ORIGINAL

0000082622

BEFORE THE ARIZONA CORPORATION

RECEIVED

2008 MAR 17 P 4: 57

AZ CORP COMMISSION
DOCKET CONTROL

05CB

COMMISSIONERS

JEFF HATCH-MILLER, Chairman
WILLIAM A. MUNDELL
MIKE GLEASON
KRISTIN K. MAYES
GARY PIERCE

In the matter of:

EDWARD A. PURVIS and MAUREEN H. PURVIS, husband and wife
1231 W. Shannon
Chandler, Arizona 85224

GREGG L. WOLFE and ALLISON A. WOLFE, husband and wife
2092 W. Dublin Lane
Chandler, Arizona 85224

NAKAMI CHI GROUP MINISTRIES INTERNATIONAL, (a/k/a NCGMI), a Nevada corporation sole
4400 N. Scottsdale Road, Suite 9-231
Scottsdale, Arizona 85251

JAMES W. KEATON, Jr. and JENNIFER KEATON, husband and wife
11398 E. Whitehorn Drive, Apt. D
Scottsdale, Arizona 85255

ACI HOLDINGS, INC., a Nevada corporation
17650 N. 25th Avenue
Phoenix, Arizona 85023

Respondents.

Docket No. S-20482A-06-0631

RESPONDENTS EDWARD AND MAUREEN PURVIS' CLOSING BRIEF

Arizona Corporation Commission
DOCKETED
MAR 17 2008
DOCKETED BY nr

MEMORANDUM OF POINTS AND AUTHORITIES

I. INTRODUCTION.

Respondents' preparation of this brief has been severely handicapped because it was difficult (if not impossible) to discern from the Securities Division's disjointed presentation exactly what claims have been leveled against Respondents. This is particularly so with respect to the Division's allegations regarding fraud. Respondents have no idea what fraudulent statements have been attributed to them, or what sales of

securities such fraud was allegedly connected with. Indeed, Respondents assert that the Division utterly failed to "connect the dots" in its case with respect to any claims of fraud (and other claims as well.) For that reason, Respondents intend to read the Division's closing brief and provide a more fulsome response to the Court thereafter.

Notwithstanding this handicap, the Division did articulate some of its claims in a somewhat understandable fashion. Specifically, the Division argued that:

1. Mr. Purvis violated A.R.S. §44-1841 by selling unregistered ACI Holdings, Inc. stock. The Division also asserts that Mr. Purvis violated A.R.S. §44-1842 by selling ACI Holdings, Inc. stock because he was not registered with the State as a dealer or salesperson.

2. Mr. Purvis violated A.R.S. §44-1841 by selling unregistered securities in the form of loans to Homes for Southwest Living and CSI, Inc. These loans were called "bridge loans" during the Division's presentation. The Division also asserts that Mr. Purvis violated A.R.S. §44-1842 in connection with these loans because he was not registered with the State as a dealer or salesperson.

3. Mr. Purvis violated A.R.S. §44-1841 and 44-1842 in connection with the sale of "corporations sole."

As discussed below, the State did not meet its burden to prove these claims

II. THE ACI HOLDINGS, INC. STOCK OFFERING.

A. Federal Law Preempts Arizona's Registration Requirements Under A.R.S. §44-1841 Regarding The ACI Holdings Stock Offering.

The National Securities Market Improvement Act of 1996 ("NSMIA") [15 U.S.C. § 77r; Pub. L. No. 104-290, 110 Stat. 3416] amended § 18(a) of the 1933 Act expressly to preempt any state Blue Sky laws requiring redundant state registration and qualification of any nationally offered and traded securities, defined by NSMIA as "covered securities." Section 18(a)(1)(A) of the 1933 Act—the NSMIA express preemption provision—specifically prohibits any state from requiring any federal "covered security" to be registered in the state:

(a) except as otherwise provided in this section, no law, rule,

> regulation, or order or other administrative action of any state or any political subdivision thereof—
>
> (1) requiring, or with respect to, registration or qualification of securities, or registration or qualification of securities transactions, shall directly or indirectly apply to a security that—
>
> (A) is a covered security; . . . . (Emphasis added.)

This preemption provision advances the primary purpose of NSMIA to eradicate the prior system of "dual registration" under both the 1933 Act as well as state blue Sky laws for nationally traded securities:

> By 1996, Congress recognized the redundancy and inefficiencies inherent in such a system and passed NSMIA to preclude states from requiring issuers to register or qualify certain securities with state authorities.
>
> ***
>
> When considered in concert, SLUSA, NSMIA and PSLRA demonstrate that Congress intended to provide national uniform standards for the securities markets and nationally marketed securities. Through these statutes, Congress erected uniform standards for registration of, and litigation concerning a defined class of securities.

Lander v. Hartford Life & Annuity Ins. Co., 251 F.3d 101, 108-112 (2d Cir. 2001) (emphasis added), quoted in *Patenaude v. Equitable Life Assur. Soc.*, 290 F.3d 1020, 1026 (9th Cir. 2002); *see also Dabit v. Merrill Luynch, Pierce, Fenner & Smith, Inc.*, 395 F.3d 25, 32 n.3 (2d Cir. 2005). "The NSMIA drafters intended the Act to eliminate the costs and burdens of duplicative and unnecessary regulation by designating the federal government as exclusive regulator of national offerings of securities." *Lillard v. Stockton*, 267 F.Supp.2d 1080, 1115 (N.D. Okla. 2003); *see also Temple v. Gorman*, 201 F.Supp.2d 1238, 1244 (M.D. Fla. 2002) ("Congress expressed its intent in NSMIA that federal regulations alone should govern the registration of national securities offerings.").

Section 18(b)(4)(D) of the 1933 Act defines a "covered security" to include any transaction exempt from registration "pursuant to. . . Commission rules or regulations issued under § 4(2)" of the 1933 Act. SEC Rule 506 was promulgated pursuant to § 4(2).

Mr. Keaton, the chief executive of ACI Holdings, Inc., testified that the stock was sold pursuant to Rule 506 of Regulation D. The offering materials further confirm this fact. As such, the ACI Holdings, Inc. stock, issued in a private offering pursuant to Rule 506 of Regulation D, are exempt from registration under § 4(2), and are "covered securities" under § 18(b)(4)(D). Arizona's state registration requirements were pre-empted.

Such was precisely the holding in *Temple v. Gorman*, 201 F.Supp.2d at 1242-44, in which private placement investors asserted claims under Florida's unregistered securities law, which is substantively identical to A.R.S. §44-1841. Despite the fact that the issuer allegedly failed to comply fully with Rule 506 of Regulation D, thereby jeopardizing its exemption from registration under § 4(2), the *Temple* court held that "the securities sold to Plaintiffs are federal 'covered securities' because they were sold pursuant to" rule 506 of Regulation D. *Id.* at 1244. Further,

> [A]ny attempt by Florida to require registration of such securities or securities transactions would be preempted by NSMIA. Congress expressed its intent in NSMIA that federal regulations alone should govern the registration of national securities offerings. Where a Form D was filed with the SEC for a transaction that purported to merit an exemption from federal registration pursuant to Regulation D, Florida law could not require duplicative registration or a transactional exemption from registration.

Id. (emphasis added).

Similarly, in *Lillard* (a case which undersigned counsel personally appeared), the court dismissed a plaintiff's state law unregistered securities claim, since Oklahoma's registration requirement for "covered securities" was preempted by NSMIA, despite the fact that plaintiff alleged that defendant's Rule 506 offering was defective, and did not qualify for exemption under § 4(2). 267 F.Supp.2d 1080, 1115. This same rule has been followed in other federal and state courts. See Pinnacle Communications, International v. Am. Family Mortgage Corp., 417 F. Supp.2d 1073, 1087 (D. Minn. 2006); Risdall v. Brown-Wilbert, Inc., 733 N.W.2d 827 (Minn. Ct. App. 2007).

As such, Arizona's state registration laws do not apply to the ACI Holdings Inc. stock offering. Only federal law does, and the enforcement of such federal law is not

within the jurisdiction of the Division. The Division's claim under A.R.S. §44-1841 must therefore be dismissed.

B. In All Events, The ACI Holdings, Inc. Stock Offering Was Exempt From Registration Under Regulation D.

As this Court knows, if a security is exempt from registration under Regulation D, Rule 506, that security is also exempt from registration under Arizona's securities laws. As this Court also knows, a private offering of securities is exempt under Regulation D if the securities are sold to accredited investors. And, the exemption under Regulation D is not lost simply because some of the purchasers turn out to be unaccredited. If there is a reasonable basis for the offeror to conclude, ***even mistakenly***, that the purchasers are accredited, the exemption is kept intact if it later turns out that the purchasers were not accredited.

In this case, every person who purchased ACI Holdings, Inc. stock was given a private offering memorandum describing the offering, specifying that it was available only to accredited investors, and defining in clear and unambiguous terms what it took to be an "accredited investor." ***Further, each and every purchaser of ACI Holdings, Inc. stock represented and warranted that they were accredited investors.*** These subscription agreements are contained in Respondents' Exhibit 4. In sum, Respondents have proven through these subscription agreements that each of the purchasers of ACI Holdings, Inc. stock was accredited.

In an effort to show that some purchasers of ACI stock were not accredited, the Division trotted out two telephonic witnesses, Joanne Brundege and Catherine Barnowski, who said at the hearing that they are not accredited. Both Brundege and Barnowski, however, signed subscription agreements and represented that they were accredited. Brundege and Barnowski, in essence, testified that they ***lied*** when they signed the subscription agreements.

The Division cannot rely upon Brundege's and Barnowski's statements to prove their case. As a matter of law, Brundege and Barnowski cannot now disavow their

representations that they were accredited investors. *See Wright v. National Warranty Company, LP*, 953 F.2d 256, 260-61 (6th Cir. 1992). In *Wright*, the plaintiffs attempted to do exactly what Brundege and Barnowski attempted in this case. The plaintiffs in Wright signed a subscription agreement where they represented that they were accredited investors under Regulation D. They later claimed that they were not accredited and sued on an unregistered securities claim. The Sixth Circuit rejected this attempt, and ruled as a matter of law that the plaintiffs could not disavow their representation. *See also Pinnacle Communications Int., Inc. v. American Family Mortgage Corp.*, 417 F. Supp.2d 1073, 1083 (D. Minn. 2006) (investors were estopped from denying representation that they were accredited); *Faye L. Roth Revocable Trust v. UBS Painewebber, Inc.*, 323 F. Supp.2d 1279, 1301 (S.D. Fla. 2004) (investors cannot disavow their representations in application that they were accredited); *Goodwin Props., LLC v. Acadia Group, Inc.*, 2001 WL 800064 (D. Me. 2001) (same holding).

C. Respondents Had a Reasonable Basis To Believe All Investors Were Accredited.

All of the purchasers of ACI Holdings, Inc. stock represented to Purvis and others that they were accredited investors. They all represented that they had read the Private Offering Memorandum and understood its contents. These representations were given to Mr. Purvis prior to the sale of ACI Holdings, Inc. stock.

Even if Barnowski and Brundege were not accredited, their representations to Mr. Purvis (which they now say were lies) gave Mr. Purvis a reasonable basis to conclude that they were accredited investors.

D. As A Director of ACI Holdings, Inc., Mr. Purvis Did Not Need to Be Registered As a Salesperson or Dealer.

SEC Rule 3(A)41 specifies that "associated persons of an issuer" such as a partner, officer, *director*, or employee need not registered as a broker/dealer if certain requirements are met. Arizona has adopted an equivalent safe harbor exemption for its registration statutes. Under Rule 14-4-140(b), an exemption from A.R.S. § 44-1842 is

available to directors of issuers who make offers or sales on behalf of the issuer if they were not retained for the primary purpose of making such sales or offers.

Mr. Purvis was a director of ACI Holdings, Inc. at the time the stock was offered for sale. Mr. Keaton testified that in fact Mr. Purvis provided substantial services to ACI Holdings, Inc. as a director, and was not made a director simply for the purpose of allowing him to offer ACI Holdings, Inc. stock. The Division offered no evidence to rebut this testimony.

As such, Mr. Purvis was exempt from A.R.S. §44-1842 with respect to the offering of ACI Holdings, Inc. stock.

III. THE HOMES FOR SOUTHWEST LIVING AND CSI LOANS.

As an initial matter, Mr. Purvis did not sell Homes For Southwest Living loans to anyone. The undisputed evidence shows that in each instance, these loans were purchased on behalf of an IRA account for which Mr. Purvis acted as an agent or pursuant to a power of attorney. That is, Mr. Purvis was "one in the same" as the purchasers. Homes For Southwest Living "sold" the loans, not Mr. Purvis.

Further, the Homes For Southwest Living loans were not securities. They were short term loans with a high interest rate secured by collateral. Repayment on the loan was not expected to come from the entrepenuerial or management efforts of anyone. Repayment was to come from a refinancing to be accomplished in the near-future. Hence the label "bridge loans."

The Division bears the burden of proving that these loans were securities. And the Division failed to prove that the Homes for Southwest Living loans were designed to earn money through the entrepreneurial or investment activities of another.

Similarly, the CSI promissory notes were short term notes, secured by valuable equipment. The borrowed money was used to pay for ongoing operations. It was not invested or used as risk capital. And cash flow from operations or new loans were to be used to pay the CSI notes back. Again, this is a classic commercial loan and is not a security.

For these reasons, the Homes For Southwest Living and CSI loans did not need to be registered.

Also, because Mr. Purvis was acting as an agent for the persons who made the loans, he did not need to be registered as a salesperson or dealer.

IV. CORPORATIONS SOLE ARE NOT SECURITIES.

In order to be a security, the investor must expect profits to be earned from an investment of money subject to the entrepreneurial managerial efforts of others. The corporations sole do not fit this definition. The Division's evidence showed that Corporations Sole were really filing corporate documents to be used as tax shelters. There was no investment of money subject to managerial efforts.

Moreover, the Division did not produce any evidence that Mr. Purvis "sold" any corporations sole. They were all done by Mr. Wolfe or others.

V. RESTITUTION IS NOT WARRANTED IN THIS CASE.

As the Court noted on several occasions, Mr. Purvis did not sell securities and did not get any money as a result of the sales of alleged securities identified by the Division in its case. Mr. Purvis did not receive any money from the proceeds paid for ACI Holdings' stock. Mr. Purvis did not receive any proceeds from the CSI or Homes for Southwest Living transactions. Further, Mr. Purvis did not receive any proceeds related to the Corporation Sole.

As a result, Mr. Purvis cannot be liable for the claims the Division has brought. And perhaps more importantly, it would constitute a manifest injustice to require him to provide restitution. He did not take anything from the alleged investors. Others did. Those other persons are the ones who should make restitution. Indeed, the Division has already obtained a substantial restitution judgment from Mr. Keaton.

VI. CONCLUSION.

Mr. Purvis recognizes that this Closing Brief is brief, however, he expects to provide a more fulsome explanation of his defenses upon reviewing the allegations made by the State in its Closing Brief. This being primarily due to the scattered and

unorganized presentation of evidence and allegations made the Division in its primary case.

RESPECTFULLY SUBMITTED this 17th day of March, 2008.

QUARLES & BRADY LLP
Renaissance One, Two North Central Avenue
Phoenix, Arizona 85004-2391

By _____
John Maston O'Neal

Attorneys for Respondents
Edward A. Purvis and Maureen H. Purvis

ORIGINAL and **13 COPIES** filed by hand-delivery this 17th day of March, 2008, with:

Docket Control, Arizona Corporation Commission
1200 West Washington
Phoenix, AZ 85007

COPY hand-delivered this 17th day of March, 2008, to:

ALJ Marc Stern
Arizona Corporation Commission/Hearing Division
1200 West Washington
Phoenix, AZ 85007

Mattew Neubert, Securities Division
Arizona Corporation Commission
1200 West Washington
Phoenix, AZ 85007

COPY of the foregoing mailed this 17th day of March, 2008, to:

Rachel Strachan, Securities Division
Arizona Corporation Commission
1300 West Washington St., 3rd Floor
Phoenix, Arizona 85007

Ashley Adams
Ryan, Rapp & Underwood, P.L.C.
3101 North Central Avenue
Phoenix, AZ 85012

_____