

BEFORE THE
DEPARTMENT OF CORPORATIONS
STATE OF CALIFORNIA

In the Matter of the Desist and Refrain Order
Issued Against:

IDC PANAMA, INC. and
ROBERT M. SCHARRINGHAUSEN,

Respondents.

Case Nos. 8508

OAH No.: 2008070293

DECISION

The attached Proposed Decision of the Administrative Law Judge of the Office of Administrative Hearings, dated October 27, 2008, is hereby adopted by the Department of Corporations as its Decision in the above-entitled matter with the following technical or other minor changes on the attached Errata Sheet pursuant to Government Code Section 11517(c)(2)(C).

This Decision shall become effective on February 5, 2009.

IT IS SO ORDERED this 4th day of February 2009.

CALIFORNIA CORPORATIONS COMMISSIONER

Preston DuFauchard

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PROPOSED DECISION

James Ahler, Administrative Law Judge, Office of Administrative Hearings, State of California, heard this matter on October 15, 2008, in San Diego, California.

Afsaneh Eghbaldari, Corporations Counsel, represented Preston DuFauchard, California Corporations Commissioner, Department of Corporations, State of California.

No appearance was made by or on behalf of respondents IDC Panama, Inc., or Robert M. Scharringhausen.

On October 15, 2008, the matter was submitted.

FACTUAL FINDINGS

The Regulation of the Offer and Sale of Securities

1. Following the 1929 stock market crash, the federal government entered into the area of securities regulation. The first effort at regulation, the Securities Act of 1933, was followed thereafter by the Securities Exchange Act of 1934. Additional federal legislation has followed since then.

The Securities and Exchange Commission (SEC) directly enforces the federal securities laws through the Securities Act of 1934, and it indirectly enforces the federal securities laws through its oversight of the National Association of Securities Dealers and several stock exchanges.

2. State securities laws, commonly known as Blue Sky laws, have been enacted in all states to provide regulation over the offer and sale of securities. California's Blue Sky law - known as the Corporate Securities Law of 1968 (the CSL) - is set forth at California Corporations Code section 25000 et seq. The CSL regulates the offer and sale of securities in California and it requires registration of broker-dealers and stockbrokers doing business in California.

3. Before a "security"¹ is sold in California, it must be qualified with the Department of Corporations, unless an exemption exists. Many securities and many security transactions are exempt from or are preempted from state regulation by federal law.²

Qualification in California may be accomplished in a number of ways including: (a) Coordination of a security for which a registration statement was filed under the Securities Act of 1933 (Corp. Code, § 25111); or (b)(i) notification that the security is registered under Section 12 of the Securities Exchange Act of 1934 (Corp. Code, § 25111); or (ii) was issued by an investment company registered under the Investment Company Act of 1940 (Corp. Code, § 25112); or (iii) was issued by permit (Corp. Code, § 25113).

4. The California Corporations Commissioner has several legal remedies available to enforce the CSL. Proscribed conduct may be enjoined by a civil action under Corporations Code section 25530 or by a Desist and Refrain Order under Corporations Code section 25532. Civil penalties may be sought under Corporations Code section 25535. Finally, criminal prosecution may be initiated under Corporations Code section 25540.

5. This matter involves the appeal of a Desist and Refrain Order.

The Principals

6. Respondent IDC Panama, Inc. (IDC Panama) is a California corporation that was founded in 2004. Respondent Robert M. Scharringhausen was IDC Panama's incorporator, and following IDC Panama's incorporation, he has served as the corporation's Chief Executive Officer.

¹ California Corporations Code section 25019 sets forth an exhaustive but not all-inclusive definition of what constitutes a "security." Under the Corporate Securities Law of 1968, a "security" includes membership in incorporated or unincorporated associations, whether or not evidenced by a written instrument.

² For example, Regulation D private offerings are exempt from registration if there has been full compliance with SEC Rules 501-503. "Covered securities" on the New York Stock Exchange, AMEX and the NASDAQ/National Market, and securities of the same issuer which are equal in rank or senior to such listed securities are preempted from state regulation by Section 18 of the Securities Act of 1933.

7. Respondents Saenz Group, LLC and Alex Saenz were associated with IDC Panama and Scharringhausen as discussed hereafter. Respondents Saenz Group, LLC and Alex Saenz did not request a hearing in this matter.

The Department of Corporations' Investigation

8. Jon Wroten (Wroten) is employed by the Department of Corporations as a Senior Corporations Examiner. In October 2007, Wroten reviewed an advertisement appearing in the *San Diego Union Tribune* in the "Investments" section of the classified ads which stated:

PANAMA. 61% Rtn. SFR Cns by So Cal Bldr. \$50K Min. www.idcpanama.com 858-587-0342x102

Wroten became aware of a similar advertisement appearing in the *Los Angeles Times* Internet advertising site.

Wroten wanted to gather more information, so he called the telephone number listed in the advertisement. He did so in an undercover capacity to determine if an unregistered security was being offered. Wroten spoke with Alex Saenz, who further described the investment opportunity, and with Robert M. "Buzz" Scharringhausen, whom Saenz said was responsible for creating the investment opportunity. Wroten was told over the telephone that investor monies would have an "equity-like" stake in property in Panama.

Wroten visited IDC Panama's website, which contained numerous documents including an offering dated March 5, 2008, entitled "Investment Opportunity – Phase 4." The offering described the proposed investment, stated that six previous projects had "gone full cycle with returns ranging from 68% to 172%," and stated:

"The minimum investment is \$50,000 and the maximum investment per investor in \$225,000. Annual Return is 50% to 60% which includes profit participation of 40% in the net cash out. The notes have a preferred rate of 11% per annum as the base interest rate. The specific lots associated with the specific investment are identified and unique to the investor. Security is shares in the actual IBC formed specifically to develop the lot or lots. The notes are held, registered and acknowledged by a prominent Panamanian Attorney that formed IBC and cleared titles on the purchased lots."

The attachments available through the website included a "sample secured promissory note" signed by R. M. Scharringhausen, President, IDC Panama, Inc., which stated, in part:

“This note is secured by the equivalent percentage of bearer shares in Hole 5 Coronado, Inc. and Majagual 7000, Inc. . . . This note is secured by 14.62% proportionate bearer shares in Hold 5 Coronado, Inc. and Majagual 7000, Inc. Shares are security only and are to be returned upon retiring the note.”

Wroten exchanged e-mails with the Saenz Group in late April 2008. In an e-mail dated April 25, 2008, Alex Saenz attached an “investment package.”

9. Neither respondent IDC Panama in its website or in other advertising, nor respondent Scharringhausen, Alex Saenz, nor the Saenz Group, LLC disclosed to Wroten or to any member of the public that:

“(1) On March 19, 1996, the Department of Corporations issued a Desist and Refrain Order to Robert “Buzz” Scharringhausen, individually and as CEO of Continental Pacific Development, for the unlawful sale of securities in California;

(2) that on March 3, a stipulated judgment was entered against The Michael Andrew Group, Inc., and to Robert M. Scharringhausen following the filing of a civil complaint by the City Attorney, City of San Diego, for making untrue and misleading statements in connection with the course of the sale of real property in San Diego and for unfair competition, and that in addition to being enjoined from further illegal activities, Scharringhausen was ordered to pay civil penalties and attorney’s fees;

(3) that on May 30, 1997, Scharringhausen was found guilty by a jury of three counts of bankruptcy fraud in the United States District Court, Southern District of California, in Case No. 96CR0415-H, and that he was ordered to pay a fine of \$10,000 and was directed to complete three months of supervision at a community corrections center;

(4) that the Saenz Group LLC, Alex Saenz, and others were directed to pay to CRPM, Inc. dba Symmetry, and Patrick Mummy, the sum of \$15,000 for breach of contract, fraud by negligent misrepresentation, and misappropriation of trade secrets in a binding arbitration; and that in a memorandum opinion filed February 12, 2008, before the United States Tax Court, the judge determined a tax lien filed against Scharringhausen was valid, finding, among other matters, that “Robert Scharringhausen files income tax returns but does not always pay the tax due, a habit that finds him owing more than \$30,000 for the tax years 2001-2003.”

Each of these items constituted the omission of a material matter which would be relevant to an ordinary, reasonable and prudent investor.

10. Wroten was not asked to make any contributions to the operation of IDC Panama other than a financial investment.

Jurisdictional Matters

11. On June 6, 2008, the Department of Corporations issued a Desist and Refrain Order to respondents IDC Panama, Inc., Robert M. Scharringhausen, President, and Alex Saenz, Managing Partner, and to respondents The Saenz Group, LLC, and to Alex Saenz, CEO.

The Order contained findings that respondents offered securities in the form of notes as early as 2008, that the notes were securities under Corporations Code section 25019, that the securities offered were issuer transactions, that the Department of Corporations had not issued a permit or other form of qualification for the offer of those securities in California, that in connection with the offer of the securities there were failures to disclose material information, and that based on those findings, respondents were ordered to desist and refrain from the further offer of securities in California.

On June 27, 2008, Richard L. Fahey, Attorney at Law, advised the Department of Corporations that he represented respondents IDC Panama, Inc. and Scharringhausen.

On August 13, 2008, the Department of Corporations served respondents, through counsel, with an amended notice of hearing, setting the appeal of the Desist and Refrain Order for October 15, 2008, to commence at 9:00 a.m., at 1350 Front Street, San Diego, CA 92101.

By letter dated August 21, 2008, which was received by the Department of Corporations on August 25, 2008, Attorney Fahey advised the Department of Corporations and the Office of Administrative Hearings that he had withdrawn from representation of respondents IDC Panama, Inc. and Scharringhausen, as well as providing the last known addresses for each respondent.

By notice dated September 24, 2008, complainant's counsel advised respondents IDC Panama, Inc. and Scharringhausen of the Department of Corporations' intent to take the testimony of Jon Wroten by telephone. The notice of intent specifically set forth the date, time, and place of the hearing in this matter.

On October 15, 2008, the record in the matter was opened. Complainant appeared by and through counsel. No appearance was made by or on behalf of any respondent. Evidence was presented establishing jurisdiction over all respondents in this matter. Thereafter, a default hearing was conducted before the administrative law judge in accordance with Government Code section 11520. Sworn telephonic testimony was given, documentary evidence was introduced, a closing argument was given, the record was closed, and the matter was submitted.

LEGAL CONCLUSIONS

Statutory Authority

1. Corporations Code section 25532 provides in part:

“(a) If, in the opinion of the commissioner, (1) the sale of a security is subject to qualification under this law and it is being or has been offered or sold without first being qualified, the commissioner may order the issuer or offeror of the security to desist and refrain from the further offer or sale of the security until qualification has been made under this law or (2) the sale of a security is subject to the requirements of Section 25100.1, 25101.1, or 25102.1 and the security is being or has been offered or sold without first meeting the requirements of those sections, the commissioner may order the issuer or offeror of that security to desist and refrain from the further offer or sale of the security until those requirements have been met.

...

(c) If, in the opinion of the commissioner, a person has violated or is violating Section 25401, the commissioner may order that person to desist and refrain from the violation. . . .”

2. Corporations Code section 25110 provides:

“It is unlawful for any person to offer or sell in this state any security in an issuer transaction (other than in a transaction subject to Section 25120), whether or not by or through underwriters, unless such sale has been qualified under Section 25111, 25112 or 25113 (and no order under Section 25140 or subdivision (a) of Section 25143 is in effect with respect to such qualification) or unless such security or transaction is exempted or not subject to qualification under Chapter 1 (commencing with Section 25100) of this part. The offer or sale of such a security in a manner that varies or differs from, exceeds the scope of, or fails to conform with either a material term or material condition of qualification of the offering as set forth in the permit or qualification order, or a material representation as to the manner of offering which is set forth in the application for qualification, shall be an unqualified offer or sale.”

3. Corporations Code section 25017 provides:

“(a) ‘Sale’ or ‘sell’ includes every contract of sale of, contract to sell, or disposition of, a security or interest in a security for value. ‘Sale’ or ‘sell’ includes any exchange of securities and any change in the rights, preferences, privileges, or restrictions of or on outstanding securities.

(b) ‘Offer’ or ‘offer to sell’ includes every attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security for value. . . .”

4. Corporations Code section 25019 provides in part:

“‘Security’ means any note . . . membership in an incorporated or unincorporated association; bond . . . certificate of interest or participation in any profit-sharing agreement . . . investment contract; viatical settlement contract or a fractionalized or pooled interest therein . . . or, in general, any interest or instrument commonly known as a ‘security’; or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing. All of the foregoing are securities whether or not evidenced by a written document. ‘Security’ does not include: (1) any beneficial interest in any voluntary inter vivos trust which is not created for the purpose of carrying on any business or solely for the purpose of voting, or (2) any beneficial interest in any testamentary trust, or (3) any insurance or endowment policy or annuity contract under which an insurance company admitted in this state promises to pay a sum of money (whether or not based upon the investment performance of a segregated fund) either in a lump sum or periodically for life or some other specified period, or (4) any franchise subject to registration under the Franchise Investment Law (Division 5 (commencing with Section 31000)), or exempted from registration by Section 31100 or 31101.”

5. Corporations Code section 25401 provides:

“It is unlawful for any person to offer or sell a security in this state or buy or offer to buy a security in this state by means of any written or oral communication which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading.”

Appellate Authority

6. Courts use two major themes or modes of analysis to determine whether a particular transaction involves a “security.” These tests have been applied, either separately or together, by both federal and California courts in making this factual determination. A transaction is considered a security if it satisfies either or both tests.

Under the first test, a security will be found when a person has invested value in a common enterprise with an expectation of profit to be derived from the substantial efforts of others. This is sometimes referred to as the *Howey* test because of the United States Supreme Court’s decision in *SEC v. W.J. Howey* (1946) 328 U.S. 293. The *Howey* analysis has been used by many California courts to determine the existence of a security. (*People v.*

Syde (1951) 37 Cal.2d 765; *Tomei v. Fairline Feeding Corp.* (1977) 67 Cal.App.3d 394; and *Moreland v. Department of Corporations* (1987) 196 Cal.App.3d 506.)

The second test is known as the “risk capital” approach, first used in California in *Silver Hills Country Club v. Sobieski* (1961) 55 Cal.2d 811. That decision permitted the finding of a security when capital was sought from third parties which would be risked in a start-up of a business venture for profit. There was no requirement that an investor have an expectation of a monetary profit from the investment. The California Supreme Court emphasized the passive position as an essential element of the risk capital test.

The *Howey* and the risk capital tests are not mutually exclusive. Sometimes their elements are combined to determine whether an investment involves a security subject to registration in California. (*Moreland v. Department of Corporations* (1987) 194 Cal.App.3d 506; see also *People v. Witzerman* (1972) 29 Cal.App.3d 169 and *People v. Schock* (1984) 152 Cal.App.3d 379.)

7. *People v. Corey* (1995) 35 Cal.App.4th 717 stands for the proposition, inter alia, that in a criminal prosecution for selling an unqualified, unexempt security in violation of Corporations Code section 25110, the element of *scienter* need not be established.

Cause Exists to Affirm the Desist and Refrain Order

8. The preponderance of the evidence established cause to affirm the Desist and Refrain Order issued against respondents HDC Panama, Inc., Robert M. Scharringhausen, The Saenz Group, LLC, and Alex Saenz under Corporations Code section 25532 insofar as these respondents were involved in the solicitation and sale of securities for which there was no exemption and no qualification. The products offered constituted securities under the Corporations Code, under the risk capital test, and under *Howey*. Furthermore, the preponderance of the evidence established that respondents failed to disclose material information in violation of Corporation Code section 5401 in the offering of the securities.

This conclusion is based on all Factual Findings and on all Legal Conclusions.

ORDER

The Desist and Refrain Order signed on June 6, 2008, directed to IDC Panama, Inc., The Sanchez Group, LLC, Robert M. “Buzz” Scharringhausen, and Alex Saenz is affirmed.

DATED: _____

JAMES AHLER
Administrative Law Judge
Office of Administrative Hearings