well as the marital
9 community of KEN AND DONNA SCHAUB.

10 16. RESPONDENTS and DONNA LOUISE SCHAUB consent to the entry of this Order
11 and agree to be fully bound by its terms and conditions. If RESPONDENTS or DONNA LOUISE
12 SCHAUB should breach any provision of this Order, the Commission may vacate this Order and
13 restore this case to its active docket.

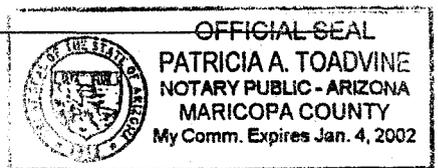
14 17. KEN SCHAUB represents that he has authority to execute this Consent to Entry of
15 Order on behalf of IPA.

16 Kenneth Eugene Schaub
17 KENNETH EUGENE SCHAUB

18 SUBSCRIBED AND SWORN TO BEFORE me this 12th day of September, 2001.

19 Patricia A. Toadvine
20 NOTARY PUBLIC

21 My Commission Expires:



INVESTMENT PLANNERS OF AMERICA,
INC.

Kenneth E. Schaub

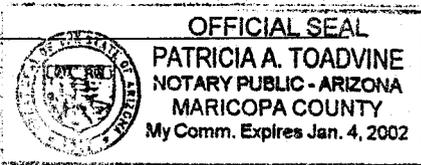
By: Kenneth E. Schaub, President

SUBSCRIBED AND SWORN TO BEFORE me this 12th day of September, 2001.

Patricia A. Toadvine

NOTARY PUBLIC

My Commission Expires:



Donna L. Schaub

DONNA LOUISE SCHAUB

SUBSCRIBED AND SWORN TO BEFORE me this 12th day of September, 2001.

Patricia A. Toadvine

NOTARY PUBLIC

My Commission Expires:

