

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF INDIANA

U.S. DISTRICT COURT
SOUTHERN DISTRICT OF INDIANA
AUG 10 11:13:15
LAURA A. BRIGGS
CLERK

UNITED STATES SECURITIES
AND EXCHANGE COMMISSION,

Plaintiff,

v.

KENNETH R. PAYNE, JOHANN M. SMITH,
DANIEL G. DANKER, CONSTANCE
BROOKS-KIEFER, HEARTLAND
FINANCIAL SERVICES, INC., JMS
INVESTMENT GROUP, LLC,

Defendants.

CIVIL ACTION
FILE NO.

00-1265 C-T/G

UNITED STATES SECURITIES AND EXCHANGE COMMISSION'S
COMPLAINT FOR EX PARTE TEMPORARY RESTRAINING ORDER,
ORDERS OF PRELIMINARY AND PERMANENT INJUNCTION
AND OTHER EQUITABLE RELIEF

Plaintiff, the United States Securities and Exchange Commission

("Commission"), alleges as follows:

1. From at least January 1998 to the present, Defendants Kenneth R. Payne ("Payne"), Johann M. Smith ("Smith"), Daniel G. Danker ("Danker"), Constance Brooks-Kiefer ("Brooks-Kiefer"), Heartland Financial Services, Inc. ("Heartland") and JMS Investment Group, LLC ("JMS") have engaged in a Ponzi scheme in which they have raised at least \$29.1 million from at least 330 investors in thirteen states through the sale of investments.

2. Defendants Payne, Smith and Danker, directly and indirectly, have engaged and, unless enjoined, will continue to engage in acts, practices and courses of business which constitute violations of Sections 5(a), 5(c) and 17(a) of the Securities Act of 1933 ("Securities Act") [15 U.S.C. §§77e(a), 77e(c), 77q(a)], and Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. §78j(b)], and Rule 10b-5 [17 C.F.R. §240.10b-5] promulgated thereunder, and have aided and abetted, and unless enjoined, will continue to aid and abet acts, practices and courses of business which constitute violations of Sections 15(a) and 15(c)(1) of the Exchange Act [15 U.S.C. §§78o(a) and 78o(c)(1)], and Rule 15c1-2 promulgated thereunder [17 C.F.R. §240.15c1-2].

3. Defendant Brooks-Kiefer, directly and indirectly, has engaged and, unless enjoined, will continue to engage in acts, practices and courses of business which constitute violations of Section 17(a) of the Securities Act [15 U.S.C. §77q(a)] and Section 10(b) of the Exchange Act [15 U.S.C. §78j(b)] and Rule 10b-5 [17 C.F.R. §240.10b-5] promulgated thereunder.

4. Defendant JMS, directly and indirectly, has engaged and, unless enjoined, will continue to engage in acts, practices and courses of business which constitute violations of Sections 5(a), 5(c) and 17(a) of the Securities Act [15 U.S.C. §§77e(a), 77e(c), 77q(a)], and Sections 10(b), 15(a) and 15(c)(1) of the Exchange Act [15 U.S.C. §§78j(b), 78o(a), and 78o(c)(1)], and Rules 10b-5 and 15c1-2 [17 C.F.R. §§240.10b-5 and 240.15c1-2] promulgated thereunder.

5. Defendant Heartland, directly and indirectly, has engaged and, unless enjoined, will continue to engage in acts, practices and courses of business which constitute violations of Section 17(a) of the Securities Act [15 U.S.C. §77q(a)] and Sections 10(b), 15(a) and 15(c)(1) of the Exchange Act [15 U.S.C. §§ 78j(b), 78o(a), 78o(c)(1)] and Rules 10b-5 and 15c1-2 [17 C.F.R. §§240.10b-5 and 240.15c1-2] promulgated thereunder.

6. The Commission brings this action to enjoin such acts, practices, and courses of business pursuant to Section 20(b) of the Securities Act [15 U.S.C. §77t(b)] and Sections 21(d) and 21(e) of the Exchange Act [15 U.S.C. §§78u(d) and 78u(e)].

JURISDICTION AND VENUE

7. The Court has jurisdiction over this action pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)] and Sections 21(e) and 27 of the Exchange Act [15 U.S.C. §§ 78u(e), 78aa] and 28 U.S.C. §1331. Venue is proper in this Court pursuant to Section 27 of the Exchange Act [15 U.S.C. §78aa].

8. The acts, practices, and courses of business constituting the violations alleged herein occurred within the jurisdiction of the United States District Court for the Southern District of Indiana and elsewhere.

9. Defendants, directly and indirectly, have made, and are making, use of the means and instrumentalities of interstate commerce and of the mails in connection with the acts, practices, and courses of business alleged herein in the Southern District of Indiana and elsewhere.

10. There is a reasonable likelihood that unless enjoined, Defendants will continue to engage in the acts, practices and courses of business set forth in this complaint, and acts, practices and courses of business of similar purport and object.

11. Pursuant to authority conferred upon the Commission by Sections 10(b) and 15(c)(1) of the Exchange Act [15 U.S.C. §§78j(b) and 78o(c)(1)], the Commission has promulgated Rules 10b-5 and 15c1-2 [17 C.F.R. §§240.10b-5 and 240.15c1-2], which were in effect at all times relevant and at the present time.

DEFENDANTS

12. Heartland is an Indiana corporation headquartered in Indianapolis, Indiana and founded by Payne in or about January 1991. Heartland holds itself out as a brokerage, insurance and estate-planning firm. In or about 1998, Heartland purportedly had over 700 clients and approximately \$22.6 million in investor funds. Heartland is not registered with the Commission as a brokerage firm or in any other capacity.

13. JMS is an Indiana limited liability company founded in or about October 1997 by Smith. JMS' objective is to invest primarily in the initial public offerings of financial institutions. From in or about December 1997 to the present, JMS offered to sell 1,000 "units" of JMS for \$10,000 a unit. JMS is not registered with the Commission as a brokerage firm or in any other capacity.

14. Payne, age 51, resides in Fishers, Indiana. Prior to 1983, Payne was an attorney licensed in Indiana. In 1983, the Indiana Supreme Court disbarred Payne, for a period of five years. Payne is the president and owner of Heartland. Payne is also a registered representative of Jonathan Roberts Financial Group ("Jonathan Roberts"), a

brokerage firm registered with the Commission. Before his association with Jonathan Roberts, Payne was a registered representative of several other brokerage firms.

15. Smith, age 42, resides in Indianapolis, Indiana. Smith is the founder and manager of JMS. Smith makes the investment decisions for JMS and recommends securities purchases to JMS investors. Smith is also the attorney for Heartland and serves as the escrow agent for investments made through JMS and offshore bank investments. Since 1985, Smith also operated his own law practice, Johann M. Smith, Inc. Smith is not registered with the Commission in any capacity.

16. Danker, age 52, resides in Indianapolis, Indiana. Danker is the vice-president and office manager of Heartland. Danker maintains Heartland's books and records. Danker was a registered representative until on or about March 27, 2000. In or about 1987, Danker's license to practice law in Colorado was suspended. In or about April 2000, Danker claimed to resign from Heartland.

17. Brooks-Kiefer, age 47, resides in Indianapolis, Indiana. Brooks-Kiefer was employed by Heartland as an administrative assistant from in or about February 1993 until she resigned in mid-July 2000. Her responsibilities at both Heartland and JMS included, among other things, preparing and issuing Heartland checks, depositing investor funds, preparing and issuing confirmations and account statements to Heartland customers and JMS customers, and serving as a contact person for Heartland customers and JMS customers with questions about their accounts. Brooks-Kiefer also maintained the books and records for JMS. Brooks-Kiefer is not registered with the Commission in any capacity.

OTHER ENTITIES

18. Caribbean Federal Ltd. ("Caribbean") is an Indiana limited liability company formed by Smith to establish and operate a banking institution of the same name in Belize. The purpose of Caribbean was to make loans and establish offshore asset protection trusts.

19. 21st Century Financial Services of Heartland ("21st Century") is a company formed by Smith. Payne is the president of 21st Century. 21st Century purports to provide its customers with estate planning, retirement advice, investment selection and tax planning and preparation.

BACKGROUND

20. From at least January 1998 through the present, Defendants have raised approximately \$29.1 million from at least 330 investors residing in thirteen states. Payne, Smith and Danker, mostly through Heartland and JMS, offered and sold the following investment opportunities: (1) initial public offerings ("IPOs") of financial institutions and Internet and technology companies represented by units of JMS; (2) shares in an offshore bank located in Belize; and (3) units of Heartland. In addition, Heartland was held out as a broker-dealer and accepted money from customers to purchase unit investment trusts, money markets and mutual funds through Heartland.

21. Regardless of the investment opportunity selected by an investor, all investor funds were deposited into a non-interest bearing bank account in the name of Lincoln Fidelity Escrow (the "Lincoln account").

22. Smith and Brooks-Kiefer are the signatories on the Lincoln account.

THE FRAUDULENT SCHEME

Solicitation of Investors

23. From in or about spring 1998 to the present, to solicit investors, Payne, Smith and Danker organized and spoke at seminars sponsored by Heartland, Caribbean and 21st Century.

24. Heartland promoted the seminars through advertisements in The Senior Beacon and in buildings in Fort Wayne and Indianapolis.

25. Heartland sent invitations to JMS and Heartland investors asking them to attend the seminars. During the seminars, Payne, Smith and Danker spoke about, among other things, investment opportunities in offshore banks and domestic financial institutions as well as estate and tax planning.

26. In or about 1998, Payne and Smith took several investors on an all expenses paid trip to Belize. The expenses for the Belize trip were paid out of the Lincoln account. In or about May 2000, JMS invited investors to attend JMS' annual meeting in Grenada. While in Belize and Grenada, Smith and Payne presented the investment opportunities to investors.

27. The investors in the investment opportunities range in age, occupation and economic background. The investors are from at least 13 states, many are elderly, most reside in Indiana.

The JMS Scheme

28. From in or about December 1997 through in or about December 1999, Smith, Payne and Danker offered and sold JMS units to the investing public.

29. During that period, they raised at least \$18.5 million from at least 257 investors.

30. The minimum investment in JMS is \$10,000 for one unit. JMS unit holders must complete subscription agreements before they invest and are required to hold their investments with JMS for a minimum of 12 to 18 months.

31. JMS units were sold to at least 42 non-accredited investors.

32. JMS charges a management incentive fee of 15% of the investor's original investment, provided that the investor has first been allocated the right to receive the return of his original investment plus 20%.

33. JMS' investment objective is to invest long-term in stocks of banks that are going public or have recently gone public or to purchase initial public offerings of Internet or technology companies.

34. The stocks to be purchased are selected under two methods. Under the first method, an investor purchases a unit and JMS, on behalf of the unit holder, determines in which financial institution stock to invest the \$10,000. Under the second method, after receiving correspondence signed by Smith recommending that they "purchase" particular initial public offerings, the investor purchases at least one unit directing JMS to purchase one or more of the recommended securities.

35. Under either method, after an investor purchases a unit, JMS never purchases the promised stocks or purchases only a limited number of shares to show to investors. The remaining funds are deposited into the Lincoln account and commingled with funds from the other two investment schemes.

36. In most, if not all instances, JMS has no allocation of stock in the initial public offerings that it recommends to its customers.

37. Brooks-Kiefer sends JMS unit holders false confirmations of their investments and false monthly statements on JMS letterhead detailing the amount of shares and supposed value of their investment holdings.

38. Smith and Brooks-Kiefer make "dividend," "principal" and "profit" payments to JMS investors on their purported investments. The funds for these payments are issued from the Lincoln account and come from other investor funds.

39. In order to lull investors and solicit new investors, JMS distributed a 1999 Statement of Condition in which it claimed to have a securities portfolio valued at \$91 million as of December 31, 1999. However, during 1999, the maximum value of JMS' securities portfolio was little more than \$1 million.

The Belize Bank Scheme

40. From at least the spring of 1998 through the present, Payne and Smith sold \$1,053,459 in shares, representing ownership interests, in Caribbean to at least 68 investors.

41. In order for Caribbean to operate, it needed a charter. Payne and Smith represented to potential investors that either the creation of the banking institution was nearly 95% complete or that they had already obtained the bank charter. In or about March or April 1999, the charter for the bank was denied.

42. Payne and Smith also represented that, pending the operation of Caribbean, investor funds would be placed in a separate, interest-bearing escrow account

and earn ten percent interest. In fact, the Caribbean investor funds were commingled with funds raised in the other two schemes and deposited into the Lincoln account, a non-interest bearing account.

43. As escrow agent, Smith sent out confirmations of an investment in Caribbean on his own letterhead.

44. Even after the charter was denied, certain Belize bank investors were not refunded their principal investments and still receive purported interest payments from the Lincoln account.

45. The funds used to repay certain other Belize investors their principal investments also came from the Lincoln account.

The Heartland Scheme

46. Payne and Danker fraudulently hold Heartland out to the public as a broker-dealer even though Heartland is not registered with the Commission in any capacity.

47. In order to open a brokerage account with Heartland, customers fill out a new account application with information regarding their financial background and investment history and objectives.

48. Payne and Danker recommend securities to Heartland customers.

49. From at least January 1998 through in or about December 1999, Payne and Danker accepted \$8.8 million to purchase unit investment trusts, mutual funds and money markets for at least 118 Heartland Customer accounts.

50. Heartland charges commissions to its customers.

51. Although some Heartland customer money is used to purchase a limited amount of the recommended securities, most is commingled with other investor funds in the Lincoln account and used to operate the Ponzi scheme and pay the personal and business expenses of Defendants.

52. Brooks-Kiefer sends false confirmations and monthly account statements on Heartland letterhead detailing the customers' investments and the purported values of their supposed securities holdings.

53. If a Heartland customer liquidates a position or expects dividend payments, Payne and Danker use other investors' money to make such payments.

54. From at least January 1998 through in or about December 1999, Payne and Danker raised approximately \$785,610 from 43 investors for the purchase of Heartland stock. Heartland's shares of common stock are not registered with the Commission.

55. Heartland investor money is not deposited into the Heartland bank account. Instead, transfers from the Lincoln account represent the vast majority of deposits into the Heartland bank account.

56. Certain Heartland stockholders receive purported dividend payments for their Heartland stock. These payments are made with other investors' funds.

The Use of Investor Proceeds

57. Most, if not all, investor funds solicited by Payne, Smith and Danker for all the investment opportunities were deposited in the Lincoln account.

58. From in or about March 1999 through in or about April 2000, approximately \$28.2 million was deposited into the Lincoln account.

59. In or about July 2000, approximately \$684,000 of investor money was deposited directly into Payne's bank account. During this time period, \$1.2 million was transferred from the Lincoln account to Heartland's corporate account.

60. Payne and Danker are signatories on the Heartland account.

61. Of all of the money deposited into the Lincoln and Payne accounts and transferred to the Heartland account, only approximately \$1.8 million was used to purchase legitimate securities.

62. From March 1999 through April 2000, of the \$28.2 million deposited into the Lincoln account, Smith and Brooks-Kiefer allocated the funds, among other things, as follows: \$15.4 million to pay investors; \$1.3 million to Payne; \$506,589 to Danker; \$227,838 to Smith; \$148,686 to Brooks-Kiefer; and \$878,260 for travel, entertainment and clothing allowances for employees.

63. From March 1999 through April 2000, Defendants withdrew approximately \$1.3 million in cash from the Lincoln, Heartland and Payne accounts.

64. During the period January 1998 through April 2000, \$1,895,937 was deposited in the Heartland account, of which \$1,837,850 was transferred from the Lincoln account.

65. The \$1,895,937 in funds were used as follows: \$242,055 was paid to investors in the form of profits, dividends or the return of principal; \$508,715 was paid to Payne and to pay his personal expenses; \$74,400 was paid to Smith; and \$26,100 was converted into cash.

COUNT I
Violations of Sections 5(a) and 5(c) of the Securities Act
[15 U.S.C. § 77e(a) and 77e(c)]

66. Paragraphs 1 through 65 are realleged and incorporated by reference herein.

67. At the times alleged in this Complaint, Defendants Payne, Smith, Danker and JMS, directly and indirectly, made and are making use of the means and instruments of transportation and communication in interstate commerce and of the mails to offer and sell, through the use or medium of a prospectus or otherwise, securities in the form of units of JMS and carried and is carrying such securities and caused and is causing them to be carried through the mails and interstate commerce by the means and instruments of transportation for the purpose of sale and delivery after sale.

68. No registration as to the securities described in Paragraph 67 above is in effect nor has any registration statement been filed with the Commission.

69. By reason of the activities described in Paragraphs 66 through 68 above, Defendants Payne, Smith, Danker and JMS have violated and are violating Sections 5(a) and 5(c) of the Securities Act [15 U.S.C. § 77e(a) and 77e(c)].

COUNT II
Violations of Section 17(a)(1) of the Securities Act [15 U.S.C. § 77q(a)(1)]

70. Paragraphs 1 through 65 are realleged and incorporated by reference herein.

71. At the times alleged in this Complaint, Defendants Payne, Smith Danker, Brooks-Kiefer, Heartland and JMS, in the offer and sale of securities in the form of: (1) IPOs of financial institutions and Internet and technology companies

represented by units of JMS; (2) shares in Caribbean; (3) units of Heartland; and (4) unit investment trusts, money markets and mutual funds to be purchased for Heartland's customers, by the use of the means and instruments of transportation and communication in interstate commerce and by the use of the mails, directly and indirectly, have employed and are employing devices, schemes and artifices to defraud, all as more fully described in Paragraph 70 above.

72. In the offer and sale of securities described above in Paragraph 71, and as part of the scheme to defraud, Defendants Payne, Smith, Danker, Brooks-Kiefer, Heartland and JMS have made and are making false and misleading statements of material fact and have omitted and are omitting to state material facts to investors and prospective investors regarding, among other things: the true use of investor funds, the amount of investor funds actually used to purchase securities, the value of allegedly purchased securities, the existence of an escrow account for Caribbean and a charter for Caribbean, all as more fully described above in Paragraphs 70 through 72 above.

73. Defendants Payne, Smith, Danker, Brooks-Kiefer, Heartland and JMS knew or were reckless in not knowing of the facts and circumstances described in Paragraphs 70 through 72 above.

74. By reason of the activities described in Paragraphs 70 through 73 above, Defendants Payne, Smith, Danker, Brooks-Kiefer, Heartland and JMS have violated and are violating Section 17(a)(1) of the Securities Act [15 U.S.C. § 77q(a)(1)].

