

STATE OF INDIANA       )  
                                  ) SS:  
COUNTY OF MARION     )

BEFORE THE INDIANA  
COMMISSIONER OF INSURANCE  
CAUSE NO. 6211-AG-08-02285-072  
CAUSE NO. 6211-AG-08-0228-073

IN THE MATTER OF:                     )  
  )  
RICHARD E. GEARHART and/or         )  
GEARHART & ASSOC. INC.,            )  
  )  
                          Producer/Respondent.)  
  )  
900 Parker Place, #B                 )  
Schererville, IN 46375             )  
  )  
Type of Agency Action: Enforcement   )  
  )  
                          License No. 2727580   )

FILED

AUG 27 2010

STATE OF INDIANA  
DEPT. OF INSURANCE

**FINAL ORDER DENYING OBJECTIONS TO RECOMMENDED ORDER AND**  
**AFFIRMING RECOMMENDED ORDER**

The Executive Director and Acting Commissioner of the Indiana Department of Insurance, Stephen W. Robertson, having read and reviewed the Administrative Law Judge John Kissling's Findings of Fact, Conclusions of Law, and Recommended Order and the Indiana Department of Insurance Enforcement Division's Objections to Findings of Fact, Conclusions of Law, and Recommended Order of June 30, 2010<sup>1</sup>, and now being duly advised in the premises and **DENIES** said Objections and issues this Final Order affirming ALJ Kissling's Recommended Order.

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<sup>1</sup> The Department timely filed Objections to the Recommended Order on July 15, 2010. On July 22, 2010, Respondent filed a Motion requesting ALJ Kissling to grant him up and through August 3, 2010, to file his Response to Objections. ALJ Kissling signed an Order granting Respondent's Motion on July 26, 2010. Respondent filed a Motion for Leave to File Belated Response to Objections of Department of Insurance and his Response to Objections on August 11, 2010. Because Respondent failed to file his Response to Objections by August 3, 2010, as ordered by ALJ Kissling, Respondent's Motion is denied and his Response to Objections was not considered.

**Adoption of Findings of Fact and Conclusions of Law**

The Commissioner incorporates ALJ Kissling's Findings of Fact and Conclusions of Law into this Order.

**Order**

The Acting Commissioner now ORDERS that charges against Respondent are hereby dismissed.

ALL OF WHICH IS ORDERED by the Commissioner this 27<sup>th</sup> day of August, 2010.



Stephen W. Robertson,  
Executive Director and  
Acting Commissioner,  
Indiana Department of Insurance

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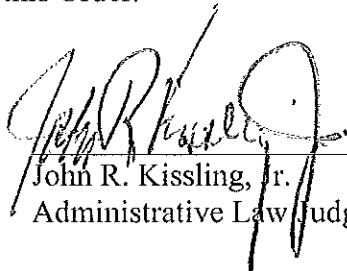
JUN 30 2010

STATE OF INDIANA  
DEPT. OF INSURANCE

**NOTICE OF FILING OF RECOMMENDED ORDER**

The parties of this action are hereby notified that the Administrative Law Judge's Findings of Fact, Conclusions of Law and Recommended Order are deemed filed as of this date.

To preserve an objection to this order for judicial review, you must object to the order in a writing that: 1) identifies the basis for your objection with reasonable particularity; and 2) is filed with the Commissioner of the Department of Insurance within eighteen (18) days from the date of this Order.

  
\_\_\_\_\_  
John R. Kissling, Jr.  
Administrative Law Judge

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**FILED**

JUN 30 2010

STATE OF INDIANA  
DEPT. OF INSURANCE

**FINDINGS OF FACT, CONCLUSIONS OF LAW**  
**AND RECOMMENDED ORDER**

Administrative Law Judge, John R. Kissling, Jr., having considered and reviewed all of the evidence, will now render a decision in the matter of Richard E. Gearhart and Gearhart & Assoc., Inc. ("Respondents"), which came to be heard on September 29, 2009, November 4, 6, and 23, 2009, February 23-24, 2010 and April 6-7, 2010, at the Indiana Department of Insurance, 311 West Washington St., Indianapolis, Indiana 46204.

The Indiana Department of Insurance was represented by counsel, Laura Levenhagen. Respondent was present and was represented by counsel, Robert Garelick of Cohen, Garelick & Glazier LLP. Witnesses testified under oath, evidence was heard, and exhibits were received into evidence.

Based upon the evidence presented at said hearing, the Administrative Law Judge now makes the following Findings of Fact and Conclusions of Law, and issues his Recommended Order as follows:

### **FINDINGS OF FACTS**

1. Respondent Gearhart is a licensed insurance agent in the State of Indiana holding license number 1396050, and is the owner of Respondent Gearhart & Associates, Inc., an Indiana Insurance Agency, holding license number 2727580. Respondent Gearhart has held an Insurance license from the state of Indiana since 1973 (Transcript, 2/24/2010, page 180) and in the 37 years he has held a license in this and in other states, he has never previously had a complaint filed against him. (Transcript, 2/24/2010, page 185.) David Rose (hereafter "Rose") investigator for the DOI confirmed that the DOI has no record of any complaints against Respondent Gearhart (Transcript, 11/04/2009, p. 195).
2. Respondent Gearhart also holds non-resident licenses in 27 other states and supervises the work of approximately 47 independent producers in those states. He estimated that he has probably sold some kind of insurance product to over 4500 people in Indiana and elsewhere (Transcript, 2/24/2010, page. 186).
3. The charges in this action include the sale of a security without a license, the sale of an investment which was a known investment and in connection with the offer, sale, and purchase of a security:
  - a. Making untrue statements of a material fact,
  - b. Omitting to state material facts necessary in order to make a statement not misleading,

c. Engaged in a course of business which operated as a fraud or deceit upon Indiana residents,

4. Count IV charges Respondent Gearhart, using his position as an insurance agent to persuade Indiana residents to invest in a known investment scam, constitutes the use of fraudulent, coercive, or dishonest practices, and is demonstrative of incompetence, untrustworthiness, and financial irresponsibility in the conduct of business in Indiana and is caused for disciplinary action under Indiana Code Section §27-1-15.6-12(b)(8).

5. Specifically, the charges against Respondents arise from the selling to Indiana residents a product known as a Universal Lease Agreement (hereafter "Universal Lease") offered by Resort Holdings International (hereafter, "RHI), (DOI, Exhibit 19), and a Management Agreement offered by either Majesty Travel (DOI, Exhibit 23) or Galaxy Properties Management (DOI, Exhibit 24) all entities allegedly owned and controlled by Kelly.

6. Kelly, through a company he formed, first known as Yucatan Investment Corporation, offered notes to investors paying a specific rate of return (DOI, Exhibit 2). According to an affidavit prepared by Jennifer Lea French, Special Agent for the Federal Bureau of Investigation, these notes were offered from late 1997 through mid-1999. Beginning in June of 1999, according to Ms. French's affidavit, various states issued Cease and Desist Orders against Yucatan Investment Corporation for selling unregistered securities concluding that the Notes were securities under their laws. (DOI, Exhibit 2, p. 3). DOI Exhibits 7, 8, 9, and 10 were Cease and Desist Orders from various states dealing with these promissory notes issued by Yucatan Investment, Corporation.

7. The essence of the transaction at issue is found in the Universal Lease Agreement, a contract between Resort Holdings International, S.A. and individual leaseholders, i.e., purchasers of the time shares of a specific unit. The Universal Lease agreement, in return for a specified lump-sum payment, entitled the leaseholder (the purchaser) over the twenty-five (25) year term of the lease with the right to occupy, use, rent, or lend a specific unit for specific time periods. (Exhibit 22). For example, in DOI Exhibit 19 the lessor was RHI and the leaseholder was Respondent Gearhart. It was for the week commencing on October 8, 2002 and then for every year until October of 2027. In the lease referenced in the Exhibit, Respondent Gearhart was leasing three (3) units, a one-bedroom Studio and 2 two-bedroom Suites.

8. The Letter of Understanding signed by all Leaseholders states, "While I own the lease I have the following options: 1. I can USE my vacation unit(s)..., 2. I can RENT my vacation unit(s) through my own effort...3. I can HIRE AN INDEPENDENT THIRD PARTY MANAGEMENT COMPANY to RENT my vacation unit(s) for me and any rental income is between the independent third party management company and myself. I fully understand that Resorts Holding International, S.A. is not responsible for any guarantees, promises, or actions made by any independent third party management company." (Exhibit 22)

9. The Letter of Understanding states, "I understand that Resort Holdings International is in no way promoting the purchase of the vacation unit(s) for investment purposes and there is no investment guarantee from RHI." (Exhibit 22)

10. If the leaseholder wished, he could exercise his rental rights by contracting in a Management Agreement (Exhibits 23&24) with Majesty Travel or Galaxy Properties Management S.A., separate legal entities to rent the purchased use-rights to third-parties and the

contracted entity would pay the leaseholder (termed the Client in the agreement) the compensation specified and agreed in the contract. (Exhibit 23)

11. In the Spring of 2002, Respondent Gearhart was approached by Steve Lawson to sell Universal Leases. Respondent Gearhart was acquainted with Lawson through Respondent Gearhart's sale of annuities. His relationship with Lawson dated back for 10 to 12 years and Respondent Gearhart, because of their positive business relationship, had developed trust and confidence in Lawson's integrity. (Transcript , 4/6/10, page 46-47)

12. Lawson had been employed by a company that Respondent Gearhart described as a wholesaler of Annuities. Lawson's company acted as the middle man between the annuity companies and the agents. (Transcript, 4/06/2010, page 45-46). Respondent Gearhart told Lawson that he would have to learn a lot more about this product and he would have to conduct due diligence to make certain this was something he would feel comfortable selling.

13. In the summer of 2002, Respondent Gearhart attended at least 2 meetings lasting from 3 to 4 hours each learning about the Universal Lease and discussing the risks and rewards of purchasing a Universal Lease. In addition during 2002, Respondent Gearhart went to Cancun, Mexico and viewed the Avalon Grand and other Kelly properties. Respondent Gearhart also met with Kelly. (Transcript, 4/6/2010, page 47).

14. Respondent Gearhart called the Better Business Bureau in Mishawaka, Indiana since Kelly had an office there and asked if there were any complaints about Kelly or RHI. He was told there were none. (Transcript, 4/6/2010, page 49-50)

15. Respondent Gearhart also conferred with other insurance agents similarly situated to gather data with regard to the viability of the Universal lease and reviewed a number of



documents including the documents referenced in Respondent Gearhart's supplementing the record filed on or about May 3, 2010.

16. One of the issues discussed by Kelly and others, when Respondent Gearhart was doing his due diligence, was whether the Universal Lease was a security thus requiring registration in Indiana. Respondent Gearhart was told the Universal Lease was developed so that it would not be considered a security and would not require registration. (Transcript, February 24, 2010, page 233 – 235)

17. Respondent Gearhart was shown 2 opinion letters issued by lawyers concentrating in securities law. The first letter was written by Joel Held, a partner in the firm of Baker & McKenzie with offices all over the world (DOI Exhibit 27). Mr. Held's curriculum vitae (Gearhart's Exhibit P.) demonstrates he is versed in securities law, having served as a trial attorney in the Division of Enforcement for the US Securities and Exchange Commission, and for many years Mr. Held has represented clients regarding security matters.

18. Respondent Gearhart also reviewed a letter written by Brantley H. Wright, an Indiana lawyer, who also gave an opinion that the Universal Lease was not a security and not subject to Indiana securities law (DOI, Exhibit 16). Mr. Wright is currently a partner at Bose McKinney & Evans, a well respected Indianapolis law firm. Mr. Wright was sufficiently experienced to render an opinion as to whether or not the Universal Lease was a security (Gearhart, Exhibit Q).

19. Mr. Wright made assumptions similar to that of Mr. Held and concluded that, "it is our view that entering into a lease of the Units will more likely than not be found to not constitute the sale of a security." (DOI, Exhibit 16, page 5).

20. Since Respondent Gearhart had reason to believe that the factual assumptions made by both Mr. Held and Mr. Wright were true and correct, it was not unreasonable for him to conclude in 2002 that the Universal Lease was not a security. (Exhibit 27 & Exhibit N)

21. After Respondents were no longer selling the product involved, federal securities fraud charges were brought against Michael Kelly and criminal information was filed on December 22, 2006 in the United States District Court for the Northern District of Illinois, Eastern Division. (DOI, Exhibit 2). Kelly was the only named Defendant, and even though there were upwards of 600 sales persons, similar to Respondent Gearhart selling the Universal Lease no salesperson has been charged with any criminal offense (Transcript, 11/04/2009, page 105-107). Since Kelly has not been tried, the allegations of securities fraud have not been established. There has been no judicial finding that Kelly or anyone associated with the Universal Lease has committed any securities fraud or other criminal offense (Transcript, 11/04/2009, p.104).

22. The Statement of Charges alleges that Respondent Gearhart recommended "that potential investors take money out of other investments to fund the purchase of the timeshare lease-back program." (Statement of Charges, paragraph 13biv.) Whether this was established or not by the evidence is of no importance to the question of Respondent Gearhart's violation of any laws administered by the Department of Insurance. It is obvious that the funds necessary to purchase a Universal Lease had to come from some other investment.

23. The persons called as witnesses understood from Respondent Gearhart that in order for them to receive any monetary or cash flow return, their unit had to be leased. (For example, see Transcript, 11/06/09, page 69). This was consistent with what the documents provided. (DOI Exhibit, 23, paragraph 1.(a)).

24. Respondent sold the program at issue for approximately nineteen (19) months from August of 2002, through March of 2004. (Exhibit 24).

25. Paragraph 48 of the Statement of Charges, alleges Respondent Gearhart for failed to disclose to his clients that: "a. the time share lease-back was not registered as a security in Indiana; b. that he didn't tell his clients about the specific risks associated with the time share lease-back; c. that he didn't tell his clients about the financial condition of the entities involved in the time share lease-back program and he provided no information concerning the prior orders against the entities or individuals involved in the timeshare lease-back program."

26. Jennifer French, Special Agent with the Federal Bureau of Investigation in Chicago testified that complaints started coming in late 2004. (Transcript, November 4, 2009, page 67)

27. Indiana did not determine that the Universal Lease was a security and therefore needed registration until September of 2009, 7 years after Respondent Gearhart began his due diligence and 5 years after he stopped offering the Universal leases to his clients. Respondent Gearhart was not required to advise his clients that the Universal Lease was not registered as a security because the Securities Division of the Indiana Secretary of States Office had not found it to be a security and Respondent Gearhart had a good faith reason to believe that the Universal Lease was not a security. The Respondent had no reasonable basis to know that such a determination would be made after the fact. (Exhibit 4)

28. Michael Kelly was charged with two counts of securities fraud for the sale of unregistered securities not because any of his business enterprises were failing. (Transcript, November 4, 2009, page 102)

29. The criminal securities fraud charges against Kelly before the U.S. District Court for the Northern District of Illinois were not filed until December 22, 2006, which was long after Respondents stopped selling Universal Leases. Those charges still remain pending and no adjudication has been made. No other persons or entities have been charged criminally in connection with the sale of Universal Leases. (Exhibit 2)

30. The Indiana Securities Division did not determine that the Universal Lease was a security until September of 2009 in its Order Adopting Hearing Officer's Proposed Findings of Fact and Proposed Conclusions of Law of July 31, 2008, which was five years after Respondent Gearhart stopped selling Universal Leases. In fact, the Securities Division did not file its action against Kelly and RHI until 2004, which is when, in response to that action, Respondent Gearhart stopped selling Universal Leases. As soon as Gearhart learned that the Universal Leases may, in fact, constitute an unregistered security he stopped selling it. (Exhibit 4).

31. The evidence presented shows that the real estate that served as the primary asset associated with the program at issue did in fact exist, was in fact operated in a manner that generated revenue, and did result in payments being made to all of the purchasers identified in the Department's charges for a significant period of time before the program was disrupted.

32. The operation of the program at issue was disrupted as a result of the Federal Securities & Exchange Commission arresting Kelly the primary proponent of the program and seizing records and documentation as a result of a securities investigation.

33. The assets involved in the program at issue are now controlled by a Federal Special Master for the benefit of those who purchased time share interests. (Exhibit 2)

34. Michael Kelly still owns the three hotels, the Avalon Grand, the Baccara, and the hotel of the Isla Mujeres, where the units subject to the Universal Lease agreement were located are now subject to the control of the special master in a restitution trust. (Exhibit 2)

35. Merriam-Webster dictionary defines "scam" as, "a fraudulent or deceptive act or operation."

36. There is no evidence to support a finding that Respondent knew or should have known that the program at issue in this case was not a legitimate program secured by an ownership in real estate.

### **CONCLUSIONS OF LAW**

1. The Commissioner of Insurance has jurisdiction over both the subject matter and the parties to this action.

2. This hearing was held in compliance with the Administrative Orders and Procedures Act of the Indiana Code.

3. The Commissioner has the discretionary authority to revoke the Respondents' license to sell insurance and to fine Respondents.

4. The determination of whether a particular program is or is not a security involves a complex analysis of the facts associated with the program and legal case law relative to that common law determination.

5. It was the burden of the Department to present evidence to establish the standard of care for an insurance agent in determining whether a product is a security and the Department provided no such evidence.

6. The determination by the Securities Commissioner in 2009, that the program involved in this matter was a security, is not binding in this administrative proceeding.
7. The Respondent did not knowingly sell a security without a license to do so.
8. It was the burden of the Department to present evidence to establish the standard of care for an insurance agent in reviewing the legitimacy and visibility of a product being sold and the Department presented no such evidence.
9. The Respondent made a reasonable investigation of the program which is the subject of this matter before selling that program to his clients.
10. The Department has jurisdiction over matters relating to insurance. Indiana Code Title 27 and the Rules promulgated thereunder authorize the Department to regulate the actions of those individuals licensed as insurance agents within the State and to enforce Indiana Insurance Law through administrative action charge. With respect to Counts I and II, whether or not Respondent violated Indiana Code Section 23-2-1-1 by acting as a broker-dealer or agent for the sale of securities without being registered to do so is beyond the authority of this Court tasked with jurisdiction over matters relating to Indiana Insurance Code Title 27, to decide.
11. Respondents have not been charged or convicted by a court, with jurisdiction over Indiana Code Section 23, of selling securities without being registered to do so.
12. The preponderance of evidence presented by the Department was insufficient to show under Indiana Code 27-1-15.6(B)(8) that the Respondents were fraudulent, coercive, dishonest, demonstrated incompetence, were untrustworthy, or financially irresponsible as charged with regard to the investigation, evaluation and conclusion by the Respondents that they were selling

a security. To the contrary, the preponderance of evidence shows that Respondents' actions in regard to the determination that they were not selling a security were sufficient and appropriate.

13. With respect to Count III, the Respondents are charged with making untrue statements of material fact, omitting material facts necessary to make a statement not misleading and engaged in a course of business which operated as a fraud. This court has chosen to make a distinction between the statements of fact or omissions of material facts made by the promoter(s) of the sale of the Universal Lease in the sales promotion of the venture and those statements of fact or omission of material fact made independently by the Respondents. Charges were not made by the Department against the promoter(s) and whether the promoter(s) made accurate or inaccurate statements is beyond the scope of this hearing to decide. Accordingly, no conclusion is made herein on those statements. At issue rather is whether or not the Respondents conveyed the facts presented by the promoter(s) while knowing that they were untrue, or, if the Respondents made untrue statements on their own or outside those presented by the promoter(s). The preponderance of evidence presented failed to identify the untruthfulness of statements made by the Respondents either in conveying the terms of the deal or on details outside those presented by the promoter(s). To the contrary, the preponderance of evidence indicates that Respondents whether through indoctrination and training by the promoter(s), or, by their own investigation and observation were persuaded that the facts they presented were true and they conveyed them truthfully and accurately as they were known at the time. This conclusion is substantiated by and consistent with evidence that a large percentage of investors traveled to the site, made their own investigation and arrived at their own independent decision to invest. Respondent, Richard Gearhart believed that the Universal Lease was a sound product and he personally purchased

leases valued at one hundred fifty-eight thousand (\$158,000.00) dollars before he offered the opportunity to third parties.

14. The Department did not meet its burden of proof that Respondents demonstrated incompetence, untrustworthiness and financial irresponsibility in the conduct of business in Indiana.

15. With respect to Counts III and IV, the charge that there was sufficient public information available that Respondents either knew or should have known that the investment was a scam is not supported by the preponderance of evidence presented and summarized herein:

a. The ownership and the rights to the time shares memorialized in the Universal Lease agreement, which represent the consideration from Resort Holdings to the Leaseholder, remains with the Leaseholder, i.e., the purchaser/investor. No evidence presented indicated that any Leaseholder's ownership and the rights to occupy, use, rent, or lend the unit(s) purchased have ceased to exist.

b. One of three options available to a leaseholder in the Universal Lease agreement permitted the leaseholder to independently contract with a management company to rent the unit(s). Majesty Travel and later Galaxy Properties Management, S.A were the management companies selected by unit owners wishing to rent their units. Evidence presented showed that Galaxy Properties Management and Majesty Travel failed to fulfill their contractual obligations by remitting rental income as agreed to the clients (who were also leaseholders in the Universal Lease agreement) but failure of either of these two entities to perform as agreed had no effect on the ownership and the rights to occupy, use, rent (by using still another management company if they wished) or lend the unit(s) purchased in the Universal Lease agreement.



c. The investment, that is, the purchase of unit(s) by leaseholders has, years subsequent to the time of purchase, been declared to be a security. Whether the purchase is viewed as a real estate/timeshare purchase or a security, the value is determined by market conditions and the economic laws of supply and demand. The value (either the increase in value from the time of purchase or the decrease in value from the time of purchase) is a function of the free market and beyond the control of Respondents.

d. The preponderance of evidence while showing that the management companies failed to fulfill their contractual obligation by paying clients rental income as agreed, was insufficient to show that such failure was the result of fraudulent or deceptive acts as required in the definition of a scam.

13. The Department failed to meet its burden by the preponderance of evidence that the investment was a scam but rather a business venture that failed.

14. Findings of Fact that can be adopted as Conclusions of Law are hereby incorporated herein as such.

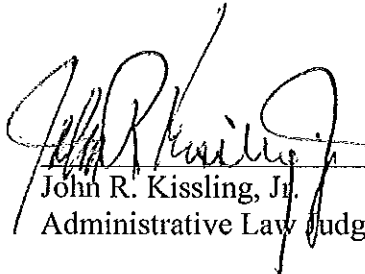
**RECOMMENDED ORDER**

With the Findings of Fact and the Conclusions of Law as stated, the Administrative Law Judge now recommends to the Commissioner of Insurance the following:

1. Charges against Respondents should be dismissed.

ALL OF WHICH IS ADOPTED by the Administrative Law Judge and recommended to the Commissioner this 30<sup>th</sup> day of June, 2010.

Dated 6-30-10

  
\_\_\_\_\_  
John R. Kissling, Jr.  
Administrative Law Judge

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