INITIAL DECISION RELEASE NO. 1030
ADMINISTRATIVE PROCEEDING
FILE NO. 3-16594

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

In the Matter of

EQUITY TRUST COMPANY : INITIAL DECISION
: June 27, 2016

APPEARANCES: David Stoelting, Andrew Dean, and Luke Fitzgerald for the Division of Enforcement, Securities and Exchange Commission

Howard M. Groedel of Ulmer & Berne LLP and
Stephen J. Crimmins and Brian M. Walsh of Murphy & McGonigle P.C.
for Respondent Equity Trust Company

BEFORE: Carol Fox Foelak, Administrative Law Judge

SUMMARY

This Initial Decision dismisses charges brought against Equity Trust Company. The charges concerned its role as custodian of so-called "self-directed" individual retirement accounts that held investments promoted by individuals who turned out to be fraudsters. Equity Trust is not registered with the Securities and Exchange Commission in any capacity.

I. INTRODUCTION

A. Procedural Background

The Commission instituted this proceeding with an Order Instituting Proceedings (OIP) on June 16, 2015, pursuant to Section 8A of the Securities Act of 1933. The undersigned held an eight-day hearing in Washington, D.C., in December 2015. The Division of Enforcement called nineteen witnesses, including two expert witnesses, from whom evidence was taken, and Respondent called eight witnesses, including three expert witnesses. Numerous exhibits were admitted into evidence.[1]

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[1] Citations to the transcript will be noted as "Tr. __." Citations to exhibits offered by the Division and Respondent will be noted as "Div. Ex. __" and "Resp. Ex. __," respectively.

The findings and conclusions in this Initial Decision are based on the record and public official records of which official notice has been taken, pursuant to 17 C.F.R. § 201.323. Preponderance of the evidence was applied as the standard of proof. *See Steadman v. SEC*, 450 U.S. 91, 96-104 (1981). Pursuant to the Administrative Procedure Act, 5 U.S.C. § 557(c), the following post-hearing pleadings were considered: (1) the Division's Proposed Findings of Fact and Conclusions of Law, filed February 1, 2016; (2) Respondent's Post-Hearing Brief, filed February 1, 2016; and (3) the parties' February 29, 2016, Replies. All arguments and proposed findings and conclusions that are inconsistent with this Initial Decision were considered and rejected.

B. Allegations and Arguments of the Parties

This proceeding concerns the role of Equity Trust Company, a custodian for individual retirement accounts, in processing investments for customers referred by two promoters who were subsequently convicted for fraud. The OIP alleges that Equity Trust's procedures were deficient such that it was a cause of violations by the two promoters of Securities Act Sections 17(a)(2) and 17(a)(3). OIP at 2. The Division is seeking a cease-and-desist order, disgorgement, a civil penalty, and an order that Equity Trust retain an independent compliance consultant for a period of three years. Div. FOF at 181-88. Equity Trust argues that this proceeding is constitutionally infirm, that the investments at issue were not securities, that it did not fail in any duties to the investors, and that, in any event, the sanctions are inappropriate. Resp. Br. at 45-50, 55-63.

C. Procedural Issues

Respondent argues that the proceeding is unconstitutional because the Commission appoints administrative law judges in a manner that is inconsistent with the Appointments Clause of the United States Constitution and because it otherwise lacks due process. Resp. Br. at 62-63. However, the Commission has rejected the Appointments Clause argument. *Raymond J. Lucia Cos., Inc.*, Securities Exchange Act of 1934 Release No. 75837, 2015 SEC LEXIS 3628, at *76-90 (Sept. 3, 2015), *appeal pending*, No. 15-1345 (D.C. Cir.); *accord Timbervest, LLC*, Investment Advisers Act of 1940 Release No. 4197, 2015 SEC LEXIS 3854, at *89-104 (Sept. 17, 2015), *appeal pending*, No. 15-1416 (D.C. Cir.); *David F. Bandimere*, Securities Act Release No. 9972, 2015 SEC LEXIS 4472, at *74-86 (Oct. 29, 2015).

Respondent's argument that the proceeding deprives it of its right to a jury trial also fails. *Atlas Roofing Co. v. OSHRC*, 430 U.S. 442 (1977).[2]

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[2] Respondent cites *Atlas Roofing* in support of its argument that it was denied its constitutional right to a jury trial even though the Supreme Court upheld administrative adjudication of violations and of imposition of monetary penalties. Resp. Br. at 63. Respondent argues that its rights were violated because the Commission could have sued it in court where it would have had a right to a jury trial – essentially, Respondent argues that the Commission's exercise of prosecutorial discretion violates the Constitution. *Id.* It is not clear why the exercise of prosecutorial discretion violates the Constitution.

Respondent urges that the Commission's administrative proceedings are inherently unfair and violate the Due Process Clause in that: the Division had years to prepare its case, taking as many depositions as it chose, while Respondent was constrained to a short timeline with limited discovery that does not include depositions; the Commission has no rules of evidence, resulting in a record that includes extensive amounts of hearsay; and, after being rushed to hearing, Equity Trust will have to wait years for the Commission's *de novo* review of the initial decision, if either party seeks review, before the Commission issues its final decision, far longer than in federal district court. Resp. Br. at 62.

Respondent cites no authority to show that the procedures of the Commission's administrative proceedings violate the Due Process clause. Indeed, "[t]he fundamental requirement of due process is the opportunity to be heard 'at a meaningful time and in a meaningful manner.'" *Matthews v. Eldridge*, 424 U.S. 319, 333 (1976) (quoting *Armstrong v. Manzo*, 380 U.S. 545, 552 (1965)); *see also Jonathan Feins*, Exchange Act Release No. 41943, 1999 SEC LEXIS 2039, at *25-26 (Sept. 29, 1999) ("Administrative due process is satisfied where the party against whom the proceeding is brought understands the issues and is afforded a full opportunity to meet the charges during the course of the proceeding."). Respondent had an eight-day hearing and the opportunity to call witnesses and cross-examine the Division's witnesses. While the procedures of the administrative proceedings may differ in some respects from those in district court, Respondent has not shown that they violate the Due Process clause.

II. FINDINGS OF FACT

A. Relevant Individuals and Entities

1. Self-Directed Individual Retirement Accounts

The investment vehicles at issue are a variation of the individual retirement account (IRA) in which investments, pursuant to the Internal Revenue Code and rules, are funded by pre-tax contributions and are not taxed until distribution to the individual account holder. Major wire houses serve as custodians for many IRAs.[3] The IRA custodian holds title, for the benefit of the customer, to the IRA assets and provides timely reporting and filings to the IRS. Tr. 990-92. A so-called "self-directed" IRA (SDIRA) is an IRA administered by a custodian that permits investments in alternative assets other than publicly traded stocks and bonds, such as promissory notes, real estate, private placement securities, and precious metals. Div. Exs. 857-58. Typically, major wire houses do not serve as custodians for SDIRAs. Tr. 962-63.

[3] Tax treatment of IRAs is as provided in 26 U.S.C. § 408, which describes an IRA as a trust and requires the trustee to be a bank; the term "bank" includes "a corporation which, under the laws of the State of its incorporation, is subject to supervision and examination by the Commissioner of Banking or other officer of such State in charge of the administration of the banking laws of such State." 26 U.S.C. § 408(a)(2), (n)(3). "[A] custodial account is treated as a trust." 26 C.F.R. § 1.408-2(d).

In a September 2011 Investor Alert, titled "Self-Directed IRAs and the Risk of Fraud," of which official notice is taken pursuant to 17 C.F.R. §201.323 and which is in the record as Respondent Exhibit 46, the Commission warned that promoters of fraudulent schemes may exploit SDIRAs because they permit investors to hold unregistered securities and the custodians of the accounts likely have not investigated the securities or the background of the promoter. Resp. Ex. 46 at 2. The Commission explained, "Self-directed IRA custodians generally do not evaluate the quality or legitimacy of any investment in the self-directed IRA or its promoters. Furthermore, most custodial agreements between a self-directed IRA custodian and an investor explicitly state that the self-directed IRA custodian has no responsibility for investment performance." *Id*.

2. Equity Trust

Equity Trust is a private corporation ultimately owned by members of the Desich family. Tr. 200, 650. Its principal place of business is in Ohio. Answer at ¶ 6. Jeffrey Desich is, and was during the relevant period, Equity Trust's CEO. Tr. 603, 964-65. Equity Trust came into being in 2003 when it assumed the SDIRA accounts of a predecessor, Mid-Ohio Securities Corp. Tr. 924-25. Mid-Ohio was a broker-dealer whose president and CEO was Desich's father.[4] Tr. 924-26, 933; Div. Ex. 598 at 38. Desich joined Mid-Ohio in 1999, when his father was still actively running the business. Tr. 924, 932-33. Equity Trust is not registered with the Commission in any capacity. It is organized and chartered under the laws of South Dakota and is regulated by the South Dakota Division of Banking as a South Dakota public trust company.[5] Tr. 1158-59; Div. Ex. 598. Equity Trust has 130,000 to 140,000 customers and currently is

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[4] *See* Mid-Ohio Securities Corp., BrokerCheck Report, *available at* http://brokercheck.finra.org (last visited May 26, 2016). Official notice is taken of this and any other Financial Industry Regulatory Authority, Inc. (FINRA), records cited herein. *See Joseph S. Amundsen*, Exchange Act Release No. 69406, 2013 SEC LEXIS 1148, at *2 n.1 (Apr. 18, 2013), *pet. denied*, 575 F. App'x 1 (D.C. Cir. 2014). Mid-Ohio was registered from 1974 to 2013; regulatory authorities imposed sanctions on it a number of times. *See* Mid-Ohio Securities Corp., BrokerCheck Report. In a 2003 settlement order, the Commission found that Mid-Ohio violated customer protection, net capital, recordkeeping, and reporting rules in the operation of its IRA custodian business; the sanctions were a cease-and-desist order, a censure, and a $25,000 civil penalty. *Mid-Ohio Sec. Corp*., Exchange Act Release No. 48635, 2003 SEC LEXIS 2446 (Oct. 15, 2003).

[5] The Division of Banking conducts examinations of public trust companies, such as Equity Trust, every twenty-four months; it follows guidance contained in the Federal Deposit Insurance Corporation trust examination manual and Office of the Comptroller of the Currency (OCC) handbooks, such as the OCC's Common Trust Funds handbook. Tr. 1161-62. It conducted an examination in 2010, after Equity Trust acquired Sterling Trust Company of Waco, Texas, with the assistance of the Texas Department of Banking. Div. Ex. 595 at 3. It conducted examinations in 2011 and 2014 with the assistance of the Texas Department of Banking and the Ohio Division of Financial Institutions. Div. Ex. 596 at 3; Div. Ex. 597 at 6.

custodian for $13 to $14 billion in SDIRA assets. Tr. 961-62. Its size increased greatly in 2009, during the time at issue, when it acquired Sterling Trust Company of Waco, Texas.[6]

Equity Trust's target investor was a person of modest resources. Its publication "Proven Wealth Building Secrets – For You and Your Children" stated:

> Equity Trust Company was formed to meet the needs of the small- and medium-sized investor. Most (99%) IRA custodians do not allow non-traditional investments. Equity Trust Company welcomes your account, of any size, and encourages your investment in real estate and other vehicles you already know. Read this report and then call Equity Trust Company at 1-888-ETC-IRAS.

Div. Ex. 548 at 6. The publication reiterated and emphasized: "**But at Equity Trust Company, they actually encourage you to invest in the very areas that other custodians won't allow!**" *Id*. at 22 (emphasis in original).

3. Equity Trust Advised Customers that it was a Passive Custodian

The custodial agreement included in Equity Trust's account opening applications and the company's direction of investment (DOI) forms (by which the account holder directed Equity Trust to make a particular investment) made clear that the account holder was solely responsible for investment decisions and that Equity Trust was a passive custodian, was not a fiduciary, and had no duties or responsibilities with respect to selecting or monitoring the investments.

a. Custodial Agreement

The custodial agreement contained the following language:

> (a) In General. You have exclusive responsibility for and control over the investment of the assets in your IRA. . . .
>
> (b) Custodian Acting in Passive Capacity Only. We are acting solely as a passive custodian to hold IRA assets and we have no discretion to direct any investment in your IRA. Accordingly, we are not a fiduciary (as said term is defined in the Internal Revenue Code, ERISA, or any other applicable federal, state, or local laws) . . . **It is not our responsibility to review the prudence, merits, viability or suitability of any investment directed by you . . . or to determine whether**

[6] As of June 30, 2007, Equity Trust had 38,434 accounts under management, with total assets over $2.4 billion. Tr. 1169; Div. Ex. 594 at 5. As of December 31, 2009, after acquiring Sterling Trust Company, Equity Trust had 128,442 accounts, with holdings approximating $8.7 billion. Div. Ex. 595 at 3, 7, 9. As of year-end 2010 and 2011, it had 133,273 and 132,484 accounts, respectively, with holdings each year approximating $10 billion. Div. Ex. 596 at 12. As of year-end 2012 and 2013, Equity Trust had 142,039 and 140,887 accounts, respectively, with holdings approximating $12 billion. Div. Ex. 597 at 14.

> **the investment is acceptable under ERISA, the Internal Revenue Code, or any other applicable law. We do not offer any investment advice, nor do we endorse any investment, investment product . . . [,] investment advisor, representative, broker, or other party selected by you. . . .**
>
> It is your responsibility to perform proper due diligence with regard to any such representative, investment advisor, broker, or other party. . . .
>
> **We shall be under no obligation or duty to investigate, analyze, monitor, verify title to, or otherwise evaluate or perform due diligence for any investment directed by you . . . .**
>
> Any review performed by us with respect to an investment shall be solely for our own purposes of determining compliance with our internal policies, practices and standards . . . and the administrative feasibility of the investment and neither such review nor its acceptance should be construed in any way as an endorsement of any investment . . . We have no duty or obligation to notify you with respect to any information, knowledge, irregularities or our concerns relating to your investment or your investment advisor, broker, agent, promoter or representative. . . .
>
> You authorize and direct us to execute and deliver, on behalf of your IRA, any and all documents delivered to us in connection with your IRA investments; and we shall have no responsibility to verify or determine that any such documents are complete, accurate or constitute the documents necessary to comply with your investment direction.

Resp. Ex. 92 at 8 (emphasis in original); *see also* Resp. Ex. 90 at 4; Resp. Ex. 91 at 4-5; Resp. Exs. 93-94 at 10; Resp. Exs. 95-96 at 10-11.

b. DOI Forms

The DOI forms contained similar language, emphasized with a bold face warning immediately preceding the Account Owner's Signature line:

> Equity Trust Company (Custodian) does not offer any investment advice, nor does it endorse any investment . . . [,] any financial advisor, representative, broker or other party. . . . It is my own responsibility to perform proper due diligence with regard to any such representative . . . Any review performed by Custodian with respect to investment shall be solely for Custodian's own purposes of determining the administrative feasibility of the investment and in no way should be construed as an endorsement of any investment, investment company, or investment strategy. . . .
>
> Neither Custodian nor any employee or agent of Custodian has selected or recommended any investment for me . . .

> Custodian is acting solely as a passive custodian to hold Retirement Account assets and in no other capacity. . . .
>
> Custodian shall be under no obligation or duty to investigate, analyze, monitor, verify title to or otherwise evaluate any investment. . . .
>
> It is not the responsibility of Custodian to review the prudence, merits, viability or suitability of any investment made by me. . . .
>
> Custodian shall have no duty or obligation to notify the undersigned with respect to any information, knowledge, irregularities or concerns of Custodian relating to my investment or my financial advisor, broker, agent, promoter or representative, except as to civil pleadings or court orders received by custodian. . . .
>
> Custodian's responsibilities and duties shall be limited to those expressly provided herein and under the Custodian's IRA Adoption Agreement. . . .
>
> **My Retirement Account is self-directed and I, alone, am responsible for the selection, due diligence, management, review and retention of all investments in my account. I agree that the Custodian is not a "fiduciary" for my account, as said term is defined in the Internal Revenue Code, ERISA, or any other applicable federal, state or local laws. I hereby direct the custodian, in a passive capacity, to enact this transaction for my account, in accordance with my adoption agreement.**
> **SIGN & DATE CHECK THIS PAGE ONE MORE TIME AND MAKE SURE IT'S COMPLETE, STOP! FORM COMPLETE**
>
> ____________________________________
> Account Owner's Signature Date

Resp. Exs. 88-89, 97-99 at 5 (emphasis in original).

4. Fees

Equity Trust charged customers an annual maintenance fee based on the value of assets in the account; for example, for $1 - $14,999 the fee was $190; for $100,000 - $199,999, $440; for $500,000 - 599,000, $1,500; and for $1,000,000 and over, $1,850. Div. Ex. 696 at 138. For 2010 and after, a $20 paper statement charge was added. *See, e.g.*, Resp. Ex. 135 at 43, 57. Additional fees are charged for special services, such as $5 for processing documents requiring a notary and $30 for wire transfers. Div. Ex. 696 at 138. Most customers pay around $300 to $400. Tr. 995. As Desich opined, this relatively low level of fees would not make economic sense if a SDIRA custodian were required to do extensive due diligence on hard-to-value assets. Tr. 996-99.

5. Privacy Policy

The account application asked for the applicant's name, address, date of birth, Social Security number, a client-selected PIN, citizenship, beneficiaries, and other information. *See, e.g.*, Resp. Ex. 135. Equity Trust included a privacy statement in account statements it sent to customers for the quarters ending September 30: "Equity Trust Company restricts access to your personal and account information to those employees and affiliates who need to know the information to provide products, education materials, or services to you and we educate our employees about the importance of confidentiality and customer privacy." *See, e.g.*, Resp. Ex. 135 at 54, 78; Resp. Ex. 142 at 22, 51; Resp. Ex. 168 at 15, 36; Div. Ex. 696 at 61, 67, 77 (Privacy Statements from selected account statements for the periods ended September 30, 2009, 2010, 2011, and 2013). This representation also appeared in Equity Trust's account opening applications.

Michael Dea is currently Equity Trust's president and during the time at issue was its president and chief financial officer. Tr. 649. Dea testified that the privacy policy allowed certain types of information to be communicated to someone who had a customer's PIN.[7] Tr. 690. Jeffery Bartlett, compliance manager, considered this appropriate. Tr. 896, 903-05, 914-16. Dea and Bartlett's interpretation was consistent with Equity Trust's internal "Customer Data Protection and Privacy Policy," which provided that it might disclose nonpublic personal information:

> In the course of business to administer, enforce, or effect a transaction requested or authorized by the consumer • To service or process a financial product or service requested or authorized by the consumer. . . . To carry out a transaction or product or service the business of which the transaction is a part, and record, service, or maintain the consumer's account in the ordinary course of providing the financial service or product.

Div. Ex. 46 at 2, 14. Investors in City Capital Corporation who submitted their Equity Trust account applications through City Capital, as found *infra*, perforce made their PINs and other personally identifiable information in the applications available to City Capital.

[7] Sales representative Robert Batt had never read the written privacy policy and applied the policy articulated by Dea in providing information to Ephren Taylor, whose assistant Kinetra Dixon had PINs of customers who invested in Taylor's entities. Tr. 306, 342-45. Keith Marsh, sales supervisor, regarded the PIN as protecting the account against unauthorized transactions or against divulging specific confidential information such as a Social Security number. Tr. 221-22, 264. If the investment sponsor was working together with the client on an investment, the sales representative would advise the sponsor whether the client's funds had arrived, or when they were expected, and a dollar amount. Tr. 222-23, 264. This was common practice. Tr. 224, 345.

6. Marketing

Sales representatives were paid $50 for each account opened. Tr. 207, 293-94, 982. Their performance was evaluated on the number of accounts opened. Tr. 201-02, 664. Sales representatives, such as Robert Batt, followed up on leads from various sources, including paid internet advertising.[8] Tr. 447-48, 672; Div. Ex. 563. To achieve his performance goal, Batt made ninety telephone calls a day to yield three new accounts. Tr. 447. Management performed random monitoring of the representatives' calls, amounting to monitoring about three calls per month per representative. Tr. 211-13. If management heard a representative speak favorably of a sponsor, the behavior was corrected through counseling. Tr. 213.

At Equity Trust the term "Center of Influence" (COI) was used interchangeably with "referral source" and "investment sponsor," and referred to persons who referred multiple accounts to Equity Trust. Tr. 210, 293, 663, 1204-05. A COI was associated with a specific sales representative, who would receive credit for accounts opened that had been referred by that COI. *See, e.g.*, Tr. 293-96, 487, 501, 1231-32; Div. Ex. 191. As discussed below, fraudsters Ephren Taylor and Randy Poulson were COIs. Taylor was one of Robert Batt's COIs. Tr. 294-96. Batt's business dealings with Taylor started in about February or March 2008. Tr. 304-05, 446; Div. Ex. 270. Poulson was one of Irene Berlovan's COIs. Tr. 1204-05. Batt understood that he could not endorse a COI or an investment. Tr. 301-03. Berlovan understood that she was not to vouch for the legitimacy of an investment but did not recall any specific training on that. Tr. 1205-06. Keith Marsh, a sales supervisor employed at Equity Trust from 2006 to 2012, who received the general training that all the employees had in about 2006 and later participated as a trainer, recalled that employees were told generally that being a passive custodian meant that they could not give investment advice or endorse any particular investment. Tr. 195-97, 210. At times, sales representatives attended sponsors' events to provide the necessary applications and support to attendees who wanted to open accounts. Tr. 665.

Equity Trust's training for new employees focused on client service etiquette, such as how to engage a prospect on the phone using techniques such as asking open-ended questions; and on features of IRAs, such as eligibility requirements. Tr. 197, 209, 266, 296-97, 301. Employees were told that Equity Trust was a passive custodian and that they could not give investment advice or recommend or endorse any investment. Tr. 209-10, 301. The training did not address the possibility that fraudulent investment promoters might use SDIRAs as vehicles for fraud. Tr. 297-98. Employees who attended sponsors' events were counseled or trained on how to be approachable (*e.g.*, don't sit behind the booth) and how to dress. Tr. 226, 235, 303-04; Div. Ex. 610.

Equity Trust had a "Do Not Process" (DNP) list, emailed to sales representatives every two weeks, of sponsors and investments that could not be processed. Tr. 219, 299; Div. Ex. 490.

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[8] Equity Trust had landing pages such that if an individual using a search engine clicked on Equity Trust's advertisement, he or she would reach a page tied to Pay Per Click asking for name, email address, and phone number that would constitute a lead that Equity Trust could follow up on. Tr. 993-94.

The list did not specify the reason that a particular sponsor or investment was on it. Tr. 299, 427. After Taylor's City Capital Corporation was placed on the list, Batt did not take their phone calls and forwarded any emails to his supervisor, Keith Marsh. Tr. 467; Div. Ex. 519 at 2. City Capital was placed on the DNP list in January 2010. Tr. 427, 470. This stopped any new City Capital investments, but a number of existing City Capital notes were extended. Tr. 763-64, 893. The justification for this was that if Equity Trust did not allow a maturing note to be extended, it would have to be distributed to the customer, resulting in tax consequences.[9] Tr. 894, 916-17. Poulson and his entity Equity Capital Investment were placed on the DNP list on October 25, 2012. Div. Ex. 247; Div. Ex. 578 at 28. If questioned, Equity Capital would tell customers or sponsors that a particular investment was "administratively not feasible," which was a catch-all term that was intended to sound innocuous. Tr. 262-63, 985, 1589-90.

Edwin Kelly worked at Equity Trust from May 2005 to January 2011.[10] Tr. 596. He often spoke at events sponsored by Equity Trust and by others to promote Equity Trust's products and services. Tr. 597-98. At one such event held from October 30 to November 2, 2008, he encountered a speaker named Al Aiello, who sold a course on how to reduce taxes. Tr. 600-01, 636. Aiello, now deceased, saw Kelly reading Taylor's book "Creating Success From the Inside Out" and told him that Taylor was a crook who had cheated a client out of $600,000. Tr. 601-02. Aiello declined to identify the client but offered to provide Kelly's contact information to the client.[11] Tr. 601-02. Kelly testified that he told Desich, while they were still at the event, that Aiello said Taylor was a crook and that Desich instructed him to tell Dea, who was president of Equity Trust and in charge of compliance. Tr. 603-04. Desich testified that he did not recall such a conversation. Tr. 934-35. Kelly testified that he told Dea but did not recall Dea's reaction. Tr. 604. Dea testified that he did not recall ever having a conversation with Kelly on the subject of Aiello's saying that Taylor was a crook. Tr. 712-13. Kelly did not recall discussing Aiello's accusation with anyone else at the time or later. Tr. 606. In light of the sketchy second-hand information originating from Aiello, as well as the fact that Kelly does not recall Dea's reaction, it is found that, even if Kelly's conversations with Desich and Dea took place as he described, they were not memorable so as to constitute red flags putting Desich and Dea on notice that Taylor was a crook.

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[9] This scenario assumes that the customer insisted on extending the note even if Equity Trust refused to hold the extended note. There is no need for a distribution of a note that matured and paid off. The resulting cash could be held in the account or used for a new investment.

[10] Kelly is now in business with Keith Marsh as a SDIRA custodian called Specialized IRA Services. Tr. 624.

[11] Kelly never heard from the unidentified client. Tr. 602.

7. Fraudsters

Equity Trust's customers included persons who invested in investments promoted by Ephren Taylor and Randy Poulson, both of whom were subsequently convicted of offenses related to the events at issue.[12]

a. Ephren Taylor

Taylor was convicted of conspiracy to commit wire fraud; he was sentenced to 235 months of imprisonment, followed by three years of supervised release, and ordered to pay $15,590,752.81 in restitution. *United States v. Taylor*, No. 1-14-cr-217 (N.D. Ga. Mar. 24, 2015), ECF No. 65.[13] Taylor was unable to attend the hearing because of imprisonment; his testimony was taken by deposition, which was admitted at the hearing in the form of a video recording and written transcript.[14] *See Equity Trust Co.*, Admin. Proc. Rulings Release No. 2975, 2015 SEC LEXIS 3045 (A.L.J. July 27, 2015); 17 C.F.R. §§ 201.233(b), .235(a)(3), (5).

b. Randy Poulson

Poulson was convicted of mail fraud; he was sentenced to seventy months of imprisonment, followed by three years of supervised release, and ordered to pay $2,580,940.94 in restitution. *United States v. Poulson*, No. 14-cr-309 (D.N.J. Jan. 22, 2016), ECF No. 27. He testified at the hearing. Tr. 489-594.

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[12] The OIP alleges that Equity Trust has been a custodian for numerous fraudulent investments, "and Poulson and Taylor were just two examples." OIP at 3. However, other fraudsters were only briefly addressed in the record. Tr. 703-04, 732-43. John Bravata was convicted of wire fraud. *United States v. Bravata*, No. 11-cr-20314 (E.D. Mich. Dec. 11, 2013), *aff'd*, 2016 U.S. App. LEXIS 1120 (6th Cir. Jan. 22, 2016). Robert Langguth was convicted of wire fraud and money laundering. *United States v. Langguth*, No. 12-cr-419 (W.D. Tex. Apr. 3, 2013). An individual named Kenneth Starr was also referenced at Tr. 703, but it is not clear whether he is the defendant who was convicted of wire fraud, money laundering, and investment adviser fraud in *United States v. Starr*, No. 10-cr-520 (S.D.N.Y. Mar. 3, 2011), based on the description of the misconduct in the complaint. Additionally, Ron LeGrand, a friend of Desich's father, who gave lectures on profiting from real estate investments, including through SDIRAs, was enjoined against violations of Securities Act Sections 5(a), 5(c), 17(a)(2), and 17(a)(3) and fined $150,000. *SEC v. LeGrand*, No. 11-cv-474 (S.D.W.V. Aug. 2, 2011); Tr. 199-200, 672-73.

[13] Of the total amount of restitution, $5,815,299.13 was ordered to be paid jointly and severally with co-defendant Wendy Connor. *Id*. at 6.

[14] The video recording of the two-day, September 30 and October 1, 2015, deposition is contained in Division Exhibit 37, and the written transcript, in Division Exhibit 36.

B. Taylor Investments

1. Taylor's Business Procedures

Taylor's primary investment vehicle was City Capital Corporation.[15] Div. Ex. 36 at 20-27; Tr. *passim*. City Capital also had subsidiaries including City Beauty Systems, LLC; City Petroleum LLC; City Juice Systems, LLC; City Laundry Services, LLC; Resilient Innovation Systems; New York City Liquidation Group; St. Clair Superior, Inc.; and Cleveland Alpha Properties. Div. Ex. 36 at 26-27, 172; Tr. 804, 809, 811; Div. Ex. 833 at 16.[16] Generally, his investors made short-term loans to Taylor's companies that were evidenced by promissory notes. Div. Ex. 36 at 25-26. The notes did not identify specific uses for the investors' money. *Id*. at 27; *see, e.g.*, Div. Ex. 684 at 126-28. Taylor used Resilient as an alternative borrower to conceal the fact that funds were going to City Capital, for example, when obtaining multiple loans from the same individual. Div. Ex. 36 at 35-36.

Generally, the investor funds were used in ways that differed from the ways Taylor had pitched the investments: the primary use of the funds was for marketing expenses, general overhead, payroll, and servicing old debt, while Taylor told investors that the funds would be used to acquire real estate or a specific business, often centered around socially conscious community development or housing. Div. Ex. 36 at 29-30. City Capital had difficulty in paying the notes from at least 2007 through 2010. *Id*. at 28-29. Also, in 2009, for example, it had insufficient revenue to cover its operating expenses, resulting in a net operating loss of over $5 million. *Id*. at 32-33, 227-29; 2009 Form 10-K. City Capital's periodic reports, filed with the Commission and available to the public on EDGAR, disclosed its parlous financial condition, which worsened each year with increasing liabilities from the notes. Its 2009 Form 10-K contained a going concern statement; the audited financial statements showed current liabilities of $9,660,684 and total assets of $2,997,088 as of December 31, 2009. 2009 Form 10-K at 82. The liabilities were primarily from notes obligations. Div. Ex. 36 at 34-35. The 2008 and 2007 Forms 10-K also contained going concern statements; and the audited financial statements showed current liabilities of $4,839,438 and total assets of $2,531,761 for 2008 and current liabilities of $3,288,319 and total assets of $2,559,742 for 2007.

One method that City Capital used to conserve cash was to persuade investors to extend their notes when they came due, paying only the interest or even incorporating the interest into the new replacement note. Div. Ex. 36 at 102, 313-16. By early 2010, when Equity Trust declined to process new City Capital notes, extensions were critical to City Capital. *Id*. at 101-02.

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[15] Official notice, pursuant to 17 C.F.R. § 201.323, is taken of City Capital's Forms 10-K and other filings with the Commission. Taylor's involvement with City Capital began in 2006. Div. Ex. 36 at 21, 165-66; *see, e.g.,* City Capital's Form 14F, filed July 11, 2006. He resigned from the company on October 22, 2010. City Capital's Form 8-K, filed Nov. 2, 2010.

[16] By December 2010, Equity Trust was aware of more than forty Taylor entities. Div. Ex. 498; Tr. 758-60.

Taylor originally obtained direct loans from individuals. Div. Ex. 36 at 39. Then he learned of SDIRAs and realized that people who did not have significant amounts of available cash might have retirement accounts. *Id*. He saw that this was a vehicle that would allow him to raise capital from significantly more people by rolling over their existing retirement accounts into SDIRAs. *Id*. Taylor held events at a number of churches, real estate seminars, and other venues, as well as making an infomercial and appearing on broadcast shows. *Id*. at 213-19, 307-09. He also was on a panel at the 2008 Democratic Convention and on a panel moderated by David Gergen at a June 2009 conference on volunteering where Michelle Obama was the introductory speaker. *Id*. at 220-22.

Generally, when an individual contacted City Capital as a result of an advertisement or seminar, City Capital evaluated the individual's current retirement account to see if it could be rolled over; if so, City Capital pitched a business option that fit within the amount of the account; if the customer bit, City Capital provided filled-out Equity Trust forms for the customer to sign and return; City Capital then sent the forms to Equity Trust and waited for the money, which often would arrive in about two weeks. Div. Ex. 36 at 47-48, 179-82, 200-03. City Capital's need for speed in processing increased as time went on and its liabilities mounted. *Id*. at 56-57.

In 2010, City Capital promoted gambling machines as SDIRA investments, but Equity Trust declined to custody such property. Div. Ex. 36 at 331-35. City Capital, through another custodian, did deploy the machines in convenience stores, gas stations, and dedicated rooms in Virginia, North Carolina, and Texas. *Id*. at 336-38. The venture failed in Virginia when police raided and seized the machines. *Id*. at 337. Elsewhere, the venture failed due to fraud in that City Capital sold machines that did not exist. *Id*. at 337-38.

2. Relationship with Equity Trust

After experience with some SDIRA custodians whose processing he found to be too slow, Taylor discovered Equity Trust. Div. Ex. 36 at 40-43, 56. After an exchange of emails with Equity Trust, Taylor spoke on the telephone with Robert Batt in approximately 2008. *Id*. at 43-45. Taylor began referring investors to Equity Trust and found its speed in processing their applications satisfactory – two weeks. *Id*. at 44-47. As the volume of business increased, Taylor obtained Equity Trust forms from Batt for Capital City sales representatives to use at Taylor events to sign people up on site. *Id*. at 52.

Taylor sent marketing information to Batt and let him know when he would appear on television or otherwise was mentioned in media. Div. Ex. 36 at 51-52. Batt also kept Taylor apprised of whether his investors' money had arrived at Equity Trust and the amounts. *Id*. at 54; *see, e.g.*, Div. Exs. 275, 335-36, 385. In July 2009, Batt visited City Capital's headquarters in Raleigh, North Carolina, to educate the staff about SDIRAs. Tr. 264-65, 349, 417-19; Div. Ex. 36 at 67-68; Div. Ex. 327. Taylor met Batt in person only once, at the New Birth Missionary Baptist Church event discussed below. Tr. 459-60; Div. Ex. 36 at 71.

3. City Capital Landing Page

Equity Trust created a "landing page" for City Capital as a sub-page on the Equity Trust website.[17] Div. Ex. 525 at 2. The page's first paragraph, headed "City Capital Corporation – Wealth Builder Network," stated "Welcome to the personalized Equity Trust Company page for members of the Wealth Builder Network," and listed Batt as the contact. *Id*. The landing page provided information about SDIRAs and links to forms for customers who wished to open an account with Equity Trust. *Id*.

Development of the landing page reached the beta test stage. Tr. 379-80. The parties dispute whether it ever went live on the Equity Trust website. In any event, the landing page did not promote Taylor or City Capital. City Capital is mentioned once, in the heading quoted above, and Taylor is not mentioned. Div. Ex. 525 at 2. The rest of the page consisted of links to Equity Capital forms and to information about holding real estate in SDIRAs. *Id*.

4. New Birth Missionary Baptist Church

New Birth Missionary Baptist Church is a large church in the Atlanta, Georgia, area, with a predominantly African-American congregation of about 25,000. Tr. 16, 19, 22, 39-40. Its long-time pastor, Bishop Eddie Long, built the church from an original membership of about 300 and was greatly respected and influential over the members. Tr. 40-45, 127-29. Long spoke highly of Taylor. Tr. 50-52, 134, 1372, 1380-81, 1395-96. In October 2009, Taylor came to New Birth to speak about investment opportunities. Tr. 15, 99. He was accompanied by twelve City Capital sales representatives, supplied with Equity Trust forms, to handle the hoped-for enormous volume of applications, appointments, and sales. Div. Ex. 36 at 86-87. He spoke briefly at the Sunday worship service and presented a seminar on the following Tuesday evening to a large group of well over 3,000.[18] Tr. 19-20; Div. Exs. 9, 800. Taylor described SDIRAs, in which the investor controlled where his money was invested, as contrasted to investing in mutual funds, which may invest in companies engaged in ungodly activities, such as strip clubs. Tr. 18, 1351; Div. Ex. 9 at 46-48. Equity Trust sales representative Robert Batt was in attendance in the audience; Taylor asked him to stand up and be recognized as his "personal banker."[19] Tr. 21, 244, 1352-53; Div. Ex. 800-A. Batt did not deny this description at the time. Tr. 26, 1355-56; Div. Ex. 9 at 3-4; Div. Ex. 800-A. Neither Batt nor anyone else from Equity Trust appeared at

[17] Landing pages were created for other investment sponsors as well. Tr. 380-81; *see, e.g.*, Div. Ex. 525 at 3-4.

[18] Taylor estimated the attendance at 6,000 or 7,000. Div. Ex. 9 at 64. Investor Crystal Turner described the church as "packed." Tr. 1352.

[19] Taylor described why he characterized Batt as his "banker": "All the money that we raised, it was coming through Equity Trust and, because of Mr. Batt, it was the same to us as going to the bank and asking to borrow money; he still was that conduit that made that happen." Div. Ex. 36 at 79-80.

any other Taylor events. Tr. 459-60. Batt met Taylor for the first and only time at the New Birth event. Div. Ex. 36 at 71.

After Taylor's speech, investor Lillian Wells approached Batt to ask about SDIRAs, and Batt introduced her to Taylor, who was engaged in signing copies of a book he had written. Tr. 24-25. Taylor handed her over to an associate who made an appointment for her to return on the following Thursday to set up an account with Equity Trust. Tr. 25-27. The appointment was with a Mr. Ferguson, whom Wells understood to be part of Taylor's organization. Tr. 26-27. On that date she signed the account opening documents without reading them closely. Tr. 27-29, 84; Div. Ex. 684 at 197-98; Resp. Ex. 183 at 1-2. She returned the account opening documents, which included a PIN, to Ferguson. Tr. 78. Wells was attracted by the SDIRA concept because she wanted to control where her money was invested. Tr. 53-54, 63. Her IRA was then at Merrill Lynch; she asked her financial advisor there about changing it to a SDIRA, but he declined. Tr. 70. Wells invested funds in a City Capital unsecured promissory note; she signed the DOI without reading it closely. Tr. 31-33; Div. Ex. 684 at 126-32. The funds were never repaid; around the time of the note's September 2010 maturity date, Wells contacted Equity Trust, which told her to contact City Capital about the payment; she did so but got the runaround. Tr. 34-36.

Church member Ronald Jones conferred with Stacey Harvin, Keith McRae, Wendy Connor, Kinetra Dixon, and John Ferguson, all of whom he understood to be associated with Taylor's company, City Capital, as well as with Batt. Tr. 101-16. Jones met with the Taylor associates after the Sunday service and with Batt on the following Tuesday. Tr. 101-14, 157. Between those dates, on October 19, 2009, Jones signed account opening documents. Resp. Ex. 142 at 1-2. On November 10, 2009, Jones signed, without having read it closely, a DOI for an investment in an unsecured promissory note[20] of Resilient Innovations, LLC, which had been filled out by Dixon. Tr. 116-17; Div. Ex. 712. In line with what Taylor described at the Sunday service Jones attended, Taylor's associates said that Resilient was in the business of urban revitalization – rebuilding communities. Tr. 136, 138-39, 149-50. The funds were never repaid; around the time of the note's August 2010 maturity date, Jones contacted Equity Trust and learned that the funds had not been paid into his account; his attempts to contact Resilient were fruitless. Tr. 117-20. Jones believed that Equity Trust endorsed Taylor. Tr. 156, 159.

Crystal Turner and her husband Kenneth Turner attended the October 2009 New Birth event. Tr. 1347-51, 1359. She was favorably impressed with Batt's presence, and spoke to him for two or three minutes after the service.[21] Tr. 1353-55. Then the Turners met with Taylor associates Wendy Connor and Ebony Roland. Tr. 1356-58. The Turners returned the next day,

[20] Jones did not, and does not, understand what an "unsecured note" is. Tr. 153-55.

[21] The next time Mrs. Turner spoke to Batt was after the Turners realized that their money was gone; she left twenty or thirty voicemails without getting a call back and eventually reached him by posing as a fictitious new investor; he told her that she needed to complain to the authorities. Tr. 1393-95. Equity Trust did not want sales representatives performing client service functions. Tr. 225, 267-68.

October 21, 2009, with information concerning their existing investments, and Roland helped Mrs. Turner fill out paperwork to open and fund her Equity Trust account and to invest with City Capital. Tr. 1356-63; Div. Ex. 696 at 117-18, 143-61. She relied on Roland's description and did not read the DOI before signing it. Tr. 1363. Mr. Turner opened an account with Equity Trust at the same time and rolled over an IRA with a relatively small balance into a City Capital promissory note. Resp. Ex. 179 at 1-10. In the spring of 2010, he lost his job and rolled over his 401(k) into an IRA; those funds were transferred in April 2010 from Equity Trust to a different custodian, Sunwest Trust, before being invested with Taylor. Tr. 1365-68; Resp. Ex. 179 at 16-22; Resp. Ex. 255. One of Taylor's associates told Mr. Turner why this needed to be done. Tr. 1367, 1388. No one from Equity Trust discussed the transfer with either of the Turners. Tr. 1367. No one from either Equity Trust or City Capital told Mrs. Turner that Equity Trust would no longer process new investments with Taylor. Tr. 1367. Of the total amount the Turners invested with Taylor, about 10 percent was invested through Equity Trust; another, non-IRA portion, was invested directly in City Capital; and the largest portion, invested after Equity Trust had placed City Capital on its Do Not Process list, was forwarded by Equity Trust to Sunwest Trust on April 20, 2010. Resp. Ex. 179 at 22; Resp. Ex. 255. None of the Turners' investments was repaid. Tr. 1368. They lost their life savings and their house; their loss was especially devastating because Mr. Turner had lost his job. Tr. 1365-70.

Taylor estimated that City Capital raised about $2 million at the New Birth event, enabling it to pay about $800,000 in debt and interest, to meet its payroll and other operational expenses, and to continue marketing. Div. Ex. 36 at 86.

5. Additional Investors

Lawrence W. Hill, Sr., a sixty-four year old truck driver and a deacon of Westside Church of Christ in Jacksonville, Florida, invested with Taylor in 2008. Tr. 165-68. His long-time pastor had invited Taylor to the church to help organize the church's finances. Tr. 168-69, 177-78. The pastor spoke highly of Taylor, saying that he was a young, successful millionaire and a good Christian. Tr. 175, 179, 183. Hill had a one-on-one meeting with Taylor, who advised that he could obtain better returns through Taylor than he was currently receiving in his retirement account. Tr. 171-72, 184. Hill testified that he had one quick phone call, which lasted about one minute, to Batt of Equity Trust about Taylor and City Capital and Batt told him "it's a good company and he's getting people right now 10 percent return on their investment." Tr. 172, 186-87. Batt did not remember the call or Hill. Tr. 340-41. Subsequent to the phone call, Hill's only contact with Equity Trust consisted of receiving quarterly account statements. Tr. 191. Hill signed his Equity Trust account application on April 12, 2008, and mailed the papers back to City Capital. Tr. 174-75, 188; Resp. Ex. 135 at 1. Thereafter, on June 28, 2008, Hill signed a DOI and unsecured promissory note directing his funds to a loan to City Capital. Tr. 188-89; Resp. Ex. 135 at 10-16. Hill signed the DOI without reading it. Tr. 190. When the note matured, Hill renewed it and loaned an additional sum to Resilient in September 2009. Tr. 176, 192; Resp. Ex. 135 at 18-35. To induce Hill to do this, Taylor paid for Hill and his wife to travel to North Carolina, where Hill visited Taylor's office and concluded that the operation looked genuine. Tr. 192-93. The DOIs for the City Capital replacement note and the new Resilient note indicated that the notes were secured, by collateral designated as "Company" – "City

Capital" and "Resilient," respectively. Resp. Ex. 135 at 23, 31. Hill was never repaid the sums he loaned to Taylor's companies, which amounted to almost all of his retirement funds. Tr. 176.

Anita Dorio invested a large sum, including her own and her mother's funds, with Taylor. Tr. 793-94. None of the invested funds was repaid. Tr. 824. Dorio first heard of Taylor when he presented a seminar at her church, Lakewood Church in Houston, Texas, pastored by Joel Osteen. Tr. 794-95, 831-32; Div. Ex. 36 at 214-15. As at New Birth, Taylor advised that mutual funds, available in traditional IRAs, may invest in companies engaged in ungodly activities, such as strip clubs; he offered SDIRAs as an alternative, enabling direct investments in businesses run by members of churches. Tr. 797, 834-35. About three weeks later Dorio and her husband met privately with Taylor, who introduced them to a man who said that he was able to retire from working due to investing with Taylor. Tr. 799, 837-38; Div. Ex. 36 at 185-87. Dorio did not invest at once; rather, she thought about it for a period of time. Div. Ex. 36 at 187. As Taylor described it, she was "on the hook, off the hook, a multitude of times." *Id.* at 115. Before actually transferring funds and investing them with Taylor, Dorio spoke once or twice a week with Taylor or one of his associates. Tr. 842-43; Div. Ex. 36 at 187-92.

Taylor introduced Dorio to Equity Trust via a conference call with Batt. Tr. 799-800. She had not previously heard of Equity Trust, but she believed in Taylor, and his vouching for Batt made her comfortable in dealing with Equity Trust. Tr. 800-01, 848. Dorio talked with Batt a total of two or three times. Tr. 856. The account for Dorio's mother, Virginia Wallace, was opened in December 2008. Div. Ex. 833. The Dorio/Wallace accounts were the biggest investment that Taylor ever landed. Div. Ex. 36 at 116. Contemporaneously, he referred to the Wallace account as "the Big one." Div. Ex. 11.

Dorio believed that the investments were in secured notes. Tr. 813-14; *see, e.g.*, Div. Ex. 833 at 152, 233, 268 (DOIs for notes of City Petroleum, City Laundry, City Juice indicating secured by collateral designated as "Company").

Dorio signed the Equity Trust account application and DOIs without reading them closely. Tr. 866. The bold-face statement: "**I agree that the Custodian is not a "fiduciary" for my account**" appears right above the signature line on one of her DOIs. Resp. Ex. 151 at 6. She acknowledged that she did not focus on it when she signed; however, she understands its meaning: "A fiduciary looks after your interests and a custodian I would say is more of a record keeper." Tr. 867.

Before she invested with Taylor, Dorio's investment advisor was Rick Wheeler, who was associated with AIG. Tr. 815. Batt intervened in Dorio's decision to invest with Taylor as follows: On January 2, 2009, Batt emailed Taylor that the transfer of the Dorio/Wallace funds was in process. Div. Ex. 275. On January 6, Batt updated Taylor on the status of the transfers. Div. Ex. 277. On January 8, Wheeler sent Dorio a letter describing the risks of private placements – illiquidity and potential for reduced income – and urging that she consider the risks as well as the benefits; he advised against overconcentration in such assets. Tr. 817-21; Div. Ex. 830. On January 12, Batt advised City Capital that he would call AIG if the funds did not arrive. Div. Ex. 281. On January 13, he advised City Capital that he had scheduled a conference call with Dorio. Div. Ex. 282. Following the January 14 Batt-Dorio-Wheeler conference call, Dorio

and Batt expected that the funds would be released shortly, and Dorio provided City Capital with the account numbers and password for the funds at AIG. Tr. 822-23, 859-60; Div. Ex. 14; Resp. Ex. 232. Batt sent Taylor an email, in which he denigrated Wheeler and took credit for convincing Dorio for proceeding with the transfer. Div. Ex. 14. Batt advised Taylor that the funds would be wired to Equity Trust the following week and said, "I am on it. . . . I will close it." *Id*. By January 22, the funds had arrived at Equity Trust. Div. Ex. 292.

Dorothy Sims first saw Taylor on a Christian TV channel; he discussed socially conscious investing and SDIRAs and stated that a 401(k) from a previous employer could be rolled over to a SDIRA. Tr. 1399. She purchased a book, titled "3 Simple Steps to Multiply Your Retirement Income," that was promoted on the program, googled SDIRAs, and visited Taylor's website. Tr. 1399-1401, 1432-34; Div. Ex. 35 at 2-60. This occurred in June 2009. Tr. 1400; Div. Ex. 728. Sims was attracted by the idea of socially conscious investing through a SDIRA, rather than by Taylor *per se*. Tr. 1428-32. After reading the book, she telephoned City Capital and was referred to Batt, who emailed an account application to her the same day, July 22, 2009. Tr. 1401-02; Div. Ex. 729. A few minutes later, Kinetra Dixon of City Capital emailed Sims, thanking her for her interest in City Capital. Div. Ex. 727. Dixon noted that Batt had forwarded an Equity Trust application to Sims. *Id.* Dixon offered to answer any questions about the application and instructed Sims to send it to her at City Capital. *Id.* Sims returned the application to Batt. Tr. 1402, 1404. Thereafter Batt telephoned her and asked when she was going to fund the account. Tr. 1404-05. This prodded her into contacting her former employer, Boeing, and arranging to have her 401(k) funds sent to Equity Trust. Tr. 1405. Thereafter, City Capital sent her the DOI, already filled out, for an investment in a promissory note of City Capital. Tr. 1405-07; Div. Ex. 719 at 132-38. She signed the DOI, without reading it closely, on August 19, 2009. Tr. 1408. The DOI indicated that the note was secured, by collateral designated as "Company" – "City Capital." Tr. 1410; Div. Ex. 719 at 137.

Sims's account statements for the quarters ended September 30, 2009, and December 31, 2009, described the note as "secured." Div. Ex. 731 at 2, 4. However, the statement for the quarter ended March 31, 2010, described it as "unsecured." *Id.* at 6. Seeing this, Sims became concerned and tried to call Batt; after multiple unsuccessful attempts, she was told he was no longer with Equity Trust.[22] Tr. 1411. Eventually, another Equity Trust representative told her that she would have to contact City Capital about the change. Tr. 1411-12. The note matured on May 20, 2010. Tr. 1414; Div. Ex. 719 at 132. The money did not, however, appear in her Equity Trust account, and Sims emailed City Capital asking about the funds. Tr. 1415. Dixon telephoned her and advised that she needed to request the funds from City Capital; accordingly, she sent an email to City Capital requesting that the funds be returned but got the runaround over a period of several weeks. Tr. 1415; Div. Ex. 719 at 191-98. Eventually, after July 26, 2010, Sims was not able to contact anyone at City Capital; its email addresses and phone numbers were no longer active. Div. Ex. 719 at 192. The funds were never repaid. Tr. 1415. On September 29, 2011, Sims executed Equity Trust's Uncollectible Unsecured Note Form in order to close her account. Tr. 1415-17; Div. Ex. 719 at 191-98. She attached a chart showing that City Capital's last bid was $0.0032 and material from the internet describing Taylor as a scam. Tr. 1417-18;

[22] Batt left Equity Trust in August 2011. Tr. 292.

Div. Ex. 719 at 185-90. Equity Trust continued to charge her maintenance fees; it waived the fee for 2012, but required her to pay $50 in 2013 and $40 in 2014, threatening to report her to the IRS if she did not pay. Tr. 1419-22.

C. Poulson Investments

1. Poulson's Business

Poulson owned and operated Equity Capital Investments, LLC, and Poulson Russo, LLC. Tr. 501, 571-72; Div. Ex. 267 at 30. Equity Capital bought and sold residential real estate. Div. Ex. 267 at 30. Poulson Russo held educational seminars on investing in real estate. Tr. 589-90; Div. Ex. 267 at 30. Poulson was also the president of South Jersey Investors, Inc.,[23] the New Jersey Association of Real Estate Professionals (NJAREP), and was founder of the Poulson Russo Real Estate Wealth Alliance. Tr. 576-80; Div. Ex. 147.

Poulson, through Equity Capital, obtained the deeds to more than twenty-five residences facing foreclosure based on his promise that he would pay the homeowners' underlying mortgages. Div. Ex. 267 at 31. To help finance these purchases, he issued promissory notes through Equity Capital, promising interest rates between 12 and 20 percent. Tr. 502; Div. Ex. 41 at 2. Poulson solicited investors from the attendees at his Poulson Russo seminars and from other members of South Jersey Investors. Div. Ex. 267 at 31-32. Poulson told investors that the funds would be used to purchase, maintain, and improve specific residential properties. *Id*. at 32. Instead, the funds raised from sale of the Poulson Notes were commingled with other Equity Capital funds and used in part to pay Poulson's personal expenses, such as a vacation to Mexico. Div. Ex. 41 at 2-3. He periodically repaid investors using other investors' money. Div. Ex. 267 at 32. Many properties that were purportedly securing the Poulson Notes were subject to multiple recorded and unrecorded mortgages, with the sum of these mortgages often exceeding the value of the property. Div. Ex. 41 at 4-5, 29. Because the mortgages were not recorded, investors did not know of the existence of other mortgages on the property. Tr. 1766.

From January 2007 through May 2011, 34 Equity Trust customers invested a total of $984,998 in 41 Poulson Notes. Tr. 502; Div. Ex. 41 at 2, 19. Only $341,513 was ever repaid to Equity Trust investors. Div. Ex. 41 at 2.

2. Relationship with Equity Trust

Poulson first heard of Equity Trust while attending real estate investment seminars offered by Ron LeGrand and others and decided to recommend the company to his investors. Tr. 498, 505-06. When he began offering promissory notes, Poulson established a relationship with

[23] This organization later changed its name to the South Jersey Real Estate Investors Association. Tr. 1278.

Equity Trust; Irene Berlovan[24] was his sales representative. Tr. 501, 505, 511. Poulson also had a few investors who used other SDIRA custodians, including Provident and Entrust. Tr. 555-56.

Poulson and Berlovan communicated about marketing opportunities. In 2008, he sent Berlovan text of remarks he proposed to deliver at an Equity Trust "Tax Free Wealth Seminar," touting the benefits of investing in real estate through SDIRAs, and, in particular, Equity Trust. Tr. 508-09; Div. Ex. 144 at 1-2. Berlovan also sent Poulson an article about the advantages of SDIRAs, with her name listed as the contact at Equity Trust. Tr. 1207-08; Div. Ex. 143. Poulson wanted the article for Poulson Russo's newsletters and website. Tr. 507.

When Poulson decided to begin conducting real estate investment seminars, he asked Equity Trust to participate to answer any questions that might arise about SDIRAs. Tr. 510-12, 515. Poulson's marketing and other materials were submitted to Desich and others for review as a "real estate education partner." Div. Exs. 145, 147, 149-51.

In April 2009, Poulson Russo held a real estate investing education event titled the "4 Day Live Interactive Liquidation Extravaganza." Div. Ex. 746; Tr. 513. Both Berlovan and another Equity Trust employee, Edwin Kelly, attended parts of the event. Tr. 587, 610, 1218-19. In the PowerPoint presentation given at the event, and shared with Berlovan beforehand, Berlovan was identified as one of fourteen members of Poulson's "power team" of professionals. Tr. 513-16; Div. Ex. 148; Div. Ex. 262-A; Div. Ex 746 at 98-99. Poulson introduced Berlovan to the crowd, as a member of his "power team," and she briefly spoke. Tr. 518, 1071-72, 1233-34; Div. Ex. 262-A; Div. Ex. 824 at 269-71. After speaking, she went to her table, outside the conference room in the vendor area, but did not recall anyone visiting her table or speaking with her during the event. Tr. 1220-21, 1234-35. However, she later reported to Equity Trust that five Equity Trust accounts had been opened at the event and 48 qualified leads had been generated. Tr. 1241-42; Div. Ex. 264 at 6. Kelly gave a presentation on SDIRAs the next day. Tr. 517-18, 610-12, 1218. Poulson Russo recorded the event, including Berlovan's two-minute speech, and sold the recording as a DVD set titled "Acquisition SuperConference 1.0." Tr. 519-20; Div. Ex. 263. Equity Trust's share of DVD sales from the event amounted to $4,819. Div. Ex. 186 at 23.

In 2009, Equity Trust and Poulson discussed sponsoring additional events.[25] Poulson invited Equity Trust, among others, to be a sponsor of a series of "monthly dinner events." Tr. 526; Div. Ex. 160. Equity Trust agreed to pay $600 to be a sponsor, and Poulson included Equity Trust marketing material in the folders that he distributed to the attendees. Tr. 527, 529-31; Div. Ex. 168 at 5. Berlovan invited Poulson to be a sponsor of Equity Trust's "October 2009 Networking Super Conference." Div. Ex. 161. Poulson did not attend Equity Trust's event, but agreed to sponsor one of the breaks for $750. Tr. 521, 527-29; Div. Ex. 163; Div. Ex. 168 at 2-4.

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[24] Berlovan estimated that she opened fewer than ten accounts from his referrals. Tr. 1236. After she left Equity Trust in 2010, Poulson's sales representative was Robert Yurgalewicz. Tr. 536.

[25] Neither attended the other's events. Tr. 529, 1237.

Equity Trust solicited Poulson for a sponsorship in 2010, but he did not purchase a sponsorship. Tr. 537-38; Div. Ex. 243.

3. Poulson Investors

Joseph Angelo Gatto, an engineer, first met Poulson when he joined the South Jersey Investors group in 2008.[26] Tr. 1255-57. Poulson was president of the group, which involved setting up and choosing speakers for periodic meetings. Tr. 1256-58. Gatto, who had recently left government employment, was looking to invest his government retirement assets in assets other than stocks and bonds. Tr. 1259.

Poulson made several presentations to the South Jersey Investors group concerning investing in real estate through an IRA. Tr. 1258. Poulson recommended Equity Trust as custodian and identified Berlovan as a contact. Tr. 1258-59, 1261-62. After hearing his presentation, Gatto invested $115,000 with Poulson through an Equity Trust SDIRA. Tr. 1260-61. Before choosing Equity Trust, Gatto spoke with representatives from two other self-directed IRAs as well as Berlovan. Tr. 1261-62. Berlovan spoke favorably of Poulson. Tr. 1261-62. Gatto had already decided to invest with Poulson. Tr. 1299-1300. However, Berlovan's testimonial influenced him to choose Equity Trust over another custodian. Tr. 1261-62; 1288-89, 1299-1300.

In March 2009, Gatto made three investments totaling $115,000 with Poulson through his Equity Trust SDIRA. Tr. 1260; Div. Ex. 751 at 80-83, 88-91, 126-29; Resp. Ex. 200. Gatto's investment was eventually lost. Tr. 1277. Gatto signed and agreed to the provisions in Equity Trust's custodial agreement and DOI. Tr. 1300-02, 1305-08; Resp. Ex. 200 at 2, 6. When making his initial investment, Gatto sent Berlovan DOI forms, promissory notes, and mortgages for two of his investments. Div. Ex. 751 at 50-75. The promissory notes or mortgages were unsigned by Gatto and Poulson, because he believed that he was prohibited from doing so, and that it was Equity Trust's responsibility to sign on his behalf. Tr. 1267-68; Div. Ex. 751 at 54, 57, 66, 71. In his quarterly account statements, each of Gatto's investments contained a note that Equity Trust was "AWAITING RECEIPT: PROMISSORY NOTE." *E.g.*, Resp. Ex. 200 at 30, 32, 38, 40; Tr. 1326, 1330-33. He called Equity Trust to inquire why his documents were not showing up as having been received, and was told that the documents were likely going through the recording process and had not yet been received back from the county clerk; what he was told was not inconsistent with the responsibility of recording the mortgage being his. Tr. 1273-74, 1341-42.

The DOIs for each of his three investments represented that the underlying promissory note was secured by a second position mortgage on real property. Div. Ex. 751 at 82, 90, 128. Equity Trust sent Gatto letters reminding him that "[i]f your investment is backed by collateral and/or is being recorded, please verify with your investment company or the person responsible for securing your collateral that they have performed accordingly to protect your interest." Resp. Ex. 200 at 11, 20, 29. Gatto admitted that he had not verified with Poulson that his collateral on

[26] Gatto has a bachelor's degree in aerospace engineering from Penn State University and a master's degree in physics from New Mexico Institute of Mining and Technology. Tr. 1256.

any of the properties, in the form of the second mortgage, had been recorded. Tr. 1307-08, 1311-14. Based on his earlier conversation with Equity Trust, he believed that his documents were already in the process of being recorded. Tr. 1273-74, 1343.

Gatto also made three loans to Poulson without the involvement of Equity Trust and without using any assets from his IRA account. Tr. 1321. The first loan was around March 2008, about a year before Gatto invested with Poulson through Equity Trust. Tr. 1323. The two other loans occurred after his investment through Equity Trust in March 2009. Tr. 1323-24.

Glenn Savary has a bachelor's degree in chemistry, and has worked for the New Jersey Department of Environmental Protection for around twenty years. Tr. 1100. He first met Poulson at meetings of the South Jersey Investors group, which he frequently attended. Tr. 1066, 1102. Poulson was president of the South Jersey Investors group and frequently moderated and introduced guests at these meetings. Tr. 1105-06. After Poulson's term as president ended, he split off and created Poulson Russo, and Savary also attended meetings organized by that company. Tr. 1106-07.

In April 2009, Savary attended Poulson Russo's "4 Day Live Interactive Liquidation Extravaganza." Tr. 1069, 1108. He spoke to Berlovan at the event, though only on "very general questions" because at that time, he was not interested in SDIRAs. Tr. 1072. In November 2009, after hearing Poulson's pitch for investments made with "private money," Savary decided to invest $20,000 with Poulson for the purchase of distressed real estate. Tr. 1115-16. This initial transaction did not involve Equity Trust or IRA funds. Tr. 1113, 1115. Savary received a promissory note and mortgage from Poulson. Tr. 1118. Savary did not perform an appraisal or title report on the property securing his investment. Tr. 1120-21. The promissory note was for a six-month period, but when it expired, Savary agreed to extend it, relying on verbal promises from Poulson. Tr. 1119-20. The lack of paperwork did not bother Savary because he trusted Poulson. Tr. 1120.

In early 2010, Savary and his wife decided to invest further with Poulson, rolling over $40,000 from her 401(k) into a SDIRA. Tr. 1073-76, 1121-22. At Poulson's recommendation, they chose Equity Trust to be their custodian. Tr. 1074. Savary only glanced over the disclosures in the DOI that described Equity Trust's limited role. Tr. 1133; Resp. Ex. 214 at 5; *see also* Tr. 1079-80; Div. Ex. 743 at 62. The investment was secured by a second position mortgage on real property, but Savary did not conduct a title search on the property. Tr. 1077-78, 1123, 1130-31; Div. Ex. 743 at 61; Resp. Ex. 214 at 4. In reality, by November of that year, there were five unrecorded mortgages, totaling over $200,000, on the property. Tr. 1098.

A few days after submitting the DOI form, Mrs. Savary received a letter from Equity Trust requesting her to remit the original promissory note and recorded mortgage to Equity Trust within sixty days of receipt of the letter. Tr. 1080; Div. Ex. 743 at 67. Savary thought this was a formality, because they never had the promissory note or recorded mortgage, so he asked Poulson to remit the documents. Tr. 1081-84, 1139-40. In fact, Savary did not see the promissory note or mortgage until months after the DOI form had been submitted. Tr. 1087-88, 1090; Div. Ex. 743 at 44, 48. The letter also noted that "[i]f your investment is backed by collateral and/or is being recorded, please verify with your investment company or the person

responsible for securing your collateral that they have performed accordingly." Div. Ex. 743 at 67; Resp. Ex. 214 at 10. Savary did not specifically speak to Poulson about this, but assumed that he knew "what he had to do." Tr. 1144. There were no further letters from Equity Trust, and Savary assumed the issues had been resolved. Tr. 1142-43.

In the September 30, 2010, quarterly account statement the asset description stated "AWAITING RECEIPT: PROMISSORY NOTE." Div. Ex. 744 at 3. Savary does not recall reading this, and admitted that he probably glanced only at the first page of the account statement. Tr. 1086-87. The March 31, 2011, quarterly statement stated that Equity Trust had received the original promissory note but was still awaiting receipt of the recorded mortgage. Div. Ex. 744 at 11; Tr. 1095-96.

D. Equity Trust's review process

1. Formation of Account Review Policy

The South Dakota Division of Banking conducted examinations of Equity Trust as of June 30, 2007, December 31, 2009, December 31, 2010, and December 31, 2013, and the Reports of Examination are in evidence as Division Exhibits 594, 595, 596, and 597, respectively. Each report stated that Equity Trust was "fundamentally sound. Only moderate weaknesses are present and are well within management's capabilities and willingness to correct. Fiduciary activities are conducted in substantial compliance with laws and regulations. Overall risk management practices are satisfactory relative to the institution's size and complexity. There are no material supervisory concerns." Div. Ex. 594 at 2; Div. Ex. 595 at 3; Div. Ex. 596 at 3; Div. Ex. 597 at 5.[27] Each report also stated "[m]anagement remains satisfactory." Div. Ex. 594 at 2; Div. Ex. 595 at 3; Div. Ex. 596 at 4; Div. Ex. 597 at 6.

The reports also contained recommendations for improvement, and Scott Kelly, who conducted the examinations, testified that Equity Trust's audit and review procedures improved on each examination. Tr. 1157, 1162, 1167. The 2007 report noted that Equity Trust's audit program contained only one employee and recommended that Equity Trust develop a "risk rating assessment to assist in the internal audit function" and "thoroughly evaluate the need for additional staffing within the internal audit program." Div. Ex. 594 at 5. The 2009 report, following the acquisition of Sterling Trust Company, noted that management had added auditing staff since the previous examination but that the current staffing level of three individuals might not be adequate in view of the volume of accounts and risks associated with alternative account holdings. Div. Ex. 595 at 7. The 2010 report noted six full-time internal auditors and seven full-time compliance personnel but stated that the increased staffing level might not be adequate in view of the volume of accounts, the complexities of two operations centers, and the risks associated with accounts holding alternative investments. Div. Ex. 596 at 4. The 2013 report noted that operations and administration had been consolidated in the Ohio location, that the

[27] The third sentence of the quoted language from the latest, December 31, 2013, examination reads: "Activities are conducted in substantial compliance with applicable laws, regulations, and principles." Div. Ex. 597 at 5.

inherent risk of administering alternative assets remained, and encouraged management to assess the adequacy of internal audit and compliance staffing, currently seven full-time internal auditors and six full-time compliance personnel. Div. Ex. 597 at 8.

In 2009, Equity Trust began to create and implement an investment review procedure.[28] Tr. 695-96. The procedure was reduced to writing and approved by the Equity Trust board on May 27, 2010. Div. Ex. 53 at 1. The policy outlined four types of reviews conducted by compliance staff. A primary review was to be conducted for certain investments, such as unsecured notes. Tr. 697; Div. Ex. 53 at 3. An administrative review was to be conducted for certain client investments, such as notes with interest rates over 20 percent or unsecured notes over $50,000. Tr. 696; Div. Ex. 53 at 4. A secondary review was to be conducted as to a particular investment when the number of clients exceeded twenty, or the dollar amount exceeded $1 million, and a tertiary review was to be conducted when those amounts reached 75 investors or $5 million. Tr. 696-97; Div. Ex. 53 at 5-9. Had these audit procedures existed in 2007, they would have highlighted deficiencies with the Poulson accounts; Dea regretted Equity Trust was not organized or equipped to perform this level of audit then. Tr. 724. However, he also stated that the intent of the review process is "not about the detection of fraud," but rather "the management of risk to Equity Trust." Tr. 1581.

During the primary review, if Equity Trust reviewed a promissory note that indicated that it was secured, but did not receive the security instrument, the documents would be sent to the operations team to resolve the deficiency. Tr. 697-99. The operations team would discuss the issues with the customer, and depending on the customer's intent, Equity Trust might release the customer's funds pending receipt of the missing document. Tr. 698-99. In a secondary review, the audit and compliance teams review and compile documents and then draft a summary, which is then presented to the governance, risk and compliance committee (GRC) for review. Tr. 1581-82.

Equity Trust had a special procedure spreadsheet for its internal use, memorializing instructions for dealing with specified clients and investment sponsors or issuers. Tr. 701-02, 704; Div. Ex. 444. As of February 15, 2010, City Capital appeared on the special procedure spreadsheet, with the notation "We accept notes secured by company with the promissory note only. No security agreement is necessary." Tr. 704; Div. Ex. 444 at 4-5.

2. Investigation of Taylor Notes

Equity Trust began its secondary review of City Capital on September 10, 2009; the review was concluded on January 13, 2010, and Taylor was informed on that date that further investments were not administratively feasible. Tr. 1579-88; Resp. Ex. 50 at 1, 3. This was one

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[28] Part of the reason for this was the increase in the size of the company due to the acquisition of Sterling Trust Company. Tr. 695-96. No other SDIRA custodian was performing these types of reviews. Tr. 972. Desich and Dea testified that this initiative was purely voluntary, to better understand the account holdings and the possible financial, legal, or reputational risk to the company. Tr. 725, 973. Whether or not the initiative was partly inspired by the recommendations of the Division of Banking is immaterial to the issues in this proceeding.

of the first secondary reviews that Equity Trust conducted, and Dea was personally involved. Tr. 1580-82. Batt and Marsh knew of the secondary review at the time of the New Birth event. Div. Ex. 344 at 1.

The review uncovered some issues. By late October, Equity Trust's compliance director Sandra Sarudis was concerned that the Taylor notes that were represented in DOIs as being secured were either unsecured or were missing documentation showing that they were actually secured. Div. Ex. 374 at 1. She communicated this to Marsh and Batt. *Id.* Batt then advised Taylor and Dixon that DOIs should indicate that notes are unsecured or, if secured, explain what they are secured by. Div. Ex. 27.

By January 2010, Sarudis and the compliance staff determined that the Taylor notes were unsecured. Div. Ex. 410 at 1; Resp. Ex. 50; Tr. 1583. By January 22, 2010, Equity Trust changed the designation in its system of the "secured" Taylor notes to "unsecured." Div. Ex. 434 at 1 ("The City Capital notes previously entered as secured have been updated to reflect unsecured promissory note."[29]). This change was disclosed to customers in their quarterly account statements (and not otherwise); their affected assets, previously described as "secured" were now described as "unsecured." Tr. 745-46; *see, e.g.*, Div. Ex. 731 at 2, 4, 6 (reflecting this change in Sims's account statements). Unless the customers saw this and called to inquire about it, no further explanation was provided. Tr. 745-46. Sims called Equity Trust to inquire about this change, but was given the runaround. Tr. 1411-12.

During the review, Equity Trust also discovered that numerous Taylor notes had matured but were unpaid. Tr. 1586; Div. Ex. 410; Div. Ex. 519 at 2. In fact, by September 2009, fifteen Taylor notes were in this category. Div. Ex. 40 at 33. Batt and Equity Trust's in-house legal counsel, Tim Khuman, spoke with Taylor as to why investors were not being repaid. Resp. Ex. 50 at 2; Div. Ex. 410; Tr. 1583-84. Equity Trust was told that the notes had either been paid or (the vast majority) extended, to benefit from compound interest. Div. Ex. 410.

Equity Trust's review also involved checking online to see if Taylor or City Capital were subject to litigation or administrative decisions, had been accused of securities violations, or had otherwise been in the news. Resp. Ex. 50 at 1-2. With the exception of one case in Pennsylvania against City Capital and Taylor, from which Taylor was dismissed, researchers found no other mentions to cause them worry. *Id.* at 1-2. In fact, given Taylor's reputation in the marketplace, many of his mentions on LexisNexis were very positive. Tr. 1586. Dea reviewed City Capital's recent audited financial statements contained in its Forms 10-K and found troubling signs, including negative net worth, rapid money loss, insufficient controls, and a going-concern statement. Tr. 756-57, 1585-86.

On December 29, 2009, City Capital was placed on "administrative hold" status. Div. Ex. 519 at 2. The reasons were Equity Trust's concern with the number of matured unpaid

[29] A January 18, 2010, email refers to reclassification of notes "classified as 'Secured by Other.'" Div. Ex. 434 at 1. "Other" was a mistake. As found above, Taylor investors' DOIs for "secured" notes indicated that they were secured by collateral designated as "Company" – City Capital, Resilient, or another Taylor company.

promissory notes and City Capital's poor financial condition as disclosed in its Commission filings. *Id.*; Answer at 5-6; Tr. 773. The hold blocked Equity Trust's system from processing City Capital transactions without a supervisor override. Tr. 1584.

After a GRC meeting on January 19, 2010, City Capital's status was changed from "administrative hold" to "Do Not Process (DNP)." Div. Ex. 519 at 2; Tr. 755. This meant that Equity Trust would no longer accept investments for City Capital. Tr. 763. Taylor was informed of this decision in a phone conversation with Sarudis, Dea, and others in January 2010. Div. Ex. 36 at 96-98; Tr. 1587-88. The reason given to Taylor was that Equity Trust was uncomfortable with the amount of "concentration" or "exposure" it had to City Capital. Div. Ex. 36 at 97-99; Tr. 1587-88. Taylor thought this was a pretext, and he and Wendy Connor perceived an insinuation of wrongdoing at City Capital. Div. Ex. 36 at 98-101. Dea denies having suspected fraud at that time, however. Tr. 1589.

Transactions after City Capital's Placement on the DNP List

Even after the Taylor notes were placed on the DNP list, Equity Trust was still willing to do business with Taylor, as long as the investment was not in *new* City Capital notes. Div. Ex. 418. For instance, Equity Trust considered a proposed investment in Resilient (but emphatically rejected a proposed investment in gambling machines). Div. Exs. 425, 435, 441. Sarudis tentatively advised Taylor that Equity Trust would consider investments in other assets, such as rental properties. Div. Ex. 449.

Equity Trust agreed to allow, on a case-by-case basis, existing City Capital notes to be extended and replaced. Tr. 763-64. The record does not show who made the decision to allow existing notes to be extended and replaced. Tr. 764, 893, 1631. In May 2010, an Equity Trust customer attempted to renew her City Capital note. Div. Ex. 477. Because City Capital was then on the DNP list, Equity Trust declined the transaction and informed the client that "her paperwork was not processed because it was not feasible to do so based on a recent decision." *Id.* Dixon requested that Equity Trust process the renewal, stating that "the last conversation between the CEO of Equity Trust and our CEO ended with, we would be able to do renewals for existing clients but no new client notes could be processed." *Id.* Equity Trust staffers, seemingly unaware of this arrangement, then requested advice from Bartlett. Div. Ex. 480; Tr. 895-96. Bartlett confirmed that a promissory note modification or replacement could be processed. Div. Ex. 479 at 1.

From February 2010 onward, Equity Trust processed eighteen renewals, extensions, or conversions of City Capital notes. Div. Ex. 40 at 33. At the same time, Equity Trust learned of at least two clients who claimed that their City Capital notes had not been paid. In mid-March 2010, Batt received and forwarded to Sarudis a letter from an attorney that had been sent to City Capital, threatening a lawsuit due to unpaid City Capital notes amounting to $216,000. Div. Ex. 461. Similarly, in June 2010, Bartlett was forwarded a letter from an attorney directed to Equity Trust and dated March 26, 2010, concerning his client's funds that were held in unpaid and overdue City Capital notes and requesting that Equity Trust's counsel contact him. Div. Ex. 485.

3. Review of Poulson Notes

Equity Trust began its secondary review of the Poulson notes in June 2010. Div. Ex. 256. By at least November 2010, Equity Trust had discovered issues with at least twenty-five investment accounts. Div. Ex. 209 at 2-3; Div. Ex. 256 at 3-4. The issues included twenty-four accounts missing recorded mortgages, ten accounts missing executed promissory notes, and ten accounts with notes that had already matured but without evidence of payment or extension. Div. Ex. 209 at 2-3.

Poulson was not contacted with specifics regarding the missing documents until November 30, 2010, when Mary Juristy from Equity Trust emailed him a list of the accounts "detailing names and documents we are missing." Div. Ex. 209; Tr. 538-39. Juristy emailed Poulson the list again on December 8, 2010. Div. Ex. 212. Juristy suggested to Poulson that he overnight the documents to her. Div. Ex. 213. Then, on December 30, 2010, Juristy again emailed, requesting the documentation, and Poulson replied that he was "in the process of putting together the paperwork" and that he expected "to send you at least a portion of the paperwork by the middle or end of this upcoming week." Div. Ex. 217 at 1. In reality, Poulson did not have any of the requested documents, and feared that his Ponzi scheme would be uncovered. Tr. 539-40.

On January 17, 2011, Poulson again emailed Juristy, apologizing for failing to send the requested documentation but promising that "the envelope containing your documents [will be] mailed tomorrow." Div. Ex. 224. On February 1, 2011, Juristy informed Poulson that she had received his package. Div. Ex. 226. Poulson replied, informing Juristy that some of the documents had been re-created "from scratch as I had never received certain original signed documents back from" Equity Trust. *Id.* In fact, Poulson had sent Juristy only a portion of the requested documents, "primarily promissory notes and extensions of promissory notes"; "[t]here might have been a couple" of recorded mortgages. Tr. 545. Poulson never heard from Juristy or anyone at Equity Trust regarding these documents again. Tr. 544-45.

Equity Trust processed its last new Poulson customer in May 2011. Div. Ex. 41 at 10, Row 43. Only one customer extended Poulson notes after that date; the customer extended two investments in January 2012. *Id.* at 11-12, Rows 3, 9.[30] In July 2011, Equity Trust conducted a secondary re-review of the Poulson notes. Div. Ex. 256 at 2. Out of thirty-three Poulson investments, twenty-five had "inadequate documentation on file to support investment." *Id.* During the secondary re-review, Juristy noted that Poulson had "13 matured notes, not collected that came due this year" and "numerous missing documents for current investments." Div. Ex. 245 at 1-2. She noted that "I did speak with Randy last year and emailed him the list of missing items, he said he would be glad to provide. But it appears we did not receive anything." *Id.* at 1. As of September 20, 2011, the review recommended that Poulson's investments be placed on hold due to "term violations (13 matured notes as per audit date, not collected. Also missing

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[30] There is no evidence in the record concerning whether or not Equity Trust advised the customer of Poulson's status with Equity Trust. Therefore, in light of the Division's burden of proof, it is found that Equity Trust did not fail to communicate Poulson's status to the customer.

numerous documents for current notes.)" Div. Ex. 256 at 2; Tr. 1591-92. On November 17, 2011, the GRC placed Poulson on hold. Div. Ex. 256 at 2; Tr. 1592-93. Six days later, the U.S. Attorney's Office for the District of New Jersey mailed Equity Trust a grand jury subpoena, requesting information regarding Poulson. Div. Ex. 248. Poulson was placed on the DNP list on October 25, 2012. Div. Ex. 578 at 28.

E. Expert Testimony[31]

William Campbell Ries, a shareholder in the Pittsburgh, Pennsylvania, law firm Tucker Arensberg, P.C., gave evidence for the Division in an expert report.[32] Div. Ex. 39. His practice includes representing both individual and institutional clients, such as banks and other financial institutions, on fiduciary matters. *Id*. at 3. He opined that, under Section 408 of the Internal Revenue Code and South Dakota law, custodians like Equity Trust are considered to be acting in a fiduciary capacity and are subject to certain fiduciary duties. *Id*. at 6-7. He enumerated, without attribution to any law or other source, a number of specific duties, such as ensuring that deeds and mortgages are properly prepared and recorded, and periodically reviewing assets for default. *Id*. at 9-10. He also opined that deficiencies in the Taylor and Poulson documents were red flags that a reasonable custodian should have investigated and that Equity Trust's activities in its business relationships with Taylor and Poulson were inappropriate and outside the activities of a passive custodian. *Id*. at 14-19.

Terry N. Prendergast, a partner in the Sioux Falls, South Dakota, law firm Murphy, Goldammer & Prendergast, LLP, testified for Respondent. Tr. 1516-60; Resp. Exs. 222, 223. His practice mostly involves South Dakota trusts and trust companies, and, since 2010, he has served on the Governor of South Dakota's Task Force on Trust Administration Review and Reform. Resp. Ex. 222 at 1-2. He was accepted as an expert in the duties of a SDIRA custodian under South Dakota law. Tr. 1515-16. Prendergast opined that, unless specifically created by a custodial agreement, SDIRA custodians have no duty under South Dakota law to review or modify any direction from a customer, citing Chapters 55-1B and 55-2 of the South Dakota Codified Laws (SDCL). Resp. Ex. 222 at 14-19. Thus, he opined, Equity Trust had no duty to perform investment or suitability reviews; inquiries; investigations; to obtain documents reflecting an investment, except those provided by the customer; or to notify a customer of matured and unpaid promissory notes. *Id*. at 15. Prendergast argued that Ries cited standards applicable to national banks but ignored the controlling SDCL 55-1B, which differentiates between "full service" trustees with "traditional" fiduciary rules and entities like Equity Trust, with fiduciary duties created only by customer contract. Resp. Ex. 223 at 1-2. He reiterated that under South Dakota law Equity Trust's only duties to its customers were defined by the customer contracts. *Id*. at 2-3.

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[31] To the extent that the expert's evidence does not lead to findings of fact, it will be summarized here and referred to as appropriate in the Conclusions of Law section of this Initial Decision.

[32] Respondent did not cross examine Ries. Tr. 337. Instead, it submitted a rebuttal expert report of Terry N. Prendergast. Resp. Ex. 223; Tr. 1514.

Tom E. Simmons, an assistant professor at the University of South Dakota School of Law, who teaches Trusts and Wills and previously practiced in estate planning and probate, gave evidence for the Division in an expert report.[33] Div. Ex. 836. Simmons opined that, contrary to Prendergast's testimony, SDCL 55-1B did not apply because Equity Trust's custodial agreement does not refer to it and, instead, states that it "is subject to all applicable federal laws and regulations and shall be governed by and construed under the applicable laws of the State of Ohio." *Id.* at 2-3. Also, Simmons opined that Equity Trust violated the terms of the custodial agreement by not acting as a passive custodian, and was therefore not protected by the language of the agreement or SDCL 55-1B. *Id.* at 4-5.

Kurt Carlson, Ph.D., a professor at Georgetown University's McDonough School of Business, testified for Equity Trust. Tr. 1455-504; Resp. Ex. 224. He was accepted as an expert in consumer choice. Tr. 1502. He opined that investors were motivated to invest with Taylor and Poulson due to their "strong brands," that they became aware of Equity Trust after they had begun to favor investing with Taylor or Poulson, and that the presence of Equity Trust negatively affected their willingness to invest because requiring an investor to create an account with a custodian adds to the complexity of the investment. Resp. Ex. 224 at 14-20.

Jennifer Golbeck, Ph.D., a professor in the College of Information Studies at the University of Maryland, testified for Equity Trust concerning the landing page. Tr. 1652-68; Resp. Ex. 248. She reviewed archived pages of City Capital's website and another site associated with Taylor, www.iracashflow.com, and found no reference to Equity Trust. Resp. Ex. 248 at 4-5. However, the City Capital website was archived only once in 2009. Tr. 1660.

III. CONCLUSIONS OF LAW

The OIP charges that Equity Trust was a cause of Taylor's and Poulson's violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act. Respondent states, and the Division does not dispute, that this is the first proceeding that the Division or the Commission has brought against a non-registrant SDIRA custodian. As discussed below, it is concluded that the charges against Equity Trust are unproven.

A. Antifraud Provisions

Sections 17(a)(2) and 17(a)(3) of the Securities Act makes it unlawful "in the offer or sale of" securities, by jurisdictional means, respectively to: obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary to make the statement made not misleading (17(a)(2)); or engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser (17(a)(3)).

Material misrepresentations and omissions violate Securities Act Section 17(a). The standard of materiality is whether or not a reasonable investor or prospective investor would

[33] Respondent did not cross examine Simmons. Tr. 337.

have considered the information important in deciding whether or not to invest. *See Basic Inc. v. Levinson*, 485 U.S. 224, 231-32, 240 (1988); *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976); *SEC v. Steadman*, 967 F.2d 636, 643 (D.C. Cir. 1992).

1. Scienter

Scienter[34] is not required to establish a violation of Section 17(a)(2) or 17(a)(3) of the Securities Act; a showing of negligence is adequate. *See Aaron v. SEC*, 446 U.S. 680, 697 (1980); *SEC v. Steadman*, 967 F.2d at 643 & n.5; *Steadman v. SEC*, 603 F.2d 1126, 1132-34 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981); *Byron G. Borgardt*, Securities Act Release No. 8274, 2003 SEC LEXIS 2048, at *37-38 (Aug. 25, 2003). Negligence is the failure to exercise reasonable care. *IFG Network Secs., Inc.*, Exchange Act Release No. 54127, 2006 SEC LEXIS 1600, at *37 (July 11, 2006).

2. "Causing" Liability

For "causing" liability, three elements must be established: (1) a primary violation; (2) an act or omission by the respondent that was a cause of the violation; and (3) the respondent knew, or should have known, that his conduct would contribute to the violation. *Robert M. Fuller*, Exchange Act Release No. 48406, 2003 SEC LEXIS 2041, at *13-14 (Aug. 25, 2003), *pet. for review denied*, 95 F. App'x 361 (D.C. Cir. 2004). Negligence is sufficient to establish liability for causing a primary violation that does not require scienter. *See KPMG Peat Marwick LLP*, Exchange Act Release No. 43862, 2001 SEC LEXIS 98, at *82 (Jan. 19, 2001), *pet. for review denied*, 289 F.3d 109 (D.C. Cir. 2002).

Equity Trust argues that Taylor's and Poulson's primary violations were criminal mail and wire fraud, which require a mental state of scienter, such that any secondary violation also requires scienter and that Equity Trust did not have scienter. However, Equity Trust was not charged in this proceeding with causing Taylor's and Poulson's mail and wire fraud or with causing violations of Securities Act Section 17(a)(1), which also requires scienter. Rather, Equity Trust was charged with causing their violations of Securities Act Sections 17(a)(2) and 17(a)(3), which do not require scienter. The evidence in this proceeding shows that Taylor and Poulson violated those sections, as discussed below, and, in any event, the Commission has made

[34] Scienter is required to establish violations of Securities Act Section 17(a)(1). *Aaron v. SEC*, 446 U.S. 680, 695-97 (1980). It is "a mental state embracing intent to deceive, manipulate, or defraud." *Aaron*, 446 U.S. at 686 n.5; *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976); *SEC v. Steadman*, 967 F.2d 636, 641 & n.3 (D.C. Cir. 1992). Recklessness can satisfy the scienter requirement. *See SEC v. Steadman*, 967 F.2d at 641-42; *David Disner*, Exchange Act Release No. 38234, 1997 SEC LEXIS 258, at *15 & n.20 (Feb. 4, 1997). Reckless conduct is "conduct which is 'highly unreasonable' and which represents 'an extreme departure from the standards of ordinary care . . . to the extent that the danger was either known to the defendant or so obvious that the defendant must have been aware of it.'" *Rolf v. Blyth, Eastman Dillon & Co., Inc.*, 570 F.2d 38, 47 (2d Cir. 1978) (quoting *Sanders v. John Nuveen & Co.*, 554 F.2d 790, 793 (7th Cir. 1977)).

clear that the same conduct can violate Section 17(a)(1), which does require scienter, and Sections 17(a)(2) and 17(a)(3), which do not. *Anthony Fields, CPA*, Securities Act Release No. 9727, 2015 SEC LEXIS 662, at *35-42 (Feb. 20, 2015).

B. Violations

Respondent argues that the "investments" at issue were not securities and also that it had no duties to the investors beyond administrative functions.

The Taylor and Poulson notes were securities within the meaning of the Securities Act. "[U]nless the context otherwise requires[,]" a security is any "***note***, stock, . . . or, in general, any interest or instrument commonly known as a 'security'[.]" 15 U.S.C. § 77b(a)(1) (emphasis added). A note is presumed to be a security. *Id.*; *Reves v. Ernst & Young*, 494 U.S. 56, 65 (1990). However, the presumption is not irrebutable. *Reves*, 494 U.S. at 65. Thus, to determine whether a note is a security, the four-part "family resemblance" test articulated in *Reves*, 494 U.S. at 63-67, is applied. Under this test the Taylor and Poulson notes were securities. Both fraudsters' claimed purpose was to raise money to finance substantial investments; each one offered his notes to a large number of people in targeted audiences; the purchasers bought the notes in order to earn a profit in the form of interest; and there was an absence of another regulatory scheme that would render the application of the Securities Act unnecessary.

1. Primary Violations

For the purpose of this Initial Decision only, it is concluded that Taylor and Poulson each violated Securities Act Sections 17(a)(2) and 17(a)(3). Specifically, Taylor told investors that their funds would be used to acquire real estate or a specific business, often centered on socially conscious community development or housing, when in fact the primary use of the funds was for marketing expenses, general overhead, payroll, and servicing old debt. These misrepresentations were clearly material and Taylor also engaged in a course of business that operated as a fraud on the purchasers of his notes. His proven misconduct with reference to Equity Trust customers extended until at least November 2009, when Equity Trust processed the customers Taylor recruited at the New Birth event. Taylor's state of mind met or exceeded the negligence standard of those sections. Poulson told investors that their funds would be used to purchase, maintain, and improve specific residential properties. Instead, the funds were commingled with other Equity Capital funds, used to pay Poulson's personal expenses, and used to repay other investors. These misrepresentations were clearly material and Poulson also engaged in a course of business that operated as a fraud on the purchasers of his notes. His proven misconduct with reference to Equity Trust customers extended until at least May 2011 when Equity Trust processed the last new Poulson customer. The schemes might have continued indefinitely had Taylor and Poulson continued to find new investors. Equity Trust's involvement with their investments might also have continued indefinitely absent its reviews of the sponsors and placing holds on new investments.

2. Act or Omission

Respondent argues that its account-opening, investment processing, record-keeping, and marketing activities were unrelated to Taylor's and Poulson's misrepresentations and misuse of funds, and thus, Respondent's conduct did not "cause" their primary violation. To the contrary, Respondent's services to its customers facilitated the receipt and retention of investor funds by the fraudsters, making their frauds successful. This included affirmatively deciding to allow customers to extend and replace notes after Equity Trust had stopped accepting new City Capital investments because of its poor financial condition and non-payment of notes that matured. Had these customers known that Equity Trust had stopped taking new City Capital investments, they might have decided not to extend their notes and possibly taken some action that would mitigate their losses. Further, in the case of Dorio, Batt actually joined in a conference call with Dorio and her then financial adviser to persuade her to switch her funds from that adviser's investment to an investment with Taylor at Equity Trust.

3. Knew or Should Have Known

This element of the charge that Equity Trust caused violations of Securities Act Sections 17(a)(2) and 17(a)(3) is unproven. Taylor appeared to be a legitimate businessman when Equity Trust started processing investments in his companies. Equity Trust eventually became aware that City Capital notes were not being paid on maturity[35] and that its audited financial statements showed a negative net worth with mounting current liabilities consisting mostly of notes payable. It had this knowledge when it allowed investors with existing notes to extend and replace them after it had placed City Capital on the Do Not Process list and had barred new City Capital investments from being custodied at Equity Trust. Yet knowing that City Capital was financially pressed and losing money is not the same as knowing that Taylor was engaged in fraud. Indeed, had Equity Trust complied with all of the duties that the Division argues that a SDIRA custodian should follow, it still would not have had knowledge of Taylor's fraud. At bottom, unless Equity Trust assumed the role of an investigator, it is unclear how it would have known of the fraud.

Poulson also appeared to be a legitimate businessman when Equity Trust started processing investments he sponsored. Eventually Equity Trust became wary as a result of his actions after being asked about missing documents. Poulson stalled on answering Equity Trust's request for information and eventually was only partially responsive, furnishing documents that he "recreate[d] from scratch." Equity Trust placed a hold on Poulson investments in November 2011 after realizing this. It processed its last new Poulson customer in May 2011, two months before it commenced the secondary re-review.[36] Again, had Equity Trust complied with all of the duties that the Division argues that a SDIRA custodian should follow, it still would not have had knowledge of Poulson's fraud. A few days after the hold, the U.S. Attorney's Office for the

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[35] Taylor's explanation in late 2009 that many investors chose to extend their notes to benefit from compound interest was plausible at the time.

[36] Equity Trust processed two extensions for one customer in January 2012, but the circumstances are unclear.

District of New Jersey sent Equity Trust a grand jury subpoena requesting information about Poulson in connection with an investigation relating to violations of several criminal laws. Thus, by the time Equity Trust knew or should have known that its conduct would contribute to a primary violation by Poulson, it had stopped the conduct.

4. Negligence Standard of Care Applicable to "Knew or Should Have Known"

A negligence standard is applied to determine whether the Respondent "knew or should have known" that its acts or omissions "would contribute to [Taylor's or Poulson's] violation." The Division concedes that the standard of care is ultimately reasonable prudence. It states that the Commission has not established a standard of care for IRA custodians. This is literally true since the Commission is not authorized to regulate a custodian such as Equity Trust that is not a broker-dealer or investment adviser or an issuer. The Division propounds a standard of care for SDIRA custodians, based on the testimony of its expert witness, listing a number of specific duties.[37] However, Equity Trust's knowledge of whether its conduct contributed to the

[37] The Division argues that reliance on its expert's opinion is essential to establish the standard of care, citing several cases, which are inapposite, in which defendants were charged with primary violations of the antifraud and other provisions: (1) *Thomas R. Delaney*, Initial Decision Release No. 755, 2015 WL 1223971, at *44 (A.L.J. Mar. 18, 2015) (citing *Vernazza v. SEC*, 327 F.3d 851, 861-62 (9th Cir. 2003), in which the court upheld the exclusion of expert testimony, observing that "expert testimony as to industry practice is relevant to show the standard of care as to a recklessness inquiry" while stating that the standard is ultimately one of "reasonable prudence."). The Division's expert testimony, however, did not address current industry practice but rather aspirational best practices. (2) *United States v. Russo*, 74 F.3d 1383, 1395 (2d Cir. 1996) (rejecting appellants' argument that district court improperly admitted expert testimony, stating that the trial court has broad discretion which will not be disturbed unless its ruling was manifestly erroneous and that in complex cases involving the securities industry, expert testimony may help a jury understand unfamiliar terms and concepts but must not usurp the roles of judge and jury by offering legal conclusions.). To the extent that the Division's experts illuminated unfamiliar terms and concepts, their evidence has been accepted. (3) *SEC v. Badian*, No. 06-cv-2621, 2010 U.S. Dist. LEXIS 123990, at *8-9 (S.D.N.Y. Nov. 19, 2010) (denying a motion for summary judgment, stating that the Commission's allegation that the defendants did not respond to red flags requires "proof through expert testimony. The types of factual situations that constitute red flags . . . are outside of the lay jury's experience and observation. . . . The problematic implications of [defendants'] dual registration are sufficiently technical that the resolution of the SEC's claims in this regard requires special knowledge or skill. A lay jury will not be familiar with the industry-accepted level of scrutiny for dually-registered brokerage professionals with supervisory responsibilities not will it be able to discern, based solely on its ordinary experience, whether [defendants] breached the relevant standard."). The undersigned is not, however, a lay jury unfamiliar with the industry-accepted level of scrutiny for dually-registered brokerage professionals. Although Equity Trust is not a registrant, it could be subject to the duties of an investment adviser if acting as an investment adviser. *See Teicher v. SEC*, 177 F.3d 1016, 1017-19 (D.C. Cir. 1999) (holding that the Commission has authority to sanction investment advisers, whether registered or unregistered); Section 202(11) of the Investment Advisers Act of 1940 (defining "Investment Adviser"). (4) *SEC v. Guenthner*, 395 F. Supp. 2d

fraudsters' violations would not have been advanced if it had complied with all the proposed duties; therefore, any failure to comply cannot show that Equity Trust knew or should have known that its acts or omissions would contribute to Taylor's and Poulson's violations. Further, while the Division's standard of care may be desirable policy and might mitigate many types of harm to customers, it is essentially made up of whole cloth and does not purport to represent or to improve on industry practice or reference industry practice at all. Indeed, the unrebutted evidence shows that no other SDIRA custodian was performing the level of review of customer accounts that Equity Trust pioneered. Additionally, the fact that using the Division's standard would require custodians to charge much higher fees than did Equity Trust, is in itself an indication that Equity Trust was not offering extensive services beyond record-keeping.

The most convincing statement of the Commission's view of standards applicable to IRA custodians such as Equity Trust is found in its September 2011 *Investor Alert: Self-Directed IRAs and the Risk of Fraud*, available at http://www.sec.gov/investor/alerts/sdira.pdf. Although the Investor Alert was issued after the Taylor and Poulson investors made their investments, there is no reason to believe that there were more stringent standards of care applicable before 2011. The Investor Alert states, "Investors should understand that the custodians and trustees of self-directed IRAs may have limited duties to investors, and that the custodians and trustees for these accounts will generally *not* evaluate the quality or legitimacy of an investment and its promoters." *Id*. at 1 (emphasis in original). It notes that the risks of private investment opportunities that custodians of SDIRAs might allow can include the risk of fraud as well as a lack of disclosure and liquidity. *Id*. It summarizes the standard of care applicable to Equity Trust:

> Self-directed IRA custodians are responsible only for holding and administering the assets in a self-directed IRA. Self-directed IRA custodians generally do not evaluate the quality or legitimacy of any investment in the self-directed IRA or its promoters. Furthermore, most custodial agreements between a self-directed IRA custodian and an investor explicitly state that the self-directed IRA custodian has no responsibility for investment performance.

Id. at 2.

This standard is consistent with the North American Securities Administrators Association's December 2014 *Informed Investor Advisory: Third-Party Custodians of Self-Directed IRAs and other Qualified Programs*, available at http://www.nasaa.org/33698/informed-investor-advisory-third-party-custodians-self-directed-iras-qualified-programs/, which states:

835, 847 (D. Neb. 2005) (dismissing fraud charges based on alleged accounting irregularities, stating that whether the defendants "complied with GAAP is a question that requires technical, and specialized knowledge. The standards of conduct . . . is [sic] not within the court's general knowledge and experience.") Such expert testimony, however, is based on Generally Accepted Accounting Principles established by the standards-setting Financial Accounting Standards Board.

> the third-party custodian['s] . . . sole obligation is to track and report to the IRS the contributions to and distributions from the account in order to maintain the tax-deferred status of the IRA. . . . The third-party custodian is merely the keeper of the deposits to and distributions from the account. The third-party custodian bills the investor for its record keeping services. The custodian does NOT hold the investment funds or assets.

5. Additional Arguments Related to Equity Trust's "Acts or Omissions"

The Division makes a number of arguments directed to inculpating Equity Trust in Taylor's and Poulson's wrongdoing that are "acts or omissions" but are not relevant to the "knew or should have known" element of causing. While Equity Trust's actions may have been undesirable and even inconsistent with Equity Trust's representations to its customers, they do not bear on whether Equity Trust knew or should have known of Taylor's or Poulson's violations.

The Division argues that, contrary to representations in its Custodial Agreement and DOI, it was promoting Taylor's and Poulson's investments[38] and for that reason it cannot rely on the provisions in those documents such as the one that warns the customer in bold typeface: **It is not our responsibility to review the prudence, merits, viability, or suitability of any investment directed by you . . . We shall be under no obligation or duty to investigate, analyze, monitor, verify title to, or otherwise evaluate or perform due diligence for any investment directed by you**. Further, the Division argues that, contrary to Equity Trust's representations, it provided customer account information to City Capital; that it engaged in sloppy record keeping, such as accepting "secured by company" Taylor notes without a separate security agreement and then reclassifying them as "unsecured"; and that it disbursed funds to Poulson investments without executed promissory notes or recorded mortgages.

The record shows, however, that it was Taylor who promoted Equity Trust, not *vice versa*. This was illustrated by the facts at the New Birth event and by others who were drawn to invest with Taylor by contact with Taylor.[39] Once Taylor selected Equity Trust as his preferred SDIRA custodian, it did not constitute promotion for Equity Trust to provide City Capital with copies of his forms to open accounts and fund investments and to advise City Capital personnel

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[38] The Division also argues that Equity Trust was promoting SDIRAs as a desirable investment vehicle and that this was inconsistent with its representations in the custodial agreement and elsewhere that it was a passive custodian that did not recommend any investment. This was not inconsistent – the whole point of SDIRAs was that the investor would make his own investment decisions. Whether or not SDIRAs should be legal or are wise investment vehicles, they are legal, and Equity Trust's promotion of its own business model was not inconsistent with its representations that it is a passive custodian.

[39] The allegation in the OIP, at ¶ II.4., that "Equity Trust knew that Taylor made false statements about Equity Trust to an audience of thousands" is an exaggerated reference to Taylor's pointing out Batt in the audience and referring to him as his "personal banker."

on how to fill them out for efficient processing. Nor was the landing page more than a convenience for persons who decided to invest with Taylor. Nonetheless, Batt's efforts to intervene with Dorio and her financial advisor, who he perceived to be a roadblock to transferring the Dorio/Wallace funds to Equity Trust for investment with Taylor, went beyond administrative assistance to facilitate a transfer from one custodian to another and constituted a recommendation to invest.[40]

The record also shows that Poulson promoted Equity Trust, not *vice versa*. This is underscored by the fact that Gatto and Savary invested with Poulson before their SDIRA investments through Equity Trust. Indeed, Gatto had sufficient confidence in Poulson that he invested non-IRA funds with him after his investment through Equity Trust.

Equity Trust's providing customer account balances to City Capital was inconsistent with its written representations to the customers (although consistent with its unwritten internal policy to require PINs before sharing account balances and with its written policy to provide nonpublic information to facilitate service authorized by the customer). However, all the Taylor witnesses opened their Equity Trust accounts for the specific purpose of investing with Taylor, and most actually provided their account opening applications, which included not only PINs, but also Social Security numbers, dates of birth, and other personal information, and DOIs to City Capital to file with Equity Trust rather than sending them directly to Equity Trust. Thus they had provided their PINs to City Capital along with their other information. In any event, providing customer account balances to City Capital was not evidence that Equity Trust knew or should have known that its conduct would contribute to Taylor's violation.

The Division cites two cases in support of its argument that Equity Trust's alleged promotional activity vitiates each customer's Custodial Agreement such that the reiterated warnings that the account holder was solely responsible for investment decisions and that Equity Trust was a passive custodian, was not a fiduciary, and had no duties or responsibilities with respect to selecting or monitoring the investments were inapplicable. *Mid-Ohio Sec. Corp. v. Estate of Burns*, 790 F. Supp. 2d 1263 (D. Nev. 2011); and *Bentley v. Equity Trust Co.*, 2015 Ohio App. LEXIS 4613 (Oh. Ct. App. Nov. 16, 2015). In the *Burns* case, the court, noting that the court's review of an arbitration award is highly deferential, declined to vacate a FINRA arbitration award, which Mid-Ohio challenged on grounds that the claimant, the beneficiary of a SDIRA, lacked standing and that the arbitration panel misapplied a FINRA time limit rule. *Mid-Ohio Sec. Corp.*, 790 F. Supp. 2d at 1271-72. This ruling on procedural grounds does not support the Division's position. In the *Bentley* case, the court ruled that the trial court erred when it granted summary judgment in favor of Equity Trust in a suit brought by a group of Equity Trust clients who had been defrauded by Robert Langguth on the basis that they were barred from bringing a common law tort claim by the provisions in the custodial agreement.

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[40] Batt's efforts to persuade Dorio to invest with Taylor and to disregard Wheeler's advice potentially fall within the definition of "investment adviser" contained in Section 202(11) of the Advisers Act: "any person who, for compensation, engages in the business of advising others, . . . as to the advisability of investing in, purchasing, or selling securities." Neither Batt nor Equity Trust has been charged with violating the Advisers Act, however.

Bentley, 2015 Ohio App. LEXIS 4613, at *8-10. Again, whether or not Equity Trust's representations to customers that it is a passive custodian and that they are solely responsible for investment decisions can shield it from liability to those customers because of sloppy record keeping, putative promotion of investments, or provision of PINs to an investment sponsor, is not relevant to whether Equity Trust is liable for a secondary violation in an enforcement charge.

The record shows that Equity Trust notified Poulson investors of missing documentation, which was the customers' obligation to furnish. Thus the fact of missing documentation in itself did not indicate that Equity Trust knew or should have known that its conduct would contribute to Poulson's fraud. However, it processed the last new Poulson investment shortly after it received Poulson's replies, which proved to be defective, to its questions to him concerning missing documents and before it commenced a secondary re-review as a result of which a hold was placed on new Poulson investments.[41] Shortly after the hold, it received a subpoena in a criminal investigation of Poulson, clearly a red flag. Thus, even if Equity Trust suspected Poulson of fraud, rather than merely of promoting a business that sustained losses, by the time Equity Trust knew or should have known that its conduct might be a cause of Poulson's violation it had stopped processing new investments.

IV. ULTIMATE CONCLUSIONS

It is concluded that Equity Trust was not a cause of Ephren Taylor's or Randy Poulson's violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act. Thus, this proceeding will be dismissed.

V. RECORD CERTIFICATION

Pursuant to Rule 351(b) of the Commission's Rules of Practice, 17 C.F.R. § 201.351(b), it is certified that the record includes the items set forth in the corrected record index issued by the Secretary of the Commission on June 20, 2016.[42]

VI. ORDER

IT IS ORDERED that this administrative proceeding IS DISMISSED.

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[41] The Division points out that Equity Trust did not place Poulson on the DNP list until October 2012. However, he was placed on hold in November 2011, which prevented processing investments without a supervisor override, and, in fact, the last new investment had been processed months earlier.

[42] The corrected record index implements changes ordered on June 15, 2016. *See Equity Trust Co.*, Admin. Proc. Rulings Release No. 3922, 2016 SEC LEXIS 2125 (A.L.J. June 15, 2016). Additionally, as requested by the Division and with the consent of Respondent, Division Exhibits 862 and 863, consisting of the final judgments entered against Poulson and Taylor, respectively, are admitted into evidence.

This Initial Decision shall become effective in accordance with and subject to the provisions of Rule 360 of the Commission's Rules of Practice, 17 C.F.R. § 201.360. Pursuant to that Rule, a party may file a petition for review of this Initial Decision within twenty-one days after service of the Initial Decision. A party may also file a motion to correct a manifest error of fact within ten days of the Initial Decision, pursuant to Rule 111 of the Commission's Rules of Practice, 17 C.F.R. § 201.111. If a motion to correct a manifest error of fact is filed by a party, then a party shall have twenty-one days to file a petition for review from the date of the undersigned's order resolving such motion to correct manifest error of fact. The Initial Decision will not become final until the Commission enters an order of finality. The Commission will enter an order of finality unless a party files a petition for review or motion to correct manifest error of fact or the Commission determines on its own initiative to review the Initial Decision as to a party. If any of these events occur, the Initial Decision shall not become final as to that party.

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Carol Fox Foelak
Administrative Law Judge