

U.S. Department of Justice

*United States Attorney
District of Utah*

FOR IMMEDIATE RELEASE

January 18, 1989

For further information call:

United States Attorney Brent D. Ward

Assistant United States Attorney Stewart C. Walz

Special Assistant United States Attorney Mary Beth Walz

524-5682

PRESS RELEASE

Brent D. Ward, United States Attorney for the District of Utah, Robert M. Bryant, Special Agent in Charge of the Salt Lake City Division of the Federal Bureau of Investigation (FBI), Robert H. Davenport, Regional Administrator of the Denver Regional Office of the United States Securities and Exchange Commission (SEC), and Donald M. Hoerl, Assistant Regional Administrator of the Salt Lake City Branch Office (SLBO) of the United States Securities and Exchange Commission, jointly announced a thirty-six count Indictment and seven Informations charging criminal conspiracy, securities fraud, violation of the registration provisions of the federal securities laws, and wire fraud. The Indictment and Informations charge a total of ten different defendants, nine of whom reside in the Salt Lake City area, with participating in a scheme to effect an unlawful public distribution of securities purportedly of Protecto Industries, Inc.; to manipulate the price of the securities upward; and to then pledge certain of the securities as collateral for a loan from a bank. Although the criminal charges vary as to the individual defendants, all charges arose from participation in the common scheme involving Protecto Industries, Inc. Involved are shell corporation promoters, an affiliate of a broker-dealer firm, transfer agents, accountants and an attorney.

The INDICTMENT charges ROBERT C. GLEAVE, a registered representative with Xcel Securities, Inc., of Denver, Colorado, with violating 18 U.S.C. § 371 (conspiracy); 15 U.S.C. § 78j(b), 17 C.F.R. § 240.10b-5 and 15 U.S.C. § 78ff (securities fraud); 15 U.S.C. § 77e and 15 U.S.C. § 77x (nonregistration of securities); and 18 U.S.C. § 1343 (wire fraud). CANDACE M. LaCASTO, with Olympic Stock Transfer, a professional transfer agent, and O. ROBERT MEREDITH, a lawyer, of the Salt Lake City area, are charged with conspiracy. Seven unindicted co-conspirators have been or will be charged by Information.

Seven separate INFORMATIONS to which pleas of guilty have been or will be entered, charge DEAN S. LEMMON, a stock broker, (one count - conspiracy); JERRY D. TIMOTHY, a salesman of public “shell corporations” (conspiracy and two counts securities fraud); LORAINÉ C. TIMOTHY (one count misdemeanor Rule 10b-5 violation); MARVIN D. HANEY, a Certified Public Accountant (conspiracy and one count securities fraud); RICH N. HANSEN, a stock promoter (conspiracy and one count securities fraud); ROGER G. COLEMAN, owner of Efficient Transfer, Inc., a professional stock transfer agent (one count misdemeanor Rule 10b-5 violation); and PAUL N. NIELSEN, a middleman for accountants and lawyers (conspiracy and one count securities fraud). Certain of the guilty pleas involve agreements to cooperate in the continuing investigation.

THE GENERAL PROBLEM OF FRAUD IN THE PENNY STOCK MARKET

Commenting on problems in the penny stock market, Mr. Ward said: “For years Utah has been criticized as a hotbed of criminal fraud. We in law enforcement have applied tremendous effort to eradicate one form of that fraud--investment fraud. Today, we launch a frontal attack on

the most fundamental source of Utah's bad reputation in the securities industry--fraud and manipulation in the over-the-counter market for low-priced securities, or the "penny stock" market. For the most part these stocks are thinly-traded and subject to domination and control by a single market maker. As a result, they are an attractive vehicle for manipulative, artificial schemes designed to raise the price or trading volume of these securities. Innocent investors are hurt by large markups and large commissions and end up holding worthless stocks for which they have paid a great deal of money. These are the type of investors who can least afford such losses." Ward added, "by this action we announce our intention to use the threat of incarceration against fly-by-night purveyors of 'hot stocks'. Investors are entitled to a level playing field, which is not always the case with penny stock transactions."

Ward said that last October David Ruder, Chairman of the Securities and Exchange Commission, said in a speech to the Twenty-First Annual Rocky Mountain - State - Federal Provincial Securities Conference in Denver, "Over the past year, we have received indications that penny stock manipulations are increasing nationwide.... They are no longer centered in Denver and its 'sister' city of Salt Lake, where, unhappily, these problems have existed for many years. They are expanding to other areas, including Miami, Seattle, Atlanta, Chicago, and Los Angeles." Ward said penny stock schemes "are growing in part because of the advent of computerized telephone calling and lower long-distance telephone rates."

NATURE OF THE CHARGES

Speaking of the particular scheme alleged in the charges announced today, Ward said:

“In this case undercover FBI agents let it be known they wanted to buy a shell corporation--usually a company with no operating history, few or no employees, few or no assets, and, often as not, no legitimate business prospects. Once this word went out, people came out of the woodwork.”

Ward said the charges describe a typical manipulative device known as a “box job”. In a “box job” a few insiders have control of all or almost all (in this case 90%) of the stock to be manipulated.

In this case the indictment alleges a scheme with three phases. First, defendants Lemmon, Timothy and Hansen allegedly contrived to revive a shell corporation old enough (pre-1933) to evade securities registration requirements.

Once the shell company was found, a dummied-up shareholder list was allegedly prepared using names selected at a genealogical library. Hansen and Lemmon charged \$40,000 for this service. Then, the shell company was merged into a new corporation known as Protecto, Industries.

Second, in order to have stock in Protecto listed on the pink sheets, which contain over-the-counter stock quotations, due diligence information must be submitted to the National Quotation Bureau. Defendant Nielsen allegedly procured the services of defendant Haney, a

CPA, to prepare fake financial statements for this purpose: a first set for \$10,000 and a second set for \$5,000. It is also alleged that defendant Meredith, an attorney, provided a legal opinion on the “tradability” of the stock which he did not modify or withdraw after learning that securities fraud was involved. Submission of this information made it possible for the stock to be “pinked” or quoted on the pink sheets.

Third, it is alleged that defendants Gleave and others conspired to manipulate the market in Protecto stock through “matched” trading, creating a false impression of real market activity and artificially driving up the price of the stock. “Matched” trades are trades among insiders using nominee names to hide their control of the stock being traded.

The alleged goal of the scheme is alleged to have been the the manipulation of Protecto stock until it reached a level of \$2.00 per share. The stock was then to be pledged as collateral on a loan to be sought in Guam.

Details of the scheme alleged in the indictment follow.

UNDERCOVER FBI INVESTIGATION

The Indictment and Informations are the first publicized results of an ongoing FBI investigation. SEC employees gave assistance and advice where expertise in securities matters was required. Evidence already presented to the U. S. Attorney’s Office is still being analyzed regarding Protecto Industries, Inc. and other schemes for additional possible charges and defendants. According to Mr. Bryant, Special Agent in Charge of the FBI’s Salt Lake City

Division, this investigation focused on criminal activities that, within the past few years, have increased in nationwide notoriety and are often associated with penny stocks in general as well as with Salt Lake City. These activities involve shell corporation promotion schemes and manipulation of penny stocks.

Messrs. Ward, Bryant, Davenport and Hoerl emphasized that this investigation illustrates the effectiveness of innovative investigative techniques used by the FBI, in particular undercover FBI operations to infiltrate highly sophisticated white collar schemes, supplemented by the expertise of the SEC. Given the already publicly announced successes of this operation, they anticipate expansion of joint and cooperative investigations to possibly include other state and federal agencies, including the Internal Revenue Service and the Utah Division of Securities.

Messrs. Davenport and Hoerl indicated that the SEC staff is analyzing information received from this investigation for possible recommendations for additional action against attorneys, accountants, broker-dealer firms, transfer agents and persons associated with these firms.

THE PROTECTO INDUSTRIES SCHEME

The Indictment alleges, among other things, that each of the defendants named above, as well as certain other unindicted co-conspirators, participated in a scheme beginning in about September 1987 and continuing to about September 1988 that involved the following. The co-conspirators were to provide to certain individuals a public shell corporation to be merged with a private corporation. In this case the individuals to acquire the shell corporation were undercover

agents. Ownership and control of 90% of the stock of the resulting purportedly public corporation was to be delivered to the purchasers (the FBI agents). The co-conspirators were then to help the FBI agents manipulate the stock price upward in public trading to enable the agents to use the stock at its artificially inflated value as security for a loan from a bank.

The Indictment further alleges, among other things, that each of the defendant-co-conspirators engaged in the overt acts described below in furtherance of the scheme.

On or about September 8, 1987, defendant Hansen brought unindicted co-conspirator Lemmon to the office of the FBI agents where they discussed the purchase and trading of a public shell corporation the agents desired to acquire for merger with their private corporation. In January, 1988, Lemmon mentioned to the agents the name of Business Finance Services, Inc. as the public shell corporation to be merged with their private corporation. Business Finance was incorporated in Delaware on May 2, 1924; its corporate status was revoked on March 16, 1927. Business Finance was fraudulently “revived” by defendant Jerry D. Timothy on May 23, 1986. Lemmon subsequently paid Timothy \$20,000 for the corporation. In return, Lemmon was furnished documents showing that two of Timothy’s associates were the last remaining officers of Business Finance. Lemmon was also furnished a purported list of shareholders of Business Finance. In fact neither of Timothy’s associates had ever been a duly elected officer of Business Finance, and the purported shareholder list was a fiction created by Timothy and his associates by taking names from records from a genealogical library in Salt Lake City.

Lemmon also told the agents in early January, 1988, that a Nevada resort check indicated they could use the name "Protecto Industries, Inc." ("Protecto") as the name of the new corporation. On or about February 1, 1988, Lemmon went to Nevada to file corporate documents for Protecto.

Also in January, 1988, the agents met with defendant Coleman at Coleman's business, Efficient Transfer, Inc. in Salt Lake City. Subsequently, Efficient Transfer went out of business and defendant LaCasto of Olympic Stock Transfer in Salt Lake City became the transfer agent for Protecto.

From September, 1987 to February, 1988, defendant Hansen attempted to provide the undercover agents with a certified public accountant who would provide false financial statements for the resulting public corporation. Financial statements must be included in the "due diligence package" which is mandated by Rule 15c2-11 of the Securities Exchange Act of 1934. In February, 1988, defendant Hansen introduced the agents to defendant Nielsen who was to find a certified public accountant to prepare the financials. In about March, 1988, defendant Nielsen introduced the agents to unindicted co-conspirator Marvin D. Haney, a certified public accountant, who provided the agents false audited financial statements which falsely showed Protecto to have assets valued at \$937,036.78 at a time Protecto had virtually no assets. Haney was paid \$10,000 for providing the false financials.

In February and March, 1988, the agents met with defendants Hansen and Gleave at Xcel Securities, Inc. in Englewood, Colorado. Gleave was a trader and broker at Xcel. Gleave was

given \$5000 cash for himself and \$500 each for three other market makers. On March 18, Lemmon received \$20,000 from the agents for the corporation purchased and provided them with stock powers for the stock of Protecto. That same day Lemmon called Gleave who told him that five accounts would be opened at Xcel Securities and other accounts at other broker-dealers.

On March 24 Gleave told the agents that certain things were needed: money for himself; three envelopes with \$500 cash in each for three other market makers; \$5000 in an Xcel account in Lemmon's name; and stock certificates in specified amounts for five accounts at Xcel. LaCasto furnished the stock certificates to the agents that same day. Also that same day, Lemmon and Gleave plotted the trading in Protecto stock. On March 31 Gleave caused the sale of 5000 shares of Protecto stock from an account at Western Capital Securities in Salt Lake City to Xcel Securities. The stock was sold in an account in the name of Lemmon's wife.

About April 15, 1988, the agents met with Lemmon and Jerry Timothy to discuss a prior sale of Business Finance by Timothy. Timothy stated he would do whatever it took to clean up the matter. About April 22 Lemmon furnished the agents documents indicating filings made in Nevada to correct the situation, but about April 29 Timothy told the agents filings would be needed in Delaware. About May 2, Loraine Timothy told the agents of an amendment regarding a name change in Delaware. That same date Lemmon provided the agents with a document entitled "Certificate of Amendment of Certificate of Incorporation of People's Jitney Taxi Company".

On about May 1, 1988, Lemmon told the agents that Loraine Timothy had told him that “For our protection and with the transfer agent as sensitive as it is, we want to surrender all the stock certs [certificates] and get brand new ones.” About May 17 Loraine Timothy told the agents that she had talked to Candace at great length and that “We’ve decided that I’m just going to take, uh, the old ones over to her and she’s going to tell, if she’s ever, you know, investigated, that the stockholders brought them in and got the new certificates. We’ve got it all figured out.”

About May 31, Loraine Timothy told the agents she was working with a lawyer on minutes. That same date, in a meeting with the agents and Lemmon, Jerry Timothy stated that defendant Meredith would prepare a legal opinion for Protecto. On about June 2 Loraine Timothy told the agents that she had received a call from the attorney regarding changes to the minutes, she would resubmit them to the attorney the following day, and he would then write the “tradability” opinion. That same date, the agents had a conversation with Meredith regarding the corporation and received from LaCasto stock holder records.

On about June 16, 1988, Lemmon provided that agents with various documents regarding People’s Jitney and Protecto, including a “tradability” opinion dated June 13, 1988, written by Meredith. The package included a Rule 15c2-11 statement falsely stating that People’s Jitney was reinstated on March 22, 1988, and the shareholders approved changing the name to Protecto on April 2, 1988.

As to the charges alleged in the Indictment, the defendants and unindicted co-conspirators are presumed innocent until proven guilty. As indicated, certain of the co-

conspirators were charged by Information, and certain of them have already entered pleas of guilty.