IN THE MARION SUPERIOR/CIRCUIT COURT
STATE OF INDIANA

STATE OF INDIANA, *ex. rel.*, CHRIS NAYLOR, INDIANA SECURITIES COMMISSIONER, Plaintiff, v. INDIANA STATE TEACHERS ASSOCIATION, ISTA INSURANCE TRUST, ISTA FINANCIAL SERVICES CORPORATION, ISTA WELFARE BENEFITS TRUST, ISTA ADMINISTRATIVE SERVICES CORPORATION, and NATIONAL EDUCATION ASSOCIATION, Defendants.	)	CAUSE NO. 49D14 09 12 CT 054676

FILED
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Elizabeth A. White
CLERK OF THE MARION CIRCUIT COURT

VERIFIED COMPLAINT FOR APPOINTMENT OF RECEIVER/CONSERVATOR, ASSET FREEZE, ACCOUNTING, AND PRELIMINARY AND PERMANENT INJUNCTIONS

Plaintiff State of Indiana, ex rel. Chris Naylor, Indiana Securities Commissioner ("Commissioner"), by its undersigned counsel, pursuant to Indiana Code § 23-19-6-3(b)(1), 23-19-6-3(b)(2)(A), and 23-19-6-3(2)(B), hereby seeks an order from this Court freezing any and all assets under the ownership, direction, custody or control of Defendants Indiana State Teachers Association ("ISTA"), ISTA Financial Services Corporation, ISTA Insurance Trust, ISTA Welfare Benefits Trust and ISTA Administrative Services Corporation (collectively referred to as the "ISTA Entities") until all assets have been properly accounted. The Commissioner specifically seeks to prohibit the ISTA Entities from distributing any funds to school districts until an independent accounting can be accomplished to confirm an equitable distribution as among the various districts. However, the Commissioner requests that the asset freeze not apply

to funds necessary to continue payment of long-term disability claims to disabled teachers. In addition, the Commissioner moves for appointment of a receiver/conservator to search out, recover, and account for all of the Defendants' assets derived from investor funds, including, but not limited to, all funds previously or currently described, characterized, or accounted for by one or more of the ISTA entities as "claims stabilization reserves" ("CSR"), "rate stabilization reserves," or the equivalent, or any assets otherwise subject to the continuing jurisdiction, direction and supervision of this court, including all ISTA real property and personal property. The accounting and receivership/conservatorship are further necessary to ensure that, to the extent possible, funds are available to continue paying for the ongoing processing and payment of long-term disability benefits without interruption and to ensure a prompt and equitable distribution of CSR funds or the equivalent to the appropriate entities. The Commissioner also seeks preliminary and permanent injunctive relief, restraining and enjoining the Defendants and persons acting in concert with them from divesting proceeds that resulted from the offer and sale of securities in violation of the Indiana Uniform Securities Act (the "Act"), Ind. Code § 29-19-1 et seq.

In support of this Complaint, the Commissioner states the following:

I. Nature of the Case

1. The Commissioner believes that Defendants have engaged in multiple acts, practices or courses of business in violation of the following provisions of the Act or its predecessor, Ind. Code § 23-2-1 et seq. (repealed 2007) (Citations to the prior version of the Act are in parentheses following the current code citations):

a. The Defendants did offer or sell securities to Indiana school districts in the form of commingled long-term disability ("LTD") and health arrangements with a

promise of a return on funds used to purchase the health arrangements, in exchange for United States currency, without registering said securities under the Act. Said securities were neither exempt from registration under Ind. Code § 23-19-2-1 through § 23-19-2-3 (§ 23-2-1-2), nor were said securities federally covered securities as defined in Ind. Code § 23-19-1-2(7) (§ 23-2-1-6.1).

b. Defendants knowingly transacted business as investment advisers as defined in Ind. Code § 23-19-1-2(15) (§ 23-2-1-1(n)) in their offer of these arrangements and received compensation without being registered with the Indiana Securities Division, as required by law, and without being exempt from registration. Ind. Code § 23-19-4-3 (§ 23-21-8 (c)).

c. Defendants knowingly acted as investment adviser representatives as defined in Ind. Code § 23-19-1-2(16) (§ 23-2-1-1(q)(E)) by supervising persons acting as investment advisers without being registered with the Indiana Securities Division, as required by law, and without being exempt from registration.

d. Defendants, in connection with the offer, sale or purchase of a security, directly or indirectly employed a device, scheme or artifice to defraud, made an untrue statement of material fact, or omitted to state a material fact necessary in order to made the statement made, in the light of the circumstances under which they were make, not misleading, or engaged in an act, practice or course of business that operates or would operate as a fraud or deceit upon another person in violation of Ind. Code § 23-19-5-1 (§ 23-2-1-12). Defendants made untrue statements of material fact regarding the financial condition of the health arrangement and the risks associated with the investment

strategy and failed to disclose the commingling of LTD and health arrangement funds; the inadequacy of the reserves backing the arrangements; the unsuitability of the investments purchased with arrangement funds; information showing the accurate financial condition of the arrangements; and the risks rendering a return on the investments as highly unlikely.

2. Defendants have engaged in acts, practices or courses of business constituting violations of the Act. These violations give rise to the Commissioner's authority to request the court to order an accounting and appoint a receiver who can take charge and control of property to equitably dispose as necessary. Under Indiana law, the Court may enjoin such conduct, order an asset freeze, an accounting and appoint a receiver/conservator to take charge and control of Defendants' property and provide a general accounting to determine the extent of the misuse and commingling of investor funds.

II. Parties

3. Plaintiff Chris Naylor is the duly appointed Indiana Securities Commissioner of the State of Indiana. The Commissioner directs the Securities Division of the Indiana Secretary of State's Office and is charged with the responsibility of administering and enforcing the Act. The Act specifically empowers the Commissioner to conduct investigations to determine whether a person has violated or is about to violate the Act, issue appropriate orders, bring an action in the name and on behalf of the State of Indiana against the person or persons violating the Act, and in addition to all other remedies, obtain injunctive relief and the appointment of a receiver or conservator

4. Defendant Indiana State Teachers Association ("ISTA") is an Indiana non-profit corporation with its headquarters and principal place of business in Indianapolis, Marion County, Indiana.

5. Defendant ISTA Insurance Trust ("IIT") is a subsidiary of ISTA with its principal place of business in Indianapolis, Marion County, Indiana.

6. Defendant ISTA Financial Services Corporation ("ISTA Financial") is a subsidiary of ISTA with its principal place of business in Indianapolis, Marion County, Indiana.

7. Defendant ISTA Welfare Benefits Trust is a subsidiary of ISTA with its principal place of business in Indianapolis, Marion County, Indiana.

8. Defendant ISTA Administrative Services Corporation is a subsidiary of ISTA with its principal place of business in Indianapolis, Marion County, Indiana.

9. The ISTA Entities shared directors, employees, officers, offices, and funds to such an overlapping and interlocking extent that it is difficult or impossible to determine what actions were being taken by and on behalf of which ISTA entity.

10. Defendant National Education Association ("NEA") is a national professional employee organization or labor union representing public school teachers, support personnel, and others, with its principal place of business in Washington, D.C.

11. NEA took over day-to-day operation of ISTA by installing Edward Sullivan as the acting chief executive officer of ISTA and sole trustee of the ISTA Trust on or about May 20, 2009. NEA is named as a defendant because of its operational control of the ISTA Entities and their assets since approximately May 20, 2009.

III. Venue

12. Venue is proper in Marion County because.

a. The ISTA Entities' business operations are located in Marion County;

b. Defendants violated the Act in Marion County;

c. The Commissioner's investigation or inquiry is being conducted in Marion County; and/or

d. The Act provides that venue is proper in the county where the Commissioner's investigation or inquiry is being conducted. Ind. Code § 23-19-6-3(a).

IV. Background

13. In 1985, ISTA established the IIT for the purpose of providing certain insurance products and LTD and health arrangements to ISTA members, who are teachers and school employees throughout Indiana.

14. IIT products and arrangements were marketed and administered by ISTA Financial and ISTA Administrative Services Corporation.

15. The IIT health arrangement, offered to school districts as an alternative to a regulated insurance company providing medical benefits, included a component primarily known as claims stabilization reserve, but also called "rate stabilization reserve," or "collaborative surplus reserve," hereinafter referred to as "CSR" or the "CSR Program."

16. The ISTA Entities, through their field representatives, in anticipation of the collective bargaining processes between school districts and their employees, represented to school districts that if they participated in the CSR Program, they would be credited with a CSR

balance if the total amount of payments by the school district to ISTA exceeded the amount of claims paid, plus administrative expenses and other overhead amounts assessed by ISTA.

17. The ISTA Entities further represented to school districts that they would receive a return on their CSR balances, calculated as a return on investment by ISTA and based, in part, on the returns earned by ISTA and the IIT on their investments. In certain cases, guaranteed rates of return were promised by the ISTA field representatives. The ISTA Entities further represented that the return on investment would be based in part on the investment returns earned by the IIT.

18. By operation of the CSR, the health arrangement offered and sold by the ISTA Entities was an investment product that was unregistered and non-exempt under the Act.

19. The ISTA Entities failed to disclose material facts with regard to the offering of the health arrangement, including the facts that it constituted an unregistered security, that the ISTA Entities were acting as investment advisers without having the requisite Indiana registration, that the health arrangement and long-term disability premium funds paid by the participants and reserves for the health arrangement and long-term disability plans would be commingled, and that some of the premium dollars would be placed by the ISTA Entities in speculative, illiquid investments, unsuitable for the objectives of the participants. The ISTA Entities further failed to disclose adverse information provided to the ISTA Entities by accountants, actuaries and consultants regarding the financial health and stability of the health arrangement and LTD plans

20. The ISTA Entities further made untrue statements of material fact regarding the health arrangement by representing that it was financially sound at a time when it was not, and by representing that CSR balances were properly accounted for and available for use by the individual school districts.

21. The ISTA Entities omitted to state material facts and made untrue statements of material fact to each of the twenty-six school districts participating in the CSR during the offer and reporting of the program.

22. Because of the unsuitable investments made by the ISTA Entities and the failures to establish appropriate reserves and actuarial models for the health arrangement and LTD plans, ISTA and the ISTA Trust sustained substantial losses and the ISTA Trust did not have sufficient funds to meet its obligations with regard to the health arrangement and LTD plans. Plaintiff is informed and believes that the unfunded LTD obligation has a present value of approximately fifty-six million dollars ($56,000,000).

23. The ISTA Entities are unable to account properly for the CSR funds which were to have been accumulated for the benefit of the participating school districts. Plaintiff is informed and believes that the ISTA Entities are responsible for the loss of approximately twenty-three million dollars ($23,000,000) in CSR funds.

24. As a result of ISTA's financial situation, it and the ISTA Entities have been taken over by the NEA, ISTA's sanctioning or parent organization and, NEA is controlling the operations, administration, and assets of the ISTA Entities.

V. Violations

Count One

25. This section incorporates by reference all preceding sections and paragraphs.

26. It is unlawful for any person to offer or sell any security in Indiana unless it is registered with the Indiana Securities Division. Ind. Code § 23-19-3-1(3) (§ 23-2-1-3(1)).

27. Because the ISTA Entities offered the CSR program as part of the health arrangement and because they represented to purchasers and offerees that participation in the CSR program would result in their sharing in investment returns earned by the ISTA Entities, the health arrangement offered and sold by the ISTA Entities was a security as defined by Ind. Code § 23-19-1-2(28) (§ 23-2-1-1(k)).

28. The security sold by the ISTA Entities was not registered with the Indiana Securities Division as required by the Act. Ind. Code § 23-19-3-1(3) (§ 23-2-1-3(1)).

Count Two

29. This section incorporates by reference all preceding sections and paragraphs.

30. It is unlawful for an individual, corporation or trust to transact business in this state as an investment adviser representative unless the individual, corporation or trust is registered under the Act as such. Ind. Code § 23-19-4-4(a) (§ 23-2-1-8(c)).

31. By receiving compensation for advising others as to the value and/or advisability of investing in or purchasing securities, Defendants ISTA and ISTA Financial acted as investment adviser representatives without being registered under the Act.

Count Three

32. This section incorporates by reference all preceding sections and paragraphs.

33. Defendants ISTA Entities received commissions and other compensation for the investment advice given by the ISTA Financial Services field representatives.

34. Defendants knowingly supervised persons acting as investment advisers and investment adviser representatives without being registered with the Indiana Securities Division, as required by law, and without being exempt from registration. Ind. Code § 23-19-1-2(16) (§ 23-2-1-1(q)(3)(E)).

Count Four

35. This section incorporates by reference all preceding sections and paragraphs.

36. Pursuant to Ind. Code § 23-19-5-1 (§ 23-2-1-12), "[i]t is unlawful for a person, in connection with the offer, sale or purchase of a security, directly or indirectly: (1) to employ a device, scheme or artifice to defraud; (2) to make an untrue statement of material fact, or to omit to state a material fact necessary in order to made the statement made, in the light of the circumstances under which they were made, not misleading...."

37. The ISTA Entities, in connection with the offer or sale of securities, made untrue statements of material fact, or omitted to state a material fact necessary in order to make the statement made, in the light of the circumstances under which it was made, not misleading. Specifically, the ISTA Entities omitted to state that the health arrangement was not registered, omitted to state that LTD and health arrangement funds would be commingled, and omitted to state that the reserves backing the arrangements were inadequate. Furthermore, the ISTA Entities made untrue statements of material fact. Specifically, they made untrue statements regarding the potential for return on investments, when in fact the risks associated with the

investments rendered the possibility of a return as highly unlikely, based on information communicated to the ISTA Entities from accountants, actuaries and consultants showing the material weaknesses of the LTD and health arrangements. The ISTA Entities further failed to provide offerees or purchasers a prospectus for the security

38. The ISTA Entities further failed to inform purchasers and offerees that their funds would be invested in a highly speculative, illiquid manner unsuitable for the purchasers and offerees.

39. The ISTA Entities made untrue statements to purchasers and offerees, specifically stating that the health arrangement was financially sound at a time when it was not.

VI. Relief Requested

40. Pursuant to Ind. Code § 23-19-6-3 (§ 23-2-1-17(a)), upon a proper showing by the Commissioner, the Court may order all such relief that it considers appropriate, including all necessary permanent or temporary injunctions, restraining orders, declaratory judgments and other appropriate forms of relief, namely an asset freeze, accounting and the appointment of a receiver/conservator.

41. Preliminary and permanent injunctive relief is appropriate because such relief is specifically authorized by Ind. Code § 23-19-6-3 for the violations committed by the ISTA Entities.

42. The Commissioner and those he is required to protect will be irreparably harmed if injunctive relief is not granted in the form requested in this Verified Complaint. The Commissioner has no adequate remedy at law, it is in the public interest to grant the requested

injunctive relief, and the benefit to Plaintiff and the public outweighs the harm to Defendants if injunctive relief is granted.

43. The Commissioner requests that this Court enter an Order appointing a receiver/conservator of all assets, including all financial accounts of the ISTA Entities, held by or under control of the ISTA Entities and NEA, including, but not limited to, proceeds of business activities, business premises, books, records, and real and personal property and order that an accounting be made.

44. The Commissioner requests that this Court enter an Order freezing any and all assets, including all financial accounts of the ISTA Entities, under the ownership, direction, custody or control of the ISTA Entities and NEA until the investor proceeds have been accounted for, subject to the continuing jurisdiction, direction and supervision of this Court; provided, however, that the asset freeze not prevent the payment of long-term disability claims to disabled teachers entitled to payment under the LTD plan.

45. The Commissioner requests that this Court enter an Order for disgorgement, restitution, rescission, and other equitable relief against the Defendants in such amounts as may be determined upon presentation and proof and upon receipt of the accountings requested in Paragraph 43, supra.

46. The Commissioner requests that this Court enter preliminary and permanent injunctions, restraining and enjoining the Defendants and persons acting in concert with them from diverting proceeds that resulted from the offer and sale of securities in violation of the Act.

WHEREFORE, the Commissioner respectfully requests that this Court grant the relief requested in Paragraphs 39-42, and all other proper relief consistent with Ind. Code § 23-19-6-3 (§ 23-2-1-17.1(a)).

FROST BROWN TODD LLC

By: _____
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Attorneys for Plaintiff
State of Indiana, *ex. rel.*, Chris Naylor,
Indiana Securities Commissioner

I AFFIRM UNDER PENALTIES OF PERJURY THAT BASED UPON AN INVESTIGATION CONDUCTED BY THE INDIANA SECRETARY OF STATE, SECURITIES DIVISION, THE FOREGOING REPRESENTATIONS ARE TRUE TO THE BEST OF MY KNOWLEDGE AND BELIEF.

INDIANA SECRETARY OF STATE,
SECURITIES DIVISION

By: _____
CHRIS NAYLOR
Indiana Securities Commissioner

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