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BEFORE THE ARIZONA CORPORATION COMMISSION

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Arizona Corporation Commission

COMMISSIONERS

AZ CORP COMMISSION
DOCKET CONTROL

DOCKETED

JUL - 8 2011

GARY PIERCE, Chairman
BOB STUMP
SANDRA D. KENNEDY
PAUL NEWMAN
BRENDA BURNS

DOCKETED BY

In the matter of:)
)
JERE PARKHURST and MICHELLE)
PARKHURST, husband and wife, doing business)
as C-Street Financial Group and C-Street)
Development, L.L.C.;)
)
C-STREET HOLDINGS, L.L.C., a dissolved)
Arizona limited liability company; and)
)
PHOENIX FINANCIAL HOLDINGS, L.L.C., a)
terminated Arizona limited liability company;)
)
)
Respondents.)

DOCKET NO. S-20761A-10-0409
SECURITIES DIVISION'S POST
HEARING BRIEF

The Securities Division ("Division") of the Arizona Corporation Commission ("Commission") submits its post-hearing brief as follows:

I. PROCEDURAL HISTORY

On October 7, 2010, the Division filed a Notice of Opportunity for Hearing Regarding Proposed Order to Cease and Desist, Order for Restitution, Order for Administrative Penalties and for Other Affirmative Action ("Notice"). The Notice alleged that Respondents JERE PARKHURST, doing business as C-Street Financial Group and C-Street Development, L.L.C., C-STREET HOLDINGS, L.L.C., a dissolved Arizona limited liability company, and PHOENIX FINANCIAL HOLDINGS, L.L.C., a terminated Arizona limited liability company engaged in acts, practices, and transactions that constituted violations of A.R.S. § 44-1991, fraud in purchase or sale of securities.

1 On October 8, 2010, the Division served JERE PARKHURST, C-STREET HOLDINGS,
2 L.L.C., and PHOENIX FINANCIAL HOLDINGS, L.L.C. via personal service.

3 On October 15, 2010, JERE PARKHURST, C-STREET HOLDINGS, L.L.C., and
4 PHOENIX FINANCIAL HOLDINGS, L.L.C. filed a Request for a Hearing.

5 On November 5, 2010, JERE PARKHURST, C-STREET HOLDINGS, L.L.C., and
6 PHOENIX FINANCIAL HOLDINGS, L.L.C. (hereinafter collectively referred to "Respondents")
7 filed an Answer.

8 On November 30, 2010, Administrative Law Judge Stern ("ALJ Stern") ordered a pre-
9 hearing conference on December 7, 2010.

10 On December 3, 2010, MICHELLE PARKHURST requested a hearing.

11 On December 7, 2010, ALJ Stern ordered the hearing to begin on April 13, 2011.

12 On February 15, 2011, the Division served MICHELLE PARKHURST via publication.

13 The hearing began on April 13, 2011.

14 The ALJ admitted Division Exhibits S-1 through S-35, and S-37 through S-41 into
15 evidence. (*Tr. p. 11, ll. 20-25 to p.12, ll.1-3*).

16 II. STANDARD OF PROOF

17 In administrative actions brought by the Commission, the well-recognized standard of proof
18 for alleged violations of the Act is the "preponderance of the evidence." *See, e.g., Steadman v.*
19 *Securities and Exchange Commission*, 450 U.S. 91 (1981) (Securities and Exchange Commission
20 properly applied the 'preponderance of the evidence' standard when determining administrative
21 proceeding); *Geer v. Ordway*, 156 Ariz. 588, 589, 754 P.2d 315, 316 (App. 1987) (in context of
22 administrative hearing, proper standard of proof is preponderance of the evidence). Therefore, the
23 preponderance of the evidence standard is applicable in this matter.

24 III. JURISDICTION

25 The Commission has jurisdiction over this matter pursuant to Article XV of the Arizona
26 Constitution and the Act.

IV. FACTS

1
2 JERE PARKHURST (“J. PARKHURST”) is a married person who at all relevant times
3 resided in Arizona. MICHELLE PARKHURST (“M. PARKHURST”) is the spouse of J.
4 PARKHURST. (*See J. Parkhurst’s Answer filed November 5, 2010*). M. PARKHURST has been J.
5 PARKHURST’s spouse during all relevant times. (*Tr. p. 118, ll. 1-25*).

6 At all relevant times, J. PARKHURST transacted business as C-Street Financial Group and
7 C-Street Development, L.L.C. (*Tr. p. 92, ll. 20-25, p. 93, ll. 1-11, and p. 93, ll. 12-20*). C-Street
8 Financial Group and C-Street Development, L.L.C. are entities of unknown origin neither of which
9 is authorized to transact business in Arizona. (*Id.*).

10 C-STREET HOLDINGS, L.L.C. (“C-STREET”) was an Arizona limited liability company
11 organized on November 19, 2004. (*Exs. S-2a and S-2b*). At all relevant times, C-STREET had its
12 principal place of business in Maricopa County, Arizona. (*Id.*).

13 C-STREET was a member-managed limited liability company. (*Ex. S-2a*). J. PARKHURST
14 was a member of C-STREET beginning November 19, 2004. (*Exs. S-2a and S-2b*).

15 PHOENIX FINANCIAL HOLDINGS, L.L.C. (“PHOENIX”) was an Arizona limited
16 liability company organized on September 12, 2002. (*Exs. S-3a, S-3b, and S-3c*). At all relevant
17 times, PHOENIX had its principal place of business in Maricopa County, Arizona. (*Id.*).

18 PHOENIX was a manager-managed limited liability company. (*Ex. S-3a*). J.
19 PARKHURST was the manager and a member of PHOENIX beginning September 12, 2002. (*Id.*).

20 On January 24, 2008, J. PARKHURST, on behalf of PHOENIX, filed Articles of
21 Termination with the Commission. (*Ex. S-3c*).

22 From as early as 2006 through at least 2007, J. PARKHURST, C-STREET, and PHOENIX
23 offered and/or sold to offerees and investors one of two types of investments. One investment was
24 a note secured by second deeds of trust and the second was a “lender agreement,” wherein an
25 investor purchased a house, J. PARKHURST would rehabilitate the house, and then the investor
26 and J. PARKHURST would split the profits after the house was sold (hereinafter “investment(s)”).

1 In either case, all of the funds were to be used to rehabilitate the house. (*Tr. p. 16, ll. 2-5, p. 38, ll.*
2 *5-17, p. 55 ll. 4-9 p. 74, ll. 5-12, p. 96 ll. 17-21, p.107 ll.4-7, p. 114 ll. 18-25, Ex. S-37, and p. 116*
3 *ll. 5-10, Ex. S-38).*

4 J. PARKHURST located investors by sending emails announcing an investment
5 opportunity. At least once, J. PARKHURST sent at an email to each of forty-three (43) offerees
6 regarding one residential property renovation wherein J. PARKHURST offered a second deed of
7 trust in exchange for an investor's funds. (*Ex. S-9*). J. PARKHURST indicated he "was looking
8 for \$106,000 that will be backed by a second trust deed and promissory note." (*Id.*). J.
9 PARKHURST said the return would be "20% annually paid monthly or compounded." (*Id.*).

10 Investors Christi Ellis ("Ellis") and Norma Heinrich ("Heinrich") each testified that they
11 learned of J. PARKHURST's investment opportunities through emails J. PARKHURST sent to
12 them. Investor Heinrich testified she learned of J. PARKHURST's investment opportunity through
13 a flier that came through her email while she was in Arizona. (*Tr. p. 53, ll. 24-25 and p.54, ll. 1-5*).
14 Investor Ellis testified, while in Arizona, she received a number of different email investment
15 opportunities but ended up investing with J. PARHURST on a different property. (*Tr. p. 14, ll. 12-*
16 *25, p. 15, ll. 1-5, and Ex. S-33*).

17 Investor Michael Olson ("Olson") testified he heard about the investment from Dan Brown.
18 (*Tr. p. 34, ll. 22-23 and p. 36 ll. 3-13, Ex. S-10*). Investor Elaine D'Aprile ("D'Aprile") testified
19 she first learned of J. PARKHURST's investment opportunities through a friend. (*Tr. p. 70, ll. 18-*
20 *25 and p.71 l. 1*).

21 Investigator Gary Clapper ("Investigator Clapper") testified regarding information received
22 from investors Gary and Catherine Muha (collectively "Muha"), Chris Reno ("Reno") and Greg
23 Baskin ("Baskin").

24 Investigator Clapper testified that investor Reno received an email with "Investment 20%
25 interest" in the subject line of the email. (*Tr. p. 103 ll. 11-21, Ex. S-22*). Chris Reno received
26 another email that stated "Another investmetn [sic] deal" in the subject line of the email. (*Id.*).

1 Each of the investor witnesses and Investigator Clapper testified that J. PARKHURST was
2 to use the funds to rehabilitate the residential properties to be purchased by C-STREET or
3 PHOENIX. (*Tr. p. 16, ll. 2-5, p. 38, ll. 5-13, p. 55 ll. 4-9 p. 74, ll. 5-12, p. 96 ll. 17-21, p.107 ll.4-7,*
4 *p. 114 ll. 18-25, Ex. S-37, and p. 116 ll. 5-10, Ex. S-38*). The investors and Investigator Clapper
5 further testified that J. PARKHURST would identify, purchase, and rehabilitate the real estate. (*Tr.*
6 *p. 42, ll. 20-25, and p. 43, l. 1.*) Furthermore, J. PARKHURST would make all the decisions
7 related to the rehabilitation. (*Tr. p. 16, ll. 22-25 to p. 17, ll. 1-12, p. 42, ll. 21-25, p. 57, ll. 4-6 and*
8 *21-25, p. 57, ll. 1-18, and p. 97, ll. 3-11*).

9 In exchange for investors' funds, C-STREET and PHOENIX issued notes that promised a
10 twenty (20) percent return. (*Exs. S-6, S-15, and S-20*) (*Tr. p. 15, ll. 16-19, and p. 54, ll. 21-23*). The
11 notes promised to repay a note by making monthly interest payments to the investor and then
12 paying the investor the investor's principal at the end of one year. (*Id.*).

13 Investors Baskin and D'Aprile entered into agreements with J. PARKHURST and C-
14 STREET whereby each investor would purchase a house but J. PARKHURST would remodel it
15 using investor funds. (*Exs. S-4, S-37 and S-38*). After the remodel was completed, the house
16 would be sold and J. PARHURST and C-STREET would split the proceeds with the investor. (*Id.*).

17 Each note was secured by a second deed of trust on the residential property purchased by
18 the Respondents. (*Exs. S-34 and S-41*) (*Tr. p. 21, ll. 17-23, p.54, ll. 24-25 to p. 55, l. 1*).

19 The investors invested with the Respondents to make a profit through the investment and
20 did not intend to live in the properties. (*Tr. p. 17, ll. 13-16 and p. 47, ll. 19-21*).

21 J. PARKHURST signed all but two of the notes on behalf of C-STREET. (*Exs. S-11, S-34,*
22 *and S-41*) (*Tr. at p. 22, ll. 24-25 to p. 23, ll. 1-5*). J. PARKHURST signed one note on behalf of
23 PHOENIX and one note on behalf of Capital Real Estate Company, LLC. (*Exs. S-15 and S-20*).
24 Investigator Clapper testified that there was no record of Capital Real Estate Company, LLC being
25 organized with the Arizona Corporation Commission. (*Tr. p. 95, ll. 21-25 to p. 96, ll. 1-10*).

1 All but two of the properties were titled in C-STREET's name. (*Exs. S-11 and S-34*). One
2 property was titled in the name of PHOENIX and the other property was titled in the name of
3 Capital Real Estate Company, LLC. (*Exs. S-15 and S-20*).

4 Investors Olson, Heinrich, and D'Aprile received checks for monthly interest payments that
5 were returned due to insufficient funds to cover the checks. (*Exs. S-7, S-14, and S-18*) (*Tr. p. 35, ll.*
6 *8-10 and p. 41, ll. 11-25*).

7 The Respondents did not tell the investors they did not have the financial resources to make
8 the interest payments. (*Tr. p. 46, ll. 8-21, p. 65, ll. 1-10, p.80, ll. 19-25 to p.81, ll. 1-6*).
9 Furthermore, the investors testified that they would have wanted to know that the Respondents
10 could not make the interest payments before they invested. (*Tr. p. 47, ll. 15-18, p. 66, ll. 1-3, p.80,*
11 *ll. 19-25 to p.81, ll. 1-6*).

12 In or around February 28, 2007, C-STREET purchased a residential property with borrowed
13 funds and executed a first deed of trust. (*Ex. S-6*). As part of this purchase, C-STREET issued a
14 note secured by a second deed of trust in exchange for Investor D'Aprile's funds. (*Id.*). On or
15 about May 16, 2007, the holder of the first deed of trust affirmed that J. PARKHURST and C-
16 STREET had not made the first payment that was due March 28, 2007. (*Ex. S-8*). As a result, the
17 holder elected to sell the property and filed a notice for a trustee's sale on or about May 17, 2007.
18 (*Id.*).

19 During March and April 2007, Respondents offered and sold notes secured by second deeds
20 of trust to Investors Olson and Heinrich. (*Exs. S-10, S-11, and S-15*). Respondents failed to tell
21 Investors Olson and Heinrich that the Respondents did not have the financial resources to make the
22 monthly principal payments on the first mortgage for the property purchased on or about February
23 28, 2007, and the investors would have wanted to know that information before they invested. (*Tr.*
24 *p. 46, ll. 22-25, p. 47, ll. 1-18, and p. 65, ll.11-20 to p. 66, ll. 1-3*).

25 The majority of the investors did not see much in the way of rehabilitation occurring at the
26 properties. Investor Ellis testified that she was monitoring the property she invested in and only

1 noticed "minimal" work was completed on it. (*Tr. p. 23, ll. 19-25 to p. 24, ll. 1-7*). Investor
2 Heinrich testified that the property she invested in was "just a mess" and no rehabilitation work was
3 completed when J. PARKHURST put the property up for sale. (*Tr. p. 61, ll. 4-25 to p. 62, ll. 1-20*).
4 Investigator Clapper testified that Investor Muha said there was no remodeling work done on the
5 property. (*Ex. S-20 and Tr. p. 96, l. 25 to p. 97, ll. 1-2*).

6 Investigator Clapper testified that Chris Reno received accounting records that showed the
7 amount and description of the rehabilitation expenses alleged to have been incurred to rehabilitate
8 the properties. (*Ex. S-28 and Tr. p. 108, ll. 1-25 to p. 109, ll. 1-19*). The accounting records showed
9 a total of \$395.00 was spent on renovations for one property and \$414.97 was spent on renovations
10 to another property. (*Id.*). Investigator Clapper testified that a further examination of the
11 accounting detail showed the funds were actually used to pay utility costs. (*Id.*). Furthermore, the
12 accounting records listed C-Street Development, L.L.C. at the top of each page. (*Id.*). However,
13 Investigator Clapper testified he did not find any records of such a company organized or
14 authorized to transact business in Arizona. (*Tr. p. 93, ll. 12-20*).

15 Investigator Clapper also testified that some of the funds from one of Reno's investments
16 were used to help fund the purchase of the property despite Reno's understanding that all the funds
17 were to be used to rehabilitate the property. (*Ex. S-26 and Tr. p. 107, ll. 4-25 to p. 108, ll. 1-7*). C-
18 STREET closed on the property located at 542 W. Cambridge Avenue, Phoenix, Arizona, 85003 on
19 or about March 6, 2007. (*Ex. S-26*). The Settlement Statement showed Chris Reno's \$100,000
20 investment, but only \$55,082.22 was returned to C-STREET and the remainder was paid to the
21 Seller. (*Id.*).

22 The investors testified that J. PARKHURST did not return the investors' funds even though
23 the promised rehabilitations did not occur. (*Tr. p. 23, ll. 23-25, p. 24, ll. 1-7 and 22-23, and p. 44,*
24 *ll. 1-19*). However, with Investors Olson and D'Aprile, J. PARKHURST and C-STREET executed
25 a settlement agreement with those investors that included an unsecured promissory note for the
26

1 amount invested. (*Exs. S-13 and S-41*). J. PARKHURST and C-STREET failed to meet terms of
2 agreements. (*Tr. p. 35, ll. 8-15 and p.82, ll. 19-25 to p.83, ll. 1-2*).

3 Investigator Clapper testified that J.PARKHURST and M. PARKHURST were married at
4 the time of the investments. (*Tr. p. 117, l. 1 to p. 118, l. 25*). Investigator Clapper testified he
5 searched records at the Maricopa County Recorder's Office and located a deed of trust with both J.
6 PARKHURST and M. PARKHURST's names on it. (*Id. and Ex. S-40*). The date on that
7 document was January 26, 2006. (*Ex. S-40*). Investigator Clapper also testified he spoke with M.
8 PARKHURST's mother and she indicated that J. PARKHURST and M. PARKHURST have been
9 married since December 1996. (*Tr. p.118, ll. 4-7*). Furthermore, Investigator Clapper testified that
10 he did not find any indication of divorce. (*Tr. p. 118, ll. 20-25*).

11 Both Investigator Clapper and Investor Ellis testified regarding the expenditure of investor
12 funds. Investigator Clapper testified that the only income J. PARKHURST had was investor
13 money. (*Tr. p. 122, ll. 1-11*). Investor Ellis testified that she believed the money was spent on
14 PARKHURST's family. (*Tr. p. 32, ll. 22-25 to p.33, ll. 1-15*)

15 Investigator Clapper testified that J. PARKHURST, C-STREET, and PHOENIX raised
16 \$879,300 from at least seven (7) investors. (*Tr. p. 117, ll. 3-20, Ex. S-39*). Investigator Clapper
17 also testified that three (3) of the investors received funds back totaling \$55,040. (*Id.*). As a result
18 of that return, a total of \$824,260 remains owed to the investors. (*Id.*).

19 **V. THE NOTES SECURED BY SECOND DEEDS OF TRUST ARE SECURITIES FOR**
20 **THE PURPOSE OF THE ANTI-FRAUD PROVISIONS OF THE SECURITIES ACT AND**
21 **THE LENDER AGREEMENTS ARE SECURITIES IN THE FORM OF INVESTMENT**
22 **CONTRACTS.**

23 **A. The Notes Sold by the Respondents are Securities for the purposes of the Anti-**
24 **Fraud Provisions of the Securities Act**

25 According to *MacCollum v. Perkinson*, the Court adopted the analysis articulated in *Reves v.*
26 *Earnst & Young*, 494 U.S. 56, 110 S. Ct. 945 (1990), to determine if a note violated the antifraud
provisions of the Arizona Securities Act. 185 Ariz. 179, 185, 913 P.2d 1097, 1103 (App. 1996).

1 Arizona courts apply it to determine whether a note is a security for purposes of fraud under the
2 Arizona Securities Act. *Id.*; *see also* A.R.S. § 44-1991(A).

3 The *Reves* court started with the *presumption* that notes are securities and established a two-
4 part test with which the presumption may be rebutted. *Reves*, 494 U.S. at 63. The first part of the
5 *Reves* test is that the presumption may be rebutted by a showing that the note “bears a strong
6 resemblance” to an instrument listed in an enumerated category of exceptions. *Id.*

7 Elaborating on the family resemblance test, the Supreme Court identified a four-factor test to
8 assist in ascertaining whether a note resembles one of the families of notes that are not securities.
9 The factors are balanced to reach a determination. The first factor established by the Court is to
10 assess the motivations of the buyer and seller to enter into the transaction at issue. If the seller’s
11 purpose is to raise money for the general use of a business enterprise or to finance substantial
12 investments and the buyer is interested primarily in the profit the note is expected to generate, the
13 instrument is likely to be a security. *Id.* The second factor is the plan of distribution. The Court
14 stated that the plan of distribution must be examined to determine if the “note” is an instrument in
15 which there is “common trading for speculation or investment.” *Id.* at 68-69; *see also MacCollum*,
16 185 Ariz. at 187, 913 P.2d at 1105 (“Offering and selling to a broad segment of the public is all that
17 is required to establish the requisite ‘common trading’ in an instrument.”), *quoting Reves*, 494 U.S.
18 at 68 and citing *Landreth Timber Co. v. Landreth*, 471 U.S. 681, 694, 105 S.Ct. 2297 (1985) (stock
19 of closely held corporation not traded on any exchange held to be a security). The second factor is
20 the plan of distribution. The Court stated that the plan of distribution must be examined to
21 determine if the “note” is an instrument in which there is “common trading for speculation or
22 investment.” *Id.* at 68-69; *see also MacCollum*, 185 Ariz. at 187, 913 P.2d at 1105 (“Offering and
23 selling to a broad segment of the public is all that is required to establish the requisite ‘common
24 trading’ in an instrument.”), *quoting Reves*, 494 U.S. at 68 and citing *Landreth Timber Co. v.*
25 *Landreth*, 471 U.S. 681, 694, 105 S.Ct. 2297 (1985) (stock of closely held corporation not traded
26 on any exchange held to be a security). In defining common trading, in *Stoiber v. Securities and*

1 *Exchange Commission*, the Court found that thirteen customers were not enough to meet the
2 common trading element. 161 F.3d 745, 751, 333 U.S.App.D.C. 195, 201 (1998). However, when
3 the Court added the fact that individuals were solicited, not sophisticated financial institutions, the
4 Court found the common trading element was satisfied. *Id.* The third factor is to examine the
5 reasonable expectations of the investment public. The Court stated that it will consider instruments
6 to be securities on the basis of such public expectations, even where an economic analysis of the
7 circumstances of the particular transaction might suggest that the instruments are not securities as
8 used in that transaction. *Id.* The fourth and final factor is whether some factor such as the existence
9 of another regulatory scheme significantly reduces the risk of the instrument, thereby rendering
10 application of the securities laws unnecessary. *Id.*

11 The second part of the *Reves* test is that if the note does not resemble one of the families of
12 notes that are not securities, then, using the same four factors, the presumption may be rebutted by
13 a showing that the note represents a category that should be added as a non-security. *Id.*

14 The evidence in the administrative record supports the determination that the notes are
15 securities under the *Reves* test because:

- 16 (1) The investors bought the notes to earn a 20 percent interest on their funds. The
17 Respondents raised the funds to finance the idea of rehabilitating homes to re-sell at
18 a profit. Additionally, in emails and in flyers J. PARKHURST referred to the
19 rehabilitation as investment opportunities.
- 20 (2) The offer and sale of the notes was widely distributed. J. PARKHURST emailed
21 one investment opportunity to 43 different individuals. Seven individuals invested
22 with J. PARKHURST and/or one of his entities;
- 23 (3) The investors reasonably expected to make money from their participations in the
24 notes. The Respondents used the term "investment" in their communications; and
- 25 (4) There was no regulatory scheme that would significantly reduce the risk of the
26 investment and thereby render the application of the securities laws unnecessary.

1 Consequently, the notes are securities for purposes of the antifraud provisions of the Arizona
2 Securities Act.

3 **B. The Lender Agreements are Securities in the form of Investment Contracts**

4 Investment contracts are included in the definition of securities. A.R.S. § 44-
5 1801(26)(“Security means . . . investment contract . . .”). The core definition of an investment
6 contract was set forth in *S.E.C. v. W.J. Howey Co.*, 328 U.S. 293 (1946). Under the *Howey* test, an
7 investment contract exists if it involves (1) an investment of money or other consideration; (2) in a
8 common enterprise; and (3) with the expectation of profits earned solely from the efforts of others.¹

9 Arizona courts and the Commission have adopted the *Howey* test as the basis for investment
10 contract analysis. Citing *Howey*, Arizona courts agree that the definition of securities including
11 investment contracts embody “a flexible rather than static principle, one that is capable of
12 adaptation to meet the countless and variable schemes devised by those who seek to use the money
13 of others on the promise of profits.” *Nutek Information Systems, Inc. v. Arizona Corporation*
14 *Commission*, 194 Ariz. 104, 108, 977 P.2d 826, 830 (App. 1998); *Rose v. Dobras*, 128 Ariz. 209,
15 211, 624 P.2d 887, 889 (App. 1981). In accordance with this view, Arizona courts have developed
16 flexible interpretations for each of the three prongs set forth in *Howey*.

17 The Respondents sought the investment of money from investors. Investigator Clapper
18 testified that J. PARKHURST, C STREET, and PHOENIX raised \$879,300 from at least seven (7)
19 investors. Investigator Clapper also testified that three (3) of the investors received funds back
20 totaling \$55,040. As a result of that return, a total of \$824,260 remains owed to the investors.

21 With respect to the second element of *Howey*, “[t]wo tests have been developed to
22 determine the existence of a common enterprise in order to satisfy the second prong of the *Howey*
23 test: (1) the horizontal commonality test and (2) the vertical commonality test.” *Daggert v. Jackie*
24 *Fine Arts, Inc.*, 152 Ariz. 559, 565, 733 P.2d 1142, 1148 (App. 1986). Arizona courts have held
25

26 ¹ The *Howey* case originally used the phrase “solely from the efforts of others,” however, this language was later
modified to “substantially” in *SEC v. Glenn W. Turner Enterprises*, 474 F.2d 476, 482 (9th Cir. 1973).

1 that commonality will be satisfied if either horizontal or vertical commonality can be shown. *Id.* at
2 566.

3 To establish vertical form of commonality, a positive correlation between the potential
4 profits of the investor and the potential profits of the promoter need only be demonstrated. *Id.* at
5 566. The investors were to receive a split of the profits after the sale of a house that had been
6 rehabilitated. Without J. PARKHURST's ability to earn a return on the houses, the investors would
7 not receive a return. Therefore, the investors' success was tied directly to J. PARKHURST'S ability
8 to earn a return on the houses. This prong of the *Howey* test is satisfied.

9 In order to satisfy the third *Howey* prong in Arizona, one must only establish that the efforts
10 made by those other than the investors were the undeniably significant ones, and were those
11 essential managerial efforts that affected the failure or success of the enterprise. *Nutek*, 194 Ariz. at
12 108. According to the investors and Investigator Clapper, J. PARKHURST would identify,
13 purchase, and rehabilitate the real estate. Furthermore, J. PARKHURST would make all the
14 decision related to the rehabilitation. Therefore, efforts of Respondents affect the success or failure
15 of the investment satisfying the final prong of the *Howey* test.

16 **C. Respondents Violated the Anti-Fraud Provisions of the Arizona Securities Act.**

17 Under A.R.S. § 44-1991, it is a fraudulent practice and unlawful for a person, in connection
18 with a transaction or transactions within or from this state involving an offer to sell or buy
19 securities, or a sale or purchase of securities, to directly or indirectly do any of the following: (1)
20 employ any device, scheme or artifice to defraud; (2) make untrue statements of material fact, or
21 omit to state any material fact necessary in order to make the statements made, in the light of the
22 circumstances in which they were made, not misleading; or (3) engage in any transaction, practice
23 or course of business which operates or would operate as a fraud or deceit. A.R.S. § 44-1991(A).
24 Securities fraud may be proven by any one of these acts. *Hernandez v. Superior Court*, 179 Ariz.
25 515, 880 P.2d 735 (App. 1994).
26

1 In the context of these provisions, “materiality” requires a showing of substantial likelihood
2 that, under all the circumstances, the misstated or omitted fact would have assumed actual significance
3 in the deliberations of a reasonable buyer. *Trimble v. American Sav. Life Ins. Co.*, 152 Ariz. 548, 553,
4 733 P.2d 1131 (1986); citing *Rose v. Dobras*, 128 Ariz. 209, 214, 624 P.2d 887, 892 (App. 1981),
5 quoting *TSC Industries v. Northway, Inc.*, 426 U.S. 438, 96 S. Ct. 2126, 48 L. Ed. 2d 757 (1976).
6 Under this objective test, there is no need to investigate whether an omission or misstatement was
7 actually significant to a particular buyer. Additionally, the affirmative duty not to mislead potential
8 investors in any way places a heavy burden on the offeror and removes the burden of investigation
9 from the investor. *Trimble*, 152 Ariz. at 553. A misrepresentation or omission of a material fact in the
10 offer and sale of a security is actionable even though it may be unintended or the falsity or misleading
11 character of the statement may be unknown. In other words, scienter or guilty knowledge is not an
12 element of a violation of A.R.S. § 44-1991(A)(2). See e.g., *State v. Gunnison*, 127 Ariz. 110, 113, 618
13 P.2d 604 (1980). Stated differently, a seller of securities is strictly liable for any of the
14 misrepresentations or omissions he makes. *Rose v. Dobras*, 128 Ariz. at 214. Additionally, there is no
15 requirement to show that investors relied on the misrepresentations or omissions, *Rose*, 128 Ariz. at
16 214, or that the misrepresentations or omissions caused injury to the investors. *Trimble*, 152 Ariz. at
17 553. “Plaintiffs’ burden of proof requires only that they demonstrate that the statements were material
18 and misleading.” *Aaron v. Fromkin*, 196 Ariz. 224, 227, 314 P.2d 1039, 1042 (App. 2000).

19 Respondents violated A.R.S. § 44-1991 by:

20 a. J. PARKHURST and C-STREET, through J. PARKHURST, misrepresented to
21 Investor Reno that all of his funds would be used for property rehabilitation when some of the
22 funds were used to purchase the same residential property;

23 b. J. PARKHURST misrepresented to the investors that each of the investor’s funds
24 would be used to rehabilitate a residential property when the promised renovations did not occur;

1 c. J. PARKHURST and C-STREET, through J. PARKHURST, misrepresented to
2 Investors Olsen, Heinrich, and D'Aprile that they would pay monthly interest payments due on the
3 notes; and

4 d. Respondents failed to tell Investors Olsen, Heinrich and D'Aprile that the
5 Respondents did not have the financial resources to maintain ownership of the residential properties
6 purchased by the Respondents.

7 Any *one* of these actions would violate the Act. Taken together, they show Respondents
8 violated the Act and a cease and desist order should be issued to prevent further harm to the investing
9 public.

10
11 **VII. THE MARITAL COMMUNITY OF J. PARKHURST AND M.
12 PARKHURST IS LIABLE.**

13 During the relevant time frame, J. PARKHURST and M. PARKHURST were married,
14 residents of Arizona, and maintained a marital community. J. PARKHURST admits in his Answer
15 that M. PARKHURST is his spouse. Furthermore, Investigator Clapper learned from M.
16 PARKHURST's mother that they had been married since 1996. Finally, neither J. PARKHURST
17 nor M. PARKHURST presented any evidence to refute the liability of the marital community.

18 Pursuant to A.R.S. § 25-211, all property acquired by either husband or wife during the
19 marriage is the community property of the husband and wife except for property that is acquired by
20 gift, devise, descent or is acquired after service of a petition for dissolution of marriage, legal
21 separation or annulment. During marriage, "the spouses have equal management, control and
22 disposition rights over their community property and have equal power to bind the community."
23 A.R.S. § 25-214(B). In addition, "[...], either spouse may contract debts and otherwise act for the
24 benefit of the community. [...]" A.R.S. § 25-215(D). During the relevant time frame, J.
25 PARKHURST was acting for his own benefit and for the benefit of C-STREET and PHOENIX.
26 Such actions were for the benefit of the PARKHURSTs' marital community.

1 The clear and convincing standard is the standard of proof that a spouse must meet to rebut
2 each community property presumption. The Arizona Supreme Court has stated that, “the clear and
3 convincing standard is an intermediate standard, between proof beyond a reasonable doubt and
4 proof by a preponderance of the evidence, and that clear and convincing evidence is evidence that
5 makes the existence of the issue propounded ‘highly probable.’” *State v. King*, 158 Ariz. 419, 426,
6 763 P.2d 239, 246 (1988).

7 First, the PARKHURSTs failed to provide clear and convincing evidence that J.
8 PARKHURST was not acting in furtherance of the community. “(T)he presumption of law is, in the
9 absence of the contrary showing, that all property acquired and **all business done and transacted**
10 **during coverture, by either spouse, is for the community.**” *Johnson v. Johnson*, 131 Ariz. 38,
11 45, 638 P.2d 705, 712 (1981) (*emphasis added*). Therefore, the presumption is J. PARKHURST
12 was acting in furtherance of the community and intended to benefit the community since he
13 transacted business during marriage. Neither J. PARKHURST nor M. PARKHURST presented
14 any evidence or even contest the fact that J. PARKHURST was acting in furtherance of the
15 community during the relevant time frame. Therefore, based on the presumption in law and the
16 evidence presented, the Division established that J. PARKHURST was conducting business, acting
17 in furtherance of the marital community, intended to benefit the marital community and that
18 J.PARKHURST failed to refute the evidence or overcome the presumption with clear and
19 convincing evidence.

20 Second, the PARKHURST failed to rebut the presumption that a debt incurred during
21 marriage is a community obligation. The Arizona Court of Appeals has stated, “[a] debt incurred
22 by a spouse during marriage is presumed to be a community obligation; a party contesting the
23 community nature of a debt bears the burden of overcoming that presumption by clear and
24 convincing evidence.” *Hrudka v. Hrudka*, 186 Ariz. 84, 91, 919 P.2d 179, 186 (App. 1995).
25 Furthermore, “[...] a debt is incurred at the time of the actions that give rise to the debt. [*Citations*
26 *omitted*].” *Arab Monetary Fund v. Hashim*, 219 Ariz. 108, 111, 193 P.3d 802, 806 (App. 2008).

1 Here, the actions giving rise to the debt occurred early 2006 through 2007, while J.
2 PARKHURST and M.PARKHURST were married. The PARKHURSTs did not present any
3 evidence to rebut the presumption that the debt was a community obligation since either spouse
4 may contract debts and otherwise act for the benefit of the community. As outlined in the facts, the
5 Respondents offer and sale of the investments resulted in a benefit and debt to the community. The
6 debt was incurred during marriage and is presumed to be a community debt. Since the
7 PARKHURSTs failed to overcome this presumption, the debt remains a liability of the community.

8 Third, the PARKHURSTs failed to produce any evidence that the community did not
9 benefit or that PARKHURST's actions were not intended to benefit the community. As part of the
10 PARKHURSTs' burden, they were required to provide evidence refuting the community property
11 presumption of benefit to the community and if applicable, refute the Division's evidence of
12 community benefit. The hearing transcript and records are void of any material evidence refuting
13 the presumption or the Division's evidence. The failure by the PARKHURSTs to overcome this
14 community property presumption and the Division's evidence means that the liability of the
15 community is for the full amount of the debts incurred.

16 Based on the foregoing, any restitution and/or administrative penalty ordered will be a
17 community debt. The Commission and the Administrative Law Judge need not determine whether
18 the non-participating spouse had knowledge, participation, or intent, in order to bind the
19 community for the debt incurred. The presumption of PARKHURSTs intent to benefit the
20 community is enough to bind the community, even if M. PARKHURST was unaware or did not
21 approve of J. PARKHURST's actions. The *Ellsworth* court stated, "[i]f the husband acts with the
22 object of benefiting the community, a fact not questioned here, the obligations so incurred by him
23 are community in nature, whether or not the wife approved thereof." *Ellsworth v. Ellsworth*, 5 Ariz.
24 App. 89, 92, 423 P.2d 364, 367 (1967) citing *Donato v. Fishburn*, 90 Ariz. 210, 367 P.2d 245
25 (1961). Since the PARKHURSTs failed to meet their burden and present "highly probable"
26

1 evidence to rebut the presumptions or the Division's evidence, the debt is a joint and several
2 liability of J. PARKHURST and M. PARKHURST'S marital community.

3 Because there was no evidence of sole and separate property and no delineation of sole and
4 separate property, all funds are still presumed to be community funds. These funds resulted from
5 the businesses operated by J. PARKHURST and those businesses resulted in a debt of the
6 community.

7 VIII. CONCLUSION

8 The evidence presented at the hearing established that Respondents offered and sold securities
9 in the form of notes and investment contracts, within or from Arizona, and committed fraud while
10 doing so.

11 Based upon the evidence presented, the Division respectfully requests this tribunal to:

12 A. Order J. PARKHURST, C-STREET, and PHOENIX to cease and desist from further
13 violations of the Act pursuant to A.R.S. §44-2032;

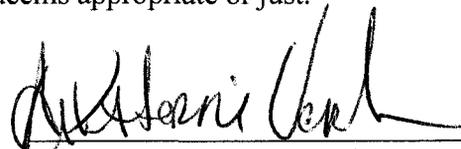
14 B. Order J. PARKHURST, C-STREET, and PHOENIX to pay an administrative penalty of
15 not less than \$70,000² pursuant to A.R.S. §44-2036(A);

16 C. Order J. PARKHURST, C-STREET, and PHOENIX to pay restitution of not less than
17 \$824,260 pursuant to A.R.S. §44-2032;

18 D. Order that J. PARKHURST acted for the benefit of his marital community and, pursuant
19 to A.R.S. §§ 25-214 and 25-215, this Order of restitution and administrative penalties is a debt of
20 the J. PARKHURST and M. PARKHURST'S marital community; and

21 E. Order any other relief this tribunal deems appropriate or just.

22 Dated this 8th day of July, 2010.

23 
24 Aikaterine Vervilos, Esq.
For the Securities Division

25 _____
26 ² Pursuant to A.R.S. §44-2036(A), the Commission is authorized to order administrative penalties in an amount not to exceed \$5,000 per violation. The Securities Division alleges violations of A.R.S. § 1991. The Securities Division seeks an administrative penalty of \$5,000 for each of the fourteen (14) violations of A.R.S. § 1991.

1 ORIGINAL AND THIRTEEN (13) COPIES
2 of the foregoing filed this
3 8th day of July, 2011, with:

4 Docket Control
5 Arizona Corporation Commission
6 1200 West Washington
7 Phoenix, AZ 85007

8 COPY of the foregoing hand-delivered this
9 8th day of July, 2011, to:

10 Administrative Law Judge Marc Stern
11 Arizona Corporation Commission/Hearing Division
12 1200 West Washington
13 Phoenix, AZ 85007

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15 8th day of July, 2011, to:

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