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BEFORE THE ARIZONA CORPORATION COMMISSION

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DEC 30 2016

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In the matter of: )  
BART J. ELLIS and COLLEEN ELLIS, husband )  
and wife, )  
OAK CAPITAL PARTNERS, LLC, an Arizona )  
limited liability company, )  
Respondents. )

DOCKET NO. S-20949A-16-0002  
**SECURITIES DIVISION'S REPLY BRIEF**  
**Hearing Date: September 12, 2016**  
**Assigned to Administrative Law Judge Mark Preny**

The Securities Division ("Division") of the Arizona Corporation Commission ("Commission") submits its Reply Brief ("Reply") with respect to the administrative hearing held on September 12, 2016.

**Introduction.** The Division's underlying case against Bart Ellis is uncontested: Ellis failed to file an answer or otherwise appear at any phase of the hearing, and Colleen Ellis ("Respondent Spouse") chose not to address the conduct of Bart Ellis in her post-hearing Memorandum (the "Memorandum"). Rather, Respondent Spouse focuses on the application of Arizona community property law to the obligations created by Ellis's violations of the Securities Act and the Investment Management Act. This Reply addresses the salient arguments in the Memorandum.

**Respondent Spouse's non-participation in Oak Capital and her ignorance of Bart Ellis's conduct is immaterial.** Respondent Spouse mistakenly finds it significant that there was no evidence that she knew of or consented to her husband's illegal conduct or that she participated in the business. She cites no case law supporting her position.

The governing statute, A.R.S. § 25-214, not only does not require spousal knowledge for one spouse to bind the community property, it specifically says that "Either spouse *separately*

1 may...bind the community....”<sup>1</sup> The three exceptions to this ability to separately create debt are  
2 listed in the statute, and do not apply here. These are certain real-estate transactions, a guaranty, or  
3 obligations acquired.<sup>2</sup>

4 Arizona case law holds that a spouse does not need to participate in or be aware of the  
5 conduct giving rise to the community debt. The Arizona court of appeals has held that a wife’s failure  
6 to acquiesce in her husband’s incurring of obligations in furtherance of the community does not  
7 avoid community liability.<sup>3</sup> Other courts have held that a spouse’s illegal conduct may bind the  
8 marital community without the other spouse being aware of the obligation.<sup>4</sup>

9 Consequently, Respondent Spouse’s lack of knowledge or participation does not affect the  
10 community’s debt obligation.

11 **The conduct creating the debt occurred within and from Arizona, in violation of**  
12 **Arizona law.** In the second paragraph of the “Argument” section of the Memorandum, Respondent  
13 Spouse appears to be arguing that Ellis’s and Oak Capital’s conduct should not create a community  
14 obligation because it is a continuation of conduct that occurred prior to Ellis moving to Arizona, or  
15 because a portion of the conduct occurred in Illinois, or both.

16 A debt is incurred at the time of the actions that give rise to the debt.<sup>5</sup> This includes  
17 obligations from a post-marital judgment arising out of premarital acts.<sup>6</sup>

18 The conduct at issue occurred within and from Arizona, through an Arizona entity, in  
19 violation of Arizona law, while Ellis and Respondent Spouse resided in Arizona.<sup>7</sup> Since Ellis was  
20 married at the time the violations creating the obligation occurred, it is presumed to be an obligation  
21 of his marital community unless Respondent Spouse presents clear and convincing evidence  
22

23 <sup>1</sup> A.R.S. § 25-214(C) (emphasis added).

24 <sup>2</sup> *Id.*

25 <sup>3</sup> *Keplinger v. Boyett*, 6 Ariz. App. 514, 517, 433 P.2d 1006, 1009 (Ct. App. 1967).

26 <sup>4</sup> *Cadwell v. Cadwell*, 126 Ariz. 460, 462, 616 P.2d 920, 922 (Ct. App. 1980); *In re Rollinson*, 322 B.R. 879, 882 &  
884 (Bankr.D.Ariz. 2005) (The community was liable for spouse’s embezzlement, even though other spouse was  
unaware of embezzlement).

<sup>5</sup> *Arab Monetary Fund v. Hashim*, 219 Ariz. 108, 111, 193 P.3d 802, 806 (Ct. App. 2008).

<sup>6</sup> *McKee v. Conkle*, 23 Ariz.App. 249, 250, 532 P.2d 191, 192 (Ct. App. 1975).

<sup>7</sup> See Division’s Opening Brief pp. 3–4, and citations therein.

1 showing that the debt is a sole and separate obligation.<sup>8</sup> At hearing, Respondent Spouse presented  
2 no evidence at all, clear and convincing or otherwise, to rebut the presumption. Consequently, the  
3 debt created by Ellis's violations of the Securities Act and the IM Act are a community debt owed  
4 to the State of Arizona.

5 **The use of separate bank accounts does not provide clear and convincing evidence to**  
6 **rebut the presumption that Ellis's actions benefited the community.** Respondent Spouse points  
7 out that she and Ellis maintained separate bank accounts. This seems to be an attempt to argue that  
8 the existence of separate accounts are sole and separate property. There is, however, no evidence  
9 that these bank accounts were intended to be or maintained as sole and separate property. In fact,  
10 the evidence showed that money from these separate accounts went to the both spouses.<sup>9</sup>

11 It is Respondent Spouse's burden to provide clear and convincing evidence of separate  
12 property. "Clear and convincing" is a higher burden than a preponderance of evidence. The Arizona  
13 Supreme Court has stated that, "the clear and convincing standard is an intermediate standard,  
14 between proof beyond a reasonable doubt and proof by a preponderance of the evidence, and that  
15 clear and convincing evidence is evidence that makes the existence of the issue propounded 'highly  
16 probable.'"<sup>10</sup> Respondent Spouse's failure to present evidence, and the Division's evidence showing  
17 the joint use of funds in Ellis's account, make meeting her high burden of proof impossible; the mere  
18 existence of separate bank accounts does not overcome this.

19 Likewise, there is no evidence that any other funds or property in either Ellis's or Respondent  
20 Spouse's possession was separate property. Respondent Spouse's Memorandum cites to page 74 of  
21 the hearing transcript as evidence that she maintained separate property. This is the testimony of the  
22 Division's investigator. His testimony does not support Respondent Spouse's claim. As shown in  
23 the transcript, Respondent Spouse's counsel asked the investigator if, as far as he could tell,  
24 Respondent Spouse maintained sole and separate *employment*. The investigator replied "As far as I

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26 <sup>8</sup> *Hrudka v. Hrudka*, 186 Ariz. 84, 91, 919 P.2d 179, 186 (Ct. App. 1995).

<sup>9</sup> Exs. S-25, S-26 and S-30.

<sup>10</sup> *State v. King*, 158 Ariz. 419, 426, 763 P.2d 239, 246 (1988).

1 know, yes, sir.”<sup>11</sup>

2       **Respondent Spouse equivocates different definitions of the word “contract” when**  
3 **interpreting A.R.S. § 25-215.** The statute states that “either spouse may contract debt.”<sup>12</sup> Ignoring  
4 the grammatical structure of the statute, and the fact that the word “contract” can mean to acquire as  
5 well as refer to written documents, Respondent Spouse reads A.R.S. § 25-215 to require a contractual  
6 agreement to create community liability. Case law makes it clear that the phrase “contract debt” in  
7 the statute has the broader meaning, i.e. to acquire debt: “Generally, all debts incurred during  
8 marriage are presumed to be community obligations unless there is clear and convincing evidence  
9 to the contrary.”<sup>13</sup> The Arizona court of appeals has referred to a “debt *or* contractual obligation”  
10 when interpreting this statute.<sup>14</sup> Community debts include those contracted by the husband in  
11 furtherance of community affairs and by the wife for necessities for herself and her children during  
12 the marriage.<sup>15</sup> Arizona courts have found that community debts can include non-contract items,  
13 such as tax liens,<sup>16</sup> medical care costs,<sup>17</sup> and debt caused by embezzlement.<sup>18</sup> Thus Ellis’s debt that  
14 binds the marital community need not be based on a contract.

15       **The Division’s action against Ellis and Oak Capital is based on statutory violations, not**  
16 **tort law.** Respondent Spouse merely asserts without citing authority that the Division’s claims  
17 against Ellis are intentional tort claims and, consequently, the Division needed to prove that Ellis  
18 intended for his actions to benefit the community. The Division was unable to find any authority  
19 supporting the assertion that an agency bringing an enforcement action for statutory violations is an  
20 intentional tort claim. In fact, the Division was unable to find any authority that even calls a case for  
21 violations of securities laws—even when brought by private parties—a tort action. In the cases the  
22

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23 <sup>11</sup> Hr. Tr. p. 74.

24 <sup>12</sup> A.R.S. § 25-215(D).

25 <sup>13</sup> *Schlaefer v. Financial Management Service, Inc.*, 196 Ariz. 336, 339, 996 P.2d 745, 748 (Ct. App. 2000).

26 <sup>14</sup> *Garrett v. Shannon*, 13 Ariz. App. 332, 333, 476 P.2s 538, 539 (Ct. App. 1970) (emphasis added).

<sup>15</sup> *Wine v. Wine*, 14 Ariz.App. 103, 104–5, 480 P.2d 1020, 1021–22 (1971).

<sup>16</sup> *Id.*

<sup>17</sup> *Schlaefer*, 196 Ariz. at 339, ¶ 10, 996 P.2d at 748 (Medical debt is presumed to be a community obligation; in this case, a premarital agreement provided clear and convincing evidence to rebut that presumption).

<sup>18</sup> *In re Rollinson*, 322 B.R. at 882.

1 Division could find that discussed both intentional torts and securities law violations, the two causes  
2 of action were either separate causes of action subject to separate analysis,<sup>19</sup> or used analogies from  
3 tort law used to explain elements of securities actions.<sup>20</sup>

4 Without establishing that violations of the Securities Act and Investment Management Act  
5 are intentional tort claims, Respondent Spouse's argument that Ellis's actions were intentional torts  
6 and, consequently, that the Division needed to prove that Ellis intended for his illegal conduct to  
7 benefit the community, fails.

8 (This line of argument would fail anyway, since the Division showed that Ellis used illegally-  
9 obtained funds to pay rent of the home Respondent Spouse leased.<sup>21</sup> As noted in a case cited by  
10 Respondent Spouse, *Garrett v. Shannon*, "The law is settled in Arizona that the community property  
11 of both spouses may be liable for an intentional tort committed by one of the spouses where the  
12 intent and purpose of the activity leading to the commission of the tort was to benefit the community  
13 interests."<sup>22</sup> It is not difficult to show that a husband's actions benefitted the community. Directly  
14 on point is *Cadwell v. Cadwell*, a divorce proceeding where the wife's debts relating to a criminal  
15 conviction for embezzlement were allocated as community debts because the community benefitted  
16 from the proceeds of the embezzlement in the form of house payments.<sup>23</sup> That court further held that  
17 benefit to the community need not be the primary object or intention; all that is required is that some  
18 benefit was intended for the community.<sup>24</sup> The Arizona bankruptcy court reached the same  
19 conclusion: where embezzled funds were used to pay family expenses, the community was obligated  
20 to repay the embezzled money.<sup>25</sup>)

21  
22 <sup>19</sup> See e.g. *In re Sevitski*, 151 B.R. 590, 593 (D.Bankry.N.D. 1993) (Securities fraud, unlike intentional torts, creates  
rights of contribution).

23 <sup>20</sup> See e.g. *Bastian v. Petren Resources Corp.* 892 F.2d 680, 683 (7th Cir. 1990) (Rules that have evolved to establish  
private 10b-5 actions are nourished by analogies from law of torts); See also *Holdsworth v. Strong*, 545 F.2d 687 (10th  
24 Cir. 1976) (Just as contributory negligence is not a defense to an intentional tort case of fraud, similarly due diligence  
is totally inapposite in the context of intentional conduct required to be proved under Rule 10b-5).

25 <sup>21</sup> Exs. S-25, S-26 and S-30.

26 <sup>22</sup> 13 Ariz. App. at 333, 476 P.2d at 539.

<sup>23</sup> 126 Ariz. 460, 462, 616 P.2d 920, 922 (Ct. App. 1980).

<sup>24</sup> *Id.*

<sup>25</sup> *In re Rollinson*, 322 B.R. at 883; see also *In re Oliphant*, 221 B.R. 506, 509 (D.Bankr.Ariz. 1998).

1           **Physical separation does not dissolve the community or a spouse's authority to**  
2 **unilaterally create community's obligations.** Respondent Spouse points out that she was  
3 physically separated from Ellis for some of the time period when he was violating the Securities Act  
4 and the Investment Management Act. The evidence at hearing suggested that Ellis and Respondent  
5 Spouse were physically separated by, and possibly before, July 15, 2016, the time the Division's  
6 investigator attempted to deliver the Division's list of witnesses and hearing exhibits to Ellis.<sup>26</sup>

7           The physical separation is irrelevant. As provided by statute, only debts accrued after filing  
8 for a *legal* separation that results in a legal separation require the other spouse's joinder.<sup>27</sup> The  
9 Arizona Supreme Court has held that even when a husband and wife are separated, the community  
10 continues to exist and each party has authority to bind the community.<sup>28</sup> Thus, Respondent Spouse  
11 and Ellis's physical separation did not affect the creation of a community obligation.

12           **Because Respondent Spouse filed for divorce after the debt-creating conduct occurred,**  
13 **her subsequent divorce does not affect the community's debt obligation.** For the same reasons  
14 discussed in the previous paragraphs, Respondent Spouse filing for divorce does not remove the  
15 community obligations. A.R.S. § 25-214 states that debts acquired after the filing of divorce are not  
16 community obligations if the divorce then becomes final. As noted above, the debt is incurred when  
17 the underlying action takes place. Here, the conduct that created the debt at issue in this case occurred  
18 from October 2012 through March 2015. Maricopa County Superior Court records show that  
19 Respondent Spouse filed for divorce on April 15, 2016, with a consent decree entered on October 5,  
20 2016. Thus, the conduct occurred well before Respondent Spouse filed a petition for divorce.  
21 Additionally, an obligation of former marital community may be collected from post-divorce  
22 separate property of each former spouse and from post-divorce property to extent of former spouse's  
23 contribution thereto.<sup>29</sup> Consequently, Ellis's debt obligations for his Securities Act and Investment

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25 <sup>26</sup> H.T. pp. 28 – 29.

26 <sup>27</sup> A.R.S. § 24-214(C)(3).

<sup>28</sup> *Neal v. Neal*, 116 Ariz. 590, 593, 570 P.2d 758, 761 (1977).

<sup>29</sup> *In re Oliphant*, 221 B.R. at 509; *Community Guardian Bank v. Hamlin*, 182 Ariz. 627, 631, 898 P.2d 1005, 1009 (Ct. App. 1995).

1 Management Act violations are, and will remain, community obligations.

2         **Respondent Spouse's description of how funds were spent is a failed attempt to shift**  
3 **her burden of proof.** Respondent Spouse points out that the Division did not show that every cent  
4 acquired by Ellis went to benefit the community. She cites no authority requiring a showing that all  
5 funds obtained through a community debt must go directly to the benefit of the community. And, as  
6 the cases above show, the focus is on whether the person contracting the debt was married when the  
7 debt was incurred. (Even the cases cited by Respondent Spouse in her mistaken argument that the  
8 Division's action is an intentional tort action only require a showing that the community obtained  
9 some benefit from the underlying activity; they do not require showing that it obtained the entire  
10 proceeds.)

11         Respondent Spouse appears to be attempting to shift her burden of proof in complete  
12 disregard to the established law. As noted above, a debt incurred by a spouse during marriage is  
13 presumed to be a community obligation.<sup>30</sup> A party contesting the community nature of a debt bears  
14 the burden of overcoming that presumption by clear and convincing evidence.<sup>31</sup> Since Respondent  
15 Spouse did not present evidence to overcome the presumption that Ellis's obligations are community  
16 obligations, the marital community is liable for Ellis's debts.

17         Respondent Spouse discusses the funds that went to the trading account and were then lost  
18 (she fails to mention that \$141,084 from the trading account was transferred back to Ellis<sup>32</sup>). The  
19 funds that went to the trading account were acquired as part of Ellis's livelihood. Many of the funds  
20 went to further support his livelihood. Because Ellis was married, it is presumed that his income is  
21 community income.

22         **Conclusion.** The evidence at hearing showed that Respondent Spouse was married to Bart  
23 Ellis while he engaged in the conduct described in the Notice, which Ellis and Oak Capital admitted  
24 to and which was established at hearing. This creates a presumption of community liability. It is

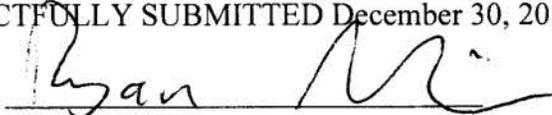
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<sup>30</sup> *Hrudka*, 186 Ariz. at 91, 919 P.2d at 186; *See also Johnson v. Johnson*, 131 Ariz. 38, 45, 638 P.2d 705, 712 (1981).

26 <sup>31</sup> *Id.*

<sup>32</sup> Ex. S-25.

1 Respondent Spouse's burden to overcome the presumption with clear and convincing evidence.  
2 Respondent Spouse presented no evidence—rebutting the presumption of community liability or  
3 otherwise—at the hearing. Though it had no obligation to do so, the Division proved that at least  
4 some of the acquired funds went directly to the community in the form of rent. Ellis also spent funds  
5 on retail purchases, utilities, medical care, elementary school tuition and daycare, and credit cards  
6 (including \$10,477 to Respondent Spouse's credit card). All evidence presented at hearing showed  
7 that Ellis's actions benefitted the community. Thus, an order of restitution and penalties against Ellis  
8 creates a community obligation.

9  
10 RESPECTFULLY SUBMITTED December 30, 2016.

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13 Attorney for the Securities Division of the  
14 Arizona Corporation Commission  
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1 On this 30th day of December, 2016, the foregoing document was filed with Docket Control as a  
2 Securities Division Brief, and copies of the foregoing were mailed on behalf of the Securities  
3 Division to the following who have not consented to email service. On this date or as soon as possible  
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5 the following who have consented to email service.

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