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12
 13 **UNITED STATES DISTRICT COURT**
 14 **CENTRAL DISTRICT OF CALIFORNIA**

15 SECURITIES AND EXCHANGE
 16 COMMISSION,

17 Plaintiff,

18 vs.

19 ANGEL ACQUISITION CORP. f/k/a
 PALOMAR ENTERPRISES, INC.,
 20 MARSHALL HOLDINGS
 INTERNATIONAL, INC. f/k/a
 21 GATEWAY DISTRIBUTORS, LTD.,
 NW TECH CAPITAL, INC. f/k/a
 22 CYBERTEL CAPITAL CORP.,
 WINSTED HOLDINGS, INC., ZANN
 23 CORP., RICHARD A. BAILEY, MARK
 T. ELLIS AND FLORIAN R. TERNES,

24 Defendants.
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Case No.

SACV08-880

JMS (AMS)

**COMPLAINT FOR VIOLATIONS
 OF THE FEDERAL SECURITIES
 LAWS**

1 Plaintiff Securities and Exchange Commission (“Commission”) alleges as
2 follows:

3 **JURISDICTION AND VENUE**

4 1. This Court has jurisdiction over this action pursuant to Sections 20(b),
5 20(d)(1) and 22(a) of the Securities Act of 1933 (“Securities Act”), 15 U.S.C.
6 §§ 77t(b), 77t(d)(1) and 77v(a). Defendants, directly or indirectly, made use of the
7 means or instrumentalities of interstate commerce, the mails or the facilities of a
8 national securities exchange in connection with the transactions, acts, practices and
9 courses of business alleged in this Complaint.

10 2. Venue is proper in this Court pursuant to Section 22(a) of the
11 Securities Act, 15 U.S.C. § 77v(a), because certain of the transactions, acts,
12 practices and courses of conduct constituting violations of the federal securities
13 laws occurred within this district. Defendant Mark Ellis resides and transacts
14 business in this district and defendants Angel Acquisition Corp. f/k/a Palomar
15 Enterprises, Inc. (“Angel Acquisition”), Marshall Holdings International, Inc. f/k/a
16 Gateway Distributors, Ltd. (“Marshall Holdings”), NW Tech Capital, Inc. f/k/a
17 Cybertel Capital Corp. (“NW Tech”), Winsted Holdings, Inc. (“Winsted
18 Holdings”), Zann Corp., Richard A. Bailey (“Bailey”) and Florian R. Ternes
19 (“Ternes”) all transact business in this district or transacted business in this district
20 during the time period relevant to this Complaint.

21 **SUMMARY**

22 3. This action concerns the abuse of Form S-8 registration statements by
23 several microcap companies. From mid-2002 through mid-2005 (the “relevant
24 period”), Angel Acquisition, Marshall Holdings, NW Tech, Winsted Holdings and
25 Zann Corp. (collectively, “Issuer Defendants”) distributed billions of shares of
26 common stock to the public in unregistered securities offerings disguised as
27 employee stock option programs. The Issuer Defendants improperly registered the
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1 shares underlying the stock options granted under the programs on Form S-8 and
2 then received the bulk of the proceeds from the sales of the shares as payment for the
3 exercise price of the options.

4 4. As designed and implemented, the so-called employee stock option
5 programs actually functioned as public offerings in which the Issuer Defendants used
6 their employees as conduits to the market so that they could raise millions of dollars
7 in capital without complying with the registration requirements of the Securities Act.
8 The money received by the Issuer Defendants under the programs greatly exceeded
9 their revenues from operations and allowed them to fund their struggling
10 operations. Moreover, the employee stock option programs resulted in billions of
11 shares being issued to the public in unregistered transactions, causing a severe
12 dilution of existing shareholder interests.

13 5. In addition to the Issuer Defendants, the Commission asserts claims
14 against three individuals, who were officers and directors of certain Issuer
15 Defendants, based on their improper conduct in connection with the employee
16 stock option programs. Defendant Ellis controlled the program at Winsted
17 Holdings. During the course of the program, Winsted had practically no revenues
18 from operations yet used the proceeds received from its employee stock option
19 program to fund \$1 million in salary payments to Ellis. Defendants Bailey and
20 Ternes were responsible Marshall Holdings' employee stock option program and
21 received significant increases to their salaries during the course of the program.

22 6. Through the activities alleged in this Complaint, the defendants,
23 directly or indirectly, engaged in and, unless enjoined, will continue to engage in
24 transactions, acts, practices or courses of business which violate Sections 5(a) and
25 5(c) of the Securities Act, 15 U.S.C. §§77e(a) and (c). The Commission seeks to
26 permanently enjoin the defendants from engaging in the wrongful conduct alleged
27 in this Complaint and also seeks other relief, including disgorgement of ill-gotten
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1 gains together with prejudgment interest and, in the case of Marshall Holdings,
2 Ellis, Bailey and Ternes, civil money penalties.

3 **DEFENDANTS**

4 7. **Angel Acquisition** is a Nevada corporation with its principal office in
5 Carson City, Nevada. Its business operations are located in Carlsbad, California
6 and Cardiff, California. The company provides mortgage brokerage services and
7 acquires and develops real estate. During the relevant period, Angel Acquisition
8 was a reporting company under Section 13 of the Securities Act, 15 U.S.C. §78m.
9 Its stock is registered with the Commission under Section 12(g) of the Securities
10 Exchange Act of 1934 (“Exchange Act”), 15 U.S.C. § 78l, and is listed on the OTC
11 Bulletin Board.

12 8. **Marshall Holdings** is a Nevada corporation with its principal place of
13 business in Las Vegas, Nevada. Through its subsidiaries, it sells and distributes
14 nutritional, health and skin products through network marketing and websites.
15 Marshall Holdings is a reporting company under Section 13 of the Securities Act,
16 15 U.S.C. § 78m. Its stock is registered with the Commission under Section 12(g)
17 of the Exchange Act, 15 U.S.C. § 78l, and is listed on the OTC Bulletin Board.

18 9. **NW Tech** is a Nevada corporation with its principal place of business
19 in Vancouver, Washington. During the relevant period, the company was located
20 in Vista, California and primarily provided telecommunication services. NW Tech
21 is a reporting company under Section 13 of the Securities Act, 15 U.S.C. § 78m.
22 Its stock is registered with the Commission under Section 12(g) of the Exchange
23 Act, 15 U.S.C. § 78l, and is listed on the OTC Bulletin Board. The company
24 currently provides consulting and management services in the areas of
25 telecommunications, wireless and broadband.

26 10. **Winsted Holdings** is a Florida corporation currently based in
27 Northfield, Illinois. During the relevant period, the company’s principal place of
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1 business was Newport Beach, California and it was a reporting company under
2 Section 13 of the Securities Act, 15 U.S.C. § 78m. Its stock was registered with
3 the Commission under Section 12(g) of the Exchange Act, 15 U.S.C. § 78l, and
4 was listed on the OTC Bulletin Board. Winsted Holdings previously provided
5 telecommunications services but currently focuses on acquiring interests in
6 emerging private companies.

7 11. **Zann Corp.** is a Nevada corporation with its principal place of
8 business in Clermont, Florida. During the relevant period, the company operated
9 out of Fenton, Michigan and focused on acquiring and developing other
10 businesses. It was a reporting company under Section 13 of the Securities Act, 15
11 U.S.C. § 78m, and its stock was registered with the Commission under Section
12 12(g) of the Exchange Act, 15 U.S.C. § 78l, and was listed on the OTC Bulletin
13 Board.

14 12. **Bailey**, age 52, is a resident of Las Vegas, Nevada. He serves as the
15 Chief Executive Officer, Chief Financial Officer, President and Chairman of
16 Marshall Holdings. During the relevant period, Bailey, along with Ternes, directed
17 Marshall Holdings' use of its employee stock option program.

18 13. **Ellis**, age 42, is a resident of Irvine, California. During the relevant
19 period, he was the Chief Executive Officer, Chief Financial Officer, President,
20 Secretary, Director and controlling shareholder of Winsted Holdings. Ellis
21 directed the company's ESIP program. Ellis resigned his positions with Winsted
22 Holdings in June 2007.

23 14. **Ternes**, age 59, is a resident of Las Vegas, Nevada. He serves as the
24 Chief Operating Officer, Secretary and Director of Marshall Holdings. Ternes,
25 along with Bailey, directed the company's use of its employee stock option
26 program.

1 **FACTS**

2 **I. Overview of the Issuer Defendants' ESIP Programs**

3 15. Starting in mid-2002, the Issuer Defendants implemented employee
4 stock option programs that were virtually identical in design and implementation.
5 The programs were adopted pursuant to plan documents titled Employee Stock
6 Incentive Plans ("ESIPs").

7 16. The Issuer Defendants learned about the ESIP programs from
8 Alexander & Wade, Inc. ("AWI"), a self-described investment banking firm
9 located in San Diego, California, hired by the Issuer Defendants to provide
10 consulting services. AWI pitched the ESIP programs to the Issuer Defendants in
11 part as a way to raise money.

12 17. The Issuer Defendants registered the shares underlying the stock
13 options on Form S-8 registration statements filed with the Commission. The ESIP
14 documents were attached as exhibits to the Form S-8s.

15 18. Pursuant to the Securities Act, registrants may use Form S-8 to
16 register securities issued to compensate employees and consultants for *bona fide*
17 services not connected with the offer or sale of securities. Because of the
18 compensatory purpose and the presumed familiarity of employees and consultants
19 with the registrant's business, Form S-8's disclosure requirements are abbreviated
20 as compared to statements registering shares used to raise capital.

21 19. As implemented by the Issuer Defendants, however, the ESIP
22 programs functioned as public offerings in which the Issuer Defendants used their
23 employees as conduits to the markets so that they could raise capital.

24 20. The ESIP programs had three features that, taken together, virtually
25 guaranteed that the options would be exercised and the underlying shares
26 simultaneously sold to the public at or near the time the options were granted to
27 employees:
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1 a. First, the options' exercise price hinged on the market value of
2 an Issuer Defendant's stock at the time of exercise (versus the date of grant).
3 The Issuer Defendants set the exercise price at a high percentage, typically
4 85%, of the proceeds received from the sale of shares underlying the options.
5 This ensured that the options were immediately "in the money" – that is, the
6 exercise price was always less than the market price whenever the options
7 were exercised – and that the Issuer Defendant, not the employee, would
8 receive most of the benefit from an increase in stock price after the time of
9 grant.

10 b. Second, the options vested immediately, meaning that there was
11 no waiting period after the options were granted or any other condition that
12 needed to be met before the options could be exercised.

13 c. Third, a cashless method was used to exercise the options so
14 that the exercise price was remitted to the Issuer Defendant from the sales
15 proceeds of the shares underlying the options. Accordingly, the employees
16 did not have to pay any money out-of-pocket to exercise the options.

17 21. Under the ESIP programs, the Issuer Defendants and virtually all of
18 their employees had brokerage accounts at the same broker-dealer firm, Finance
19 500, Inc. in Irvine, California.

20 22. When Finance 500 opened the accounts for the employees, it typically
21 obtained standing orders or other instructions from the employees that the options
22 should be exercised immediately after grant.

23 23. Also, Finance 500 required the employees to fill out and have
24 notarized multiple blank authorizations before the Issuer Defendants granted any
25 options. The Issuer Defendants collected and forwarded these authorizations to
26 Finance 500 as part of setting up the ESIP programs. The authorizations gave
27 Finance 500 authority to (i) sell the shares underlying any options granted by the
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1 Issuer Defendants and (ii) exercise the options using the sales proceeds from the
2 underlying shares to pay the exercise price.

3 24. When the Issuer Defendants granted options, they sent Finance 500
4 share certificates representing the number of Form S-8 shares underlying the
5 options granted. Upon receipt of the certificates, Finance 500 relied on the
6 standing orders and authorizations from the employees to sell the shares underlying
7 the options to the public. It then calculated the option exercise price at 85% of the
8 sales price and routed that amount to the Issuer Defendant accounts and the
9 remainder, minus fees, to the employee accounts.

10 25. The Issuer Defendants issued options to employees frequently,
11 sometimes as many as five times in a given month.

12 26. In some cases, the employees were not notified of an option grant
13 until after they received their portion of the sales proceeds from the underlying
14 shares.

15 27. The employees received relatively modest amounts under the
16 programs (approximately 7%-8% of the sales proceeds, after brokerage fees and
17 costs) compared to the Issuer Defendants. Accordingly, the ESIP programs
18 provided no practical incentive for an employee to work to increase the stock price
19 for an Issuer Defendant because the employee's share of the sales proceeds was
20 always limited to a small percentage.

21 28. In contrast, the Issuer Defendants received the vast majority of the
22 sales proceeds from the underlying stock as payment for the exercise price ("ESIP
23 proceeds"). These amounts greatly exceeded the revenues earned by the Issuer
24 Defendants.

25 29. The Issuer Defendants relied on the ESIP proceeds to fund the
26 operations of their otherwise failing businesses.

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1 30. The ESIP programs resulted in billions of shares of each Issuer
2 Defendant's stock being sold to the public, which severely diluted the ownership
3 interests of existing shareholders. Throughout the programs, the Issuer
4 Defendants' stock generally traded at fractions of a penny and their stock prices
5 trended downward.

6 31. The design of the ESIP programs (*i.e.*, the high-percentage exercise
7 price that was always "in the money," the immediate vesting and the use of the
8 cashless exercise method that allowed exercise without any payment by the
9 employees up-front) – combined with the standing orders to exercise immediately
10 – all but guaranteed that the underlying shares were sold to the public nearly
11 immediately upon the grant of the stock options.

12 32. By virtue of the design and implementation of the ESIP programs, the
13 Issuer Defendants controlled the timing of the sales to the public through the
14 timing of their option grants. This allowed the Issuer Defendants to anticipate
15 receipt of ESIP proceeds shortly after granting options.

16 33. The ESIP programs essentially functioned as public offerings in that
17 the Issuer Defendants used their employees as conduits to raise significant amounts
18 of capital in the marketplace.

19 34. Because Form S-8 cannot be used to raise capital, no registration
20 statements were in effect or filed as to the shares issued under the ESIP programs.

21 **II. Additional Allegations As To Specific Defendants**

22 A. Angel Acquisition's ESIP Program

23 35. Paragraphs 1 through 34 are realleged and incorporated by reference
24 herein.

25 36. One month before it implemented its ESIP program, Angel
26 Acquisition was essentially a shell company in very poor financial condition. At
27 the time it started the program in June 2003, the company had just undergone a
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1 change in control and had implemented a new business plan.

2 37. Angel Acquisition's new management learned of the ESIP program
3 from AWI. The firm told the company that the program would not only grow the
4 company by allowing it to recruit, train and retain employees, but also provided the
5 benefit of generating proceeds that could be used for operations.

6 38. Angel Acquisition implemented the ESIP program to generate money
7 to fund the business and to compensate and retain employees.

8 39. The following table summarizes Angel Acquisition's Form S-8 filings
9 under the program:

#	S-8 Filing Date	# of Shares Registered
1	6/23/2003	16,000,000
2	8/13/2003	70,000,000
3	10/14/2003	23,000,000
4	11/21/2003	90,000,000
5	2/12/2004	160,000,000
6	5/28/2004	220,000,000
7	9/14/2004	750,000,000
8	10/18/2004	1,150,000,000
	Total:	2,479,000,000

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21 (This table as well as similar tables in this Complaint detail the Form S-8 filings
22 and post-effective amendments that register the offer and sale of shares underlying
23 the stock options issued under the ESIP programs.)

24 40. Prior to the ESIP program's launch, Angel Acquisition had 31.9
25 million shares of common stock outstanding. Its stock was thinly traded, with
26 daily trading volumes ranging between zero and the tens of thousands and the price
27 ranging between \$.017 and \$.095. After the launch, the daily trading volume
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1 significantly increased to the millions and often to the tens of millions. Towards
2 the end of the program, the stock price fell as low as \$.00019.

3 41. For the first half of 2003, Angel Acquisition had no revenue or
4 operations, and suffered a net loss of \$272,000. After the company launched the
5 program in June 2003, the ESIP proceeds far exceeded revenues:

6	Year	Revenues	ESIP Proceeds
7	2003	\$9,000	\$749,000
8	2004	\$737,000	\$2,358,000
9	2005 (first 3 mos.)	\$87,000	\$182,000
10	Totals:	\$833,000	\$3,289,000

11 (The figures for revenues and ESIP proceeds in this Complaint are rounded to the
12 nearest thousand.)

13 42. The company operated at a loss during the course of the program and
14 used the ESIP proceeds to fund its business.

15 43. Angel Acquisition acknowledged that it used the ESIP program to
16 raise capital and fund operations in its periodic filings with the Commission.

17 44. For example, in the company's Form 10-Q for the quarterly period
18 ended March 31, 2004, Angel Acquisition stated:

19 The Company raises capital through the issuance and exercise of
20 options under the Company's ESIP. During the three months ended
21 March 31, 2004 the Company raised \$943,735 net of brokerage
22 commissions through its ESIP.

23 45. Furthermore, in its Form 10-Q for the quarterly period ended
24 September 30, 2004, Angel Acquisition stated:

25 Cash flows provided from financing activities w[ere] \$2,487,910 for
26 the nine months ended September 30, 2004. This was mainly from
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1 proceeds received from officers and employees for stock options
2 exercised during this period in the amount of \$2,419,590.

3 46. Angel Acquisition ended its ESIP program in early 2005.

4 B. Marshall Holdings' ESIP Program

5 47. Paragraphs 1 through 34 are realleged and incorporated by reference
6 herein.

7 48. Before it implemented the ESIP program, Marshall Holdings was in
8 poor financial condition. The company's 2002 financial statements show that,
9 while it earned \$1.15 million in revenues, it recognized a net loss of \$2.8 million.

10 49. Bailey and Ternes decided to implement the ESIP program to bring
11 money into the company and to retain employees through increased pay.

12 50. The following table summarizes Marshall Holdings' Form S-8 filings
13 under the ESIP program:

	S-8 Filing	# of Shares
#	Date	Registered
1	4/11/2003	1,000,000,000
2	1/22/2004	900,000,000
3	3/17/2004	2,000,000,000
4	4/22/2004	2,000,000,000
5	5/27/2004	3,009,243,200
6	6/18/2004	3,884,253,600
7	8/24/2004	8,000,000,000
	Total:	16,793,496,800

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24 51. Just prior to the ESIP program launch, Marshall Holdings had 4.2
25 billion shares of common stock outstanding. During the course of the ESIP
26 program, the daily trading volume for the company's stock was regularly in the
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1 tens and hundreds of millions and, on a few occasions, exceeded one billion. The
2 stock price also fell as low as \$.00013.

3 52. Marshall Holdings received ESIP proceeds that were significantly
4 greater than revenues earned during the existence of the program:

5	Year	Revenues	ESIP Proceeds
6	2003	\$1,120,000	\$1,888,507
7	2004	\$1,150,000	\$6,857,743
8	2005 (first 6 mos.)	\$391,000	\$227,783
9	Totals:	\$2,661,000	\$8,974,033

10 53. While Marshall Holdings consistently operated at a loss, the company
11 was able to fund operations, acquire assets and pay debt because of its receipt of
12 ESIP proceeds.

13 54. Marshall Holdings acknowledged that it used the ESIP program to
14 raise funds for operations in its periodic filings with the Commission. For
15 example, in its Form 10-K for the fiscal year ended 2003, Marshall Holdings
16 stated:

17 In 2003 an Employee Stock Incentive Plan (ESIP) was set up and[,]
18 through stock issues to the public, we raised \$1,888,507 in cash to
19 provide the vehicle to finance the activities for 2003. . . . [I]t is likely
20 that we may rely heavily on the issuance of our shares to pay
21 consultants and other professionals and to raise cash during 2004.

22 55. Similarly, in its Form 10-Q for the quarterly period ended March 31,
23 2004, Marshall Holdings stated:

24 During January through March 2004, the company issued the
25 remaining 447,745,400 shares authorized out of the 1,000,000,000
26 shares approved in the ESIP Plan 2003. Also during January through
27 March 2004, the company issued 2,581,432,000 shares out of the
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1 2,900,000,000 total shares approved as of March 31, 2004 in the
2 ESIP Plans 2004. . . . The total net proceeds received from these stock
3 issues during January through March 2004 are \$2,310,487.

4 The Form 10-Q further added:

5 We had a net working capital deficit of \$2,860,000 at the end of
6 March 31, 2004, as compared to a \$4,284,000 deficit at the end of
7 December 31, 2003. Our working capital deficit decreased
8 \$1,424,000 primarily as a result of raising additional capital through
9 stock issues of \$2,310,000.

10 56. In its Form 10-Q for the quarterly period ended June 30, 2004,
11 Marshall Holdings stated:

12 Cash flow provided from financing activities was \$6,084,206 for the
13 six months ended June 30, 2004. This was mainly from proceeds
14 received from employees for stock options exercised during this
15 period of \$5,099,411. . . .

16 57. Bailey and Ternes were the primary decision-makers behind Marshall
17 Holdings' ESIP program. They decided when to file Form S-8s, decided how
18 many shares to register on those Form S-8s, signed the Form S-8s and determined
19 when to grant options to particular employees.

20 58. Bailey's and Ternes' salaries significantly increased during the course
21 of the program. In 2003, when the program first began, Bailey earned \$101,500
22 and Ternes \$89,500. Bailey's salary increased to \$216,000 in 2004 and \$240,000
23 in 2005. Ternes' salary increased to \$186,000 in 2004 and \$204,000 in 2005.

24 59. Marshall Holdings continued to issue options under its ESIP program
25 until Spring 2005.

1 C. NW Tech's ESIP Program

2 60. Paragraphs 1 through 34 are realleged and incorporated by reference
3 herein.

4 61. NW Tech learned of the ESIP program from AWI, which told NW
5 Tech that the ESIP program would help the company pay its bills and retain its
6 employees.

7 62. According to the Independent Client Service Agreement between NW
8 Tech and AWI, NW Tech retained the consulting firm to "[a]dvice, assist and
9 provide all documentation . . . in setting up S-8 for employee payroll and stock
10 options to pay monthly [NW Tech's] expenses."

11 63. The following table summarizes NW Tech's Form S-8 filings under
12 the ESIP program:

#	S-8 Filing Date	# of Shares Registered
1	7/12/02	6,000,000
2	9/20/02	9,000,000
3	12/13/02	20,000,000
4	4/11/03	30,000,000
5	6/11/03	100,000,000
6	7/3/03	100,000,000
7	9/2/03	450,000,000
8	1/14/04	450,000,000
9	6/1/04	750,000,000
10	7/23/04	900,000,000
11	8/3/04	4,000,000,000
	Total:	6,815,000,000

1 64. Prior to the launch of the ESIP program, NW Tech had 10.3 million
2 shares of common stock outstanding with daily trading volumes in the tens of
3 thousands and prices ranging between \$.07 and \$.38. By March 2003, the shares
4 regularly traded at tenths of a cent and, by July 2003, daily volume was regularly
5 in the tens of millions. When NW Tech filed its last Form S-8 on August 3, 2004,
6 the shares were trading at \$.00038 and the daily trading volume was over 31
7 million.

8 65. When it implemented the ESIP program, NW Tech was struggling
9 financially with revenues of \$623,000 and a net loss of \$701,000 for the first half
10 of 2002. Soon after the program's launch in July 2002, however, the ESIP
11 proceeds began to exceed revenues earned by large margins:

12	Year	Revenues	ESIP Proceeds
13	2002	\$1,170,000	\$190,000
14	2003	\$844,000	\$2,311,000
15	2004	\$218,000	\$2,152,000
16	2005 (first 6 mos.)	\$36,000	\$677,000
17	Totals:	\$2,281,000	\$5,330,000

18 66. The company, which was operating at a loss during the program's
19 existence, used the ESIP proceeds to pay its bills and run the business.

20 67. NW Tech terminated the ESIP program in mid-2005.

21 D. Winsted Holdings' ESIP Program

22 68. Paragraphs 1 through 34 are realleged and incorporated by reference
23 herein.

24 69. Ellis assumed control of Winsted Holdings in February 2003. He
25 implemented Winsted Holdings' ESIP program in April 2003. At the time, the
26 company had no operations and was in poor financial condition with revenues in
27 2002 of \$0 and a net loss of \$778,000.

1 70. The following table summarizes Winsted Holdings' Form S-8 filings
2 under its ESIP program:

#	S-8 Filing Date	# of Shares Registered
1	4/17/2003	40,000,000
2	5/29/2003	75,000,000
3	6/20/2003	310,000,000
4	8/13/2003	255,000,000
5	4/2/2004	350,000,000
6	5/27/2004	210,000,000
7	7/26/2004	300,000,000
8	9/3/2004	120,000,000
9	10/18/2004	200,000,000
10	1/18/2005	400,000,000
	Total:	2,260,000,000

16 71. Just prior to the ESIP program's implementation, the company had
17 376 million shares of common stock outstanding; a share price ranging between
18 \$.002 and \$.019 and a daily trading volume consistently below one million shares
19 and often zero shares. After the launch of the program, the daily trading volume
20 rose so that it was consistently in the tens of millions and, on multiple occasions,
21 exceeded one hundred million shares. Additionally, the price fell as low as
22 \$.00063.

23 72. The proceeds received under the ESIP program dwarfed the
24 company's practically non-existent revenues:
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Year	Revenues	ESIP Proceeds
2003	\$0	\$1,283,162
2004	\$24,000	\$1,087,050
2005 (first 3 mos.)	\$0	\$63,973
Totals:	\$27,000	\$2,434,185

73. The company operated at a loss throughout the program and relied on ESIP proceeds as its only means to pay expenses and fund operations, including Ellis' salary. In 2003, the company used 27% of the ESIP proceeds to pay a \$350,000 salary to Ellis. In 2004, the company used 64% of the ESIP proceeds to pay a \$692,000 salary to Ellis.

74. Winsted Holdings acknowledged that it used the ESIP program to finance its operations in its periodic filings with the Commission. For example, its Form 10-K for the fiscal year ended December 31, 2003, Winsted Holdings stated that it "financed its operations entirely with . . . [the] proceeds from the exercise of options to acquire its common stock."

75. Similarly in its Form 10-K for the fiscal year ended December 31, 2004, Winsted Holdings stated that it "financed its operations entirely with . . . proceeds from the exercise of options to acquire its common stock."

76. Ellis was the primary decision-maker for Winsted Holdings' ESIP program. He decided when to file Form S-8s, decided how many shares to register on those statements, signed the statements and determined when to grant options to particular employees.

77. Winsted Holdings terminated its ESIP program in early 2005.

1 E. Zann Corp.'s ESIP Program

2 78. Paragraphs 1 through 34 are realleged and incorporated by reference
3 herein.

4 79. When Zann Corp. implemented its ESIP program in June 2003, the
5 company had recently undergone a change in control and was essentially a shell
6 company.

7 80. Zann Corp. first learned of the ESIP program after contacting AWI to
8 seek help in locating funding. AWI mentioned the ESIP program while discussing
9 potential funding options.

10 81. Zann Corp. decided to implement the ESIP program to receive the
11 ESIP proceeds and to incentivize employees.

12 82. The following table summarizes Zann Corp.'s Form S-8 filings under
13 the ESIP program:

#	S-8 Filing Date	# of Shares Registered
1	6/6/03	33,000,000
2	8/29/03	20,860,000
3	9/29/03	22,000,000
4	10/14/03	26,000,000
5	11/13/03	78,000,000
6	1/27/04	100,000,000
7	6/17/04	160,000,000
8	9/24/04	130,000,000
9	11/4/04	87,000,000
10	12/1/04	800,000,000
	Total:	1,456,860,000

1 83. Before the ESIP program's launch, Zann Corp. had 52.8 million
2 shares of common stock outstanding. Its stock often had no daily trading volume
3 and, when it did have volume, it was in the tens of thousands with a price ranging
4 between \$.0115 and \$.05. After the program's launch, the stock's daily trading
5 volume was in the millions and tens of millions. The stock price was at a tenth of a
6 cent and, by October 2004, was at a thousandth of a cent.

7 84. Zann Corp. was in poor financial condition when it implemented its
8 ESIP program with 2002 revenues of \$783,000 and a net loss of \$11.5 million.

9 85. Under the program, the company received significant amounts of
10 ESIP proceeds compared to its almost non-existent revenues:

11	Year	Revenues	ESIP Proceeds
12	2003	\$0	\$1,192,659
13	2004	\$1,400	\$1,741,499
14	2005 (first 6 mos.)	\$0	\$289,652
15	Totals:	\$1,400	\$3,223,810

16 86. Without the ESIP proceeds, the company would not have survived.
17 Zann Corp had little to no operations and consistently operated at a loss during the
18 program's existence. The company used ESIP proceeds to pay expenses such as
19 salaries, inventory and debt reduction.

20 87. Zann Corp. ended the ESIP program in Spring 2005.

21 **FIRST CLAIM FOR RELIEF**

22 **Unregistered Offer and Sale of Securities**

23 **Violations of Section 5(a) and 5(c) of the Securities Act**

24 88. Paragraphs 1 through 87 are realleged and incorporated by reference
25 herein.

26 89. The defendants, and each of them, by engaging in the conduct
27 described above, directly or indirectly, made use of means or instruments of
28

1 transportation or communication in interstate commerce or of the mails, to offer to
2 sell or to sell securities, or to carry or cause such securities to be carried through
3 the mails or in interstate commerce for the purpose of sale or for delivery after
4 sale.

5 90. No registration statements have been filed with the Commission or
6 have been in effect with respect to any of the offerings alleged herein.

7 91. By reason of the foregoing, each of the defendants violated and,
8 unless enjoined, will continue to violate Sections 5(a) and 5(c) of the Securities
9 Act, 15 U.S.C. §§ 77e(a) and 77e(c).

10 **PRAYER FOR RELIEF**

11 WHEREFORE, the Commission respectfully requests that the Court:

12 **I.**

13 Find that Defendants committed the violations alleged above.

14 **II.**

15 Issue orders, in a form consistent with Rule 65(d) of the Federal Rules of
16 Civil Procedure, permanently enjoining defendants and their officers, agents,
17 servants, employees and attorneys, and those persons in active concert or
18 participation with them who receive actual notice of the order or judgment by
19 personal service or otherwise, and each of them, from directly or indirectly
20 violating Sections 5(a) and 5(c) of the Securities Act, 15 U.S.C. §§ 77e(a) and (c).

21 **III.**

22 Order the defendants to disgorge all ill-gotten gains that they received as a
23 result of the acts and courses of conduct complained of herein, together with
24 prejudgment interest thereon.

25 **IV.**

26 Order defendants Marshall Holdings, Ellis, Bailey and Ternes to pay civil
27 penalties pursuant to Section 20(d) of the Securities Act, 15 U.S.C. § 77t(d).

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V.

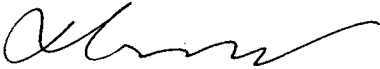
Retain jurisdiction of this action in accordance with the principles of equity and the Federal Rules of Civil Procedure in order to implement and carry out the terms of all orders and decrees that may be entered or to entertain any suitable application or motion for additional relief within the jurisdiction of this Court.

VI.

Grant such other and further relief as the Court may determine to be just and necessary.

DATED: August 6, 2008

Respectfully submitted,



David J. Van Havermaat
Attorney for Plaintiff
Securities and Exchange Commission