STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
DEPARTMENT OF BUSINESS REGULATION
1511 PONTIAC AVENUE, BLDG. 69-2
CRANSTON, RHODE ISLAND 02920

IN THE MATTER OF:	:	
TIMOTHY M. KELLY	:	**DBR No. 15IN006**
RESPONDENT.	:	

DECISION AND ORDER OF REVOCATION

Hearing Officer: Ellen R. Balasco, Esq.

Close of Record: April 5, 2016

Appearances:

For Respondent: Respondent appeared *pro se.*

For the Department: Matthew Gendron, Esq.

I. INTRODUCTION

Timothy Kelly ("Respondent") holds a Rhode Island insurance producer's license No. 1071705 for Life and Health insurance lines. The Department of Business Regulation's Securities Division issued to the Respondent, a co-Respondent and four (4) business entities an Emergency Order to Cease and Desist, Notice of Opportunity for Hearing, and Notice of Intent to Impose Civil Penalty ("Emergency Order"), executed by the Director of the Department on September 16, 2015. That Emergency Order effected a mandate against this Respondent and other parties that "Respondents and any person associated therewith shall immediately cease and desist from any further violation of Sections 201, 301 and 501 of the Rhode Island Uniform

Securities Act (RIUSA)", in accordance with the Department's authority as expressed in R.I. Gen. Laws §§ 7-11-212 and 7-11-603.

The Insurance Division of the Department ("Department") issued to this Respondent an Order to Show Cause, Notice of Hearing and Appointment of Hearing Officer on the same date. ("Order") That Order was amended on January 28, 2016 which included additional allegations not addressed in the first Order.

These Orders issued as a result of a complaint received by the Division on August 12, 2015 from a consumer alleging that he had been solicited by the Respondent to invest in a plan called The GetEasy Membership, which was later learned to comprise a fraudulent investment scheme.[1]

A pre-hearing conference was held on January 28, 2016 at the Department, and an Order was issued that the cease and desist previously issued by the Director would remain in full force and effect pending a final hearing and Decision of the Director. A full, evidentiary hearing was held on March 22, 2016, and the administrative record closed on April 5, 2016, to allow the parties to submit written memoranda.

II. JURISDICTION

The Department has jurisdiction over this matter pursuant R.I. Gen. Laws § 27-2.4-1, *et seq.*, R. I. Gen. Laws § 42-14-1, *et seq.*, and R.I. Gen. Laws § 42-35-1, *et seq.*

III. ISSUES PRESENTED

The three issues presented in this hearing were whether Respondent Kelly's insurance license should be revoked, whether the temporary cease and desist Emergency Order should be

[1] Respondent Kelly was previously licensed to sell securities in Rhode Island, but that he had been barred from association with broker-dealers in 2002 by the National Association of Securities Dealers, and later barred from selling securities by the Department of Business Regulation on September 4, 2003.

made permanent and whether he should be fined for participating in the sale of securities without a valid license to do so, and his participation perpetrating a fraudulent investment scheme. The Department identified and presented evidence regarding three separate bases for Kelly's insurance producer's license to be revoked. The Department also presented substantial evidence about Kelly's role in an investment (so-called 'Ponzi') scheme[2] and that that he knew or should have known that the Get Easy "membership" was an investment contract, and thus met the definition of a security under Rhode Island law.

The Department's request for a permanent cease and desist order and penalties are both tied to Kelly's role in the GetEasy scheme. It is alleged that he sold or solicited the sale of tens of thousands of dollars of worthless Get Easy "memberships" to Rhode Island consumers, and because of that, those people lost large sums of money that they had invested. This, the Department contends, establishes grounds for revocation of his insurance producer license for incompetence in participating in this scheme, and also based on his untrustworthiness in that he falsified his renewal application for his insurance producer license in 2015.

The Respondent argued in his defense that he believed the GetEasy membership investment to be a multi-level marketing business, such as Amway and Avon, and that he was completely unaware that it would meet the criteria as a security.

IV. MATERIAL FACTS AND TESTIMONY

In its pleadings, and the evidence presented at hearing, the Division outlined its three-fold grounds in support of its request to revoke the Respondent's insurance license: (1) That he had been

[2] The United States Securities and Exchange Commission defines a Ponzi scheme as an investment fraud that involves the payment of purported returns to existing investors from funds contributed by new investors. Ponzi scheme organizers often solicit new investors by promising to invest funds in opportunities claimed to generate high returns with little or no risk. In many Ponzi schemes, the fraudsters focus on attracting new money to make promised payments to earlier-stage investors to create the false appearance that investors are profiting from a legitimate business.

barred from selling securities in Rhode Island in 2003 and was now engaging in unlicensed activity; (2) that he intentionally and materially misled the Department in 2015 when he renewed his insurance license; and (3) that his involvement with the Get Easy investment involved either dishonesty to his clients or incompetency based on his failure to understand the fraudulent nature of the investment.

The Division argued that this Respondent has a history of being involved in Ponzi-like investment schemes, intended to defraud investors by taking their money, and offering no or little return on their investment. The Division alleges that the consumers to whom the Respondent offered and sold this security were his insurance customers.

The parties presented a Joint Stipulation of Undisputed Facts to the Hearing Officer prior to the hearing. That document is attached hereto, and incorporated in this Decision by reference, and is marked as Joint Exhibit #1.

Counsel for the Division presented three witnesses and nine documents, which were admitted as full exhibits: They include:

#1 Final Order to Bar issued by the RI Department of Business Regulation dated 9/4/03

#2 NIPR online application for insurance license renewal by the Respondent

#3 and #4 Copies of electronic messages from consumer complainant against Respondent and the responses by Division personnel

#5 GetEasy registration form and copy of $10,000 check paid by complainant

#6 51 pages of documents provided to Division from Respondent including website screenshots and GetEasy registrations by consumers

#7 Documents which accompanied consumer complaint

#8 Electronic message from Respondent explaining his position to counsel

#9 September 19, 2014 letter from Respondent to one of his annuity clients

#10 Copies of webpage for "T & T Retirement Specialist Presidents"

#11 Letter from Respondent to client dated January 13, 2012

The witnesses presented by the Division offered sworn testimonial evidence in support of the Orders, and the request for revocation. First, Elizabeth Kelleher Dwyer, Superintendent for the Insurance Division testified regarding the policies and procedures regarding dual licensure with the Insurance and Securities Divisions of the Department. She indicated that when an insurance producer is banned from selling securities in the state by the licensing agency, they become ineligible for licensing as an insurance producer, and that insurance license is effectively revoked at the time of the ban, in accordance with the provisions of R.I. Gen. Laws § 27-2.4-14.

She authenticated Exhibit #2 as being the Respondent's most recent renewal application for his insurance producer license for the 2013-2015 renewal period. Her testimony revealed that the Respondent should have answered "yes" to background question number 2, which asks whether the applicant had ever had any professional license censured, suspended, revoked, canceled, terminated or assessed a fin to resolve an administrative action with a licensing agency. Respondent answered "no", which was an untruthful answer. This would have flagged a denial of the insurance license renewal at the time of application. It is her belief that the Respondent believed the Insurance Division would not catch this misrepresentation, and he would be renewed.

Principal Securities Examiner Joanne Sullivan was called next by the Division. As part of her duties, she processes securities applications, and investigates complaints filed against licensees. She reviewed the files and prior licensing history of this Respondent as part of her duties, as well. As part of this Respondent's licensing file, she reviewed the Final Order to Bar (Dept.'s Exhibit #1) which outlines the history of his prior administrative actions. Her

investigation into this matter revealed that the Respondent's prior violations included an investment scam regarding pay phones, and the sale of Viatical Settlement Contracts, which the Division determined under the law to be a security, therefore, subject to registration by the Division. The Division at that time (prior to the Final Order to Bar) found that the Respondent, in offering and selling a Future First viatical contract in the State of Rhode Island had violated a number of sections of RIUSA.[3]

With respect to the Complainant/investors in this matter, Kelly failed to be available to them after they had made a ten thousand dollar ($10,000) investment with him in the GetEasy scheme. At the time, according to Examiner Sullivan" Respondent Kelly was operated at T and T Tax Advisory, whose letterhead listed him as "President". According to the witness, she made an unannounced visit to the T and T Tax Advisory offices, where Respondent Kelly and his partner, Mr. Maranda were present and cooperative with the Examiner's investigation. She stated that they both expressed frustration with the GetEasy program, as they had each invested some of their own funds in it.

Sullivan further testified that, after an examination of computer website records of the Respondent that she developed serious concerns about GetEasy when she learned that there were no financial background requirements for investors, the investment check payee was Unique Financial Services (a third party) and that the informational materials used the phrase "guaranteed 12 month return", and offered investors over 100% return on their investment. All of this, she explained, is a red flag for a Ponzi scheme. She testified that the GetEasy program made no sense at all from a business perspective.

According to Sullivan, the highest return on investment she has ever seen in a security is around 10% to 12%, and that that occurred in approximately 1986. The GetEasy scheme, she

[3] See Department's Exhibit #1, attached which is incorporated by reference herein and made a part hereof.

stated, was very similar to the pay phone scheme in the previous violations by Respondent; the only difference being that this one was not international. She testified that the use of the internet adds a "smoke and mirrors" effect to Ponzi schemes, making them appear to be legitimate causing unwary consumers to invest.

As she described it, the Respondent brought in new members to the GetEasy sales process. The plan was for him to receive "bones" (or bonuses) for each new member. According to her, the difference between a "multi-level marketing" program and a Ponzi scheme, is that the latter makes promises which are impossible to keep. That is when it becomes illegal. GetEasy's promises, she said, were ridiculous.

Her investigation revealed that Respondent Kelly had approximately twenty clients. Despite his statement to the Department that he had never offered the GetEasy investment to his annuity/insurance clients, her investigation revealed that the Respondent had often done this. A significant finding in the witness' investigation was that she uncovered absolutely no evidence of any GetEasy investor receiving any return on their investment whatsoever. Her conclusion was, therefore, that this was a Ponzi scheme and there was no tangible investment that ever existed.

The next witness to offer testimony was Donald DeFedele, Chief Securities Examiner for the Department, who has been with the Department for four years, and has worked in the investment and insurance industries for the past fourteen years.

This witness testified similarly to Examiner Sullivan's testimony, that he participated in the GetEasy investigation, and the fact that the investment offered a 100% return on investment was astronomical. He stated that the Respondent was paid bonuses for recruiting new investors, so this was a commission-based business, and for all intents and purposes met the definition of a Ponzi scheme.

At this point in the hearing, Counsel for the Division rested its case.

The Respondent testified that his belief was that he was selling memberships in a group. He was present at his office when witness DeFedele "and his team" showed up and went through their computer files. He stated that it was at this point that he stopped selling the GetEasy investment – a period of time before being served with the Emergency Order to Cease and Desist.

He testified that he collected a fee of $60 Euro when he brought in a new customer. His testimony is that he used his Euro balance on account to purchase his own memberships. The contact person for the investment was named Tony Dossantos. He does not believe that Dossantos know that "this was a scheme."

The testimony revealed that approximately 75% of the GetEasy investors were also his insurance clients. In questioning by the Hearing Officer, he stated that he "never asked the question" whether GetEasy was a security. In closing, the Respondent indicated that he is sorry that people lost money.

Upon re-direct questioning by counsel for the Division, he testified that the "did not have an explanation" as to why he answered "no" to background question number 2 on his 2015 insurance producer license application, when he know that to be a false answer.[4] He assumed that, because the Securities Division of the Department shared its information with the Insurance Department, so the insurance "people" should have known what happened with FINRA and his securities problems, which resulted in the Final Order to Bar him from engaging in securities transactions.

[4] Question 2 reads, in pertinent part: "Have you been named or involved as a party to an administrative proceeding, including a FINRA sanction proceeding regarding any professional or occupational license which has not been previously reported to this insurance department?"

V. STANDARD OF REVIEW FOR AN ADMINISTRATIVE HEARING

It is well settled that in formal or informal adjudications modeled on the federal Administrative Procedures Act, the initial burdens of production and persuasion rest with the moving party. 2 Richard J. Pierce, *Administrative Law Treatise* § 10.7 at 759 (2002).

In this case, the proponent of this enforcement action is the Department. Unless otherwise specified, a preponderance of the evidence is generally required in order to prevail. *Id.* at 763-766; see also, *Lyons v. Rhode Island Pub. Employees Council 94*, 559 A.2d 130, 134 (R.I. 1989) (preponderance standard is the "normal" standard in civil cases); *Parker v. Parker*, 238 A.2d 57, 60 (R.I. 1968) ("satisfaction by a 'preponderance of the evidence' [is] the recognized burden [of proof] in civil actions"). This means that, for each element to be proven, the fact finder must believe that the facts asserted by the proponent are more probably true than false. See *Parker*, 238 A.2d at 60. When there is no direct evidence on a particular issue, a fair preponderance of the evidence may be supported by circumstantial evidence. *Narragansett Electric. Co. v. Carbone*, 898 A.2d 87, 100 (R.I. 2006).

The Rhode Island Supreme Court has consistently held that it effectuates legislative intent by examining the statute in its entirety and giving words their plain and ordinary meaning. *In re Falstaff Brewing Corp.*, 637 A.2d 1047, 1049 (R.I. 1994). See *Parkway Towers Associates v. Godfrey*, 688 A.2d 1289 (R.I. 1997). The Rhode Island Supreme Court has also established that it will not interpret legislative enactments in a manner that renders them nugatory or that would produce an unreasonable result. See *Defenders of Animals v. Dept. of Environmental Management,* 553 A.2d 541 (R.I. 1989) (citing *Cocchini v. City of Providence*, 479 A.2d 108, 111 (R.I. 1984); *Beaudoin v. Petit,* 409 A.2d 536, 540 (1979); *Raymond Construction Co. v. Bisbano,* 326 A.2d 858, 861 (1974)). In cases where statutory language is ambiguous, the Rhode

Island Supreme Court has consistently held that legislative intent must be considered. *Providence Journal Co. v. Rodgers*, 711 A.2d 1131, 1134 (R.I. 1998). The statutory provisions must be examined in their entirety and the meaning most consistent with the policies and purposes of the legislature must be effectuated. *Id.* It is also necessary to take into account the scope of the statute and the purpose sought to be accomplished through the enactment of the statute when determining how it is to be construed. *New England Die Co., Inc. v. General Products Co., Inc.*, 168 A.2d 150 (R.I. 1961).

VI. DISCUSSION

Rhode Island law authorizes the Department to oversee the licensure and regulation of insurance producers. An insurance producer is required to be licensed under the laws of this state to sell, solicit or negotiate insurance. *(R. I. Gen. Laws § 27-2.4-2)*

In examining R.I. Gen. Laws § 27-2.4-1 *et seq.*, it is clear that the legislature intended to place express requirements upon insurance producer license applicants. This comprehensive statutory scheme clearly reflects the legislative intent to ensure that the insurance industry is comprised of licensees who are competent, withstand the scrutiny of the process of application, and submit complete and accurate information under penalties of perjury. The application process is clearly intended to ensure that the licensed insurance producers do not pose a threat to the public interest or may, once licensed, affect the integrity of the insurance industry marketplace.

Because this matter involves the revocation of an insurance producer license, the purpose and scope of the statutory licensing and revocation process at issue pursuant to R.I. Gen. Laws § 27-2.4-14(a) must therefore, be analyzed in the context of this statutory scheme.

Here, the Department bears the burden for establishing why it is more likely than not that Respondent conducted activities and business practices that violated the statutes and regulations under which he holds his insurance producer license.

R.I. Gen. Laws § 27-2.4-14 (a)(8) establishes that "The insurance commissioner may place on probation, suspend, revoke or refuse to issue or renew an insurance producer's license or may levy an administrative penalty in accordance with § 42-14-16 or any combination of actions, for any one or more of the following causes: . . . demonstrating incompetence, untrustworthiness, or financial irresponsibility in this state . ." It is this section of Title 27, and the Department's policies and procedures as testified to by the Superintendent, on which the Division bases their request for revocation of the Respondent's insurance producer license.

With respect to the Department's assertion that Respondent's License should be revoked pursuant to R.I. Gen. Laws § 27-2.4-14(a)(8), the Department is well within its statutory authority given the facts stated herein to assert those statutory provisions as a basis for revocation. Furthermore, assuming *arguendo* that Respondent had provided a true correct and complete application as required by R.I. Gen. Laws §§ 27-2.4-8, the Department has established that Respondent's license should be revoked pursuant to R.I. Gen. Laws § 27-2.4-14(a)(8) because the actions indicated in the Final Order to Bar constitute evidence of "fraudulent, coercive, or dishonest practices or demonstrating incompetence, untrustworthiness or financial irresponsibility in this state or in another place."

The Hearing Officer finds reliable authority in the findings made in a 2007 Department administrative enforcement decision *In the Matter of Scott Lyons*, DBR No. 06-I-065. In that matter, the Director found that the Insurance Division may revoke a producer's license for later discovery of a revocation by another licensing entity. There, the Insurance Division renewed Lyons insurance producer's license in January 2006, but learned later that Lyons had entered into

a 2005 Consent Agreement with the Securities Division previously. The Consent Agreement had been known to the licensing aide responsible for renewing Lyons license, but the licensing aide failed to follow established departmental procedure. When the prior Consent Agreement was discovered, it initiated an administrative enforcement action and was successful in obtaining an Order revoking that license.

VII. FINDINGS OF FACT

1. A full evidentiary hearing was held on March 22, 2016, and the formal record for that hearing closed on April 5, 2016.
2. The facts contained in Sections IV and VI herein, and the Joing (sp.) Stipulation of Facts marked as Joint Exhibit 1 are incorporated by reference herein.

VIII. CONCLUSIONS OF LAW

In accordance with the testimony and facts presented:

1. The Department has jurisdiction over this matter as set forth in Section II, *supra*.

2. Under the standard set forth in Section V and the statutory framework and analysis set forth in Section VI, the Department established by a preponderance of the evidence that Respondent's insurance producer license should be revoked for cause and a failure to properly serve the interests of the public under the license in violation of R.I. Gen. Laws § 27-2.4-14(a)(8).

3. The Department has established that there is sufficient cause to revoke Respondent's insurance producer license pursuant to R.I. Gen. Laws § 27-2.4-14(a)(8) (which allows revocation for using fraudulent, coercive, or dishonest practices or demonstrating incompetence, untrustworthiness or financial irresponsibility in this state or in another place) based on the fraudulent and incompetent actions supported by the evidence that the Respondent knew or should

have known that the GetEasy investment was fraudulent, but that he solicited investment in the scheme from unwary consumers whom he had personally recruited.

8. The Department has established that there is sufficient cause to revoke Respondent's insurance producer license pursuant to R.I. Gen. Laws § 27-2.4-14(a)(8) due to Respondent's false answer to a background question on his 2015 insurance producer's license renewal application which demonstrates untrustworthiness and dishonesty.

IX. RECOMMENDATION

Based on the above analysis, and due consideration of the facts presented, the Hearing Officer recommends that the Director of the Department of Business Regulation enter an Order revoking the insurance producer license of the Respondent, and re-affirming the Final Order to Bar Respondent from engaging in securities transaction in the State of Rhode Island.

Dated: August 5, 2016

Ellen R. Balasco, Esq.
Hearing Officer

ORDER OF THE DIRECTOR

I have read the Hearing Officer's Decision and Order in this matter, and I hereby take the following action with regard to her recommendations:

- [X] ADOPT
- [ ] REJECT
- [ ] MODIFY

DATED: 8/22/16

Macky McCleary
Director

THIS DECISION CONSTITUTES A FINAL DECISION OF THE DEPARTMENT OF BUSINESS REGULATION PURSUANT TO RHODE ISLAND GENERAL LAWS TITLE 42, CHAPTER 35. AS SUCH, THIS DECISION MAY BE APPEALED TO THE SUPERIOR COURT SITTING IN AND FOR THE COUNTY OF PROVIDENCE WITHIN THIRTY (30) DAYS OF THE DATE OF THIS DECISION. SUCH APPEAL, IF TAKEN, MAY BE COMPLETED BY FILING A PETITION FOR REVIEW IN SAID COURT.

CERTIFICATION

I hereby certify on this 23rd day of August, 2016 of the within Decision and Order of Revocation was sent by first class mail, postage prepaid, to Timothy Kelly, 85 Douglas Pike, Smithfield, RI 02817 at the Department of Business Regulation: and to the following parties by electronic mail at the Department of Business Regulation: Elizabeth Kelleher Dwyer, Esq., Superintendent of Banking and Insurance, and Matthew Gendron, Esq.

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
DEPARTMENT OF BUSINESS REGULATION
DIVISION OF INSURANCE
1511 PONTIAC AVENUE, BUILDING 69-2
CRANSTON, RI 02920

IN THE MATTER OF: **TIMOTHY M. KELLY** **RESPONDENT.**	**DBR No. 15-IN-006**

JOING STIPULATION OF UNDISPUTED FACTS

Both the Department of Business Regulation (the "Department") and Respondent Timothy M. Kelly ("Kelly") agree to stipulate that the following facts are undisputed:

1) Tim Kelly has had an insurance license in good standing since 1982.
2) Tim Kelly had been licensed by the Rhode Island securities division from 1983-2001.
3) Tim Kelly offered and sold Viatical Settlements between March 7, 2001 and March 19, 2002.
4) Tim Kelly offered and sold investments in pay telephones located in the State of Utah prior to March 16, 2000.
5) Tim Kelly was barred from associating with any broker-dealer or investment advisor on September 4, 2003.
6) Tim Kelly invested some of his own money in Get Easy.
7) Tim Kelly offered and sold Get Easy memberships to numerous individuals in Rhode Island.
8) Tim Kelly received a small fee (in Euro's) for bringing in other "members" to Get Easy.
9) Tim Kelly would receive overrides on what business the "members" he had recruited brought into Get Easy.
10) Purchasing a "membership fee" would supposedly link a certain amount of GPS trackers to your Get Easy account, which were rented out by Get Easy, and they would guarantee each membership to double their investment within 12 months.
11) Tim Kelly got involved in selling Get Easy "memberships" to supplement his income.
12) Tim Kelly was emailed and handed a copy of the T&T et al. Emergency Cease and Desist Order and the Insurance Division's Original Order to Show Cause on September 24, 2015.

13) Tim Kelly applied to renew his insurance producer's license on September 30, 2015.

14) Get Easy was a common enterprise, where money was pooled and organized together.

15) Investors bought Get Easy "memberships" with an expectation of profit.

16) Investors who bought Get Easy "memberships" expected that the Get Easy Group would undertake any efforts required for the investment to make money.

The undersigned parties agree to the above listed undisputed facts:

Respondent Kelly:

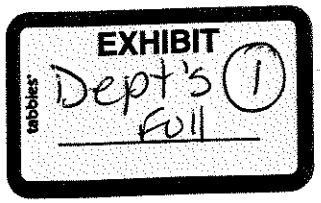
Timothy M. Kelly

Date: 3/10/16

For the Department:

Legal Counsel Matthew Gendron, Esq.

Date: 3/16/2016



STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
DEPARTMENT OF BUSINESS REGULATION
DIVISION OF SECURITIES
233 RICHMOND STREET
PROVIDENCE, RHODE ISLAND 02903-4232

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IN THE MATTER OF	:
TIMOTHY M. KELLY	:
Respondent.	:

FINAL ORDER TO BAR

The Director ("Director") of the Rhode Island Department of Business Regulation issues this Order pursuant to R.I. Gen. Laws §§ 7-11-710 and 42-35-1 et seq. and the Rules of Practice and Procedure in Administrative Hearings Before the Department of Business Regulation. On December 2, 2002 the Department issued a Notice of Intent to Bar, Impose Civil Penalty and of Opportunity for Hearing. The Director hereby enters a Final Order to Bar against Timothy M. Kelly based upon his failure to timely request a hearing in accordance with R.I. Gen. Laws § 7-11-710.

Entered this 4th day of September, 2003.

Marilyn Shannon McConaghy
Marilyn Shannon McConaghy, Esq., Director
Rhode Island Department of Business Regulation

Order No.: 03-118

DB-KellyFinalOrderToBar

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
DEPARTMENT OF BUSINESS REGULATION
233 RICHMOND STREET
PROVIDENCE, RHODE ISLAND 02903

IN THE MATTER OF:	:	
	:	NOTICE OF INTENT TO BAR, IMPOSE CIVIL PENALTY AND OF OPPORTUNITY FOR HEARING
TIMOTHY M. KELLY	:	
Respondent.	:	

The Director of the Department of Business Regulation ("Director") hereby issues this Notice Of Intent To Bar, To Impose Civil Penalty And Of Opportunity For A Hearing ("Notice"), pursuant to § 602 of the Rhode Island Uniform Securities Act of 1990 ("RIUSA"), § 7-11-101 et seq., of the Rhode Island General Laws, 1989, as amended, and Rhode Island General Laws, § 42-35-1 et seq., to Timothy M. Kelly ("Respondent").

The Director issues this Notice for the following reasons:

1. Respondent is a Rhode Island resident residing at 1076 Overlook Circle, North Providence, Rhode Island 02904.
2. During the period from May 1, 2000 to April 3, 2001 Respondent was licensed with the State of Rhode Island Department of Business Regulation Securities Division ("Division") as a sales representative of Protective Group Securities Corporation ("Protective Group"), pursuant to R.I. Gen. Laws § 7-11-201. Respondent was licensed as a sales representative of WMA Securities, Inc. ("WMA Securities") from November 28, 1995 to November 4, 1999.

3. Protective Group and WMA Securities were during the time period Respondent was licensed, and are currently, licensed with the Division, as broker-dealers, pursuant to R.I. Gen. Laws § 7-11-201.

4. Respondent is not currently licensed as a sales representative with the Division.

5. The Director issued an Emergency Order To Cease And Desist (the "Order") against Respondent on March 16, 2000 (Attached as Exhibit "A"). The Order was related to Respondent's sale of payphone investments.

6. On March 7, 2001, the Division issued its Policy Statement On Viatical Settlement Contracts, which clarifies the Division's position that viatical contracts are securities (Attached as Exhibit "B").

7. On March 18, 2002 the Division's review of Respondent's web site disclosed that he was offering viatical contracts over the internet.

8. On March 19, 2002 the Division conducted an unannounced examination of Respondent's books and records pursuant to R. I. Gen. Laws § 7-11-211.

9. Respondent informed the Division staff that he had made a viatical contract sale in April of 2001, and provided documentation disclosing the sale.

10. The documentation disclosed that Respondent sold a viatical contract to one investor in the amount of $27,000.00 on April 25, 2001.

11. The Futures First viatical contract was not registered as a security with the state of Rhode Island, pursuant to R. I. Gen. Laws § 7-11-301.

12. Respondent was not licensed as a broker-dealer or a sales representative at the time of the viatical contract sale.

13. On March 21, 2002, the National Association of Securities Dealers Regulation, Inc. ("NASDR"), a self regulatory organization, barred Respondent from association with any broker-dealer, due to his sale of viatical contracts and payphone investments while he was registered with WMA Securities.

COUNT I

VIOLATION OF R. I. GEN. LAWS §7-11-301 FOR THE OFFER AND SALE OF UNREGISTERED SECURITIES

14. The Division herein restates the allegations and facts set forth in paragraphs 1 through 13.

15. R.I. Gen. Laws § 7-11-301 provides that a person may not sell, or offer to sell, a security in this state unless the security is registered, exempt from registration, or is a federal covered security.

16. Pursuant to the Division's Policy Statement On Viatical Settlement Contracts, which went into effect on March 7, 2001, viatical contracts are securities. Therefore, the viatical contracts must be registered as securities, and the person selling the viatical contract must be licensed, under RIUSA.

17. Respondent offered and sold a Futures First viatical contract, in the State of Rhode Island which was not registered with the Division, on April 25, 2001, in violation of RIUSA.

COUNT II

VIOLATION OF R.I. GEN. LAWS § 7-11-201 FOR THE OFFER AND SALE OF SECURITIES WITHOUT LICENSURE

18. The Division herein restates the allegations and facts set forth in paragraphs 1 through 13.

19. R.I. Gen. Laws § 7-11-201 provides that no person may transact business in Rhode Island as a broker-dealer or sales representative unless that person is licensed under this chapter.

20. Respondent offered and sold securities, in the form of viatical contracts, without being licensed at the time of the offer and sale as a broker-dealer or sales representative, in violation of RIUSA.

COUNT III

VIOLATION OF R.I. GEN. LAWS § 7-11-501 FOR THE MISLEADING OFFER AND SALE OF A SECURITY

21. The Division herein restates the allegations and facts set forth in paragraphs 1 through 13.

22. R.I. Gen. Laws § 7-11-501(2) provides that a person may not make an untrue statement of a material fact or omit to state a material fact necessary in order to make the statement made, in light of the circumstances under which they are made, not misleading, in connection with the offer or sale of a security.

23. Respondent offered and sold securities, in the form of viatical contracts, without disclosing material facts about the viatical contract and the risks involved, which made the sale misleading, in violation of RIUSA.

COUNT IV

VIOLATION OF R.I. GEN. LAWS § 7-11-212 FOR A CURRENTLY EFFECTIVE ORDER ISSUED BY A SELF REGULATORY ORGANIZATION

24. The Division herein restates the allegations and facts set forth in paragraphs 1 through 13.

25. R.I. Gen. Laws § 7-11-212(b)(7)(ii) states that the Director may bar a person who has been barred by a self regulatory organization.

26. Respondent was barred by NASD Regulation, Inc. from association with any broker-dealer, on March 21, 2002, in violation of RIUSA.

THEREFORE, unless the Director receives a written request for a hearing within thirty (30) days of the date of this Notice, the Director will regard the Respondent as having been provided with notice and an opportunity for a hearing, and as having waived the right to a hearing. Further, unless such written request for a hearing is received within the time period specified above, no hearing will be held on this matter, and the Director will by final order bar Respondent from association with any broker-dealer or investment advisor, a partner, officer or director, a person occupying similar status or performing similar functions, or a person directly or indirectly controlling the broker-dealer or investment adviser.

Pursuant to R.I. Gen. Laws § 7-11-602, if the Director reasonably believes that a violation has occurred, she may (after such notice and hearing in an administrative proceeding unless the right to notice and hearing is waived by a person against whom the sanction is imposed), impose a civil penalty up to a maximum of ten thousand dollars ($10,000) for a single violation or of one hundred thousand dollars ($100,000) for multiple violations, in addition to any specific powers granted under R.I. Gen. Laws § 7-11-101 et seq.

Dated this 2nd day of December, 2002.

Order No. 02-102

Marilyn Shannon McConaghy

Marilyn Shannon McConaghy, Esq. Director
Rhode Island Department of Business Regulation

DB-KellyNoticeToBar

CERTIFICATION

I hereby certify on this 2nd day of December, 2002 that a copy of this Notice was sent by certified mail, return receipt requested and by first class mail, postage prepaid to Timothy M. Kelly and by hand-delivery to Maria D'Alessandro Piccirilli, Associate Director and Superintendent of Securities, and David F. Briden, Esq., Chief Securities Examiner, Department of Business Regulation, 233 Richmond Street, Providence, RI 02903

Antoinetta Budano

EXHIBIT A

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
DEPARTMENT OF BUSINESS REGULATION
DIVISION OF SECURITIES
233 RICHMOND STREET
PROVIDENCE, RHODE ISLAND 02903-4232

IN THE MATTER OF	EMERGENCY ORDER TO CEASE AND DESIST AND IMPOSE CIVIL PENALTY UNDER SECTIONS 602 AND 712 AND OF OPPORTUNITY FOR A HEARING
TIMOTHY M. KELLY,	
Respondent.	

I.

Pursuant to Sections 7-11-602 and 7-11-712 of the Rhode Island Uniform Securities Act of 1990 ("RIUSA") and Section 42-35-14 of the Rhode Island General Laws, ("R.I.G.L.") the Director (the "Director") of the Rhode Island Department of Business Regulation (the "Department") hereby issues this Emergency Order to Cease and Desist and of Intent to Impose Civil Penalty under Sections 7-11-602 and 7-11-712 and of Opportunity for a Hearing (the "Notice") to Timothy M. Kelly (the"Respondent").

II.

The Director makes the following findings of fact and conclusions of law with respect to this order:

1. Upon information and belief, Timothy M. Kelly ("Kelly") is licensed as an insurance producer by the Department of Business Regulation, and is a resident of the State of Rhode Island.
2. On February 22, 2000 the Securities Division of the Department of Business Regulation (the "Securities Division") received a complaint that a senior resident of this state had been offered

and sold an investment in fourteen pay telephones located in the State of Utah for a total cost of $70,000.

3. According to the complaint the investment was offered and sold by AB to Z Financial and Gayle M. Jendzejec to the investor who was told that the pay telephone investment carried a fourteen percent rate of return and was appropriate for retirement income.

4. The Securities Division is aware of actions by several jurisdictions against companies and their sales representatives who have offered and sold pay telephone investments without registration and licensing under the securities laws.

5. On February 23, 2000 the Securities Division conducted an examination of the books and records of the AB to Z Financial and extensive interviews with Gayle M. Jendzejec and Louisa M. Montecalvo, the sole members of AB to Z Financial and licensed sales representatives of Lincoln Financial Advisors Corp, a licensed broker dealer. During the course of the interview they told the examiners that Marc Sutherland, Leonard Martin and Jeffrey Massey were also selling pay telephone investments.

6. On March 6, 2000 an examination of the books and records of Leonard Martin and Jeffrey Massey was conducted by the Division. During that examination documents and files were located which show that individuals were offered and sold pay telephone investments by Jeffrey Massey, Leonard Martin, and Timothy M. Kelly.

7. Prior to these sales, Kelly executed sales representative agreements with Jeffrey Massey and his company, Massey and Associates, which provided that he would be paid a 14% commission for all pay telephone sales procured by him.

8. Jeffrey Massey also received override compensation on Kelly's sales and in addition sold pay telephones to his clients for which he received the full commission.

9. The pay telephone investments sold by the Respondent constitute an investment contract and therefore securities under 7-11-101(22) of RIUSA. These investments are subject to the registration, licensing and disclosure requirements under the statute.

COUNT I

VIOLATION OF SECTION 501 OF RIUSA BY NOT PROVIDING ADEQUATE DISCLOSURE TO INVESTORS

10. Paragraph 1 through 9 above are incorporated in this Count I.

11. Section 501 of RIUSA provides that in the offer to sell, offer to purchase or purchase of a security, a person may not directly or indirectly make an untrue statement of material fact or omit to state a material fact necessary in order to make the statement made, in light of the circumstances under which they are made, not misleading.

12. The Respondent offered and sold securities to several investors without making adequate disclosures and failing to inform the investors of material facts with respect to their investment

including, but not limited to, risk of the investment and the fact that these investments constitute securities under RIUSA.

COUNT II

VIOLATION OF SECTION 301 OF RIUSA BY SELLING UNREGISTERED SECURITIES

13. Paragraph 1 through 9 above are incorporated in this Count II.

14. Section 301 provides that a person may not offer to sell or sell a security in this state unless the security is registered, exempt from registration or is a federally covered security.

15. The Respondent offered and sold securities in the State of Rhode Island without registration in violation of RIUSA.

COUNT III

VIOLATION OF SECTION 201 OF RIUSA BY NOT BEING LICENSED AS A BROKER DEALER OR SALES REPRESENTATIVE

16. Paragraph 1 through 9 above are incorporated in this Count III.

17. Section 201 of RIUSA provides that no person may transact business in this state as a broker dealer or sales representative unless licensed or exempt from licensing.

18. Respondent Timothy Kelly was acting as a broker dealer as defined in Section 101 (1) of RIUSA, and a sales representative under section 101 (20) of RIUSA, without proper licensure in violation of RIUSA.

Based on the foregoing, the Director determines that the following action is necessary to prevent or avoid an immediate

danger to the public welfare, that it is in the public interest, appropriate for the protection of investors and consistent with the purposes fairly intended by the policy and provisions of RIUSA.

Accordingly, IT IS HEREBY ORDERED THAT:

(1) Respondent and any person associated therewith shall immediately cease and desist from any further violation of Sections 201, 301, 501 of RIUSA.

(2) Respondent and any person associated therewith shall retain and maintain all written and computer records regarding its business activities and the subject offering until further order of the Director.

THEREFORE, unless the Director receives a written request for a hearing and answer to this Notice within thirty (30) days of the date of this Notice, the Director will regard Respondent as having been provided notice and an opportunity for hearing, and as having waived the right to a hearing. Further, unless such written request for a hearing is received within the time period specified above, no hearing will be held on this matter and the Director will by order grant the relief requested herein.

Pursuant to Section 7-11-602(b), if the Director reasonably believes that a violation of RIUSA has occurred, he may (after such notice and hearing in an administrative proceeding unless the right to notice and hearing is waived by a person against whom the sanction is imposed), issue a Cease and Desist Order against a person who violates this chapter or rule of the director, and impose a civil penalty up to a maximum of ten thousand dollars

Should say FURTHER re penalty

($10,000) for a single violation or of one hundred thousand dollars ($100,000) for multiple violations, in addition to any specific power granted under the Act.

Dated this 16 day of March, 2000.

Tom Schumpert Director
Rhode Island Department of
Business Regulation

DBR #00-0083

THE DIRECTOR RESERVES THE RIGHT TO PUBLISH A NOTICE OF THIS ORDER IN A NEWSPAPER OF GENERAL CIRCULATION IN THE STATE OF RHODE ISLAND.

kelly.c&d

CERTIFICATION

I hereby certify that on this 30th day March, 2000, that I caused a copy of the within Emergency Order to Cease and Desist to be mailed, via certified and first class mail to: Timothy M. Kelly, 840 Smithfield Avenue, Lincoln, Rhode Island 02865

Antonetta Budano

EXHIBIT D

STATE OF RHODE ISLAND
DEPARTMENT OF BUSINESS REGULATION
SECURITIES DIVISION

POLICY STATEMENT ON VIATICAL SETTLEMENT CONTRACTS

The Securities Division (the "Division") of the Rhode Island Department of Business Regulation has received numerous inquiries from investors, viatical settlement companies and participants in the securities industry generally regarding the treatment of viatical settlements under the Rhode Island Uniform Securities Act ("RIUSA"), *R.I. Gen. Laws* §§ 7-11-101, et. seq. (1990). The Division is aware of instances in which viatical settlements are advertised to the investing public as 100% secure, with "guaranteed" rates of return as high as 40% or more. Many persons making such claims have not registered the viatical settlement agreements for sale in Rhode Island, and more often than not, the persons offering the same have not been registered under RIUSA as broker-dealers, agents, investment advisers or investment adviser representatives.

The Director of the Department of Business Regulation has the statutory authority to enforce the laws governing the issuance, sale and other transactions relative to securities in Rhode Island, and to utilize any specific power granted under RIUSA if he "reasonably believes . . . that a person has violated [RIUSA] or a rule or order of the Director under [RIUSA]." *R.I. Gen. Laws* § 7-11-602 (1990). Toward that end, and following a careful consideration of the applicable provisions of RIUSA, the regulations promulgated thereunder, and relevant case authority, the Division concludes that for the reasons set forth herein, viatical settlement investments should be treated as securities subject to the registration and other provisions of RIUSA.

EFFECTIVE DATE MARCH 7, 2001

In general, a viatical settlement agreement is a written agreement entered into among a viatical company facilitating the transaction, an investor (or a group of investors) and a medically documented terminally ill person who is the owner of a life insurance policy or who is covered under a group policy insuring the life of such person. The premise behind the viatical settlement is to give those with a catastrophic or terminal illness monetary means with which to live and to pay medical expenses when the medical condition is at a stage where continued employment may not be possible. The viatical settlements are also being offered as life settlements to individuals who desire to sell their life insurance policy but are not terminally ill. In the agreement described above, the insured agrees to sell the life insurance policy at a discount, the amount of which is based on the life expectancy of the insured, current interest rates and the profit requirement of the investors and the viatical company. The viatical company (or a trust established by the viatical company) is named as the irrevocable beneficiary and is obligated to continue making the necessary premium payments.

In the alternative, the viatical company may simply match potential buyers with the policyholders in an arrangement whereby the investor acquires direct ownership rights in the policy. Under either arrangement, the viatical company offers and sells fractional interests in the policy to investors, thus eliminating the need for direct contact between the insured and the investor. Upon the death of the insured, the viatical company receives the face value of the policy, which is then used to repay investors a profit equal to the difference between the discounted purchase price paid to the insured and the death benefit collected under the policy from the insurer, less certain administrative costs and expenses, including premiums and a commission to the viatical company.

The question of whether or not, the foregoing arrangement, the sale of these viaticals to investors is properly characterized as a security is answered by reference to long-standing principles governing the interpretation of RIUSA by both the Division and the courts. The statutory definition of a "security," *R.I. Gen. Laws* § 7-11-101 (22) (1990), is in all material respects identical to that contained in most state acts and the Securities Act of 1933. This

...tion of a security includes the term "investment contract." In *SEC v. W.J Howey Co.*, 328 U.S. 293 (1946), the United States Supreme Court held that an investment contract has four principal elements or criteria: (i) the investment of money; (ii) in a common enterprise; (iii) with an expectation of profits; (iv) to be earned through the efforts of others. Although Rhode Island courts have not yet explicitly adopted the "Howey test," virtually every other jurisdiction has adopted *Howey's* definition of investment contract in some form.

We are aware of the decision in *SEC v. Life Partners, Inc.*, 87 F.3d 536 (D.C. Cir. 1996), in which the Securities and Exchange Commission ("SEC") sought to enjoin a viatical settlement company from violating the registration requirements of the Securities Act of 1933. Prior to ... in life insurance policies, the viatical company evaluated the selling fractionalized interests ... price and insured's medical condition, reviewed the insurance policies, negotiated a purchase price ... prepared legal documents. The SEC argued that this arrangement was an investment contract under the *Howey* standard and that the company was accordingly in violation of section 5 of the Securities Act of 1933.

Although the Court of Appeals found the first three elements of *Howey* to be satisfied, it disagreed with the SEC's position regarding the fourth element. The court concluded that the investor's return was not dependent upon the effort of the viatical company, but rather from the length of time the insured remained alive. "In this case it is the length of the insured's life that is the overwhelming importance to the value of the viatical settlements." 87 F.3d at 548. The court noted that the fourth prong in *Howey* is concerned only with the promoter's activities after the investor parts with his money, and that the company's post-purchase activities in that case had no effect on the investor's return, constituting merely administrative or ministerial functions.

The Division does not agree with the outcome or rationale in the *Life Partner's* decision. The Division is of the view that the first three elements of the *Howey* investment contract analysis are clearly present in a viatical settlement arrangement. Furthermore, there is little support in over fifty years of judicial authority since the *Howey* decision, for drawing the "bright-line" distinction between "pre-investment" and "post-investment" managerial efforts

which the Court of Appeals attempted to draw in *Life Partners*. Both federal and state case law support the conclusion that the fourth element of the Howey definition is met when, upon a review of all of the efforts of the promoter as a whole, a court may conclude that the investor's realization of a profit depends substantially upon the essential management efforts of the promoter, regardless of the time at which such services are performed.

In fact, the investors in typical viatical settlement arrangements are, as a rule, completely passive, relying upon the expertise of and information gathered by the viatical company in predicting the insured's life expectancy, preparing the documentation for investment and performing all other functions essential to the investor's ability to achieve a profit. The investors do not have the skill, knowledge or access to information to perform the tasks which are necessary for their investment to be successful.

The actions which may be, and usually are, performed by the viatical company in connection with the settlement transaction include, but are not limited to: identification of insured parties with short life expectancies; evaluation of the medical condition of the insured; analysis of the life expectancy of the insured; determination of the discount at which to purchase the policy; evaluation of the terms and conditions of the policies; effectuation of the legal transfer of the policy from the insured; effectuation of changes in beneficiaries; determination of whether an insured party has died to ensure timely submission of claims for death benefits; submission of clause for death benefits to insurance companies; acceptance of payment of death benefits from insurance companies; pooling of the policies for investors; computation and distribution of pro rata shares of benefits to investors; and other actions in the process of selecting, evaluating, acquiring and packaging insurance policy benefits to be purchased. These functions are at the very heart of the entire viatical settlement transaction; accordingly, they are the type of entrepreneurial efforts which are sufficient to satisfy the fourth prong of the *Howey* test.

The *Life Partners* court further ignored a critical element vital to the success of a viatical investment and which must occur after the viatical agreement is consummated. This element is

the necessity of payment of premiums on the policy. If this task is not performed, the policy will lapse and the entire investment will collapse. Very rarely is it left to the investor to ensure that the premiums are paid. Rather, it is the promoter's responsibility (or the escrow agent picked by the promoter) to ensure these payments are made.

In *Howey*, the Supreme Court stated that the definition of a security "embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits." 328 U.S. at 299. To adopt the "bright line" distinction of the Court of Appeals in *Life Partners* would be to accept the "static principle" about which the Supreme Court warned, and to elevate the form of the transaction over its substance. The Division is of the view that a more flexible approach is consistent with the remedial purpose of RIUSA, which should be interpreted broadly to afford the maximum possible protection to Rhode Island investors.

Moreover, the position adopted today is consistent with that of other jurisdictions. In response to fraud within the viatical industry, forty-four of the fifty states currently regulate viatical settlements to some degree. *See, e.g.*, "Division Announces its Position on Viatical Settlements," Ohio Sec. Bull. 98:3 (Ohio Div. of Sec.); *Viatical Settlement Agreements, No.* 0-0 1997, 1997 Wa. Sec. Lexis 21 (Wash. Sec. Div., July 14, 1997); *Viatical Settlements*, 1996 Wy.-No Act. Lexis 3 (Wy. Sec. Div. April 26, 1996); Interpretative Opinion, 1995 Kan. Sec. No Act. Lexis 188 (Kan. Sec. Comm'r, Nov. 14, 1995).

For the foregoing reasons, the Division opines that investments in viatical settlement agreements as described in this statement are investment contracts, and therefore constitute securities, within the meaning of *R.I. Gen. Laws* § 7-11-101 (22) (1956). A number of consequences flow directly from this conclusion. RIUSA requires that every security offered and sold in this state must be registered with the Division unless the security itself is exempt or unless the transaction pursuant to which the security is sold is exempt. *R.I. Gen. Laws* § 7-11-301 (1990). If the security or transaction is exempt from registration under *R.I. Gen. Laws* §§ 7-11-401, 7-11-402 (1990), the issuer should determine if the exemption is self-executing or if it

requires a form filing with the Commission. If no exemption is available and registration is therefore required, the issuer should review the provisions of *R.I. Gen. Laws* §§ 7-11-302 through 7-11-305 (1990) to determine the appropriate form of registration filing and to review other substantive and procedural requirements.

Persons engaged in the business of effecting transactions in securities must be registered with the Division as broker dealers, and individuals who represent broker dealers must be registered as sales representatives, unless they qualify for an exemption from registration. Persons engaged in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issue or promulgate analyses or reports concerning securities must be registered with the Division as investment advisers and certain individuals employed by or associated with an investment adviser must be registered as investment adviser representatives, unless they qualify for an exemption from registration.

Finally, all persons involved in the offer and sale of viatical settlements in Rhode Island should be aware of the nature and extent of the antifraud provisions of RIUSA. *R.I. Gen. Laws* § 7-11-501 (1990) provides that, in connection with the sale of any security in Rhode Island, it is unlawful to employ any device, scheme or artifice to defraud; to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they are made, not misleading; or to engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person. The antifraud provisions of RIUSA apply in the case of every offer or sale of a security in Rhode Island, including those instances in which the sale of the security is exempt from registration and the seller is exempt from licensing. Violation of the registration, licensing or antifraud provisions of RIUSA constitute a felony and may result in criminal prosecution of the offender.

The Rhode Island Uniform Securities Act was promulgated to regulate viatical settlement investments. Such investments involve unknown risks that unscrupulous promoters may misrepresent or fail to disclose to investors. The Division concludes that viatical settlements are securities as that term is defined under Rhode Island law, and it is therefore appropriate for the Division to assert its regulatory jurisdiction. The Division arrived at its conclusions based on current Rhode Island law and the long-standing public policy of investor protection. The Securities Division has no position and makes no representations on the social value of viatical settlements.

Dated this the 14th day of February, 2001.

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TIMOTHY M. KELLY
1159 DOUGLAS AVE. APT 7
NORTH PROVIDENCE, RI
02904

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