UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-16594

In the Matter of

EQUITY TRUST COMPANY,

Respondent.

REPLY BRIEF OF THE DIVISION OF ENFORCEMENT IN RESPONSE TO RESPONDENT'S POST-HEARING BRIEF

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The Division of Enforcement respectfully submits this Reply Brief in response to Respondent's Post-Hearing Brief dated January 28, 2016 ("Resp. Br.").[1]

PRELIMINARY STATEMENT

Equity Trust's primary defense is that the "limited duties" in its customer agreements shield it from any liability. "Limited duties," however, does not mean "no duties." And Equity Trust's undisputed duties include taking custody of documents evidencing its customers' investment intent; refraining from endorsing or promoting investment sponsors; avoiding conflicts of interest; and protecting the privacy of customer account information.

Equity Trust negligently and unreasonably failed to discharge these duties. Equity Trust endorsed Ephren Taylor and Randy Poulson to customers; attended their events; never took custody of crucial documentation; and routinely provided confidential customer information to Taylor and Poulson. Rather than acting for the exclusive benefit of its customers,[2] Equity Trust catered to the issuers and investment sponsors like Taylor and Poulson that generated account openings. On its website and in conferences across the country, Equity Trust aggressively promoted self-directed IRAs as get-rich-quick vehicles, gave shady promoters platforms and legitimacy, and urged investors to place promissory notes into their IRAs, even though it knew of the risk of fraud. This was business as usual for Equity Trust. Taylor and Poulson were

[1]In this Reply Brief, "DE" means Division Exhibit; "RE" means Respondent's Exhibit; and "Div. FOF" and "Div. COL" means the Proposed Findings of Fact and Conclusions of Law of the Division of Enforcement dated January 28, 2018. In addition, the defined terms used in the Div. FOF and Div. COL have the same meanings here.

[2] Section 408(a) of the Internal Revenue Code defines "individual retirement account" as "***a trust*** created or organized in the United States for the ***exclusive benefit of an individual*** or his beneficiaries[.]" 28 U.S.C. § 408(a) (emphasis added). Equity Trust's written trust company policy also required it to "administer accounts solely in the best interests of" account holders. DE 49 at 11.

handled exactly as other investment sponsors were handled, and Equity Trust's employees did what they were trained to do.

Equity Trust argues that its customer agreements provide an ironclad defense, and that its customers only have themselves to blame for making poor investment choices. Equity Trust, however, failed to live up to its part of the bargain. The customer agreements, for example, state that Equity Trust "does not offer investment advice, nor does it endorse any investment, investment product or investment strategy." Equity Trust, however, did offer investment advice and did endorse investment products and strategies. As a result, any protections afforded by the customer agreements do not apply.

Equity Trust also seeks to ratchet up the burden of proof by asserting that the Division must prove that it caused the primary violations intentionally or recklessly, rather than negligently. However, the primary violations alleged in the OIP – Sections 17(a)(2) and (a)(3) of the Securities Act – do not require proof of scienter. Under longstanding precedent, therefore, the Division need only prove that Equity Trust acted negligently. The fact that Taylor and Poulson were also charged with scienter-based violations in other proceedings does not change the basic rule that only negligence is required to cause primary violations that do not require scienter.

Equity Trust further claims that a decision against it would result in "serious disruption to the industry" because it would impose on IRA custodians "burdens that they do not presently have." Resp. Br. at 44. This is nonsense. The applicable standard of care is largely undisputed – Equity Trust did not challenge the Ries Report – and there is nothing about this proceeding that would impose new obligations on the IRA custodial industry. Instead, this case concerns Equity Trust's conduct and whether Equity Trust acted reasonably and consistently with its fundamental

duties. The evidence presented in the Division's Proposed Findings of Fact proves that Equity Trust was a cause of the violations of Sections 17(a)(2) and (a)(3) of the Securities Act. Its acts and omissions contributed to the primary violations, and its conduct was unreasonable and fell far below the undisputed standard of care.

With regard to the requested sanctions, Equity Trust's post-hearing brief does not dispute the need, in the event of a finding of liability, for a cease-and-desist order, the appointment of an independent compliance monitor for three years, or the creation of a Fair Fund.

Equity Trust does, however, dispute the Division's disgorgement and penalty calculations. Equity Trust argues that its disgorgement should be zero because the customer fees it received during the period it negligently administered the Taylor and Poulson accounts are not ill-gotten gains, and because "the Division has presented no evidence on such fees." Resp. Br. at 61. The fees that Equity Trust received from customers during the period of its negligence, however, is an appropriate measure of disgorgement. Equity Trust's customers trusted the custodian with their hard-earned retirement savings, and Equity Trust betrayed its customers with its negligent and unreasonable conduct. And the Division has calculated the total amount of fees paid to Equity Trust in connection with the Taylor/City Capital and Poulson accounts at $180,336.18. This number is based on two sources: Equity Trust's own transaction account records, and the unchallenged fee calculations done by the Division's summary witness, Kerri L. Palen. DE 40 at 7, 24-27 (Palen Decl.); Div. COL ¶¶ 117-120.

Equity Trust also argues that it deserves no penalty. Resp. Br. at 61. Equity Trust's conduct, however, put investor funds at risk and recklessly disregarded regulatory requirements. As a result, although the underlying conduct was negligent, Second Tier or Third Tier penalties may be imposed. Using a per-violation approach, Equity Trust, during the relevant period,

committed twenty-one violations, and under Section 8A(g) of the Securities Act the maximum penalties for First Tier, Second Tier and Third Tier is, respectively, $75,000, $375,000 and $725,000 per violation.

ARGUMENT

Under Section 8A of the Securities Act, Equity Trust is liable if the evidence shows: (1) Taylor, City Capital and Poulson violated Sections 17(a)(2) and (a)(3) of the Securities Act; (2) Equity Trust engaged in an act or omission that contributed to the primary violations; and (3) Equity Trust was negligent and, therefore, should have known that its conduct would contribute to the primary violations.

The first three sections of this Reply Brief address the factual and legal arguments of Equity Trust regarding the three causing elements. The following sections address, in turn: a number of incorrect factual representations in Equity Trust's brief; Equity Trust's arguments against disgorgement and a civil penalty; and, finally, Equity Trust's constitutional arguments.

I. THE PRIMARY VIOLATIONS ARE PROVEN THROUGH SUBSTANTIAL EVIDENCE

A. Taylor and City Capital Violated Sections 17(a)(2) and (a)(3) of the Securities Act

Equity Trust argues that the Division has not met its burden of proving that Taylor, City Capital and Poulson violated Sections 17(a)(2) and (a)(3) of the Securities Act. With regard to Taylor, it argues that although "great financial harm" came to Taylor's investors, and that he "deserve[s] to have been punished," it is "less 'black-and-white'" that Taylor and City Capital violated Sections 17(a)(2) and (a)(3). Resp. Br. at 51. Equity Trust claims that the evidence shows Taylor had "genuine" intentions but was only "waylaid" by "mismanagement and overspending." *Id.* City Capital, moreover, made EDGAR filings and "did not hide the financial

challenges it was facing." *Id.* If there were violations, according to Equity Trust, they occurred "perhaps in mid-2010 or later," after Equity Trust stopped accepting new Taylor investments, and only resulted because "the ship was sinking" and Taylor "began grasping at straws." *Id.*

Equity Trust's unconvincing attempt to rehabilitate Taylor and City Capital flies in the face of overwhelming evidence. Sufficient evidence of the primary violations is contained in Taylor's guilty plea allocution, when he admitted to operating a scheme to defraud investors and to making material misrepresentations and omissions. Div. FOF ¶¶ 105-115; 124-126.

The conduct to which Taylor admitted in pleading guilty to charges of conspiracy to commit wire fraud is sufficient to establish violations of Sections 17(a)(2) and (a)(3). In his testimony in this proceeding, Taylor admitted to this conduct constituting the primary violations. DE 36 (Taylor Dep. at 10:15-24) (confirming the statements made during his plea allocution).

In addition, the Division submitted extensive evidence – unchallenged by Equity Trust – that proves the primary violations. Using investor files, bank records, City Capital financial records and other documents, Kerri L. Palen, a Division accountant, summarized the $5.3 million that Ephren Taylor and City Capital raised from Equity Trust customers from April 2008 through December 2009. DE 40. The Palen Declaration also demonstrates that the vast majority of investor funds were not used on investment related activity, but instead were commingled with other funds and were used primarily to pay City Capital's operating expenses, with a small amount returned to investors. DE 40 at 3-5. This was not consistent with investors' understanding of how their funds would be used. *See e.g.*, Tr. 102:21 & 136:8-15 & 139:2-4 (Jones believed funds would be invested in urban community revitalization); Tr. 185:17-21 (Hill believed funds would be invested in building houses); Tr. 1431:18-1432:4 (Sims believed funds

would be invested in ways that would also help the community); Tr. 804:20-805:1 & 811:9-15 (Dorio believed funds would be invested in certain businesses). This conduct was at least negligent.

Numerous other actions by Taylor and City Capital were at least negligent. For example, Taylor should have known that his statements at New Birth Church in October 2009 about Robert Batt and Equity Trust's role were misleading. Div. FOF ¶¶ 103-104; 144-145; 219-238; Div. COL ¶ 26. In addition, Taylor and City Capital acted unreasonably by representing to investors, including through Equity Trust's DOI forms, that Taylor Notes were secured when in fact they were unsecured. Div. COL ¶ 24; DE 40 at 33 (Palen Decl.). Taylor's and City Capital's primary violations started at least as early as 2008. *See, e.g.*, DE 40 at 3-5 (Palen Decl.: showing misuse of funds starting as early as 2008); Tr. 165-193 (Hill: investment in Taylor Note in June 2008).

Equity Trust points to three witnesses to support its theory that City Capital was merely a "struggling start-up[] with real aspirations of becoming profitable": Raoul Davis, who ran a public relations firm that had Taylor as a client; Linda Keeton-Cardno, an outside consultant who assisted City Capital with its public filings; and Robert Bovarnick, an attorney who represented City Capital in the many customer cases brought against it. Resp. Br. at 51-52. Although Equity Trust asserts that the "Division has not rebutted" their testimony (Resp. Br. at 51), none of these three witnesses support Equity Trust's position.

Davis described the close working relationship between Equity Trust and Taylor. Davis knew from Taylor that Equity Trust was the custodian that Taylor used, and Davis testified that "when [Taylor] was doing presentations at some of the community groups and the churches . . . [h]is PowerPoint would be about traditional investing versus self-directed IRAs." Tr.

1689. Davis also testified that even before New Birth Church, there was "an email here, an email there, people expressing concerns" about Taylor, that Taylor was "getting more arrogant, that he was losing focus on being socially conscious" and did not want his "ministry background" mentioned. Tr. 1694:1-7.

Keeton-Cardno established that City Capital was at all times a house of cards with no revenue and sky-high debt arising from its promissory notes. She testified that City Capital and Taylor were "sustaining themselves by financing activities primarily and debt securities . . . They were basically issuing notes for cash." Tr. 1742:5-9. City Capital, moreover, "never got to what I would consider to be a sustainable, operating model . . . this was a speculative company[.]" Tr. 1725:6-11.

And Bovarnick, City Capital's lawyer, helped establish the string of investor lawsuits filed against Taylor that began in 2006, which undermines Equity Trust's claims that, before 2010, it searched for negative information about Taylor, including investor lawsuits, and found nothing. Tr. 1793:23-1800:10. Bovarnick also had a role in helping City Capital give Dorothy Sims the runaround in 2010 when Sims called to find out about why her note was suddenly marked unsecured. Tr. 1792:10-1793:22 (Bovarnick); Tr. 1447:18-14:50:23 (Sims).

B. Poulson Violated Sections 17(a)(2) and (a)(3) of the Securities Act

After noting that his investors suffered "great financial harm" and that Poulson should be punished "for what he did," Equity Trust portrays Poulson as merely someone "engaged in the business of buying, renting and selling houses." Resp. Br. at 53. On occasion, according to Equity Trust, Poulson would meet with someone "on a one-on-one basis" to discuss a "personal loan" to Poulson to allow him "to buy a property, fix it up, and find a tenant." *Id.* Equity Trust then asserts that "Poulson reasonably believed that his contemplated real estate transaction[s]

would be successful," however, due to "the 2008 real estate and financial market crisis," when Poulson's tenants could not keep up with the rent, Poulson began "facing increasing financial strain" and sought to extend the terms of the notes. "To the extent that any of Poulson's conduct constituted securities fraud," says Equity Trust," it was "at a point in time beyond that relevant for ETC." *Id.* at 54.

Equity Trust's farfetched description of Poulson as a well-meaning real estate developer has no support in the record. Like Taylor, Poulson admitted his illegal conduct during his plea allocution, including that his scheme occurred from July 2006 through November 2011. DE 269 at 2 (indictment); DE 267 at 20 (plea colloquy). In his hearing testimony, Poulson admitted to his conduct constituting the primary violations. Tr. 492:6-494:14 (confirming the statements made during Poulson's plea allocution). Poulson's admissions constitute evidence of his conduct violating Section 17(a)(2) and (a)(3).

The Division also proved the primary violations through additional evidence. Roseann Daniello, a Division accountant, reviewed bank records, investor files and account statements, and summarized the total investments made by Poulson's investors. The Daniello Declaration proves that, from 2008 through 2011, Poulson commingled funds into a single account and used these funds for personal expenses, including vacations, credit card payments, children's tuition, and life insurance premiums. Div. FOF ¶¶ 119; 124-126; DE 41 at 2-3 (Daniello Decl.).

Poulson acted at least negligently by commingling customer funds and using those funds for personal expenses and in other ways not disclosed to investors. Tr. 1117:3-22 (Savary); Tr. 1322:17-23 (Gatto). *See SEC v. Murphy*, 626 F.2d 633, 638 (9th Cir. 1980) (affirming judgment for SEC in offering fraud case; issuer did not disclose that it was "commingling the funds from the various partnerships"); *SEC v. Brooks*, 99 Civ. 1326, 1999 WL 493052, *2 (N.D. Texas

1999) (granting preliminary injunction in offering fraud case because, in part, "defendants commingled funds and used funds for personal expenses").

In addition, Poulson unreasonably issued Poulson Notes without informing investors that there were other unrecorded mortgages associated with those properties, meaning that there was less security for each individual note holder. Div. FOF ¶¶ 120-123. Finally, Poulson unreasonably failed to record mortgages securing the Poulson Notes, which resulted in a worse lien position and served to cover up the scheme. Div. FOF ¶ 123.[3]

C. The Taylor Notes and Poulson Notes Are Securities

In a makeweight argument raised for the first time in its post-hearing brief, Equity Trust asserts that the Taylor and Poulson Notes are not "securities" under the test in *Reves v. Ernst & Young,* 494 U.S. 56 (1990). Resp. Br. at 52-54. This argument is without merit. The Taylor and Poulson Notes are "securities" under *Reves* and Section 2(a)(1) of the Securities Act.

The *Reves* "'family resemblance'" test begins "with a presumption that every note is a security." 494 U.S. at 64. The presumption can be rebutted if the note in question "bears a strong resemblance" to one of several judicially-designated instruments that are not securities.[4]

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[3] In connection with Poulson's fraud, Equity Trust misstates the purpose of the Appraisal Reports (DE 38) of the New Jersey properties submitted (without objection) by the Division. The appraisals were used by the Division's summary witness, Roseann Daniello, to compare the appraised value of five Poulson properties with the value of the properties subject to the multiple recorded and unrecorded mortgages that purportedly secured them. DE 41 at 29 (Daniello Ex. 6). Equity Trust, however, cites to the Appraisal Reports in connection with its statement that "ETC did not independently appraise either Poulson's promissory notes or properties he bought with funds he obtained from the notes." Resp. Br. at 42. This point is irrelevant because the Division does not allege that Equity Trust had a duty to "independently appraise" either the notes or any properties.

[4] "[The] types of notes that are not 'securities' include 'the note delivered in consumer financing, the note secured by a mortgage on a home, the short-term note secured by a lien on a small business or some of its assets, the note evidencing a 'character' loan to a bank customer, short-term notes secured by an assignment of accounts receivable, or a note which simply formalizes an open-account debt incurred in the ordinary course of business . . . . [and] 'notes

Reves, 494 U.S. at 68. The comparison takes into account four factors. First, the motives of the seller and buyer are examined. If the seller's purpose is to raise money for a business enterprise or to finance investments, and the buyer is interested in the profit the note is expected to generate, then the note is likely to be a security. Second, under the "plan of distribution" factor, if the note is "offered and sold to a broad segment of the public" then it is likely a security. The third factor examines "the public's reasonable perceptions," which includes "its character as an 'investment.'" The last factor depends on whether "another regulatory scheme significantly reduces the risk of the instrument, thereby rendering application of the Securities Acts unnecessary." *Id.* at 66-67.

Application of the *Reves* factors leaves little doubt that the Taylor Notes and Poulson Notes are securities. First, Taylor and Poulson intended for the Notes to raise money for their business enterprises or to finance investments. City Capital's ostensible business involved "buying and acquiring real estate and acquiring small businesses" and funding operations "[t]hrough borrowing capital" primarily from "small investors or the general public." DE 36 (Taylor Dep. 23:7-15). Similarly, Poulson's purported business purpose was to raise money to fix up properties and sell them at a profit. Tr. 547:4-550:6 (Poulson). Investors understood that their funds would be invested in business enterprises (in the case of Taylor) and real estate (in the case of Poulson). And clearly the purchasers of the notes – looking to increase their retirement nest eggs – were motivated by the investment profits they hoped the Notes would generate. *See, e.g.*, Tr. 136:8-15 & 139:2-4 (Jones); Tr. 185:17-21 (Hill); Tr. 1431:18-1432:4 (Sims); Tr. 804:20-805:1 & 811:9-15 (Dorio); Tr. 1117:3-22 (Savary); Tr. 1322:17-23 (Gatto).

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evidencing loans by commercial banks for current operations.'" *Reves*, 494 U.S. at 566.

Second, although not traded on an exchange, the Notes were offered and sold to a broad segment of the public. As Taylor stated in his deposition, he traveled around the country pitching the Taylor Notes and solicited "investors via advertising: media, radio, direct mail, seminars, events." DE 36 (Taylor Dep. at 23:16-17). Similarly, Poulson advertised widely and promoted his marketing events, which were opportunities for him to offer and sell Poulson Notes to the public. *See, e.g.*, Div. FOF ¶¶ 150; 152; 157; 327; 511; 530-32. The plan of distribution was more than sufficient for the Notes to be considered securities. *See Deal v. Asset Management Group*, 92 Civ. 187, 1992 WL 212482, at *4 (Aug. 28, 1992) (finding that an offering of notes to six investors evidenced the wide offering of the notes).

Third, the public reasonably viewed the Poulson and Taylor Notes as investments. Both Notes were repeatedly characterized as "investments," and Taylor and Poulson promoted them as investments. The investors viewed the self-directed IRA as an alternative retirement investment option compared with investments like mutual funds. *See, e.g.*, Tr. 172:16-173:7 & 184:12-25 (Hill); Tr. 111:16-112-1 (Jones); Tr. 1428:9-18 (Sims); Tr. 1070:25-1071:10 (Savary); Tr. 1258:9-15 (Gatto); 1259:12-19 (Gatto). *See also George J. Kolar*, SEC Release No. 152, 1999 WL 977373, at *21 (Oct. 28, 1999) (finding notes were securities; investors viewed the notes as an opportunity to earn a profit on their money and regarded the notes as a "stock market substitute"). In addition, Taylor and Poulson repeatedly referred to the noteholders as "investors" and the notes as "investments." *See, e.g.*, DE 36 (Taylor Dep. 23:7-17; 64:11; 308:8-18); Tr. 563:10-13 (Poulson); 565:5 (Poulson).

Equity Trust also viewed the Notes as investments. Most obviously, the instrument by which customers transferred their retirement funds from the custodial account to a Taylor or Poulson account was called a "Direction of ***Investment***" form. Equity Trust also generally

promoted self-directed IRAs as vehicles to hold investments. DE 548 at 21 (*Proven Wealth Building Secrets* book: self-directed IRAs provide "the greatest variety of ***investment*** selection and the greatest amount of ***investment*** control because you make ***investments*** of your own choice") (emphasis added). Even Equity Trust's counsel, in questioning Taylor and Poulson, repeatedly referred to the noteholders as "investors" and the notes as "investments." *See, e.g.*, DE 36 (Taylor Dep. 189:20-23; 190:7-9; 308:17); Tr. 549:14-17; 556:22-25; 557:22-24.

Finally, there are no risk-reducing factors, such as FDIC insurance, to suggest the Notes are not securities. Trying to identify a risk-reducing factor, Equity Trust argues that the Taylor Notes were theoretically secured by one of Taylor's companies, and that the Poulson Notes were supposed to be secured by mortgages. Resp. Br. at 54-55; 21-22; 32; 36-38; 41-42. In fact, however, the Taylor Notes were unsecured, and the mortgages supposedly securing the Poulson Notes were unrecorded and therefore worthless. This phony collateralization does not constitute a risk-reducing factor under *Reves*. *See Mercer v. Jaffe, Snider, Raitt and Heuer, P.C.*, 736 F. Supp. 764, 771 (W.D. Mich. 1990) (finding "first mortgage notes" were securities under *Reves*; "purchasers were in fact unsecured because [they received] fraudulent mortgages to secure their notes").

Accordingly, Equity Trust fails to rebut the presumption that the Taylor and Poulson Notes are securities. *See also Deal,* 1992 WL 212482 at *4 (finding promissory notes secured by liens on a single family residence to be securities); *Pollack v. Laidlaw Holdings, Inc.*, 27 F. 3d 808, 811-15 (2d Cir. 1994) (finding mortgage participation notes to be securities); *SEC v. R.G. Reynolds Enterprises, Inc.*, 952 F.2d 1125, 1131-33 (9th Cir. 1991) (finding promissory notes to be securities even where the notes had a maturity of less than nine months).

The cases cited by Equity Trust do not compel a different result; instead, these cases involve instruments more like the list of non-securities in *Reves* and, therefore, are factually distinguishable. *See Asset Protection Plans, Inc. v. Oppenheimer & Co., Inc.*, 11 Civ. 440, 2011 WL 2533839, at *1-3 (M.D. Fl. June 27, 2011) (loans to athletes were "highly similar" to notes "'delivered in consumer financing'" and therefore not securities under *Reves*); *Bass v. Janney Montgomery Scott, Inc.*, 210 F.3d 577, 583-86 (6th Cir. 2000) (notes were determined to be similar to a commercial bridge loan, with a single buyer and seller); *SEC v. Life Partners, Inc.*, 87 F.3d 536, 548-49 (D.C. Cir. 1996) (applying *Howey* test, viatical contract was not a security).

II. EQUITY TRUST'S ACTS AND OMISSIONS CONTRIBUTED TO THE PRIMARY VIOLATIONS

To satisfy the second causing element, the evidence must show an act or omission by Equity Trust that contributed to the primary violations. Equity Trust asserts that its conduct was "completely unrelated" to the primary violations and that all it did was provide "custodial services in the ordinary course of business." Resp. Br. at 45. The thrust of Equity Trust's argument is to isolate specific conduct of Taylor and Poulson and then to assert that Equity Trust did not cause that particular act. In support, Equity Trust presents lengthy portions of the SEC's complaint against Taylor and the Poulson indictment, which delineate certain conduct, and states that Equity Trust "did not 'cause' any of this specified Taylor [and Poulson] ***conduct***." Resp. Br. at 47-49 (emphasis added).

This argument ignores the words of Section 8A of the Securities Act, the OIP's allegations, and the applicable caselaw. Under Section 8A, causing liability can result if a person "is, was, or would be a cause of the ***violation***," and the act or omission was one that the person knew or should have known "would contribute to such ***violation***." (Emphasis added). Similarly,

the OIP alleges that "Equity Trust was a cause of Taylor's and Poulson's ***violations*** of Sections 17(a)(2) and (a)(3) of the Securities Act." OIP ¶ 62 (emphasis added).

Caselaw confirms that causing may be found if the acts or omissions contributed to the statutory violation, rather than specific conduct. *See, e.g., KPMG Peat Marwick LLP*, Rel. No. 1360, 2001 WL 47245 at *19 (Jan. 19, 2001), *aff'd*, 289 F.3d 109 (D.C. Cir. 2002) (referring to whether a person "is alleged to 'cause' a primary ***violation***...") (emphasis added); *Warren Lammert, et al.*, S.E.C. Rel. No. 348, 2008 WL 1867960, at *17 (Init. Dec. Apr. 28, 2008) (Finality Order: May 28, 2008) (referring to "causing a primary violation").

Equity Trust also overstates the level of proof required to establish that Equity Trust's acts and omissions contributed to the primary violations.[5] Under Equity Trust's reasoning, only proof that Equity Trust actually knew of the illegal conduct would suffice. Causing, however, is designed to apply to those such as Equity Trust that, despite not knowing of the illegal conduct, acted (or failed to act) negligently in a way that contributed to the primary violations. *See KPMG* 2001 WL 47245 at *20 ("causing" liability is "designed to provide a flexible remedy against persons who commit isolated infractions and present less threat to investors than do persons against whom injunctive relief is sought").

Section 8A of the Securities Act requires proof that the act or omission "would contribute to" the primary violation. This means that the Division need not prove that Equity Trust was "the causing factor," "the primary cause" or "the primary proximate cause" of the primary

[5] Equity Trust claims that proof of a "sufficient nexus" is required, citing to *Jeffrey M. Steinberg*, a 2001 Initial Decision that a deadlocked Commission dismissed. Resp. Br. at 46; *Jeffrey Steinberg at al.*, S.E.C. Rel. No. 2272, 2005 WL 1584969 (July 6, 2005) (dismissal). As a result of this dismissal, under Rule 411(f), the *Steinberg* Initial Decision is "of no effect." Equity Trust also notes that a February 2005 Initial Decision, *Public Finance Consultants*, applied the *Steinberg* "sufficient nexus" test. *Id.* at 45. Five months after the *Public Finance* Initial Decision, however, the Commission dismissed *Steinberg*.

violations. *Harrison Securities, Inc.*, S.E.C. Rel. No. 256, 2004 WL 2109230, at *47 (Init. Dec. Sept. 21, 2004) (Finality Order Oct. 29, 2004) (citing Black's Law Dictionary definition of "contributing cause" as "a factor that–though not the primary cause–plays a part in producing a result.'"); Div. COL ¶ 34 (collecting cases).

The level of proof required to show a respondent negligently caused a nonscienter primary violation is below that required to establish aiding-and-abetting. For example, in *Lammert,* a portfolio manager, a fund vice president, and a sales director were alleged to have aided and abetted and caused the primary violations, which concerned undisclosed market timing. 2008 WL 1867960. The Court found that "[n]o respondent acted with knowledge" and therefore rejected the aiding-and-abetting claim. *Id.* at *19. However, the Court found sufficient acts and omissions by all three respondents to satisfy the causing element. With regard to the sales director, the Court found the connection between his actions and the primary violations to be "more tenuous" because he had "limited control" over the trading; nevertheless, the Court found the acts and omissions requirement satisfied.[6] *Id.* at *24.

In any event, Equity Trust's conduct far exceeded the minimum requirements for causing a violation, whether the requirement is phrased as "sufficient nexus," "nexus," or "contributing factor." There were numerous acts and omissions by Equity Trust that contributed to the violations. Div. COL ¶¶ 34-74.

Equity Trust's legal argument on the causation element rests primarily on *Public Finance Consultants*, S.E.C. Rel. No. 274, 2005 WL 464865 (Init. Dec. Feb. 25, 2005). In *Public Finance*, a municipal issuer violated Sections 17(a)(2) and (a)(3) of the Securities Act through material misrepresentations and omissions. The issuer's financial advisor was alleged to have

[6] The Court ultimately found that although the sales director "contributed to" the primary violations through his acts or omissions, he "did not act negligently." 2008 WL 1867960, at *24.

caused these primary violations because he reviewed the offering documents but failed to identify the material omissions. Finding that the financial adviser had "no duty to speak on disclosure issues," the Court found that there was not proof of a "a sufficient nexus" between the financial adviser's silence and the issuer's violations. 2005 WL 464865 at *55.

Public Finance is distinguishable on the facts and its legal reasoning also does not apply to Equity Trust's argument. First, *Public Finance* has nothing to do with the duties of a custodian. Second, the Court's finding that the financial adviser had no duty to disclose to the issuer had nothing to do with a financial adviser's duty of care. Instead, "limiting language" in the offering documents, which was negotiated between the adviser and the issuer, did not require the adviser to offer legal advice on the disclosures. This language was treated "just like any other negotiated term" because the issuer and the adviser had negotiated those terms and they were "entitled to the benefit of the bargain they struck." *Id.* at *53-54.

In contrast, Equity Trust's lawyers drafted the customer agreements in order to protect Equity Trust's interests. The customers had no opportunity to negotiate the terms, which were presented to them on a take-or-leave-it basis. An additional distinguishing factors are that the financial adviser acted within the scope of the "limiting language" in the offering statement, whereas Equity Trust breached the terms of its customer agreements by failing to act passively.

III. EQUITY TRUST WAS NEGLIGENT

Proof of negligence suffices to prove the third causing element. *Daniel Bogar*, Rel. No. 502, 2013 WL 3963608, at *24 (Init. Dec. Aug. 2, 2013) (Finality Order as to Two Respondents Dec. 18, 2013) ("Negligence is sufficient to establish liability for causing a primary violation that does not require scienter."); *Albert Glenn Yesner, CPA*, S.E.C. Rel. No. 184, 2001 WL 587989, *29-30 (Init. Dec. May 22, 2001) (controller's negligent "inaction" in not reporting certain

practices to audit committee was "unreasonable" and therefore a cause of company's violations of Sections 17(a)(2) and (a)(3)).

A. The Ries Report Establishes the Standard of Care

While the standard of care is ultimately one of reasonable prudence, expert opinion on the standard of care for IRA custodians is essential. No single source authoritatively sets forth the standard of care for IRA custodians, and the Commission has not established any such standard of care. In addition, the duties of an IRA custodian are specialized and outside the realm of common knowledge. As a result, evidence in the form of expert testimony is needed to establish the standard of care. *See Thomas R. Delaney*, Rel. No. 755, 2015 WL 1223971, at *44 ("expert testimony as to industry practice is generally relevant in a securities case to show the standard of care"). *See, e.g., United States v. Russo*, 74 F.3d 1383, 1395 (2d Cir. 1996) ("particularly in complex cases involving the securities industry, expert testimony may help a jury understand unfamiliar terms and concepts"); *SEC v. Badian*, 2010 WL 4840063, *3 (S.D.N.Y. Nov. 19, 2010) (expert testimony required because the "implications of dual registration are sufficiently technical that the resolution of the SEC's claims in this regard requires special knowledge or skill"); *SEC v. Guenthner*, 395 F. Supp. 2d 835, 846 (D. Neb. 2005) ("Generally, expert testimony is required to establish the relevant standard of care applicable to a professional."). Equity Trust did not object to the admission of the Ries Report at the hearing, and its post-hearing brief also does not dispute any aspect of the Ries Report.

Here, the proof of Equity Trust's negligence, which dates to at least early 2008 for Taylor and 2007 for Poulson, is largely unrebutted by Equity Trust. *See, e.g.*, Div. COL ¶¶ 75-104 (Taylor and Poulson); Div. FOF ¶¶ 185-191 (October 2008 warning that Taylor as "a crook");

DE 270 (February 2008 email from Taylor to Batt: "Look forward to making some money together."); DE 41 (unrecorded mortgages for Poulson Notes as early as July 2007).

B. The Division is Required to Prove that Equity Trust Acted Negligently, Not with Scienter

Equity Trust argues that the Division must prove that Equity Trust acted intentionally or recklessly, and that the negligence standard is inapplicable. Resp. Br. at 55-56. In the *KPMG* decision, however, the Commission stated: "We hold today that negligence is sufficient to establish 'causing' liability under Exchange Act Section 21C(a), at least in cases in which a person is alleged to 'cause' a primary violation that does not require scienter." *KPMG* 2001 WL 47245 at *20. On appeal, the D.C. Circuit affirmed that "negligence is an appropriate basis" for causing violations that do not require scienter. 289 F.3d at 126. Given that the OIP (¶ 62) alleges that the primary violations are of Sections 17(a)(2) and (a)(3), which do not require scienter, Equity Trust's negligence is sufficient to establish causing liability.

In an attempt to replace the negligence standard with a scienter requirement, Equity Trust incorrectly states that the primary violations alleged in the OIP are scienter-based. Resp. Br. at 45 (claiming that the primary violations are "wire and mail fraud"); 55-56 (the "primary violations here were criminal mail and wire fraud" that are "clearly scienter-based."). The OIP, however, plainly alleges nonscienter primary violations, and Equity Trust cannot pick and choose which primary violations it would like to defend against.

Equity Trust also argues that *KPMG* requires the Division to prove scienter. *KPMG*, however, holds that the determining factor is the violation that the respondent "is alleged" to have caused. *KPMG,* 2001 WL 47245 at *19-20. Equity Trust nevertheless insists that "the primary violations were clearly scienter based," therefore, the Division has a "duty to prove

scienter." Resp. Br. at 55-56. Nothing in *KPMG*, or any other case, supports Equity Trust's view.

Equity Trust incorrectly claims that, in the SEC's District Court action against Taylor and City Capital, the SEC charged only "scienter-based (i.e., reckless or intentional) violations." Resp. Br. at 32. The SEC's complaint, however, charged both scienter and non-scienter violations, including Sections 17(a)(2) and (a)(3) of the Securities Act. DE 5 at 13 (SEC Complaint: "First Claim: Violations of Securities Act Section 17(a)(1), (2), and (3)"). The Final Judgments entered against Taylor and City Capital included injunctions against future violations of Sections 17(a)(2) and (a)(3). DE 6 at 3.

Equity Trust's argument appears to be that, in framing the causing allegation in the OIP, the Division must select a scienter-based primary violation when the respondent has been charged with both scienter and nonscienter violations. This has never been the rule. Simply because Taylor and Poulson were convicted of scienter-based conduct in the criminal actions does not somehow transform the primary violations in this proceeding from nonscienter to scienter. As has been the case for decades, causing allegations are frequently asserted against respondents when the evidence shows scienter and nonscienter primary violations.

In *Daniel Bogar*, for example, the three respondents were associated with the infamous Stanford Ponzi scheme. 2013 WL 3963608. The Division charged the respondents with causing both the scienter (Advisers Act § 206(1)) and nonscienter (Advisers Act § 206(2)) primary violations of the Stanford entities. The Court found that the respondents did not cause the scienter-based Section 206(1) primary violation because "none of them acted with knowledge." 2013 WL 3963608 at *24. With regard to the nonscienter Section 206(2) violation, however, the Court concluded that each respondent "was at least negligent," that the evidence showed "a

failure to exercise reasonable care" and, therefore, each respondent caused the Stanford entities' violations of 206(2). 2013 WL 3963608, at *23-24.

Similarly, in *Albert Glenn Yesner*, the respondent, an auditor, was charged with causing violations of Sections 17(a)(1), (2) and (3) committed by his employer, an electronics company. 2001 WL 587989, at *29. With regard to the Section 17(a)(1) primary violation, the Court required evidence of scienter and, finding none, held that the auditor "did not cause [the company's] primary violations of Section 17(a)(1)." However, "[w]ith respect to the non-scienter primary violations," the Court applied "a negligence standard." *Id.* Under a "reasonableness" standard, the Court determined that the auditor did not act consistently with the "standard of care," and held that the auditor "was a cause of [the company's] primary violation of Sections 17(a)(2) and 17(a)(3) of the Securities Act." 2001 WL 587989, at *29-30.

Finally, that Taylor and Poulson may have acted with scienter is entirely consistent with a finding that they also acted negligently in violating Sections 17(a)(2) and (a)(3). In *Bogar* and *Yesner*, for example, the Court looked to essentially the same conduct in finding that Sections 17(a)(1), (2), and (3) were violated. *See also Anthony Fields, CPA,* S.E.C. Rel. No. 4028, 2015 WL 728005, *10 (Comm'n Feb. 20, 2015) (finding same conduct by respondent supported violations of Sections 17(a)(1) and (a)(3); "We have long recognized that the subsections of Section 17(a) are 'mutually supporting rather than exclusive.'"); *Martin Herer Engelman,* S.E.C. Rel. No. 40, 1993 WL 469125, at *8 (Init. Dec. Nov. 8. 1993) ("Scienter is not an element that must be shown to establish Section 17(a)(2) or (3) violations but when the evidence reflects that a respondent acted with scienter, that showing does not exclude a finding that the proved misconduct also constituted violations of Section 17(a)(2) or (3) of the Securities Act.").

Equity Trust argues that the negligence standard "utterly eviscerates" *KPMG*; that the Division is seeking improperly to "lighten its load"; is an "indefensible and unjust prosecutorial position"; and is "an unreasonable interpretation of precedent." Resp. Br. at 56. This over-the-top and baseless rhetoric merely serves to demonstrate the complete lack of substance to Equity Trust's position.[7] As *Bogar* and *Yesner*, among other decisions, plainly establish, when the primary violation is nonscienter such as Section 17(a)(2) and (a)(3), only negligence is required to prove causing. This holds true even if the primary violator has also committed scienter-based violations.

C. Equity Trust's Duty to Take Custody of Documents Evidencing Its Customers' Investment Intent

Seeking to explain away its negligent failure to fulfill a custodian's most basic responsibility – taking custody of the documentation evidencing its customer's investment – Equity Trust argues that "it would not be reasonable or feasible to expect ETC to chase after the investment documents." Resp. Br. at 8-9. This is a straw-man argument: neither the Ries Report nor the Division has argued that Equity Trust was required to "chase after" documents. Instead, as Equity Trust's own documents and statements show, Equity Trust was required to take possession of the documents evidencing an investment.

The Ries Report states that Equity Trust is "responsible for taking title to the assets of a principal." DE 39 at 9, 11 ¶¶ 23-24, 30. In addition, Equity Trust's DOI form states that the form "must" be accompanied by certain documentation (e.g., a note secured by collateral must include the "*Original Note* clearly stating the associated collateral") (DE 40 at 35), and states

[7] Equity Trust is left to argue that "one of ETC's undersigned counsel was lead counsel for the Division" in the *KPMG* matter fifteen years ago. Resp. Br. at 56; Resp. Pre-Hearing Brief at 24 (same). It goes without saying that the prior employment of an Equity Trust lawyer does not constitute evidence of any kind and is wholly irrelevant.

that Equity Trust's role is "to hold Retirement Account assets." Div. FOF ¶ 42. Equity Trust's marketing material represented that Equity Trust would safeguard account documentation and would not transfer account documentation until all documentation was complete. FOF ¶¶ 50-51. As S. Kelly from the South Dakota Division of Banking testified, as the custodian, Equity Trust "hold[s] the asset so they have to have documentation that the asset exists and it's in their possession." Div. FOF ¶ 36.

By caricaturing the argument as one about "chasing documents," Equity Trust hopes to shift the attention away from the standard of care and its own shortcomings. As the evidence shows, however, Equity Trust systematically failed to collect documentation for Taylor and Poulson. Even after senior Equity Trust officers learned that the documentation was insufficient, Equity Trust continued to process new investments in Taylor and Poulson Notes. Indeed, for Taylor Notes, Equity Trust created a special exception to its policy of seeking security agreements that was undisclosed to customers. Div. FOF ¶ 610.

Equity Trust emphasizes Keith Marsh's testimony that "it's the duty of the customer to supply" account documentation. Resp. Br. at 8. In the very next sentence, however – which Equity Trust does not quote – Marsh testified that "Equity Trust and we would request [documents] over period of time." Tr. 262:3-9.

D. Equity Trust's Arguments About the Role of IRA Custodian

Equity Trust's assortment of legal and factual arguments under the heading "ETC's Role as an SDIRA Custodian," (Resp. Br. at 1-10) aim to shrink the range of Equity Trust's custodial duties to almost nothing while at the same time expanding the scope of the exculpatory clauses in the customer agreements. The evidentiary record, however, shows that Equity Trust repeatedly violated the terms of those agreements and failed to comply with a custodian's duties.

1. Neither Section 408 of the Internal Revenue Code, nor the Cited Federal Court Cases, Support Equity Trust's Position

Equity Trust cites to seven federal court cases, and to Section 408 of the Internal Revenue Code, to support its arguments that "IRA custodians are not fiduciaries." Resp. Br. at 2 (emphasis in original). In fact, however, Equity Trust is a limited-purpose fiduciary. Section 408 ensures that custodians of IRAs do have limited fiduciary duties by requiring that a custodian must be either "a bank" or "such other person who demonstrates to the satisfaction of the Secretary that the manner in which such person will administer the trust will be consistent with the requirements of this section." IRC § 408(a)(2). Equity Trust qualified as a "bank" custodian under Section 408(n)(3) because it is subject to the examination and supervision of a state banking authority (here, South Dakota). As such, Equity Trust is a "public trust company" whose business is defined as "engaging in, or representing or offering to engage in, the business of acting as a ***fiduciary for hire***..." SDCL 51A-6A-1(12A), (13), & (14) (emphasis added); DE 39 at 7, ¶ 18 (Ries Report); Tr. 1160:22-25 (S. Kelly). A "fiduciary for hire" is defined to include a "custodian," like Equity Trust. SDCL 51A-6A-1(7).

A non-bank custodian – such as Mid-Ohio Securities, Equity Trust's predecessor – must also have the ability to act as a fiduciary. In particular, in order to serve as a custodian under Section 408, a non-bank must submit an application to the Secretary to serve as a custodian where it "must demonstrate in detail its ability to act within the accepted rules of ***fiduciary*** conduct." 26 CFR § 1-408-2(e) (emphasis added).

The federal court cases relied upon by Equity Trust, in which customers brought private actions against IRA custodians, are all premised on much different legal theories and far less developed factual records than this proceeding. In particular, in none of these cases were there

allegations that the IRA custodian endorsed a promoter; engaged in joint marketing activities with a promoter; or failed to take custody of customer documentation.[8]

One of the cases Equity Trust cites, *Holtz v. Hilliard*, 1 F. Supp.2d 887 (S.D. Ind. 1988), states that the account holder's "IRA accounts were trusts," and that the IRA custodian "owed limited fiduciary duties in managing the assets in his account." 1 F. Supp.2d at 894.[9]

In another case cited by Equity Trust, *Abbot v. Chemical Trust*, 2001 WL 492388 (D. Kan. Apr. 26, 2001), customers sued an IRA custodian after the investments in their self-directed IRAs turned out to be fraudulent. The Court stated that "to the extent [the IRA custodian] owed a fiduciary duty to [its customers], that duty was limited to executing the transactions requested by [its customers]." *Id.* at 8. Notably, in *Abbot*, the customers admitted that they had no written or oral communications with the custodian concerning the asset. *Id.* at 8-9.

In a sub-section entitled "Congress and the IRS," in which Equity Trust claims that "IRA custodians are not fiduciaries" (Resp. Br. at 2 (emphasis in original)), Equity Trust cites to two cases, *Mandelbaum v. Fiserv, Inc.*, 787 F Supp.2d 1226 (D. Colo. 2011), and *Hines v. Fiserv, Inc.* 2010 WL 1249838 (M.D. Fla. Mar. 25, 2010). In *Mandelbaum*, victims of the Bernard Madoff Ponzi scheme brought contract and tort claims against the IRA custodian that

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[8] The only case to have any such allegation was *Matkin v. Fidelity Nat'l Bank*, 2002 WL 32060182, at *1 (D.S.C. July 11, 2002), where a sales representative for an IRA custodian told a customer that the investment "appeared to be a 'good deal' and that she would invest if she had the money." The court, with regard to the customer's breach of fiduciary duty claim, found that these comments were "insufficient to establish that [the custodian]exceeded its limited role as a custodian of the SDIRA." *Id.* at *4. In contrast, the evidence in this proceeding that Equity Trust exceeded its role as a custodian is far more extensive.

[9] The facts of *Holtz* were far different from this proceeding. In *Holtz*, the sister of a deceased IRA account holder sued the custodian claiming that she was the intended beneficiary. The account holder, however, had left the beneficiary designation blank. 1 F. Supp.2d at 890 ("That blank space is at the heart of this lawsuit."). The Court found that neither the trustee not the custodian had any duties running to the sister and dismissed the case.

administered their Madoff investments. Although Madoff allegedly required the plaintiffs to use Fiserv as their IRA custodian, there was no allegation that Fiserv endorsed or promoted Madoff, or that Fiserv failed to take custody of all documents evidencing the investment. 787 F Supp.2d at 1241-42.

The federal court cases cited by Equity Trust, moreover, are consistent with the Ries Report, which finds that the custodian's duties are determined typically by the terms of the custodian agreement. DE 39 at 8, ¶ 20 (Ries Report). Neither *Mandelbaum* nor *Hines*, moreover, involved custodians that were chartered by South Dakota, and acting as a custodian is considered to be acting in a fiduciary capacity under South Dakota law. *See supra* at 23.[10]

Equity Trust's discussion of the relevant caselaw conveniently omits two decisions in which courts rejected the same arguments it makes in this proceeding. In *Bentley v. Equity Trust*, the Ohio Court of Appeals held that "the Custodial Account Agreements do not preclude [the victims] from bringing their tort claims against Equity Trust." Div. FOF ¶¶ 681-682. And in *Mid-Ohio Securities v. Burns*, a federal district court affirmed a $290,000 customer arbitration award against Mid-Ohio, Equity Trust's predecessor, which alleged that Mid-Ohio failed to act on several red flags. Div. FOF ¶ 683. Equity Trust also makes no mention of the long series of regulatory and enforcement proceedings brought against it and its predecessor, Mid-Ohio. Div. FOF ¶¶ 686-690.

[10] Equity Trust also cites to the Kenneth B. Siegel Declaration (RE 69). Resp. Br. at 3. Siegel is a lawyer who represents RITA, the trade association representing the interests of IRA custodians, and Siegel also represents a number of IRA custodians. As a result of Siegel's inherent bias, his Declaration should be given little weight. In any event, Siegel's declaration and the attached documents pertains to whether IRA custodians have an obligation to conduct independent valuations of assets. This is not alleged in the OIP and has no relevance to this proceeding.

2. The Investor Alerts Do Not Establish a Standard of Care and, in any event, Are Consistent with the Ries Report

Equity Trust argues that in a 2011 release from the SEC's Office of Investor Education and Advocacy – "Investor Alert: Self-Directed IRAs and the Risk of Fraud" – the SEC "acknowledged that SDIRA custodians like ETC do not perform due diligence or an evaluation of the investments that customers chose to put in their SDIRAs." Resp. Br. at 3.

The purpose of this Investor Alert, which was joined by the North American Securities Administrators Association (NASAA), is contained in the first sentence: "to warn investors of the potential risks associated with investing through self-directed Individual Retirement Accounts." RE 46 at 1. A disclaimer on the Investor Alert states that it is intended only as a "service to investors. It is neither a legal interpretation nor a statement of SEC policy." RE 46 at 5.

Given that this Investor Alert draws attention to the same risks that Equity Trust exposed its own customers to, it is surprising that Equity Trust believes that it is somehow exculpatory. Indeed, the Alert reads like it was written with Equity Trust in mind: "State securities regulators have investigated numerous cases where a self-directed IRA was used in an attempt to lend credibility to a fraudulent scheme." This was exactly how Taylor and Poulson used Equity Trust. *See, e.g.*, Div. FOF ¶¶ 133-139 (Taylor promoted his relationship with Equity Trust through the City Capital whitepaper, *Three Simple Steps to Double Your Return on Investment Tax Free*); 140-141(in the press); 142 (used Equity Trust marketing materials to "close" investors); 143 (emphasized City Capital's presence on Equity Trust's website to promote his scheme); 144-145; (made false statements at New Birth Church about Equity Trust to lend credibility to his scheme); and 148-158 (Poulson emphasized Equity Trust to promote and

market his scheme). *See also* Div. FOF ¶¶ 695-698 (collecting fraud cases brought by state regulators in which Equity Trust was used by fraudulent promoters as part of a scheme).

To be sure, the Alert makes certain representations about the duties of IRA custodians, but these representations are expressed in terms of what a custodian "may", "generally" or will "likely" do. And these statements, moreover, are consistent with the standard of care for IRA custodians set forth in the Ries Report. *Compare* RE 46 (Investor Alert: IRA custodians "generally with not evaluate the quality or legitimacy of an investment and its promoters") *with* DE 39 at 8, ¶ 20 (Ries Report: "the custodian does not typically exercise investment discretion over the assets in the custody account and does not usually provide investment advice").

Equity Trust also incorrectly characterizes a 2014 NASAA investor alert as a policy statement "of the state securities regulators that are [NASAA] members." Resp. Br. at 4. In fact, the release is only a statement of NASAA itself, and not of its constituent members. NASAA, moreover, has no enforcement powers. As Anne-Valerie Mirko, NASAA's general counsel, testified, "NASAA is not a regulator." Tr. 1835:24-1836:5.

Mirko, testifying on behalf of NASAA, made clear that the 2014 alert was not intended to express industry standards of care, and does not reflect its members' views of the standard of care owed by self-directed IRA custodians. Tr. 1833:5-16. Instead, it was a general "investor educational tool that draws attention to an issue where investors could be defrauded." Tr. 1825:18-22; 1825:1-8.

Mirko distinguished the 2014 investor alert from NASAA's model rules and policy statements, and testified that industry participants "would look to [NASAA's] model rules and statements of policy ... as adopted at the state level through a rule-making process." Tr.

1825:21-1826:1. The 2014 alert, however, was intended for investors; "[i]ts audience is not industry participants." Tr. 1843:15-18.

3. The Ohio and South Dakota Statutes Do Not Protect Equity Trust

Equity Trust makes two misguided arguments based on South Dakota and Ohio statutes. First, Equity Trust's brief relies on an expert witness, Terry Prendergast, to argue that under South Dakota's statute dealing with "Directed Trusts," S.D.C.L. § 55-1B ("Section 55"), Equity Trust is an "excluded fiduciary" and therefore is "not liable . . . for any loss," "has no duty to perform investment or suitability reviews," and is also relieved "of any duty to communicate with, warn, or apprise any party." Resp. Br. 4-5.

Prendergast's expert opinion on the applicability of Section 55 was discredited in the Rebuttal Report of Tom Simmons, another South Dakota lawyer. Simmons concluded that Section 55 does not apply because Equity Trust is not a "Directed Trust" under South Dakota law. DE 836 (Simmons Report). Scott Kelly from the South Dakota Division of Banking confirmed that Section 55 does not apply because Equity Trust is not a "Directed Trust" under South Dakota law. Tr. 1159:25-1160:17 (S. Kelly). As a result, Prendergast's conclusions, which depend on the applicability of Section 55, should be given no weight.

In addition, as the Simmons Report stated, Section 55 does not apply because Equity Trust's custodial agreement – which Equity Trust insists governs the relationship with its customers – does not refer to or incorporate Section 55. Instead, the custodial agreement provides that it is to be "governed by and construed under the applicable laws of the State of Ohio." *See, e.g.*, DE 696 at 125 (Section 8.15); DE 836 at 3-4 (Simmons Report).

Even if Section 55 did apply, it would not protect Equity Trust from liability, particularly given that it did not conduct itself as a passive custodian. DE 836 at 4-5 (Simmons Report). *See*

also Tr. 1529:21-1545:24 (Prendergast: cross examination showing how reports of Prendergast excluded key language of the South Dakota statute that changed its meaning).

Apparently realizing that Prendergast's Section 55 theory is off the mark, Equity Trust's post-hearing brief unveils a new theory: that Ohio has its own "excluded fiduciary" provision, Ohio Rev. Code § 5815.25 ("Section 5815.25"), that protects Equity Trust from liability. Equity Trust's pre-hearing brief and Answer, however, did not mention Section 5815.25. And Equity Trust's skimpy description of Section 5815.25 – consisting of a single sentence – fails to explain how or why Section 5815.25 applies to this case. Resp. Br. at 4.

Equity Trust claims that Section 5815.25 defines the "duties and standards for custodians" (Resp. Br. at 4); however, the word "custodian" does not appear in Section 5815.25. Equity Trust does not cite to any caselaw or other authority to support its position that Section 5815.25 applies to IRA custodians, and it also does not point to any customer communication where this provision was identified.[11]

Section 5815.25, moreover, states that it applies to any person "acting in a fiduciary capacity for any person, trust, or estate." Ohio Rev. Code § 5815.25(A). Equity Trust, however, claims that "IRA custodians are not fiduciaries." Resp. Br. at 2 (emphasis added). Equity Trust fails to explain how it can enjoy the benefits of a statute aimed at fiduciaries, while at the same time insisting it is not a fiduciary. The same have-it-both-ways problem applies to Equity Trust's Section 55 argument. *See* S.D.C.L. 55-1B (an excluded fiduciary is defined as "any fiduciary excluded from exercising certain powers"); Ohio Rev. Code § 5815.25(A) & (B)

[11] In a cryptic "see also" citation, Equity Trust refers to Section 5815.08(B) of the Ohio Revised Code. Resp. Br. at 5. This provision, entitled "Deposit to personal credit of fiduciary," is irrelevant to this case, and Equity Trust does not explain the citation.

(referring to the excluded fiduciary as an "administrative fiduciary" that could exercise certain administrative powers).

In any event, even if Section 55 or Section 5815.25 apply, neither would protect Equity Trust from liability in this proceeding. Both provisions assume, even under Equity Trust's reading of them, that the custodian acts consistently with the terms of the written agreement and does not endorse or promote issuers. As the evidence shows, Equity Trust failed in both respects; accordingly, any protections in these statutes are not applicable. *See also* DE 836 at 4-5 (Simmons Report).

4. Equity Trust's Customer Agreement And DOI Forms Do Not Immunize It From The Consequences Of Its Negligence

Equity Trust emphasizes the "lawful and appropriate disclaimers of duty" in its customer documents. Resp. Br. at 5. At the hearing, J. Desich claimed that these disclaimers operated as "fail-safe" and that the customers have themselves to blame if they invest in fraudulent schemes and "didn't read the very important legal documents that they signed." Tr. 945:4-12, 947:10-14.

The disclosures figure prominently in Equity Trust's litigation defense, but they were ignored by Equity Trust's sales representatives. The evidence does not show any disclaimer given by Batt or Berlovan in any written or oral interaction they had with customers. Equity Trust emphasizes that each of its customers who purchased a Taylor Note signed a form that included an Equity Trust disclaimer of duty. *See, e.g.*, Resp. Br. at 29. No customer ever testified that anyone from Equity Trust ever explained these forms to them, or what they meant. *See, e.g.*, Tr. 153:21-154:5 (Jones: "No one from Equity Trust was explaining any of this to us"); Tr. 806:8-17 (Dorio: disclosures were hard to read, "pretty fuzzy" and "typical boilerplate contract fine print" and that she did not read them).

The disclaimers are inapplicable because Equity Trust acted beyond the terms of those agreements. Div. COL ¶¶ 105-111. *See* DE 39 at 8, ¶ 22 (Ries Report: "If the custodian takes on duties and responsibilities that are outside the duties and responsibilities set forth in the custody agreement, the custodian is responsible for performing those additional duties in accordance with the standard of care applicable for the services provided. For example, if a custodian choses to provide investment advice, the investment advice provided would be subject to . . . the Investment Advisers Act"). *See also Matkin v. Fidelity Nat'l Bank*, 2002 WL 32060182, at *4 (D.S.C. Aug. 6, 2002) ("A bank-depositor relationship may become a fiduciary relationship if the bank exceeds the scope of the contract and undertakes the responsibility of advising the customer as part of the relationship.").

5. Equity Trust's Arguments That It was Not Negligent Incorrectly Focus on Intent and Knowledge

Equity Trust's argues that its conduct does not "rise to the level of negligence." Resp. Br. at 56. Its arguments, however, primarily relate to Equity Trust's knowledge. For example, Equity Trust claims that it regarded Taylor and Poulson as "respected business people and entrepreneurs"; that it was unaware of customer complaints; that it "lacked a basis to accuse [Taylor] of fraud; and that Equity Trust stopped taking on new City Capital accounts long before the law enforcement actions. Resp. Br. at 56, 58, 51. Equity Trust also argues that it believed Poulson to be a "solid and responsible" person who was "particularly knowledgeable about real estate" and "ran well-attended multi-day educational seminars." *Id.* at 59. When Equity Trust conducted a secondary review, Poulson promised to provide the requested materials. *Id.* at 43. Equity Trust put a hold on Poulson's account in November 2011, and the information it had then "did not support charging Poulson with fraud or other violations." *Id.* at 59. This conduct

regarding Taylor and Poulson, Equity Trust argues, was "plainly not the acts of one seeking to 'cause' a negligence-based securities law violation." *Id.* at 60.

These arguments, even if accepted as true, are beside the point because intent and recklessness are not elements of negligence. There has been many cases, moreover, when a respondent was found to have not acted intentionally or recklessly but was found to have caused primary violations of Sections 17(a)(2) and (a)(3). *See, e.g., Lammert*, 2008 WL 1867960.

Equity Trust, however, did have knowledge of a number of red flags. Edwin Kelly, a top sales representative, J. Desich, and Michael Dea were all aware that in late 2008, a speaker at one of Equity Trust's conferences had called Taylor "a crook." Div. FOF ¶¶ 185-191. Equity Trust also knew about Taylor's numerous misstatements at New Birth Church; that the Taylor Notes were marked as secured on the DOI form when they were not; and that City Capital had failed to pay off numerous Taylor Notes at maturity. DE 40 at 33 (Palen Decl.); Div. FOF ¶¶ 185-191; 219-238; 244-249; 383-386. Equity Trust had knowledge of red flags in connection with Poulson Notes. Equity Trust knew that it had not received any recorded mortgages even though the account documentation reflected that intent.[12] DE 41 at 19 (Daniello Decl.); Div. FOF ¶¶ 349-381.

Equity Trust failed to discharge its duties, and acted unreasonably, in numerous ways, including by failing to take custody of documentation reflecting its customers' investment intent; promoting and endorsing Poulson and Taylor; creating conflicts of interest between itself and its

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[12] Equity Trust also repeatedly states that the Taylor and Poulson accounts were only a small portion of the "130,000" accounts that it administered. Resp. Br. at 58. This is the number of accounts that Equity Trust has currently (Div. FOF ¶ 5), not during the relevant period. In any event, the standard of care is not affected by the number of accounts at an IRA custodian; the same standard applies to large and small IRA custodians. DE 39 at 7, ¶ 16 (Ries Report: "All IRA custodians are governed under IRC Section 408 and are otherwise subject to the same administrative duties as other custodians.").

customers interests; and failing to maintain the privacy of customer account information. Div. COL ¶¶ 75-104.

IV. EQUITY TRUST'S PROPOSED FACTUAL FINDINGS ARE MISLEADING AND UNSUPPORTED BY THE EVIDENCE

A. Witness Testimony Confirms that Equity Trust Endorsed Taylor and Poulson

By reciting its version of victims' testimony, Equity Trust attempts to downplay its endorsement of Taylor and Poulson. Resp. Br. at 16-30 (Taylor); 37-42 (Poulson). Equity Trust's rendition of the facts ignores the reality that Equity Trust not only endorsed Taylor and Poulson time and time again, but in many instances played a critical role in the decision to invest.

For example, Lawrence Hill was not sure whether he should invest with Taylor; at Taylor's urging, Hill called Batt to get comfortable; and Hill only invested after a conversation with Batt where Batt gave him positive information about City Capital. Div. FOF ¶¶ 411-422. Ronald Jones only decided to invest after Batt made "glowing" remarks about Taylor, which remarks "absolutely" had an effect on his decision to invest. Div. FOF ¶¶ 423-443. Anita Dorio decided to invest only after she was on a conference call involving Taylor and Batt that gave her comfort given Equity Trust's role, and only after Batt told her to ignore the advice of her investment adviser who was warning her about investing with City Capital. Div. FOF ¶¶ 393-410. Crystal Turner and Lillian Wells decided to invest based in part on the New Birth Church event where Taylor made false statements about Equity Trust's role to lend himself an air of credibility. Div. FOF ¶¶ 472-488 (Turner); 489-504 (Wells). In addition, Turner's conversation with Batt at that event, where Batt discussed his relationship with Taylor and explained that Equity Trust was an established company that was insured, gave her comfort to invest with Taylor. Div. FOF ¶¶ 472-488. And at that same event, Batt told Wells that she would need to

meet with Taylor if she was interested in self-directed investing, even though she did not express an interest in investing with Taylor. Div. FOF ¶¶ 489-504. Glenn Savary invested with Poulson after he attended Poulson's event where Berlovan was introduced as a member of Poulson's power team. Div. FOF ¶¶ 528-551. And Joseph Gatto invested with Poulson after hearing Berlovan's "glowing recommendation" about Poulson. Div. FOF ¶¶ 505-527.

While the Division need not prove that customers relied on Equity Trust in deciding to invest with Taylor and Poulson, Equity Trust mistakenly suggests in some instances that investors had decided to invest with Taylor and Poulson earlier than was actually the case. For example, Equity Trust argues that Dorio had finally decided to invest with Taylor prior to Batt telling her to ignore her investment adviser's warning about the investment. Resp. Br. 17-20. Equity Trust misconstrues its own investment process. The first time that Dorio (or any other person) indicated intent to invest with City Capital – or was legally obligated in any way – was when the customer submitted the signed the DOI form, which was the purpose of that form, and signed promissory note. *See, e.g.*, Tr. 721:14-722:11 (Dea: describing the DOI form as the document that tells Equity Trust what to do with funds in the Equity Trust account). Until then, the funds could not be transferred to City Capital, and Dorio still had the opportunity to heed her investment adviser's advice and Batt still had the opportunity to persuade her otherwise.

B. Equity Trust Was Not "A Pioneer" in Conducting Account Reviews

Equity Trust's argument that it was "a pioneer in developing reviews" is not supported by the record. Resp. Br. at 9-10. Far from being a pioneer, Equity Trust was slow to adopt policies and procedures and only did to upon the urging of the South Dakota Division of Banking. As Scott Kelly testified, as of June 2007, Equity Trust had only a single employee in its audit program monitoring more than 38,000 accounts valued at $2.4 billion. Tr. 1168:23-1169:14. In

early 2010, Kelly again warned Equity Trust that it "wasn't inputting the maturity dates on the notes," so Kelly recommended that they "put procedures in place to address promissory notes that get past due." Tr. 1171:14-18. At that time, Kelly was "really surprised" that there were more than 8,000 nonperforming promissory notes in its IRA accounts. Tr. 1171:23-1172:24. Despite the warnings, Kelly still "didn't see the audit staff increasing to a size commensurate with the accounts. . . . the Division of Banking didn't feel the internal audit staff grew to a level commensurate with the increase in the accounts." Tr. 1173:18-1174:21. Far from being "a pioneer," Kelly testified that the compliance culture at Equity Trust was "reactionary rather than proactive." Tr. at 1192:20-1193:23. *See also* Div. FOF ¶¶ 52-54; 615-626; 653-655; Div. COL ¶¶ 85-87.

C. Equity Trust Sales and Marketing Representatives Received Inadequate Training

Equity Trust argues that its sales staff, including Batt and Berlovan, received adequate training, and quotes a snippet of Marsh's testimony that the training was "pretty in-depth." Resp. Br. at 11. This reliance is misplaced. Marsh did state that Equity Trust's training for new hires was "in-depth," but he was plainly referring to, for example, training on the types of investments that a customer could put in an IRA, and not the conflicts of interests inherent to its relationship with so-called "centers of influence" such as Taylor and Poulson. Tr. 266:9-18 (Marsh); Div. FOF ¶¶ 556-568. In any event, the training relating to issuer events centered around an effective elevator speech and how to dress and wear makeup appropriately. Div. FOF ¶ 567.

Equity Trust also omits that Batt's "training" as it related to "outside events" came not from any formal training program but from a colleague who was later terminated by Equity Trust for entering into a kickback arrangement with an investment sponsor. Tr. 302:15-303:8 (Batt); DE 518 at 5. The record reflects that the only training on investments sponsors was the simple

statement that Equity Trust could not endorse them, without discussing what acts or statements might constitute endorsement. Div. FOF ¶¶ 556-568.

D. Batt Did Much More than Provide Mere "Updates" to City Capital on Individuals Intending to Invest, and He Never Received PIN Numbers

Equity Trust claims that all Batt did was provide City Capital with innocuous updates on customers "who had recently been referred to ETC by City Capital and who were already in the process of investing in one of the City Capital-related entities." Resp. Br. at 12.

This is not supported by the evidence. Batt's relationship with Taylor and City Capital went far beyond mere "updates," and he treated Taylor and City Capital as the client rather than the customers in whose interests Equity Trust was supposed to act. In numerous emails, Batt provided detailed information on dozens of potential customers to City Capital, and he tracked the progress of the retirement funds from the customer's IRA account to the custodial account. Seeking to ingratiate himself with City Capital, Batt interjected himself into the process in order to expedite the transfers of retirement funds into the custodial account and out to City Capital. Div. FOF ¶¶ 192-194. Taylor was delighted by the speed with which Batt was able to move retirement funds into and out of custodial accounts, which he testified "cut down the processing time tremendously" compared to City Capital's previous custodians. Div. FOF ¶¶ 196-198.

In addition, Equity Trust's claim that Batt "obtained PIN numbers before providing information" to City Capital, also comes solely from Batt's testimony. No evidence exists that any PIN numbers were ever requested or exchanged between City Capital and Equity Trust, and none of the many emails between Batt and City Capital refer to PIN numbers ever being requested or provided. Resp. Br. at 12; Div. FOF ¶¶ 192-195.

E. Equity Trust's Internal, Undisclosed Privacy Policy is Irrelevant Because Its Customers Were Assured that Their Account Information Would be Protected

Equity Trust points to an internal privacy policy, which it admits customers never saw, that "expressly allowed it to communicate appropriate customer information with third parties as part of carrying out the customer's intended transactions." Resp. Br. at 12 (emphasis added). Without citation to anything in the record, Equity Trust also states that "[s]uch a privacy policy was reasonable and designed to help ETC service the investment desires of customers." *Id.*

This internal and undisclosed policy is contradicted by the privacy disclosure statement provided to investors and upon which investors justifiably relied. Div. FOF ¶¶ 69-72; 630-636. The customer privacy disclosure statements were sent on a regular basis to Equity Trust customers, and stated that "Equity Trust Company does not disclose nonpublic personal information about you to any unaffiliated third parties, unless required by law." *See, e.g.*, RE 101-221 (customer files including the privacy disclosure statement sent to customers, with examples for one customer at RE 101 at 9, 38-39; 58-59).

F. No Evidence Exists that Customers Invested with Taylor Due To His "Prominent National Profile"

Equity Trust's arguments that its customers invested with Taylor "based on his prominent national profile" (Resp. Br. at 13) rather than in reliance on Equity Trust role is squarely contradicted by the evidence, and is in any case irrelevant because reliance is not an element of enforcement cases brought by the Division. *SEC v. Goble*, 682 F.3d 934, 943 (11th Cir. 2012) (reliance is not required elements in an SEC action); *see also SEC v. Pirate Investor LLC*, 580 F.3d 233, 239 (4th Cir. 2009) (same).

Equity Trust vastly overstates the influence of Taylor's media appearances on investors, and also minimizes the negative information that was publicly available during the years Equity Trust administered the Taylor notes. Indeed, no investor even recalled having seen the video

clips the Equity Trust put into evidence. *See, e.g.*, RE 27-31. Instead, the investors stated uniformly that they had no prior knowledge of Taylor. Anita Dorio, for example, testified that she had never heard of Taylor before he came to a seminar at her church, and that she had never seen him on television news or talk shows prior to that. Div. FOF ¶ 394. And Lawrence Hill likewise testified that he heard of Taylor for the first time when Taylor was invited to his local church, and that he had never seen Taylor on television. Tr. 167:24-168:16. *See also* Div. FOF ¶¶ 426 (Jones); 474 (Turner); 492 (Wells).

Dorothy Sims, the only witness who had any recollection of seeing Taylor on television, testified to seeing Taylor "on a Christian channel . . . talking about the socially conscious investment programs and self-directed IRAs." Tr. 1399:1-8. Based on this program Sims purchased Taylor's book, *3 Simple Steps to Multiplying Your Retirement Income*, through which Sims learned of Taylor's relationship with Equity Trust. Div. FOF ¶¶ 448-451.

Even Batt was unaware of "any national image that [Taylor] had." Tr. 449:15-21 ("Q. Did Ephren Taylor, to your knowledge, have any other publicity aside from that New York Stock Exchange floor interview? A. That's the only one I saw, was that one. Q. Do you know of any national image that he had? A. No.").

In addition, Equity Trust's assertion that "[m]ajor media outlets uniformly profiled Taylor in a strongly positive and attractive light" (Resp. Br. at 14) is not accurate. Taylor testified in his deposition that negative articles about him began appearing in 2004, beginning with "a Fox News thing about a housing deal we did in Kansas City that didn't go right." DE 36 (Taylor dep. 222:23-227:1) (Taylor describing other negative media coverage and lawsuits). In addition, a 2006 Kansas City Business Journal article reported that Taylor was accused of "swindle[ing]" investors. Div. FOF ¶ 248. Even the 2009 Forbes Magazine online article cited

by Equity Trust notes that, at City Capital, Taylor's "touch has been less than golden. . . For the trailing 12 months ended last September, the company lost $2.9 million on sales of $305,000." Div. FOF ¶ 247; RE 36.

One of the more prescient warnings concerning Taylor appeared on a web site called Ripoff Report in May 2007, the year before Equity Trust began processing Taylor Notes. Michael Dea testified that Ripoff Report was regularly reviewed at Equity Trust. Div. FOF ¶ 245. The May 2007 posting stated that Taylor was "dishonest . . . manipulative and not to be trusted." Div. FOF ¶ 246. A September 2009 posting stated that Taylor was "my personal Bernard Madoff" and "has devastated my family because he has taken my life savings and refuses to make payment." *Id. See also* Div. FOF ¶ 467 (Sims' awareness of Ripoff Report); Tr. 1695:13-23 (Raoul Davis knowledge of negative Ripoff Report regarding Taylor).

Seeking to buttress its argument that Taylor had a spotless reputation, Equity Trust points to Taylor's former public relations manager, Raoul Davis, who booked many of Taylor's media appearances. Resp. Br. at 14. Davis, however, knew nothing about the promissory notes Taylor was peddling and became alarmed when he learned about them. Tr. 1690:13-15 (Davis testified that he "didn't know about the promissory notes until New Birth ... and I became upset with him after I did find out about that."). Davis's concern, which was well founded, was that "the company was in debt . . . [when] you're in debt and you're offering promissory notes so that just did not seem like a good formula to me." Tr. 1690:22-25; 1691:12-16.

G. Equity Trust's Last-Minute Reversal that the Landing Page Never Went Live Is Not Credible

Equity Trust argues that the Division "has not carried its burden of establishing whether [the City Capital] 'landing page' was ever actually made available to the public, and if it was, for what portion of these final four months." Resp. Br. at 22. However, Batt's emails, Taylor's

testimony, and numerous admissions from Equity Trust itself prove that the website was live from at least August 2009 to sometime in 2012 or 2013. Div. FOF ¶¶ 239-243; 673-678.

Equity Trust states that Batt "consistently testified that the landing page never went live." Resp. Br. at 22. Equity Trust, however, fails to account for its own inexplicable flip-flop on this issue, in which after years of representations to the Division that the landing page was live it changed its mind at the end of the hearing. *See* Div. FOF 673-678.

Equity Trust also claims that the landing page "references investing in real estate not promissory notes, let alone, City Capital notes." In fact, "City Capital Corporation – Wealth Builder Network" is the most prominent lettering at the top of the page, which also has links to "Investment Form – Promissory Note," and information on "Purchasing Promissory Note in IRAs." DE 525 at 2; Div. FOF ¶¶ 239-243. Although there are also links to "real estate IRAs," this was consistent with Taylor's marketing pitch that the funds obtained through the promissory notes would be used, in part, to invest in real estate. Div. FOF ¶ 96; Tr. 20:8-16; 61:11-22 (Wells); 1351:9-16 (Turner); Div. FOF ¶ 407; Tr. 884:18-885:9 (Dorio). And the "disclaimer" referred to by Equity Trust was not in the "second substantive paragraph of the landing page," but rather in the smallest font on the bottom of the page. DE 525 at 5.

Finally, Equity Trust claims that an email exchange between Batt and a "senior copywriter" at Equity Trust referring to a "checklist for traditional rollover for the 401k info" suggests that the landing page "was still not finalized" in October 2009. Resp. Br. at 22; DE 360 (email between Batty and copywriter). This email, in which the context is far from clear, proves nothing of the sort. In any event, as Equity Trust's expert witness Dr. Golbeck testified, live websites can be changed, so the fact that the City Capital landing page was updated in October

2009 is not relevant to the question of whether it was live. Tr. 1660:8-17 (Dr. Golbeck testimony that content of live websites can change).

H. Equity Trust Minimizes Batt's Appearance at New Birth Church

Equity Trust argues that Taylor "did not need" Equity Trust "to gain credibility" and that Batt's presence at New Birth Church, and its failure to correct Taylor's false and misleading statements about Batt and Equity Trust, "counted for nothing." Resp. Br. at 24-27. In fact, the investor testimony establishes that Equity Trust's presence was significant to their decision to invest with Taylor.

Ronald Jones, who met with Batt at New Birth, testified that "Mr. Batt, a representative or agent for Equity Trust did endorse Mr. Taylor and City Capital Corp." Div. FOF ¶ 438. Jones also testified that, with regard to Batt's effusive comments about Taylor, that "most people would be very complimentary of anyone they had some sort of mutual relationship with" (Div. FOF ¶ 433). For Jones, Batt's presence "absolutely" had an effect on his decision to make the investment. Div. FOF ¶ 436.

Crystal Turner testified that when Batt was introduced by Taylor that she was impressed that "the bank actually flew [Batt] to Atlanta to be here for the presentation" (Div. FOF ¶ 477), and she believed that "this is legit because you don't often get big established banks sending their people to do business with a black guy in a predominantly black church." Div. FOF ¶ 479.

Taylor also emphasized that Equity Trust's presence at the New Birth Church event constituted an endorsement and was significant to his scheme. Taylor confirmed that "to have a representative from [Equity Trust] in the audience, it wasn't going to get any better than that. That was the – all the little endorsement I needed – to make it happen." Div. FOF ¶ 234.

In a further attempt to minimize its significance to the New Birth Church investors, Equity Trust offers what it purports is "a verbatim transcript of everything Taylor said about Batt and Equity Trust [at New Birth Church]." Resp. Br. at 26. Equity Trust, however, omits two explicit references to Batt and Equity Trust:

> "All right, there's a lot of people in here right now, there's about almost six, 7,000 people. Why couldn't this row get together and say, all right, we're going to go buy a gas station together? Why couldn't this row say, all right, we're going to buy a gas station, too? Or better yet, how come we didn't go buy the oil well? I got one of those, too. I look at things -- invest in things that cause pain. For instance, like with Robert's bank and some of the things, we can actually take that gas station and put it inside of people's retirement account, where it's growing kind of tax free. Interesting isn't it? The same with real estate, you can do the same thing. The same thing with the gas...." RE 66 at 278.
>
> "Matter of fact, Robert has this funny story. He called me one day, we're on the phone, I was like, 'Robert, I got this one client, wants to know can he put pigs inside of his retirement account.' He was like, 'Yeah, we just did that.' I was like, 'Really?' 'Yeah,' he's like, 'all you got to do is tag them with a special blue tag and then we can track them inside the retirement account.'" RE 66 at 280-281.

Batt confirmed in his testimony that he received four phone calls following the New Birth Church event asking about placing pigs or cows in an IRA. Tr. 419:21-420:7. *See also* DE 26 (Oct. 22, 2009 email exchange between Batt and Taylor, Batt: "you are awesome – i have gotten 4 phone calls about IRA buying pigs and cows – thank you thank you..." Taylor: "Ha! We make it rain?" Batt: "From the National Weather Service: Weather Bulletin: - Category 4 Hurricane named 'Ephren' just hit Cleveland OH").

I. Equity Trust Had Ample Opportunity to Correct Taylor's Misstatements Before Processing Customer Investments in the Taylor Notes

Equity Trust's contention that because Batt "did not have a microphone to correct or otherwise respond to Taylor's description" (Resp. Br. at 26-27), that Equity Trust is absolved of its responsibility to correct Taylor's false and misleading statements fails. Batt and Equity Trust

had ample opportunity to correct the misstatements prior to processing any customer investments in the Taylor Notes.

Batt did not correct the misstatements when approached by potential investors following the event. Batt testified that when customers and potential customers approached him after the Taylor event about opening accounts, that he did not tell them that Equity Trust was not a bank and that he was not a banker, "because it never came up." Div. FOF ¶ 230. Asked, "[s]o in other words, you were waiting for someone to affirmatively ask, hey, are you a banker, before you would have clarified your role?", Batt agreed, "Yes." Tr. 406:6-9.

Equity Trust also admits that "[o]n returning to his office [following the event], Batt told his supervisor Keith Marsh about Taylor's reference to Batt as a "banker" at the Atlanta church event.... [And] ETC took no further action to correct Taylor's reference to Batt." Resp. Br. at 27.

Indeed, at no point did anyone at Equity Trust tell Batt that he should have made an effort to correct Taylor's characterization (Div. FOF ¶ 233), and Batt was not disciplined. Div. FOF ¶ 236. Instead, Equity Trust's marketing department sought to capitalize on the event with a webinar, and it created a landing page for City Capital on Equity Trust's website that went active in August 2009. Div. FOF ¶ 175 (webinar); 239-243 (landing page). And Equity Trust proceeded to release the IRA savings of customers who were solicited at the New Birth Church event to Taylor, without telling them that Taylor had misrepresented Equity Trust's role.

J. Equity Trust's Negligence in Handling the "Secured" Taylor Notes Was Much More than a Mere "Reclassification" Issue

Equity Trust admits that the Taylor Notes marked as secured were, in fact, unsecured. Equity Trust does not attempt to explain away Equity Trust's director of compliance Sandra Sarudis' statement that she was "very concerned" that the notes were incorrectly marked as

secured. Resp. Br. at 31-32; Div. FOF ¶ 257. *See also* UCC 9-108 (providing that a valid security agreement must reasonably identify the security); *Law of Sec. Trans. Under the UCC* ¶ 2.02[1][a]; [3] (UCC "requires 'reasonable identification' of the collateral"). In 2009, Equity Trust understood those Taylor Notes were actually unsecured and attempted to correct account statements to reflect "unsecured" when those statements had been reporting them as "secured." Div. FOF ¶¶ 255-266 (describing Equity Trust's determination that it "incorrectly" labelled the Taylor Notes as secured, and decision to unilaterally change the designation in customer accounts from "secured" to "unsecured.")

Equity Trust argues that marking the notes as "secured" was simply indicating that City Capital would stand behind the payment obligation. Resp. Br. at 31-32 ("By simultaneously signing the DOI form and the note, the customer saw that the DOI form's description of the note as 'secured' by 'the company' referred simply to the company's promise to pay as reflected in the promissory note."). Taylor and Equity Trust both knew at the time, however, that there was a material difference between a secured note and an unsecured note. Div. FOF ¶ 102.

In addition, the evidence shows the investors knew that having a "secured" note gave them an increased level of protection. Dorio testified that "[i]f someone didn't pay the note, then that would mean that the company is the collateral. I would own the company." Tr. 881 at 4-6. *See also* Tr. 806:3-7 (Dorio: Q. And what's your understanding of what [secured note] means? A. It's an investment that's backed up by something tangible. And in this case, the secured note was backed up by a business.").

Sims testified that she noted that the DOI form stated "secured" at the time it was provided to her (Tr. 1407:13-15), and that it was important to her to have "a secured note as opposed to an unsecured note...[b]ecause a secured note, it protects you against risk, I would

say. I didn't feel there would by any problem in investing and I thought I would get the money back." Tr. 1407:20-1408:3.

When Equity Trust unilaterally changed the designation of her statement from "secured" to "unsecured," Sims testified that she was upset at the change. She contacted Equity Trust to ask why her investment was suddenly "changed from a secured note to an unsecured note," but was told only that she need to check with City Capital. Div. FOF ¶¶ 462-463. Undeniably, Sims believed she owned a secured and collateralized promissory note.

K. Equity Trust Discounts Taylor's Significance as a Batt Client

Equity Trust states that "Taylor was a 'low' source of referrals for Batt." Resp. Br. at 11-12. However, the record reflects that Batt saw Taylor and City Capital as an important referral source. For example, on August 11, 2009, Batt sent Taylor an email that only included a message in the subject line: "THANK YOU FOR MAKING ME #1 LAST MONTH—LETS MAKE MONEY TOGATHER !!!!" DE 23; *See also* Div. FOF ¶¶ 202-206. In addition, Taylor and City Capital referrals represented at least 10% of Batt's commission revenue in 2009. DE 40 at 10-14 (Palen Decl.: reflecting over 60 investments in 2009); Div. FOF ¶¶ 159-161 (describing commissions and salary). In any event, it was clear that all referral sources were important to Equity Trust and sales representatives did their best to foster those relationships. Div. FOF ¶¶ 159-180.

L. Poulson's Events Were Not "Purely Educational"

Equity Trust argues that Poulson's events were strictly "educational," claiming, for example, that Poulson's "seminars were purely educational as were [his] dinner events." Resp. Br. at 33. The evidence proves, however, that the Poulson "educational" events were a platform from which Poulson promoted his promissory note scheme.

As Equity Trust admits, Poulson solicited investments from Glenn Savary and others. Describing Savary's initial investment, for example, Equity Trust states: "more than a year after joining SJREIA and seven months after Poulson Russo's Runnemede seminar, Savary approached Poulson in order to loan "private money" to Poulson, which Poulson was soliciting." Resp. Br. at 41.

What Equity Trust omits from Savary's narrative is that Poulson did not "solicit" Savary "one on one", but instead that "he solicited to everybody", that "[h]e would talk about private money, da, da, da, I do this all the time .... I'm currently doing a lot of deals. I could use the money." Tr. 1113:23-25; 1113:17-22. Savary continued to say: "see, what he did, it was very clever. During these presentations, he would bring up the private money and say, well, it's safe, da, da, there is insurance against it ... you're in second position .... [and] basically lowered your guard as safe." Tr. 1114:13-24. As such, Savary plainly understood that whatever "educational" component there was to Poulson's scheme, Poulson's purpose was to solicit "private money" investments, and Poulson solicited Savary and others during his presentations.

Joseph Gatto also testified that Poulson "made no [] secret" of the fact that he was selling investments at events. Div. FOF ¶ 509. Gatto stated that, after attending only a couple of the Poulson Russo events, it was plain that their purpose was to solicit investment and that, contrary to Equity Trust's claim that Poulson ran "purely educational" events, his seminars were in truth just a "sales pitch", "guise" and "marketing scheme to get more investors." Div. FOF ¶ 511.

Contemporaneous communications also show that Equity Trust knew that Poulson's "educational" events could not be separated from his note offerings. In a 2008 email to Berlovan, Poulson boasted that "I have probably worked with 10 or 12 customers of Equity Trust [...] most of whom I referred" and "I frequently use private money in my real estate investment

business to complete and settle transactions..." Div. FOF ¶ 151. In another example, Jeanette Arnholt emailed J. Desich among others that Poulson was "a client" who "had consistently been referring people to us." Div. FOF ¶¶ 302, 309.

Between January 2007 through May 2011, a total of 34 Equity Trust customers invested a total of $974,998 in 41 Poulson Notes. DE 41 at 2 (Daniello Decl.). And many of these same Equity Trust customers holding Poulson Notes were also included in the event attendance sheets that Poulson provided Berlovan for leads, including Savary and Gatto. Div. FOF ¶ 333; *see also* DE 184 at 3, 7 (listing Savary at line 48, Gatto at line 106).

M. Despite the Evidence to the Contrary, Equity Trust Fails to Acknowledge It Sponsored Poulson's Monthly Dinner Events

Equity Trust claims that it and Poulson merely "initially indicated" that they would sponsor each other's events, and that "Equity Trust never actually did pay to sponsor the Poulson Russo education dinners, and Poulson never actually did pay to sponsor an Equity Trust event." Resp. Br. at 35.

Numerous emails between Berlovan, Arnholt and Poulson demonstrate that there was an agreement between Poulson and Equity Trust to sponsor each other's events, and that the terms of the payments were also agreed upon. Equity Trust prepared signage in order to promote Poulson at an Equity Trust conference, and Berlovan sought out Poulson material to display. Div. FOF ¶¶ 334-342. Equity Trust's point that no money appears to have been exchanged is irrelevant: Equity Trust agreed to net the $750 that Poulson owed Equity Trust for the "break sponsorship" against the $600 that Equity Trust agreed to pay as a "dinner sponsor" of the Poulson's events. After the netting – agreed to by both sides – Poulson owed Equity Trust $150. Div. FOF ¶¶ 327-348.

N. No Evidence Exists that Customers Invested with Poulson Due To His "Regional Prominence"

Equity Trust claims that its customers invested with Poulson not because of Equity Trust's role and endorsement of Poulson, but instead due to Poulson's "regional prominence." Resp. Br. at 35. This argument is baseless, as Poulson was never "regionally prominent," and the victims of Poulson's scheme testified conclusively that Equity Trust's custodial role and endorsement of Poulson was important to their investment decision.

In his testimony, Joseph Gatto was clear that Poulson's role as president of the South Jersey Investors Association was "not a big deal." Tr. 1283:22-1284:1 (Gatto on cross-examination: Q. "Was this a big deal if you were a real estate investor in South Jersey to see the president of the REIA? A. A guy just like me. It's not a big deal. I'm not into celebrities."). Gatto went on to say that while Poulson was elected president of the organization, that many times candidates were unopposed in the election. Tr. 1284:12-17. Gatto similarly dismissed his own role as the "executive director" of the group, and explained that all it meant was that he functioned as its "administrative assistant." Tr. 1279:10-14.

By contrast, Gatto was categorical that Equity Trust and its endorsement of Poulson was significant to his decision to invest. Gatto said that his conversation with Berlovan and her "glowing recommendation" of Poulson was "pretty much the deciding factor" in his decision to invest with Poulson using Equity Trust. Div. FOF ¶ 516.

There is also no evidence that Savary invested in Poulson based on his "regional prominence" as Respondent claims. *See, e.g.*, Tr. 1102:5-23; 1105:2-17 (Savary testimony of South Jersey Investors as a "local club"; attraction to Poulson because he was "local" and seemed successful). Savary instead emphasized Equity Trust's importance to his investment decision, and in particular the expectation that it would diligently perform its custodial duties.

When Savary opened an Equity Trust account – as Poulson directed – he expected that as custodian Equity Trust would not release the funds without a signed promissory note and mortgage in place. Div. FOF ¶¶ 533, 539. And when Equity Trust released the money without these required documents, Savary stated doing so was "like gross negligence." Div. FOF ¶ 539. He also believed that Equity Trust "failed" in its custodial responsibilities by failing to collect and hold required documentation, and characterized Equity Trust's conduct as "aiding and abetting." Div. FOF ¶ 550.

V. THE DISGORGEMENT AND PENALTY CALCULATIONS ARE APPROPRIATE

A. Disgorgement

Apparently conceding that a cease-and desist order, prejudgment interest on any disgorgement amount, and the retention of a three-year independent compliance consultant are appropriate in the event of a liability finding, Equity Trust argues only that there should be no disgorgement and no penalty.[13]

The Division's straightforward basis for disgorgement is consistent with precedent that management and other fees received during the period of violative conduct are subject to disgorgement. Div. COL ¶¶ 117-119. *See also Bogar*, 2013 WL 3963608, at *26 ("commissions from management fees are appropriately disgorged where they constitute ill-gotten gains earned during the course of violative activities"). The management fees received by Equity Trust during the period it administered the Taylor and Poulson accounts were $180,336.18. This disgorgement figure derives from two sources. First, it includes $62,598.81 in fees paid by City Capital to Equity Trust, and was determined based on account records

[13] The Division's pre-hearing brief dated November 23, 2015 (at 23-25), made clear the Division's intention to seek a cease-and-desist order, prejudgment interest and an independent compliance monitor. Equity Trust's post-hearing brief makes no arguments opposing these forms of relief.

reviewed by the Division's summary witness, Kerri L. Palen. DE 40 at 7, 24-27 (Palen Decl.). Equity Trust consented to the admission of the Palen Declaration without objection. The other source is Equity Trust's own transaction account records, which were admitted into evidence as Division Exhibit 797 and 798, with the fees summarized at Attachment A to the Division's Proposed Findings of Fact and Conclusions of Law, for a total of $117,737.37.

All fees should be disgorged because Equity Trust's violative conduct, including its failure to act as a passive custodian, took place during the period it administered the Taylor or Poulson accounts. Although the Commission distinguishes between "amounts earned through legitimate activities and those connected to violative activities," *Bogar*, 2013 WL 3963608 at *36, in this instance Equity Trust's fees cannot be attributed to "legitimate activities." Equity Trust had a narrow and defined role as an IRA custodian, and it deviated from that role throughout the relevant period. The deviations from its passive custodian role became more egregious in 2009 and later, but its violative conduct occurred throughout.

Equity Trust cites to *Natural Blue Resources*, S.E.C. Rel. No. 863, 2015 WL 4929878 (Init. Dec. Apr. 18, 2015) (on review to Commission), to support its argument that disgorgement should be zero. Resp. Br. at 60. In *Natural Blue*, the respondents were found to have violated the antifraud provisions by running a public company as consultants, while also acting as *de facto* officers, and concealing negative information about their backgrounds. The Division sought disgorgement of all compensation received, including expense reimbursement for consulting work. The Court ruled that the Division should have distinguished between the work done as legitimate consultants and the work done as *de facto* officers. 2015 WL 4929878, *32.

Unlike *Natural Blue*, however, where the respondents performed legitimate work for the company that could potentially be distinguished from the violative work, Equity Trust performed

a narrow range of custodial services that cannot be so readily bifurcated. Given the totality of Equity Trust's conduct, which caused these two schemes to continue on for longer than they otherwise would, disgorgement of all fees is appropriate.

B. Civil Penalties

Equity Trust argues that there is "simply no basis for assessing a penalty," but this is based on its claim that it did nothing wrong. Resp. Br. at 61. With regard to the "deterrence" element of the penalty analysis, Equity Trust contends that "[d]eterrence should not be considered in the Division's first-ever case against an SDIRA custodian acting within the scope of its limited responsibilities."[14] Resp. Br. at 61. This is just a variation on Equity Trust's position that no penalty is justified because the underlying violation has not been proven. However, Equity Trust's egregious conduct demonstrates that deterrence is a critical component of the penalty analysis. And it is because this is "the Division's first-ever case against an SDIRA custodian" that the deterrence factor should be given consideration.

First, the entire thrust of this case is that Equity Trust was not acting "within the scope of its limited responsibilities." At the hearing, J. Desich and Dea – the CEO and President – testified that they believed Equity Trust did nothing wrong and they failed to address any of its own deficiencies that led to its involvement in the Taylor and Poulson investments. Div. COL ¶¶ 113-116; 122-132. The evidence also reflects that, contrary to Equity Trust's insinuation, most other custodians did not engage in the type of sales and marketing relationship as Equity Trust.

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[14] For this argument, Equity Trsut incorrectly cites to *Spring Hill Capital Markets*, S.E.C. Rel. No. 919, 2015 WL 7730856 (Init. Dec. Nov. 30, 2015). In *Spring Hill*, the respondents were found to have aided-and-abetted and caused violations of registration and books-and-records provisions. The Court determined that the deterrence factor did require second-tier penalties. *Id.* at 19. In another case cited by Equity Trust, *David B. Havanich, Jr.*, S.E.C. Rel. 935, 2016 WL 25746, *10 (Init. Dec. Jan. 4, 2016), the Court imposed a second-tier penalty even though there was no fraud and no previous violations by the respondent.

See, e.g., DE 36 (Taylor Dep. 309:17-19 (even though City Capital had dealt with four other IRA custodians, only Equity Trust sent a representative to one of Taylor's events)); Tr. 283:9-24 (Marsh: two other custodians did not attend events of issuers).

Second, Equity Trust was clearly on notice that issuers regularly perpetrated frauds through self-directed IRAs, including accounts at Equity Trust. Div. FOF ¶¶ 86-88; 681-685; 688-690; 695-698. In the face of these risks, Equity Trust eschewed its role as a passive custodian and encouraged its sales representatives to develop sales and marketing relationships with issuers, which contributed to the frauds here. Div. FOF ¶¶ 159-180.

Third, Equity Trust has a history of improving its business practices only when prompted by regulators or bad press. As the South Dakota Division of Banking made clear, Equity Trust's compliance culture was reactive (Div. FOF ¶ 621), and Equity Trust only began warning investors of the risks of fraud at some point in 2012 despite being on notice for years. Div. FOF ¶¶ 658-672.

Finally, the Division of Banking made clear that Equity Trust circumvented any oversight into the most problematic areas of Equity Trust – the sales and marketing department – by putting those departments into an affiliate company. Tr. 1179:6-1182:5 (S. Kelly). Indeed, S. Kelly testified that he was not even aware that Equity Trust had a sales and marketing department or that an Equity Trust employee went to New Birth Church. Tr. 1179:6-1184:10. It was clear, though, that the sales and marketing departments were fully coordinated with Equity Trust and represented themselves as Equity Trust employees. *See, e.g.*, Answer at ¶¶ 34; 36; 38-40; 55 (referring to Batt, Berlvoan, and E. Kelly as Equity Trust representatives); DE 673 (signature line of Batt email to customer states "Equity Trust Company"); DE 767 (Berlovan's business card given to Gatto states "Equity Trust Company"). Thus, Respondent's suggestion

that a "satisfactory" grade from its regulator (Resp. Br. at 61) reflects its compliant nature is disingenuous. Instead, it is clear that Equity Trust has not been forthcoming with its regulator because Equity Trust's sales representatives were all operating as Equity Trust employees.

VI. EQUITY TRUST'S CONSTITUTIONAL ARGUMENTS ARE WITHOUT MERIT

A. This Proceeding is Consistent with Due Process

Equity Trust erroneously asserts that this proceeding violates its due process rights on multiple grounds, including that the Commission's Rules of Practice unfairly limit Equity Trust's ability to take discovery and that the rules give Equity Trust an insufficient amount of time to prepare for the hearing. Resp. Br. 62. The Commission and the courts have repeatedly rejected "[s]uch broad attacks on the procedures of the administrative process." *Harding Advisory LLC*, S.E.C. Rel. No. 3796, 2014 WL 988532, at *8 (Mar. 14, 2014); *see also John Thomas Capital Management Group. LLC*, S.E.C. Rel. No. 3733, 2013 WL 6384275, at *5-6 (Dec. 6, 2013) (rejecting respondents' argument that it was not feasible for them to review the Division's disclosures prior to the hearing); *Gregory M. Dearlove*, S.E.C. Rel. No. 2779, 2008 WL 281105, at *37 (Jan. 31, 2008) (holding that Rule 360(a) is consistent with due process). Indeed, to accept such challenges "would do considerable violence to Congress['s] purposes in establishing" specialized administrative agencies and would "work a revolution in administrative (not to mention constitutional) law." *Blinder, Robinson & Co. v. SEC*, 837 F.2d 1099, 1107 (D.C. Cir. 1988). Due process requires "the opportunity to be heard 'at a meaningful time and in a meaningful manner,'" *Mathews v. Eldridge*, 424 U.S. 319, 333 (1976), and Equity Trust has been afforded that opportunity here.

Equity Trust also asserts that the "Rules of Practice lack rules of evidence," Resp. Br. at 62, but this is incorrect because the Rules of Practice do have evidentiary rules. To the extent

that Equity Trust contends that the Commission must apply instead the Federal Rules of Evidence, that argument is foreclosed by Commission precedent. *Ralph Calabro*, S.E.C. Rel. No. 9798, 2015 WL 3439152, at *10 & n.66 (May 29, 2015). Further, courts have held that the fact that an administrative proceeding is not governed by the federal rules does not render the proceeding unfair. *See, e.g.*, *Cunanan v. INS*, 856 F.2d 1373, 1374 (2d Cir. 1988). Finally, Equity Trust has not shown how the application of the Commission's Rules of Practice in this proceeding caused the type of prejudice sufficient to establish a due process violation. *See, e.g.*, *Horning v. SEC*, 570 F.3d 337, 347 (D.C. Cir. 2009) ("In the absence of any suggestion of prejudice, we cannot conclude that Horning was deprived ... of procedural due process.").

B. The Commission's Administrative Proceedings Do Not Violate the Seventh Amendment or the Fifth Amendment

Equity Trust argues that by instituting this action in the administrative forum, the Commission has denied it a right to a jury trial. Resp. Br. at 62. But it is well established that Congress "may assign th[e] adjudication" of cases involving so-called "public rights" to "an administrative agency with which a jury trial would be incompatible[] without violating the Seventh Amendment[] ... even if the Seventh Amendment would have required a jury where the adjudication of those rights is assigned instead to a federal court of law." *Atlas Roofing Co. v. Occupational Safety & Health Review Comm'n*, 430 U.S. 442, 455 (1977). Here, in pursuing civil penalties against Equity Trust, the Commission is acting in the government's "sovereign capacity under an otherwise valid statute creating enforceable public rights," *id.* at 458, and thus, Congress's choice of the administrative forum is proper.

Also unavailing is Equity Trust's assertion that the Commission's decision to pursue this action in an administrative proceeding rather than in federal court offends the Fifth Amendment. Resp. Br. 63. The sole allegation in the OIP is that Equity Trust "caused" violations by others,

and Section 8A of the Securities Act, 15 U.S.C. 77h-1, authorizes the Commission to bring such actions in administrative proceedings only, not in federal court.

In any event, even assuming that the Commission could have brought this action in federal court, Equity Trust has not shown that the Commission's decision to use the administrative forum violated Equity Trust's due process rights. Congress has given the Commission authority to initiate administrative proceedings, as well as to bring civil actions in federal court, and the "Commission's choice to use either or both of those means to enforce the securities laws is a matter of broad agency" that reflects "a highly individualized assessment of the facts and circumstances of a given case." *Timbervest, LLC,* S.E.C. Rel. No. 4197, 2015 WL 5472520, at *29 (Sept. 17, 2015). In order to show such discretion has been abused in a particular case, Equity Trust must present "clear evidence" that the decision to proceed in a particular forum was based on impermissible grounds. *United States v. Armstrong*, 517 U.S. 456, 464–65 (1996). For example, to establish that it has been irrationally singled out for disparate treatment, Equity Trust would need to show an "invidious" motive on the Division's part, which it has not done. *United States v. Moore*, 543 F.3d 891, 900 (7th Cir. 2008); *Armstrong*, 517 U.S. at 646-65 (decision to prosecute must "not be based on 'an unjustifiable standard such as race, religion, or other arbitrary classification"); *China-Biotics, Inc.*, S.E.C. Rel. No. 70800, 2013 WL 5883342, at *15 (Nov. 4, 2013). Accordingly, its Fifth Amendment challenge fails.

C. The Appointment and Removal of Administrative Law Judges Is Constitutional

Equity Trust mistakenly contends that the hearing was unconstitutional because the Commission's appointment of ALJs and the manner for their removal violates Article II of the Constitution. Resp. Br. at 63. These arguments are without merit because Commission ALJs are employees, not constitutional officers, and thus they are not subject to Article II's requirements.

Raymond J. Lucia Cos., S.E.C. Rel. No. 4190, 2015 WL 5172953, at *21 (Sept. 3, 2015); *Timbervest, LLC*, 2015 WL 5472520, at *23-26; *David F. Bandimere*, S.E.C. Rel. No. 9972, 2015 WL 6575665, at *19-21 (Oct. 29, 2015).

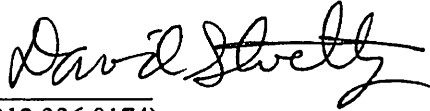
CONCLUSION

The Division of Enforcement respectfully requests that this Court make findings of fact and conclusions of law consistent with the evidence showing Respondent Equity Trust Company's illegal conduct, and that the requested sanctions be imposed.

Dated: New York, NY
February 29, 2016

Respectfully submitted,

DIVISION OF ENFORCEMENT

/s David Stoelting 

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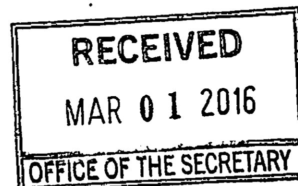
CERTIFICATE OF SERVICE

I hereby certify that I served true copies by overnight courier and electronic mail of the foregoing Reply Brief of the Division of Enforcement in response to Respondent's Post-Hearing Brief on the following on the 29th day of February, 2016.



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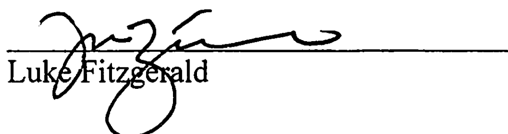

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