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Arkansas Securities Dept.

BEFORE THE ARKANSAS SECURITIES COMMISSIONER

Case No. S-08-048

**IN THE MATTER OF
DIVERSIFIED LENDING GROUP, INC.,
BRUCE FRIEDMAN and MICHAEL GARDNER**

No. S-08-048-09-CD01

CEASE AND DESIST ORDER

On March 9, 2009, the staff of the Arkansas Securities Department (Staff) filed its Request for a Cease and Desist Order, as amended by its Amended Request for Cease and Desist Order filed March 16, 2009 (Request), stating that it has information and certain evidence that indicates Diversified Lending Group, Inc. (DLG), Bruce Friedman, and Michael Gardner have violated provisions of the Arkansas Securities Act (Act), codified at Ark. Code Ann. §§ 23-42-101 – 509. The Arkansas Securities Commissioner (Commissioner) has reviewed the Request, and based upon representations made therein, finds that:

FINDINGS OF FACT

1. The Request contains the following representations of fact:
 - a. DLG is a corporation organized and existing under the laws of California, with its principal place of business located at 15260 Ventura Boulevard, Suite 1240, Sherman Oaks, California 91403.
 - b. Friedman is the president of DLG. He is known to use the following addresses to conduct business: 15260 Ventura Boulevard, Suite 1240, Sherman Oaks, California 91403; 106 West Lime Avenue, Suite 206, Monrovia, California 91016; and 14930 Ventura Boulevard, Suite 340, Sherman Oaks, California 91403.

- c. Gardner is licensed as a resident producer agent by the Arkansas Insurance Department (License No. 32497). Gardner is the president of Gardner Insurance Agency, Inc. and maintains a principal place of business at 206 East Merriman, Wynne, Arkansas 72396. Gardner is a salesperson in Arkansas for DLG. Although Gardner passed the series 6 and 63 tests for registration pursuant to the Act (CRD No. 2321798), those examination scores lapsed in 1993, and it appears that he was never registered as or with an investment adviser.
- d. In June 2008, the Staff opened an investigation of the Respondents. In response to inquiry from the Staff (DLG Response), DLG furnished information showing that from March 23, 2007, through May 12, 2008, twenty-nine Arkansas investors (Arkansas Investors) invested \$3,456,024 with DLG. The Staff also obtained documentation of these sales from Gardner in response to a subpoena (Gardner Response). The details of each contract is summarized as follows:

	INVESTOR	DATE OF NOTE	AMOUNT INVESTED	TERM	RATE
a.	AR1	1/28/2008	237,609.71	5 YEAR	12%
b.	AR2	3/23/2007	60,000.00	5 YEAR	9%
c.	AR3	4/26/2007	52,000.00	1 YEAR	9%
d.	AR4	5/9/2007	52,000.00	1 YEAR	9%
e.	AR5	5/17/2007	300,000.00	5 YEAR	12%
f.	AR6	6/22/2007	700,000.00	1 YEAR	9%
g.	AR7	7/2/2007	60,000.00	5 YEAR	12%
h.	AR8	7/2/2007	150,000.00	5 YEAR	12%
i.	AR9	7/26/2007	70,000.00	1 YEAR	12%
j.	AR10	8/27/2007	200,000.00	5 YEAR	12%
k.	AR11	9/4/2007	100,000.00	5 YEAR	9%
l.	AR12	10/6/2007	100,000.00	5 YEAR	12%
m.	AR13	10/26/2007	60,000.00	5 YEAR	12%
n.	AR14	12/21/2007	67,001.00	5 YEAR	12%
o.	AR15	1/2/2008	65,000.00	1 YEAR	12%
p.	AR16	1/11/2008	50,000.00	1 YEAR	12%
q.	AR17	1/18/2008	200,000.00	5 YEAR	12%
r.	AR18	1/23/2008	50,000.00	1 YEAR	12%
s.	AR19	1/25/2008	50,000.00	1 YEAR	12%
t.	AR20	1/31/2008	94,588.55	1 YEAR	12%
u.	AR21	3/1/2008	102,000.00	5 YEAR	12%
v.	AR22	3/3/2008	141,000.00	5 YEAR	12%
w.	AR23	3/10/2008	67,232.94	5 YEAR	12%
x.	AR24	3/13/2008	51,826.19	5 YEAR	12%
y.	AR25	3/20/2008	100,765.61	5 YEAR	12%
z.	AR26	4/1/2008	50,000.00	5 YEAR	12%
aa.	AR27	4/28/2008	75,000.00	5 YEAR	12%
bb.	AR28	5/1/2008	50,000.00	1 YEAR	12%
cc.	AR29	5/12/2008	100,000.00	1 YEAR	12%

- e. According to the DLG Response and an offering circular obtained in the Staff's investigation (Circular), DLG is engaged in the acquisition and operation of income producing real estate, real estate lending, insurance premium financing strategies, financial service brokerage business, and private investment pools. DLG acknowledges that it conducts certain business through its wholly-owned subsidiary, AEI. AEI contracts with Your Platinum Distributors Insurance Marketing Co. ("YPD"), a Texas corporation and wholesaler of annuity, life insurance, and investment products. YPD, in turn, contracts with insurance agents, whom DLG authorizes to represent DLG to the insurance agent's existing clients. The insurance agents, such as Gardner, then solicit investments ranging from \$50,000 to \$2,000,000. According to DLG, the DLG products are designed to be shown only to the insurance agent's existing clients, whom the agent knows to be accredited investors and appropriate candidates.
- f. In the Management's Discussion and Analysis of Risk Factors section of the Circular, it states: "there are risks associated with investing in 'the Fund,' most of which [DLG] does not control, such as trends in the economy, general interest rates, income tax laws, governmental regulations, and the availability of satisfactory investment."
- g. In the Real Estate Program Objectives section of the Circular, it states: "We cannot assure you that we will achieve these objectives or that your capital will not decrease."

- h. In the Disposition section of the Circular, it states: “[DLG] will have absolute discretion as to whether and when to sell a property, and we will have no obligation to sell properties as any particular time.”
- i. In the Real Estate Program Policies and Guidelines section of the Circular, it states: “[DLG] will have absolute discretion with respect to the selection of specific investments.”
- j. On DLG’s Investor Application, a form used to facilitate investments in DLG, investors are required to choose between a “Secured 12% Yield” and a “Principal Reinsured 9% Yield.”
- k. With the 9% rate, investors are led to believe that their investment in DLG is insured. According to a “Reinsurance Endorsement” included in the Circular, “The principal amount of the investment will be insured by a AA Rated or better insurance company” by means of a collateral assignment of an insurance contract.
 - i. AR2 was given an “Assignment of Policy as Collateral Security” which purports to assign an insurance policy issued by American National Insurance Company of Galveston, Texas, identified by a policy number. This document permits the assignee, AR2, in the event of a default by DLG to surrender the insurance policy to the insurance company “for its Cash Value in which event the [Insurance] Company shall pay to the assignee [AR2] the amount of the indebtedness [owed to AR2] not in excess of the Cash Value.” AR2's investment was for \$60,000.

- ii. AR25 was also promised insurance on her investment with the use of this same insurance policy. AR25 first chose the insured 9% option, but later changed to the uninsured 12% option. In making this change, AR25 signed a document entitled "Release of Assignment of Policy as Collateral Security". It identified the policy as a fixed annuity issued by the same company and policy number, the insured as Friedman and the owner as DLG. AR25's investment was for \$100,765.61.
- l. American National Insurance Company confirmed that this insurance policy referred to in AR2's Collateral Assignment and in AR25's Release of Assignment is in fact a fixed annuity owned by DLG, Friedman is indeed the annuitant/insured, but the cash value of the annuity is presently \$6,407.77. It was purchased for \$6,000 on or about May 22, 2007, and has accumulated \$407.77 in earnings.
- m. Although the Circular states that DLG employs seventeen people, it identified none of them. It also identified no one on the board of directors or any officers of the company. Other than Gardner, no employees or officers of DLG were identified in any documentation obtained from the Gardner Response, either.
- n. Friedman founded DLG, is its sole shareholder and has served as chief executive officer and a member of the board of directors since May 2004. The following matters concerning Friedman would be material matters to a reasonable investor:
 - i. In 1981, Friedman was convicted of grand theft in the Superior Court of Los Angeles County and sentenced to two years imprisonment. In

accordance with that conviction Friedman served twenty-three months in the California state prison system.

- ii. In April 1993, Friedman filed for personal bankruptcy pursuant to Chapter 7 of the United States Bankruptcy Code, being discharged in August, 1993.
- iii. In November 1999, Friedman settled a law suit filed against him and others by entering into a Stipulation for Judgment and Judgment Thereon in the Superior Court for Los Angeles County, California. In this case Friedman was sued for breach of three promissory notes, breach of contract and fraud. The case involved loans made to Entertainment & Mortgage Corporation (EMC), of which Friedman was president, on specific motion pictures. Friedman was alleged to have induced the plaintiff to make loans on the basis of Friedman's false statements that two of the motion pictures involved had been pre-sold and that revenue streams from the showing of those motion pictures would commence and be available for repayment of the loans within thirty to thirty-five days. Judgment was entered against all defendants on all causes of action for \$1,250,000. Judgment was entered against Friedman, personally, for \$700,000. *See Interbank Funding Special Purpose Corp., etc., et al., v. Entertainment & Mortgage Corp., etc., et al.*, No. BC186480, Superior Court of Los Angeles, California.

- iv. In November 2002, Friedman settled a law suit filed against him and others by entering into a Stipulation for Judgment and Judgment Thereon in the Superior Court for Orange County, California. Friedman was sued in this case also in connection with loans made while he was acting as president of EMC, and EMC was a party defendant in this action. Here, the plaintiff alleged six causes of action, and Friedman and EMC settled for a judgment against them for (1) fraud and deceit, (2) conspiracy to defraud and (3) negligent misrepresentation in the amount of \$950,000, the defendants being jointly and severally liable for the money judgment. In this case the plaintiff alleged that Friedman and others fraudulently induced it to loan them money to be used for development of property in Nevada by promising that the plaintiff would provide part of the financing and the rest would come from EMC, which Friedman represented had obtained a \$7.5 million loan commitment. In reality, EMC had no such loan commitment, and the defendants intended to abscond with the money loaned. *See IBF Special Purpose Corporation v. West Wendover Associates, et al.*, No. 795868, Superior Court of Orange County, California.
- v. Following the entry of judgment in Orange County, as set out immediately above in Paragraph 1.n.iv, Friedman and the other defendants initiated a “sham” foreclosure on the land in question in Elko County, Nevada in an effort to defeat the plaintiff’s Orange County judgment. The plaintiff’s

trustee in bankruptcy initiated a state court proceeding and reached a settlement against Friedman and his codefendants of \$150,000 in September 2004.

- o. The matters set out in Paragraph 1.n were not disclosed in the Circular.
- p. The Staff interviewed ten of the Arkansas Investors. None of them were aware of the matters set out in Paragraph 1.n before they invested. There was no evidence that any of the Arkansas Investors were informed of these matters in either the DLG Response or the Gardner Response.
- q. Gardner received \$122,790.27 in commissions paid from YPD for the period of April 20, 2007, through June 11, 2008, on sales to the Arkansas Investors identified in Paragraph 1.d as AR1 through AR29.
- r. The investment contracts offered by DLG and Gardner were not registered as securities pursuant to the Act. In connection with these investment contracts the Arkansas Securities Department has no record of a filing evidencing either an exemption from registration pursuant to the Act, or a notice filing as a federal covered security.
- s. None of the Respondents was registered under the Act in any capacity.

CONCLUSIONS OF LAW

2 The investments made by the Arkansas Investors in DLG were investment contracts and therefore securities. Ark. Code Ann. § 23-42-102(15)(A)(xi). An investment contract is the investment of money into the risk capital of a common enterprise or venture with the expectation of benefit or profit with no effective control over the venture. According to the

Circular and the DLG Response, this was the investment in the risk capital of a common enterprise in which DLG was using the money invested for a variety of businesses. The investors were totally without control and dependent on the efforts of others, specifically DLG, because decisions as to how to use the investors' money were solely within DLG's "absolute discretion," which would necessarily deprive investors of any control.

3. It is unlawful for any person to offer or sell any security which is not registered or which is not exempt from registration under the terms of the Act. Ark. Code Ann. § 23-42-501. The DLG securities were neither registered nor exempt under the Act. Accordingly, the Respondents have violated Ark. Code Ann. § 23-42-501 by selling the DLG securities to the Arkansas Investors.

4. A broker-dealer is any person engaged in the business of effecting transactions in securities for the account of others or for his or her own account. Ark. Code Ann. § 23-42-102(2). It is unlawful for any person to transact business in this state as a broker-dealer unless he is registered as such pursuant to the Act. Ark. Code Ann. § 23-42-301(a). By engaging in the business of a broker-dealer in the sales of the DLG securities to the Arkansas Investors without registration as a broker-dealer, Gardner has violated Ark. Code Ann. § 23-42-301(a).

5. It is unlawful for any person in connection with the offer or sale of any security, directly or indirectly, to make any untrue statement or omit to state a material fact necessary in order to make the statements made not misleading in light of the circumstances under which they are made. Ark. Code Ann. § 23-42-507(2). By means of the material omissions set forth in Paragraph 1.n above, DLG, under the control of Friedman, violated Ark. Code Ann. § 23-42-507(2). These matters, which were not included in the Circular, were material because the

disclosure of this information would have significantly altered the total mix of information available to investors. Although the Arkansas Investors were given seemingly detailed information concerning the business of DLG, there was a total void of information concerning the officers and personnel of DLG. Stated differently, there was ostensibly a great deal of information about what DLG did and how DLG did it, but no information as to who managed or performed DLG business. Such information would have been viewed by a reasonable investor as significant or important in deciding whether to invest in DLG. Further, DLG and Friedman failed to inform two of the Arkansas Investors who opted to purchase the “Principal Reinsured 9%” yield, AR2 and AR25, that the insurance policy they were informed was at their disposal to cover their combined investments of \$160,765.61 had a cash value of only \$6,407.77, an amount greatly short of an amount necessary to cover their two investments. This information is material because the disclosure of this information would have significantly altered the total mix of information available to investors. The information would have alerted AR2 and AR25 that DLG and Friedman were not truthful about the guarantee of the investment by insurance, which would have been significant or important to a reasonable investor when considering other representations made about DLG’s business activities and, thus, whether to invest in DLG.

ORDER

6. Diversified Lending Group, Inc. (DLG), Bruce Friedman, and Michael Gardner shall immediately CEASE AND DESIST from any further actions in the state of Arkansas in connection with the offer or sale of securities until such time as securities in question are all properly registered or shown to be exempt from registration pursuant to the Arkansas Securities Act.

7. Michael Gardner shall immediately CEASE AND DESIST from any further actions as a broker-dealer in the state of Arkansas until such time as he becomes registered as a broker-dealer or agent of a licensed broker-dealer in accordance with the Act.

8. Diversified Lending Group, Inc., and Bruce Friedman shall immediately CEASE AND DESIST from engaging in the fraudulent activity as set forth herein in connection with the offer or sale of any security in Arkansas.

9. A hearing on this Order shall be held if requested by the Respondents in writing within thirty days of the date of the entry of this Order, or if otherwise ordered by the Commissioner. Such request should be addressed to the Commissioner and submitted to the following address:

Arkansas Securities Commissioner
201 East Markham, Suite 300
Little Rock, Arkansas 72201

10. If no hearing is requested and none is ordered by the Commissioner, this Order will remain in effect until it is modified or vacated by the Commissioner. Ark. Code Ann. § 23-42-209(a)(2).



A. Heath Abshire
Arkansas Securities Commissioner

March 19, 2009
Date