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SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

LC2021-000011-001 DT 02/02/2022

HONORABLE DANIEL J. KILEY

CLERK OF THE COURT
J. Eaton
Deputy

UPSTATE LAW GROUP L L C
CANDY KERN-FULLER

ROBERT B ZELMS

v.

ARIZONA CORPORATION COMMISSION (001)

JAMES DUANE BURGESS

ANTHONY S VITAGLIANO
JUDGE KILEY
OFFICE OF ADMINISTRATIVE HEARINGS
REMAND DESK-LCA-CCC

RECORD APPEAL RULING / AFFIRMED

Arizona Corporation Commission Decision No. 77806

Appellants Upstate Law Group ("ULG") and Candy Kern-Fuller ("Kern-Fuller") (ULG and Kern-Fuller collectively, "Appellants") appeal from the November 12, 2020 Opinion and Order (the "Final Decision") of Appellee Arizona Corporation Commission ("Appellee" or the "Commission"). For the following reasons, this Court affirms.

FACTUAL BACKGROUND & PROCEDURAL HISTORY

Viewed in the requisite light most favorable to sustaining the administrative decision, *see Shorey v. Ariz. Corp. Comm'n*, 238 Ariz. 253, 258 ¶ 14 (App. 2015), the relevant facts can be summarized as follows:

This case arises of certain transactions, referred to herein as "income stream investments," pursuant to which Respondent Mark Corbett ("Corbett") and others solicited

military veterans who were receiving an income stream from a military pension or disability benefits to sell future monthly payments to investors in exchange for a discounted lump sum payment. Index of Record ("I.R.") A-106, Final Decision, at pp. 182-83.

From October 2013 through November 2015, the income stream investments were offered through entities known as BIAC, Inc. ("BAIC") and SoBell Corp. ("SoBell").[1] *Id*. at pp. 11, 183-84. From March 2017 and May 2017, such investments were offered through Performance Arbitrage Company, Inc. ("PAC") and Financial Product Distributors, LLC ("FPD"). *Id*. at pp. 182, 184.

Respondent Andrew Gamber ("Gamber") was the President of BAIC, the incorporator of SoBell, and a part owner of PAC through his company, AAG Holdings. I.R. A-106, Final Decision, at pp. 183-84. As discussed more fully below, Gamber and/or companies he controlled were the subject of cease-and-desist orders entered in various states arising out of transactions similar to the income stream investments at issue here. Respondent Michelle Plant ("Plant") worked at various times as BAIC's Director of Compliance, an independent contractor for SoBell, and PAC's Chief Operating Officer. *Id*. at pp. 182, 184.

ULG was a South Carolina law firm of which Kern-Fuller was a partner. I.R. A-106, Final Decision, at pp. 182-83. Marketing materials for the investments offered through BAIC and SoBell from October 2013 through November 2015, and the investments offered through PAC from March 2017 through May 2017, identified ULG's role in the income stream transactions as including reviewing documents and processing payments through its trust accounts. *Id*. at p. 184.

To complete an income stream investment, BAIC, SoBell, PAC and FPD would provide form documents in a so-called "Closing Book" or "Fulfillment Kit" to the parties, *i.e*, each veteran/seller and investor/purchaser. I.R. A-106, Final Decision, at pp. 6, 185-86. *See also* I.R. C-24, Fulfillment Kit, at pp. ACC000921 – ACC001011; I.R. C-258, Closing Book, at pp. ACC004379 – ACC004439; I.R. C-281, Closing Book, at pp. ACC001926 – ACC001997. The documents provided for the investor/purchaser's signature included a Purchase Assistance Agreement which provided that the investor/purchaser was engaging the services of BAIC, SoBell, PAC or FPD to assist in purchasing a veteran/seller's future income stream payments. I.R. A-106, Final Decision, at p. 185. *See also* I.R. C-24, Purchase Assistance Agreement, at pp. ACC000979 – ACC000981; I.R. C-258, Purchase Assistance Agreement, at pp. ACC004403 – ACC004404; I.R. C-281, Purchase Assistance Agreement, at pp. ACC001941 – ACC001942.

[1] The name "BAIC" stands for "Buyers of Annuities and Investment Contracts." I.R. A-106, Final Decision, at p. 90.

The documents provided for the veteran/seller's signature included a Sales Assistance Agreement which provided that the veteran would, at closing, pay a commission to BAIC, SoBell, or Corbett. I.R. A-106, Final Decision, at p. 185. *See also* I.R. C-24, Sales Assistance Agreement, at p. ACC000927; I.R. C-258, Sales Assistance Agreement, at p. ACC004380; I.R. C-281, Sales Assistance Agreement, at p. ACC001927.

Each Closing Book for the investments through BAIC and SoBell provided that the veteran/seller was to arrange for his or her monthly pension or disability payments to be directly deposited into a ULG trust account. I.R. A-106, Final Decision, at p. 185. *See also* I.R. C-24, Purchase Assistance Agreement, at p. ACC000981; I.R. C-258, Contract for Sale of Payments, at p. ACC004387. Upon receipt of the funds, ULG would then transfer the funds from its trust account to the investor/purchaser each month. I.R. A-106, Final Decision, at pp. 185, 186.

Similarly, each Purchase Assistance Agreement for the investments through PAC and FPD required the veteran/seller to provide ULG with an automatic draft from the veteran/seller's bank account into which the Department of Veterans Affairs or other agency deposited the monthly benefits. I.R. A-106, Final Decision, at pp. 185-86. The documents provided to the veteran/seller for the investments through PAC and FPD also included a Payment and Account Verification form for the veteran/seller to sign, authorizing ULG to make debits and withdrawals from the veteran/seller's account. I.R. A-106, Final Decision, at p. 186.

None of the documents provided to the investors/purchasers made any reference to the Federal Anti-Assignment Acts, 38 U.S.C. § 5301(a) and 37 U.S.C. § 701(c), or put investor/purchasers on notice of the possibility that the investments might be found to violate those statutes. I.R. A-106, Final Decision, at p. 185. Likewise, none of the documents provided to the investors/purchasers disclosed that cease-and-desist orders had been issued against Gamber and/or his company by securities regulators in other states for violations of securities laws arising out of the sale of income stream investments involving veterans' pensions and disability benefits. *Id.* at p. 187.[2]

From October 28, 2013 through November 17, 2015, 21 investors purchased a total of 53 income stream investments through BAIC and SoBell, for a total of $2,776,952.62. I.R. A-106, Final Decision, at p. 187. From these sales, ULG received fees of at least $48,695.62. *Id.*

[2] Between April 2013 and November 2014, securities regulators in six states had issued cease-and-desist orders against Gamber and/or his company for violations of securities laws arising out of the sale of income stream investments involving veterans' pensions and disability benefits. I.R. A-106, Final Decision, at p. 187.

From March 17, 2017 through May 23, 2017, four investors entered six income stream investment through PAC and FPD for a total of $371,191.23. I.R. A-106, Final Decision, at p. 188.

The Securities Division of the Commission (the "Division") initiated administrative proceedings in 2018 with the filing of a Notice of Opportunity for Hearing Regarding Proposed Order to Cease and Desist, Order for Restitution, Order for Administrative Penalties, Order of Revocation, and Order for Other Affirmative Action against Appellants, PAC, FPD, Corbett, Plant, and others. I.R. A-106, Final Decision, at p. 4. At the conclusion of the administrative proceedings, the Commission issued the Final Decision in which it determined, *inter alia*, that the income stream investments constitute "securities" within the meaning of A.R.S. § 44-1801(27); that Appellants and others "made, participated in or induced the offer and sale of securities" in violation of A.R.S. §§ 44-1841 and -1842; that Appellants and others had "failed to meet their burden of proof…to establish that the securities…were exempt from regulation under the [Arizona Securities Act]"; that Appellants and others "committed fraud by having made, participated in or induced the offer and sale of securities, in violation of A.R.S. § 44-1991"; and that Kern-Fuller directly or indirectly controlled ULG and so "is jointly and severally liable with ULG for violations of A.R.S. § 44-1991." *Id*. at pp. 188-89. The Commission concluded its Final Decision by issuing various orders, including an order that Appellants cease and desist from the violations found in the Final Decision and that Appellants pay restitution in the principal amount of $2,572,247.37 in connection with the BAIC and SoBell transactions and in the principal amount of $371,191.23 in connection with the PAC and FPD transactions. *Id*. at pp. 189-90. The Final Decision also required Appellants to pay administrative penalties of $240,000. *Id*. at pp. 190-91.

Appellants filed a timely Notice of Appeal. This Court has jurisdiction pursuant to Ariz. Const. art. 6, § 14 and A.R.S. §§ 12-124(A), 12-905(A), and 44-1981.

ISSUES PRESENTED

1. Did the Commission abuse its discretion or otherwise err in concluding that the pension income stream transactions constitute "securities" as defined in A.R.S. § 44-1801(27)?

2. Did the Commission abuse its discretion or otherwise err in concluding that the pension income stream transactions are not "exempt" pursuant to the Arizona Securities Act?

3. Did the Commission abuse its discretion or otherwise err in concluding that Appellants "participated in and induced" the unlawful sale of securities?

4. Did the Commission abuse its discretion or otherwise err in concluding that Appellants committed fraudulent practices in violation of A.R.S. § 44-1991(A)?

5. Did the Commission abuse its discretion or otherwise err in concluding that Appellants violated A.R.S. §§ 44-1841 and -1842?

6. Did the Commission abuse its discretion or otherwise err in concluding that Appellants did not act in the ordinary course of their professional capacity in connection with the pension income stream transactions?

7. Did the Commission abuse its discretion or otherwise err in concluding that Kern-Fuller has "control person" liability for ULG pursuant to A.R.S. § 44-1999(B)?

8. Did the Commission abuse its discretion or otherwise err in entering orders against Appellants to cease and desist and to pay restitution and administrative penalties?

STANDARD OF REVIEW & APPLICABLE LEGAL PRINCIPLES

The Court's review of a final decision by the Commission is limited to "whether the administrative action was illegal, arbitrary, capricious or involved an abuse of discretion." *Hirsch v. Ariz. Corp. Comm'n*, 237 Ariz. 456, 461-62 ¶ 18 (App. 2015) (citation and internal quotations omitted). An abuse of discretion will be found if the record does not provide substantial support for the agency's decision, or if the agency committed an error of law in making its decision. *See Carey v. Soucy*, 245 Ariz. 547, 552 ¶ 19 (App. 2018) ("A court abuses its discretion where the record fails to provide substantial support for its decision or the court commits an error of law in reaching the decision."). The party challenging the Commission's decision has the "burden" of "show[ing] by clear and satisfactory evidence that the Commission's decision was unreasonable or unlawful." *Ariz. Corp. Comm'n v. Pacific Motor Trucking Co*., 116 Ariz. 465, 467 (App. 1977).

"In reviewing the facts determined by" the Commission, the reviewing court does not "reweigh the evidence," and will affirm the decision "if substantial evidence supports" it. *Nutek Info. Sys., Inc. v. Ariz. Corp. Comm'n*, 194 Ariz. 104, 107 ¶ 15 (App. 1998). *See also DeGroot v. Ariz. Racing Comm'n*, 141 Ariz. 331, 336 (App. 1984) ("[I]n order to reverse the agency's decision, the trial court must find that there was no substantial evidence to support the agency

decision."). The "substantial evidence" required to affirm an agency decision will be found to exist "if either of two inconsistent factual conclusions are supported by the record." *Eastern Vanguard Forex, Ltd. v. Ariz. Corp. Comm'n*, 206 Ariz. 399, 409 ¶ 35 (App. 2003). *See also Wales v. Ariz. Corp. Comm'n*, 249 Ariz. 263, 268 ¶ 19 (App. 2020) ("Substantial evidence exists if the evidentiary record supports the decision, even if the record would also support a different conclusion."). Moreover, a court reviewing a decision by the Commission "view[s] the evidence in the light most favorable to upholding the Commission's decision." *Shorey*, 238 Ariz. at 258 ¶ 14.

Courts review questions of law *de novo*. A.R.S. § 12-910(F). Whether a particular investment or transaction constitutes a "security" within the Arizona Security Act ("ASA") is a question of law. *See Vairo v. Clayden*, 153 Ariz. 13, 18 (App. 1987).

An administrative agency's decision will be affirmed if it is correct for any reason, even a reason not relied upon by the agency itself. *See Lewis v. Ariz. St. Personnel Bd.*, 240 Ariz. 330, 334 ¶ 15 (App. 2016) (administrative agency's decision "will [be] affirm[ed] if any reasonable interpretation of the record supports the decision"); *BNSF Ry. Co. v. Ariz. Corp. Comm'n*, 228 Ariz. 481, 485 ¶ 12 (App. 2012) ("The court of appeals will affirm the trial court's decision if it is correct for any reason[].") (citation and internal quotations omitted).

DISCUSSION

A. The Commission Did Not Commit an Error of Law, or Abuse Its Discretion, in Determining that the Investments Constitute "Securities" Within the Meaning of the Act.

In Appellants' Opening Brief ("Opening Brief" or "O.B."), Appellants argue that, "[c]ontrary to" the Final Decision, the income stream investments at issue here "are not 'investment contracts' as" the term is used in A.R.S. § 44-1801(27) "and therefore not 'securities' under the ASA." O.B. at p. 12.[3] In response, Appellee contends that "there is no question that the income stream investments were securities in the form of investment contracts." Answering Brief of [Appellee] ("Answering Brief" or "A.B.") at p. 9.

[3] Appellants' claim that the income stream transactions are not "investment contracts" cannot be reconciled with the fact that the term "investment contracts" appears in the name of one of the principal participants in the investment stream transactions. As noted above, "BAIC" stands for "Buyers of Annuities *and Investment Contracts*." I.R. A-106, Final Decision, at p. 90 (emphasis added).

The ASA defines the term "security" to include "investment contract[s]." A.R.S. § 44-1801(27). As all parties to this case acknowledge, *see* O.B. at 13 *and* A.B. at p. 9, "the test adopted by Arizona courts to determine whether a given transaction is an investment contract is" the so-called "*Howey* test." *Daggett v. Jackie Fine Arts, Inc*., 152 Ariz. 559, 565 (App. 1986), *citing S.E.C. v. W.J. Howey Co*., 328 U.S. 293 (1946). Under the *Howey* test, "an investment contract" is defined as "a transaction where (1) an individual is led to invest money (2) in a common enterprise (3) with the expectation that he will earn a profit solely through the efforts of others." *Daggett*, 152 Ariz. at 565. *See also Howey*, 328 U.S. at 301 ("The test is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others.").

In its Final Decision, the Commission found that the income stream investments meet all three prongs of the *Howey* test. A-106, Final Decision, at pp. 113-27. Specifically, the Final Decision found "the first prong of the *Howey* test…satisfied" because "[t]he record established that investors made monetary investments in the 59 income stream investments at issue"; the "second prong of the *Howey* test…satisfied" because ULG stood to "collect[] escrow service fees over the life of the investment" as long as the veteran/seller "continu[ed] to make monthly payments," which, in turn, gave ULG "an ongoing financial interest in the income stream investments" that created a common enterprise with the investors; and the third prong of the *Howey* test was "satisfied" because "the income stream investors had an expectation of profits to be attained through the efforts of others." *Id*. at pp. 113, 118, 127. In support of these findings, the Final Decision cites to specific portions of the record. *See generally id*. at pp. 113-27.

Appellants challenge each of these findings.

1. The Commission Did Not Abuse Its Discretion or Commit an Error of Law in Finding that the First Prong of the *Howey* Test Was Satisfied.

Appellants argue that the first prong of the *Howey* test is not met here because, they contend, the income stream investment transactions "do not have the characteristics required to be a 'security' under the *Howey* test." O.B. at p. 13. They explain that, because "*Howey*'s second and third prongs are not met," the transactions are not securities, "and therefore the first prong also is not met." *Id*. at p. 14.

In effect, Appellants argue that, because the transactions at issue are not securities, the first prong of the *Howey* test cannot possibly be met, since the transactions are not securities. This argument, which Appellee correctly characterizes as "circular," overlooks the fact that each of the three prongs of the *Howey* test must be considered separately. The first prong of the

Howey test requires simply a determination of whether money was, in fact, invested. *See, e.g.*, *Vairo*, 153 Ariz. at 17 ("There is no question that [plaintiff] invested money. Thus, the first prong of the *Howey* test is met."). Here, there is no question that the investor/purchasers invested money in the income stream investments. The Court therefore finds that the Commission did not abuse its discretion or commit an error of law in finding that the first prong of the *Howey* test is met.

2. The Commission Did Not Abuse Its Discretion or Commit an Error of Law in Finding that the Second Prong of the *Howey* Test Was Satisfied.

Appellants contend that the second prong of the *Howey* test is not met because there is "no 'common enterprise'" here. O.B. at p. 14. Noting that, in finding a "common enterprise," the Commission relied on case holding that a "common enterprise" can be established by "vertical commonality," Appellant argue that the Commission incorrectly interpreted and applied the relevant case law, and so "wrongly determined that vertical commonality existed." *Id*., *citing Daggett*, 152 Ariz. at 565, and other cases.

In response, Appellee cites case law holding that vertical commonality exists where there is "a positive correlation between the success of the investor and the success of the promoter, without requiring a pooling of funds." A.B. at p. 11, *quoting Daggett*, 152 Ariz. at 565. Applying this principle, Appellee argues that the Commission correctly found vertical commonality in this case in part because ULG's interest "continued for the life of the investment, and the fortunes of the investors were linked with those of…ULG[.]" A.B. at p. 12.

As Appellee correctly notes, evidence in the record establishes that ULG's duties under, and interest in, the income stream investments continued throughout the life of each such investment. ULG served as escrow agent for the life of each investment, receiving monthly deposits into its trust account and disbursing them to the investors. *See, e.g.*, I.R. C-120, Contract for Sale of Payments dated February 26, 2015, at pp. ACC001490 – ACC001491 ("The servicer of the Payments shall be [ULG], located in Easley, South Carolina (the 'Escrow Company') in accordance with the following:…Seller shall direct that the Payments will be received and serviced by the Escrow Company…Beginning at Closing, Seller shall receive the Payments at the designated escrow account at [ULG]…"). ULG received a financial benefit over the life of the investment for performing these services in the form of periodic escrow services fees. *See* I.R. C-288, Escrow Services and Fee Agreement, at p. 1 ¶ 2(A) (providing that ULG was to receive "payment for certain Closing Costs, including fee payment for Escrow Services," and that such fees include initial fees and a $215.00 fee "to be disbursed yearly…after the second year of escrowing"). On the other hand, ULG would no longer receive annual fees if the

veteran/seller stopped the deposit of the pension or disability payments into ULG's account. The Court therefore agrees with Appellee that, because "neither the investor nor ULG got paid" if "the veteran stopped payments," "a positive correlation" existed "between the success of the investor and the success of the promoter." A.B. at pp. 12-13. *See also Daggett*, 152 Ariz. at 565 ("Vertical commonality requires a positive correlation between the success of the investor and the success of the promoter, without requiring a pooling of funds.").

Indeed, in their Opening Brief, Appellants admit that ULG received a fee each time a veteran's monthly benefit payment was deposited into ULG's trust account and then disbursed to the investor. *See* O.B. at p. 9 ("[D]uring performance, once a payment had been distributed and received into the account of the Seller, the Seller directed it be deposited into the escrow account; ULG received a nominal fee from the Buyer, deducted applicable fees and commissions, and remitted the agreed-upon amount…ULG distributes the agreed-upon amount to the Buyer each month…") (record citations omitted). Appellants' admission on this point establishes the existence of a "positive correlation" between the financial success of the investor and that of Appellants, and therefore establishes a "common enterprise." *Daggett*, 152 Ariz. at 565.

Further confirmation of the existence of a "common enterprise" is found in the fact that Kern-Fuller invoked her right against self-incrimination when asked, "You, ULG, [Gamber], BAIC, SoBell, PAC, [Plant], [FPD], and [another entity] were all engaged in a common enterprise, weren't you?" I.R. A-106, Final Decision, at p. 95. *See also* I.R. B-7, Hearing Transcript, at p. 1052. Kern-Fuller's invocation of her right against self-incrimination supports the inference that, had she answered, the answer would have been adverse to her position. *See, e.g., Castro v. Ballesteros v. Suarez*, 222 Ariz. 48, 53 ¶ 20 (App. 2009) ("[A] a witness or party in a civil case can invoke their Fifth Amendment privilege against self-incrimination, but the trier of fact is free to infer the truth of the charged misconduct.") (citations omitted); *Montoya v. Superior Court*, 173 Ariz. 129, 131 (App. 1992) (noting that, in child custody case, "the trial judge may draw a negative inference from [a party's] invocation of the Fifth Amendment").

Appellants assert that a court may not "draw an adverse inference" from a party's invocation of the right against self-incrimination "if there is not sufficient independent evidence to establish the fact about which the party refuses to testify." O.B. at p. 26. In support of this assertion, Appellants cite Federal case law from various circuits, including the Ninth Circuit. *See id., citing Doe ex rel. Rudy-Glanzer v. Glanzer*, 232 F.3d 1258 (9th Cir. 2000); *State Farm Life Ins. Co. v. Gutterman*, 896 F.2d 116 (5th Cir. 1990), and *Prudential Ins. Co. of Am. v. Thomas*, 2018 WL 3586439 (D.Ariz., July 26, 2018).

Federal courts have not, however, uniformly adopted the principle that an adverse inference may not be drawn from a witness's refusal to answer questions absent independent corroborating evidence. *See Coquina Inv. v. TD Bank, N.A.*, 760 F.3d 1300, 1313 (11th Cir. 2014) (finding it unnecessary, under the facts of the case, to "decide whether to adopt," "as the law of this Circuit," the principle that adverse inference may be drawn only if supported by corroborating evidence).

The parties have cited no reported Arizona case adopting this principle, and the Court is aware of none. On the contrary, Arizona courts holding that the trier-of-fact may draw an adverse inference from the invocation of the right against self-incrimination have not indicated that the availability of such an inference is dependent on the presence of corroborating evidence. *See Castro*, 222 Ariz. at 53 ¶ 20; *Montoya*, 173 Ariz. at 131. Moreover, to qualify or limit the availability of an adverse inference from a witness's refusal to answer a question would be inconsistent with the United States Supreme Court case law recognizing that "[s]ilence is often evidence of the most persuasive character," *Baxter v. Palmigiano*, 425 U.S. 308, 319 (1976) (citation and internal quotations omitted), and therefore that, "in a civil proceeding," an adverse inference may be drawn from a "refusal to answer questions…without offending the Fifth Amendment." *Ohio Adult Parole Authority v. Woodard*, 523 U.S. 272, 286 (1998). For these reasons, the Court finds the Federal case law cited by Appellants unpersuasive.[4]

Even accepting, however, Appellants' position that no adverse inference may be drawn from a witness's refusal to answer questions absent corroborating evidence of the fact about which the witness refuses to testify, such corroborating evidence is, in fact, present here. Among other things, the adverse inference to be drawn from Kern-Fuller's refusal to answer questions about the existence of a "common enterprise" is corroborated by the undisputed evidence that ULG stood to earn fees as long as the monthly deposits continued to be made into ULG's account for the benefit of the veteran/purchaser. As noted above, this undisputed evidence establishes the requisite "positive correlation between the success of the investor and the success of the promoter." *Daggett*, 152 Ariz. at 565.

[4] The Court also finds unpersuasive Appellants' reliance on Justice Brennan's statement that "compulsion violating the privilege is present in any proceeding, criminal or civil, where a government official puts questions to an individual with the knowledge that the answers might tend to incriminate him." O.B. at p. 27 n. 13, *quoting Baxter*, 425 U.S. at 319 (Brennan, J., concurring in part and dissenting in part). In making this statement, Justice Brennan was not speaking on behalf of the Court, but only for himself and Justice Marshall.

In denying the existence of a "common enterprise," Appellants rely on the decision by the Ninth Circuit Court of Appeals in *Brodt v. Bache & Co., Inc*., 595 F.2d 459 (9th Cir. 1978). *See* O.B. at pp. 14-16. In *Brodt*, the Court considered whether a discretionary commodities trading account is an investment contract. 595 F.2d at 459. In answering that question in the negative, the Court found "vertical commonality" absent because the brokerage house "could reap large commissions for itself" even while "individual accounts" were being "wiped out." *Id*. at 460. In the absence of any "correlation between promoter failure and investor loss," the *Brodt* court concluded, a commodities trading account cannot be considered an investment contract. *Id*.

Brodt is clearly distinguishable. Unlike the circumstances presented in *Brodt*, there is a clear correlation here between the financial fate of the investors and that of Appellants. As Appellee correctly argues, "both the investor's success and ULG's ongoing receipt of fees depended on the veteran continuing to direct the pension or disability payments to ULG's IOLTA account." A.B. at p. 13. The "correlation between promoter failure and investor loss" which was absent in *Brodt, see* 595 F.2d at 460, is, therefore present here. That correlation establishes the requisite vertical commonality. The Court therefore finds that the Commission did not abuse its discretion or commit an error of law in finding that the second prong of the *Howey* test is met.

3. The Commission Did Not Abuse Its Discretion Or Commit an Error of Law in Finding that the Third Prong of the *Howey* Test Was Satisfied.

The parties agree that the third prong of the *Howey* test is met when the efforts made by those other than the investor "are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise." O.B. at p. 17 (citation omitted); A.B. at p. 17 (citations omitted). They disagree, however, on whether these circumstances are present here. According to Appellants, "the escrow services and other tasks handled by" Appellants and others "were routine" tasks that could be performed by "any one of a number of competent managers." O.B. at p. 17. The performance of such routine tasks, they insist, cannot "be said to be essential to the success of" the income stream transactions. *Id*. at p. 18, *citing Foy v. Thorp*, 186 Ariz. 151, 158 (App. 1996). Appellee, by contrast, argues that these circumstances are found here because "the investors' role was completely passive," and they "were relying on ULG" and others "for the investments to succeed." A.B. at p. 23.

The record contains ample evidence to support the Commission's determination that the tasks performed by those other than the investors, including ULG, were more than merely "routine or operational." I.R. A-106, Final Decision, at p. 126. As the Commission correctly points out, "[t]he income stream investments were marketed to potential investors by advertising

the contributions of those involved." *Id*. Among other things, the marketing materials told potential investors that ULG would (1) "provide[] legal, escrow and payment services," (2) "provide[] a credit report and LexisNexis search report of [each] seller," (3) "ensure[] all documentation is complete," (4) "prepare[] and file[] a UCC-1 to perfect the investor's security interest," and (5) "process[] monthly payments through the law firm's trust accounts." *Id*. *See also* I.R. C-76, FPD Brochure entitled "Structured Assets Buyer's Guide," at p. ACC000347 ("To further protect Buyers, we engage independent counsel through [ULG] to review all of the supporting documentation…to ensure the due diligence process is completed as set out in the Buyer's Purchase Assistance Agreement. Additionally, the utilization of ULG for closing the transactions and servicing the ongoing payments ensures a Buyer's funds are always in the hands of an insured escrow agent."); *id*. at p. ACC000350 ("Funds escrowed with ULG are held in an IOLTA account (Interest on Lawyers Trust Account) therefore legally segregated from the firm's operating account; and for further protection ULG maintains Lawyers' Professional Responsibility Liability insurance."); I.R. C-80, Brochure entitled "Structured Income Assets Executive Summary presented by Strategic Marketing Innovators ("SMI"), at p. ACC000330 ("[SMI] engages [ULG] to ensure the documentation for this transaction is accurate and complete. ULG provides Seller's background and history and credit report to both SMI and the Buyer for review, prior to the Buyer authorizing the completion of this transaction.").

Kern-Fuller herself identified the critical services performed by ULG in a September 11, 2012 email in which she told Gamber,

> Once the closing book is provided to ULG, we will review the documentation, make contact with the Pension company to verify the income stream, and then assure that the Buyer has received the closing book and either a) signed the acceptance; or b) that the three days have elapsed since they received it…Once these items are in order, *the case will then be approved by ULG to* "*close*."

I.R. C-204, September 11, 2012 email from Kern-Fuller to Gamber, at p. ACC003093 (emphasis added).

Moreover, evidence in the record supports the Commission's determination that the investors' role in the income stream investments was passive. I.R. A-106, Final Decision, at p. 127. When, for example, investment advisor Andy Smith ("Smith"), who sold BAIC and SoBell income stream investments to clients, was asked what his clients had to do "in order to generate" a return "other than invest the money," Smith replied, "Nothing." I.R. B-4, Hearing Transcript, at pp. 321, 332, 344.

The lack of any evidence that any investor performed any services in an effort to generate the hoped-for profits from the transactions supports the Commission's determination that the income stream investment is an investment contract. *See Rose v. Dobras*, 128 Ariz. 209, 213 (App. 1981) ("[W]hen an investor is relatively uninformed and then turns over [his] money to others, essentially depending upon their representations and their honesty and skill in managing it, the transaction is generally considered to be an investment contract.") (citation and internal quotations omitted). The Court therefore finds that the Commission did not abuse its discretion or commit an error of law in finding that the third prong of the *Howey* test is met.

For the foregoing reasons, the Court finds that substantial evidence supports the Commission's determination that the *Howey* test is satisfied and that the income stream investments are investment contracts, and therefore constitute "securities."

B. The Commission Did Not Commit an Error of Law, or Abuse Its Discretion, in Determining that the Investments Were Not Exempt Pursuant to the Arizona Securities Act.

Appellants argue in the alternative that, if the income stream investments are securities, they are exempt from registration requirements. O.B. at p. 19. In support of their position, Appellants argue, first, that the transactions did "not involve any public offering." *Id*. *See also* A.R.S. § 44-1844(A)(1) (establishing exemption for "[t]ransactions by an issuer not involving any public offering"). In response, Appellee maintains that the Commission correctly determined that "Appellants failed to prove the applicability of" of the "non-public offering" exemption. A.B. at p. 29.

Arizona courts have found Federal case law instructive in interpreting A.R.S. 44-1844(A)(1). *See Wales v. Ariz. Corp. Comm'n*, 249 Ariz. 263, 270 ¶ 30 (App. 2020). Federal case law holds that the test for a non-public offering under Federal securities law "focus[es] upon: (1) the number of offerees, (2) the sophistication of the offerees, (3) the size and manner of the offering, and (4) the relationship of the offerees to the issuer." *S.E.C. v. Murphy*, 626 F.2d 633, 644-45 (9th Cir. 1980) (citations omitted). Moreover, "[t]he party claiming the exemption must show that it is met not only with respect to each purchaser, but also with respect to each offeree." *Id*. To establish this exemption, a party must come forward with "evidence of the exact number and identity of all offerees[.]" *Western Fed. Corp. v. Erickson*, 739 F.2d 1439, 1442 (9th Cir. 1984).

The burden of proof of establishing an exemption is on the party asserting it. A.R.S. § 44-2033. Here, the record amply supports the Commission's determination that Appellants "have

not presented adequate evidence to meet their burden of proof to establish applicability of the Non-Public Offering Exemption." I.R. A-106, Final Decision, at p. 131. As the Commission correctly noted, "[t]he record does not reveal the number, identity, or the sophistication of all offerees of the income stream investments at issue because there has been no evidence presented that these particular income stream investments were not offered to others prior to being sold to the investors." I.R. A-106, Final Decision, at p. 130. The absence of such evidence is fatal to Appellants' claim that the transactions at issue qualify for a "non-public offering" exemption.

In support of their position regarding the purported sophistication of the investors, Appellants argue that "[a]ll the Buyers here had professional advice from" others, such as Smith or insurance producer Joseph DeSimone ("DeSimone"),[5] and the "knowledge and business experience" of these advisors should be "imputed" to the investors for purposes of assessing the investors' degree of sophistication. O.B. at pp. 19, 20. *See also id*. at p. 8 ("All Buyers had professional advice…and therefore each with their professional advisor had the knowledge and experience in financial and business matters that made them capable of evaluating the merits and risks of the Transactions."); Appellants' Reply Brief ("Reply Brief" or "R.B.") at p. 13 ("Under…Arizona law, any available information the professional advisor-representatives could have accessed is imputed to their clients.").

This argument is unpersuasive, for two reasons.

First, this argument assumes, in the absence of evidence, that the income stream investments were not offered to any prospective investors other than the ones who ultimately purchased them. The Commission saw no basis for this assumption, and neither does the Court. *See* I.R. A-106, Final Decision, at p. 130 ("[T]here has been no evidence presented that these particular income stream investments were not offered to others prior to being sold to the investors.").

Second, the argument that investors' consultation with advisors somehow demonstrates the investors' sophistication under an "imputed knowledge" theory turns applicable case law on its head. As the Ninth Circuit has made clear, the fact that investors felt the need to seek out third parties for advice on investment transactions is proof not of the investors' *sophistication,* but of their *lack of sophistication*. *See Murphy*, 626 F.2d at 646 (promoter's statement "that 60 percent of the investors used offeree representatives suggests at least that the majority of the

[5] DeSimone, an insurance agent, sold FPD's income stream investments to clients. *See* I.R. B-5, Hearing Transcript, at pp. 524-25, 527.

purchasers…lacked the sort of business acumen necessary to qualify as sophisticated investors.").

In further support of their position that the income stream investments were exempt, Appellants argue, in a cursory manner, that, "due to the small size and single transaction between each Buyer and Seller, each Transaction would…have satisfied the requirements of Reg D and AZ Reg D." O.B. at p. 20.

An exemption under "Regulation D," 17 C.F.R. §§ 230.500 – 230.508, and its Arizona counterpart, A.A.C. R14-4-126, is conditioned upon the satisfaction of certain requirements regarding integration of sales, disclosure requirements, limitations on the manner of offering, and limitations on resale. *See* 17 C.F.R. §§ 230.502, 230.506(b)(1); Ariz. Admin. Code R14-4-126(C). In their Opening Brief, Appellants address none of these requirements. *See generally* O.B. They have therefore failed to meaningfully develop this argument, and so the Court will not consider it. *See State v. Johnson*, 247 Ariz. 166, 180 ¶ 13 (2019). Instead, the Court agrees with, and adopts, the reasoning the Commission aptly set forth for rejecting Appellant's position on this point:

> [Appellants] make no assertion as to specifically which of the Regulation D rules, and Arizona counterparts, create an exemption for the income stream investments. [Appellants] make no contentions and cite no evidence as to how they believe the income stream investments satisfy information requirements, limitations on the manner of offering, or limitations on resale.

A-106, Final Decision, at p. 132. The Court finds that substantial evidence supports the Commission's determination that Appellants "have not presented sufficient evidence to meet their burden to establish the applicability of an exemption under Regulation D and the corresponding Arizona rules." *Id*.

C. The Commission Did Not Commit an Error of Law, or Abuse its Discretion, in Determining that Appellants "Participated in and Induced" the Unlawful Sale of Securities.

A.R.S. § 44-2003(A) provides for joint and several liability against "any person…who made, participated in or induced the unlawful sale or purchase" of securities. In its Final Decision, the Commission determined that Appellants both "participated in" and "induced" the unlawful sale of securities within the meaning of A.R.S. § 44-2003(A). I.R. A-106, Final

Decision, at pp. 143-44. In their Opening Brief, Appellants challenge the Commission's determination.

In support of their challenge, Appellants argue, first, that they cannot possibly have participated in or induced the unlawful sale of securities because the income stream investments either "are not 'securities' under the ASA" or, if they are, the investments "would have been exempt under the ASA." O.B. at p. 22. For the reasons discussed above, the Court rejects Appellants' contention that the Commission erred in determining that the income stream investments were non-exempt securities.

Appellants go on to argue that they cannot be said to have "participated in" or "induced" the income stream investments because they "had no dealings whatsoever with any Sellers, Buyers, or any of their professional advisor-representatives prior to their entering into" the income stream investments. O.B. at p. 22. All they did, they insist, was "perform[] professional services for a fee," and "performing professional services…without actively soliciting a purchase of the alleged underlying securities" is insufficient to support "liability under A.R.S. § 44-2003(A)." *Id*. at pp. 23, 25. *See also* R.B. at p. 14 ("ULG had no dealings whatsoever with any Seller, Buyer, or any Buyer's professional advisor-representatives prior to a Buyer entering into a Transaction.").

As Appellee correctly argues, however, the record contains evidence that ULG had a far greater role in the income stream investments than merely providing professional services for a fee. On the contrary, Kern-Fuller herself admitted that ULG played a critical decision-making role in essentially "vetting" each income stream transaction before it was permitted to close. In a September 11, 2012 email, Kern-Fuller described ULG's role as to "approve[]" each income stream transaction after first "review[ing] the documentation" and "mak[ing] contact with the Pension company to verify the income stream." I.R. C-204, September 11, 2012 email from Kern-Fuller, at p. ACC003093.[6]

Further evidence of the centrality of Appellants' role in effectuating and enforcing the income stream investment transactions is found in the fact that the relevant documents in the

[6] *See* I.R. C-204, September 11, 2012 email from Kern-Fuller to Gamber, at p. ACC003093 ("Once the closing book is provided to ULG, we will review the documentation, make contact with the Pension company to verify the income stream, and then assure that the Buyer has received the closing book and either a) signed the acceptance; or b) that the three days have elapsed since they received it…Once these items are in order, the case will then be approved by ULG to 'close'.").

Closing Books provide that the agreements were to be construed in accordance with the law of Appellants' home state of South Carolina, and that the venue for any legal proceeding involving such transactions was to be Greenville County, South Carolina.[7] *See, e.g.*, I.R. C-258, Sales Assistance Agreement, at p. ACC004382 ("This Agreement shall be construed according to the laws of the State of South Carolina," and "[t]he Seller agrees to personal jurisdiction in Greenville County, South Carolina and for venue in any proceeding relating to this agreement to be in…Greenville County, South Carolina."). *Accord* I.R. C-24, Sales Assistance Agreement, at p. ACC000929; I.R. C-258, Contract for Sale of Payments, at p. ACC004390; I.R. C-259, Sales Assistance Agreement, at p. ACC004437; I.R. C-259, Contract for Sale of Payments, at p. ACC004453.

Further evidence of Appellants' active role in the income stream investments is found in the fact that ULG enforced the income stream investment agreements by bringing and threatening to bring legal action against veteran sellers who stopped the diversion of their pension and disability payments into ULG's trust account. *See* I.R. C-49, October 12, 2015 Demand Letter from ULG, at p. 1 ("We have not received your monthly deposit from VA for the month of October in the contracted amount of $1100.00. Please note that the redirection of your funds if done intentionally is considered an intentional breach of contract and all legal actions allowable by law will be taken."); I.R. C-52, Undated Email from ULG, at p. 1 ("We received your deposit for 9/1/2014 from VA but it was short in the amount of $599.10. The redirection of your funds if done intentionally is considered an intentional breach of contract and all legal actions allowable by law will be taken.); I.R. C-53, June 7, 2016 Demand Letter from ULG, at p. 1 ("We have not received your monthly deposit from VA for the month of June in the contracted amount of $544.71. Please note that the redirection of your funds if done intentionally is considered an intentional breach of contract and all legal actions allowable by law will be taken."); I.R. C-149, Complaint signed by Kern-Fuller in *Cole v. Simpson,* South Carolina Court of Common Pleas Case No. 2017-CP-230560, p. 2 ¶ 6, pp. 4-7 ¶¶ 18-48 (asserting various claims arising out of alleged breach of agreement "to sell a series of future payments derived from a guaranteed, life contingent income stream,").

Moreover, as Appellee correctly points out, the marketing materials presented to potential investors emphasized ULG's active role in the transactions, portraying ULG as a virtual guarantor of the security of the investments. A Strategic Marketing Innovators ("SMI") brochure, for example, tells prospective investors that ULG will act as "[t]he Buyer's attorney" in the transaction, listing the services that ULG would perform as follows:

[7] It is undisputed that ULG was located in South Carolina. *See* I.R. C-258, Contract for Sale of Payments, at p. ACC004387.

- "ULG provides a credit report and LexisNexis search report on each individual Seller and provides a transaction summary to the Buyer and SMI for review prior to closing."
- "ULG ensures all documentation is complete and the purchased payments are directed to ULG's Trust Account prior to closing."
- "All Structured Income Asset monthly payments are processed in [ULG's] Trust Accounts."
- "[ULG] prepares and files a UCC-1 against the Seller's purchased income in their state of residence…The intent of this filing is to establish a 'Perfected Security Interest' for the Buyer."

I.R. C-77, SMI Brochure entitled "Structured Income Assets," at pp. 4, 9. Other marketing materials contain representations to the same effect. *See* I.R. C-76, FPD Brochure entitled "Structured Assets Buyer's Guide," at p. ACC000347 ("To further protect Buyers, we engage independent counsel through [ULG] to review all of the supporting documentation…to *ensure* the due diligence process is completed as set out in the Buyer's Purchase Assistance Agreement. Additionally, the utilization of ULG for closing the transactions and servicing the ongoing payments *ensures* a Buyer's funds *are always in the hands of an insured escrow agent*.") (emphasis added); *id*. at p. ACC000349 (stating that certain documents would be provided to the investor at closing "[a]fter ULG has completed its review of the case"); *id*. at p. ACC000350 ("We are proud to have a contractual relationship with [ULG] to perform escrow, servicing, and account management for buyers[.]"); *id*. ("Funds escrowed with ULG are held in an IOLTA account (Interest on Lawyers Trust Account) therefore legally segregated from the firm's operating account; and for further protection ULG maintains Lawyers' Professional Responsibility Liability insurance."); I.R. C-77, SMI brochure entitled "Structured Income Assets," at p. 2 (identifying ULG as "[t]he Buyer's attorney," and stating that ULG "prepares and files a UCC-1 against the Seller's cash flow" to establish "secured creditor status" for investors); I.R. C-80, Brochure entitled "Structured Income Assets Executive Summary presented by [SMI], at p. ACC000330 ("[SMI] engages [ULG] to *ensure* the documentation for this transaction is accurate and complete. ULG provides Seller's background and history and credit report to both SMI and the Buyer for review, prior to the Buyer authorizing the completion of this transaction.") (emphasis added).

Evidence in the record establishes that Appellants' advertised role in the income stream investors did, in fact, influence their decision to invest. Investor Dean Hebb, for example,

testified that the representation that ULG would "prepare[] and file[] a UCC-1 against seller's cash flow to create a first position secured creditor status" had an impact on his decision to invest because it led him to conclude that, because "a law group…is behind this," "it's been vetted." I.R. B-3, Hearing Transcript, at p. 171. He went on that the representation that "[ULG] ensures all documentation is complete" led him to believe "that this is a legal transaction." *Id*. at pp. 172-73. Similarly, Charles Zimmerman, the agent of an investor trust, testified that he understood ULG personnel to be "the coordinators" who represented "all the players," "put the package together," and "had all the bases covered." *Id*. at pp. 411, 413, 414.

Smith, who sold the income stream investments to clients, testified that the representations in marketing materials about ULG's role was "absolutely" important to him. I.R. B-4, Hearing Transcript, at pp. 321, 326. He testified that the fact that the funds were to be maintained in ULG's trust account was "comforting to [him]" since it indicated that ULG was "watching and controlling the flow of funds." *Id*. at p. 334. When asked whether the involvement of a law firm in the income stream transactions "[lent] legitimacy to the investment," Smith replied, "Totally, yes." *Id*. at p. 374. Likewise, DeSimone testified that, in deciding to sell FPD's income stream investment products to clients, "What attracted me was it's working with a law firm that had done extensive due diligence." I.R. B-5, Hearing Transcript, at p. 530. DeSimone went on to state that "[t]he two items that had a great impact" on his decision "to offer this to clients" were "the fact that the funds were" processed through ULG's "IOLTA account, under the supervision of the State Bar of South Carolina," and that ULG's "professional liability insurance was featured as an additional layer of protection" for investors. *Id*. at pp. 534-35.

Appellants argue that they cannot be responsible for the contents of marketing materials provided to prospective investors because, they contend, "there is no evidence whatsoever that ULG knew of" these marketing materials, or that the materials "misrepresented ULG's role and responsibilities" in connection with the income stream investments. O.B. at p. 28. "[U]nder Arizona agency law," they contend, they "are not liable for…alleged…misrepresentations" in marketing materials created and distributed by others. *Id*.

Evidence in the record, however, supports the Commission's determination that "[t]he weight of the evidence establishe[s] that ULG and [Kern-Fuller] were aware of ULG's appearance in promotional materials for the income stream investments." I.R. A-106, Final Decision, at p. 143. Among other things, evidence in the record indicates that Appellants did, in fact, perform the tasks as promised in the marketing materials. *See* I.R. C-204, September 11, 2012 email from Kern-Fuller to Gamber, at p. ACC003093 ("Once the closing book is provided to ULG, we will review the documentation, make contact with the Pension company to verify the income stream, and then assure that the Buyer has received the closing book and either a) signed

the acceptance; or b) that the three days have elapsed since they received it…Once these items are in order, the case will then be approved by ULG to 'close'. The money will be wired from the Buyer to our trust account and should be disbursed back out by the end of the next business day."); I.R. C-287, ULG Legal Services and Fee Agreement with distributors, at p. 1 ("There shall be no costs fronted by the Law Firm. Any costs such as those for UCC filings, recording fees, or overnight fees shall be built into the transactions closing costs and fronted by Client, its seller or buyer."); I.R. C-288, ULG Escrow Services and Fee Agreement with investors providing for ULG to perform escrow services). The fact that Appellants performed as promised in the marketing materials supports the inference that they were aware of the marketing materials' promises.

Further, evidence in the record establishes that Kern-Fuller had a close relationship with the principals of PAC, one of the entities involved in these income stream transactions. Investment advisor Andy Smith testified that he attended a meeting in Dallas in 2015 or 2016 between Appellants and the principals of PAC, and that he was struck by the sight of Kern-Fuller exchanging "hugs" with the PAC representatives. I.R. B-4, Hearing Transcript, at p. 391. "I guess it seems a little odd to me from a professional standpoint," he stated, "but they seemed very close." *Id*. The warm relationship Kern-Fuller exhibited with others involved in the income stream investments supports the inference that they worked together closely.

Appellants' awareness of the contents of the marketing materials may also be inferred from the fact that Kern-Fuller invoked her right against self-incrimination when asked about the issue. *See* I.R. A-106, Final Decision, at p. 96.

Finally, the record contains evidence indicating that Appellants made disclosures to distributors (such as SMI) but not to investors, suggesting an intent to mislead investors by withholding information from them. The Legal Services and Fee Agreement that ULG provided to distributors contains an express disclaimer that neither ULG nor any "member of the firm" were purporting to offer or provide either "securities advice" or "tax advice." I.R. C-287, Legal Services and Fee Agreement – Hourly/Retainer between "Distributor" and "Law Firm," at p. 2 ("Law firm hereby represents that no member of the firm or its staff is competent to provide tax advice, or securities advise [*sic*] to you or your entity. Any questions regarding securities advice or tax advice should be directed to another firm with appropriate tax and/or securities experience."). Significantly, however, while the agreement that ULG provided to investors contains a similar disclaimer regarding *tax advice*, the agreement that ULG provided to investors contains no reference at all to *securities*. *See* I.R. C-288, Escrow Services and Fee Agreement between "Buyer" and "Law Firm," at p. 2 ("Law firm hereby represents that no member of the Law Firm or its staff is competent to provide tax advice to you…[Y]ou should consult an

appropriate tax professional for such advice."). In light of the fact that ULG's agreement with distributors made reference to securities, the omission of any reference to securities in ULG's comparable agreement with investors supports the inference that the omission was intentional, a deliberate omission designed to avoid raising questions in investors' minds that might cause the investors to decide against entering into the transactions. The omission of any reference to securities in ULG's agreement with investors, in other words, supports the Commission's determination that ULG "induced" investors to enter into the income stream transactions.

All of the above evidence, taken together, constitutes more than "substantial evidence" to support the Commission's determination that Appellants both "participated in" and "induced" the sale of non-exempt securities.

In support of their position, Appellants rely on *Standard Chartered PLC v. Price Waterhouse*, 190 Ariz. 6 (App. 1996). O.B. at pp. 22-24. In *Standard Chartered*, the plaintiffs purchased United Bank ("United") after reviewing the bank's financial statements and other documents that had been audited by the accounting firm that performed annual auditing services for United. When the plaintiffs later determined that United's financial statements overstated its value, the plaintiffs brought securities and other claims against the accounting firm, alleging that it "had carelessly carried out the audit of United" and "erroneously approved financial statements that significantly exaggerated the value of United's assets." 190 Ariz. at 15. The *Standard Chartered* court held that the accounting firm "neither 'participated in' nor 'induced' a securities transaction within the meaning of A.R.S. § 44-2003," and therefore that the trial court should have entered judgment in favor of the accounting firm on that claim. *Id*. at 22-23. In so holding, the Court noted that the accounting firm's actions in "issu[ing] audit opinions about United's financial status" was only "tangentially related to" the sale because the accounting firm would have performed the same auditing services even if "no merger or sale [had] been in process." *Id*. at 21. The accounting firm "had no stake in the sale," the Court found, and, instead, "merely provide[d] information" that the plaintiffs took into consideration in closing the sale. *Id*. at 21, 22. Because the accounting firm "neither financially participate[d]" in, "nor promote[d] or solicit[ed] the transaction," the Court concluded, its role was too "remote from the transaction" to support a finding of liability under A.R.S. § 44-2003. *Id*. at 22.

Standard Chartered is inapposite because, as discussed above, Appellants here had a far greater role in the income stream investments than the role of the accounting firm in the *Standard Chartered* plaintiffs' purchase of United. Unlike the work performed by the accounting firm in *Standard Chartered*, which would have been performed whether or not the plaintiffs were considering purchasing United, the work performed by Appellants here was performed solely in connection with the income stream investments. Moreover, unlike the accounting firm

in *Standard Chartered*, which had no financial stake in the sale of United, Appellants here stood to benefit financially from the income stream investments. Finally, unlike the accounting firm in *Standard Chartered*, which "merely provide[d] information," 190 Ariz. at 22, by Kern-Fuller's own admission, Appellants here "approved" the closing of each income stream transaction. *See* I.R. C-204, September 11, 2012 email from Kern-Fuller, at p. ACC003093 ("Once these items are in order, the case will then be approved by ULG to 'close'."). The Court therefore finds that *Standard Chartered* is of no assistance to Appellants.

The Court finds that substantial evidence supports the Commission's determination that Appellants both "participated in" and "induced" the "unlawful sale of securities" within the meaning of A.R.S. § 44-2003(A). I.R. A-106, Final Decision, at p. 144.

D. The Commission Did Not Commit an Error of Law, or Abuse Its Discretion, in Concluding that Appellants Engaged in Fraudulent Practices in Violation of A.R.S. § 44-1991(A).

A.R.S. § 44-1991(A) provides in part that "[i]t is a fraudulent practice and unlawful for a Person," in connection with the sale, or offer to engage in the sale, of securities, to

> 1. [e]mploy any device, scheme or artifice to defraud[;]
>
> 2. [m]ake any untrue statement of material fact, or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading[; or]
>
> 3. [e]ngage in any transaction, practice or course of business which operates or would operate as a fraud or deceit.

A.R.S. § 44-1991(A). In its Final Decision, the Commission found that Appellants had violated all three subsections of this statute. The Commission found that Appellants violated A.R.S. § 44-1991(A)(1) ("Subsection 1") and A.R.S. § 44-1991(A)(3) ("Subsection 3") "through the marketing of ULG's role in the investments," finding that "the marketing of ULG's role deceived the investors into a false sense of the investment's safety." I.R. A-106, Final Decision, at pp. 161-62. The Commission found that Appellants violated A.R.S. § 44-1991(A)(2) ("Subsection 2") by failing to disclose to investors the risk that a court would find the income stream investments to be unenforceable "due to application of the Federal Anti-Assignment Acts," *see* 37 U.S.C. § 701(c) and 38 U.S.C. § 5301(a)(3)(A), and because they failed to disclose material information about others involved in the income stream investments. I.R. A-106, Final

Decision, at pp. 160, 162, 165.[8] Specifically, the Commission found that Appellants failed to disclose investment advisor Smith's poor track record of managing money (as shown by an IRS tax lien against him in excess of $125,000) and cease-and-desist orders that had been entered in other states against Gamber and/or his companies in connection with income stream investments "similar to the ones in this matter." *Id*. at pp. 162, 165. The Commission found "the orders against" Gamber and/or his companies "and the tax lien against" Smith to "constitute information that would be considered material to a reasonable investor." *Id*. at p. 164.

Appellants challenge these findings. In support of their position, Appellants first reiterate their arguments that the income stream investments "are not securities under the ASA" and they did "not 'participate[] in and induce[]' their sales under Arizona law." O.B. at p. 36. The Court has already rejected these arguments for the reasons set forth above, and need not address them further.

Appellants go on to argue that the evidence does not establish that they "employed any device, scheme or artifice to defraud," "made any untrue statements" or omissions of "material fact," or "engaged in any [fraudulent] transaction, practice or course of business." O.B. at pp. 36-37. They justify this assertion by contending, first, that "the Commission correctly ruled" that the income stream investments "do not," in fact, "constitute unlawful assignments" as the Division had alleged. *Id*. at p. 37.

In the Court's view, Appellants misinterpret the Final Decision, which contains no such ruling. In its Final Decision, the Commission concluded that "[t]he Division has not met its burden of proof to show that the income stream investments violate the Federal Anti-Assignment Acts." I.R. A-106, Final Decision, at p. 160. A finding that the Division failed to meet its burden of proving that the transactions violate anti-assignment statutes does not constitute a finding that the transactions do not violate those statutes. Finding that an allegation has not been proven true is not the same as finding that the allegation is false.

Noting that the Commission based its determination that Appellants violated A.R.S. § 44-1991(A) in part on representations in the marketing materials about ULG's role in the investments, Appellants reiterate their argument that the marketing materials "should not be

[8] 37 U.S.C. § 701(c) provides that "[a]n enlisted member of the Army, Navy, Air Force, Marine Corps, or Space Force may not assign the member's pay, and if the member does so, the assignment is void." 38 U.S.C. § 5301(a)(3)(A) provides that, with limited exceptions, an agreement by which a person "acquires for consideration" another person's right to receive military pension or similar benefits "shall be deemed to be an assignment and is prohibited."

considered or given any weight" because there is, purportedly, no "substantial evidence in the record" to indicate that Appellants were aware of the contents of those materials. O.B. at pp. 25, 37. The Court rejects this contention, for the reasons set forth above.

Appellants go on to argue that "the Transaction documents adequately disclosed the risks inherent in the Transactions and did not mislead regarding…the risk of nonpayment" by the veteran/seller. O.B. at p. 37. As Appellee correctly notes in its Answering Brief, however, long before the income stream investments here were sold, numerous courts had held similar transactions to be unenforceable as violative of Federal anti-assignment statutes. *See* A.B. at p. 33 and cases cited therein. The Disclosure of Risks Statement that was provided to investors contains no reference to any of these court decisions. On the contrary, the Disclosure of Risks Statement states only that "there is no assurance" that a court would "permit the enforcement of payment rights under this arrangement." I.R. C-118, Disclosure of Risks Statement, at p. ACC003457. The Disclosure of Risks Statement notes that some courts have upheld the enforceability of these transactions, but fails to mention the numerous other court decisions in which transactions of this type were held to be unenforceable. *Id*. (stating that "certain courts have held transactions of this nature to be enforceable even in the presence of an anti-assignment clause."). *See also* I.R. C-119, Disclosure of Risks Statement, at p. ACC003536 (same); I.R. C-121, Disclosure of Risks Statement, at p. ACC005303 (same); I.R. C-123, Disclosure of Risks Statement, at p. ACC000467 (same). The Disclosure of Risks Statement thus presented the risk of an adverse court decision to be nothing more than a hypothetical future possibility. The Court thus agrees with Appellee that the statement in the Disclosure of Risks Statement that "certain courts" have found such transactions "to be enforceable," with no reference to the contrary holdings of other courts, constitutes "a misleading half-truth." A.B. at p. 33.

Likewise, the Disclosure of Risks Statement informs prospective investors that "[n]on-receipt of Payments could occur for a number of reasons," identifying such possible "reasons" as "administrative delays," "the death of" the seller, and "an intentional payment diversion." I.R. C-118, Disclosure of Risks Statement, at p. ACC003457. *See also* I.R. C-119, Disclosure of Risks Statement, at p. ACC003536 (same); I.R. C-121, Disclosure of Risks Statement, at p. ACC005303 (same); I.R. C-123, Disclosure of Risks Statement, at p. ACC000467 (same). The Disclosure of Risks Statement does not, however, include an adverse court ruling among its list of possible reasons for a buyer's non-receipt of payments. The Court agrees with Appellee that the disclosure about possible causes for the non-receipt of payment is "misleading" in light of "the failure to disclose that the Federal Anti-Assignment Acts might prohibit the sale or assignment of those payments in the first place." A.B. at p. 33.

In asserting that the "Buyers were not deceived," Appellants argue that ULG did, in fact, serve, as promised, "as the Escrow Company after a Transaction's closing." O.B. at p. 37. As noted above, however, ULG's advertised role was far more than merely the provision of escrow services. Ample record evidence supports the Commission's determination that "the description of ULG's role in the marketing materials gave confidence to investors that induced the unlawful sales of these securities." I.R. A-106, Final Decision, at p. 161. *See* I.R. B-3, Hearing Transcript, at p. 171 (Investor Dean Hebb testifying that ULG's advertised role in the transactions led him to conclude that, because "a law group…is behind this," "it's been vetted"); *id*. at pp. 411, 413, 414 (Investor's agent Charles Zimmerman testifying that he was led to believe that ULG personnel were "the coordinators" who represented "all the players," "put the package together," and "had all the bases covered"); I.R. B-4, Hearing Transcript, at pp. 321, 326 (Investment advisor Smith testifying that the representations in marketing materials about ULG's role was "absolutely" important to him); *id*. at p. 530 (Insurance producer DeSimone testifying that, in deciding to sell FPD's income stream investment products to clients, "What attracted me was it's working with a law firm that had done extensive due diligence.").

Appellants further argue that any misrepresentations in the marketing materials could not be said to have "assumed actual significance" in the investors' deliberations, and therefore could not be said to have been "material," because, among other reasons, the investors had the opportunity to "review[]" the relevant documents "along with their professional advisor-representatives." O.B. at pp. 37, 38.

Appellants' assertion on this point amounts to the contention that misrepresentations in the marketing materials were not material because the investors had access to other advice, and so should have known better than to believe the misrepresentations in the marketing materials. Not surprisingly, case law does not support this argument. *See Trimble v. American Sav. Life Ins. Co*., 152 Ariz. 548, 553 (App. 1986) (rejecting as "unfounded" securities fraud defendants' argument "that investors must act with due diligence and that they would have discovered any misrepresentations had they so acted"; "The statutes do not require investors to act with due diligence…To the contrary, defendants have an affirmative duty not to mislead potential investors.").

Subsection 2 prohibits false statements or omissions of "material fact." A.R.S. § 44-1991(A)(2). Materiality is measured by an objective standard, and "[t]he requirement of materiality is satisfied by a showing of substantial likelihood that, under all the circumstances, the misstated or omitted fact would have assumed actual significance in the deliberations of a reasonable buyer." *Hirsch*, 237 Ariz. at 463 ¶ 27 (emphasis, citations, and internal quotations omitted). There can be no doubt of the materiality of the fact that other courts have found income

stream investment agreements unenforceable, and the risk that the income stream investments at issue here would likely be held unenforceable. Likewise, there can be no doubt of the materiality of the fact that authorities in multiple other states had entered cease-and-desist orders against Gamber based on income stream investments like those at issue here.

Appellants argue that the cease-and-desist orders against Gamber need not have been disclosed because they were entered "either [by] default or consent," and so were not the result of "adversarial litigation of the legal and factual issues." O.B. at p. 38. "[N]on-litigated unopposed orders" entered by agencies of "other states" are "irrelevant" and "unreliable," particularly since "ULG was not made a party to…any of those actions" and so had "no opportunity to defend itself." *Id*. at p. 39. In any event, Appellants suggest, the existence of such orders is information in the public domain, and so need not be disclosed anyway. *Id*. at pp. 39-40. "[C]ontrary to the [Final Decision]," Appellants maintain, "there is legal authority that the securities laws require disclosure only of information that is not otherwise in the public domain." *Id*. at p. 40, *citing In re Allstate Life Ins. Co. Litig*., 2013 WL 5161688 (D.Ariz., Sept. 13, 2013).

Appellants' contention that they had no obligation to disclose the cease-and-desist orders from other states is contrary to case law. *See State ex rel. Corbin v. Goodrich*, 151 Ariz. 118, 126 (App. 1986) (affirming trial court's determination that defendants who offered and sold certain securities "omitted…material facts," and finding that the issuance of cease-and-desist orders "by the states of Minnesota, Iowa, Missouri and Massachusetts" to be a fact that "would have been…important to an investor's decision"). *See also S.E.C. v. Merchant Capital, LLC*, 483 F.3d 747, 771 (11th Cir. 2007) ("The existence of a state cease and desist order against identical instruments is clearly relevant to a reasonable investor, who is naturally interested in whether management is following the law in marketing the securities."); *S.E.C. v. Paro*, 468 F.Supp. 635, 646 (N.D.N.Y. 1979) ("[I]nvestors would have been…dubious" of the investment "if they had been apprised of the cease and desist orders and injunctions which had been issued against [defendants'] predecessor by the state and federal courts. The materiality of these omissions is therefore manifest[.]").

Similarly, there can be no doubt of the materiality of the existence of a $125,000 tax lien against Smith. As Appellee correctly argues, "a promoter's failed financial dealings, such as bankruptcies and unpaid judgments or liens, are also material facts that must be disclosed." A.B. at p. 36. *See, e.g., Merchant Capital*, 483 F.3d at 771 ("Knowledge of [defendant's] previous bankruptcy clearly would have been helpful to a reasonable investor assessing the quality and extent of [his] experience."); *Direct Benefits, LLC v. TAC Financial, Inc*., 2020 WL 2769982 at *16 (D.Md., May 28, 2020) ("As several courts have held, personal bankruptcies of corporate directors can be material in evaluating securities transactions.") (citing cases).

In support of their contention that "the securities laws require disclosure only of information that is not otherwise in the public domain," O.B. at p. 40, Appellants rely on *In re Allstate Life Ins. Co. Litig*. *In re Allstate,* however, is distinguishable. In that case, the Court held that a law firm could not be said to have violated Subsection 2 by failing to "disclose[] Arizona budgetary laws" in preparing documents relating to the offer and sale of municipal revenue bonds. 2013 WL 5161688 at *27. In stating that "[t]he securities laws require disclosure only of information that is not otherwise in the public domain," the *In re Allstate* court quoted case law holding that "[s]ellers of securities need not 'disclose' the statutes at large of the states in which they operate." *Id*. at *26, *quoting Acme Propane, Inc. v. Tenexco, Inc*., 844 F.2d 1317, 1323 (7th Cir. 1988). This principle is inapplicable here, however, because, although state statutes are online and readily accessible to the public, there is no evidence in the record to indicate that the same is true of the cease-and-desist orders against Gamber or the tax lien against Smith. In any event, as the Commission correctly found, "there is no controlling legal authority" establishing "a public domain exception…to a violation of A.R.S. § 44-1991(A)(2)." I.R. A-106, Final Decision, at p. 165.

The Court finds that substantial evidence supports the Commission's determination that Appellants engaged in fraudulent practices in violation of Subsection 1, Subsection 2, and Subsection 3 of A.R.S. § 44-1991(A). I.R. A-106, Final Decision, at pp. 160-62, 165.

E. The Commission Did Not Commit an Error of Law, or Abuse Its Discretion, in Concluding that Appellants Violated A.R.S. §§ 44-1841 and -1842.

A.R.S. § 44-1841 prohibits the "[sale] or offer for sale" of unregistered non-exempt securities "within or from this state." A.R.S. § 44-1842 prohibits unregistered dealers or salespeople from "sell[ing]," "purchas[ing]," or "offer[ing] to sell or buy" non-exempt securities "within or from this state." In its Final Decision, the Commission determined that Appellants, who are not registered as securities dealers or salespeople, "committed 59 violations of A.R.S. §§ 44-1841 and 44-1842 from the sales of the income stream investments." I.R. A-106, Final Decision, at p. 146.

In their Opening Brief, Appellants challenge this determination. In support of their position, they simply point to arguments that they made in connection with other issues. O.B. at pp. 35-36. Specifically, Appellants re-urge their arguments that the income stream investments are not securities; that, if they are securities, they are exempt from registration; and they did not participate in or induce their sales. *Id*. at p. 35. Because the Commission's contrary findings "are

not supported by substantial evidence" and "are errors of law and abuses of discretion," they conclude, they cannot have "committed any such violations." *Id*. at pp. 35-36.

For the reasons set forth elsewhere in this ruling, the Court rejects the premise of Appellants' argument on this point. The Court finds, in other words, that the Commission did not err or abuse its discretion in determining that the income stream investments are non-exempt securities and in determining that Appellants participated in and induced the sales. Moreover, Appellants do not dispute that the investments were offered or sold "within or from" Arizona as is required to establish a violation of A.R.S. § 44-1841 or A.R.S. § 44-1842. *See generally* O.B. The Court therefore rejects Appellants' argument that the Commission's determination that they violated A.R.S. §§ 44-1841 and -1842 should be set aside because, purportedly, the Commission's underlying findings in support of that determination should be set aside as well.

F. The Commission Did Not Commit an Error of Law, or Abuse Its Discretion, in Determining that Appellants Did Not Act in the Ordinary Course of Their Professional Capacity in Connection with the Pension Income Stream Transactions.

A.R.S. § 44-2003(A) establishes what is sometimes referred to as a "safe harbor" for professionals acting in their professional capacity, providing in part that "[n]o person shall be deemed to have participated in any sale or purchase solely by reason of having acted in the ordinary course of that person's professional capacity in connection with that sale or purchase." In its Final Decision, the Commission found that Appellants "failed to meet their burden of proof to establish the applicability of the professional capacity defense." I.R. A-106, Final Decision, at p. 171. In so finding, the Commission noted, *inter alia*, that Appellants "induced as well as participated in the unlawful sale of securities," and that their inducement of those sales "place[s] them outside the scope of the [professional capacity] defense." *Id*.

Appellants challenge the Commission's determination, asserting that "the Commission's finding that ULG did not act in the ordinary course of their professional capacity…is not supported by substantial evidence in the record, is an error of law and abuse of discretion." O.B. at p. 35. Appellants do not dispute that, by its terms, A.R.S. § 44-2003(A) establishes a defense only for *participation*, not *inducement*. *See* A.R.S. § 44-2003(A). *See also Grand v. Nacchio*, 225 Ariz. 171, 176 ¶ 23 (2010) (stating that, had A.R.S. § 44-2003(A) been intended to create an exemption for "inducement liability," "the legislature…surely would have said so."). Instead, they argue that the Commission erred in finding that they "induced" the unlawful sale of securities. O.B. at pp. 34-35. Because, for the reasons set forth above, the Court affirms the Final Decision's determination that Appellants "induced" the unlawful sales, the Court rejects Appellant's argument on this point.

In support of its determination that the "safe harbor" defense established by A.R.S. § 44-2003(A) does not apply here, the Commission observed that "[p]rofessionals who knowingly or recklessly violate the standards of their profession when advising their clients are not providing legitimate professional advice for which statutory protection should exist." I.R. A-106, Final Decision, at p. 165, *quoting* Richard G. Himelrick, *Arizona Securities Law: Civil Liability, Defenses and Remedies* at p. 271, § 5.1.5 (5th ed. 2018). The Commission further found that Appellants did, in fact, recklessly violate the standards of their profession, and therefore they cannot claim the protection of A.R.S. § 44-2003(A). I.R. A-106, Final Decision, at p. 171. In so finding, the Commission relied on the opinions of John Freeman ("Freeman"), a South Carolina attorney and law professor who was called as an expert witness by the Division. *See id*. ("[W]e find the testimony of [Freeman] established that [Appellants] acted in a reckless, unprofessional manner that violated the applicable ethical rules for attorneys in South Carolina."). Freeman prepared a report in which he opined that Kern-Fuller violated rules of professional conduct applicable to South Carolina lawyers by, *inter alia*, purporting to simultaneously represent clients with potentially conflicting interests "without any effective conflict of interest waivers being obtained" and by failing to adequately advise clients by providing "seriously deficient disclosures" to "the investors who paid for those investments." I.R. C-47, Expert Report of Professor John P. Freeman ("Freeman Report"), at pp. 11, 12. Freeman further opined that "unethical behavior is not conduct in the ordinary course of a lawyer's professional capacity." *Id*. at p. 8 (citation and internal quotations omitted). Appellants' violations of professional ethics, in other words, render the "professional capacity" defense inapplicable. *See id*. At the administrative hearing, Freeman offered testimony to the same effect. *See, e.g.*, I.R. B-6, Hearing Transcript, at pp. 820-27, 832-33, 836-40.

Appellants argue that the Commission improperly relied on Freeman's testimony because, they contend, Freeman's testimony was "based on assumptions and conjecture that are sheer speculation and not supported by competent evidence in the record." O.B. at p. 29. As an example of Freeman's "wrong assumptions," Appellants point to Freeman's assumptions "that the transactions at issue did involve the unlawful sale or purchase of a security and were wrongful fraudulent schemes." *Id*. at p. 30.

In its Final Decision, the Commission rejected Appellants' challenge to the purported "wrong assumptions" on which Freeman's opinions are based. Noting that Freeman's assumptions "that the income stream investments were sold fraudulently and in violation of securities law," the Commission found that "[t]hese assumptions are not speculation." I.R. A-106, Final Decision, at p. 169. On the contrary, the Commission itself "reached these same conclusions based on the evidence in the record." *Id*.

For the reasons set forth above, this Court finds that substantial evidence in the record supports the Commission's determinations that the transactions at issue involved the unlawful sale of securities and were undertaken fraudulently. The Court therefore rejects Appellants' argument that Freeman's opinions are based on "wrong assumptions." Instead, the Court finds, as the Commission did, that substantial evidence in the record bears out the assumptions on which Freeman's opinions were based.

In support of their argument that the Commission improperly considered Freeman's opinions, Appellants assert that Freeman's opinions amount to "legal conclusions" that are "questions of law…for the court and not expert opinion." O.B. at p. 33. The Court finds this assertion unpersuasive; "[a]n opinion is not objectionable just because it embraces an ultimate issue." Ariz.R.Evid. 704(a).

In further support of their argument that the Commission improperly relied on Freeman's testimony, Appellants contend that Freeman's opinions were based on unreliable and inadmissible hearsay. O.B. at pp. 30-32. They contend that Freeman's opinions are "based on testimony" given by Gamber, Plant, and others in unrelated proceedings to which Appellants were not parties and so had no "right of cross-examination." *Id*. at pp. 30-31. They concede that an expert witness may rely on "hearsay evidence that is reliable, probative, relevant, and material," but insist that the third party testimony on which Freeman relied "is none of these." *Id*. at p. 31. Accordingly, they conclude, Freeman's testimony was "not reliable, probative, relevant, or material," and "should not" have been "considered or given any weight." *Id*. at p. 33.

Because, as Appellee asserts (and Appellants do not dispute), Appellants stipulated to the admission of the report prepared by Freeman at the administrative hearing, *see* I.R. B-3, Hearing Transcript, at pp. 78-80, the Court finds that Appellants waived any objection to the Commission's considering Freeman's opinions. *See Estate of Reinen v. Northern Ariz. Orthopedics, Ltd*., 198 Ariz. 283, 286-87 ¶ 9 (2000).

Moreover, it is not the case that Freeman's opinions as set forth in his written report and his testimony are based exclusively on testimony provided by Gamber, Plant, and others in separate proceedings. On the contrary, Freeman's opinions are based in large part on evidence whose admissibility in these proceedings is not disputed, including documents taken from the Closing Books that were exhibits in the administrative proceedings, marketing materials presented to potential investors, and pleadings filed in civil litigation against Appellants. I.R. C-47, Freeman Report, at pp. 5, 6. In opining, for example, that Appellants engaged in "material deceptions," Freeman cited, *inter alia*, unreconcilable inconsistencies in litigation positions taken

by Appellants. *Id*. at pp. 12. Freeman cited *Lyons v. BAIC, et al*., a lawsuit filed against Kern-Fuller, ULG, and others in federal district court in South Carolina in 2018. Fuller explained that the attorney for Kern-Fuller and ULG in that case argued "in open court" that "the military pension benefits sold by the three plaintiffs in that case were not covered by the anti-assignment statute" because the investors/buyers "had no legal right to the money." *Id*. Freeman quoted from a portion of a transcript of a hearing in that case in which the attorney for Kern-Fuller and ULG told the district court judge that the income stream transactions could not constitute "assignments" because they are "not enforceable" and the buyers "have no rights." *Id*. at p. 13. Freeman observed that, despite asserting, in *Lyons v. BAIC*, that the income stream transactions are not enforceable, Kern-Fuller and ULG filed suit against "pension benefit sellers" in other cases to enforce such transactions. *Id*. at p. 14, *citing Life Funding Options v. Blunt*, South Carolina Federal District Court Case No. 6:18-944-DCC-KFM *and Cole v. Simpson*, Greenville County Court of Common Pleas Case No. 2017-CP-23-00560. "The in-court admission by counsel for Kern-Fuller and ULG that...the investment contracts are not enforceable," Freeman opined, "do not square with" the actions of Kern-Fuller and ULG in "suing pension benefit sellers to collect on those same contracts." I.R. C-47, Freeman Report, at pp. 13, 14.

Similarly, in opining that Appellants violated applicable ethical rules by purporting to represent parties with potentially conflicting interests without "any effective conflict of interest waivers being obtained," Freeman cited to the provision of the marketing materials which state that ULG would act "for the exclusive benefit of the Buyer and [the distributor]." I.R. C-47, Freeman Report, at pp. 9, 11. *See also* I.R. C-78, SMI brochure entitled "Structured Income Assets," at p. ACC000336. Freeman stated that, in view of "the different, conflicting interests existing between a distributor and a buyer," the reference to "*the exclusive benefit of both*" the distributor and the buyer in these promotional materials was "an oxymoron." I.R. C-47, Freeman Report, at p. 11 (emphasis added).

These and other specific examples given by Freeman to support his opinions that Appellants engaged in ethical violations are clearly based on evidence that was admissible in this case. These examples thus refute Appellants' contention that Freeman's opinions are improperly based on inadmissible evidence. *See generally* O.B. at p. 30.

In any event, Rule 702 of the Arizona Rules of Evidence permits an expert to base his or her opinion on hearsay or other inadmissible evidence as long as the information of the type that experts in the field reasonably rely upon. Ariz.R.Evid. 702. Here, Freeman has stated under oath that "the facts and the data" that he "reviewed" in forming his opinions "are standard for an expert…to review" in "a case like this" to "offer an opinion on the conduct of professional participants." I.R. B-6, Hearing Transcript, at p. 797. The Court therefore finds that the

Commission correctly determined that Freeman's opinions are admissible under the Arizona Rules of Evidence. I.R. A-106, Final Decision, at p. 169.

The Court further finds that Freeman's opinions, along with the evidence of Appellants' securities violations discussed above, provide ample support for the Commission's determination that Appellants "failed to meet their burden of proof to establish the applicability of the professional capacity defense." I.R. A-106, Final Decision, at p. 171.

G. The Commission Did Not Commit an Error of Law, or Abuse Its Discretion, in Determining that Kern-Fuller Has "Control Person" Liability for ULG Pursuant to A.R.S. § 44-1999(B).

A.R.S. § 44-1999 provides in part that

> [e]very person who, directly or indirectly, controls any person liable for a violation of section 44-1991 or 44-1992 is liable jointly and severally with and to the same extent as the controlled person to any person to whom the controlled person is liable unless the controlling person acted in good faith and did not directly or indirectly induce the act underlying the action.

A.R.S. § 44-1999(B). As the Arizona Court of Appeals has recognized, A.R.S. § 44-1999(B) thus imposes "presumptive control liability on those persons who have the *power* to directly or indirectly control the activities of those persons or entities liable as primary violators." *Eastern Vanguard*, 206 Ariz. at 412 ¶ 42 (emphasis in original). Moreover, a finding of control liability "may be premised on the *power* to control[,] and does not require *actual participation* in the wrongful conduct[.]" *Id*. at 413 ¶ 44 (emphasis added). The burden of proof to establish the applicability of the defense afforded by A.R.S. § 44-1999(B) "falls on the controlling person." *Id*. at 413 ¶ 46.

In its Final Decision, the Commission found that the "good faith defense" established by A.R.S. § 44-1999(B) "is unavailable to" Kern-Fuller, and that she is "liable as a control person." I.R. A-106, Final Decision, at p. 173. In so finding, the Commission noted that, "as a partner of ULG, [Kern-Fuller] was in a position of control over ULG," and determined that, because "[w]e have found…that [Kern-Fuller] and ULG both induced unlawful sales of the income stream investments," A.R.S. § 44-1999(B), by its terms, does not apply. *Id*. at pp. 172-73. *See* A.R.S. § 44-1999(B) (providing that the statutory defense is available only if "the controlling person…did not directly or indirectly induce the act underlying the action").

In their Opening Brief, Appellants do not dispute the Commission's finding that, as a ULG partner, Kern-Fuller was in a position of control at ULG. *See generally* O.B. They assert, however, that the defense created by A.R.S. § 44-1999(B) is available to her because, they contend, "the record indicates Kern-Fuller acted in good faith and had no knowledge of or reason to believe" that "providing professional legal and escrow services…violated § 44-1991." *Id*. at p. 40. They also assert that Kern-Fuller maintained a "reasonable and proper system of supervision and internal controls" for ULG. *Id*. at pp. 40-41. In support of that contention, they assert that ULG's IOLTA trust account "was maintained pursuant to South Carolina law." *Id*.

Kern-Fuller's undisputed status as a control person of ULG presumptively exposes her to liability under A.R.S. § 44-1999(B). *See Eastern Vanguard*, 206 Ariz. at 412 ¶ 42. For several reasons, the Court finds that Appellants have failed to meet their burden of overcoming that presumption.

First, as noted above, the Commission did not abuse its discretion in determining that Kern-Fuller "induced" the sales of the income stream investments. That fact alone renders A.R.S. § 44-1999(B) inapplicable. See A.R.S. § 44-1999(B) (providing a defense for controlling persons who both "acted in good faith" and "*did not…induce* the act underlying the action.") (emphasis added).

Second, as Appellee correctly notes, Appellants' cursory assertion that "the record indicates Kern-Fuller acted in good faith," O.B. at p. 40, is not supported by any citation to the record. A.B. at p. 48. As such, Appellants have failed to properly present this argument, and thereby waived it. *See Henderson v. Henderson*, 241 Ariz. 580, 590 ¶ 35 (App. 2017) (holding that party waived claim for fee award because "she has provided no legal authority for such an award, nor has she provided any citations to the record to support her factual assertions").

Third, although ULG acknowledged, in its agreement with distributors, that ULG and its members are not qualified to offer securities advice, investment advisor Andy Smith, who sold the income stream investments to clients, testified that Kern-Fuller told him, during a meeting in 2015, that the income stream product was not a security. *Compare* I.R. C-287, Legal Services and Fee Agreement – Hourly/Retainer, at p. 2 ("Law firm hereby represents that no member of the firm or its staff is competent to provide…securities advise [*sic*] to you or your entity.") *with* I.R. B-4, Hearing Transcript, at p. 342 (testifying about a meeting in 2015, Smith responded, "Correct" when asked, "And [Kern-Fuller] told you that the income stream product was not a security?"). Kern-Fuller's offering of a legal opinion on a matter that ULG itself admitted she is not qualified to offer is hardly consistent with her claim to have acted in good faith.

Fourth, Appellants' attempt to invoke A.R.S. § 44-1999(B) is defeated by Kern-Fuller's invocation of her right against self-incrimination when asked about her role in the income stream transactions. I.R. A-106, Final Decision, at pp. 89-104. Kern-Fuller invoked her right against self-incrimination, for example, when asked whether she "acted towards the veterans and towards investors with the intent to defraud them." *Id*. at p. 104. *See also* I.R. B-7, Hearing Transcript, at p. 1090. Kern-Fuller's unwillingness to answer such a question is incompatible with her claim to have met her burden of proving that she acted in good faith within the meaning of A.R.S. § 44-1999(B).

The Court therefore finds that the Commission did not abuse its discretion or commit an error of law in determining that "a good faith defense is unavailable" to Kern-Fuller, and that she "is liable as a control person for the antifraud violations of ULG, pursuant to A.R.S. 44-1999(B)." I.R. A-106, Final Decision, at p. 173.

H. The Commission Did Not Commit an Error of Law, or Abuse Its Discretion, in Entering Orders Against Appellants to Cease and Desist and to Pay Restitution and Administrative Penalties.

In its Final Decision, the Commission ordered Appellants to "cease and desist from their actions, as described above, in violation of A.R.S. §§ 44-1841, 44-1842, and 44-1991," to make restitution in the total amount of $2,943,438.50 (jointly and severally with other Respondents), and to each pay administrative penalties of $240,000. I.R. A-106, Final Decision, at pp. 189-90.

Appellants assert that the Commission's orders "are not supported by substantial evidence" and "are errors of law and abuses of discretion." O.B. at p. 41. Appellants do not, however, allege any infirmity with the orders themselves. Instead, Appellants assert that they cannot "have [any] liability for restitution or administrative penalties" because, they insist, they did not engage in the acts alleged by the Division. *Id*. They go on to reiterate their arguments that they "have not made, participated in or induced any unlawful sale or purchase of securities in violation of the ASA regarding the Transactions." *Id*.

Because, for the reasons discussed above, the Court rejects Appellants' challenges to the Commission's determinations regarding their liability, Appellants' challenge to the remedies ordered by the Commission necessarily fails as well.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

LC2021-000011-001 DT 02/02/2022

CONCLUSION & ORDERS

In accordance with the foregoing,

IT IS ORDERED affirming Decision No. 77806 of the Arizona Corporation Commission.

IT IS FURTHER ORDERED remanding this matter to the Arizona Corporation Commission for such further proceedings, if any, as may be appropriate.

No matters remain pending in connection with this appeal. This is a final order pursuant to JRAD 13 and Ariz.R.Civ.P. 54(c).

/s/ Daniel J. Kiley
THE HON. DANIEL J. KILEY
Judge of the Superior Court

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