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**STATE OF WASHINGTON
DEPARTMENT OF FINANCIAL INSTITUTIONS
SECURITIES DIVISION**

IN THE MATTER OF DETERMINING
whether there has been a violation of the
Securities Act of Washington by:

Partners Mortgage Corporation and Gary Lynn
Craig,

Respondents.

Order Number S-04-245-05-SC01

STATEMENT OF CHARGES AND NOTICE
OF INTENT TO ENTER AN ORDER TO
CEASE AND DESIST; TO IMPOSE FINES;
AND TO BAR SECURITIES BROKER-
DEALER, SECURITIES SALESPERSON,
INVESTMENT ADVISER, AND
INVESTMENT ADVISER
REPRESENTATIVE REGISTRATION

THE STATE OF WASHINGTON TO:

Partners Mortgage Corporation
Gary Lynn Craig, CRD #874487

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STATEMENT OF CHARGES

Please take notice that the Securities Administrator of the State of Washington has reason to believe that the Respondents, Partners Mortgage Corporation and Gary Lynn Craig, have each violated the Securities Act of Washington. The Securities Administrator believes those violations justify a bar of Gary Lynn Craig from applying to be a securities broker-dealer, securities salesperson, investment adviser, or investment adviser representative pursuant to RCW 21.20.110(1); the entry of an order against both Respondents to cease and desist from such violations pursuant to RCW 21.20.390; and the imposition of fines pursuant to RCW 21.20.110(4) and 21.20.395(1). The Securities Administrator finds as follows:

STATEMENT OF CHARGES AND NOTICE OF INTENT
TO ENTER AN ORDER TO CEASE AND DESIST; TO
IMPOSE FINES; AND TO BAR SECURITIES BROKER-
DEALER, SECURITIES SALESPERSON, INVESTMENT
ADVISER, AND INVESTMENT ADVISER
REPRESENTATIVE REGISTRATION

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DEPARTMENT OF FINANCIAL INSTITUTIONS
Securities Division
PO Box 9033
Olympia, WA 98507-9033
360-902-8760

1 **TENTATIVE FINDINGS OF FACT**

2 Respondents

3 1. Partners Mortgage Corporation (“PMC”), unified business identifier no. 601 641 141, is an
4 inactive Washington corporation that was incorporated in June 1995. PMC’s principal place of business
5 was in King County, Washington. PMC was in the business of making high-interest, real estate secured
6 loans.

7 2. Gary Lynn Craig (“Craig”), an individual residing in King County, Washington, owned
8 100% of PMC and was PMC’s president and registered agent. Craig was also the president of Craig &
9 Associates, a securities broker-dealer registered with the National Association of Securities Dealers
10 (“NASD”). The NASD Central Registration Depository number for Craig is 874487. Craig was
11 registered in the State of Washington as a securities salesperson from June 1986 until May 2006.

12 Offering of Real Estate Secured Notes

13 3. In June 1995, Respondents made a Regulation D, Rule 506 exemption filing with the
14 Washington Securities Division for a \$100 million offering of notes.

15 4. In total from 1995 to 2003, Respondents sold approximately \$81 million of promissory
16 notes (“Notes”) purportedly secured by an undivided interest in a pool of real estate secured loans
17 (“Collateral Mortgage Pool”) to approximately 585 investors, most of whom were Washington residents.
18 The proceeds of the Notes were pooled together and used to fund real estate secured loans. Investors
19 relied on Respondents’ expertise to establish and service the Collateral Mortgage Pool and to conduct the
20 business operations. The Collateral Mortgage Pool was the only security provided for the Notes.

1 Notes without fully disclosing PMC's financial condition, including its liquidity problems and high loan
2 default rate.

3 PMC's Financial Condition

4 10. Starting in at least September 2001 Respondents were experiencing liquidity problems and a
5 high loan default rate. At that time the value of the Notes outstanding was \$5.7 million more than the value
6 of the loans in the Collateral Mortgage Pool and significant loan write-offs had to be made for problem
7 loans in the Collateral Mortgage Pool. However, in October 2001, Respondents sent a letter to investors
8 ("October 2001 Letter") stating that the "problem loans" were not unreasonable as a percentage.
9 Respondents failed to disclose the dollar amount of the problem loans to investors, the liquidity problems,
10 the loan default rate, or the risk of purchasing or rolling over the Notes.

11 11. In January 2002, Respondents were still experiencing liquidity problems and a high default
12 rate. PMC had an operating deficiency of \$1.7 million and of the \$62 million in loans outstanding in the
13 Collateral Mortgage Pool, approximately 45% were in default and another 14% were delinquent. At this
14 time, Respondents routinely allowed delinquent loans to be carried until the principal and interest due
15 exceeded the value of the property before foreclosing on the property. Respondents failed to disclose to
16 new investors and to investors rolling over Notes the liquidity problems, the loan default rate, the
17 foreclosure policy, or the risk of purchasing or rolling over the Notes.

18 12. In May 2002, Respondents were unable to obtain outside financing from BayView Financial
19 Trading Group ("BayView"), an investment bank located in Florida. BayView was unwilling to provide
20 financing because of Respondents' failure to provide valid loan documentation, as many of the loans were
21 past their maturity and the loan documents had not been modified, and because Respondents failed to
22 provide adequate appraisals for the underlying real estate. Respondents failed to disclose to new investors

1 and to investors rolling over Notes that they were seeking outside funding and that their inability to provide
2 valid loan documentation and adequate appraisals resulted in Respondents being unable to obtain financing.

3 13. In August 2002, Respondents sent a letter encouraging the investors to move funds from
4 “Wall Street” to PMC. The letter stated that the outstanding loans were secured by local real estate worth
5 130% of the value of the outstanding loans. Respondents failed to disclose to new investors and to investors
6 rolling over Notes that they did not have adequate appraisals to substantiate the value of the real estate that
7 ostensibly secured the PMC loans and the risks of purchasing or rolling over Notes.

8 14. In October 2002, Respondents sent a management report (“October 2002 Management
9 Report”) to investors. The report said that Craig could show them how to invest their individual retirement
10 accounts in PMC. The October 2002 Management Report stated that the Collateral Mortgage Pool was in
11 good financial condition and that the \$140 million of real estate in the Collateral Mortgage Pool more than
12 secured the \$83 million that had been loaned out. Respondents failed to disclose to new investors and to
13 investors rolling over Notes that they did not have adequate appraisals to substantiate the value of the real
14 estate that ostensibly secured the PMC loans. The October 2002 Management Report further stated that
15 typically about 10% of the loans go into foreclosure and that most of them are cured within the 6 month
16 foreclosure process. Respondents failed to disclose to new investors and to investors rolling over Notes
17 PMC’s actual loan default rate, their policy of not foreclosing on delinquent loans until the outstanding
18 principal and interest due exceed the value of the property, and the risk of purchasing or rolling over the
19 Notes.

20 15. By February 2003 Respondents were still experiencing a high default rate as there were \$3.9
21 million of loans in foreclosure, \$14.7 million of loans that had been foreclosed, and \$9.9 million of other
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1 problem loans, for a total of at least \$28.5 million in problem loans. Respondents failed to disclose this to
2 new investors and to investors rolling over Notes and the risks of purchasing or rolling over the Notes.

3 16. To address its financial problems, in June 2003, Respondents hired a Chief Executive
4 Officer, Ray Bell (“Bell”). Bell was supposed to analyze PMC’s troubled financial condition and the status
5 of the Collateral Mortgage Pool, to prepare a set of recommendations for PMC, and to provide a report to
6 the investors. Respondents failed to disclose PMC’s troubled financial condition to new investors and to
7 investors rolling over Notes and instead sent a July 2003 letter with the heading “HERE’S AN IDEA TO
8 INCREASE YOUR INCOME.” The letter suggested that investors take advantage of the spread between
9 the current low mortgage rates and the current high interest rate on PMC Notes by refinancing their homes
10 and using their home equity to buy Notes. Investors would supposedly benefit because their mortgage
11 interest rate would be lower than the interest rate they would earn from the Notes. Respondents failed to
12 disclose new investors and to investors rolling over Notes the risks of purchasing or rolling over Notes,
13 including the risk of PMC’s insolvency.

14 17. In September 2003, Respondents sent a letter to investors stating that PMC was no longer
15 able to pay its debts as they came due and that PMC was not making any further redemption of Notes,
16 would not be paying interest on Notes, and would not make any new loans.

17 18. On September 26, 2003, PMC filed for Chapter 11 bankruptcy. At that time, of the \$74
18 million of loans outstanding in the Collateral Mortgage Pool, approximately one-third, or \$23 million, had
19 been foreclosed. Loans that were delinquent but had not yet been foreclosed made up another \$29 million.
20 In total, more than \$52 million, or approximately 70%, of the loans in the Collateral Mortgage Pool were
21 delinquent. The value of the assets underlying the loans was estimated to be approximately \$54 million,
22 after deducting the interests that had been subordinated to third parties.

Subordination or Sale of Security Interests

19. The PPM states that the borrower notes and deeds of trust will be held for the investors in the Collateral Mortgage Pool subject to the Trust and Security Agreement. However, from 1999 through 2003, Respondents engaged in acts that were in violation of the Trust and Security Agreement.

20. First, from as early as 1999 and continuing through July 2003, Respondents subordinated the security interests in the Collateral Mortgage Pool when it sold and/or assigned loans to a third party in violation of the Trust and Security Agreement. PMC sold and/or assigned approximately \$14 million of loans in exchange for \$10 million. The loans assigned were generally of higher quality than the remaining loans in the Collateral Mortgage Pool.

21. Second, in February 2003, in order to secure a line of credit, PMC and Craig subordinated the security interest in the Collateral Mortgage Pool by giving a bank first lien priority against \$2.2 million of loans in exchange for a \$1.3 million line of credit in violation of the Trust and Security Agreement. The loans assigned were generally of higher quality than the remaining loans in the Collateral Mortgage Pool.

22. Lastly, in June 2003, just three months prior to filing for bankruptcy, Respondents entered into a transaction with an investor wherein the investor exchanged Notes valued at \$12.8 million for an undivided 75% interest in specific mortgage loans valued at \$17 million in violation of the Trust and Security Agreement. The loans assigned were generally of higher quality than the remaining loans in the Collateral Mortgage Pool.

23. From 1999 to 2003, Respondents failed to disclose to new investors and to investors rolling over Notes, PMC's liquidity problems, the sale and subordination of \$33.2 million of the security interests in the Collateral Mortgage Pool, the violations of the Trust and Security Agreement, and the resulting risks.

1 Based upon the above Tentative Findings of Fact, the following Conclusions of Law are made:

2 **CONCLUSIONS OF LAW**

3 1. The offer or sale of the promissory notes and the pooling of investor funds to finance the
4 business operations of Partners Mortgage Corporation, as described above, constitutes the offer or sale of a
5 security as defined in RCW 21.20.005 (10) and (12).

6 2. Respondents, Partners Mortgage Corporation and Gary Lynn Craig, as described above in
7 paragraphs 10, 11, 12, 13, 14, 15, 16, 20, 21, 22, and 23, in connection with the offer and sale of securities
8 in the form of new Notes and in rolling over existing Notes between January 1, 2003 and September 26,
9 2003, each made untrue statements of material fact or omitted to state material facts necessary in order to
10 make the statements made, in light of the circumstances under which they were made, not misleading, in
11 violation of RCW 21.20.010. Each violation of RCW 21.20.010 is independent grounds for the denial of
12 Craig's securities broker-dealer and salesperson registration pursuant to RCW 21.20.110(1)(b).

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14 **NOTICE OF INTENT TO ORDER RESPONDENT TO CEASE AND DESIST**

15 Pursuant to RCW 21.20.390, and based upon the above Tentative Findings of Fact and Conclusions
16 of Law, the Securities Administrator intends to order that Respondents Partners Mortgage Corporation and
17 Gary Lynn Craig shall each permanently cease and desist from violations of RCW 21.20.010.

1 **NOTICE OF INTENT TO IMPOSE FINES**

2 Pursuant to RCW 21.20.110(4) and RCW 21.20.395(1), and based upon the above Tentative
3 Findings of Fact and Conclusions of Law, the Securities Administrator intends to order that Respondent,
4 Gary Lynn Craig, shall be liable for and shall pay a fine of \$100,000.

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6 **NOTICE OF INTENT TO BAR SECURITIES BROKER-DEALER, SECURITIES**
7 **SALESPERSON, INVESTMENT ADVISER, AND INVESTMENT ADVISER**
8 **REPRESENTATIVE REGISTRATION**

9 Pursuant to RCW 21.20.110(1), and based upon the above Tentative Findings of Fact and
10 Conclusions of Law, the Securities Administrator intends to bar Respondent, Gary Lynn Craig, from
11 registering as a securities broker-dealer, securities salesperson, investment adviser, and investment adviser
12 representative. Any such applications in the State of Washington will be denied registration.

13
14 **AUTHORITY AND PROCEDURE**

15 This Statement of Charges is entered pursuant to the provisions of RCW 21.20.110, RCW
16 21.20.390, and RCW 21.20.395 and is subject to the provisions of RCW 21.20.120, RCW 21.20.440 and
17 Chapter 34.05 RCW. Respondents may each make a written request for a hearing as set forth in the
18 NOTICE OF OPPORTUNITY TO DEFEND AND OPPORTUNITY FOR HEARING accompanying this
19 Order. If a Respondent does not request a hearing, the Securities Administrator intends to adopt the
20 foregoing Tentative Findings of Fact and Conclusions of Law as final; and to enter a permanent cease and
21 desist order against that Respondent; to bar the Respondent from registering as a securities broker-dealer

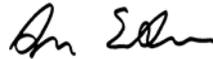
1 and salesperson, investment adviser, and investment adviser representative; and to impose the payment of a
2 fine.

3 DATED and ENTERED this 13th day of June, 2007.

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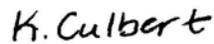
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7 MICHAEL E. STEVENSON
8 Securities Administrator

9 Approved by:

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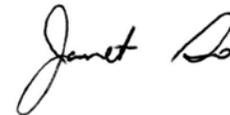
11 _____
12 Suzanne Sarason
13 Chief of Compliance

14 Presented by:

15 

16 _____
17 Kristen Culbert
18 Financial Legal Examiner

19 Presented by:

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21 _____
22 Janet So
23 Financial Legal Examiner