

UNITED STATES OF AMERICA  
Before the  
SECURITIES AND EXCHANGE COMMISSION

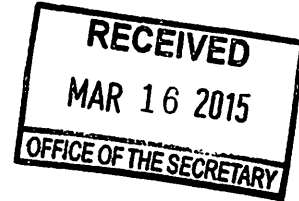
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**ADMINISTRATIVE PROCEEDING**  
**File No. 3-16182**

In the Matter of

PAUL EDWARD "ED" LLOYD, JR., CPA

Respondent.



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**RESPONDENTS PREHEARING BRIEF**

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Respondent.

**RESPONDENT'S PREHEARING BRIEF**

Pursuant to SEC Rule 222 and this court's order, Paul Edward "Ed" Lloyd, Jr., CPA respectfully submits this Prehearing Brief.

**I. NATURE OF THE CASE**

This action is an administrative proceeding brought by the Division of Enforcement. The Order Instituting Proceedings was issued September 30, 2014. The Division alleged violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Sections 206(1), 206(2) and 206(4) of the Investment Advisors Act in connection with three LLC's, Forest Conservation 2011, Forest Conservation, 2012 and Forest Conservation II 2012, all organized for the purpose of making and securing the tax benefit from conservation easement donations. Following an Order on Respondent's Motion for Summary Disposition, the only remaining claims are for violations of Sections 206(1), 206(2) and 106(4) of the Investment Advisors Act for acts related to Forest Conservation 2012. All other claims have been dismissed. The matter is before this court for a hearing under Commission Rules 300-360

## **II. STATEMENT OF FACTS**

### **A. BACKGROUND.**

Paul Edward "Ed" Lloyd, Jr. ("Ed Lloyd" or "Mr. Lloyd") is a certified public accountant. He owns and operates Ed Lloyd & Associates, PLLC where he offers tax planning and preparation services.

Before 2011, Mr. Lloyd learned of the conservation easement tax planning technique at a seminar. He was told he could contact Nancy Zak with The Strategic Financial Alliance, Inc. ("SFA") to obtain a better understanding of the process. After speaking with Ms. Zak, Mr. Lloyd first began to offer the conservation easement to his clients in 2011, and then he did so again in 2012.<sup>1</sup>

Typically, Ms. Zak notified Mr. Lloyd when a conservation easement opportunity became available, and he then explained the process to interested clients. He described the total amount that must be contributed by each participant, his fee for performing the service, and the net tax benefit for each client.

### **B. FOREST CONSERVATION 2012.**

In 2012, a conservation easement opportunity was presented by Piney Cumberland Holdings, LLC ("PCH"). A Summary prepared for PCH, dated October 15, 2012, said that the LLC was offering common units of membership interest in the company at an offering price of \$2,384 per unit. The minimum subscription per participant was 20 common units, requiring a minimum investment of \$47,680. The offering was made for the purpose of acquiring units of ownership interest in Piney

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<sup>1</sup> From 2006 through 2013 legislation allowed a taxpayer a deduction of up to 50% of adjusted gross income for qualified conservation easements. That special provision has now expired and the deduction for a donation of a conservation easement is now limited to 30% of AGI, as with other charitable donations. See *generally* 26 U.S.C. § 170(h).

Cumberland Resources, LLC ("PCR") which had as its principal asset approximately 439.86 acres of unimproved real estate located in Van Buren County, Tennessee, all for the purpose of donating a conservation easement.

Mr. Lloyd created Forest Conservation 2012, LLC, a Wyoming limited liability company, to group his clients' contributions, so that their contribution amount would be in accordance with their tax needs (which might be greater than or less than the unit amount). Additionally, by creating the LLC, each participant was able to secure a deduction for the fee paid to Mr. Lloyd for his services. Forest Conservation 2012, LLC amassed \$543,552.00, net of fees, from a total of 18 members, including Mr. Lloyd who contributed \$16,802.00, cash. Mr. Lloyd wired \$543,552.00 from the Forest Conservation 2012, LLC bank account to PCH on December 7, 2012, and Forest Conservation 2012, LLC purchased 228 units in PCH. PCH then purchased membership interests in PCR, the entity that owned the real estate. PCR donated a conservation easement to a qualifying land trust. Forest Conservation 2012, LLC received a Schedule K-1 for its portion of the contribution easement deduction, and Mr. Lloyd (on behalf of the LLC) issued individual K-1's to all 18 participants indicating their respective percentages of the deduction. (See K-1's of FC 2012 Participants, Respondent's Exhibit 24.) The participants received tax benefits substantially greater than their cash contribution.

The Operating Agreement for Forest Conservation 2012, LLC was prepared by Mr. Lloyd. The initial draft was in March, 2012, before any client contributed, and listed Mr. Lloyd as the sole member. It defined a "member" to be "each person designated as a member of the Company on Schedule I hereto or any other persons admitted as a

member of the Company in accordance with this agreement or the Act.” It was first revised in December, 2012 (Respondent’s Exhibit 15) and the Schedule I then listed the members of the LLC and their respective ownership percentages. Three of the participants in the Forest Conservation 2012, LLC transaction with PCH were not listed on the December 2012 Schedule I: Chris Brown, James Carson, and Mike Malloy, however, all had made actual contributions and were admitted as members by the organizer, Mr. Lloyd. No writing was required to do this. In the spring of 2013 all 18 members, including the omitted three, received K-1’s correctly reflecting their original contribution, and showing the expected tax benefit. (Respondent’s Exhibit 24)

In the summer of 2014, all 18 members of Forest Conservation 2012, LLC signed an amendment to the Operating Agreement, (Respondent’s Exhibit 16), confirming that the December 7, 2012 version of Schedule I attached to the Operating Agreement had a scrivener’s error and, stating the correct membership contributions, fees paid and percentages of ownership, (which match the K-1s), and ratifying all actions of Ed Lloyd.

Of the 18 clients who participated in Forest Conservation 2012, four were Investment Advisory clients: Vernon (Ray) Branch, Timothy Goss, Leslie (Lee) Powell and Larry Price. Their participation was:

Name	Total	Contribution	Fee	Percent	Date	Bates	Exhibit
Branch	\$40,000.00	\$33,500.00	\$6,500.00	6.163164%	11/12/12	ELA_002224	R17
Goss	\$35,000.00	\$29,000.00	\$6,000.00	5.335276%	11/19/12	ELA_002227	R17
Powell	\$60,000.00	\$51,500.00	\$8,500.00	9.474714%	9/25/12	ELA_002234	R17
Price	\$40,000.00	\$33,500.00	\$6,500.00	6.163164%	11/12/12	ELA_002234A	R17



**III. STATEMENT OF QUESTIONS PRESENTED**

- A. Whether there is sufficient evidence of a “device, scheme, or artifice to defraud any client or prospective client” to support a substantive violation of Section 206(1) of the Investment Advisers Act of 1940.
- B. Whether there is sufficient evidence of a “transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client,” or an act, practice, or course of business which is fraudulent, deceptive” to support a substantive violation of Sections 206(2), or (4) of the Investment Advisers Act of 1940.

**IV. ARGUMENT**

**A. THERE IS NO EVIDENCE TO SUPPORT A SUBSTANTIVE VIOLATION OF SECTION 17(A) OF THE SECURITIES ACT OF 1933.**

**The Division’s Claim. Wrong and the facts and wrong on the law.** The Enforcement Division alleges a violation of Section 206 in connection with the Forest Conservation 2012 transaction. The essence of the Enforcement Division’s claim is that because three participants (Carson, Brown, Malloy, none of them Investment Advisory clients) were not listed on a Schedule I in December 2012 due to a scrivener’s error, they did not receive what they paid for: a membership interest and a tax deduction. (Order Instituting Proceeding ¶¶ 46-51). The other members did not receive what they were promised because they should have received larger percentage interests, which were diminished by the percentage interests that the Division alleges were not given to the three members, but which in fact were. In other words, the Division tries to have its cake and eat it too, there was a fraud because the three were given too little, but also

because the three were given their shares so the others were given too little. The Division selectively and incorrectly reads the facts and is flatly wrong as a matter of Wyoming LLC law.

The Enforcement Division argues that Mr. Brown, Mr. Carson, and Mr. Malloy were not members of Forest Conservation 2012, LLC because their names were not listed on Schedule I attached to the Operating Agreement. (See ¶ 50 of Order Instituting Proceedings.) Consequently, the Enforcement Division believes these three participants were not qualified to receive their portion of the conservation easement deduction, and therefore they did not receive what they were promised

**The Truth. Four Satisfied Clients Who Received What They Were Promised.** At the outset, that the three (“A,” “B,” and “C,” referred to in the Order Instituting Proceeding ¶¶ 46-51) (Brown, Carson and Malloy) were not Investment Advisory clients should in and of itself end the Division’s case. Accountants, such as Mr. Lloyd, providing advice incidental to the practice of their profession, 15 U.S.C. § 80b-2(a)(11)(B) are excluded from the definition of “Investment Advisors.” Mr. Lloyd’s potential liability and the Commission’s jurisdiction extend, at most, to his Investment Advisory Clients, none of whom are the “A,” “B,” or “C,” alleged in the Order Instituting Proceeding. On the merits, all have provided affidavits (included in Respondent’s Exhibit 39) declaring that they were told what they would receive, and they in fact received it. So far as the question of Wyoming law, simply put, the enforcement division is wrong. (See Report, Respondents Exhibit 40, and expected Testimony of Tom Long, Esq.)

1. **There is no evidence of a device, scheme, or artifice to defraud or that Mr. Lloyd acted with scienter with respect to the 2012 transaction and thus no support for a violation of § 206(1).**

The Enforcement Division cannot establish a violation of § 206(1) because there is no evidence of a device, scheme, or artifice to defraud the participants, nor of scienter. Section 206(1) of the Investment Advisor's Act provides that is unlawful for any investment adviser "to employ any device, scheme, or artifice to defraud any client or prospective client. 15 U.S.C. § 80b-6(1) (2014). In order to prove a violation of Section 206(1), the SEC must prove scienter, i.e., "an intent to deceive, manipulate, or defraud." *Steadman v. SEC*, 603 F.2d 1126, 1134 (5th Cir. 1979) *aff'd sub nom. Steadman v. SEC*, 450 U.S. 91, 101 S. Ct. 999, 67 L. Ed. 2d 69 (1981).

There are no facts that point to a misrepresentation made by Mr. Lloyd, much less any knowingly false statements. The failure to include the three participants on Schedule I was inadvertent, not intentional, and there is no evidence to the contrary. Thus, there was no purposeful scheme to defraud clients, and there is no evidence of a violation of § 206(1) for the 2012 transaction.

The Operating Agreement for Forest Conservation 2012, LLC defines a "member" as "each person designated as a member of the Company on Schedule I hereto or any other persons admitted as a member of the Company in accordance with this agreement *or the Act*" (emphasis added). The Wyoming Limited Liability Company Act states that "(b) If a limited liability company is to have more than one (1) member . . . those persons become members as agreed by them. The organizer acts on behalf of the persons in forming the company . . . ." Wyo. Stat. Ann. § 17-29-401 (2010)

(emphasis added). Moreover, the operating agreement for the LLC may be oral or implied. Wyo. Stat. Ann. § 17-29-102(xiv) (2010). It is not required to be written.

The failure to include the three participants at issue on Schedule I was simply a clerical error. The bank records clearly show that all of the money from all 18 participants was deposited and then sent to Piney Cumberland Holdings, LLC via wire transfer on December 7, 2012. (See Respondent's Exhibit 19) Each of the participants, (including the three not listed), received a Schedule K-1 (Respondent's Exhibit 12) with their individual share of the contribution easement deduction, and the percentages on the K-1's were correct.

Mr. Lloyd was authorized to act on behalf of all members of the LLC as its organizer and sole member, originally. Theoretically, he could have stated out loud to an empty room that he was admitting the additional 17 participants as members of the LLC and still have fallen within the confines of the Wyoming Limited Liability Company Act. There was no requirement that the Operating Agreement or any amendments thereto be in writing. All persons were made members in full compliance with Wyoming law.

There is no evidence of any intentional deceit or fraud on Mr. Lloyd's part. It is clear that each of the participants in the 2012 PCH transaction received the exact benefit they intended to receive. Had Mr. Lloyd not issued K-1's to them or had Mr. Lloyd's share of the contribution easement been increased by using the money of the three participants at issue for his benefit, then there might be evidence of intent to deceive or defraud. However, neither of these scenarios occurred.

Moreover, even if a writing were required, which it clearly is not, all 18 members of Forest Conservation 2012, LLC signed an amendment to the Operating Agreement indicating that the failure to list the three members on Schedule I was a scrivener's error and ratifying all actions to date. (See Respondent's Exhibit 16) The members have "agreed" that all 18 participants are in fact members of the LLC. Thus, there was no material misrepresentation or omission made by Mr. Lloyd, and there is no evidence in the record to support a finding of scienter. Each of the participants was indeed a member of the LLC and received the exact benefit he or she intended to receive. Therefore, § 206(1) was not violated during the 2012 transaction.

**B. THERE IS NO EVIDENCE TO SUPPORT A SUBSTANTIVE VIOLATION OF SECTIONS 206(2), OR 206(4) OF THE INVESTMENT ADVISERS ACT OF 1940.**

Sections 206((2), and (4) of the Investment Advisers Act of 1940 provide that it is unlawful:

[F]or any investment adviser . . . (2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client . . . (4) to engage in any act, practice, or course of business which is fraudulent, deceptive, or manipulative.

15 U.S.C. § 80b-6 (2014).

Scienter is not required in for a violation of Section 206(2). *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195, 84 S.Ct. 275, 284 (1963). Likewise, scienter is not required for a violation of Section 206(4) *SEC v. Steadman*, 967 F.2d 636, 647 (D.C.Cir.1992).

1. **There is no evidence of any fraud, deceit, or manipulation with respect to the 2012 transaction and thus no support for a violation of Sections 206(2) or (4)**

The Division cannot prove any of the alleged violations of §§ 206(2) and (4) for the 2012 transaction because, simply put, there was no fraud, deceit, or manipulation. for any client, much less an Investment Advisory client. Each member, including the Investment Advisory clients, received their intended tax benefit, and they were entitled to do so because they were members of the LLC, as evidenced by their inclusion by Mr. Lloyd as organizer, and by the amended Operating Agreement.

V. **CONCLUSION**

For the reasons set forth above, the respondent respectfully requests that all remaining claims be dismissed because there is no evidence at all of any fraud, scheme to defraud, or fraudulent or deceptive act or practice, much less of a knowing fraudulent or deceptive act.

This the 9 day of March, 2015.

  
\_\_\_\_\_  
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## CERTIFICATE OF COMPLIANCE

The signature of respondent's attorney below certifies that, in compliance with the requirements of Securities Exchange Commission Rule 154(c), the word count for the Respondents Prehearing Brief filed with the Securities and Exchange Commission on March 9, 2015, contains a total of 2476 words, as reported by the word processing program used to prepare the respondent's brief.

This the 9 day of March, 2015.



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**CERTIFICATE OF SERVICE**

I certify that the **RESPONDENTS PREHEARING BRIEF** was served upon the parties to this action by mailing a copy thereof by first-class, postage pre-paid mail to the following counsel of record:

Honorable Carol Fox Foelak  
Administrative Law Judge  
Securities and Exchange Commission  
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Mr. Brent J. Fields (Via fax and Original &  
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This the 9 day of March, 2015.



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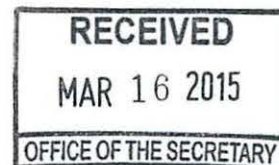
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March 9, 2015



**Sent via facsimile (202) 772-9324 and U.S. Mail**

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**Re: In the Matter of Paul Edward "Ed" Lloyd, Jr., CPA;  
Administrative Proceeding File No. 3-16182; Our File No. 10965**

Dear Mr. Fields:

I enclose an original and three copies of Respondent's Prehearing Brief.

Sincerely yours,

A handwritten signature in black ink, appearing to read "FKS", with a long horizontal line extending to the right.

Frederick K. Sharpless

FKS:drc  
Encls.

cc: Honorable Carol Fox Foelak (via email and US mail)  
Mr. Robert F. Schroeder/Mr. Brian Basinger (via email and US mail)  
Mr. Alex Rue (via email and US mail)  
Mr. Woody Webb (via email and US mail)  
Mr. Ed Lloyd (via email)