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BEFORE THE ARIZONA CORPORATION COMMISSION

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COMMISSIONERS

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

AZ CORP COMMISSION
DOCKET CONTROL

In the matter of:
CRAIG RANDAL MUNSEY, an unmarried man,
MARKETING RELIABILITY CONSULTING, LLC (d.b.a. MRC LLC), an Arizona limited liability company,
DENVER ENERGY EXPLORATION, LLC, a Texas limited liability company,
MICHAEL LEE CHRISTOPHER (CRD#2695315), an unmarried man
Respondents.

DOCKET NO. S-20804A-11-0208

REPLY IN SUPPORT OF SECURITY DIVISION'S POST-HEARING BRIEF

Assigned to Administrative Law Judge Marc E. Stern

The Securities Division ("Division") of the Arizona Corporation Commission ("Commission") submits this Reply in support of its Post-Hearing Brief ("Division Brief") and in response to the post-hearing submissions filed by Respondents. Many of the arguments raised by Respondents in their respective post-hearing submissions have been addressed in the Division's Brief and, to avoid duplication, will be cross-referenced in this Reply.

A. RESPONDENTS VIOLATED A.R.S. §§ 44-1841, 1842, & 1991.

Respondents do not dispute that the oil and gas well investments at issue in this matter are securities. See e.g. DEE and Christopher's Closing Brief, p. 7. In fact, the Division established that the investments offered and sold were both fractionalized undivided interests in oil or gas and also investment contracts.

Arizona Corporation Commission

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1 Instead, DEE and Christopher argue that they did not violate A.R.S. § 44-1841 and § 44-
2 1842, which, respectively, prohibit the offer and sale of unregistered securities in or from Arizona,
3 and prohibit unregistered dealers or salesmen from offering and selling securities in or from
4 Arizona. They also argue that there was no fraud pursuant to A.R.S. § 44-1991. As shown in the
5 Division's Brief, there was ample evidence at hearing of both offers and sales of the oil and gas well
6 investment in and from Arizona, of lack of registration, and of fraud. *See* Division Brief, at pp. 13-
7 24.

8 **1. Intent is not a requirement for a violation, nor a defense.**

9 Throughout their closing brief, DEE and Christopher argue that the Division failed to
10 establish "intentional" violations the Securities Act. Respondents misstate the standard required
11 under the Securities Act. Violations of A.R.S. §§ 44-1841, 44-1842 and 44-1991(A)(2) require no
12 intent or scienter. *See Eastern Vanguard Forex Ltd. v. Ariz. Corp. Com'n*, 206 Ariz. 399, 414, 79
13 P.3d 86, 101 (App. 2003); *Allstate Life Insurance Company v. Baird & Co., Inc.*, 756 F.Supp.2d
14 1113 (2010); *State v. Gunnison*, 127 Ariz. 110, 113, 618 P.2d 604, 609 (1980); *State v. Burrows*, 13
15 Ariz. App. 130, 474 P.2d 849 (1970). The Division does not have the burden of proving
16 Respondents' intent to violate, or knowledge that they were violating, the Securities Act. Further,
17 Respondents cannot use these arguments as a defense.

18 For a violation of A.R.S. § 44-1841 and § 44-1842, the Division need only establish that
19 Respondents were offering and/or selling securities and the Respondents and the securities were not
20 registered. The Division established this at hearing. *See* Division Brief, p. 13. In addition, for a
21 violation of A.R.S. § 44-1991(A)(2), the Division is required to show that the Respondents, directly
22 or indirectly, made an untrue statement of material fact, or omitted to state any material fact
23 necessary in order to make the statements made, in the light of the circumstances under which they
24 were made, not misleading or operated as a fraud or deceit. *See* A.R.S. § 44-1991(A)(2). This was
25 also established. *See* Division Brief, p. 13-18. Again, no scienter is necessary, nor is lack of it a
26 defense.

1 DEE and Christopher attempt to pass the blame for the violations of A.R.S. § 44-1842 to
2 DEE's salesmen, including Munsey. They claim that the independent contractor agreements
3 contained an addendum requiring the salesmen to be registered if state law required such
4 registration. *See* DEE and Christopher's Closing Brief, p. 10. The only addendum containing this
5 language that was introduced at hearing was undated and signed by Munsey. (Ex. S-8, at
6 ACC000440). No such addenda were produced for DEE's other salesmen, including Don Howard
7 who sold to one Arizona investor, and Randall Becklund who sold the DEE investments from
8 Arizona. (Ex. S-9).

9 The argument that DEE and Christopher appear to be making is that, because they intended
10 their salesmen to be registered per the language of the addendum, they are not liable for non-
11 registration. Again, as stated above, intent is not an element or defense to A.R.S. § 44-1842. There
12 is no "reasonable reliance" defense. The salesmen either were or were not registered, and here, they
13 were not. Even if reliance was a factor, which it is not, the reliance would not be reasonable because
14 the language of the addendum does not verify that Munsey was a registered salesman at the time he
15 signed the addendum. (Ex. S-8). Munsey testified that he responded to a Craigslist ad posted by
16 DEE for salesmen, and that the ad had no requirements for the salesmen to be registered, nor did he
17 recall discussing his registration status during the interview. (H.T. p. 179:4-9, p. 184:22 – p.
18 185:20). Further, DEE could have easily checked the FINRA website or with the Division to
19 determine the salesmen's registration status (or lack thereof) to guard against violations of A.R.S. §
20 44-1842. Respondent's attempt to distract the focus to that of intent is disingenuous and must be
21 rejected.

22 Finally, pointing the finger at the salesmen does not relieve DEE from its own registration
23 requirements under A.R.S. § 44-1842. Section 44-1842 requires both a salesman and a *dealer*
24 offering and selling securities to be registered. A.R.S. § 44-1801(9)(b) defines "dealer" to include
25 an issuer, such as DEE.

26 ///

1 **2. Munsey was not acting as a finder.**

2 Although not directly raised as an argument by Munsey, and referenced in passing with no
3 legal authority by DEE and Christopher, Munsey refers to himself several times as a “finder” in his
4 closing submission. *See* Munsey Closing Brief dated November 30, 2012; DEE and Christopher’s
5 Closing Brief, p. 3. There is no basis for a finding that Munsey acted as a finder as opposed to a
6 salesman when offering and selling the DEE investments.

7 The “finder” argument is an attempt by Munsey to avoid the registration requirements of
8 a salesman under A.R.S. § 44-1842. In interpreting federal registration requirements similar to
9 the Arizona statute, the Securities and Exchange Commission (“SEC”) has issued numerous no-
10 action letters that establish when a person is acting as a “finder”, which does not require
11 registration, and that of a broker or salesman, which does require registration. The “finder”
12 classification is very narrow and applies to a person who makes a referral of a potential purchaser
13 of securities to an issuer. A finder is limited to doing little more than providing the issuer the
14 name and phone number of the prospective investor to qualify. *See* SEC No Action Letter re:
15 Paul Anka, 1991 WL 176891 (July 24, 1991); *see also Ten Often Asked Questions About an*
16 *Issuer’s Ability to Obtain Investors in Private Placements*, SF71 ALI-ABA 41, 43 (March 15,
17 2001) (“A finder is a person, be it a company, service or individual, who brings together buyers
18 and sellers for a fee, but who has no active role in negotiations and may not bind either party to
19 the transaction.”)

20 The SEC has repeatedly referenced that a finder does not engage in negotiations,
21 substantive discussions, or communications with the potential investors regarding the investment.
22 *See* SEC No Action Letter re: Paul Anka, 1991 WL 176891; SEC No Action Letter re: Richard
23 Appel, 1983 WL 30911 (February 14, 1983). Here, Munsey acted as much more than a finder.
24 He contacted potential investors with whom he had no pre-existing relationship and discussed the
25 investment opportunity at length. (H.T. p. 128:14-17; Ex. S-126). Munsey also emailed
26

1 potential investors investment materials, including prospectuses. (H.T. p. 123:3-25, p. 131:6-9,
2 p. 139:21 – p. 141:10; Exs. S-57, S-58, S-63, S-64).

3 Importantly, the SEC has continuously pointed to one factor that negates a finding that a
4 person is acting as a finder – commission based compensation. This is considered a “red flag”
5 toward a finding that the person should have been a registered broker or salesman. When a
6 person that receives transaction-based compensation for effecting or inducing, or attempting to
7 induce, another’s purchase or sale of securities, this negates a person’s “finder” status, and
8 instead requires that person to be registered. *See* SEC No Action Letter re: Brumberg, Mackey &
9 Wall, P.L.C., 2010 WL 1976174 (May 17, 2010); *see also* SEC Release No. 61884, 2010 WL
10 1419216, *2 (April 9, 2010) (“Indeed, the receipt of transaction- based compensation often
11 indicates that such a person is engaged in the business of effecting transactions in securities.”)
12 Here, Munsey received commission-based compensation based on the amount of his investor’s
13 investments. (H.T. p. 121:5-19, p. 138:12-20, p. 146:1-5). Munsey does not qualify as a finder
14 and instead, was a salesman that was required to be registered under A.R.S. § 44-1842. *See* SEC
15 Release No. 61884, 2010 WL 1419216, *2 (“Registration helps to ensure that persons who have
16 a ‘salesman’s stake’ in a securities transaction operate in a manner that is consistent with
17 customer protection standards governing broker-dealers and their associated persons.”)

18 **3. Respondents have no defense to violations of A.R.S. § 44-1991.**

19 DEE and Christopher attempt to argue that, because they told investors that the oil and gas
20 investments were risky, there was no fraud. In fact, the Division has not alleged, nor did it argue at
21 hearing, that the fraud was a failure to disclose the generalized “riskiness” of the investment. *See*
22 Amended Notice of Opportunity. Instead, the fraud is much more specific: (1) failing to disclose a
23 previously issued securities cease and desist order against DEE; and (2) making representations
24 about existing production from various wells that were false at the time the statements were made.

25 It should not go unnoticed that DEE and Christopher avoid using the term “order” when
26 referencing the Pennsylvania proceedings. Instead, they attempt to downplay the securities violation

1 by referencing it as “[t]he alleged non-disclosure of the Pennsylvania \$1,500 fine”. The simple fact
2 is that there is an order against DEE by the Pennsylvania Securities Commission relating to the same
3 type of investment as is at issue in the Arizona proceedings. (Exs. S-3, S-4). The Division’s
4 Opening Brief adequately counters DEE and Christopher’s argument that the failure to disclose the
5 2010 Pennsylvania securities order was not material. In fact, Arizona law and opinions from other
6 jurisdictions interpreting identical fraud provisions in the federal securities laws establish that this
7 lack of disclosure was material as a matter of law. See Brief, pp. 14-16. The simple fact is that it
8 was not up to DEE and Christopher to decide for the investors whether or not the Pennsylvania order
9 was material or not, and thus fail to disclose it.¹ In fact, if it was not material as Respondents
10 suggest, why hide it from investors?

11 DEE and Christopher do not address the second fraud – misrepresentation of production
12 from various oil and gas wells. To be clear, the Division’s allegation of fraud is not that the
13 *projected* production for these wells was misrepresented, but that *actual* production at the time
14 was misrepresented. The Division established at hearing that DEE and Munsey made
15 representations to potential investors that the Koomey/Morrison #3 well (the subject of the
16 purportedly immaterial Pennsylvania order) was substantially producing, and that all of the wells
17 on the Johnson 3 Well project were producing, as well as the “Karber” well. See Brief, pp. 16-
18 18. Texas Railroad Commission (“TRRC”) reports introduced into evidence at hearing provide
19 the evidence that these statements were misrepresentations. *Id.*

20 Munsey tangentially raises the issue of the validity of the TRRC reports in his closing
21 submission claiming the TRRC is “months behind” in updating the production reports on their
22 website. See Munsey Closing Brief dated November 30, 2012, ¶ 8. The only testimony at
23

24 ¹ DEE and Christopher also appear to insinuate that they are not responsible for the failure to disclose the Pennsylvania
25 order to investors because their independent contractor agreements with the salesmen require the salesmen to be
26 “honest” with the prospective investors. See DEE and Christopher’s Closing Brief, p. 11. However, there was no
evidence presented at hearing that the Pennsylvania order was disclosed to the salesmen or that they were directed to
disclose its existence to potential investors. In fact, based on Munsey’s closing submission, he was never told about
the Pennsylvania order. See Munsey Closing Brief dated November 30, 2012, ¶ 4. Further, this does not excuse
DEE’s failure to disclose the Pennsylvania order in the investor materials it prepared. This attempt to shift blame to
the salesmen has no basis in law or fact.

1 hearing supporting such a backlog came from Christopher where he testified that the TRRC is up
2 to six months backlogged in processing such reporting. (H.T. p. 468:11-20). Even assuming
3 this is true, the reports run on July 31, 2012, from the TRCC website would be current and
4 correct as of January 2012. Thus, the reports showing production – in this case, lack thereof – in
5 2010 and 2011 would be up to date.

6 **B. CHRISTOPHER HAS CONTROL PERSON LIABILITY.**

7 Christopher incorrectly argues that he is not a controlling person liable under A.R.S. § 44-
8 1999(B). The Division alleged and proved at hearing that Christopher was a controlling person
9 of DEE. Section 44-1999 of the Securities Act makes a controlling person jointly and severally
10 liable with and to the same extent as the controlled person.

11 The Securities Act, “attaches vicarious or secondary liability to “controlling persons” as it
12 does to a person or entity that commits a primary violation of §§ 44–1991 or 1992.” *Facciola v.*
13 *Greenberg Traurig, LLP*, 781 F. Supp. 2d 913, 922-23 (D. Ariz. 2011); *see also Eastern*
14 *Vanguard Forex Ltd. v. Ariz. Corp. Com’n*, 206 Ariz. at 412, 79 P.3d at 89 (App. 2003). The
15 Brief submitted by the Division outlined the evidence presented at hearing that established
16 Christopher was a controlling person of DEE, the issuer and a primary violator of the antifraud
17 provisions of the Securities Act. *See* Brief, pp.18-20. Control person liability attaches to the
18 primary fraud violations by DEE under A.R.S. § 44-1999(B).

19 As noted in Section IV(B) of the Division’s Brief, the Division alleged and proved at
20 hearing the primary fraud violations by DEE. DEE violated the antifraud provision of the
21 Securities Act by the lack of disclosure of the Pennsylvania securities order to potential and
22 actual investors. By virtue of Christopher’s control over DEE, something that Christopher does
23 not appear to dispute in the closing brief, he is jointly and severally liable with DEE for these
24 violations. Christopher does not address this direct fraud by DEE, and his resulting control
25 person liability, at all.

26

1 Christopher attempts to argue that he acted in “good faith”, claiming that he did not
2 directly or indirectly induce the underlying fraud of the DEE salespersons, and did not know
3 about Munsey’s actions. The Division proved at hearing that both the offering materials and oral
4 representations by Munsey concerning oil production from various wells were fraudulent. *See*
5 Division Brief, pp. 16-18. Christopher cannot claim he did not know about this because Munsey
6 testified that all of the offering materials came from DEE, as well as the information that Munsey
7 orally represented to offerees. (H.T. p. 122:13 – p. 124:25). As a result, Christopher fails to
8 establish the affirmative defense of “good faith” because he cannot meet the language of the
9 statute that requires a showing that the control person “did not directly or indirectly induce the
10 act underlying the action.”² DEE induced the oral misrepresentations and the dissemination of
11 written misrepresentations made by its salesman regarding, and since Christopher controlled
12 DEE, he is jointly and severally liable for the violations.

13 **C. RESPONDENTS DID NOT ESTABLISH ANY EXEMPTION.**

14 Respondents ineffectively attempt to argue a Rule 506 exemption, also known as the safe
15 harbor non-public offering exemption. However, the issuer, DEE, did not comply with Rule 506.
16 Respondents failed to meet their burden to prove an exemption exists.³ 15 U.S.C. § 77r provides for
17 federal preemption of state registration requirements for “covered securities”, which include a
18 transaction exempt from registration pursuant to SEC rules or regulations, such as Rule 506.
19 However, there must be actual compliance with Rule 506 at the federal level before state registration
20 requirements can be preempted. *See e.g. Brown v. Earthboard Sports USA*, 481 F.3d 901 (6th Cir.
21 2007). Actual compliance on the federal level is not a state-specific inquiry, and instead must
22 include analysis of *all* offers and sales for that particular offering. Respondents’ attempt to restrict

23 ² The burden of proof of establishing the good faith affirmative defense is on the controlling person – here,
24 Christopher. *See Eastern Vanguard Forex Ltd. v. Ariz. Corp. Com’n*, 206 Ariz. at 413, 79 P.3d at 100.

25 ³ DEE and Christopher insinuate that the Division has the burden to effectively disprove an exemption. As noted in the
26 Division’s Brief, Respondents have the burden of proof on establishing the applicability of any exemption. *See* Division
Brief, p. 23. Under the Securities Act, the burden of establishing an exemption from registration is upon the party
claiming it. *See* A.R.S. § 44-2033. Our Supreme Court has held that, “[b]ecause of the vital public policy underlying the
registration requirement, there must be strict compliance with all the requirements of the exemption statute.” *State v.*
Baumann, 125 Ariz. 404, 411, 610 P.2d 38, 45 (1980) (*en banc*).

1 their analysis for this exemption to offers and sales in and from Arizona is inappropriate when Rule
2 506 (and any other federal exemption for that matter) contains no such state-specific limitation.

3 As acknowledged by DEE and Christopher, a Rule 506 private offering exemption
4 requires offers and sales satisfy the terms and conditions of 17 C.F.R. §§ 230.501 and 230.502
5 and contains substantive purchaser limitations. *See* 17 C.F.R. § 230.506. Again, Respondents
6 ignore that the analysis of these requirements is on the federal level, i.e. all offers and sales, and
7 is not limited to those made in or from Arizona.

8 **1. Respondents failed to prove all offers and sales met the requirement of**
9 **§ 230.506(b)(2)(ii).**

10 As noted in the Division's Brief, in order to qualify under Rule 506, the issuer must prove
11 that they complied with Rule 230.506(b)(2)(ii), which requires that the security be sold to only
12 accredited investors and no more than thirty-five non-accredited investors who are sophisticated
13 purchasers. Again, DEE and Christopher inappropriately focus their analysis under this prong on
14 the investments sold in or from Arizona. To obtain the federal exemption, and thus qualify to
15 preempt any state registration requirement, *all* investors must be evaluated under this
16 requirement, not just those in or from Arizona. DEE cannot prove that its unaccredited investors
17 were sophisticated.

18 DEE's own Form D filing upon which they base their purported exemption states that
19 there were seven unaccredited investors. (**Ex. S-114**). Given that this Form D filing was
20 submitted on October 14, 2010, this does not even include Lori Cook, who did not invest until
21 2011. (**Ex. S-35**). Thus, there were at least eight unaccredited investors. To obtain the
22 exemption, DEE was required to prove that each of these investors was "sophisticated" as the
23 Rule requires. *See Mark v. FSC Sec. Corp.*, 870 F.2d 331, 334 (6th Cir. 1989) (Respondent "is
24 required to offer evidence of the issuer's reasonable belief as to the nature of *each* purchaser.").

25 The term "sophisticated" refers to the requirement that the purchaser "has such
26 knowledge and experience in financial and business matters that he is capable of evaluating the

1 merits and risks of the prospective investment.” 17 C.F.R. §§ 230.506(b)(2)(ii)). Christopher
2 admitted at hearing that he did not know the names of the seven unaccredited investors
3 referenced in the Form D, and could not provide any information or documentary evidence on
4 their backgrounds to establish that they were sophisticated. (H.T. p.465:18 – p. 466:19). In fact,
5 the only unaccredited investor that Christopher could identify by name was Arizona investor Lori
6 Cook. Christopher was only able to state that Ms. Cook was an accountant, and “pretty sharp”,
7 but that he had never met her, and that she had no experience in investing in oil and gas. (H.T. p.
8 472:15 – p. 473:10, p. 460:18-25). Simply because Ms. Cook has an accounting degree does not
9 make her sophisticated in evaluating the merits of an oil and gas investment where she has never
10 done so before. See 17 C.F.R. §§ 230.506(b)(2)(ii) (requiring that the unaccredited investor be
11 “capable of evaluating the merits and risks of **the prospective investment**”) (emphasis added).

12 Respondents failed to provide any evidence to prove that all unaccredited investors were
13 sophisticated at the time of investment or that there was a reasonable belief of sophistication.
14 For this reason alone, DEE failed to prove it qualifies for a Rule 506 exemption.

15 **2. DEE did not prove it complied with §§ 230.501 and 230.502.**

16 In order to establish a Rule 506 exemption, an issuer must also prove that all offers and
17 sales meet the terms and conditions of §§ 230.501 and 230.502. See 17 C.F.R. § 230.506(b)(1).

18 **ii. 17 C.F.R. § 230.502(b)(1)**

19 Rule 230.502(b)(1) requires certain information be furnished to unaccredited investors:
20 “When information must be furnished. If the issuer sells securities under § 230.505 or § 230.506
21 to any purchaser that is not an accredited investor, the issuer shall furnish the information
22 specified in paragraph (b)(2) of this section to such purchaser a reasonable time prior to sale.”
23 Section (b)(2) requires substantive information about the offering be provided to unaccredited
24 investors including, *inter alia*, “the same kind of information as required in Part I of a registration
25 statement filed under the Securities Act” and a financial statement of the issuer. See 17 C.F.R. §
26 230.506(b)(2). Respondents submitted no evidence that they complied with this provision for

1 any of their eight unaccredited investors. For this reason alone, DEE fails to qualify for the Rule
2 506 exemption.

3 **iii. 17 C.F.R. § 230.502(c)**

4 As noted in the Division's Brief, DEE was also required to prove that there were no offers
5 or sales by means of general solicitation or general advertising by the issuer or anyone acting on
6 its behalf. *See* 17 C.F.R. § 230.502(c). DEE has not and cannot prove it did not use general
7 solicitation or advertising in the offer and sale of the DEE investments. *See* Division Brief, pp.
8 24-26.

9 In order to get a Rule 506 exemption, DEE was required to establish that each investor
10 and offeree had a pre-existing business relationship with DEE. The relationship must be
11 established *prior to the offering* that is the subject of the Regulation D exemption. *See E.F.*
12 *Hutton Co.*, SEC No-Action Letter, 1985 WL 55680, *1 (Dec. 3, 1985). At hearing, Christopher
13 testified that DEE and Christopher had no pre-existing relationship with any of the offerees or the
14 investors that invested in DEE. (H.T. p. 253:8-11, p. 263:25 – p. 264:3, p. p. 264:23 – p. 265:4,
15 p. 265:19-24, p. 274:13-19). This alone precludes the exemption.

16 DEE and Christopher attempt to argue they had a pre-existing relationship with its
17 purchasers and offerees because they only offered and sold to those on “prequalified . . .
18 accredited investor lead lists.” Even assuming the purchase of such lists is sufficient to establish
19 the requisite relationship, which it is not, Respondents provided no evidence that *all* offerees and
20 purchasers came from these lead lists. Respondents focused on Arizona offers and sales, and did
21 not establish that all offerees and purchasers in all states came from these lists. And even in
22 Arizona, offers were made to individuals that were not on the lead lists. (Exs. S-57, S-58, S-98,
23 S-126).

24 Even if DEE and Christopher were able to establish that all offers and sales came from
25 the lead lists, this does not establish that there was no general solicitation. *See Interpretive*
26 *Release on Regulation D*, SEC Release No. 33-6455, 1983 WL 409415, Q.60 (Mar. 3, 1983)

1 ("The mere fact that a solicitation is directed only to accredited investors will not mean that the
2 solicitation is in compliance with Rule 502(c)" because "Rule 502(c) relates to the nature of the
3 offering not the nature of the offerees."). Respondents attempt to create a pre-existing
4 relationship to avoid general solicitation by arguing that the lead lists they purchased provide
5 them with the requisite information and relationship with each offeree and purchaser.
6 Respondents cite to Lamp Technologies and H.B. Shane & Co., two SEC No-Action Letters,
7 both of which do not support this argument.

8 First, *H.B. Shane & Co.* involved a registered broker-dealer issuing questionnaires to
9 potential investors to establish a pre-existing relationship to avoid the general solicitation
10 prohibition. See SEC No Action Letter re: *H.B. Shane & Co.*, 1987 WL 108648 (May 1, 1987).
11 The SEC stated that, as long as sufficient time elapsed between the completion of the
12 questionnaire and any offering, "a satisfactory response by a prospective offeree to a
13 questionnaire that provides a broker-dealer with sufficient information to evaluate the
14 respondent's sophistication and financial situation will establish a substantive relationship." *Id.*
15 Here, there was no evidence that the lead list brokers were registered broker-dealers, nor any
16 specific evidence of the procedures that each lead list broker utilized to establish the substantive
17 relationship. In fact, Christopher simply took the lead brokers at their word that the individuals
18 in the lead lists were "accredited"; Christopher guessed at what procedures they employed and
19 DEE failed to produce any materials from the lead list brokers that showed their efforts to qualify
20 these individuals, if in fact any were used, including questionnaires. (H.T. p. 329:10 – p. 330:6,
21 p. 425:2 – p. 426:3). In fact, it appears that DEE had reason to believe the lead lists the brokers
22 sold them were inaccurate. (H.T, p. 436:8-20; Ex. M-2).

23 Lamp Technologies also fails to support Respondents' argument. In Lamp Technologies,
24 the SEC staff determined that the proposed operation of a website would not involve a general
25 solicitation since it was password-protected and accessible only to members who had been pre-
26 qualified via a detailed questionnaire as accredited investors. See SEC No Action Letter re:

1 Lamp Technologies, 1997 WL 282988 (May 29, 1997). However, the SEC has since issued
2 guidance on this No Action Letter: “We understand that securities lawyers may have interpreted
3 staff responses to Lamp Technologies, Inc. as extending the ‘pre-existing, substantive
4 relationship’ doctrine to solicitations conducted by third parties other than a registered broker-
5 dealer. See Divisions of Investment Management and Corporation Finance no-action letters
6 Lamp Technologies, Inc. (May 29, 1998) and Lamp Technologies, Inc. (May 29, (1997). We
7 disagree.” *See* SEC Release No. 7856 (April 28, 2000). The SEC has made it clear that
8 utilization of appropriate detailed questionnaires *when used by registered broker-dealers* may be
9 an appropriate way to establish a substantive pre-existing relationship, if done correctly and
10 appropriate waiting periods are in place. Again, there was no evidence at hearing that the lead
11 list brokers utilized by DEE were registered broker-dealers, nor any evidence of the use of
12 detailed questionnaires by the lead list brokers. Further, DEE did not use these lead list brokers
13 to offer their investments, but used third party salesman who had no part in the lead list broker
14 process.

15 Respondents also argue that the DEE website was not general advertising because certain
16 language was placed in the footer of the webpage indicating that it was not a solicitation. *See*
17 DEE and Christopher’s Closing Brief, p. 8. However, it begs the question, if the website was not
18 a general solicitation, why did it caution on every page of the website that “THERE ARE
19 SIGNIFICANT RISKS ASSOCIATED WITH INVESTING IN OIL AND GAS VENTURES.”
20 (Ex. S-72). Further, the website allowed potential investors to input their information into the
21 DEE website to “request information”. (Ex. S-72). Further, counsel misrepresents the testimony
22 of Christopher at hearing regarding whether there were any inquiries of anyone interested in
23 purchasing the DEE investments via the DEE website. Christopher’s answer to this question was
24 not “no” it was “not that I know of, no.” (H.T. p. 337:13-16). In fact, the Division established at
25 hearing that at least one offeree was provided offering materials for the joint ventures after
26 representing to DEE that he had visited the DEE website. (Exs. S-57, S-58, S-98). Munsey

1 contacted this individual as a result.

2 **3. Respondents cite to inapplicable law.**

3 DEE and Christopher have also disingenuously cited to inapplicable law in an attempt to
4 avoid the effect of their actions. Specifically, Respondents cite to 15 U.S.C. § 77d, which now
5 allows general solicitation and advertising in certain instances. This change was made as a part of
6 the Jumpstart Our Business Startups Acts (“JOBS Act”). A copy of the full text of the JOBS Act is
7 attached as Exhibit A. Respondents fail to note that this amendment to the statute took place in
8 *April 2012*, and prior to that contained no such language. *See* 15 U.S.C. § 77d (2010). Further,
9 Respondents also fail to note that the newly amended statute contains no provision allowing for
10 retroactivity. *See e.g. Bowen v. Georgetown University Hospital*, 488 U.S. 204, 208, 109 S.Ct. 468,
11 471 (1988) (“Retroactivity is not favored in the law. Thus, congressional enactments and
12 administrative rules will not be construed to have retroactive effect unless their language requires
13 this result.”).

14 Even if the statute were somehow deemed retroactive to apply to the DEE investments
15 offered and sold in 2010 and 2011, the amended text of Section 77d specifically requires SEC
16 rulemaking on Rule 506 before the amendment is effective. *See* 15 U.S.C. § 77d(b) (2012) (“Offers
17 and sales exempt under [Rule 506] (as revised pursuant to section 201 of the Jumpstart Our Business
18 Startups Act) shall not be deemed public offerings under the Federal securities laws as a result of
19 general advertising or general solicitation.”). Further, once modified as required by the JOBS Act,
20 Rule 506 exemptions may allow public advertising or solicitation, but *all* purchasers of the securities
21 must be accredited investors. *See* JOBS Act, attached as Exhibit A, at Title II, § 201. Thus, even if
22 retroactive, which it is not, DEE cannot establish the exemption under the new statute as it sold to at
23 least eight unaccredited investors.⁴

24 ⁴ DEE and Christopher relegate to a footnote vague references to R14-4-140, R14-4-126, and A.R.S. § 44-1844. It is
25 unclear if Respondents are arguing an exemption exists under these provisions. R14-4-140 requires compliance with
26 17 C.F.R. § 230.504, which only applies to sales not exceeding \$1,000,000. Here, Christopher admitted that sales
exceeded \$5,000,000. (H.T. p. 277: 23 – p. 278:12). Further, sales must be made to only accredited investors. *See*
R14-4-140 (D). Sales were made to at least eight unaccredited investors. For either of these reasons, DEE cannot
establish an exemption under R14-4-140. Further, for the same reason as Respondents cannot establish a Rule 506
exemption, they cannot establish an exemption under R14-4-126, Arizona’s private offering counterpart. Finally,

1 1. Order DEE, Christopher, Munsey, and MRC, pursuant to A.R.S. § 44-2032(1), to
2 jointly and severally pay restitution in the amount of \$372,279.40 (\$420,407.25 minus \$48,127.85
3 reflected in investor repayments), plus pre-judgment interest from the date of each investor's
4 investment as set forth in Exhibit S-128 (interest rate to be calculated at the time of judgment
5 under A.R.S. § 44-1201);

6 2. Order DEE, Christopher, Munsey, and MRC to pay an administrative penalty of not
7 more than five thousand dollars (\$5,000) for each violation of the Act, as the Court deems just and
8 proper, pursuant to A.R.S. § 44-2036(A). The Division recommends DEE, Christopher, Munsey,
9 and MRC to pay jointly and severally an administrative penalty in the amount of \$200,000.00.

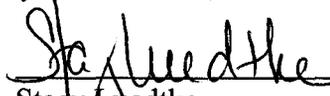
10 3. Order DEE, Christopher, Munsey, and MRC to cease and desist from further
11 violations of the Act pursuant to A.R.S. § 44-2032.

12 4. Order any other relief this tribunal deems appropriate or just.

13

14 RESPECTFULLY SUBMITTED this 19th day of December, 2012.

15



Stacy Luedtke
Attorney for the Securities Division of the
Arizona Corporation Commission

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19 ORIGINAL AND THIRTEEN (13) COPIES of the foregoing
filed this 19th day of December, with:

20

Docket Control
Arizona Corporation Commission
1200 W. Washington St.
Phoenix, AZ 85007

21

22

23 COPY of the foregoing hand-delivered
this 19th day of December, to:

24

Mr. Marc E. Stern
Administrative Law Judge
Arizona Corporation Commission/Hearing Division
1200 W. Washington St.
Phoenix, AZ 85007

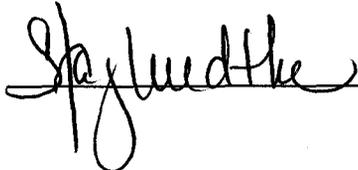
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26

1 COPY of the foregoing mailed
2 this 19th day of December, to:

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16 By:  _____
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