

1 The investor filled in the information and returned the card. SCAFETTA telephoned the investor
2 and scheduled an appointment to meet with her, at her residence, sometime in April or May
3 1996. SCAFETTA scheduled monthly meetings with Investor One during the next several months.
4 During one of the meetings the investor disclosed that she had approximately \$380,000 in a
5 diversified liquid account with Bank One.¹ She was not an accredited investor. SCAFETTA
6 advised her to immediately sell her stock because she could lose all her money and never be able to
7 recover financially. Investor One's husband, who had always managed their financial affairs, had
8 recently died. She did not fully understand everything SCAFETTA said, but trusted his opinion.
9 She told him she needed an investment to supplement her income. It was after this disclosure that
10 SCAFETTA and the investor were involved in four separate transactions.

11 2. In the first transaction, SCAFETTA convinced Investor One to move the
12 \$380,000 into two separate annuities (for which she was assessed capital gains taxes). She closed
13 her Bank One account and withdrew her funds. The first annuity was purchased from American
14 Investors Life Insurance Company ("American"). On February 19, 1997, the investor signed an
15 annuity application with American, policy #293077. The cost was \$250,000 for the annuity. The
16 maturity date was February 20, 2012, at which time Investor One would be 82 years old. The
17 second annuity, purchased from American Equity Investment Life Insurance Company
18 ("American Equity"), on or about April 1, 1997, cost \$130,000. The American Equity policy
19 would mature April 7, 2025. Investor One would be 95 years old when the policy matured.
20 American paid interest of 8.25% for the first year and the minimum guaranteed interest rate was
21 3.25%. American Equity paid 8.4% for the first year and the minimum guaranteed interest rate was
22 3% thereafter. Investor One remembers SCAFETTA telling her that she would earn 8.5% interest
23 for the next five years on each of the investments. SCAFETTA received commissions of \$34,900
24 for the sale of the two annuities.

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26 ¹ The Bank One account included investments in the stock market, mutual funds, money market
account, municipal bonds, government securities, tax-free trusts, and unit investment trusts.

1 3. The third transaction between the investor and SCAFETTA occurred in February
2 1997. SCAFETTA sold the investor a \$37,000 single premium, Universal Life contract with an
3 extended rider, and the benefit of convalescent care. Some time afterwards, the investor's
4 accountant reviewed the material regarding the Universal Life contract. He informed her that she
5 did not need that coverage. The investor canceled the policy and received her money back
6 without penalty.

7 4. During their monthly meetings SCAFETTA told the investor that he developed a
8 method of playing the stock market. SCAFETTA guaranteed a 20% rate of return and suggested
9 they each invest \$6,000. If his investments provided more than 20% interest, he would split any
10 additional income with her. On May 14, 1997, the investor wrote SCAFETTA a check from her
11 money market account for \$6,000 and entered into her fourth transaction with SCAFETTA. In
12 return for the money, Investor One received a one-page agreement entitled a "Demand Note"
13 ("Note"). The Note was typed, with blank spaces filled in by SCAFETTA. The Note specified an
14 interest rate of 20% on the investment, due within 365 days of demand. SCAFETTA could use the
15 investment money "as he sees fit." The Note also specified that any profits above and beyond the
16 interest paid were to be split 50% to each individual, minus taxes. Investor One would receive no
17 less than the principal plus 20% interest. A handwritten statement at the bottom of the contract
18 stated that the Note was void and replaced by a note dated September 23, 1998.

19 5. On September 23, 1998, Investor One and SCAFETTA signed another agreement
20 entitled "Demand Note" ("1998 Note"). SCAFETTA did not think it was fair that he assumed all of
21 the investment risk and asked Investor One to sign a second note. The single page 1998 Note was
22 the same type used in the previous agreement. SCAFETTA entered information in the blank spaces.
23 All references to interest had been crossed out on the document. The reference to Investor One's
24 receipt of no less than the principal plus 20% was not included in this 1998 Note. The 1998 Note
25 specified that SCAFETTA could invest the money "as he sees fit." Further, the profits would be
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1 split 50% each, between Investor One and SCAFETTA after deduction of taxes. Both parties signed
2 the form.

3 6. The investor attended an American Express seminar in Sun City. Someone
4 reviewed her annuity contracts and informed her that the 8.5% rate of return was only guaranteed
5 for the first year and not five years. Since SCAFETTA told her that she would receive 8.5%
6 interest for five years she became concerned. She met with her accountant and attorney who
7 reviewed her annuity contracts. Both informed her that the annuities were unsuitable for
8 someone her age, and confirmed that the 8.5% rate of return was only for the first year of the
9 contract. The investor contacted American and explained that she had been misled. American
10 denied her request for a full refund of her policy without surrender charges in February 1999.
11 The accumulated value was \$250,198.62 and the surrender value was \$225,698.62.

12 7. Investor One realized she had not received any account statement on either Note
13 for approximately sixteen months. She had asked SCAFETTA for a statement of her account and
14 received an account statement from First Albany Corporation. The statement was dated May
15 1998, and was in SCAFETTA'S name only. The statement showed the purchase of stock costing
16 \$4,577.16. The stock was purchased May 7 and 13, 1998. The account balance in May 1998, was
17 \$3,937.78. The balance amount consisted of the combined total of funds invested in stocks and
18 cash in a money market. The investor requested that SCAFETTA return the money. He
19 explained that he needed more time because he did not have the money.

20 8. After repeated requests for a refund, Investor One eventually filed complaints with
21 the Insurance Department and the Better Business Bureau. After the complaints were filed,
22 SCAFETTA provided Investor One with a personal check for \$8,200.

23 Investor Two

24 9. Investor Two met SCAFETTA in 1995. She was a 67 year-old widow and a
25 resident of Arizona. She did not graduate from college and was not a sophisticated investor.
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1 Investor Two was interested in purchasing a Certificate of Deposit ("CD") paying 6.9% annually.
2 Her investments consisted of bonds, money market funds, and mutual funds. Investor Two read a
3 newspaper advertisement offering good rates on CD's. She called the telephone number and
4 talked to SCAFETTA. At the time he was an independent representative with Banknet and
5 offered bank CD's through its brokerage. Investor Two wrote a check for the investment, but the
6 transaction fell through. When she asked about other available investments, SCAFETTA
7 convinced her to invest \$100,000 of her retirement money into a note, Government Financial
8 Series C Commercial Paper Investment ("SERIES C") bearing annual interest at 11.75%.
9 SCAFETTA described this investment as "safe," "insured" and "guaranteed."

10 10. SCAFETTA told Investor Two that the SERIES C investment money would be
11 used to purchase notes through Direct Participation Services, Inc. ("DPSI"), d.b.a. Government
12 Financial. Government Financial engaged in the purchase or financing of short term "account
13 receivables." The receivables represented money owed to small companies that were awarded
14 government contracts, or that had credit insured receivables. On or about March 30, 1995,
15 Investor Two invested \$100,000 or approximately 40% of her retirement money in this program,
16 by investing through SCAFETTA. The subscription agreement, dated March 27, 1995, shows
17 that National Banking Associates employed SCAFETTA. National Banking Associates was not
18 an Arizona registered securities dealer or licensed investment adviser.

19 11. Investor Two was notified in a letter dated June 12, 1995, that the Securities and
20 Exchange Commission ("SEC") had taken possession of the books and records of DPSI.
21 Investor Two received a letter in June 1996, from United Avalon Group, Inc., which identified it
22 as the "trustee for the commercial paper offerings." Investor Two received a check for
23 \$30,294.00 that represented her share of the distribution of funds remaining. On September 19,
24 1996, the SEC filed a complaint in federal court for the Central District of California against
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1 DPSI, Government Financial, and others.² The complaint alleged that the defendants
2 fraudulently sold \$26 million of unregistered securities.

3 12. Investor Two filed a civil suit in Maricopa County Superior Court against
4 SCAFETTA alleging that he sold her an unregistered security, without disclosure of all material
5 facts. A Settlement Agreement was entered into and judgment of \$69,706.00 was entered on
6 December 11, 1998. SCAFETTA is currently in default on the judgment.

7 Investor Three

8 13. In approximately October 1995, Investor Three, then a 66 year-old Arizona
9 resident, read an advertisement in a newspaper. The ad was placed by Senior Information
10 Update ("SIU") and promoted the benefits of establishing a trust. Investor Three called the
11 telephone number listed and scheduled an appointment for a representative to visit to discuss the
12 possibility of establishing a trust. SCAFETTA was the SIU representative that met with Investor
13 Three. She estimates she met with SCAFETTA approximately five times. All of the meetings
14 occurred at her residence.

15 14. SCAFETTA advised her that establishing a trust would be the best thing she could
16 do for her children. Investor Three wrote SIU a check on October 18, 1995, for \$545. The
17 money was to cover the trust fees. SCAFETTA said he needed information regarding her assets
18 and income for the trust. She provided that information. Several days after receiving the trust
19 papers, SCAFETTA came to her residence and took records regarding her mutual funds.
20 Investor Three mentioned to SCAFETTA that if she reinvested the money that was in her mutual
21 funds, she wanted an investment that would provide a regular income. She also wanted to hold
22 back \$10,000 to purchase a vehicle. SCAFETTA provided several forms, which he instructed
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25 ² Securities and Exchange Commission v. Direct Participation Services, Inc. d/b/a Government
26 Financial, Jeffrey A. Lobel, William Rossi, United Avalon Group, LTD., and Frank M. Naft, Civil
Action No. 96-6594 LGB (MCx) (C.D. Cal.).

1 Investor Three to sign. She signed the forms without reading them. Copies of the forms were
2 later sent to her and she noticed they were notarized.

3 15. SCAFETTA said that Investor Three would receive checks every month from the
4 new investment. He did not explain what he invested her money in or whether he received any
5 compensation.

6 16. Investor Three began receiving four monthly checks from USG Annuity & Life
7 Company ("USG"). She discovered that two of the checks were proceeds from her IRA account.
8 She contacted the company and advised them to cancel the two checks. She did not want her
9 IRA balance reduced. Investor Three began receiving two checks each month. She also learned
10 that SCAFETTA did not hold back \$10,000, and she was unable to purchase a vehicle. She
11 contacted SCAFETTA but could not get any clear answers regarding what he invested in and
12 why.

13 17. Investor Three contacted a friend who is an attorney licensed in Arizona. She was
14 told that two of the investments, both annuities, were not the right type for her. The mutual funds
15 had been earning double-digit returns. The annuities only earned a 5% return for a limited period
16 of time. The attorney assisted her in filing a complaint with the Arizona Department of
17 Insurance.

18 18. USG revealed that there are three policies involved. SCAFETTA earned
19 approximately \$16,000 in commissions as a result of selling the three different annuities to
20 Investor Three. The policies include the following:

- 21 a. Policy number 418310 was issued November 13, 1995. It matured April 1,
22 2000. The policy qualifies as an IRA; therefore the money went from one
23 IRA into another. The amount of \$48,718.76 was transferred from a Fidelity
24 IRA account to USG. The interest rate on the USG policy varies, with higher
25 interest during the first year of the policy, but it will not be less than three
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1 percent. SCAFETTA received \$4,871.88 in commissions for the sale of this
2 annuity policy.

3 b. Policy number 418311 is an annuity whose effective date was November 13,
4 1995, and it matures on November 13, 2029, when Investor Three is 100 years
5 old. The amount of \$73,788.68 was transferred from Fidelity mutual funds.
6 The interest rate is higher during the first year of the policy, however the
7 policy will not earn less than three percent annually. SCAFETTA was paid
8 \$7,378.86 in commissions for the sale of this annuity policy.

9 c. Policy number 418290 is an annuity whose effective date was November 18,
10 1995, and the policy matures on November 18, 2029, when Investor Three is
11 100 years old. The amount of \$41,560.29 was transferred from mutual fund
12 accounts with Scudder, Dreyfus and T. Rowe Price. Again, the interest rate on
13 this policy was higher during the first year, and guaranteed no lower than three
14 percent. SCAFETTA was paid \$4,156.02 in commissions for the sale of this
15 annuity policy.

16 19. Investor Three suffered a tax consequence as a result the purchase of these
17 annuities. When the mutual funds were liquidated she had to declare \$15,000 in capital gains and
18 pay an additional \$2,800 in tax. If she had not had to declare capital gains income she would
19 have received a tax refund of between five and six hundred dollars.

20 20. Investor Three contacted USG and requested a refund. The company refused. It
21 explained that after receipt of the policies, the customer had twenty days to review them, and
22 could cancel and receive a full refund, without penalty. In this case, too much time had gone by
23 and USG was not willing to refund the money.

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1 Investor Four

2 21. A local Phoenix attorney filed a complaint against SCAFETTA with the Arizona
3 Attorney General's Office on October 17, 1996. In her complaint, she alleged that SCAFETTA
4 attempted to exploit the estate of Investor Four for his benefit. Investor Four, an Arizona resident
5 who was 78 years old at the time of the incident, was a widow. She and her husband executed a
6 declaration of Living Trust ("Trust") in which they were named the Trustors and Trustees. After
7 her husband's death, Investor Four appointed her nephew as Successor Trustee under the Trust.
8 In January 1995, Investor Four was diagnosed as having dementia, memory loss, and possible
9 Alzheimer's disease, and a moderate degree of cognitive impairment.

10 22. Investor Four met SCAFETTA after she responded to a mailing, in or around May
11 or early June 1996. SCAFETTA contacted Investor Four and arranged a meeting. His business
12 card identified him as "Senior CFO" for SIU. He befriended her and convinced her to allow him
13 access to her assets. Investor Four had the Trust in place, with a savings account in the name of
14 the Trust at World Savings Bank. SCAFETTA appeared with Investor Four at World Savings
15 Bank on June 13, 1996. Investor Four withdrew all of her funds, which totaled approximately
16 \$128,000. The money was put into a new bank account in her name only. SCAFETTA
17 convinced her to use the money to purchase two annuities from Equitable of Iowa Companies in
18 her own name, not the name of the Trust. The combined cost of the annuities was approximately
19 \$158,000. The beneficiary of the annuities was Investor Four.³ The effective date of policy
20 number 450651 is June 25, 1996. The interest rate for the first year was 5% with a guaranteed
21 minimum annual interest rate of 3%. The policy data page indicates Investor Four was 72 years
22 old. The Petition for Emergency Appointment of Temporary Conservator lists her date of birth
23 as November 9, 1918 ("to the best of Petitioner's knowledge"). It appears that Investor Four was
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26 ³ This designation would result in unnecessary probate in the event of her death.

1 actually 77 years old at the time the policy was issued. The policy maturity date is June 25,
2 2024. The policy sold by SCAFETTA will not mature until Investor Four is 105 years old.

3 23. The effective date of the second policy, number 453285, is July 12, 1996. It also
4 lists Investor Four's age as 72 years old. The maturity date on this policy is July 12, 2024.
5 Again, she would be 105 years old before the policy SCAFETTA sold her matures.

6 24. On or around June 18, 1996, SCAFETTA had Investor Four sign an amendment
7 to her Trust reinstating herself as Trustee and removing her nephew as Trustee. This gave her
8 sole control over all her assets. An attorney, unlicensed in Arizona, drew up the amendment.

9 25. SCAFETTA contacted an accountant allegedly on behalf of Investor Four. The
10 accountant sent a letter to Investor Four's nephew requesting that he provide a full accounting,
11 and all Trust financial records.

12 26. Investor Four's nephew became suspicious and filed a petition for the
13 appointment of a conservator. An investigative report by the Probate Court confirmed that the
14 investor's short and long term memories appeared impaired. In addition, Investor Four had great
15 difficulty in providing personal and financial information. The court assigned a conservator to
16 oversee Investor Four's affairs. That individual was successful in canceling the annuities
17 purchased through Equitable of Iowa without any surrender penalty.

18 27. SCAFETTA filed a document with the Probate Court on November 12, 1996,
19 objecting to the probate proceedings. The conservator had alleged that SCAFETTA exploited
20 Investor Four by having her estate plan and assets transferred into another form to his benefit.
21 She also felt that SCAFETTA was attempting to locate and liquidate other assets, which would
22 benefit him to the detriment of Investor Four. Because of early intervention, Investor Four's
23 losses were not large.

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II.

CONCLUSIONS OF LAW

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

5 2. SCAFETTA offered or sold securities within or from Arizona, within the meaning
6 of A.R.S. §§ 44-1801(15), 44-1801(21), and 44-1801(26).

7 3. SCAFETTA violated A.R.S. § 44-1841 by offering or selling securities that were
8 neither registered, nor exempt from registration.

9 4. SCAFETTA violated A.R.S. § 44-1842 by offering or selling securities while
10 neither registered as dealer or salesman, nor exempt from registration.

11 5. SCAFETTA violated A.R.S. § 44-1991 by offering or selling securities within or
12 from Arizona.

13 6. SCAFETTA'S conduct is grounds for a cease and desist order pursuant to A.R.S. §
14 44-2032.

15 7. SCAFETTA'S conduct is grounds for an order of restitution pursuant to A.R.S. §
16 44-2032.

17 8. SCAFETTA'S conduct is grounds for penalties under A.R.S. § 44-2036.

18 III.

19 ORDER

20 THEREFORE, on the basis of the Findings of Fact, Conclusions of Law, and
21 SCAFETTA'S consent to the entry of this Order, the Commission finds that the following relief is
22 appropriate, in the public interest, and necessary for the protection of investors:

23 IT IS ORDERED, pursuant to A.R.S. § 44-2032, that SCAFETTA, his agents, employees,
24 successors and assigns, permanently cease and desist from violating the Securities Act.

1 IT IS FURTHER ORDERED, pursuant to A.R.S. § 44-2032, that SCAFETTA shall pay
2 restitution to investors shown on the records of the Commission in the amount of \$114,200, plus
3 interest at the rate of 10% per annum from the date of each investment until paid in full, subject to
4 legal setoffs for reimbursement received. Payment shall be made in monthly installments as
5 follows: \$3,000 on the date of this Order; \$100 per month on or before the 1st day of each month
6 beginning on May 1, 2001, to September 1, 2002. Beginning September 1, 2002, SCAFETTA
7 shall make monthly installments of \$1,000 per month on or before the 1st day of each month.
8 Payment shall be made by cashier's check or money order payable to the "State of Arizona" to be
9 placed in an interest-bearing account maintained and controlled by the Arizona Attorney General.
10 The Arizona Attorney General shall disburse the funds on a pro rata basis to investors. If all
11 investors are paid in full, any excess funds shall revert to the state of Arizona.

12 If SCAFETTA does not comply with this order of restitution, any outstanding balance shall
13 be in default and shall be immediately due and payable.

14 IT IS FURTHER ORDERED, pursuant to A.R.S. § 44-2036, that SCAFETTA shall pay an
15 administrative penalty in the amount of \$5,000. Payment shall be made by cashier's check or
16 money order payable to the "State of Arizona" in installments as follows: \$1,000 per month on or
17 before the 1st day of each month beginning immediately after complete payment of the full
18 restitution amount. Any amount outstanding shall accrue interest at the rate of 10% per annum

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1 from the date of this Order until paid in full. The payment obligations for these administrative
2 penalties shall be subordinate to any restitution obligations ordered herein and shall become
3 payable after restitution payments have been paid in full. However, if SCAFETTA has defaulted
4 prior to fulfilling his restitution obligations, full penalties are immediately due and payable without
5 regard to subordination.

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

8 **BY ORDER OF THE ARIZONA CORPORATION COMMISSION**

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11 CHAIRMAN

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COMMISSIONER

COMMISSIONER

IN WITNESS WHEREOF, I, BRIAN C. McNEIL,
Executive Secretary of the Arizona Corporation
Commission, have hereunto set my hand and caused the
official seal of the Commission to be affixed at the
Capitol, in the City of Phoenix, this 10th day of
August, 2001.

BRIAN C. McNEIL
Executive Secretary

DISSENT
(KEM)

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.

N/Enforce/Cases/Scafetta/Pleadings/Consent

Decision No. 63949

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CONSENT TO ENTRY OF ORDER

1. PHILIP MICHAEL SCAFETTA ("SCAFETTA"), an individual, admits the jurisdiction of the Commission over the subject matter of this proceeding. SCAFETTA acknowledges that he has been fully advised of his right to a hearing to present evidence and call witnesses and SCAFETTA knowingly and voluntarily waives any and all rights to a hearing before the Commission and all other rights otherwise available under Article 11 of the Securities Act and Title 14 of the Arizona Administrative Code. SCAFETTA acknowledges that this Order To Cease And Desist, Order of Restitution, Order for Administrative Penalties and Consent to Same ("Order") constitutes a valid final order of the Commission.

2. SCAFETTA knowingly and voluntarily waives any right he may have under Article 12 of the Securities Act to judicial review by any court by way of suit, appeal, or extraordinary relief resulting from the entry of this Order.

3. SCAFETTA acknowledges and agrees that this Order is entered into freely and voluntarily and that no promise was made or coercion used to induce such entry.

4. SCAFETTA acknowledges that he has been represented by counsel in this matter, he has reviewed this Order with his attorney and understands all terms it contains.

5. SCAFETTA neither admits nor denies the Findings of Fact and Conclusions of Law contained in this Order. SCAFETTA agrees that he shall not challenge their validity in any present or future administrative proceeding before the Commission or any other state agency concerning the denial or issuance of any license or registration required by the State to engage in the practice of any business or profession.

6. By consenting to the entry of this Order, SCAFETTA agrees not to take any action or to make, or permit to be made, any public statement denying, directly or indirectly, any Finding of Fact or Conclusion of Law in this Order or creating the impression that this Order is without

1 factual basis. SCAFETTA will undertake steps necessary to assure that all of his agents and
2 employees understand and comply with this agreement.

3 7. While this Order settles this administrative matter between SCAFETTA and the
4 Commission, SCAFETTA understands that this Order does not preclude the Commission from
5 instituting other administrative proceedings based on violations that are not addressed by this
6 Order.

7 8. SCAFETTA understands that this Order does not preclude the Commission from
8 referring this matter to any governmental agency for administrative, civil, or criminal proceedings
9 that may be related to the matters addressed by this Order.

10 9. SCAFETTA understands that this Order does not preclude any other agency or
11 officer of this State or its subdivisions from instituting administrative, civil or criminal proceedings
12 that may be related to matters addressed by this Order.

13 10. SCAFETTA agrees that he will not apply in Arizona for registration as a securities
14 dealer or salesman or for licensure as an investment adviser or investment adviser representative at
15 any time in the future.

16 11. SCAFETTA agrees that he will not exercise any control over any entity that offers
17 or sells securities within or from Arizona.

18 12. SCAFETTA agrees that until restitution and penalties are paid in full, SCAFETTA
19 will notify the Director of the Securities Division within 30 days of any change in home address or
20 any change in SCAFETTA'S ability to pay amounts due under this Order.

21 13. SCAFETTA understands that default will render him liable to the Commission for
22 its costs of collection and interest at the maximum legal rate.

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1 14. SCAFETTA consents to the entry of this Order and agrees to be fully bound by its
2 terms and conditions. If SCAFETTA breaches any provision to which he has consented, the
3 Commission may vacate this Order and restore this case to its active docket.

4
5 Philip Michael Scafetta
6 PHILIP MICHAEL SCAFETTA

7 SUBSCRIBED AND SWORN TO BEFORE me this 23rd day of July,
8 2001.

9 Leanne W. Blankinship
NOTARY PUBLIC

10 My Commission Expires:

11 3/22/04



Decision No. 63949