

**UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF COLUMBIA**

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**SECURITIES AND  
EXCHANGE COMMISSION,  
100 F. Street, N.E  
Washington, D.C. 20549  
Tel. (202) 551-4511**

**Plaintiff,**

v.

**BANCINSURANCE CORPORATION,  
and JOHN S. SOKOL,**

**Defendants.**

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Case: 1:09-cv-02155  
Assigned To : Kollar-Kotelly, Colleen  
Assign. Date : 11/16/2009  
Description: General Civil

**COMPLAINT**

Plaintiff Securities and Exchange Commission (“SEC” or “Commission”) alleges:

**SUMMARY**

1. This case concerns a financial fraud at Bancinsurance Corporation, an Ohio-based insurance company. Defendant Bancinsurance Corporation (“Bancinsurance” or the “Company”) failed to account properly for more than \$2 million of reinsurance claims and Bancinsurance’s president, Defendant John S. Sokol (“Sokol”), failed to ensure that the Company’s principal financial officer or its external auditors were informed of the claims. As a result, the Company’s financial condition in the Company’s Form 10-K for fiscal year 2003 and the Company’s Form 10-Q for the first quarter of fiscal year 2004 was materially misstated.

2. During the period 2001 through 2004, Bancinsurance participated in a bail and immigration bond program (the “Program”) as a reinsurer. On or before March 11,

2004, shortly before Bancinsurance filed its Form 10-K for the fiscal year 2003, Bancinsurance and Sokol were notified that the Company would receive more than \$1 million in reinsurance claims under the Program. Sokol understood, or was reckless in not understanding, that these claims represented 2003 losses and therefore were required to be reflected in Bancinsurance's fiscal 2003 financial statements. Sokol failed to ensure that the Company's principal financial officer or its external auditors were informed of the claims. As a result, the claims were not properly recorded in the Company's books and records, which caused Bancinsurance's 2003 financial statements to materially understate the Company's expenses and loss reserves.

3. On or about March 25, 2004, Bancinsurance received invoices for more than \$1 million in additional claims. Sokol understood, or was reckless in not understanding, that these claims were required to be included in Bancinsurance's financial statements filed with its Form 10-Q for the quarter ended March 31, 2004. Sokol again failed to ensure that the Company's principal financial officer or its external auditors were informed of the claims. As a result, the claims were not properly recorded in the Company's books and records, which caused Bancinsurance's financial statements for that quarter to materially understate the Company's expenses.

4. As a result of this conduct, the Commission requests that this Court permanently enjoin Bancinsurance and Sokol from violating the federal securities laws and rules pursuant to Section 21(d)(1) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. §78u(d)(1)]; and impose civil penalties on Sokol pursuant to Exchange Act Section 21(d)(3) [15 U.S.C. §78u(d)(3)].

## JURISDICTION AND VENUE

5. This Court has jurisdiction over this action pursuant to Sections 21(d), 21(e), and 27 of the Exchange Act [15 U.S.C. §§78u(d), 78u(e), and 78aa].

6. Defendant Bancinsurance and Defendant Sokol, directly or indirectly, have made use of the means and instrumentalities of interstate commerce, or of the mails, or of the facilities of a national securities exchange in connection with the acts, practices, and courses of business alleged herein.

7. Venue is proper in this district pursuant to Section 27 of the Exchange Act [15 U.S.C. §78aa] because certain of the acts, transactions, practices and courses of business alleged herein took place in this district.

## DEFENDANTS

8. **Bancinsurance Corporation** (“Bancinsurance” or “the Company”), is an Ohio insurance holding company, headquartered in Columbus, Ohio. Bancinsurance’s common stock was registered under Section 12(g) of the Exchange Act and traded on the Nasdaq National Market System until February 22, 2005, when Nasdaq delisted it. Bancinsurance’s common stock is currently dually quoted on the OTC Bulletin Board and in the “pink sheets” in the over-the-counter market.

9. **John S. Sokol**, age 47, has served as president of Bancinsurance since June 1999. In June 2007, Sokol became the Company’s Chairman and CEO. Sokol resides in Columbus, Ohio.

## FACTUAL ALLEGATIONS

10. From approximately 2001 through 2004 Bancinsurance participated as a reinsurer in the Program.

11. The Program for which Bancinsurance served as a reinsurer was administered by a privately-held corporation (hereafter the "Program Administrator"). The Program's customers included criminal defendants and immigration detainees throughout the United States. In exchange for the Program Administrator's posting of a bond to release them from governmental custody, customers paid a premium. The Program Administrator kept a percentage of the premium, and forwarded a percentage of the remaining premium to the Program's insurers. The primary insurers in turn divided their share of the premium with the Program's reinsurers, among them Bancinsurance. In exchange for the premium, the reinsurers agreed to assume a portion of the Program's losses.

12. Losses on forfeited bonds reached the primary insurers only if the Program Administrator did not have the means to pay them. To encourage insurance company participation, the Program Administrator represented that it secured each bond with a promissory note collateralized by property. Thus for each claim the Program Administrator paid, it anticipated recovering almost 100 percent of its losses. To further minimize the risk of loss to the insurance companies, the Program also required the Program Administrator to maintain "build-up" funds as cash reservoirs for bond liabilities. The Program Administrator provided additional financial protection in the form of guarantees, including a corporate guarantee by the Program Administrator itself, and a personal guarantee by the Program Administrator's CEO.

13. In 2001, Bancinsurance joined the reinsurer pool and contracted for a 15 percent share of the reinsurer pool's premium and a 15 percent share of the Program's total liabilities.

14. To comply with generally accepted accounting principles (“GAAP”), Bancinsurance was required, at the end of each reporting period, to reserve for an amount sufficient to settle all unpaid claims. Specifically, Statement of Financial Accounting Standards No. 60 ¶18, GAAP required that the reserve established for unpaid claims “be based on the estimated ultimate cost of settling claims . . . using past experience adjusted for current trends, and any other factors that would modify past experience.” During the period March 2001 until April 2004, Bancinsurance employed an “expected loss ratio” method to calculate its reserves on the Program. The Company’s external auditors approved Bancinsurance’s use of the expected loss ratio method. Under this method, the Company established reserves that were equal to the amount of the premiums the Company received. If claims exceeded premiums, Bancinsurance was required to increase its reserves to an amount equal to the claims. If Bancinsurance did not do so, the Company was required to record the amount by which claims exceeded reserves as an expense on its income statement.

15. On January 30, 2004, the Company’s external auditors issued an audit report on Bancinsurance’s financial statements for the fiscal year ended December 31, 2003. The audit report stated that, in the opinion of the auditors, Bancinsurance’s financial statements “present fairly, in all material respects, the consolidated financial position of Bancinsurance Corporation at December 31, 2003 . . . in conformity with accounting principles generally accepted in the United States.” In its annual report to its shareholders, on January 30, 2004, Bancinsurance publicly disseminated its financial statements, with the audit report.

16. After Bancinsurance issued its annual report, Sokol and Bancinsurance

learned that the Program Administrator's financial condition had deteriorated to the point that the Program Administrator would be unable to prevent large claims from flowing to the primary insurers, and to the reinsurers.

17. On or before March 11, 2004, Bancinsurance and Sokol learned that approximately \$10 million in claims had been reported to the reinsurer pool, and that Bancinsurance would be requested to pay \$1.5 million—its 15 percent share of the claims. Sokol understood, or was reckless in not understanding, that the claims pertained to the 2003 fiscal year, that Bancinsurance would need to account for the claims in its financial statements for the fiscal year ended December 31, 2003, that Bancinsurance's financial records reflected a \$415,000 reserve for the Program, and that, under the expected loss ratio method that Bancinsurance was utilizing at the time, Bancinsurance was required to record an additional expense and increase its loss reserves.

18. Consistent with what Sokol had learned earlier, on March 18, 2004, Bancinsurance received \$1.3 million in invoices. Sokol was aware of these invoices and knew, or was reckless in not knowing, that these claims reflected losses incurred in 2003 for Bancinsurance and were required to be included in the Company's fiscal 2003 financial statement. Sokol did not ensure that Bancinsurance's principal financial officer or its external auditors were informed of the \$1.3 million in invoices the Company had received on March 18.

19. On March 19, 2004, and again on March 22, 2004, Sokol provided the auditors with two separate management representation letters ("representation letters") that he signed. Both of the representation letters stated, in pertinent part:

No events or transactions have occurred since the date of our previous letter or are pending that would have a material affect on the audited financial statements included in the 10-K filing or that are of such significance in relation to the Company's affairs to require mention in a note to the audited financial statements in order to make them not misleading regarding the financial position, results of operations, or cash flows of the Company.

When Sokol signed the March 19, and 22, 2004 representation letters, he knew, or was reckless in not knowing, that the claims received in March 2004 pertained to the Company's 2003 fiscal year and that, as a result, the statements were materially misleading.

20. Relying on management's representations, on March 22, 2004, Bancinsurance's auditors consented to the incorporation by reference of their January 30, 2004 unqualified audit report, which was included in Bancinsurance's 2003 annual report.

21. On March 22, 2004, Bancinsurance filed with the Commission its Form 10-K for the fiscal year ended December 31, 2004, signed by Sokol as President and as a Director. The Company's balance sheet, included in the Form 10-K, did not include reserves for the approximately \$1.3 million in claims the Company had received. As a result of receiving these claims, Bancinsurance should have reported an additional expense on the Company's income statement and an additional liability on its balance sheet. Because the Company failed to do so, the Company's financial statements materially understated the Company's expenses by approximately \$1.3 million and understated its reserves by approximately \$1.3 million. Consequently, Bancinsurance's reported income from continuing operations of \$5.5 million was overstated by approximately \$1.3 million. Bancinsurance's reported basic earnings per share of \$0.79,

was overstated by approximately \$0.19. Sokol knew, or was reckless in not knowing, that the financial statements included in Bancinsurance's Form 10-K were materially misleading.

22. Shortly after Bancinsurance filed its fiscal 2003 Form 10-K, on March 24 and 25, 2004, Bancinsurance received invoices for additional claims totaling approximately \$1.1 million. By at least April 29, 2004, Sokol was aware of the additional invoices. Sokol did not ensure that the Company's principal financial officer or its external auditors were informed of the claims.

23. Bancinsurance disclosed its first quarter financial results for the fiscal quarter ended March 31, 2004, in a press release issued on April 30, 2004, and in a Form 10-Q filed with the Commission on May 7, 2004. The Company's reported financial results did not reflect the \$1.1 million in claims Bancinsurance had received on March 24 and 25, 2004.

24. The Company, in fact, received invoices of at least \$1.6 million during the period March 24, 2004 to April 23, 2004 that represented losses attributable to the quarter ended March 31, 2004. The invoices were greater than the Company's \$83,000 program reserve at March 31, 2004. As a result, Bancinsurance's first quarter fiscal 2004 financial statements materially understated the Company's expenses by approximately \$1.5 million and understated its loss reserves by approximately \$1.5 million. Consequently, Bancinsurance's reported income from continuing operations before taxes, of \$1.6 million, was overstated by approximately \$1.5 million. Bancinsurance's reported basic earnings per share of \$0.24, was overstated by approximately \$0.23. Sokol knew, or was reckless in not knowing, that Bancinsurance's April 30, 2004 press release, and its Form



10-Q, were materially misleading.

**FIRST CLAIM**  
**Violations of Exchange Act Section 10(b) and Exchange Act Rule 10b-5**  
**(Bancinsurance and Sokol)**

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

26. Defendant Bancinsurance and Defendant Sokol, directly or indirectly, by use of the means or instruments of interstate commerce, or of the mails, or of a facility of a national securities exchange, knowingly or recklessly: (a) employed devices, schemes, or artifices to defraud; (b) made untrue statements of a material fact or omitted to state a material fact, necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or (c) engaged in acts, transactions, practices, or courses of business which operated or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of securities.

27. By engaging in the conduct alleged above, Defendant Bancinsurance and Defendant Sokol violated Exchange Act Section 10(b) [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5].

**SECOND CLAIM**  
**Violations of Exchange Act Section 13(a) and Exchange Act Rules 12b-20,**  
**13a-1, and 13a-13**  
**(Bancinsurance)**

28. Paragraphs 1 through 24 are realleged and incorporated herein by reference.

29. Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)], and Rules 12b-20, 13a-1 and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1 and 240.13a-13] thereunder,

require issuers of registered securities to file with the Commission factually accurate annual and quarterly reports.

30. By engaging in the conduct alleged above, Defendant Bancinsurance violated Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-20, 13a-1 and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1 and 240.13a-13].

**THIRD CLAIM**  
**Violations of Exchange Act Sections 13(b)(2)(A) and 13(b)(2)(B)**  
**(Bancinsurance)**

31. Paragraphs 1 through 24 are realleged and incorporated herein by reference.

32. Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)] requires issuers to make and keep books, records, and accounts which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of its assets. Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. § 78m(b)(2)(B)] requires issuers to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that transactions were recorded as necessary to permit preparation of financial statements in conformity with GAAP and to maintain the accountability of assets.

33. By engaging in the conduct alleged above, Bancinsurance violated Exchange Act Sections 13(b)(2)(A) and 13(b)(2)(B) [15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(2)(B)].

#### **FOURTH CLAIM**

##### **Violations of Exchange Act Section 13(b)(5) and Exchange Act Rule 13b2-1** (Sokol)

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

35. Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78m(b)(5)] forbids any person from knowingly circumventing or knowingly failing to implement a system of internal accounting controls or knowingly falsifying any book, record or account as described in Section 13(b)(2) of the Exchange Act [15 U.S.C. § 78m(b)(2)]. Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1] prohibits any person from directly or indirectly falsifying or causing to be falsified, any relevant book, record or account.

36. By engaging in the conduct alleged above, Sokol violated Exchange Act Section 13(b)(5) [15 U.S.C. § 78m(b)(5)] and Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1].

#### **FIFTH CLAIM**

##### **Aiding and Abetting Violations of Exchange Act Sections 13(a), 13(b)(2)(A) and 13(b)(2)(B) and Exchange Act Rules 12b-20, 13a-1, and 13a-13** (Sokol)

37. Paragraphs 1 through 24 are realleged and incorporated herein by reference.

38. Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)], and Rules 12b-20, 13a-1 and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1 and 240.13a-13] thereunder, require issuers of registered securities to file with the Commission factually accurate annual and quarterly reports.

39. Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)] requires issuers to make and keep books, records, and accounts which, in reasonable detail, accurately and fairly reflected the transactions and dispositions of its assets. Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. § 78m(b)(2)(B)] requires issuers to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that transactions were recorded as necessary to permit preparation of financial statements in conformity with GAAP and to maintain the accountability of assets.

40. By engaging in the conduct alleged above, Sokol aided and abetted violations of Exchange Act Sections 13(a) [15 U.S.C. § 78m(a)], 13(b)(2)(A) and 13(b)(2)(B) [15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(2)(B)] and Exchange Act Rules 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13].

**SIXTH CLAIM**  
**Violations of Exchange Act Rule 13b2-2**  
**(Sokol)**

41. Paragraphs 1 through 24 are realleged and incorporated herein by reference.

42. Exchange Act Rule 13b2-2 [17 C.F.R. § 240.13b2-2] requires that no director or officer of an issuer shall, directly or indirectly: (1) Make or cause to be made a materially false or misleading statement to an accountant in connection with; or (2) Omit to state, or cause another person to omit to state, any material fact necessary in order to make statements made, in light of the circumstances under which such statements were made, not misleading, to an accountant in connection with: (i) Any audit, review or examination of the financial statements of the issuer required to be made pursuant to this

subpart; or (ii) The preparation or filing of any document or report required to be filed with the Commission.

43. By engaging in the conduct alleged above, Sokol violated Exchange Act Rule 13b2-2 [17 C.F.R. § 240.13b2-2].

### **PRAYER FOR RELIEF**

WHEREFORE, the Commission respectfully requests that this Court:

(a) Permanently restrain and enjoin Defendant Bancinsurance from violating Exchange Act Sections 10(b), 13(a), 13(b)(2)(A) and 13(b)(2)(B) [15 U.S.C. §§ 78j(b), 78m(a), 78m(b)(2)(A), and 78m(b)(2)(B)], and Exchange Act Rules 10b-5, 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.10b-5, 240.12b-20, 240.13a-1, and 240.13a-13]; and

(b) Permanently restrain and enjoin Defendant Sokol from violating Exchange Act Sections 10(b) and 13(b)(5) [15 U.S.C. §§ 78j(b) and 78m(b)(5)], and Exchange Act Rules 10b-5 [17 C.F.R. § 240.10b-5], 13b2-1 [17 C.F.R. § 240.13b2-1] and 13b2-2 [17 C.F.R. § 240.13b2-2], and from aiding and abetting violations of Exchange Act Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) [15 U.S.C. §§ 78m(a), 78m(b)(2)(A), and 78m(b)(2)(B)] and Exchange Act Rules 12b-20 [17 C.F.R. § 240.12b-20], 13a-1 [17 C.F.R. § 240.13a-1], and 13a-13 [17 C.F.R. § 240.13a-13]; and

(c) Order Defendant Sokol to pay civil penalties pursuant to Exchange Act Section 21(d)(3) [15 U.S.C. §78u(d)(3)]; and

(d) Grant such other relief as the Court may deem just and appropriate.

Dated: November 16, 2009  
Washington DC

Respectfully submitted,



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