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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

BOB STUMP - Chairman
GARY PIERCE
BRENDA BURNS
BOB BURNS
SUSAN BITTER SMITH

Arizona Corporation Commission

DOCKETED

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IN THE MATTER OF:

PATRICK LEONARD SHUDAK, an unmarried man,
PROMISE LAND PROPERTIES, LLC, an Arizona
limited liability company,
and
PARKER SKYLAR & ASSOCIATES, LLC, an
Arizona limited liability company,

RESPONDENTS.

DOCKET NO. S-20859A-12-0413

DECISION NO. 74743

OPINION AND ORDER

DATES OF PRE-HEARING CONFERENCES: November 8, 2012, January 10, 2013, and May 13, 2013

DATES OF HEARING: June 17, 18, and 19, 2013

PLACE OF HEARING: Phoenix, Arizona

ADMINISTRATIVE LAW JUDGE: Marc E. Stern¹

APPEARANCES: Mr. Brian J. Schulman, GREENBERG TRAURIG, LLP, on behalf of Respondent Patrick Leonard Shudak; and

Mr. Ryan Millecam, Staff Attorney, on behalf of the Securities Division of the Arizona Corporation Commission.

BY THE COMMISSION:

On September 21, 2012, the Securities Division ("Division") of the Arizona Corporation Commission ("Commission") filed a Notice of Opportunity for Hearing ("Notice") against Patrick Leonard Shudak, an unmarried man, Promise Land Properties, LLC, an Arizona limited liability company ("PLP"), and Parker Skylar & Associates, LLC, an Arizona limited liability company

¹ Administrative Law Judge Belinda A. Martin wrote the Recommended Opinion and Order.

1 (“PSA,” and together with Mr. Shudak and PLP, the “Respondents”) in which the Division alleged
 2 multiple violations of the Arizona Securities Act, Arizona Revised Statutes (“A.R.S.”) § 44-1801, *et*
 3 *seq.* (“Securities Act”).

4 * * * * *

5 Having considered the entire record herein and being fully advised in the premises, the
 6 Commission finds, concludes, and orders that:

7 **FINDINGS OF FACT**

8 **The Respondents**

9 **Patrick Leonard Shudak**

10 1. Mr. Shudak is an unmarried man² who resided in Arizona and was the manager of
 11 both PLP and PSA at all times relevant to this matter. Mr. Shudak also controlled a number of other
 12 companies,³ including Spirit Graphics, LLC, a sales and marketing company (“Spirit Graphics”),⁴
 13 and Sticks, Stones and Dirt, LLC (“Stick, Stones and Dirt”), a real estate investment company.⁵ At
 14 the time of the hearing in June 2013, Mr. Shudak lived in Hawaii.⁶

15 2. The Division issued a Certification of Non-Registration certifying that between May
 16 1, 2007, to April 14, 2013, Mr. Shudak was not registered with the Commission as a securities
 17 salesman or dealer pursuant to Article 9 of the Securities Act (A.R.S. § 44-1941, *et seq.*); and had not
 18 made a notice filing and was not licensed with the Commission as an investment adviser or an
 19 investment advisor representative pursuant to Article 4 of the Arizona Investment Act (A.R.S. § 44-
 20 3151, *et seq.*).⁷

21 _____
 22 ² Patrick and Lisa Shudak divorced in May 2009. Hearing Exhibit (“Ex. ___”) S-6, page 45.

23 ³ Pursuant to Arizona Administrative Code (“A.A.C.”) R14-3-109(T), Official Notice is taken of the organizational
 24 documents for the entities controlled and/or managed by Mr. Shudak, which are public records and can be found at the
 25 Commission’s Corporations Division website.

26 ⁴ Ex. S-6, pages 7, 46. Mr. Shudak was the sole member of Spirit Graphics. On November 11, 2008, a lawsuit was filed
 27 in Maricopa County Superior Court against co-defendants Spirit Graphics, Patrick Shudak and Lisa Shudak. Ex. S-43.
 28 See also, Ex. S-6, page 42. On August 14, 2009, the Commission issued a Certificate of Dissolution to Spirit Graphics
 for failure to maintain a statutory agent.

⁵ Ex. S-6, pages 7, 46. Ex. S-6 lists Mr. Shudak as a 35 percent owner of this LLC, Jill and Todd Noetzelman as 35
 percent owners, and Darren and Esther Griggs as 30 percent owners. Exs. S-41 and S-42 contain copies of foreclosure
 actions filed in Maricopa County Superior Court on September 8, 2008, and September 17, 2008, against co-defendants
 Sticks, Stones and Dirt, Patrick and Lisa Shudak, the Noetzelmans and the Griggs, and copies of the resulting default
 judgments. See also Ex. S-6, page 42. The LLC has not been dissolved.

⁶ Transcript of Hearing, page 363 (hereinafter, “Tr. at ___”).

⁷ Ex. S-3.

Promise Land Properties, LLC⁸

3. PLP is an Arizona manager-managed limited liability company. It originally was organized under the name Tombstone Holdings, LLC on March 1, 2007, by Mr. Shudak and Roger Keller as a member-managed entity. On May 22, 2007, Amended and Restated Articles of Organization were filed changing the name of the entity to Promise Land Properties, LLC, and listing its members as PSA and R & J Ventures, LLC. PLP again amended its Articles on June 26, 2008, vesting PLP's management in one or more managers, listing Mr. Shudak and Mr. Keller as the managers. Mr. Shudak and Mr. Keller remained the managers until they assigned their PLP membership interests to one of PLP's investors on April 14, 2010, effective April 1, 2010.⁹

Parker Skylar & Associates, LLC

4. Mr. Shudak organized PSA on May 17, 2007, as an Arizona member-managed limited liability company. Mr. Shudak was the sole member. On June 26, 2008, Mr. Shudak amended the Articles, converting it to a manager-managed company.¹⁰ Mr. Shudak was manager until December 15, 2009, when he resigned and relinquished his PSA membership interests to its investors.¹¹

5. The Division issued a Certification of Non-Registration certifying that between May 1, 2008, to April 14, 2013, PSA had not filed with the Commission a notice pursuant to A.R.S. § 44-1850 of the Securities Act or Article 12 of the Arizona Investment Management Act (A.R.S. § 44-3321, *et seq.*); had not registered securities with the Commission by description pursuant to Article 6 of the Securities Act (A.R.S. § 44-1871, *et seq.*) or by qualification pursuant to Article 7 of the Securities Act (A.R.S. § 44-1891, *et seq.*); had not registered with the Commission as a dealer pursuant to Article 9 of the Securities Act (A.R.S. § 44-1941, *et seq.*); and had not made a notice filing and was not licensed with the Commission as an investment adviser pursuant to Article 4 of the Arizona Investment Act (A.R.S. § 44-3151, *et seq.*).¹²

...

...

⁸ Official Notice is taken of PLP's organizational documents.

⁹ Ex. S-13.

¹⁰ Ex. S-5.

¹¹ Ex. R-1.

¹² Ex. S-2.

1 **Other Individuals and Entities**

2 Alan Thome

3 6. Alan Thome is a real estate developer¹³ and one of the organizers and/or member
4 and/or managers of Cochise County Land, LLC, Cochise County 1900, LLC, Gadsden Holdings,
5 LLC, and Poncho Holdings, LLC.

6 Cochise County Land, LLC

7 7. Cochise County Land, LLC (“CCL”) is an Arizona manager-managed limited liability
8 company organized on May 22, 2007, for the purpose of acquiring and developing approximately
9 1,280 acres of raw land near Tombstone, Arizona (“Tombstone Project”).¹⁴ CCL’s members are PLP
10 and Gadsden Holdings, LLC, with Mr. Thome as CCL’s manager. CCL’s land for the Tombstone
11 Project was encumbered by a \$2.33 million deed of trust and note, which has been foreclosed upon.¹⁵
12 CCL held no assets other than the land and currently is not conducting business.¹⁶

13 Cochise County 1900, LLC

14 8. Cochise County 1900, LLC (“CC1900”) is an Arizona manager-managed limited
15 liability company organized on February 29, 2008, by PLP and Poncho Holdings, LLC and was
16 originally managed by Mr. Thome. CC1900 amended its Articles of Organization on March 28,
17 2008, to replace PLP with Mr. Shudak as a member, and amended the Articles again on June 26,
18 2008, to replace Mr. Shudak with PSA as a member. On September 10, 2010, CC1900 filed an
19 amendment to its Articles removing PSA as a member and replacing it with 1900 Investors, LLC.¹⁷
20 Mr. Shudak and Mr. Thome formed CC1900 for the purpose of acquiring and developing
21 approximately 1,900 acres of raw land on three parcels between Sierra Vista and Bisbee, in Cochise
22 County (“Bisbee Project”). As of the date of the hearing, CC1900 still held the land for the Bisbee
23 Project but the property was in danger of being foreclosed upon.¹⁸

24 ¹³ Division Post-Hearing Brief, page 3.

25 ¹⁴ Notice, page 3.

26 ¹⁵ Ex. S-6, page 5.

27 ¹⁶ Ex. S-6, page 6; Notice, page 3.

28 ¹⁷ The Commission’s Corporation Division’s records reflect that another amendment to CC1900’s Articles was filed on July 30, 2013, one month after the conclusion of the hearing. This amendment replaced Mr. Thome as manager with Martin Swank, 1900 Investors, LLC’s manager. At hearing, however, Mr. Schwank testified that Mr. Thome had been replaced as manager in December 2012. Tr. at 168.

¹⁸ Answer, page 10; Tr. at 76 – 79.

Poncho Holdings, LLC

9. Poncho Holdings, LLC ("Poncho Holdings") is an Arizona limited liability company organized on January 30, 2008, managed by Mr. Thome and owned by Mr. Thome and three others. Poncho Holdings remains a member of CC1900.¹⁹

1900 Investors, LLC

10. In December 2009, Mr. Shudak resigned as manager of PSA and relinquished his membership interests to PSA investors. Some of PSA's investors assumed control of PSA and on February 10, 2010, they re-organized as 1900 Investors, LLC ("1900 Investors"). 1900 Investors subsequently replaced PSA as a member of CC1900.²⁰

Summary of the Notice

11. This matter involves the Respondents' efforts to raise capital for the Tombstone Project and the Bisbee Project.

12. According to the Division's Notice, the terms of CCL's Operating Agreement state that PLP was responsible for obtaining debt financing for the 1,280 acres being purchased and for additional capital contributions of \$2,185,000 needed to take the Tombstone Project through the final plat process.²¹

13. The Notice claimed that under CC1900's Operating Agreement, Mr. Shudak was responsible for obtaining debt financing for the purchase of the 1900 acres, and also for additional capital contributions of \$2,500,000 needed to take the Bisbee Project through the final plat process.²²

14. The Division alleged that in order to obtain the financing for the two projects, Mr. Shudak, PLP and PSA offered or sold unregistered securities in the form of membership interests, investment contracts and notes within or from Arizona in violation of A.R.S. § 44-1841; Mr. Shudak, PLP and PSA offered or sold securities in the form of membership interests, investment contracts and

¹⁹ Official Notice is taken of Poncho Holdings, LLC's organizational records found at the Commission's Corporations Division website.

²⁰ Official Notice is taken of 1900 Investors' organizational records found at the Commission's Corporations Division website.

²¹ Notice, page 3.

²² Notice, page 4. CC1900's Operating Agreement was effective as of April 14, 2008. At that time, Mr. Shudak was a member in his individual capacity. As noted above, CC1900's Articles were amended on June 26, 2008, to replace Mr. Shudak with PSA as a member.

1 notes within or from Arizona while not registered as dealers or salesmen in violation of A.R.S. § 44-
2 1842; and Mr. Shudak and PSA committed fraud in connection with the offer or sale of securities
3 within or from Arizona in violation of A.R.S. § 44-1991.

4 15. In addition, the Division maintained that Mr. Shudak directly or indirectly controlled
5 PSA within the meaning of A.R.S. § 44-1999(B) and he is jointly and severally liable with PSA for
6 any violations of A.R.S. § 44-1991.

7 16. The Division requested that the Commission order: a) Mr. Shudak, PLP and PSA to
8 permanently cease and desist from further violations of the Securities Act; b) the Respondents to pay
9 restitution pursuant to A.R.S. § 44-2032; c) the Respondents to pay administrative penalties pursuant
10 to A.R.S. § 44-2036; and d) any other relief the Commission deemed appropriate.

11 **Procedural History**

12 17. The Division filed the Notice on September 21, 2012.

13 18. On October 16, 2012, the Division submitted an Affidavit of Service stating that
14 copies of the Notice were served on the attorney for Mr. Shudak and PSA on October 12, 2012.

15 19. On October 22, 2012, Mr. Shudak and PSA docketed a Request for Hearing.

16 20. By a Procedural Order docketed October 24, 2012, a procedural conference was held
17 on November 8, 2012. The Division appeared through counsel. Mr. Shudak and PSA appeared
18 through counsel, who related that he also would be representing PLP; however, counsel noted that an
19 unresolved issue had arisen regarding his continued representation of PSA, and that the Division was
20 aware of the problem. The parties agreed that Mr. Shudak and PLP would file an Answer by
21 November 26, 2012, and attempt to resolve PSA's representation issue.

22 21. On November 9, 2012, a Procedural Order was issued setting a status conference for
23 January 10, 2013.

24 22. Mr. Shudak and PLP docketed their Answer to Notice of Opportunity for Hearing on
25 November 26, 2012, but PSA did not submit an answer.

26 23. On January 8, 2013, the Division filed an Affidavit of Service stating that copies of the
27 Notice were served on PSA's statutory agent on December 3, 2012.

28 ...

1 24. On January 10, 2013, the status conference convened as scheduled. Mr. Shudak, PLP,
2 and the Division appeared through counsel, but no one appeared on PSA's behalf. Mr. Shudak's and
3 PLP's attorney related that he did not represent PSA, explaining that its status was unclear given the
4 Division's belief that Mr. Shudak no longer controlled PSA. Counsel concluded that Mr. Shudak did
5 not have the authority to retain counsel on PSA's behalf.

6 25. A Procedural Order issued January 23, 2013, set the hearing on the Notice for June 17,
7 2013, and scheduled other procedural deadlines.

8 26. On February 26, 2013, the Division docketed a Proposed Order to Cease and Desist,
9 Order for Restitution, and Order for Administrative Penalties against PSA. The proposed order noted
10 that PSA's statutory agent had been served with the Notice, but the times for answering the Notice
11 and requesting a hearing and had passed without an answer or hearing request from PSA.

12 27. In Decision No. 73784 (March 21, 2013), the Commission concluded that PSA had
13 violated A.R.S. §§ 44-1841, 44-1842, and 44-1991, and found PSA's conduct was grounds for a
14 cease and desist order and an order of restitution pursuant to A.R.S. § 44-2032, and administrative
15 penalties pursuant to A.R.S. § 44-2036. The Commission awarded restitution in the amount of
16 \$1,942,000 and \$50,000 in administrative penalties, plus interest.

17 28. On March 6, 2013, Mr. Shudak and PLP filed their First Request for Production of
18 Documents ("Request for Production"), and the Division filed its Response objecting to the Request
19 for Production on March 26, 2013.

20 29. On April 2, 2013, Mr. Shudak and PLP filed a Response to the Securities Division's
21 Objections to Respondents' First Request for Production of Documents, and Motion to Compel.

22 30. The Request for Production was denied by Procedural Order on April 30, 2013.

23 31. On May 1, 2013, the parties filed their Preliminary Witness and Exhibit Lists.

24 32. On May 9, 2013, the Division filed an Affidavit of Service stating that a copy of the
25 Notice had been served on the statutory agent for PLP on May 9, 2013.

26 33. On May 10, 2013, PLP's attorney filed a Notice of Withdrawal as Counsel and
27 Request to Continue Hearing. Counsel observed that one of the documents included in the Division's
28 Exhibit List was "Agreement of Absolute Transfer and Assignment," effective April 1, 2010, in

1 which Mr. Shudak and Mr. Keller assigned all of their PLP membership interests to a PLP investor.²³
2 Counsel claimed he was not aware of the assignment when he agreed to represent both Mr. Shudak
3 and PLP, and since Mr. Shudak did not have the authority to engage counsel on PLP's behalf, he had
4 to withdraw as PLP's lawyer. Given these developments, Mr. Shudak's attorney requested a
5 continuance of the June 17, 2013, hearing.

6 34. The Division filed its Opposition to Respondent Shudak's Request to Continue
7 Hearing on May 21, 2013.

8 35. On May 31, 2013, the Division docketed a Motion to Allow Telephonic Testimony,
9 requesting permission to present some of its witnesses by telephone.

10 36. A Procedural Order issued June 4, 2013, denied Mr. Shudak's Motion to Continue and
11 granted the Division's Motion to Allow Telephonic Testimony.

12 37. The hearing convened as scheduled on June 17, 2013, at the Commission's Phoenix
13 offices. The Division was represented by counsel and presented witnesses Martin Schwank, Craig
14 Swandal (telephonically) and Steven Berendes (telephonically), each a PSA investor, Andrea
15 McDermitt-Fields, Securities Division CPA, and Dulance Morin, Securities Division investigator.
16 Mr. Shudak was represented by counsel, but he was not present at the hearing and no witnesses
17 testified on his behalf. At the conclusion of the hearing, a schedule for filing post-hearing briefs was
18 established, and the matter was taken under advisement pending submission of a Recommended
19 Opinion and Order to the Commission.

20 38. On July 2, 2013, the Division docketed a Proposed Order to Cease and Desist, Order
21 for Restitution, and Order for Administrative Penalties against PLP. The proposed order noted that
22 PLP's statutory agent had been served with the Notice, but the times for answering the Notice and
23 requesting a hearing and had passed without an answer or hearing request from PLP.

24 39. In Decision No. 74015 (July 30, 2013), the Commission concluded that PLP had
25 violated A.R.S. §§ 44-1841, and 44-1842, and found PLP's conduct was grounds for a cease and
26 desist order and an order of restitution pursuant to A.R.S. § 44-2032, and for administrative penalties

27
28 ²³ Ex. S-13, ACC006055.

1 pursuant to A.R.S. § 44-2036. The Commission awarded restitution in the amount of \$958,000 and
 2 \$25,000 in administrative penalties, both subject to interest under A.A.C. R-14-4-308(C).

3 40. On August 9, 2013, the Division and Mr. Shudak filed their post-hearing briefs, and
 4 on August 30, 2013, the parties docketed their responsive briefs.

5 BACKGROUND

6 41. The issues at hearing were whether Mr. Shudak violated A.R.S. §§ 44-1841, 44-1842,
 7 and 44-1991, and also whether Mr. Shudak was a “controlling person” within the meaning of A.R.S.
 8 § 44-1999, making him jointly and severally liable with PSA for violations of A.R.S. § 44-1991. At
 9 the time of the June 2013 hearing, the Commission had entered its default order against PSA.

10 The Operating Agreements

11 CC1900 Operating Agreement

12 42. CC1900’s Operating Agreement dated April 14, 2008,²⁴ states the initial phase of the
 13 Bisbee Project would “deal generally with the acquisition, planning, entitlement and related early
 14 development and pre-construction activities up to and including approval of the final plat for the
 15 Project (the “Entitlement Phase”).²⁵ Mr. Shudak’s obligations during this initial phase are described
 16 in Section 3.2(A) of the CC1900 Operating Agreement as follows:

17 During the Entitlement Phase, *Shudak shall facilitate the Company obtaining debt*
 18 *financing to be secured by the Property* (with Shudak to act as co-maker and Poncho
 19 [Holdings] and its affiliates, to the extent necessary, to provide guaranties) in amounts
 20 sufficient to fund the acquisition of the Property, property taxes, insurance, consulting
 21 and professional services, fees, and other costs and normal business operating expenses
 22 incurred by the Company during the Entitlement Phase. *Shudak shall be obligated, and*
 23 *hereby agrees, to make Additional Capital Contributions to the Company in an aggregate*
 24 *amount not to exceed \$2,500,000, and on such dates and for such purposes as are*
 25 *determined by the Manager (the “Entitlement Phase Financing Costs”) in order to fund*
 26 *the financing costs component of the Entitlement Phase budget. If the Manager issues an*
 27 *assessment that is needed to pay Entitlement Phase Financing Costs, Shudak shall pay the*
 28 *same within ten (10) days from the date of the assessment notice. It is contemplated by*
 29 *the parties that Shudak shall bear the economic burden of discharging such costs and*
 30 *related Company liabilities and the total risk of economic loss with respect to the*
 31 *Entitlement Phase Financing Costs.* (Emphasis added.)²⁶

32 43. CC1900’s Articles were amended on June 26, 2008, to replace Mr. Shudak with PSA
 33 as a member.

34 ²⁴ Ex. S-14. There are no signatures on the copy of CC1900’s Operating Agreement. Tr. at 46.

35 ²⁵ Ex. S-14, page 2, Section 1.5(A).

36 ²⁶ Ex. S-14, page 13.

1 PSA Operating Agreement

2 44. The pertinent terms in PSA's Operating Agreement, dated April 1, 2008,²⁷ follow:

- 3 • Mr. Shudak is PSA's manager and pursuant to Section 6.3, Mr. Shudak has the
- 4 authority to carry out PSA's business and affairs without further authorization from
- 5 the members.
- 6 • Section 5.12 allows the manager to set his salary and compensation.
- 7 • Section 6.4 states that the manager may open bank accounts in PSA's name and shall
- 8 be the signatory on the bank accounts.
- 9 • Section 7.2(a) requires the manager to provide reports to members at least annually
- 10 that include at a minimum PSA's income statement, balance sheet and a statement of
- 11 the balance in each member's capital account.
- 12 • Section 7.4 states that, "[p]roper and complete records and books of account shall be
- 13 kept or shall be caused to be kept by the Manager in which shall be entered fully and
- 14 accurately all transactions and other matters relating to the Company's business in
- 15 such detail and completeness as is customary and usual for businesses of the type
- 16 engaged in by the Company."²⁸

17 45. From PSA's organization in May 2007 until December 2009, Mr. Shudak was PSA's

18 only manager, and the only one who signed documents on PSA's behalf. Each investor witness

19 testified that Mr. Shudak made all management and operational decisions and never convened any

20 member meetings or submitted anything to a vote of the members. Mr. Shudak controlled PSA's

21 bank accounts and the members stated they never received any type of financial statement or a list of

22 PSA's members in spite of requests for the documents.²⁹

23 Forms of Investment Purchase Agreements, Notes and Assignments of Interests

24 46. Almost all of PSA's investors signed substantially similar investment purchase

25 agreements ("IPAs").³⁰ The IPAs state that PSA was formed for the "acquisition, financing,

26 ²⁷ Ex. S-56. There are no signatures on the copy of PSA's Operating Agreement. Tr. at 250.

27 ²⁸ Ex. S-56.

27 ²⁹ Tr. at 37, 66 – 67, 202 – 206, 253.

28 ³⁰ The exceptions are investment agreements signed by Frank Lamer and Tim Olp in January 2008, and a Collateral Assignment of Membership Interest in LLC, signed by Donald Van Hook in July 2009.

1 entitlement, development, subdivision, marketing and sale” of the Bisbee Project. At the top of the
2 first page of the IPA is the following statement:

3 This is neither an offer to sell nor a solicitation of an offer to buy any securities. An offer
4 can only be made by personal invitation from a representative of the company to
5 *accredited investors* (as defined in regulation D under the Securities Act of 1933). Each
6 prospective investor is invited to ask questions and obtain information from the company
7 concerning the company and its proposed real estate business, the property, the terms of
8 the investment and risk factors. These securities have not been registered with the
9 Securities and Exchange Commission or any state securities administrator and are,
10 therefore, subject to restrictions on transfer. These are speculative securities involving
11 certain risk factors. (Emphasis original.)³¹

12 47. The IPA states: “The Securities purchased under this [IPA] are Units in the Company
13 (“Units” or “Securities”).”³² The Securities consist of a note bearing an interest rate of 14 percent per
14 year of simple interest on the principal balance and payable at the end of two years (“Note”). Each
15 Note states it is being issued “for value received,” being delivered in Scottsdale, Arizona, and will be
16 governed by Arizona law. Investors received an Assignment of Interest (“Assignment”) for a
17 percentage of PSA membership Units. The Assignment contains a covenant and warranty that the
18 membership interest conveyed was “free and clear of any liens and encumbrances of any kind,
19 character or nature....”³³

20 48. Attached to each IPA was a document entitled Additional Terms and Conditions, in
21 which each investor represented and warranted, among other things, that the investor: 1) had
22 carefully reviewed the information provided by PSA; 2) had a reasonable opportunity to ask
23 questions and receive answers from PSA; 3) investigated the facts in connection with the purchase of
24 the Units; 4) was aware that the Units involved a high degree of risk; 5) was an accredited investor;
25 and 6) acknowledged that the solicitation for the offering was by a personal invitation from PSA.³⁴

26 49. All IPAs, Notes and Assignments were signed by Mr. Shudak as PSA’s manager.

27 50. Although the PSA investment documents for each investor were substantially similar,
28 the terms of the IPAs varied depending on the amount of the investment and/or the price per Unit.³⁵

³¹ Ex. S-31. These investment documents signed by PSA investor Craig Swandal are used as examples of the investment documents signed by the majority of PSA’s investors.

³² *Id.*

³³ *Id.*

³⁴ *Id.*

³⁵ Exs. S-16 – S-32.

1 For example, Mr. Schwank made three different investments, but none of his IPAs stated a price per
 2 Unit,³⁶ whereas the IPA signed by Mr. Swandal stated the price per Unit was \$33,333,³⁷ and investor
 3 Rosan Knapp's IPA valued the price per Unit at \$25,000.³⁸

4 51. Each IPA contains the following statement:

5 The Units may be purchased only by 'Accredited Investors' as defined in Rule 501(a) of
 6 Regulation D under the Securities Act of 1933 [17 CFR § 230.501(a)] for whom an
 7 investment illiquid, in non-marketable securities is suitable. The Investor has completed,
 8 signed and delivered to the Company an Investor Suitability Questionnaire certifying, and
 hereby confirms, that the Investor is an 'Accredited Investor.' The Investor is aware the
 Company will rely on Investor's representation in the Investor Suitability Questionnaire.
 (Emphasis original.)³⁹

9 52. Copies of the investment documents given to the Division by Mr. Shudak and
 10 investors contained Investor Suitability Questionnaires for only five PSA investors. Mr. Shudak did
 11 not present any evidence that he or someone else on PSA's behalf had reviewed these Questionnaires
 12 to ensure they had been properly completed.

13 **Acquisition of the Bisbee Project Property**

14 53. PSA investor Martin Schwank testified that the 1900 acres of land purchased for the
 15 Bisbee Project were owned by Lee Esch.⁴⁰ Mr. Esch provided seller carryback financing for 70
 16 percent of the \$1.9 million sales price under the terms of a note and took a first position lien on the
 17 property. CC1900 was to pay Mr. Esch the remaining 30 percent (\$570,000) in cash at closing.⁴¹

18 54. Prior to CC1900's formation in February 2008, Mr. Shudak, as manager for PSA,
 19 entered into an investment agreement with Frank & Associates, LLC, signed by Frank Lamer, a
 20 resident of Nebraska, the LLC's managing member.⁴² Mr. Shudak entered into a second investment
 21 agreement with Tim Olp, an Arizona resident.⁴³ Each document denotes a \$128,000 investment and
 22 both were dated January 7, 2008.⁴⁴ According to these investment agreements,⁴⁵ these funds would

24 ³⁶ Ex. S-30. Mr. Schwank's investment equaled \$361,000 for which he received 20 Units, or \$18,050 per Unit.

25 ³⁷ Ex. S-31.

26 ³⁸ Ex. S-19.

27 ³⁹ Ex. S-31, Section 3.

28 ⁴⁰ Tr. at 79.

⁴¹ Ex. S-50, page 4.

⁴² Ex. S-20.

⁴³ Ex. S-26.

⁴⁴ The bank records reflect that Mr. Lamer and Mr. Olp provided some, if not all, of their investment funds prior to January 1, 2008.

1 be used for the earnest money required under the real estate purchase contract. Upon close of escrow,
 2 their earnest money would be returned, plus an “approximate” \$80,000 in interest, on or before
 3 January 1, 2009. In exchange for the investments, PSA executed Assignments of Interest granting
 4 Frank & Associates, LLC, a ten percent PSA membership interest,⁴⁶ and granting Mr. Olp an eight
 5 percent PSA membership interest.⁴⁷ The documents state they are legally binding in Arizona.

6 55. In May 2008, Mr. Shudak contacted Nascent Investments, LLC (“Nascent”) seeking a
 7 \$250,000 bridge loan as part of the \$570,000 cash payment due at closing.⁴⁸ Nascent is an Arizona
 8 limited liability company that provides short-term, alternative financing for commercial real estate
 9 ventures, and is owned and controlled by Eric Falbe.⁴⁹ Nascent agreed to loan the money to PSA and
 10 Spirit Graphics, evidenced by a Loan and Security Agreement and a Secured Promissory Note;⁵⁰
 11 however, Mr. Esch refused to allow Nascent to have a priority lien against the property as security for
 12 the bridge loan. As such, Nascent required Mr. Shudak to sign a personal guaranty and to grant
 13 Nascent a blanket security interest in all of PSA’s and Spirit Graphics’ assets. Nascent also received
 14 an Assignment of Interest for 20 percent of PSA’s membership interests.⁵¹ Under the terms of the
 15 Secured Promissory Note, interest accrued at \$25,000 per month until the principal balance was paid
 16 in full. The note matured on December 31, 2008. Upon default, interest would accrue at 15 percent
 17 per month.⁵² The Loan and Security Agreement states that any payments received would be applied
 18 to interest first, and then to the principal balance.⁵³

19 56. Section 4.4.8 of the Loan and Security Agreement authorized Nascent to file a UCC –
 20 1 Financing Statement to perfect its interests. Nascent filed UCC – 1 Financing Statements for PSA,
 21 Spirit Graphics, and Mr. Shudak with the Arizona Secretary of State’s Office on June 6, 2008.⁵⁴

23 ⁴⁵ The investment agreements executed by Mr. Lamer and Mr. Olp were simple, one page agreements and contained no
 24 language regarding the offer or sale of securities or requirement that they be accredited investors. These two documents
 are significantly different from the Investor Purchase Agreement used by Mr. Shudak for other investors.

⁴⁶ Ex. S-20.

⁴⁷ Ex. S-26.

⁴⁸ Ex. S-50, page 3.

⁴⁹ Ex. S-50, Exhibit A-2.

⁵⁰ Ex. S-15.

⁵¹ Ex. S-50, page 4.

⁵² Ex. S-15.

⁵³ *Id.*

⁵⁴ Ex. S-15, Exhibit B.

1 57. According to a cash flow spreadsheet prepared by Mr. Thome, the real estate
2 transaction closed on May 27, 2008. Mr. Thome recorded the cash due at closing as coming from the
3 following sources: Nascent loan – \$250,000; Alan Thome – \$200,000; Pat Shudak – \$ 110,000; and
4 \$10,000 from a survey reimbursement credited to the closing account.⁵⁵ There is no indication on the
5 spreadsheet of how the \$256,000 invested by Mr. Lamer and Mr. Olp as earnest money for the
6 transaction was used or if it was returned to them.

7 **Offer and Sale of Investments**

8 58. In April 2008, Mr. Shudak began selling PSA securities using the investment forms
9 discussed earlier. The first to invest in PSA under an IPA was Craig Swandal. Mr. Swandal, who
10 lives in Minnesota, testified that he was not previously acquainted with Mr. Shudak. Mr. Swandal
11 became aware of the investment opportunity through his friend, Jim Peterson, who is an Arizona real
12 estate broker and a friend of Mr. Shudak's.⁵⁶ Mr. Swandal testified that he was initially interested in
13 investing in the Tombstone Project and he flew to Arizona in March 2008 to visit the proposed
14 development site and discuss the transaction with Mr. Shudak and Mr. Peterson.⁵⁷ Mr. Swandal
15 related that during the meeting, Mr. Shudak gave him detailed documents about the Tombstone
16 Project and PLP.⁵⁸ As they were returning to Scottsdale, Mr. Shudak began to talk about the Bisbee
17 Project, which Mr. Shudak claimed would be similar in structure to the Tombstone Project.⁵⁹ From
18 their discussions, Mr. Swandal testified it was his belief that Mr. Shudak's role in Bisbee Project was
19 to market PSA securities to raise capital.⁶⁰

20 59. After Mr. Swandal received PSA's documents, he observed that they were not as
21 detailed as those for the Tombstone Project.⁶¹ Mr. Swandal tried to have his own attorney review
22 them, but he was out of the country.⁶² Mr. Swandal testified that Mr. Shudak was calling him every
23

24 ⁵⁵ Ex. S-54. The information recounted in the spreadsheet Mr. Thome produced to the Division contained little support
for where, when or how the funds were provided to CC1900 for closing.

25 ⁵⁶ Tr. at 199, 215. Mr. Swandal later learned Mr. Peterson originally held the sales listing for the three parcels comprising
the Bisbee Project. Tr. at 193.

26 ⁵⁷ Tr. at 216 – 218.

27 ⁵⁸ Tr. at 194.

28 ⁵⁹ Tr. at 195.

⁶⁰ Tr. at 196.

⁶¹ Tr. at 194, 219.

⁶² Tr. at 223, 254.

1 day to find out when Mr. Swandal would be making his investment so the development could move
 2 forward.⁶³ At Mr. Shudak's recommendation, Mr. Swandal consulted with Arizona attorney Dan
 3 Curtis regarding the investment and the documents. Mr. Swandal testified that he specifically asked
 4 Mr. Curtis if it was a good investment, and he responded, yes, it was, and told Mr. Swandal not to be
 5 concerned about anything in documents.⁶⁴

6 60. In April 2008, Mr. Swandal invested \$300,000 in PSA and \$200,000 in PLP.⁶⁵ At Mr.
 7 Curtis' suggestion, Mr. Swandal wired his funds to Mr. Curtis, who then wired the money to Mr.
 8 Shudak.⁶⁶ Mr. Swandal received nine percent of PSA's membership Units for his investment. He
 9 recalls seeing a document Mr. Shudak gave him reflecting Mr. Shudak's interest as 91 percent and
 10 Mr. Swandal's as nine percent, even though Mr. Lamer and Mr. Olp had been given a combined 18
 11 percent of PSA's membership Units in January.⁶⁷

12 61. By the time the Bisbee Project land purchase closed at the end of May 2008, Mr.
 13 Shudak had transferred 53 percent of PSA's membership interests to others, six percent of which was
 14 not related to cash investments in PSA. Mr. Shudak had executed an Assignment of Interest on
 15 January 22, 2008, to John Schnaible, a resident of Nebraska, granting him a six percent PSA
 16 membership interest,⁶⁸ but the Division did not receive from either Mr. Shudak or Mr. Schnaible an
 17 investment agreement or other document indicating Mr. Schnaible made any cash investment for his
 18 PSA membership interest. Division investigator Dulance Morin testified it was his understanding
 19 from the interviews he conducted with PSA investors that Mr. Shudak had given some people PSA
 20 membership interests in return for bringing investors into the transaction.⁶⁹

21
 22 ⁶³ Tr. at 223.

23 ⁶⁴ Tr. at 255 – 256.

24 ⁶⁵ Tr. at 192, 216.

25 ⁶⁶ Mr. Swandal testified that he later learned Mr. Shudak and Mr. Curtis had done a lot of work together. According to
 26 Mr. Swandal, when issues arose between PSA investors and Mr. Shudak, Mr. Curtis was not cooperative in providing
 27 details regarding the money that went into the Bisbee Project. Tr. at 198 – 199.

28 ⁶⁷ Tr. at 200.

⁶⁸ Ex. S-29. Mr. Schwank testified that he believed Mr. Schnaible was a financial advisor to some of the investors in
 Nebraska and Iowa. Tr. at 50.

⁶⁹ Tr. at 400. Others holding membership interests without an accompanying cash investment or investment agreement
 to PSA are Mr. Lamer (Ex. S-20, excluding the \$128,000 investment made in January 2008), John McCardle/JPMAC,
 LLC (Ex. S-24), and Jim Peterson (Ex. S-27); Tr. at 386. Some of the Assignments may correspond to loans made to Mr.
 Shudak, rather than investments in PSA, for example, Ex. S-20, ACC00266 – ACC002670, and Ex. S-24, ACC002721 –
 ACC002729. See also, Tr. at 73 – 76.

1 62. Next to invest was Martin Schwank, who lives in Arizona. Mr. Schwank testified that
 2 he first became friends Mr. Shudak in 2008. In the course of their conversations, they began to
 3 discuss the Bisbee Project, which Mr. Shudak described as a large housing subdivision that would
 4 serve the area near Fort Huachuca and a new Border Patrol unit.⁷⁰ Prior to investing in PSA, Mr.
 5 Schwank and his wife, and Mr. Shudak and his girlfriend, Jill Noetzelman, drove down to view the
 6 property.⁷¹ In addition, Mr. Schwank met with Alan Thome,⁷² and he also reviewed both CC1900's
 7 and PSA's Operating Agreements.⁷³ Mr. Schwank testified that from his review of CC1900's
 8 Operating Agreement, he understood that Mr. Shudak had to raise the \$2.5 million needed to take the
 9 Bisbee Project through the Entitlement Phase. Mr. Thome was to manage the property development
 10 side of the business.⁷⁴

11 63. Mr. Schwank invested in PSA in July 2008 using two LLCs: AshAli Holdings, LLC
 12 for \$54,166.67 and LindaMar Holdings, LLC for \$270,833.36. Mr. Schwank made a third
 13 investment in his own name in November 2008 for \$36,000.⁷⁵ For his \$361,000 investment, Mr.
 14 Schwank received 20 percent of PSA's membership Units, which he understood to be 20 Units out of
 15 a total 100 Units.⁷⁶

16 64. Mr. Schwank stated that he introduced Mr. Shudak to Jack Sandner and Craig
 17 Thompson. Neither of them knew Mr. Shudak, but both eventually invested in PSA.⁷⁷

18 65. In August, September and October, there were no purchase of PSA securities;
 19 however, Mr. Shudak issued Assignments to three individuals or entities reflecting 11 percent of
 20 PSA's membership interests. Mr. Schwank made his third investment on November 14, 2008,
 21 bringing the total assigned membership interests as of December 1, 2008, to 84 percent.⁷⁸

22 ...

24

⁷⁰ Tr. at 25 – 26, 86 – 87.

25 ⁷¹ Tr. at 32 – 33, 80, 86.

26 ⁷² Tr. at 91 – 92.

27 ⁷³ Tr. at 33, 90.

28 ⁷⁴ Tr. at 34 – 35.

⁷⁵ Ex. S-30.

⁷⁶ Tr. at 32.

⁷⁷ Tr. at 97 – 98; Exs. S-28, S-32.

⁷⁸ Ex. S-48; S-30.

1 66. At the beginning of December 2008, Mr. Schwank's friends, Craig Thomson⁷⁹ and
 2 Jack Sandner⁸⁰ invested in PSA, as well as two other people, Gary Bates⁸¹ and Mitchell Lane.⁸² Each
 3 of these four received one percent of PSA's membership Units. On December 3, 2008, Tim Banghart
 4 made two separate investments; one of \$100,000 for five membership Units and the second of
 5 \$50,000 for two Units.⁸³ On December 6, 2008, Mr. Shudak issued another Assignment with no
 6 corresponding capital investment, for four percent of PSA's membership interests.⁸⁴ On December
 7 21, 2008, William Livingston invested \$50,000 for two percent of PSA's membership Units.⁸⁵ As of
 8 December 31, 2008, Mr. Shudak had assigned 101 percent of PSA's membership interests.

9 67. PSA investor Steve Berendes lives in Iowa. Mr. Berendes testified that he learned
 10 about the investment in the fall of 2008 and was introduced to Mr. Shudak through a "friend of a
 11 friend," John Schnaible.⁸⁶ Mr. Shudak and Mr. Schnaible flew to Iowa in January 2009 to meet with
 12 Mr. Berendes at his office. During their meeting, Mr. Shudak told Mr. Berendes that he had
 13 personally invested in PSA.⁸⁷ Mr. Shudak said the investment would be used to secure the land⁸⁸ and
 14 in return for his investment, Mr. Berendes would receive a Note, and in one year his principal would
 15 be returned, plus 14 percent interest.⁸⁹ In addition, PSA would issue an Assignment of PSA
 16 membership Units, but Mr. Berendes stated he had no interest in them.⁹⁰ Mr. Berendes commented
 17 that Mr. Shudak gave him "enough paper to choke a horse" and claimed he told Mr. Shudak: "I'm
 18 only interested in one thing, and that is, you're telling me if this is cleared, that's all I need to know,
 19 is that I'll invest this money for one year, then I will get my money back with 14 percent return, is
 20 that right? He said yes. I said then I am not going to read 50 pages of documents."⁹¹ Mr. Berendes
 21 asserted he specifically asked Mr. Shudak if there were any risks associated with the investment, to

22 ⁷⁹ Ex. S-32.

23 ⁸⁰ Ex. S-28.

24 ⁸¹ Ex. S-17.

24 ⁸² Ex. S-21.

24 ⁸³ Ex. S-16.

25 ⁸⁴ Ex. S-24.

25 ⁸⁵ Ex. S-22.

26 ⁸⁶ Tr. at 282.

26 ⁸⁷ Tr. at 278.

27 ⁸⁸ Tr. at 274, 278.

27 ⁸⁹ Mr. Berendes' IPA states PSA would return the investment in two years, not one. Ex S-18.

28 ⁹⁰ Tr. at 276.

28 ⁹¹ Tr. at 276, 280.

1 which Mr. Shudak responded, “if they got the money raised, absolutely none.”⁹² Mr. Berendes
 2 testified that his discussions with Mr. Shudak were such that Mr. Berendes believed he was investing
 3 with Mr. Shudak, and that PSA “was not on his radar screen.”⁹³

4 68. At the end of their meeting, Mr. Berendes gave Mr. Shudak two checks from two
 5 different entities—REBS, LLC and Heartland Livestock, LLC—for \$50,000 each, made payable to
 6 PSA. In return, Mr. Berendes received three percent of PSA’s membership Units.⁹⁴

7 69. Between January 1, 2009, and June 30, 2009, Mr. Shudak issued another 31.5 percent
 8 in PSA membership interests, of which 3.5 percent were not associated with a capital investment.⁹⁵
 9 This represented a total of 132.5 percent in PSA membership interests assigned.

10 70. On July 15, 2009, Mr. Shudak, in his individual capacity, gave a promissory note to
 11 Donald Van Hook in return for \$200,000 (“Van Hook Note”). Unlike the other investors, Mr. Van
 12 Hook did not sign an IPA. Instead, Mr. Shudak and Mr. Van Hook executed a Collateral Assignment
 13 of Member’s Interest in Limited Liability Company (“Collateral Assignment”). The Collateral
 14 Assignment states that in order to induce Mr. Van Hook to accept the Note, Mr. Shudak granted Mr.
 15 Van Hook “as a secured party a security interest in and to a fifty percent (50%) interest in and to
 16 Parker Skylar & Associates, LLC, an Arizona limited liability company....”⁹⁶ Mr. Morin testified
 17 that Mr. Van Hook explained he had expected his \$200,000 would be used for the Bisbee Project and
 18 he had described himself as an investor in the development.⁹⁷ Section 4.1 of the Collateral
 19 Assignment states that Mr. Van Hook had the right to perfect his PSA security interest,⁹⁸ but no
 20 documents were presented indicating he had done so. According to Mr. Morin, Mr. Van Hook
 21 related he had not received any return on his investment.⁹⁹

22 71. With Mr. Van Hook’s 50 percent interest, Mr. Shudak, either as manager for PSA or
 23 in his individual capacity, had assigned 182.5 percent in PSA interests.

24
 25 ⁹² Tr. at 283.

⁹³ Tr. at 285.

⁹⁴ Tr. at 275.

⁹⁵ Ex. S-48.

⁹⁶ Ex. S-33, ACC004614.

⁹⁷ Tr. at 382.

⁹⁸ Ex. S-33, ACC004615

⁹⁹ Tr. at 382 – 383.

1 72. At hearing, the Division presented copies of the five Investor Suitability
 2 Questionnaires it received from Mr. Shudak or investors.¹⁰⁰ Mr. Berendes testified that he was not an
 3 accredited investor.¹⁰¹ Mr. Schwank testified he did not recall having any paperwork about whether
 4 he was an accredited investor.¹⁰² Mr. Morin stated that during an interview with Gerald
 5 Gruetzemacher, the husband of PSA investor Rosan Knapp (who had transferred \$100,000 out of her
 6 401k account in order for Mr. Gruetzemacher to invest in PSA), Mr. Gruetzemacher claimed that he
 7 was not an accredited investor.¹⁰³

8 **Amount and Tracking of PSA Investor Funds**

9 73. The Division presented Ex. S-48, which is a table prepared by Ms. McDermitt-Fields
 10 consolidating information she gleaned from IPAs, Notes, and Assignment of Interests provided to the
 11 Division by Mr. Shudak and investors. Ex. S-48 reflects that PSA assigned a total of 132.5
 12 membership interests,¹⁰⁴ representing total investments of \$1,942,000.¹⁰⁵ This information is mostly
 13 corroborated by Ex. S-6, Mr. Shudak's Bankruptcy Filing, Schedule F – Creditors Holding
 14 Unsecured Non-Priority Claims. The filing lists all PSA investors except for Mr. Olp and Mr. Lamer,
 15 who are not listed in any of the Bankruptcy Filing's creditor schedules.¹⁰⁶ Additionally, the
 16 investment amounts indicated for each PSA investor on Ex. S-48 mirror the amounts stated on
 17 Schedule F, with two exceptions. Mr. Shudak's debt to Mr. Schwank is listed as \$360,000, instead of
 18 \$361,000, as denoted in his investor documents, and the amount owed to Tim Banghart is listed as
 19 \$200,000, rather than the \$175,000 reflected in his investment documents.¹⁰⁷ The Division claims
 20

21 ¹⁰⁰ Exs. S-16 (Banghart), S-17 (Bates), S-21 (Lane), S-22 (Livingston), and S-28 (Sandner).

22 ¹⁰¹ Tr. at 278 – 279.

23 ¹⁰² Tr. at 41 – 43.

24 ¹⁰³ Tr. at 378 – 381.

25 ¹⁰⁴ The Division's Post-Hearing Brief stated Ex. S-48 contained an error. The Exhibit reflected that 133.5 percent in
 26 membership interests had been assigned, but one of Mr. Lamer's Assignments for two Units had been listed twice, and
 27 another Assignment to Mr. Lamer for 1.5 Units had been omitted. The correct total of PSA membership Units assigned is
 28 132.5. (Division's Post-Hearing Brief, page 8, footnote 38.)

¹⁰⁵ See Exs. S-16 through S-32.

¹⁰⁶ Ex. S-6.

¹⁰⁷ Ex. S-6. The discrepancy is possibly explained by conflicting language in on one of Mr. Banghart's December 3,
 2008, IPAs and its associated Note and Assignment. The IPA states that the price per Unit was \$25,000 and the signature
 page reflects that Mr. Banghart received 5 Units (the number '4' had been written down, but crossed out and initialed by
 Mr. Shudak). The Assignment also reflects five PSA membership Units, which, at a price per Unit of \$25,000 would
 equal an investment of \$125,000. The amount of the Banghart Note, however, is for \$100,000, not \$125,000. Ex. S-16,
 ACC004512 – ACC004517.

1 that with the \$200,000 Van Hook Note, the amount of funds invested totaled \$2,142,000. Like Mr.
2 Lamer and Mr. Olp, Mr. Van Hook is not listed on any of Bankruptcy Filing's creditor schedules.¹⁰⁸

3 74. The Division presented records showing that PSA investors paid for their investments
4 by wire transfers, personal checks, cashier's checks or money orders payable to Patrick Shudak, PSA,
5 and a separate, related entity controlled by Mr. Shudak.¹⁰⁹ Ms. McDermitt-Fields reviewed the
6 deposit records for Mr. Shudak's and PSA's bank accounts provided by JPMorgan Chase Bank, N.A.
7 ("Chase Bank") pursuant to Division subpoena and summarized her findings in table form, which the
8 Division presented as Ex. S-57. Ms. McDermitt-Fields stated that she reviewed the records for the
9 period January 1, 2008, through December 31, 2009, which was the timeframe that the majority, but
10 not all, of the financial activity took place.¹¹⁰ Based on Ms. McDermitt-Fields' review, the Division
11 confirmed deposits of investor payments totaling \$1,675,500 during the review period. Wire
12 transfers totaling \$101,000 from Tim Olp had been made in December 2007, outside of Ms.
13 McDermitt-Fields' timeframe for review, for total deposits of \$1,776,500.¹¹¹ The amounts stated in
14 the investment documents, but not reflected in a corresponding deposit record were: 1) Gary Bates,
15 \$25,000 (out of \$25,000); 2) Steve Berendes, \$50,000 (out of \$100,000); 3) Tim Banghart, \$90,500
16 (out of \$175,000); 4) Frank Lamer; \$100,000 (out of \$128,000); and 5) Rosan Knapp/Gary
17 Gruetzemacher, \$100,000 (out of \$100,000). Ms. McDermitt-Fields testified the bank was not able
18 provide deposit information for this remaining \$365,500.¹¹²

19 75. The Division subsequently received a copy of Steve Berendes' check for REBS, LLC
20 to PSA dated January 14, 2009, for \$50,000, and also a copy of Gary Bates' check dated December 4,

21 ...

22 ...

23 ...

24 ...

25 ...

26 ¹⁰⁸ Ex. S-6.

27 ¹⁰⁹ Exs. S-53, S-57 and S-58.

¹¹⁰ Tr. at 302, 328 – 329.

28 ¹¹¹ Exs. S-57, S-53; Tr. at 304 – 306, 308 – 309.

¹¹² Tr. at 342; Ex. S-53(B).

1 2008, to PSA for \$25,000.¹¹³ A wire-transfer receipt to Mr. Shudak's personal account for \$100,000
 2 can reasonably be corroborated as being from Mr. Lamer.¹¹⁴ In addition, Mr. Morin testified that Mr.
 3 Gruetzemacher and Ms. Knapp explained that, like Mr. Swandal, they had wired their \$100,000
 4 investment to Dan Curtis, who then forwarded their payment directly to CC1900, instead of to
 5 PSA.¹¹⁵ These checks and transfers total \$275,000 of the \$365,500 in unaccounted for investments.
 6 According to his investment documents, Tim Banghart invested \$175,000,¹¹⁶ but the Division was
 7 only able to substantiate payments/deposits of \$84,500, leaving \$90,500 of his claimed investment
 8 funds unsupported.¹¹⁷

9 Use and Management of PSA Investor Funds

10 76. The investor witnesses testified that they expected their investments would be used for
 11 the purchase and development of the Bisbee project and they never authorized Mr. Shudak or PSA to
 12 use their investment funds for any other purposes. Although PSA's Operating Agreement states that
 13 Mr. Shudak could set a salary, Mr. Swandal, Mr. Schwank and Mr. Berendes testified that, based on
 14 their discussions with Mr. Shudak, they did not think Mr. Shudak would be collecting a salary; rather,
 15 his compensation would come on the "back-end" of the transaction.¹¹⁸ Nor was there any indication
 16 that he might use investor funds to support his other companies.¹¹⁹

17 77. Mr. Shudak opened the PSA account on April 7, 2008, with himself as the only
 18 signatory. Ex. S-52 contains copies of the signature cards for the PSA account provided by Chase
 19 Bank. On April 1, 2009, the PSA account signature card was modified to add Jill Noetzelman¹²⁰ as a
 20

21 _____
 22 ¹¹³ Ex. S-58(A).

23 ¹¹⁴ Ex. S-58(A). The copy of the wire transfer shows a transfer of \$100,000 in December 2007 from the account of what
 24 Mr. Schwank believed was one of Mr. Lamer's businesses in Nebraska, Poling Place II, LLC, to Patrick Shudak into an
 25 account ending 4245, which are the last four numbers of Mr. Shudak's personal account. (The PSA account had not been
 26 opened yet.) Exs. S-57, S-58(A); Tr. at 410. Ex. S-20, has copies of Mr. Lamer's PSA investment and assignment
 27 documents and copies of other wire transfers to PSA from an entity called Poling Transportation, also in Nebraska.
 28 Given the similarity of the companies' names and that the transfer originated from the same bank in Nebraska, and was
 the exact amount of Mr. Lamer's missing funds, the evidence is sufficient to conclude that the \$100,000 wire transfer was
 from an entity owned by Mr. Lamer.

¹¹⁵ Tr. at 380 – 381.

¹¹⁶ Ex. S-16.

¹¹⁷ Ex. S-57.

¹¹⁸ There is no evidence that Mr. Shudak collected a salary as PSA's manager.

¹¹⁹ Tr. at 38 – 40, 199 – 200, 274, 277.

¹²⁰ Ms. Noetzelman was not a PSA manager or member.

1 co-signatory to the account. Both signatories have equal rights to make deposits and withdrawals on
2 the signature of only one signer.¹²¹

3 78. To obtain an overview of how investor funds were disbursed, Ms. McDermitt-Fields
4 reviewed the banking records for PSA's accounts and summarized two specific periods where
5 investor funds coming into the PSA account were from only one individual in order to track the flow
6 of funds into and out of PSA's bank account.¹²²

7 79. The first period Ms. McDermitt-Fields evaluated was April 7, 2008, through April 30,
8 2008.¹²³ At the beginning of the period, PSA's bank account had a zero balance. On April 7, 2008,
9 Mr. Curtis wired Mr. Swandal's \$300,000 PSA investment to PSA's bank account.¹²⁴ A \$100
10 deposit was also made in April for total deposits of \$300,100.¹²⁵

11 80. On April 10, 2008, Mr. Shudak transferred \$190,000 from PSA's account into his
12 personal account. On April 14, 2008, Mr. Shudak transferred \$16,000 from his personal account into
13 PSA's account. The amounts paid against the PSA account to others were a wire transfer to Kathy
14 Shudak of \$100,000 and wire transfer to Tim Olp of \$25,000. An additional \$114 was taken out of
15 the account for wire transfer fees and a non-sufficient funds charge.¹²⁶ There is no indication of why
16 Mr. Shudak transferred \$100,000 out of the PSA account to Kathy Shudak,¹²⁷ nor is there evidence of
17 how Mr. Shudak used the \$190,000 of PSA funds he transferred into his personal account.

18 81. The second period Ms. McDermitt-Fields reviewed was August 1, 2008, through
19 August 31, 2008.¹²⁸ PSA's bank account had a beginning balance of \$314.50. Mr. Shudak deposited
20 three personal checks from Mr. Schwank payable to PSA for a total of \$325,000. One other deposit
21 of \$500 was made in August, for total deposits in August 2008 of \$325,500.¹²⁹

22 82. During August, Mr. Shudak affected five transfers from PSA's account into his
23 personal account for \$68,000. Mr. Shudak also made two transfers from PSA's account into an

24 ¹²¹ Ex. S-52, ACC000473.

25 ¹²² Tr. at 310, 317.

26 ¹²³ Ex. S-36. Mr. Shudak opened PSA's account on April 7, 2008. Ex. S-52.

27 ¹²⁴ Tr. at 198 – 199.

28 ¹²⁵ Ex. S-36.

¹²⁶ *Id.*

¹²⁷ Mr. and Mrs. Shudak were still married at the time of the transfer.

¹²⁸ Ex. S-38.

¹²⁹ *Id.*

1 account at Chase Bank held by Ms. Noetzelman, totaling \$15,000. On August 18, 2008, Mr. Shudak
2 transferred \$7,000 from PSA's account into Spirit Graphics' Chase Bank account, and on August 28,
3 2008, he transferred \$14,000 into PLP's Chase Bank account. There is no evidence demonstrating
4 for what purposes Mr. Shudak used the PSA funds in his account or why he transferred money from
5 PSA to PLP's, Spirit Graphics' or Ms. Noetzelman's accounts.¹³⁰

6 83. Amounts paid against PSA's account in August include a cash withdrawal of \$6,000, a
7 check to Tim Olp for \$15,000 and one to Church USA for \$15,000 (an entity owned by Tim Olp), a
8 wire transfer for \$8,000 to a person named Tish Selk, a cashier's check to Jaburg & Wilk for
9 \$10,000, two wire transfers to CCL totaling \$50,000, a wire transfer to CC1900 for \$100,000, a
10 check to Security Title for \$3,529.33, and a wire transfer of \$13,000 to a person named Michael
11 Dunphy. An additional \$100 was debited from the account for wire transfer fees and a non-sufficient
12 funds charge and a check for \$550.¹³¹ There is no information explaining who Tish Selk and Michael
13 Dunphy are, or why funds were transferred from PSA's account into CCL's account or what was the
14 purpose of the \$10,000 cashier's check to Jaburg & Wilk, or the check to Security Title.

15 84. Ex. S-54 is a copy of a ledger prepared by Mr. Thome purportedly reflecting deposits
16 and expenses for CC1900. The spreadsheet shows that funds were shifted between CCL and CC1900,
17 and lists deposits from Mr. Shudak, PSA, Kathy Shudak, and Jill Noetzelman, as well as loans to
18 CC1900 from, and re-paid to, Mr. Thome. Although this record is not substantiated or supported, and
19 is, therefore, unreliable, it does tend to support the contention that funds were not coming solely from
20 PSA's account to pay CC1900's expenses.

21 **Mr. Shudak's Financial Obligations**

22 85. As noted earlier, CC1900's Operating Agreement states that Mr. Shudak was
23 responsible for raising \$2.5 million for development of the Bisbee Project and that he would bear all
24 economic burdens and losses with respect to the Entitlement Phase financing costs. The investor
25 witnesses testified that Mr. Shudak represented to them that he was capable of soliciting the capital
26 needed to meet these obligations.¹³²

27 ¹³⁰ Ex. S-6, page 9.

28 ¹³¹ Ex. S-38.

¹³² Tr. at 33 – 35, 196, 206.

1 86. In spite of this representation, the Division provided documentation that not long after
 2 Mr. Shudak began selling PSA securities to raise capital for the Bisbee Project, a number of lawsuits
 3 were filed in Maricopa County Superior Court against Mr. Shudak, or other companies of which he
 4 was a member or manager.¹³³

5 87. The first lawsuit was filed on July 8, 2008, against Mr. Shudak and Kathy Shudak. At
 6 that point in time, only Mr. Lamer, Mr. Olp and Mr. Swandal had invested in PSA, and Nascent had
 7 perfected its security interests against Mr. Shudak, PSA and Spirit Graphics. Between July 8, 2008,
 8 and the entry of default judgment on December 23, 2008, seven more people invested funds in
 9 PSA.¹³⁴ Seven more individuals and/or entities invested in PSA after the first entry of default, five of
 10 whom were first time PSA investors.¹³⁵ The Division provided copies of four of complaints filed
 11 against Mr. Shudak in 2008; however, the Statement of Financial Affairs in Mr. Shudak's Bankruptcy
 12 Filing indicates eleven lawsuits were filed against Mr. Shudak in 2008 and 2009.¹³⁶

13 Status of the Bisbee Project

14 88. Mr. Schwank testified that by the summer or fall of 2009, Mr. Shudak had stopped
 15 returning his calls and did not respond to requests for information about the Project or PSA's
 16 finances.¹³⁷ In December 2009, Mr. Schwank received a telephone call from Mr. Thome expressing
 17 concern about a lack of communication and funds from Mr. Shudak.¹³⁸ Mr. Schwank stated that he
 18 and a few other investors met with Mr. Thome at his office in Mesa to discuss the situation.¹³⁹ These
 19 investors subsequently asked Mr. Shudak to resign as manager because they believed he had taken
 20 approximately \$800,000 to \$1,000,000 of investor funds.¹⁴⁰ Mr. Shudak resigned as manager and
 21 relinquished his PSA membership interests on December 15, 2009.¹⁴¹

22 ...

23 ¹³³ Exs. S-40, S-41, S-42, and S-43.

24 ¹³⁴ Ex. S-48.

25 ¹³⁵ Ex. S-48.

26 ¹³⁶ Ex. S-6, page 42; Exs. S-40, S-41, S-42, and S-43. Mr. Swandal testified that he was unaware of the lawsuits until after
 he had invested and if he had known, he would not have invested. Tr. at 261 – 262. However, at the time Mr. Swandal
 invested in PSA in April 2008, none of the lawsuits involving Mr. Shudak had yet been filed.

27 ¹³⁷ Tr. at 166.

28 ¹³⁸ Tr. at 101.

¹³⁹ Tr. at 43 – 44.

¹⁴⁰ Tr. at 71, 236.

¹⁴¹ Ex. R-1.

1 89. Mr. Schwank testified that it took several months before the investors who initially
2 met in December 2009 believed they had identified all PSA investors.¹⁴² After a series of
3 teleconferences, they voted to continue with the Bisbee Project to try to save the Project and recoup
4 some of their money.¹⁴³ However, Mr. Schwank testified that he and the other investors he was
5 working with at that time did not have any real estate development or finance experience.¹⁴⁴ In
6 February 2010, those investors who had made cash investments in PSA formed 1900 Investors, LLC,
7 with Mr. Schwank as its manager. 1900 Investors subsequently replaced PSA as a member of
8 CC1900.¹⁴⁵ Some of the investors put in additional funds in order to meet the annual interest
9 payments to the seller and continue with their efforts to complete Entitlement Phase of the Bisbee
10 Project.¹⁴⁶

11 90. Mr. Schwank testified that in February 2010, he received a telephone call from Eric
12 Falbe about the Nascent loan. Mr. Falbe stated that Nascent had perfected its interest in all PSA's
13 assets and that Nascent held 20 percent of PSA's membership Units.¹⁴⁷ Mr. Schwank stated he and
14 some of the other investors were not aware of the Nascent loan.¹⁴⁸ On April 23, 2013, Nascent filed a
15 lawsuit in Maricopa County Superior Court naming Mr. Shudak, Mr. and Mrs. Schwank, 1900
16 Investors as Successor to PSA, 1900 Investors' members, CC1900, Poncho Holdings and Alan
17 Thome, as defendants.¹⁴⁹

18 91. The balloon payment on the seller carry back note for the Property was due at the end
19 of May 2013. Concerned that CC1900 would not be able to make the payment, in approximately
20 February or March 2013, CC1900 listed all the property for sale at \$2.5 million, but dropped the price
21 to \$1,699,000 in June 2013.¹⁵⁰ At hearing, Mr. Schwank testified that the property had not sold, the
22 investors had not made the balloon payment on the property, and it now was subject to foreclosure.¹⁵¹

24 ¹⁴² Tr. at 49 – 51, 72.

¹⁴³ Tr. at 108, 233 – 235.

25 ¹⁴⁴ Tr. at 159.

¹⁴⁵ Tr. at 73 – 75.

26 ¹⁴⁶ Tr. at 79, 266.

¹⁴⁷ Tr. at 67 – 71.

27 ¹⁴⁸ Tr. at 69. Mr. Swandal was aware of the Nascent loan. Tr. at 195.

¹⁴⁹ Ex. S-50.

28 ¹⁵⁰ Tr. at 77, 122 – 125.

¹⁵¹ Tr. at 76 – 79.

LEGAL ANALYSIS AND CONCLUSIONS

Applicable Law

92. A.R.S. § 44-1841 states it is unlawful to sell or offer for sale within or from Arizona any securities that have not been registered pursuant to the Securities Act, unless the securities are exempt from registration.

93. A.R.S. § 44-1842 states it is unlawful for any dealer or salesman to sell or offer for sale within or from Arizona unless the dealer or salesman is registered as required under Article 9 of the Securities Act.

94. A.R.S. § 44-1844(A)(1) states an issuer is exempt from the requirements of §§ 44-1841 and 44-1842 where the transaction does not involve a public offering.

95. A.R.S. § 44-2033 states the respondent bears the burden of proving that an offering is exempt from registration.

96. A.R.S. § 44-1991(A) states it is a fraud to misstate or omit any material fact that might mislead an investor. This includes statements made in the offering and sale of exempt securities.

97. A.R.S. § 44-1999(B) states every person who controls anyone liable for a violation of A.R.S. § 44-1991 is jointly and severally liable with, and to the same extent as, the controlled person.

98. A.R.S. § 44-2032 allows the Commission to issue a cease and desist order and direct payment of restitution if a person has engaged in any act, practice or transaction constituting a violation of the Securities Act.

99. A.R.S. § 44-2036 allows the Commission to impose administrative penalties against a person who is in violation the Securities Act not to exceed \$5,000 per violation.

100. A.A.C. R14-4-308(C)(1) requires restitution to be made in cash equal to the fair market value of the consideration paid, together with interest, less offsets for any principal, interest, or other distributions received on the security for the period from the date of repayment.

Summary of Positions

101. The Division claims that Mr. Shudak repeatedly offered and sold securities within and from Arizona in the form of notes and investment contracts through PSA membership interests, and Mr. Shudak was not registered as a dealer or salesman. Further, the Division alleges that Mr. Shudak

1 committed fraud in the offer and sale of securities, and that Mr. Shudak was a controlling person of
2 PSA; as such, he is jointly and severally liable for any fraudulent acts committed by PSA. According
3 to the Division, Mr. Shudak should be required to pay restitution in an amount of \$2,142,000 and
4 administrative penalties of \$150,000, each subject to interest.

5 102. Mr. Shudak asserts that he did not violate registration requirements, claiming PSA's
6 securities were exempt from registration as part of a private offering. Mr. Shudak also asserts there is
7 no evidence on the record supporting the Division's allegation that he and PSA committed fraud
8 when selling the securities. Mr. Shudak rejects any claim that the investors are entitled to restitution
9 because they have not proven any loss or loss causation.

10 **Violation of A.R.S. § 44-1841 and A.R.S. § 44-1842**

11 Division's Position

12 103. The Division noted Mr. Shudak does not dispute PSA offered and sold securities, but
13 rather, insists the securities were exempt from registration. The Division contends Mr. Shudak failed
14 to meet his burden of proving the investments were exempt from registration as part of a private
15 offering, emphasizing that Mr. Shudak presented no testimony to support this assertion and the two
16 exhibits he did present at hearing had nothing to do with his exemption claims.

17 104. The Division argues that in *SEC v. Ralston Purina Co.*,¹⁵² the U.S. Supreme Court
18 held that the inquiry into whether an offering is public or private must focus on the offerees' needs
19 for the protections afforded by securities registration requirements. Where the offerees already have
20 knowledge of the same type of information that would be provided in a registration statement, or
21 have ready access to that type of information, the offering may fall under a private offering
22 exemption.¹⁵³ The Division declares the copies of the documents Mr. Shudak gave to PSA investors
23 did not contain the type of information required in a registration statement,¹⁵⁴ and notes the investor
24 witnesses testified they had requested information such as financial statements or financial plans or
25 an investor list, but Mr. Shudak never provided them.

26 _____
27 ¹⁵² 346 U.S. 119 (1953).

28 ¹⁵³ 346 U.S. at 124 – 125.

¹⁵⁴ See 15 U.S.C. § 77aa, Schedule A of the Securities Act of 1933, listing 32 categories of information which an issuer should include in a registration statement.

1 105. The Division explains that other factors used to determine whether an offering is
2 public include: 1) the number of offerees; 2) the sophistication of the offerees; 3) the size and manner
3 of the offering; and 4) the relationship between the issuer and the offerees.¹⁵⁵

4 106. The Division emphasizes that although a small number of investors may indicate that
5 an offering is private, the number of investors is not entirely dispositive. In *Ralston*, the U.S.
6 Supreme Court emphasized that, depending on the facts, sale of a security to even one investor could
7 constitute a public offering.

8 107. The Division next contends the term “sophisticated” indicates that an offeree “has
9 such knowledge and experience in financial and business matters that he is capable of evaluating the
10 merits and risks of the prospective investment.”¹⁵⁶ The Division asserts that the testimony and
11 evidence presented at hearing demonstrate the investors were not real estate developers and had little-
12 to-no experience or knowledge about evaluating and managing real estate developments, as
13 demonstrated by the investors’ experiences with the Bisbee Project in their attempt to manage it and
14 save their investments. Further, only a few investors completed an Investor Suitability Questionnaire.
15 The Division maintains there is no evidence PSA reviewed the Questionnaires to ensure they were
16 correctly completed, much less whether PSA evaluated the information to determine whether the
17 person completing the form was an accredited investor.

18 108. Third, although some of the investors were friends with Mr. Shudak prior to investing,
19 many were not, and merely knowing someone who knows someone who is selling an investment in a
20 company does not automatically create a relationship between the offeree and the company. The
21 Division asserts that in order to support a conclusion that an offering is private, an offeror must show
22 the relationship between the investor and the issuer reflects the investors’ ability to access or obtain
23 information from the company. The Division claims Mr. Shudak has failed to show any relationships
24 supporting accessibility to information for most investors, suggesting instead that Mr. Shudak sold
25 securities “to whoever was interested, no matter how that person became interested.”¹⁵⁷

26 . . .

27 ¹⁵⁵ *Mary S. Krech Trust v. The Lakes Apartments*, 642 F.2d 98 (5th Cir. 1981).

28 ¹⁵⁶ Reply in Support of Security Division’s Post-Hearing Brief (“Reply”), page 5, citing 17 C.F.R. §§ 230.506(b)(2)(ii).

¹⁵⁷ Reply, page 6.

1 109. The Division stresses that in order to establish violations of A.R.S. §§ 44-1841 and
2 44-1842, it only need establish that Mr. Shudak and PSA were offering or selling securities within
3 and from Arizona and that the securities, Mr. Shudak and PSA were not registered, which, the
4 Division asserts, it did at hearing. Mr. Shudak, on the other hand, had the burden of proving the
5 applicability of an exemption, which he did not do. The Division concludes, therefore, that the Notes
6 and PSA membership interests were subject to registration, as were Mr. Shudak and PSA.

7 110. The Division stated that even if the PSA securities had been lawfully registered or
8 exempt from registration, Mr. Shudak and PSA would still be subject to the anti-fraud provisions of
9 the Securities Act.

10 111. As to the Van Hook Note, the Division argues that, contrary to Mr. Shudak's
11 assertions, this Note is a security, reiterating that an offer made to one person may still be considered
12 as a public offering.¹⁵⁸ According to the Division, the evidence indicated that Mr. Van Hook
13 believed himself to be an investor in PSA and he understood his investment would be used with other
14 investor funds for the Bisbee Project. Mr. Shudak presented no evidence to show that Mr. Van Hook
15 was an accredited or sophisticated investor or had access to the sort of information available in a
16 registration statement. Given the law and circumstances, the Division claims the Van Hook Note is
17 an unregistered security.

18 112. The Division asserts that Mr. Shudak and PSA offered and sold unregistered securities
19 within or from Arizona. The securities state that they were delivered in Scottsdale, Arizona, and
20 governed by Arizona law. At hearing, the Division provided Certificates of Non-Registration
21 certifying that Mr. Shudak and PSA were not registered in Arizona as securities dealers or salesmen.
22 The Division concludes that Mr. Shudak's and PSA's offer and sale of unregistered securities was in
23 violation of A.R.S. § 44-1842.

24 Mr. Shudak's Position

25 113. Mr. Shudak does not contest the Division's assertion that the PSA investments—
26 whether notes, membership interests or investment contracts—are securities for purposes of
27

28 ¹⁵⁸ *Ralston*, 346 U.S. at 124 – 125.

1 registration or the anti-fraud provisions of the Securities Act. Instead, he claims the investments sold
2 by PSA were a private offering pursuant to A.R.S. § 44-1844(A) and, therefore, exempt from the
3 registration requirements of A.R.S. §§ 44-1841 and 44-1842.

4 114. At the outset, Mr. Shudak emphasizes that only three PSA investors actually testified
5 at the hearing and he protests there is no evidence as to the part he played in the remaining investors'
6 decisions to invest, or even whether the investments were made within or from Arizona. Mr. Shudak
7 claims the evidence does not establish what he may or may not have said to the other investors, or
8 what the other investors knew or did not know before they invested in PSA.

9 115. Mr. Shudak agrees with the Division that the number of offerees is not necessarily
10 dispositive of whether an offering is public or private, but states that the fewer offerees there are, the
11 more likely it is that the investment is a private offering.¹⁵⁹ Mr. Shudak notes there are only 17
12 investors, supporting a conclusion that the securities were part of a private offering.

13 116. Pointing to the Investor Suitability Questionnaires and the terms of the IPAs, Mr.
14 Shudak claims that the investors were accredited and sophisticated. Mr. Shudak refers to sections in
15 the IPAs in which the investors affirmed they had read the information provided regarding the
16 investments and that they had had a reasonable opportunity to ask questions. The investors also
17 represented they conducted whatever investigation they believed necessary in order to evaluate the
18 risks and understood that the investment was speculative in nature and involved certain risks. Mr.
19 Shudak also stated the Division's evidence showed that "the offerees signed Investor Suitability
20 Questionnaires indicating they were all accredited investors," and states that "based on their own
21 admissions, the offerees were all sophisticated."¹⁶⁰ Mr. Shudak concludes this also supports a finding
22 that the investments were part of a private offering.

23 117. Where the offering is small and made directly to offerees by the issuer, this may also
24 betoken a private offering. With only 17 investors, Mr. Shudak maintains it is clear the PSA
25 securities were privately offered to only to a few potential investors and points to the provisions in
26 the IPA where investors acknowledged that the offering was communicated directly to them.

27 ¹⁵⁹ *SEC v. Ralston Purina Co.*, 346 U.S. 119 (1953); *Doran v. Petroleum Mgmt. Corp.*, 545 F.2d 893 (5th Cir. 1977); *Hill*
28 *York Corp. v. Am Intern. Franchises, Inc.*, 448 F.2d 680 (5th Cir. 1971).

¹⁶⁰ Respondent's Post-Hearing Brief, page 15.

1 118. As for the final factor, the relationship between the issuer and offeree, Mr. Shudak
2 states only that the investors acknowledged in their IPAs that they were given access to whatever
3 information they thought necessary.

4 119. Taken as a whole, Mr. Shudak reasons that because this was a small offering made
5 directly to only 17 offerees, each of whom was an accredited and sophisticated investor who was
6 given an opportunity to ask questions, the evidence supports a finding that the investments were part
7 of a private offering and, therefore, exempt from registration.

8 120. Regarding the Van Hook Note, Mr. Shudak argues that nothing in the record supports
9 the allegation that he induced Mr. Van Hook to loan him \$200,000 in exchange for the Collateral
10 Assignment granting a security interest of 50 percent of PSA. Mr. Shudak denies that the Van Hook
11 Note is a security under Arizona law because there is nothing to demonstrate that this Note was
12 anything other than a private loan transaction unrelated to any public offering and, therefore, exempt
13 from registration under Arizona law.¹⁶¹

14 121. Mr. Shudak relied on his contention that PSA's offering was private and, therefore, he
15 was not subject to registration under A.R.S § 44-1842. However, in his Post-Hearing Brief, Mr.
16 Shudak stated: "The Division did not offer any evidence of what role, if any, Shudak had concerning
17 the investments made by the 14 non-testifying investors, or even if those investments were 'within or
18 from' Arizona."¹⁶²

19 Conclusion

20 122. Inquiry into whether an offering was private or public focuses on the offerees' need
21 for the protections afforded through securities registration. In this case, the investors would have
22 benefitted from information similar to that contained in a registration statement since Mr. Shudak did
23 not make available to investors that level and type of information prior to investment or upon
24 requests from investors for the information.

25 123. The PSA investor documents presented at hearing do contain some of the type of
26 information contained in a registration statement, but they lack other information an investor could

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28 ¹⁶¹ *State v. Tober*, 173 Ariz. 211, 841 P.2d 206 (1992); A.R.S. § 44-1844.

¹⁶² Respondent's Post-Hearing Brief, page 3.

1 find meaningful, such as financial statements, financial plans, business plans, executive summaries,
2 legal opinions and/or investor lists.

3 124. Both Mr. Shudak and the Division agree that a small number of investors may be
4 indicative of a private offering, but it is not always dispositive. There were only 17 offerees, but this
5 alone is not enough to support a finding that the offering was private.

6 125. The Division provided the Investor Suitability Questionnaires for a few investors, but
7 not all. Mr. Shudak points out that in the IPA, the investor affirms that he has completed the
8 Questionnaire, and he is an accredited investor. Yet Mr. Shudak provided nothing to corroborate his
9 claims that *all* PSA investors completed the Questionnaire, or were accredited, or that they were
10 sophisticated investors with experience in evaluating and managing real estate investments.

11 126. Although some of the investors were Mr. Shudak's friends, most others were not
12 acquainted with him prior to investing and were only made aware of the investment through "friends
13 of friends." This belies an assertion that the offering was exclusive and limited only to those who had
14 an existing relationship with PSA that would permit access to information. There is also no evidence
15 demonstrating how investors could gain access to the information. The investors were geographically
16 dispersed and obtaining needed information would have been a challenge for many of them.

17 127. Mr. Shudak has not presented evidence to show by a preponderance of the evidence
18 the offering was private and he has failed to meet his burden of proof that the securities are exempt.

19 128. Mr. Shudak also stated that the evidence does not support the allegation that he
20 induced Mr. Van Hook to buy a \$200,000 note in exchange for a security interest of 50 percent of
21 PSA. However, the Collateral Assignment states exactly that: "[Mr. Shudak] in order to induce [Mr.
22 Van Hook] to accept the Note..."¹⁶³ granted a 50 percent membership interest in PSA.

23 129. We reject Mr. Shudak's assertion that the Van Hook Note was part of a private loan
24 transaction and exempt from registration. Although the Note was signed by Mr. Shudak individually,
25 it was secured by the Collateral Assignment, through which Mr. Van Hook received 50 percent of
26 Mr. Shudak's (non-existent) membership interests in PSA. This assignment was not solely a hedge
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28 ¹⁶³ Ex. S-33.

1 against default—it would not be returned to Mr. Shudak upon repayment of the Note. Nor was it to
2 be in lieu of interest, which was provided for in the Note. The Note’s execution so close in time with
3 other PSA investments also indicates this was intended as an investment in PSA. Further, Mr. Morin
4 testified that during their interview, Mr. Van Hook described himself as investor in the Bisbee Project
5 and explained he had expected his \$200,000 investment would be added to other investment funds
6 and used for development. Even if Mr. Shudak’s assertions were accurate that the Van Hook Note
7 was exempt as a private loan transaction, this would not negate the applicability of the anti-fraud
8 provisions of the Securities Act.

9 130. Both Mr. Shudak and Mr. Van Hook lived in Arizona at the time and the Note and
10 Collateral Assignment state they are governed by Arizona law.

11 131. PSA’s securities were not registered, nor were they exempt from registration. Mr.
12 Shudak was an Arizona resident during the time relevant to this matter. PSA was organized by Mr.
13 Shudak under Arizona law and he was the manager of PSA during the time relevant to this matter.
14 Mr. Shudak signed all PSA investment documents as manager, on behalf of PSA, and the investment
15 documents state they are governed by Arizona law. As such, the evidence supports a finding that the
16 securities were offered and sold within and from Arizona. The Division presented Certificates of
17 Non-Registration certifying that Mr. Shudak and PSA were not registered when Mr. Shudak offered
18 and sold the securities within and from Arizona on PSA’s behalf.

19 132. Based on the testimony and evidence presented in this matter, we find the following:

- 20 a) PSA’s offering in the form of membership interests, investment contracts and/or
21 notes constitute securities within the meaning of A.R.S. § 44-1801(26).
22 b) Mr. Shudak acted as a dealer and/or a salesman within the meaning of A.R.S. § 44-
23 1801(22).
24 c) The actions and conduct of Mr. Shudak constitute the offer and sale of securities
25 within the meaning of A.R.S. § 44-1801(15) and 44-1801(21).
26 d) The securities were neither registered nor exempt from registration under A.R.S. §
27 44-1841.
28 e) Mr. Shudak offered and sold unregistered securities within and from Arizona in

1 violation of A.R.S. § 44-1841.

2 f) Mr. Shudak offered and sold securities within and from Arizona without
3 registering as a dealer and/or salesman in violation of A.R.S. § 44-1842.

4 **Violation of A.R.S. § 44-1991 (Fraud in Connection with the Offer or Sale of Securities)**

5 133. Under the Securities Act, it is fraud to misstate or omit any material fact that might
6 mislead an investor. The Division asserts that the standard for materiality is: a) whether a reasonable
7 investor would have wanted to know the misstated or omitted facts; and b) there is a substantial
8 likelihood that, under the totality of the circumstances, the misstatement or omission would have
9 been of significance to an investor when evaluating an investment.¹⁶⁴ An issuer of securities has an
10 affirmative duty not to mislead potential investors. Further, in the instance of anti-fraud provisions of
11 the Securities Act (as opposed to common law fraud), an investor is not required to perform due
12 diligence before making an investment.¹⁶⁵

13 134. The Division also stresses that misstatement or omission of a material fact in the offer
14 and sale of securities is actionable under the Securities Act regardless of whether the person making
15 the statement or omission is aware of its misleading nature at the time the misstatement or omission is
16 made.¹⁶⁶ A seller of securities is strictly liable for any misstatement or omission made; the anti-fraud
17 provisions of the Securities Act do not require a showing that the investor relied upon the offeror's
18 misstatement when deciding to make an investment and the reliance resulted in loss.

19 135. Mr. Shudak dismissed the Division's legal arguments as flawed, claiming that under
20 Arizona law, one of the elements of securities fraud is loss causation. This requires the investors to
21 show that Mr. Shudak's supposed fraudulent actions and statements proximately caused their losses.
22 If losses are due to other circumstances, such as market decline, depreciation, or intervening
23 transactions, then loss causation is not present and the fraud charges fail.

24 136. The evidence presented at hearing, according to Mr. Shudak, shows that the investors
25 waited until early 2013 to try to sell the property, initially listing it for sale at \$2.5 million. In June
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27 ¹⁶⁴ *Rose v. Dobras*, 128 Ariz. 209, 211, 624 P.2d 887, 889 (App. 1981); *Trimble v. American Sav. Life Ins. Co.*, 152 Ariz.
548, 733 P.2d 1131 (1986); *TSC Industries v. Northway, Inc.*, 426 U.S. 438 (1976).

28 ¹⁶⁵ *Rose v. Dobras*, 128 Ariz. 209, 624 P.2d 887, (App. 1981).

¹⁶⁶ See, for example, *State v. Gunnison*, 128 Ariz. 110, 618 P.2d 604 (1980).

1 2013, they dropped the price to \$1.699 million. Mr. Shudak believes that if the investors had chosen
2 to sell the property in early 2010 after they first assumed control of PSA, instead of trying to develop
3 the property, they could have recovered their investments and may even have made a profit. They
4 chose not to sell the property and Mr. Shudak repudiates any claim that the investors may have lost
5 money as a result of his alleged fraudulent acts—any losses experienced by the investors were of
6 their own making and there is no loss causation.

7 Fraudulent Acts

8 137. In the Notice, the Division alleged Mr. Shudak and PSA committed four different
9 fraudulent acts in the offer and sale of PSA securities.

10 Oversubscription

11 138. The evidence reflects that Mr. Shudak and PSA assigned 132.5 percent of PSA
12 membership Units. The Division contends that the investor documents presented at hearing support
13 its assertion that each Unit assigned represented 1/100 of a percent because both the word “percent”
14 and the percent symbol were used to denote the value of the membership interest. Also, Mr.
15 Schwank testified he understood one Unit to mean 1/100 percent, not 1/132.5 percent. The Division
16 claims Mr. Shudak knew how many Units had been assigned since a simple calculation would have
17 shown the cumulative number of Units assigned after each transaction. The Division asserts that the
18 assignment of over 100 percent in interests dilutes an investment and negatively affects an investor’s
19 right to a fair return. As such, the Division maintains that by assigning more than 100 percent in PSA
20 membership interests, Mr. Shudak’s actions constitute fraud.

21 139. Mr. Shudak counters that the evidence presented at hearing by the Division supports a
22 finding that Mr. Shudak only sold 88 percent in PSA membership Units, contending that the
23 witnesses for the Division could not state with certainty what was the consideration for the remaining
24 44.5 Units. Mr. Shudak also insists that Mr. Olp, who received eight membership Units, received
25 \$55,000 back from PSA for partial repayment of his investment and the total number of Units sold
26 should be reduced accordingly.

27 140. Mr. Shudak argues that, as a matter of law, oversubscription is not the proximate cause
28 of any asserted investor damages. After Mr. Shudak resigned in 2009, the PSA investors agreed to

1 continue with development of the Bisbee Project. They created 1900 Investors, exchanged their PSA
2 membership interests with those of 1900 Investors, and replaced PSA as a member of CC1900. Mr.
3 Shudak asserts that by and through the investors' own actions, any existing issues regarding the
4 number of PSA membership Units issued were rendered moot. Further, by replacing PSA with 1900
5 Investors as a member of CC1900, 1900 Investors assumed the membership interest in CC1900,
6 which was the only asset PSA held.

7 141. According to Mr. Shudak, even if he did oversubscribe the offering, the Division's
8 calculations do not acknowledge that the investors actually received a benefit from the additional
9 funds generated by oversubscription. Under the Division's numbers, if Mr. Shudak did, in fact, sell
10 132.5 percent of PSA membership Units, each member's percentage of Units owned would have
11 been diluted by approximately 25 percent. However, the eight investors who received PSA
12 membership interests after Mr. Shudak had allegedly sold 100 percent of the Units invested a total of
13 \$775,000, or approximately 40 percent of the total capital generated. "So, the question posed by the
14 Division's allegation is whether the investors were 'defrauded' when they thought they were getting a
15 25% larger percentage in a much smaller company (based on working capital), but instead received a
16 25% smaller percentage in a 40% bigger company."¹⁶⁷ Mr. Shudak concludes "it appears that each of
17 the investors actually owned *more* of Parker Skylar (on a percentage basis) than what they thought."
18 (Emphasis original.)¹⁶⁸

19 Conclusion

20 142. We believe the Division presented more than sufficient evidence demonstrating that
21 Mr. Shudak oversubscribed the offering. Mr. Schwank and Mr. Morin testified that those individuals
22 who received Assignments of PSA membership interests without a cash investment as consideration
23 had provided consideration in some other form such as bringing investors into the Project. The
24 Assignments state that they were given for good and valuable consideration, and there is no
25 requirement that the consideration had to be cash. As such, those membership interests will not be
26 excluded. In addition, Mr. Shudak's argument that the investors somehow benefitted from having
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28 ¹⁶⁷ Respondent's Post-Hearing Brief, page 6.

¹⁶⁸ Respondent's Post-Hearing Brief, page 5.

1 their membership interests diluted is without merit and we reject it. Further, Mr. Shudak's assertion
2 that PSA's repayment of \$55,000 to Mr. Olp should result in a corresponding reduction of the total
3 number of Units sold does not comport with the terms of the investment documents, which state that
4 membership Units survive repayment of the Note.

5 143. We find that Mr. Shudak oversubscribed the offering constituting a violation of the
6 anti-fraud provisions of the Securities Act.

7 144. We also find that Mr. Shudak committed fraud regarding the Van Hook Note since at
8 the time Mr. Shudak signed the Note and the Collateral Assignment granting Mr. Van Hook 50
9 percent in PSA membership interests, he had already assigned 132.5 percent of PSA membership
10 interests as PSA's manager.

11 *Mishandling of Funds*

12 145. The Division alleges that Mr. Shudak misused investor funds. The investor witnesses
13 testified that based on their discussions with Mr. Shudak, they believed their funds would only be
14 used to purchase and develop the Bisbee Project. They received the impression that Mr. Shudak
15 would not be taking a salary as PSA's manager, but rather any money he received would come when
16 the property was developed and/or sold. Mr. Schwank and Mr. Swandal testified that some of their
17 understanding on these and other issues came from reviewing the few investment documents Mr.
18 Shudak provided, such as the CC1900 and PSA Operating Agreements.

19 146. The Division asserts that the evidence presented at hearing demonstrated Mr. Shudak
20 transferred PSA investor funds on several occasions that benefitted neither CC1900 nor the Bisbee
21 Project and points out that Mr. Shudak did not present any evidence to show that the funds were used
22 solely for the benefit of CC1900 and PSA investors. The Division concludes that Mr. Shudak's use
23 of investor funds for purposes other than those represented to investors constitute a violation of the
24 anti-fraud provisions of the Securities Act.

25 147. According to Mr. Shudak, the testimony of the three investor witnesses reflects their
26 failure to conduct any due diligence regarding the specifics of the investment and the Division
27 produced no evidence supporting the contention that Mr. Shudak made the representations the
28 investors claim he made. Specifically, Mr. Shudak states there is no evidence he represented to PSA

1 investors that all their investment funds would be transferred into CC1900's bank account upon the
2 funds' deposit for project costs.

3 148. Further, Mr. Shudak notes Ms. McDermitt-Fields testified that she had traced funds
4 into and out of PSA's bank account for only two of the 17 investments, but she could not determine,
5 even for this limited sampling, for what purposes the funds were used. Mr. Shudak also noted Mr.
6 Schwank testified it was possible that PSA could have paid CC1900's expenses directly, rather than
7 transferring money from PSA's account to CC1900's bank account.

8 Conclusion

9 149. Using Chase Bank records, Ms. McDermitt-Fields demonstrated that during April
10 2008 and August 2008, Mr. Shudak transferred funds out of PSA's account and into his personal
11 account, the accounts of other individuals, or the bank accounts of his other businesses. The Division
12 did not submit any direct evidence that the funds were used for impermissible purposes after they
13 were transferred. The records reflect that some checks written against PSA's account during those
14 two months were for unknown people or entities, or for unidentifiable expenses. The Division did
15 not offer direct evidence showing how the funds were used. Further, there is no evidence that the act
16 of transferring the funds out of PSA's account to anywhere other than CC1900's account was, of
17 itself, fraudulent. Mr. Schwank acknowledged it was possible that PSA or Mr. Shudak may have paid
18 some costs directly, rather than transfer the funds to CC1900 for payment of project costs.

19 150. In addition to the verbal representations the investor witnesses claim Mr. Shudak made
20 about the use of investor funds, two of the witnesses stated they formed some of their expectations of
21 how Mr. Shudak would manage their funds from the Operating Agreements.

22 151. Section 3.2(A) of CC1900's Operating Agreement stated Mr. Shudak was to pay
23 assessment notices for project costs from CC1900 within ten days of the notice's receipt. It does not
24 specify that the funds must be transferred to CC1900 for payment.

25 152. Section 6.4 of PSA's Operating Agreement allows the manager to open bank accounts
26 and shall be PSA's signatory; it does not state the manager shall be one of several signatories, but *the*
27 signatory, indicating the manager must be the sole signatory on the account. In April 2009, Jill
28 Noetzelman was added as a signatory to the account. The terms on the signature card give Ms.

1 Noetzelman rights equal to Mr. Shudak's to write checks and withdraw funds from the account.
2 Further, at the time she was added as a co-signatory, Ms. Noetzelman was a co-defendant with Mr.
3 Shudak in the two lawsuits filed by creditors against Sticks, Stones and Dirt, resulting in default
4 judgments. Also, Mr. Shudak's Bankruptcy Filing notes "Mr. Shudak has been depositing earnings
5 into [Jill Noetzelman's] account to protect from garnishments."¹⁶⁹

6 153. Adding a second signatory to the PSA account was not permissible under its Operating
7 Agreement. Adding a second signatory who was neither a PSA manager or member and who had a
8 dubious financial history, and giving that person equal access to investor funds, is contrary to the
9 representations made to members under the Operating Agreement; this act was harmful to investors
10 because it placed investor funds at risk.

11 154. Further, Section 7.4 states that the manager will keep proper and complete records and
12 books of account reflecting all transactions fully and accurately. Although there is no evidence
13 showing how Mr. Shudak used the funds that were transferred into his or others' accounts, the act of
14 commingling investor funds with non-investor funds without any books or records demonstrating
15 fully and accurately the purposes of the transfer, is contrary to the manner agreed to by the manager
16 and adverse to the interests of investors.

17 155. There is no evidence that Mr. Shudak ever advised investors that Ms. Noetzelman had
18 been added as a signatory to PSA's bank accounts. Further, despite requests from investors for
19 copies of PSA's financial records, they never received them. If Mr. Shudak recorded each
20 transaction involving investor funds, they would have reflected that investor money was being
21 commingled with non-investor funds.

22 156. Investors should have been advised that an individual with a history of financial
23 mismanagement and who held no office with PSA had been given access to investor funds. Investors
24 should have also been told that investor funds were being commingled with non-investor funds.
25 Information of this sort would alert an investor of the potential for financial mismanagement, which
26 would factor into an investor's decisions.

27

28 ¹⁶⁹ Ex. S-6, page 9.

1 157. We conclude that commingling investor funds with non-investor funds, and allowing a
2 person to have access to investor funds who was not a PSA officer and who had a dubious financial
3 background, constitutes misuse and mishandling of investor funds.

4 158. We find that Mr. Shudak's failure to advise investors that the PSA account and
5 investor funds were being handled in a manner contrary to that represented to investors under the
6 Operating Agreement constitutes an omission of a material fact in violation of the anti-fraud
7 provisions of the Securities Act.

8 *Failure to Disclose Perfected Security Interest*

9 159. The Division contends Mr. Shudak's failure to disclose Nascent's perfected security
10 interest in all of PSA's assets constituted fraud, since PSA represented in the investor's Assignments
11 that there were no liens or encumbrances on membership interests of any kind. The Division asserts
12 that knowledge of a perfected security interest in all of an issuer's assets is material information that
13 would impact an investor's decision to invest. In this instance, given Nascent's 2013 lawsuit against
14 1900 Investors as successor to PSA, the investors have been impacted by the omission. The Division
15 concludes that Mr. Shudak's failure to disclose Nascent's loan constitutes a fraudulent act in violation
16 of the Securities Act.

17 160. Mr. Shudak noted that under Section 6.3 of PSA's operating agreement, he had the
18 authority to borrow money on behalf of the company. Mr. Shudak contends that there is nothing in
19 the record to show when Nascent perfected its security interest or if Mr. Shudak was aware Nascent
20 had done so. Nor was there anything to indicate when Nascent considered PSA to be in default and
21 whether Mr. Shudak was aware Nascent considered PSA to be in default. Mr. Shudak states that if he
22 did not know of either the perfected security interest or Nascent's belief that PSA had defaulted, then
23 he could not have advised investors about it.¹⁷⁰ Mr. Shudak also notes that three of the investors
24 invested before the Nascent loan was made, so he had nothing to disclose to those investors
25 beforehand. In any event, Nascent's note matured on December 31, 2008, and he claims it would not
26

27 ¹⁷⁰ Mr. Shudak cites to several cases supporting a contention that there can be no fraud where the information omitted was
28 not known to the seller: *Hollinger v. Titan Capital Corp.*, 914 F.2d 1564 (9th Cir. 1990); *Golden Rule Ins. Co. v. Montgomery*, 436 F.Supp.2d 980 (D.Ariz. 2006); *In re MicroStrategy, Inc. Secs. Litig.*, 148 F.Supp. 2d 654 (E.D. Va. 2001).

1 have been considered in default until after that date at the earliest.

2 161. Nascent recorded the UCC – 1 Financing Statement with PSA as debtor encumbering
3 all PSA assets with the Arizona Secretary of State’s Office on June 6, 2008. Mr. Shudak asserts that
4 fraud allegations cannot be based on a publicly disclosed loan since the investors could have easily
5 discovered Nascent’s UCC – 1 Financing Statement during due diligence.¹⁷¹ According to the terms
6 of the IPAs, each investor represented and warranted that he had conducted due diligence.

7 Conclusion

8 162. At the time Mr. Shudak entered into the Nascent loan and Nascent perfected its
9 security interest, Mr. Lamer, Mr. Olp and Mr. Swandal had already received their respective PSA
10 membership interests. However, the investor Assignments signed by Mr. Shudak on behalf of PSA
11 contain a covenant and warranty that the membership interest conveyed by PSA was free and clear of
12 any liens and encumbrances of any kind, character or nature. Given Nascent’s perfected security
13 interest, this is a material misstatement.

14 163. Contrary to Mr. Shudak’s contentions, a copy of Nascent’s UCC – 1 Financing
15 Statement recorded on June 6, 2008, was admitted into evidence.¹⁷² Mr. Shudak’s claim that he was
16 not aware Nascent had filed the UCC – 1 Financing Statement conflicts with his assertion that fraud
17 allegations cannot be based on a publicly disclosed loan because the investors could have easily
18 discovered Nascent’s UCC – 1 Financing Statement during their due diligence. If the investors could
19 have discovered it, so, too, could have Mr. Shudak. Also, as stated by the Division, an investor is not
20 required to conduct due diligence before investing. Further, the Loan and Security Agreement signed
21 by Mr. Shudak authorized Nascent to file the UCC – 1 Financing Statement, so Mr. Shudak cannot
22 claim that Nascent’s action was a surprise.

23 164. Mr. Shudak makes a similar argument about whether Nascent considered PSA to be
24 in default. Mr. Shudak signed the loan documents on behalf of PSA and they clearly state the Note’s
25 maturity date and the fact that the Note would not be in default until December 31, 2008. However,
26 whether and when the Note was declared in default is irrelevant. Investors should have been advised

27 ¹⁷¹ *In re Progress Energy Inc.*, 371 F.Supp.2d 548 (S.D. N.Y. 2005); *Drobbin v. Nicolet Instrument Corp.*, 631 F.Supp.
28 860 (S.D. N.Y. 1986).

¹⁷² Ex. S-15, ACC004628.

1 of the perfected security interest prior to making their investments – not just if and when Mr. Shudak
2 defaulted on the loan – and its omission constitutes a violation of the Securities Act.

3 *Failure to Disclose Lawsuits and Default Judgments*

4 165. The Division contends that Mr. Shudak represented to investors, verbally and in
5 CC1900's Operating Agreement, that not only did he have the capability and marketing skills to raise
6 \$2.5 million in capital for a large real estate development, he also had the financial wherewithal to
7 bear the total risk of economic loss if the Project failed.

8 166. The Division reported that contrary to these representations, at the same time as Mr.
9 Shudak was soliciting PSA investors, a number of creditors had filed lawsuits against Mr. Shudak,
10 and/or one of Mr. Shudak's other LLCs, for failure to pay certain debts unrelated to the Bisbee
11 Project. The first lawsuit was filed on July 8, 2008, but more complaints quickly followed. The
12 Division claims Mr. Shudak did not disclose the lawsuits or subsequent entries of default to investors.
13 The Division asserts this type of information is vital to an investor when evaluating the ability of an
14 entity and its managers to raise large sums of money as capital for a significant real estate
15 development. The Division concludes that Mr. Shudak's failure to disclose the lawsuits constitutes a
16 material omission in violation of the anti-fraud provisions of the Securities Act.

17 167. Mr. Shudak maintains that the three investor witnesses never claimed Mr. Shudak
18 represented he had the experience and ability to raise the significant capital needed for CC1900's
19 development plans. Additionally, Mr. Shudak argues there is no evidence in the record that he knew
20 creditors had filed lawsuits against him, and he could not provide investors with information that he
21 did not have. Even if he did know, Mr. Shudak asserts that the Division did not present any evidence
22 that he failed to advise investors of the lawsuits and judgments.

23 168. Mr. Shudak finds the Division's claim that he misrepresented his ability to raise
24 capital questionable, stating that if the Division's assertions are to be believed, Mr. Shudak proved
25 *too* capable of raising capital, resulting in oversubscription of the offering. As such, if Mr. Shudak
26 made the representation, it turned out to be true, rather than fraudulent.¹⁷³

27 ¹⁷³ That the offering was oversubscribed does not reflect on Mr. Shudak's ability to raise capital, but rather on Mr.
28 Shudak's willingness to assign large amounts of membership interests disproportionate to the amount of cash capital
required.

1 Conclusion

2 169. Support for the investors' testimony that Mr. Shudak had represented he was capable
3 of raising large amounts of capital for the purchase and development of a significant real estate
4 venture is found in CC1900's Operating Agreement, which states that not only is Mr. Shudak
5 responsible for the debt financing for the property purchase, but also for contributing additional
6 capital of \$2.5 million, as well as bearing the brunt of the economic loss if the project should fail. To
7 successfully entice potential investors to put tens or hundreds of thousands of dollars into a project,
8 Mr. Shudak would have had to convince them not only of the viability of the project, but also his
9 capabilities as a marketer and salesman. Further, he had to convince them that he was an effective
10 money manager who could be trusted with their investment funds and that he had the financial
11 wherewithal to bear the burden of the entire economic loss if the project failed.

12 170. The existence of multiple lawsuits and/or judgments against Mr. Shudak or his other
13 entities for failure to pay debt does not portray someone who has the financial wherewithal to raise
14 millions of dollars and remain financially viable. This would have been information vital to an
15 investor when evaluating whether to place their money in the Bisbee Project. Mr. Shudak's failure to
16 advise investors of the lawsuits and judgments constitutes an omission of a material fact in violation
17 of the Securities Act.

18 Findings of Fraud

19 171. Based on the testimony and evidence presented in this matter, we find that Mr. Shudak
20 and/or PSA committed fraud in the offer and sale of unregistered securities, engaging in transactions,
21 practices, or a course of business which involved untrue statements and omissions of material facts in
22 violation of A.R.S. § 44-1991 by: 1) Oversubscribing the offering; 2) mishandling and mismanaging
23 investor funds; 3) failing to advise investors of the existence of a perfected security interest in PSA's
24 assets; and 4) and failing to advise investors of lawsuits and default judgments against Mr. Shudak
25 and Mr. Shudak's other business.

26 ...

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1 **Controlling Person Under A.R.S. § 44-1999(B)**

2 172. According to the Division, Mr. Shudak was a controlling person of PSA as defined in
3 A.R.S. § 44-1999(B). In *Eastern Vanguard Forex Ltd. v. Ariz. Corp. Com'n*, the court adopted the
4 SEC's definition of control as "the possession, direct or indirect, of the power to direct or cause the
5 direction of the management and policies of a person, whether through the ownership of voting
6 securities, by contract or otherwise."¹⁷⁴ As PSA's only manager and sole member, Mr. Shudak
7 performed all managerial tasks and marketing duties, and signed every PSA investment document on
8 PSA's behalf. The Division also states that Mr. Shudak had control over PSA's bank accounts and
9 disposition of investor funds under the terms of PSA's operating agreement. The Division asserts the
10 evidence demonstrates Mr. Shudak's power to control and manage PSA, from the entities' formation
11 until he resigned as manager in December 2009. As such, Mr. Shudak is jointly and severally liable
12 with PSA for violations of the Securities Act.

13 173. Mr. Shudak did not address this allegation in his post-hearing briefs.

14 **Conclusion**

15 174. We agree with Staff's evaluation of the facts and application of law regarding this
16 allegation and we find that Mr. Shudak directly or indirectly controlled PSA within the meaning of
17 A.R.S. § 44-1999.

18 175. We further find that Mr. Shudak is jointly and severally liable with PSA for violations
19 of A.R.S. § 44-1991.

20 **Restitution and Administrative Penalties**

21 **Restitution**

22 176. The Division claims that PSA's investors are entitled to restitution under A.R.S. § 44-
23 2032(1), as calculated under A.A.C. R14-4-308(C)(1). According to the Division, the evidence at
24 hearing established that PSA investors and Mr. Van Hook paid to Mr. Shudak, PSA, or an entity
25 controlled by Mr. Shudak, a total of \$2,142,000. PSA's bank records showed that PSA made one
26 payment of \$25,000 and two payments of \$15,000 each to Mr. Olp, or an entity controlled by Mr.

27
28 ¹⁷⁴ 206 Ariz. 399, 412, 79 P.3d 86, 89 (App. 2003).

1 Olp, for a total of \$55,000. Offset against the total amount invested, the Division claims Mr. Shudak
2 owes net restitution of \$2,087,000.

3 177. Mr. Shudak asserts that neither restitution nor administrative penalties are supported
4 by the evidence or Arizona law. Citing *Murdock-Bryant Constr., Inc. v. Pearson*, Mr. Shudak claims
5 that restitution is warranted only in situations where it would be inequitable or unjust for a party to
6 retain any benefit from another party without some form of compensation.¹⁷⁵

7 178. In Mr. Shudak's view, the Division's construction of A.A.C R14-4-308(C)(1) to
8 support restitution calculations "is invalid and should not be followed because it fails to comport with
9 the ordinary meaning and purpose of restitution under Arizona law."¹⁷⁶ He claims the rule does not
10 require evidence that a respondent has benefitted and does not restrict the amount of a restitution
11 award to a respondent's wrongfully obtained profits.

12 179. According to Mr. Shudak, there is not sufficient evidence that he or PSA received any
13 investor funds, or that Mr. Shudak used investor funds for anything other than Bisbee Project
14 expenses. He argues that even if he had benefitted some way from the investments, restitution is
15 limited to the amount of profit wrongfully obtained. Mr. Shudak claims, however, that the evidence
16 does not demonstrate that he wrongfully retained any profit. Further, Mr. Shudak asserts that the
17 Division has failed to prove a valid restitution amount, noting that although the Division is requesting
18 \$2,142,000 in restitution, it only presented bank records supporting \$1,675,000 in investor deposits.

19 180. Mr. Shudak concludes that ordering a restitution award for the amount sought by the
20 Division would penalize Mr. Shudak and give the investors a windfall since they would not only
21 recover their investment, but also retain their interests in CC1900 and the Bisbee Project.

22 181. The Division counters that the law cited by Mr. Shudak relates to private-party
23 contract disputes, not to violations of the Securities Act. Further, if the Commission fails to follow
24 the rules requiring restitution in cash equal to fair market value, it is acting unlawfully.

25 ...

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27 ¹⁷⁵ 146 Ariz. 48, 703 P.2d 1197 (1985).

28 ¹⁷⁶ Respondent's Post-Hearing Brief, page 18, citing *Sharpe v. Ariz. Health Care Cost Containment Sys.*, 220 Ariz. 488,
207 P.2d 741 (App. 2009).

1 Administrative Penalties

2 182. Based on the evidence, the Division calculates Mr. Shudak committed 90 violations of
3 the registration requirements and that for each offer and sale of securities, fraud was involved,
4 resulting in 90 violations of A.R.S. § 44-1991, for 180 total violations of the Securities Act.

5 183. Imposition of a \$5,000 administrative penalty for each violation of the Securities Act
6 would result in a \$900,000 fine. Instead, the Division asserts that at a minimum, the Commission
7 should direct Mr. Shudak, as PSA’s control person, to pay an administrative penalty of \$150,000.

8 Conclusion

9 184. We reject Mr. Shudak’s assertions that the law regarding restitution awards in private-
10 action securities cases applies to actions brought before the Commission for violations of the
11 Securities Act. The Commission is bound by the law as stated in Arizona statutes and the Arizona
12 Administrative Code.

13 185. The Division claims the total amount of investments reflected under the investment
14 documents and the Van Hook Note is \$2,142,000. But as noted in Finding of Fact No. 75, the
15 Division was able to produce evidence supporting only \$84,500 of Tim Banghart’s supposed
16 \$175,000 investment, leaving \$90,500 of his claimed investment funds unaccounted for. Without
17 sufficient records reflecting Mr. Banghart’s payment or the deposit of the remaining \$90,500,
18 restitution of that amount would be improper and it must be excluded from the restitution award.

19 186. Accordingly, we find that Mr. Shudak is liable for total restitution to investors of
20 \$2,051,500 (\$2,142,000 - \$90,500). With the \$55,000 offset for the amounts paid to Mr. Olp, Mr.
21 Shudak owes net restitution of \$1,996,500, plus interest.

22 187. The Division claims that Mr. Shudak and PSA committed 180 violations of the
23 Securities Act. Under A.R.S. § 44-2036, the Commission may impose administrative penalties in an
24 amount not to exceed \$5,000 for each violation, or a maximum of \$900,000. We believe the record
25 in this docket supports the Division’s recommendation that Mr. Shudak should pay an administrative
26 penalty of \$150,000, plus interest.

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28 ...

CONCLUSIONS OF LAW

1
2 1. The Commission has jurisdiction of this matter pursuant to Article XV of the Arizona
3 Constitution and A.R.S. § 44-1801, *et seq.*

4 2. The investment offerings in the form of membership interests, investment contracts
5 and/or notes and sold by Mr. Shudak constitute securities within the meaning of A.R.S. § 44-
6 1801(26).

7 3. Mr. Shudak acted as a dealer and/or a salesman of securities within the meaning of
8 A.R.S. § 44-1801(22).

9 4. The actions and conduct of Mr. Shudak constitute the offer and sale of securities
10 within the meaning of A.R.S. § 44-1801(15) and 44-1801(21).

11 5. Mr. Shudak failed to meet the burden of proof pursuant to A.R.S. § 44-2033 to
12 establish that the securities offered and sold were exempt from regulation under the Securities Act.

13 6. The securities were neither registered nor exempt from registration in violation of
14 A.R.S. § 44-1841.

15 7. Mr. Shudak offered and sold unregistered securities within and from Arizona in
16 violation of A.R.S. § 44-1841.

17 8. Mr. Shudak offered and sold securities within and from Arizona without being
18 registered as a dealer and/or salesman in violation of A.R.S. § 44-1842.

19 9. Mr. Shudak and PSA committed fraud in the offer and sale of unregistered securities,
20 engaging in transactions, practices, or a course of business which involved untrue statements and
21 omissions of material facts in violation of A.R.S. § 44-1991.

22 10. Mr. Shudak directly or indirectly controlled PSA within the meaning of A.R.S. § 44-
23 1999.

24 11. Mr. Shudak is jointly and severally liable with PSA for violations of A.R.S. § 44-
25 1991.

26 12. Mr. Shudak has violated the Securities Act and should cease and desist pursuant to
27 A.R.S. § 44-2032 and from any future violations of A.R.S. §§ 44-1841, 44-1842, 44-1991 and all
28 other provisions of the Securities Act.

1 IT IS FURTHER ORDERED pursuant to authority granted to the Commission under A.R.S. §
2 44-2036, Patrick Leonard Shudak shall pay an administrative penalty of \$150,000. The payment
3 obligations for this administrative penalty shall be subordinate to any restitution obligations and shall
4 become immediately due and payable only after restitution payments have been paid in full or upon
5 Patrick Leonard Shudak's default with respect to Patrick Leonard Shudak's restitution obligations.

6 IT IS FURTHER ORDERED that pursuant to the authority granted to the Commission under
7 A.R.S. § 2036, that Patrick Leonard Shudak shall pay the administrative penalty of \$150,000 payable
8 by either cashier's check or money order, payable to "the State of Arizona" and presented to the
9 Arizona Corporation Commission for deposit in the general fund for the State of Arizona.

10 IT IS FURTHER ORDERED that if Patrick Leonard Shudak fails to pay the administrative
11 penalty of \$150,000, any outstanding balance, plus interest at the rate of the lesser of 10 percent *per*
12 *annum*, or at a rate *per annum* that is equal to one percent plus the prime rate as published by the
13 Board of Governors of the Federal Reserve System of Statistical Release H.15, or any publication
14 that may supersede it on the date that the judgment is entered, may be deemed in default and shall be
15 immediately due and payable, without further notice.

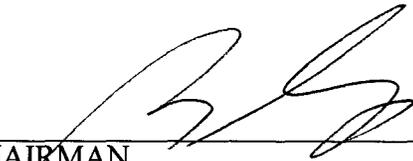
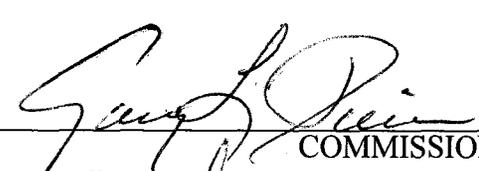
16 IT IS FURTHER ORDERED that default shall render Patrick Leonard Shudak liable to the
17 Commission for its costs of collection and interest at the rate of the lesser of 10 percent *per annum*, or
18 at a rate *per annum* that is equal to one percent plus the prime rate as published by the Board of
19 Governors of the Federal Reserve System of Statistical Release H.15 or any publication that may
20 supersede it, on the date that the judgment is entered.

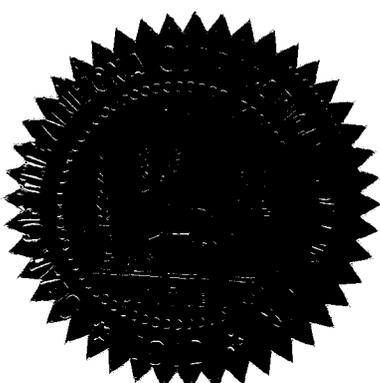
21 IT IS FURTHER ORDERED that if Patrick Leonard Shudak fails to comply with this
22 Decision, the Commission may bring further legal proceedings against Patrick Leonard Shudak,
23 including application to the Superior Court for an Order of Contempt.

24 ...
25 ...
26 ...
27 ...
28 ...

1 IT IS FURTHER ORDERED that pursuant to A.R.S. § 44-1974, upon application the
2 Commission may grant rehearing of this Decision. The application must be received by the
3 Commission at its offices within twenty (20) calendar days after entry of this Decision and, unless
4 otherwise ordered, filing an application for rehearing does not stay this Decision. If the Commission
5 does not grant a rehearing within twenty (20) calendar days after the filing of the application, the
6 application is considered to be denied. No additional notice will be given of such denial.

7 IT IS FURTHER ORDERED that this Decision shall become effective immediately.
8 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

9
10  CHAIRMAN  COMMISSIONER
11
12  COMMISSIONER  COMMISSIONER  COMMISSIONER
13



14
15 IN WITNESS WHEREOF, I, JODI JERICH, Executive
16 Director of the Arizona Corporation Commission, have
17 hereunto set my hand and caused the official seal of the
18 Commission to be affixed at the Capitol, in the City of Phoenix,
19 this 15th day of September 2014.

20 
21 JODI JERICH
22 EXECUTIVE DIRECTOR

23 DISSENT _____

24 DISSENT _____
25 BAM:tv

1 SERVICE LIST FOR: PATRICK LEONARD SHUDAK, PROMISE LAND
2 PROPERTIES, LLC, and PARKER SKYLAR &
ASSOCIATES, LLC

3 DOCKET NO.: S-20859A-12-0413

4
5 Brian J. Schulman
6 GREENBERG TRAUERIG, LLP
7 2375 East Camelback Road, Suite 700
8 Phoenix, AZ 85016
9 Attorney for Respondent Patrick Leonard Shudak

10 PROMISE LAND PROPERTIES, LLC
11 PARKER SKYLAR & ASSOCIATES, LLC
12 ATTN: Roger Keller
13 30 North Cerro Alto Drive
14 Fountain Hills, Arizona 85258

15
16 Matt Neubert, Director
17 Securities Division
18 ARIZONA CORPORATION COMMISSION
19 1300 West Washington Street
20 Phoenix, AZ 85007
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23
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