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: Gregory Pinneo; East Edgar Partners, LLC; Franklin Avenue Partners, LLC; Yale Avenue Partners, LLC; 2344-2345 Franklin Twins, LLC, Respondents	Order Number S-10-047-10-SC01 STATEMENT OF CHARGES AND NOTICE OF INTENT TO ENTER ORDER TO CEASE AND DESIST, IMPOSE FINES, AND RECOVER COSTS

THE STATE OF WASHINGTON TO:

Gregory Pinneo
East Edgar Partners, LLC
Franklin Avenue Partners, LLC
Yale Avenue Partners, LLC
2344-2345 Franklin Twins, LLC

STATEMENT OF CHARGES

Please take notice that the Securities Administrator of the State of Washington has reason to believe that Respondents Gregory Pinneo; East Edgar Partners, LLC; Franklin Avenue Partners, LLC; Yale Avenue Partners, LLC; and 2344-2345 Franklin Twins, LLC have each violated the Securities Act of Washington and that their violations justify the entry of an order of the Securities Administrator under RCW 21.20.390 against each to cease and desist from such violations. The Securities Administrator finds as follows:

TENTATIVE FINDINGS OF FACT

<u>Respondents</u>

1. Gregory Pinneo ("Pinneo") is a Washington resident. Pinneo acted as managing member of East Edgar Partners, LLC; Franklin Avenue Partners, LLC; Yale Avenue Partners, LLC; and 2344-2345 Franklin Twins, LLC. In 1997, Pinneo pleaded guilty to one count of conspiracy to commit bank fraud and spent six months in prison. His real estate license was revoked as part of the plea agreement.

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2. East Edgar Partners, LLC ("East Edgar Partners") is a Washington limited liability company formed on February 8, 2006. East Edgar Partners owns a 12-unit apartment building located in Seattle, Washington.

3. Franklin Avenue Partners, LLC ("Franklin Avenue Partners") is a Washington limited liability company formed on July 7, 2006. Franklin Avenue Partners owns a 6-unit apartment building located in Seattle, Washington.

4. Yale Avenue Partners, LLC ("Yale Avenue Partners") is an inactive Washington limited liability company formed on March 26, 2007. Yale Avenue Partners owned a 6-unit apartment building located in Seattle, Washington.

5. 2344-2345 Franklin Twins, LLC ("Franklin Twins") is a Washington limited liability company formed on April 24, 2008. Franklin Twins owns two apartment buildings: a 3-unit building and a 6-unit building located in Seattle, Washington.

Related Entity

6. Reach Returns, Inc. ("Reach Returns") is a Washington state corporation formed on May 8, 2003. Its principal place of business is in Everett, Washington. Reach Returns is in the business of conducting real estate and motivational seminars, including a multiple-day paid seminar program called "Power Player Intensive" that covers topics such as negotiation skills, real estate finance techniques, and property management. Individuals who complete this program are referred to as "Power Players." Pinneo is the owner of Reach Returns.

Nature of the Conduct

Background

7. From approximately December 2005 through October 2008, Pinneo raised approximately $4.5 million through the offer and sale of interests in East Edgar Partners, Franklin Avenue Partners, Yale Avenue Partners, and Franklin Twins to approximately 76 investors, the majority of whom were Washington residents. Each limited liability company ("LLC") owned one apartment building located in

Seattle, Washington, except for Franklin Twins, which owned two apartment buildings. All apartment buildings, except for one, were initially owned by Pinneo. Pinneo transferred his interest in the property to each LLC via quitclaim deed.

8. According to Pinneo, he began selling LLC interests because he wanted to sell some equity in the property he owned while remaining a part of the overall project. He was in the process of building a home and decided to sell a portion of his interests in the LLCs to fund the building of his new home. Pinneo did not disclose to all investors that they were purchasing his interests and their funds would be going to him. A few investors thought their funds would be used to pay down the mortgage on the building. According to Pinneo, investor funds were deposited into each LLC's bank account and then withdrawn as a distribution to the individual selling the shares.

9. Investors received a percentage ownership in an LLC that was proportional to the amount of their investment. The great majority of investors did not actively participate in the management of the apartment complexes. The apartment complexes were to be managed by Pinneo or other third party for a fee of 7% of incoming rents. The investors relied upon Pinneo and other third parties to generate a return on their investment.

10. Pinneo typically solicited friends and Power Players to invest in his various LLCs. Several investors who had met Pinneo through Reach Returns and completed the Power Players program indicated that they trusted Pinneo and considered him a mentor. Not all investors were accredited or experienced in making real estate investments. Pinneo did not screen investors for net worth, income, or investment experience. He usually arranged one-on-one meetings with prospective investors, during which he would go over a binder of information concerning the investment opportunity.

East Edgar Partners, LLC Offering

11. From approximately December 2005 through March 2008, Pinneo raised approximately $2.3 million from approximately 32 investors through the offer and sale of interests in East Edgar Partners. At least 11 investors purchased interests in East Edgar Partners prior to its formation on February 8, 2006.

The offering materials provided to these investors failed to disclose the fact that the entity had not yet been formed, or about Pinneo's intentions to form the entity.

12. Investors who purchased their interests in 2006 paid $27,404 for a 1% interest in East Edgar Partners. The price was increased to $30,239 per 1% interest in 2007. Investors typically received a binder of documents prior to investing, which included a document entitled "Partnership Opportunity 100 East Edgar," a partnership agreement, tenant list, and insurance documents.

13. The offering materials described the building as having "a strong equity position." A page entitled "Current Financials" illustrated how Pinneo calculated the value of the building. The scheduled annual rent for the building was calculated to be $207,960. Pinneo used an expense ratio of 25% of the scheduled annual rent to arrive at a net operating income of $155,970. He then used an income approach to value and a capitalization rate of 3.13% to calculate the current value of the building to be approximately $4,975,000. The expense ratio Pinneo used was an estimate. He did not look back at previous financial statements to view what the actual expenses were. The offering materials failed to disclose that the expense ratio or net operating income were projections or estimates. The offering materials further failed to disclose that for valued year 2005, the King County Department of Assessments assessed the taxable total value of the property to be $1,602,000. Pinneo failed to explain why the value he calculated was so much greater than the tax assessed value. He did not provide any reasonable basis for his purported value.

14. According to the offering materials, there was $2,235,000 worth of debt on the property. Pinneo subtracted that debt from the value he calculated for the building to arrive at $2,740,500 as the equity available in the building.

15. The offering materials represented that the management's plan was to hold the building long-term. The plan was to update the building in a few years and increase rents, make additional principal payments, and pay monthly dividends to investors once the building was owned free and clear. The offering materials also contained two different expansion ideas Pinneo had for the building, Phase I and

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Phase II. Phase I was a plan that involved converting the apartments into corporate housing. The offering materials projected that the gross annual income for the first year would be $660,600, with a net annual positive cash flow of $200,000. The materials further projected that if the additional positive cash flow was used to make additional principal payments, the debt on the property would be paid off in less than ten years, and nearly $500,000 would be available for distribution to the investors each year based on a percentage ownership basis, "assuming increases in revenues offset rising operation costs, taxes, and insurance." Phase II involved the construction and rental of houseboats. The offering materials projected that if the 8 units were rented out 4 nights per week at $150 per night, it would generate income of $19,200 per month, with a net monthly income of $11,000. The offering materials failed to disclose whether any permits would be required for the construction and rental of houseboats, or for the conversion of apartment units into corporate housing. Pinneo testified that he did not know if permits were required, and he was not sure if the area was zoned for the changes. The offering materials projected that $765,000 would be required to complete Phase I, but failed to disclose how the LLC would obtain additional funds.

16. At least one investor did not have the funds to immediately invest in East Edgar Partners. The investor borrowed $27,404 from Pinneo to purchase a 1% interest. The investor was to pay 3% interest on the borrowed funds. Another investor took out money from a credit line on his home in order to invest.

17. Data from the East Edgar Partners' income and expense sheet showed that, from January 2006 through October 2006, the building experienced negative cash flow in eight out of the ten months:

	Total Income (Rental & laundry income, security & pet deposit)	Expenses (Includes maintenance, mortgage payments, & property taxes)	Net Income
January 2006	$ 16,156.84	$ 19,879.29	$ (3,722.45)
February 2006	$ 15,110.34	$ 20,902.76	$ (5,792.42)
March 2006	$ 19,065.05	$ 19,026.41	$ 38.64
April 2006	$ 14,559.50	$ 28,498.71	$ (13,939.21)
May 2006	$ 16,448.55	$ 21,002.09	$ (4,553.54)
June 2006	$ 16,747.50	$ 20,309.09	$ (3,561.59)
July 2006	$ 16,134.50	$ 19,966.43	$ (3,831.93)

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August 2006	$ 15,371.00	$ 20,837.06	$ (5,466.06)
September 2006	$ 18,491.35	$ 18,202.59	$ 288.76
October 2006	$ 14,534.07	$ 31,661.32	$ (17,127.25)

18. In a letter dated March 10, 2006, East Edgar Partners informed investors that half yearly property taxes were due in April, and there was not enough money in the account to cover the full bill of approximately $8,000. Investors were requested to send in their share of the $8,000 by April 15. Another letter dated May 10, 2006 represented that investors would have to cover any monthly shortfalls because the reserve money had been used up. The letter anticipated shortfalls of approximately $4,500 in May, $3,000 in June, and $2,500 in July. In an email dated November 24, 2006, East Edgar anticipated that investors would need to continue to fund the building through the first and second quarter of 2007.

19. Pinneo testified that investors have been required to make capital contributions, and there were months when East Edgar was dependent upon additional capital contributions from investors to stay current on its expenses. Pinneo failed to provide prospective investors with financial statements for the apartment building. He also failed to disclose to at least some individuals that the building was experiencing negative cash flow and capital contributions were being required.

20. As of December 2010, no dividends or profits had been paid to any investors.

Franklin Avenue Partners, LLC Offering

21. From approximately July 2006 through November 2006, Pinneo raised approximately $900,000 from approximately 17 investors through the offer and sale of interests in Franklin Avenue Partners. Investors typically received several documents prior to investing, including “2338 Franklin Avenue East, Seattle, WA Partnership Opportunity,” “Highlights of the 2338 Franklin Avenue East Model and Expandability,” “Average Monthly Income/Expense,” “Average Annual Income/Expense,” a rent roll list, a partnership agreement, information concerning existing financing on the building, and insurance information. Investors who invested through a self-directed IRA were also required to a sign a subscription agreement. The “Average Monthly Income/Expense” document represented that the building

generated a monthly net income of $211. An investor could purchase a 5% interest for $50,000. $868.70 of the investor's funds was to go towards a cash reserve account.

22. The offering documents represented that the building was currently valued at $1,650,000, and there was $667,374 worth of debt on the property. Pinneo arrived at that value by looking at similar buildings in the area, their value, and the capitalization rate the buildings were selling at. The offering materials failed to provide any reasonable basis for Pinneo's purported value. The offering materials further failed to disclose that for valued year 2006, the King County Department of Assessments assessed the taxable total value of the property to be $947,000. Pinneo failed to explain why the value he calculated was so much greater than the tax assessed value.

23. According to the document entitled "Highlights of the 2338 Franklin Avenue East Model and Expandability," the current value of the building, if converted into condominium units at $375 to $400 per square foot, was approximately $2,069,687 to $2,215,000. The document further went on that the LLC remained open to the condominium conversion possibility and would consider selling the units as condominiums when they could be sold for $500 per square foot, which would result in a net conversion value of approximately $2,796,250. The offering materials failed to provide a reasonable basis for such projections. The offering materials further failed to disclose whether any permits would be required, or how the LLC would obtain financing necessary for such a conversion.

24. As of December 2010, no dividends or profits had been paid to any investors.

Yale Avenue Partners, LLC Offering

25. From approximately April 2007 through June 2007, Pinneo raised approximately $630,000 from approximately 13 investors through the offer and sale of interests in Yale Avenue Partners. Investors typically received several documents prior to investing, including "2311 Yale Avenue East, Seattle, WA Membership Opportunity," "Highlights of the 2311 Yale Avenue East Model and Expandability," "Average Monthly Income/Expense," a rent roll list, information concerning current financing on the building, insurance information, and LLC agreement. Investors who invested through a self-directed IRA

were also required to a sign a subscription agreement. The offering materials showed the building to be operating at a monthly net loss of $2,424. At least one investor was told that the "rent has nowhere to go but up."

26. The offering materials listed the current value of the building as $1,720,000. The offering materials further represented that there was $1,087,000 worth of debt on the property. Pinneo subtracted the loans on the building from the current value to arrive at $633,000 as the total equity in the building. He retained 10% ownership for him and his wife, and made 90% of the equity, or $569,700, available for sale. An investor could purchase a 5% interest in Yale Avenue Partners for $35,000. Of that, $3,350 was to go towards a cash reserve account.

27. Pinneo calculated the value of the building by using an expense ratio of 35.85% of the total annual gross scheduled income to arrive at an annual net operating income of $54,193. He then used a capitalization rate of 3.15% to arrive at a total value of $1,720,000. The offering materials failed to disclose that for valued year 2007, the King County Department of Assessments assessed the taxable total value of the property to be $782,000. The offering materials further failed to explain why the value Pinneo calculated was so much greater than the tax assessed value.

28. The offering materials represented that the investment plan was to hold the building in its current state and consider redeveloping the site into condominium or townhouse units when the land value reached $500,000 per unit. The materials further represented that "[u]ntil that time, the anticipated appreciation of land in this area makes this investment a sure winner."

29. The materials represented that all underlying debt on the property was personally signed by Pinneo and his wife, and they alone would continue to be responsible for the LLC's debts. However, the monthly mortgage payments were made from the LLC's operating account, and the two promissory notes were secured by deeds of trust against the building owned by Yale Avenue Partners, so a default on the notes could mean that the building could be foreclosed upon.

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30. The offering materials represented that the cash reserve, which was calculated to be $67,000 in the beginning, would be good for 27 months. However, a letter from Pinneo to the investors, dated October 2008, stated that Yale Avenue Partners' working capital account was getting low and requested a capital contribution of $500 per 5% of ownership interest to pay for the second half property tax payment. Pinneo indicated in the same letter that "[o]ur investment on Yale is doing great." Pinneo testified that Yale Avenue Partners would not have requested a capital contribution had there been any funds remaining in its cash reserve account. Capital contributions were also requested in December 2008 and March 2009. As of December 2010, Yale Avenue Partners was dependent upon capital contributions to stay current on its expenses.

31. On or about April 22, 2011, a Notice of Trustee's Sale was recorded with the King County Recorder's Office, and the building owned by Yale Avenue Partners was subsequently sold at a Trustee's Sale on or about July 29, 2011 for $756,000.

2344-2345 Franklin Twins, LLC Offering

32. From approximately April 2008 through October 2008, Pinneo offered and sold approximately $708,000 worth of LLC interests in Franklin Twins to approximately 36 investors. Unlike the other LLCs, Franklin Twins owned two apartment buildings, which were initially owned by Pinneo and another individual. They each quitclaimed their interests in the buildings to Franklin Twins. Each retained 10% ownership in the LLC, and the remaining 80% was made available for sale.

33. Investors typically received several documents prior to investing, including "2344-2345 Franklin Twins LLC Membership Opportunity," "Membership Game Plan for Franklin Twins LLC," "Income and Expense for the Franklin Twins," rent roll list, LLC agreement, insurance information, information concerning current financing on the two buildings, and a subscription agreement if they invested through a self-directed IRA. A 1% interest in Franklin Twins cost $13,880 to purchase. Of that amount, $1,120 was to be deposited into a reserve account. The offering materials show that the two buildings were operating at a loss of $500 per month. The materials represented that the reserve account, which was

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calculated to be over $113,000 in the beginning, was "intended to carry the negative and any unforeseen expenses until such time as rent raises will result in a positive cash flow on the building."

34. The offering materials listed the current value of both buildings as $3,225,000. Pinneo arrived at the current value by using an annual net operating income of $117,360 and a capitalization rate of 3.63%. The offering materials failed to disclose that for valued year 2008, the King County Department of Assessments assessed the taxable total value of the properties at $689,000 and $980,000. The offering materials further failed to explain why the value Pinneo calculated was so much greater than the tax assessed value.

35. The offering materials represented that the investment plan for the buildings was a long term hold, but there were several other possibilities for the buildings, such as converting into condominiums, building additional units, or replacing both buildings with high-end condominiums. The materials failed to disclose whether additional funds would be required for such conversions or how the LLC would obtain the funds. The offering materials further indicated that positive cash flow would go towards paying down the principal, and the buildings would become "a life long annuity" once they were free and clear. The offering materials described the model as "fool proof in that the long term financing is in place, and we are in the crossroads of consistent and predictable demand."

36. Investors were requested to make a capital contribution around September or October 2010 because there weren't enough funds left in the reserve account to do major capital improvements on the building.

<u>Misrepresentations/Omissions</u>

37. Respondents failed to provide material information to all investors, including but not limited to: complete financial statements, a full representation of company history, and prior performance information and results of operations for the buildings involved.

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38. Respondents failed to provide any property appraisal information for the real property owned by each of the LLCs.

39. Respondents failed to disclose material information concerning the risks involved, including but not limited to: risks arising from changes in the real estate regulatory environment, from possible environmental liabilities, and from ownership of real property, such as liability for injury to persons and property occurring on the real property.

<u>Registration Status</u>

40. Gregory Pinneo is not currently registered as a securities salesperson or broker-dealer in the State of Washington and has not previously been so registered.

41. East Edgar Partners, LLC is not currently registered to sell its securities in the State of Washington and has not previously been so registered.

42. Franklin Avenue Partners, LLC is not currently registered to sell its securities in the State of Washington and has not previously been so registered.

43. Yale Avenue Partners, LLC is not currently registered to sell its securities in the State of Washington and has not previously been so registered.

44. 2344-2345 Franklin Twins, LLC is not currently registered to sell its securities in the State of Washington and has not previously been so registered.

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

CONCLUSIONS OF LAW

1. The offer or sale of the limited liability company interests described above constitutes the offer or sale of a security as defined in RCW 21.20.005(14) and (17).

2. The offer or sale of said securities violated RCW 21.20.140 because no registration for such offer or sale is on file with the Securities Administrator.

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3. Respondent Gregory Pinneo violated RCW 21.20.040 by offering or selling said securities while not registered as a securities salesperson or broker-dealer in the state of Washington.

4. The offer or sale of said securities violated RCW 21.20.010 because Respondents Gregory Pinneo; East Edgar Partners, LLC; Franklin Avenue Partners, LLC; Yale Avenue Partners, LLC; and 2344-2345 Franklin Twins, LLC, in connection with the offer or sale of said securities directly or indirectly made untrue statements of material fact or omitted to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading.

NOTICE OF INTENT TO ORDER THE RESPONDENT TO CEASE AND DESIST

Based on the above Tentative Findings of Fact and Conclusions of Law, the Securities Administrator intend to order, pursuant to RCW 21.20.390(1), that Respondents Gregory Pinneo; East Edgar Partners, LLC; Franklin Avenue Partners, LLC; Yale Avenue Partners, LLC; and 2344-2345 Franklin Twins, LLC and their agents and employees, each cease and desist from violations of RCW 21.20.010, RCW 21.20.040, and RCW 21.20.140.

NOTICE OF INTENT TO IMPOSE FINES

Pursuant to RCW 21.20.395, and based upon the Tentative Findings of Fact and Conclusions of Law, the Securities Administrator intends to order that Respondent Gregory Pinneo shall be liable for and pay a fine of $25,000.

NOTICE OF INTENT TO RECOVER COSTS

Pursuant to RCW 21.20.390, and based upon the Tentative Findings of Fact and Conclusions of Law, the Securities Administrator intends to order that Respondent Gregory Pinneo shall be liable for and pay the costs, fees, and other expenses incurred in the investigation of not less than $6,000.

AUTHORITY AND PROCEDURE

This Statement of Charges is entered pursuant to the provisions of Chapter 21.20 RCW and is subject to the provisions of Chapter 34.05 RCW. The respondents may each make a written request for a

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hearing as set forth in the NOTICE OF OPPORTUNITY TO DEFEND AND OPPORTUNITY FOR HEARING accompanying this order.

If a respondent does not request a hearing, the Securities Administrator intends to adopt the above Tentative Findings of Fact and Conclusions of Law as final and enter an order to cease and desist permanent as to that respondent.

Dated this _15th________ day of December, 2011.

WILLIAM M. BEATTY
Securities Administrator

Approved by:

Suzanne E. Sarason
Chief of Enforcement

Presented by:

Jiyoung C. Kwon
Financial Legal Examiner

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